



ALPHA

29 OCT 2022

TCS Ltd. – Pioneer of IT Sector

Market Data

CMP	Rs. 3161
Date	28-Oct-22
New Target Price	Rs. 3680
Old Target Price	Rs. 4140
Upside Potential	16.00%
52 Week High/Low	4043/2926
Market Cap	Large Cap
NSE Code	TCS
Sector	IT
Rating	ACCUMULATE

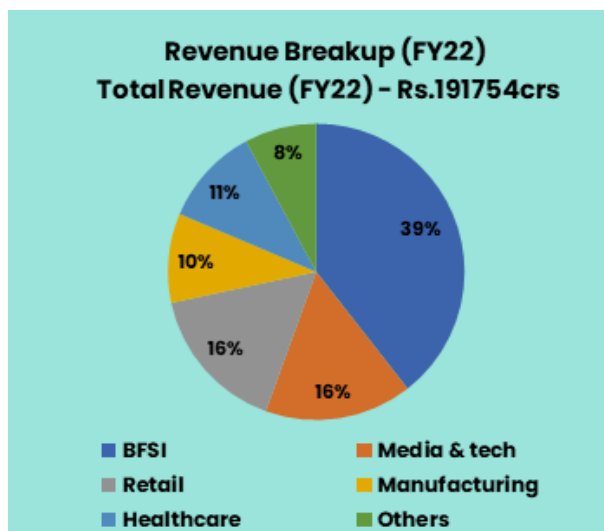
Established in 1968 as a division of Tata Sons, Tata Consultancy Services (TCS) Limited is currently the largest Indian IT services company. The company pioneered the concept of offshore IT services in 1974 and emerged as an integrated full-service provider with a global footprint. TCS is a part of the Tata Group, with Tata Sons holding a 72.3% equity share (as on March 31, 2022) in the company. A part of the Tata group, India's largest multinational business group, TCS has over 592,000 of the world's best-trained consultants in 55 countries. The workforce continues to be very diverse, comprising 157 nationalities and with women making up 35.7% of the base. The company serves to some of the biggest conglomerates in the world like Google, Amazon, Azure, openstack, Adobe, Intel, Bosch, IBM, Apple, Oracle, Symantec, etc.



Products & Services: TCS offers a rich portfolio of services, which includes consulting and service integration, digital transformation services and cognitive business operations. Based on industry classification, the company has five key verticals: a.) banking, financial services and insurance (BFSI); b.) retail and consumer business; c.) communication, media and technology; d.) manufacturing; and e.) other businesses. The last category includes life sciences and healthcare, technology and services, energy, resources and utilities, and others.

SHP	Sep - 22 (%)	Jun - 22 (%)	Change
Promoters	72.30	72.30	0.00
FPI	13.05	13.50	-0.45
DII	8.58	8.36	0.22
Public & Others	6.06	5.85	0.21
Pledged	0.48	0.48	0.00

Subsidiaries: The Company has 52 subsidiaries as on March 31, 2022. There are no associates or joint venture companies.



Margins - FY22	
EBITDA	28%
EBIT	25%
PAT	20%



Key Rationale

- **Diversified Clientele** – The company's ability to offer full-service capability has helped it win deals across a wide spectrum of verticals. The company has strong domain expertise and contextual knowledge and has demonstrated its ability to structure and execute large-scale projects globally. This has differentiated it in the marketplace, enabling it to continually gain market share over its competitors. TCS' significant organic investments in manpower training and developing capabilities have also given it a competitive edge, and helped it capture many transformational digital deals. The company has a large, diversified, and growing client base with meaningful incremental addition of clients in the above \$20-million, \$50-million and \$100-million buckets in recent fiscals, including FY2022.
- **Deal Wins** – On a reported basis, TCV for the Q2FY23 was at US\$8.1 bn, which was largely constant for two consecutive quarters (it reported US\$8.2 bn TCV in Q1FY23). The company continued to maintain that steady state deal win number for the quarter could be in the range of US\$7-9 bn in the foreseeable future. There were multiple large deals wins for the digital transformation of operations in data center and network, digital workspace, and customer experience. TCS's deep domain and contextual knowledge coupled with differentiated value propositions underpinned by MFDM, ignio and Cognix are helping capture opportunities. TCS also indicated that the deal win number was also impacted by currency movement.
- **Q2FY23** – The company's revenues stood at Rs.55,309 crs, up 18% YoY. It reported EBIT at Rs.13,279 crs with EBIT Margin at 24% (expanded 80bpsQoQ). This was on account of superior execution by the company and lower operating costs during the quarter. Life Sciences & Healthcare grew by 14.5% YoY, BFSI by 13.1% YoY, Manufacturing by 14.5% YoY and Technological Services by 15.9% YoY. Furthermore, Communication & Media grew by 18.7% YoY and Regional Markets & Others, too, improved by 13.1% YoY. The company added 9,840 net associates in Q2, taking the total to 616,171. TCS also indicated that it hired around 20,000 freshers in Q2. The company's Net profit crossed Rs.10,000 crs mark for the first time in Q2FY23.
- **Financial Performance** – The company's financial profile remains robust as reflected in its high operating profitability at 28% in FY22, High ROE & ROCE of 43% & 54% in the same period, strong capital structure, Zero Debt to Equity, recurring operating cash flows and robust liquidity position in the form of a strong cash and investment balance of Rs.50,468 crs as on Sept 30, 2022. The five-year average ROE and ROCE stands at 37% and 48% for the period of FY18-22.

**Ratios - FY22**

ROE	43%
ROCE	54%
Div. Yield	1.35%
PE Ratio	30.00
Face Value	1.00
EPS	Rs. 104.75

Industry Analysis

The IT & BPM sector has become one of the most significant growth catalysts for the Indian economy, contributing significantly to the country's GDP and public welfare. The IT industry accounted for 8% of India's GDP in 2020, and it is expected to contribute 10% to India's GDP by 2025. India is the leading sourcing destination across the world, accounting for approximately 55% market share of the US\$ 200-250 billion global services sourcing business in 2019-20. The Indian IT industry's revenue touched US\$ 227 billion in FY22, a 15.5% YoY growth. In FY21, the Indian IT sector exported goods worth US\$ 149 billion. The largest contributor, accounting for more than 51% of all IT exports, has been the export of IT services (including hardware). The IT industry added 4.45 lakh new employees in FY22, bringing the total employment in the sector to 50 lakh employees.

Growth Drivers

New IT-based technologies such as Tele-medicine, remote monitoring, etc. are expanding and boosting the demand in the digital economy. The roll out of fifth-generation (5G) communication technology, growing adoption of artificial intelligence, Big Data analytics, cloud computing and the Internet of Things (IoT) will further expand the size of the IT industry in India.

The government introduced the STP Scheme, which is a 100% export-oriented scheme for the development and export of computer software, including export of professional services.

The computer software and hardware sector in India attracted cumulative foreign direct investment (FDI) inflows worth US\$ 85.51 billion between April 2000-March 2022.



Peer Analysis

Competitors: Infosys, Wipro, HCL tech., etc.

TCS being the largest IT company in India has the robust and best return ratios when compared to its peers. Though the P/E is trading slightly premium than the industry P/E and little high among its closest peers, the fundamentals of the stock is extremely great backed by a strong balance sheet.

Company	CMP	Mcap.	ROE	ROCE	P/E	EPS
TCS	3161	1157340	43.00%	54.00%	30	104.75
Wipro	383	210320	19.00%	19.00%	17	22.31
Infosys	1513	637040	29.00%	38.00%	29	52.56

Outlook

The management indicated that it expects a margin improvement, going forward. Some margin tailwinds are i) rupee depreciation, ii) pricing increase, iii) utilisation improvement (as fresher hiring is likely come down), iv) moderation of subcontractor costs, which is likely to get mitigated by the normalisation of travel expenses and facility expenses. Regarding hiring, TCS indicated that it has hired 35,000 freshers in H1FY23 (15,000 in Q1 and 20,000 in Q2) and maintained guidance of 40,000 fresher additions in FY23, which implies that pace of fresher additions is likely to come down in H2. It has also indicated that 70% of employees have been paid 100% variable payout while rest 30% of employees would be paid on the basis of performance. It also indicated that demand for the US market continued to robust, which is a function of continued strong deal execution and the near-term outlook also looks strong with healthy TCV of US\$2 bn+ for the market. The management is watchful of the emerging situation and remains optimistic about the opportunities in the company's core markets and verticals. TCS is well-positioned and operating diligently to participate aggressively in the identified opportunities.



Valuation

From a long-term perspective, we believe TCS has built a resilient business model by securing multiple long-term contracts with the world's leading brands. Given TCS size, order book and exposure to long duration orders and portfolio, it is well positioned to withstand the weakening macro environment and ride on the anticipated industry growth. Hence, we recommend an ACCUMULATE rating in the stock with the target price (TP) of Rs.3680, 28x FY24E EPS.

Risks

- **Client Concentration Risk** – Company has a large concentration of revenues, primarily in the BFSI (almost one-third of revenues) segment, although the same is mitigated by its established relationship with clients as well as deep domain knowledge.
- **Forex risk** – Rupee appreciation and/or any adverse cross-currency movements will impact the growth of the company since 50% of the sales are generated from US.
- **Cost Related Risk** – Rising attrition levels coupled with rising travel costs as well as subcontracting costs remain key concerns for the company. The discretionary spend cuts may arise due to economic uncertainties in the USA and Europe.

Source – Tickertape, Company's Website, BSE Website.

Thanks & Regards

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