

**SELL**

TP: Rs 170 | ▼ 9%

**WIPRO**

| IT Services

| 16 April 2020

## Weak quarter; guidance and dividends suspended

Wipro (WPRO) reported a subpar Q4FY20 with a miss on both revenue and operating margins. The company suspended quarterly guidance citing Covid-19 uncertainties and decided not to recommend final dividend. The latter came as a negative surprise, highlighting potential vulnerability despite a healthy balance sheet. We cut FY21/FY22 EPS by 13%/14% and lower our target FY22E P/E multiple to 11x (from 13.5x) to factor in the volatile business climate – reiterate SELL with a revised Mar'21 TP of Rs 170 (vs. Rs 240 earlier).

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**Subpar quarter:** WPRO underperformed our estimates on both revenue and operating margins. IT services revenue declined 1% QoQ in US dollar terms (+0.4% QoQ CC) vs. consensus estimates of sequentially flat dollar revenues. Adjusted for US\$ 14mn-16mn of Covid-led headwinds (0.7-0.8% of revenue), IT services revenue was nearer the midpoint of the company's guided range of 0-2% QoQ CC growth. Segmental EBIT margins slipped 80bps QoQ to 17.6% vs. consensus estimates of 20bps contraction.

Ticker/Price	WPRO IN/Rs 187
Market cap	US\$ 13.9bn
Shares o/s	5,715mn
3M ADV	US\$ 11.9mn
52wk high/low	Rs 302/Rs 159
Promoter/FPI/DII	74%/9%/17%

Source: NSE

**Quarterly guidance suspended:** Unsurprisingly, management suspended quarterly guidance citing Covid-led uncertainties. We expect other Indian IT services peers to follow suit. US-listed peers such as Cognizant (CTSH), EPAM and Virtusa have already withdrawn their respective guidance. Management expects QoQ revenue contraction for Q1FY21 but refrained from commenting on margins, merely affirming that WPRO remains focused on cost optimisation.

## STOCK PERFORMANCE



Source: NSE

**No final dividend:** The board did not recommend final dividend, which was a negative surprise given cash & liquid investments worth Rs 334bn or US\$ 4.3bn and a debt-free balance sheet. We highlight the contrast with CTSH which paused its share repurchase scheme (and credit drawdown) in the US primarily due to a geographical mismatch in cash balance (parked in India) and requirement.

## KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20A	FY21E	FY22E
Total revenue (Rs mn)	5,46,359	5,89,060	6,13,401	6,15,956	6,45,651
EBITDA (Rs mn)	1,05,418	1,21,661	1,24,867	1,15,903	1,27,293
Adj. net profit (Rs mn)	80,046	90,074	95,295	85,396	92,160
Adj. EPS (Rs)	13.3	14.9	16.7	14.4	15.5
Adj. EPS growth (%)	4.0	12.3	11.6	(13.9)	7.9
Adj. ROAE (%)	15.9	17.1	16.9	14.3	13.6
Adj. P/E (x)	14.0	12.5	11.2	13.0	12.0
EV/EBITDA (x)	10.7	9.5	8.7	8.7	7.8

Source: Company, BOBCAPS Research

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## Earnings call highlights

### Covid-19 impact

- 90% of WPRO's workforce is currently working from home; only ~7% of the workload cannot be migrated to this model.
- The demand environment has changed drastically, especially for verticals that have borne the initial brunt of the worldwide lockdown, i.e. retail, oil and gas, and manufacturing (automobiles in particular). BFSI will also suffer due to the possibility of negative interest rates.
- Most clients from the affected verticals have asked for extended payment cycles. Discretionary spending has slowed considerably and pricing pressure has increased. Players are facing increased demands to ramp up efficiency in the 'run-the-business' segment.
- Operating margins are expected to face headwinds going forward. Management acknowledged the possibility of furloughing employees to minimise the toll on margins.
- On the positive side, two of the big bets – cloud and cybersecurity – are gaining traction and WPRO sees opportunities to gain market share. The company is well equipped to manage costs in the short term by optimising hiring and reducing overhead costs.

### Other highlights

- CEO succession is well on track and an announcement in this regard will be made in Q1FY21.

**FIG 1 – MAR-20 QUARTERLY PERFORMANCE**

(Rs mn)	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	FY20	FY19	YoY (%)
<b>US\$ revenues (IT Services excluding ISRE)*</b>	<b>2,074</b>	<b>2,076</b>	<b>(0.1)</b>	<b>2,095</b>	<b>(1.0)</b>	<b>8,256</b>	<b>8,120</b>	<b>1.7</b>
<b>Total Revenue</b>	<b>1,58,103</b>	<b>1,50,379</b>	<b>5.1</b>	<b>1,55,432</b>	<b>1.7</b>	<b>6,13,401</b>	<b>5,89,060</b>	<b>4.1</b>
Operating Expenditure	1,32,109	1,23,125	7.3	1,28,199	3.0	5,08,815	4,86,873	4.5
Cost of revenues	1,14,133	1,05,462	8.2	1,09,673	4.1	4,36,085	4,11,553	6.0
as % of sales	72.2	70.1	-	70.6	-	71.1	69.9	-
SG&A expenses	17,976	17,663	1.8	18,526	(3.0)	72,730	75,320	(3.4)
as % of sales	11.4	11.7	-	11.9	-	11.9	12.8	-
<b>EBIT</b>	<b>25,994</b>	<b>27,254</b>	<b>(4.6)</b>	<b>27,233</b>	<b>(4.5)</b>	<b>1,04,586</b>	<b>1,02,187</b>	<b>2.3</b>
Other Income	3,267	4,747	(31.2)	3,560	(8.2)	17,530	13,228	32.5
PBT	29,261	32,001	(8.6)	30,793	(5.0)	1,22,116	1,15,415	5.8
Total Tax	6,205	7,064	(12.2)	6,164	0.7	24,799	25,242	(1.8)
<b>Adjusted PAT</b>	<b>23,056</b>	<b>24,937</b>	<b>(7.5)</b>	<b>24,629</b>	<b>(6.4)</b>	<b>97,317</b>	<b>90,173</b>	<b>7.9</b>
(Profit)/loss from JV's/Ass/MI	(191)	(104)	-	(71)	-	(495)	(142)	-
APAT after MI	22,865	24,833	(7.9)	24,558	(6.9)	96,822	90,031	7.5
Extra ordinary items	0	0	-	0	-	0	0	-
<b>Reported PAT</b>	<b>23,260</b>	<b>24,833</b>	<b>(6.3)</b>	<b>24,558</b>	<b>(5.3)</b>	<b>97,217</b>	<b>90,031</b>	<b>8.0</b>
Reported EPS	4.1	4.1	(1.2)	4.1	(1.4)	16	15	10.0
<b>Margins (%)</b>								
EBIT margin-IT Services (excluding ISRE)	17.6	19.2	(160)	18.4	(80)	18.8	17.4	140
EBIT	16.4	18.1	(170)	17.5	(110)	17.1	17.3	(30)
EBT	18.5	21.3	(280)	19.8	(130)	19.9	19.6	30
PAT	14.7	16.5	(180)	15.8	(110)	15.8	15.3	60
Effective Tax rate	21.2	22.1	(90)	20.0	120	20.3	21.9	(160)

Source: Company, BOBCAPS Research | \*India state run enterprises.

**FIG 2 – MAR-20 OPERATING METRICS**

(In US\$ terms)	Q4FY20 (% Contr. to Revenue)	Growth	
		QoQ (%)	YoY (%)
Digital Revenues	41.2	2.8	18.6
<b>Revenue by Practices</b>			
Technology Infrastructure Services	25.8	(0.7)	2.6
Analytics	7.2	(0.7)	0.2
BPO	14.6	(5.2)	(1.8)
Product Engg and Mobility	7.7	1.9	1.5
Application Services	44.7	0.4	(0.7)
<b>Revenue by Vertical</b>			
Global Media & Telecom	5.5	(4.5)	(3.6)
Finance Solutions	30.4	(2.6)	(3.6)
Manufacturing & Hitech	8.2	(1.0)	2.4
Healthcare, Life Sciences & Services	13.5	2.0	2.2
Retail & Transportation	16.8	(1.6)	3.6
Energy & Utilities	12.8	(1.8)	(0.1)
Technology	12.8	3.0	1.5
<b>Revenue by Geography</b>			
US	59.1	(1.2)	1.5
Europe	24.1	0.7	(2.1)
ROW	16.8	(2.7)	(2.4)
<b>Customer Concentration</b>			
Top customer	3.0	(1.0)	(19.0)
Top 5 customers	12.2	(1.8)	(11.0)
Top 10 customers	19.3	(0.5)	(5.5)
Non-Top 10	80.7	(1.1)	1.3
<b>Utilisation</b>			
Global IT services ex IFOX -Gross	73.4	70.2	75.4
Global IT services ex IFOX-Net	82.4	78.5	84.1
Global IT services ex IFOX-Net ex trainees	82.6	79.6	85.4
<b>Attrition</b>			
Voluntary Attrition TTM	14.7	15.7	17.6
Global IT services-Voluntary	12.6	12.5	16.6

Source: Company, BOBCAPS Research

Technology and Healthcare were the only verticals with sequential revenue growth

Revenue from N. America was the weakest at -0.7% QoQ CC; Europe/RoW grew 3.4%/0.4% QoQ CC

## Valuation methodology

We cut FY21/FY22 EPS estimates by 13%/14% as we moderate revenue growth and operating margin assumptions due to the Covid-19 crisis. In our view, the street is not capturing the worst-case scenario for WPRO and hence we find limited valuation comfort despite the recent correction.

Given a patchy track record of strategy execution and a laggardly performance amongst peers, we stay apprehensive about the company's resilience in the current challenging environment. We reiterate SELL with a revised Mar'21 target price of Rs 170 (vs. Rs 240 earlier), set at a target FY22E P/E multiple of 11x (vs. 13.5x earlier to account for Covid-related uncertainties).

**FIG 3 – REVISED ESTIMATES**

(Rs mn)	FY21E			FY22E		
	Old	New	Change (%)	Old	New	Change (%)
IT Services revenues (excluding ISRE, in US\$ mn)	8,816	7,955	(9.8)	9,440	8,353	(11.5)
IT Services revenues (excluding ISRE, in US\$ mn), YoY growth (%)	6.2	(3.7)		7.1	5.0	
Company Wide Revenues	6,35,136	6,15,956	(3.0)	6,78,615	6,45,651	(4.9)
EBIT	1,11,202	95,576	(14.1)	1,19,033	1,05,986	(11.0)
EBIT margins (%)	17.5	15.5		17.5	16.4	
Net profits	98,434	85,396	(13.2)	1,06,801	92,160	(13.7)
EPS (Rs)	16.5	14.4	(13.2)	17.9	15.5	(13.7)

Source: BOBCAPS Research

**FIG 4 – 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)	FY18A	FY19A	FY20A	FY21E	FY22E
<b>Total revenue</b>	<b>5,46,359</b>	<b>5,89,060</b>	<b>6,13,401</b>	<b>6,15,956</b>	<b>6,45,651</b>
EBITDA	1,05,418	1,21,661	1,24,867	1,15,903	1,27,293
Depreciation	21,124	19,474	20,281	20,327	21,306
EBIT	84,294	1,02,187	1,04,586	95,576	1,05,986
Net interest income/(expenses)	18,169	15,548	16,752	12,809	12,463
Other income/(expenses)	0	0	0	0	0
Exceptional items	0	0	0	0	0
EBT	1,02,463	1,15,458	1,20,589	1,08,385	1,18,449
Income taxes	22,390	25,242	24,799	22,789	26,089
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	27	142	495	200	200
<b>Reported net profit</b>	<b>80,046</b>	<b>90,074</b>	<b>95,295</b>	<b>85,396</b>	<b>92,160</b>
Adjustments	0	0	0	0	0
<b>Adjusted net profit</b>	<b>80,046</b>	<b>90,074</b>	<b>95,295</b>	<b>85,396</b>	<b>92,160</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20A	FY21E	FY22E
Accounts payables	0	0	0	0	0
Other current liabilities	1,33,177	1,58,894	1,56,761	1,36,691	1,43,281
Provisions	799	640	612	1,519	1,592
Debt funds	1,38,259	99,467	78,042	78,042	78,042
Other liabilities	3,059	3,417	2,825	2,825	2,825
Equity capital	9,048	12,068	11,427	11,427	11,427
Reserves & surplus	4,76,298	5,58,685	5,47,906	6,23,224	7,04,493
Shareholders' fund	4,85,346	5,70,753	5,59,333	6,34,651	7,15,920
<b>Total liabilities and equities</b>	<b>7,60,640</b>	<b>8,33,171</b>	<b>7,97,573</b>	<b>8,53,729</b>	<b>9,41,661</b>
Cash and cash eq.	44,925	1,58,529	1,44,499	1,52,172	2,30,998
Accounts receivables	1,00,990	1,00,489	1,04,474	1,26,566	1,16,748
Inventories	3,370	3,951	1,865	5,063	5,307
Other current assets	1,45,107	1,29,457	1,08,891	1,27,410	1,42,397
Investments	2,59,200	2,33,798	2,03,345	2,03,345	2,03,345
Net fixed assets	64,443	70,601	81,120	85,793	89,487
CWIP	15,166	0	0	0	0
Intangible assets	1,35,697	1,30,742	1,47,374	1,47,374	1,47,374
Deferred tax assets, net	6,908	5,604	6,005	6,005	6,005
Other assets	0	0	0	0	0
<b>Total assets</b>	<b>7,60,640</b>	<b>8,33,171</b>	<b>7,97,573</b>	<b>8,53,729</b>	<b>9,41,661</b>

Source: Company, BOBCAPS Research

### Cash Flows

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20A	FY21E	FY22E
Net income + Depreciation	73,043	1,09,690	1,16,071	1,05,922	1,13,667
Interest expenses	0	(15,548)	(16,752)	(12,809)	(12,463)
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(877)	41,128	16,506	(62,972)	1,250
Other operating cash flows	12,067	14,424	14,919	0	0
<b>Cash flow from operations</b>	<b>84,233</b>	<b>1,49,694</b>	<b>1,30,744</b>	<b>30,142</b>	<b>1,02,454</b>
Capital expenditures	(20,699)	(40,798)	(45,057)	(25,000)	(25,000)
Change in investments	47,973	0	0	0	0
Other investing cash flows	8,679	15,548	16,752	12,809	12,463
<b>Cash flow from investing</b>	<b>35,953</b>	<b>(25,250)</b>	<b>(28,305)</b>	<b>(12,191)</b>	<b>(12,537)</b>
Equities issued/Others	(1,21,435)	0	(1,05,000)	0	0
Debt raised/repaid	0	0	0	0	0
Interest expenses	(3,123)	0	0	0	0
Dividends paid	(5,420)	(10,840)	(11,469)	(10,277)	(11,092)
Other financing cash flows	0	0	0	0	0
<b>Cash flow from financing</b>	<b>(1,29,978)</b>	<b>(10,840)</b>	<b>(1,16,469)</b>	<b>(10,277)</b>	<b>(11,092)</b>
<b>Changes in cash and cash eq.</b>	<b>(9,792)</b>	<b>1,13,604</b>	<b>(14,029)</b>	<b>7,673</b>	<b>78,826</b>
<b>Closing cash and cash eq.</b>	<b>44,925</b>	<b>1,58,529</b>	<b>1,44,499</b>	<b>1,52,172</b>	<b>2,30,998</b>

### Per Share

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20A	FY21E	FY22E
Reported EPS	13.3	14.9	16.7	14.4	15.5
Adjusted EPS	13.3	14.9	16.7	14.4	15.5
Dividend per share	1.0	1.5	1.7	1.4	1.5
Book value per share	80.7	94.7	97.9	106.7	120.3

### Valuations Ratios

Y/E 31 Mar (x)	FY18A	FY19A	FY20A	FY21E	FY22E
EV/Sales	2.1	2.0	1.8	1.6	1.5
EV/EBITDA	10.7	9.5	8.7	8.7	7.8
Adjusted P/E	14.0	12.5	11.2	13.0	12.0
P/BV	2.3	2.0	1.9	1.7	1.6

### DuPont Analysis

Y/E 31 Mar (%)	FY18A	FY19A	FY20A	FY21E	FY22E
Tax burden (Net profit/PBT)	78.1	78.0	79.0	78.8	77.8
Interest burden (PBT/EBIT)	121.6	113.0	115.3	113.4	111.8
EBIT margin (EBIT/Revenue)	15.4	17.3	17.1	15.5	16.4
Asset turnover (Revenue/Avg TA)	70.3	73.9	75.2	74.6	71.9
Leverage (Avg TA/Avg Equity)	1.5	1.5	1.4	1.4	1.3
Adjusted ROAE	15.9	17.1	16.9	14.3	13.6

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

**Ratio Analysis**

Y/E 31 Mar	FY18A	FY19A	FY20A	FY21E	FY22E
<b>YoY growth (%)</b>					
Revenue	(1.4)	7.8	4.1	0.4	4.8
EBITDA	(6.6)	15.4	2.6	(7.2)	9.8
Adjusted EPS	4.0	12.3	11.6	(13.9)	7.9
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	19.3	20.7	20.4	18.8	19.7
EBIT margin	15.4	17.3	17.1	15.5	16.4
Adjusted profit margin	14.7	15.3	15.5	13.9	14.3
Adjusted ROAE	15.9	17.1	16.9	14.3	13.6
ROCE	14.0	18.6	20.7	18.0	18.7
<b>Working capital days (days)</b>					
Receivables	67	62	61	68	69
Inventory	3	3	2	2	4
Payables	100	109	113	103	95
<b>Ratios (x)</b>					
Gross asset turnover	8.1	8.7	8.1	7.4	7.4
Current ratio	2.2	2.5	2.3	3.0	3.4
Net interest coverage ratio	4.6	6.6	6.2	7.5	8.5
Adjusted debt/equity	0.2	(0.1)	(0.1)	(0.1)	(0.2)

Source: Company, BOBCAPS Research

## Disclaimer

### Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

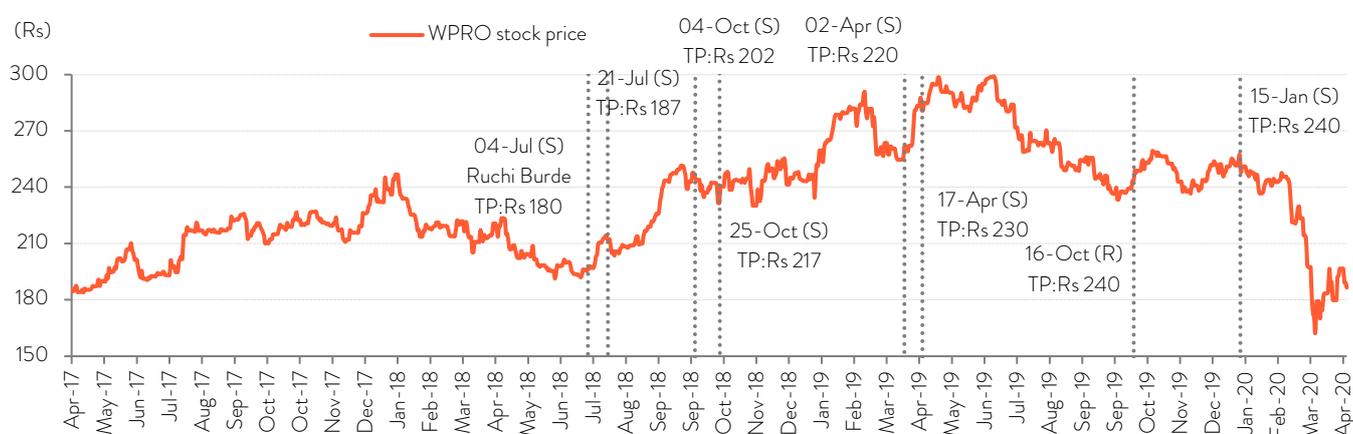
**ADD** – Expected return from >+5% to +15%

**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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