

SELL

TP: Rs 230 | ▼ 11%

WIPRO

| IT Services

| 18 July 2019

Another disappointing quarter

Wipro (WPRO) reported another tepid quarter as a wind-down of large projects in the retail & CPG verticals and delayed ramp-up of some contracts led to a dollar revenue decline of 1.8% QoQ. Adj. IT services EBIT margin at 17.9% was below estimates. Q2 revenue growth guidance of 0-2% QoQ was uninspiring. We tweak estimates but retain our TP at Rs 230 upon rollover to Jun'20. A muted BFSI outlook, regulatory uncertainty in healthcare, and restructuring of India & Middle East operations continue to hamper recovery prospects.

Poor operating performance: WPRO reported a 1.8% QoQ drop in dollar revenues for Q1FY20 vs. our/street estimates of a 0.9%/0.2% QoQ decline. Reported IT services EBIT margins at 18.4% (-80bps QoQ) were in line, albeit aided by Rs 669mn of exceptional gains on divestment of businesses. Adjusted for this, margins at 17.9% came in lower than estimates.

Uninspiring Sep'19 quarter guidance: Q2FY20 revenue growth guidance of 0-2% QoQ was subdued and below our estimate of 1-3% sequential growth. We highlight that the Sep'19 quarter will include inorganic revenues from consolidation of International TechneGroup (which had annual revenues of US\$ 23.2mn in FY18). The midpoint of the guided range implies moderation of WPRO's annual growth trajectory to low single-digits for FY20.

Retain SELL: We cut FY20/FY21 EPS estimates by 1.6%/2.1% as we accommodate the muted Jun'19 quarter performance. In our view, a growth recovery will continue to elude WPRO, inviting downside risks to consensus earnings estimates. We model for a 6.4% earnings CAGR over FY19-FY21 and retain SELL with an unchanged Jun'20 TP of Rs 230, valuing the stock at 13.5x one-year forward P/E.

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Ticker/Price	WPRO IN/Rs 260
Market cap	US\$ 17.0bn
Shares o/s	4,512mn
3M ADV	US\$ 27.3mn
52wk high/low	Rs 302/Rs 198
Promoter/FPI/DII	74%/9%/17%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY17A	FY18A	FY19A	FY20E	FY21E
Adj. net profit (Rs mn)	82,723	80,046	90,074	89,218	96,547
Adj. EPS (Rs)	12.8	13.3	14.9	15.6	16.9
Adj. EPS growth (%)	(5.8)	4.0	12.3	4.6	8.2
Adj. ROAE (%)	16.7	15.9	17.1	16.0	16.4
Adj. P/E (x)	20.3	19.5	17.4	16.6	15.3
EV/EBITDA (x)	10.6	12.0	10.0	9.3	8.7

Source: Company, BOBCAPS Research

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FIG 1 – JUN'19 QUARTER PERFORMANCE

(Rs mn)	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20	YoY (%)	QoQ (%)
US\$ revenues (IT Services excluding ISRE)*	1,989	2,010	2,047	2,076	2,039	2.5	(1.8)
Total revenue	1,40,548	1,46,627	1,51,506	1,50,379	1,48,019	5.3	(1.6)
Operating expenditure	1,19,771	1,21,139	1,22,838	1,23,125	1,23,345	3.0	0.2
Cost of revenues	1,00,350	1,01,770	1,03,971	1,05,462	1,04,273	3.9	(1.1)
as % of sales	71.4	69.4	68.6	70.1	70.4	-	-
SG&A expenses	19,421	19,369	18,867	17,663	19,072	(1.8)	8.0
as % of sales	13.8	13.2	12.5	11.7	12.9	-	-
EBIT	20,777	25,488	28,668	27,254	24,674	18.8	(9.5)
Other Income	6,024	(1,285)	3,742	4,747	6,045	0.3	27.3
PBT	26,801	24,203	32,410	32,001	30,719	14.6	(4.0)
Total Tax	5,865	5,347	6,966	7,064	6,699	14.2	(5.2)
Adjusted PAT	20,936	18,856	25,444	24,937	24,020	14.7	(3.7)
(Profit)/loss from JV's/Ass/MI	270	33	(341)	(104)	(147)	-	-
APAT after MI	21,206	18,889	25,103	24,833	23,873	12.6	(3.9)
Extra ordinary items	0	0	0	0	0	-	-
Reported PAT	21,206	18,889	25,103	24,833	23,873	12.6	(3.9)
Reported EPS	3.5	3.1	4.2	4.1	4.0	12.3	(3.9)
Margins (%)						(bps)	(bps)
EBIT margin-IT Services (excluding ISRE)	17.6	18.4	19.8	19.2	17.9	34	(126)
EBIT	14.8	17.4	18.9	18.1	16.7	189	(145)
EBT	19.1	16.5	21.4	21.3	20.8	168	(53)
PAT	15.1	12.9	16.6	16.5	16.1	104	(39)
Effective Tax rate	21.9	22.1	21.5	22.1	21.8	(8)	(27)

Source: BOBCAPS Research | *Indian State Run Enterprises.

Earnings call highlights

- Management pointed to a “stable” demand environment but cautioned about slower decision-making in pockets of BFSI, namely capital markets and European banks – commentary similar to that of TCS and Infosys.
- Management is hopeful of regaining growth momentum through the rest of FY20 aided by a strong deal pipeline.
- WPRO awaits clarity on the buyback tax in the final finance bill and remains committed to completing its plan of capital return to shareholders.
- The company has achieved 65% localisation in North America.

Valuation methodology

Despite several strategic interventions, WPRO has underperformed its tier-I IT service peers in terms of revenues and earnings over the past seven years.

Regulatory uncertainty for the healthcare business, restructuring of India and Middle East operations, and a muted outlook for the BFSI and manufacturing verticals cloud recovery prospects. While we acknowledge that the company's strategic moves are steps in the right direction, we believe patchy, inconsistent execution will remain a drag on growth.

We cut FY20/FY21 EPS estimates by 1.6%/2.1% as we accommodate the muted Jun'19 quarter performance. Upon rolling valuations forward, our Jun'20 target price remains unchanged at Rs 230, set at 13.5x one-year forward P/E. Maintain SELL.

FIG 2 – REVISED ESTIMATES

(Rs mn)	FY20E			FY21E		
	Old	New	Change (%)	Old	New	Change (%)
IT Services revenues (excluding ISRE, in US\$ mn)	8,488	8,299	(2.2)	9,080	8,857	(2.5)
IT Services revenues (excluding ISRE, in US\$ mn), YoY growth (%)	4.5	2.2	-	7.0	6.7	-
Company-wide revenues	6,12,162	5,91,012	(3.5)	6,55,012	6,35,753	(2.9)
EBIT	1,05,890	1,02,726	(3.0)	1,14,089	1,11,635	(2.2)
EBIT margins (%)	17.3	17.4	-	17.4	17.6	-
Net profits	90,569	89,218	(1.5)	98,420	96,547	(1.9)
EPS (Rs)	15.9	15.6	(1.6)	17.3	16.9	(2.1)

Source: BOBCAPS Research

FIG 3 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

Upside risks to our estimates include:

- a sharper recovery in demand than expected,
- stronger-than-estimated large deal wins, and
- sharp, favourable currency movements.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19A	FY20E	FY21E
Total revenue	5,54,179	5,46,359	5,89,060	5,91,012	6,35,753
EBITDA	1,12,904	1,05,418	1,27,072	1,19,485	1,35,789
EBIT	89,797	84,294	1,02,187	1,02,726	1,11,635
Net interest income/(expenses)	13,521	18,169	15,548	14,148	13,992
Other income/(expenses)	4,867	0	0	0	0
Exceptional items	0	0	0	0	0
EBT	1,08,185	1,02,463	1,15,458	1,16,175	1,25,626
Income taxes	25,214	22,390	25,242	26,661	28,879
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	248	27	142	297	200
Reported net profit	82,723	80,046	90,074	89,218	96,547
Adjustments	0	0	0	0	0
Adjusted net profit	82,723	80,046	90,074	89,218	96,547

Balance Sheet

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19A	FY20E	FY21E
Accounts payables	0	0	0	0	0
Other current liabilities	1,20,521	1,33,177	1,58,894	1,31,156	1,41,085
Provisions	1,274	799	640	1,457	1,568
Debt funds	1,42,412	1,38,259	99,467	99,467	99,467
Other liabilities	6,614	3,059	3,417	3,417	3,417
Equity capital	4,861	9,048	12,068	12,068	12,068
Reserves & surplus	5,17,834	4,76,298	5,58,685	5,32,462	6,17,590
Shareholders' fund	5,22,695	4,85,346	5,70,753	5,44,530	6,29,658
Total liabilities and equities	7,93,516	7,60,640	8,33,171	7,80,027	8,75,194
Cash and cash eq.	52,710	44,925	1,58,529	89,969	1,65,965
Accounts receivables	98,844	1,00,990	1,00,489	1,06,868	1,14,958
Inventories	3,915	3,370	3,951	4,858	5,225
Other current assets	1,12,296	1,45,107	1,29,457	1,30,346	1,40,214
Investments	2,99,133	2,59,200	2,33,798	2,33,798	2,33,798
Net fixed assets	69,794	64,443	70,601	77,842	78,688
CWIP	8,951	15,166	0	0	0
Intangible assets	1,41,718	1,35,697	1,30,742	1,30,742	1,30,742
Deferred tax assets, net	15,106	6,908	5,604	5,604	5,604
Other assets	0	0	0	0	0
Total assets	7,93,516	7,60,640	8,33,171	7,80,027	8,75,194

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY17A	FY18A	FY19A	FY20E	FY21E
Net income + Depreciation	82,803	73,043	1,15,101	1,06,273	1,20,902
Interest expenses	0	0	(15,548)	(14,148)	(13,992)
Non-cash adjustments	0	0	0	0	0
Changes in working capital	4,511	(877)	41,128	(35,096)	(8,286)
Other operating cash flows	5,459	12,067	14,424	0	0
Cash flow from operations	92,773	84,233	1,55,105	57,030	98,624
Capital expenditures	(19,646)	(20,699)	(46,209)	(24,000)	(25,000)
Change in investments	(83,684)	47,973	0	0	0
Other investing cash flows	(12,373)	8,679	15,548	14,148	13,992
Cash flow from investing	(1,15,703)	35,953	(30,661)	(9,852)	(11,008)
Equities issued/Others	0	24	0	(1,05,000)	0
Debt raised/repaid	0	0	0	0	0
Interest expenses	(14,018)	(1,24,582)	0	0	0
Dividends paid	(8,734)	(5,420)	(10,840)	(10,737)	(11,619)
Other financing cash flows	0	0	0	0	0
Cash flow from financing	(22,752)	(1,29,978)	(10,840)	(1,15,737)	(11,619)
Changes in cash and cash eq.	(45,682)	(9,792)	1,13,604	(68,560)	75,996
Closing cash and cash eq.	52,710	44,925	1,58,529	89,969	1,65,965

Per Share

Y/E 31 Mar (Rs)	FY17A	FY18A	FY19A	FY20E	FY21E
Reported EPS	12.8	13.3	14.9	15.6	16.9
Adjusted EPS	12.8	13.3	14.9	15.6	16.9
Dividend per share	2.0	1.0	1.5	1.6	1.7
Book value per share	80.8	80.7	94.7	95.4	110.4

Valuations Ratios

Y/E 31 Mar (x)	FY17A	FY18A	FY19A	FY20E	FY21E
EV/Sales	2.2	2.3	2.1	1.9	1.9
EV/EBITDA	10.6	12.0	10.0	9.3	8.7
Adjusted P/E	20.3	19.5	17.4	16.6	15.3
P/BV	3.2	3.2	2.7	2.7	2.4

DuPont Analysis

Y/E 31 Mar (%)	FY17A	FY18A	FY19A	FY20E	FY21E
Tax burden (Net profit/PBT)	76.5	78.1	78.0	76.8	76.9
Interest burden (PBT/EBIT)	120.5	121.6	113.0	113.1	112.5
EBIT margin (EBIT/Revenue)	16.2	15.4	17.3	17.4	17.6
Asset turnover (Revenue/Avg TA)	73.0	70.3	73.9	73.3	76.8
Leverage (Avg TA/Avg Equity)	1.5	1.5	1.5	1.4	1.4
Adjusted ROAE	16.7	15.9	17.1	16.0	16.4

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY17A	FY18A	FY19A	FY20E	FY21E
YoY growth (%)					
Revenue	7.3	(1.4)	7.8	0.3	7.6
EBITDA	1.1	(6.6)	20.5	(6.0)	13.6
Adjusted EPS	(5.8)	4.0	12.3	4.6	8.2
Profitability & Return ratios (%)					
EBITDA margin	20.4	19.3	21.6	20.2	21.4
EBIT margin	16.2	15.4	17.3	17.4	17.6
Adjusted profit margin	14.9	14.7	15.3	15.1	15.2
Adjusted ROAE	16.7	15.9	17.1	16.0	16.4
ROCE	16.0	14.0	18.6	19.1	19.8
Working capital days (days)					
Receivables	66	67	62	64	64
Inventory	4	3	3	3	4
Payables	96	100	109	108	95
Ratios (x)					
Gross asset turnover	8.2	8.1	8.7	8.0	8.1
Current ratio	2.2	2.2	2.5	2.5	3.0
Net interest coverage ratio	6.6	4.6	6.6	7.3	8.0
Adjusted debt/equity	0.2	0.2	(0.1)	0.0	(0.1)

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

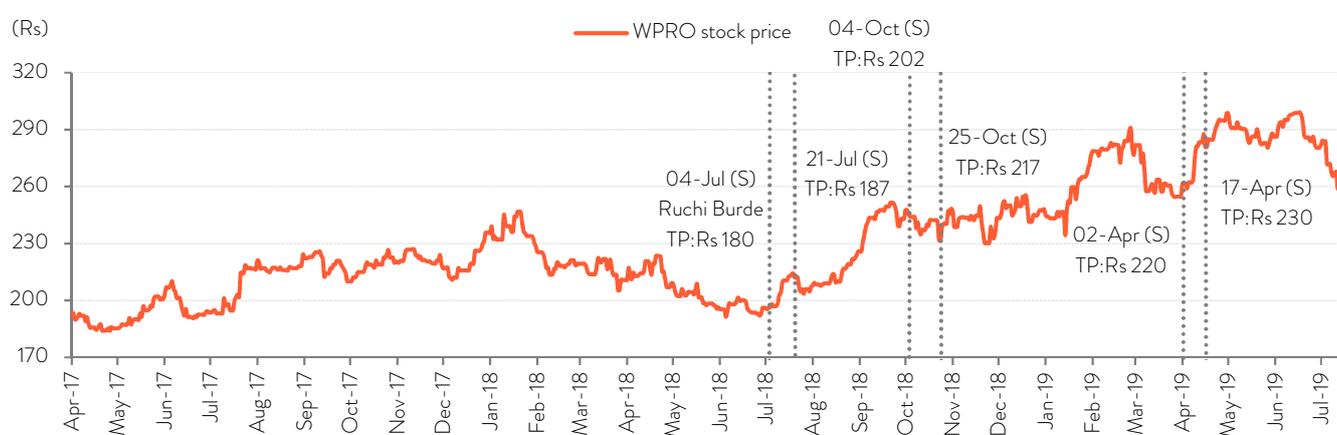
ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

HISTORICAL RATINGS AND TARGET PRICE: WIPRO (WPRO IN)



B – Buy, A – Add, R – Reduce, S – Sell

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