

## Infosys Ltd Result Synopsis

**Accumulate**

**CMP: Rs.2787**

**Target: Rs. 3035**

### **Q313 – Revenue, PAT beat estimates, OPMs (excl. Lodestone) stable Volume growth, pricing uptick – positive**

Infosys positively surprised at both the top-line and bottom-line level while stable OPMs was further comforting despite the wage hikes undertaken during the quarter. Revenues grew 6.3 % ( 4.2% excl. Lodestone) to \$1911 while PAT grew 1% to \$434mn. Lodestone contributed \$39mn to revenues in Q313. The strong performance was delivered by the healthy ramp-ups in the high margin C&SI space, which largely mitigated the negative impact of longer than expected furloughs, wage hikes during the quarter. The management has reiterated its cautious stance on the environment however is far more optimistic than mid-quarter.

Revenues in INR terms grew 5.7% to Rs.10,424cr driven by volume growth of 2 % ( 1.5% excl. Lodestone), higher realizations 2.8% (+1.8% excluding Lodestone). The management retained its revenue guidance of at-least 5% organically for FY13, which post the strong show in Q3, seems attainable. The revised revenue guidance including Lodestone stands at 6.5% for FY13. The IT heavyweight has maintained that environment remains challenging on account of vendor consolidation, tight budgets and discretionary spend on tight leash however company sounds confident of revenue growth driven by strong pipeline, and ramp-ups in existing deals won over last few quarters.

Operating Margins excluding Lodestone dipped marginally to 26.1% vs. 26.3% in Q2FY13, as Infosys has been aggressive on rationalizing costs while improved realizations mitigated the (100bps) impact of offshore wage hikes. OPMs including Lodestone stood at 25.7%. Pricing environment is expected to be stable while further ramp-ups in the large deals won in previous quarter could boost realizations.

**We have upgraded our FY14 revenue estimate while reset our INR/\$ estimates for FY13 and FY14 from Rs.53/\$ & Rs.49.5/\$ to Rs.54.5/\$ and Rs.51/\$ respectively. Consequently, earnings have been raised 2.8% and 6.5% respectively. Infosys currently trades at 14.7x FY14e of Rs.189.67 and in-order to factor in the improvement in deals, prospects of revival in discretionary spend and possible ramp-ups in existing deals, we raise our PE multiple to 16x (from 13x earlier) to arrive at our target price of Rs.3035.**

### **Performance Snapshot**

Description Rs.cr	Q313	Q213	QoQ (%)	YoY%
Net Sales	10424	9858	5.7	12.1
Op. Profit(excl. OI)	2677	2597	3.1	-7.7
OPM (%)	25.7	26.3	(66)bps	(550)bps
PAT	2369	2369	0.0	-0.1

## Revenue Profile:

### Revenue by service offering:

**Business operations** which account for 61.9% of revenues have grown 2.1%QoQ on account of healthy growth IMS and Testing and BPO. Revenue share of Application development and maintenance eroded 260bps QoQ on account of flattish growth in respective segments. Application development revenues declined 1.2%QoQ resulting in revenue share dipping to 15.8% vs. 17% in Q213. Similarly revenues from Application maintenance declined 0.6% resulting in revenue share declining to 20% vs. 21.4% in Q213. IMS, Testing and BPO which together account for 20.5% of revenues, reported healthy growth of 7.9%, 3.9%, 17.7% QoQ respectively. Infosys won 8 large deals business and IT operations amounting to \$731mn. Infosys expects the BPO business to sustain its momentum in the quarters ahead.

**Business transformation** segment revenue share rose to 32.6% compared to 30% in Q213 primarily on account of the Lodestone acquisition during the quarter, excluding which revenue share stood at 31.2%. Consulting and system integration revenues grew robust 16% driven by the 8 large deal wins in the second quarter, ramp-ups seen in the deals, while Lodestone added to the growth rate. Excluding Lodestone, C&SI revenues still grew a healthy 8%QoQ.

**Business Innovation** segment which consists of the Products, Platforms and Solutions, recorded an increase in revenues of 6.3% QoQ. Revenues from the segment accounted for 5.5% of overall revenues and remains important focus area for Infosys. The company added 14 clients during the quarter. The company added more than 15 engagements across Cloud service, Big Data and Security. Infosys ended the quarter with a TCV of \$603mn vs. \$485 mn earlier.

Revenue by service offering:	% of sales	QoQ	YoY
<b>Business IT Services</b>	<b>61.9</b>	<b>2.1%</b>	
<i>Application Development</i>	15.8	-1.2%	-2.2%
<i>App Maintainance</i>	20.0	-0.6%	-2.9%
<i>IMS</i>	6.9	7.9%	19.7%
<i>Testing</i>	8.4	3.9%	12.5%
<i>Bus. Process Mgmt Services</i>	5.2	17.7%	25.1%
<i>Products Eng Services</i>	3.2	0.1%	-5.9%
<i>Others*</i>	2.4	-1.8%	-2.3%
<b>Consulting, Package Implementation &amp; Others</b>	<b>32.6</b>	<b>16%</b>	
<i>Consulting &amp; System Integration &amp; Others</i>	32.6	16%	12.7%
<b>Products, Platforms &amp; Solutions</b>	<b>5.5</b>	<b>6.3%</b>	
<i>Products</i>	3.9	9.1%	-14%
<i>Bus. Process Mgmt (BPM) Platform*</i>	1.3	6.3%	71.9%
<i>Others</i>	0.3	-20.2%	5.8%

\*Reported under "Business IT Services" in previous quarters; Source: Company and Banham Research

## Revenue by Industry

**FSI** reported 6.4% sequential growth and 6% in constant currency. B&FS revenues grew 5.6% QoQ while Insurance fell 9.5% QoQ. The management reiterated that the B&FS sector remains under pressure resulting in clients focusing on reducing costs and vendor consolidation, however expects spend on customer centric applications, risk management and regulatory compliance to be robust.

**Manufacturing** sector continues to perform relatively well, growing 4.6% sequentially and 4% in constant currency. The mfg sector accounts for 21.7% of overall revenues. The mgmt remains confident of the sector, and expects pick up across geographies.

**Retail and Life sciences** remains a key investment area for the Infosys, witnessed healthy traction. RCL grew 6.6% sequentially and 6.2% in constant currency terms. Life sciences and Healthcare grew 30.9% and 13.9% QoQ respectively. Transport & Logistics grew 12.6%QoQ. Retail & CPG which accounts for 66% of segment and 16% of overall revenues was flat, grew 0.1% sequentially.

**ECS** revenues grew by 7.8% sequentially and 7.1% in constant currency, as Telecom which accounts for almost half of segment (ECS) revenues, grew 3.1% QoQ. Energy and Utility which contributes 5.4% of overall revenues grew 8.4% QoQ.

Revenue by Industry	% of Sales Q313	Growth QoQ
<b>Insurance, Banking &amp; Financial Services</b>	<b>33.7</b>	<b>6.4%</b>
<i>B&amp;FS</i>	26.8	5.56%
<i>Insurance</i>	6.9	9.5%
<b>Mfg</b>	<b>21.7</b>	<b>4.6%</b>
<b>Retail &amp; Life sciences</b>	<b>24.1</b>	<b>6.6%</b>
<i>Retail &amp; CPG</i>	16	0.1%
<i>Transport &amp; Logistics</i>	1.8	12.6%
<i>Life sciences</i>	4.8	30.9%
<i>Healthcare</i>	1.5	13.9%
<b>Energy, Utilities, Communications &amp; Services</b>	<b>20.5</b>	<b>7.8%</b>
<i>Energy &amp; Utilities</i>	5.4	8.4%
<i>Telecom</i>	9.6	3.1%
<i>Others</i>	5.5	17.0%

Source: Company and Banham Research

## Revenues by Geography

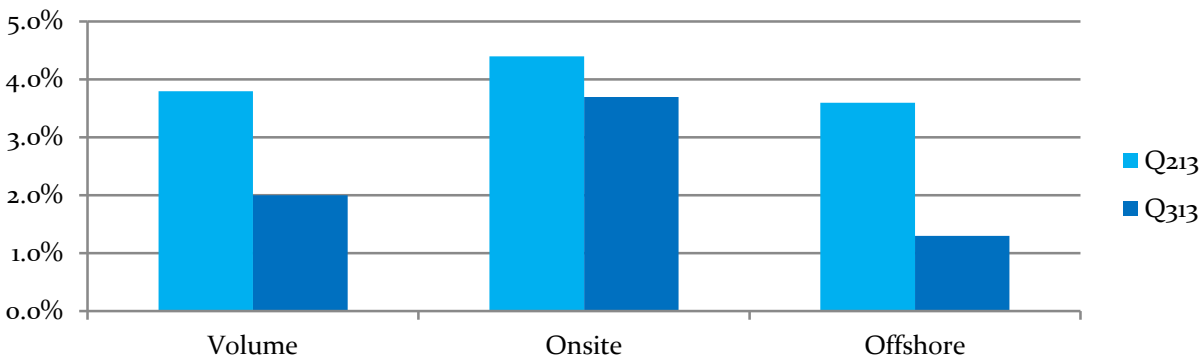
Revenue share from North America declined 290bps QoQ to 61%. Revenue contribution from Europe rose 210bps QoQ to 24% on account of Lodestone and traction in business. The company reiterated the challenging environment in Europe however client discussions in high margin transformation space remain in place, raising possibility of tailwinds on realizations. Revenues from NA grew 1.6% QoQ (1.6%ccy) while Europe revenues grew 16.6% QoQ (14.4%ccy). India revenue contribution grew to 2.2% from 1.6% in Q213 while revenues grew 44.7%QoQ. ROW revenue share rose marginally to 12.8% while revenues grew 7.4% both sequentially and in constant currency.

## Revenues by Project Type

The share of fixed price projects grew 90bps QoQ to 41.3% while Time and Material project dipped to 58.7% vs. 59.6% in Q213.

## Pricing and Volume Growth

Infosys posted volume growth of 2.0%. Onsite efforts grew 3.7% QoQ vs. 4.4% in Q213 while offshore efforts grew 1.3% vs. 3.6% seen in the Q213 quarter. Volume growth excluding Lodestone grew 1.5%QoQ. Pricing rose 2.8%QoQ and 1.8% excluding Lodestone impact.



Source: Company, Banham Research

## Client additions:

Infosys continued to witness robust client additions, acquiring 89 (53 excluding Lodestone) new clients in Q313 compared to 39 clients in the Q213. Infy added 8 large deals during the quarter, 4 from US, 3 from Europe and 1 in India. Number of clients active rose to 776 from 715 at end of Q213. Revenue concentration declined, with Top client, Top 5 and Top 10 clients accounting for 3.6%, 14.6% and 23.9% respectively. Share of Repeat business eased to 97.5% from 98.2% in Q213.

## Guidance:

Infosys kept its full year organic dollar revenue guidance of at least 5%. The company expects FY13 revenues at \$7.450bn (incl. \$104mn from Lodestone). Infosys has guided for FY13 EPS of at least Rs.162.80 translating to YoY growth of 11.9%. Infosys has now assumed INR/USD rate of Rs.54.5 compared to Rs.53 earlier for rest of fiscal 2013.

Revised Guidance to account for currency reset (54/\$ vs. 53/\$ earlier) and Lodestone (\$104mn)

	FY13	FY13
Rupee Guidance	Guidance	Revised
Revenues	Rs.39582cr	Rs.40746cr
YoY	17.3%	20.8%
EPS	160.61	162.80
YoY	10.3%	11.9%
Rs./\$	53	54.5
Dollar Guidance		
Revenues	\$7.343bn	\$7.450bn
YoY	5%	6.5%
EPADS	\$2.97	\$2.97
YoY	-1%	-1%

Source: Company, Banham Research

**View:**

Infosys has managed to deftly handle the pressures in terms of pricing, attrition and revenue growth as environment continues to remain fragile. The acquisition of Swiss based Lodestone has revived Consultancy and System Integration segment - a focus area for Infosys. We expect, as the global economy crises shows signs of abatement and incremental signs of recovery, Infosys seems to be well positioned to benefit from ramp-ups in past deal-wins, up-ward shift in its business approach from having a client-vendor relationship to being an essential partner in driving client business and further traction in non-linear revenues.

The improvement in global macro data is a positive for the entire IT space, has raised clients' confidence levels and is expected to translate to higher spend. We see the improved environment as positive for Infosys, given 1/3<sup>rd</sup> of its revenues exposed to discretionary spend. The environment in the B&FS space remains tough, however higher regulatory requirements are expected to increase compliance related spend. Hence business environment for segments which account of 2/3<sup>rd</sup> of revenue are showing signs of recovery.

Infosys decision of combining wage hikes and promotions to deflect attrition pressures seems to be playing out well with incremental attrition flattening out. Infosys has tightened its employee performance measurement to reduce pressure on margins. The company is likely to award 6000-9000 promotions in Q413 besides undertake 2-3% wage hike for onsite employees, combined impact is expected to erode margins by 100 bps. Lateral additions in Q313 accounted for 48% of gross additions, excluding the impact of Lodestone, vs. 45% avg. seen in previous three quarters. Thus Infosys seems to be positioning itself to address higher traction in business.

**Overall we see the increased flexibility on margins, improving business environment, well positioned business approach, early indications of revival in discretionary spend and higher traction in the products and platforms space as positive for Infosys. Hence upgrade the stock from Neutral to Accumulate.**

**We have upgraded our FY14 revenue estimate while reset our INR/\$ estimates for FY13 and FY14 from Rs.53/\$ & Rs.49.5/\$ to Rs.54.5/\$ and Rs.51/\$ respectively. Consequently, earnings have been raised 2.8% and 6.5% respectively. Infosys currently trades at 14.7x FY14e of Rs.189.67 and in-order to factor in the improvement in deals, prospects of revival in discretionary spend and possible ramp-ups in existing deals, we raise our PE multiple to 16x (from 13x earlier) to arrive at our target price of Rs.3035.**

Quarterly (Rs.cr)	Q313	Q213	QoQ	YoY
<b>Revenues</b>	<b>10424</b>	<b>9858</b>	<b>5.7%</b>	<b>12.1%</b>
COS	6566	6102	7.6%	24.2%
Gross Profit	3858	3756	2.7%	-3.8%
<b>GPM (%)</b>	<b>37.0%</b>	<b>38.1%</b>	<b>-109bps</b>	<b>612bps</b>
Selling & Mkt	541	506	6.9%	20.0%
Admin	640	653	-2.0%	-3.0%
Total Opex	1181	1159	1.9%	6.3%
Op profit	2677	2597	3.1%	-7.7%
<b>OPM (%)</b>	<b>25.7%</b>	<b>26.3%</b>	<b>-66bps</b>	<b>-550bps</b>
other income	503	706	-28.8%	19.2%
PBT	3180	3303	-3.7%	-4.2%
Tax	811	934	-13.2%	-14.5%
Tax Rate	25.50%	28.28%	-277bps	-307bps
<b>PAT</b>	<b>2369</b>	<b>2369</b>	<b>0.0%</b>	<b>-0.1%</b>

Quarterly (\$ mn)	Q313	Q213	QoQ	YoY
<b>Revenues</b>	<b>1911</b>	<b>1797</b>	<b>6.3%</b>	<b>5.8%</b>
COS	1203	1114	8.0%	16.8%
Gross Profit	708	683	3.7%	-8.8%
<b>GPM (%)</b>	<b>37.0%</b>	<b>38.0%</b>	<b>-96bps</b>	<b>-592bps</b>
Selling & Mkt	99	92	7.6%	12.5%
Admin	118	119	-0.8%	-7.8%
Total Opex	217	211	2.8%	0.5%
Op profit	491	472	4.0%	-12.3%
<b>OPM (%)</b>	<b>25.7</b>	<b>26.3%</b>	<b>-57bps</b>	<b>-531bps</b>
other income	92	129	-28.7%	12.2%
PBT	583	601	-3.0%	-9.2%
Tax	149	170	-12.4%	-19.0%
Tax Rate	25.6%	28.3%	-273ps	-310bps
<b>PAT</b>	<b>434</b>	<b>431</b>	<b>0.7%</b>	<b>-5.2%</b>

All figures in Rs.cr

P/L	FY10	FY11	FY12	FY13e	FY14e
Revenues	22742	27501	33734	40786	44273
Cost of sales	12078	15054	18871	23411	25191
Gross Profit	10664	12447	14863	17374	19082
<b>GPM (%)</b>	<b>46.9%</b>	<b>45.3%</b>	<b>44.1%</b>	<b>42.6%</b>	<b>43.1%</b>
Selling & Mktg	1184	1512	1757	2154	2218
Admin exp	1628	1971	2390	3061	3237
Total Opex	2812	3483	4147	5215	5454
EBITDA	7852	8964	10716	12159	13628
<b>EBITDA Margin</b>	<b>34.5%</b>	<b>32.6%</b>	<b>31.8%</b>	<b>29.8%</b>	<b>30.8%</b>
Depreciation	942	862	937	1169	1203
EBIT	6910	8102	9779	10990	12424
Other Income	990	1211	1904	2553	2628
Interest	0	0	0	0	0
PBT	7900	9313	11683	13543	15052
Tax	1681	2490	3367	3792	4215
Tax Rate	21.3%	26.7%	28.8%	28.0%	28.0%
<b>PAT</b>	<b>6219</b>	<b>6823</b>	<b>8316</b>	<b>9751</b>	<b>10838</b>
EPS	108.89	119.42	145.54	170.65	189.67

Balance sheet	FY10	FY11	FY12	FY13e	FY14e
<b>Assets</b>					
Cash and Cash Eq	12111	16666	20591	26953	34426
Other Current Assets	8779	7023	9655	10160	10777
Non Current Assets	6722	7574	8102	8460	8830
<b>Total Assets</b>	<b>27612</b>	<b>31263</b>	<b>38348</b>	<b>45573</b>	<b>54032</b>
<b>Liabilities</b>					
Equity	286	286	286	286	286
Net worth	24073	27303	33461	40399	48441
Liabilities	3539	3960	4887	5173	5591
<b>Total Liabilities</b>	<b>27612</b>	<b>31263</b>	<b>38348</b>	<b>45573</b>	<b>54032</b>

Cash Flow	FY10	FY11	FY12	FY13e	FY14e
Cash from Operations	6,873	5,907	8,212	10685	11756
Cash from Investments	-4,388	2,231	-2061	-1684	-1511
Cash from Financing	-1,480	-3,641	-2,321	-2639	-2,772
Net Chg in cash	1,005	4,497	3830	6362	7473



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**RATINGS**

Buy	Accumulate	Neutral	Reduce	Sell
>15%	+5>15%	+5%/-5%	-5%<-15%	>-15%

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