

RETAIL EQUITY RESEARCH

Tata Consultancy Services Ltd.

IT

BSE CODE: 532540

NSE CODE: TCS

Bloomberg CODE: TCS:IN

SENSEX: 29,422

HOLD

Rating as per Largecap

12months investment period

CMP Rs2328 TARGET Rs2346 RETURN 1% 20th April, 2017**Secular growth still missing...**

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

- Despite volume growth of 1.7% in Q4FY17, TCS' consolidated revenue declined by 0.3% QoQ owing to lower realisation (pricing pressure in traditional verticals).
- EBIT margin came in lower at 25.7% in Q4FY17 down by 30bps QoQ largely impacted by adverse cross currency movement and higher employee cost.
- Although management reiterated EBIT margin target of 26-28% in FY18E, we expect EBIT margin to remain under pressure due to subdued demand in BFSI and Retail verticals and higher investments in offshore hiring.
- The management is confident of recovery in BFSI vertical on the back of strong deal pipeline, increasing size of digital projects and better diligenta performance.
- However, growth in traditional vertical (BFSI) is yet to gain pace and the demand environment still remains elusive, we reckon. Hence, we maintain HOLD rating with a revised TP of Rs2,346 (earlier Rs2,346) (based on 15.5x FY19E P/E).

Revenue misses estimates

TCS' Q4FY17 performance was slightly below our expectations with revenue declining by 0.3% QoQ despite volume growth of 1.7%, clearly indicating pricing pressure in the traditional verticals. Realisation during the quarter fell 0.7% QoQ in CC terms. Revenue was also impacted by adverse cross currency movement (1.3%). While revenue in dollar terms increased 1.5% QoQ, it rose 1% in constant currency. Geographically, revenue from North America and Latin America fell 1.8% and 7.3% respectively in constant currency, while India grew by 9.3% QoQ. Notably, digital business (accounted for 16.7% of overall revenue in FY17) is gaining pace with revenue growth of 29% YoY in FY17.

Poor show in BFSI & Retail verticals

BFSI vertical continued its weak performance in Q4FY17 with revenue declining by 1.6% QoQ due to cyclical factors and completion of one large project in the previous quarter in North America. Further revenue from Retail segment fell 2.9% amid structural challenges in the industry. However, the communication, media & technology segment posted 5.3% growth during the quarter. Deal signing was healthy with the company bagging 9 large deals during the quarter.

EBIT margin hurt by volatility in currency

TCS reported lower EBIT margin of 25.7% in Q4FY17 as against 26% in Q3FY17 largely due to the impact of cross currency during the quarter and higher employee costs. The management reiterated EBIT margin target of 26-28% in FY18 owing to various levers including increasing size of digital business, improving demand environment, better diligenta performance and higher productivity. However, with growing concerns over tougher US visa policy and subdued demand in BFSI & Retail verticals, we expect margin to come under pressure. We factor EBIT margin of 25.2%/25.1% in FY18E/19E.

Weakness in BFSI & Retail vertical to persist

However, the management sounded optimistic on the BFSI vertical, we expect the demand to remain soft for the next few quarters as growing concerns over Brexit and expected regulatory changes in US visa policy could defer client spending. Besides, structural weakness in retail segment will further dampen growth of the company. Hence, we expect revenue to grow at a CAGR of 8% over FY17-19E.

Outlook & Valuation

We have reduced our EBIT margin by 70bps for FY18E/19E to factor in higher investments by the company towards building digital capabilities and higher offshore hiring. As a result, we expect the net profit to grow at a moderate CAGR of 6.5% over FY17-19E. Thus, we have slightly toned down our PAT estimates for FY18E/FY19E by 2.8%/3.7%. Maintain HOLD with a revised TP of Rs2,346 (earlier Rs2,436) based on 15.5x FY19E P/E.

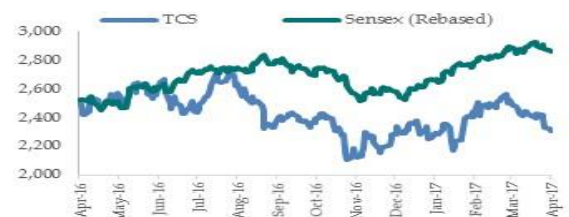
Company Data

Market Cap (Rs cr)	458,785
Enterprise Value (Rs cr)	399,896
Outstanding Shares (cr)	197.0
Free Float	26%
Dividend Yield	1.9%
52 week high	Rs2,740
52 week low	Rs2,055
6m average volume (cr)	0.1
Beta	0.3
Face value	Rs1

Shareholding %	Q1FY17	Q2FY17	Q3FY17
Promoters	73.3	73.3	73.3
FII's	17.0	17.0	16.8
MFs/Insti	5.2	5.2	5.4
Public	4.0	4.0	4.0
Others	0.5	0.5	0.5
Total	100.0	100.0	100.0

Price Performance	3mth	6mth	1 Year
Absolute Return	1.8%	(3.0%)	(5.0%)
Absolute Sensex	8.8%	4.6%	13.8%
Relative Return*	(7.0%)	(7.6%)	(18.9%)

*over or under performance to benchmark index



Consolidated (Rs.cr)	FY17	FY18E	FY19E
Sales	1,17,966	1,26,931	1,37,659
Growth (%)	8.6%	7.6%	8.5%
EBITDA	32,311	34,178	36,929
Margin(%)	27.4	26.9	26.8
PAT Adj	26,289	27,790	29,822
Growth (%)	8.2%	5.7%	7.3%
Adj.EPS	133.4	141.1	151.4
Growth (%)	8.2%	5.7%	7.3%
P/E	17.4	16.5	15.4
P/B	5.3	4.5	3.9
EV/EBITDA	12.8	11.7	10.5
RoE (%)	34.7	29.5	27.0
D/E	(0.5)	(0.6)	(0.6)

Quarterly Financials (Consolidated)

Profit & Loss Account

(Rs cr)	Q4FY17	Q4FY16	YoY Growth %	Q3FY17	QoQ Growth %
Sales	29,642	28,449	4.2	29,735	(0.3)
EBITDA	8,132	7,907	2.8	8,229	(1.2)
Margin (%)	27.4	27.8	(36) bps	27.7	(24) bps
Depreciation	505	495	2.0	496	1.8
EBIT	7,627	7,412	2.9	7,733	(1.4)
Interest	8	10	(20.0)	7	14.3
Other Income	997	915	9.0	1192	(16.4)
Exceptional Items	-	-	-	-	-
PBT	8,616	8,317	3.6	8,918	(3.4)
Tax	1994	1970	1.2	2,104	(5.2)
PAT	6,622	6,347	4.3	6,814	(2.8)
Minority Interest/ PL from associates	14	7	100.0	36	(61.1)
Reported PAT	6,608	6,340	4.2	6,778	(2.5)
Adjustment	-	-	-	-	-
Adj PAT	6,608	6,340	4.2	6,778	(2.5)
No. of shares (cr)	197.0	197.0	-	197.0	-
EPS (Rs)	33.5	32.2	4.2	34.4	(2.5)

Segmental Revenue

(Rs cr)	Q4FY17	Q4FY16	YoY Growth %	Q3FY17	QoQ Growth %
Banking, Financial Services & Insurance	11,828	11,644	1.6	12,021	(1.6)
Manufacturing	3,148	2,951	6.7	3,155	(0.2)
Retail & Consumer Business	4,993	3,085	61.8	5,143	(2.9)
Communication, Media & Technology	5,001	4,021	24.4	4,751	5.3
Others	4,672	6,748	(30.8)	4,665	0.2
Total revenue from operations	29,642	28,449	4.2	29,735	(0.3)

Source: Company, Geojit Research

Change in estimates

Year / Rs cr	Old estimates		New estimates		Change %	
	FY18E	FY19E	FY18E	FY19E	FY18E	FY19E
Revenue	129,201	141,444	126,931	137,659	(1.8)	(2.7)
EBIT	33,518	36,657	31,983	34,488	(4.6)	(5.9)
Margins (%)	25.9	25.8	25.2	25.1	(70bps)	(70bps)
PAT	28,591	30,961	27,790	29,822	(2.8)	(3.7)
EPS	145.1	157.1	141.1	151.4	(2.8)	(3.6)

Consolidated Financials

Profit & Loss Account

Y.E March (Rs cr)	FY15	FY16	FY17	FY18E	FY19E
Sales	1,08,646	1,17,966	1,26,931	1,37,659	1,08,646
% change	14.8%	8.6%	7.6%	8.5%	14.8%
EBITDA	30,590	32,311	34,178	36,929	30,590
% change	24.9%	5.6%	5.8%	8.0%	24.9%
Depreciation	1,948	1,987	2,195	2,441	1,948
EBIT	28,642	30,324	31,983	34,488	28,642
Interest	20	32	37	37	20
Other Income	3,054	4,221	4,542	4,640	3,054
PBT	31,676	34,513	36,488	39,091	31,676
% change	22.7%	9.0%	5.7%	7.1%	22.7%
Tax	7,301	8,156	8,623	9,186	7,301
Tax Rate (%)	23.0%	23.6%	23.6%	23.5%	23.0%
Reported PAT	24,292	26,289	27,790	29,822	24,292
Adj*	-	-	-	-	-
Adj PAT	24,292	26,289	27,790	29,822	24,292
% change	25.5%	8.2%	5.7%	7.3%	25.5%
No. of shares (cr)	197.0	197.0	197.0	197.0	197.0
Adj EPS (Rs)	123.3	133.4	141.1	151.4	123.3
% change	24.7%	8.2%	5.7%	7.3%	24.7%
DPS (Rs)	43.5	47.0	51.7	56.9	43.5

Cash flow

Y.E March (Rs cr)	FY15	FY16	FY17	FY18E	FY19E
Pre-tax profit	26,298	31,676	26,357	36,488	39,091
Depreciation	1,309	1,948	1,987	2,195	2,441
Changes in W.C	747	(4,824)	(631)	(1,446)	(1,812)
Others	(1,504)	(2,116)	5,456	(4,505)	(4,603)
Tax paid	(7,482)	(7,569)	(7,946)	(8,623)	(9,186)
C.F.O	19,369	19,115	25,223	24,109	25,931
Capital exp.	(2,949)	(2,047)	(1,990)	(3,541)	(4,041)
Change in inv.	1,990	(19,626)	(18,625)	(13,000)	(13,000)
Other invest.CF	(742)	16,464	3,883	4,542	4,640
C.F - investing	(1,701)	(5,209)	(16,732)	(11,999)	(12,401)
Issue of equity	-	-	-	-	-
Issue/repay debt	43	(73)	87	-	-
Dividends paid	(17,106)	(9,524)	(10,973)	(11,868)	(13,055)
Other finance.CF	(105)	(19)	(140)	(37)	(37)
C.F - Financing	(17,168)	(9,616)	(11,026)	(11,905)	(13,092)
Chg. in cash	500	4,291	(2,535)	206	438
Closing cash	18,556	6,785	4,149	4,355	4,793

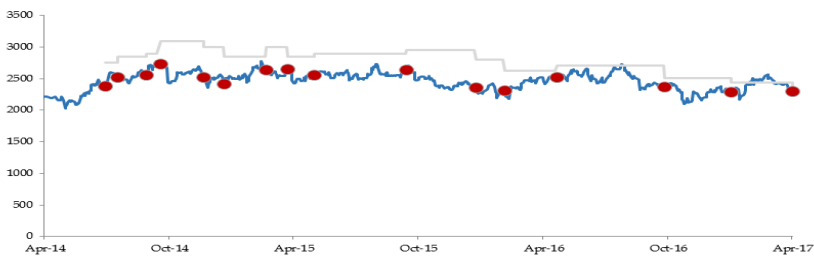
Balance Sheet

Y.E March (Rs cr)	FY15	FY16	FY17	FY18E	FY19E
Cash	18,556	6,785	4,149	4,355	4,793
Accounts Receivable	24,265	28,061	28,035	30,166	32,715
Inventories	16	16	21	21	21
Other Cur. Assets	4,483	5,846	6,685	7,248	7,900
Investments	1,662	22,586	41,636	54,636	67,636
Gross Fixed Assets	17,316	19,932	21,349	24,390	27,431
Net Fixed Assets	9,545	10,674	10,104	10,950	11,550
CWIP	2,766	1,671	1,541	2,041	3,041
Intangible Assets	2,093	1,952	1,597	1,597	1,597
Def. Tax (Net)	251	382	1,909	1,909	1,909
Other Assets	9,680	10,970	6,656	6,656	6,656
Total Assets	73,318	88,943	1,02,333	1,19,579	1,37,818
Current Liabilities	20,133	21,863	14,312	15,560	16,950
Provisions	-	-	-	-	-
Debt Funds	300	195	271	271	271
Other Liabilities	1,123	1,022	1,170	1,170	1,170
Equity Capital	196	197	197	197	197
Reserves & Surplus	50,439	65,164	86,017	1,01,939	1,18,707
Shareholder's Fund	50,635	65,361	86,214	1,02,136	1,18,904
Minority Interest	1,128	502	366	441	523
Total Liabilities	73,318	88,943	1,02,333	1,19,579	1,37,817
BVPS (Rs)	258.5	331.7	437.6	518.5	603.6

Ratios

Y.E March	FY15	FY16	FY17	FY18E	FY19E
Profitab. & Return					
EBITDA margin (%)	25.9	28.2	27.4	26.9	26.8
EBIT margin (%)	24.0	26.4	25.7	25.2	25.1
Net profit mgn.(%)	20.5	22.4	22.3	21.9	21.7
ROE (%)	38.8	41.9	34.7	29.5	27.0
ROCE (%)	50.7	53.7	45.2	38.5	35.2
W.C & Liquidity					
Receivables (days)	93.6	94.3	86.7	86.7	86.7
Inventory (days)	0.1	0.1	0.1	0.1	0.1
Payables (days)	45.9	35.3	26.8	26.8	26.8
Current ratio (x)	2.4	2.9	5.6	6.2	6.7
Quick ratio (x)	2.4	2.9	5.6	6.2	6.7
Turnover &Levg.					
Gross asset T.O (x)	6.1	5.8	5.7	5.6	5.3
Total asset T.O (x)	1.4	1.3	1.2	1.1	1.1
Adj. debt/equity (x)	(0.4)	(0.4)	(0.5)	(0.6)	(0.6)
Valuation ratios					
EV/Sales (x)	4.6	4.0	3.5	3.2	2.8
EV/EBITDA (x)	17.9	14.1	12.8	11.7	10.5
P/E (x)	23.6	18.9	17.4	16.5	15.4
P/BV (x)	9.0	7.0	5.3	4.5	3.9

Recommendation Summary (last 3 years)



Dates	Rating	Target
17 July 2014	BUY	2750
05 August 2014	BUY	2850
16 September 2014	BUY	2900
07 October 2014	BUY	3100
09 December 2014	BUY	3000
07 January 2015	BUY	2850
10 March 2015	BUY	3000
10 April 2015	BUY	2850
20 May 2015	BUY	2900
01 October 2015	BUY	2950
11 January 2016	BUY	2800
22 February 2016	BUY	2630
09 May 2016	HOLD	2708
18 October 2016	HOLD	2505
20 January 2017	HOLD	2436
20 April 2017	HOLD	2346

Source: Bloomberg, Geojit Research

Investment Rating Criteria

Large Cap Stocks;		Mid Cap and Small Cap;			
Buy	-	Upside is 10% or more.	Buy	-	Upside is 15% or more.
Hold	-	Upside or downside is less than 10%.	Accumulate*	-	Upside between 10% - 15%.
Reduce	-	Downside is 10% or more.	Hold	-	Absolute returns between 0% - 10%.
			Reduce/Sell	-	Absolute returns less than 0%.

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.

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