

**ADD**

TP: Rs 860 | ▲ 6%

**INFOSYS**

| IT Services

| 12 October 2019

## Guidance signals industrywide growth headwinds

**Infosys (INFO) met expectations with 3.3% QoQ CC revenue growth and 21.7% EBIT margins, delivering a better performance than TCS in Q2FY20. Management's H2 outlook, as inferred from its below-expected revenue guidance and cautious BFSI/retail commentary, echoes the weakening growth trends seen at TCS and signals industrywide challenges ahead. We keep FY21/FY22 EPS estimates broadly unchanged and roll forward to a Sep'20 TP of Rs 860 (Rs 820 earlier). Retain ADD.**

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**In-line operating performance:** INFO's operating performance met expectations, with 3.3% QoQ CC revenue growth and EBIT margins at 21.7%. Revenue growth was aided by a 90bps increase in share of inorganic revenues. Improved utilisation and a better offshore mix supported 120bps QoQ EBIT margin expansion despite the partial impact of a wage hike. Compensation revision for senior management will be effected in Q3FY20.

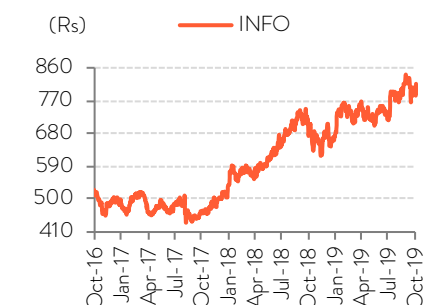
Ticker/Price	INFO IN/Rs 815
Market cap	US\$ 49.9bn
Shares o/s	4,349mn
3M ADV	US\$ 93.4mn
52wk high/low	Rs 847/Rs 600
Promoter/FPI/DII	13%/35%/52%

Source: NSE

**Strong deal wins but largely renewal-led:** Large deal wins held strong at US\$ 2.8bn (up 5% QoQ and 40% YoY), but were shored up by a higher proportion of renewals (at 90% vs. <50% renewal deal contribution in the prior two quarters).

**Revised revenue guidance implies growth moderation in H2:** From 8.5-10% guided earlier, INFO now expects FY20 revenue growth of 9-10% YoY CC, below our expectation of an upward reset to 9.5-10.5%. This implies a CQGR of -0.6% to +0.6% for the remaining two quarters of FY20 vs. +2.4%/+2.2% reported/organic CQGR in the same period last year. In a gloomy readthrough for the sector, we note the trend similarities with TCS, namely a soft BFSI and retail outlook along with growth moderation in H2.

## STOCK PERFORMANCE



Source: NSE

## KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue (Rs mn)	7,05,220	8,26,760	8,91,741	9,78,255	10,82,541
EBITDA (Rs mn)	1,90,100	2,08,890	2,18,425	2,52,046	2,78,916
Adj. net profit (Rs mn)	1,60,280	1,54,170	1,62,781	1,81,375	2,04,186
Adj. EPS (Rs)	36.9	35.4	37.7	42.0	47.3
Adj. EPS growth (%)	17.3	(4.0)	6.6	11.4	12.6
Adj. ROAE (%)	23.9	24.5	25.5	25.6	26.0
Adj. P/E (x)	22.1	23.0	21.6	19.4	17.2
EV/EBITDA (x)	17.5	16.0	15.5	13.2	11.7

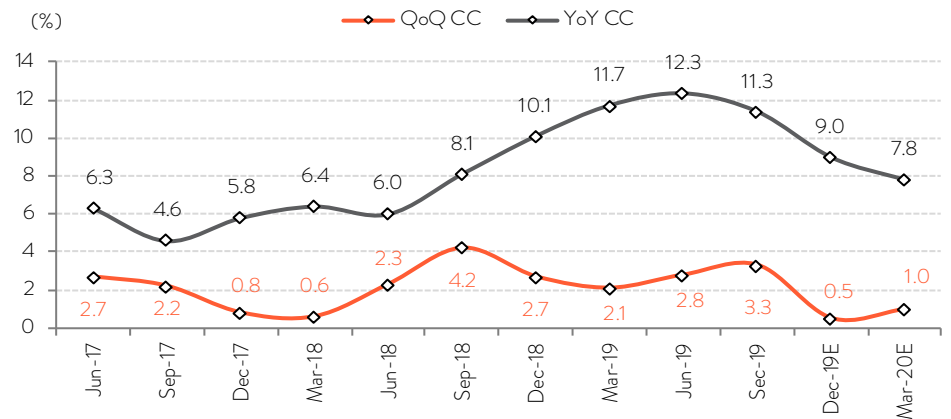
Source: Company, BOBCAPS Research

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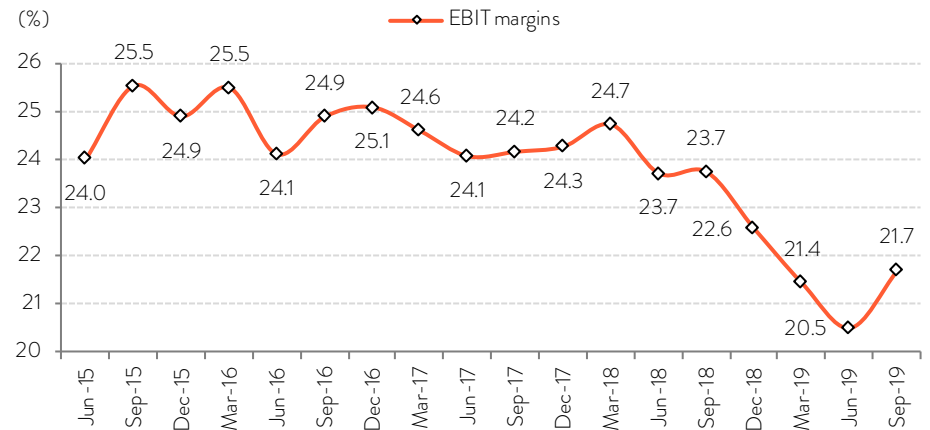


**FIG 1 – REVENUE GUIDANCE BELOW ESTIMATES**



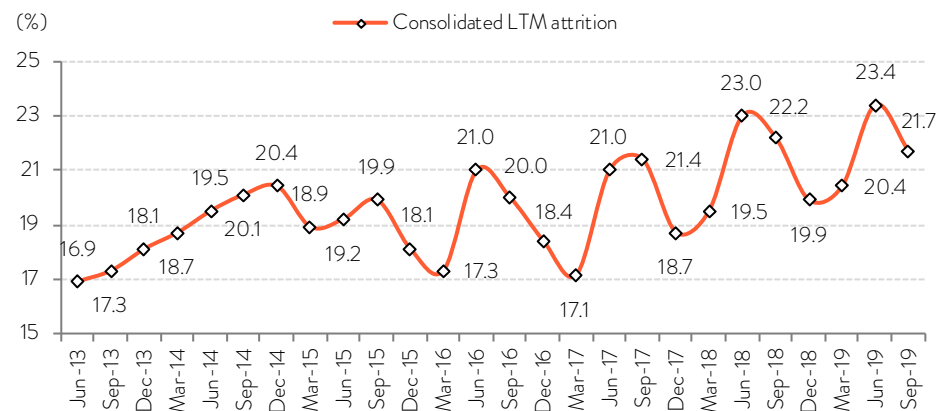
Source: Company, BOBCAPS Research

**FIG 2 – SEQUENTIAL MARGIN IMPROVEMENT AFTER 5 QUARTERS WAS A RESPITE; EBIT MARGIN GUIDANCE FOR FY20 UNCHANGED AT 21-23%**



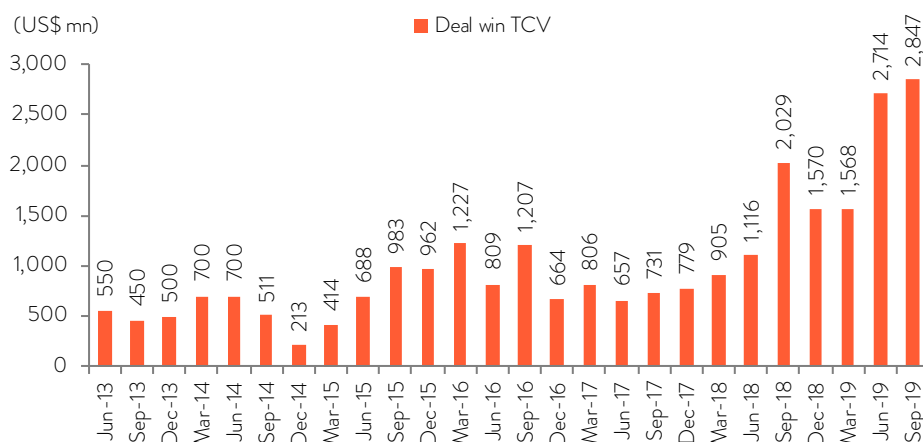
Source: Company, BOBCAPS Research

**FIG 3 – ATTRITION EASED QOQ BUT STILL NOT IN COMFORT ZONE**



Source: Company, BOBCAPS Research

**FIG 4 – US\$ 2.8BN DEAL WINS IN Q2FY20 INCLUDE ONLY 10% NET NEW DEALS; RENEWALS FORM BALANCE 90%**



Source: Company, BOBCAPS Research

**FIG 5 – SEP'19 QUARTER PERFORMANCE**

(Rs mn)	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20	Q2FY20	YoY (%)	QoQ (%)	H1FY19	H1FY20	YoY (%)
<b>Revenue (US\$ mn)</b>	<b>2,831</b>	<b>2,921</b>	<b>2,987</b>	<b>3,060</b>	<b>3,131</b>	<b>3,210</b>	<b>9.9</b>	<b>2.5</b>	<b>5,752</b>	<b>6,341</b>	<b>10.2</b>
<b>Revenue</b>	<b>1,91,280</b>	<b>2,06,090</b>	<b>2,14,000</b>	<b>2,15,390</b>	<b>2,18,030</b>	<b>2,26,290</b>	<b>9.8</b>	<b>3.8</b>	<b>3,97,370</b>	<b>4,44,320</b>	<b>11.8</b>
Operating Exp	1,41,550	1,52,520	1,59,900	1,63,900	1,66,510	1,69,900	11.4	2.0	2,94,070	3,36,410	14.4
Cost of revenues	1,18,520	1,28,180	1,34,360	1,37,520	1,40,980	1,43,520	12.0	1.8	2,46,700	2,84,500	15.3
as % of sales	62.0	62.2	62.8	63.8	64.7	63.4	-	-	62.1	64.0	-
SG&A expenses	23,030	24,340	25,540	26,380	25,530	26,380	8.4	3.3	47,370	51,910	9.6
as % of sales	12.0	11.8	11.9	12.2	11.7	11.7	-	-	11.9	11.7	-
<b>EBITDA</b>	<b>49,730</b>	<b>53,570</b>	<b>54,100</b>	<b>51,490</b>	<b>51,520</b>	<b>56,390</b>	<b>5.3</b>	<b>9.5</b>	<b>1,03,300</b>	<b>1,07,910</b>	<b>4.5</b>
Depreciation	4,360	4,630	5,800	5,310	6,810	7,270	57.0	6.8	8,990	14,080	56.6
<b>EBIT</b>	<b>45,370</b>	<b>48,940</b>	<b>48,300</b>	<b>46,180</b>	<b>44,710</b>	<b>49,120</b>	<b>0.4</b>	<b>9.9</b>	<b>94,310</b>	<b>93,830</b>	<b>(0.5)</b>
Other Income	7,260	7,390	7,530	6,650	7,360	6,260	-	-	14,650	13,620	(7.0)
PBT	52,630	56,330	55,830	52,830	52,070	55,380	(1.7)	6.4	1,08,960	1,07,450	(1.4)
Total Tax	13,810	15,230	15,220	12,050	13,650	14,590	(4.2)	6.9	29,040	28,240	(2.8)
<b>Adjusted PAT</b>	<b>38,820</b>	<b>41,100</b>	<b>40,610</b>	<b>40,780</b>	<b>38,420</b>	<b>40,790</b>	<b>(0.8)</b>	<b>6.2</b>	<b>79,920</b>	<b>79,210</b>	<b>(0.9)</b>
(Profit)/loss from JV's/Ass/MI	0	0	0	0	0	0	-	-	0	0	-
APAT after MI	38,820	41,100	40,610	40,780	38,420	40,790	(0.8)	6.2	79,920	79,210	(0.9)
Extraordinary items	(2700)	0	(4510)	0	0	0	-	-	(2,700)	0	-
<b>Reported PAT</b>	<b>36,120</b>	<b>41,100</b>	<b>36,100</b>	<b>40,780</b>	<b>38,420</b>	<b>40,790</b>	<b>(0.8)</b>	<b>6.2</b>	<b>77,220</b>	<b>79,210</b>	<b>2.6</b>
Reported EPS	8.3	9.4	8.3	9.4	8.8	9.4	-	7.2	18	18	2.8
<b>Margins (%)</b>							<b>(bps)</b>	<b>(bps)</b>			<b>(bps)</b>
EBITDA	26.0	26.0	25.3	23.9	23.6	24.9	(107)	129	26.0	24.3	(171)
EBIT	23.7	23.7	22.6	21.4	20.5	21.7	(204)	120	23.7	21.1	(262)
EBT	27.5	27.3	26.1	24.5	23.9	24.5	(286)	59	27.4	24.2	(324)
PAT	18.9	19.9	16.9	18.9	17.6	18.0	(192)	40	20.1	17.8	(228)
Effective Tax rate	26.2	27.0	27.3	22.8	26.2	26.3	(69.2)	13	26.7	26.3	(37)

Source: Company, BOBCAPS Research

**FIG 6 – SEP'19 QUARTER OPERATING METRICS**

Particulars	Q2FY20 (% Contr. to Revenue)	QoQ (%)	YoY (%)
TCV of deal wins (US\$ mn)	2,847	4.9	40.3
Digital Revenues	38.3	10.0	35.8
<b>Revenue by Geography</b>			
North America	61.4	2.2	11.9
Europe	24.1	4.7	10.4
India	2.7	20.4	18.7
ROW	11.8	(3.2)	(1.8)
<b>Revenue by Vertical</b>			
BFSI	31.9	4.2	8.9
Retail	15.2	(1.4)	(0.6)
Communications	13.1	(2.7)	17.0
Energy, Utilities, Resources and Services	13.1	3.3	17.0
Manufacturing	10.1	7.9	15.6
Hi Tech	7.6	1.2	11.4
Life Sciences	6.4	7.6	9.9
Others	2.6	2.5	(1.5)
<b>Client concentration</b>			
Top Client	3.2	2.5	(9.8)
Top 10 Clients	19.2	(1.6)	8.8
Non-Top 10 Clients	(1.4)	3.5	10.2
<b>(%)</b>	<b>Q2FY20</b>	<b>Q1FY20</b>	<b>Q2FY19</b>
<b>Onsite-Offshore effort split</b>			
Onsite	28.2	28.7	28.4
Offshore	71.8	71.3	71.6
<b>Utilisation measures (IT Services and Consulting)</b>			
Including trainees	81.6	80.3	80.2
Excluding trainees	84.9	83.1	85.6

Source: Company, BOBCAPS Research

## Valuation methodology

Post the Q2FY20 results, we largely retain our operating assumptions. Above-expected other income for the quarter pushes up FY20 EPS by 3% while FY21/FY22 EPS remain broadly unchanged. Our revised estimates build in 9%/10.7% YoY dollar revenue growth and 22.7%/23% EBIT margins for FY21/FY22.

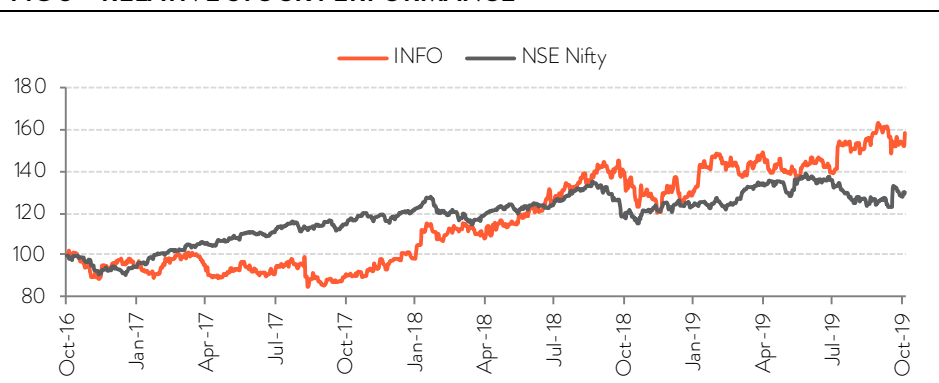
We continue to value INFO at an unchanged P/E multiple of 19x, which is one standard deviation above the stock's five-year average 12-month forward P/E. On rolling valuations forward, we have revised Sep'20 target price of Rs 860. Retain ADD.

**FIG 7 – REVISED ESTIMATES**

(Rs mn)	FY20E			FY21E			FY22E		
	Old	New	Chg (%)	Old	New	Chg (%)	Old	New	Chg (%)
Revenues (US\$ mn)	12,855	12,825	(0.2)	14,041	13,975	(0.5)	15,538	15,465	(0.5)
YoY revenue growth (%)	9.0	8.7		9.2	9.0		10.7	10.7	
Revenues	8,89,015	8,91,741	0.3	9,82,900	9,78,255	(0.5)	10,87,682	10,82,541	(0.5)
EBITDA	2,16,164	2,18,425	1.0	2,53,243	2,52,046	(0.5)	2,80,240	2,78,916	(0.5)
EBITDA margins (%)	24.3	24.5		25.8	25.8		25.8	25.8	
EBIT margins (%)	21.2	21.4		22.7	22.7		23.0	23.0	
Net profits	1,58,157	1,62,781	2.9	1,82,163	1,81,375	(0.4)	2,05,010	2,04,186	(0.4)
EPS (Rs)	36.7	37.7	2.9	42.2	42.0	(0.4)	47.5	47.3	(0.4)

Source: BOBCAPS Research

**FIG 8 – RELATIVE STOCK PERFORMANCE**



Source: NSE

## Key risks

Downside risks to our estimates are:

- a more pronounced adverse impact of global trade tensions, Brexit and other negative external events, leading to weaker-than-expected demand;
- more stringent visa regulations;
- below-expected operating margins for new engagements/renewals; and
- leadership changes.

## FINANCIALS

### Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Total revenue</b>	<b>7,05,220</b>	<b>8,26,760</b>	<b>8,91,741</b>	<b>9,78,255</b>	<b>10,82,541</b>
EBITDA	1,90,100	2,08,890	2,18,425	2,52,046	2,78,916
Depreciation	18,620	20,100	27,882	29,788	29,788
EBIT	1,71,480	1,88,790	1,90,544	2,22,258	2,49,127
Net interest income/(expenses)	26,130	21,620	24,497	26,201	30,579
Other income/(expenses)	32,400	28,900	29,527	26,201	30,579
Exceptional items	(1,180)	(7,210)	0	0	0
EBT	2,02,700	2,10,480	2,20,071	2,48,459	2,79,706
Income taxes	42,420	56,310	57,289	67,084	75,521
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
<b>Reported net profit</b>	<b>1,60,280</b>	<b>1,54,170</b>	<b>1,62,781</b>	<b>1,81,375</b>	<b>2,04,186</b>
Adjustments	0	0	0	0	0
<b>Adjusted net profit</b>	<b>1,60,280</b>	<b>1,54,170</b>	<b>1,62,781</b>	<b>1,81,375</b>	<b>2,04,186</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Accounts payables	0	0	0	0	0
Other current liabilities	1,44,740	1,68,940	1,88,121	2,06,372	2,28,372
Provisions	4,920	5,230	7,329	8,040	8,898
Debt funds	0	0	0	0	0
Other liabilities	0	0	0	0	0
Equity capital	10,880	21,700	21,700	21,700	21,700
Reserves & surplus	6,38,360	5,85,160	6,49,988	7,22,220	8,03,537
Shareholders' fund	6,49,240	6,06,860	6,71,688	7,43,920	8,25,237
<b>Total liabilities and equities</b>	<b>7,98,900</b>	<b>7,81,030</b>	<b>8,67,138</b>	<b>9,58,332</b>	<b>10,62,506</b>
Cash and cash eq.	1,98,180	1,65,060	2,24,351	2,82,729	3,43,477
Accounts receivables	1,31,420	1,36,990	1,61,246	1,76,890	1,95,747
Inventories	0	0	0	0	0
Other current assets	42,610	46,550	46,419	50,923	56,351
Investments	1,21,630	1,24,990	1,24,990	1,24,990	1,24,990
Net fixed assets	1,46,010	1,49,560	1,48,100	1,46,311	1,48,023
CWIP	0	0	0	0	0
Intangible assets	0	0	0	0	0
Deferred tax assets, net	12,820	13,000	13,000	13,000	13,000
Other assets	1,46,230	1,44,880	1,49,031	1,63,489	1,80,918
<b>Total assets</b>	<b>7,98,900</b>	<b>7,81,030</b>	<b>8,67,137</b>	<b>9,58,332</b>	<b>10,62,506</b>

Source: Company, BOBCAPS Research

### Cash Flows

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Net income + Depreciation	1,10,630	1,74,270	1,90,663	2,11,163	2,33,974
Interest expenses	(23,600)	(28,900)	(29,527)	(26,201)	(30,579)
Non-cash adjustments	0	0	0	0	0
Changes in working capital	840	16,350	(6,996)	(15,644)	(18,857)
Other operating cash flows	43,780	(98,005)	73,287	0	0
<b>Cash flow from operations</b>	<b>1,31,650</b>	<b>63,715</b>	<b>2,27,426</b>	<b>1,69,319</b>	<b>1,84,538</b>
Capital expenditures	(19,980)	(23,650)	(26,421)	(28,000)	(31,500)
Change in investments	21,810	0	0	0	0
Other investing cash flows	43,500	28,900	29,527	26,201	30,579
<b>Cash flow from investing</b>	<b>45,330</b>	<b>5,250</b>	<b>3,106</b>	<b>(1,799)</b>	<b>(921)</b>
Equities issued/Others	50	(9,313)	(73,287)	0	0
Debt raised/repaid	0	0	0	0	0
Interest expenses	0	0	0	0	0
Dividends paid	(2,05,100)	(92,772)	(97,954)	(1,09,142)	(1,22,869)
Other financing cash flows	0	0	0	0	0
<b>Cash flow from financing</b>	<b>(2,05,050)</b>	<b>(1,02,085)</b>	<b>(1,71,240)</b>	<b>(1,09,142)</b>	<b>(1,22,869)</b>
<b>Changes in cash and cash eq.</b>	<b>(28,070)</b>	<b>(33,120)</b>	<b>59,292</b>	<b>58,377</b>	<b>60,748</b>
<b>Closing cash and cash eq.</b>	<b>1,98,180</b>	<b>1,65,060</b>	<b>2,24,351</b>	<b>2,82,729</b>	<b>3,43,477</b>

### Per Share

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20E	FY21E	FY22E
Reported EPS	36.9	35.4	37.7	42.0	47.3
Adjusted EPS	36.9	35.4	37.7	42.0	47.3
Dividend per share	43.5	21.5	18.9	21.1	23.7
Book value per share	149.3	139.3	155.7	172.4	191.3

### Valuations Ratios

Y/E 31 Mar (x)	FY18A	FY19A	FY20E	FY21E	FY22E
EV/Sales	4.7	4.0	3.8	3.4	3.0
EV/EBITDA	17.5	16.0	15.5	13.2	11.7
Adjusted P/E	22.1	23.0	21.6	19.4	17.2
P/BV	5.5	5.8	5.2	4.7	4.3

### DuPont Analysis

Y/E 31 Mar (%)	FY18A	FY19A	FY20E	FY21E	FY22E
Tax burden (Net profit/PBT)	79.1	73.2	74.0	73.0	73.0
Interest burden (PBT/EBIT)	118.2	111.5	115.5	111.8	112.3
EBIT margin (EBIT/Revenue)	24.3	22.8	21.4	22.7	23.0
Asset turnover (Revenue/Avg TA)	86.4	104.7	108.2	107.2	107.1
Leverage (Avg TA/Avg Equity)	1.2	1.3	1.3	1.3	1.3
Adjusted ROAE	23.9	24.5	25.5	25.6	26.0

Source: Company, BOBCAPS Research | Note: TA = Total Assets

**Ratio Analysis**

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
<b>YoY growth (%)</b>					
Revenue	3.0	17.2	7.9	9.7	10.7
EBITDA	2.2	9.9	4.6	15.4	10.7
Adjusted EPS	17.3	(4.0)	6.6	11.4	12.6
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	27.0	25.3	24.5	25.8	25.8
EBIT margin	24.3	22.8	21.4	22.7	23.0
Adjusted profit margin	22.7	18.6	18.3	18.5	18.9
Adjusted ROAE	23.9	24.5	25.5	25.6	26.0
ROCE	29.6	31.0	31.7	35.7	38.6
<b>Working capital days (days)</b>					
Receivables	66	59	61	63	63
Inventory	0	0	0	0	0
Payables	101	93	97	99	99
<b>Ratios (x)</b>					
Gross asset turnover	4.6	5.6	6.0	6.6	7.4
Current ratio	3.5	2.8	3.0	3.1	3.3
Net interest coverage ratio	6.6	8.7	7.8	8.5	8.1
Adjusted debt/equity	(0.3)	(0.3)	(0.3)	(0.4)	(0.4)

Source: Company, BOBCAPS Research



## Disclaimer

### Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

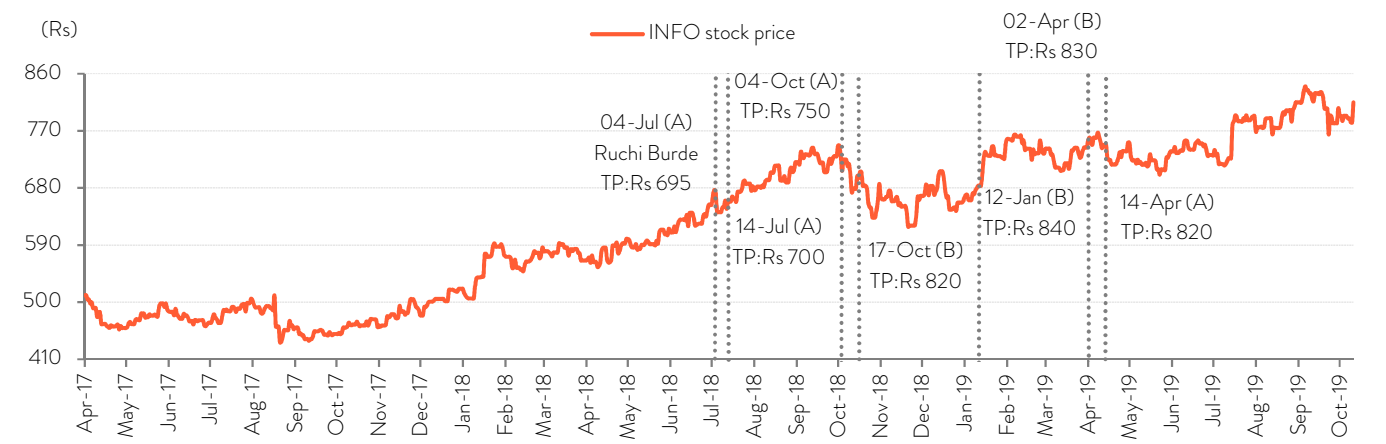
**ADD** – Expected return from >+5% to +15%

**REDUCE** – Expected return from -5% to +5%

**SELL** – Expected return <-5%

**Note:** Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

### HISTORICAL RATINGS AND TARGET PRICE: INFOSYS (INFO IN)



B – Buy, A – Add, R – Reduce, S – Sell

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