TCS

BSE SENSEX	S&P CNX
62,626	18,563

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We request your ballot.

Stock Info

Bloomberg	TCS IN
Equity Shares (m)	3752
M.Cap.(INRb)/(USDb)	11747.2 / 142.5
52-Week Range (INR)	3575 / 2868
1, 6, 12 Rel. Per (%)	-4/-3/-19
12M Avg Val (INR M)	6830
Free float (%)	27.7

Financials Snapshot (INR b)

Y/E Mar	2023	2024E	2025E
Sales	2,255	2,498	2,808
EBIT Margin (%)	24.1	24.5	25.5
PAT	421	484	565
EPS (INR)	115.3	132.4	154.3
EPS Gr. (%)	10.9	14.8	16.6
BV/Sh. (INR)	247	240	232
Ratios			
RoE (%)	46.9	54.3	65.4
RoCE (%)	40.5	45.6	53.5
Payout (%)	99.8	90.0	90.0
Valuations			
P/E (x)	27.8	24.3	20.8
P/BV (x)	13.0	13.4	13.8
EV/EBITDA (x)	19.5	17.3	14.9
Div Yield (%)	3.6	3.7	4.3

CMP: INR3,210 TP: INR3,860 (+20%) Buy

FY23 AR Analysis – Re-energising the core in a tough time

- The analysis of TCS AR23 not only highlights the widespread adoption of digital technologies in customer-facing operations, but also the increasing penetration of AI and automation in middle and back-office operations.
- With the growing intensity of adverse macro-economic environment in the latter half of the year, the clients are reprioritizing their spends and expressing interest in transforming their operating model.
- Apart from demand for driving operational efficiency and optimizing costs, Cloud transformation remained a high priority area for enterprises in FY23.
- Despite demonstrating strong resilience, TCS anticipates the possibility of a moderate full-year revenue growth in FY24 if similar instances of delayed decision-making and cash conservation from clients reoccur.

Balanced growth across vectors

- In FY23, TCS reported CC revenue growth of 13.7% YoY, led by Retail & Consumer and Communications segments (up 19.7% YoY and 14.0% YoY).
- Despite the challenging demand for Banking in 2HFY23, the BFSI (~32% of revenues) vertical grew in double-digits (up 11.8% YoY CC) in FY23.
- North America and UK that collectively contribute 70% to the company's revenues, exceeded consolidated level growth. It grew 15.3% and 15.0% YoY CC, respectively.

Poor margin performance - but multiple levers ahead

- TCS was unable to recover the intensity of wage hike through the year, leading to a 120-bp YoY decline in margin at 24.1%. This was majorly attributed to backfilling and retention expenses (accounted for 140-bp drag), which were partly offset by cost optimization and INR depreciation.
- On a segmental basis, major margin dilution has come from the Manufacturing segment at 27.5% (down 260 bp YoY). This was followed by Retail and Life Science, which were down 200 bp YoY each, at 25.7% and 28.0%, respectively.
- The subcon expenses as percentage of revenue stood at 9.2% (up 40 bp YoY). The uptick is partly attributed to the elevated attrition (at 20.1%), leading to higher dependency on outsourcing for immediate execution.
- The company has identified several margin levers that are expected to come into effect in FY24: (1) reduction in subcon expenses (2) improvement in utilization (3) pyramid rationalization, and (4) currency support.

Robust cash conversion with improved return profile

- Cash conversion remained strong; while pre-tax OCF/EBITDA came in at 94.5%, FCF/PAT stood at 92.2%.
- The company generated ROE and ROCE of 47% and 41% in FY23 v/s 44% and 37% in FY22.
- TCS has consistently maintained a robust payout ratio by distributing 108% of its FCF, surpassing its established payout policy of returning 80-100% of FCF.
- Net Cash & Cash Equivalent stood at INR 475b, translating to 4.1% of market cap.

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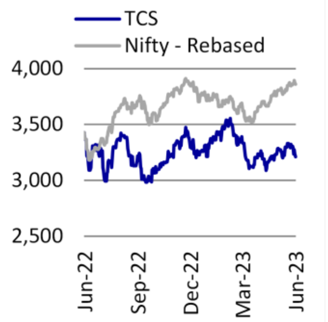
Investors are advised to refer through important disclosures made at the last page of the Research Report.
Motilal Oswal research is available on www.motilaloswal.com/Institutional-Equities, Bloomberg, Thomson Reuters, Factset and S&P Capital.

Shareholding pattern (%)

As On	Mar-23	Dec-22	Mar-22
Promoter	72.3	72.3	72.3
DII	9.6	9.3	7.9
FII	12.7	12.9	14.2
Others	5.4	5.5	5.7

FII Includes depository receipts

Stock performance (one-year)



Operating Metrics

- In FY23, the company witnessed a net addition of 22k+ employees, while the gross hiring of freshers stood at 44k. Additionally, the company achieved a record number of lateral recruits onboarded during the year.
- In FY23, ~500k employees received training in digital technologies, with an average of ~7.5 competencies per employee.
- 60k open positions were fulfilled using up-skilled/cross-skilled employees; and over 22k employees were identified as high talent and rewarded with increased compensation.
- The LTM attrition rate has increased further by 270 bp YoY at 20.1%.
- In FY23, the company signed 29 large operating model transformation deals, covering business and IT operations, against 18 in FY22.
- TCS exited FY23 with an overall deal TCV of USD 34.1b, translating to 1.2x (BTB).

ESG Metrics

- Initiatives include conservation, sewage treatment and reuse, rainwater harvesting (RWH) and employee awareness.
- All new campuses have been designed for 50% higher water efficiency, 100% treatment and recycling of sewage, and rainwater harvesting.
- There has been a 3% YoY reduction in freshwater consumption across campuses
- The water resources for the company comprised 2.5% from RWH; 90% from third-party sources; 7.6% from ground water.
- Renewable energy accounted for 55.2% of the total energy consumed, with a rooftop solar capacity of 10.2MWp installed across campuses
- The company intends to reduce waste generation, maximize recycling/reuse to minimize the amount of waste sent to landfill
- The company has achieved 100% recycling of regulated wastes, e-waste, printer cartridges, paper, packaging and plastics,

Valuation and view

- Given TCS's 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.
- Owing to its steadfast market leadership position and best-in-class execution, the company has been able to maintain its industry-leading margin and demonstrate superior return ratios.
- We maintain our positive stance on TCS. Our TP of INR 3,860 implies 25x FY25E EPS, with a 20% upside potential. We reiterate our **BUY** rating.

Multi-service capabilities – Insulated to macros

Despite the looming uncertainties and challenging macro-environment, TCS reported robust CC revenue growth of 13.7% YoY. The growth was broad based across verticals and geographies. Almost all the verticals have reported double-digit CC revenue growth, while the growth from key geographies has outperformed consol level growth. TCS' full-service offerings, coupled with strong participation in the functional value chain, have resulted in disproportionate wins, surpassing its competitors. This is evident from the company's strong order booking in FY23. The deal TCV of USD 34.1b (1.2x BTB) and a healthy mix of deal pipeline, are building strong revenue visibility for FY24. However, considering the macro headwinds, the management has cited near-term uncertainties with healthy growth outlook in the medium term.

"During the up-cycle, we help clients accelerate and expand their technology-led innovation to differentiate themselves and drive growth. On the down cycle, we help them adapt, using technology to drive the efficiency, agility, and resilience needed to cope with a faltering economy, and prepare for better times ahead."

- Rajesh Gopinathan
Ex-CEO and MD

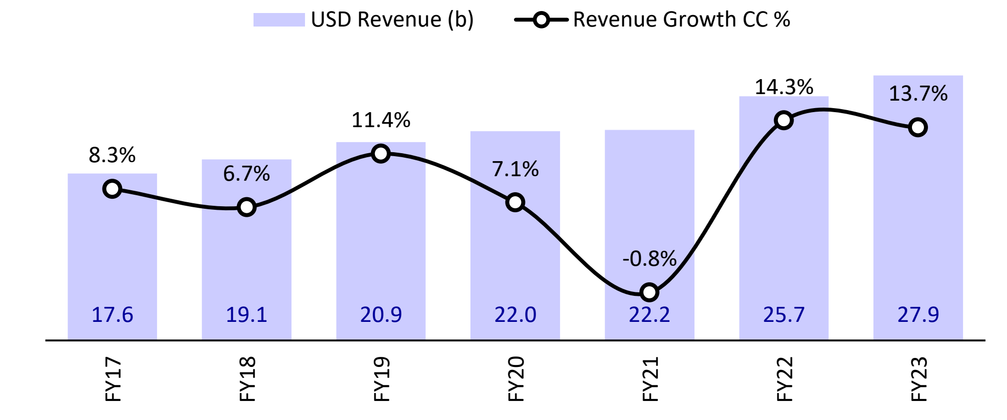
The digital services continue to gain strong traction with sustained focus on cloud adoption, data architecture, customer experience, and business model transformation. In addition to these current focus areas, technologies such as 5G, IoT, Generative AI, VR/Metaverse, and Digital Twin are likely to attract investments in the short to medium term. Furthermore, under traditional outsourcing deal, it is witnessing multi-service integrated deals in the areas of business process, application, and infrastructure with underlying technologies. These deals are also driving vendor consolidation opportunities through strategic partners, which are benefiting clients by de-risking their exposure to a single vendor.

"These business and technology trends drove a strong deal flow throughout FY 2023, peaking in the fourth quarter. We closed the year with an order book of $34.1Bn. This along with the strong pipeline replenishment gives us a good visibility for the medium term."

- K Krithivasan
CEO and Managing Director

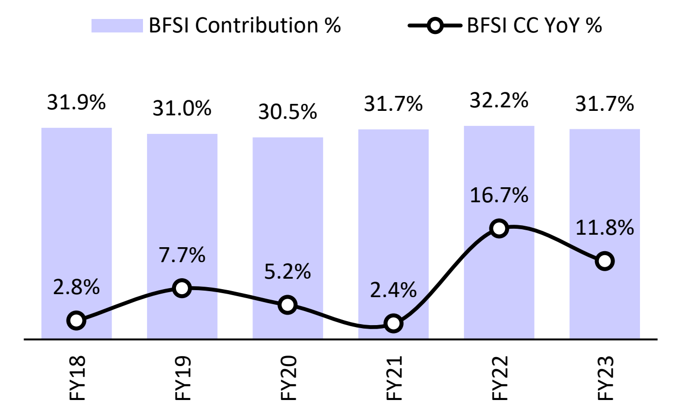
FY23 revenue growth has witnessed slight moderation over that of FY22, but historically higher than the average growth

Exhibit 1: USD Revenue and CC Growth %



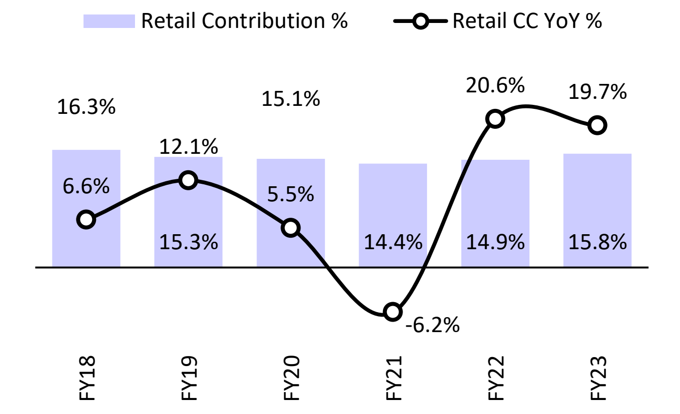
Source: MOFSL, Company

Exhibit 2: BFSI CC growth moderated a bit



Source: MOFSL, Company

Exhibit 3: Retail CC growth stabilized

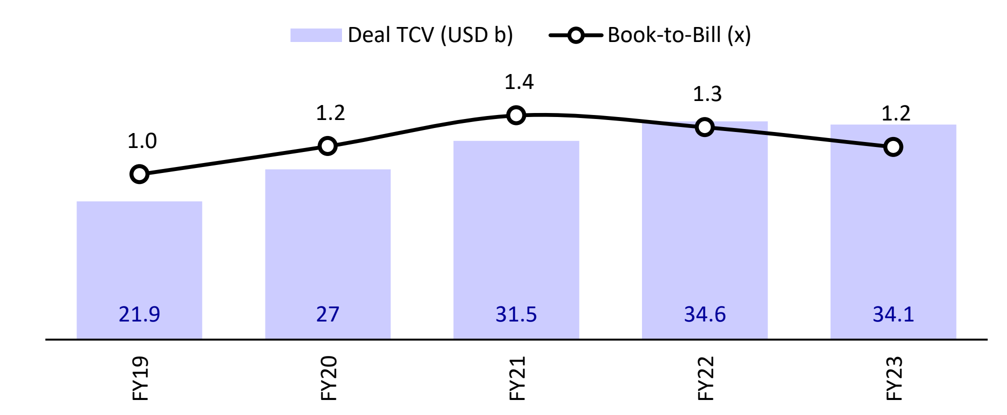


Source: MOFSL, Company

The book-to-bill ratio still remains above 1x, despite the looming uncertainties and global slowdown

Signed 29 large operating model transformation deals in FY23 v/s 18 in FY22

Exhibit 4: Deal TCV still remains attractive



Source: MOFSL, Company

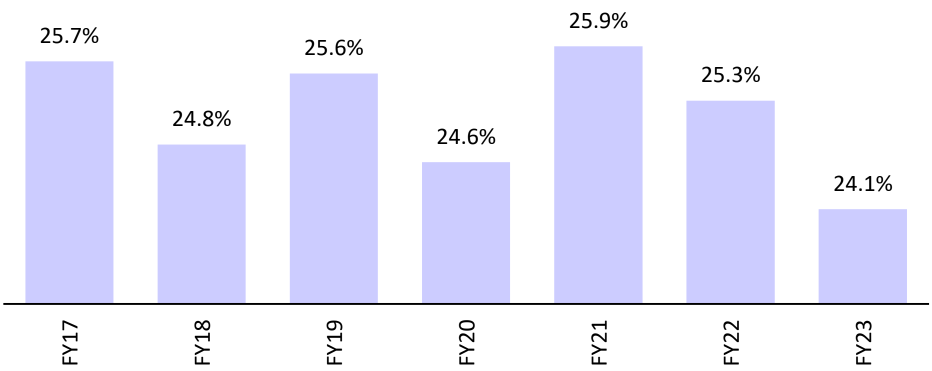
Flexing mutliple margin levers

In the short term, higher onsite wage inflation is a headwind because its legacy contracts have much lower cost-of-living adjustments written in. But in the medium and longer term, it is expected to get adjusted.

Leveraging AI and machine learning to reduce human intervention, while improving process velocity and operational resilience.

- The EBIT margin continues to moderate at 24.1% (down 120 bp) in FY23 from its peak in FY21, on account of backfilling and retention expenses, which adversely impacted the margin by 140 bp in FY23.
- Although the company recruited a large number of freshers (~44k in FY23 v/s 110k freshers in FY22), TCS faced limitations in reducing subcon expenses. The subcon expense as a percentage of revenue has increased further by 40 bp at 9.2% in FY23.
- The elevated attrition (LTM 20.1%) is limiting the scope for improving utilization and reducing dependency on third-party contractors.
- The management also indicated that the company experienced its highest-ever number of lateral recruits during the year, which further limited the scope for optimizing cost and drive efficiency.

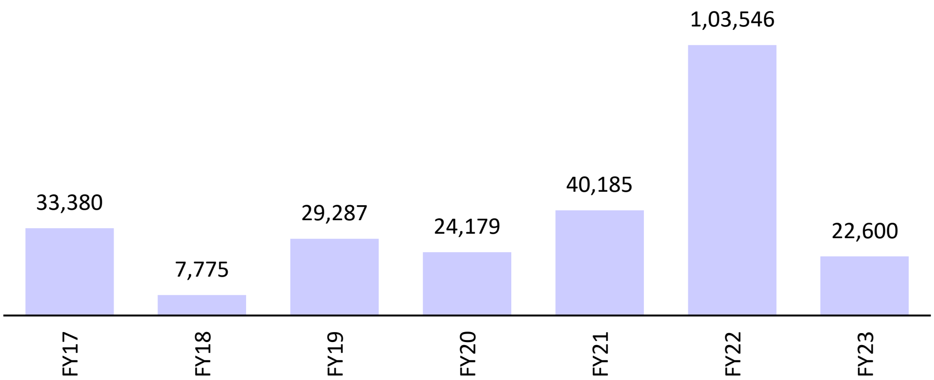
Exhibit 5: Backfilling and retention continue to pressurize EBIT margins



Source: MOFSL, Company

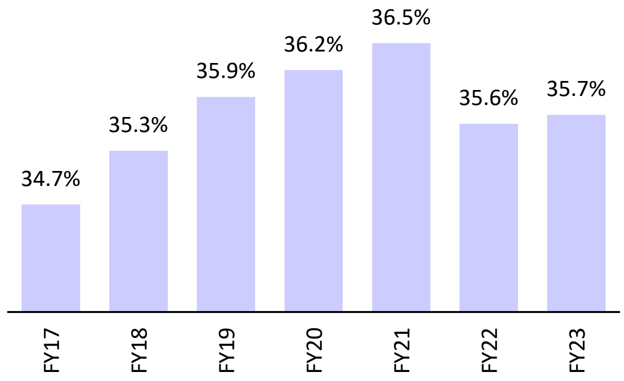
The adoption of Generative AI is expected to significantly reduce the effort required per function point, driving up programmer productivity. As a result, there will be greater capacity for consumption, with volume growth compensating for the reduced effort per unit.

Exhibit 6: Net headcount addition ('000) moderated in FY23 after a sharp uptick in FY22



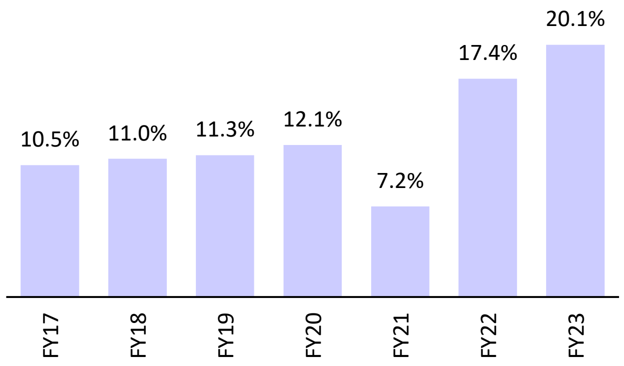
Source: MOFSL, Company

Exhibit 7: Percentage of Women Associates (%) in FY23



Source: MOFSL, Company

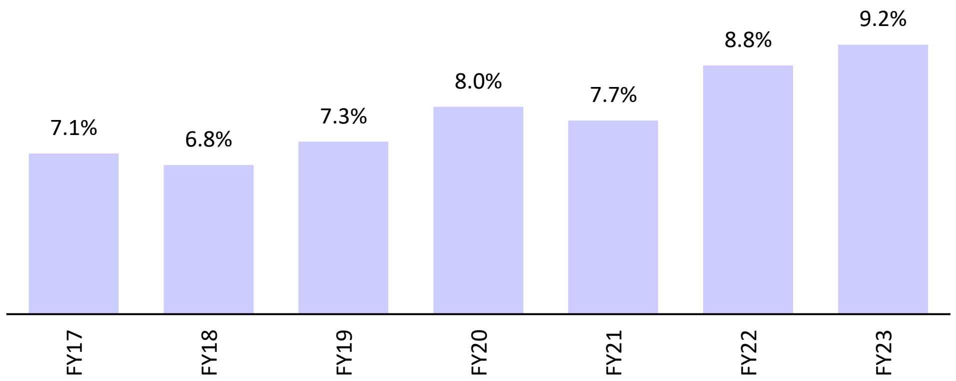
Exhibit 8: Attrition rate witnessed a strong uptick in FY23



Source: MOFSL, Company

The higher attrition among women in FY23 is a setback to the company's efforts, but it is doubling down on the same.

Exhibit 9: Subcontracting expenditure as a percentage of revenue is inching up



Source: MOFSL, Company

With supply-side challenges easing, the lateral hiring at premium and subcon expenses should get moderated in FY24.

Currency depreciation basically helps the company offset wage inflation in India; however, the benefits have never been passed on to the clients.

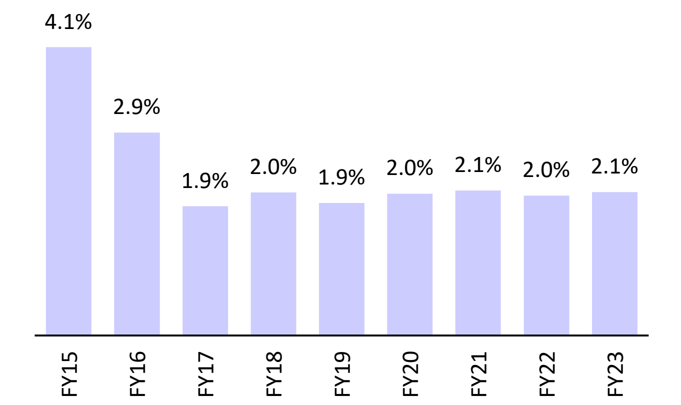
Margin outlook

- The management expects to trim down attrition in FY24, which was unusually high due to the transition from remote work setups, especially impacting women employees. The key focus would be on maximizing the effective utilization of the existing bench.
- The company has identified several margin levers that are expected to come into effect in FY24: (1) reduction in subcon expense (2) improvement in utilization (3) pyramid rationalization and (4) currency support.

Robust return profile

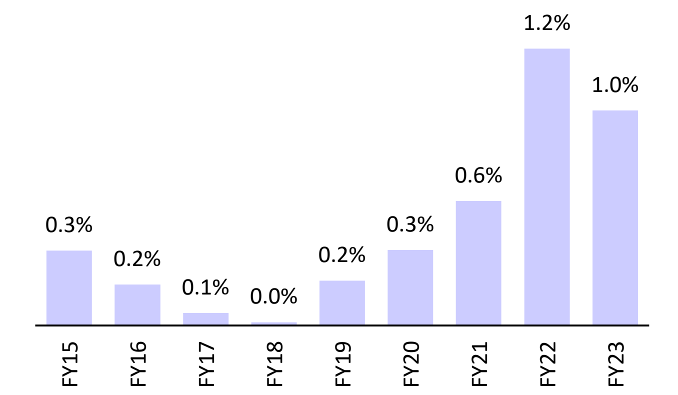
- TCS's payout ratio remains quite attractive at 99.8% (108% of FCF) in FY23, which is in line with its capital allocation policy of at least 80-100% of FCF.
- The return profile remains quite strong with an ROE of 46.9% and ROCE of 40.5%.
- The Goodwill as a percentage of net worth remained stable; however, the intangible assets have witnessed a sharp uptick over the last two years, on account of software licensing and customer-related intangibles.

Exhibit 10: Share of goodwill/intangible assets …



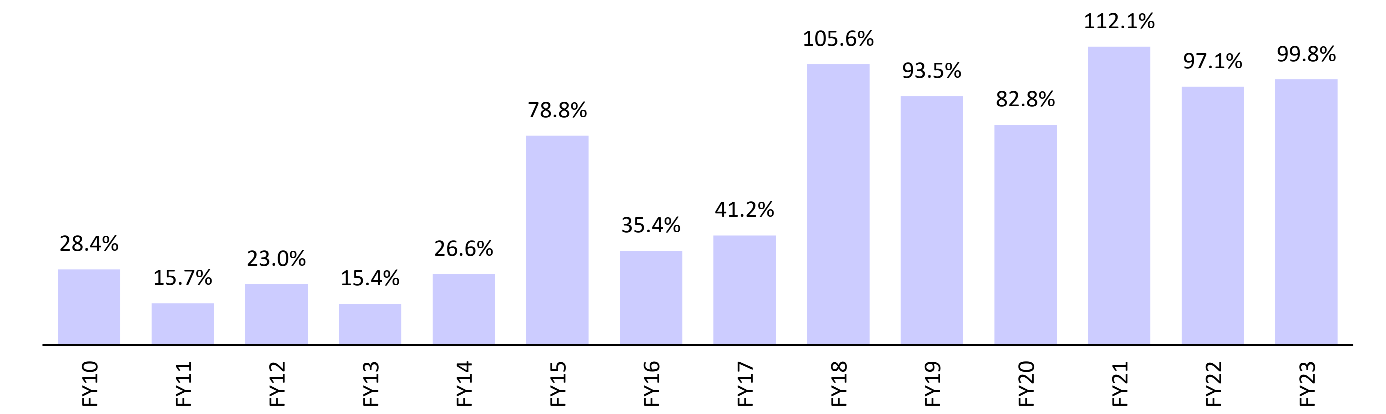
Source: Company, MOFSL

Exhibit 11: …% of net worth



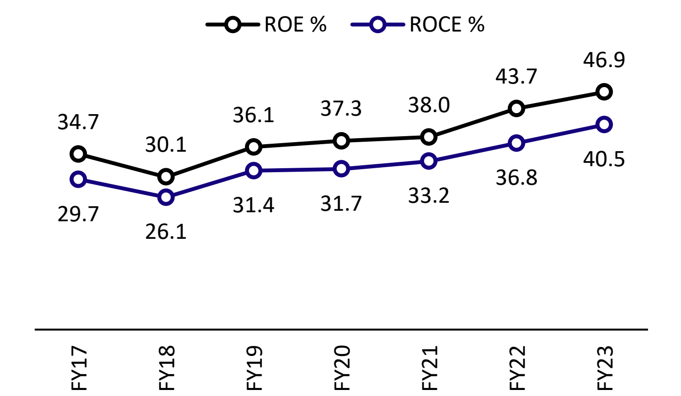
Source: Company, MOFSL

Exhibit 12: Payout (dividend + buyback) % remains robust



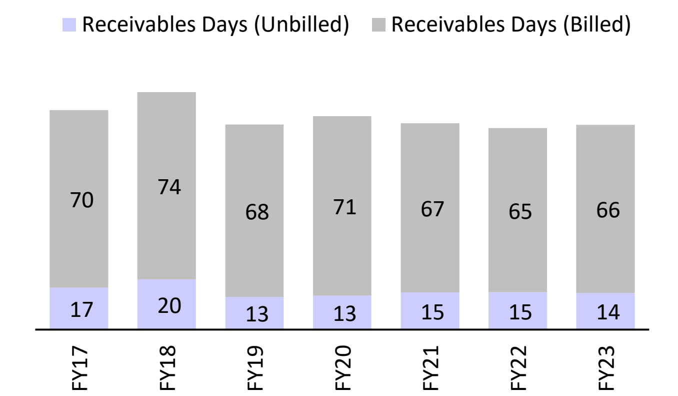
Source: MOFSL, Company

Exhibit 13: Improving ROE % and ROCE % - aided by payout



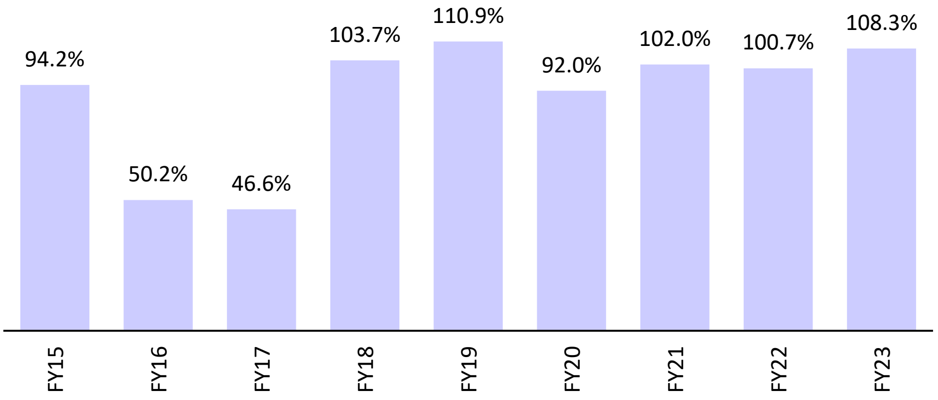
Source: MOFSL, Company

Exhibit 14: Billed & Unbilled Days remained stable



Source: MOFSL, Company

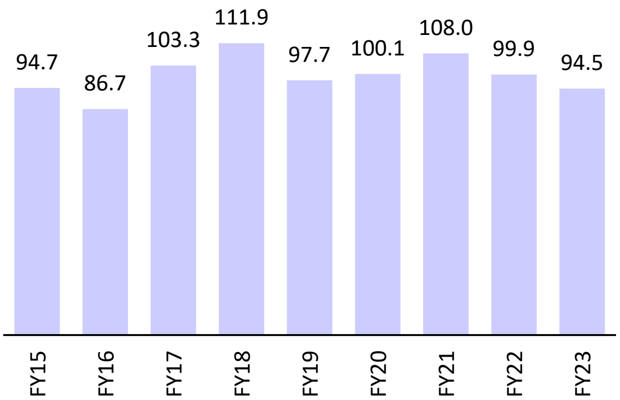
Exhibit 15: Payout % of FCF stood above the actual policy of retuning 80-100% of FCF



Source: MOFSL, Company

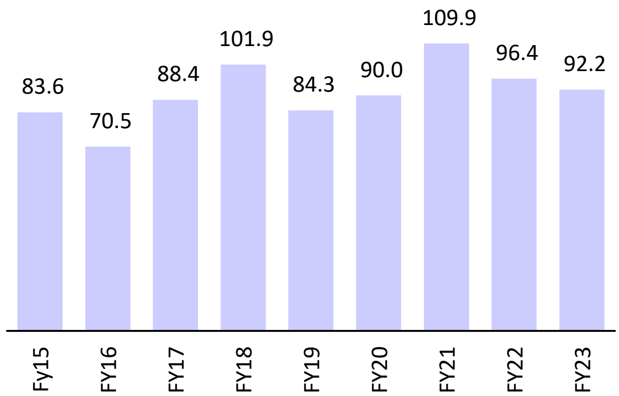
Cash conversion remains strong. Pre-tax OCF/EBITDA came in at 94.5% and FCF/PAT stood at 92.2% in FY23.

Exhibit 16: Pre-tax OCF/EBITDA and…



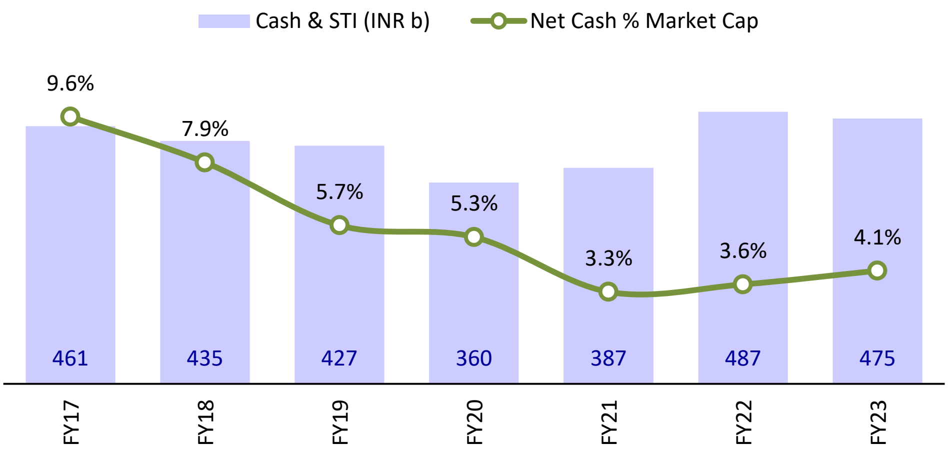
Source: MOFSL, Company

Exhibit 17: …FCF/PAT moderated, but still remain strong



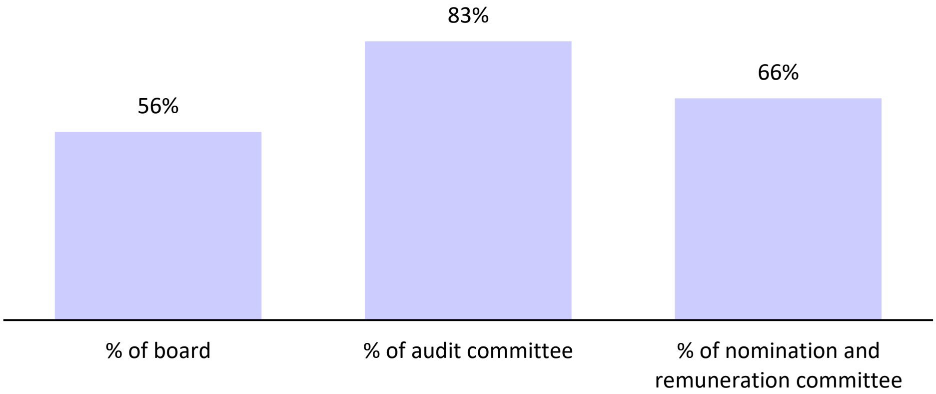
Source: MOFSL, Company

Exhibit 18: Cash & Cash Equivalent – healthy liquidity



Source: Company, MOFSL

Exhibit 19: Independent Directors % of board/audit/remuneration committee



Source: MOFSL, Company

Exhibit 20: Management remuneration

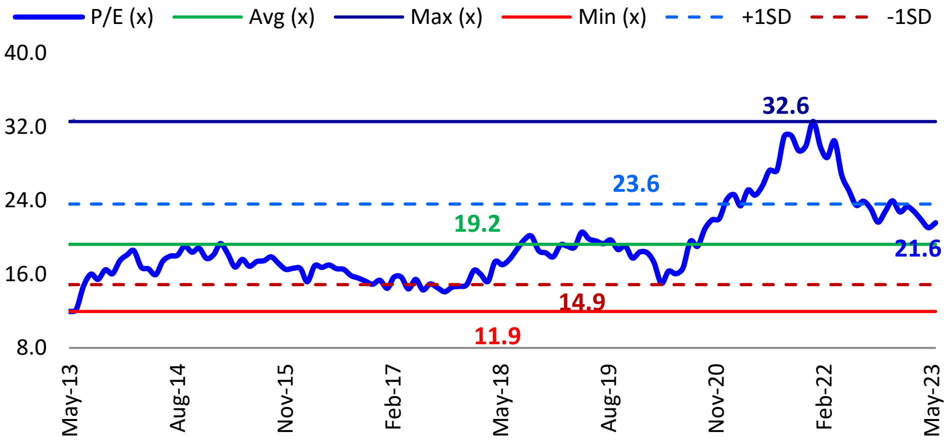
(INR m)	FY16	FY17	FY18	FY19	FY20	FY21	FY22	FY23
CEO	257	342	125	160	134	204	258	292
CFO	30	46	34	41	40	64	NA	NA
COO	NA	62	93	116	101	161	207	236
Total	286	449	252	318	275	429	465	528
Mgmt. remuneration as a % of PAT	0.10	0.20	0.10	0.10	0.10	0.10	0.12	0.12

Source: Company, MOFSL

Valuation and view

- Given TCS's 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.
- Owing to its steadfast market leadership position and best-in-class execution, the company has been able to maintain its industry-leading margin and demonstrate superior return ratios.
- We maintain our positive stance on TCS. Our TP of INR 3,860 implies 25x FY25E EPS, with a 20% upside potential. We reiterate our **BUY** rating.

Exhibit 21: PE Chart 1-year forward - TCS



Source: Company, MOFSL

Financials and valuations

Income Statement								(INR b)
Y/E March	**FY18**	**FY19**	**FY20**	**FY21**	**FY22**	**FY23**	**FY24E**	**FY25E**
Sales	**1,231**	**1,465**	**1,569**	**1,642**	**1,918**	**2,255**	**2,498**	**2,808**
Change (%)	4.4	19.0	7.2	4.6	16.8	17.6	10.8	12.4
Cost of Services	713	852	923	971	1,146	1,363	1,498	1,663
SG&A Expenses	213	239	260	246	287	350	386	430
EBITDA	**325**	**395**	**421**	**465**	**532**	**599**	**675**	**785**
% of Net Sales	26.4	27.0	26.8	28.4	27.8	26.6	27.0	28.0
Depreciation	20	21	35	41	48	56	62	70
EBIT	**305**	**375**	**386**	**425**	**485**	**542**	**613**	**715**
% of Net Sales	24.8	25.6	24.6	25.9	25.3	24.1	24.5	25.5
Other Income	36	41	37	25	32	27	39	45
PBT	**341**	**416**	**422**	**450**	**517**	**569**	**652**	**760**
Tax	82	100	98	115	132	146	166	194
Rate (%)	24.1	24.1	23.2	25.5	25.6	25.7	25.5	25.5
PAT	**259**	**316**	**324**	**335**	**384**	**423**	**486**	**566**
Extraordinary gains/loss	0	0	0	-10	0	0	0	0
Adjusted PAT	**259**	**316**	**324**	**326**	**384**	**423**	**486**	**566**
Minority Interest	1	1	1	1	1	2	2	2
Reported PAT	**258**	**315**	**323**	**324**	**383**	**421**	**484**	**565**
Change (%)	-1.8	21.9	2.8	0.3	18.2	10.0	14.9	16.6

Balance Sheet								(INR b)
Y/E March	**FY18**	**FY19**	**FY20**	**FY21**	**FY22**	**FY23**	**FY24E**	**FY25E**
Share capital	2	4	4	4	4	4	4	4
Reserves	849	891	838	861	888	901	875	845
Net Worth	**851**	**894**	**841**	**864**	**891**	**904**	**879**	**849**
Minority Interest & Others	33	34	97	102	100	97	124	139
Loans	1	0	0	0	0	0	0	0
Capital Employed	**885**	**929**	**938**	**966**	**992**	**1,001**	**1,003**	**988**
Gross Block	266	287	408	449	502	550	611	680
Depreciation	151	171	207	247	295	351	414	484
Net Block	**115**	**116**	**201**	**201**	**207**	**199**	**198**	**196**
Intangibles	52	44	45	57	55	52	56	52
Other LT assets	84	69	60	56	70	83	99	102
Curr. Assets	**812**	**921**	**902**	**993**	**1,083**	**1,103**	**1,114**	**1,129**
Debtors	316	325	363	367	418	500	548	608
Cash & Bank Balance	49	72	97	69	125	71	73	64
Investments	380	347	261	316	360	401	356	311
Other Current Assets	67	177	182	241	180	131	137	146
Current Liab. & Prov	**178**	**221**	**271**	**342**	**424**	**436**	**464**	**493**
Net Current Assets	**634**	**700**	**632**	**651**	**660**	**667**	**651**	**637**
Application of Funds	**885**	**929**	**938**	**966**	**992**	**1,001**	**1,003**	**988**

Financials and valuations

Ratios								
Y/E March	**FY18**	**FY19**	**FY20**	**FY21**	**FY22**	**FY23**	**FY24E**	**FY25E**
Basic (INR)								
EPS	**67.0**	**82.3**	**86.2**	**86.7**	**104.0**	**115.3**	**132.4**	**154.3**
Cash EPS	72.2	87.6	95.6	97.6	117.0	130.7	149.4	173.4
Book Value	220.9	233.8	224.2	231.1	241.8	247.3	240.0	231.9
DPS	70.7	76.9	71.4	97.2	100.9	115.1	119.1	138.8
Payout (%, Div+Buyback)	105.6	93.5	82.8	112.1	97.1	99.8	90.0	90.0
Valuation (x)								
P/E	47.9	39.0	37.2	37.0	30.9	27.8	24.3	20.8
Cash P/E	44.4	36.6	33.6	32.9	27.4	24.6	21.5	18.5
EV/EBITDA	37.9	30.9	28.4	25.6	22.0	19.5	17.3	14.9
EV/Sales	10.0	8.3	7.6	7.3	6.1	5.2	4.7	4.2
Price/Book Value	14.5	13.7	14.3	13.9	13.3	13.0	13.4	13.8
Dividend Yield (%)	2.2	2.4	2.2	3.0	3.1	3.6	3.7	4.3
Profitability Ratios (%)								
RoE	30.1	36.1	37.3	38.0	43.7	46.9	54.3	65.4
RoCE	26.1	31.4	31.7	33.2	36.8	40.5	45.6	53.5
Turnover Ratios								
Debtors (Days)	94	81	84	82	80	81	80	79
Fixed Asset Turnover (x)	10.7	12.7	7.8	8.1	9.3	11.3	12.6	14.3

Cash Flow Statement								(INR b)
Y/E March	**FY18**	**FY19**	**FY20**	**FY21**	**FY22**	**FY23**	**FY24E**	**FY25E**
CF from Operations	282	308	370	379	427	462	536	622
Cash for Working Capital	0	-22	-47	9	-28	-42	-21	-27
Net Operating CF	**282**	**286**	**324**	**388**	**399**	**420**	**515**	**595**
Net Purchase of FA	-19	-21	-32	-32	-30	-31	-48	-54
Free Cash Flow	**263**	**265**	**291**	**356**	**370**	**389**	**467**	**541**
Net Purchase of Invest.	16	36	118	-50	21	31	45	45
Net Cash from Invest.	**-3**	**16**	**86**	**-81**	**-9**	**0**	**-3**	**-9**
Proc. from equity issues	0	0	0	0	0	0	0	0
Proceeds from LTB/STB	0	-2	-13	-211	-195	-57	0	0
Others	0	-2	-9	-6	-7	-8	0	0
Dividend Payments	-268	-275	-377	-109	-134	-414	-510	-595
Cash Flow from Fin.	**-268**	**-279**	**-399**	**-326**	**-336**	**-479**	**-510**	**-595**
Net Cash Flow	**13**	**23**	**14**	**-18**	**56**	**-54**	**1**	**-9**
Opening Cash Bal.	**41**	**54**	**77**	**91**	**73**	**130**	**76**	**77**
Add: Net Cash	13	23	14	-18	56	-54	1	-9
Closing Cash Bal.	**54**	**77**	**91**	**73**	**130**	**76**	**77**	**69**

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NOTES

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BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
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