

March 24, 2020

Tata Consultancy Services Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term/Short-term Fund-based Limits	200.0	200.0	[ICRA]AAA(Stable)/[ICRA]A1+; reaffirmed
Long-term/Short-term Non-fund Based Limits	5,000.0	5,000.0	[ICRA]AAA(Stable)/[ICRA]A1+; reaffirmed
Long-term/Short-term Fund-based/Non-fund Based	1,800.0	1,800.0	[ICRA]AAA(Stable)/[ICRA]A1+; reaffirmed
Total	7,000.0	7,000.0	

*Instrument details are provided in Annexure-1

Rationale

The ratings favourably factor in Tata Consultancy Services Limited's (TCS) leading position among Indian players in the global information technology (IT) and IT enabled services (ITeS) outsourcing segment, its diversified and growing client base, wide range of services offered, scale of operations and strong financial profile characterised by healthy revenue growth and recurring cash accruals and strong liquidity in the form of free cash reserves. The ratings continue to draw comfort from the company's presence in diversified verticals and solid execution track record, which has helped it build scale. TCS' key vertical, banking, finance services and insurance (BFSI), reported subdued growth in the current fiscal (BFSI growth decelerated to 5.3% in Q3 FY2020 from 9.2% in Q1 FY2020) due to lower spending by large banks across North America and the UK and deflationary pressure due to the increased use of automation and machine learning. Despite this, the company is confident of the vertical's prospects in the medium to long term, given the recent deal closures, its strong expertise and ability to participate in large digital transformation deals. The BFSI vertical's resilient performance during past periods of turmoil demonstrates the strength of TCS' business and the goodwill it enjoys from its clients. ICRA notes that the growth of traditional services and Indian IT services sector companies has been constrained by disruption due to cloud adoption, a sharp shift towards digital services and intense competition from local as well as international players. However, with its early investments in digital services, TCS has been able to capture higher spends on digital technologies. Further, the company's integrated service offerings, backed by its own intellectual property rights (IPRs) and domain knowledge, have helped it participate in and execute large deals, thus enabling it to withstand competitive pressure. The above factors combined with the continued cost benefit through the outsourcing model have resulted in market share gains for the company. TCS' continued ability to win a higher share in digital technologies will remain critical to drive its growth.

The Indian IT services industry continues to face geopolitical uncertainties such as proposed legislations on restricting outsourcing or immigration in its key markets, which may have an adverse impact on the current business model of the industry. The demand for IT services remains exposed to macro-economic uncertainties such as a growth slowdown in key markets in the US and Europe and the Brexit-related challenges, which may pose a challenge to the Indian IT services industry. The fallout from the ongoing coronavirus outbreak may also have a bearing on the company's operating performance in the near term.

The margins for the Indian IT services companies will continue to reflect the challenging operating environment characterised by pressure on commoditised IT services, wage inflation, and higher onsite costs necessitated by visa curbs leading to increased local hiring as well as lower discretionary spend by corporate firms. These risks are, however, mitigated by TCS' large scale of operations, diversified customer base across geographies and established presence in the IT services business. ICRA also notes its ability to generate operational efficiencies to counter such pressures. Further, the company's liquidity profile remains strong, given the cash and equivalents balance of Rs. 43,136 crore as on December 31, 2019, and the low capital expenditure requirements, which provide a buffer against any short-term fluctuations. However, its liquid reserves will remain sensitive to the level of dividend payouts and further buybacks, if any.

Key rating drivers and their description

Credit strengths

Largest Indian company in global IT services outsourcing segment; remains competitive given its access to large technical talent pool and cost advantages in India – With a scale of Rs. 1,46,463 crore in FY2019 (\$20.9 billion), TCS is the largest Indian company in the global IT services outsourcing industry lending scale efficiencies. Indian IT services companies, including TCS, continue to benefit from India's massive educated workforce that provides a large technical talent pool resulting in global competitiveness.

Full service capability with increasing share of digital business; proven ability to win and handle large-scale projects globally – The company's ability to offer full service capability has helped it win deals across a wide spectrum of verticals. It has also demonstrated the ability to structure and execute large-scale projects globally, enabling it to continually gain market share over its competitors in the past five fiscals. TCS has made significant organic investments in manpower training and developing capabilities, which has helped it drive high sequential growth in its digital business and win transformational digital deals. This has led to an improvement in the share of its digital business, which stood at 33.2% in Q2 FY2020 against 28.1% in Q2 FY2019.

Diversified client base with high repeat business – The company has a large, diversified and growing client base with meaningful incremental addition of clients in the above \$20 million, \$50-million and \$100-million buckets in previous fiscals. Its superior execution ability has resulted in high repeat business, thus providing stability to the revenue stream.

Robust financial profile, given healthy profitability, cash accruals and robust liquidity position – The company's financial profile remains robust as reflected in its high operating profitability, strong capital structure and robust liquidity position in the form of a strong cash and equivalents balance of Rs. 43,136 crore as on December 31, 2019.

Credit challenges

Slowing revenue growth from traditional outsourcing business; continued ability to win fresh digital business at scale would be critical for future growth – The IT services industry has been facing headwinds in the form of slowing demand for traditional services such as application development and maintenance as well as infrastructure management services (IMS), which have been negatively impacted by cloud computing. Companies are spending more on initiatives built around digital technologies to drive business outcomes. Against this backdrop, TCS' continued ability to win a higher share of digital business at scale would be critical for driving future growth.

Legislation to restrict outsourcing or restriction on immigration such as implementation of the US immigration bill could be detrimental for current business model leading to revenue and margin pressures – In the past three years, there has been uncertainty regarding the US Government’s visa policies towards its non-immigrant and temporary visa programmes such as the H-1B and L1 visas. Any adverse development may prove to be detrimental to TCS’ current business model and will lead to pressure on its revenues and margins. ICRA, nevertheless, notes the company’s increased local hiring across countries, particularly in the US, to mitigate the above risks.

High concentration in BFSI vertical mitigated by track record of consistent performance – The company has a high concentration of revenues, primarily in the BFSI (almost one-third of revenues) segment, although the same is mitigated by its established relationship with clients as well as deep domain knowledge. Demand for the sector had been adversely impacted by the macro-economic conditions affecting the industry, including sustained low interest rates, continued focus on cost optimisation and management of discretionary spends as well as in-sourcing by a few clients for greater operational control. The business is supported by digitisation efforts, cost optimisation, regulatory, compliance and security-driven initiatives. Though there was a recovery in the growth of the BFSI vertical in FY2019, the vertical has again faced headwinds in the form of lower spending by large banks in North America and the UK and deflationary pressure due to automation and machine learning. This has resulted in a deceleration in the growth of the vertical to 5.3% in Q3 FY2020 from 9.2% in Q1 FY2020.

Liquidity position: Superior

TCS has been consistently able to generate strong cash flow from operations supported by its healthy operating profitability and controlled working capital intensity. The company had a robust liquidity position with cash and equivalents of Rs. 43,136 crore as on December 31, 2019. Despite the high dividend payouts and buybacks during the current and past two fiscals, the company’s liquidity is expected to remain strong given the high recurring operating cash flows. However, ICRA has not factored in any material inorganic expansion plan by the company.

Rating sensitivities

Positive triggers – Not applicable

Negative triggers – Pressure could arise in case of a material deterioration in the company’s credit profile because of a sharp decline in its operating performance and/or disproportionate dividend payouts and/or a large debt-funded acquisition.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Information Technology (Services) Industry
Parent/Group Support	Not applicable
Consolidation/Standalone	The ratings are based on the consolidated financial profile of the company. As on December 31, 2019, TCS had 50 subsidiaries that are listed in Annexure-2.

About the company

Established in 1968 as a division of Tata Sons, Tata Consultancy Services Limited is currently the largest Indian IT services company. The company pioneered the concept of offshore IT services in 1974 and emerged as an integrated full service provider with a global footprint. It was listed on the National Stock Exchange (NSE) and the Bombay Stock Exchange (BSE) in August 2004. TCS is a part of the Tata Group, with Tata Sons (rated [ICRA]AAA(Stable)/[ICRA]A1+) holding a 72.02% equity share (as on December 31, 2019) in the company.

TCS offers a rich portfolio of services, which includes consulting and service integration, digital transformation services and cognitive business operations. Based on industry classification, the company has five key verticals: 1) banking, financial services and insurance (BFSI), 2) retail and consumer business, 3) communication, media and technology, 4) manufacturing, and 5) others. The last category includes life sciences and healthcare, technology and services, energy, resources and utilities, and others. TCS has a widespread geographical presence across North America, Latin America, continental Europe, the United Kingdom (UK), India, Asia Pacific, West Asia and Africa.

Key financial indicators (audited)

	FY2018	FY2019
Operating Income (Rs. crore)	1,23,104.0	1,46,463.0
PAT (Rs. crore)	25,880.0	31,562.0
OPBDIT/OI (%)	26.4%	27.0%
RoCE (%)	40.3%	48.2%
Total Outside Liabilities/Tangible Net Worth (times)	0.2	0.2
Total Debt/OPBDIT (times)	0.0	0.0
Interest Coverage (times)	625.3	199.5
DSCR	388.4	161.4

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

	Instrument	Current Rating (FY2020)			Rating History for the Past 3 Years			
		Type	Amount Rated	Amount Outstanding	Rating	FY2019	FY2018	FY2017
					24-Mar 2020	19-Mar 2019	21-Dec-2017	21-Dec-2016
1	Fund-based Limits	Long Term / Short Term	200.0	NA	[ICRA]AAA/[ICRA]A1+	[ICRA]AAA (Stable)/[ICRA]A1+	[ICRA]AAA (Stable)/[ICRA]A1+	[ICRA]AAA (Stable)/[ICRA]A1+
2	Non-fund based Limits	Long Term / Short Term	5,000.0	NA	[ICRA]AAA/[ICRA]A1+	[ICRA]AAA (Stable)/[ICRA]A1+	[ICRA]AAA (Stable)/[ICRA]A1+	[ICRA]AAA (Stable)/[ICRA]A1+
3	Fund-based/Non-fund Based	Long Term / Short Term	1,800.0	NA	[ICRA]AAA/[ICRA]A1+	[ICRA]AAA (Stable)/[ICRA]A1+	[ICRA]AAA (Stable)/[ICRA]A1+	[ICRA]AAA (Stable)/[ICRA]A1+

Amount in Rs. crore

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Long-term/Short-term Fund-based Limits	NA	NA	NA	200.00	[ICRA]AAA/Stable/[ICRA]A1+
NA	Long-term/Short-term Non-fund Based Limits	NA	NA	NA	5,000.0	[ICRA]AAA/Stable/[ICRA]A1+
NA	Long-term/Short-term Fund Based/Non-fund Based	NA	NA	NA	1,800.0	[ICRA]AAA/Stable/[ICRA]A1+

Source: TCS

Annexure-2: List of entities considered for consolidated analysis (as on December 31, 2019)

Company Name	Ownership %	Consolidation Approach
APT Online Limited	89.00	Full consolidation
C Edge Technologies Limited	51.00	Full consolidation
Diligenta Limited	100.00	Full consolidation
MP Online Limited	89.00	Full consolidation
Tata Consultancy Services Canada Inc.	100.00	Full consolidation
Tata America International Corporation	100.00	Full consolidation
Tata Consultancy Services Asia Pacific Pte Ltd.	100.00	Full consolidation
Tata Consultancy Services Belgium SA	100.00	Full consolidation
Tata Consultancy Services Deutschland GmbH	100.00	Full consolidation
Tata Consultancy Services Netherlands BV	100.00	Full consolidation
Tata Consultancy Services Sverige AB	100.00	Full consolidation
TCS FNS Pty Limited	100.00	Full consolidation
TCS Iberoamerica SA	100.00	Full consolidation
Tata Consultancy Services (Africa) (PTY) Ltd.	100.00	Full consolidation
MahaOnline Limited	74.00	Full consolidation
Tata Consultancy Services Qatar S.S.C.	100.00	Full consolidation
TCS e-Serve International Limited	100.00	Full consolidation
TCS Foundation	100.00	Full consolidation
CMC Americas, Inc.	100.00	Full consolidation
W12 Studios Limited	100.00	Full consolidation
TCS Financial Solutions Beijing Co., Ltd.	100.00	Full consolidation
Tata Consultancy Services (China) Co., Ltd.	93.20	Full consolidation
TCS Solution Center S.A.	100.00	Full consolidation
Tata Consultancy Services Argentina S.A.	100.00	Full consolidation
Tata Consultancy Services Do Brasil Ltda	100.00	Full consolidation
Tata Consultancy Services De Mexico S.A., De C.V.	100.00	Full consolidation
Tata Consultancy Services De Espana S.A.	100.00	Full consolidation
TCS Italia s.r.l.	100.00	Full consolidation
Tata Consultancy Services Japan, Ltd. (w.e.f. June 26, 2019)	66.00	Full consolidation

Tata Consultancy Services Malaysia Sdn Bhd	100.00	Full consolidation
Tata Consultancy Services Luxembourg S.A.	100.00	Full consolidation
Tata Consultancy Services (Portugal) Unipessoal, Limitada	100.00	Full consolidation
TCS Inversiones Chile Limitada	100.00	Full consolidation
Tata Consultancy Services Chile S.A.	100.00	Full consolidation
TATASOLUTION CENTER S.A.	100.00	Full consolidation
TCS Financial Solutions Australia Holdings Pty Limited	100.00	Full consolidation
TCS Financial Solutions Australia Pty Limited	100.00	Full consolidation
PT Tata Consultancy Services Indonesia	100.00	Full consolidation
Tata Consultancy Services Switzerland Ltd.	100.00	Full consolidation
Tata Consultancy Services (South Africa) (PTY) Ltd.	100.00	Full consolidation
Tata Consultancy Services (Thailand) Limited	100.00	Full consolidation
Tata Consultancy Services (Philippines) Inc.	100.00	Full consolidation
TCS e-Serve America, Inc.	100.00	Full consolidation
TCS Uruguay S.A.	100.00	Full consolidation
MGDC S.C.	100.00	Full consolidation
Tata Consultancy Services Osterreich GmbH	100.00	Full consolidation
Tata Consultancy Services Danmark ApS	100.00	Full consolidation
Tata Consultancy Services France SA	100.00	Full consolidation
Tata Consultancy Services Saudi Arabia	76.00	Full consolidation
Technology Outsourcing S.A.C.	100.00	Full consolidation

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