



TCS

Sector: Technology

1QFY17 Result Update

CMP: ₹2,520

Decent quarter, Outlook positive

Recommendation: Hold

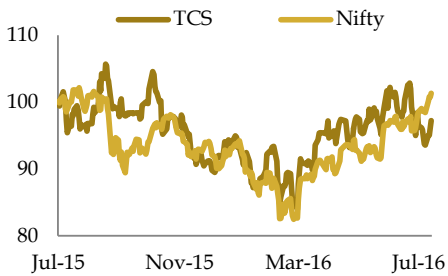
Market statistics

Current stock price (₹)	2,520
Shares O/S (cr.)	197.0
Mcap (₹ cr)	496,922
52W H/L (₹)	2,770/2,115
6m avg. volume	1,075,232
Bloomberg	TCS.IN

Shareholding pattern

Promoters	73.34
Domestic Institution	5.14
Foreign Institution	16.98
Non-institution	4.54
of which more than 1%	
Life Insurance Corporation of India	3.07

TCS vs Nifty



Capital efficiency & valuations

Particulars	FY16	FY17E	FY18E
RoE (%)	37.1	33.7	32.2
EPS (₹)	122.9	134.2	151.5
CEPS (₹)	133.1	144.2	162.4
P/E (x)	20.6	18.8	16.6
P/BV (x)	6.8	5.9	4.9
EV/EBITDA (x)	15.9	14.4	12.4
Income growth (%)	14.8	11.2	11.0
EBITDA growth (%)	12.4	8.5	13.0
PAT growth (%)	8.3	8.6	12.9

TCS results were higher than expectations – both on the revenue and margin front. TCS' revenue increased 3.7% QoQ (3.1% in cc terms, volume growth of 3.4%), while the EBIT margin stood at 25.1%. This was the lowest margin in 28 quarters, but higher-than-expected. TCS maintained a decent demand growth environment for its services. In Q1FY17, the revenues of TCS increased 3% QoQ (in INR terms). We maintain our Hold recommendation on the stock on account of improvement in US, initiatives taken by TCS towards new technologies and large deal wins providing revenue visibility.

Quarter details: Revenues at US\$4,362mn (3.7% QoQ) was higher-than our estimates (higher by 0.2%). Volume growth in the quarter stood at 3.4% QoQ as compared to 3.2% in the 4QFY16. Company attributed higher-than-expectations revenue growth to bottoming out in the India, Diligenta and Japan. Most of the other verticals, contributed to the growth. TCS added 4, 6, 10 clients in US\$50mn+, US\$20mn+, US\$5mn+ bucket QoQ to take the count to 77, 179 and 439 respectively in Q1FY17. EBIT margins were down by 99bps QoQ to 25.1%. TCS has declared an interim dividend of ₹.6.5/share

Operating metrics robust: Revenues were up 3.1% QoQ in constant currency terms. Pricing was up 110bps QoQ. Growth was led by North America (up 2.5% QoQ in cc terms), while Continental Europe grew 4.6%. The long term target operating range of EBIT margin remains 26-28%. TCS announced that it closed 9 large deals during the quarter, spanning across verticals and geographies (6 in North America, 2 in EU/ UK and 1 in APAC). Deals were won across verticals. Manufacturing was up 3.1%, Communication and Media (7%), Life Science & Healthcare (3.9%), BFSI (1.7%) and Energy & Utilities (7.4%) QoQ, while Hi-Tech was down 0.3%. TCS closed the quarter with a consolidated headcount of 362,079 a net addition of 8,236 from the previous quarter. TCS would be absorbing ~32,000 freshers from campuses for FY17, while mentioning number of additions in FY17 would be lower compared to earlier years as benefits of automation kick in. TCS indicated digital revenue contributed nearly 15.9% to its revenue, up 6% QoQ.

Healthy outlook: Management mentioned that deal pipeline is healthy and closure rates are normal. TCS also indicated that it is reaping benefits of investments in areas like Continental Europe and Latin America. Management also indicated that Latin America business, which had remained soft for quite some time has bottomed out and is expected to grow positively. The company maintained positive growth outlook and demand commentary for FY17. Company expects to see positive traction in UK insurance business (Diligenta).

No mention of qualitative/quantitative guidance: TCS delivered on revenue expectations second time in a row after missing it six times in a row, but it came at a lower margin (margin at a 28 quarter low), though it was higher-than expected. TCS is seeing increased spending and improved budgets in the digital space. Digital revenue accounted for 15.9% of TCS revenue for Q1FY17 (growing 6% QoQ) TCS maintains IMS is still a high traction business and growth rates will remain strong going forward.

Valuation: TCS has robust revenue visibility – looking at deal wins, ramp ups, hiring pattern even in the tough environment. We maintain our Hold recommendation on the stock to account in for deal wins, given consistency in execution and revenue predictability.

ANALYST

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Exhibit 1: Quarterly details

₹ mn	1QFY16	4QFY16	1QFY17	QoQ (%)	YoY (%)	Comments
Revenues (in US\$ mn)	4,036	4,208	4,362	3.7	8.1	In constant currency, revenues were up 3.1% QoQ. Volume growth of 3.4% QoQ, while pricing was up 110bps.
Revenues	256,681	284,486	293,050	3.0	14.2	
- Operating costs	184,662	205,418	214,679	4.5	16.3	
EBITDA	72,019	79,068	78,371	(0.9)	8.8	
EBITDA margin (%)	28.1	27.8	26.7	(105)bps	(131)bps	Lower margin was primarily on account of salary hikes.
- Interest expense	74	97	120	23.6	63.0	
- Depreciation	4,535	4,949	4,910	(0.8)	8.3	
+ Other income, net (incl forex)	7,784	9,147	9,750	6.6	25.3	
PBT	75,195	83,169	83,091	(0.1)	10.5	
- Taxes	17,468	19,702	19,920	1.1	14.0	
Effective tax rate (%)	23.2	23.7	24.0	29bps	74bps	Effective tax rate for FY17 to be ~24%
PAT	57,727	63,468	63,171	(0.5)	9.4	
Minority interest	638	56	-			
Consolidated profits	57,090	63,412	63,171	(0.4)	10.7	
Net Margin	22.2	22.3	21.6	(73)bps	(69)bps	
Reported PAT	57,090	63,412	63,171	(0.4)	10.7	

Source: Company

Exhibit 2: Change in estimates

₹ mn	FY17E			FY18E		
	Old	New	%Chg	Old	New	%Chg
Revenue (US\$ mn)	18,383	18,429	0.3	20,566	20,634	0.3
Revenue	1,194,911	1,207,947	1.1	1,336,762	1,341,242	0.3
EBITDA margin (%)	27.7	27.6	(5)bps	28.1	28.0	(5)bps
EPS (₹)	134.1	134.2	0.1	151.3	151.5	0.1

Source: Trust Research

Geography wise Revenues: Growth was led by North America (up 2.5% QoQ in cc terms), while Continental Europe grew 4.6%.

Exhibit 3: Geographical wise Performance

Geographical mix	Q1FY15	Q2FY15	Q3FY15	Q4FY15	Q1FY16	Q2FY16	Q3FY16	Q4FY16	Q1FY17
Americas	54.4	52.9	54.0	54.5	54.7	54.5	55.6	56.0	55.5
----->North America	52.2	51.0	51.9	52.4	52.8	52.7	53.5	54.0	53.5
----->Ibero America	2.2	1.9	2.1	2.1	1.9	1.8	2.1	2.0	2.0
Europe	29.7	28.6	27.8	27.0	27.1	27.2	26.8	26.1	26.3
----->UK	17.7	17.1	16.1	15.9	16.1	16.4	15.9	14.9	14.8
----->Continental Europe	12.0	11.5	11.7	11.1	11.0	10.8	10.9	11.2	11.5
India	6.3	6.5	6.5	6.6	6.4	6.5	6.0	5.9	6.2
Others	9.6	12.0	11.7	11.9	11.8	11.8	11.6	12.0	12.0
----->APAC	7.6	10.1	9.7	9.8	9.6	9.4	9.4	9.6	9.6
----->MEA	2.0	1.9	2.0	2.1	2.2	2.4	2.2	2.4	2.4
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Company



Vertical wise Performance: Manufacturing was up 3.1%, Communication and Media (7%), Life Science & Healthcare (3.9%), BFSI (1.7%) and Energy & Utilities (7.4%) QoQ, while Hi-Tech was down 0.3%.

Exhibit 4: Vertical wise Performance

Geographical mix	Q1FY15	Q2FY15	Q3FY15	Q4FY15	Q1FY16	Q2FY16	Q3FY16	Q4FY16	Q1FY17
BFSI	41.7	40.4	40.5	40.6	40.6	40.5	40.5	40.9	40.4
Communication & Media	12.1	11.6	11.6	10.8	11.1	10.8	10.9	10.8	11.3
Manufacturing	8.6	10.1	10.1	10.2	9.9	9.8	9.9	10.4	10.4
Retail & distribution	13.8	13.5	13.4	13.6	13.8	13.8	13.8	14.1	14.0
Hitech	5.5	5.7	5.9	6.0	5.8	5.9	6.0	5.6	5.4
Life sciences & health care	6.3	6.3	6.4	6.7	6.9	7.0	7.3	7.3	7.3
Transportation	3.6	3.5	3.5	3.4	3.5	3.6	3.6	3.7	3.9
Energy & utilities	3.9	4.3	4.2	3.9	4.0	4.0	4.1	4.1	4.2
Others	4.5	4.6	4.4	4.8	4.4	4.6	3.9	3.1	3.1
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Company

Human Resources: TCS closed the quarter with a consolidated headcount of 362,079 a net addition of 8,236 from the previous quarter. TCS would be absorbing ~32,000 freshers from campuses for FY17, while mentioning number of additions in FY17 would be lower compared to earlier years as benefits of automation kick in.

Exhibit 5: Employee strength of TCS

Vertical Mix	Q1FY15	Q2FY15	Q3FY15	Q4FY15	Q1FY16	Q2FY16	Q3FY16	Q4FY16	Q1FY17
Total employees	305,431	313,757	318,625	319,656	324,935	335,620	344,691	353,843	362,079
----->IT services (LTM)	NA	NA	NA	NA	NA	NA	NA	NA	NA
----->BPO (LTM)	12.0	12.8	13.4	13.8	15.9	16.2	15.9	15.5	13.6
Trainees	3,452	7,583	5,529	5,569	6,425	9,943	7,593	8,623	5,038
Laterals (India)	8,488	8,924	6,129	5,853	9,337	10,978	10,451	10,659	9,877
Gross addition	15,817	20,350	16,561	14,395	20,302	25,186	22,118	22,576	17,792
Net addition	4,967	8,326	4,868	1,031	5,279	10,685	9,071	9,152	8,236

Source: Company

Client Concentration and order intake: TCS added 4, 6, 10 clients in US\$50mn+, US\$20mn+, US\$5mn+ bucket QoQ to take the count to 77, 179 and 439 respectively in Q1FY17.

Exhibit 6: Client details

Vertical Mix	Q1FY15	Q2FY15	Q3FY15	Q4FY15	Q1FY16	Q2FY16	Q3FY16	Q4FY16	Q1FY17
US\$1m (LTM)	724	743	764	791	804	819	838	829	847
US\$5m (LTM)	359	367	387	389	391	404	413	429	439
US\$10m (LTM)	244	247	249	261	268	274	281	298	298
US\$20m (LTM)	144	153	159	162	172	171	173	173	179
US\$50m (LTM)	58	62	65	68	69	65	65	73	77
US\$100m (LTM)	24	24	25	29	30	33	34	37	37

Source: Company, Trust Research

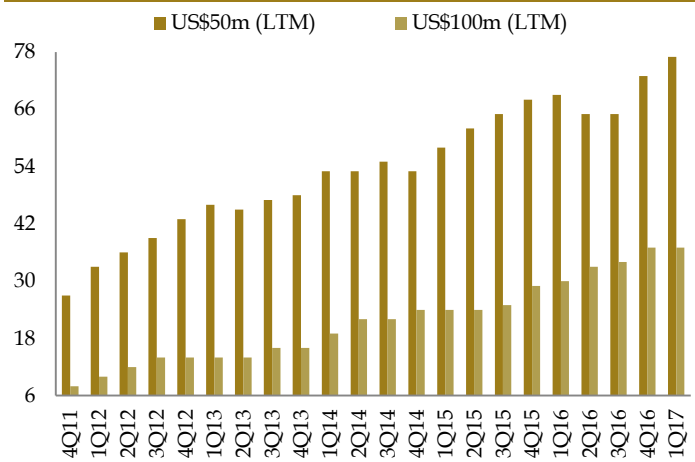


Exhibit 7: Service Offerings

Client concentration	Q1FY15	Q2FY15	Q3FY15	Q4FY15	Q1FY16	Q2FY16	Q3FY16	Q4FY16	Q1FY17
---->ADM	40.8	40.5	39.5	40.1	40.3	40.0	39.7	39.4	38.5
---->Enterprise solutions (with Consulting)	19.1	18.8	19.1	18.6	18.0	17.5	17.4	17.1	17.7
---->Assurance services	8.6	8.4	8.5	8.4	8.5	8.7	8.6	8.8	8.8
Engineering & industrial services	4.5	4.6	4.5	4.5	4.5	4.5	4.5	4.7	4.8
Infrastructure services	12.6	13.8	14.3	14.5	14.7	14.7	15.2	15.2	15.5
Asset leverage solutions	2.5	2.3	2.4	2.3	2.5	3.2	2.8	3.2	3.2
Business process outsourcing	11.9	11.6	11.7	11.6	11.5	11.4	11.8	11.6	11.5
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

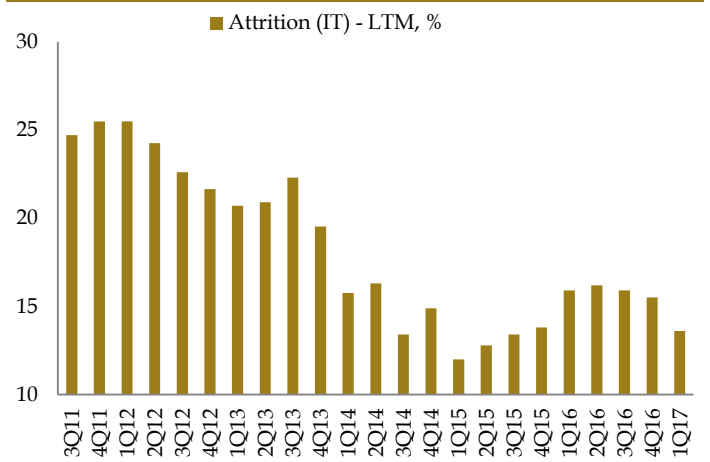
Source: Company

Exhibit 8: Clint addition remained strong



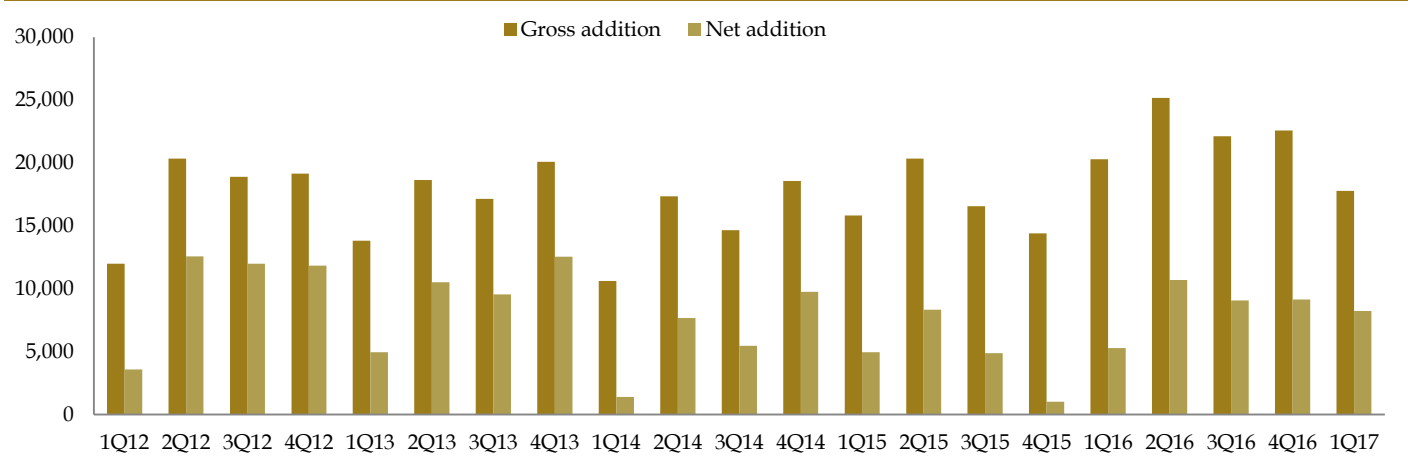
Source: Company, Trust

Exhibit 9: Attrition dipped 190bps QoQ



Source: Company, Trust

Exhibit 10: TCS would be absorbing ~32,000 freshers from campuses for FY17



Source: Company, Trust

Financials

Income Statement (₹ mn)

Year End-March	FY14	FY15	FY16	FY17E	FY18E
Revenues	818,094	946,484	1,086,462	1,207,947	1,341,242
Op. Expenses	566,771	673,543	779,682	874,994	965,058
EBITDA	251,323	272,941	306,780	332,953	376,184
Other Income	16,613	32,532	30,833	35,135	38,463
Depreciation	13,243	18,698	18,879	19,797	21,407
EBIT	254,692	286,775	318,734	348,291	393,241
Interest	722	1,135	331	480	480
PBT	253,971	285,640	318,403	347,811	392,761
Tax	60,713	60,830	75,026	83,383	94,263
PAT	193,258	224,810	243,376	264,428	298,498
Minority + Ex. Ordin.	2,090	28,327	1,227	-	-
Adj Pat	191,168	196,483	242,149	264,428	298,498

Valuations Summary

Year End-March	FY14	FY15	FY16	FY17E	FY18E
Per share (₹)					
EPS	97.7	113.8	122.9	134.2	151.5
CEPS	105.5	124.4	133.1	144.2	162.4
BVPS	282.7	293.7	371.4	426.1	514.4
DPS	32.0	79.0	43.5	47.5	54.0
Payout (%)	38.3	81.2	41.4	41.4	41.7
Valuation (x)					
P/E	25.8	22.5	20.6	18.8	16.6
P/BV	8.9	8.7	6.8	5.9	4.9
EV/EBITDA	19.6	18.4	15.9	14.4	12.4
Dividend Yield (%)	1.3	3.1	1.7	1.9	2.1
Return ratio (%)					
EBIDTA Margin	30.7	28.8	28.2	27.6	28.0
PAT Margin	23.4	20.8	22.3	21.9	22.3
ROAE	39.7	39.5	37.1	33.7	32.2
ROACE	47.2	43.0	48.1	44.0	42.2
Leverage Ratios (x)					
Total D/E	0.0	0.0	0.0	0.0	0.0
Net Debt/Equity	(0.3)	(0.3)	(0.4)	(0.5)	(0.5)
Current ratio	3.9	3.3	4.1	4.6	5.1
Growth Ratios (%)					
Income growth	29.9	15.7	14.8	11.2	11.0
EBITDA growth	39.0	8.6	12.4	8.5	13.0
PAT growth	37.2	16.3	8.3	8.6	12.9
Turnover Ratios					
Inventory Days	-	-	-	-	-
Debtors Days	72	75	75	76	76
Payable days	32	39	38	35	33

Balance Sheet (₹ mn)

Year End-March	FY14	FY15	FY16	FY17E	FY18E
Liabilities					
Equity Share Capital	1,959	1,959	1,970	1,970	1,970
Reserves & Surplus	551,396	572,808	729,920	884,842	1,058,849
Total Shareholders Fund	553,355	574,767	731,890	886,813	1,060,819
Minority Interest	6,902	9,136	3,540	3,540	3,540
Non-current liabilities	(4,943)	(5,900)	(7,820)	(3,159)	(1,432)
Long term Borrowings	1,273	1,143	830	830	830
Deferred tax liabilities	(23,060)	(26,150)	(20,770)	(20,770)	(20,770)
Other LT liab & prov	16,845	19,107	12,120	16,781	18,508
Current Liabilities	110,752	146,716	155,690	171,824	189,344
Short-term borrowings	1,696	2,434	1,620	1,620	1,620
Trade payables	55,365	88,318	75,410	83,904	92,540
Unearned & def revenue	10,507	10,623	13,590	14,383	15,864
Other cur liab. & Prov	43,183	45,340	65,070	71,917	79,320
Total Liabilities	666,065	724,719	883,300	1,059,018	1,252,271
Assets					
Non-current Assets	236,452	235,708	251,170	265,368	277,917
Fixed assets	105,415	117,909	119,240	120,385	121,978
Non-current investments	77,555	44,650	45,700	45,700	45,700
Other non-current assets	53,482	73,150	86,230	99,283	110,239
Current assets	429,613	489,011	632,130	793,650	974,354
Current investments	141,385	178,838	225,320	225,320	225,320
Trade receivables	182,304	204,399	240,730	264,755	293,971
Unbilled revenue	40,056	38,271	39,920	46,332	51,445
Cash & bank balances	14,688	18,622	62,950	184,434	322,776
Other curr fin. assets	34,273	27,142	40,990	46,332	51,445
Other current assets	16,907	21,739	22,220	26,476	29,397
Total Assets	666,065	724,719	883,300	1,059,018	1,252,271

Cash flow Statement

Year End-March	FY14	FY15	FY16	FY17E	FY18E
PBT	253,971	285,640	318,403	347,811	392,761
Depreciation	11,605	15,608	24,259	19,797	21,407
Others	(2,090)	(28,327)	(1,227)	-	-
CF before W.cap	263,486	272,921	341,434	367,608	414,168
Inc/dec in W.cap	32,985	190	62,588	32,294	34,072
Op CF after W.cap	230,501	272,731	278,846	335,314	380,096
Less Taxes	60,713	60,830	75,026	83,383	94,263
Net CF From Operations	169,788	211,902	203,819	251,931	285,834
Inc/(dec) in F.A + CWIP	35,288	31,191	20,210	20,942	23,000
(Pur)/sale of Investments	90,937	4,548	47,532	-	-
CF from Invest Activities	(126,224)	(35,739)	(67,742)	(20,942)	(23,000)
Loan Raised/(repaid)	(13)	2,842	(6,723)	-	-
Equity Raised	26,020	5,964	15,177	0	0
Dividend	73,317	181,034	100,203	109,506	124,492
CF from Fin Activities	(47,309)	(172,229)	(91,748)	(109,505)	(124,492)
Net inc/(dec) in cash	(3,745)	3,934	44,328	121,484	138,342
Op. bal of cash	18,432	14,687	18,622	62,951	184,434
Cl. balance of cash	14,688	18,622	62,950	184,434	322,776



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