



Growth momentum to sustain, margins capped

TCS Q2FY22 performance was a marginally below our estimates across the board

- \$ Revenue came in at \$ 6,333 Mn, +2.9% qoq / +16.8% yoy and 0.7% below our estimates
- INR revenue came in at INR 468,670 Mn, +3.8% qoq / +16.8% yoy and 0.8% below our estimates
- EBIT was reported at INR 120,000 Mn, +3.6% qoq / +13.9% yoy and 4.2% below our estimates
- EBIT margins at 25.6%, vs 25.5% / 26.2% in Q1FY22 / Q2FY21 respectively and 90 bps below our est.
- PAT came in at INR 96,240 Mn, +6.8% qoq / +14.1% yoy and 1% below our estimates
- EPS at INR 26.02 in Q2FY22 vs 24.35 / 22.5 in Q1FY22 / Q2FY21 respectively
- Company also declared a final dividend of INR 7 per share
- Attrition stood at 11.9% vs 8.6% in the previous quarter

Segmental Performance

- **Vertical-wise:**
 - Sequential growth was primarily led by Technology & Services (8.8% of rev) at 5.3% qoq, Comms & Media (6.5% of rev) at 4.5% qoq and Retail & CPG (15% of rev) at 4.3% qoq in reported terms. Manufacturing (9.9% of rev) and BFSI (32.4% of rev) followed closely at 4% qoq and 2.6% qoq growth in reported terms
 - Sequential Client additions were strong as TCS added 5 clients in \$100 Mn+ category, 17 clients in \$50 Mn+ bucket, 19 in \$20 Mn+ bucket, +31 in \$10 Mn bucket, +44 clients in the \$5 Mn+ bucket and +68 clients in the \$1 Mn+ bucket
- **Geographically:**
 - Sequential growth during the quarter was largely driven by North America (50.3% of rev) at +4.8% qoq and bounce-back of India (5.1% of rev) in Q2 at +14.1% qoq after a dismal Q1FY22.
 - Europe (15.9% of rev) had a soft quarter at -2% qoq

Financial Summary

Y/E Mar (Rs mn)	FY 20	FY 21	FY 22E	FY 23E
Net sales	15,69,490	16,41,770	18,96,770	20,56,097
EBIT	3,85,800	4,24,810	4,86,918	5,25,981
Adjusted net profit	3,22,382	3,41,916	3,95,415	4,28,304
Free cash flow	2,07,759	3,19,840	3,21,762	3,81,132
EPS (Rs)	85.9	92.5	107.0	115.9
growth (%)	3%	8%	16%	8%
P/E (x)	45.8	42.5	36.8	34.0
P/B (x)	17.6	16.5	13.9	11.9
EV/EBITDA (x)	35.1	31.2	27.2	25.2
D/E	-	-	-	-
ROCE (%)	28.8	33.1	33.4	31.3
RoE (%)	37.1	39.7	41.1	37.8
Dividend yield (%)	2.2	0.8	1.4	1.5

Source: Company

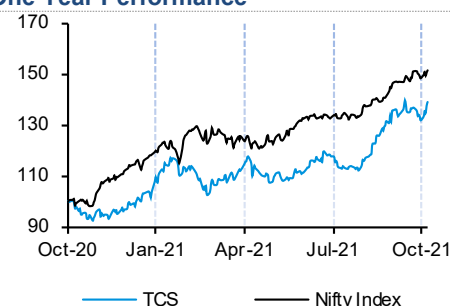
Rating	TP (Rs)	Up/Dn (%)
HOLD	3707	-6

Market data

Current price	Rs	3936
Market Cap (Rs.Bn)	(Rs Bn)	14558
Market Cap (US\$ Mn)	(US\$ Mn)	194665
Face Value	Rs	1
52 Weeks High/Low	Rs	1990/2600
Average Daily Volume	('000)	1694
BSE Code		532540
Bloomberg		TCS:IN

Source: Bloomberg

One Year Performance



Source: Bloomberg

% Shareholding	Sep-21	Jun-21
Promoters	72.19	72.19
Public	27.81	27.81
Others	0.00	0.00

Source: BSE

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Conference Call KTAs

- Demand environment continues to be strong in the short and medium term
- Supply side shortages led to greater use of subcontracting – which along with unfavourable currency (others excluding dollar) movements restricted margins.
- Drivers of growth include: Increased outsourcing, investment in building a digital core and Growth & Transformation initiatives.
- Operations optimization by clients is leading to higher outsourcing and TCS differentiates itself through its Machine First Delivery Model (MFDM) – which enables TCS to command industry leading margins (TCS Cognix at the heart of this)
- Cloud Adoption and Transformations: provides big opportunity and TCS has won many large deals. As part of modernization, TCS also saw shifting of ERPs from on-premise to SaaS and hosted models. Key focus areas are Customer Experience & E-commerce, Supply Chain & Human Capital, Medical Tech, etc.
- Investment agenda in talent and R&D in Services, P&P and geographies for growth will continue going ahead
- Tightness in margins will continue as supply side margins continue and due to continuous investments
- Have planned for growth 2 quarters prior and that's why TCS has hired 42000 freshers in H1
- Europe had a soft quarter but no structural change and see good outsourcing opportunity and new deal signings are higher than before. A very large program has come to an end – which had an impact
- TCV of \$7.6 Bn was up 25% YoY (excluding the large deal signed in Q2FY21) and had a good mix of large, mid and small deals. BFSI recorded \$ 2.1 Bn and Retail - \$1.2 Bn. Geographically, North America won \$3.9 Bn in deals
- Attrition should remain elevated for another quarter or 2, however, do not see that as a cause of major concern
- Net Addition of 19,690 during the quarter
- Engineering Services: TCS participating in the automotive revolution by working with all major auto OEMs for autonomous vehicles, BMS, cloud based connected cars, etc.
- B2B commerce and direct to consumer provides a massive opportunity as CPG companies have been participating in this by adopting technology and removing the intermediary
- M&A and divestitures continues to be a major growth area

Products & Platforms

- Ignio had 22 customer wins and 8 go-lives
- TCS Bancs: 5 new wins and 3 go-lives
- Hobbs (for telecom service providers): 4 new wins and 6 go-lives
- Quartz Blockchain platform had 2 new wins and 1 go-live
- TwinX: 4 new wins and 6 Go-lives
- MasterCraft: 22 new wins
- Jile: 3 new wins

Financial Parameters

- Net Cash from Operations at \$99.45 Bn, which is 103% of PAT
- FCF stood at \$92.29 Bn
- Investments stood at INR 605.48 Bn

Quarterly Performance Analysis

Exhibit 1

YE March (Rs. mn)	Q2 FY22	Q1 FY22	Q-o-Q change %	Q2 FY21	Y-o-Y change %	Q2FY22 Est.	Deviation %
Total Revenue (USD Mn)	6,333	6,154	2.9%	5,424	16.8%	6,380	-0.7%
Total Revenue (INR Mn)	468,670	454,110	3.2%	401,350	16.8%	472,616	-0.8%
Less:							
Cost of Revenues	270,480	262,400	3.1%	229,580	17.8%	264,748	2.2%
SG&A Expenses	67,040	65,070	3.0%	56,640	18.4%	70,892	-5.4%
Total Expenditure	337,520	327,470	3.1%	286,220	17.9%	335,640	0.6%
EBIDTA	131,150	126,640	3.6%	115,130	13.9%	136,975	-4.3%
Less: Depreciation	11,150	10,760	3.6%	9,980	11.7%	10,760	3.6%
EBIT	120,000	115,880	3.6%	105,150	14.1%	126,215	-4.9%
Other income (expense), net	9,690	5,750	68.5%	7,400	30.9%	6,144	57.7%
Profit Before Tax	129,690	121,630	6.6%	112,550	15.2%	131,309	-1.2%
Total Tax	33,160	31,320	5.9%	27,930	18.7%	33,812	-1.9%
PAT before Minority Interest	96,530	90,310	6.9%	84,620	14.1%	97,497	-1.0%
Minority Interest	290	230	N.A.	290	N.A.	248	
Profit After Tax	96,240	90,080	6.8%	84,330	14.1%	97,248	-1.0%
Basic & Diluted EPS (Rs.)	26.0	24.0	8.4%	22.5	15.8%	25.9	0.4%
Basic & Diluted Outstanding (mn)	3,699	3,752		3,752		3,752	
Margin Analysis %			Change In bps		Change In bps		
EBIDTA Margin	28.0%	27.9%	10	28.7%	-70	29.0%	-100
Operating Margin	25.6%	25.5%	9	26.2%	-59	26.7%	-110
PBT Margin	27.7%	26.8%	89	28.0%	-37	27.8%	-11
NPM	20.5%	19.8%	70	21.0%	-48	20.6%	-4
Effective Tax Rate (%)	25.6%	25.8%	-18	24.8%	75	25.8%	-18
Cost Analysis %			Change In bps		Change In bps		
Cost of Revenues/ Sales	57.7%	57.8%	-7	57.2%	51	56.0%	169
SG&A/Sales	14.3%	14.3%	-2	14.1%	19	15.0%	-70
Other income/ PBT	7.5%	4.7%	274	6.6%	90	4.7%	279

TCS' USD revenue growth of 2.9% qoq was below our est. for the 2nd consecutive quarter. Margins were restricted due to unfavourable currency movement, retention costs and on-going investments. Going ahead, we expect company to maintain growth momentum but margins to be capped at current levels

Valuation & Outlook

TCS is currently trading at 36.8x / 34x FY22e / FY23e EPS. TCS' results were weaker than we expected. Sequential revenue growth momentum was slower than the last few quarters despite the robust demand environment. Additionally, we believe that the company has not been able to absorb previous quarter's wage hike - partly because of higher retention costs on the back of the supply side crunch and partly due to continuous investments for growth.

We believe that TCS will be able to sustain the current growth momentum, however margins will be restricted at current levels due to several headwinds such as retention costs and returning of facility and travel expenses post-COVID.

We continue to maintain our HOLD rating on the stock but increase the target price from INR 3,469 to INR 3,707, i.e. 32x FY23e EPS which is an 8% premium to Infosys' forward multiple of 30x FY23 owing to the similar premium of TCS' operating profitability. Although, we maintain a HOLD rating on the stock, we believe it would be prudent for investors to book partial profits and HOLD on to the balance.

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