Tata Consultancy Services

BUY

INDUSTRY	IT
CMP *(as on 10 July 2018)*	Rs 1,875
Target Price	Rs 2,130
Nifty	10,947
Sensex	36,240
KEY STOCK DATA	
Bloomberg	TCS IN
No. of Shares (mn)	3,829
MCap (Rs bn) / ($ mn)	7,179/104,321
6m avg traded value (Rs mn)	7,259

STOCK PERFORMANCE (%)

52 Week high / low	Rs 1,930 / 1,167		
	3M	6M	12M
Absolute (%)	27.7	33.6	54.0
Relative (%)	20.7	28.4	39.8

SHAREHOLDING PATTERN (%)	
Promoters	71.92
FIs & Local MFs	6.65
FPIs	16.95
Public & Others	4.48

Source : BSE

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Better late than never

Our optimism has admittedly trailed TCS' recent performance. Our (belated) upgrade derives from confidence on TCS' growth trajectory, supported by (1) Scale and growth dominance of Digital business (25% of rev and 45.5% YoY), (2) Growth visibility (deal wins), (3) Strong recovery and outlook in BFSI vertical (across geos) and NorthAm geography and (4) Continuity in efficient capital allocation (80 to 100% of FCF as payout).

1QFY19 was inspiring (CC rev +4.1% QoQ) with revival in TCS' core vertical (BFSI) and geography (NorthAm). Reported revenue at USD 5,051mn, +1.6/10.0% QoQ/YoY was hit by cross currency impact. BFSI and NorthAm grew at 3.7% QoQ CC each (11/12-qtr high). EBIT margin was in-line at 25% (-36bps QoQ) as rising and INR depreciation offset wage hikes. APAT at Rs 73.62bn was boosted by higher other income.

Book-to-bill stood at 0.97x, with USD 4.9bn deal TCV in 1Q (includes USD 1.6bn from BFSI).

Our estimates rise ~3% as we build in USD rev/EPS at 10/14% CAGR over FY18-20E. We have factored USD rev growth of 10% and 10.1% for FY19/20E, implying 2.3/2.4% CQGR, respectively. EBIT at 25.5/26.2% is rock steady. Upgrade to BUY (Neutral earlier) with TP of Rs 2,130, 24x FY20E (20% premium to its 5-yr avg. valuations), supported by ~4.5% FCF yield and >60% RoIC.

Highlights of the quarter

- (1) TCS' >USD 100mn client band posted strongest sequential increase in last nine qtrs taking the count to 40, (2) Net headcount additions (5,877 adds in 1Q as compared to 7,775 in FY18) were the strongest in last five quarters taking the headcount to 400,875, (3) Demand environment strong across NorthAm (USD 2.7bn TCV in 1Q) and Europe.
- **Near-term outlook:** Growth trajectory expected to remain strong and margin expected to trend towards the target band as currency tailwinds persist.

Financial Summary (Consolidated)

(Rs bn)	1QFY19	1QFY18	*YoY (%)*	4QFY18	*QoQ (%)*	FY16	FY17	FY18	FY19E	FY20E
Net Revenue	342.61	295.84	*15.8*	320.75	*6.8*	1,086.46	1,179.66	1,231.04	1,418.40	1,559.24
EBIT	85.78	69.14	*24.1*	81.47	*5.3*	287.89	303.24	305.02	362.28	409.90
APAT	73.62	59.50	*23.7*	69.25	*6.3*	242.69	262.89	258.26	299.87	333.27
Diluted AEPS (Rs)	19.2	15.5	*23.5*	18.0	*6.3*	123.5	133.4	134.9	79.5	88.8
P/E (x)						30.4	28.1	27.8	23.6	21.1
EV / EBITDA (x)						22.0	20.4	20.3	17.2	15.0
RoE (%)						39.9	33.4	30.1	35.5	37.6

Source: Company, HDFC sec Inst Research

Revenue came at USD 5,051mn, 4.1/9.3% QoQ/YoY in CC terms with best sequential performance in last 15 qtrs

EBIT% came at 25%, -36bps QoQ (25% est.) with -180bps QoQ impact of wage increase offset by INR depreciation (+70bps impact) and higher efficiencies (+70bps impact)

Quarterly Consolidated Financials Snapshot

Particulars (Rs bn)	1QFY19	1QFY18	YoY (%)	4QFY18	QoQ (%)
Net Revenues (USD mn)	**5,051**	**4,591**	***10.0***	**4,972**	***1.6***
Net Revenues	**342.61**	**295.84**	***15.8***	**320.75**	***6.8***
Employee Expenses	185.48	161.83	*14.6*	171.83	*7.9*
SG&A And Other Operating Expenses	66.42	59.88	*10.9*	62.40	*6.4*
EBITDA	**90.71**	**74.13**	***22.4***	**86.52**	***4.8***
Depreciation	4.93	4.99	*(1.2)*	5.05	*(2.4)*
EBIT	**85.78**	**69.14**	***24.1***	**81.47**	***5.3***
Interest Cost	0.17	0.27	*(37.0)*	0.12	*41.7*
Other Income	12.25	9.59	*27.7*	9.94	*23.2*
PBT	**97.86**	**78.46**	***24.7***	**91.29**	***7.2***
Tax	24.24	18.96	*27.8*	22.04	*10.0*
APAT	**73.62**	**59.50**	***23.7***	**69.25**	***6.3***
E/o (adj for tax)	-	-		-	
RPAT	73.62	59.50	*23.7*	69.25	*6.3*

Source: Company, HDFC sec Inst Research

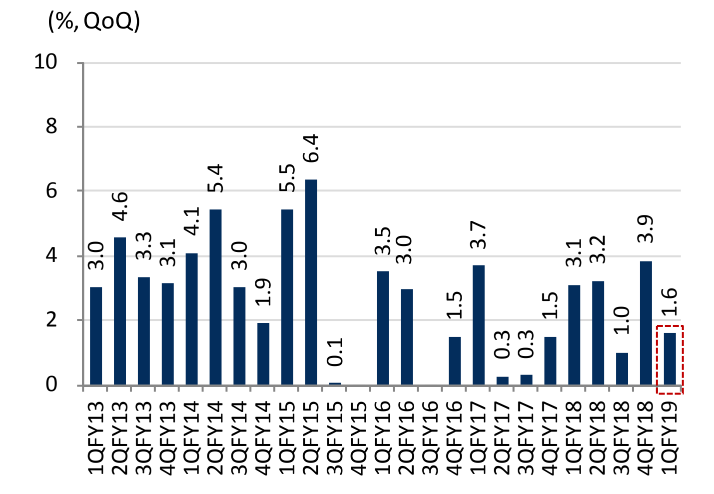
Margin Analysis

Particulars	1QFY19	1QFY18	YoY (bps)	4QFY18	QoQ (bps)
Employee Expenses % Net Revenues	54.1	54.7	*(56)*	53.6	*57*
SG&A And Other Expenses % Net Revenues	19.4	20.2	*(85)*	19.5	*(7)*
EBITDA Margin (%)	26.5	25.1	*142*	27.0	*(50)*
EBIT Margin (%)	**25.0**	**23.4**	***167***	**25.4**	***(36)***
Tax Rate (%)	24.8	24.2	*60*	24.1	*63*
APAT Margin (%)	21.5	20.1	*138*	21.6	*(10)*

Source: Company, HDFC sec Inst Research

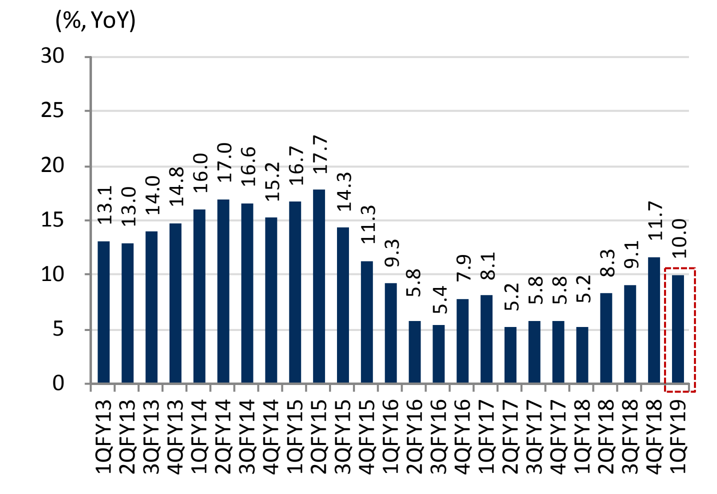
Digital stood at 25% of revenue and grew 6.7% QoQ and 45.5% YoY

QoQ USD Revenue Growth Trajectory



Source: Company, HDFC sec Inst Research

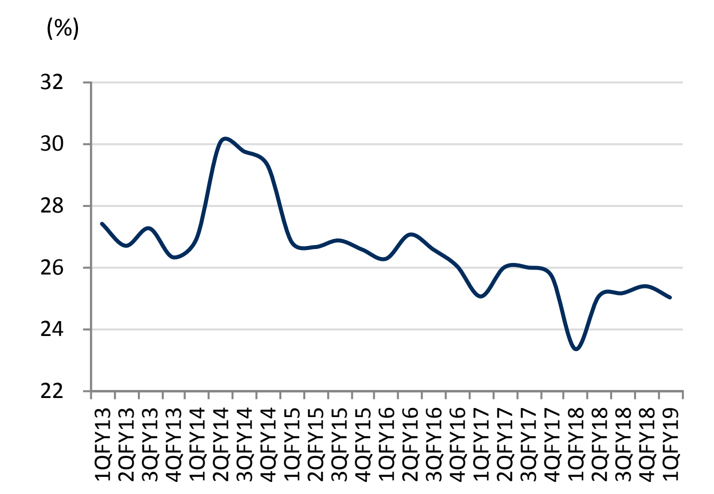
YoY USD Revenue Growth Trajectory



Source: Company, HDFC sec Inst Research

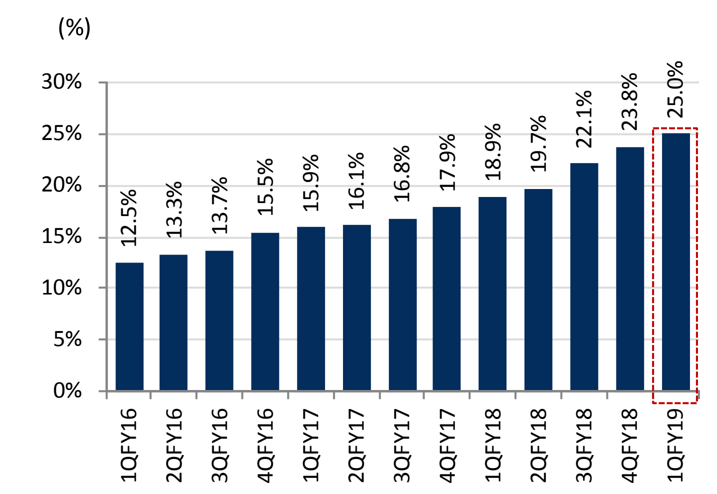
Digital revenue crossed USD 5bn revenue annual rate and has grown 2.5x in the past three yrs

EBIT Margin Trajectory



Source: Company, HDFC sec Inst Research

Digital % Of Revenue



Source: Company, HDFC sec Inst Research

Growth was broad-based across verticals with BFSI and Retail & CPG posting 3.7% and 3.6% QoQ in CC terms

Communication & Media (strong acceleration) and E&U verticals led the growth at 5.1% and 5.2% QoQ in CC terms

Vertical Revenue Break-up

(% of revenue)	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19
BFSI	NA	NA	32.5	32.6	31.6	31.1	31.1
Retail & CPG	NA	NA	16.0	15.9	16.7	16.6	16.6
Communication & Media	NA	NA	7.1	7.1	7.1	7.1	7.1
Life Science & Healthcare	NA	NA	7.1	7.2	7.3	7.2	7.3
Manufacturing	NA	NA	7.4	7.4	7.5	7.4	7.3
Energy & Utilities	NA	NA	4.0	4.2	4.5	4.8	4.8
Technology & Services	NA	NA	7.9	8.0	7.9	7.8	7.7
Regional Markets & Others	NA	NA	18.0	17.6	17.4	18.0	18.1
Total	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Source: Company, HDFC Sec Inst Research

Vertical-wise Revenue Growth

(QoQ, %)	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19
BFSI	NA	NA	NA	3.5	(2.1)	2.2	1.6
Retail & CPG	NA	NA	NA	2.6	6.1	3.2	1.6
Communication & Media	NA	NA	NA	3.2	1.0	3.9	1.6
Life Science & Healthcare	NA	NA	NA	4.8	2.4	2.4	3.0
Manufacturing	NA	NA	NA	3.2	2.4	2.5	0.2
Energy & Utilities	NA	NA	NA	9.6	8.2	10.8	1.6
Technology & Services	NA	NA	NA	4.1	(0.2)	2.5	0.3
Regional Markets & Others	NA	NA	NA	0.9	(0.1)	7.4	2.2
Total	**NA**	**NA**	**NA**	**3.2**	**1.0**	**3.9**	**1.6**

Source: Company, HDFC Sec Inst Research

Europe led the growth with UK posting 8.2% QoQ CC and Continental Europe growth at 5.3% QoQ CC

NorthAm growth of 3.7% QoQ was its fastest growth in the past 11 qtrs

Geographic Revenue Break-up

(% of revenue)	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19
Americas	**57.2**	**55.4**	**54.6**	**54.1**	**54.2**	**52.2**	**52.9**
North America	*55.0*	*53.3*	*52.5*	*51.9*	*52.0*	*50.2*	*51.0*
Latin America	*2.2*	*2.1*	*2.1*	*2.2*	*2.2*	*2.0*	*1.9*
Europe	**24.4**	**25.5**	**26.4**	**27.4**	**27.6**	**29.4**	**29.5**
UK	*13.3*	*13.7*	*13.9*	*14.0*	*14.1*	*15.2*	*15.5*
Continental Europe	*11.1*	*11.8*	*12.5*	*13.4*	*13.5*	*14.2*	*14.0*
India	6.3	6.8	7.0	6.3	6.3	6.2	5.8
Asia-Pacific	9.6	9.7	9.5	9.8	9.5	9.7	9.6
Middle East and Africa	2.5	2.6	2.5	2.4	2.4	2.5	2.2
Total	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Source: Company, HDFC Sec Inst Research

Geographic Revenue Growth

(QoQ, %)	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19
Americas	**2.4**	**(1.7)**	**1.6**	**2.3**	**1.2**	**0.0**	**3.0**
North America	*2.2*	*(1.7)*	*1.6*	*2.0*	*1.2*	*0.3*	*3.2*
Latin America	*10.3*	*(3.1)*	*3.1*	*8.1*	*1.0*	*(5.6)*	*(3.5)*
Europe	**(4.4)**	**6.1**	**6.8**	**7.1**	**1.8**	**10.6**	**1.9**
UK	*(3.3)*	*4.5*	*4.6*	*4.0*	*1.7*	*12.0*	*3.6*
Continental Europe	*(5.7)*	*7.9*	*9.2*	*10.7*	*1.8*	*9.3*	*0.2*
India	8.9	9.5	6.2	(7.1)	1.0	2.2	(5.0)
Asia-Pacific	(5.6)	2.5	1.0	6.5	(2.1)	6.1	0.5
Middle East and Africa	4.5	5.5	(0.8)	(0.9)	1.0	8.2	(10.6)
Total	**0.3**	**1.5**	**3.1**	**3.2**	**1.0**	**3.9**	**1.6**

Source: Company, HDFC Sec Inst Research

Change In Estimates

Particulars	Earlier estimates	Revised estimates	% change
FY19E			
Revenue (USD mn)	20,787	20,989	*1.0*
Revenue (Rs bn)	1,400.59	1,418.40	*1.3*
EBIT (Rs bn)	360.25	362.28	*0.6*
EBIT margin (%)	*25.7*	*25.5*	*(18)bps*
EPS (Rs)	78.5	79.5	*1.3*
FY20E			
Revenue (USD mn)	22,594	23,100	*2.2*
Revenue (Rs bn)	1,525.13	1,559.24	*2.2*
EBIT (Rs bn)	396.72	409.90	*3.3*
EBIT margin (%)	*26.0*	*26.3*	*28bps*
EPS (Rs)	85.8	88.8	*3.5*

Source: HDFC sec Inst Research

Key Assumptions

Particulars	FY15	FY16	FY17	FY18	FY19E	FY20E
Volume Growth (%)	16.7	8.6	7.1	8.5	6.3	6.7
Pricing Change (%)	(1.5)	(1.5)	(0.8)	0.1	3.4	3.1
USD Revenue Growth (%)	15.0	7.1	6.2	8.6	10.0	10.1
USD/INR Rate	61.25	65.67	67.12	64.49	67.58	67.50
EBIT Margin (%)	24.0	26.5	25.7	24.8	25.5	26.3

Source: Company, HDFC Sec Inst Research

Peer Valuations

Company	Mcap (Rs bn)	CMP (Rs)	RECO	TP (Rs)	EPS (Rs)				P/E (x)				RoE (%)			
					FY17	FY18	FY19E	FY20E	FY17	FY18	FY19E	FY20E	FY17	FY18	FY19E	FY20E
TCS	**7,179**	**1,875**	**BUY**	**2,130**	**66.7**	**67.5**	**79.5**	**88.8**	**28.1**	**27.8**	**23.6**	**21.1**	**33.4**	**30.1**	**35.5**	**37.6**
Infosys	2,829	1,301	BUY	1,430	62.8	66.1	72.3	79.4	20.7	19.7	18.0	16.4	22.0	24.5	24.5	26.1
Wipro	1,224	271	NEU	280	18.8	17.7	19.3	21.5	14.4	15.3	14.0	12.6	16.4	16.5	17.1	17.1
HCL Tech	1,364	980	BUY	1,160	57.6	62.7	71.2	77.5	17.0	15.6	13.7	12.6	27.0	25.3	25.5	24.7
TechM	580	651	BUY	780	31.6	42.7	45.9	51.8	20.6	15.3	14.2	12.6	18.1	21.5	20.3	20.2

Source: HDFC sec Inst Research

Consolidated Income Statement

Year ending March (Rs bn)	FY16	FY17	FY18	FY19E	FY20E
Net Sales (USD mn)	**16,544**	**17,575**	**19,089**	**20,989**	**23,100**
Growth (%)	***7.1***	***6.2***	***8.6***	***10.0***	***10.1***
Net Sales	**1,086.46**	**1,179.66**	**1,231.04**	**1,418.40**	**1,559.24**
Growth (%)	***14.8***	***8.6***	***4.4***	***15.2***	***9.9***
Employee Expenses	553.48	616.21	663.96	757.77	822.73
SG&A and Other Op Exp.	226.21	240.34	241.92	275.12	299.37
EBIDTA	**306.77**	**323.11**	**325.16**	**385.51**	**437.14**
EBIDTA (%)	***28.2***	***27.4***	***26.4***	***27.2***	***28.0***
EBIDTA Growth (%)	***25.3***	***5.3***	***0.6***	***18.6***	***13.4***
Depreciation	18.88	19.87	20.14	23.24	27.24
EBIT	**287.89**	**303.24**	**305.02**	**362.28**	**409.90**
Other Income	30.74	42.21	36.42	38.54	35.46
Interest	0.23	0.32	0.52	0.35	0.36
PBT	**318.40**	**345.13**	**340.92**	**400.47**	**445.00**
Tax (incl deferred)	75.02	81.56	82.12	99.89	111.01
RPAT	**242.69**	**262.89**	**258.26**	**299.87**	**333.27**
APAT	**242.69**	**262.89**	**258.26**	**299.87**	**333.27**
APAT Growth (%)	***22.2***	***8.3***	***(1.8)***	***16.1***	***11.1***
EPS (Rs)	**61.8**	**66.7**	**67.5**	**79.5**	**88.8**
EPS Growth (%)	***21.9***	***8.0***	***1.1***	***17.9***	***11.7***

Source: Company, HDFC sec Inst Research

Consolidated Balance Sheet

Year ending March (Rs bn)	FY16	FY17	FY18	FY19E	FY20E
SOURCES OF FUNDS					
Share Capital - Equity	1.97	1.97	1.91	3.75	3.75
Reserves	708.75	860.17	849.37	835.97	927.44
Total Shareholders' Funds	**710.72**	**862.14**	**851.28**	**839.72**	**931.19**
Minority Interest	3.55	3.66	4.02	4.32	5.05
Total Debt	**1.96**	**2.71**	**2.35**	**3.60**	**3.48**
Net Deferred Taxes	(21.03)	(19.09)	(22.79)	(17.99)	(17.99)
Long-term Provisions & Others	12.12	11.70	17.14	17.21	16.07
TOTAL SOURCES OF FUNDS	**707.32**	**861.12**	**852.00**	**846.86**	**937.80**
APPLICATION OF FUNDS					
Net Block	99.71	100.57	102.16	106.13	112.75
CWIP	16.70	15.41	12.78	16.71	16.71
Goodwill & Other Intangible Assets	18.03	16.44	17.57	18.54	19.94
Investments	16.68	11.69	9.92	11.69	11.69
LT Loans & Advances, Others	78.63	54.87	70.59	85.53	92.03
Total Non Current Assets	**229.75**	**198.98**	**213.02**	**238.60**	**253.12**
Debtors	240.73	226.84	250.37	275.91	303.30
Cash & Equivalents	292.67	457.85	428.68	398.80	473.67
Other Current Assets	98.73	120.57	136.40	145.31	155.61
Total Current Assets	**632.13**	**805.26**	**815.45**	**820.02**	**932.58**
Creditors	75.41	62.79	50.94	72.06	78.40
Other Current Liabilities & Provns	79.15	80.33	125.53	139.69	169.51
Total Current Liabilities	**154.56**	**143.12**	**176.47**	**211.75**	**247.91**
Net Current Assets	**477.57**	**662.14**	**638.98**	**608.27**	**684.67**
TOTAL APPLICATION OF FUNDS	**707.32**	**861.12**	**852.00**	**846.86**	**937.80**

Source: Company, HDFC sec Inst Research

Consolidated Cash Flow

Year ending March (Rs bn)	FY16	FY17	FY18	FY19E	FY20E
Reported PBT	318.40	345.13	340.92	400.47	445.00
Non-operating & EO items	-	-	-	-	-
Interest expenses	0.23	0.32	0.52	0.35	0.36
Depreciation	18.88	19.87	20.14	23.24	27.24
Working Capital Change	(48.24)	(18.90)	(7.75)	0.31	(1.82)
Tax paid	(75.02)	(81.56)	(82.12)	(99.89)	(111.01)
OPERATING CASH FLOW (a)	**214.24**	**264.86**	**271.71**	**324.47**	**359.77**
Capex	(20.47)	(18.57)	(18.75)	(32.31)	(35.26)
Free cash flow (FCF)	*193.78*	*246.29*	*252.96*	*292.16*	*324.51*
Investments	3.18	28.75	(13.95)	(16.71)	(6.50)
Non-operating income	-	-	-	-	-
INVESTING CASH FLOW (b)	**(17.28)**	**10.18**	**(32.70)**	**(49.02)**	**(41.77)**
Debt Issuance	(1.04)	0.75	(0.36)	1.25	(0.12)
Interest expenses	(0.23)	(0.32)	(0.52)	(0.35)	(0.36)
FCFE	*192.51*	*246.72*	*252.08*	*293.06*	*324.02*
Share capital Issuance	0.01	-	(0.06)	(0.08)	-
Dividend	(102.25)	(109.47)	(271.99)	(300.85)	(241.47)
FINANCING CASH FLOW (c)	**(103.50)**	**(109.04)**	**(272.92)**	**(300.01)**	**(241.95)**
NET CASH FLOW (a+b+c)	**93.46**	**166.00**	**(33.91)**	**(24.57)**	**76.05**
Closing Cash & Equivalents	292.67	457.85	428.68	398.80	473.67

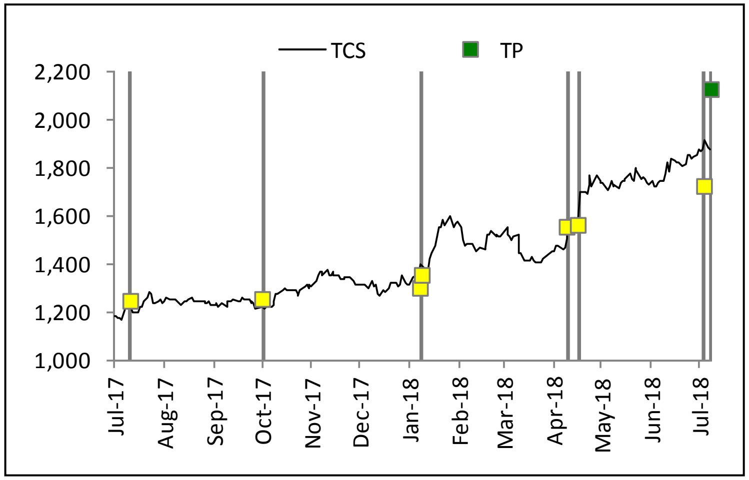
Source: Company, HDFC sec Inst Research

Key Ratios

	FY16	FY17	FY18	FY19E	FY20E
PROFITABILITY (%)					
EBITDA Margin	28.2	27.4	26.4	27.2	28.0
APAT Margin	22.3	22.3	21.0	21.1	21.4
RoE	39.9	33.4	30.1	35.5	37.6
RoIC or Core RoCE	59.2	56.6	56.0	62.4	67.5
RoCE	39.3	33.6	30.2	35.3	37.4
EFFICIENCY					
Tax Rate (%)	23.6	23.6	24.1	24.9	24.9
Fixed Asset Turnover (x)	5.6	5.6	5.4	5.6	5.4
Debtors (days)	*81*	*70*	*74*	*71*	*71*
Other Current Asset (days)	*33*	*37*	*40*	*37*	*36*
Payables (days)	*25*	*19*	*15*	*19*	*18*
Other Current Liab & Prov (days)	*27*	*25*	*37*	*36*	*40*
Cash Conversion Cycle (days)	62	63	62	54	49
Net Debt/EBITDA (x)	(0.9)	(1.4)	(1.3)	(1.0)	(1.1)
Net Debt/Equity (x)	(0.4)	(0.5)	(0.5)	(0.5)	(0.5)
Interest Coverage (x)	1,278	948	587	1,046	1,137
PER SHARE DATA					
EPS (Rs/sh)	61.8	66.7	67.5	79.5	88.8
CEPS (Rs/sh)	69.7	75.4	74.2	86.1	96.1
DPS (Rs/sh)	43.5	47.0	52.0	32.0	55.0
BV (Rs/sh)	189	230	227	224	248
VALUATION					
P/E	30.4	28.1	27.8	23.6	21.1
P/BV	9.9	8.2	8.3	8.4	7.6
EV/EBITDA	22.0	20.4	20.3	17.2	15.0
OCF/EV (%)	2.5	3.7	4.0	4.9	5.5
FCF/EV (%)	2.2	3.5	3.7	4.4	4.9
FCFE/mkt cap (%)	2.1	3.2	3.5	4.2	4.6
Dividend Yield (%)	1.2	1.3	1.4	1.7	2.9

Source: Company, HDFC sec Inst Research

RECOMMENDATION HISTORY



Date	CMP	Reco	Target
14-Jul-17	1,223	NEU	1,250
4-Oct-17	1,224	NEU	1,253
10-Jan-18	1,355	NEU	1,303
12-Jan-18	1,394	NEU	1,353
12-Apr-18	1,507	NEU	1,553
20-Apr-18	1,596	NEU	1,565
6-Jul-18	1,913	NEU	1,720
11-Jul-18	1,875	BUY	2,130

Rating Definitions

BUY : Where the stock is expected to deliver more than 10% returns over the next 12 month period
NEUTRAL : Where the stock is expected to deliver (-)10% to 10% returns over the next 12 month period
SELL : Where the stock is expected to deliver less than (-)10% returns over the next 12 month period

Disclosure:

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