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Technology

Q4FY22 result review and earnings revision

Target price: Rs3,519

Earnings revision

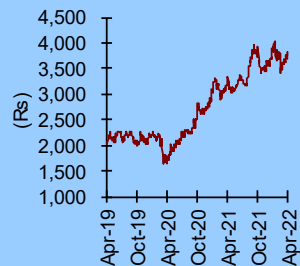
(%)	FY23E	FY24E
Sales	↑ 0.2	↑ 0.2
EBITDA	↑ 0.2	↑ 0.2
EPS	↑ 0.2	↑ 0.2

Shareholding pattern

	Jun '21	Sep '21	Dec '21
Promoters	72.2	72.2	72.2
Institutional investors	23.4	23.3	22.9
MFs and others	3.0	3.1	3.3
FIs/Bank	0.0	0.0	0.0
Insurance Cos.	4.9	4.7	4.5
FII	15.5	15.5	15.1
Others	4.4	4.6	4.9

Source: www.nseindia.com

Price chart



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INDIA

Tata Consultancy Services

HOLD

Maintain

Rs3,696

Tailwinds to be back ended...

Tata Consultancy Services (TCS) reported revenue growth of 2.6% QoQ USD terms (3.2%QoQ CC) and margins of 25% in line with our estimates. Revenue growth was broad-based across verticals with communications, BFSI and retail leading the growth. TCV was strong at US\$11.3bn (all-time high) growing 49% QoQ and 23% YoY- partly aided by two mega-deals of ~US\$1 bn each.

Company benefited on margins from reduction in travel costs in Q4FY22 (down from 0.94% of revenue to 0.50%). Apart from travel costs, every cost item moved up for TCS during the quarter. We believe these costs will further increase as companies may plan to return workers to offices (travel, facility, communications). Though TCS has better-than-peers' supply-side management, upcoming salary hikes, retention costs and wage inflation will add to the headwinds on margins.

We would like to highlight that employee addition remained strong (+35k) in Q4 with average of 23k in past three quarters, which still showcases strength in demand. Attrition rate on ltm basis increased further to 17.4%, an increase of 210 bps QoQ and 1,020 bps YoY. Demand remains democratic in nature, but its fulfilment will come at a cost, which will further dampen the earnings momentum. Talent shortage will continue even as the IT industry has added a record number of freshers. High cost to backfill attrition and retain talent will leak into margins across companies. Talent constraint exists not only offshore, but onsite as well. Tailwinds will be back-ended & headwinds will be upfront.

We are forecasting revenue growth of 11.2%/10.1% and margins of 24.8%/25% for FY23E/FY24E respectively. TCS has better-than-peers' supply-side management, breadth of capabilities and deep domain capabilities, but the stock is trading at 28.3x on FY24EPS with PEG of 2.4x – this leaves limited room for upside. We reiterate our HOLD rating on account of slowing earning growth and elevated PEG ratios with a fair value of Rs3,519 based on 27x FY24E earnings. Our estimates remain intact.

- **Inline revenues:** TCS reported revenues of US\$6,696mn, up 2.6% QoQ USD, 3.2% QoQ CC. US led with 4.5% \$ growth, growth slowed down in Continental Europe on expected lines due to anniversary of a couple of large deals, which had ramped up in Mar 2021. Growth was led by communications & media (+5.8% QoQ USD) followed by retail & CPG (+4.7% QoQ USD). Manufacturing and Life sciences grew 3.7% QoQ USD each while BFSI reported tepid growth of 2% QoQ USD. Regional markets remained flat. For the full year, TCS crossed US\$25bn in revenues, up 15.4% YoY in constant currency terms.

Market Cap	Rs13673bn/US\$180bn
Reuters/Bloomberg	TCS.BO/TCS IN
Shares Outstanding (mn)	3,699.1
52-week Range (Rs)	4019/3036
Free Float (%)	27.8
FII (%)	15.1
Daily Volume (US\$'000)	1,41,548
Absolute Return 3m (%)	(5.4)
Absolute Return 12m (%)	12.5
Sensex Return 3m (%)	(2.5)
Sensex Return 12m (%)	20.1

Year to March	FY21	FY22E	FY23E	FY24E
Revenue (Rs mn)	16,41,750	19,17,540	21,71,582	24,21,825
Net Income (Rs mn)	3,33,880	3,83,260	4,32,556	4,82,979
EPS (Rs)	89.3	103.6	117.0	130.6
% Chg YoY	3.8	3.6	16.0	12.9
P/E (x)	41.4	35.7	31.6	28.3
CEPS (Rs)	100.1	116.1	131.1	146.4
EV/E (x)	28.9	25.0	22.4	19.8
Dividend Yield (%)	1.0	1.2	2.7	2.7
RoCE (%)	32.9	36.4	38.3	38.6
RoE (%)	38.8	43.8	46.7	47.3

Please refer to important disclosures at the end of this report

- **Margins remained stable sequentially.** Margins came in at 25%, in line with estimates. The quarter witnessed headwinds from tactical interventions (-70bps) and sub-con costs (-20bps), which were offset by operational efficiencies and currency fluctuations (+10bps). Management indicated their intent to give wage hikes as per normal cycle starting from 1st April. TCS will face headwinds in the form of higher wage costs due to elevated attrition and return of discretionary expenses as majority of employees return to pre-Covid mode of working. **Attrition rate on ltm basis increased further to 17.4%, an increase of 210 bps QoQ and 1,020 bps YoY. TCS expects to give 6-8% hike in India, similar to the last year, we believe expectations will have an upward bias.**

High cost to backfill attrition and retain talent will leak into margins across companies. Talent constraint exists not only offshore, but onsite as well. Tailwinds will be back-ended & headwinds will be upfront.

- **Order book at all-time high.** Orderbook for the quarter stood at US\$11.3bn (all-time high). BFSI reported deals worth US\$3.2bn, retail US\$4.6bn and North America US\$6.1bn. Deal wins include two mega deals of ~US\$1 bn each, cumulatively adding up to ~US\$1.8 bn. Deal TCV of US\$9.5 bn ex-mega deals is strong and increased 3.3% YoY and 25% QoQ. Deal tenures are in the 7-10 year range implying cumulative average ACV of ~US\$200 mn over the deal tenure. For the full year, TCV grew 9.5% YoY.

We believe the magnitude of growth contribution of mega deals will be lower in FY23E on account of elevated supply side pressures.

- **Hiring spree continues.** TCS reported its highest-ever net addition during the quarter (~35k). Though attrition rose on LTM basis, on a quarterly annualised basis the number is plateauing and is expected to start tapering in a couple of quarters. For FY23, management has targeted to hire ~40k freshers.

TCS plans to bring 80% of workforce back to offices before initiating the move to 25*25 operating model. They have started gradual shift to office starting with 50,000 senior associates and expects majority of workforce to return to office by middle of FY23.

- **Other highlights.** Company reported a robust OCF/NI of 111% and declared dividend of Rs22 per share.

Table 1: Q4FY22 actuals vs estimates

	Q4FY22	Q3FY22	QoQ	Q4FY21	YoY	Q4FY22E-ISEC	vs our estimates
Sales (\$ m)	6,696	6,524	2.6%	5,989	11.8%	6,681	0.22%
Sales	506	488.85	3.5%	437	15.8%	503	0.56%
EBIT Margin	25.0%	25.0%	-7 bps	26.8%	-189 bps	25.0%	-4 bps
PBT	134	132	1.3%	125	6.7%	132	1.42%
Tax	34.1	33.9	0.6%	32	4.9%	32.3	5.47%
Tax Rate	25.5%	25.7%	-0.7%	25.9%	-43 bps	24.5%	98 bps
Reported PAT	99	98	1.6%	93	7.3%	99	0.14%
EPS	26.9	26.4	1.7%	25.0	7.4%	26.8	0.20%

Source: Company data, I-Sec research

Table 2: Change in estimates

	Revised		Old		Change (%)	
	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
Rs bn						
Revenues	2,172	2,422	2,168	2,418	0.2%	0.2%
EBIT	539	605	538	604	0.2%	0.2%
EBIT margin	24.8	25.0	24.8	25.0	0bps	0bps
EPS (Rs/share)	117.0	130.6	116.7	130.3	0.2%	0.2%
Revenues (US\$ mn)	28,573	31,452	28,529	31,400	0.2%	0.2%
Revenue growth (US\$, %)	11.2	10.1	11.0	10.1	10bps	0bps

Source: Company data, I-Sec research

Table 3: Segmental growth

	Revenues (US\$ mn)	QoQ (%)	YoY (%)	% of total	YoY CC growth (%)
Total Revenues	6,696	2.6	11.8	100.0	14.3
Revenue by geography					
North America	3,455	4.5	18.7	51.6	18.7
Latin America	114	2.6	18.8	1.7	20.6
UK	1,045	2.6	9.0	15.6	13.0
Continental Europe	1,038	(0.6)	3.2	15.5	10.1
India	341	(4.8)	(4.8)	5.1	7.0
Asia Pacific	569	1.4	1.1	8.5	5.5
MEA	134	8.0	11.8	2.0	7.3
Revenue by verticals					
BFSI	2,136	2.0	10.8	31.9	12.9
Retail & CPG	1,031	4.7	18.7	15.4	22.1
Communication & Media	449	5.8	15.2	6.7	18.7
Manufacturing	670	3.7	16.5	10.0	19.0
Life sciences & healthcare	670	3.7	15.3	10.0	16.4
Technology & services	583	2.6	15.8	8.7	18.0
Regional markets & others	1,158	(0.2)	1.3	17.3	4.0

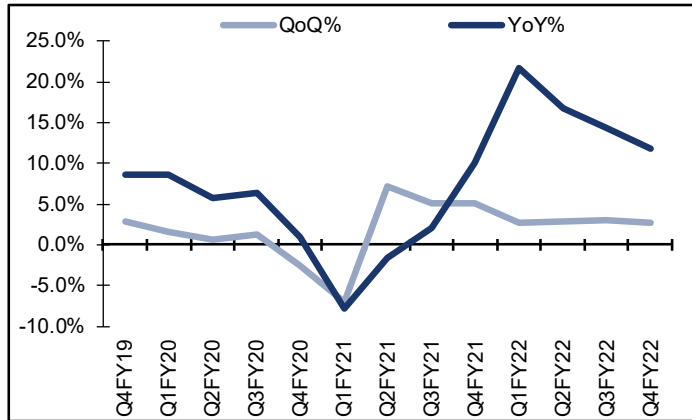
Source: Company data, I-Sec research

Table 4: All costs are gradually increasing...

	Q1FY21	Q2FY21	Q3FY21	Q4FY21	Q1FY22	Q2FY22	Q3FY22	Q4FY22
COGS								
Employee Cost	45.32%	44.52%	43.72%	42.43%	44.39%	44.00%	43.29%	43.87%
Fees to External Consultants	7.71%	7.22%	7.14%	8.49%	8.25%	8.62%	8.95%	9.16%
Cost of Equipment and Software Licenses	0.90%	0.66%	0.71%	1.04%	0.57%	0.45%	0.88%	0.51%
Depreciation	1.90%	1.89%	1.90%	1.88%	1.85%	1.86%	1.90%	1.82%
Travel	0.61%	0.54%	0.48%	0.49%	0.61%	0.65%	0.94%	0.50%
Communication	0.86%	0.89%	0.95%	0.85%	0.81%	0.79%	0.77%	0.83%
Facility Expenses	0.87%	0.81%	0.71%	0.85%	0.74%	0.67%	0.74%	0.68%
Other Costs	2.40%	2.55%	2.14%	2.75%	2.41%	2.52%	2.52%	2.50%
SG&A								
Employee Cost	0.28%	0.38%	0.48%	0.38%	0.34%	0.32%	0.29%	0.33%
Fees to External Consultants	0.14%	0.19%	0.24%	0.09%	0.09%	0.07%	0.09%	0.03%
Provision for Doubtful Debts	0.65%	0.60%	0.48%	0.56%	0.52%	0.51%	0.54%	0.58%
Depreciation	0.53%	0.43%	0.48%	0.44%	0.40%	0.38%	0.43%	0.42%
Facility Expenses	0.14%	0.16%	0.24%	0.10%	0.15%	0.18%	0.10%	0.17%
Travel	0.34%	0.30%	0.24%	0.27%	0.28%	0.23%	0.28%	0.29%
Communication	1.41%	0.70%	0.71%	0.92%	0.98%	0.83%	0.95%	1.16%
Other Costs	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%

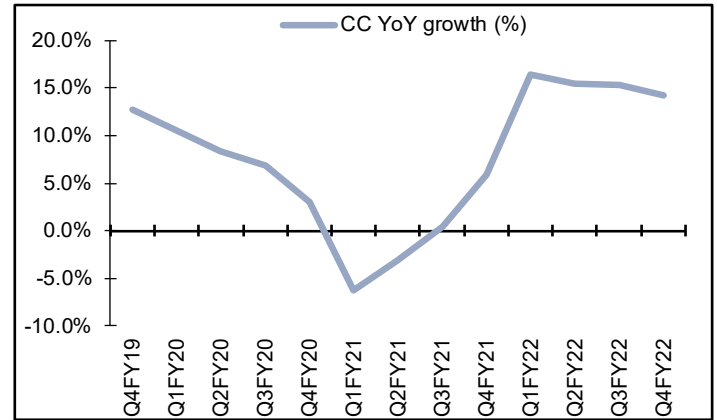
Source: Company data, I-Sec research

Chart 1: Steady QoQ growth at 2.6%



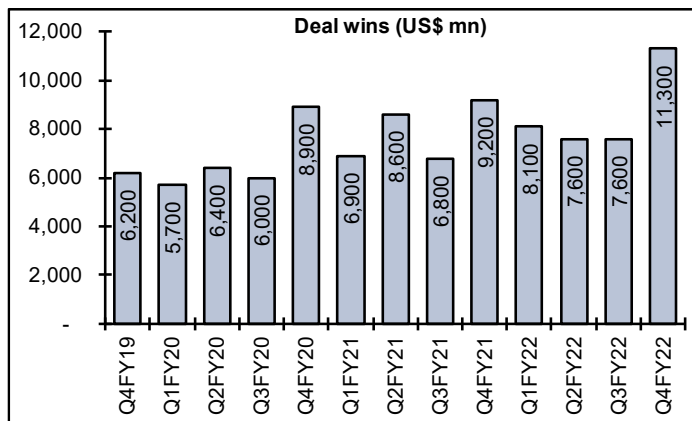
Source: Company, I-Sec research

Chart 2: Healthy growth of 14.3% YoY CC



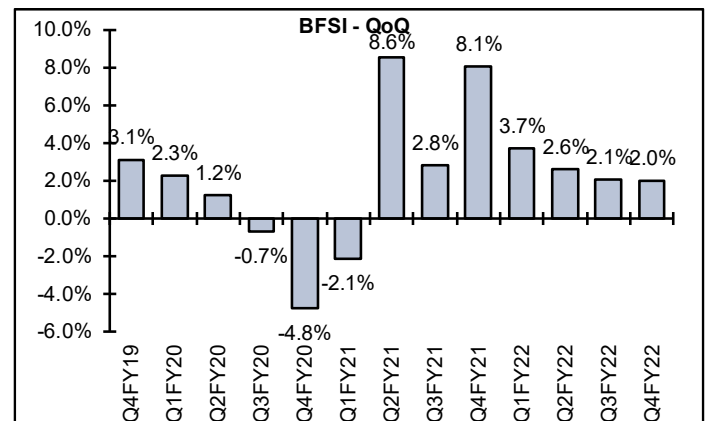
Source: Company, I-Sec research

Chart 3: Company reported highest ever TCV



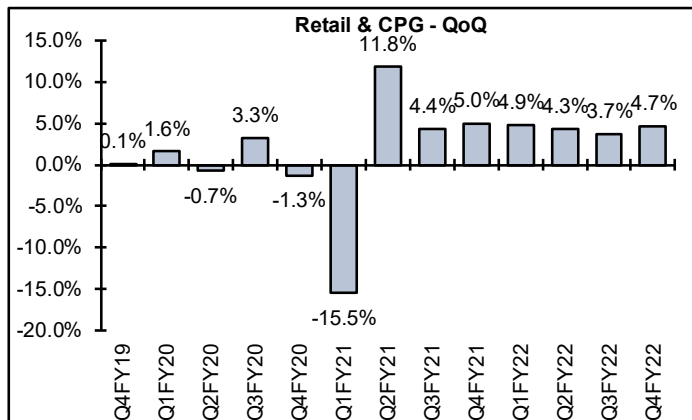
Source: Company, I-Sec research

Chart 4: BFSI growth remained steady



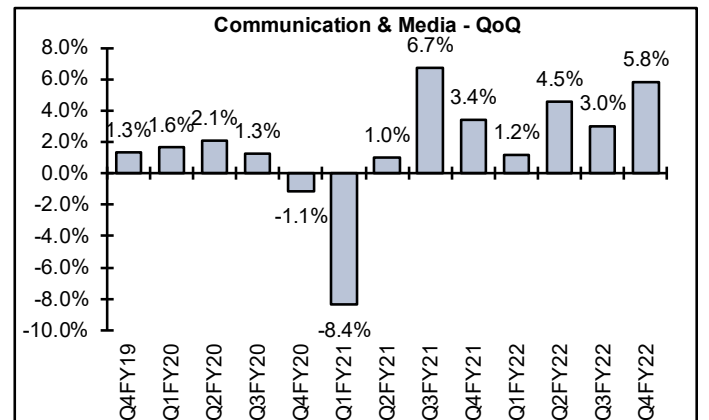
Source: Company, I-Sec research

Chart 5: Retail & CPG saw uptick in growth



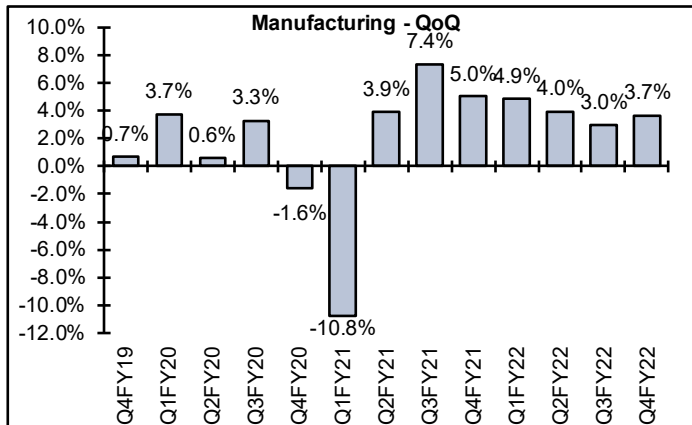
Source: Company, I-Sec research

Chart 6: Communications & Media led growth



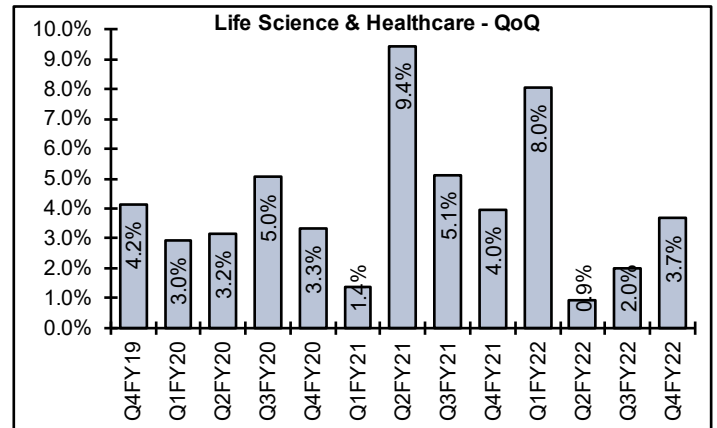
Source: Company, I-Sec research

Chart 7: Robust growth in Manufacturing



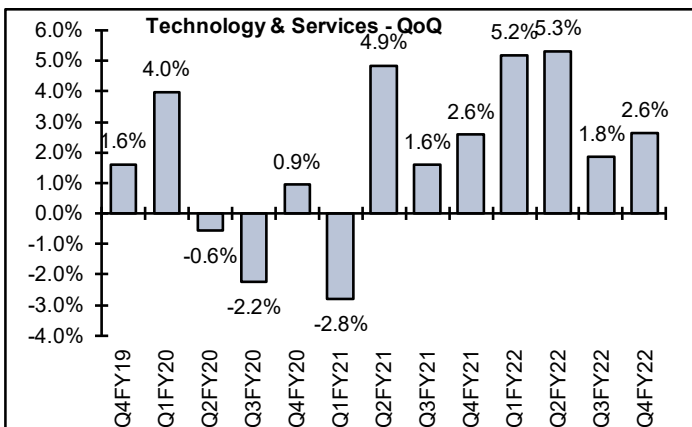
Source: Company, I-Sec research

Chart 8: Growth picked up in Life Sciences



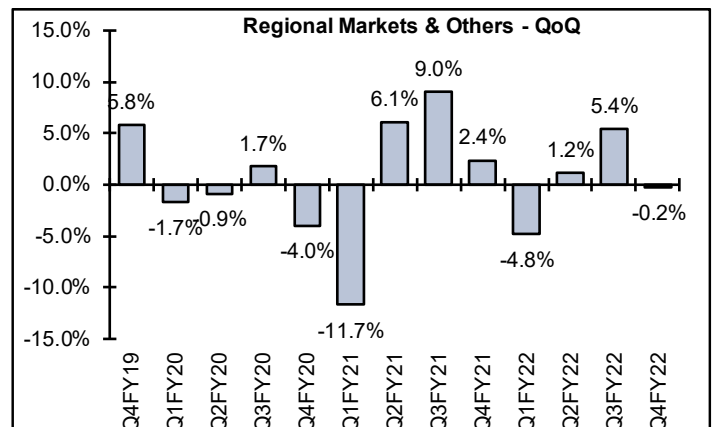
Source: Company, I-Sec research

Chart 9: Growth stabilising in Tech. & services



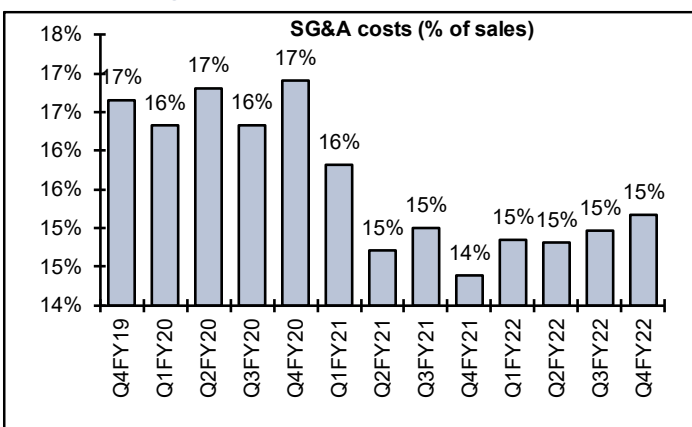
Source: Company, I-Sec research

Chart 10: Regional markets growth remained flat



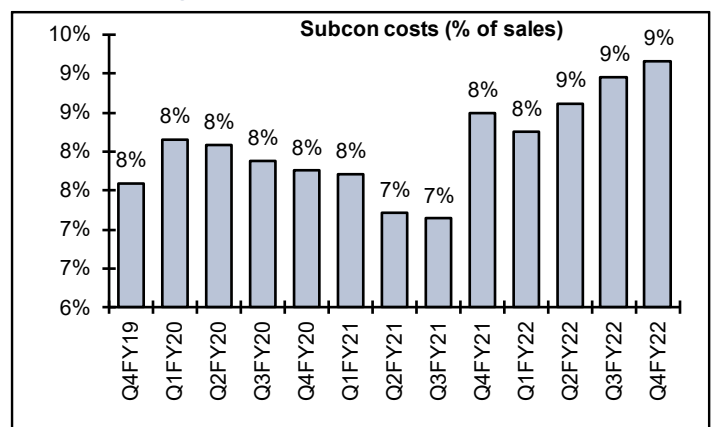
Source: Company, I-Sec research

Chart 11: Slight increase in SG&A costs



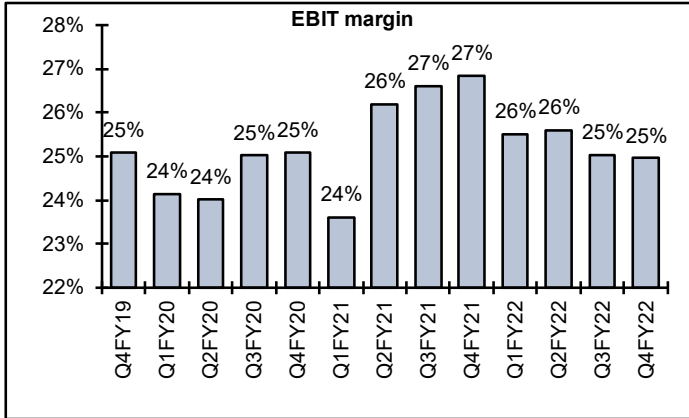
Source: Company, I-Sec research

Chart 12: Slight increase in sub-con costs



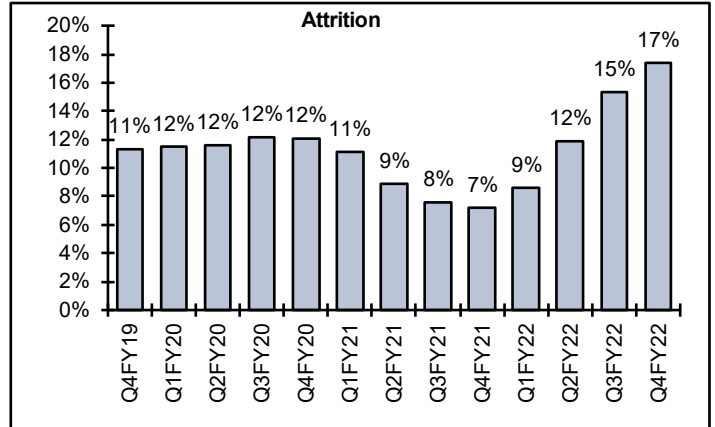
Source: Company, I-Sec research

Chart 13: Margins remained stable



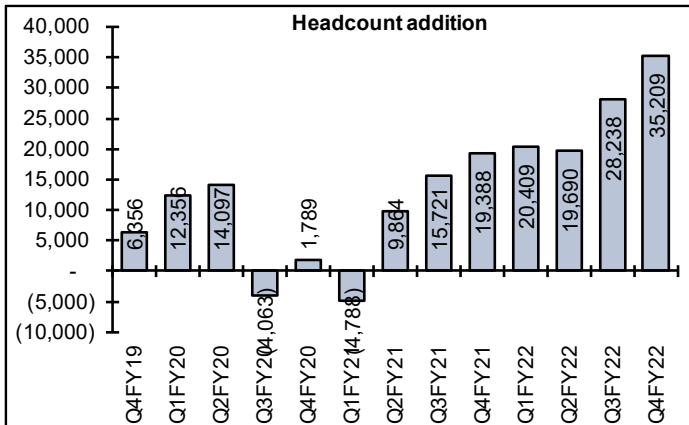
Source: Company, I-Sec research

Chart 14: Attrition rose on LTM basis



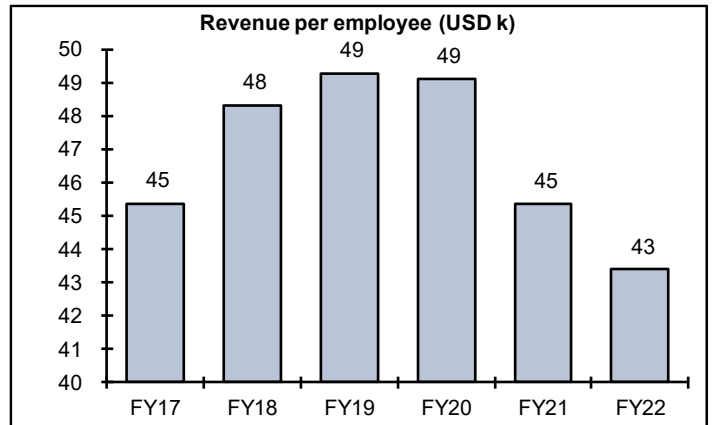
Source: Company, I-Sec research

Chart 15: Highest headcount addition in a quarter



Source: Company, I-Sec research

Chart 16: Decline was led by expanding base



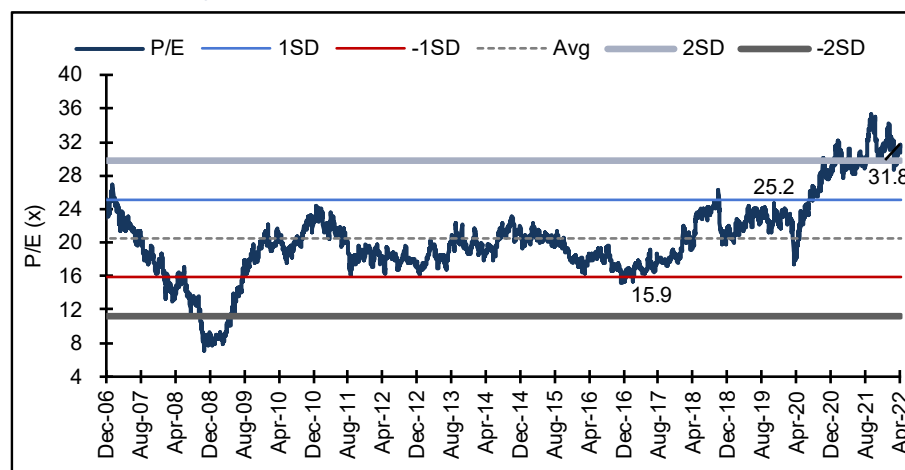
Source: Company, I-Sec research

Table 5: TCS Summary

Rs bn	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
USD Rev (mn)	19,089	20,913	22,031	22,174	25,706	28,573	31,452
YoY	8.6%	9.6%	5.3%	0.6%	15.9%	11.2%	10.1%
Revenues	1,231	1,465	1,569	1,642	1,918	2,172	2,422
YoY	4.4%	19.0%	7.2%	4.6%	16.8%	13.2%	11.5%
EBIT	305	375	386	425	485	539	605
Margin	24.8%	25.6%	24.6%	25.9%	25.3%	24.8%	25.0%
PAT	258	315	323	334	383	433	483
EPS (Rs)	67	83	86	89	104	117	131
Payout	106%	43%	102%	90%	91%	84%	75%
OCF	251	286	324	388	399	402	453
FCF	232	264	291	361	375	346	391
RoE	29%	35%	36%	39%	44%	47%	47%
P/E	54.8	44.5	42.9	41.4	35.7	31.6	28.3

Source: Company data, I-Sec research

Chart 17: One year forward PE



Source: Bloomberg, I-Sec research.

Financial summary

Table 6: Profit and Loss statement

(Rs mn, year ending March 31)

	FY21	FY22E	FY23E	FY24E
Revenues (US\$ mn)	22,174	25,706	28,573	31,452
Operating Revenues (Sales)	16,41,750	19,17,540	21,71,582	24,21,825
Operating Expenses	11,76,360	13,86,980	15,80,793	17,58,245
EBITDA	4,65,390	5,30,560	5,90,788	6,63,580
% margin	28.3	27.7	27.2	27.4
Depreciation & Amortisation	40,560	46,030	52,118	58,124
EBIT	4,24,830	4,84,530	5,38,670	6,05,456
% margin	25.9	25.3	24.8	25.0
Other Income	24,940	32,330	36,000	36,000
Recurring PBT	4,49,770	5,16,860	5,74,670	6,41,456
Add: Extraordinaries	0	0	0	0
Less: Taxes	1,14,580	1,32,380	1,40,794	1,57,157
Add: Earnings in Affiliates	0	0	0	0
Less: Minority Interest	-1,310	-1,220	-1,320	-1,320
Net Income (Reported)	3,33,880	3,83,260	4,32,556	4,82,979

Source: Company data, I-Sec research

Table 7: Balance sheet

(Rs mn, year ending March 31)

	FY21	FY22E	FY23E	FY24E
Net Worth	8,59,690	8,91,390	9,61,656	10,82,346
Minority Interest	6,750	7,070	8,390	9,710
Other Long term liabilities	95,100	93,170	93,170	93,170
Total liabilities	9,61,540	9,91,630	10,63,216	11,85,226
Net Block	1,96,660	1,96,150	2,00,150	2,04,150
Intangibles	22,800	28,880	28,880	28,880
Other LT assets	94,640	1,07,010	1,07,010	1,07,010
Curr. Assets	9,90,340	10,82,484	11,64,096	13,02,793
Debtors	3,66,800	4,17,434	4,63,569	5,14,910
Cash & Bank Balance	68,500	1,24,880	1,49,104	2,23,936
Other Current Assets	5,55,040	5,40,170	5,51,423	5,63,946
Current Liab. & Prov	3,42,900	4,22,894	4,36,919	4,57,607
Net Current Assets	6,47,440	6,59,590	7,27,176	8,45,186
Application of Funds	9,61,540	9,91,630	10,63,216	11,85,226

Source: Company data, I-Sec Research

Table 8: Quarterly trend

(Rs mn, year ending March 31)

	Jun-21	Sep-21	Dec-21	Mar-22
Net sales	4,54,110	4,68,670	4,88,850	5,05,910
% growth (YoY)	3.9	3.2	4.3	3.5
EBITDA	1,26,630	1,31,150	1,34,330	1,38,450
Margin (%)	27.9	28.0	27.5	27.4
Other income	5,740	9,690	9,540	7,360
Extraordinaries Inc / (Loss)	0	0	0	0
Recurring Net Income	90,070	96,240	97,690	99,260

Source: Company data, I-Sec research

Table 9: Cashflow statement

(Rs mn, year ending March 31)

	FY21	FY22E	FY23E	FY24E
CF from Operations	3,74,390	4,15,700	4,48,674	5,05,103
Cash for Working Capital	12,610	(16,210)	(46,497)	(51,970)
Net Operating CF	3,87,000	3,99,490	4,02,177	4,53,133
Net Purchase of FA	(27,000)	(24,830)	(56,118)	(62,124)
Free Cashflow	3,60,000	3,74,660	3,46,059	3,91,010
Net Purchase of Invest.	(54,000)	15,860	36,000	36,000
Net Cash from Invest.	(81,000)	(8,970)	(20,118)	(26,124)
Proceeds from LTB/STB	-	-	2,518	8,792
Others	(19,000)	(22,550)	1,320	1,320
Dividend Payments	(3,06,000)	(3,13,260)	(3,62,290)	(3,62,290)
Cashflow from Fin.	(3,25,000)	(3,35,810)	(3,58,452)	(3,52,177)
Net Cashflow	(19,000)	54,710	23,608	74,832

Source: Company data, I-Sec research

Table 10: Key ratios

(Year ending March 31)

	FY21	FY22E	FY23E	FY24E
Per Share Data (Rs)				
Diluted Recurring EPS	89.3	103.6	117.0	130.6
Recurring Cash EPS	100.1	116.1	131.1	146.4
Dividend per share (DPS)	38.0	43.0	98.0	98.0
Book Value per share (BV)	229.9	241.0	260.1	292.8
Growth Ratios (%)				
Operating Income (Sales) - US\$	0.6	15.9	11.2	10.1
Operating Income (Sales)	4.6	16.8	13.2	11.5
EBIT	10.1	14.1	11.2	12.4
Recurring Net Income	3.2	14.8	12.9	11.7
Diluted Recurring EPS	3.8	3.6	16.0	12.9
Diluted Recurring CEPS	4.8	15.9	13.0	11.6
Valuation Ratios (x)				
P/E	41.4	35.7	31.6	28.3
P/CEPS	36.9	31.8	28.2	25.3
P/BV	16.1	15.3	14.2	12.6
EV / EBITDA	28.9	25.0	22.4	19.8
EV / Sales	8.2	6.9	6.1	5.4
Operating Ratios				
Other Income / PBT (%)	5.5	6.3	6.3	5.6
Effective Tax Rate (%)	25.5	25.6	24.5	24.5
Fixed Asset Turnover (x) on average	8.3	9.8	10.8	11.9
Receivables (days)	82	79	78	78
Return/Profitability Ratios (%)				
Recurring Net Income Margins	20.3	20.0	19.9	19.9
RoIC	65.3	84.3	85.5	87.4
RoCE	32.9	36.4	38.3	38.6
RoNW	38.8	43.8	46.7	47.3
Dividend Payout Ratio	42.6	41.5	83.8	75.0
Dividend Yield	1.0	1.2	2.7	2.7
EBITDA Margins	28.3	27.7	27.2	27.4
EBIT Margins	25.9	25.3	24.8	25.0

Source: Company data, I-Sec research

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