

ADD

TP: Rs 450 | ▲ 7%

WIPRO

| IT Services

| 05 March 2021

Bold Capco acquisition

The Capco acquisition, Wipro's (WPRO) largest to date, for a cash consideration of US\$ 1.45bn is another of CEO Thierry's bold moves to achieve industry-leading growth. Although EBIT margin-dilutive, the buyout will strengthen the BFSI vertical and help WPRO bag large deals. Factoring in ~US\$ 700mn of annual revenue from the acquisition and ~2% EBIT margin dilution, we change FY22/FY23 EPS by -3%/+15% and raise our target P/E to 18.8x (vs. 17.2x). Upgrade from SELL to ADD as we roll to a new Mar'22 TP of Rs 450 (vs. Rs 350).

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BFSI strengthened: WPRO's management expects the acquisition of UK-based Capco to strengthen its capabilities in BFSI in terms of scale, delivery, digital workforce skills and global presence. Management estimates that post acquisition BFSI revenue will be on track to increase from US\$ 2.5bn to US\$ 3.2bn. Capco brings expertise in banking and payments, wealth management, insurance and capital markets. It also brings a global footprint and strong foothold in Europe (41% exposure) which has been one of Thierry Delaporte's focus areas. Its client roster includes 100 global enterprises that will be of strategic importance to WPRO.

Deal win impetus: Scale matters when it comes to bagging large deals in BFSI and hence WPRO has undertaken this acquisition to pursue contracts in the order of billions of dollars. Since Thierry's induction into WPRO, he has pursued large deals aggressively to accelerate growth. WPRO has also appointed a new Chief Growth Officer to achieve its growth ambitions.

EBIT margin dilution: WPRO expects the acquisition to be EBIT margin-dilutive by ~2% for the first year and EPS-accretive from the third year. We see EPS upsides by FY23 due to the technology demand upcycle, revenue plus cost-based synergies and large-deal acceleration. Management will, however, need to work on the consulting segment as it has been hit by the Covid crisis.

Ticker/Price	WPRO IN/Rs 421
Market cap	US\$ 32.9bn
Shares o/s	5,715mn
3M ADV	US\$ 89.9mn
52wk high/low	Rs 467/Rs 159
Promoter/FPI/DII	74%/9%/17%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	589,060	613,401	620,057	739,371	852,836
EBITDA (Rs mn)	121,661	124,867	138,710	149,397	185,472
Adj. net profit (Rs mn)	90,074	95,295	103,797	105,900	133,774
Adj. EPS (Rs)	14.9	16.7	18.4	18.8	23.7
Adj. EPS growth (%)	12.3	11.6	10.5	2.0	26.3
Adj. ROAE (%)	17.1	16.9	18.6	17.6	18.9
Adj. P/E (x)	28.2	25.2	22.8	22.4	17.7
EV/EBITDA (x)	20.5	19.4	16.9	15.9	12.7

Source: Company, BOBCAPS Research

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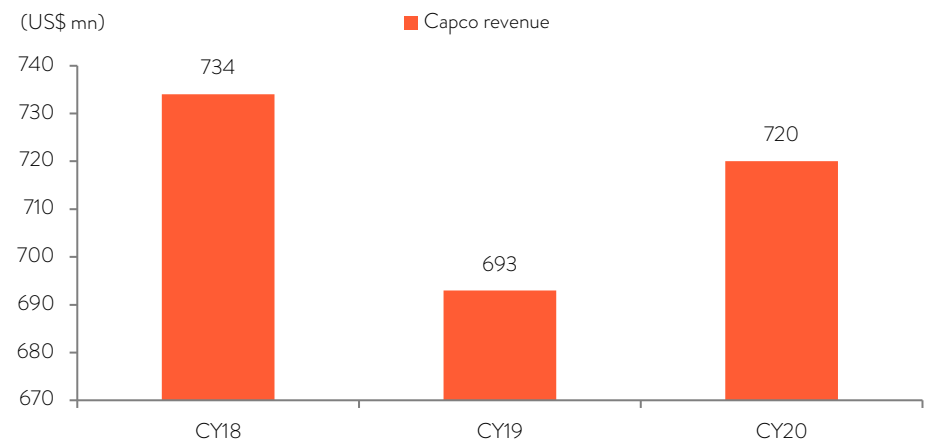


Capco acquisition

About Capco

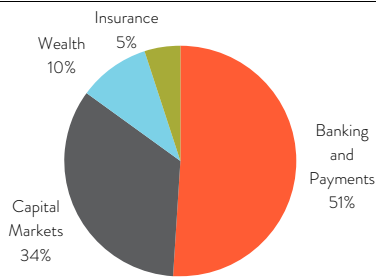
Founded in 1998, UK-based Capco is a global financial services management consultancy that specialises in driving digital transformation, with CY20 revenue of ~US\$ 700mn. It has headquarters in London and a global presence across 30 locations in 16 countries. The company has exposure to various subsegments of BFSI such as banking and payments, capital markets, wealth and insurance.

FIG 1 – CAPCO’S HISTORICAL REVENUE



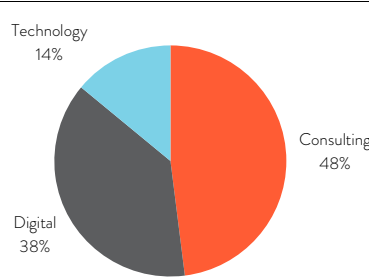
Source: BOBCAPS Research, Company

FIG 2 – REVENUE BY SECTOR



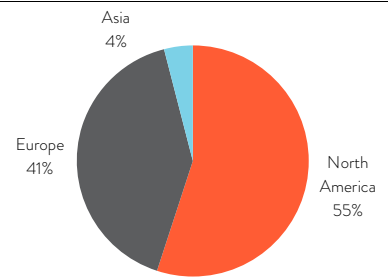
Source: BOBCAPS Research, Company

FIG 3 – REVENUE BY SERVICE



Source: BOBCAPS Research, Company

FIG 4 – REVENUE BY GEOGRAPHY



Source: BOBCAPS Research, Company

Acquisition details

- The Capco acquisition is the largest in WPRO’s history and entails a cash consideration of US\$ 1,450mn (17.6% of WPRO’s FY20 revenues).
- Financing will be through internal cash and debt. The transaction is expected to close by end-Q1FY22.
- A total of 5,000 employees will be added to WPRO’s workforce.

- Management expects the acquisition to be EBIT margin-dilutive by ~2% in Year 1.
- Cash EPS will be impacted in Year 1 with the deal guided to turn EPS-accretive from Year 3 based on projected synergies.

New CEO's initiatives to pave way for growth

Key senior management changes

Over the last few months, WPRO has hired several senior leaders from global IT giants such as DXC Technology, Accenture, Capgemini and Cognizant as it aspires to reenter the big league. Among the new appointees are Pierre Bruno as CEO for Europe and Stephanie Trautman as Chief Growth Officer – a new position created solely to focus on accelerating WPRO's growth.

FIG 5 – RECENT KEY SENIOR MANAGEMENT HIRES

Name	Designation	Comment
Pierre Bruno	CEO - Europe	Ex-DXC Technology
Stephanie Trautman	Chief Growth Officer	Ex-Accenture
Graziella Neuveglise	Regional Head - Southern Europe	Ex-Accenture and Capgemini
Rene Mulder	Country Head - Switzerland	Ex-DXC Technology
Douglas Silva	Country Head - Brazil	Ex-AWS, Capgemini, SAP and TCS
Tomoaki Takeuchi	Country Manager - Japan	Ex-Cognizant

Source: BOBCAPS Research, Company

Deal win acceleration

After winning the US\$ 700mn Metro AG deal in Q3FY21, WPRO has bagged more large contracts. We expect the Capco acquisition to accelerate large deal wins in the company's BFSI vertical.

FIG 6 – RECENT LARGE DEAL WINS AND PARTNERSHIPS

Geography	Duration	Client	Description
Germany	5 years	Telefonica Germany (O2)	To work towards transforming O2's business support systems and enable superior customer experience
US	Multiyear	Fiat Chrysler	To source and build a talent pool of more than 1,000 skilled consultants and technologists for FCA ICT India who will help develop capabilities around futuristic technologies

Source: BOBCAPS Research, Company

Valuation methodology

The Capco acquisition is the biggest in WPRO's history and will strengthen its BFSI vertical. With a multiyear technology upcycle underway, the demand outlook for BFSI looks robust and WPRO will have the advantage of complementary expertise in the vertical via this acquisition. Though the integration process will take time to bear fruit, we believe it is a step in the right direction.

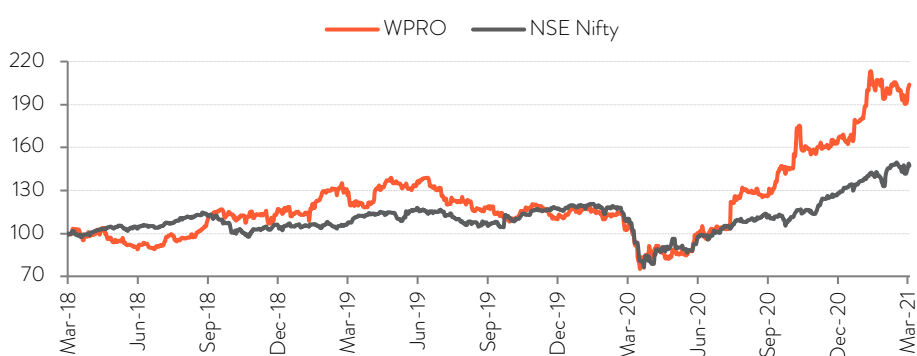
We adjust our FY22/FY23 EPS estimates by -3%/+15% factoring in margin dilution for FY22 and Capco revenue flowthrough. On rollover, we move to a revised Mar'22 target price of Rs 450 (from Rs 350), set at a higher one-year forward P/E multiple of 18.8x (17.2x earlier), which is based on the last five-year average P/E + 1sd. The revision in multiple comes on the back of a slew of measures taken by WPRO's management to improve growth. Upgrade from SELL to ADD.

FIG 7 – REVISED ESTIMATES

(Rs mn)	FY21E			FY22E			FY23E		
	Old	New	Change (%)	Old	New	Change (%)	Old	New	Change (%)
IT Services revenues (US\$ mn)	8,122	8,122	0.0	8,981	9,562	6.5	9,707	10,650	9.7
IT Services revenues (US\$ mn), YoY growth (%)	(1.6)	(1.6)	-	10.6	17.7	-	8.1	11.4	-
Company-wide revenues	624,397	620,057	(0.7)	704,142	739,371	5.0	779,291	852,836	9.4
EBIT	119,030	118,249	(0.7)	129,238	124,998	(3.3)	134,469	157,328	17.0
EBIT margins (%)	19.1	19.1	-	18.4	16.9	-	17.3	18.4	-
Net profits	104,406	103,797	(0.6)	108,930	105,900	(2.8)	116,338	133,774	15.0
EPS (Rs)	18.5	18.4	(0.6)	19.3	18.8	(2.8)	20.6	23.7	15.0

Source: BOBCAPS Research

FIG 8 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

Key downside risks to our estimates are:

- synergies taking long to materialise,
- high competition, and
- sustained low operating margins.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	589,060	613,401	620,057	739,371	852,836
EBITDA	121,661	124,867	138,710	149,397	185,472
Depreciation	19,474	20,281	20,462	24,399	28,144
EBIT	102,187	104,586	118,249	124,998	157,328
Net interest income/(expenses)	15,548	16,752	15,898	10,793	14,548
Other income/(expenses)	0	0	0	0	0
Exceptional items	0	0	0	0	0
EBT	115,458	120,589	134,147	135,791	171,876
Income taxes	25,242	24,799	29,604	29,690	37,902
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	142	495	746	200	200
Reported net profit	90,074	95,295	103,797	105,900	133,774
Adjustments	0	0	0	0	0
Adjusted net profit	90,074	95,295	103,797	105,900	133,774

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	0	0	0	0	0
Other current liabilities	158,894	156,761	137,602	164,079	189,260
Provisions	640	612	1,529	1,823	2,103
Debt funds	99,467	78,042	78,042	78,042	78,042
Other liabilities	3,417	2,825	2,825	2,825	2,825
Equity capital	12,068	11,427	10,952	10,952	10,952
Reserves & surplus	558,685	547,906	545,432	638,787	756,661
Shareholders' fund	570,753	559,333	556,384	649,739	767,613
Total liabilities and equities	833,171	797,573	776,382	896,509	1,039,843
Cash and cash eq.	158,529	144,499	82,579	154,315	252,251
Accounts receivables	100,489	104,474	127,409	133,694	154,211
Inventories	3,951	1,865	5,096	6,077	7,010
Other current assets	129,457	108,891	118,915	156,990	181,082
Investments	233,798	203,345	203,345	204,795	204,795
Net fixed assets	70,601	81,120	85,658	87,259	87,115
CWIP	0	0	0	0	0
Intangible assets	130,742	147,374	147,374	147,374	147,374
Deferred tax assets, net	5,604	6,005	6,005	6,005	6,005
Other assets	0	0	0	0	0
Total assets	833,171	797,573	776,382	896,509	1,039,843

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	109,690	116,071	125,005	130,500	162,118
Interest expenses	(15,548)	(16,752)	(15,898)	(10,793)	(14,548)
Non-cash adjustments	0	0	0	0	0
Changes in working capital	41,128	16,506	(54,433)	(18,569)	(20,082)
Other operating cash flows	14,424	14,919	0	0	0
Cash flow from operations	149,694	130,744	54,673	101,138	127,488
Capital expenditures	(40,798)	(45,057)	(25,000)	(26,000)	(28,000)
Change in investments	0	0	0	(1,450)	0
Other investing cash flows	15,548	16,752	15,898	10,793	14,548
Cash flow from investing	(25,250)	(28,305)	(9,102)	(16,657)	(13,452)
Equities issued/Others	0	(105,000)	(95,000)	0	0
Debt raised/repaid	0	0	0	0	0
Interest expenses	0	0	0	0	0
Dividends paid	(10,840)	(11,469)	(12,492)	(12,745)	(16,100)
Other financing cash flows	0	0	0	0	0
Cash flow from financing	(10,840)	(116,469)	(107,492)	(12,745)	(16,100)
Changes in cash and cash eq.	113,604	(14,029)	(61,920)	71,736	97,936
Closing cash and cash eq.	158,529	144,499	82,579	154,315	252,251

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	14.9	16.7	18.4	18.8	23.7
Adjusted EPS	14.9	16.7	18.4	18.8	23.7
Dividend per share	1.5	1.7	1.8	1.9	2.4
Book value per share	94.7	97.9	98.7	115.3	136.2

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	4.2	3.9	3.8	3.2	2.8
EV/EBITDA	20.5	19.4	16.9	15.9	12.7
Adjusted P/E	28.2	25.2	22.8	22.4	17.7
P/BV	4.4	4.3	4.3	3.7	3.1

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	78.0	79.0	77.4	78.0	77.8
Interest burden (PBT/EBIT)	113.0	115.3	113.4	108.6	109.2
EBIT margin (EBIT/Revenue)	17.3	17.1	19.1	16.9	18.4
Asset turnover (Revenue/Avg TA)	73.9	75.2	78.8	88.4	88.1
Leverage (Avg TA/Avg Equity)	1.5	1.4	1.4	1.4	1.4
Adjusted ROAE	17.1	16.9	18.6	17.6	18.9

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

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	7.8	4.1	1.1	19.2	15.3
EBITDA	15.4	2.6	11.1	7.7	24.1
Adjusted EPS	12.3	11.6	10.5	2.0	26.3
Profitability & Return ratios (%)					
EBITDA margin	20.7	20.4	22.4	20.2	21.7
EBIT margin	17.3	17.1	19.1	16.9	18.4
Adjusted profit margin	15.3	15.5	16.7	14.3	15.7
Adjusted ROAE	17.1	16.9	18.6	17.6	18.9
ROCE	18.6	20.7	22.5	22.1	26.8
Working capital days (days)					
Receivables	62	61	68	64	62
Inventory	3	2	3	3	3
Payables	109	113	107	90	93
Ratios (x)					
Gross asset turnover	8.7	8.1	7.4	8.6	9.8
Current ratio	2.5	2.3	2.4	2.7	3.1
Net interest coverage ratio	6.6	6.2	7.4	11.6	10.8
Adjusted debt/equity	(0.1)	(0.1)	0.0	(0.1)	(0.2)

Source: Company, BOBCAPS Research

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Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

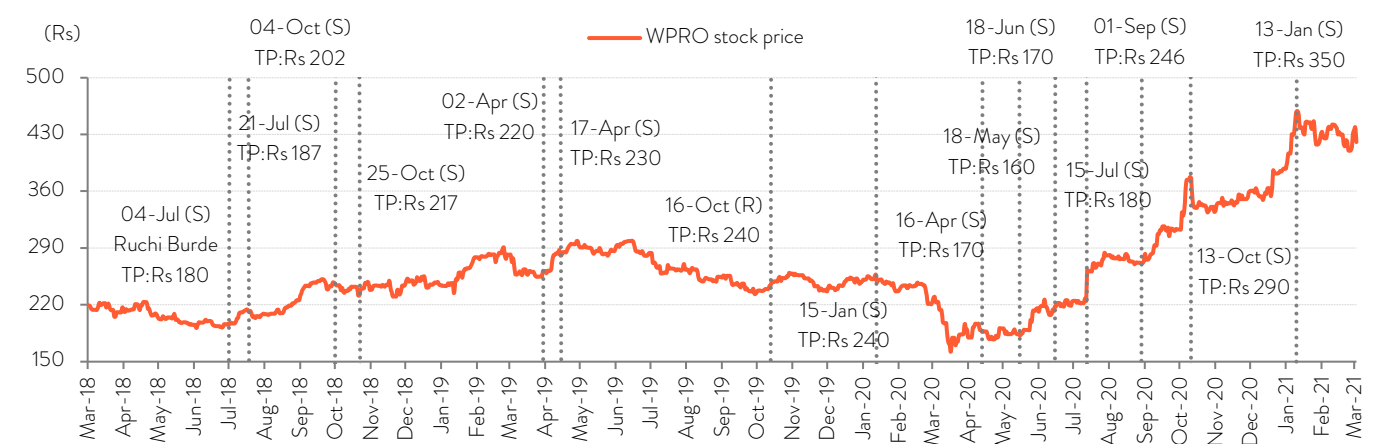
ADD – Expected return from >+5% to +15%

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): WIPRO (WPRO IN)



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

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