

BUY

TP: Rs 2,010 | ▲ 25%

L&T INFOTECH

| IT Services

| 18 October 2019

On course for a rebound

L&T Infotech (LTI) did better than expected in Q2FY20, posting 2.4% QoQ CC revenue growth despite client-specific challenges. Management believes the worst is over and expects growth in the top account to resume from Q3, which brightens the near-term outlook. The company continues to bag large deals, adding three new clients with an aggregate TCV of US\$ 100mn in Q2. Management has guided for double-digit revenue growth in FY20. We tweak estimates and reiterate BUY; on rollover to Sep'20 our TP remains at Rs 2,010.

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Above-expected Q2: LTI reported a beat on revenues, growing at 2.4% QoQ CC vs. 1.4% estimated in Q2FY20. EBIT margins were largely in line at 15.5%, down 40bps QoQ.

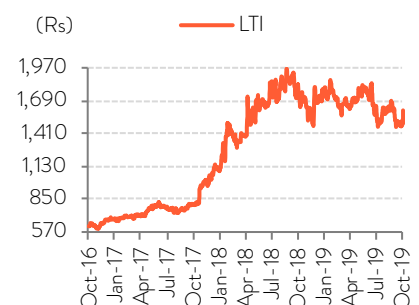
Client-specific challenges abating: After two quarters of decline, revenue from the top 5 clients returned to positive territory (+3.4% QoQ in dollar terms). Management indicated that the top client account (a drag on growth for the last two quarters) should witness a growth recovery from Q3FY20. Similarly, the hi-tech vertical is also guided to resume its growth trajectory from Q3, after headwinds from the loss of an account in Q2. Non-top 20 client revenue (+5% QoQ in dollar terms) continued to grow ahead of companywide growth.

Stellar deal signings: LTI maintained its streak of large deal wins, adding three new logos with an aggregate TCV of US\$ 100mn during the quarter. H1FY20 net new deal TCV increased by 37% YoY to US\$ 144mn, lending visibility for growth in H2. Management has guided for double-digit revenue growth in FY20 and retained the net margin guidance at 14-15%.

| | |
|------------------|-------------------|
| Ticker/Price | LTI IN/Rs 1,611 |
| Market cap | US\$ 4.0bn |
| Shares o/s | 175mn |
| 3M ADV | US\$ 2.6mn |
| 52wk high/low | Rs 1,897/Rs 1,436 |
| Promoter/FPI/DII | 75%/8%/10% |

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

| Y/E 31 Mar | FY18A | FY19A | FY20E | FY21E | FY22E |
|-------------------------|--------|--------|----------|----------|----------|
| Total revenue (Rs mn) | 73,064 | 94,458 | 1,03,286 | 1,14,878 | 1,28,327 |
| EBITDA (Rs mn) | 11,875 | 18,835 | 19,232 | 22,606 | 25,252 |
| Adj. net profit (Rs mn) | 11,124 | 15,157 | 15,082 | 17,613 | 19,002 |
| Adj. EPS (Rs) | 63.5 | 86.5 | 85.9 | 100.3 | 108.3 |
| Adj. EPS growth (%) | (8.2) | 36.1 | (0.6) | 16.8 | 7.9 |
| Adj. ROAE (%) | 31.8 | 34.6 | 28.3 | 28.1 | 25.9 |
| Adj. P/E (x) | 25.4 | 18.6 | 18.7 | 16.1 | 14.9 |
| EV/EBITDA (x) | 23.4 | 14.8 | 14.4 | 12.0 | 10.4 |

Source: Company, BOBCAPS Research

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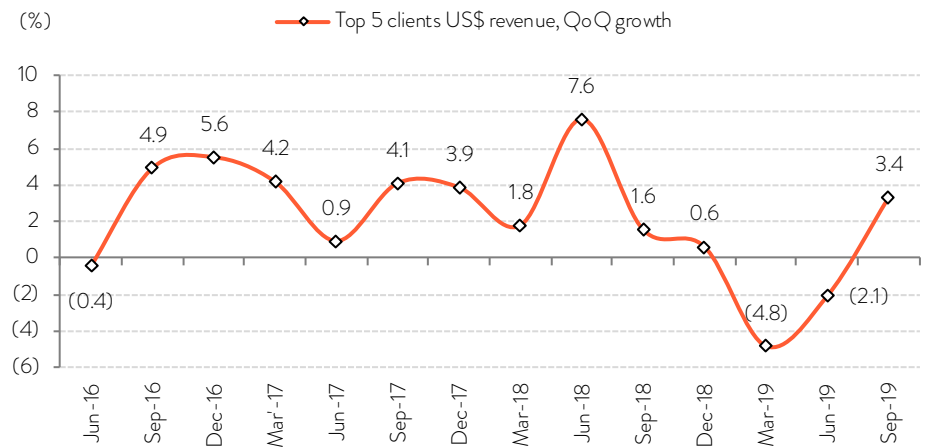
H1FY20 net new deal TCV rose 37% YoY to US\$ 144mn

FIG 1 – LARGE DEAL WINS CONTINUE TO IMPRESS

| Quarter | Large deal wins |
|---|--|
| Sep-19 | 3 new logos opened with aggregate net new TCV of US\$ 100mn |
| Jun-19 | Opened a new logo in the insurance vertical with TCV of US\$ 44mn |
| Won 2 large deals with net new TCV of US\$100mn+ | |
| Mar-19 | <ul style="list-style-type: none"> ▪ Deal 1: Multi-year multi-million-dollar deal for transforming global application operations of an engineering equipment manufacturer ▪ Deal 2: New logo opening with a large IT transformation deal in the insurance vertical |
| Dec-18 | Secured large deal for a payments company in the Nordic region as primary IT partner post vendor consolidation |
| Sep-18 | Secured a large deal for a global pharma company with net new TCV of US\$ 55mn |
| Jun-18 | Multi-year deal with net new TCV of US\$ 50mn in ERP, data and analytics for global consumer and pharmaceutical conglomerate |

Source: Company, BOBCAPS Research

FIG 2 – AFTER TWO CONSECUTIVE QUARTERS OF DECLINE, REVENUE FROM TOP 5 CLIENTS RETURNED TO GROWTH



Source: Company, BOBCAPS Research

FIG 3 – SEP'19 QUARTER PERFORMANCE

| (Rs mn) | Q1FY19 | Q2FY19 | Q3FY19 | Q4FY19 | Q1FY20 | Q2FY20 | YoY (%) | QoQ (%) | H1FY20 | H1FY19 | YoY (%) |
|---------------------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|--------------|---------------|---------------|--------------|
| Revenues (US\$ mn) | 319.9 | 328.5 | 346.9 | 353.8 | 356.5 | 363.8 | 10.7 | 2.0 | 720.3 | 648.4 | 11.1 |
| Revenue | 21,557 | 23,312 | 24,729 | 24,860 | 24,849 | 25,707 | 10.3 | 3.5 | 50,556 | 44,869 | 12.7 |
| Operating Expenditure | 17,367 | 18,522 | 19,639 | 20,095 | 20,270 | 21,050 | 13.6 | 3.8 | 41,320 | 35,889 | 15.1 |
| Cost of revenues | 13,977.0 | 15,124.0 | 16,125.0 | 16,417.0 | 16,625.0 | 17,525.0 | 15.9 | 5.4 | 34,150 | 29,101 | 17.3 |
| as % of sales | 64.8 | 64.9 | 65.2 | 66.0 | 66.9 | 68.2 | - | - | 67.5 | 64.9 | - |
| SG&A expenses | 3,390.0 | 3,398.0 | 3,514.0 | 3,678.0 | 3,645.0 | 3,525.0 | 3.7 | (3.3) | 7,170 | 6,788 | 5.6 |
| as % of sales | 15.7 | 14.6 | 14.2 | 14.8 | 14.7 | 13.7 | - | - | 14.2 | 15.1 | - |
| EBITDA | 4,190 | 4,790 | 5,090 | 4,765 | 4,579 | 4,657 | (2.8) | 1.7 | 9,236 | 8,980 | 2.9 |
| Depreciation | 378.0 | 367.0 | 355.0 | 371.0 | 611.0 | 664.0 | 80.9 | 8.7 | 1,275 | 745 | 71.1 |
| EBIT | 3,812 | 4,423 | 4,735 | 4,394 | 3,968 | 3,993 | (9.7) | 0.6 | 7,961 | 8,235 | (3.3) |
| Other Income | 1,036.0 | 943.0 | 288.0 | 648.0 | 812.0 | 739.0 | - | - | 1,551 | 1,979 | - |
| PBT | 4,848 | 5,366 | 5,023 | 5,042 | 4,780 | 4,732 | (11.8) | (1.0) | 9,512 | 10,214 | (6.9) |
| Total Tax | 1,236.0 | 1,363.0 | 1,268.0 | 1,255.0 | 1,225.0 | 1,130.0 | (17.1) | (7.8) | 2,355 | 2,599 | (9.4) |
| Reported PAT | 3,612 | 4,003 | 3,755 | 3,787 | 3,555 | 3,602 | (10.0) | 1.3 | 7,157 | 7,615 | (6.0) |
| Reported EPS | 20.6 | 22.6 | 21.6 | 21.6 | 20.3 | 20.5 | (9.2) | 1.1 | 40.8 | 43.2 | (5.5) |
| Margins (%) | | | | | | | (bps) | (bps) | | | (bps) |
| EBITDA | 19.4 | 20.5 | 20.6 | 19.2 | 18.4 | 18.1 | (243) | (31) | 18.3 | 20.0 | (174) |
| EBIT | 17.7 | 19.0 | 19.1 | 17.7 | 16.0 | 15.5 | (344) | (44) | 15.7 | 18.4 | (261) |
| EBT | 22.5 | 23.0 | 20.3 | 20.3 | 19.2 | 18.4 | (461) | (83) | 18.8 | 22.8 | (395) |
| PAT | 16.8 | 17.2 | 15.2 | 15.2 | 14.3 | 14.0 | (316) | (29) | 14.2 | 17.0 | (282) |
| Effective Tax Rate | 25.5 | 25.4 | 25.2 | 24.9 | 25.6 | 23.9 | (152) | (175) | 24.8 | 25.4 | (69) |

Source: Company, BOBCAPS Research

FIG 4 – SEP'19 QUARTER OPERATING METRICS

| | Q2FY20 (% Contr. to Revenue) | Growth | |
|---------------------------------------|---------------------------------|---------|---------|
| | | QoQ (%) | YoY (%) |
| Revenue by Vertical | | | |
| BFS | 27.1 | (0.2) | 0.4 |
| Insurance | 18.7 | 5.4 | 15.7 |
| Manufacturing | 16.4 | 10.1 | 17.9 |
| Energy & Process | 12.1 | 15.4 | 25.2 |
| CPG, Retail & Pharma | 11.5 | 5.7 | 24.9 |
| High-Tech, Media & Entertainment | 10.8 | (11.8) | 6.8 |
| Others | 3.5 | (22.4) | (17.5) |
| Revenue by Geography | | | |
| North America | 68.7 | 2.0 | 12.9 |
| Europe | 16.4 | 4.6 | 6.2 |
| India | 6.0 | (11.3) | 3.8 |
| RoW | 8.9 | 6.8 | 7.1 |
| Client Contribution to Revenue | | | |
| Top 5 clients | 31.7 | 3.4 | (3.0) |
| Top 10 clients | 45.5 | 3.2 | 1.0 |
| Top 20 clients | 61.4 | 0.3 | 3.8 |
| Non-top 20 client revenues | 38.6 | 5.0 | 23.9 |
| Digital Revenues | 40.3 | 5.4 | 20.6 |

Source: Company, BOBCAPS Research

Valuation methodology

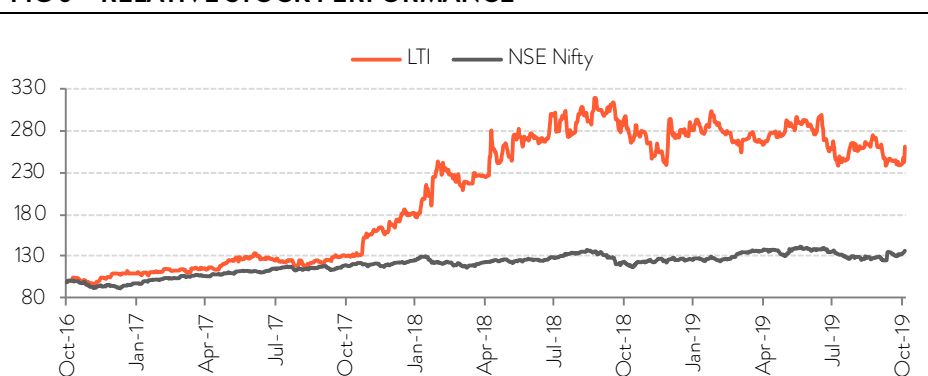
LTI's medium-to-long term prospects look robust given its strong sales engine, 'outcome-focused' digital capabilities, client mining skills and strong leadership. We tweak our earnings assumptions following the Q2FY20 results; on rollover to Sep'20 our target price remains unchanged at Rs 2,010, set at 19.3x one-year forward EPS. Retain BUY.

FIG 5 – REVISED ESTIMATES

| (Rs mn) | FY20E | | | FY21E | | | FY22E | | |
|--------------------|----------|----------|------------|----------|----------|------------|----------|----------|------------|
| | Old | New | Change (%) | Old | New | Change (%) | Old | New | Change (%) |
| Revenues (US\$ mn) | 1,462 | 1,474 | 0.8 | 1,624 | 1,641 | 1.0 | 1,814 | 1,833 | 1.0 |
| YoY growth (%) | 8.4 | 9.2 | - | 11.1 | 11.4 | - | 11.7 | 11.7 | - |
| Revenues | 1,01,136 | 1,03,286 | 2.1 | 1,13,699 | 1,14,878 | 1.0 | 1,27,010 | 1,28,327 | 1.0 |
| EBITDA | 18,803 | 19,232 | 2.3 | 22,374 | 22,606 | 1.0 | 24,993 | 25,252 | 1.0 |
| EBITDA margins (%) | 18.6 | 18.6 | - | 19.7 | 19.7 | - | 19.7 | 19.7 | - |
| Net profits | 14,980 | 15,082 | 0.7 | 17,238 | 17,613 | 2.2 | 18,717 | 19,002 | 1.5 |
| EPS (Rs) | 85.5 | 85.9 | 0.5 | 98.4 | 100.3 | 2.0 | 106.8 | 108.3 | 1.3 |

Source: BOBCAPS Research

FIG 6 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- **Currency risk:** A sharp fluctuation in exchange rates may materially impact the company's operating profits.
- **Leadership flux:** LTI has suffered from a leadership flux in the past (prior to FY14) – a repeat of this situation would pose a risk to our thesis.
- **Inability to sustain large deal momentum:** Steady large deal wins are critical for the company to sustain its strong growth traction. An inability to do so may derail growth.

- **Client concentration risk:** Top 5/10 clients account for ~32%/46% of LTI's revenue. Any prolonged weakness in top client revenue would pose a downside risk to our estimates.
- **Benchmarking clause:** Some of LTI's client contracts contain benchmarking clauses (22% of revenues in FY16) and most favoured customer provisions (29% of revenues in FY16) – if triggered, they could result in lower contractual revenues and profitability in future.

FINANCIALS

Income Statement

| Y/E 31 Mar (Rs mn) | FY18A | FY19A | FY20E | FY21E | FY22E |
|--------------------------------|---------------|---------------|-----------------|-----------------|-----------------|
| Total revenue | 73,064 | 94,458 | 1,03,286 | 1,14,878 | 1,28,327 |
| EBITDA | 11,875 | 18,835 | 19,232 | 22,606 | 25,252 |
| Depreciation | 1,563 | 1,471 | 2,593 | 2,872 | 3,208 |
| EBIT | 10,312 | 17,364 | 16,639 | 19,734 | 22,044 |
| Net interest income/(expenses) | 0 | 0 | 0 | 0 | 0 |
| Other income/(expenses) | 4,102 | 2,915 | 3,440 | 3,908 | 3,462 |
| Exceptional items | 0 | 0 | 0 | 0 | 0 |
| EBT | 14,414 | 20,279 | 20,079 | 23,642 | 25,506 |
| Income taxes | 3,290 | 5,122 | 4,997 | 6,029 | 6,504 |
| Extraordinary items | 0 | 0 | 0 | 0 | 0 |
| Min. int./Inc. from associates | 0 | 0 | 0 | 0 | 0 |
| Reported net profit | 11,124 | 15,157 | 15,082 | 17,613 | 19,002 |
| Adjustments | 0 | 0 | 0 | 0 | 0 |
| Adjusted net profit | 11,124 | 15,157 | 15,082 | 17,613 | 19,002 |

Balance Sheet

| Y/E 31 Mar (Rs mn) | FY18A | FY19A | FY20E | FY21E | FY22E |
|---------------------------------------|---------------|---------------|---------------|---------------|-----------------|
| Accounts payables | 0 | 0 | 0 | 0 | 0 |
| Other current liabilities | 12,960 | 15,291 | 16,720 | 18,597 | 20,774 |
| Provisions | 2,123 | 2,402 | 2,626 | 2,921 | 3,263 |
| Debt funds | 0 | 0 | 0 | 0 | 0 |
| Other liabilities | 132 | 56 | 56 | 56 | 56 |
| Equity capital | 171 | 171 | 171 | 171 | 171 |
| Reserves & surplus | 38,439 | 48,772 | 57,498 | 67,690 | 78,684 |
| Shareholders' fund | 38,610 | 48,943 | 57,669 | 67,861 | 78,855 |
| Total liabilities and equities | 53,825 | 66,692 | 77,072 | 89,434 | 1,02,948 |
| Cash and cash eq. | 3,633 | 4,150 | 11,346 | 19,453 | 28,029 |
| Accounts receivables | 22,327 | 23,845 | 18,393 | 20,458 | 22,853 |
| Inventories | 0 | 0 | 0 | 0 | 0 |
| Other current assets | 7,121 | 10,878 | 13,017 | 14,478 | 16,173 |
| Investments | 12,643 | 17,402 | 17,402 | 17,402 | 17,402 |
| Net fixed assets | 5,281 | 8,031 | 8,020 | 8,020 | 8,020 |
| CWIP | 0 | 0 | 0 | 0 | 0 |
| Intangible assets | 0 | 0 | 0 | 0 | 0 |
| Deferred tax assets, net | 2,821 | 2,386 | 2,386 | 2,386 | 2,386 |
| Other assets | 0 | 0 | 6,508 | 7,239 | 8,086 |
| Total assets | 53,826 | 66,692 | 77,072 | 89,435 | 1,02,949 |

Source: Company, BOBCAPS Research

Cash Flows

| Y/E 31 Mar (Rs mn) | FY18A | FY19A | FY20E | FY21E | FY22E |
|-------------------------------------|----------------|----------------|----------------|----------------|----------------|
| Net income + Depreciation | 9,106 | 16,628 | 17,675 | 20,485 | 22,210 |
| Interest expenses | 134 | (1,089) | (933) | (2,012) | (2,580) |
| Non-cash adjustments | 0 | 0 | 0 | 0 | 0 |
| Changes in working capital | (3,760) | (2,665) | (1,542) | (2,084) | (2,418) |
| Other operating cash flows | 2,958 | 1,010 | 0 | 0 | 0 |
| Cash flow from operations | 8,438 | 13,884 | 15,200 | 16,389 | 17,212 |
| Capital expenditures | (982) | (4,221) | (2,582) | (2,872) | (3,208) |
| Change in investments | (2,501) | (4,324) | 0 | 0 | 0 |
| Other investing cash flows | (1,041) | 1,089 | 933 | 2,012 | 2,580 |
| Cash flow from investing | (4,524) | (7,456) | (1,649) | (860) | (628) |
| Equities issued/Others | 3 | 0 | 0 | 0 | 0 |
| Debt raised/repaid | 0 | 0 | 0 | 0 | 0 |
| Interest expenses | (1,045) | 0 | 0 | 0 | 0 |
| Dividends paid | (3,034) | (5,911) | (6,356) | (7,422) | (8,007) |
| Other financing cash flows | 0 | 0 | 0 | 0 | 0 |
| Cash flow from financing | (4,076) | (5,911) | (6,356) | (7,422) | (8,007) |
| Changes in cash and cash eq. | (162) | 517 | 7,195 | 8,107 | 8,576 |
| Closing cash and cash eq. | 3,633 | 4,150 | 11,346 | 19,453 | 28,029 |

Per Share

| Y/E 31 Mar (Rs) | FY18A | FY19A | FY20E | FY21E | FY22E |
|----------------------|-------|-------|-------|-------|-------|
| Reported EPS | 63.5 | 86.5 | 85.9 | 100.3 | 108.3 |
| Adjusted EPS | 63.5 | 86.5 | 85.9 | 100.3 | 108.3 |
| Dividend per share | 21.5 | 28.0 | 30.1 | 35.1 | 37.9 |
| Book value per share | 220.5 | 279.2 | 328.5 | 386.6 | 449.2 |

Valuations Ratios

| Y/E 31 Mar (x) | FY18A | FY19A | FY20E | FY21E | FY22E |
|----------------|-------|-------|-------|-------|-------|
| EV/Sales | 3.8 | 2.9 | 2.7 | 2.4 | 2.0 |
| EV/EBITDA | 23.4 | 14.8 | 14.4 | 12.0 | 10.4 |
| Adjusted P/E | 25.4 | 18.6 | 18.7 | 16.1 | 14.9 |
| P/BV | 7.3 | 5.8 | 4.9 | 4.2 | 3.6 |

DuPont Analysis

| Y/E 31 Mar (%) | FY18A | FY19A | FY20E | FY21E | FY22E |
|---------------------------------|-------|-------|-------|-------|-------|
| Tax burden (Net profit/PBT) | 77.2 | 74.7 | 75.1 | 74.5 | 74.5 |
| Interest burden (PBT/EBIT) | 139.8 | 116.8 | 120.7 | 119.8 | 115.7 |
| EBIT margin (EBIT/Revenue) | 14.1 | 18.4 | 16.1 | 17.2 | 17.2 |
| Asset turnover (Revenue/Avg TA) | 148.9 | 156.8 | 143.7 | 138.0 | 133.4 |
| Leverage (Avg TA/Avg Equity) | 1.4 | 1.4 | 1.3 | 1.3 | 1.3 |
| Adjusted ROAE | 31.8 | 34.6 | 28.3 | 28.1 | 25.9 |

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

Ratio Analysis

| Y/E 31 Mar | FY18A | FY19A | FY20E | FY21E | FY22E |
|--|-------|-------|-------|-------|-------|
| YoY growth (%) | | | | | |
| Revenue | 12.4 | 29.3 | 9.3 | 11.2 | 11.7 |
| EBITDA | (3.4) | 58.6 | 2.1 | 17.5 | 11.7 |
| Adjusted EPS | (8.2) | 36.1 | (0.6) | 16.8 | 7.9 |
| Profitability & Return ratios (%) | | | | | |
| EBITDA margin | 16.3 | 19.9 | 18.6 | 19.7 | 19.7 |
| EBIT margin | 14.1 | 18.4 | 16.1 | 17.2 | 17.2 |
| Adjusted profit margin | 15.2 | 16.0 | 14.6 | 15.3 | 14.8 |
| Adjusted ROAE | 31.8 | 34.6 | 28.3 | 28.1 | 25.9 |
| ROCE | 32.8 | 43.4 | 36.5 | 41.6 | 44.4 |
| Working capital days (days) | | | | | |
| Receivables | 85 | 89 | 75 | 62 | 62 |
| Inventory | 0 | 0 | 0 | 0 | 0 |
| Payables | 12 | 11 | 11 | 11 | 11 |
| Ratios (x) | | | | | |
| Gross asset turnover | 13.6 | 14.2 | 12.9 | 14.3 | 16.0 |
| Current ratio | 2.2 | 2.2 | 2.5 | 2.9 | 3.1 |
| Net interest coverage ratio | NA | NA | NA | NA | NA |
| Adjusted debt/equity | (0.1) | (0.1) | (0.2) | (0.3) | (0.4) |

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

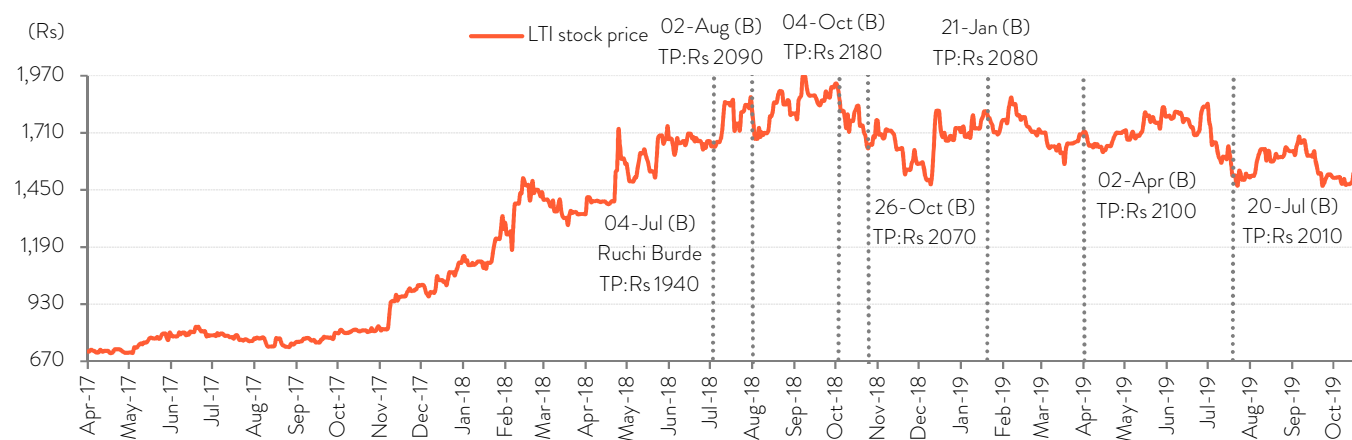
ADD – Expected return from >+5% to +15%

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: L&T INFOTECH (LTI IN)



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

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