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## Technology

### Q2FY23 result review and earnings revision

Target price: Rs3,191

### Earnings revision

(%)	FY23E	FY24E
Sales (US\$)	↓ 0.5	↓ 0.9
EBIT	↑ 1.4	↑ 1.5
EPS	↑ 1.2	↑ 1.5

### Target price revision

Rs3,191 from Rs3,142

### Shareholding pattern

	Dec '21	Mar '22	Jun '22
Promoters	72.2	72.3	72.3
Institutional investors	22.9	22.0	21.9
MFs and others	3.3	3.2	3.4
FIs/Bank	0.0	0.0	0.0
Insurance Cos.	4.5	4.5	4.9
Fills	15.1	14.3	13.6
Others	4.9	5.7	5.8

Source: www.nseindia.com

### ESG disclosure score

Year	2020	2021	Chg
ESG score	51.8	52.0	0.2
Environment	31.1	40.5	9.4
Social	33.1	30.5	-2.6
Governance	91.1	84.9	-6.3

Note - Score ranges from 0 - 100 with a higher score indicating higher ESG disclosures.

Source: Bloomberg, I-sec research

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## INDIA

# Tata Consultancy Services

## HOLD

Maintain

Rs3,121

### On expected lines

Tata Consultancy Services (TCS) has reported better-than-expected revenue growth of 4% QoQ in CC terms vs I-Sec/consensus expectations of 3.4%/3.5% for Q2FY23. However, US\$ revenue growth was lower at 1.4% QoQ due to cross-currency headwinds of 260bps QoQ. Sequential revenue growth was led by technology & services, life sciences & healthcare, manufacturing and retail & CPG. Financial services reported below company average growth in Q2FY23 due to weakness in insurance segment. In terms of markets, US led with 3.3% QoQ US\$ growth. Broad based revenue growth and margins in line with estimates despite rising attrition were comforting.

Deal TCV was healthy at US\$8.1bn, but growth in TCV was modest at 6.6% YoY, -1.2% QoQ. Book-to-bill was healthy at 1.2x. However, management alluded elongation of decision-making cycle reflected in qualified deal pipeline growing at slower pace than overall pipeline. Management also cited that clients are cautious on their spending decisions, especially in Europe & UK given the tough winter which might lead to shutting down of manufacturing plants creating ripple effect across industries. Discretionary retail and P&C insurance segments are also exhibiting slowdown in spending due to macro impact. We expect muted revenue growth in H2FY23 due to furloughs in Q3FY23 and weak macro environment especially in Europe & UK.

Net headcount addition reduced further to 9,840 employees, 1.6% QoQ vs 25.8K net addition per quarter in FY22. Whereas LTM attrition inched up to 21.5% (+180bps QoQ). Slowing hiring momentum despite elevated attrition levels indicates lower demand visibility ahead.

TCS reported in line EBIT margin of 24%, +90bps QoQ benefitted by tailwinds of 50bps from currency movement and operational efficiencies from pyramid, productivity-linked realisation improvement and lower sub-con costs partially offset by headwinds of 20bps from higher facility costs. Near-term margin levers are improvement in utilisation and realisation and headwind from attrition subsiding. Management expects quarterly attrition to taper down from next quarter (Q3FY23).

We slightly decrease our US\$ revenue estimates, but our EPS estimates increase due to FX changes (increased USD/INR assumption from 80 to 82 for H2FY23 & FY24). We forecast revenue growth of 7.6% and 6.4% for FY23E and FY24E, respectively. TCS has better-than-peers supply-side management, breadth of capabilities and deep domain expertise. While demand may slowdown in future, TCS will likely gain share from peers. It will also most likely gain in vendor consolidation exercise. Maintain HOLD with a fair value of Rs3,191 based on a target multiple of 25x FY24E earnings.

Market Cap	Rs11411bn/US\$138.5bn
Reuters/Bloomberg	TCS.BO/TCS IN
Shares Outstanding (mn)	3,659.1
52-week Range (Rs)	4019/2982
Free Float (%)	27.7
FII (%)	13.6
Daily Volume (US\$'000)	99,470
Absolute Return 3m (%)	(4.2)
Absolute Return 12m (%)	(19.7)
Sensex Return 3m (%)	6.7
Sensex Return 12m (%)	(2.2)

Year to March	FY21	FY22	FY23E	FY24E
Revenue (Rs mn)	16,41,770	19,17,540	22,29,730	24,13,695
Net Income (Rs mn)	3,33,880	3,83,270	4,17,939	4,63,254
EPS (Rs)	90.3	103.6	114.2	126.6
% Chg YoY	2.8	4.7	14.8	10.2
P/E (x)	34.6	30.1	27.3	24.7
CEPS (Rs)	101.2	117.3	127.1	142.4
EV/E (x)	24.0	20.7	18.7	16.3
Dividend Yield (%)	1.2	1.4	1.5	1.5
RoCE (%)	32.8	36.3	33.0	29.5
RoE (%)	39.2	43.7	41.9	37.1

- ▶ **Beat in revenue growth:** TCS reported revenue of US\$6,877mn, +4% QoQ CC, 1.4% QoQ US\$. Growth in CC terms was above our and consensus estimates, but lower in US\$ terms due to higher cross-currency headwinds. Growth was led by technology services at 3.7% QoQ US\$, life sciences & healthcare at 2.4% QoQ US\$, manufacturing at 1.4% QoQ US\$ and retail & CPG at 1.4% QoQ US\$. In retail, clients are spending on supply-chain transformation. TCS also witnessed an uptick in demand in travel transportation and hospitality sub-segments in Retail vertical. In communication, demand is driven by investments in 5G and providing personalised offerings to end consumers. BFSI clients are spending on cloud, data analytics and customer experience.
- ▶ **In-line margins:** TCS reported in line EBIT margin of 24%, +90bps QoQ benefitted by tailwinds of 50bps from currency movement and operational efficiencies from pyramid, productivity linked realisation improvement and lower sub-con costs partially offset by headwinds of 20bps from higher facility costs. Currency benefit due to depreciation of INR against US\$ was partially offset by appreciation of INR against GBP and EUR. Near-term margin levers are improvement in utilisation and realisation and headwind from attrition subsiding.
- ▶ **Muted growth in TCV.** Orderbook for Q2FY23 stood at US\$8.1bn, -1.2% QoQ and +6.6% YoY (vs average of US\$8.7mn per quarter in FY22). Moderation in deal win momentum has set in. Book-to-bill is healthy at 1.2x. BFSI segment reported deals worth US\$2.3bn. Retail posted deal TCV of US\$1.6bn. North America reported deal wins of US\$4.3bn. Management mentioned deal wins in UK & Europe are also healthy and improved QoQ. However, it experienced elongation in decision making in some deals. Plus, clients are prioritising deals with faster payback period over longer payback period. Management retains its endeavour to achieve deal TCV of US\$7bn-9bn range going forward.
- ▶ **Fresher addition on track:** Company added 35k freshers in H1FY23 and is expected to add 10-12K freshers in H2FY23, exceeding its initial target of 45K fresher additions in FY23. Despite strong healthy fresher intake, net headcount addition was low at 9,840 employees (up 1.6% QoQ). It was much lower vs the average ~26k per quarter in FY22.
- ▶ **Other highlights.** Company reported a robust OCF/NI of 102.3% and declared dividend of Rs8 per share.
- ▶ **Read through for Indian IT sector**
  1. TCS reported beat in revenue growth of 4% QoQ in CC terms but high cross-currency headwinds of 260bps QoQ. We believe revenue momentum will likely be intact and in line with street estimates for peers. At the same time, we do not expect positive surprises on revenue front from peers under our coverage.
  2. TCS management cited that clients are cautious in their spending decisions especially in Europe & UK, where they are preparing for tough winter amidst energy crisis. We believe Europe IT spending growth (discretionary) may slow down in H2FY23 and FY24 on account of uncertain macro environment.
  3. TCV growth was muted for TCS at US\$8.2bn, up 6.6% YoY, -1.2% QoQ. Deal momentum may soften for peers as well both in QoQ and YoY terms.
  4. TCS reported in-line margins led by productivity improvement and currency tailwinds. We expect margins to increase on QoQ basis for companies that have

completed their wage hike in Q1. However, on YoY basis margins are expected to remain muted led by elevated attrition levels, slowing demand and return of discretionary costs.

- Hiring momentum slowed for TCS for the second consecutive quarter. We saw similar moderation in hiring for Accenture. We expect softness in hiring momentum across IT stocks under our coverage going forward.
- In line with our expectations of attrition inching up in H1FY23 due to wage increment cycles, LTM attrition inched up further to 21.5%, +180bps QoQ for TCS. We expect attrition to remain at elevated levels for the sector and cool down gradually Q3 onwards due to normalisation of demand.

Slowing hiring momentum despite elevated attrition levels indicates lower demand visibility ahead.

**Table 1: Q2FY23 actuals vs estimates (Rs bn)**

(Rs bn)	Q2FY23	Q1FY23	QoQ	Q2FY22	YoY	Q2FY23E-ISEC	vs our estimates
Sales (\$ m)	6,877	6,780	1.4%	6,333	8.6%	6,895	-0.26%
Sales	553	527.58	4.8%	469	18.0%	549	0.78%
EBIT Margin	24.0%	23.1%	91 bps	25.6%	-160 bps	24.0%	1 bps
PBT	141	128	10.3%	130	8.7%	141	0.17%
Tax	36.3	32.6	11.5%	33	9.5%	35.9	1.19%
Tax Rate	25.8%	25.5%	1.0%	25.6%	19 bps	25.5%	26 bps
Reported PAT	104	95	10.1%	96	8.4%	104	-0.11%
EPS	28.5	25.9	10.1%	26.0	9.6%	28.5	-0.10%

Source: Company data, I-Sec research

**Table 2: Change in estimates**

	Revised		Old		Change (%)	
	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
Revenues (US\$ mn)	27,670	29,435	27,797	29,713	-0.5%	-0.9%
Revenue growth (US\$, %)	7.6	6.4	8.1	6.9	-50bps	-50bps
<b>Rs bn</b>						
Revenues	2,230	2,414	2,199	2,377	1.4%	1.5%
EBIT	533	592	526	583	1.4%	1.5%
EBIT margin	23.9	24.5	23.9	24.5	0bps	0bps
EPS (Rs/share)	114.2	126.6	112.9	124.7	1.2%	1.5%
Revenues	2,230	2,414	2,199	2,377	1.4%	1.5%

Source: Company data, I-Sec research

**Table 3: Segmental growth**

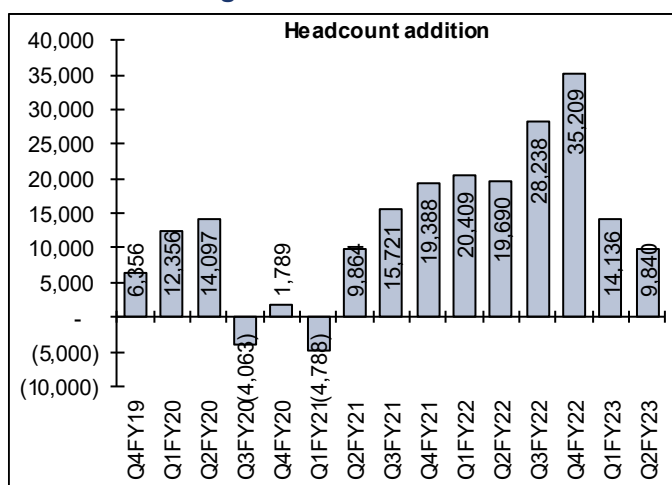
	Revenues (US\$ mn)	QoQ (%)	YoY (%)	% of total	YoY CC growth (%)
Total Revenues	6,877	1.4	8.6	100.0	15.4
<b>Revenue by geography</b>					
North America	3,734	3.5	17.2	54.3	17.6
Latin America	117	(4.2)	15.4	1.7	19.0
UK	997	(1.3)	(2.2)	14.5	14.8
Continental Europe	997	(3.2)	(1.0)	14.5	14.1
India	351	7.8	7.8	5.1	7.0
Asia Pacific	550	(2.2)	(3.5)	8.0	16.7
MEA	131	7.1	3.2	1.9	8.2
<b>Revenue by verticals</b>					
BFSI	2,194	0.8	6.9	31.9	13.1
Retail & CPG	1,093	1.4	15.1	15.9	22.9
Communication & Media	461	(0.1)	11.9	6.7	18.7
Manufacturing	681	1.4	8.6	9.9	14.5
Life sciences & healthcare	701	2.4	10.8	10.2	14.5
Technology & services	619	3.7	11.1	9.0	15.9
Regional markets & others	1,128	1.4	2.3	16.4	13.1

Source: Company data, I-Sec research

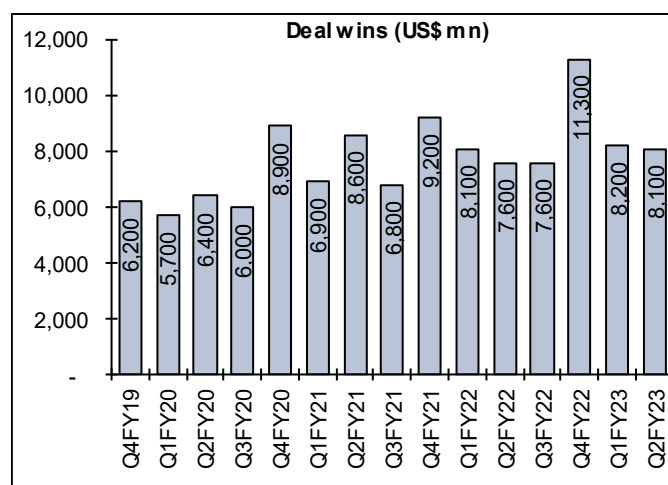
**Table 4: Cost headwinds to gradually decrease**

	Q3FY21	Q4FY21	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23
<b>COGS</b>								
Employee Cost	43.72%	42.43%	44.39%	44.00%	43.29%	43.87%	44.89%	43.51%
Fees to External Consultants	7.14%	8.49%	8.25%	8.62%	8.95%	9.16%	9.67%	9.63%
Cost of Equipment and Software Licenses	0.71%	1.04%	0.57%	0.45%	0.88%	0.51%	0.41%	0.73%
Depreciation	1.90%	1.88%	1.85%	1.86%	1.90%	1.82%	1.77%	0.74%
Travel	0.48%	0.49%	0.61%	0.65%	0.94%	0.50%	0.81%	1.69%
Communication	0.95%	0.85%	0.81%	0.79%	0.77%	0.83%	0.67%	0.86%
Facility Expenses	0.71%	0.85%	0.74%	0.67%	0.74%	0.68%	0.74%	0.64%
Other Costs	2.14%	2.75%	2.41%	2.52%	2.52%	2.50%	2.61%	2.70%
Total cost of sales	57.8%	58.8%	59.6%	59.6%	60.0%	59.9%	61.6%	60.5%
<b>SG&amp;A</b>								
Employee Cost	11.90%	11.67%	12.09%	12.29%	12.29%	12.18%	12.59%	12.61%
Fees to External Consultants	0.48%	0.38%	0.34%	0.32%	0.29%	0.33%	0.35%	0.33%
Provision for Doubtful Debts	0.24%	0.09%	0.09%	0.07%	0.09%	0.03%	0.03%	0.44%
Depreciation	0.48%	0.56%	0.52%	0.51%	0.54%	0.58%	0.56%	0.54%
Facility Expenses	0.48%	0.44%	0.40%	0.38%	0.43%	0.42%	0.42%	0.32%
Travel	0.24%	0.10%	0.15%	0.18%	0.10%	0.17%	0.25%	0.30%
Communication	0.24%	0.27%	0.28%	0.23%	0.28%	0.29%	0.26%	0.07%
Other Costs	0.71%	0.92%	0.98%	0.83%	0.95%	1.16%	0.87%	0.88%

Source: Company data, I-Sec research

**Chart 1: Slowing headcount addition**

Source: Company, I-Sec research

**Chart 2: Muted deal wins**

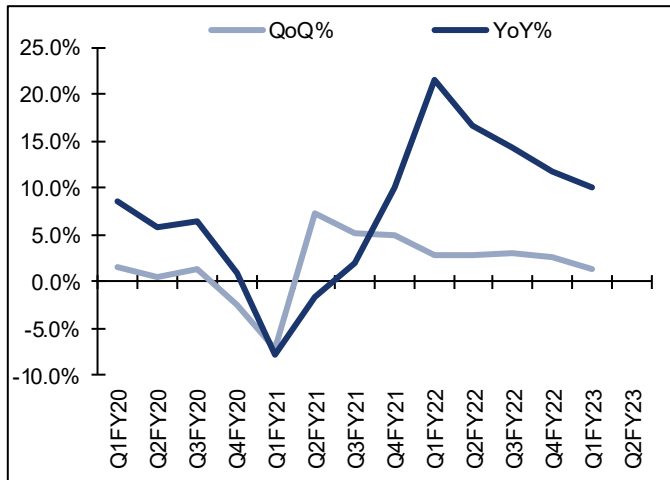
Source: Company, I-Sec research

**Table 5: Moderation BFSI and Retail vertical growth**

YoY CC %	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23
UK	16%	16%	13%	13%	13%	15%
Continental Europe	20%	14%	18%	10%	12%	14%
BFSI	19%	17%	18%	13%	14%	13%
Retail & CPG	22%	18%	20%	22%	25%	23%
Regional Markets & Others	8%	6%	5%	4%	10%	13%
Overall company growth	16.4%	15.5%	15.4%	14.3%	15.5%	15.4%

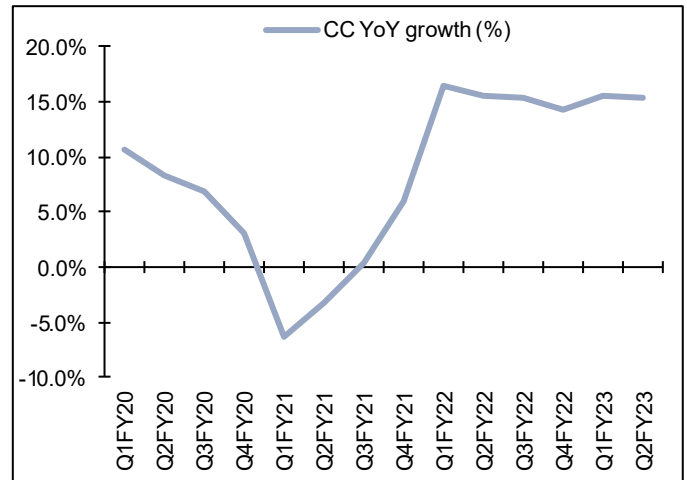
Source: Company, I-Sec research

**Chart 3: Moderation in YoY\$ revenue growth**



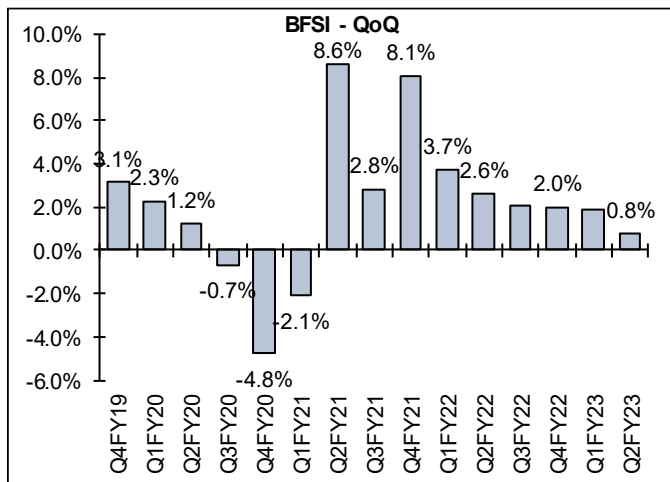
Source: Company, I-Sec research

**Chart 4: Healthy YoY CC growth**



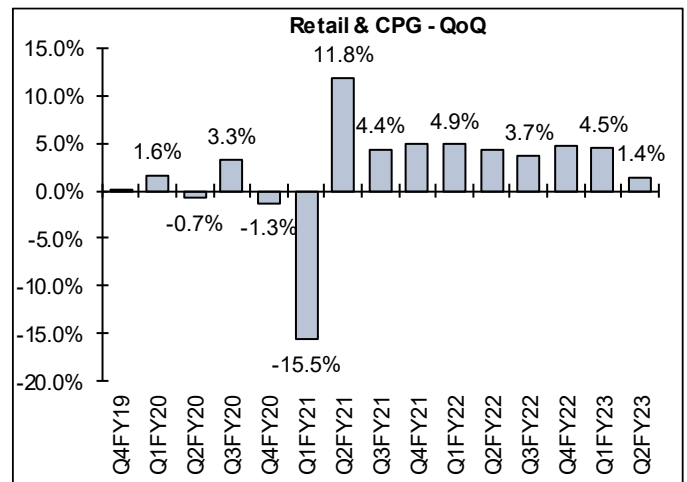
Source: Company, I-Sec research

**Chart 5: BFSI growth remained tepid**



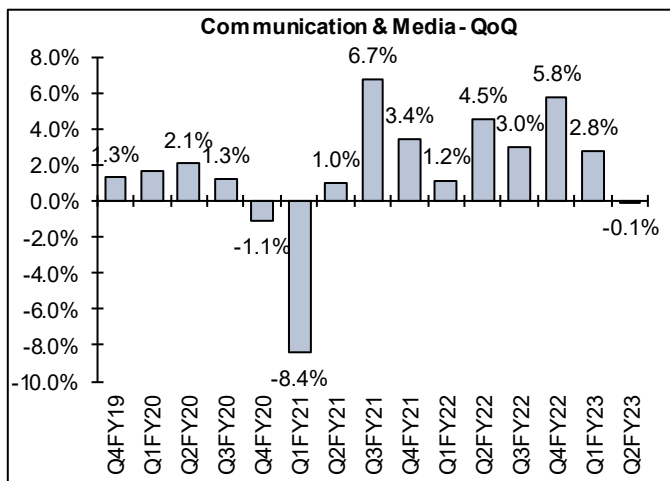
Source: Company, I-Sec research

**Chart 6: Moderation in Retail & CPG growth**



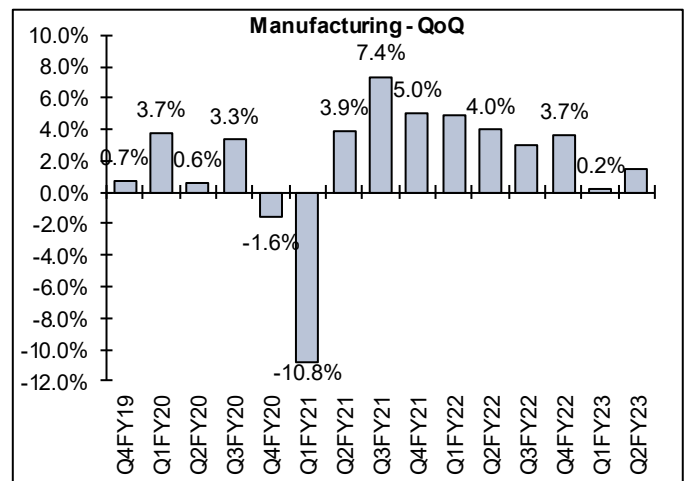
Source: Company, I-Sec research

**Chart 7: C&M growth moderating**



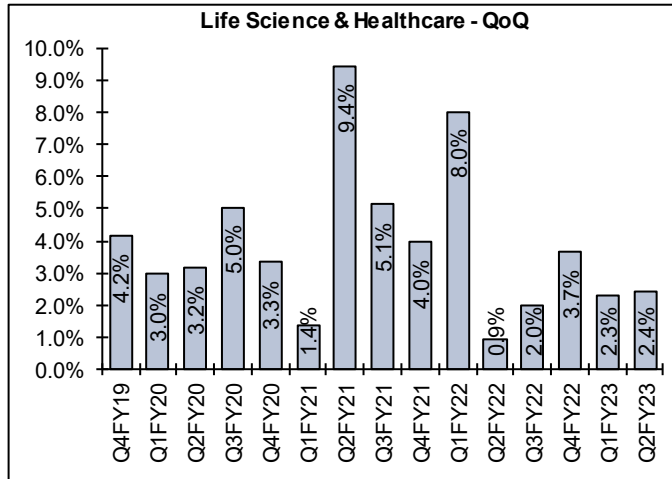
Source: Company, I-Sec research

**Chart 8: Steady growth in manufacturing segment**



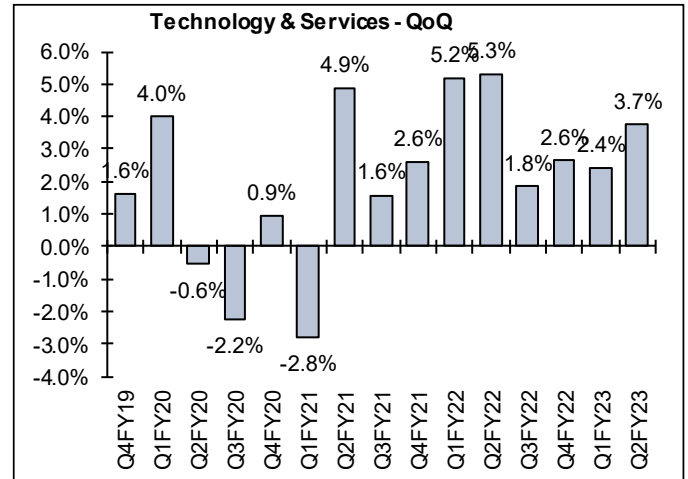
Source: Company, I-Sec research

**Chart 9: Stable growth in life sciences**



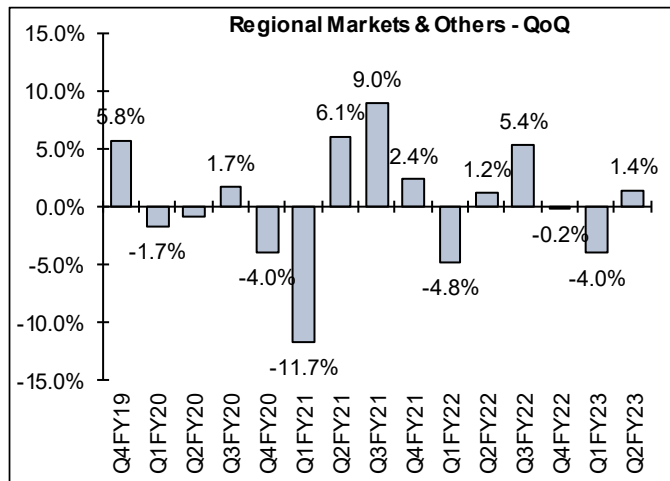
Source: Company, I-Sec research

**Chart 10: Strong growth in tech & services**



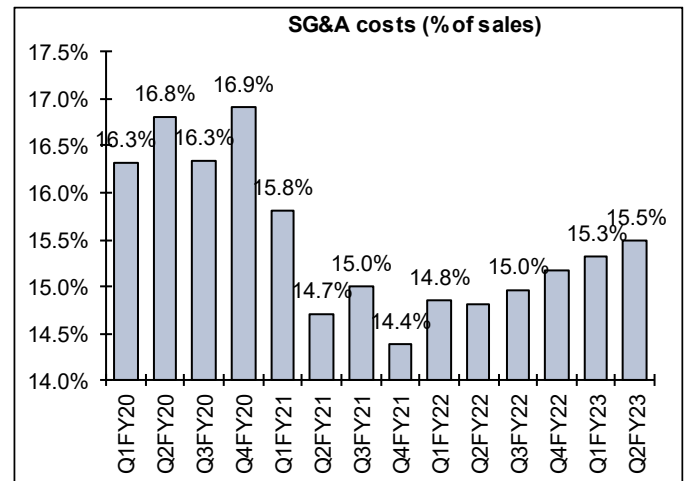
Source: Company, I-Sec research

**Chart 11: Regional markets growth remains weak**



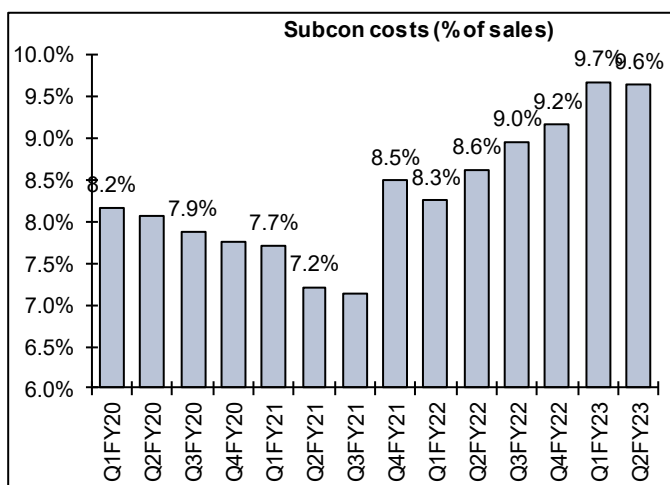
Source: Company, I-Sec research

**Chart 12: Slight increase in SG&A costs again**



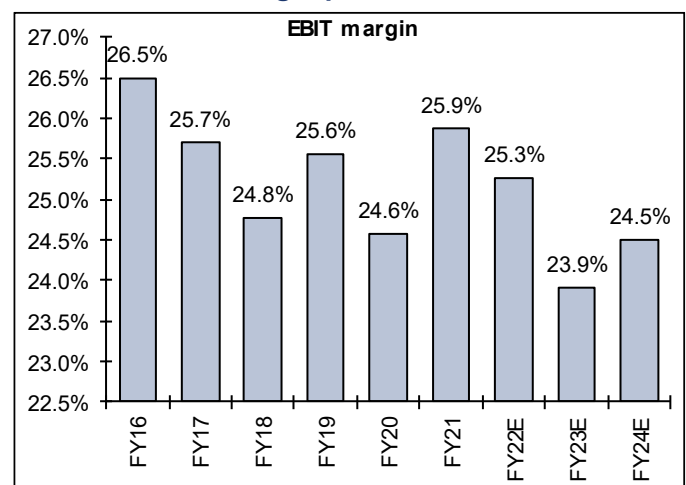
Source: Company, I-Sec research

**Chart 13: Stable sub-con costs**



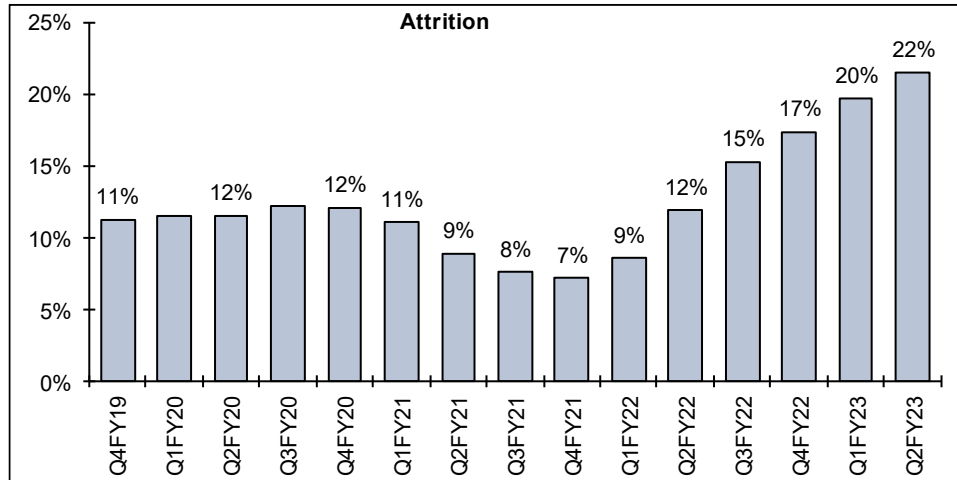
Source: Company, I-Sec research

**Chart 14: Weak margin performance**



Source: Company, I-Sec research

**Chart 15: Attrition rose on LTM basis**



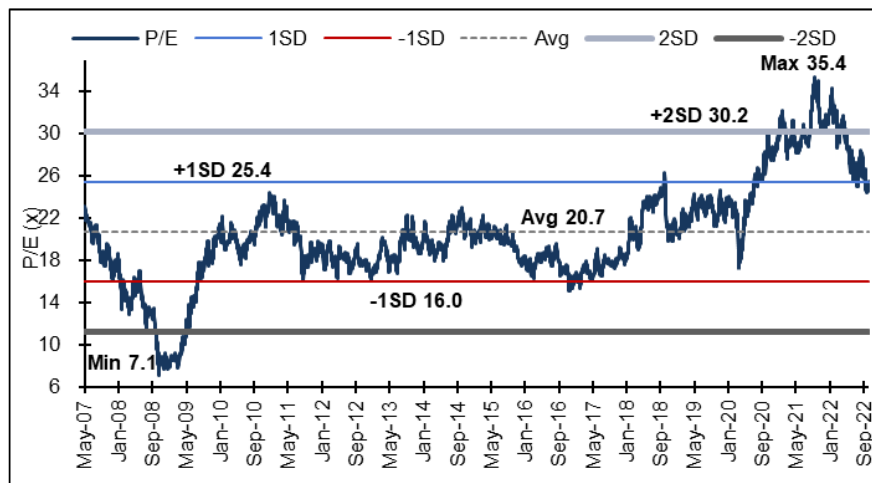
Source: Company, I-Sec research

**Table 6: TCS financial summary**

Rs bn	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
US\$ rev (mn)	20,913	22,031	22,174	25,706	27,670	29,435	32,487
YoY	9.6%	5.3%	0.6%	15.9%	7.6%	6.4%	10.4%
Revenues	1,465	1,569	1,642	1,918	2,230	2,414	2,664
EBIT	375	386	425	485	533	592	653
Margin	25.6%	24.6%	25.9%	25.3%	23.9%	24.5%	24.5%
PAT	315	323	334	383	418	463	512
EPS (Rs)	84	86	90	104	114	127	140
RoE	36%	37%	39%	44%	42%	37%	33%
P/E					27.3	24.7	22.3

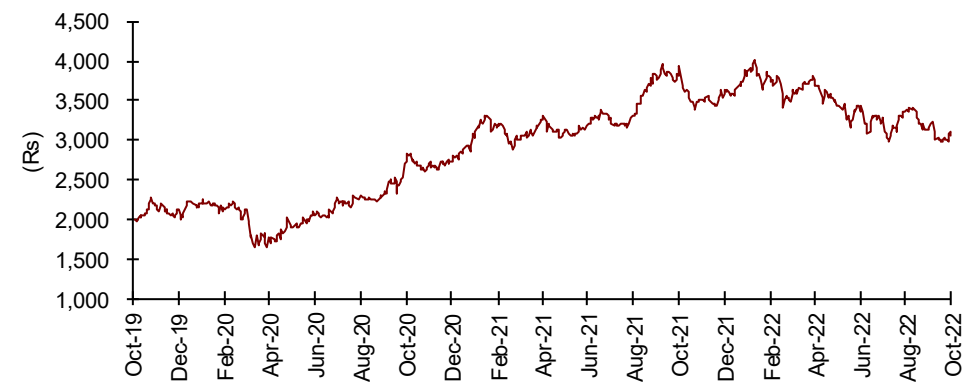
Source: Company data, I-Sec research

**Chart 16: 1-year forward P/E**



Source: Bloomberg, I-Sec research.

**Price chart**



Source: Bloomberg



## Financial summary

Table 7: Profit and loss statement

(Rs mn, year ending March 31)

	FY21	FY22	FY23E	FY24E
<b>Revenues (US\$ mn)</b>	<b>22,174</b>	<b>25,706</b>	<b>27,670</b>	<b>29,435</b>
<b>Operating Revenues (Sales)</b>	<b>16,41,770</b>	<b>19,17,540</b>	<b>22,29,730</b>	<b>24,13,695</b>
<b>Operating Expenses</b>	<b>11,76,400</b>	<b>13,86,980</b>	<b>16,49,403</b>	<b>17,64,123</b>
<b>EBITDA</b>	<b>4,65,370</b>	<b>5,30,560</b>	<b>5,80,327</b>	<b>6,49,572</b>
% margin	28.3	27.7	26.0	26.9
Depreciation & Amortisation	40,560	46,030	47,007	57,929
<b>EBIT</b>	<b>4,24,810</b>	<b>4,84,530</b>	<b>5,33,319</b>	<b>5,91,643</b>
% margin	25.9	25.3	23.9	24.5
Other Income	24,970	32,340	30,070	32,000
<b>Recurring PBT</b>	<b>4,49,780</b>	<b>5,16,870</b>	<b>5,63,389</b>	<b>6,23,643</b>
Add: Extraordinaries	0	0	0	0
Less: Taxes	1,14,580	1,32,380	1,44,021	1,59,029
Add: Earnings in Affiliates	0	0	0	0
Less: Minority Interest	-1,320	-1,220	-1,430	-1,360
<b>Net Income (Reported)</b>	<b>3,33,880</b>	<b>3,83,270</b>	<b>4,17,939</b>	<b>4,63,254</b>

Source: Company data, I-Sec research

Table 8: Balance sheet

(Rs mn, year ending March 31)

	FY21	FY22	FY23E	FY24E
<b>Net Worth</b>	<b>8,64,330</b>	<b>8,91,390</b>	<b>11,04,737</b>	<b>13,92,373</b>
Minority Interest	6,750	7,070	7,260	8,620
Other Long term liabilities	94,960	93,170	90,730	90,730
<b>Total liabilities</b>	<b>9,66,040</b>	<b>9,92,246</b>	<b>12,02,727</b>	<b>14,91,723</b>
<b>Net Block</b>	<b>1,96,690</b>	<b>1,96,150</b>	<b>1,93,600</b>	<b>1,97,600</b>
Intangibles	22,780	28,880	48,660	48,660
Other LT assets	95,320	1,07,010	96,510	96,510
Curr. Assets	9,92,800	10,83,100	12,85,773	15,86,081
Debtors	3,66,620	4,18,100	4,78,482	5,10,904
Cash & Bank Balance	68,580	1,24,880	1,56,557	4,17,570
Other Current Assets	5,57,600	5,40,120	6,50,734	6,57,607
Current Liab. & Prov	3,41,550	4,22,894	4,21,816	4,37,128
<b>Net Current Assets</b>	<b>6,51,250</b>	<b>6,60,206</b>	<b>8,63,957</b>	<b>11,48,953</b>
<b>Application of Funds</b>	<b>9,66,040</b>	<b>9,92,246</b>	<b>12,02,727</b>	<b>14,91,723</b>

Source: Company data, I-Sec Research

Table 9: Quarterly trend

(Rs mn, year ending March 31)

	Sep-21	Dec-21	Mar-22	Jun-22
Net sales	4,88,850	5,05,910	5,27,580	5,53,090
% growth (YoY)	16.4	15.8	16.2	18.0
EBITDA	1,34,330	1,38,450	1,34,160	1,39,920
Margin (%)	27.5	27.4	25.4	25.3
Other income	9,540	7,360	5,900	8,170
Extraordinaries Inc / (Loss)	0	0	0	0
Recurring Net Income	97,690	99,260	94,780	1,04,310

Source: Company data, I-Sec research

Table 10: Cashflow statement

(Rs mn, year ending March 31)

	FY21	FY22	FY23E	FY24E
<b>CF from Operations</b>	<b>3,74,370</b>	<b>4,15,700</b>	<b>4,34,876</b>	<b>4,89,183</b>
Cash for Working Capital	12,630	(16,210)	(70,262)	(29,527)
<b>Net Operating CF</b>	<b>3,87,000</b>	<b>3,99,490</b>	<b>3,64,614</b>	<b>4,59,656</b>
Net Purchase of FA	(27,000)	(24,830)	(64,237)	(61,929)
<b>Free Cashflow</b>	<b>3,60,000</b>	<b>3,74,660</b>	<b>3,00,377</b>	<b>3,97,728</b>
Net Purchase of Invest.	(54,000)	15,860	(67,100)	32,000
<b>Net Cash from Invest.</b>	<b>(81,000)</b>	<b>(8,970)</b>	<b>(1,31,337)</b>	<b>(29,929)</b>
Proceeds from LTB/STB	-	-	2,801	5,544
Others	(19,000)	(22,550)	(36,097)	1,360
Dividend Payments	(3,06,000)	(3,13,260)	(1,68,304)	(1,75,618)
<b>Cashflow from Fin.</b>	<b>(3,25,000)</b>	<b>(3,35,810)</b>	<b>(2,01,600)</b>	<b>(1,68,715)</b>
<b>Net Cashflow</b>	<b>(19,000)</b>	<b>54,710</b>	<b>31,677</b>	<b>2,61,013</b>

Source: Company data, I-Sec research

Table 11: Key ratios

(Year ending March 31)

	FY21	FY22	FY23E	FY24E
<b>Per Share Data (Rs)</b>				
Diluted Recurring EPS	90.3	103.6	114.2	126.6
Recurring Cash EPS	101.2	117.3	127.1	142.4
Dividend per share (DPS)	38.0	43.0	46.0	48.0
Book Value per share (BV)	233.7	243.6	301.9	380.6

**Growth Ratios (%)**

Operating Income (Sales) - US\$	0.6	15.9	7.6	6.4
Operating Income (Sales)	4.6	16.8	16.3	8.3
EBIT	10.1	14.1	10.1	10.9
Recurring Net Income	3.2	14.8	9.0	10.8
Diluted Recurring EPS	2.8	4.7	14.8	10.2
Diluted Recurring CEPS	5.9	15.9	8.3	12.1

**Valuation Ratios (x)**

P/E	34.6	30.1	27.3	24.7
P/CEPS	31.2	26.9	23.9	21.4
P/BV	13.6	10.8	10.2	9.2
EV / EBITDA	24.0	20.7	18.7	16.3
EV / Sales	6.8	5.7	4.9	4.4

**Operating Ratios**

Other Income / PBT (%)	5.6	6.3	5.3	5.1
Effective Tax Rate (%)	25.5	25.6	25.6	25.5
Fixed Asset Turnover (x) on average	8.3	9.8	11.5	12.2
Receivables (days)	82	80	78	77

**Return/Profitability Ratios (%)**

Recurring Net Income Margins	20.3	20.0	18.7	19.2
RoIC	64.9	84.2	84.0	88.1
RoCE	32.8	36.3	33.0	29.5
RoNW	39.2	43.7	41.9	37.1
Dividend Payout Ratio	42.1	41.5	40.3	37.9
Dividend Yield	1.2	1.4	1.5	1.5
EBITDA Margins	28.3	27.7	26.0	26.9
EBIT Margins	25.9	25.3	23.9	24.5

Source: Company data, I-Sec research

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