

CMP: ₹ 4,291

Target: ₹ 4,750 (11%)

Target Period: 12 months

HOLD

January 13, 2025

Mixed bag quarter; Deal TCV growth healthy...

About the stock: Tata Consultancy Services (TCS) is one of the leading IT service providers with a presence in BFSI, communication, manufacturing, retail & hi tech.

Q3FY25 Performance: TCS reported revenue of US\$ 7,539 mn, down 1.7% QoQ & up 3.5% YoY (up 4.5% YoY in CC terms). EBIT margin came at 24.5%, up ~40 bps QoQ despite headwinds led by operating efficiency through productivity, utilization & pyramid improvement. TCV was at US\$10.2 bn, up 18.6% QoQ & 26% YoY.

Investment Rationale:

- Healthy TCV growth & reduced deal cycles signal improved demand environment:** TCS reported a broad based and healthy TCV growth of 18.6% QoQ and 26% YoY signalling improved demand environment. As per the management, the deal cycles have reduced compared to the previous quarters, indicating improved client decision making which will aid revenue recovery in the short-medium term. The core markets are expected to drive revenues in CY25 and we expect dollar revenue to grow by **4.6%, 5.1% & 8.8% in FY25E, FY26E & FY27E respectively implying CAGR of 6.1% between FY24-27E compared to CAGR of 8.8% between FY19-24.**
- Improved margin outlook:** We believe that tapering off of the BSNL deal (lower margin project, in our view) over the next few quarters, will aid TCS to expand its EBIT margins. Furthermore, Pyramid and productivity improvements are expected to drive margin growth going forward. We note that management remains committed to a margin band of 26-28%, and expects to exit Q4 with an EBIT margin of 26%. Accordingly, we **bake in EBIT margins of 24.7%/26%/26.2% in FY25E/FY26E/FY27E.**
- Revival in overall demand environment:** The management has indicated early signs of revival in the discretionary spend environment. Key segment viz. North America BFSI continues to grow positively with large accounts contributing to growth. Additionally, the client specific issues in Lifesciences and Manufacturing have now stabilised and the overall demand environment remains net positive for CY25 and CY26.

Rating and Target Price

- Improving discretionary spend environment coupled with healthy TCV growth position TCS well for medium to long term growth.
- We maintain **HOLD**, and assign a **target price of ₹4,750 at 28x P/E on FY27E EPS (vs ₹4,500 earlier).**



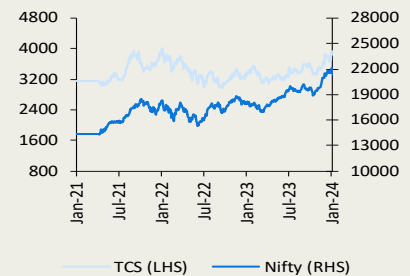
Particulars

Particular	Amount
Market Cap (₹ Crore)	15,56,600
Total Debt (₹ Crore)	8,021
Cash & equiv. (₹ Crore)	40,497
EV (₹ Crore)	15,24,124
52 week H/L	4592/ 3591
Equity capital (₹ Crore)	362
Face value	1.0

Shareholding pattern

	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24
Promoters	72.3	72.4	71.8	71.8	71.8
FII	12.5	12.5	12.7	12.4	12.7
DII	10.1	10.1	10.7	11.1	10.9
Others	5.2	5.0	4.9	4.8	4.7

Price Chart



Key risks

- Better than expected revenue growth;
- Lower than expected alternate revenue streams to compensate for the BSNL deal revenues

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Key Financial Summary

₹ crore	FY22	FY23	FY24	5 year CAGR (FY19-24)	FY25E	FY26E	FY27E	3 year CAGR (FY24-27E)
Net Sales	1,91,754	2,25,458	2,40,893	10.5	2,56,823	2,75,220	3,01,052	7.7
EBITDA	53,057	59,260	63,337	9.9	68,571	77,062	84,897	10.3
EBITDA Margins (%)	27.7	26.3	26.3		26.7	28.0	28.2	
Net Profit	38,327	42,147	45,908	7.8	49,272	55,309	61,423	10.2
EPS (₹)	104.7	115.2	125.9		136.2	152.9	169.8	
P/E	41.0	37.3	33.8		31.5	28.1	25.3	
RoNW (%)	43.0	46.6	50.7		48.9	48.8	47.8	
RoCE (%)	51.4	56.0	60.9		58.9	59.1	58.4	

Source: Company, ICICI Direct Research

Performance highlights and outlook

- **Revenue performance:** TCS in Q3 reported revenue of US\$ 7,539 mn, down 1.7% QoQ & up 3.5% YoY (in CC terms, flat QoQ and up 4.5% YoY). In rupee terms it reported revenue of ₹63,973 crore, down 0.4% QoQ & up 5.6% YoY. **BSNL deal is expected to taper off by H1FY26 and the management indicated that there are enough opportunities in India (including 5G RFP floated by BSNL.) and regional markets to offset revenue decline from the current BSNL deal.**
- **Geography performance:** Geography wise the growth was led by India (9.8% of mix), MEA (2.3% of mix), Asia (7.8% of mix) & UK (16.6% of mix) which reported YoY CC growth of 70.2%, 15%, 5.8% & 4.1% respectively while North America (47.6% of mix) and Continental Europe (14% of the mix) declined by 2.3% & 1.5% respectively. Core markets are expected to drive growth in CY25.
- **Segment performance:** Segment wise in CC terms on YoY basis growth was led by Regional Markets (16.4% of mix), Energy, Resources and Utilities (5.6% of mix) Retail (15.3% of the mix), BFSI (30.5% of the mix), and Manufacturing (8.4% of mix) which grew by 40.9%, 3.4% 1.1%, 0.9% and 0.4% while Communications (5.8% of mix), Life Sciences (10.1% of the mix) Technology & Services (8% of the mix) declined by 10.6%, 4.3% and 0.4% respectively. On a QOQ basis Lifesciences, Manufacturing, Communication, BFSI, Technology and Retail were down by 4.5%, 4%, 3.4%, 2.7%, 1.7% & 0.4% while Energy, Resources & Utilities was the only positive sequential growth segment reporting a growth of 3.4%.
 - **Lifesciences:** This segment, as per the management, stabilised this quarter post a one-off client incident in the previous quarter. The company holds a wait and watch stance for the segment as they await more policy clarity in the US market.
 - **Manufacturing:** The segment continues to see softness due macro and industry-specific issues in auto and aerospace. **As per the management, it may bottom out in Q4FY25 and revive subsequently, thereafter. Good large deals in areas such as factory of the future, SDV, AI/GenAI are expected to aid revival.**
 - **BFSI & CBG: BFSI continues to see improvement driven by interest rate cuts, falling unemployment rates, stable government and lowering inflation.** However, management maintained a cautious optimism owing to unresolved geopolitical headwinds. **North America continues to grow positively with large accounts contributing to growth.** The growth is also back on track for CBG Segment with recovery seen in all major markets.
- **Margin performance:** The company's EBIT margin came at 24.5%, up ~40 bps QoQ despite headwinds on account of furloughs and Q3 seasonality, and were driven by operating efficiency through improvement in productivity, utilization and pyramid. The PAT margin came at 19.4%, up ~80 bps QoQ.
- **Deal Wins:** The company during the quarter won TCV of US\$ 10.2 bn (up 18.6% QoQ/ 26% YoY) with BFSI, Retail & US reporting TCV of US\$ 3.2 bn, \$1.3 bn & \$5.9 bn respectively. **The deal wins going up after two quarters and being well diversified across industries, geographies, and service lines, gives confidence for medium term growth. Notably, no mega deal wins were added during the quarter.**
- **Demand Outlook:** As per the company, the clients still keep their focus on cost optimisation and business transformation deals with high RoI expectations. **The management remains optimistic on discretionary spends recovery driven reduction in the interest rates, easing of inflation and post-US election stability.**
- **AI/GenAI Outlook:** On the GenAI front, clients are investing in Agentic AI which is being described as the next frontier in AI by the management. TCS shall use its deep contextual knowledge of customers' businesses to design, train and deploy agents to solve high-value business problems.

- **Margin Guidance/ Aspiration:** The management reiterated their commitment to the aspirational margin band of 26-28%, with an expectation of exiting FY25 with 26% margins. **Moreover, tapering off of the BSNL deal expected over the next few quarters (till September'26) will aid TCS to expand its profit margins primarily due to lower 3rd party costs.**
- **Attrition and employee addition:** Attrition further expanded by 70 bps QoQ to 13%. The company's headcount declined by 5.3K employees taking the total employee headcount to 6,07,354 in Q3. They expect to hire increased numbers of campus hires next year. With respect to the expected curbs and increased regulations on H1B visas the management commented that their dependence on the H-1B visa is quite low and hence they do not expect any major disruption in business.
- **Dividend:** The company in Q3FY25 declared an interim dividend of ₹10 per share and a special dividend of ₹66 per share which is in line with its practice of returning 80-100% of FCFs back to shareholders.

Exhibit 1: Quarter Performance

	Q3FY25	Q3FY24	YoY (%)	Q2FY25	QoQ (%)	Comments
Revenue (US\$ mn)	7,539	7,281	3.5	7,670	-1.7	In CC terms Revenue grew 1.1% QoQ 4.5% YoY
Revenue (₹ crore)	63,973	60,583	5.6	64,259	-0.4	On a QoQ basis growth was led by Regional Markets, EMEA and Latin America region which grew by 8.2%, 7.7% and 3.8% respectively. On the vertical front, ERU grew by 4%
Employee expenses	38,061	34,920	9.0	38,734	-1.7	
Gross Margin	25,912	25,663	1.0	25,525	1.5	
Gross margin (%)	40.5	42.4	-186 bps	39.7	78 bps	
SG&A expenses	8,879	10,233	-13.2	8,793	1.0	
EBITDA	17,033	15,430	10.4	16,732	1.8	
EBITDA Margin (%)	26.6	25.5	116 bps	26.0	59 bps	
Depreciation	1,376	1,233	11.6	1,267	8.6	
EBIT	15,657	14,197	10.3	15,465	1.2	
EBIT Margin (%)	24.5	23.4	104 bps	24.1	41 bps	EBIT margin expanded by 40 bps QoQ despite headwinds on account of furloughs and Q3 seasonality, which was offset by operating efficiency through improvement in productivity, utilization and pyramid
Other income (less interest)	1,009	632	59.7	567	78.0	
PBT	16,666	14,829	12.4	15,074	10.6	
Tax paid	4,222	3,732	13.1	4,077	3.6	
Reported PAT	12,380	11,058	12.0	11,909	4.0	
Adjusted PAT	12,380	11,058	12.0	11,909	4.0	

Source: Company, ICICI Direct Research

Financial Summary

Exhibit 2: Profit and loss statement				
	₹ crore			
(Year-end March)	FY24	FY25E	FY26E	FY27E
Total operating Income	2,40,893	2,56,823	2,75,220	3,01,052
Growth (%)	6.8	6.6	7.2	9.4
COGS (employee expenses)	1,39,775	1,52,377	1,59,903	1,74,309
S,G&A expenses	37,781	35,875	38,256	41,846
Total Operating Expenditure	1,77,556	1,88,252	1,98,158	2,16,156
EBITDA	63,337	68,571	77,062	84,897
Growth (%)	6.9	8.3	12.4	10.2
Depreciation	4,984	5,183	5,504	6,021
Other Income less interest	3,644	2,977	2,879	3,809
PBT	61,997	66,365	74,436	82,685
Total Tax	15,898	16,854	18,907	21,002
Minority Interest	191	239	220	260
PAT	45,908	49,272	55,309	61,423
Growth (%)	8.9	7.3	12.3	11.1
EPS (₹)	126	136	153	170
PAT	45,908	49,272	55,309	61,423
EPS - Reported (₹)	125.9	136.2	152.9	169.8

Source: Company, ICICI Direct Research

Exhibit 3: Cash flow statement				
	₹ crore			
(Year-end March)	FY24	FY25E	FY26E	FY27E
Profit before Tax	61,997	66,365	74,436	82,685
Add: Depreciation	4,985	5,183	5,504	6,021
(Inc)/dec in Current Assets	(6,793)	(4,794)	(5,536)	(7,773)
Inc/(dec) in CL and Provisions	(89)	3,436	3,598	5,052
Taxes paid	(12,489)	(16,854)	(18,907)	(21,002)
CF from operating activities	44,338	50,360	56,217	61,173
(Inc)/dec in Investments	5,657	(2,750)	(546)	(767)
(Inc)/dec in Fixed Assets	(2,647)	(4,366)	(3,055)	(3,342)
Others	3,016	2,977	2,879	3,809
CF from investing activities	6,026	(4,140)	(722)	(299)
Inc/(dec) in loan funds	(1,614)	-	-	-
Dividend paid & dividend tax	(25,137)	(39,095)	(42,529)	(46,265)
Others	(21,785)	-	-	-
CF from financing activities	(48,536)	(39,095)	(42,529)	(46,265)
Net Cash flow	1,828	7,125	12,965	14,609
Exchange difference	65	-	-	-
Opening Cash	7,123	9,016	16,141	29,107
Closing cash and Bank	9,016	16,141	29,107	43,715

Source: Company, ICICI Direct Research

Exhibit 4: Balance Sheet				
	₹ crore			
(Year-end March)	FY24	FY25E	FY26E	FY27E
Liabilities				
Equity Capital	362	362	362	362
Reserve and Surplus	90,127	1,00,305	1,13,085	1,28,242
Share Premium	0	0	0	0
Total Shareholders funds	90,489	1,00,667	1,13,447	1,28,604
Total debt	8,021	8,121	8,235	8,397
Other liabilities & Provisions	1,533	1,920	1,997	2,105
Deferred tax liability(net)	977	977	977	977
Minority Interest / Others	830	1,069	1,289	1,549
Total Liabilities	1,01,850	1,12,753	1,25,945	1,41,632
Assets				
Net assets & CWIP	19,336	18,519	16,070	13,391
Goodwill	1,832	1,832	1,832	1,832
Other non current assets	12,297	15,047	15,594	16,360
Debtors	44,434	47,372	50,766	55,531
Loans and Advances	642	684	733	802
Other Current Assets	27,411	29,224	31,317	34,256
Current Investments	31,481	31,481	31,481	31,481
Cash	9,016	16,141	29,107	43,715
Trade Payable	9,981	10,641	11,403	12,474
OCL & Provisions	34,618	36,907	39,551	43,263
Application of Funds	1,01,850	1,12,753	1,25,945	1,41,632

Source: Company, ICICI Direct Research

Exhibit 5: Key ratios				
(Year-end March)	FY24	FY25E	FY26E	FY27E
Per share data				
Adjusted EPS (Diluted)	125.9	136.2	152.9	169.8
BV per share	250.0	278.1	313.4	355.3
DPS	73.0	108.1	117.6	127.9
Cash Per Share	24.9	44.6	80.4	120.8
Operating Ratios (%)				
EBIT margins	24.2	24.7	26.0	26.2
PBT Margins	25.7	25.8	27.0	27.5
PAT Margin	19.1	19.2	20.1	20.4
Debtor days	67	67	67	67
Creditor days	15	15	15	15
Return Ratios (%)				
RoE	50.7	48.9	48.8	47.8
RoCE	60.9	58.9	59.1	58.4
RoIC	95.1	97.3	109.5	118.7
Valuation Ratios (x)				
P/E	33.9	31.5	28.1	25.3
EV / Net Sales	6.3	5.9	5.5	4.9
Market Cap / Sales	6.5	6.1	5.7	5.2
Solvency Ratios				
Debt / EBITDA	0.1	0.1	0.1	0.1
Debt / Equity	0.1	0.1	0.1	0.1
Current Ratio	1.6	1.6	1.6	1.6
Quick Ratio	1.6	1.6	1.6	1.6

Source: Company, ICICI Direct Research

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