

Sector: IT & ITES
Results update

	Change
Reco: Hold	↔
CMP: Rs. 260	
Price Target: Rs. 285	↓

↑ Upgrade ↔ No change ↓ Downgrade

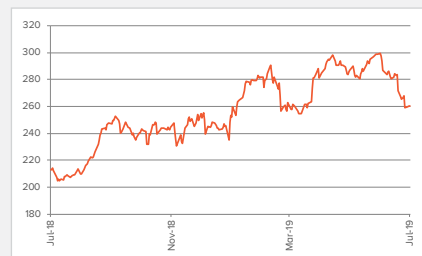
Company details

Market cap:	Rs. 1,56,738 cr
52-week high/low:	Rs. 301 / 197
NSE volume: (No of shares)	66.4 lakh
BSE code:	507685
NSE code:	WIPRO
Sharekhan code:	WIPRO
Free float: (No of shares)	157.8 cr

Shareholding (%)

Promoters	73.9
FII	11.7
DII	8.6
Others	5.8

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-13.0	-7.4	3.3	22.8
Relative to Sensex	-12.4	-7.5	-4.8	12.7

Sharekhan Research, Bloomberg

Wipro delivered lower-than-expected revenue performance for Q1FY2020. However, adjusted EBIT IT margin remained a tad ahead of our estimates. Soft growth was due to weakness in the BFSI, consumer, healthcare and manufacturing verticals. BFSI growth was impacted by weakness in European Banking and overall capital market. However, management expects the healthcare vertical and engineering practices to bounce back during 2HFY2020E. Digital business reported strong growth during the quarter, contributing 37.4% to total revenue. Management has guided for revenue growth of 0% to +2% for Q2FY2020E. The tepid growth guidance was due to softness in the BFSI and manufacturing verticals and delay in the ramp-up of deal wins. Management highlighted that the capital return policy would be maintained at 40-50% of net profit despite change in taxation policy, as free cash flow to net profit remains strong at 98%. We maintain Hold with a revised price target (PT) of Rs. 285.

Key positives

- Adjusted EBIT IT margin remained at 18%, above our estimate.
- Continued strong digital growth at 34.6% y-o-y, which now contributes 37.4% to total revenue.
- Strong cash conversion as free cash flow to net profit remained at 98%.
- Added three clients in \$100 million+ revenue bucket and one client in \$75 million+ revenue bucket.

Key negatives

- Tepid revenue growth guidance for Q2FY2020E owing to continued softness in certain industry pockets.
- Delay in ramp-up of projects and decision-making process on discretionary spending from clients.
- Softness in the BFSI, healthcare and manufacturing verticals.

Our Call

Valuation – Maintain Hold with a revised PT of Rs. 285: We have revised downward our earnings estimates for FY2020E/FY2021E, factoring in lower-than-expected revenue growth in Q1FY2020 along with muted growth in Q2 revenue guidance and reset of USD/INR rate. With inconsistent execution along with macro uncertainties, underperformance in revenue growth among large peers is expected to continue for FY2020E. At the CMP, the stock is trading at 15.8x/14.2x its FY2020/FY2021 earnings estimates, which is justified due to continued underperformance. Wipro continues to remain our least preferred IT company among top-tier companies. Hence, we maintain Hold with a revised PT of Rs. 285.

Key Risks

Rupee appreciation and/or adverse cross-currency movements; slackening pace in deal closures and/or constraint in local talent supply in the U.S.; and stringent visa regime to adversely impact earnings.

	Rs cr				
Valuation					
Particulars	FY17	FY18	FY19	FY20E	FY21E
Revenues	55,040.2	54,487.1	58,906.0	61,225.9	66,878.7
OPM (%)	20.6	19.7	19.5	20.7	21.3
Adjusted PAT	8,489.5	8,329.3	9,011.4	9,907.0	11,003.4
% YoY growth	-4.7	-1.9	8.2	9.9	11.1
Adjusted EPS (Rs.)	14.1	13.8	14.9	16.4	18.2
P/E (x)	18.5	18.8	17.4	15.8	14.2
P/B (x)	1.3	2.6	3.1	3.2	2.9
EV/EBITDA (x)	6.5	6.7	5.0	4.7	3.9
RoNW (%)	16.4	17.4	15.2	17.9	18.1
RoCE (%)	13.1	13.8	14.6	16.7	17.7

Source: Company; Sharekhan estimates

Revenue miss, margin beats estimates

Wipro delivered lower-than-expected revenue performance in Q1FY2020, with a 0.7% decline in constant currency (CC) revenue growth, adjusted for divestment of Workday and Cornerstone business versus our estimate of 0.4% revenue growth. Soft revenue growth was attributed to weak performance in the BFSI, consumer, healthcare and manufacturing businesses. On reported basis, USD revenue declined by 1.8% q-o-q to \$2,038.8 million. Adjusted for the Workday and Cornerstone divestiture, USD revenue dropped by 1.3% q-o-q, below our estimates. EBIT margin for IT services contracted by 85 BPS q-o-q to 18.4%, above our estimates, owing to salary increase, investment in utilisation and higher onsite mix. These margin headwinds were partially offset by forex benefit and margin benefit from lease accounting. Adjusted EBIT margin for IT services (excluding Rs. 69.9 crore gain from Workday and Cornerstone divestiture) stood at 18%, a tad above our estimates. Net profit of Rs. 2,387.4 crore (+12.6% y-o-y, -3.9% q-o-q) was 3.9% ahead of our estimate, aided by higher-than-expected net other income and lower tax rate.

Strong digital momentum and solid client metrics

Digital revenue growth accelerated to 34.6% y-o-y in Q1FY2020 (versus 34% in Q4FY2019), which now contributes 37.4% to overall revenue. The strong growth momentum in digital business indicates Wipro's smart acquisitions as well as aggressive bets in select digital competencies. The company added three clients under its \$100 million client bucket and one client under \$75 million client bucket. Client mining also remained strong – top 5 and top 10 client revenue growth accelerated to 18.7% y-o-y and 13.8% y-o-y, respectively, while the top client's revenue growth remained muted during the quarter.

Soft BFSI owing to macro uncertainties, however healthcare performance improved

Weak seasonality in Q1 also persisted during the quarter, as four of the seven verticals reported revenue decline during the quarter. After several quarters of strong performance, CC revenue growth of the BFSI and consumer verticals declined by 0.6% and 4.4% on a sequential basis, respectively. BFSI growth during the quarter was impacted by softness in European Banking and overall capital market; though on a y-o-y basis, BFSI grew by 11.2% in CC terms. Soft growth in the consumer vertical was due to closure of certain large projects and deferment of some new order wins during the quarter. Healthcare and manufacturing also declined 1.5% and 2% q-o-q on CC basis, respectively. Importantly, healthcare revenue grew by 0.4% y-o-y after several quarters of underperformance, led by good traction in the core healthcare business. However, technology, energy and utilities and communication grew by 2.7%, 0.2% and 2.8% on a sequential basis, respectively, in CC terms. In service line, application services growth continued to decline due to completion of certain large programmes. Digital operations and platform and data, analytics and AI reported strong growth of 22.4% and 11.5% on a y-o-y basis, respectively.

In-line growth guidance, Q2FY2020 performance remains important

Wipro's management has guided for revenue growth of 0% to +2% for Q2FY2020E, in-line with our modest estimates. Despite the postponement of certain deal signings to Q1FY2020 from Q4FY2019, the guidance does not seem encouraging. The slow start in Q1FY2020 along with anticipated soft performance in Q2FY2020E would impact the overall growth performance for FY2020E. The tepid growth guidance was due to continued softness in BFSI (especially European Banking and overall capital market) and manufacturing verticals, weakness in HPS business and engineering services, delayed decision-making process in discretionary spending from clients, restructuring activities in India, Middle East and Continental Europe and delay in the ramp-up of deal wins. However, management remains more optimistic now compared to beginning of the quarter for better growth trajectory in H2FY2020E on account of recovery in engineering, consumer and healthcare, continued strong digital momentum, ramp-up of new deal signings and strong deal pipelines across industries. On the margin front, margins are expected to improve in Q2FY2020E on account of absence of two-month salary revision and operational efficiencies. Further, management highlighted that the capital return policy (40-50% of net profit) would be maintained despite change in taxation policy and strong cash conversion at 98% of net income.

Results

Particulars	Rs cr				
	Q1FY20	Q1FY19	Q4FY19	YoY (%)	QoQ (%)
Revenues (\$ mn)	2,038.8	2,026.5	2,075.5	0.6	-1.8
Net sales	14,716.1	13,977.7	15,037.9	5.3	-2.1
Direct costs	10,427.3	10,035.0	10,694.2	3.9	-2.5
Gross profit	4,541.7	3,942.7	4,596.6	15.2	-1.2
SG&A	1,907.2	1,942.1	1,766.3	-1.8	8.0
EBIT	2,634.5	2,000.6	2,830.3	31.7	-6.9
Net other income	536.3	354.8	469.8	51.2	14.2
PBT	3,170.8	2,355.4	3,300.1	34.6	-3.9
Tax provision	669.9	586.5	706.4	14.2	-5.2
Net profit	2,387.4	2,120.6	2,483.3	12.6	-3.9
EPS (Rs.)	4.0	3.5	4.1	12.7	-3.8
Margin (%)				BPS	BPS
EBIT margins (Blended)	17.9	14.3	18.8	359	-92
EBIT margin (IT Services)	18.4	15.6	19.2	275	-85
NPM	16.2	15.2	16.5	105	-29

Source: Company; Sharekhan Research

Revenue mix: Geographies, industry verticals and other operating metrics

Particulars	Revenues	Contribution	\$ Growth (%)		CC growth (%)	
	(\$ mn)	(%)	q-o-q	y-o-y	q-o-q	y-o-y
Revenues (\$ mn)	2,039	100	-1.8	0.6	-0.7	5.9
Geographic mix						
Americas	1,197	58.7	-0.9	7.6	0.2	11.2
Europe	502	24.6	-1.8	-3.3	-0.4	0.0
APAC & others	340	16.7	-4.6	-6.1	-4.3	-1.8
Industry verticals						
BFSI	644	31.6	-1.5	6.0	-0.6	11.2
Consumer	318	15.6	-5.4	-1.9	-4.4	7.7
Technology	265	13.0	1.4	-7.9	2.7	-1.6
Healthcare	269	13.2	-1.8	-0.9	-1.5	0.4
Energy & utilities	261	12.8	-1.8	3.0	0.2	7.8
Manufacturing	161	7.9	-3.0	-4.2	-2.0	-0.1
Communications	120	5.9	1.7	6.0	2.8	8.8
Service line						
Application services	909	44.6	-2.9	-2.7	-0.9	1.0
Cloud and infrastructure services	524	25.7	0.2	-5.6	0.5	6.6
Digital operation & platform	300	14.7	-3.1	19.3	-2.9	22.4
Product engineering	155	7.6	-1.8	-0.7	-0.9	1.4
Data, analytics and AI	151	7.4	1.0	7.9	0.8	11.5
Clients Contribution						
Top client	75	3.7	-1.8	0.6	-	-
Top 5	281	13.8	-1.1	18.7	-	-
Top 10	422	20.7	-0.3	13.8	-	-

Source: Company; Sharekhan Research

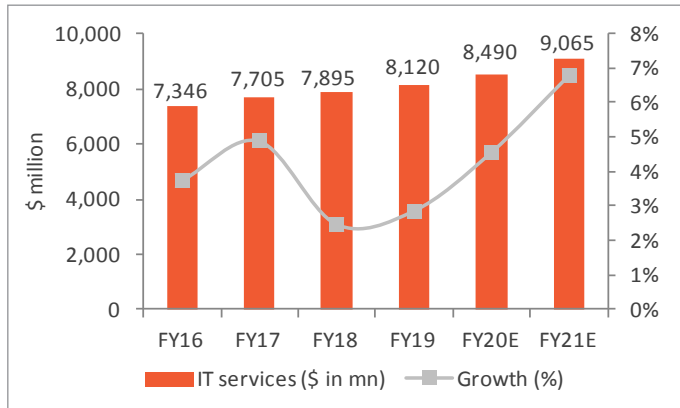
Revenue mix: Geographies, industry verticals and other operating metrics

Particulars	Revenues	Contribution (%)		Margin (%)	
	(\$ mn)	Q1FY19	Q1FY20	Q1FY19	Q1FY20
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Consumer	318	16.0	15.6	12.7	15.7
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Source: Company; Sharekhan Research

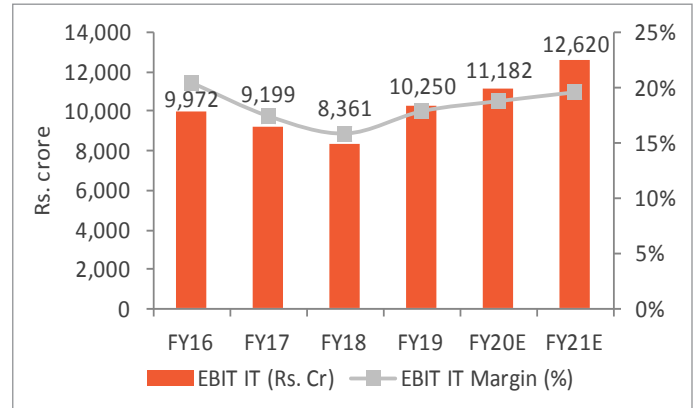
Financials in charts

Revenue in US\$ (mn) and growth (%)



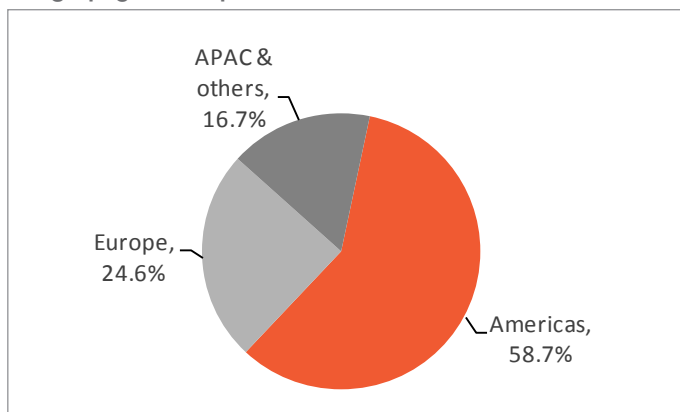
Source: Company, Sharekhan Research

EBIT IT (Rs. cr) and EBIT IT margin (%)



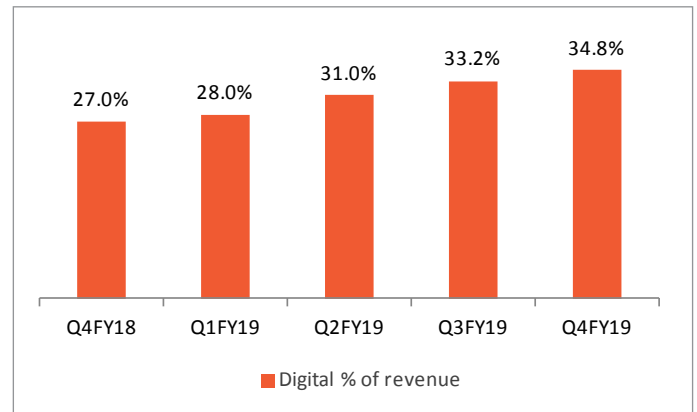
Source: Company, Sharekhan Research

Geography break-up



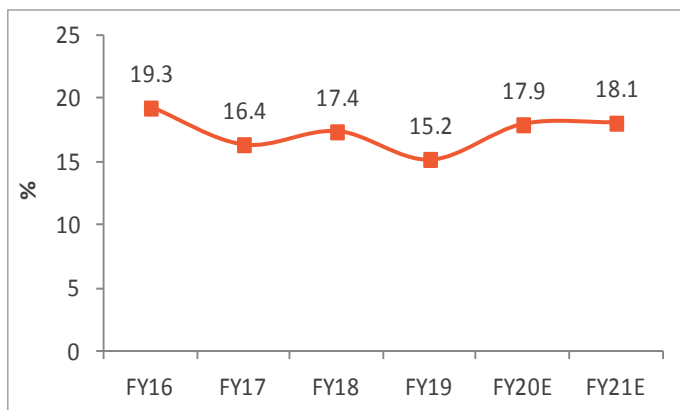
Source: Company, Sharekhan Research

Digital % of total revenue



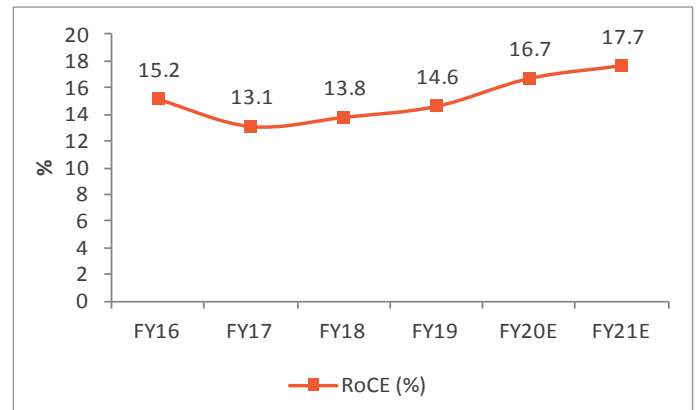
Source: Company, Sharekhan Research

RoE



Source: Company, Sharekhan Research

RoCE



Source: Company, Sharekhan estimate

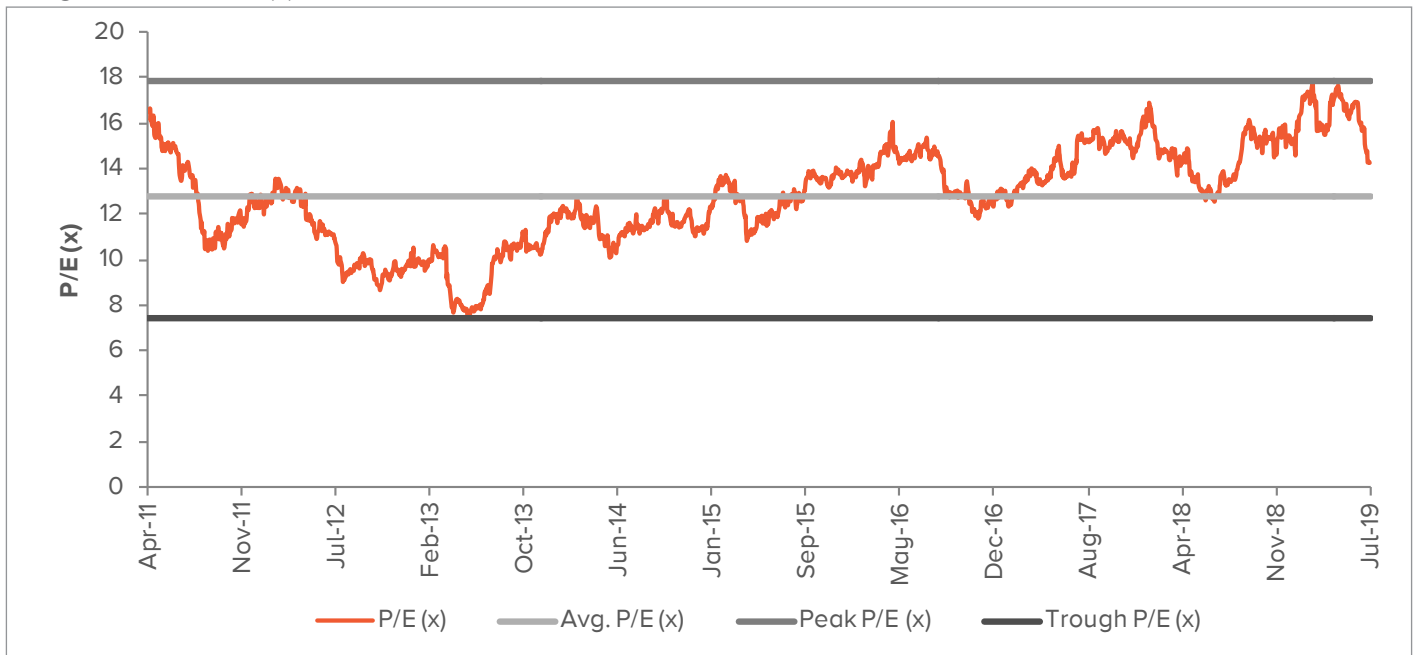
Outlook

Growth for Indian IT is expected to accelerate from 6-7% currently as demand for digital services is growing rapidly. India will continue to remain the preferred destination for talent supply and would create a gradual shift of digital business from onsite. Wipro's CEO, Mr. Abidali has laid out six strategic themes to drive business growth, with investments in creating digital capabilities, training and incentivising employees and acquiring businesses. Though the long track record of underperformance implies execution issues, the company has been focusing on higher client mining and increasing deal wins momentum to catch up the industry's average growth rate. Further, the bottoming out of healthcare issues and continued growth momentum in BFSI would aid in the company's overall growth. The company aims to maintain its margin performance going ahead, with improved revenue growth rate.

Valuation

We have revised downward our earnings estimates for FY2020E/FY2021E, factoring in lower-than-expected revenue growth in Q1FY2020 along with muted growth in Q2 revenue guidance and reset of USD/INR rate. With inconsistent execution along with macro uncertainties, underperformance of revenue growth among large peers is expected to continue for FY2020E. At the CMP, the stock is trading at 15.8x/14.2x of its FY2020/FY2021 earnings estimates, which is justified due to continued underperformance. Wipro continues to remain our least preferred IT company among top-tier companies. Hence, we maintain our Hold rating on the stock with a revised PT of Rs. 285.

One year forward P/BV (x) band



Source: Sharekhan Research

Peer valuation

Particulars	CMP (Rs / Share)	O/S Shares (Cr)	MCAP (Rs Cr)	P/E (x)		EV/EBIDTA (x)		P/BV (x)		RoCE (%)	
				FY20E	FY21E	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
HCL Tech	1,041	136	1,41,141	13.2	11.8	9.0	8.1	3.1	2.7	24.4	24.2
Infosys	794	436	3,46,452	20.8	18.2	14.7	12.9	2.9	2.8	25.3	29.0
TCS	2,117	375	7,94,436	23.5	21.4	17.6	15.9	8.0	7.2	35.6	35.4
Tech M	691	96	66,542	13.0	12.0	9.6	8.8	2.9	2.6	21.2	20.0
Wipro	260	603	1,56,738	15.8	14.2	10.3	8.9	3.2	2.9	17.9	18.1

Source: Company, Sharekhan Research

About company

Wipro is the leading global IT services company with business interests in export of IT, consulting and BPO services. The company offers the widest range of IT and ITeS services, including digital strategy advisory, client-centric design, technology consulting, IT consulting, systems integration, software application development and maintenance, package implementation, and R&D services. Wipro develops and integrates innovative solutions that enable its clients to leverage IT to achieve their business objectives at competitive costs. The company generates revenue from the BFSI, manufacturing, retail, utilities and telecom verticals. Wipro has more than 1.6 lakh employees.

Investment theme

With six strategic themes and higher client-mining strategy, Wipro has been focusing on driving business growth. Though Wipro has been active on the investment front, including building digital capabilities, training and incentivising employees and acquiring businesses, it has been underperforming the large peers in terms of overall growth owing to execution challenges and account-specific issues. The company hopes that its growth trajectory would catch up with the industry's average growth rates, led by increasing deal wins, continued growth momentum in BFSI, receding of concerns in certain industry pockets and higher growth in the digital business. Higher revenue growth would help the company to report margin improvement going ahead.

Key Risks

1) Any hostile regulatory visa norms could impact employee expenses; 2) prolonged weakness in healthcare/manufacturing verticals; 3) rupee appreciation and/or adverse cross-currency movements; 4) softness in top accounts; 5) any further client-related/portfolio-related issues impacting sales/margins; and 6) any major macro issues in developed markets, especially in the U.S. and Europe.

Additional Data

Key management personnel

Abidali Neemuchwala	CEO
Bhanumurthy B. M.	President & Chief Operating Officer
Jatin Dalal	Chief Financial Officer
Anand Padmanabhan	President, energy, utilities & construction
Ankur Prakash	Senior Vice President, Communications

Source: Company Annual Report

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Premji Azim Hasham	73.8
2	Life Insurance Corp of India	4.3
3	BlackRock Inc	0.9
4	Vanguard Group Inc	0.6
5	Norges Bank	0.5
6	ICICI Prudential Asset Management	0.5
7	Dimensional Fund Advisors LP	0.4
8	Azim Premji Philanthropic Initiatives	0.3
9	SBI Funds Management Pvt Ltd	0.3
10	Pinebridge Investments LP	0.2

Source: Bloomberg

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