

BUY

TP: Rs 3,590 | ▲ 16%

L&T INFOTECH

| IT Services

| 21 October 2020

Robust growth and pipeline; margin shines

L&T Infotech's (LTI) Q2FY21 revenue beat estimates, with 2.3% QoQ CC growth due to an uptick in the manufacturing and BFS verticals. Operating margins stood at a record high of 19.9% backed by increased offshoring and tight SG&A cost control. We raise FY21/FY22/FY23 EPS by 12%/10%/9% given LTI's strong revenue mix, favourable offshore presence, client mining skills and robust leadership. Rolling valuations over, we move to a new Sep'21 TP of Rs 3,590 (vs. Rs 3,290), set at an unchanged target P/E of 27x. BUY.

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Record high EBIT margin: In line with the V-shaped recovery across the sector, LTI's 2.3% QoQ CC revenue growth (against 1.4% est.) was driven by traction in BFS and manufacturing. The top client continues to grow well. Insurance, retail, CPG, pharma and hi-tech remained weak due to the Covid impact. Two key areas of emerging demand are cloud (partnership with hyperscalers such as AWS and Google Cloud) and data-driven products. EBIT margin stood at an all-time high of 19.9% (17.8% est.), increasing 240bps QoQ amid LTI completing five years of operations.

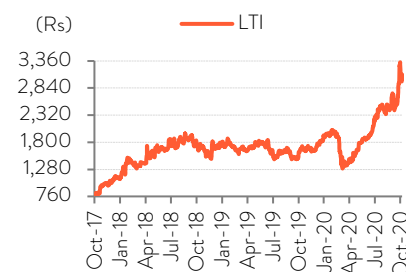
TCV recovery: Q2 TCV stood at US\$ 40mn, recovering QoQ but still down 60% YoY. As per management, large deals are taking longer to close post Covid-19. Q2 deal wins came from hi-tech, manufacturing and BFS, including new Fortune-500 clients. A total of 20 new logos were added across verticals.

Increased FY21 visibility: Management outlook remains cautiously positive on the back of a healthy deal pipeline and strong client mining. The Q3FY21 outlook is upbeat as revenue has already crossed Q4FY20 figures QTD. PAT margin guidance for FY21 is in the range of 14-15%, despite salary hikes and hiring starting from Jan'21, as LTI will continue leveraging offshoring of work.

| | |
|------------------|-------------------|
| Ticker/Price | LTI IN/Rs 3,100 |
| Market cap | US\$ 7.4bn |
| Shares o/s | 176mn |
| 3M ADV | US\$ 12.3mn |
| 52wk high/low | Rs 3,513/Rs 1,210 |
| Promoter/FPI/DII | 75%/8%/10% |

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

| Y/E 31 Mar | FY19A | FY20A | FY21E | FY22E | FY23E |
|-------------------------|--------|---------|---------|---------|---------|
| Total revenue (Rs mn) | 94,458 | 108,786 | 126,041 | 156,270 | 180,528 |
| EBITDA (Rs mn) | 18,835 | 20,291 | 26,757 | 30,740 | 35,306 |
| Adj. net profit (Rs mn) | 15,157 | 15,198 | 18,419 | 21,656 | 24,988 |
| Adj. EPS (Rs) | 86.5 | 86.4 | 105.0 | 123.4 | 142.4 |
| Adj. EPS growth (%) | 36.1 | 0.0 | 21.5 | 17.6 | 15.4 |
| Adj. ROAE (%) | 34.6 | 29.5 | 31.0 | 30.5 | 29.6 |
| Adj. P/E (x) | 35.9 | 35.9 | 29.5 | 25.1 | 21.8 |
| EV/EBITDA (x) | 28.8 | 26.7 | 20.3 | 17.7 | 15.2 |

Source: Company, BOBCAPS Research

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Other highlights

- LTI's CEO believes that the dichotomy between economic indicators and technology spend is increasing post Covid. Technology has proven to be a redeeming factor in current difficult times. Organisations now need to reimagine their operating models, incorporating digital transformation to remain relevant in the marketplace. This in turn is driving growth in the digital and cloud business.
- Management is hopeful of sustaining margin benefits from the pandemic by continued leveraging of parameters such as offshoring and increased operational efficiency.
- In keeping with the likes of Infosys and HCL Tech, LTI launched Canvas PolarSled, a cloud migration framework to help enterprises accelerate their data transition to Snowflake, the company's cloud data platform.
- Europe posted sharp growth at 16% QoQ USD in Q2 as enterprises began recovering from lockdown.
- DSO improved substantially, standing at 62 days vs. 70 days in Q1.
- The board has declared first interim dividend for FY21, at Rs 15/sh.

FIG 1 – QUARTERLY PERFORMANCE

| (Rs mn) | Q2FY21 | Q2FY20 | YoY (%) | Q1FY21 | QoQ (%) |
|---------------------------|--------------|--------------|--------------|--------------|--------------|
| Revenues (US\$ mn) | 404.5 | 363.8 | 11.2 | 390.3 | 3.6 |
| Revenue | 29,984 | 25,707 | 16.6 | 29,492 | 1.7 |
| Operating Expenditure | 23,128 | 21,050 | 9.9 | 23,570 | (1.9) |
| Cost of revenues | 19,537 | 17,525 | 11.5 | 19,916 | (1.9) |
| as % of sales | 65.2 | 68.2 | - | 67.5 | - |
| SG&A expenses | 3,591 | 3,525 | 1.9 | 3,654 | (1.7) |
| as % of sales | 12.0 | 13.7 | - | 12.4 | - |
| EBITDA | 6,856 | 4,657 | 47.2 | 5,922 | 15.8 |
| Depreciation | 899 | 664 | 35.4 | 781 | 15.1 |
| EBIT | 5,957 | 3,993 | 49.2 | 5,141 | 15.9 |
| Other Income | 174 | 739 | - | 450 | - |
| PBT | 6,131 | 4,732 | 29.6 | 5,591 | 9.7 |
| Total Tax | 1,563 | 1,130 | 38.3 | 1,425 | 9.7 |
| Reported PAT | 4,568 | 3,602 | 26.8 | 4,166 | 9.6 |
| Reported EPS | 26.0 | 20.5 | 26.9 | 23.7 | 9.6 |
| Margins (%) | | | (bps) | | (bps) |
| EBITDA | 22.9 | 18.1 | 470 | 20.1 | 280 |
| EBIT | 19.9 | 15.5 | 430 | 17.4 | 240 |
| EBT | 20.4 | 18.4 | 200 | 19.0 | 150 |
| PAT | 15.2 | 14.0 | 120 | 14.1 | 110 |
| Effective Tax rate | 25.5 | 23.9 | 160 | 25.5 | - |

Source: BOBCAPS Research

FIG 2 – OPERATING METRICS

| (in US\$ terms) | Q2FY21 (% Contr. to Revenue) | Growth | |
|---------------------------------------|---------------------------------|---------|---------|
| | | QoQ (%) | YoY (%) |
| Revenue by Vertical | | | |
| BFS | 29.9 | 11.9 | 22.7 |
| Insurance | 16.0 | (3.6) | (4.9) |
| Manufacturing | 16.2 | 6.3 | 9.8 |
| Energy & Process | 10.6 | 1.7 | (2.6) |
| CPG, Retail & Pharma | 11.0 | (0.9) | 6.4 |
| High-Tech, Media & Entertainment | 10.6 | (5.3) | 9.1 |
| Others | 5.7 | 9.4 | 81.1 |
| Revenue by Geography | | | |
| North America | 68.7 | 0.6 | 11.2 |
| Europe | 16.1 | 15.9 | 9.2 |
| India | 6.9 | 3.6 | 27.9 |
| RoW | 8.2 | 7.6 | 2.4 |
| Client Contribution to Revenue | | | |
| Top 5 clients | 30.0 | 1.9 | 5.2 |
| Top 10 clients | 42.9 | 2.4 | 4.8 |
| Top 20 clients | 57.8 | 2.9 | 4.7 |
| Non top 20 client revenues | 42.2 | 4.6 | 21.6 |
| Digital Revenues | 42.9 | 5.9 | 18.4 |

Source: BOBCAPS Research

Valuation methodology

Overall, LTI has outperformed management's earlier conservative outlook for Q2FY21. We increase FY21/FY22/FY23 EPS estimates by 12%/10%/9% to factor in the Q2 performance. Rolling valuations forward, our Sep'21 target price increases from Rs 3,290 to Rs 3,590, based on an unchanged one-year forward P/E multiple of 27x.

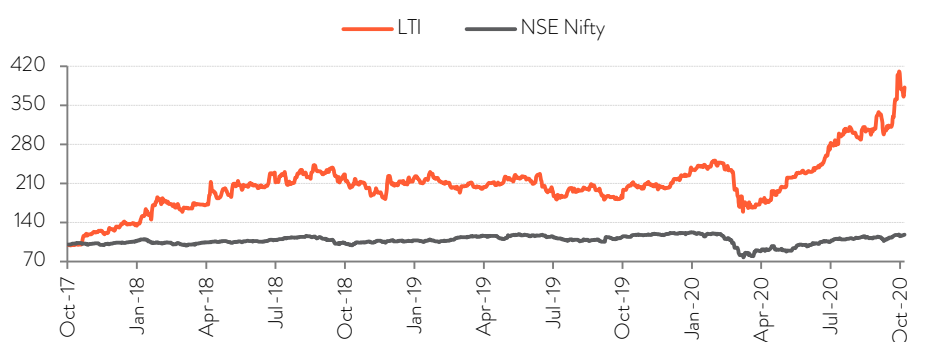
Our BUY rating is justified by LTI's best-in-class fundamentals among IT mid-caps. The company continues to exhibit strong growth leadership amid current challenging times backed by a robust sales engine, marquee clientele and evolving service offerings, which will pave the way for a swift growth rebound post crisis. The share price has risen 31% QoQ in Q2FY21 and we see further upside potential.

FIG 3 – REVISED ESTIMATES

| (Rs mn) | FY21E | | | FY22E | | | FY23E | | |
|--------------------|---------|---------|------------|---------|---------|------------|---------|---------|------------|
| | Old | New | Change (%) | Old | New | Change (%) | Old | New | Change (%) |
| Revenues (US\$ mn) | 1,597 | 1,673 | 4.8 | 1,843 | 2,003 | 8.7 | 2,110 | 2,314 | 9.7 |
| YoY growth (%) | 4.7 | 9.8 | - | 15.4 | 19.7 | - | 14.5 | 15.5 | - |
| Revenues | 121,780 | 126,041 | 3.5 | 143,715 | 156,270 | 8.7 | 164,544 | 180,528 | 9.7 |
| EBITDA | 23,412 | 26,757 | 14.3 | 27,922 | 30,740 | 10.1 | 32,180 | 35,306 | 9.7 |
| EBITDA margins (%) | 19.2 | 21.2 | - | 19.4 | 19.7 | - | 19.6 | 19.6 | - |
| Net profits | 16,378 | 18,419 | 12.5 | 19,723 | 21,656 | 9.8 | 22,874 | 24,988 | 9.2 |
| EPS (Rs) | 93.3 | 105.0 | 12.5 | 112.4 | 123.4 | 9.8 | 130.3 | 142.4 | 9.2 |

Source: BOBCAPS Research

FIG 4 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- Steady large deal wins are critical for the company to sustain its strong growth traction. An inability to do so may derail growth.
- Unsustainable margins

FINANCIALS

Income Statement

| Y/E 31 Mar (Rs mn) | FY19A | FY20A | FY21E | FY22E | FY23E |
|--------------------------------|---------------|----------------|----------------|----------------|----------------|
| Total revenue | 94,458 | 108,786 | 126,041 | 156,270 | 180,528 |
| EBITDA | 18,835 | 20,291 | 26,757 | 30,740 | 35,306 |
| Depreciation | 1,471 | 2,731 | 3,677 | 3,907 | 4,513 |
| EBIT | 17,364 | 17,560 | 23,080 | 26,833 | 30,793 |
| Net interest income/(expenses) | 0 | 0 | 0 | 0 | 0 |
| Other income/(expenses) | 2,915 | 2,463 | 1,556 | 2,042 | 2,525 |
| Exceptional items | 0 | 0 | 0 | 0 | 0 |
| EBT | 20,279 | 20,023 | 24,635 | 28,875 | 33,318 |
| Income taxes | 5,122 | 4,825 | 6,216 | 7,219 | 8,329 |
| Extraordinary items | 0 | 0 | 0 | 0 | 0 |
| Min. int./Inc. from associates | 0 | 0 | 0 | 0 | 0 |
| Reported net profit | 15,157 | 15,198 | 18,419 | 21,656 | 24,988 |
| Adjustments | 0 | 0 | 0 | 0 | 0 |
| Adjusted net profit | 15,157 | 15,198 | 18,419 | 21,656 | 24,988 |

Balance Sheet

| Y/E 31 Mar (Rs mn) | FY19A | FY20A | FY21E | FY22E | FY23E |
|---------------------------------------|---------------|---------------|----------------|----------------|----------------|
| Accounts payables | 0 | 0 | 0 | 0 | 0 |
| Other current liabilities | 15,291 | 23,618 | 27,364 | 33,927 | 39,193 |
| Provisions | 2,402 | 2,908 | 3,369 | 4,177 | 4,826 |
| Debt funds | 0 | 7,571 | 7,571 | 7,571 | 7,571 |
| Other liabilities | 56 | 101 | 101 | 101 | 101 |
| Equity capital | 171 | 174 | 174 | 174 | 174 |
| Reserves & surplus | 48,772 | 53,877 | 64,534 | 77,064 | 91,523 |
| Shareholders' fund | 48,943 | 54,051 | 64,708 | 77,238 | 91,697 |
| Total liabilities and equities | 66,692 | 88,249 | 103,114 | 123,015 | 143,388 |
| Cash and cash eq. | 4,150 | 5,252 | 11,377 | 23,598 | 34,761 |
| Accounts receivables | 23,845 | 27,541 | 34,532 | 38,532 | 44,514 |
| Inventories | 0 | 0 | 0 | 0 | 0 |
| Other current assets | 10,878 | 10,442 | 12,086 | 14,985 | 17,311 |
| Investments | 17,402 | 22,186 | 22,186 | 22,186 | 22,186 |
| Net fixed assets | 8,031 | 19,788 | 19,892 | 20,674 | 21,576 |
| CWIP | 0 | 0 | 0 | 0 | 0 |
| Intangible assets | 0 | 1,316 | 1,316 | 1,316 | 1,316 |
| Deferred tax assets, net | 2,386 | 3,039 | 3,039 | 3,039 | 3,039 |
| Other assets | 0 | 0 | 0 | 0 | 0 |
| Total assets | 66,692 | 88,248 | 103,113 | 123,014 | 143,387 |

Source: Company, BOBCAPS Research

Cash Flows

| Y/E 31 Mar (Rs mn) | FY19A | FY20A | FY21E | FY22E | FY23E |
|-------------------------------------|----------------|----------------|----------------|----------------|-----------------|
| Net income + Depreciation | 16,628 | 17,929 | 22,096 | 25,563 | 29,501 |
| Interest expenses | (1,089) | (342) | (1,422) | (1,560) | (2,293) |
| Non-cash adjustments | 0 | 0 | 0 | 0 | 0 |
| Changes in working capital | (2,665) | 5,573 | (4,427) | 472 | (2,392) |
| Other operating cash flows | 1,010 | (6,887) | 0 | 0 | 0 |
| Cash flow from operations | 13,884 | 16,273 | 16,246 | 24,475 | 24,816 |
| Capital expenditures | (4,221) | (5,480) | (3,781) | (4,688) | (5,416) |
| Change in investments | (4,324) | 0 | 0 | 0 | 0 |
| Other investing cash flows | 1,089 | (3,287) | 1,422 | 1,560 | 2,293 |
| Cash flow from investing | (7,456) | (8,767) | (2,359) | (3,129) | (3,123) |
| Equities issued/Others | 0 | 0 | 0 | 0 | 0 |
| Debt raised/repaid | 0 | 0 | 0 | 0 | 0 |
| Interest expenses | 0 | 0 | 0 | 0 | 0 |
| Dividends paid | (5,911) | (6,404) | (7,762) | (9,126) | (10,530) |
| Other financing cash flows | 0 | 0 | 0 | 0 | 0 |
| Cash flow from financing | (5,911) | (6,404) | (7,762) | (9,126) | (10,530) |
| Changes in cash and cash eq. | 517 | 1,102 | 6,125 | 12,221 | 11,163 |
| Closing cash and cash eq. | 4,150 | 5,252 | 11,377 | 23,598 | 34,761 |

Per Share

| Y/E 31 Mar (Rs) | FY19A | FY20A | FY21E | FY22E | FY23E |
|----------------------|-------|-------|-------|-------|-------|
| Reported EPS | 86.5 | 86.4 | 105.0 | 123.4 | 142.4 |
| Adjusted EPS | 86.5 | 86.4 | 105.0 | 123.4 | 142.4 |
| Dividend per share | 28.0 | 30.2 | 36.7 | 43.2 | 49.8 |
| Book value per share | 279.2 | 307.3 | 368.7 | 440.1 | 522.5 |

Valuations Ratios

| Y/E 31 Mar (x) | FY19A | FY20A | FY21E | FY22E | FY23E |
|----------------|-------|-------|-------|-------|-------|
| EV/Sales | 5.7 | 5.0 | 4.3 | 3.5 | 3.0 |
| EV/EBITDA | 28.8 | 26.7 | 20.3 | 17.7 | 15.2 |
| Adjusted P/E | 35.9 | 35.9 | 29.5 | 25.1 | 21.8 |
| P/BV | 11.1 | 10.1 | 8.4 | 7.0 | 5.9 |

DuPont Analysis

| Y/E 31 Mar (%) | FY19A | FY20A | FY21E | FY22E | FY23E |
|---------------------------------|-------|-------|-------|-------|-------|
| Tax burden (Net profit/PBT) | 74.7 | 75.9 | 74.8 | 75.0 | 75.0 |
| Interest burden (PBT/EBIT) | 116.8 | 114.0 | 106.7 | 107.6 | 108.2 |
| EBIT margin (EBIT/Revenue) | 18.4 | 16.1 | 18.3 | 17.2 | 17.1 |
| Asset turnover (Revenue/Avg TA) | 156.8 | 140.4 | 131.7 | 138.2 | 135.5 |
| Leverage (Avg TA/Avg Equity) | 1.4 | 1.5 | 1.6 | 1.6 | 1.6 |
| Adjusted ROAE | 34.6 | 29.5 | 31.0 | 30.5 | 29.6 |

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

Ratio Analysis

| Y/E 31 Mar | FY19A | FY20A | FY21E | FY22E | FY23E |
|--|-------|-------|-------|-------|-------|
| YoY growth (%) | | | | | |
| Revenue | 29.3 | 15.2 | 15.9 | 24.0 | 15.5 |
| EBITDA | 58.6 | 7.7 | 31.9 | 14.9 | 14.9 |
| Adjusted EPS | 36.1 | 0.0 | 21.5 | 17.6 | 15.4 |
| Profitability & Return ratios (%) | | | | | |
| EBITDA margin | 19.9 | 18.7 | 21.2 | 19.7 | 19.6 |
| EBIT margin | 18.4 | 16.1 | 18.3 | 17.2 | 17.1 |
| Adjusted profit margin | 16.0 | 14.0 | 14.6 | 13.9 | 13.8 |
| Adjusted ROAE | 34.6 | 29.5 | 31.0 | 30.5 | 29.6 |
| ROCE | 43.4 | 34.7 | 39.3 | 43.9 | 48.9 |
| Working capital days (days) | | | | | |
| Receivables | 89 | 86 | 90 | 85 | 84 |
| Inventory | 0 | 0 | 0 | 0 | 0 |
| Payables | 11 | 11 | 12 | 11 | 11 |
| Ratios (x) | | | | | |
| Gross asset turnover | 14.2 | 7.8 | 6.4 | 7.7 | 8.5 |
| Current ratio | 2.2 | 1.6 | 1.9 | 2.0 | 2.2 |
| Net interest coverage ratio | NA | NA | NA | NA | NA |
| Adjusted debt/equity | (0.1) | 0.0 | (0.1) | (0.2) | (0.3) |

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

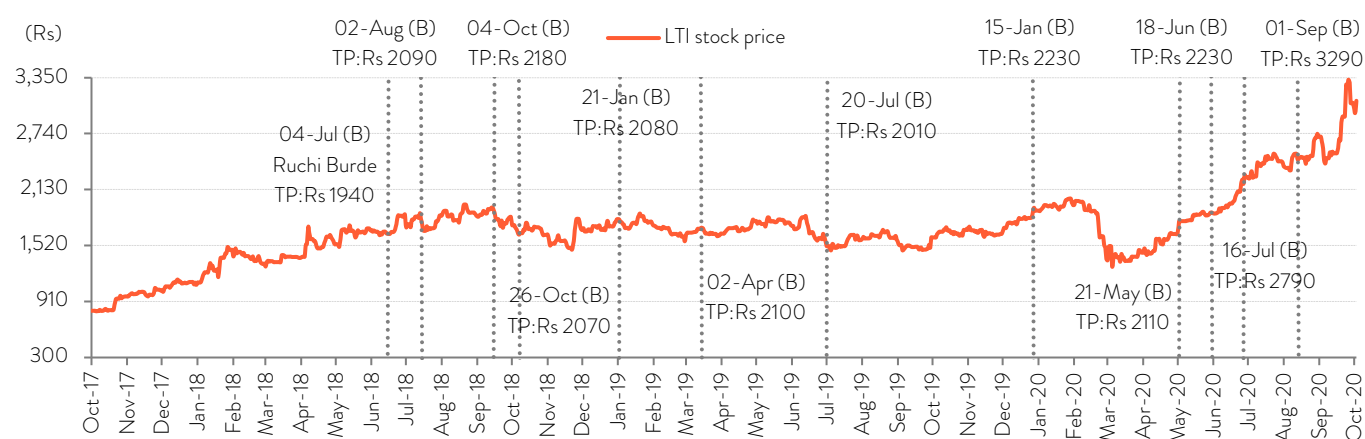
ADD – Expected return from >+5% to +15%

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)

RATINGS AND TARGET PRICE (3-YEAR HISTORY): L&T INFOTECH (LTI IN)



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

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