

BUY

TP: Rs 2,790 | ▲ 22%

L&T INFOTECH

| IT Services

| 16 July 2020

Resilient show in a challenging quarter

L&T Infotech's (LTI) Q1FY21 revenue was in line with estimates, with a 4.7% QoQ CC decline due to a drop in the manufacturing and energy/utilities verticals. Operating margins bettered expectations backed by tight SG&A cost control. We keep FY21 EPS unchanged and increase FY22 EPS by ~3%, while raising our target P/E multiple by 20% to 24x given LTI's strong revenue mix, favourable offshore presence, client mining skills and robust leadership. Rolling valuations over, we have a new Jun'21 TP of Rs 2,790 (vs. Rs 2,230). BUY.

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Resilient operating performance: LTI's revenue declined 4.7% QoQ CC (-4.8% QoQ in USD terms), in line with our estimate (-4.8% QoQ CC). Utilisation excluding trainees dropped 100bps owing to the pandemic impact. Revenues were affected by significant weakness in the manufacturing and energy/utilities verticals which declined 16.4% and 10% QoQ respectively. Reported EBIT margins rose 70bps QoQ to 17.4%, outperforming our estimate of 17.2%, driven by tight control over SG&A (-120bps QoQ as % of sales).

Ticker/Price	LTI IN/Rs 2,291
Market cap	US\$ 5.4bn
Shares o/s	176mn
3M ADV	US\$ 3.8mn
52wk high/low	Rs 2,336/Rs 1,210
Promoter/FPI/DII	75%/8%/10%

Source: NSE

Large deals slow but chase continues: Despite a challenging Q1, LTI bagged a large BFSI deal in the UK and added 16 new logos, including one Fortune-500 logo from the manufacturing vertical, to its client roster. While large deal wins slowed slightly in Q1 compared to the previous three quarters, management expects some sizeable contract signings in Q2FY21. As per LTI, the FY21 pipeline has risen 19% YoY and is steady across segments, barring the manufacturing and energy/utilities verticals.

STOCK PERFORMANCE



Source: NSE

Comforting outlook: Management expects Q1FY21 to be the trough and recovery to follow. LTI guided Q2 revenues to be flat with a positive bias, and management aims to keep EBIT margins rangebound around Q1 levels (of 17.4%).

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	94,458	108,786	121,780	143,715	164,544
EBITDA (Rs mn)	18,835	20,291	23,412	27,922	32,180
Adj. net profit (Rs mn)	15,157	15,198	16,378	19,723	22,874
Adj. EPS (Rs)	86.5	86.4	93.3	112.4	130.3
Adj. EPS growth (%)	36.1	0.0	8.0	20.4	16.0
Adj. ROAE (%)	34.6	29.5	27.9	28.5	28.0
Adj. P/E (x)	26.5	26.5	24.5	20.4	17.6
EV/EBITDA (x)	21.2	19.7	17.2	14.4	12.3

Source: Company, BOBCAPS Research

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Other highlights

No. of active clients stood at 409, declining by 15 QoQ

Attrition at 15.2% declined 130bps QoQ

- A few customers have been given one-time pricing discounts. LTI has not seen material delays in deal ramp-up yet. The deal pipeline is expected to be stable given the company's limited footprint in travel and non-CPG retail. Hybrid cloud migration has been gaining momentum. Growth recovery will depend on the possibility of a second wave of the pandemic.
- The BFS vertical was affected due to delay in work-from-home approvals. Insurance clients faced significant challenges too. Manufacturing was hit the hardest due to the absence of pass-through revenues in Q1. Hi-tech was flat sequentially. The defence and professional vertical grew ~29% QoQ due to a small base and some India-based project wins.
- Europe revenues plunged 9.2% QoQ. India and ROW also declined heavily.
- LTI followed a three-pronged strategy of focusing on a customer-first approach, operational resilience, and P&L protection to tackle the Covid-19 impact. The salary cycle for July has also been delayed to manage margins.
- LTI Canvas, an integrated platform with Microsoft, delivers the 'everything from home' (XFH) framework. Employees will be returning to offices in a staggered manner. Currently, 99% of LTI's employees have been enabled to work from home.
- In a display of strong receivables management, DSOs decreased by 7 days QoQ to 70 in Q1FY21.

FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q1FY21	Q1FY20	YoY (%)	Q4FY20	QoQ (%)
Revenues (US\$ mn)	390.3	356.5	9.5	409.9	(4.8)
Revenue	29,492.0	24,849.0	18.7	30,119.0	(2.1)
Operating Expenditure	23,570	20,270	16.3	24,338	(3.2)
Cost of revenues	19,916.0	16,625.0	19.8	20,251.0	(1.7)
as % of sales	67.5	66.9	-	67.2	-
SG&A expenses	3,654.0	3,645.0	0.2	4,087.0	(10.6)
as % of sales	12.4	14.7	-	13.6	-
EBITDA	5,922	4,579	29.3	5,781	2.4
Depreciation	781.0	611.0	27.8	747.0	4.6
EBIT	5,141	3,968	29.6	5,034	2.1
Other Income	450.0	812.0	-	479.0	-
PBT	5,591	4,780	17.0	5,513	1.4
Total Tax	1,425.0	1,225.0	16.3	1,239.0	15.0
Reported PAT	4,166	3,555	17.2	4,274	(2.5)
Reported EPS	23.7	20.3	17.0	24.3	(2.3)
Margins (%)			(bps)		(bps)
EBITDA	20.1	18.4	170	19.2	90

(Rs mn)	Q1FY21	Q1FY20	YoY (%)	Q4FY20	QoQ (%)
EBIT	17.4	16.0	150	16.7	70
EBT	19.0	19.2	(30)	18.3	70
PAT	14.1	14.3	(20)	14.2	(10)
Effective Tax rate	25.5	25.6	(10)	22.5	300

Source: BOBCAPS Research

FIG 2 – OPERATING METRICS

	Q1FY21 (% Contr. to Revenue)	Growth (%)	
		QoQ	YoY
Revenue by Vertical			
BFS	27.7	(4.4)	9.5
Insurance	17.2	(2.5)	4.0
Manufacturing	15.8	(16.4)	13.8
Energy & Process	10.8	(9.8)	10.5
CPG, Retail & Pharma	11.5	(2.2)	13.4
High-Tech, Media & Entertainment	11.6	0.4	1.6
Others	5.4	28.5	28.5
Revenue by Geography			
North America	70.8	(2.2)	12.8
Europe	14.4	(9.2)	(1.5)
India	7.9	(3.6)	25.3
RoW	6.9	(18.9)	(11.1)
Client Concentration			
Top 5 clients	30.5	(6.9)	6.7
Top 10 clients	43.4	(9.8)	5.6
Top 20 clients	58.2	(7.3)	1.9
Non top 20 client revenues	41.8	(1.0)	22.0
Digital Revenues	42.0	(1.7)	17.9

Source: BOBCAPS Research

Management highlighted that its top client revenue (featuring in BFS vertical) continued to grow in Q1

Valuation methodology

We increase FY21/FY22 EPS estimates by 0.3%/2.8% as we factor in LTI's largely in-line Q1FY21 performance. We also introduce FY23 EPS at Rs 130.3 and estimate 14.5% dollar revenue growth with 19.6% EBITDA margins.

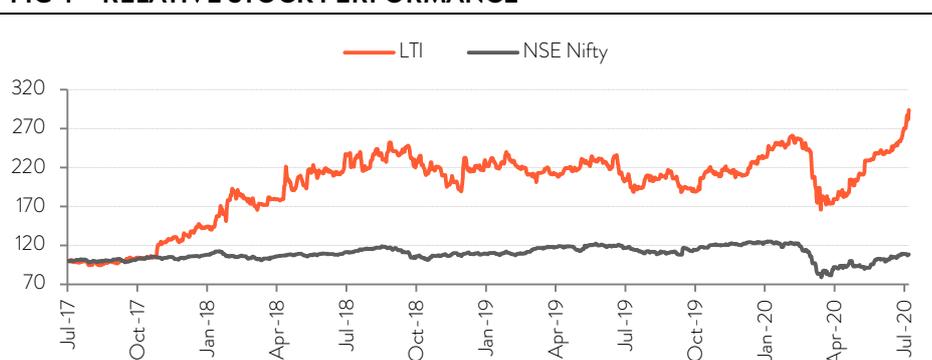
Our Jun'21 target price increases from Rs 2,230 to Rs 2,790, based on a higher one-year forward P/E multiple of 24x (vs. 20x earlier). Our target P/E revision is justified by LTI's best-in-class fundamentals among IT mid-caps. We expect its strong growth leadership in the current challenging times backed by a robust sales engine, marquee clientele and evolving service offerings to pave the path for a swift growth rebound post crisis. Reiterate BUY. We flag the possibility of near-term stock price consolidation post a 21%+ stock price up-move in the last month.

FIG 3 – REVISED ESTIMATES

(Rs mn)	FY21E			FY22E			FY23
	Old	New	Change (%)	Old	New	Change (%)	New
Revenues (US\$ mn)	1,631	1,597	(2.1)	1,788	1,843	3.1	2,110
YoY growth (%)	7.0	4.7	-	9.6	15.4	-	14.5
Revenues	124,777	121,780	(2.4)	139,456	143,715	3.1	164,544
EBITDA	23,410	23,412	0.0	27,092	27,922	3.1	32,180
EBITDA margins (%)	18.8	19.2	-	19.4	19.4	-	19.6
Net profits	16,370	16,378	0.0	19,227	19,723	2.6	22,874
EPS (Rs)	93.1	93.3	0.3	109.3	112.4	2.8	130.3

Source: BOBCAPS Research

FIG 4 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- Sharp fluctuation in exchange rates may materially impact the company's operating profits.
- Steady large deal wins are critical for the company to sustain its strong growth traction. An inability to do so may derail growth.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	94,458	108,786	121,780	143,715	164,544
EBITDA	18,835	20,291	23,412	27,922	32,180
Depreciation	1,471	2,731	3,088	3,593	4,114
EBIT	17,364	17,560	20,323	24,329	28,066
Net interest income/(expenses)	0	0	0	0	0
Other income/(expenses)	2,915	2,463	1,550	1,968	2,432
Exceptional items	0	0	0	0	0
EBT	20,279	20,023	21,873	26,298	30,498
Income taxes	5,122	4,825	5,496	6,574	7,625
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
Reported net profit	15,157	15,198	16,378	19,723	22,874
Adjustments	0	0	0	0	0
Adjusted net profit	15,157	15,198	16,378	19,723	22,874

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	26,439	31,201	35,723
Provisions	2,402	2,908	3,255	3,842	4,398
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	63,353	74,765	88,000
Shareholders' fund	48,943	54,051	63,527	74,939	88,174
Total liabilities and equities	66,692	88,249	100,894	117,654	135,968
Cash and cash eq.	4,150	5,252	10,272	22,139	32,496
Accounts receivables	23,845	27,541	33,364	35,437	40,573
Inventories	0	0	0	0	0
Other current assets	10,878	10,442	11,678	13,781	15,778
Investments	17,402	22,186	22,186	22,186	22,186
Net fixed assets	8,031	19,788	20,353	21,072	21,894
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	100,893	117,653	135,967

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	16,628	17,929	19,466	23,316	26,987
Interest expenses	(1,089)	(342)	(1,334)	(1,493)	(2,205)
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(2,665)	5,573	(3,890)	1,173	(2,054)
Other operating cash flows	1,010	(6,887)	0	0	0
Cash flow from operations	13,884	16,273	14,241	22,996	22,728
Capital expenditures	(4,221)	(5,480)	(3,653)	(4,311)	(4,936)
Change in investments	(4,324)	0	0	0	0
Other investing cash flows	1,089	(3,287)	1,334	1,493	2,205
Cash flow from investing	(7,456)	(8,767)	(2,319)	(2,818)	(2,731)
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)	(6,902)	(8,311)	(9,639)
Other financing cash flows	0	0	0	0	0
Cash flow from financing	(5,911)	(6,404)	(6,902)	(8,311)	(9,639)
Changes in cash and cash eq.	517	1,102	5,020	11,866	10,358
Closing cash and cash eq.	4,150	5,252	10,272	22,139	32,496

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	86.5	86.4	93.3	112.4	130.3
Adjusted EPS	86.5	86.4	93.3	112.4	130.3
Dividend per share	28.0	30.2	32.7	39.3	45.6
Book value per share	279.2	307.3	362.0	427.0	502.5

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	4.2	3.7	3.3	2.8	2.4
EV/EBITDA	21.2	19.7	17.2	14.4	12.3
Adjusted P/E	26.5	26.5	24.5	20.4	17.6
P/BV	8.2	7.5	6.3	5.4	4.6

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	74.7	75.9	74.9	75.0	75.0
Interest burden (PBT/EBIT)	116.8	114.0	107.6	108.1	108.7
EBIT margin (EBIT/Revenue)	18.4	16.1	16.7	16.9	17.1
Asset turnover (Revenue/Avg TA)	156.8	140.4	128.8	131.5	129.8
Leverage (Avg TA/Avg Equity)	1.4	1.5	1.6	1.6	1.6
Adjusted ROAE	34.6	29.5	27.9	28.5	28.0

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	11.9	18.0	14.5
EBITDA	58.6	7.7	15.4	19.3	15.3
Adjusted EPS	36.1	0.0	8.0	20.4	16.0
Profitability & Return ratios (%)					
EBITDA margin	19.9	18.7	19.2	19.4	19.6
EBIT margin	18.4	16.1	16.7	16.9	17.1
Adjusted profit margin	16.0	14.0	13.4	13.7	13.9
Adjusted ROAE	34.6	29.5	27.9	28.5	28.0
ROCE	43.4	34.7	34.6	40.1	45.3
Working capital days (days)					
Receivables	89	86	91	87	84
Inventory	0	0	0	0	0
Payables	11	11	11	11	11
Ratios (x)					
Gross asset turnover	14.2	7.8	6.1	6.9	7.7
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	0.0	(0.2)	(0.3)

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

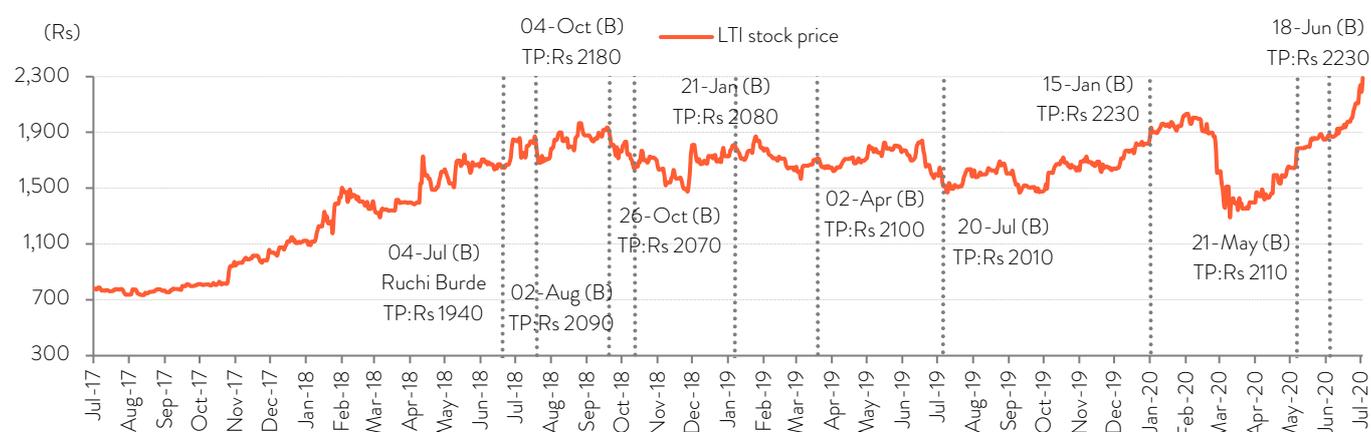
ADD – Expected return from >+5% to +15%

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)

HISTORICAL RATINGS AND TARGET PRICE: L&T INFOTECH (LTI IN)



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

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