Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Wipro Ltd

Eyeing strong growth momentum despite mixed Q3

IT & ITES		Sharekhan code: WIPRO		
Reco/View: Hold	↔	CMP: Rs. 650	Price Target: Rs. 750	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)		✓	

\+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

ESG Disclosure Score NEW

ESG RISK RATING 13.28

Updated Jan 08, 2022

Low Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

Company details

Market cap:	Rs. 3,56,203 cr
52-week high/low:	Rs. 739 / 398
NSE volume: (No of shares)	76.6 lakh
BSE code:	507685
NSE code:	WIPRO
Free float: (No of shares)	147.9 cr

Shareholding (%)

Promoters	73.0
FII	10.3
DII	2.9
Others	13.8

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	0.5	-8.2	15.7	41.7
Relative to Sensex	-4.9	-8.0	-0.0	17.9

Sharekhan Research, Bloomberg

Summary

- Q3FY22 revenue growth lagged our expectations, while IT services' EBIT margin met our expectations. Net headcount additions, client mining and deal pipeline stayed strong, but attrition continued to inch up.
- The management guided for revenue growth of 2-4% q-o-q for Q4FY2022, as we expected, led by broad-based demand. Organic growth is estimated at a decent 1.4-3.4% q-o-q.
- Supply-side challenges, skill-based premium, amortisation expense of intangibles from recent acquisitions, increasing discretionary expenses, and investments in frontline sales to weigh on its margins in the near term. The management expects to maintain EBIT margin in a narrow band of 17-17.5% for FY2022.
- Though Wipro is progressing well in its turnaround journey, we believe a valuation of 23x FY2024E factors in the growth potential. Hence, we maintain a Hold on Wipro with an unchanged PT of Rs. 750.

Wipro clocked constant currency (CC) revenue growth of 3% q-o-q (at mid-point of its revenue growth guidance) in Q3FY2022, which lagged our estimates. Reported USD revenue grew 2.3% q-o-q and 27.5% y-o-y to $2,639.7 million, led by broad-based demand and better client mining. EBIT margin for IT services declined 20 bps on q-o-q basis at 17.6%, broadly in line with expectations. Revenue growth guidance of 2-4% q-o-q (includes ~60 bps revenue contribution from recent acquisitions) for Q4FY2022 was on the expected lines. As enterprises are aggressively spending on emerging technologies such as Cloud transformation, engineering, data, digital transformation and security, the management remains confident of maintaining strong revenue growth going ahead.

Key positives

- Deal win rate improved 300bps y-o-y
- Added two and three clients, respectively, in $100 mn and $50 mn bucket on q-o-q
- FCF to net profit ratio improved to 82% from 64% in Q2FY2022

Key negatives

- Attrition inched up 220 bps q-o-q to 22.7%
- Deal win TCVs remained flat q-o-q at $600 million

Management Commentary

- The management provided revenue growth guidance of 2-4% q-o-q on CC for Q4FY2022
- Wipro remains confident of growth prospects going ahead, led by robust deal pipeline, improving leadership profile, deep partnership with hyperscalers and good client mining
- Management expects to maintain EBIT margin in a narrow band of 17-17.5% in medium-term.

Revision in estimates – We broadly maintain EPS estimate for FY22E/FY23E/FY24E. .

Our Call

Valuation – Maintain Hold with a PT of Rs. 750: The new management's refreshed strategy including simplified organisation structure, sharpening focus on large deals and a client-centric and growth-focused approach has driven up organic revenue growth, healthy deal wins, new logo additions and growth in large accounts. We expect Wipro to report USD revenue/net profit CAGR of 11.6%/12.5% over FY2022-FY2024E. We believe the company has limited margin levers to offset headwinds in the coming quarters. At CMP, the stock trades at an expensive valuation of 26x/23x its FY2023/FY2024 earnings estimates. Hence, we maintain a Hold rating on Wipro with a price target (PT) of Rs. 750.

Key Risks

Rupee appreciation and/or adverse cross-currency movements, war for talent in major markets, constraint in local talent supply in the US and a stringent visa regime could affect earnings.

Valuation (Consolidated) Rs cr

Particulars	FY21	FY22E	FY23E	FY24E
Revenue	62,235.2	79,975.0	91,411.3	1,02,045.9
OPM (%)	24.2	21.7	21.9	22.2
Adjusted PAT	10,794.6	12,211.0	13,645.7	15,442.2
% YoY growth	11.0	13.1	11.7	13.2
Adjusted EPS (Rs.)	19.1	22.3	24.9	28.2
P/E (x)	34.0	29.1	26.1	23.0
P/B (x)	7.0	6.2	5.5	4.9
EV/EBITDA (x)	23.0	19.8	16.9	14.7
RoNW (%)	19.5	19.8	19.9	20.1
RoCE (%)	18.2	19.7	20.9	21.9

Source: Company; Sharekhan estimates

Revenue misses mark, margins in-line

Wipro reported below-than-expected revenue growth performance, while EBIT margin performance remained in-line with our expectations. The company delivered strong CC revenue growth of 3.0% q-o-q and 28.5% y-o-y, but it remained below our estimates. Reported USD revenue grew 2.3% q-o-q and 27.5% y-o-y to $2,639.7 million, led by broad-based growth across verticals (excluding energy, natural resources and utilities) and better client mining (strong growth across top accounts). EBIT margin for IT services remained declined by 20 bps on q-o-q basis at 17.6%, owing to impact of wage revision for junior and mid-level employees (i.e 80% of workforce from September 1, 2021), higher subcontractor expenses, rising cost to backfill attrition and. Decline in EBIT margin was on the expected lines, aided by lower depreciation charge and cost efficiencies. Net profit of Rs. 2,969 crore (flat on y-o-y, but up 1.3% q-o-q) was in-line with our estimates.

Margins to remain under pressure in subsequent quarters

Wipro's EBIT margin declined 20 bps q-o-q to 17.6% (though remained above its guided range of 17-17.5% for FY2022), owing to wage hikes for 80% of its total workforce (effective from September 1, 2021), rising cost to backfill attrition, higher subcontractor expenses and decline in utilisation rates. These margin headwinds were partially mitigated by revenue growth, operating efficiencies and increase in realisation. In the subsequent quarters, supply-side challenges, higher attrition, skill-based premium, integration of acquisitions, unsustainable utilisation and investments in frontline capabilities are expected to weigh on margins in the near term. The amortization expense of intangibles from the recent acquisitions would impact margin profile. In addition, increasing discretionary expenses (travel, marketing, facility, etc) would put pressure on margins in coming quarters. Wipro's voluntary attrition rate inched up by 220 bps q-o-q to 22.7% in Q3FY2022. However, the company indicated that attrition would moderate in the next couple of quarters and sustain of over 20%. Management expects to maintain EBIT margin in a narrow band of 17-17.5% in medium-term. We estimate a slight improvement in margins in FY2023 on the back of operational efficiencies and increase in realisation.

Key result highlights

- **Demand remains strong:** Wipro highlighted that its new business strategy model, simplified operating model and broad approach started showing results in terms of continued improvement in revenue growth trajectory and healthy deal wins. Further, demand environment remains robust, which is reflected in a strong deal pipeline. It sees rapid expansion of small and medium deals in both existing accounts and new clients. Enterprises are focusing on technologies such as cloud transformation, engineering, data, digital transformation and security. The deal pipeline has a mix of small, medium, and large deals. Management expects higher participation in clients' transformation journey and increasing deal win rate going ahead given its investments in talents and building capability in niche areas, building competencies in engineering areas and strong demand across industries.

- **Growth guidance for Q4FY2022:** Wipro provided revenue growth guidance of 2-4% on q-o-q (which translates to 27-28% y-o-y) for Q3FY2022, in line with our expectations. This includes revenue contribution from the acquisition of Edgile and Leanswift.

- **Muted deal wins:** The company reported deal win TCVs of $600 million versus average quarterly deal wins run rate of $974 million over last four quarter. However, the company's deal ACV increased 27% y-o-y in 9MFY2022 on account of strong execution and improving win rates (up 300 bps y-o-y).

- **Huge opportunity in cloud:** The company's Cloud business, which accounted for 30% of its total revenue, grew by over 30% y-o-y. The company has entered into partnerships with cloud providers. Management indicated that order wins with partners grew by 40% y-o-y. It sees massive cloud opportunity for the next five years.

- **Expect strong growth in Europe:** Management cited that the Germany business grew 2x y-o-y, while the UK business registered 40% y-o-y growth. The management is confident of reporting strong growth in Europe business in coming quarters.

- **Large account growth remained strong:** Revenues from the top, top 5 and top 10 clients grew by 5.6%, 4% and 2.8% on q-o-q basis and accounted for 3.2%, 12.7% and 20.2% of overall revenues as against 3.1%, 12.5% and 20.1% during Q2FY2022.

- **Cash flows improved:** OCF and FCF increased 26% q-o-q and 30% q-o-q respectively during Q3FY2022. Effectively, the FCF to net profit ratio improved to 82% from 64% in Q2FY2022. Cash & cash equivalents stood at $4.6 billion at December 30, 2021 and net cash balance stood at $2.8 billion.

Results

Rs cr

Particulars	Q3FY22	Q3FY21	Q2FY22	YoY (%)	QoQ (%)
Revenues ($ mn)	**2,639.7**	**2,070.8**	**2,580.0**	**27.5**	**2.3**
Net sales	**20,433.7**	**15,726.6**	**19,762.2**	**29.9**	**3.4**
Direct costs	14,277.8	10,431.3	13,756.2	36.9	3.8
Gross profit	**6,408.8**	**5,295.3**	**6,258.9**	**21.0**	**2.4**
SG&A	2,602.4	1,914.0	2,514.0	36.0	3.5
EBIT	**3,806.4**	**3,381.3**	**3,744.9**	**12.6**	**1.6**
Net other income	217.5	457.5	265.5	-52.5	-18.1
PBT	**4,023.9**	**3,838.8**	**4,010.4**	**4.8**	**0.3**
Tax provision	806.3	852.4	825.9	-5.4	-2.4
Minority interest	3.3	29.8	0.1	-88.9	-
Net profit	**2,969.0**	**2,966.7**	**2,930.5**	**0.1**	**1.3**
EPS (Rs.)	5.4	5.2	5.4	4.0	1.3
Margin (%)				**BPS**	**BPS**
EBIT margin (Blended)	18.6	21.5	18.9	-287	-32
EBIT margin (IT Services)	17.6	21.7	17.8	-414	-19
NPM	14.5	18.9	14.8	-433	-30
Tax rate	20.0	22.2	20.6	-217	-56

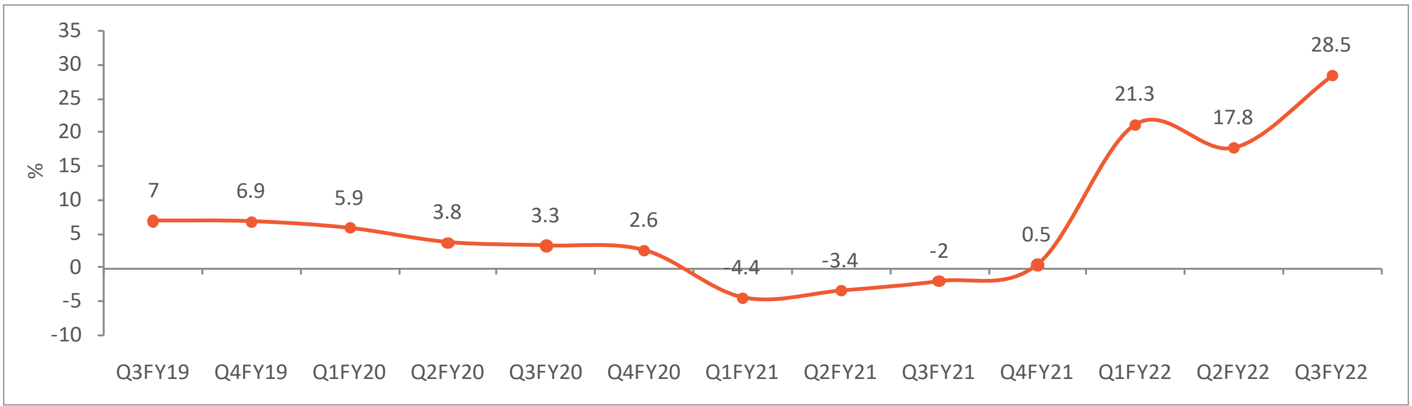
Source: Company, Sharekhan Research

Operating metrics

Particulars	Revenue	Contribution	$ Growth (%)		CC growth (%)	
	($ mn)	(%)	Q-o-Q %	Y-o-Y %	Q-o-Q %	Y-o-Y %
Revenue ($ mn)	2,640	100	2.3	27.5	3.0	28.5
Geographic mix						
Americas 1	744	28.2	4.9	22.3	5.2	22.7
America 2	802	30.4	1.6	33.2	1.7	32.7
Europe	784	29.7	0.6	35.2	2.3	38.0
APMEA	309	11.7	2.3	10.5	2.9	12.5
Industry verticals						
BFSI	929	35.2	3.5	47.1	4.1	47.4
Consumer	467	17.7	4.7	37.6	5.2	37.9
Technology	314	11.9	-0.2	20.4	0.9	21.9
Healthcare	311	11.8	3.2	8.2	3.8	9.1
Energy & utilities	309	11.7	-2.7	13.8	-2.2	15.0
Manufacturing	177	6.7	2.3	2.9	2.7	4.9
Communications	132	5.0	2.3	22.6	3.8	26.5
Global business lines						
iDEAS	1,610	61.0	1.8	35.7	2.7	37.0
iCORE	1,029	39.0	3.1	16.4	3.4	17.1
Client's Contribution						
Top client	84	3.2	5.6	31.6	-	-
Top 5	335	12.7	4.0	36.0	-	-
Top 10	533	20.2	2.8	36.2	-	-

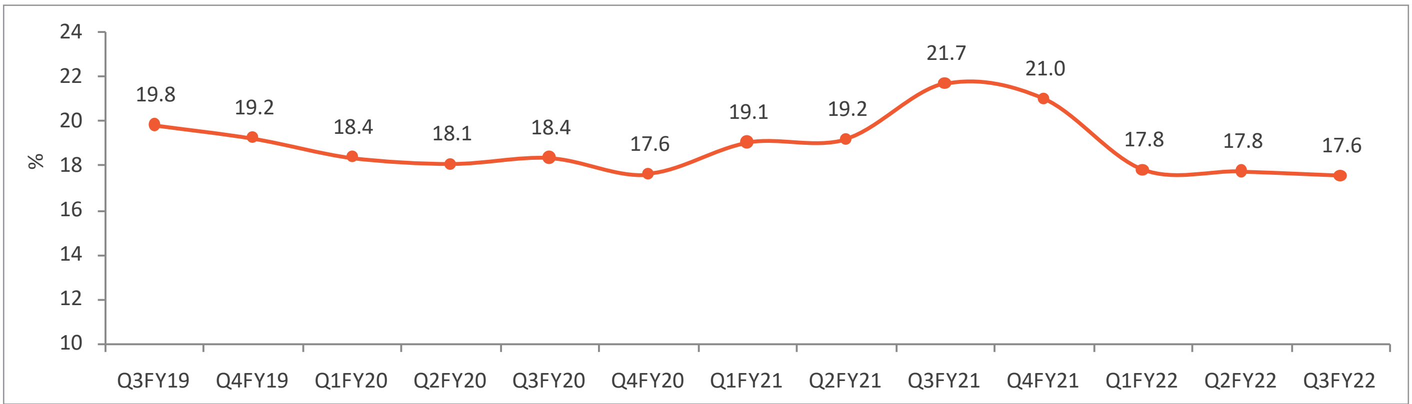
Source: Company; Sharekhan Research

Wipro' CC revenue growth trend (y-o-y)



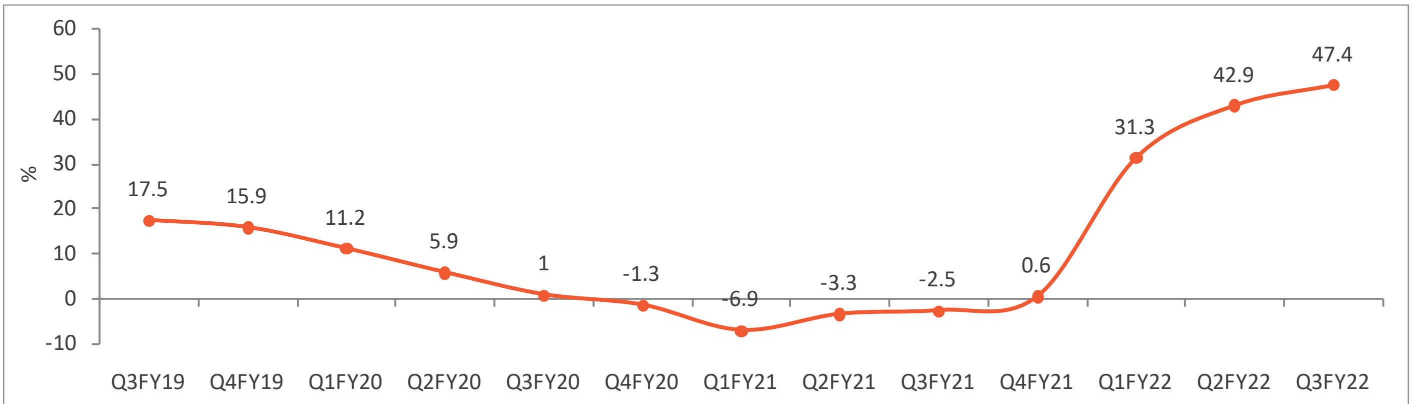
Source: Company, Sharekhan Research

EBIT margin for IT Services trend (%)



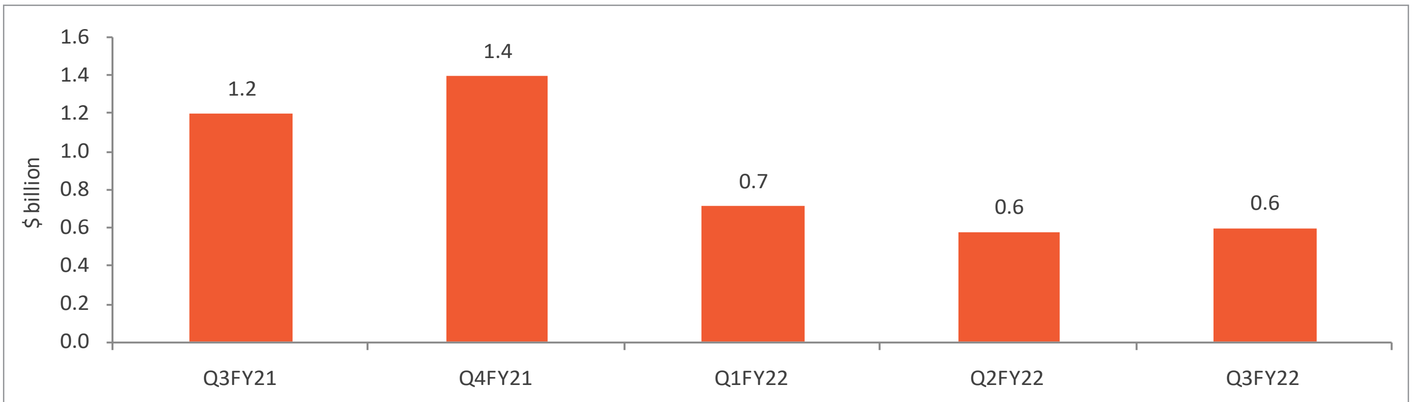
Source: Company, Sharekhan Research

Wipro' BFSI constant-currency revenue growth trend (% y-o-y)



Source: Company, Sharekhan Research

Large deal win TCVs



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Expect acceleration in technology spending going forward

The need for business continuity, operational resilience, and the switch to digital transactions have led to strong demand for cloud and digital technologies. Industry analysts such as Gartner estimate that IT services spending would grow by 7-9% over CY2021-CY2024E as compared to the average of 3.6% achieved over CY2010-CY2020. Forecasts indicate higher demand for Cloud infrastructure services, a potential increase in specialised software, potential investments in transformation projects by clients and increased online adoption across verticals.

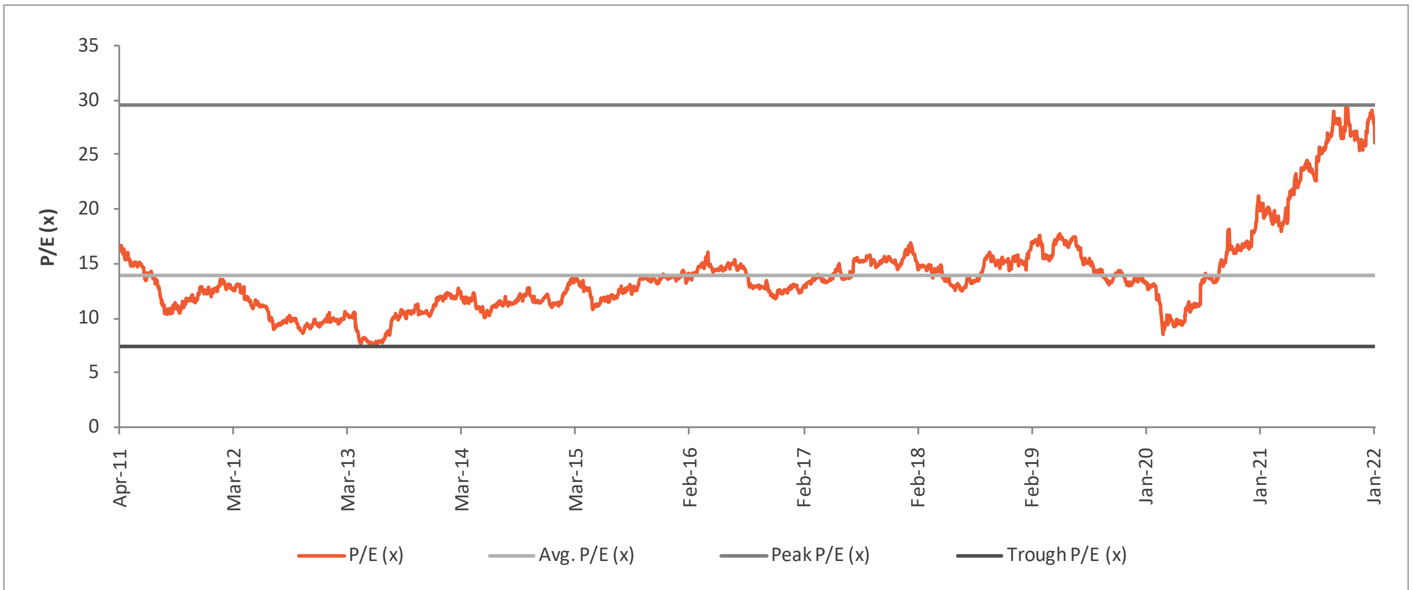
■ Company outlook - Well-placed to reduce revenue growth gap with large peers

Wipro focuses on higher client mining, enhancing digital capabilities, blend of both external and internal talent and large deal wins to drive organic revenue growth. The recent acquisition of Capco would strengthen the company's position significantly in the global financial services market. The management remains optimistic on growth of the BFSI space as demand in this sector is strong across all service offerings.

■ Valuation - Maintain Hold with a PT of Rs. 750

The new management's refreshed strategy including simplified organisation structure, sharpening focus on large deals and a client-centric and growth-focused approach has driven up organic revenue growth, healthy deal wins, new logo additions and growth in large accounts. We expect Wipro to report USD revenue/net profit CAGR of 11.6%/12.5% over FY2022-FY2024E. We believe the company has limited margin levers to offset headwinds in the coming quarters. At CMP, the stock trades at an expensive valuation of 26x/23x its FY2023/FY2024 earnings estimates. Hence, we maintain a Hold rating on Wipro with a price target (PT) of Rs. 750.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer valuation

Company	CMP (Rs / Share)	O/S Shares (Cr)	MCAP (Rs Cr)	P/E (x)		EV/EBITDA (x)		P/BV (x)		RoE (%)	
				FY22E	FY23E	FY22E	FY23E	FY22E	FY23E	FY22E	FY23E
TCS	3,898	370	14,41,761	37.6	32.3	26.7	23.0	16.2	15.8	43.6	49.5
Infosys	1,897	421	7,97,806	35.9	30.7	24.5	21.1	5.4	5.0	27.5	29.9
Wipro	650	548	3,56,203	29.1	26.1	19.8	16.9	6.2	5.5	19.7	20.9

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 2.3 lakh employees.

Investment theme

With the company's large-deal focus and customer-first approach, management hopes that its growth trajectory would catch up with the industry's average growth rates. Wipro is expected to report strong revenue growth in coming years, led by increasing deal wins, continued growth momentum in BFSI, and higher adoption of digital transformation initiatives. We expect margin headwinds to be partially offset with strong revenue growth, higher offshoring revenue, WFH efficiencies, and focus on cost synergies after the acquisition.

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 US and Europe.

Additional Data

Key management personnel

Thierry Delaporte	Chief Executive Officer
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

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Life Insurance Corp. of India	3.90
2	BlackRock Inc	0.97
3	SBI Funds Management Pvt. Limited	0.86
4	Axis Asset Management Co. Limited	0.51
5	Vanguard Group Inc	0.62
6	Norges Bank	0.46
7	Goldman Sachs Group Inc	0.33
8	Dimensional Fund Advisors	0.30
9	ICICI Prudential Asset Management	0.26
10	UTI Asset Management Co. Limited	0.21

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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by BNP PARIBAS

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