

## RETAIL EQUITY RESEARCH

## Tata Consultancy Services Ltd.

IT

BSE CODE: 532540

NSE CODE: TCS

Bloomberg CODE: TCS:IN

SENSEX: 36,318

**HOLD**

Rating as per Largecap

12months investment period

CMP Rs. 1,864 TARGET Rs. 2,036 RETURN 9% 16<sup>th</sup> January 2019**Below-par performance...**

Tata Consultancy Services Ltd (TCS) is the country's largest software exporter with a strong global footprint across 46 countries.

- TCS' dollar revenue growth of 0.7% QoQ was below expectation due to cross-currency headwinds.
- EBIT margin came in below expectation at 25.6% weighed down by higher subcontracting and employee costs due to increased hiring to meet demand.
- We have reduced our EBIT margin estimate for FY19E/20E given significant miss in margin in Q3FY19 and increasing sub contacting cost.
- Owing to sustained acceleration in BFSI and retail coupled with increasing enterprise wide digital implementation by clients, we factor revenue CAGR of 13% over FY18-21E.
- We continue to maintain our 'HOLD' rating on the stock with a revised TP of Rs. 2,036, valuing at 20x FY21E EPS.

**Currency fluctuations weighed on dollar revenue growth**

TCS delivered muted performance in Q3FY19 with consolidated revenue growth of 0.7% QoQ in dollar terms due to cross-currency headwinds. However, constant currency (CC) revenue growth stood at 1.8% QoQ/12.1% YoY in an otherwise seasonally weak quarter. The CC growth YoY (the highest in 14 quarter) was driven by continued acceleration across key verticals and geographies. Vertically, the growth was powered by BFSI (8.6% YoY), retail (10.5%), Telecom (10.8%) and life-sciences (15.7%), while UK (25.1%) & Europe (18%) led growth geographically. Further sustained momentum in digital business (grew strongly by 52.7% YoY) with revenue contribution increasing to 30.1% in Q3FY19 as compared to 28% in Q2FY19 also aided growth.

**Higher sub-contacting & employee costs hurt margin**

Tepid revenue growth along with higher sub-contracting cost led to 90bps QoQ decline in EBIT margin came to 25.6% which was below the guided range of 26-28%. Margin was also hurt by currency volatility and incremental onsite hiring. However, net profit grew by 2.6% QoQ mainly aided by higher other income. Despite pressure on margin in Q3FY19 and expectation of higher sub-contracting cost in short to medium term as the company tries to capture demand opportunities (digital technologies) and overcome supply (talent) constraints, the management is confident of sustaining margin in the target range in FY19 owing to expanding participation in digital transformation. However, we have reduced our EBIT margin estimate by 30bps each for FY19E/20E given miss in margin in Q3FY19 and increase in sub contacting cost.

**Enterprise wide adoption of digital led to strong deal wins**

Deal wins continued to stay robust for the company with the company bagging strong deal wins of USD 5.9 bn during the quarter as against USD 4.9 bn in Q2FY19 largely driven by increasing traction of digital business. Of the recent deal wins in Q3FY19, BFSI vertical accounted for USD 2 bn and retail USD 800 mn led by increasing spending by clients on digital technologies. The key BFSI (banking, financial services and insurance) vertical continued with its growth recovery, and management commentary suggests the momentum should continue. Driven by strong deal wins along with healthy deal pipeline and sustained traction in digital business due to enterprise-wide adoption of digital technologies by clients, management exuded confidence of continued growth momentum. Resultantly, we factor revenue CAGR of 13% over FY18-21E.

**Outlook & Valuation:** We have revised downwards our earnings estimate for FY19E/20E led by miss in margin in Q3FY19 and sustained investments to tap demand opportunities. However, strong order-book/pipeline, robust commentary and traction in digital, the company will continue to trade at premium valuation, we believe. Hence, we maintain 'HOLD' rating on the stock with a revised rolled-over TP of Rs. 2,036 based on 20x FY21E EPS.

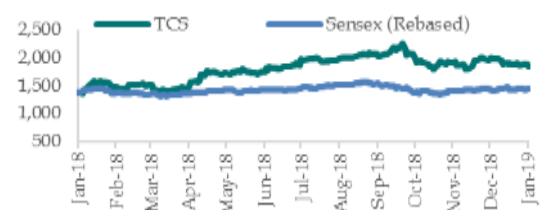
**Company Data**

Market Cap (Rs. cr)	699,710
Enterprise Value (Rs. cr)	658,038
Outstanding Shares (cr)	375.4
Free Float	28%
Dividend Yield	1.4%
52 week high	Rs. 2,273
52 week low	Rs. 1,368
6m average volume (cr)	0.3
Beta	0.6
Face value	Rs. 1

Shareholding %	Q4FY18	Q1FY19	Q2FY19
Promoters	71.9	71.9	72.0
FII's	16.9	16.6	16.1
MFs/Insti	6.9	6.9	7.4
Public	3.6	3.8	3.8
Others	0.7	0.8	0.7
Total	100.0	100.0	100.0

Price Performance	3mth	6mth	1 Year
Absolute Return	(5%)	(7%)	31%
Absolute Sensex	3%	-	4%
Relative Return*	(8%)	(7%)	27%

\*over or under performance to benchmark index



Consolidated (Rs.cr)	FY19E	FY20E	FY21E
Sales	1,46,829	1,61,901	1,77,245
Growth (%)	19.3%	10.3%	9.5%
EBITDA	40,012	44,603	49,008
Margin(%)	27.3	27.5	27.6
PAT Adj	31,578	34,943	38,221
Growth (%)	22.3%	10.7%	9.4%
Adj.EPS	84.1	93.1	101.8
Growth (%)	24.4%	10.7%	9.4%
P/E	22.2	20.0	18.3
P/B	7.9	6.4	5.3
EV/EBITDA	16.5	14.4	12.7
RoE (%)	36.5	35.5	31.9
D/E	(0.5)	(0.5)	(0.6)

## Quarterly Financials (Consolidated)

### Profit & Loss Account

(Rs cr)	Q3FY19	Q3FY18	YoY Growth %	Q2FY19	QoQ Growth %	9MFY19	9MFY18	YoY Growth %
Sales	37,338	30,904	20.8	36,854	1.3	1,08,453	91,029	19.1
EBITDA	10,083	8,287	21.7	10,278	(1.9)	29,432	23,864	23.3
Margin (%)	27.0	26.8	19bps	27.9	(88bps)	27.1	26.2	92bps
Depreciation	519	506	2.6	507	2.4	1519	1,509	0.7
EBIT	9,564	7,781	22.9	9,771	(2.1)	27,913	22,355	24.9
Interest	16	6	166.7	137	(88.3)	170	40	325.0
Other Income	1,163	870	33.7	730	59.3	3118	2,648	17.7
Exceptional Items	-	-	-	-	-	-	-	-
PBT	10,711	8,645	23.9	10,364	3.3	30,861	24,963	23.6
Tax	2590	2100	23.3	2,437	6.3	7451	6,008	24.0
PAT	8,121	6,545	24.1	7,927	2.4	23,410	18,955	23.5
Minority Interest	16	14	14.3	26	(38.5)	64	33	93.9
Reported PAT	8,105	6,531	24.1	7,901	2.6	23,346	18,922	23.4
Adjustment	-	-	-	-	-	-	-	-
Adj PAT	8,105	6,531	24.1	7,901	2.6	23,346	18,922	23.4
No. of shares (cr)	375.0	191.0	96.3	375.0	-	375.0	375.0	-
Adj. EPS (Rs)	21.6	17.4	24.1	21.1	2.6	62.3	50.5	23.4

### Segmental Revenue

(Rs cr)	Q3FY19	Q3FY18	YoY Growth %	Q2FY19	QoQ Growth %	9MFY19	9MFY18	YoY Growth %
Banking, Financial Services & Insurance	14,722	11,970	23.0	14,648	0.5	42,834	35,988	19.0
Manufacturing	3,958	3,315	19.4	3,919	1.0	11,623	9,785	18.8
Retail & Consumer Business	6,449	5,383	19.8	6,348	1.6	18,703	15,488	20.8
Communication, Media & Technology	6,090	5,370	13.4	6,009	1.3	17,829	15,680	13.7
Others	6,119	4,866	25.8	5,930	3.2	17,464	14,088	24.0
<b>Total revenue from operations</b>	<b>37,338</b>	<b>30,904</b>	<b>20.8</b>	<b>36,854</b>	<b>1.3</b>	<b>1,08,453</b>	<b>91,029</b>	<b>19.1</b>

Source: Company, Geojit Research

### Change in estimates

Year / Rs cr	Old estimates		New estimates		Change %	
	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E
Revenue	1,47,263	1,64,990	1,46,829	1,61,901	(0.3)	(1.9)
EBIT	38,506	43,515	37,946	42,316	(1.5)	(2.8)
EBIT Margins (%)	26.1	26.4	25.8	26.1	(30bps)	(30bps)
PAT	31,843	35,611	31,578	34,943	(0.8)	(1.9)
Adj. EPS	84.8	94.9	84.1	93.1	(0.8)	(1.9)

## Consolidated Financials

### Profit & Loss Account

Y.E March (Rs cr)	FY17	FY18	FY19E	FY20E	FY21E
<b>Sales</b>	<b>1,17,966</b>	<b>1,23,104</b>	<b>1,46,829</b>	<b>1,61,901</b>	<b>1,77,245</b>
% change	8.6%	4.4%	19.3%	10.3%	9.5%
<b>EBITDA</b>	<b>32,311</b>	<b>32,516</b>	<b>40,012</b>	<b>44,603</b>	<b>49,008</b>
% change	5.3%	0.6%	23.1%	11.5%	9.9%
Depreciation	1,987	2,014	2,066	2,288	2,524
<b>EBIT</b>	<b>30,324</b>	<b>30,502</b>	<b>37,946</b>	<b>42,316</b>	<b>46,484</b>
Interest	32	52	176	-	-
Other Income	4,221	3,642	3,907	3,796	3,948
<b>PBT</b>	<b>34,513</b>	<b>34,092</b>	<b>41,677</b>	<b>46,111</b>	<b>50,431</b>
% change	8.4%	-1.2%	22.2%	10.6%	9.4%
Tax	8,156	8,212	10,003	11,067	12,104
Tax Rate (%)	23.6%	24.1%	24.0%	24.0%	24.0%
<b>Reported PAT</b>	<b>26,289</b>	<b>25,826</b>	<b>31,578</b>	<b>34,943</b>	<b>38,221</b>
Adj*	-	-	-	-	-
<b>Adj PAT</b>	<b>26,289</b>	<b>25,826</b>	<b>31,578</b>	<b>34,943</b>	<b>38,221</b>
% change	8.3%	-1.8%	22.3%	10.7%	9.4%
No. of shares (cr)	394.0	382.0	375.4	375.4	375.4
<b>Adj EPS (Rs)</b>	<b>66.7</b>	<b>67.6</b>	<b>84.1</b>	<b>93.1</b>	<b>101.8</b>
% change	8.3%	1.3%	24.4%	10.7%	9.4%
DPS (Rs)	23.5	25.0	28.0	32.0	35.0

### Balance Sheet

Y.E March (Rs cr)	FY17	FY18	FY19E	FY20E	FY21E
Cash	4,149	7,161	5,664	8,393	9,763
Accounts Receivable	22,684	24,943	29,750	32,804	35,913
Inventories	21	26	26	26	26
Other Cur. Assets	12,036	13,387	15,023	16,535	18,167
Investments	41,980	36,008	36,008	51,008	69,008
Gross Fixed Assets	21,391	23,258	25,349	27,849	30,849
Net Fixed Assets	10,104	10,228	10,253	10,466	10,942
CWIP	1,541	1,278	1,278	1,278	1,278
Intangible Assets	1,597	1,745	1,726	1,726	1,726
Def. Tax (Net)	1,909	2,279	2,279	2,279	2,279
Other Assets	6,312	8,071	8,071	8,071	8,071
<b>Total Assets</b>	<b>1,02,333</b>	<b>1,05,126</b>	<b>1,10,078</b>	<b>1,32,586</b>	<b>1,57,172</b>
Current Liabilities	14,312	17,647	19,772	21,649	23,674
Provisions	-	-	-	-	-
Debt Funds	271	235	-	-	-
Other Liabilities	1,170	1,714	1,714	1,714	1,714
Equity Capital	197	191	375	375	375
Reserves & Surplus	86,017	84,937	87,718	1,08,246	1,30,700
Shareholder's Fund	86,214	85,128	88,093	1,08,621	1,31,076
Minority Interest	366	402	499	601	708
<b>Total Liabilities</b>	<b>1,02,333</b>	<b>1,05,126</b>	<b>1,10,078</b>	<b>1,32,586</b>	<b>1,57,172</b>
<b>BVPS (Rs)</b>	<b>218.8</b>	<b>222.8</b>	<b>234.7</b>	<b>289.4</b>	<b>349.2</b>

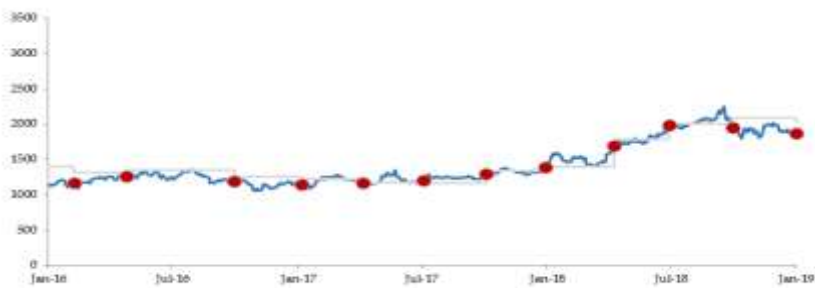
### Cash flow

Y.E March (Rs cr)	FY17	FY18	FY19E	FY20E	FY21E
<b>Pre-tax profit</b>	<b>26,357</b>	<b>25,880</b>	<b>41,677</b>	<b>46,111</b>	<b>50,431</b>
Depreciation	1,987	2,014	2,066	2,288	2,524
Changes in W.C	(631)	(209)	(4,318)	(2,689)	(2,716)
Others	5,456	4,991	(3,731)	(3,796)	(3,948)
Tax paid	(7,946)	(7,609)	(10,003)	(11,067)	(12,104)
<b>C.F.O</b>	<b>25,223</b>	<b>25,067</b>	<b>25,692</b>	<b>30,848</b>	<b>34,188</b>
Capital exp.	(1,990)	(1,862)	(2,072)	(2,500)	(3,000)
Change in inv.	(18,627)	3,721	-	(15,000)	(18,000)
Other invest.CF	3,885	1,027	3,907	3,796	3,948
<b>C.F - investing</b>	<b>(16,732)</b>	<b>2,886</b>	<b>1,835</b>	<b>(13,704)</b>	<b>(17,052)</b>
Issue of equity	-	(16,042)	(16,000)	-	-
Issue/repay debt	87	(19)	(235)	-	-
Dividends paid	(10,973)	(10,760)	(12,613)	(14,415)	(15,766)
Other finance.CF	(140)	(64)	(176)	-	-
<b>C.F - Financing</b>	<b>(11,026)</b>	<b>(26,885)</b>	<b>(29,024)</b>	<b>(14,415)</b>	<b>(15,766)</b>
Chg. in cash	(2,535)	1,068	(1,497)	2,729	1,370
Closing cash	4,149	7,161	5,664	8,393	9,763

### Ratios

Y.E March	FY17	FY18	FY19E	FY20E	FY21E
<b>Profitab. &amp; Return</b>					
EBITDA margin (%)	27.4	26.4	27.3	27.5	27.6
EBIT margin (%)	25.7	24.8	25.8	26.1	26.2
Net profit mgn.(%)	22.3	21.0	21.5	21.6	21.6
ROE (%)	33.4	30.1	36.5	35.5	31.9
ROCE (%)	43.6	39.6	48.0	46.6	41.9
<b>W.C &amp; Liquidity</b>					
Receivables (days)	70	74	74	74	74
Inventory (days)	0	0	0	0	0
Payables (days)	27	21	21	21	21
Current ratio (x)	5.7	4.6	4.4	5.0	5.6
Quick ratio (x)	5.6	4.6	4.4	5.0	5.6
<b>Turnover &amp; Levq.</b>					
Gross asset T.O (x)	5.7	5.5	6.0	6.1	6.0
Total asset T.O (x)	1.2	1.2	1.4	1.3	1.2
Adj. debt/equity (x)	(0.5)	(0.5)	(0.5)	(0.5)	(0.6)
<b>Valuation ratios</b>					
EV/Net Sales (x)	5.8	5.4	4.5	4.0	3.5
EV/EBITDA (x)	21.3	20.6	16.5	14.4	12.7
P/E (x)	27.9	27.6	22.2	20.0	18.3
P/BV (x)	8.5	8.4	7.9	6.4	5.3

## Recommendation Summary (last 3 years)



Source: Bloomberg, Geojit Research

Dates	Rating	Target
07 January 2015	BUY	1425
10 March 2015	BUY	1500
10 April 2015	BUY	1425
20 May 2015	BUY	1450
01 October 2015	BUY	1475
11 January 2016	BUY	1400
22 February 2016	BUY	1315
09 May 2016	HOLD	1354
18 October 2016	HOLD	1253
20 January 2017	HOLD	1218
20 April 2017	HOLD	1173
18 July 2017	HOLD	1161
18 October 2017	HOLD	1342
15 January 2018	HOLD	1394
25 April 2018	HOLD	1779
16 July 2018	HOLD	2011
16 October 2018	HOLD	2087
16 January 2019	HOLD	2036

## Investment Rating Criteria

### Large Cap Stocks;

Buy	-	Upside is above 10%.
Hold	-	Upside is between 0% - 10%.
Reduce	-	Downside is more than 0%.
Neutral	-	Not Applicable.

### Mid Cap and Small Cap;

Buy	-	Upside is above 15%.
Accumulate	-	Upside is between 10% - 15%.
Hold	-	Upside is between 0% - 10%.
Reduce/Sell	-	Downside is more than 0%.
Neutral	-	Not Applicable.

To satisfy regulatory requirements, we attribute 'Accumulate' as Buy and 'Reduce' as Sell. The recommendations are based on 12 month horizon, unless otherwise specified. The investment ratings are on absolute positive/negative return basis. It is possible that due to volatile price fluctuation in the near to medium term, there could be a temporary mismatch to rating.

For reasons of valuations/return/lack of clarity/event we may revisit rating at appropriate time. Please note that the stock always carries the risk of being upgraded to BUY or downgraded to a HOLD, REDUCE or SELL.

Neutral - The analyst has no investment opinion on the stock under review.

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