Fundamental Research Report

Wipro Ltd.

Date : 30-10-2020

Equity99

Creating Wealth Through Unfolded Research

BUY

CMP	: Rs.339.55
Target	: 586.00
BSE Code	: 507685
NSE Code	: WIPRO
Market Cap	: Rs.194,054.16 Cr.
52 Week High /	: Rs.381.70 /
Low	Rs.159.40
Stock PE	: 19.8x
Dividend Yield	: 0.29%
Recommendation	: BUY
Book Value	: Rs.106.00
Face Value	: Rs.2.00
ROCE	: 19.9%
ROE	: 17.5%

In Q2-2021, the company experienced a -ve 0.1% y-o-y growth in revenue to Rs. 15,114.50 Cr. However, notably the growth was led entirely by rupee depreciation of 3.8% y-o-y. The sales decline has been at around 3.7% y-o-y, dollar revenue basis.

The reason for the fall in dollar revenue was decline in the revenue of all the verticals' revenue except healthcare. Communication and technology verticals experienced the sharpest revenue decline y-o-y in Q2-2021 followed by energy, BFSI and consumer. The revenue decline was also driven by decline in revenue of Americas and Europe (major segments) while rest of the world showed increase y-o-y.

As per the following, it shows that the constant dollar revenue growth is still negative for Wipro on a y-o-y basis. So, the recovery is not still evident to the pre-COVID levels.

Constant currency USD revenue growths

Y-o-Y growth	Q2 2019	Q2 2020	Q2 2021
BFSI	16%	6%	-3%
Communications	-7%	2%	-10%
Consumer	8%	6%	-2%
Engery	0%	6%	-5%
Health	-4%	3%	2%
Manufacturing	-2%	1%	-2%
Technology	5%	-3%	-7%
IT Services	5%	4%	-3%

The company has reported a 130-bps y-o-y rise in EBIT margins in Q2-2020, driven by large work force working from home, improved utilization, automation, increased share of offshore revenue and rupee depreciation.

However, the company posted a 3% y-o-y decline in net income to Rs. 2,484.30 Cr for the quarter as PBT growth was slower due to sharp fall in other income besides lower growth in EBIT.

Rs in Cr.	Q2 2020	% of sales	Q2 2021	% of sales	Y-o-Y
Revenue	15,125.60	100%	15,114.50	100%	-0.1%
Costs	12,516.20	83%	12,317.00	81%	-1.6%
EBIT	2,609.40	17%	2,797.50	19%	7.2%
Other Income	749.60	5%	536.30	4%	-28.5%
Finance exp	224.70	1%	126.70	1%	-43.6%
PBT	3,134.30	21%	3,207.10	21%	2.3%
Tax	573.10	18%	722.80	23%	26.1%
PAT	2,561.20	17%	2,484.30	16%	-3.0%

Share buy-back: The company has announced a share buy-back of 23.75 Cr shares (4.16% of the outstanding shares) at Rs. 400 / share. This is expected to result in a pretax outflow of Rs. 9,500 Cr. and Rs. 11,700 Cr including tax outflow. The company has had cash and cash equivalents of Rs. 15,242 Cr as of Q2-2021. This is an appropriate move to enhance value to the shareholders and thereby also its capital returns ratios. The ROE improves by approximately 170 bps y-o-y in FY2021 to 17.8% from 16.1% earlier without buyback. If the company continues to resort to such buy backs in the future, it can enhance the return ratios over a long term.

New Acquisition: The company has announced acquisition of Eximius Design, an engineering services company with expertise in semiconductor, software, and systems design for USD 80.00 million. This will be the fourth such deal the company has engaged in in CY2020. The acquisitions are expected to augment offerings and client's acquisition.

Outlook: Some of the important new strategic focus for the company are growth, augmentation of offerings and talent pool, and simplification of operating model. The growth will be driven by mining in top accounts of the company, winning large transformational deals, and through striking of partnerships with business vendors.

The company intends to augment its offerings by having industry specific solutions by using offerings of large technology players and startups. At the same time, the company will augment its talent pool through deployment of domain and technology experts, large program managers, and digital transformation architects etc. Also, the company will try and strive for leaner organization to be able to stay closer to clients. The leaner organization will be achieved through leadership hierarchies, simplifying process, and reduce number of P&Ls and KPIs.

Investment rationale: We believe the company is seeing a healthy deal pipeline within the small and medium size segment. However, it is seeing a huge declines y-o-y in most of its verticals' revenues except in case of Healthcare as of Q2-2021. Similarly, the US and Europe revenue have declined y-o-y as of Q2-2021. We believe the company may take a couple of quarters before it can fall back to its pre-COVID levels of business growth on a y-o-y basis. Nevertheless, increased demand for digitization coupled with recovery and consistent growth across all its verticals, horizontals and geographies should help it regain momentum in the business and profits growth over medium – long term.

The company is trading at 22x TTM PE (as of Q2-2021) against an industry average TTM PE of 27x. The company generates ROE of 16.9% against industry peers generating average ROE of 26%. As a result, we believe the company is steeply undervalued at the current PE levels. On a forward PE basis, we value the company at 28x its estimated FY2022 EPS of Rs. 21 and at 23x its estimated FY2023 EPS of Rs. 26. On a TTM PE basis, we value Wipro shares at 34x TTM PE (as of Q2-2021) and assign it a target value at Rs. 586 a share over medium term. We believe the PE as of Q2-2021 will expand up-to 34x over a period of time to catch up with the fair valuation on a DCF basis we arrive at as follows.

Driven by likely consistent growth in its digital offerings, recovery and growth in its prominent geographies and verticals, and the fact that they can resort to buybacks in the future given healthy cash balance they hold, we arrive at a target price for Wipro's shares at Rs.586 on a DCF basis over a long term and hence recommend a BUY on the stock. This is because it appears to be trading at a 72% discount compared to the fair valuation on a DCF basis. Any visible improvements in constant currency or USD sales growth y-o-y, and recoveries across its verticals and geographies' revenues y-o-y will be the key triggers.

Disclosure:

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