

**Cautious Outlook !!**

14<sup>th</sup> July, 2017

**CMP:** Rs.2,446  
**Target Price:** Rs.2,416  
**Recommendation:** **NETURAL**

**Stock Info**

BSE Group	A
BSE Code	532540
NSE Symbol	TCS
Bloomberg	TCS.IN
Reuters	TCS.BO
BSE Sensex	32,099
NSE Nifty	9,891

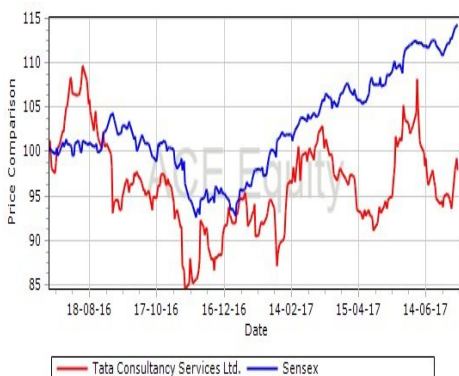
**Market Info**

Market Capital	Rs.477,027cr
Equity Capital	Rs.191.0cr
Avg. Trading Vol.	12,87,374
52 Wk High/ Low	2744/2051
Face Value	Rs.1

**Shareholding Pattern (%) Mar ( 2017)**

Promoters	73.3
Domestic Institutions	5.4
Foreign Institutions	17.0
Public & Others	4.3

**Price VS Sensex Chart**



- Strong volume growth of 3.5% qoq but a decline in earnings of 10% qoq:**  
TCS has delivered a strong topline performance with 3.5% qoq volume growth, driven by sustained traction in the Digital service offerings. The growth in focus geographies was encouraging across verticals with a cautiously optimistic approach towards Insurance and Retail. Focus shifted to profitability given the declining operating leverage, appreciating INR and compulsive commitments towards onsite hiring, digital skill training and sales with contextual expertise.
- Strong segmental commentary:**  
TCS has restructured its business in Emerging Markets (India, ME, APAC ex-Australia) that were more volatile owing to project-based nature of delivery, product-platform sales and inconsistency in business opportunities. This collective base accounts for ~17.6% of total revenues as of Q1FY18 and is termed as 'Regional Markets & Others'. The company reported 2.3% qoq growth in BFSI, driven by a platform win in Insurance and a Core Banking win in USA. The traction in BFSI is improving and is also reflected in healthy pipeline for Diligenta business. Retail revenues grew 2% qoq and saw some very encouraging deal engagements. The remaining segments grew in the range of 4-7% qoq and are showing sustained promise. The only dampener would be the performance of low focus 'Regional Markets & Others' segment.
- Operating margins:**  
EBIT margin at 23.4% declined ~240bps qoq, impacted by wage revision (~150bps) and adverse currency movements. Management maintains its medium term target EBIT margin range of 26-28% though outside currency fluctuations.
- Highlights of conference call:**

  - Management commentary was mixed on Banking and Financial Services (BFS) vertical stating that diverse spending trends across clients constrains secular visibility . While revenues from Retail rebounded with 2% qoq growth in CC terms (V/s decline of 4.4% qoq in Mar'17 quarter), the management remains cautious on its prospects given the challenges clients are facing.
  - Digital business revenues accounted for ~18.9% of overall revenues (up 7.6% qoq /26% yoy in CC terms). Management indicated that Digital deal sizes are progressively increasing citing an IoT & Analytics multi-year deal worth US\$50mn.
  - Headcount at 3,85,809 people declined by 1414 sequentially. TCS has reported a sequential decline in headcount for the first time since Jun'09 quarter.
  - Management has restructured its service practices to bring in new edge services under a new horizontal group named 'Business and Technology Services Group (BTS)'. Within BTS, the company has 3 groups, namely (1) Digital Transformation Services Group, (2) Cognitive Business Operations and (3) Consulting & Service Systems Integration. Management believes this reorganization will enhance focus and delivery capabilities while keeping stability in other customer-facing organization.
- Outlook:**  
The outlook on the business growth has been largely kept intact with strong growth in Digital business and improved business metrics on the segment - size, scale, and competitiveness. Taking into account the risk to growth estimates and likely impact on profitability, we have a **NETURAL** rating on the stock with TP of Rs 2416 based on P/E of 16x FY19E EPS of Rs 151.



Financials:

Y/E March (Rs. In Crore)	FY17	FY18E	FY19E
Net Revenue	117966	127403	136322
Growth %	9%	8%	7%
EBIDTA	32311	33125	35775
EBIDTA Margin	27.4%	26%	26%
Net Profit	26357	26658	28790
Growth %	9%	1%	8%
EPS	134	140	151
P/E	16.9	16.2	15.0
ROE	30.6	27.0	25.3

Quarterly Results:

Particulars (Rs. Cr)	Q1 FY18	Q4FY17	QoQ%	Q1FY17	YoY%
Information technology and consultancy services	29584	29642	-0.2%	29305	1.0%
Total Income	29584	29642	-0.2%	29305	1.0%
Employee cost	16183	15692	3.1%	15374	5.3%
Gross Profit	13401	13950	-3.9%	13931	-3.8%
Gross Margin%	45.3%	47.1%	-3.7%	47.5%	-4.7%
Other expenses	5988	5818	2.9%	6094	-1.7%
EBITDA	7413	8132	-8.8%	7837	-5.4%
EBITDA Margin	25.1%	27.4%	-8.7%	26.7%	-6.3%
Depreciation	499	505	-1.2%	490	1.8%
EBIT	6914	7627	-9.3%	7347	-5.9%
EBIT Margin	23.37%	25.73%	-9.2%	25.07%	-6.8%
Interest	27	8	237.5%	12	125.0%
Other Income	959	997	-3.8%	975	-1.6%
PBT	7846	8616	-8.9%	8310	-5.6%
Tax paid	1896	1994	-4.9%	1992	-4.8%
Effective tax rate%	24%	23%	4.4%	24%	0.8%
Net Profit	5950	6622	-10.1%	6318	-5.8%
EPS	30.40	33.61	-9.5%	32.06	-5.2%

Source: Company data, Arihant Research



**Profit and Loss statement**

Particulars (Rs. In Crore)	FY17	FY18E	FY19E
Information technology services	117966	127403	137596
<b>Total</b>	<b>117966</b>	<b>127403</b>	<b>136322</b>
Employee costs	61621	63702	68798
Operation and other expenses	24034	30577	33023
Total Operating Expenses	85655	94278	101821
<b>EBIDTA</b>	<b>32311</b>	<b>33125</b>	<b>35775</b>
EBIDTA Margin	27.4%	26.0%	26.0%
Depreciation	1987	2293	2477
EBIT	30324	30832	33298
Interest	32	33	36
Other Income	4221	3822	4128
<b>PBT</b>	<b>34513</b>	<b>34621</b>	<b>37390</b>
Tax	8156	7963	8600
<b>PAT</b>	<b>26357</b>	<b>26658</b>	<b>28790</b>
Growth (%)	8.5%	1.1%	8.0%
<b>EPS</b>	<b>134</b>	<b>140</b>	<b>151</b>

**Cash Flow Statement**

Particulars (Rs. In Crore)	FY17	FY18E	FY19E
<b>Profit After taxes</b>	<b>26357</b>	<b>26658</b>	<b>28790</b>
Add:- Depreciation	1987	2293	2477
Change in Working Capital	4825	3860	3088
Cash generated from operations	33169	32811	34355
Taxes paid	-7946	-7963	-8600
Net cash flow from operating activities	25223	24848	25755
Purchase of fixed assets	-1989	-2586	-3361
Others	-14743	-16217	-17839
Net cash flow from investing activities	-16732	-18803	-21200
<b>Dividend paid, including dividend tax</b>	<b>-10947</b>	<b>-14000</b>	<b>-14000</b>
Other	-79	-76	-76
<b>Net cash used in financing activities</b>	<b>-11026</b>	<b>-14076</b>	<b>-14076</b>
Net Cash Flow	-2535	-68	-921
<b>Opening Cash balance</b>	<b>6295</b>	<b>3760</b>	<b>3692</b>
Exchange Difference on transaction of Foreign Currency	-163	-163	-163
<b>Closing Cash balance</b>	<b>3597</b>	<b>3692</b>	<b>2771</b>

**Balance Sheet**

Particulars (Rs. In Crore)	FY17	FY18E	FY19E
Shareholder's funds			
Share Capital	197	191	191
Reserves & Surplus	86017	98675	113465
<b>Total</b>	<b>86214</b>	<b>98866</b>	<b>113656</b>
Minority Interest	366	350	350
Total Non Current Liabilities	2160	2477	2773
Total Current Liabilities	14512	18785	21595
<b>Total Liabilities</b>	<b>103252</b>	<b>120478</b>	<b>138374</b>
Net Block	10057	13330	13760
Capital Work-in-Progress	1541	4943	5683
Goodwill on consolidation	1597	1977	2273
Total Non Current Assets	22726	24133	25477
Cash and bank balance	3597	3692	2771
Total Current Assets	80526	96345	112897
<b>Total Assets</b>	<b>103252</b>	<b>120478</b>	<b>138374</b>

**Key Ratios**

Particulars	FY17	FY18E	FY19E
EPS	133.8	139.6	150.7
Book Value	440.5	504.7	580.3
DPS	52	52	52
Payout %	39	37	34
Dividend Yield %	2.1	2.1	2.1
P/E	16.9	16.2	15.0
EBIDTA Margin	27%	26%	26%
PBT Margin	29%	27%	27%
PAT Margin	22%	21%	21%
Debt/Equity	0.0	0.0	0.0
Current Ratio	5.55	5.13	5.23
ROE	30.6	27.0	25.3

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**Stock Rating Scale**

	<b>Absolute Return</b>
BUY	>20%
ACCUMULATE	12% to 20%
HOLD	5% to 12%
NEUTRAL	-5% to 5%
REDUCE	<-5%

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