

ADD

TP: Rs 1,210 | ▲ 6%

INFOSYS

| IT Services

| 14 October 2020

Stellar recovery based on strong TCV

Infosys' (INFO) Q2 topline grew ahead of estimates at 4% QoQ CC and it also posted its highest ever TCV of US\$ 3.15bn. Cloud migration, automation-based cost takeout and vendor consolidation were primary growth drivers. Management upped FY21 guidance to 2-3% CC vs. 0-2% earlier, which indicates a lukewarm H2. We hike FY21/FY22/FY23 EPS by 10%/9%/7% and raise our target P/E by 10% to 23x, baking in the enhanced performance, pipeline and outlook. On rollover, we have a new Sep'21 TP of Rs 1,210 (vs. Rs 1,020). Retain ADD.

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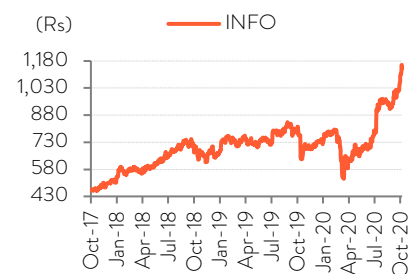
Strong operational performance: On the heels of a solid Q1, INFO beat our expectations, clocking 4% QoQ CC revenue growth vs. 2.2% estimated. Growth was driven by exceptional traction in hi-tech, BFSI and retail. BFSI saw a pickup in the mortgage and lending service subsegments as well as digital transformation programmes. Digital business grew 12.8% QoQ, forming 47% of revenues. EBIT margin at 25.3% rose 260bps QoQ helped by lower employee and sales costs from an improved onsite-offshore mix. INFO will carry out salary hikes and promotions from Q3 through to Jan'21.

Ticker/Price	INFO IN/Rs 1,137
Market cap	US\$ 67.5bn
Shares o/s	4,349mn
3M ADV	US\$ 163.8mn
52wk high/low	Rs 1,166/Rs 509
Promoter/FPI/DII	13%/35%/52%

Source: NSE

Robust deal pipeline: INFO clocked its highest ever deal TCV of US\$ 3.15bn, an increase of 81% QoQ and 11% YoY. Net new deals stood at 86% of TCV. Out of the 16 large contracts signed in Q2FY21, 6 were from the BFSI vertical, 3 from retail, 2 from communication and hi-tech each, and 1 each from energy-utilities, manufacturing, and others.

STOCK PERFORMANCE



Upbeat outlook: Management has upgraded its FY21 growth guidance to 2-3% YoY CC from 0-2% earlier based on the stellar TCV showing. The Vanguard deal will also ramp-up from Q3FY21. Operating margin guidance for the year has been revised upward to 23-24% from 21-23%. Q3 will be impacted by furloughs. Based on the guidance, growth will normalise in H2FY21.

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	826,760	907,910	1,000,614	1,141,036	1,248,535
EBITDA (Rs mn)	208,890	222,680	272,750	306,794	327,875
Adj. net profit (Rs mn)	154,100	167,350	192,696	215,908	231,657
Adj. EPS (Rs)	35.4	39.0	45.2	50.7	54.4
Adj. EPS growth (%)	(4.0)	10.3	15.9	12.0	7.3
Adj. ROAE (%)	24.5	26.5	27.7	27.7	26.7
Adj. P/E (x)	32.1	29.1	25.1	22.4	20.9
EV/EBITDA (x)	22.7	21.4	17.5	15.5	14.5

Source: Company, BOBCAPS Research

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Other key highlights

- INFO launched Cobalt – a set of services, solutions and platforms for enterprises to accelerate their cloud journey – in Q3FY21. It consists of 14,000 cloud components and has been built based on strong partnerships with cloud hyper-scalers in response to increased demand post Covid-19.
- The company is pushing for greater localisation in the US. It plans to hire 12,000 US workers over the next two years, taking its total US local employee count to 25,000. This push comes amidst changing H1B visa rules i.e. increase in minimum wage.
- INFO carried out three acquisitions in the last three months: GuideVision (specialising in enterprise services management consultancy), Blue Acorn (Adobe specialist) and Kaleidoscope (product design).
- Q2FY21 voluntary attrition for IT services dropped to 7.8% from 18.3% in the year-ago quarter – marking one of the company’s lowest ever attrition rates.
- 99% of INFO’s workforce continues to work from home.
- The board has declared interim dividend of Rs 12/sh.

FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)
Revenues (US\$ mn)	3,312	3,210	3.2	3,121	6.1
Revenue	245,700	226,290	8.6	236,650	3.8
Operating Expenditure	174,870	169,900	2.9	175,180	(0.2)
Cost of revenues	149,160	143,520	3.9	149,370	(0.1)
as % of sales	60.7	63.4	-	63.1	-
SG&A expenses	25,710	26,380	(2.5)	25,810	(0.4)
as % of sales	10.5	11.7	-	10.9	-
EBITDA	70,830	56,390	25.6	61,470	15.2
Depreciation	8,550	7,270	17.6	7,560	13.1
EBIT	62,280	49,120	26.8	53,910	15.5
Other Income	5,700	6,260	-	4,750	-
PBT	67,500	55,380	21.9	58,080	16.2
Total Tax	18,920	14,590	29.7	15,200	24.5
Adjusted PAT	48,580	40,790	19.1	42,880	13.3
(Profit)/loss from JV's/Ass/MI	130	0	-	0	-
APAT after MI	48,450	40,790	18.8	42,880	13.0
Extra ordinary items	-	0	-	(580)	-
Reported PAT	48,450	40,790	18.8	42,300	14.5
Reported EPS	11.4	9.4	20.8	10.0	14.3
Margins (%)			(bps)		(bps)
EBITDA	28.8	24.9	391	26.0	285
EBIT	25.3	21.7	364	22.8	257
EBT	27.5	24.5	300	24.5	293
PAT	19.7	18.0	169	17.9	184
Effective tax rate	28.0	26.3	168.4	26.2	186

Source: BOBCAPS Research

FIG 2 – OPERATING METRICS

(in US\$ terms)	Q2FY21 (% Contr. to Rev)	Growth	
		QoQ (%)	YoY (%)
TCV of deal wins (US\$ mn)	3,150	81.0	10.6
Digital Revenues	47.3	12.8	27.4
Revenue by Geography			
North America	60.7	4.7	2.0
Europe	24.3	7.4	4.0
India	3.0	9.8	14.6
ROW	12.0	9.8	4.9
Revenue by Industry Group			
BFSI	32.0	7.8	3.5
Retail	14.9	10.6	1.1
Communications	12.6	(0.2)	(0.8)
Energy, Utilities, Resources and Services	12.3	2.0	(3.1)
Manufacturing	9.1	1.7	(7.0)
Hi Tech	9.1	11.0	23.5
Life Sciences	6.8	7.7	9.6
Others	3.2	9.5	27.0
Client Concentration			
Top 10 Clients	18.7	2.8	0.5
Non-Top 10 Clients	81.3	6.9	3.8
(%)			
	Q2FY21	Q1FY21	Q2FY20
Onsite-Offshore Effort Split			
Onsite	26.1	28.0	28.2
Offshore	73.9	72.0	71.8
Utilisation Measures (IT Services and Consulting)			
Including trainees	80.6	78.2	81.6
Excluding trainees	83.6	81.2	84.9

Source: BOBCAPS Research

Valuation methodology

We increase FY21/FY22/FY23 EPS estimates by 10%/9%/7% to factor in the above-estimated Q2 performance and robust revenue and margin guidance for FY21. Rolling valuations over, we have a revised Sep'21 target price of Rs 1,210 (Rs 1,020 earlier), set at a one-year forward target P/E of 23.1x – a 10% increase from our earlier multiple of 21x.

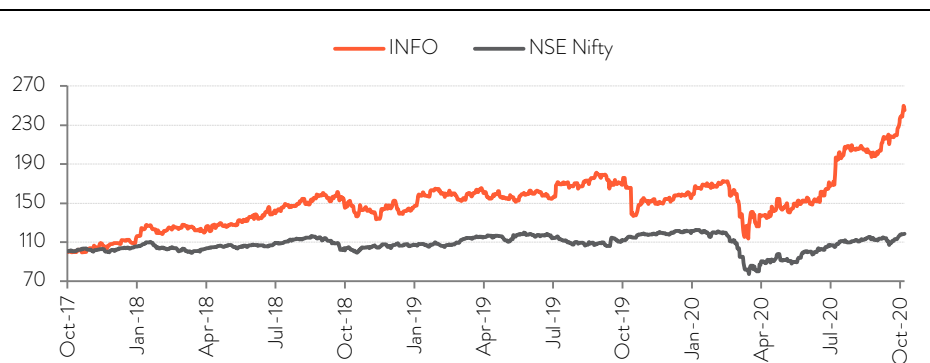
We have raised our target multiple based on (1) INFO's above-estimated Q2FY21 revenue and margins, (2) the FY21 guidance upgrade which has come despite an uncertain economic environment and indicates growth normalisation in H2FY21, (3) a stronger deal pipeline, and (4) possible market share gains in the emerging areas of hi-tech and life sciences. That said, the guided 23-24% margin band does not appear sustainable beyond FY21, in our view. Maintain ADD.

FIG 3 – REVISED ESTIMATES

(Rs mn)	FY21E			FY22E			FY23E		
	Old	New	Change (%)	Old	New	Change (%)	Old	New	Change (%)
Revenues (US\$ mn)	12,800	13,274	3.7	14,285	14,629	2.4	15,686	16,007	2.0
YoY revenue growth (%)	0.2	3.9	-	11.6	10.2	-	7.2	9.4	-
Revenues	977,107	1,000,614	2.4	1,114,204	1,141,036	2.4	1,223,534	1,248,535	2.0
EBITDA	252,141	272,750	8.2	292,407	306,794	4.9	316,444	327,875	3.6
EBITDA margins (%)	25.8	27.3	-	26.2	26.9	-	25.9	26.3	-
EBIT margins (%)	22.5	23.9	-	22.8	23.5	-	22.5	22.9	-
Net profits	174,605	192,696	10.4	197,489	215,908	9.3	215,398	231,657	7.5
EPS (Rs)	41.1	45.2	9.9	46.5	50.7	8.9	50.7	54.4	7.1

Source: BOBCAPS Research

FIG 4 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

Downside risks to our estimates include:

- a more pronounced adverse impact of Covid-19, global trade tensions, Brexit and other negative external events, leading to weaker-than-expected demand,
- slower deal conversions to revenue, and
- below-expected operating margins for new engagements/renewals.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	826,760	907,910	1,000,614	1,141,036	1,248,535
EBITDA	208,890	222,680	272,750	306,794	327,875
Depreciation	20,100	28,930	33,651	38,170	41,465
EBIT	188,790	193,750	239,099	268,623	286,410
Net interest income/(expenses)	21,550	16,120	16,938	16,341	20,129
Other income/(expenses)	28,830	28,030	24,768	27,141	30,929
Exceptional items	(7,210)	0	0	0	0
EBT	210,410	221,780	263,867	295,764	317,339
Income taxes	56,310	53,680	71,171	79,856	85,681
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	0	750	0	0	0
Reported net profit	154,100	167,350	192,696	215,908	231,657
Adjustments	0	0	0	0	0
Adjusted net profit	154,100	167,350	192,696	215,908	231,657

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	0	0	0	0	0
Other current liabilities	168,940	263,520	211,088	240,712	263,389
Provisions	5,230	5,720	8,224	9,378	10,262
Debt funds	0	0	0	0	0
Other liabilities	0	0	0	0	0
Equity capital	21,700	21,220	21,220	21,220	21,220
Reserves & surplus	585,160	637,220	713,961	799,946	892,204
Shareholders' fund	606,860	658,440	735,181	821,166	913,424
Total liabilities and equities	781,030	927,680	954,494	1,071,256	1,187,075
Cash and cash eq.	165,060	186,490	163,477	221,755	294,476
Accounts receivables	136,990	184,870	205,606	234,459	256,548
Inventories	0	0	0	0	0
Other current assets	46,550	71,210	68,535	78,153	85,516
Investments	124,990	87,920	87,920	87,920	87,920
Net fixed assets	149,560	250,530	247,032	243,962	239,937
CWIP	0	41,680	41,680	41,680	41,680
Intangible assets	0	0	0	0	0
Deferred tax assets, net	13,000	17,440	17,440	17,440	17,440
Other assets	144,880	129,220	164,485	187,568	205,239
Total assets	781,030	927,680	954,494	1,071,257	1,187,075

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	174,200	196,280	226,347	254,078	273,122
Interest expenses	(28,830)	(28,030)	(24,768)	(27,141)	(30,929)
Non-cash adjustments	0	0	0	0	0
Changes in working capital	16,350	38,190	(103,253)	(30,777)	(23,561)
Other operating cash flows	(98,005)	49,198	0	0	0
Cash flow from operations	63,715	255,638	98,326	196,160	218,632
Capital expenditures	(23,650)	(88,220)	(30,153)	(35,100)	(37,440)
Change in investments	0	0	0	0	0
Other investing cash flows	28,830	28,030	24,768	27,141	30,929
Cash flow from investing	5,180	(60,190)	(5,384)	(7,959)	(6,511)
Equities issued/Others	(9,313)	(73,287)	0	0	0
Debt raised/repaid	0	0	0	0	0
Interest expenses	0	0	0	0	0
Dividends paid	(92,730)	(100,703)	(115,955)	(129,923)	(139,400)
Other financing cash flows	0	0	0	0	0
Cash flow from financing	(102,043)	(173,990)	(115,955)	(129,923)	(139,400)
Changes in cash and cash eq.	(33,148)	21,458	(23,014)	58,278	72,721
Closing cash and cash eq.	165,032	186,490	163,477	221,755	294,476

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	35.4	39.0	45.2	50.7	54.4
Adjusted EPS	35.4	39.0	45.2	50.7	54.4
Dividend per share	21.5	19.5	22.6	25.4	27.2
Book value per share	139.3	153.5	172.5	192.7	214.3

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	5.7	5.2	4.8	4.2	3.8
EV/EBITDA	22.7	21.4	17.5	15.5	14.5
Adjusted P/E	32.1	29.1	25.1	22.4	20.9
P/BV	8.2	7.4	6.6	5.9	5.3

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	73.2	75.5	73.0	73.0	73.0
Interest burden (PBT/EBIT)	111.5	114.5	110.4	110.1	110.8
EBIT margin (EBIT/Revenue)	22.8	21.3	23.9	23.5	22.9
Asset turnover (Revenue/Avg TA)	104.7	106.3	106.3	112.7	110.6
Leverage (Avg TA/Avg Equity)	1.3	1.4	1.4	1.3	1.3
Adjusted ROAE	24.5	26.5	27.7	27.7	26.7

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

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	17.2	9.8	10.2	14.0	9.4
EBITDA	9.9	6.6	22.5	12.5	6.9
Adjusted EPS	(4.0)	10.3	15.9	12.0	7.3
Profitability & Return ratios (%)					
EBITDA margin	25.3	24.5	27.3	26.9	26.3
EBIT margin	22.8	21.3	23.9	23.5	22.9
Adjusted profit margin	18.6	18.4	19.3	18.9	18.6
Adjusted ROAE	24.5	26.5	27.7	27.7	26.7
ROCE	31.0	32.1	33.5	33.5	34.3
Working capital days (days)					
Receivables	59	65	71	70	72
Inventory	0	0	0	0	0
Payables	93	115	119	99	100
Ratios (x)					
Gross asset turnover	5.6	4.5	4.0	4.6	5.2
Current ratio	2.8	2.1	2.7	2.9	3.1
Net interest coverage ratio	8.8	12.0	14.1	16.4	14.2
Adjusted debt/equity	(0.3)	(0.3)	(0.2)	(0.3)	(0.3)

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

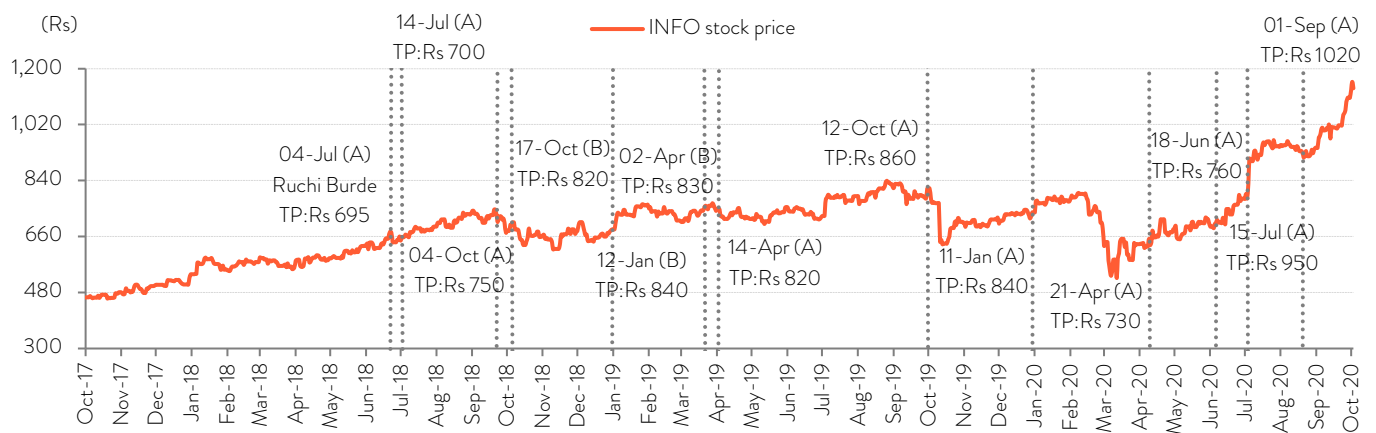
ADD – Expected return from >+5% to +15%

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): INFOSYS (INFO IN)



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

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