

Sustained Operating Margins

13th January 2018

CMP: Rs.1078
Target Price: Rs.1238
Recommendation: Accumulate

Stock Info

BSE Group	A
BSE Code	500209
NSE Symbol	INFOSYSTCH
Bloomberg	INFO IN
Reuters	INFY.BO
BSE Sensex	34,592
NSE Nifty	10,681

Market Info

Market Capital	Rs.2,35,517cr
Equity Capital	Rs. 1091 cr
6M Avg. Trading Vol	6,474,478
52 Wk High/ Low	1086/860
Face Value	Rs.5

Shareholding Pattern (%)	(Dec , 17)
Promoters	12.9
Domestic Institutions	21.8
Foreign Institutions	35.0
Public & Others	30.3

Price Vs Sensex Chart



Highlights of the quarter:

- Revenues grew year-on-year by 8.0% in USD terms; 5.8% in constant currency terms.
- Revenues grew sequentially by 1.0% in USD terms; 0.8 % in constant currency terms.
- Operating margin improved to 24.3% from 24.2% in Q2 18. EPS at Rs 22.5, year-on-year growth of 39% and sequential growth of 38%.
- EPS of Rs 22.5 includes positive impact of Rs 6.29 from Advance Pricing Agreement (APA) with the US IRS.
- 9 months year-on-year revenue growth at 6.5% in USD terms; 5.6% in constant currency terms.
- Cash flow from operating activities were at Rs 4257 crore, compared to Rs 2831 cr in Q2 18.
- Standalone attrition declined to 15.8% from 17.2% in Q2 18.
- Signing of the Advance Pricing Agreement (“APA”) with the US Internal Revenue Service:** Infosys has concluded an Advance Pricing Agreement (“APA”) with the U.S. Internal Revenue Service (“IRS”). Under the APA, Infosys and the IRS have agreed on the methodology to allocate revenues and compute the taxable income of the Company’s U.S. operations. This agreement covers financial years from 2011 to 2021. The APA will enhance predictability of Infosys’ tax obligations in respect of its U.S. operations. In accordance with the APA, Infosys has reversed tax provisions of approximately Rs 1,432 crore made in previous periods which are no longer required (both under International Financial Reporting Standards and Indian Accounting Standards). Further, in line with the APA, Infosys expects to payout approximately US\$ 233 million due to the difference between the taxes payable for prior periods as per the APA and the actual taxes paid for such periods. This amount is expected to be paid over the next few quarters. The reversal of the tax provisions of approximately Rs 1,432 crore had a positive impact on the consolidated Basic EPS for the quarter ending December 31, 2017 by approximately Rs 6.29. Further, on account of the APA methodology, Infosys expects its overall effective tax rate to be lower by about 100 basis points for future periods covered under the APA.

Segment Highlights:

- North America grew by 0.7% both sequentially and in constant currency.
- Europe grew by 5.9% sequentially; and 4.7% in constant currency.
- India declined by 6.1% sequentially; and 5.9% in constant currency.
- Rest of the world declined by 4.6% sequentially; and 4.0% in constant currency.

Industry segment growth:

- FSI grew by 0.3% sequentially; and 0.1% in constant currency.
- MFG & Hi-Tech grew by 0.1% sequentially; and declined by 0.1% in constant currency.
- RCL grew by 1.4% sequentially; and 1.2% in constant currency.
- ECS grew by 2.6% sequentially; and 2.5% in constant currency.

Concall Highlights:

- Strong Demand for Digitisation.
- 8 large Deal Wins.
- Growth expected to pickup in FY19.
- 1.9% increase in Revenue per employee.
- Utilization increase from 81.9% to 84.9%.
- 79 Client additions in the quarter.
- Effective tax rate to lower by 100 basis point.
- Plans to hire 10,000 employees in USA.
- Insurance segment is growing strong.
- Confident of increase in revenue from FSI sector as the management expect FSI spending to pickup.
- Good quarter for Retail and expect the trend to continue.
- Revenues are expected to grow 5.5%-6.5% in constant currency;
- Revenues are expected to grow 6.5%-7.5% in USD terms based on the exchange rates.

Outlook:

- Even in weak quarter and after lot of head winds, new management of Infosys has maintained its good and stable run by maintaining its margins. We expect Infosys to perform well in the coming quarter under the new management and have assigned a PE of 16.5x to its FY19E EPS of Rs 75 and have arrived at fair value of Rs 1,238 per share. At CMP Rs 1078 stock trades at 14(x) its FY19E earnings. We have **Accumulate** rating on the stock.

Financial Snapshot:

Y/E March (Rs. In Crore)	FY17	FY18E	FY19E
Net Revenue	68484	72468	77541
Growth %	10%	6%	7%
EBIT	16901	17539	19271
EBIT Margin	24.7%	24.2%	24.9%
Net Profit	14353	16749	17130
Growth %	5%	17%	2%
EPS	63	74	75
P/E	15	15	14
ROE	20.8	22.5	19.2

Source: Company data, Arihant Research

Quarterly Results:

Quarter Ended					
Particulars (Rs. Cr)	Q3 FY 18	Q2 FY18	Q3 FY17	QoQ	YoY
Revenues	17,794	17567	17,273	1.3%	3.0%
Cost of services	10,910	10693	10,840	2.0%	0.6%
Gross Profits	6,884	6874	6,433	0.1%	7.0%
S&M,G&A. Expenses	2,565	2628	2,099	-2.4%	22.2%
EBIT	4,319	4246	4,334	1.7%	-0.3%
Other Income	962	883	820	8.9%	17.3%
Share in associate's profit/(loss)	0	0	-		
PBT	5,281	5129	5,154	3.0%	2.5%
Income tax expense	152	1403	1,446	-89.2%	-89.5%
Net PAT	5,129	3726	3,708	37.7%	38.3%
EPS	23.6	16.3	16.2	44.7%	45.3%

Profit and Loss statement

Particulars (Rs. In Crore)	FY17	FY18 E	FY19 E
Income	68,484	72,468	77,541
Software development expenses	43,253	44,248	46,524
Gross Profit	25,231	28,220	31,016
Sales and development expenses	3,591	4,485	4,265
General and administrative expenses	5,239	6,197	7,480
EBIT	16,901	17,539	19,271
EBIT Margin	24.7	24.2	24.9
Interest	0	0	0
Other Income	3,050	3,660	3,877
PBT	19,951	21,199	23,148
Tax	5,598	4,451	6,019
PAT	14,353	16,749	17,130
Growth (%)	5%	17%	2%
EPS	63	74	75

Balance Sheet

Particulars (Rs. In Crore)	FY17	FY18 E	FY19 E
Shareholder's funds			
Share Capital*	1,144	1,092	1,092
Reserves & Surplus	67,838	73,362	88,081
Total	68,982	74,454	89,173
Minority Interest	0	0	0
Total Non Current Liabilities	360	177	186
Total Current Liabilities	14,013	16,941	10,190
Total Liabilities	83,355	91,573	99,549
Net Block	15,344	18,029	19,002
Capital Work-in-Progress	800	1,324	1,489
Total Non Current Assets	29,650	34,882	37,456
Cash and bank balance	22,625	23,886	24,936
Total Current Assets	53,705	56,690	62,094
Total Assets	83,355	91,573	99,549

Cash Flow Statement

Particulars (Rs. In Crore)	FY17	FY18 E	FY19 E
Profit After taxes	14,353	16,749	17,130
Add:- Depreciation	1,703	1,931	1,230
Change in Working Capital	-1,972	-5,218	-5,108
Cash generated from operations	17,184	15,145	16,503
Taxes paid	-5,653	-4,451	-6,019
Net cash flow from operating activities	11,531	10,694	10,485
Purchase of fixed assets and Capital Exp	-2,760	-4,000	-3,500
Others	-11,782	2,155	1,965
Net cash flow from investing activities	-14,542	-1,845	-1,535
Proceeds long term borrowings	0	812	500
Dividend paid, including dividend tax	-6,939	-8,365	-8,365
Net cash used in financing activities	-6,939	-7,553	-7,865
Exchange fluctuations	-122	-35	-35
Net Cash Flow	-9,950	1,296	1,085
Opening Cash balance	32,697	22,625	23,886
Closing Cash balance	22,625	23,886	24,936

Particulars	FY17	FY18 E	FY19 E
EPS	62.8	73.6	75.3
Book Value	301.8	327.3	392.0
DPS	30	40	40
Payout %	48	54	53
Dividend Yield %	3.2	3.7	3.7
P/E	14.8	14.6	14.3
EBIT Margin	24.7%	24.2%	24.9%
PBT Margin	29%	29%	30%
PAT Margin	21%	23%	22%
Debt/Equity	0.0	0.0	0.0
Current Ratio	3.83	3.35	6.09
ROE	20.8	22.5	19.2
ROCE	25.2	27.4	23.6

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Stock Rating Scale

	Absolute Return
BUY	>20%
ACCUMULATE	12% to 20%
HOLD	5% to 12%
NEUTRAL	-5% to 5%
REDUCE	<-5%

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