

Estimate change



TP change



Rating change



Motilal Oswal values your support in the Asiamoney Brokers Poll 2022 for India Research, Sales, Corporate Access and Trading team. We request your ballot.



Bloomberg	TCS IN
Equity Shares (m)	3,752
M.Cap.(INRb)/(USD b)	11946.3 / 150.7
52-Week Range (INR)	4046 / 3023
1, 6, 12 Rel. Per (%)	-3/-6/-3
12M Avg Val (INR M)	9715
Free float (%)	27.7

Financials & Valuations (INR b)

Y/E Mar	2022	2023E	2024E
Sales	1,918	2,221	2,428
EBIT Margin (%)	25.3	24.2	25.0
PAT	384	429	487
EPS (INR)	104.0	117.2	133.1
EPS Gr. (%)	19.9	12.7	13.5
BV/Sh. (INR)	242	252	260

Ratios

RoE (%)	43.7	47.2	52.0
RoCE (%)	36.8	39.8	43.4
Payout (%)	97.1	80.0	80.0

Valuations

P/E (x)	31.4	27.9	24.5
P/BV (x)	13.5	13.0	12.5
EV/EBITDA (x)	22.4	19.9	17.7
Div Yield (%)	3.1	2.9	3.3

Shareholding pattern (%)

As On	Mar-22	Dec-21	Mar-21
Promoter	72.3	72.2	72.2
DII	7.9	8.0	7.9
FII	14.2	15.0	15.6
Others	5.7	4.9	4.3

FII Includes depository receipts

CMP: INR3,265
TP: INR3,730 (+14%)
Buy

Well placed to ride out macro headwinds

Supply-led drag on margins to moderate in H2 FY23

- TCS reported revenue of USD6.7b in 1QFY23, up 3.5%/1.3% QoQ in constant currency (CC)/USD terms, in-line with our estimates. Revenue in 1QFY23 was led by Retail & CPG, while regional markets remain a drag. It reported deal TCV of USD8.2b (flat YoY, book-to-bill ratio at 1.2x), in-line with its historical trajectory, although down 27% from its 4QFY22 record booking.
- Q1 EBIT margin was at multi-year low, as it dipped 190bp QoQ to 23.1% (vs. our estimate of 23.9%) due to elevated supply side pressure. Wage hike in Q1 negatively impacted EBIT margins by 150bp. Elevated attrition, all time high subcontractor cost and resumption of travel expenses also impacted margins during the quarter. Lower other income also resulted in lower Net Profit, down 4% QoQ to INR95b.
- As expected, management commentary on the demand environment and deal pipeline remained intact with no visible impact of weakening macro environment, although they remain watchful. Despite intact commentary, they indicated that the US will do better than Europe, due to client concerns over the slowdown. In our view, this is an initial sign of industry commentary turning more realistic vs the current view of no impact on tech spends. We are factoring in TCS revenue growth of 10.2% YoY in CC terms in FY23 (vs 15.5% in Q1), as the growth moderates in H2 FY23.
- The drop in margins was higher than our expectation, led by elevated salary hikes and subcontractor expenses. Given elevated attrition and TCS focus on growth, we expect EBIT margin in FY23 to decline 110bps YoY to 24.2% (vs 26-28% medium-term guidance). Moreover, with an exit margin guidance of 25%, FY24 EBIT margin should also remain below target guidance (MOFSLe of 25%) despite a favorable pricing environment. In addition, TCS should start seeing some benefit in overall cost in FY23 with a fresher hiring of 100K in FY22.
- Q1 LTM attrition rose 230bp QoQ to 19.7%. The management indicated that attrition will remain elevated in 2Q, before normalizing from 3Q. TCS generated FCF of INR 101b in 1Q, leading to total cash and investments at the end of quarter at INR 528b. It also gave a dividend of INR 8/share.
- We have tweaked our FY23/FY24 EPS by ~4% to account for lower margins. We expect a USD revenue CAGR of 9.3% over FY22-24 and INR EPS CAGR of 13.1% during the same period. Our TP of INR3,730 implies 28x FY24E EPS, with a 14% upside potential. We maintain our **Buy** rating on the stock.

In-line topline performance but miss margin on high employee cost

- Revenue (CC) grew 3.5% QoQ, INR EBIT/INR PAT rose 5% YoY each in 1QFY23.
- EBIT margin of 23.1% (down 190bps QoQ) was below our estimate of 23.9%
- It added 14k associates (the lowest net adds in the last seven quarters), although it was on an all-time high Q4 base.
- TCS announced a dividend of INR8/share.

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Investors are advised to refer through important disclosures made at the last page of the Research Report.

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Key highlights from the management commentary

- TCS continues to see a strong demand environment, with clients maintaining spend in Cloud adoption, operating model transformation and vendor consolidation.
- Management indicated a good visibility on the pipeline over the next few months. It is not witnessing any budget cuts or deferrals in client spend, although some European clients have expressed concerns on macro-economic demand. It expects North America to lead the growth in FY23.
- TCS expects margins to improve sequentially for the remaining quarters of FY23, leading to flat YoY margins by Q4.

Valuation and view

- Increase in interest rates, slow economic growth, and elevated geo-political tensions have impacted the macro environment and raised concerns over IT spends.
- Given TCS' size, order book, and exposure to long duration orders, and portfolio, it is well positioned to withstand the weakening macro environment and ride on the anticipated industry growth.
- TCS has consistently maintained its market leadership position and shown best-in-class execution. It allows the company to maintain its industry-leading margin and demonstrate superior return ratios.
- We maintain our positive stance on TCS. Our TP of INR3,730 implies 28x FY24E EPS, with a 14% upside potential. We reiterate our **Buy** rating.

Quarterly performance (IFRS)

Y/E March	FY22				FY23E				FY22	FY23E	(INR b)	
	1Q	2Q	3Q	4Q	1Q	2QE	3QE	4QE			FY23	Variance
											1QE	(%/bp)
Revenue from IT Services (USD m)	6,154	6,333	6,524	6,696	6,780	6,980	7,121	7,338	25,707	28,220	6,795	-0.2
QoQ (%)	2.8	2.9	3.0	2.6	1.3	3.0	2.0	3.1	15.9	9.8	1.5	-23bp
Overall revenue (INR b)	454	469	489	506	528	551	563	580	1,918	2,221	523	0.8
QoQ (%)	3.9	3.2	4.3	3.5	4.3	4.5	2.0	3.1			3.4	86bp
YoY (%)	18.5	16.8	16.4	15.8	16.2	17.7	15.1	14.6	16.8	15.8	15.2	96bp
GPM (%)	40.4	40.4	40.0	40.1	38.4	38.9	39.3	39.9	40.2	39.1	38.7	-28bp
SGA (%)	14.8	14.8	15.0	15.2	15.3	14.8	14.8	14.8	15.0	14.9	14.8	52bp
EBITDA	127	131	134	138	133	144	149	157	530	584	136	-2.3
EBITDA Margin (%)	27.9	28.0	27.4	27.4	25.2	26.2	26.6	27.1	27.7	26.3	26.0	-81bp
EBIT	116	120	122	126	122	133	138	145	485	538	125	-2.6
EBIT Margin (%)	25.5	25.6	25.0	25.0	23.1	24.1	24.5	25.1	25.3	24.2	23.9	-80bp
Other Income	6	10	10	7	6	9	10	10	32	35	9	-33.7
PBT	122	130	132	134	128	142	147	155	517	573	134	-4.6
ETR (%)	25.8	25.6	25.7	25.5	25.5	25.0	25.0	25.0	25.6	25.1	25.0	49bp
Adj. PAT	90	97	98	100	95	107	111	116	384	429	100	-5.2
Exceptional Items	0	0	0	0	0	0	0	0	0	0	0	
Reported PAT	90	97	98	100	95	107	111	116	384	429	100	-5.2
QoQ (%)	-2.7	6.9	1.6	1.6	-4.4	12.1	3.6	5.4			0.9	-529bp
YoY (%)	28.1	28.6	12.4	7.3	5.4	10.5	12.7	17.0	18.1	11.6	11.2	-584bp
EPS (INR)	24.4	26.0	26.4	27.2	26.0	29.2	30.2	31.9	104.0	117.2	27.6	-5.9

Key performance indicators

Y/E March	FY22				FY23E				FY22	FY23E
	1Q	2Q	3Q	4Q	1Q	2QE	3QE	4QE		
Revenue (QoQ CC %)	2.4	4.0	3.9	3.2	3.5				14.3	
Costs (as a percentage of revenue)										
COGS	59.6	59.6	60.0	59.9	61.6	61.1	60.7	60.1	59.8	60.9
SGA	14.8	14.8	15.0	15.2	15.3	14.8	14.8	14.8	15.0	14.9
Margins										
Gross Margin	40.4	40.4	40.0	40.1	38.4	38.9	39.3	39.9	40.2	39.1
EBIT Margin	25.5	25.6	25.0	25.0	23.1	24.1	24.5	25.1	25.3	24.2
Net Margin	19.9	20.6	20.1	19.7	18.0	19.4	19.7	20.1	20.1	19.3
Operating Metrics										
Headcount (k)	509	529	557	592	606				509	
Attrition (%)	8.6	11.9	15.3	17.4	17.4				8.6	
Deal win TCV (USD b)	8.1	7.6	7.6	11.3	8.2				32.7	
Key verticals (YoY CC %)										
BFSI	19.3	17.0	17.9	12.9	13.9				16.7	
Retail	21.7	18.4	20.4	22.1	25.1				20.6	
Key geographies (YoY CC %)										
North America	15.8	17.4	18.0	18.7	19.1				17.5	
UK	16.3	15.6	12.7	13.0	12.6				14.3	
Continental Europe	19.7	13.5	17.5	10.1	12.1				15.1	



Highlights from the management commentary

1QFY23 performance and demand outlook

- In 1QFY23, TCS reported revenue growth of 1.3% QoQ and 10.2% YoY in USD terms and 3.5% QoQ and 15.5% in CC terms.
- All verticals performed well, with Retail and CPG leading at 25% YoY growth.
- Q1 TCV was USD8.2b, with two USD 400mn+ deals. Other small to medium sized deals included USD2.6b from the BFSI segment and USD1.2b from the Retail segment. North America posted a TCV of USD4.5b.
- TCS continues to see a strong demand environment, with clients Cloud adoption, operating model transformation, and vendor consolidation.
- Management indicated a good visibility of the pipeline over the next few months. It is not witnessing any budget cuts or deferrals in client spend, although some European clients have expressed concerns on macro-economic demand. It expects North America to lead the growth in FY23.

Margin performance and outlook

- Operating margins were 23.1% in 1QFY23, down 190bps QoQ and 240bps YoY. There was a 150bp impact of wage hikes. In addition, the company saw an increase in expenses such as backfilling due to high attrition, higher subcontractor expenses, and travel normalization. This was partially compensated by operating efficiencies and currency movements (+25bps).
- TCS announced wage hikes of 5-8% in Q1, with onsite hikes of 4-5%.
- TCS expects margins to improve sequentially for the rest of FY23, leading to flat YoY margins by Q4.
- Pricing continues to be supportive, although they are seeing more specific impact rather than large scale hikes. On an aggregate basis, impact of price hikes is still not positive due to higher employee expenditure.

Other highlights

- The company added 14k employees in Q1, with limited fresher hires due to seasonality. It continues to target hiring c40k freshers in FY23.
- LTM attrition in IT services was at 19.7% in Q1 and the company expects it to rise further in Q2, before moderating in the second half of the current year.

Exhibit 1: Growth led by Latin America

Geographies	Contribution to revenue (%)	QoQ growth (%)
North America	53.2	4.4
Latin America	1.8	7.2
UK	14.9	-3.3
Continental Europe	15.2	-0.7
India	4.8	-4.7
Asia Pacific	8.3	-1.1
MEA	1.8	-8.9

Source: Company, MOFSL

Exhibit 2: Retail and CPG witness strong growth

Verticals	Contribution to revenue (%)	QoQ CC growth (%)
BFSI	32.1	1.9
Retail and CPG	15.9	4.5
Communications and Media	6.8	2.8
Manufacturing	9.9	0.2
Life Sciences and Healthcare	10.1	2.3
Technology and Services	8.8	2.4
Regional Markets and Others	16.4	-4.0

Source: Company, MOFSL

Maintain Buy with a TP of INR3,730

- Increase in interest rates, slow economic growth, and elevated geo-political tensions have impacted the macro environment and raised concerns over IT spends.
- Given TCS' size, capabilities, and portfolio stretch, it is rightly positioned to withstand the weakening macro environment and ride on the anticipated industry growth.
- TCS has consistently maintained its market leadership position and shown best-in-class execution. This allows the company to maintain its industry-leading margin and demonstrate superior return ratios.
- We maintain our positive stance on TCS. Our TP of INR3,730 implies 28x FY24E EPS, with a 14% upside potential. We reiterate our **Buy** rating.

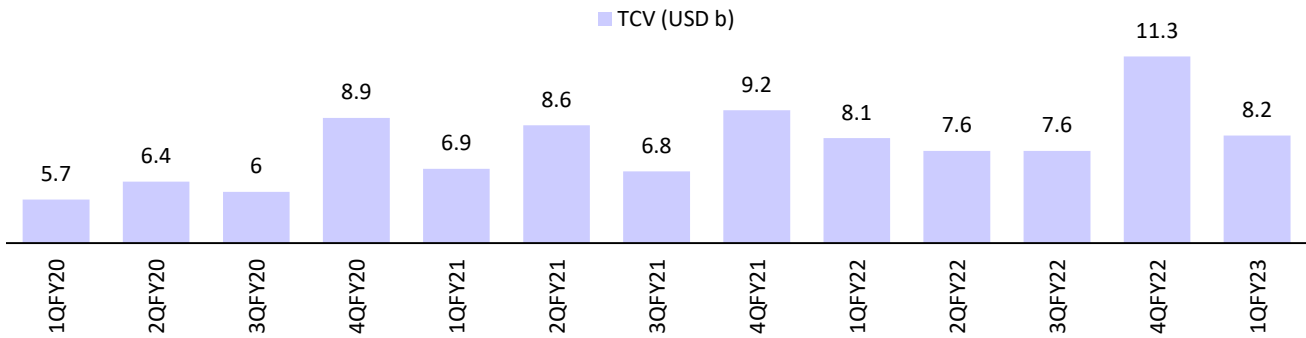
Exhibit 3: Revisions to our estimates

	Revised		Earlier		Change	
	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
USD:INR	78.7	79.0	78.5	79.0	0.3%	0.0%
USD revenue (m)	28,220	30,731	28,188	31,335	0.1%	-1.9%
Growth (%)	9.8	8.9	9.7	11.2	10bps	-230bps
EBIT margin (%)	24.2	25.0	24.9	25.3	-70bps	-20bps
PAT (INR b)	428	485	444	503.7	-3.8%	-3.6%
EPS	117.2	133.1	121.8	138.1	-3.8%	-3.6%

Source: MOFSL

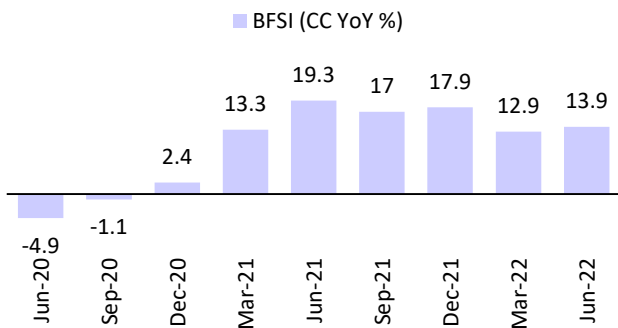
Story in charts

Exhibit 4: TCS reports modest deal wins in 1QFY23



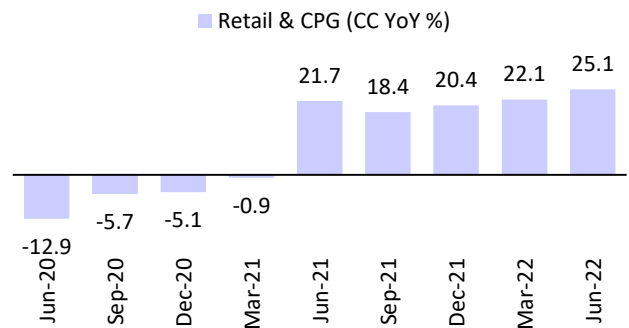
Source: Company, MOFSL

Exhibit 5: Strong growth in BFSI...



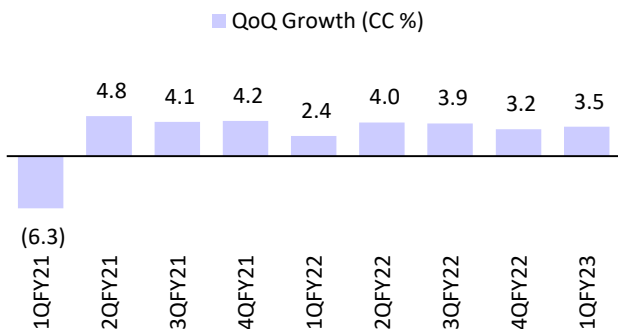
Source: Company, MOFSL

Exhibit 6: ...and in Retail



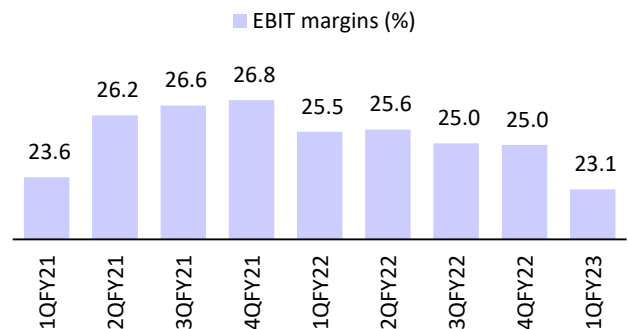
Source: Company, MOFSL

Exhibit 7: TCS delivers strong growth in 1QFY23



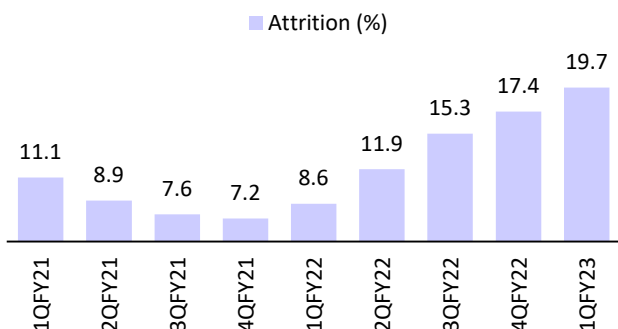
Source: Company, MOFSL

Exhibit 8: Margins take a hit due to high employee cost



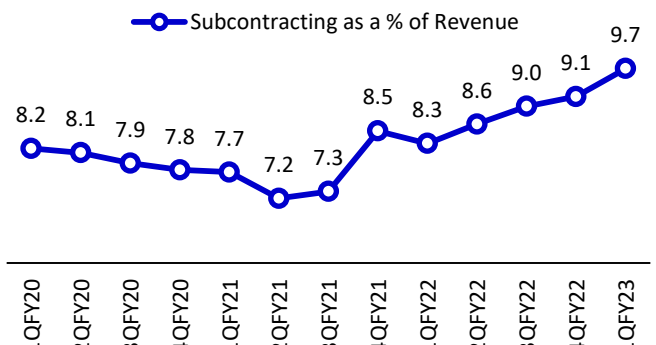
Source: Company, MOFSL

Exhibit 9: Attrition jumps to 19.7%



Source: Company, MOFSL

Exhibit 10: Sub-contracting cost rose 60bp QoQ



Source: Company, MOFSL

Operating metrics

Exhibit 11: Operating metrics

	1QFY21	2QFY21	3QFY21	4QFY21	1QFY22	2QFY22	3QFY22	4QFY22	1QFY23
Verticals (%)									
BFSI	31.3	31.9	31.3	32.2	32.5	32.4	32.1	31.9	32.1
Retail and CPG	14	14.6	14.5	14.5	14.8	15.0	14.5	15.4	15.9
Communications and Media	7.1	6.5	6.6	6.5	6.4	6.5	6.6	6.7	6.8
Manufacturing	9.7	9.4	9.6	9.6	9.8	9.9	9.6	10.0	9.9
Life Sciences and Healthcare	9.6	9.8	9.8	9.7	10.2	10.0	9.8	10.0	10.1
Technology and Services	9.1	8.9	8.6	8.4	8.6	8.8	8.6	8.7	8.8
Regional markets and others	19.2	18.9	19.6	19.1	17.7	17.4	18.8	17.3	16.4
Geographies (%)									
North America	51.4	49.9	49.1	48.6	49.4	50.3	50.7	51.6	53.2
Latin America	1.7	1.7	1.7	1.6	1.6	1.6	1.7	1.7	1.8
UK	15.3	15.5	15.7	16.0	16.3	16.1	15.6	15.6	14.9
Continental Europe	15.6	16.3	16.2	16.8	16.7	15.9	16.0	15.5	15.2
India	4.3	5.0	5.6	5.6	4.6	5.1	5.5	5.1	4.8
Asia Pacific	9.8	9.7	9.7	9.4	9.3	9.0	8.6	8.5	8.3
MEA	1.9	1.9	2	2	2.1	2.0	1.9	2.0	1.8
QoQ growth (%)									
BFSI	(2.1)	9.3	3.1	8.1	3.7	2.6	2.1	2.0	1.9
Retail and CPG	(15.5)	11.8	4.4	5.0	4.9	4.3	-0.4	9.0	4.5
Communications and Media	(8.4)	(1.8)	6.7	3.4	1.2	4.5	4.6	4.2	2.8
Manufacturing	(10.8)	3.9	7.4	5.0	4.9	4.0	-0.1	6.9	0.2
Life Sciences and Healthcare	1.4	9.4	5.1	4.0	8.1	0.9	1.0	4.7	2.3
Technology and Services	(2.8)	4.9	1.6	2.6	5.2	5.3	0.7	3.8	2.4
Regional markets and others	(11.2)	5.5	9.0	2.4	(4.8)	1.2	11.3	-5.6	-4.0
North America	(5.0)	4.1	3.4	4.0	4.4	4.8	3.8	4.5	4.4
Latin America	(12.2)	7.2	5.1	(1.1)	2.8	2.9	9.5	2.6	7.2
UK	(11.1)	8.6	6.5	7.0	4.7	1.6	-0.2	2.6	-3.3
Continental Europe	(4.6)	12.0	4.5	8.9	2.1	-2.0	3.7	-0.6	-0.7
India	(27.3)	24.7	17.7	5.0	(15.6)	14.1	11.1	-4.8	-4.7
Asia Pacific	(2.1)	6.1	5.1	1.8	1.7	-0.4	-1.6	1.4	-1.1
MEA	(7.1)	7.2	10.7	5.0	7.9	-2.0	-2.1	8.0	-8.9
Total Employees (k)	444	454	469	489	509	528.7	557.0	592.2	606.3
Net Additions (k)	-5	10	16	19	20	19.7	28.2	35.2	14.1
Attrition (LTM %)	11.1	8.9	7.6	7.2	8.6	11.9	15.3	17.4	19.7

Source: Company, MOFSL

Financials and valuations

Income Statement								(INR b)
Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Sales	1,180	1,231	1,465	1,569	1,642	1,918	2,221	2,428
Change (%)	8.6	4.4	19.0	7.2	4.6	16.8	15.8	9.3
Cost of Services	669	713	852	923	971	1,146	1,352	1,466
SG&A Expenses	208	213	239	260	246	287	332	354
EBITDA	323	325	395	421	465	532	594	668
As a percentage of Net Sales	27.4	26.4	27.0	26.8	28.4	27.8	26.7	27.5
Depreciation	20	20	21	35	41	48	56	61
EBIT	303	305	375	386	425	485	538	608
As a percentage of Net Sales	25.7	24.8	25.6	24.6	25.9	25.3	24.2	25.0
Other Income	42	36	41	37	25	32	35	41
PBT	345	341	416	422	450	517	573	649
Tax	82	82	100	98	115	132	144	162
Rate (%)	23.6	24.1	24.1	23.2	25.5	25.6	25.1	25.0
PAT	264	259	316	324	335	384	429	487
Extraordinary Gains/Losses	0	0	0	0	-10	0	0	0
Adjusted PAT	264	259	316	324	326	384	429	487
Minority Interest	1	1	1	1	1	1	1	1
Reported PAT	263	258	315	323	324	383	428	485
Change (%)	8.6	-1.8	21.9	2.8	0.3	18.2	11.6	13.5

Balance Sheet								(INR b)
Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Share capital	2	2	4	4	4	4	4	4
Reserves	860	849	891	838	861	888	915	946
Net Worth	862	851	894	841	864	891	919	950
Minority Interest and Others	25	33	34	97	102	100	112	119
Loans	1	1	0	0	0	0	0	0
Capital Employed	888	885	929	938	966	992	1,031	1,069
Gross Block	247	266	287	408	449	502	555	612
Depreciation	131	151	171	207	247	295	351	411
Net Block	116	115	116	201	201	207	204	201
Intangibles	44	52	44	45	57	55	62	66
Other LT assets	67	84	69	60	56	70	81	88
Current Assets	805	812	921	902	993	1,083	1,120	1,166
Debtors	280	316	325	363	367	418	494	546
Cash and Bank Balance	41	49	72	97	69	125	80	91
Investments	416	380	347	261	316	360	335	310
Other Current Assets	67	67	177	182	241	180	211	218
Current Liab. and Prov.	145	178	221	271	342	424	437	451
Net Current Assets	660	634	700	632	651	660	683	714
Application of Funds	887	885	929	938	966	992	1,031	1,069

Financials and valuations

Ratios

Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Basic (INR)								
EPS	66.7	67.0	82.3	86.2	86.7	104.0	117.2	133.1
Cash EPS	71.8	72.2	87.6	95.6	97.6	117.0	132.5	149.7
Book Value	218.8	220.9	233.8	224.2	231.1	241.8	251.9	260.4
DPS	27.5	70.7	76.9	71.4	97.2	100.9	93.8	106.5
Payout (%)	41.2	105.6	93.5	82.8	112.1	97.1	80.0	80.0
Valuation (x)								
P/E	48.9	48.7	39.7	37.9	37.7	31.4	27.9	24.5
Cash P/E	45.5	45.2	37.3	34.1	33.5	27.9	24.6	21.8
EV/EBITDA	39.7	38.6	31.4	28.9	26.1	22.4	19.9	17.7
EV/Sales	10.9	10.2	8.5	7.7	7.4	6.2	5.3	4.9
Price/Book Value	14.9	14.8	14.0	14.6	14.1	13.5	13.0	12.5
Dividend Yield (%)	0.8	2.2	2.4	2.2	3.0	3.1	2.9	3.3
Profitability Ratios (%)								
RoE	34.7	30.1	36.1	37.3	38.0	43.7	47.2	52.0
RoCE	29.7	26.1	31.4	31.7	33.2	36.8	39.8	43.4
Turnover Ratios								
Debtors (Days)	87	94	81	84	82	80	81	82
Fixed Asset Turnover (x)	10.1	10.7	12.7	7.8	8.1	9.3	10.9	12.1

Cash Flow Statement

Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
								(INR b)
CF from Operations	259	282	308	370	379	427	475	538
Cash for Working Capital	-6	0	-22	-47	9	-28	-101	-51
Net Operating CF	252	282	286	324	388	399	374	487
Net Purchase of FA	-20	-19	-21	-32	-32	-30	-43	-47
Free Cash Flow	232	263	265	291	356	370	331	440
Net Purchase of Invest.	-147	16	36	118	-50	21	25	25
Net Cash from Invest.	-167	-3	16	86	-81	-9	-18	-22
Proceeds from Equity Issues	-1	0	0	0	0	0	0	0
Proceeds from LTB/STB	0	0	-2	-13	-211	-195	0	0
Others	0	0	-2	-9	-6	-7	0	0
Dividend Payments	-110	-268	-275	-377	-109	-134	-400	-454
Cash Flow from Fin.	-110	-268	-279	-399	-326	-336	-400	-454
Net Cash Flow	-27	13	23	14	-18	56	-44	10
Opening Cash Balance	68	41	54	77	91	73	130	85
Add: Net Cash	-27	13	23	14	-18	56	-44	10
Closing Cash Balance	41	54	77	91	73	130	85	96

Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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