

# Stock Update

Stable performance, strong deal wins continue

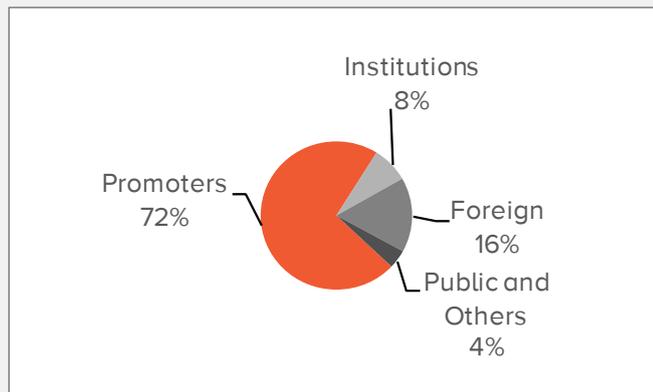
## Tata Consultancy Services

Reco: Buy | CMP: Rs1,888

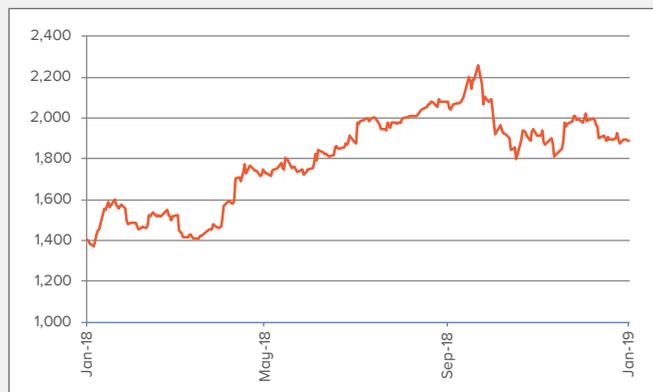
### Company details

Price target:	Rs2,400
Market cap:	Rs708,507 cr
52-week high/low:	Rs2,273/1,348
NSE volume: (No of shares)	27.6 lakh
BSE code:	532540
NSE code:	TCS
Sharekhan code:	TCS
Free float: (No of shares)	104.9 cr

### Shareholding pattern



### Price chart



### Price performance

(%)	1m	3m	6m	12m
Absolute	-5.4	-9.6	0.6	41.4
Relative to Sensex	-6.9	-14.6	-0.7	32.8

### Key points

- In-line revenue, margins missed the mark:** Tata Consultancy Services (TCS) delivered in-line revenue performance during Q3FY2019E, while operating margins missed our estimates. Despite a seasonally weak quarter, TCS delivered constant currency (CC) revenue growth of 1.8% q-o-q and 12.1% y-o-y (highest in the past 14 quarters). The double-digit y-o-y revenue growth was driven by BFSI (8.6% CC), retail and CPG (10.5% CC), communication and media (10.8% CC) and regional markets (22.6% CC). Digital revenue continued to grow strongly at 52.7% y-o-y. On a reported basis, USD revenue increased by 0.7% q-o-q to \$5,250 million, below our estimates, owing to higher-than-expected 110 BPS q-o-q cross-currency headwinds. EBIT margin declined by 90 BPS q-o-q to 25.6% (below our estimates), owing to increased cost of doing business (subcontractor cost increased by 60 BPS q-o-q), employee expenses (net addition of 6,827 employees during the quarter) and currency headwinds (50 BPS q-o-q). Lower profitability was offset by higher-than-expected other income (93.4% q-o-q), which resulted in 2.6% q-o-q growth in net profit during the quarter.
- Digital growth acceleration continues, growth accelerated in key markets and verticals:** Digital revenue growth remained strong at 52.7% y-o-y in Q3FY2019 compared to 60% y-o-y in Q1FY2019. Digital business contributed 31% to the total revenue (vs. 28% in Q2FY2019) in Q3FY2019. However, revenue from the core business declined by 2.3% q-o-q in Q3FY2019. Region wise, U.K. and continental Europe led the revenue growth in Q3FY2019, with CC revenue growth of 25.1% y-o-y and 17.6% y-o-y, respectively. APAC growth was at 12.6% y-o-y on CC terms during the quarter. North America grew by 8.2% y-o-y on CC terms on account of strong growth in BFSI. BFSI CC revenue growth accelerated to 8.6% y-o-y (versus 6.1% y-o-y and 4.1% y-o-y in Q2FY2019 and Q1FY2019, respectively) on account of strong growth from North America and insurance. Retail and CPG, energy and utilities (18.1% y-o-y CC) and life sciences and healthcare (15.7% y-o-y CC)

continued to drive revenue growth during the quarter. Communication and media CC revenue growth bounced back to 10.8% y-o-y. Client addition metrics remained solid, with addition of one new client in \$100 million+ revenue bracket during the quarter. Net headcount addition was 27,049 on a y-o-y basis to meet the increasing demand, while the attrition rate remained at 11.2% LTM (industry-leading retention).

♦ **Demand commentary remains strong:**

Management remains confident of delivering double-digit revenue growth in FY2019 on account of strong revenue growth in 9MFY2019, increasing IT spending in BFSI, retail along with markets such as Europe and robust deal wins in Q3FY2019. Total contract value (TCVs) of large deals increased by 20.4% q-o-q to \$5.9 billion during the quarter. Strong execution capability along with strong deal closures in CY2018 and healthy deal pipeline would help TCS to maintain the revenue growth momentum in the medium term. Further, management highlighted that major verticals (except technology, manufacturing and communication) that constitute 70-80% of total revenue are in a strong growth trajectory. TCS sees huge opportunity in the BFSI vertical especially in North America and Europe in areas of cloud migration, micro services, payments, trading platforms and blockchain technologies. As spending is moving

away from front-end to back-end, TCS expects a good demand environment in the retail vertical to continue going forward (though certain blips may happen owing to increasing bankruptcies in the U.S.). However, there would be pressure on margins across the industry owing to increased cost of doing business because of talent crunch and higher local hiring. We believe it would be transient in nature for TCS as it would rationalise the cost structure in the medium term given its execution capability and ability in taking price hike.

♦ **Valuation: Maintain Buy with a PT of Rs. 2,400:**

We have fine-tuned our earnings estimates for FY2019E/FY2020E/FY2021E on account of margin miss during the quarter. However, we remain positive on the revenue growth momentum of TCS in FY2020E, given acceleration in deal wins with increasing TCVs (driven by BFSI deal wins), strong digital growth (>50% y-o-y in the past two quarters) and acceleration in BFSI (management cited double-digit exit growth rate). At the CMP, the stock is trading at 20x its FY2020E EPS, which commands an industry-leading PE multiple, given its superior digital execution capabilities and increasing market share among large peers. Therefore, we maintain our Buy rating on the stock with a price target (PT) of Rs. 2,400.

**Valuation**

Particulars	Rs cr			
	FY18	FY19E	FY20E	FY21E
Total revenue	1,23,104.0	1,46,787.6	1,63,581.7	1,77,357.2
EBIT margin (%)	24.8	26.0	26.3	26.3
Net profit	25,826.0	31,545.0	34,888.7	37,898.8
EPS (Rs.)	68.8	84.1	93.0	101.0
P/E (x)	27.4	22.5	20.3	18.7
EV/EBITDA	11.0	8.7	7.7	7.1
RoE (%)	29.5	34.2	34.0	34.4
RoCE (%)	37.6	43.8	44.0	44.6

Results					Rs cr	
Particulars	Q3FY19	Q3FY18	Q2FY19	YoY (%)	QoQ (%)	
Revenue (\$ mn)	5,250.0	4,787.0	5,215.0	9.7	0.7	
Revenue in INR (cr)	37,338.0	30,904.0	36,854.0	20.8	1.3	
Direct costs	21,320.0	17,461.0	20,795.0	22.1	2.5	
<b>Gross profit</b>	<b>16,018.0</b>	<b>13,443.0</b>	<b>16,059.0</b>	<b>19.2</b>	<b>-0.3</b>	
SG&A	5,935.0	5,155.0	5,781.0	15.1	2.7	
<b>EBITDA</b>	<b>10,083.0</b>	<b>8,288.0</b>	<b>10,278.0</b>	<b>21.7</b>	<b>-1.9</b>	
Depreciation	519.0	507.0	507.0	2.4	2.4	
<b>EBIT</b>	<b>9,564.0</b>	<b>7,781.0</b>	<b>9,771.0</b>	<b>22.9</b>	<b>-2.1</b>	
Other income	1,147.0	864.0	593.0	32.8	93.4	
PBT	10,711.0	8,645.0	10,364.0	23.9	3.3	
Tax provision	2,590.0	2,100.0	2,437.0	23.3	6.3	
<b>Net profit</b>	<b>8,121.0</b>	<b>6,545.0</b>	<b>7,927.0</b>	<b>24.1</b>	<b>2.4</b>	
Minority interest	16.0	14.0	26.0	14.3	-38.5	
<b>Adj. Net Profit</b>	<b>8,105.0</b>	<b>6,531.0</b>	<b>7,901.0</b>	<b>24.1</b>	<b>2.6</b>	
<b>EPS (Rs)</b>	<b>21.6</b>	<b>17.4</b>	<b>21.1</b>	<b>24.1</b>	<b>2.6</b>	
<b>Margin (%)</b>				<b>BPS</b>	<b>BPS</b>	
EBITDA	27.0	26.8	27.9	19	-88	
EBIT	25.6	25.2	26.5	44	-90	
NPM	21.7	21.1	21.4	57	27	

## Operating metrics

Particulars	Revenue	Contribution	\$ Growth (%)		CC growth (%)
	(\$ mn)	(%)	q-o-q	y-o-y	y-o-y
Revenue (\$ mn)	5,250	100	0.7	9.7	12.1
<b>Geographic mix</b>					
North America	2,688	51.2	0.9	8.0	8.2
Latin America	105	2.0	0.7	-0.3	7.6
U.K.	814	15.5	0.0	20.6	25.1
Continental Europe	740	14.1	1.4	14.5	17.6
India	299	5.7	2.5	-0.8	9.7
APAC	494	9.4	-1.4	8.5	12.6
MEA	110	2.1	0.7	-4.0	-3.3
<b>Industry verticals</b>					
BFSI	1,617	30.8	-0.6	6.9	8.6
Retail & CPG	866	16.5	0.1	8.4	10.5
Communication & media	362	6.9	0.7	6.6	10.8
Manufacturing	378	7.2	0.7	5.3	6.7
Energy & utilities	247	4.7	2.9	14.5	18.1
Technology & services	399	7.6	0.7	5.5	5.8
Regional markets and others	982	18.7	2.3	17.9	22.6
<b>Service offerings</b>					
Digital	1,580	30.1	8.2	49.4	52.7
Core	3,670	69.9	-2.3	-1.6	NA

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