

Stock Update

Mixed quarter

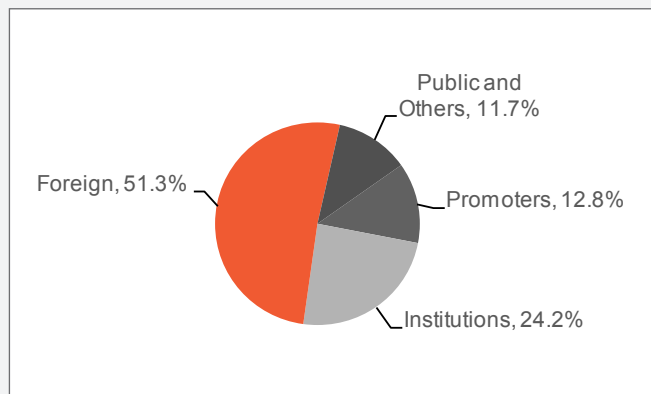
Infosys

Reco: Hold | CMP: Rs927

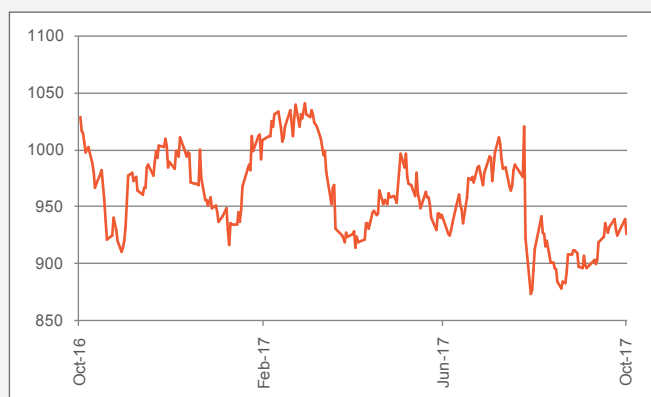
Company details

Price target:	Rs1,000
Market cap:	Rs212,874 cr
52-week high/low:	Rs1,045/861
NSE volume: (No of shares)	54.6 lakh
BSE code:	500209
NSE code:	INFY
Sharekhan code:	INFY
Free float: (No of shares)	200.4 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	4.6	-4.1	3.3	-8.1
Relative to Sensex	2.7	-5.7	-7.6	-21.6

Key points

- ♦ **Revenues missed, guidance disappoints, margins surprises positively:** For Q2FY18, Infosys has reported a mixed set of numbers, with constant currency revenues growth of 2.2% (lower than estimates) and 2.9% on reported basis (70bps tailwinds from cross-currencies). The revenue growth was led by volume growth of 1.6% (onsite, down 0.7% and offshore up by 2.6%) and blended pricing increase of 1.3% qoq (onsite 1.9% up and offshore 2.6% up), positive surprise (back to back quarters of pricing improvement, though partly led by cross currencies tailwinds).

EBIT margins have improved by 10bps qoq to 24.2%, much ahead of our expectation led by operational improvement. PAT at Rs3726 crore up by 7.0% qoq, beat estimates owing to higher than expected other income up by 18.8% qoq. Infosys has cut its revenue guidance for FY2018 on cc term to 5.5-6.5% from 6.5-8.5% earlier, which is much steeper than expected.

- ♦ **Nandan Nilekani highlights at strategy refresh, CEO appointment on the cards:** Achieving complete clarity on the “the things to do” going forward is topmost on the agenda of the newly appointed Chairman Nandan Nilekani. Mr. Nilekani will also briefly chalk out the broad strategy that the management will execute over coming years. Mr. Nilekani highlighted refreshing existing strategy and giving it the required push it requires. He also stated the larger focus on integration of services and products strategy. Over the next 12-18 months, the company will accelerate pace of execution to drive growth will also consider M&A, if it requires to fill up the services or products gaps. Further, the process of the appointment of a new CEO has already commenced and will be completed soon, though has not stated any timeline. The commentary from Mr. Nilekani has no major departure from Dr. Vishal Sikka’s strategy to accelerate growth though the newer services, which we view as a positive for Infosys. However, execution under the new upcoming CEO will be key for growth revival, given the tough macro environment.

♦ **Valuation: Maintain Hold with TP of Rs1,000:**

We have broadly maintained our earnings estimates for FY18/19E. At the current levels stock is trading at 13x FY19E estimates, which mostly factoring a weaker earnings trajectory over FY17-19E. We believe the downside risk is protected to certain extent as Infosys is currently trading at steep discount to TCS, which has similar growth profile and upcoming buyback program (record

date on November 1st, 2017) will also protect the downside risk. Though, Infosys has shown sign of resilience post the departure of its CEO and key board members, it still doesn't provide enough confidence to become constructive on stock. With the absence of growth triggers and management transition issues, we maintain our HOLD rating on the stock with unchanged price target of Rs1,000.

Valuations

				Rs cr
Particulars	FY2016	FY2017	FY2018E	FY2019E
Total revenue	62,441.0	68,484.0	70,344.2	77,173.0
EBITDA margin (%)	27.4	27.2	26.7	26.8
Net profit	13,492.0	14,357.0	14,619.9	15,933.8
EPS (Rs)	59.0	62.8	64.0	69.7
P/E (x)	15.7	14.8	14.5	13.3
EV/EBITDA (x)	10.5	9.7	8.6	7.4
RoE (%)	23.2	22.0	20.1	19.9
RoCE (%)	32.1	30.5	27.9	27.6

Results

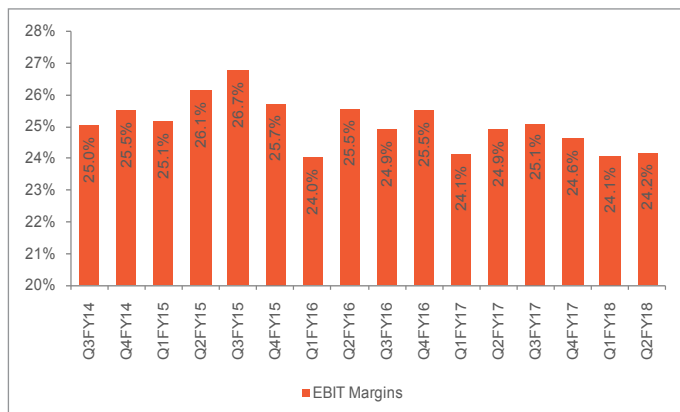
					Rs cr
Particulars	Q2FY18	Q2FY17	Q1FY18	YoY (%)	QoQ (%)
Revenues (\$ mn)	2,728.0	2,587.0	2,651.0	5.5	2.9
Net sales	17,567.0	17,310.0	17,078.0	1.5	2.9
Direct costs	10,771.0	10,538.0	10,450.0	2.2	3.1
Gross profit	6,796.0	6,772.0	6,628.0	0.4	2.5
SG&A	2,094.0	2,039.0	2,067.0	2.7	1.3
EBITDA	4,702.0	4,733.0	4,561.0	-0.7	3.1
Depreciation & amortisation	456.0	424.0	450.0	7.5	1.3
EBIT	4,246.0	4,309.0	4,111.0	-1.5	3.3
Other income	883.0	760.0	743.0	16.2	18.8
PBT	5,129.0	5,069.0	4,854.0	1.2	5.7
Tax provision	1,403.0	1,460.0	1,371.0	-3.9	2.3
Reported net profit	3,726.0	3,606.0	3,483.0	3.3	7.0
EPS (Rs)	16.3	15.8	15.2	3.3	7.0
Margin (%)				BPS	BPS
EBITDA	26.8	27.3	26.7	-58	6
EBIT	24.2	24.9	24.1	-72	10
NPM	21.2	20.8	20.4	38	82

Decent volume growth at 1.6%

Particulars	Q2FY16	Q3FY16	Q4FY16	Q1FY17	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18
Revenues	2,392.0	2,407.0	2,446.0	2,501.0	2,587.0	2,551.0	2,569.0	2,651.0	2,728.0
QoQ \$ revenue growth (%)	6.0	0.6	1.6	2.2	3.5	-1.4	0.7	3.2	2.9
CC growth (%)	6.9	1.1	1.9	1.7	3.9	-0.3	-	2.7	2.2
Volume	3.7	3.1	2.4	2.2	4.0	0.2	1.2	1.7	1.6
Onsite (%)	3.5	4.4	2.7	3.3	3.1	0.6	1.9	2.0	-0.7
Offshore (%)	3.7	2.5	2.3	1.8	4.4	0.1	0.9	1.5	2.6
Blended realisation	2.6	-2.5	-1.1	-0.5	0.2	-2.2	-0.2	1.8	1.3

Source: Company, Sharekhan research

Margins improved led by operational efficiencies



Source: Company, Sharekhan research

Other highlights of Q2FY2018

- ◆ The utilisation rate (ex-trainees) improved by 70BPS on a sequential basis at 84.7%. Infosys has been consistently maintaining the utilisation rate at more than 80% for the last ten quarters.
- ◆ The cash & cash equivalents stood at Rs41,392 crore in Q1FY2018 as against Rs39,335 crore in the previous quarter.
- ◆ The company's days sales outstanding (DSO) increased by three days on QoQ to 71 days.
- ◆ Added 72 gross clients during the quarter versus 59 clients added in Q1FY18. Total number of active clients reached to 1,173 at the end of Q2FY18.
- ◆ The revenue per employee increased 1.5%QoQ and 3.4%YoY to \$52,684 in Q2FY18
- ◆ During Q2FY2018, volume increased by 1.2%QoQ, while price realization grew by 1.3% QoQ
- ◆ Won five large deals during the quarter, total TCV wins for the quarter stood at \$700 mn vs.

Operating metrics

Particulars	Q2FY18	Q2FY17	Q1FY18	YoY (%)	QoQ (%)	Comments
Geographic mix (%)						
North America	60.6	61.5	61.1	3.9	2.1	Europe grew by 4.1% QoQ on CC basis, while US grew by 1.9% QoQ. The management sees good traction in Europe
in \$ mn	1,653.2	1,591.0	1,619.8			
Europe	23.2	22.5	22.4	8.7	6.6	
in \$ mn	632.9	582.1	593.8			
India	3.3	3.4	3.6	2.3	-5.7	
in \$ mn	90.0	88.0	95.4			
Rest of world	12.9	12.6	12.9	8.0	2.9	
in \$ mn	351.9	326.0	342.0			
Services offerings:						
Application development	15.6	15.6	15.4	5.5	4.2	Infrastructure and BPM delivered strong growth of 10.3% and 5.0% on QoQ basis
in \$ mn	425.6	403.6	408.3			
Appl maint	16.0	18.1	16.7	-6.8	-1.4	
in \$ mn	436.5	468.2	442.7			
ADM	31.6	33.7	32.1	-1.1	1.3	
in \$ mn	862.0	871.8	851.0			
BPM	5.1	4.9	5.0	9.8	5.0	
in \$ mn	139.1	126.8	132.6			
Consulting & package	32.5	32.1	32.6	6.8	2.6	
in \$ mn	886.6	830.4	864.2			
IMS	9.0	8.4	8.4	13.0	10.3	
in \$ mn	245.5	217.3	222.7			
Product Engineering Services	4.1	3.7	4.1	16.9	2.9	
in \$ mn	111.8	95.7	108.7			
Testing	9.4	9.2	9.3	7.7	4.0	
in \$ mn	256.4	238.0	246.5			
Others	3.1	2.9	3.1	12.7	2.9	
in US\$ mln	84.6	75.0	82.2			
Products and Platforms	5.2	5.1	5.4	7.5	-0.9	
in \$ mn	141.9	131.9	143.2			
Business operations	62.3	62.8	62.0	4.6	3.4	
in \$ mn	1,699.5	1,624.6	1,643.6			
Business consulting	32.5	32.1	32.6	6.8	2.6	
in \$ mn	886.6	830.4	864.2			
Products, platforms & solutions	5.2	5.1	5.4	7.5	-0.9	
in \$ mn	141.9	131.9	143.2			

Particulars	Q2FY18	Q2FY17	Q1FY18	YoY (%)	QoQ (%)	Comments
New Services	9.4	NA	8.3	-	16.5	New services area contributed 50% of the incremental revenue during the quarter
in US\$ mln	256.4	NA	220.0			
New Software (Edge, NIA, Panaya, Skava)	1.6	NA	1.6	-	2.9	
in US\$ mln	43.6	NA	42.4			
Industry verticals:						
Insurance	6.4	5.7	6.2	18.4	6.2	Financial services grew by 2.6% QoQ on CC basis, compared to 2.0% in Q1FY18. Excluding Finacle, BFSI vertical grew by 3.0% QoQ on CC basis
in \$ mn	174.6	147.5	164.4			
Banking and financial services	27.0	27.4	27.1	3.9	2.5	
in \$ mn	736.6	708.8	718.4			
BFSI	33.4	33.1	33.3	6.4	3.2	
in \$ mn	911.2	856.3	882.8			
Manufacturing	22.0	22.5	22.2	3.1	2.0	
in \$ mn	600.2	582.1	588.5			
Retail and CPG	13.8	14.9	14.2	-2.3	0.0	
in \$ mn	376.5	385.5	376.4			
Telecom	10.4	9.4	10.4	16.7	2.9	
in \$ mn	283.7	243.2	275.7			
Energy & utilities	5.5	4.8	5.2	20.8	8.8	
in \$ mn	150.0	124.2	137.9			
Transportation and logistics	2.0	1.9	1.9	11.0	8.3	
in \$ mn	54.6	49.2	50.4			
Life sciences and healthcare	6.8	6.7	6.6	7.0	6.0	
in \$ mn	185.5	173.3	175.0			
Others	6.1	6.7	6.2	-4.0	1.2	
in \$ mn	166.4	173.3	164.4			
BFSI	33.4	33.1	33.3	6.4	3.2	
in \$ mn	911.2	856.3	882.8			
Manufacturing	22.0	22.5	22.2	3.1	2.0	
in \$ mn	600.2	582.1	588.5			
Retail, life sciences & transportation	22.6	23.5	22.7	1.4	2.5	
in \$ mn	616.5	607.9	601.8			
Energy, utilities, comm & services	22.0	20.9	21.8	11.0	3.8	
in \$ mn	600.2	540.7	577.9			
Client contribution (%)						
Top client	3.4	3.5	3.3	2.4	6.0	Top client revenue grew by 6.0% QoQ, versus 3.2%% in Q1FY18
in \$ mn	92.8	90.5	87.5			
Top 10 clients	19.5	21.8	20.0	-5.7	0.3	
in \$ mn	532.0	564.0	530.2			
Others than top 10	80.5	78.2	80.0	8.6	3.5	
in \$ mn	2,196.0	2,023.0	2,120.8			

Particulars	Q2FY18	Q2FY17	Q1FY18	YoY (%)	QoQ (%)	Comments
Number of clients						
Number of clients						Added one new client in \$100 million bucket on QoQ basis, while one client was reduced in \$50 million bucket
1 million dollar +	620	577	606	43	14	
5 million dollar +	286	277	279	9	7	
10 million dollar +	186	186	190	0	-4	
25 million dollar +	100	89	97	11	3	
50 million dollar +	55	54	56	1	-1	
75 million dollar +	31	30	31	1	0	
100 million dollar +	19	18	18	1	1	

Employee metrics

Particulars	Q2FY18	Q2FY17	Q1FY18	
Total employees	1,98,440	1,99,829	1,98,553	Attrition inched up to 21.4% in Q2FY18. Net addition of employees declined by 113 during the quarter
Gross addition	10,514	12,717	8,645	
Net addition	-113	2,779	-1,811	
Attrition (Annualised%)	21.4	20.0	21.0	
Revenue per FTE - Consolidated	52.7	51.0	51.9	

Source: Company, Sharekhan research

Utilisation (%)

Particulars	Q2FY18	Q2FY17	Q1FY18	Change in BPS YoY	Change in BPS QoQ	
Including trainees	81.8	77.7	80.2	410	160	Utilisation (ex- trainees) improved by 70BPS on QoQ basis
Excluding trainees	84.7	82.5	84.0	220	70	

Source: Company, Sharekhan research

Revenue by project type

Particulars	Q2FY18	Q2FY17	Q1FY18	YoY (%)	QoQ (%)	
Fixed price	51.3	47.1	50.3	14.9	5.0	Fixed-price projects up by 5.0% QoQ vs 5.1% QoQ in Q1FY18
in \$ mn	1,399.5	1,218.5	1,333.5			
Time and material	48.7	52.9	49.7	-2.9	0.8	
in \$ mn	1,328.5	1,368.5	1,317.5			

Source: Company, Sharekhan research

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