11 December 2023

Company Update | Sector: Technology

Wipro

BSE SENSEX	S&P CNX
69,929	20,997

Bloomberg	WPRO IN
Equity Shares (m)	5693
M.Cap.(INRb)/(USDb)	2184.3 / 26.2
52-Week Range (INR)	444 / 352
1, 6, 12 Rel. Per (%)	1/-8/-10
12M Avg Val (INR M)	1980

Financials & Valuations (INR b)

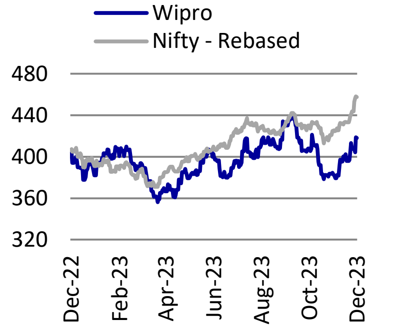
Y/E MARCH	FY23	FY24E	FY25E
Sales	905	894	962
EBIT Margin (%)	15.4	14.6	15.6
PAT	114	106	122
EPS (INR)	20.7	19.6	23.1
EPS Gr. (%)	(5.5)	(5.5)	18.2
BV/Sh. (INR)	142.7	142.0	141.0
Ratios			
RoE (%)	15.8	13.8	16.4
RoCE (%)	12.8	11.1	13.2
Payout (%)	4.8	104.4	90.0
Valuations			
P/E (x)	20.2	21.4	18.1
P/BV (x)	2.9	3.0	3.0
EV/EBITDA (x)	11.8	11.8	10.2
Div. Yield (%)	0.2	4.9	5.0

Shareholding pattern (%)

As On	Sep-23	Jun-23	Sep-22
Promoter	72.9	72.9	73.0
DII	8.0	7.6	8.0
FII	9.0	8.7	9.1
Others	10.0	10.8	10.0

FII Includes depository receipts

Stock Performance (1-year)



CMP: INR420 | TP: INR460 (+10%) | Neutral

Consulting exposure and muted expectation offer potential recovery play

Maintain Neutral as we await macro visibility

Wipro's (WPRO) business performance has been lackluster over the last six quarters, following a robust FY22 performance after Thierry Delaporte assumed the role of CEO in Jul-20. The demand softness in key verticals (BFSI and Consumer) and high exposure to discretionary Consulting vertical (especially Capco) have weighed on WPRO's operational performance, despite significant internal changes to improve decision making and refresh business leadership. Improvement in large deal wins and quarterly deal TCV (USD 1b+) indicate that these strategies are proving to be effective despite challenging macroeconomic conditions. While there is limited clarity on the timeline for macro recovery in key markets, easing inflation and lower interest rates might encourage the release of discretionary spends. Given the high consulting exposure (c15% of revenues), WPRO should be among the early names to benefit from a demand revival. This can act as an upside surprise for a stock with low expectations and large valuation gap with peers (16%/23% discount to large cap/overall peer median FY25 P/E).

We continue to see weak near-term performance (revenue decline of 4.4% CC in FY24E), followed by a recovery of 7.3% CC in FY25E, but keep a close watch on macro recovery and discretionary spend revival. We maintain NEUTRAL with a TP of INR 460 (premised on 20x FY25E EPS).

Macro recovery to fuel consulting service growth

- WPRO's inorganic investments in building consulting capabilities have been instrumental in stimulating growth from key Business Units (BUs) before the macro headwinds impaired its growth in 2HFY23. Wipro clocked ~4% CQGR between 1QFY21 and 2QFY23
- The company's notable acquisitions (on consulting) strengthen cross-functional capabilities on both horizontal (Rizing on SAP) and vertical fronts (Capco on BFSI). The discretionary nature of spend has impacted its key verticals, BFSI and Consumer (~50% of revenue) and consulting service lines (~15% of revenue). However, these segments are expected to regain their earlier growth trajectory once macroeconomic recovery takes place.
- WPRO has demonstrated robust performance in its BFSI and Consumer verticals, achieving a ~10% CAGR each between FY18 and FY23. This growth notably surpasses its Consol revenue CAGR of 6.1% over the same period.
- Additionally, the client-facing account executives with individual P&L responsibilities are enabling deeper client mining and gaining higher wallet share. WPRO's investments in overhauling leadership team and restructuring management hierarchy are incentivizing in terms of improving deal TCVs (quarterly run-rate still remains elevated at USD1b+).

Mukul Garg – Research analyst (Mukul.Garg@MotilalOswal.com)
Pritesh Thakkar – Research analyst (Pritesh.Thakkar@motilaloswal.com)

Earlier investments to get incentivized

- WPRO is doubling down on improving its operating margin, which faced a decline due to inorganic investments. The company is strategically adjusting the margins of acquired business units to align with those of the Core business.
- Many of these acquired entities are operating on a meaningful onshore model. The company is adopting a calibrated approach to redefine offshore-led business mix.
- The company continues to rationalize its employee pyramid mix with incremental fresher hiring (FY23 witnessed 22k fresher additions), which is resulting in limited usage of subcon and trimming down average employee cost.
- Additionally, the company is capitalizing on the improving supply-led challenges, and mitigating the cost of expensive resources (subcon or lateral hires), which typically command a premium of 25-30% over existing talent.
- The company has further scope for margin improvement through pyramid rationalization, utilization, and offshoring. We remain conservative and forecast IT Service EBIT margin of 17.0% in FY25E, lower-end of the medium-term guided range (17%-17.5%).

Attractive payout yield and Cash Conversion

- Wipro has maintained a consistent capital allocation policy and continued to return a substantial portion (three-year trailing 40-50% of net income) of its cash generation.
- It has maintained healthy balance sheets with robust net cash & equivalents-to-market cap ratio of ~9% in 1HFY24.
- Given its strong operating cash conversion rate (90%+) and minimal capex, we expect Wipro to maintain a robust cash payout policy, encompassing both dividends and buybacks.

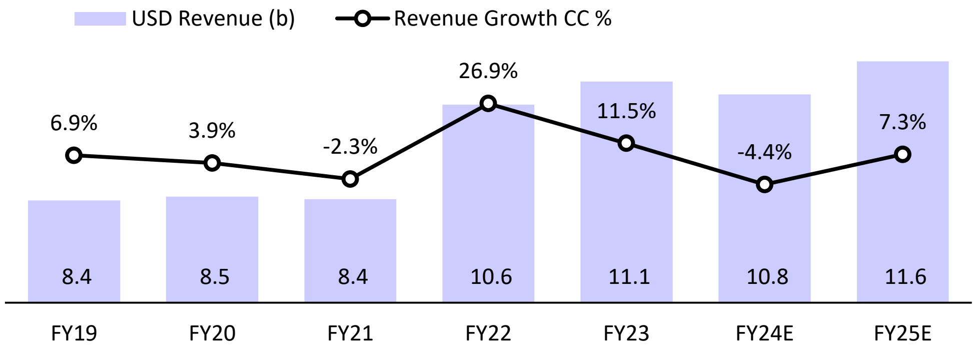
Valuation and View – Maintain Neutral

- WPRO had undergone structural changes while overhauling its key leadership team and making bold investments to acquire inorganic capabilities. We expect the revenue conversion to improve once the macro challenges recede and enterprises resume their discretionary IT spends.
- It is doubling down its efforts to improve margins. Although the company has witnessed partial recovery post the inorganic investments, it is making further efforts to turnaround and improve the margin profile of the acquired entities.
- We expect an FY24E/FY25E USD revenue decline of -4.4%/+7.3% CC YoY with FY24E/FY25E IT Service margin at 15.7%/17.0% (vs. the guided range of 17%-17.5%).
- We believe that the current valuation of 18x FY25E EPS is relatively inexpensive and can improve once the macroeconomic environment improves. We keep a close watch on macro recovery and the discretionary spends before we turn positive on the name. We remain NEUTRAL with a TP of INR 460 (premised on 20x FY25E EPS).

Macro factors mislead the near-term performance

WPRO's revenue performance had inherently been weak over the past couple of years between FY15 and FY20 (CAGR of 2.9%), which was primarily attributed to the structural instability and meaningful dependency on legacy portfolio. Additionally, the company had struggled to keep pace with its peers in transitioning to digital and cloud services, areas which early adopters reaped significant benefits during the same period. However, the company's bold investments in overhauling key leadership team and building front-end capabilities (in FY21) have started incentivizing in terms of delivering sustainable performance.

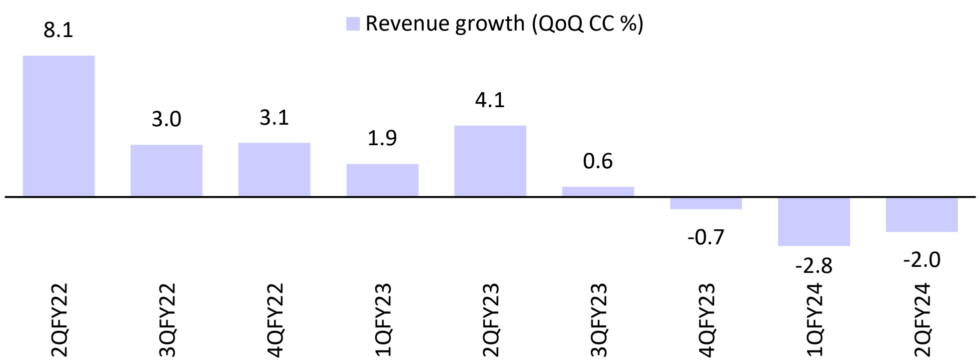
Exhibit 1: USD Revenue and CC revenue growth (%)



Source: MOFSL, Company

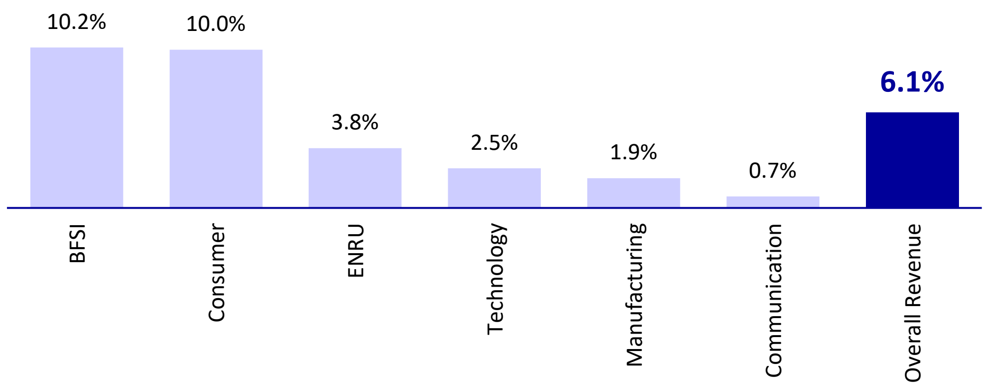
The strategic inorganic investments in consulting capabilities (such as Capco and Rizing) effectively complemented its IT service line, fostering sustainable growth until it encountered headwinds amid macroeconomic challenges in 2HFY23, subsequently contributing to a negative trajectory in 1QFY24. The discretionary nature of consulting service is adversely impacting the near-term growth over the last three quarters. Despite the slower revenue conversion due to project deferrals and delayed ramp-ups, the large deal signing activities have continued its pace with elevated BTB at 0.5x in 2QFY24.

Exhibit 2: Revenue growth QoQ CC (%)



Source: MOFSL, Company

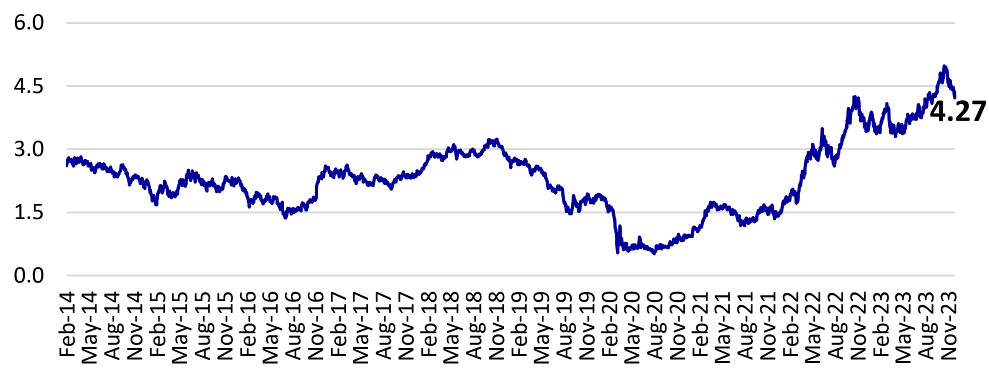
Exhibit 3: Performance CAGR FY18-FY23 (%)



Source: MOFSL, Company

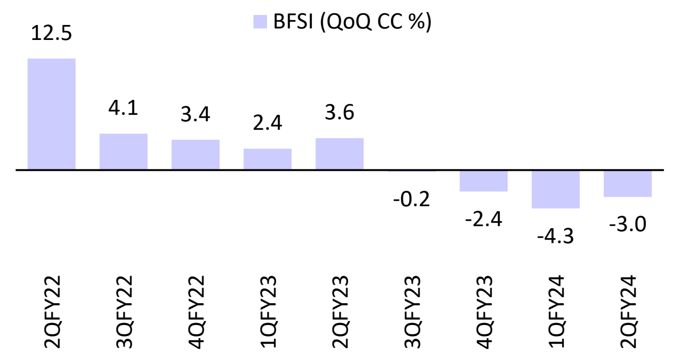
WPRO has established deep presence and built robust capabilities under BFSI and Consumer verticals with strong foothold around adjacencies. Additionally, the BFSI-led (Capco) consulting capabilities have been instrumental in executing end-to-end solutions with comprehensive value offerings. WPRO has demonstrated robust performance for BFSI and Consumer verticals by achieving ~10% CAGR each between FY18 and FY23 and outpacing its Consol revenue CAGR of 6.1%. The current demand weakness in key economies is impacting the near-term performance of these two verticals; however, they have a strong potential to outperform peers significantly. We expect these verticals to recover in tandem with macroeconomic improvements and resume their earlier growth trajectory. The reduction in interest rates (Exhibit 4) and controlled inflation should improve the discretionary spends for key geographies (US and Europe). In this scenario, Wipro is well-positioned to reap the most benefits, particularly within its consulting service lines.

Exhibit 4: US 10-y Interest rate has started moderating in last few weeks



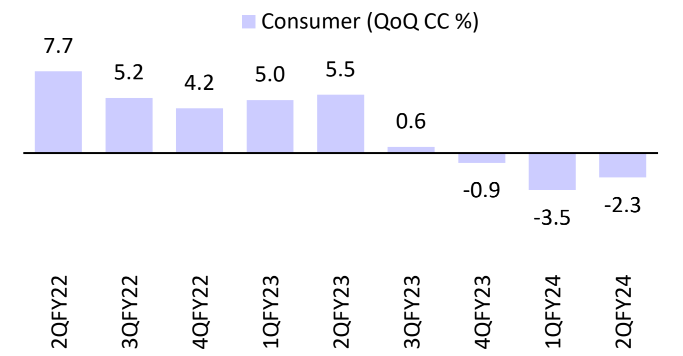
Source: MOFSL, FRED

Exhibit 5: BFSI revenue growth QoQ CC (%)



Source: Company, MOFSL

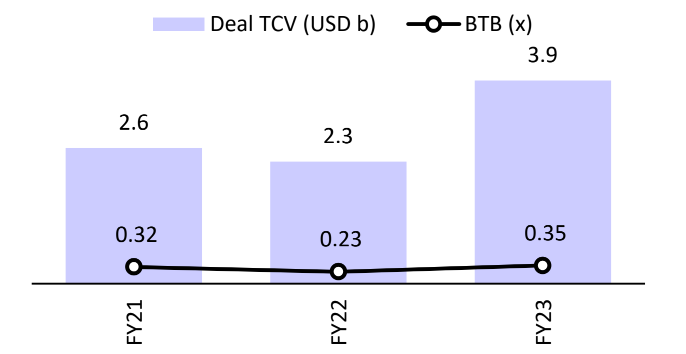
Exhibit 6: Consumer revenue growth QoQ CC (%)



Source: Company, MOFSL

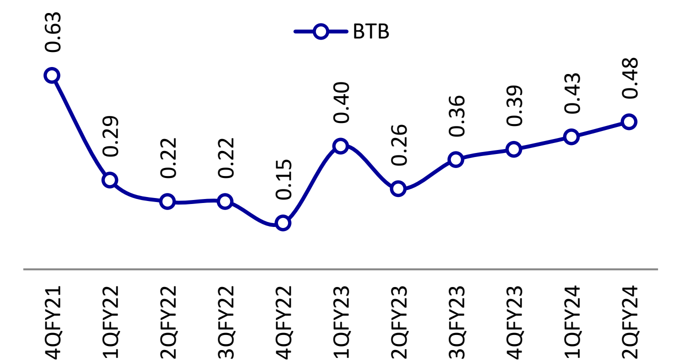
The sustained deal TCV (quarterly run-rate of USD1b) and elevated BTB provide strong revenue visibility with enterprises' intent to spend in the mid-long term. We believe that the integration of consulting businesses is enabling better cross-selling and delivering bundled offerings to accounts that are strategic in nature and are scalable. We believe, once the macro headwinds recede, WPRO would get benefited from the improvement in demand recovery and ramp ups in consulting service lines, which are anchored to key verticals: BFSI and Consumer, together contributing ~50%+ to its overall revenues.

Exhibit 7: Improving deal TCVs



Source: Company, MOFSL

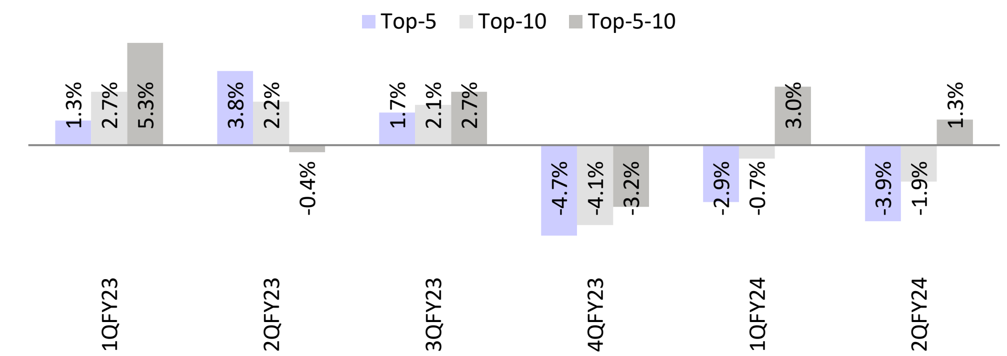
Exhibit 8: Q2 BTB (X) stayed elevated



Source: Company, MOFSL

The top-5 accounts have contributed meaningfully to its topline growth with ~4.7% CQGR between 1QFY22 and 2QFY23 (before macro impacts) vs 0.43% CQGR between 2QFY22 and 2QFY24. WPRO's operational restructuring of 4X4 Strategic Market Units (SMUs) and Global Business Lines (GBLs) have streamlined its execution strategy through better cross-selling carried through its top accounts. Additionally, the investments in global account executives (GAE) are addressing the long-standing issues of client mining and retention activities. We believe, the combination of regional and functional capabilities would further broaden its revenue stream and gain meaningful wallet share through strategic accounts.

Exhibit 9: Growth (%) from top accounts

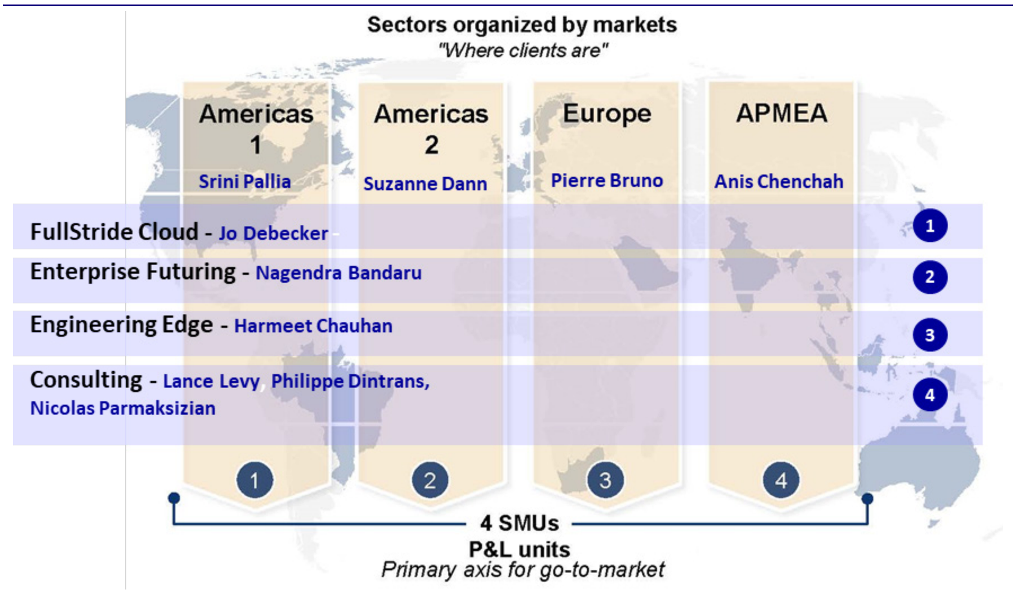


Source: MOFSL, Company

Wipro's functional capabilities through Global Business Lines (GBLs):

- **FullStride Cloud: Jo Debecker is leading the segment.** It offers an entire suit of cloud capabilities: cloud native applications, cloud architecture, and migration.
- **Enterprise Futuring: Nagendra Bandaru is leading the segment.** The business line aims to drive business transformation by seamlessly integrating enterprise solutions with new technologies, focusing on areas such as intelligent insights and data, application platforms, digital operations, and cybersecurity.
- **Engineering Edge: Harmeet Chauhan is leading Wipro Engineering Edge.** He is responsible for scaling and strengthening Wipro's capabilities in technologies such as 5G, Industry 4.0, IoT (Internet of Things), Silicon Design and Embedded System.
- **Consulting: The objective is to bring the organic and acquired segments under a singular entity, Wipro Consulting.** This unified domain and consulting business, comprising Capco led by Philippe Dintrans, Designate led by Lance Levy, and Designate led by Nicolas Parmaksizian, aims to streamline operations and enhance synergy across the organization.

Exhibit 10: Cross-Functional structure with dedicated accounts heads and individual P&L responsibility

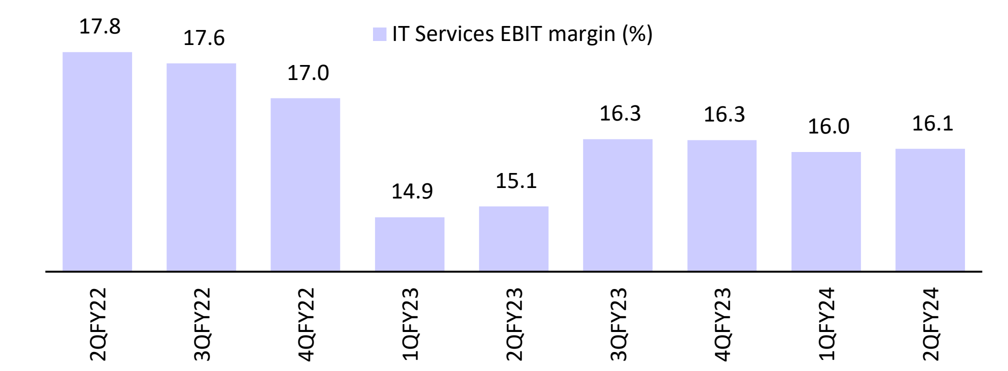


Source: MOFSL, Company

Investments are yet to get materialized

WPRO has stabilized its margins and largely absorbed the dent it has created through investing in inorganic capabilities and pyramid rationalization initiatives in FY23. The company is putting incremental efforts to turnaround the inorganic bets, while realigning them with Consol level margins. Several of the acquired entities operate with meaningful onshore models, prompting the company to adopt a measured approach in redefining the offshore-led business mix. Additionally, the company is capitalizing on the improving supply-led challenges, and mitigating the cost of expensive resources (subcon or lateral hires), which typically command a premium of 25-30% over existing talent.

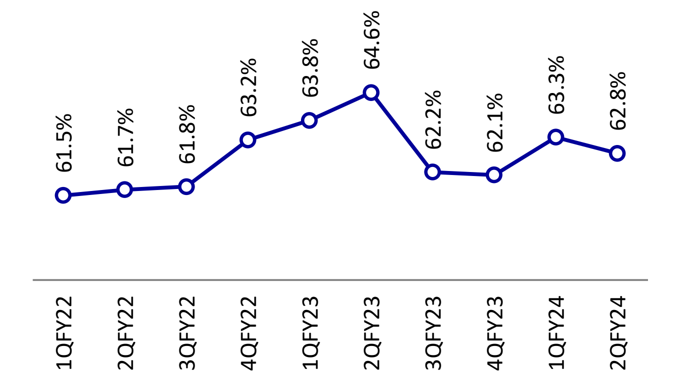
Exhibit 11: Margins to see gradual recover in FY25E (%)



Source: MOFSL, Company

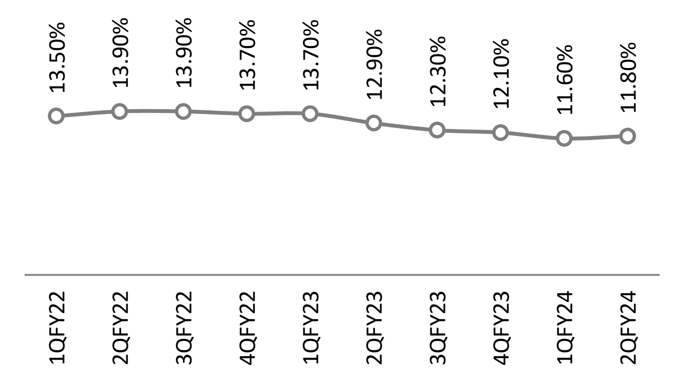
Additionally, the usage of subcontractors is cooling off gradually with easing supply-led challenges and improving attritions. The subcontractors' percentage of revenue stood at 11.8% in 2Q. WPRO continues to streamline its employee pyramid with a large number of fresher recruitment. It hired 22k fresher (gross) in FY23, reflecting the declining utilization rate during the period. We expect a notable potential for utilization levels to improve from their current state level as these freshers integrate into the billing cycle. Further, a gradual reduction in attrition rates and decreased reliance on subcontracting are expected to support margins in FY25E.

Exhibit 12: Employee costs % of revenue



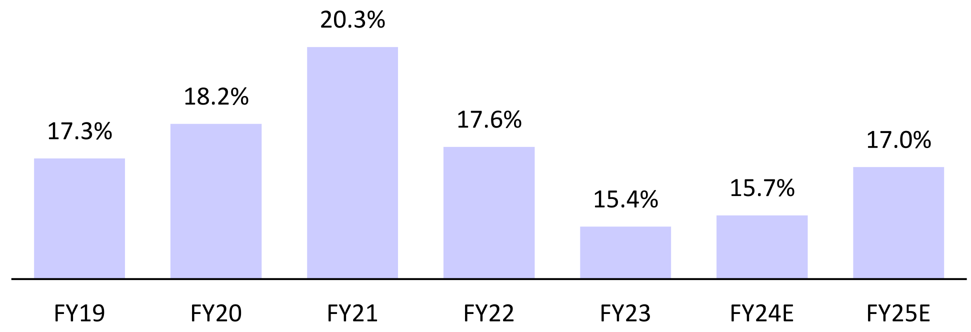
Source: Company, MOFSL

Exhibit 13: Subcon cost % of revenue



Source: Company, MOFSL

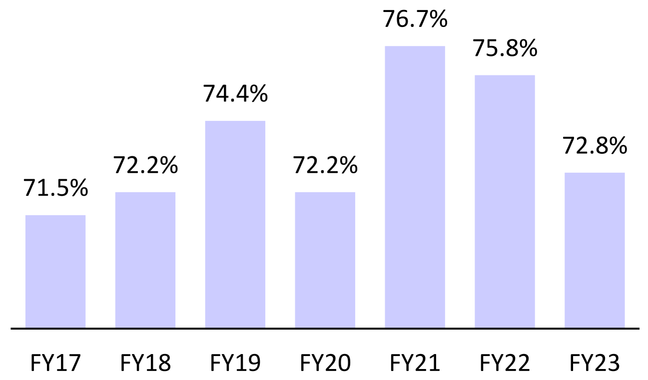
Exhibit 14: IT Service EBIT Margins to see recover in FY25E (%)



Source: MOFSL, Company

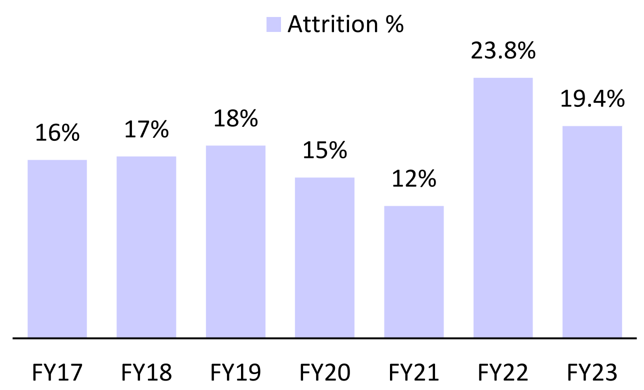
The company is leveraging multiple margin levers: Fixed price contract mix, utilization, and fixed costs. It believes that it has further room for improvement in utilization for the rest of the year. It aspires to reach 17-17.5% operating margin in the medium term and it continues to progress toward achieving the thresholds, but it's the near-term uncertainty, which is weighing on the improvement. We forecast FY24/FY25 IT services segment margins to be at 15.7%/17.0%, lower-end of the management's medium-term guided range, that translates into a 3.9% INR PAT CAGR over FY23-25.

Exhibit 15: Utilization %



Source: Company, MOFSL

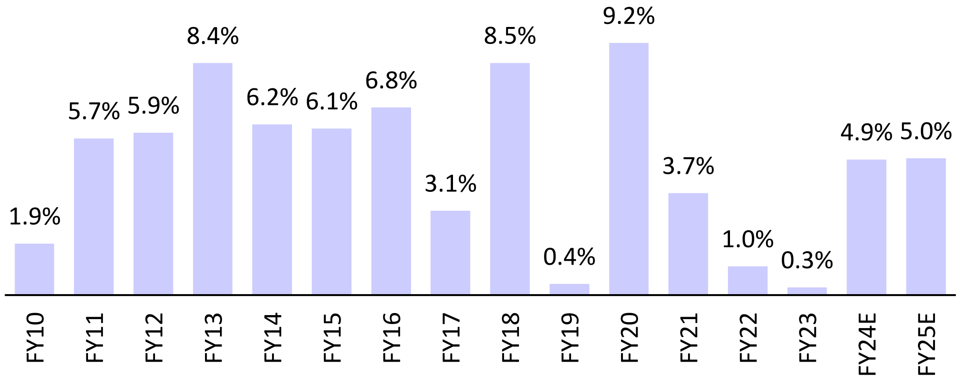
Exhibit 16: Attrition %



Source: Company, MOFSL

Attractive payout yield

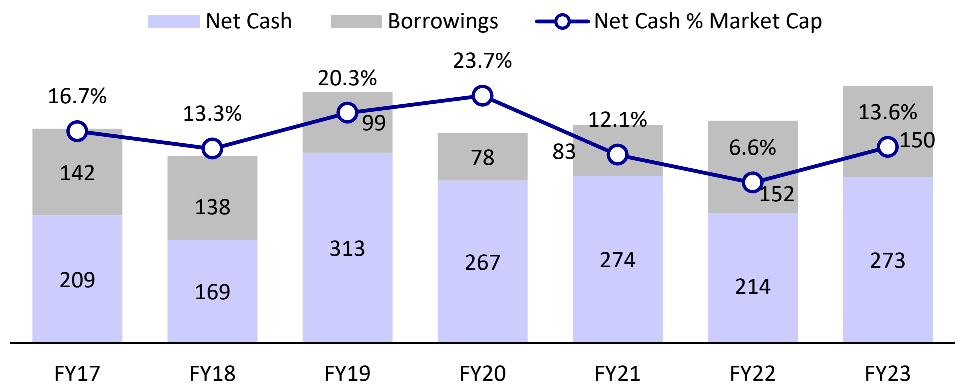
Exhibit 17: Payout Yield (%)



Source: MOFSL, Company

- Wipro has maintained consistent capital allocation policies and continued to return a substantial portion (40-50% of Net Income) of its cash generation throughout the year.
- Wipro has maintained healthy balance sheets with robust net cash & equivalents-to-market cap ratio of ~9% in 1HFY24.
- Given its strong operating cash conversion rate (90%+) and minimal capex, we expect Wipro to maintain a robust cash payout policy, encompassing both dividends and buybacks.

Exhibit 18: Healthy Net Cash % MCap



Source: MOFSL, Company

Valuation and View – Maintain Neutral

- WPRO had undergone structural changes while overhauling its key leadership team and making bold investments to acquire inorganic capabilities. We expect the revenue conversion to improve once the macro challenges recede and enterprises resume their discretionary IT spends.
- It is doubling down its effort to improve margins. Despite witnessing some recovery following the inorganic investments, the company is committed to putting further efforts toward a complete turnaround, specifically aiming to enhance the margin profile of the acquired entities.
- We expect an FY24E/FY25E USD revenue decline of -4.4%/+7.3% CC YoY with FY24E/FY25E IT Service margin at 15.7%/17.0% (vs. the guided range of 17%-17.5%).
- We believe that the current valuation of 18x FY25E EPS is relatively inexpensive and can improve once the macroeconomic environment improves. We keep a close watch on macro recovery and the discretionary spends before we turn positive on the name. We reiterate our NEUTRAL rating on the stock with a TP of INR 460 (premised on 20x FY25E EPS).

Exhibit 19: 1-Year forward P/E Chart

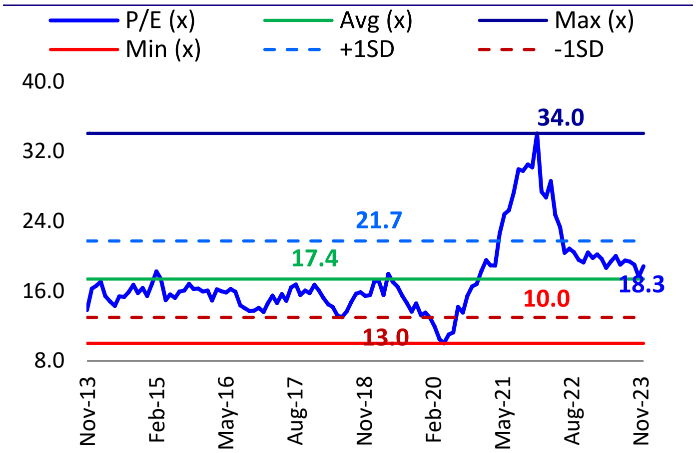
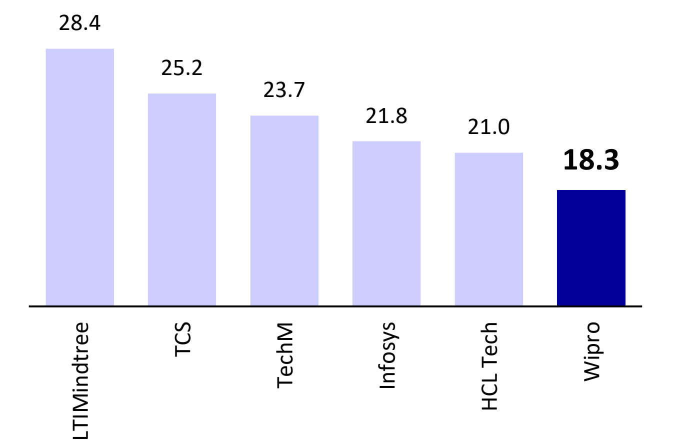


Exhibit 20: Peer comparison - 1-Year forward P/E (x)



Financials and valuations

Income Statement								(INR b)
Y/E March	**FY18**	**FY19**	**FY20**	**FY21**	**FY22**	**FY23**	**FY24E**	**FY25E**
Sales	**545**	**586**	**610**	**619**	**791**	**905**	**894**	**962**
Change (%)	-1.0	7.5	4.2	1.5	27.7	14.4	-1.2	7.6
Operating Costs	386	413	436	423	556	645	640	682
SG&A	75	75	69	73	97	120	124	130
EBITDA	**105**	**117**	**126**	**151**	**169**	**173**	**163**	**186**
As a percentage of Net Sales	19.3	19.9	20.6	24.3	21.4	19.1	18.2	19.3
Depreciation and Amort.	21	19	21	28	31	33	33	36
EBIT	**84**	**97**	**105**	**123**	**138**	**140**	**130**	**150**
Margin	15.5	16.6	17.2	19.8	17.5	15.4	14.6	15.6
Other Income	18	18	17	16	13	8	10	12
PBT	**102**	**115**	**123**	**139**	**151**	**148**	**140**	**162**
Tax	22	25	25	30	29	34	34	39
Rate (%)	21.8	21.9	20.2	21.8	19.1	23.0	24.0	24.0
PAT	**80**	**90**	**98**	**109**	**122**	**114**	**107**	**123**
Minority Interest	0	0	0	1	0	0	1	1
Adjusted PAT	**80**	**90**	**97**	**108**	**122**	**114**	**106**	**122**
Change (%)	-5.7	12.4	8.0	11.0	13.2	-7.1	-6.7	15.6

Balance Sheet								(INR b)
Y/E March	**FY18**	**FY19**	**FY20**	**FY21**	**FY22**	**FY23**	**FY24E**	**FY25E**
Share Capital	9	12	11	11	11	11	11	11
Reserves	474	556	546	542	647	770	741	727
Net Worth	**483**	**568**	**557**	**553**	**658**	**781**	**752**	**738**
Minority Interest and others	19	22	38	41	56	66	54	58
Loans	138	99	78	83	152	150	140	130
Capital Employed	**640**	**690**	**674**	**677**	**866**	**997**	**946**	**926**
Gross Block	194	220	268	299	338	369	383	402
Less: Depreciation	130	149	170	198	228	262	295	330
Net Block	64	71	98	102	110	107	88	71
Investments	13	13	11	12	20	22	22	22
Intangible Assets	136	131	147	152	291	351	351	351
Other non-current assets	41	47	41	42	38	35	50	54
Curr. Assets	**506**	**572**	**520**	**523**	**621**	**661**	**689**	**698**
Debtors	143	123	130	121	176	187	184	198
Inventories	3	4	2	1	1	1	1	1
Cash and Bank Balance	45	159	144	170	104	92	103	73
Adv., Other Current Assets	65	46	54	55	98	72	72	77
Investments	249	240	190	176	242	309	329	349
Current Liab. and Prov.	**121**	**143**	**143**	**154**	**213**	**179**	**254**	**269**
Net Current Assets	**386**	**429**	**377**	**369**	**408**	**482**	**436**	**429**
Application of Funds	**640**	**690**	**674**	**677**	**866**	**997**	**946**	**926**

E: MOFSL estimates

Financials and valuations

Ratios								
Y/E March	**FY18**	**FY19**	**FY20**	**FY21**	**FY22**	**FY23**	**FY24E**	**FY25E**
Basic (INR)								
EPS	**12.5**	**14.6**	**16.4**	**18.8**	**21.9**	**20.7**	**19.6**	**23.1**
Cash EPS	16.0	18.2	20.2	23.9	27.9	26.8	26.0	30.1
Book Value	76.5	94.8	95.6	97.9	120.4	142.7	142.0	141.0
DPS	1.0	1.0	1.0	1.0	6.0	1.0	20.4	20.8
Payout (%, Div+Buyback)	145.3	6.7	113.9	93.3	26.9	4.8	104.4	90.0
Valuation (x)								
P/E ratio	33.5	28.7	25.5	22.3	19.1	20.2	21.4	18.1
Cash P/E ratio	26.2	23.0	20.7	17.5	15.0	15.6	16.1	13.9
EV/EBITDA ratio	23.6	18.9	17.4	14.0	12.4	11.8	11.8	10.2
EV/Sales ratio	4.6	3.8	3.6	3.4	2.7	2.3	2.2	2.0
Price/Book Value ratio	5.5	4.4	4.4	4.3	3.5	2.9	3.0	3.0
Dividend Yield (%)	0.2	0.2	0.2	0.2	1.4	0.2	4.9	5.0
Profitability Ratios (%)								
RoE	16.0	17.1	17.3	19.4	20.2	15.8	13.8	16.4
RoCE	11.9	13.1	13.7	16.0	16.3	12.8	11.1	13.2
Turnover Ratios								
Debtors (Days)	96	77	78	72	81	75	75	75
Asset Turnover ratio (x)	0.7	0.7	0.7	0.8	0.8	0.8	0.8	0.8

Cash Flow Statement								(INR b)
Y/E March	**FY18**	**FY19**	**FY20**	**FY21**	**FY22**	**FY23**	**FY24E**	**FY25E**
CF from Operations	85	89	124	125	147	145	139	158
Cash for Wkg. Capital	-1	27	-24	23	-36	-15	51	-3
Net Operating CF	**84**	**116**	**101**	**148**	**111**	**131**	**190**	**155**
Net Purchase of FA	-21	-21	-22	-19	-19	-14	-13	-19
Other change in investments	56	71	56	27	-205	-70	-20	-20
Net Cash from Invest.	**36**	**50**	**34**	**8**	**-224**	**-84**	**-33**	**-39**
Issue of Shares/Other adj	0	0	0	0	0	0	0	0
Proceeds from LTB/STB	-14	-44	-143	-122	53	-28	-19	-19
Dividend Payments	-116	-5	-8	-6	-7	-33	-127	-128
Net CF from Finan.	**-130**	**-49**	**-151**	**-129**	**47**	**-61**	**-145**	**-146**
Free Cash Flow	64	95	78	129	91	116	177	135
Net Cash Flow	**-10**	**117**	**-16**	**26**	**-67**	**-14**	**12**	**-31**
Forex difference	0	1	2	-1	1	2	0	0
Opening Cash Bal.	**49**	**39**	**157**	**142**	**168**	**102**	**90**	**102**
Add: Net Cash	-10	118	-14	26	-66	-12	12	-31
Closing Cash Bal.	**39**	**157**	**142**	**168**	**102**	**90**	**102**	**71**

E: MOFSL estimates

Explanation of Investment Rating	
Investment Rating	**Expected return (over 12-month)**
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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Grievance Redressal Cell:

Contact Person	Contact No.	Email ID
Ms. Hemangi Date	022 40548000 / 022 67490600	query@motilaloswal.com
Ms. Kumud Upadhyay	022 40548082	servicehead@motilaloswal.com
Mr. Ajay Menon	022 40548083	am@motilaloswal.com

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