

Mixed numbers for Q2; Accumulate

Q2FY24 Result Update | Sector: IT | October 12, 2023

Accumulate

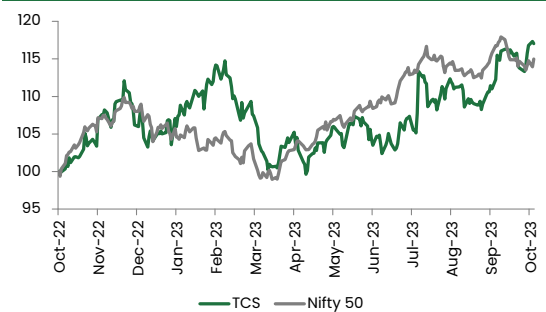
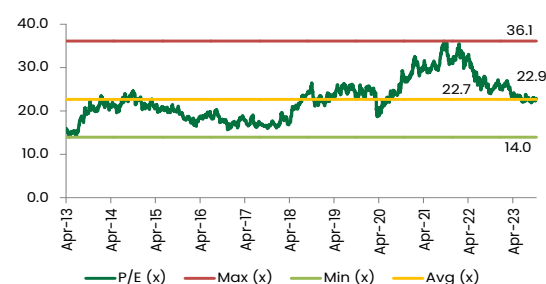
CMP (Rs)	3,610
Target Price (Rs)	4,089
Potential Upside	13.3%
Sensex	66,596
Nifty	19,772

Key Stock data

BSE Code	532540
NSE Code	TCS
Bloomberg	TCS:IN
Shares o/s, Cr (FV 1)	366.0
Market Cap (Rs Cr)	1,123,164
3M Avg Volume	1,997,551
52 week H/L	3,679/3,052

Shareholding Pattern

(%)	Dec-22	Mar-23	Jun-23
Promoter	72.3	72.3	72.3
FII	12.9	12.7	12.5
DII	9.3	9.6	9.8
Others	5.5	5.4	5.4

1 Year relative price performance

1 year PE Forward (x)

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Revenue a miss: TCS Q2FY24 revenue came in below our expectations. Its rupee revenue was up by 0.5% QoQ and 7.9% YoY to Rs 59,692cr and revenue in USD came in at USD 7,210mn, de-growth of 0.2% but growth of 4.8% YoY. Further, growth in constant currency was higher by 2.8% YoY. There is uncertainty around client spending and they are more focused on optimization of deals, so some of them are getting reprioritized which resulted in moderate revenue growth. Amongst geographies, North American region growth was flat and amongst verticals BFSI, media and technology witnessed negative CC growth, so this impacted the overall revenue performance. On the flip side, the UK region showed decent growth of 10.7% YoY in CC and manufacturing as well as energy & Resources grew by 5.8% YoY and 14.8% YoY, respectively.

Healthy improvement of margins: TCS EBIT grew by 9.1% YoY and 5.3% QoQ to Rs 14,483cr while margin improved by 25bps YoY and 110bps QoQ to 24.3%. For margins, improving utilization & productivity as well as reduction in sub contract and curtailing discretionary spends aided improvement while margin impacted by higher investment in infrastructure. In the long run, management aspires to achieve margins of 26-28%.

Attrition Moderated: TCS attrition further eased to 14.9% in Q2FY24 as compared to 17.8% (down by 290bps) in Q1FY24 and 21.5% in Q2FY23 (down by 660bps) is positive. Meanwhile, the company strategy is to train employees and improve productivity, so ~over 1 lakh employees are trained for artificial intelligence skill sets, even though the avg. contracts on generative AI are worth less than USD 1mn.

Record order book for Q2FY24: The company won deals worth USD 11.2 bn, up by 9.8% QoQ and 38.3% YoY. Geographically and vertically the deals are earned from North America TCV at USD 4.5bn, BFSI TCV at USD 3bn and Consumer Business TCV at USD 1.4bn but did not see much translation into revenue. Amongst the deals, BSNL and JLR is the largest followed by other deals from government of India, GE Healthcare, Athora Netherlands, ASDA, British Council, Georgia Department of Labor, Culina UK's supply chain manager, etc.

Announcement of BuyBack: The company has proposed a buyback wherein its offer price is at 15% premium from current closing price of Rs 3,610. They have approved upto 4.09 lakh Equity Shares worth Rs 17,000cr representing 1.12% of the paid-up equity at a price of Rs 4,150/share. The Buyback is subject to shareholders approval.

Management outlook: 1) TCS strategy of hiring freshers, training them and improving productivity is aiding growth. 2) Clients are looking for definitive signs of recovery and they are expected to start spending on cloud, digital and new technology. 3) BSNL deal is important for the company. 4) Announced dividend of Rs 9/share.

Outlook & Valuation: TCS posted mixed numbers for Q2FY24 wherein revenue missed our estimates but margins improved, order inflow was strong and attrition eased. Further, management still remains cautious for the near term on the back of anticipated uncertainty around macro environment, however from a long term perspective strong demand for newer technology, record order inflows, client willingness to commit for long term deals and investment towards development of technology and training employees is positive. Meanwhile, the company's focus continues on translating deals to revenue, managing cost and improving margins. On the financial front, we have estimated its revenue/EBIT to grow at 16.5/19.8% CAGR over FY23-25E. Our view remains mixed for TCS and that is the reason we have revised our rating to **Accumulate** from Buy earlier, with upward revision in target price to **Rs 4,089**.

Financial Summary - consolidated

Particulars, Rs cr	FY22	FY23	FY24E	FY25E
Net revenue	191,754	225,458	261,531	305,992
EBIT	48,453	54,237	64,039	77,863
EBITM (%)	25.3	24.1	24.5	25.4
APAT	38,449	42,303	49,011	59,627
APATM (%)	20.1	18.8	18.7	19.5
EPS (Rs)	105.1	115.6	133.9	162.9
PE (x)	34.4	31.2	27.0	22.2
RoE (%)	43.1	46.8	41.7	42.4

Source : RBL Research

Key Highlights: 1) Clients are focused on operating model transformation, vendor consolidation and Enterprise IT as a Service 2) For Buyback, The public announcement and Letter of Offer, timelines and other requisite details will be released by the company in due course in accordance with the Buyback Regulations. 3) Amongst geographies, North America region which is its largest revenue earning region (contributing 51.7% revenue) witnessed flat growth which impacted revenue growth. Besides, the downside was capped as growth was seen in other regions wherein Europe growth driven by UK region growth of 10.7% in CC, Middle East & Africa grew by 15.9% in CC as well as India and Asia Pacific grew by 3.9% and 4.1%, respectively. 4) Amongst verticals, mixed sentiment was observed as the company's 50% revenue is earned by BFSI, Media and Technology saw de-growth of 0.5%, 2.1% and 2.2% in CC. However, the verticals such as Energy, Manufacturing, Life-science and Retail grew by 14.8%, 5.8%, 5.0% and 1.0% in CC, respectively.

P&L Account Quarterly - consolidated

Particulars, Rs cr	Q2FY24	Q2FY23	Y-o-Y %	Q1FY24	Q-o-Q %
Net Sales (\$ Mn)	7,210	6,877	4.8	7,226	(0.2)
Net Sales (Rs Cr)	59,692	55,309	7.9	59,381	0.5
Employee Cost	35,123	31,041	13.2	35,148	(0.1)
Cost of equipment and licenses	462	401	15.2	506	(8.7)
Other Expense	8,361	9,351	(10.6)	8,729	(4.2)
Total Expenditure	43,946	40,793	7.7	44,383	(1.0)
EBITDA	15,746	14,516	8.5	14,998	5.0
EBITDA Margins (%)	26.4	26.2	13bps	25.3	112bps
Depreciation	1,263	1,237	2.1	1,243	1.6
EBIT	14,483	13,279	9.1	13,755	5.3
EBIT Margins (%)	24.3	24.0	25bps	23.2	110bps
Other Income	1,006	965	4.2	1,397	(28.0)
Interest	159	148	7.4	163	(2.5)
PBT	15,330	14,096	8.8	14,989	2.3
PBT Margin (%)	25.7	25.5	20bps	25.2	44bps
Tax	3,950	3,631	8.8	3,869	2.1
PAT	11,380	10,465	8.7	11,120	2.3
PAT Margin (%)	19.1	18.9	14bps	18.7	34bps
EPS	31.1	28.6	8.7	30.4	2.3

Source : RBL Research

Client prioritizing spending led to moderate revenue growth

Better utilization and improving productivity helped margin improvement

North America region growth was flat while UK led the growth

Revenue Distribution by Geography & growth in Constant Currency (%)

Particulars	Q2FY24	Q2FY23	Y-o-Y %
Americas	53.7	56.0	-
North America	51.7	54.3	0.1
Latin America *	2.0	1.7	13.1
Europe	31.4	29.0	-
UK	16.5	14.5	10.7
Continental Europe	14.9	14.5	1.3
India	4.9	5.1	3.9
Asia Pacific	7.8	8.0	4.1
MEA	2.2	1.9	15.9

Source : RBL Research

Energy & Manufacturing vertical led the growth

Revenue Distribution by Industry & Growth in Constant Currency (%)

Particulars	Q2FY24	Q2FY23	Y-o-Y %
BFSI	32.6	31.9	(0.5)
Retail & CPG	15.9	15.9	1.0
Communication & Media	6.9	6.7	(2.1)
Manufacturing	8.5	9.9	5.8
Life Science & Healthcare	10.9	10.2	5.0
Technology & Services	8.6	9.0	(2.2)
Energy, Resources and Utilities	5.6	5.0	14.8
Regional Markets & Others	11.0	11.4	14.3

Source : RBL Research

Steady Client addition

Clients Contribution

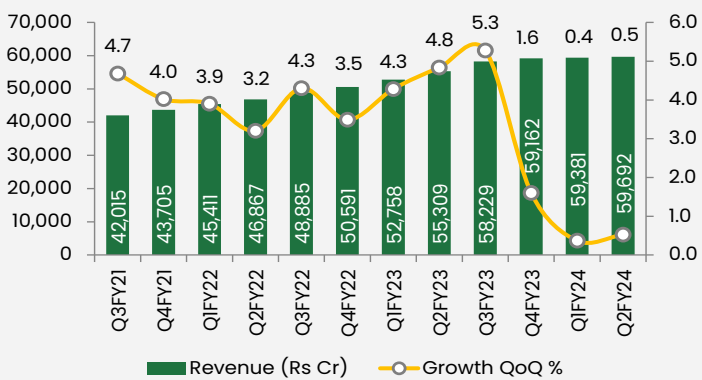
Particulars	Q2FY24	Q2FY23
USD 1 mn clients *	1,272	1,210
USD 5 mn clients *	688	650
USD 10 mn clients *	483	455
USD 20 mn clients *	292	283
USD 50 mn clients *	137	124
USD 100 mn clients *	61	59

* Last Twelve Months' services revenues; includes clients in India

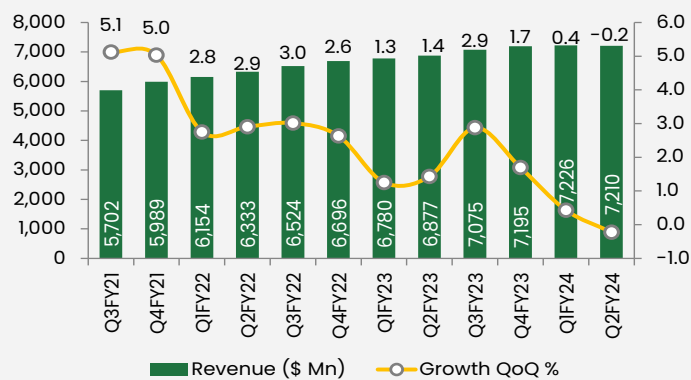
Source : RBL Research

Story in charts

Revenue in rupee grew by 0.5% QoQ and 7.9% YoY

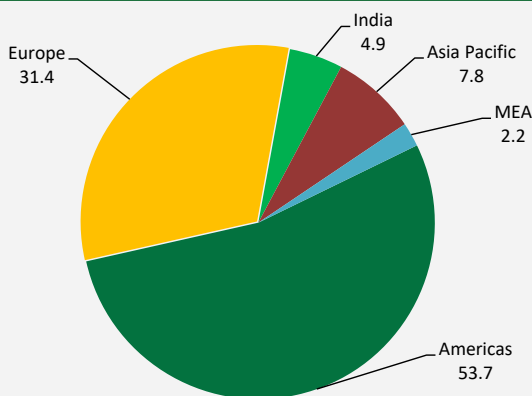


Revenue in dollar de-grew by 0.2% QoQ and grew by 4.8% YoY

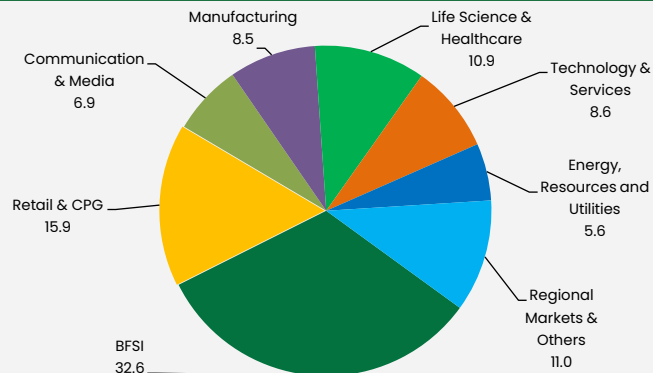


Source : RBL Research

Revenue Distribution by Geography (%)

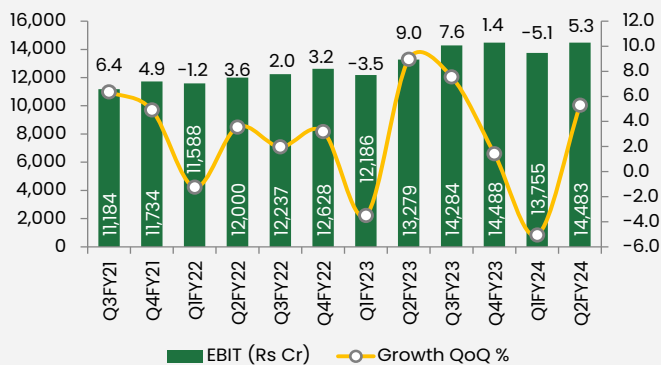


Revenue Distribution by Industry Vertical (%)

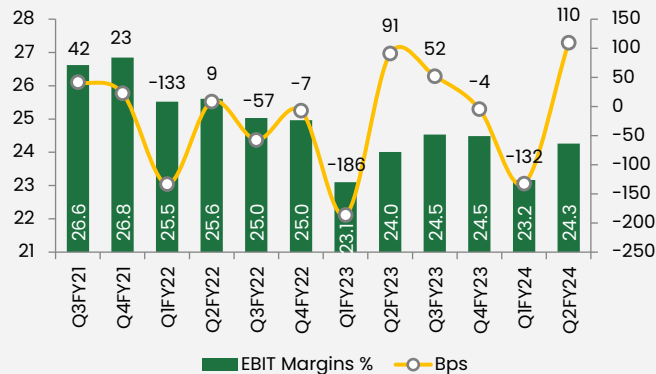


Source : RBL Research

EBIT grew by 5.3% QoQ and 9.1% YoY

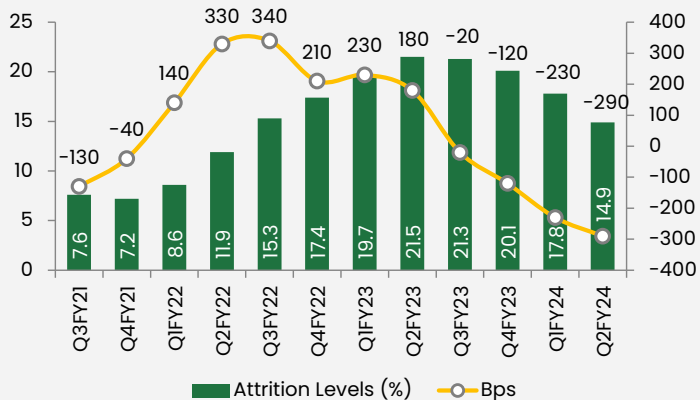


EBIT margin improved by 110bps QoQ and 25bps YoY

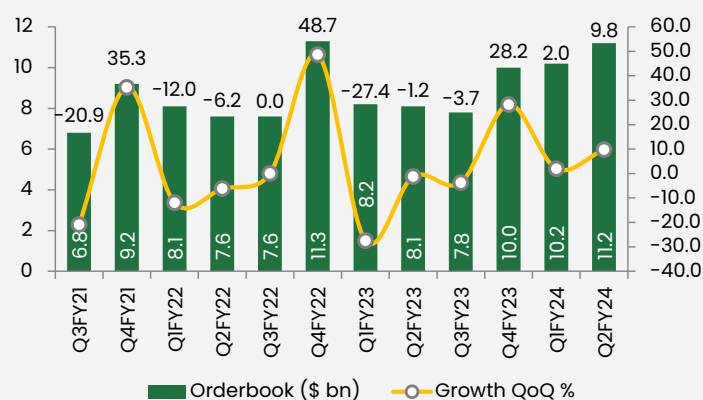


Source : RBL Research

Attrition further moderated to 14.9% in Q2FY24



Order Book was strong at USD 11.2bn, up by 9.8% QoQ



Source : RBL Research

P&L Account – consolidated

Particulars, Rs cr	FY22	FY23	FY24E	FY25E
Net Sales (\$ Mn)	25,707	27,927	32,412	38,249
Net sales	191,754	225,458	261,531	305,992
Employee cost	107,554	127,522	146,981	170,131
Advertisements cost	1,163	1,881	3,174	3,714
Other expenses	29,980	36,796	42,107	48,959
Total expenditure	138,697	166,198	192,262	222,804
EBITDA	53,057	59,260	69,270	83,188
EBITDAM (%)	27.7	26.3	26.5	27.2
Depreciation	4,604	5,023	5,231	5,324
EBIT	48,453	54,237	64,039	77,863
EBITM (%)	25.3	24.1	24.5	25.4
Other income	4,018	3,449	2,615	3,060
Interest expenses	784	779	779	779
PBT	51,687	56,907	65,875	80,144
Tax	13,238	14,604	16,864	20,517
PAT (after Exceptional)	38,449	42,303	49,011	59,627
PAT Margin %	20.1	18.8	18.7	19.5
EPS	105.1	115.6	133.9	162.9

Source : RBL Research

Balance Sheet – consolidated

Particulars, Rs cr	FY22	FY23	FY24E	FY25E
Share Capital	366	366	366	366
Reserves & Surplus	88,773	90,058	117,109	140,137
Total Shareholder's Fund	89,139	90,424	117,475	140,503
Minority Interest	707	782	782	782
Deferred tax liabilities	590	792	811	949
Other long term liabilities	8,727	8,095	9,154	10,710
Total	9,317	8,887	9,964	11,658
Current Liabilities				
Trade payables	8,045	10,515	11,823	13,413
Short term provisions	1,411	345	400	468
Other current liabilities	32,895	32,698	35,307	41,309
Total	42,351	43,558	47,530	55,190
Total liabilities	141,514	143,651	175,751	208,133
Application of Assets				
Net Block	19,511	18,657	19,013	19,376
Current work in process	1,205	1,234	1,234	1,234
Goodwill on consolidation	1,787	1,858	1,858	1,858
Non current investment	223	266	262	306
Deferred Tax assets	3,708	3,307	3,923	4,590
Long term loans and advances	311	173	201	235
Other non-current assets	6,459	7,886	9,154	10,710
Total	33,204	33,381	35,644	38,308
Current Assets				
Current investments	30,262	36,897	44,460	52,019
Inventories	20	28	27	32
Trade receivables	34,074	41,049	46,574	54,492
Cash balance	12,488	7,123	20,062	30,037
Bank balance	5,733	3,909	3,909	3,909
Short term loans and advances	6,445	1,325	1,537	1,798
Other current assets	19,288	19,939	23,538	27,539
Total	108,310	110,270	140,108	169,825
Total assets	141,514	143,651	175,751	208,133

Source : RBL Research

Cashflow – consolidated

Particulars, Rs cr	FY22	FY23	FY24E	FY25E
Profit before tax	51,687	56,907	65,875	80,144
Add: Depreciation	4,604	5,023	5,231	5,324
Add: Interest cost	784	779	779	779
Others	(204)	(313)	-	-
Operating profit before working capital changes	54,204	59,148	69,270	83,188
Changes in working capital	(2,769)	(4,217)	(6,198)	(5,087)
Cash from Operations	51,435	54,931	63,072	78,100
Less: Taxes	(11,486)	(12,966)	(16,864)	(20,517)
Cash flow from Operations	39,949	41,965	46,208	57,583
Net cash used in Investing				
Purchase of fixed assets	(2,995)	(3,100)	(5,586)	(5,687)
Purchase of investments	(5,519)	(7,056)	(7,559)	(7,603)
Sales of fixed assets	31	37	-	-
Dividend Income//Interest Rec.	2,704	3,093	2,615	3,060
Cash flow from investing	(897)	39	(10,530)	(10,230)
Cash flow from Financing				
Proceeds from Equity shares	(18,000)	(4,192)	-	-
Dividend (Incl dividend tax)	(13,317)	(41,347)	(21,960)	(36,600)
Interest cost	(698)	(779)	(779)	(779)
Others	(1,566)	(1,560)	-	-
Cash flow from Financing	(33,581)	(47,878)	(22,739)	(37,379)
Net cash Inflow/Outflow	5,471	(5,874)	12,939	9,974
Opening cash	6,858	12,488	7,123	20,062
Exchange gain/loss	159	509	-	-
Closing Cash	12,488	7,123	20,062	30,037

Source : RBL Research

Key ratios – consolidated

Particulars	FY22	FY23	FY24E	FY25E
Per share Data				
EPS (Rs)	105.1	115.6	133.9	162.9
Book value per share (Rs)	243.5	247.1	321.0	383.9
Dividend per share (Rs)	36.4	113.0	60.0	100.0
Dividend Yield (%)	34.6	97.7	44.8	61.4
Dividend Yield %	1.0	3.1	1.7	2.8
Profitability Ratios				
EBITDAM(%)	27.7	26.3	26.5	27.2
PBTM (%)	27.0	25.2	25.2	26.2
NPM (%)	20.1	18.8	18.7	19.5
RoE (%)	43.1	46.8	41.7	42.4
RoCE (%)	54.4	60.0	54.5	55.4
Efficiency Data				
Debt-Equity Ratio	0.0	0.0	0.0	0.0
Fixed Asset Ratio	0.1	0.1	0.1	0.1
Debtors (Days)	64.9	66.5	65.0	65.0
Inventory (Days)	0.0	0.0	0.0	0.0
Payable (Days)	15.3	17.0	16.5	16.0
WC (Days)	49.6	49.5	48.5	49.0
Valuation				
P/E (x)	34.4	31.2	27.0	22.2
P/BV	14.8	14.6	11.2	9.4
EV/EBITDA	24.7	22.2	18.8	15.5
EV/Sales	6.8	5.8	5.0	4.2

Source : RBL Research

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Statements on ownership and material conflicts of interest, compensation– Research Analyst (RA)

S. No.	Statement	Answer	
		Yes	No
		Tick appropriate	
		Yes	No
	I/we or any of my/our relative has any financial interest in the subject company? [If answer is yes, nature of Interest is given below this table]		No
	I/we or any of my/our relatives, have actual/beneficial ownership of one per cent. or more securities of the subject company, at the end of the month immediately preceding the date of publication of the research report or date of the public appearance?		No
	I / we or any of my/our relative, has any other material conflict of interest at the time of publication of the research report or at the time of public appearance?		No
	I/we have received any compensation from the subject company in the past twelve months?		No
	I/we have managed or co-managed public offering of securities for the subject company in the past twelve months?		No
	I/we have received any compensation for brokerage services from the subject company in the past twelve months?		No
	I/we have received any compensation for products or services other than brokerage services from the subject company in the past twelve months?		No
	I/we have received any compensation or other benefits from the subject company or third party in connection with the research report?		No
	I/we have served as an officer, director or employee of the subject company?		No
	I/we have been engaged in market making activity for the subject company?		No

[Please note that only in case of multiple RAs, if in the event answers differ inter-se between the RAs, then RA specific answer with respect to questions under F (a) to F(j) below, are given separately]

Nature of Interest (if answer to F (a) above is Yes :

.....

Name(s) with Signature(s) of RA(s).

[Please note that only in case of multiple RAs and if the answers differ inter-se between the RAs, then RA specific answer with respect to questions under F (a) to F(j) above , are given below]

SS.No.	Name(s) of RA.	Signatures of RA	Serial Question of question which the signing RA needs to make a separate declaration / answer	Yes	No.

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