

BUY

TP: Rs 3,180 | ▲ 16%

**TATA CONSULTANCY
SERVICES**

| IT Services

| 08 October 2020

Demand recovery drives outperformance

TCS' growth of 7.2% USD outperformed street's estimates. The growth was broad-based driven by BFSI and life-sciences, along with surprising growth in retail. The demand recovery for FY21 has happened earlier than expected. Adjusted EBIT margin stood at 26.2%, growing 260bps QoQ. US \$8.6bn TCV is back to 96% of pre-covid levels. TCS announced buyback of 53.3mn shares at Rs 3,000/share. Factoring in demand recovery and buyback, we increase FY22/FY23 EPS by ~19%/23%, raising our Sep'22 TP to Rs 3,180. BUY.

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Recovery outperforms: TCS' QoQ growth of 7.2 % exceeded our expectation of 2.8% USD growth, registering its best QoQ growth in last twenty quarters. The recovery was driven by traction in BFSI, retail-cpg and life-sciences and healthcare which grew by 6.2%/8.8%/6.9%, cc, respectively. Cloud and digital demand lead to an earlier than expected demand recovery. TCS benefited from the vendor consolidation exercise of clients. The EBIT margin stood at 23.2%, impacted by ~Rs 1.2bn legal settlement for EPIC systems case vs. our estimate of 24.3%. Adjusted EBIT stood strong at 26.2%, growing by a stellar 260 bps QoQ. TCS will also be resuming its salary hike cycles for FY21.

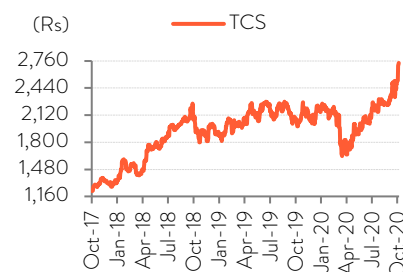
TCV back to pre-covid levels; pipeline healthy: TCV stood strong at US\$ 8.6bn bouncing, back to pre-covid level of US\$ 8.9bn. It grew 25% QoQ and 34% YoY. Pipeline is an even mix of large and small deals. Excluding the Phoenix deal win, the TCV stood at US\$ 6.1bn. Management is confident of H2FY21 growth despite uncertainties and seasonal weakness of Q3.

Buyback approved: TCS' board approved buyback of 53.3mn equity shares for an aggregate amount not exceeding Rs 160bn being 1.42% of the total paid-up equity share capital, at Rs 3,000/ share. This is similar to TCS' previous buyback of Rs 160bn in FY18. Interim dividend of Rs 12/share has been announced.

Ticker/Price	TCS IN/Rs 2,736
Market cap	US\$ 140.1bn
Shares o/s	3,753mn
3M ADV	US\$ 152.4mn
52wk high/low	Rs 2,770/Rs 1,506
Promoter/FPI/DII	72%/17%/11%

Source: NSE

STOCK PERFORMANCE



KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	1,464,630	1,569,490	1,673,534	2,135,763	2,487,379
EBITDA (Rs mn)	395,050	421,100	454,419	611,431	702,151
Adj. net profit (Rs mn)	315,240	323,400	327,360	450,338	517,277
Adj. EPS (Rs)	84.0	86.2	88.5	121.7	139.8
Adj. EPS growth (%)	25.3	2.6	2.7	37.6	14.9
Adj. ROAE (%)	35.5	37.0	36.7	44.3	42.2
Adj. P/E (x)	32.6	31.8	30.9	22.5	19.6
EV/EBITDA (x)	25.9	24.2	22.5	16.8	14.5

Source: Company, BOBCAPS Research

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FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)
Revenues (US\$ mn)	5,424	5,517	(1.7)	5,059	7.2
Revenue (Rs mn)	401,350	389,770	3.0	383,220	4.7
Operating Expenditure	298,400	287,510	3.8	282,970	5.5
Cost of revenues	229,580	224,100	2.4	224,860	2.1
as % of sales	57.2	57.5	-	58.7	-
SG&A expenses	68,820	63,410	8.5	58,110	18.4
as % of sales	17.1	16.3	-	15.2	-
EBITDA	102,950	102,260	0.7	100,250	2.7
Depreciation	9,980	8,650	15.4	9,770	2.1
EBIT	92,970	93,610	(0.7)	90,480	2.8
Other Income	7,400	11,680	(36.6)	4,560	62.3
PBT	100,370	105,290	(4.7)	95,040	5.6
Total Tax	25,330	24,710	2.5	24,550	3.2
Adjusted PAT	75,040	80,580	(6.9)	70,490	6.5
(Profit)/loss from JV's/Ass/MI	(290)	(160)	-	(410)	-
APAT after MI	74,750	80,420	(7.1)	70,080	6.7
Reported PAT	74,750	80,420	(7.1)	70,080	6.7
Reported EPS	19.9	21.4	(7.1)	18.7	6.7
Margins (%)			(bps)		(bps)
EBITDA	25.7	26.2	(60)	26.2	(50)
EBIT	23.2	24.0	(90)	23.6	(40)
EBT	25.0	27.0	(200)	24.8	20
PAT	18.6	20.6	(200)	18.3	30
Effective Tax rate	25.2	23.5	180	25.8	(60)

Source: BOBCAPS Research

FIG 2 – OPERATING METRICS

(In US\$ terms)	Q2FY21 (% Contr. to Revenue)	QoQ (%)	YoY (%)
Deal win TCW (US\$ mn)	8,600	24.6	34.4
Revenues by Geography			
Americas	49.9	4.1	(3.0)
UK	15.5	8.6	(2.3)
Europe	16.3	12.0	9.8
India	5.0	24.7	(13.8)
Asia Pac	9.7	6.1	1.5
Ibero America	1.7	7.2	1.9
MEA	1.9	7.2	(15.1)
Revenue breakup by Domain			
BFSI	31.9	8.6	1.2
Manufacturing	9.4	3.9	(5.7)
Telecom & Media	6.5	(1.8)	(8.7)
Life Sciences & Healthcare	9.8	9.4	18.9
Retail & CPG	14.6	11.8	(3.0)
Technology & Services	8.9	4.9	0.6
Regional Markets & Others	18.9	5.5	(9.8)
	Q2FY21	Q1FY21	Q2FY20
Attrition (LTM) (%)	8.9	11.1	11.6

Source: BOBCAPS Research

Valuation methodology

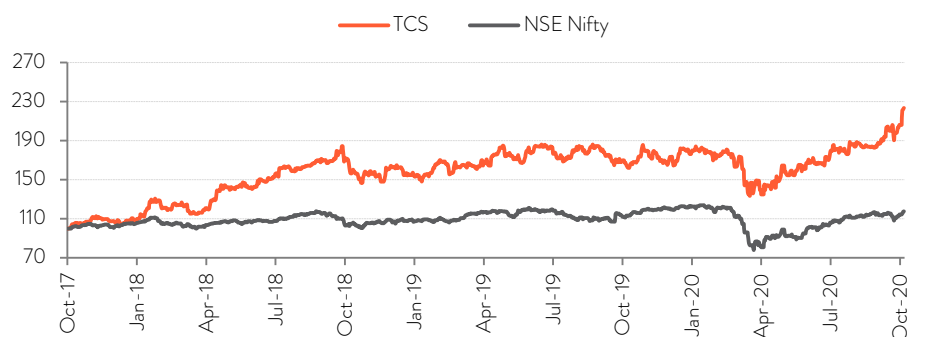
Following the sharp demand and margin recovery in Sep'20 quarter and incorporating the buyback worth Rs 160bn, we increase our FY21/22/23 EPS by 9.2%/19%/23%, respectively. Without buyback, the EPS increase stands at 7.7%/20%/23% for FY21/22/23. Retain BUY as we believe that TCS's strong structural backbone will lend it resilience over peers to recover from the crisis. We roll over to a new Sep'22 target price of Rs 3,180 (vs. Rs 2,620 earlier) based on an unchanged one-year forward P/E multiple of 24.2x.

FIG 3 – REVISED ESTIMATES

(Rs mn)	FY21E			FY22E			FY23E		
	Old	New	Change (%)	Old	New	Change (%)	Old	New	Change (%)
Revenues (US\$ mn)	20,852	22,215	6.5	23,296	27,382	17.5	26,059	31,889	22.4
YoY growth (%)	(5.4)	0.8	-	11.7	23.3	-	11.9	16.5	-
Revenues	1,591,402	1,673,534	5.2	1,817,106	2,135,763	17.5	2,032,632	2,487,379	22.4
EBITDA	424,612	454,419	7.0	511,077	611,431	19.6	571,048	702,151	23.0
EBITDA margins (%)	26.7	27.2	-	28.1	28.6	-	28.1	28.2	-
Net profits	304,048	327,360	7.7	383,401	450,338	17.5	427,497	517,277	21.0
EPS (Rs)	81.0	88.5	9.2	102.2	121.7	19.2	113.9	139.8	22.7

Source: BOBCAPS Research

FIG 4 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

Key downside risks to our estimates are:

- non-conversion of TCV
- another wave of Covid-19,
- a sharp decline in IT spending, and
- inability to refresh service offerings amid rapidly changing technologies.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	1,464,630	1,569,490	1,673,534	2,135,763	2,487,379
EBITDA	395,050	421,100	454,419	611,431	702,151
Depreciation	20,550	35,300	38,862	40,905	45,048
EBIT	374,500	385,800	415,557	570,526	657,103
Net interest income/(expenses)	0	0	0	0	0
Other income/(expenses)	41,130	36,680	20,551	22,813	24,313
Exceptional items	0	0	0	0	0
EBT	415,630	422,480	436,108	593,339	681,417
Income taxes	100,010	98,010	107,648	142,401	163,540
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	(380)	(1,070)	(1,100)	(600)	(600)
Reported net profit	315,240	323,400	327,360	450,338	517,277
Adjustments	0	0	0	0	0
Adjusted net profit	315,240	323,400	327,360	450,338	517,277

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	0	0	0	0	0
Other current liabilities	250,000	292,440	288,857	368,639	429,328
Provisions	0	0	0	0	0
Debt funds	440	69,060	69,060	69,060	69,060
Other liabilities	0	0	0	0	0
Equity capital	3,750	3,750	3,750	3,750	3,750
Reserves & surplus	0	0	0	0	0
Shareholders' fund	898,990	847,490	938,359	1,092,504	1,361,364
Total liabilities and equities	1,149,430	1,208,990	1,296,276	1,530,203	1,859,752
Cash and cash eq.	72,240	86,460	79,778	176,653	363,746
Accounts receivables	273,460	305,320	366,802	409,598	477,032
Inventories	0	0	0	0	0
Other current assets	243,530	239,510	275,101	351,084	408,884
Investments	349,540	273,760	273,760	273,760	273,760
Net fixed assets	113,740	198,410	193,019	194,829	199,529
CWIP	0	0	0	0	0
Intangible assets	18,790	19,930	19,930	19,930	19,930
Deferred tax assets, net	26,560	28,280	28,280	28,280	28,280
Other assets	51,570	57,320	59,605	76,068	88,592
Total assets	1,149,430	1,208,990	1,296,276	1,530,203	1,859,753

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	236,600	359,770	367,322	491,843	562,924
Interest expenses	(25,640)	(36,680)	(20,551)	(22,813)	(24,313)
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(21,690)	8,850	(102,942)	(55,460)	(77,066)
Other operating cash flows	96,660	(2,965)	0	0	0
Cash flow from operations	285,930	328,975	243,829	413,569	461,545
Capital expenditures	(21,320)	(119,970)	(33,471)	(42,715)	(49,748)
Change in investments	73,820	(75,780)	0	0	0
Other investing cash flows	(36,050)	36,680	20,551	22,813	24,313
Cash flow from investing	16,450	(159,070)	(12,920)	(19,902)	(25,434)
Equities issued/Others	0	0	(80,000)	(80,000)	0
Debt raised/repaid	(1,940)	0	0	0	0
Interest expenses	(162,310)	0	0	0	0
Dividends paid	(114,720)	(155,685)	(157,591)	(216,793)	(249,017)
Other financing cash flows	0	0	0	0	0
Cash flow from financing	(278,970)	(155,685)	(237,591)	(296,793)	(249,017)
Changes in cash and cash eq.	23,410	14,220	(6,682)	96,875	187,093
Closing cash and cash eq.	72,240	86,460	79,778	176,653	363,746

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	84.0	86.2	88.5	121.7	139.8
Adjusted EPS	84.0	86.2	88.5	121.7	139.8
Dividend per share	30.0	34.5	35.4	48.7	55.9
Book value per share	239.5	225.8	253.6	295.3	368.0

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	7.0	6.5	6.1	4.8	4.1
EV/EBITDA	25.9	24.2	22.5	16.8	14.5
Adjusted P/E	32.6	31.8	30.9	22.5	19.6
P/BV	11.4	12.1	10.8	9.3	7.4

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	75.8	76.5	75.1	75.9	75.9
Interest burden (PBT/EBIT)	111.0	109.5	104.9	104.0	103.7
EBIT margin (EBIT/Revenue)	25.6	24.6	24.8	26.7	26.4
Asset turnover (Revenue/Avg TA)	131.1	133.1	133.6	151.1	146.7
Leverage (Avg TA/Avg Equity)	1.3	1.4	1.4	1.4	1.4
Adjusted ROAE	35.5	37.0	36.7	44.3	42.2

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

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	19.0	7.2	6.6	27.6	16.5
EBITDA	21.5	6.6	7.9	34.6	14.8
Adjusted EPS	25.3	2.6	2.7	37.6	14.9
Profitability & Return ratios (%)					
EBITDA margin	27.0	26.8	27.2	28.6	28.2
EBIT margin	25.6	24.6	24.8	26.7	26.4
Adjusted profit margin	21.5	20.6	19.6	21.1	20.8
Adjusted ROAE	35.5	37.0	36.7	44.3	42.2
ROCE	34.3	35.8	35.6	45.3	48.7
Working capital days (days)					
Receivables	65	67	73	66	65
Inventory	0	0	0	0	0
Payables	78	86	87	79	82
Ratios (x)					
Gross asset turnover	12.8	10.1	8.6	11.0	12.6
Current ratio	2.6	2.4	2.7	2.7	3.1
Net interest coverage ratio	NA	NA	NA	NA	NA
Adjusted debt/equity	(0.1)	0.0	0.0	(0.1)	(0.2)

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

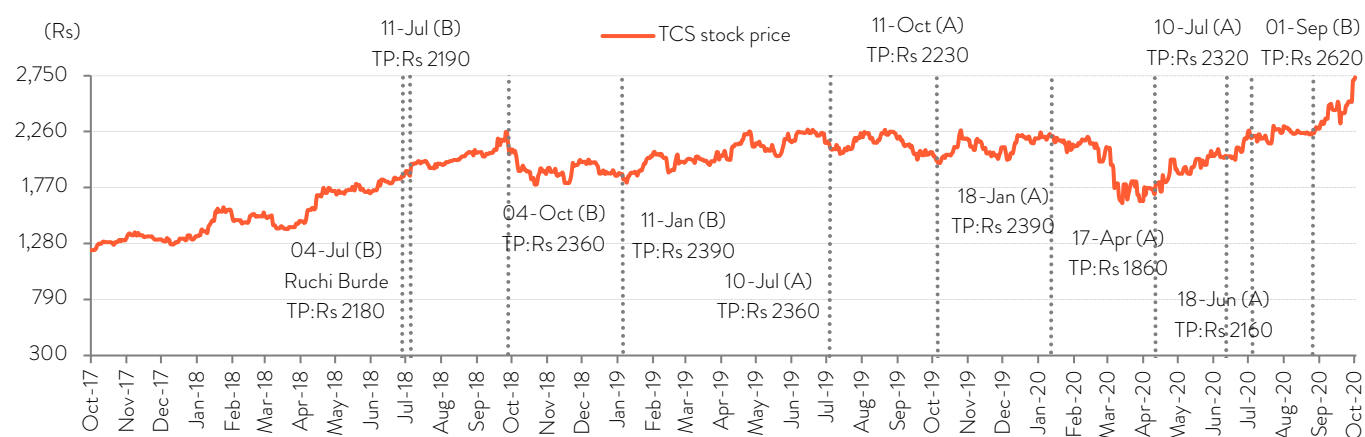
ADD – Expected return from >+5% to +15%

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)

RATINGS AND TARGET PRICE (3-YEAR HISTORY): TATA CONSULTANCY SERVICES (TCS IN)



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

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