

**HOLD**

TP: Rs 1,503 | ▲ 5%

**INFOSYS**

| Technology &amp; Internet

| 25 April 2024

## Muted performance; weak discretionary delays recovery

- Cost optimisation/vendor consolidation to be the prime growth driver for Infosys in FY25
- Sequential decline in operating margin; orderbook stood at US\$ 17.7bn in FY24
- Maintain HOLD with a new TP of Rs 1,503, based on 21.2x on FY26E EPS, as the discretionary demand climate remains volatile

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**Lower-than-expected revenue growth driven by a few sectors:** Company reported muted revenue growth in Q4FY24, down 2.2% QoQ CC, due to 100bps impact of one-off rescoping of revenue at a large BFSI client and weak discretionary spending despite the ramp-up of mega deals and absence of furloughs. Major verticals, such as BFSI/Retail/Life Science, were down in Q4 but Telecom and Hi-Tech drove growth. Revenue guidance for FY25 stood at 1-3%, lower than the Street's expectation. Incremental improvement in revenue visibility will be possible on the back of large/mega deal revenue contribution and slower ramp down in the existing business. Infosys announced the acquisition of the Germany-based ER&D company in-tech Holding GmbH, with US\$ 180mn in revenue. The acquisition is likely to close in H1FY25 (not included in the revenue guidance).

**Despite robust deal wins, weakness in discretionary services continues:** Infosys posted a strong TCV of US\$ 4.5bn, up by 39% QoQ backed by 30 large deal wins. 16 large deal wins came from the Americas, bringing relief in terms of revival of geography. Large deal bookings of US\$ 17bn in FY24, including US\$ 9.2bn of net new large deals, will help FY25 growth momentum despite slower discretionary spending. INFO's deal activity is driven by cost optimisation deals and vendor consolidation deals with strength in services such as SAP S4/Hana implementation.

**Limited upside potential for margin due to poor exit run rate:** Despite increasing utilisation, lower subcontracting cost and recalibration of employee pyramid, elevated levels of pass-through and third-party hardware/software expenses dragged the operating model, along with recent client-specific issues and the McCamish cybersecurity incident. Its operating margin guidance remained at 20-22% for FY25.

**Valuation outlook:** Despite near-term weakness, we expect Infosys to be a key beneficiary of the acceleration in IT spending in the medium term. INFO trades at 22.3x FY25E and 20.3x FY26E EPS and our TP of Rs 1,503 (previously Rs 1,592) is based on 21.2x (20% discount to TCS) on FY26E EPS. INFO extending its payout policy by five years for 85% of FCF is a positive.

### Key changes

Target	Rating
▼	◀ ▶

Ticker/Price	INFO IN/Rs 1,431
Market cap	US\$ 72.1bn
Free float	86%
3M ADV	US\$ 132.7mn
52wk high/low	Rs 1,733/Rs 1,215
Promoter/FPI/DII	15%/36%/49%

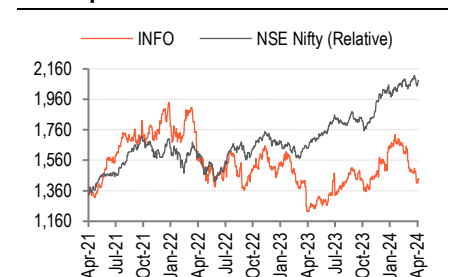
Source: NSE | Price as of 24 Apr 2024

### Key financials

Y/E 31 Mar	FY24A	FY25E	FY26E
Total revenue (Rs mn)	15,36,710	15,93,572	17,11,085
EBITDA (Rs mn)	3,63,410	3,76,083	4,08,949
Adj. net profit (Rs mn)	2,62,480	2,68,117	2,93,451
Adj. EPS (Rs)	63.4	64.8	70.9
Consensus EPS (Rs)	63.4	68.2	76.1
Adj. ROAE (%)	32.1	29.7	31.1
Adj. P/E (x)	22.6	22.1	20.2
EV/EBITDA (x)	15.9	15.4	14.1
Adj. EPS growth (%)	9.1	2.1	9.4

Source: Company, Bloomberg, BOBCAPS Research

### Stock performance



Source: NSE

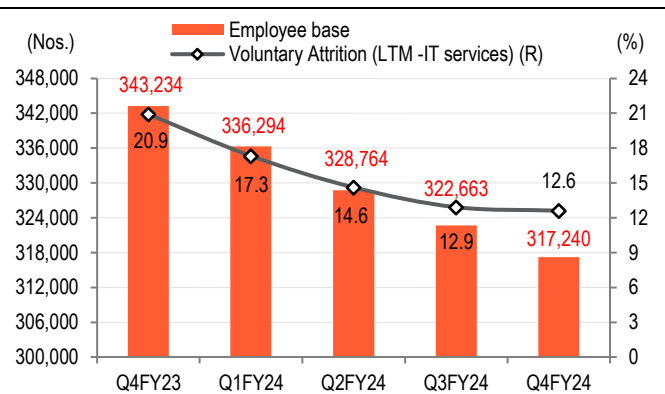


**Fig 1 – Quarterly performance**

(Rs mn)	Q4FY24	Q3FY23	Q4FY23	QoQ (%)	YoY (%)	Estimates	Variance (%)
US\$ Revenue	4,564	4,663	4,554	(2.1)	0.2	4,643	(1.7)
INR Revenue	379,230	388,210	374,410	(2.3)	1.3	385,328	(1.6)
EBIT	76,210	79,610	78,770	(4.3)	(3.2)	79,185	(3.8)
PAT	79,750	61,130	61,340	30.5	30.1	60,111	32.7
EBIT Margin (%)	20.1	20.5	21.0	(41bps)	(94bps)	20.6	(45bps)
PAT Margin (%)	21.0	15.7	16.4	528bps	465bps	15.6	543bps

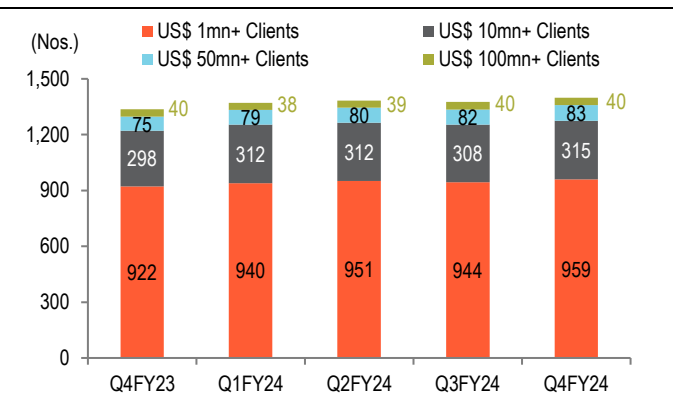
Source: Company, BOBCAPS Research

**Fig 2 – Employee base & Attrition**



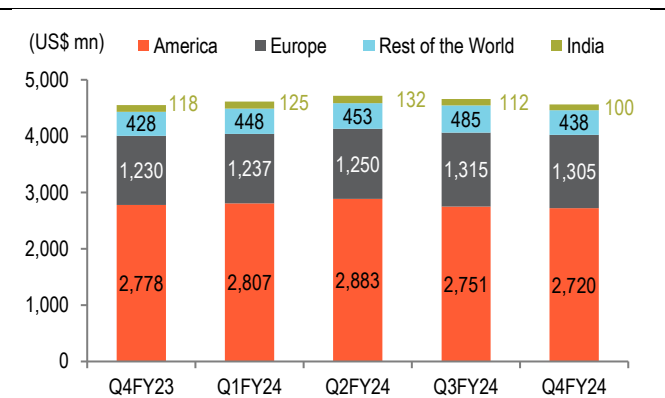
Source: Company, BOBCAPS Research

**Fig 3 – Client category**



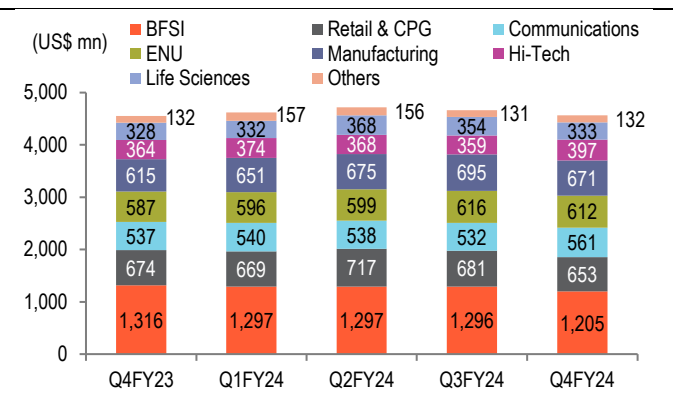
Source: Company, BOBCAPS Research

**Fig 4 – Revenue by geography**



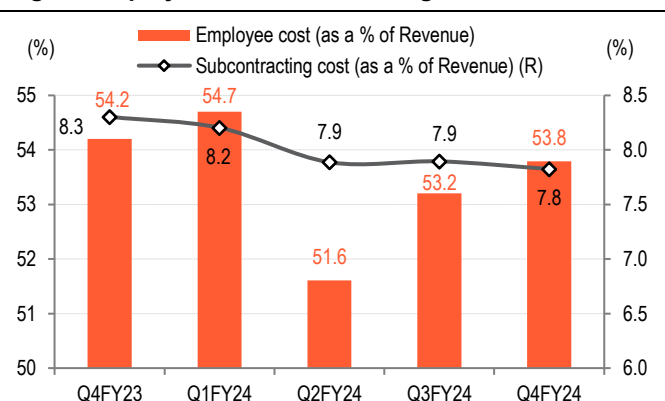
Source: Company, BOBCAPS Research

**Fig 5 – Revenue by vertical**



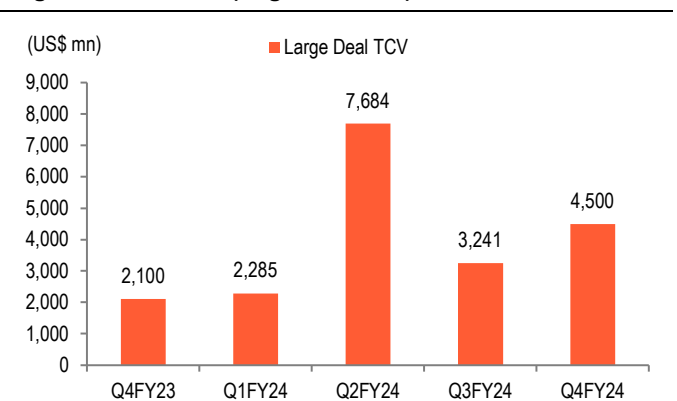
Source: Company, BOBCAPS Research

**Fig 6 – Employee and subcontracting cost**



Source: Company, BOBCAPS Research

**Fig 7 – Order book (large deal TCV)**



Source: Company, BOBCAPS Research

## Earnings call highlights

- The demand outlook for discretionary work is similar to FY24. Large deals won in FY24 should support growth in FY25. The company is seeing solid traction in cost efficiency/vendor consolidation deals.
- In Q4, INFO signed eight large deals in communication, six in retail, four each in manufacturing and life sciences. By region, 16 were from North America, 10 from Europe, and four from the rest of the world.
- Revenue guidance for FY25 stood at 1-3%, operating margin guidance remained stable at 20-22%.
- Due to one-off rescoping/renegotiating for a large BFSI client (1% of the revenue), 85% of the contract was retained and no further renegotiation is expected in the near term.
- Margin headwinds were -100bps from the one-off of the contract renegotiation/rescoping, -80bps impact of salary hike and visa expense (effective Nov'23), offset by tailwinds such as +40bps from project Maximus and +40bps from lower provision for client receivables.
- INFO acquired in-tech, a Germany-based automotive ER&D service provider, which is involved in design, consulting, advanced electronics platform development and validation of automotive-specific software and hardware systems, infotainment for OEM customers (clients include BMW, Bosch, Ford, Rolls Royce, etc).
- Gen AI saw strong traction in the SaaS business. Cloud remains the foundation of AI/Gen AI.

## Valuation methodology

Despite the soft results and weak guidance, INFO has the potential to deliver industry-leading growth once we see a turnaround in the demand environment. TCV to revenue conversion remains weak in FY25 due to the slowdown and postponement of deals. Going with gradual recovery ahead, we have factored in revenue growth at 3.3% and 7.9% CC for FY25E/FY26E and EBITM at 20.7%/21%, translating to 5.7% EPS CAGR over FY24-26E. We maintain our HOLD rating on the stock with a lower target price of Rs 1,503 (previously Rs 1,592) at P/E of 21.2x on FY26E EPS.

**Fig 8 – Revised estimates**

(Rs mn)	New		Old		Change (%)	
	FY25E	FY26E	FY25E	FY26E	FY25E	FY26E
Revenue (US\$ mn)	19,177	20,691	19,690	21,634	(2.6)	(4.4)
Revenue	1,593,572	1,711,085	1,636,209	1,789,111	(2.6)	(4.4)
EBIT	329,312	358,745	367,083	413,505	(10.3)	(13.2)
Margin (%)	20.7	21.0	22.4	23.1	(177bps)	(215bps)
EPS (Rs)	64.8	70.9	65	73.7	(0.3)	(3.8)

Source: BOBCAPS Research

## Key risks

Key upside/downside risks to our estimates are:

- elongated decision-making cycle, especially in BFSI/Retail/Hi-Tech;
- further decline in interest rates.

## Glossary

Glossary of Abbreviations			
<b>ACV</b>	Annual contract value	<b>AI</b>	Artificial intelligence
<b>BFSI</b>	Banking, financial services and insurance	<b>CC</b>	Constant currency
<b>EMEA</b>	Europe, Middle East, and Africa	<b>ER&amp;D</b>	Engineering, Research & Development
<b>IT</b>	Information Technology	<b>OEM</b>	Original equipment manufacturers
<b>SG&amp;A</b>	Selling, general, and administrative expenses	<b>TCV</b>	Total contract value

## Financials

### Income Statement

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24A	FY25E	FY26E
<b>Total revenue</b>	<b>12,16,410</b>	<b>14,67,670</b>	<b>15,36,710</b>	<b>15,93,572</b>	<b>17,11,085</b>
EBITDA	3,14,820	3,51,310	3,63,410	3,76,083	4,08,949
Depreciation	34,770	42,250	45,940	46,771	50,204
EBIT	2,80,050	3,09,060	3,17,470	3,29,312	3,58,745
Net interest inc./(exp.)	16,570	18,290	20,670	19,303	22,556
Other inc./(exp.)	21,050	24,160	42,420	28,177	32,520
Exceptional items	0	0	0	0	0
EBT	3,01,100	3,33,220	3,59,890	3,57,489	3,91,265
Income taxes	79,640	92,140	97,410	89,372	97,816
Extraordinary items	0	0	0	1	2
Min. int./Inc. from assoc.	250	0	0	0	0
<b>Reported net profit</b>	<b>2,21,210</b>	<b>2,41,080</b>	<b>2,62,480</b>	<b>2,68,116</b>	<b>2,93,449</b>
Adjustments	0	0	0	1	2
<b>Adjusted net profit</b>	<b>2,21,210</b>	<b>2,41,080</b>	<b>2,62,480</b>	<b>2,68,117</b>	<b>2,93,451</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24A	FY25E	FY26E
Accounts payables	41,340	38,650	39,560	41,024	44,049
Other current liabilities	2,84,940	3,40,140	3,30,420	3,30,082	3,54,423
Provisions	9,750	13,070	17,960	17,464	18,752
Debt funds	0	0	0	0	0
Other liabilities	0	0	0	0	0
Equity capital	20,980	20,690	20,690	20,690	20,690
Reserves & surplus	7,32,520	7,33,380	8,60,450	9,00,667	9,44,685
Shareholders' fund	7,53,500	7,54,070	8,81,140	9,21,357	9,65,375
<b>Total liab. and equities</b>	<b>10,48,190</b>	<b>11,07,280</b>	<b>12,29,520</b>	<b>12,68,903</b>	<b>13,38,549</b>
Cash and cash eq.	1,74,720	1,21,730	1,47,860	1,33,720	1,42,851
Accounts receivables	2,26,980	2,54,240	3,01,930	3,27,446	3,37,529
Inventories	0	0	0	0	0
Other current assets	1,04,690	1,47,300	1,54,720	1,61,540	1,64,077
Investments	2,03,240	1,94,780	2,46,230	2,86,230	3,56,230
Net fixed assets	2,62,160	2,95,130	2,79,150	2,58,282	2,37,311
CWIP	4,160	2,880	2,930	4,930	5,930
Intangible assets	0	0	0	0	0
Deferred tax assets, net	73,640	77,040	98,940	98,940	98,940
Other assets	1,33,420	1,67,940	1,49,290	1,52,808	1,54,701
<b>Total assets</b>	<b>11,78,850</b>	<b>12,58,160</b>	<b>13,78,120</b>	<b>14,18,967</b>	<b>14,91,638</b>

### Cash Flows

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24A	FY25E	FY26E
<b>Cash flow from operations</b>	<b>2,38,850</b>	<b>2,24,670</b>	<b>2,52,100</b>	<b>2,51,486</b>	<b>3,25,275</b>
Capital expenditures	(75,030)	(76,500)	(29,910)	(25,904)	(29,233)
Change in investments	(59,920)	9,780	(44,660)	(40,000)	(70,000)
Other investing cash flows	70,790	54,630	24,480	28,177	32,520
<b>Cash flow from investing</b>	<b>(64,160)</b>	<b>(12,090)</b>	<b>(50,090)</b>	<b>(37,727)</b>	<b>(66,713)</b>
Equities issued/Others	210	350	50	0	0
Debt raised/repaid	0	0	0	0	0
Interest expenses	(1,19,320)	(1,30,770)	(27,780)	0	0
Dividends paid	(1,27,310)	(1,36,530)	(1,47,310)	(2,27,899)	(2,49,431)
Other financing cash flows	0	0	0	0	0
<b>Cash flow from financing</b>	<b>(2,46,420)</b>	<b>(2,66,950)</b>	<b>(1,75,040)</b>	<b>(2,27,899)</b>	<b>(2,49,431)</b>
<b>Chg in cash &amp; cash eq.</b>	<b>(71,730)</b>	<b>(54,370)</b>	<b>26,970</b>	<b>(14,140)</b>	<b>9,131</b>
<b>Closing cash &amp; cash eq.</b>	<b>1,74,720</b>	<b>1,21,730</b>	<b>1,47,860</b>	<b>1,33,720</b>	<b>1,42,851</b>

### Per Share

Y/E 31 Mar (Rs)	FY22A	FY23A	FY24A	FY25E	FY26E
Reported EPS	52.8	58.1	63.4	64.8	70.9
Adjusted EPS	52.8	58.1	63.4	64.8	70.9
Dividend per share	26.3	29.1	31.7	55.1	60.3
Book value per share	179.0	181.7	212.9	222.6	233.2

### Valuations Ratios

Y/E 31 Mar (x)	FY22A	FY23A	FY24A	FY25E	FY26E
EV/Sales	4.7	3.9	3.8	3.6	3.4
EV/EBITDA	18.1	16.3	15.9	15.4	14.1
Adjusted P/E	27.1	24.6	22.6	22.1	20.2
P/BV	8.0	7.9	6.7	6.4	6.1

### DuPont Analysis

Y/E 31 Mar (%)	FY22A	FY23A	FY24A	FY25E	FY26E
Tax burden (Net profit/PBT)	73.5	72.3	72.9	75.0	75.0
Interest burden (PBT/EBIT)	107.5	107.8	113.4	108.6	109.1
EBIT margin (EBIT/Revenue)	23.0	21.1	20.7	20.7	21.0
Asset turnover (Rev./Avg TA)	107.5	120.4	116.6	113.9	117.6
Leverage (Avg TA/Avg Equity)	1.5	1.6	1.6	1.6	1.5
<b>Adjusted ROAE</b>	<b>29.1</b>	<b>32.0</b>	<b>32.1</b>	<b>29.7</b>	<b>31.1</b>

### Ratio Analysis

Y/E 31 Mar	FY22A	FY23A	FY24A	FY25E	FY26E
<b>YoY growth (%)</b>					
Revenue	21.1	20.7	4.7	3.7	7.4
EBITDA	12.7	11.6	3.4	3.5	8.7
Adjusted EPS	15.9	10.1	9.1	2.1	9.4
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	25.9	23.9	23.6	23.6	23.9
EBIT margin	23.0	21.1	20.7	20.7	21.0
Adjusted profit margin	18.2	16.4	17.1	16.8	17.2
Adjusted ROAE	29.1	32.0	32.1	29.7	31.1
ROCE	37.5	36.9	27.6	23.3	24.0
<b>Working capital days (days)</b>					
Receivables	63	60	66	72	71
Inventory	0	0	0	0	0
Payables	120	102	104	99	96
<b>Ratios (x)</b>					
Gross asset turnover	4.6	5.3	5.4	5.9	6.9
Current ratio	1.9	1.8	1.9	2.0	1.9
Net interest coverage ratio	16.9	16.9	15.4	17.1	15.9
<b>Adjusted debt/equity</b>	<b>(0.2)</b>	<b>(0.2)</b>	<b>(0.2)</b>	<b>(0.1)</b>	<b>(0.1)</b>

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

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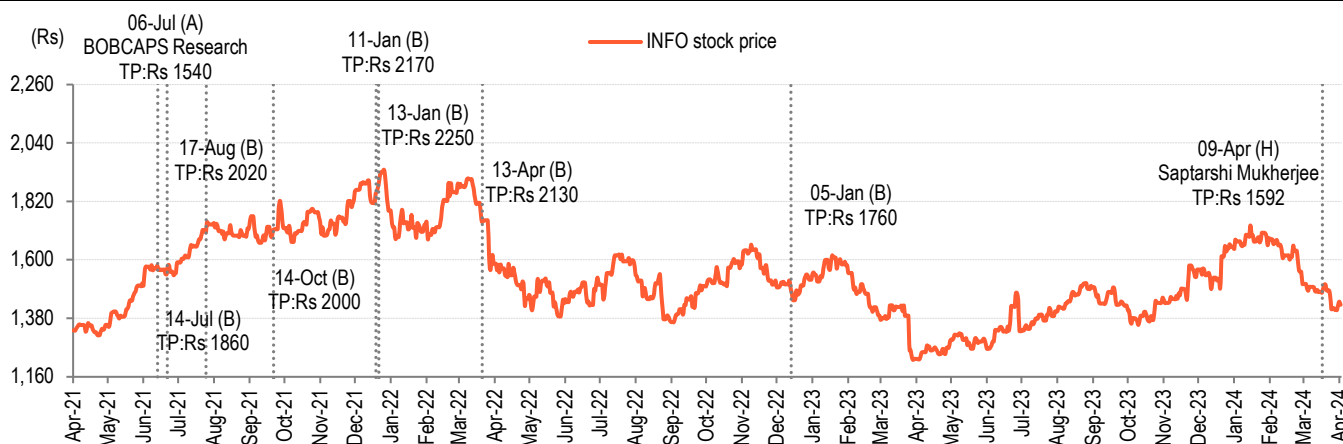
**HOLD** – Expected return from -6% to +15%

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**Note:** Recommendation structure changed with effect from 21 June 2021

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

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