

Robust order book to drive growth; Gen AI, a key theme

TCS reported Q2FY24 revenues at \$7,210mn (below our estimates), up 4.8%YoY in USD terms and 2.8%YoY in CC terms. In INR terms, revenue stood at INR596.9bn, up 7.9% YoY and 0.5% sequentially. Q2FY24 order book TCV stood second highest ever at \$11.2bn led by robust North America order book at \$4.5bn and BFSI order book at \$3.03bn. Book-to-Bill ratio came at 1.6 for Q2FY24. Net CFO stood at 104.2% of net income to INR118.2bn.

- **Q2 growth led by UK geography and Energy & Utilities vertical:** Q2 revenue was neutralized by reduction in the revenue base as the transformation projects got completed. However, growth was led by UK geography (+10.7% YoY), Energy, Resources and Utilities (+14.8%), Manufacturing (+5.8%) and Lifesciences & Healthcare vertical (+5%). Geographically, management sees maximum caution in North America and Continental Europe. Middle East and Africa grew 15.9%, Latin America grew 13.1% and Asia Pacific grew 4.1%.
- **Honouring all trainee offers:** LTM attrition stood at 14.9% (down 290 bps sequentially). There was a net addition of -6,333 employees resulting in workforce strength at 608,985. Company has recalibrated hiring, keeping it below the deposits to drive productivity and enhance project outcomes. Management is proactively hiring freshers and trainees and is investing in training in them.
- **Margins target band 26%+:** Operating margins in Q2FY24 expanded 110bps sequentially to 24.3% mainly due to disciplined execution which resulted in improved utilization and productivity and further optimization of sub-contract expenses. Company also benefitted from driving efficiencies in discretionary expenses. Management also mentioned that getting employees to work from office wont impact margins as it is continuously investing in infrastructure. Improved utilization and optimization of sub-contract expenses will help company expand its operating margin going forward. Management aspires the margin band between 26-28% going ahead. Net margin came in at 19% for Q2FY24.
- **Management Outlook:** Management is cautious of slower discretionary spends and expects H2 to be worse than H1. Europe turned out to be positive and order book in Europe appears to be good for long term. Quarterly TCV expectation range has been upgraded to \$9-10bn range from earlier \$7-9bn range. Clients continue to prioritize business agility and cost optimization initiatives even while exploring innovative uses of Gen AI. Clients are also focused on operating model transformation, vendor consolidation and Enterprise IT as a Service.
- **Valuation:** The resilience of demand for services, commitment to long tenure programs and the continued appetite for experimentation with Gen AI and other new technologies boosts confidence in longer-term growth prospects. We have introduced FY26E and expect Revenue/EBIT/PAT to grow at a CAGR of 8.3%/9.5%/9% respectively over FY23-FY26E. We upgrade our rating to **ADD** with a revised target price of INR4,040 implying a PE of 25x (unchanged) on FY26E EPS of INR162.

Financial Snapshot

Particulars	FY22	FY23	FY24	FY25E	FY26E
Revenue (USD Mn.)	25,707	27,927	29,217	31,730	34,858
Revenue (INR Mn.)	19,57,720	22,89,070	24,16,269	26,38,828	29,10,638
Gross Profit (INR Mn.)	6,96,450	7,81,690	8,14,519	9,10,207	10,14,817
EBIT (INR Mn.)	5,24,710	5,76,860	5,99,461	6,76,250	7,56,533
EBIT Margin (%)	26.8	25.2	24.8	25.6	26.0
EPS (INR)	104	115	129	145	162

Source: Company, CEBPL

Oct 12, 2023

CMP (Rs.)	3,610
Target Price (Rs.)	4,040
Potential Upside (%)	11.9

Company Info

BB Code	TCS IN EQUITY
ISIN	INE467B01029
Face Value (Rs.)	1.0
52 Week High (Rs.)	3,680.0
52 Week Low (Rs.)	3,053.3
Mkt Cap (Rs Bn.)	13,209.9
Mkt Cap (\$ Bn.)	160.8
Shares o/s (Mn.)/Float	3,659/28
FY23 EPS (Rs.)	115
FY26E EPS (Rs.)	162

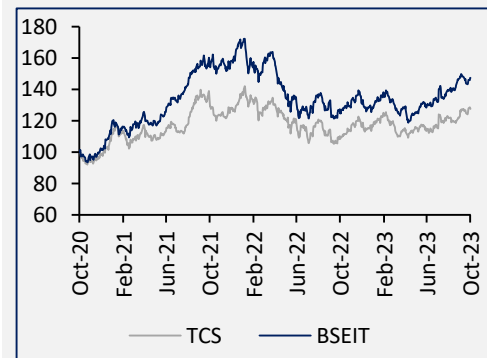
Shareholding Pattern (%)

	Jun-23	Mar-23	Dec-22
Promoters	72.30	72.30	72.30
FII's	12.46	12.72	12.94
DII's	9.80	9.58	9.25
Public	5.44	5.40	5.51

Relative Performance (%)

YTD	3Y	2Y	1Y
BSE IT	47.3	(5.2)	18.2
TCS	27.5	(2.1)	17.6

Rebased Price Performance



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Sequential Operating Performance

	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24
Income Statement						
Revenues (USD Mn.)	6,780	6,877	7,075	7,226	7,226	7,210
Revenues (INR Mn.)	5,27,580	5,53,090	5,82,290	5,93,810	5,93,810	5,96,920
Gross Profit (INR mn.)	1,69,310	1,83,580	1,96,400	1,91,440	1,91,440	1,98,160
Gross Margin (%)	32.1	33.2	33.7	32.2	32.2	33.2
EBIT (INR mn.)	1,21,860	1,32,790	1,42,840	1,37,550	1,37,550	1,44,830
EBIT Margin (%)	23.1	24.0	24.5	23.2	23.2	24.3
PAT (INR mn.)	94,780	1,04,310	1,08,460	1,10,740	1,10,740	1,13,420
Basic EPS (INR)	25.9	28.5	29.6	30.3	30.3	31.0
Operating Metrics						
Revenue – Geography (%)						
Americas	55.0	56.0	55.5	54.2	54.0	53.7
Europe	30.1	29.0	29.7	30.8	31.3	31.4
India	4.8	5.1	5.1	8.0	4.9	4.9
Asia Pacific	8.3	8.0	7.9	5.0	7.8	7.8
MEA	1.8	1.9	1.8	2.0	2.0	2.2
Total	100.0	100.0	100.0	100.0	100.0	100.0
Revenue – Industry (%)						
BFSI	32.1	33.6	33.1	32.9	32.5	32.6
Retail & CPG	15.9	16.1	16.0	16.0	16.1	15.9
Communication & Media	6.8	7.3	7.2	7.1	7.0	6.9
Manufacturing	9.9	8.2	8.2	8.2	8.3	8.5
Life Science & Healthcare	10.1	10.7	10.8	10.9	11.0	10.9
Energy & Utilities	-	5.0	5.2	5.4	5.5	5.6
Technology & Services	8.8	9.1	9.0	8.9	8.7	8.6
Regional Markets & Others	16.4	10.0	10.5	10.6	10.9	11.0
Total	100.0	100.0	100.0	100.0	100.0	100.0
Clients Buckets						
USD 1 mn clients	1,196	1,210	1,217	1,241	1,268	1,272
USD 5 mn clients	650	650	658	665	677	688
USD 10 mn clients	446	455	456	461	468	483
USD 20 mn clients	272	283	290	291	296	292
USD 50 mn clients	124	124	130	133	137	137
USD 100 mn clients	59	59	59	60	60	61
Employee Metrics						
Total Headcount	6,06,331	6,16,171	6,13,974	6,14,795	6,15,318	6,08,985
Attrition Rate %	19.7	21.5	21.3	20.1	17.8	14.9

Source: Company, CEBPL

CEBPL Estimates vs Actual for Q2FY24

TCS (INR Mn.)	Q2FY24	Q2FY23	YoY(%)	Q1FY24	QoQ (%)	CEBPL Est.	Dev. (%)
Revenues (\$ mn.)	7,210	6,877	4.8	7,226	(0.2)	7,290	(1.1)
Revenues	5,96,920	5,53,090	7.9	5,93,810	0.5	6,01,398	(0.7)
Employee Cost	3,98,760	3,69,510	7.9	4,02,370	(0.9)		
Gross Profit (INR mn.)	1,98,160	1,83,580	7.9	1,91,440	3.5	1,99,916	(0.9)
Gross Margin (%)	33.2	33.2	1 bps	32.2	96 bps	33.2	(4) bps
Other costs	40,710	38,420	6.0	41,460	(1.8)		
Depreciation	12,620	12,370	2.0	12,430	1.5		
EBIT (INR mn.)	1,44,830	1,32,790	9.1	1,37,550	5.3	1,45,047	(0.1)
EBIT Margin (%)	24.3	24.0	25 bps	23.2	110 bps	24.1	14 bps
Other Income	10,060	9,650	4.2	13,970	(28.0)		
Interest	1,590	1,480	7.4	1,630	(2.5)		
PBT (INR mn.)	1,53,300	1,40,960	8.8	1,49,890	2.3		
Tax	39,500	36,310	8.8	38,690	2.1		
Adj. PAT (INR mn.)	1,13,420	1,04,310	8.7	1,10,740	2.4	1,14,063	(0.6)
Basic EPS (INR)	31.00	28.51	8.7	30.26	2.4	31.17	(0.6)

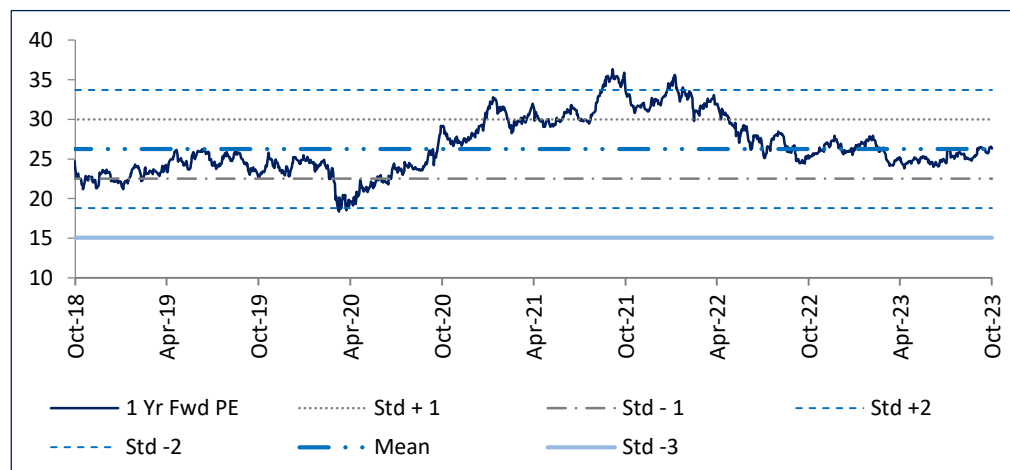
Source: Company, CEBPL

Change in Estimates

Income Statement (INR Mn.)	FY24E			FY25E			FY26E
	Old	New	Dev. (%)	Old	New	Dev. (%)	New
Revenues (USD Mn.)	29,562	29,217	(1.2)	32,303	31,730	(1.8)	34,858
Revenues	24,55,286	24,16,269	(1.6)	27,18,533	26,38,828	(2.9)	29,10,638
Gross Profit Margin (%)	33.7	33.7	1 bps	34.4	34.5	9 bps	34.9
EBIT	6,07,170	5,99,461	(1.3)	6,93,403	6,76,250	(2.5)	7,56,533
EBIT Margin (%)	24.7	24.8	8 bps	25.5	25.6	12 bps	26.0
EPS	130.6	129.0	(1.2)	147.0	144.5	(1.7)	161.6

Source: Company, CEBPL

Historical 1 Yr Fwd PE Band suggest multiples are reverting to mean

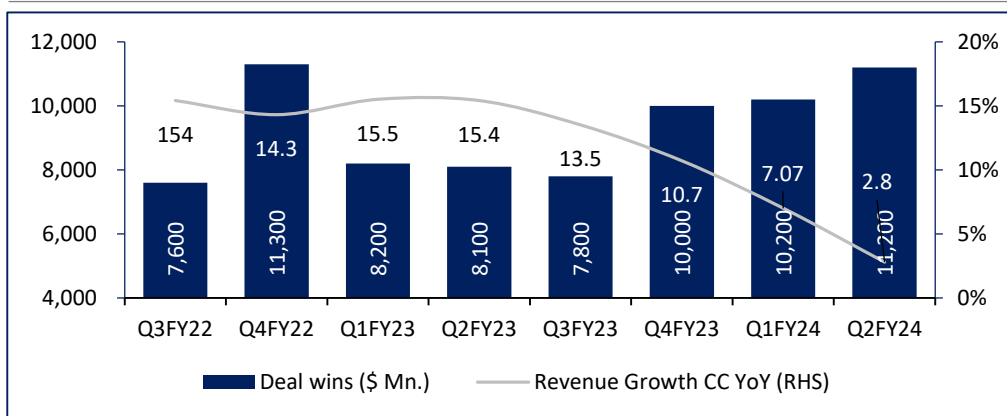


Source: Company, CEBPL

Management Call - Highlights

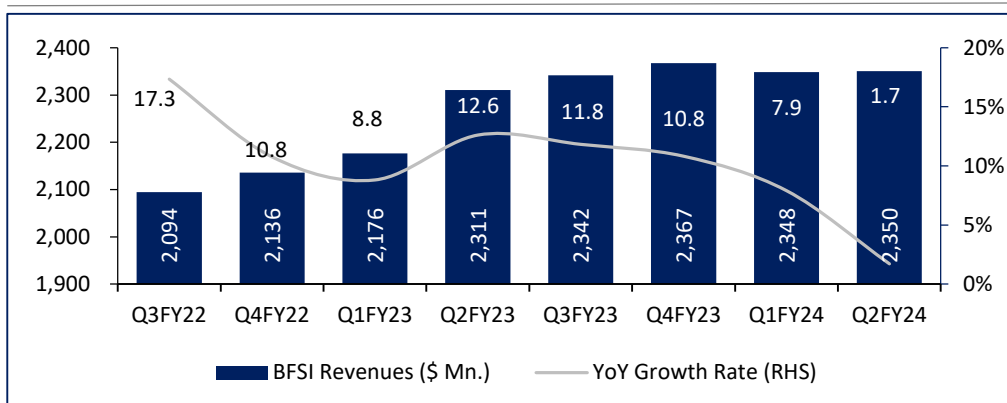
- Net cash generated from operations reached INR118.3bn, equivalent to 104.2% of net income. Free cash flow amounted to INR113.57bn, and the invested funds as of September 30th totalled as INR596.77 bn.
- The Board has proposed an interim dividend of INR9 per share. Additionally, the board recommended a buyback of INR170bn through the tender route at a price of INR4,150 per share.
- TCS currently has a workforce of over 100,000 Gen AI-ready employees, and the company is actively investing in enhancing its expertise in this innovative technology.
- TCS reported revenues from North America, Latin America, the UK, Europe, and Australia under the industry verticals separating out the emerging market revenues products and platforms.
- BSNL has chosen TCS to deploy an advanced 4G and 5G mobile communication infrastructure throughout India, encompassing 100,000 telecom sites. This project encompasses the supply, planning, installation, commissioning, and optimization of the mobile network to meet specific requirements compliant with 3GPP standards.
- Growth was led by the Energy, Resources and Utilities vertical which grew 14.8%, Manufacturing which grew 5.8% and Life Sciences and Healthcare which grew 5%. The Consumer Business Group (CBG) grew 1%, BFSI grew -0.5%, Communications & Media grew -2.1% and Technology & Services grew -2.2%. Among major markets, the United Kingdom led with 10.7% growth; North America grew 0.1% and Continental Europe grew 1.3%. In emerging markets, Middle East & Africa grew 15.9%, Latin America grew 13.1%, Asia Pacific grew 4.1% and India grew 3.9%.
- JLR has expanded its strategic partnership with TCS to accelerate digital transformation across its business. As a part of this deal, TCS will deliver a broad range of services spanning application development & maintenance, enterprise infrastructure management, cloud migration, cybersecurity, and data services. TCS will help JLR transform to a leaner and scalable operating model with a future-ready digital core, by leveraging new technologies to transform IT operations and adopting new ways of working.

Outperform on the Deal wins



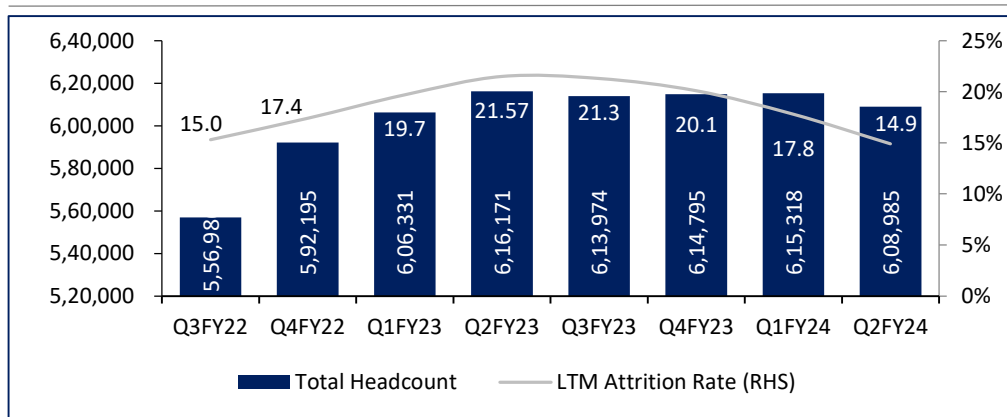
Source: Company, CEBPL

BFSI segment particularly experienced a flattish quarter



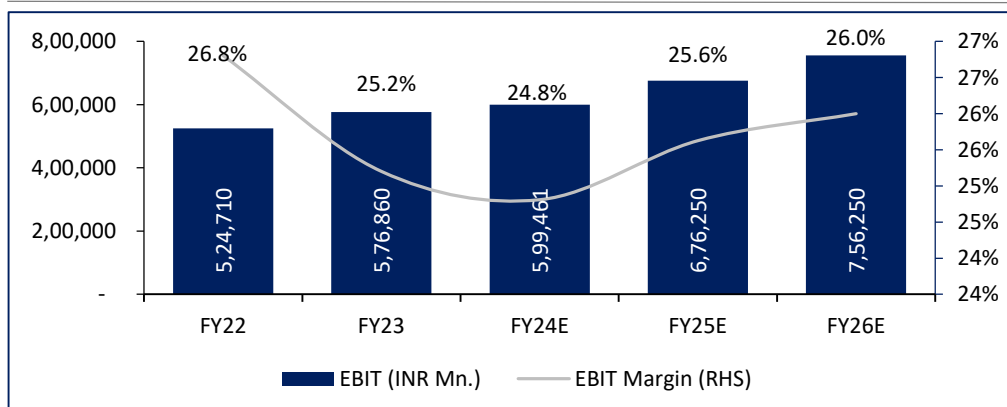
Source: Company, CEBPL

Attrition rate is dipping from the peak in Q2FY23



Source: Company, CEBPL

Operating Margins band to be between 26-28%



Source: Company, CEBPL

Financial Summary (Consolidated in INR Mn.)

Income Statement (INR Mn.)	FY22	FY23	FY24E	FY25E	FY26E
Revenue (USD Mn.)	25,707	27,927	29,217	31,730	34,858
Revenue	19,57,720	22,89,070	24,16,269	26,38,828	29,10,638
Gross profit	6,96,450	7,81,690	8,14,519	9,10,207	10,14,817
EBITDA	5,70,750	6,27,090	6,43,425	7,17,014	8,10,112
Depreciation	46,040	50,230	43,963	40,764	53,579
EBIT	5,24,710	5,76,860	5,99,461	6,76,250	7,56,533
Other income	80,360	68,980	44,453	42,085	43,794
Interest expense	7,840	7,790	7,836	8,534	10,157
Exceptional items	-	-	-	-	-
Reported PAT	5,57,050	6,03,560	6,36,078	7,09,802	7,90,170
Adjusted PAT	4,23,450	4,55,960	4,72,067	5,28,702	5,91,108
EPS	104	115	129	145	162

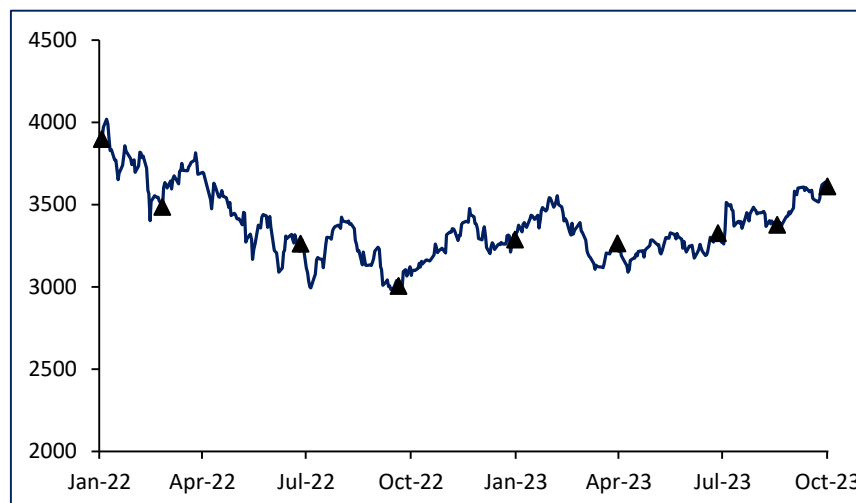
Balance Sheet (INR Mn.)	FY22	FY23	FY24E	FY25E	FY26E
Tangible fixed assets	1,19,790	1,14,640	1,15,745	1,25,286	1,35,613
Goodwill & intangible assets	1,05,240	1,02,850	1,24,680	1,33,426	1,42,893
Investments	3,04,850	3,71,630	5,38,066	5,92,025	6,51,403
Cash & Cash equivalents	1,82,210	1,10,320	1,29,200	1,32,624	1,56,329
Other non-current assets	1,04,780	1,13,660	1,13,905	1,21,764	1,31,292
Other current assets	5,98,270	6,23,410	5,37,315	5,61,613	5,70,179
Total assets	14,15,140	14,36,510	15,58,910	16,66,738	17,87,710
Shareholder's funds	8,91,390	9,04,240	9,97,373	10,75,387	11,62,761
Minority interest	7,070	7,820	7,820	7,820	7,820
Borrowings	-	-	-	-	-
Lease liabilities	78,180	76,880	80,724	84,760	88,998
Other non-current liabilities	29,490	26,840	26,840	26,840	26,840
Other current liabilities	4,09,010	4,20,730	4,46,152	4,71,931	5,01,290
Total equity & liabilities	14,15,140	14,36,510	15,58,910	16,66,738	17,87,710

Cash Flows (INR Mn.)	FY22	FY23	FY24E	FY25E	FY26E
Cash flows from Operations	4,39,670	4,54,140	5,43,479	5,78,836	6,76,308
Cash flows from Investing	(8,970)	390	(2,32,934)	(1,12,552)	(1,32,224)
Cash flows from financing	(3,34,010)	(4,78,960)	(3,88,370)	(4,60,742)	(5,15,410)

Ratio Analysis	FY22	FY23	FY24E	FY25E	FY26E
Growth Ratios (%)					
Revenues	17.0	16.9	5.6	9.2	10.3
Gross Profit	14.5	12.2	4.2	11.7	11.5
EBITDA	14.9	9.9	2.6	11.4	13.0
EBIT	15.0	9.9	3.9	12.8	11.9
Margin Ratios (%)					
Gross Profit Margin	35.6	34.1	33.7	34.5	34.9
EBITDA Margin	29.2	27.4	26.6	27.2	27.8
EBIT Margin	26.8	25.2	24.8	25.6	26.0
Profitability (%)					
Return on equity	47.8	51.0	49.8	51.2	53.0
Return on invested capital	41.2	44.6	41.5	43.6	45.5
Return on capital employed	53.3	58.1	55.0	57.8	60.0
Valuation					
OCF / Net profit (%)	103.5	99.3	114.7	109.2	114.1
EV / EBITDA (x)	23.62	18.74	18.24	16.36	14.45
Book Value per share (x)	240.98	244.45	269.63	290.72	314.34
Free Cash flow yield (%)	3.8	4.7	5.4	5.9	6.7

Source: Company, CEBPL

Historical recommendations and target price: TCS



Tata Consultancy Services Ltd.

1.	14-01-2022	Outperform,	Target Price 4,815
2.	12-04-2022	Outperform,	Target Price 4,265
3.	11-07-2022	Outperform,	Target Price 3,993
4.	10-10-2022	Neutral,	Target Price 3,449
5.	10-01-2023	Neutral,	Target Price 3,454
6.	15-04-2023	Add,	Target Price 3,536
7.	13-07-2023	Add,	Target Price 3,507
8.	25-09-2023	Neutral,	Target Price 3,730
9.	12-10-2023	Add,	Target Price 4,040

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ADD	The security is expected to generate greater than 5% to less than 15% returns over the next 12 months
NEUTRAL	The security expected to show downside or upside returns by 5% over the next 12 months
REDUCE	The security expected to show less than -5% to greater than -15% over the next 12 months
UNDERPERFORM	The security is expected to generate returns in excess of -15% over the next 12 months

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