



Tata Consultancy Services (TCS IN)

Marginal Miss; Maintain BUY

INDIA | IT SERVICES | Quarterly Update

TCS reported result growth below expectations

USD revenues at \$3.90bn declined by 0.8% QoQ – lower than street expectation of 0.8% QoQ growth. The revenue growth in constant currency terms was 1.6% - implying a cross-currency impact of 240bps. INR revenues at Rs242bn declined 1.1% QoQ. Volumes and realizations grew by 1.4% and 0.6% respectively.

Cross currency impacted significantly during the quarter and hence QoQ is not strictly comparable. Amongst verticals, weakness was mainly on account of telecom (down 9.7% QoQ) and Energy & Utilities (down 7.9% QoQ). BFSI declined by 0.5% QoQ (CC growth of 2.0% QoQ), while manufacturing and retail remained only major verticals to report positive growth. Among geographies UK and Continental Europe declined 2.0% and 5.9% QoQ respectively – primarily on the back of weak performance by Diligenta and CC impact. US reported muted growth of 0.2%. Among services, consulting declined by 15% QoQ, Asset leverage solutions declined by 4.9%. Growth was anemic in most other verticals.

EBITDA margins at 29.2% expanded by 40bps QoQ – better than expectations due to positive impact of realizations (60bps), better business mix (60bps) – partly offset by currency impact (~80bps). Other Income of Rs 11.2bn (FX gain of Rs8bn) led to recurring PAT of Rs 59bn (+8.5% QoQ) – better than our estimates of Rs54bn. The company paid a one-time bonus of Rs 26.3bn to its employees – adjusting for that, PAT was Rs 38.90bn (-29% QoQ).

Client Metrics showed improvement, with increase in number of US\$100mn (+4 QoQ to 29) and US\$50mn (+3 QoQ to 68). Utilizations declined by 120bps QoQ to 85.4%. Attrition stood at 13.8% – increase of 40bps QoQ.

Guidance and Commentary – The commentary hasn't changed much.

Management commentary continues to allude for strong growth ahead. Management confidence is based on its interaction with clients on budget. Client budgets are expected to increase for FY16 in CC terms, with broad theme of simplification, governance and digital to continue and improving discretionary spends. However, management declined to commit that the growth in FY16 will be 'better' than FY15.

As per the management, demand environment looks strong in Manufacturing and Retail. BFS seems good to grow in line with company average and insurance business (ex-Diligenta) has bottomed out. However, E&U and telecom are expected to remain weak and volatile (~12% of revenues). Geographically, US appear stable while growth in Europe remains strong. The company is seeing lot of opportunities in IMS and Digital space. The overall deal pipeline remains strong for the company, and the margins are expected to remain in their targeted band of 26-28%.

We maintain our positive stand on TCS and expect it to continue to deliver robust results on the back of –broad based service offerings and geographical reach, sustained investment in creating of new growth engines and leadership in digital. Concerns on the stock are pertaining more to 12% of revenues (Telecom, E&U) and we believe they are overdone. We have made minor revisions to our estimates, on the back of revenue miss in this quarter.

The stock is currently trading at 18x FY17 earnings – which we perceive as inadequate, in view of consistency premium that TCS should command, against turnaround stories of Infosys (16.5x FY17E earnings). We continue to value the company at 20x FY17 earnings. Our price target of Rs2800 represents +13% upside from current levels. We maintain BUY.

BUY

CMP RS 2475

TARGET RS 2800 (+13%)

COMPANY DATA

O/S SHARES (MN) :	1959
MARKET CAP (RSBN) :	5141
MARKET CAP (USDBN) :	82.4
52 - WK HI/LO (RS) :	2834 / 1970
LIQUIDITY 3M (USDMN) :	55
PAR VALUE (RS) :	1

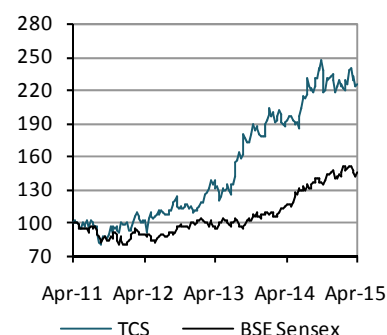
SHARE HOLDING PATTERN, %

PROMOTERS :	73.9
FII / NRI :	16.8
FI / MF :	4.7
NON PROMOTER CORP. HOLDINGS :	0.4
PUBLIC & OTHERS :	4.2

PRICE PERFORMANCE, %

	1MTH	3MTH	1YR
ABS	1.7	3.1	18.4
REL TO BSE	0.7	-2.2	-8.9

PRICE VS. SENSEX



Source: Phillip Capital India Research

KEY FINANCIALS

Rs mn	FY15	FY16E	FY17E
Net Sales	946.5	1,087.3	1,254.0
EBIDTA	246.7	299.3	331.9
Net Profit	196.5	241.6	272.1
EPS, Rs	100.3	123.4	138.9
PER, x	24.7	20.1	17.8
EV/EBIDTA, x	19.5	16.2	14.5
P/BV, x	9.1	7.3	6.0
ROE, %	36.8	36.5	33.7

Source: PhillipCapital India Research Est.

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Quarterly performance

Rs mn	4QFY14	1QFY15	2QFY15	3QFY15	4QFY15	4QFY15- Adj
US\$ revenues	3,503	3,694	3,929	3,931	3,900	3,900
QoQ growth %	1.9%	5.5%	6.4%	0.1%	-0.8%	-0.7%
Net sales	215,511	221,110	238,165	245,011	242,198	2,42,198
QoQ growth %	1.2%	2.6%	7.7%	2.9%	-1.1%	1.7%
YoY growth %	31%	23%	14%	15%	12%	14%
Cost of revenues	112,171	118,824	129,529	132,161	151,760	1,32,051
SGA & other exp	36,806	38,616	40,549	42,319	46,064	39,494
EBITDA	66,534	63,670	68,087	70,531	44,374	70,653
QoQ growth %	-0.5%	-4.3%	6.9%	3.6%	-37.1%	3.8%
YoY growth %	43%	24%	3%	5%	-33%	6%
Margins (%)	30.9%	28.8%	28.6%	28.8%	18.3%	29.2%
Depreciation	3,724	5,521	4,145	4,290	4,742	4,742
EBIT	62,810	58,149	63,942	66,241	39,632	65,911
Margins (%)	29.1%	26.3%	26.8%	27.0%	16.4%	27.2%
Other income	6,990	8,151	5,659	6,295	11,291	11,291
Pre-tax profit	69,800	66,300	69,601	72,536	50,923	77,202
Tax provided	16,313	15,312	16,045	17,453	12,018	17,754
Profit after tax	52,967	50,578	52,883	54,441	38,582	59,448
QoQ growth %	-0.3%	-4.5%	4.6%	2.9%	-29.1%	12.4%
YoY growth %	47%	33%	12%	2%	-27%	12%
Margins (%)	24.6%	22.9%	22.2%	22.2%	15.9%	24.5%
EPS, Rs	27.0	25.8	27.0	27.8	19.7	30.2

Operating metrics

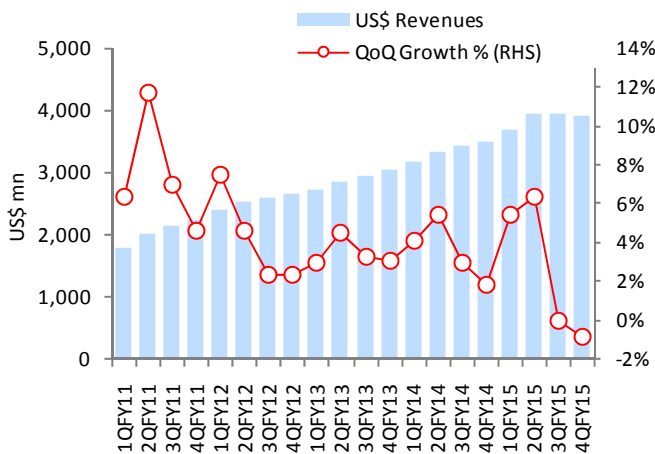
QoQ growth	4QFY14	1QFY15	2QFY15	3QFY15	4QFY15
Service Lines					
ADM	0.9%	4.9%	5.6%	-2.4%	0.7%
Engineering and Industrial Services	6.3%	-1.1%	8.7%	-2.1%	-0.8%
Infrastructure Services	1.9%	10.7%	16.5%	3.7%	0.6%
Ent Solutions + BI	1.9%	6.8%	4.4%	-1.2%	-0.8%
Global Consulting	1.9%	-0.8%	6.4%	15.7%	-14.2%
BPO	15.2%	1.4%	-2.1%	4.4%	-4.9%
Industry Verticals					
BFSI	2.4%	2.5%	3.0%	0.3%	-0.5%
Manufacturing	-0.4%	5.5%	24.9%	0.1%	0.2%
Telecom	-1.3%	6.6%	0.7%	0.1%	-9.7%
Life Sciences & Healthcare	5.3%	8.9%	6.4%	1.6%	3.9%
Retail & Distribution	-0.3%	7.8%	4.0%	-0.7%	0.7%
Transportation	1.9%	8.5%	3.4%	0.1%	-3.6%
Energy and Utilities	1.9%	8.2%	17.3%	-2.3%	-7.9%
Media & Entertainment	15.2%	9.5%	6.4%	0.1%	-0.8%
Hi-Tech	1.9%	9.4%	10.2%	3.6%	0.9%
Geographies					
US	0.9%	5.5%	3.9%	1.8%	0.2%
UK	3.6%	4.9%	2.8%	-5.8%	-2.0%
Rest of Europe	6.3%	4.6%	1.9%	1.8%	-5.9%
Europe	4.7%	4.7%	2.4%	-2.7%	-3.6%
India	0.3%	7.2%	9.7%	0.1%	0.7%
APAC	1.9%	8.3%	41.3%	-3.9%	0.2%
Ibero America	-2.5%	5.5%	-8.1%	10.6%	-0.8%
MEA	-2.7%	0.4%	1.0%	5.3%	4.2%

Changes in estimates

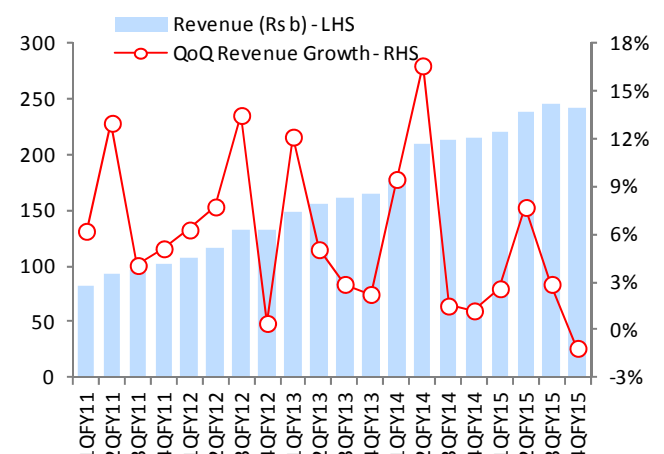
Rs bn	New		Old		Change	
	FY16E	FY17E	FY16E	FY17E	FY16E	FY17E
Rev (\$ mn)	17,536	20,225	17,575	20,359	-0.2%	-0.7%
Rev	1,087.3	1,254.0	1,089.7	1,262.3	-0.2%	-0.7%
EBITDA	299.3	331.9	294.9	337.0	1.5%	-1.5%
PAT	241.6	272.1	241.9	279.6	-0.1%	-2.7%
EPS (Rs)	123.4	138.9	123.5	142.8	-0.1%	-2.7%

Source: Company, PhillipCapital India Research

US\$ revenue and QoQ growth

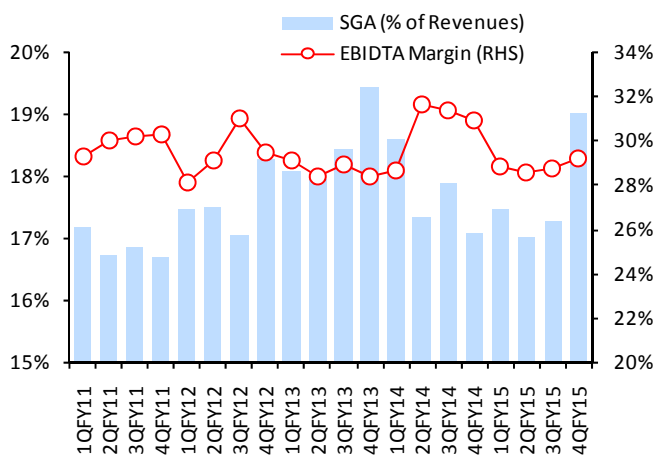


INR revenues and QoQ growth

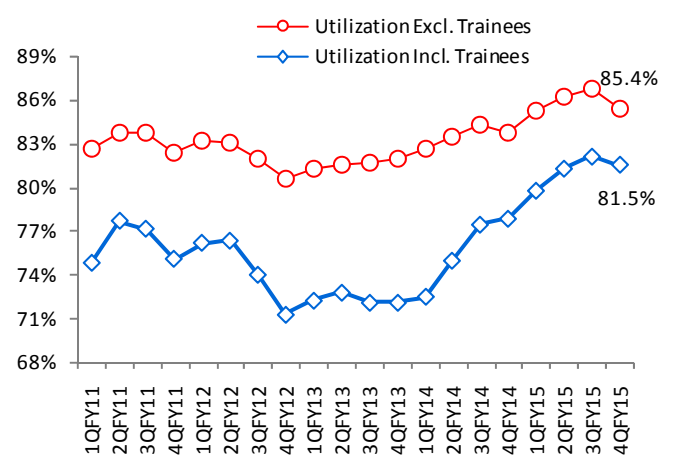


Source: Company, PhillipCapital India Research

SG&A spend and EBITDA margins

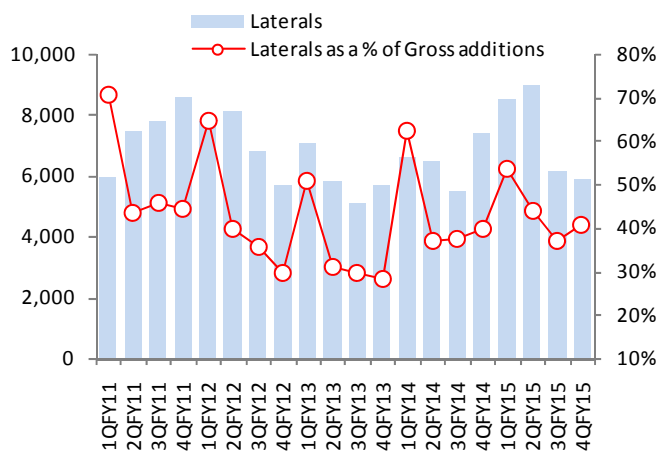


Utilizations

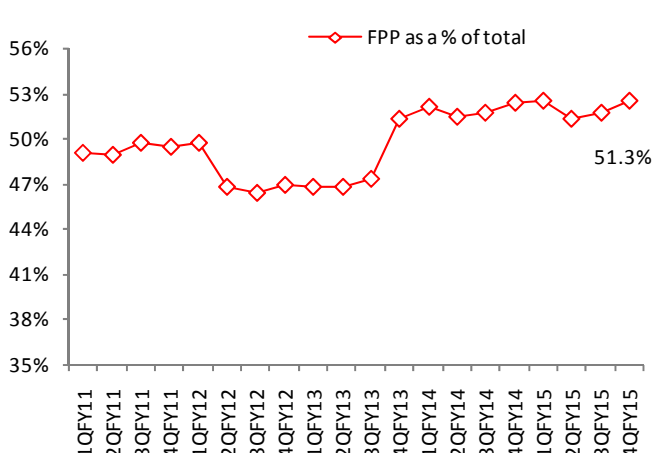


Source: Company, PhillipCapital India Research (4QFY15 margins adjusted for non-recurring expense)

Laterals added as a % of gross



FPP contribution



Source: Company, PhillipCapital India Research

Financials

Income Statement

Y/E Mar, Rs mn	FY14	FY15	FY16E	FY17E
Net sales	818,094	946,484	1,087,258	1,253,966
Growth, %	29.9	15.7	14.9	15.3
Employee expenses	-422,065	-532,274	-589,042	-694,761
Other Operating expenses	-144,707	-167,548	-198,917	-227,334
EBITDA (Core)	251,322	246,662	299,299	331,871
Growth, %	39.0	(1.9)	21.3	10.9
Margin, %	30.7	26.1	27.5	26.5
Depreciation	-13,243	-18,698	-20,477	-22,716
EBIT	238,079	227,964	278,822	309,155
Growth, %	40.0	(4.2)	22.3	10.9
Margin, %	29.1	24.1	25.6	24.7
Interest paid	0	0	0	0
Other Non-Operating Inc	15,809	31,396	35,976	45,925
Pre-tax profit	253,888	259,360	315,467	355,078
Tax provided	-60,712	-60,828	-72,557	-81,668
Profit after tax	193,176	198,532	242,910	273,410
Others (Minorities, Assocs)	-2,089	-2,048	-1,292	-1,357
Net Profit	191,087	196,484	241,618	272,053
Growth, %	37.1	2.8	23.0	12.6
Net Profit (adjusted)	191,087	196,484	241,618	272,053
Wtd avg shares (m)	1,959	1,959	1,959	1,959

	FY14	FY15	FY16E	FY17E
US\$ Revenue (\$ mn)	13,443	15,454	17,536	20,225
Growth, %	16.2	15.0	13.5	15.3
Re / US\$ (rate)	60.9	61.2	62.0	62.0

Balance Sheet

Y/E Mar, Rs mn	FY14	FY15	FY16E	FY17E
Cash & bank	14,688	27,033	15,180	43,801
Marketable securities at cost	0	0	0	0
Debtors	182,304	199,067	237,632	274,733
Inventory	0	0	0	0
Other current assets	221,122	236,226	290,786	336,187
Total current assets	418,114	462,326	543,599	654,721
Investments	34,489	6,847	29,347	59,347
Net fixed assets	236,522	245,295	280,840	318,708
Non-current assets	0	0	0	0
Total assets	689,125	714,467	853,785	1,032,776
Total current liabilities	110,751	150,834	157,436	186,857
Non-current liabilities	18,117	20,640	23,519	26,993
Total liabilities	128,868	171,474	180,955	213,851
Paid-up capital	1,957	1,957	1,957	1,957
Reserves & surplus	551,395	531,761	660,306	805,044
Minorities	6,905	9,275	10,567	11,924
Shareholders' equity	560,257	542,993	672,831	818,925
Total equity & liabilities	689,125	714,467	853,785	1,032,776

Source: Company, PhillipCapital India Research Estimates

Cash Flow

Y/E Mar, Rs mn	FY14	FY15	FY16E	FY17E
Pre-tax profit	253,888	259,360	315,467	355,078
Depreciation	13,243	18,698	20,477	22,716
Chg in working capital	-91,200	10,749	-83,646	-49,606
Total tax paid	-60,712	-60,828	-72,557	-81,668
Other operating activities	0	0	0	0
Cash flow from operating activities	115,219	227,979	179,741	246,520
Capital expenditure	-54,800	-27,471	-56,022	-60,584
Chg in investments	-14,086	27,642	-22,500	-30,000
Chg in marketable securities	0	0	0	0
Other investing activities	0	0	0	0
Cash flow from investing activities	-68,886	171	-78,522	-90,584
Free cash flow	60,419	200,508	123,719	185,936
Equity raised/(repaid)	0	0	0	0
Debt raised/(repaid)	-1,037	-9	0	0
Dividend (incl. tax)	-73,328	-181,042	-113,072	-127,316
Other financing activities	26,033	-35,076	0	0
Cash flow from financing activities	-50,077	-215,805	-113,072	-127,316
Net chg in cash	-3,744	12,345	-11,853	28,620

Valuation Ratios

	FY14	FY15	FY16E	FY17E
Per Share data				
EPS (INR)	97.6	100.3	123.4	138.9
Growth, %	37.0	2.8	23.0	12.6
Book NAV/share (INR)	282.5	272.5	338.1	412.0
CFPS (INR)	50.8	100.4	73.4	102.4
DPS (INR)	32.0	79.0	49.3	55.6
Return ratios				
Return on assets (%)	31.9	28.3	31.0	29.0
Return on equity (%)	34.5	36.8	36.5	33.7
Return on capital employed (%)	38.2	34.8	38.6	35.5
Turnover ratios				
Asset turnover (x)	1.8	1.9	1.9	1.9
Sales/Total assets (x)	1.4	1.3	1.4	1.3
Sales/Net FA (x)	3.8	3.9	4.1	4.2
Working capital/Sales (x)	0.4	0.3	0.3	0.3
Receivable days	81.3	76.8	79.8	80.0
Liquidity ratios				
Current ratio (x)	3.8	3.1	3.5	3.5
Quick ratio (x)	3.8	3.1	3.5	3.5
Dividend cover (x)	3.0	1.3	2.5	2.5
Total debt/Equity (%)	0.2	0.2	0.2	0.2
Net debt/Equity (%)	(8.7)	(6.1)	(6.5)	(12.6)
Valuation				
PER (x)	25.4	24.7	20.1	17.8
PEG (x) - y-o-y growth	0.7	8.7	0.9	1.4
Price/Book (x)	8.8	9.1	7.3	6.0
Yield (%)	1.3	3.2	2.0	2.2
EV/Net sales (x)	5.9	5.1	4.4	3.8
EV/EBITDA (x)	19.2	19.5	16.2	14.5
EV/EBIT (x)	20.3	21.2	17.3	15.5

Management

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