

Earnings beats all street estimates; To be driven along with technological requirement of overseas clients

CMP: Rs 2,818

Rating: HOLD

Target Price: Rs 2,994

Stock Info

| | |
|--------------------------|--------------|
| BSE | 532540 |
| NSE | TCS |
| Bloomberg | TCS IN |
| Reuters | TCS.BO |
| Sector | IT |
| Face Value (Rs) | 1 |
| Equity Capital (Rs mn) | 3,754 |
| Mkt Cap (Rs mn) | 1,06,03,113 |
| 52w H/L (Rs) | 2,885/ 1,506 |
| Avg Yearly Vol (in 000') | 3,438 |

Shareholding Pattern %

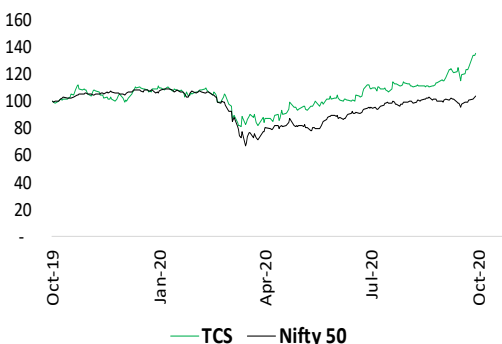
(As on March, 2020)

| | |
|-----------------|-------|
| Promoters | 72.05 |
| FII | 16.00 |
| DII | 7.92 |
| Public & Others | 4.03 |

Stock Performance (%)

| | 3m | 6m | 12m |
|-------|------|------|------|
| TCS | 27.0 | 59.6 | 39.5 |
| Nifty | 9.6 | 31.6 | 4.6 |

TCS Vs Nifty



Source: Arihant Research, Company Filings, Ace Equity, Bloomberg

TCS beat all street estimates with the Q2FY21 earnings figures. Consolidated revenue stood at Rs 401,350 mn, registering +3.0% YoY/4.7% QoQ. Consolidated EBIT stood at Rs 105,150 mn, up by 12.3% YoY/16.2% QoQ. On the margins front, EBIT margin improved by 218bps YoY/259bps QoQ to 26.2%, due to check on other operating expenses. Consolidated PAT saw a fall of 7.1% YoY to Rs 74,750 mn vs 80,420 mn in Q2FY20 due to provisioning of Rs 12,180 mn for legal case against the company. It proposed a share buyback of Rs 160,000 mn (roughly 1.5% of shareholder's equity) for a price of Rs 3,000 per share. The company also announced of second interim dividend of Rs 12 per equity share of Re 1 each, over last quarter's interim dividend of Rs 5 per share.

Q2FY21 Segment Highlights

Industries: Retail & CPG bounced back to grow at 8.8% QoQ. All other industry verticals showed positive growth but Media & Communications: BFSI (+6.2%), Life Sciences and Healthcare (+6.9%), Manufacturing (+1.4%), Technology & Services (+3.1%) and Communications & Media (-2.4%) sequentially.

Markets: Pandemic induced changes brought about technological growth by geography. North American market grew by (+3.6%), UK (+3.8%), and Continental Europe (+6.1%). In the emerging markets, Latin America grew (+5.5%), Asia Pacific (+2.9%), MEA (+8%) and India outperformed (+20%).

Services:

Consulting & Services Integration: Strong traction continued in M&A and Location Independent Agile services. Finance and shared services, as well as digital strategy and integration services saw strong traction.

Cognitive Business Operations: TCS' Zero Touch model, AI & ML enabled processes leveraged for 100% remote execution, saw strong traction and recognition.

Digital Transformation Service: Strong growth momentum in both Public & Private cloud services with access controls platforms grew strongly.

Outlook & Valuation

TCS is well positioned to capitalize on opportunities, currently visible in the more advanced markets of North America and Europe. With the pandemic induced changes to consumer lifestyle and preferences, the technology space will witness continued growth in the near term due to strong demand for Cloud services. From here on, TCS should see continuous demand from almost all business segments. At CMP of Rs 2,818, TCS currently trades at FY20 P/E of 34.7x. Despite marginally fallen Q1FY21 results, we remain bullish on TCS for both near and long term. We value TCS at PE of 32x to its FY22E EPS of Rs 94, which yields a target price of Rs 2,994 per share. **We maintain our rating at HOLD for TCS.**

| Particulars (Rs mn) | FY19 | FY20 | FY21E | FY22E |
|---------------------|-----------|-----------|-----------|-----------|
| Net Sales | 14,64,630 | 15,69,490 | 15,73,598 | 16,99,951 |
| EBITDA | 3,95,060 | 4,21,090 | 4,18,577 | 4,58,987 |
| PAT | 3,15,620 | 3,24,470 | 3,13,007 | 3,51,196 |
| EPS (per share) | 84 | 86 | 83 | 94 |
| ROE | 35.3% | 38.6% | 27.1% | 30.4% |
| P/E | 26.2 | 25.5 | 26.4 | 23.6 |

Note that the company's buyback has just been announced and hence not accounted for in the Projections.

Q2 FY21 - Quarterly Performance (Consolidated)

(in Rs Mn)

| Income Statement | Q2FY21 | Q1FY21 | Q2FY20 | Q-o-Q | Y-o-Y | H1FY21 | H1FY20 | Y-o-Y |
|--------------------------|----------------|----------------|----------------|---------------|----------------|----------------|----------------|----------------|
| Net Revenue | 401,350 | 383,220 | 389,770 | 4.7% | 3.0% | 784,570 | 771,490 | 1.7% |
| Employee Costs | 226,650 | 220,930 | 214,700 | 2.6% | 5.6% | 447,580 | 422,790 | 5.9% |
| Other Operating Expenses | 59,570 | 62,050 | 72,820 | -4.0% | -18.2% | 121,620 | 146,080 | -16.7% |
| Depreciation | 9,980 | 9,760 | 8,640 | 2.3% | 15.5% | 19,740 | 16,810 | 17.4% |
| EBIT | 105,150 | 90,480 | 93,610 | 16.2% | 12.3% | 195,630 | 185,810 | 5.3% |
| EBIT margin % | 26.2% | 23.6% | 24.0% | 259bps | 218bps | 24.9% | 24.1% | 85bps |
| Other Income | 9,140 | 5,980 | 13,610 | 52.8% | -32.8% | 15,120 | 30,360 | -50.2% |
| Finance Costs | 1,740 | 1,420 | 1,930 | 22.5% | -9.8% | 3,160 | 4,500 | -29.8% |
| Exceptional Items | 12,180 | - | - | NA | NA | 12,180 | - | NA |
| PBT | 100,370 | 95,040 | 105,290 | 5.6% | -4.7% | 195,410 | 211,670 | -7.7% |
| Tax Expense | 25,330 | 24,550 | 24,710 | 3.2% | 2.5% | 49,880 | 49,560 | 0.6% |
| Effective Tax Rate % | 25.2% | 25.8% | 23.5% | -59bps | 177bps | 25.5% | 23.4% | 211bps |
| Reported PAT | 75,040 | 70,490 | 80,580 | 6.5% | -6.9% | 145,530 | 162,110 | -10.2% |
| MI & Associates | -290 | -410 | -160 | | | -700 | -380 | |
| Consolidated PAT | 74,750 | 70,080 | 80,420 | 6.7% | -7.1% | 144,830 | 161,730 | -10.4% |
| PAT Margin % | 18.6% | 18.3% | 20.6% | 34bps | -201bps | 18.5% | 21.0% | -250bps |
| EPS (Rs) | 19.9 | 18.7 | 21.4 | 6.7% | -7.1% | 38.6 | 43.1 | -10.4% |

Source: Arianth Research, Company Filings, Ace Equity, Bloomberg

Q2 FY21 – Key Concall Highlights

- Revenue growth was broad-based across verticals and geographies. Margin expansion was largely driven by revenue growth. Overall, the performance in Q2FY21 was better than the management's expectation.
- The deal pipeline is strong, with a good mix of large and small deals. Deal wins in Q2FY21 comprised a larger number of small and medium deals and fewer large deals.
- Management expects to see the typical seasonal impact of furloughs in Q3FY21.
- The company plans to offer wage hikes (similar to last year) across the hierarchy, effective from 1st October.
- Management hinted at the ability to maintain margins in a narrow band despite the impact of furloughs and wage hikes in the near term.
- TCS has won several vendor consolidation deals in the quarter, resulting in market share gains in certain accounts.
- Demand recovery is seen across verticals. Travel and Hospitality would take longer to recover, while BFSI, Retail (excluding discretionary), and Healthcare continue to do well.
- The pandemic has turned out to be a catalyst as clients now see business value in resiliency, which was neglected in the past. This change in view has resulted in accelerated demand for cloud, security and digital technologies.
- The medium to long term outlook for IT Services is healthy as technology spends/budgets are expected to increase on the back of increasing digital investments.

Key Financials

| Profit and Loss statement | | | | |
|------------------------------|----------------|----------------|----------------|----------------|
| Particulars (Rs Mn) | FY19 | FY20 | FY21E | FY22E |
| Net Revenue | 1464630 | 1569490 | 1573598 | 1699951 |
| Employee costs | 782460 | 859520 | 856037 | 917974 |
| Operation and other expenses | 287110 | 288880 | 298984 | 322991 |
| Total Operating Expenses | 1069570 | 1148400 | 1155021 | 1240964 |
| EBIDTA | 395060 | 421090 | 418577 | 458987 |
| EBIDTA Margin | 27.0% | 26.8% | 26.6% | 27.0% |
| Depreciation | 20560 | 35290 | 34619 | 35699 |
| EBIT | 374500 | 385800 | 383958 | 423288 |
| Interest | 1980 | 9240 | 7868 | 8500 |
| Other Income | 43110 | 45920 | 31472 | 42499 |
| PBT | 415630 | 422480 | 407562 | 457287 |
| Tax | 100010 | 98010 | 94554 | 106091 |
| PAT | 315620 | 324470 | 313007 | 351196 |
| Growth (%) | 22.0% | 2.8% | -3.5% | 12.2% |

| Balance Sheet | | | | |
|-------------------------------|----------------|----------------|----------------|----------------|
| Particulars (Rs Mn) | FY19 | FY20 | FY21E | FY22E |
| Shareholder's Funds | | | | |
| Share Capital | 3754 | 3754 | 3754 | 3754 |
| Reserves & Surplus | 890710 | 837510 | 1150517 | 1152802 |
| Net Worth | 894464 | 841260 | 1154271 | 1156556 |
| Minority Interest | 4530 | 6230 | 7080 | 7830 |
| Total Non Current Liabilities | 27366 | 90900 | 33316 | 46268 |
| Total Current Liabilities | 220840 | 270600 | 231293 | 254388 |
| Total Liabilities | 1147200 | 1208990 | 1425960 | 1465042 |
| Net Block | 104110 | 109410 | 110152 | 118997 |
| Capital Work-in-Progress | 9630 | 9060 | 9000 | 9500 |
| Goodwill on consolidation | 17000 | 17100 | 17000 | 17300 |
| Total Non Current Assets | 228120 | 306620 | 343414 | 355433 |
| Cash and bank balance | 72240 | 86460 | 596573 | 858211 |
| Total Current Assets | 919080 | 902370 | 1082546 | 1109610 |
| Total Assets | 1147200 | 1208990 | 1425960 | 1465042 |

| Cash Flow Statement | | | | |
|--|----------------|----------------|----------------|----------------|
| Particulars (Rs Mn) | FY19 | FY20 | FY21E | FY22E |
| PAT | 315620 | 324470 | 313007 | 351196 |
| Add:- Depreciation | 20560 | 35290 | 34619 | 35699 |
| Change in Working Capital | 55656 | 59790 | 59790 | 59790 |
| Cash generated from operations | 391836 | 418980 | 418980 | 418980 |
| Taxes paid | -100010 | -97140 | -97140 | -97140 |
| Net cash flow from operating activities | 291826 | 321840 | 321840 | 321840 |
| Purchase of fixed assets | -20482 | -22530 | -24783 | -27262 |
| Others | -65860 | 0 | 0 | 0 |
| Net cash flow from investing Activities | -86342 | -22530 | -24783 | -27262 |
| Dividend paid, including dividend tax | -126248 | -130080 | -130080 | -130080 |
| Others | -160360 | 0 | 0 | 0 |
| Net cash flow from financing Activities | -286608 | -130080 | -130080 | -130080 |
| Net Cash Flow | 18886 | 266370 | 264117 | 261638 |
| Opening Cash Balance | 48830 | 72240 | 332456 | 596573 |
| Exchange difference on Forex | 4524 | -6154 | 0 | 0 |
| Closing Cash Balance | 72240 | 332456 | 596573 | 858211 |

| Key Ratios | | | | |
|-------------------|-------|-------|-------|-------|
| Particulars | FY19 | FY20 | FY21E | FY22E |
| EPS (Rs) | 84 | 86 | 83 | 94 |
| Book Value (Rs) | 238 | 224 | 307 | 308 |
| DPS (Rs) | 50 | 50 | 50 | 50 |
| Payout % | 59 | 58 | 60 | 53 |
| Dividend Yield % | 1.8 | 1.8 | 2.8 | 2.8 |
| P/E (x) | 33.5 | 32.6 | 33.8 | 30.1 |
| EBIDTA Margin | 27.0% | 26.8% | 26.6% | 27.0% |
| PBT Margin | 28.4% | 26.9% | 25.9% | 26.9% |
| PAT Margin | 21.5% | 20.7% | 19.9% | 20.7% |
| Debt/Equity (x) | 0.0 | 0.1 | 0.0 | 0.0 |
| Current Ratio (x) | 4.2 | 3.3 | 4.7 | 4.4 |
| ROE | 35.3% | 38.6% | 27.1% | 30.4% |

Source: Arianth Research, Company Filings, Ace Equity, Bloomberg

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| Stock Rating Scale | Absolute Return |
|--------------------|-----------------|
| BUY | >20% |
| ACCUMULATE | 12% to 20% |
| HOLD | 5% to 12% |
| NEUTRAL | -5% to 5% |
| REDUCE | -5% to -12% |
| SELL | <-12% |

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