

## Healthy quarter...

Infosys reported a healthy set of numbers in Q1FY20 with revenue above our expectations and in-line margins. The key highlights of the quarter were, strong large deal wins (up 1.7x QoQ to \$2.7 billion) and robust growth in digital revenues (up 39.4% YoY & 8.1% QoQ). Further, owing to the healthy start, Infosys has raised its constant currency revenue growth guidance to 8.5-10% (from 7.5-9.5%) for FY20E while maintained operating margin guidance of 21%-23%.

## Deal wins, digital growth to drive double digit growth

Infosys reported 2.8% sequential revenue growth in constant currency with Stater acquisition contributing 60 bps to it. This quarter growth was broad based and across verticals with communication and Energy & utilities segment leading in terms of growth trajectory. Going forward, retail, communication and energy & utilities are expected to drive growth while BFSI & manufacturing are expected to be under pressure (due to weakness in capital markets, European banks and softness in European auto). Retail segment is expected to witness acceleration mainly led by higher spending towards digital IT and communication segment is expected to remain strong led by large deal wins and 5G. Further, strong deal wins of \$2.7 billion (new deals comprising 55% of overall deal TCV), two client additions QoQ in US\$100 million category and digital growth story (35.7% of revenue, 8% QoQ) bodes well for double digit growth in FY20E. Taking this into consideration and healthy Q1 performance, we expect dollar revenues to grow at a CAGR of 10% YoY over FY19-21E.

## Presence of tailwinds to lead to improve margin trajectory

Margins in Q1FY20E declined 90 bps sequentially to 20.5% on account of currency (-40 bps), wage hike (-60 bps), visa costs (-80 bps), Stater acquisition (-20 bps) partially offset by utilisation (70 bps), realization (20 bps) and new accounting rule (10 bps). Going ahead, with most of its investments complete and presence of levers of utilization, employee pyramid, onsite-offshore mix, we expect margins to see an improving trajectory hereon. Hence, we expect margins to increase to 22.5% in FY20E and 23% in FY21E.

## Valuation & Outlook

Healthy quarter performance, digital growth, visibility from deal pipeline and improving margin trajectory lead us to maintain our positive stance on Infosys. Further, we believe this would narrow the revenue and margin gap with TCS. However, recent run up in stock prompt us to downgrade the stock from Buy to **HOLD** with a target price of ₹ 845 (based on 19x FY21E EPS).



### Particulars

Particular	Amount
Market Capitalization (₹ Crore)	335,118.5
Total Debt	-
Cash and Investments (₹ Crore)	26,195.0
EV (₹ Crore)	308,923.5
52 week H/L	777 / 600
Equity capital	2,170.0
Face value	₹ 5

### Key Highlights

- Strong large deal wins (up 1.7x QoQ to \$2.7 billion) and robust growth in digital revenues (up 39.4% YoY & 8.1% QoQ) to drive double digit revenue growth in FY20E
- Expect margins to see improved trajectory with presence of several tailwinds
- Revise our recommendation from BUY to HOLD with a revised target price of ₹ 845

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### Key Financial Summary

₹ Crore	FY17	FY18	FY19	FY20E	FY21E	CAGR (FY19-21E)
Net Sales	50,133	70,522	82,676	91,239	99,911	9.9%
EBITDA	13,415	19,010	20,890	23,357	26,077	11.7%
EBITDA Margins (%)	27.2	27.0	25.3	25.6	26.1	
Net Profit	2,369	14,597	15,411	17,161	19,346	
EPS (₹)	47	32.3	35.4	39.4	44.5	12.1%
P/E	21.9	23.8	21.7	19.5	17.3	
RoNW (%)	25.7	22.5	23.7	24.3	25.3	
RoCE (%)	28.5	30.9	32.9	32.8	34.2	

Source: Company, ICICI Direct Research

**Exhibit 1: Variance Analysis**

	Q1FY20	Q1FY20E	Q1FY19	YoY (%)	Q4FY19	QoQ (%)	Comments
Revenue	21,803	21,743	19,128	14.0	21,539	1.2	Constant currency (cc) revenues grew 2.8% QoQ (vs. our estimate of 2.6% QoQ. Growth was led by digital, energy & utilities and communication vertical
Employee expenses	14,098	14,079	11,852	19.0	13,752	2.5	
Gross Profit	7,705	7,664	7,276	5.9	7,787	-1.1	
Gross margin (%)	35.3	35.3	38.0	-270 bps	36.2	-81 bps	
Selling & marketing costs	1,174	1,239	1,005	16.8	1,226	-4.2	
G&A expenses	1,379	1,435	1,298	6.2	1,412	-2.3	
EBITDA	5,152	4,990	4,973	3.6	5,149	0.1	
EBITDA Margin (%)	23.6	23.0	26.0	-237 bps	23.9	-28 bps	
Depreciation	681	559	436	56.2	531	28.2	
EBIT	4,471	4,431	4,537	-1.5	4,618	-3.2	
EBIT Margin (%)	20.5	20.4	23.7	-321 bps	21.4	-93 bps	Margins declined 90 bps QoQ sequentially to 20.5% on account of currency (-40 bps), wage hike (-60 bps), visa costs (-80 bps), Stater acquisition (-20 bps) partially offset by utilisation (70 bps), realization (20 bps) and new accounting rule (10 bps)
Other income	736	600	726	1.4	665	10.7	
PBT	5,207	5,032	5,263	-1.1	5,283	-1.4	
Tax paid	1,365	1,147	1,381	-1.2	1,205	13.3	
Reported PAT	3,802	3,884	3,612	5.3	4,078	-6.8	Reported PAT came in slightly below our estimate due to higher tax rate

**Key Metrics**

Closing employees	229,029	229,000	209,905	9.1	228,123	0.4	Net addition of 906 employees in the quarter
LTM attrition-standalone (%)	21.5	18.8	20.6	90 bps	18.3	320 bps	Higher attrition remains key concern
Utilisation -ex trainees (%)	83.1	83.0	85.7	-260 bps	82.3	80 bps	
Average \$/₹	69.6	69.5	67.6	3.1	70.4	-1.1	

Source: Company, ICICI Direct Research

**Exhibit 2: Change in estimates**

(₹ Crore)	FY19				FY20E				FY21E				Comments
	Current	Old	New	% Change	Old	New	% Change	Old	New	% Change			
Revenue	82,676	90,475	91,239	0.8	99,126	99,911	0.8	99,126	99,911	0.8	Healthy revenue growth in Q1 and deal pipeline lead us to revise revenue estimates		
EBIT	18,879	20,850	20,529	-1.5	23,394	22,980	-1.8	23,394	22,980	-1.8			
EBIT Margin (%)	22.8	23.0	22.5	-54 bps	23.6	23.0	-60 bps	23.6	23.0	-60 bps	Revision in margin estimates taking into consideration impact from Stater acquisition and rising attrition		
PAT	15,411	17,194	17,161	-0.2	19,613	19,346	-1.4	19,613	19,346	-1.4			
EPS (₹)	35.4	39.5	39.4	-0.2	45.1	44.5	-1.4	45.1	44.5	-1.4			

Source: Company, ICICI Direct Research

## Conference Call Highlights

- **Revenue outlook:** Owing to the healthy start and visibility from deal pipeline, Infosys has raised its constant currency revenue growth guidance to 8.5-10% (from 7.5-9.5%) for FY20E
- **Margin trajectory:** Company has maintained its EBIT margin guidance of 21-23% for FY20E. With most of its investments complete and presence of levers of utilization, employee pyramid, onsite-offshore mix, we expect margins to see an improving trajectory hereon
- **Capital allocation plan:** Board has revised its Capital Allocation Policy. Effective from FY20, the company expects to return approximately 85% of the FCF cumulatively over a 5-year period through a combination of dividends/share buyback, subject to applicable laws and requisite approvals. Company's current policy is to pay up to 70% of the free cash flow annually by way of dividend and/or buyback
- **TCV:** Large deal TCV was robust with deal signings worth ~US\$2.7 billion in the quarter, up 1.7x sequentially. Out of the overall deal pipeline, 55% is net new deal wins, which would enhance revenue growth visibility. Infosys had 13 large deals with eight in the US, four in Europe and one in RoW. Among verticals, financial services, retail constituted 3 deals each; manufacturing, communication and energy & utilities bagged two deals each and one in lifesciences
- **Digital story:** Digital continues to drive the growth of the company with 39% YoY growth and constituting 35.7% of revenues (vs. 32.2% of revenues for TCS). Further, the company is seeing traction in areas of cloud, IoT, data analytics and customer experience, which, we believe, will be key growth drivers
- **Vertical commentary:** BFSI (31.4% of revenue) grew 1.7% sequentially including Stater contribution. Weakness in capital markets and European banks are expected to be the pain points for the vertical (same as TCS). However, there are growth opportunities in consumer, corporate and commercial banking, costs and payments, and wealth management. Communication as a segment looks healthy based on deal pipeline while manufacturing is expected to see some impact from softness in Europe
- **Client update:** It was a good quarter from client perspective. Two clients were added in US\$100 million and six in US\$10 million buckets. One client transitioned from US\$50 million category
- **Employee update:** With net addition of 906 employees in the quarter, employee strength stood at 229,029 at end of Q1FY20. Attrition (consolidated) and attrition (standalone) both witnessed an increase of 300 bps and 320 bps to 23.4% and 21.5%, respectively. Higher attrition remains a concern since if this is not controlled it will have an impact on revenue and margins. Utilization (ex-trainees) increased 80 bps to 83.1%.

## Key Metrics

**Exhibit 3: Geography-wise split up**

	Q4FY18	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20
<b><u>Revenue by geography (%)</u></b>						
North America	59.4	60.0	60.3	60.4	61.2	61.6
Europe	24.8	24.3	24.0	24.2	24.0	23.6
India	2.8	2.6	2.5	2.6	2.3	2.3
ROW	13.0	13.1	13.2	12.8	12.5	12.5
<b><u>Growth QoQ in \$ terms (%)</u></b>						
North America	0.1	1.9	3.7	2.4	3.8	3.0
Europe	3.5	-1.1	1.9	3.1	1.6	0.6
India	-5.0	-6.3	-0.8	6.3	-9.4	2.3
ROW	8.5	1.7	4.0	-0.8	0.0	2.3

Source: Company, ICICI Direct Research

*Growth was led by North America and RoW*

**Exhibit 4: Vertical-wise split up**

	% contribution to revenues Q1FY20	% contribution to revenues Q4FY19	Growth QoQ (%)
<b>Revenue by verticals (%)</b>			
Financial Services	31.4	31.6	1.7
Retail	15.8	15.9	1.7
Communication	13.8	13.5	4.6
Energy, Utilities, Resources & Services	13.0	12.7	4.7
Manufacturing	9.6	10.0	-1.8
Hi Tech	7.7	7.7	2.3
Life Sciences	6.1	6.0	4.0
Others	2.6	2.6	2.3

Source: Company, ICICI Direct Research

*Among verticals, growth was strong in communication and energy & utilities*

**Exhibit 5: Client & human resource matrix**

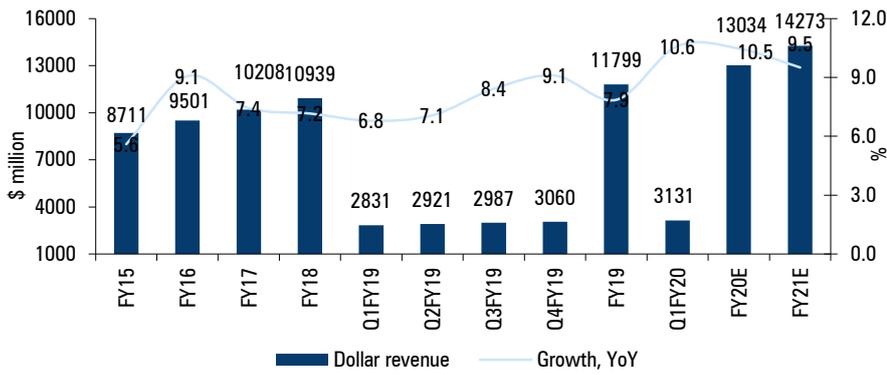
	Q4FY18	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20
<b><u>Client metrics</u></b>						
5 Million \$ clients	634	627	633	651	662	680
25 Million \$ clients	198	200	205	214	222	228
50 Million \$ clients	57	56	58	59	60	59
100 Million \$ clients	20	24	23	23	25	27
<b><u>Headcount, Utilization &amp; Attrition</u></b>						
Total Employees	204107	209905	217739	225501	228123	229029
Utilization (Excluding trainees)	84.7	85.7	85.6	83.8	82.3	83.1
LTM Attrition (Standalone)	16.6	20.6	19.9	17.8	18.3	21.5

Source: Company, ICICI Direct Research

*Two clients added in US\$100 million category*

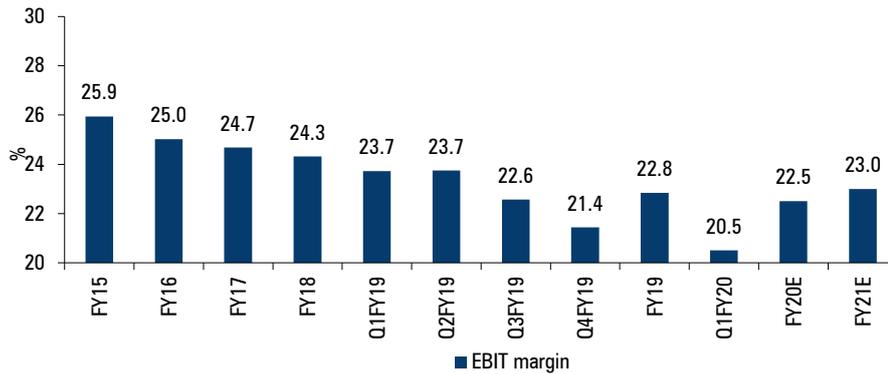
## Financial story in charts

Exhibit 6: Dollar revenues may grow at 10% CAGR in FY19-21E



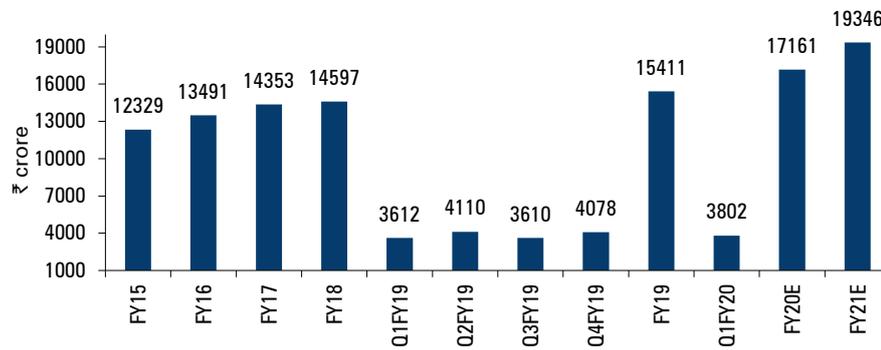
Source: Company, ICICI Direct Research

Exhibit 7: Change in margin estimates for FY20E and FY21E



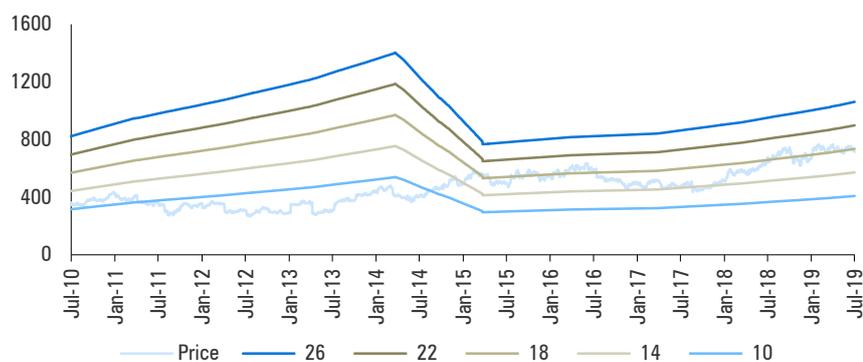
Source: Company, ICICI Direct Research

Exhibit 8: PAT trend



Source: Company, ICICI Direct Research

Exhibit 9: One year forward rolling PE



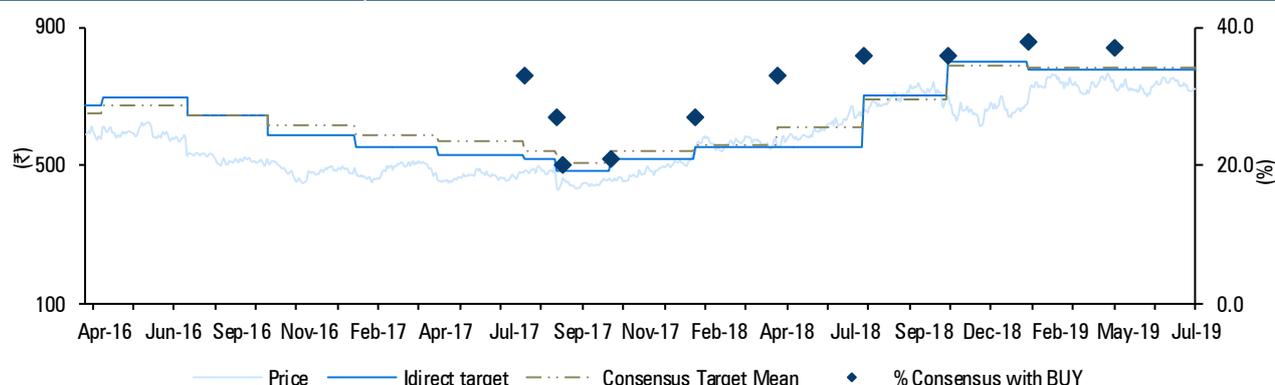
Source: Company, ICICI Direct Research

Exhibit 10: Valuation

	Sales (₹ cr)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY17	68,485	9.7	31.4	6.4	24.5	16.3	20.8	28.8
FY18	70,522	3.0	32.3	3.0	23.8	16.2	22.5	30.9
FY19	82,676	17.2	35.4	9.5	21.7	14.8	23.7	32.9
FY20E	91,239	10.4	39.4	11.4	19.5	13.0	24.3	32.8
FY21E	99,911	9.5	44.5	12.9	17.3	11.4	25.3	34.2

Source: Company, ICICI Direct Research

Exhibit 11: Recommendation History vs. Consensus



Source: Bloomberg, Company, ICICI Direct Research

Exhibit 12: Top 10 Shareholders

Rank	Name	Latest Filing Date	% O/S	Position (m)	Change (m)
1	DWS Investment GmbH	31-Mar-19	17.5%	746.3	744.9
2	Life Insurance Corporation of India	31-Mar-19	5.9%	254.3	-17.2
3	Gopalakrishnan (Sudha)	31-Mar-19	3.2%	137.2	0.0
4	The Vanguard Group, Inc.	31-May-19	3.0%	128.1	1.8
5	HDFC Asset Management Co., Ltd.	31-May-19	2.9%	123.7	-0.4
6	BlackRock Institutional Trust Company, N.A.	30-Jun-19	2.6%	109.3	0.1
7	SBI Funds Management Pvt. Ltd.	31-May-19	2.3%	99.0	-0.5
8	ICICI Prudential Asset Management Co. Ltd.	30-Jun-19	2.2%	93.7	-0.2
9	GIC Private Limited	31-Mar-19	1.9%	82.6	-2.9
10	Murty (Rohan)	31-Mar-19	1.4%	60.8	0.0

Source: Reuters, ICICI Direct Research

Exhibit 13: Recent Activity

Buys			Sells		
Investor name	Value	Shares	Investor name	Value	Shares
DWS Investment GmbH	8009.1m	744.9m	Life Insurance Corporation of India	-184.6m	-17.2m
First State Investments (Singapore)	88.8m	9.4m	First State Investments (U.K.) Ltd	-151.0m	-14.0m
Caisse de Depot et Placement du Quebec	80.9m	8.5m	Stewart Investors	-61.5m	-5.8m
Norges Bank Investment Management (NBIM)	49.0m	4.6m	APG Asset Management N.V.	-58.0m	-5.4m
Amundi Hong Kong Limited	24.8m	2.3m	Reliance Nippon Life Asset Management Limited	-49.2m	-4.6m

Source: Reuters, ICICI Direct Research

Exhibit 14: Shareholding Pattern

(in %)	Mar-18	Sep-18	Dec-18
Promoter	12.90	12.82	12.82
Public	86.61	86.70	86.70
Others	0.49	0.48	0.47
Total	100.00	100.00	100.00

Source: Company, ICICI Direct Research

## Financial summary

Exhibit 15: Profit and loss statement				
	₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E
Total operating Income	70,522	82,676	91,239	99,911
Growth (%)	3.0	17.2	10.4	9.5
COGS (employee expenses)	43,267	51,857	57,389	62,844
Admin expenses	4,684	5,454	5,566	5,695
S&M expenses	3,560	4,475	4,927	5,295
Total Operating Expenditure	51,511	61,786	67,882	73,834
EBITDA	19,010	20,890	23,357	26,077
Growth (%)	2.2	9.9	11.8	11.6
Depreciation	1,863	2,011	2,828	3,097
Other Income	3,193	2,883	2,979	3,522
PBT	20,270	21,041	23,508	26,501
Total Tax	4,241	5,630	6,347	7,155
PAT	14,597	15,411	17,161	19,346
Growth (%)	1.7	5.6	11.4	12.7
EPS (₹)	32.3	35.4	39.4	44.5
Growth (%)	3.0	9.5	11.4	12.9

Source: Company, ICICI Direct Research

Exhibit 16: Cash flow statement				
	₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E
Profit after Tax	14,597	15,411	17,161	19,346
Add: Depreciation	1,863	2,011	2,828	3,097
(Inc)/dec in Current Assets	(1,899)	(3,720)	(1,421)	(1,640)
Inc/(dec) in CL and Provisions	1,793	3,128	1,537	1,556
Taxes paid	(6,829)	(6,832)	(6,347)	(7,155)
<b>CF from operating activities</b>	<b>14,559</b>	<b>15,844</b>	<b>17,126</b>	<b>18,837</b>
(Inc)/dec in Investments	5,374	1,369	2,979	3,522
(Inc)/dec in Fixed Assets	(1,998)	(2,445)	(3,500)	(3,000)
<b>CF from investing activities</b>	<b>3,111</b>	<b>(1,578)</b>	<b>(521)</b>	<b>522</b>
Dividend paid & dividend tax	(7,464)	(13,705)	(11,582)	(13,462)
Others	5	6	-	-
<b>CF from financing activities</b>	<b>(20,505)</b>	<b>(14,512)</b>	<b>(11,582)</b>	<b>(13,462)</b>
Net Cash flow	(2,835)	(246)	5,023	5,897
Exchange difference	81	(57)	-	-
Opening Cash	22,625	19,818	19,568	24,591
<b>Closing Cash</b>	<b>19,818</b>	<b>19,568</b>	<b>24,591</b>	<b>30,489</b>

Source: Company, ICICI Direct Research

Exhibit 17: Balance sheet				
	₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E
Equity Capital	2,258	2,170	2,170	2,170
Reserve and Surplus	62,666	62,836	68,415	74,299
Total Shareholders funds	64,924	65,006	70,585	76,469
Employee benefit obligations	48	44	44	44
Debt	-	-	-	-
Deferred Tax Liability	541	672	672	672
Other non current liabilities	272	378	378	378
<b>Total Liabilities</b>	<b>65,785</b>	<b>66,100</b>	<b>71,679</b>	<b>77,563</b>
<b>Assets</b>				
Property, plant and equipment	12,143	13,356	14,028	13,930
Goodwill	2,211	3,540	3,540	3,540
Intangibles	247	691	691	691
Available for sale assets	5,756	4,634	4,634	4,634
Other assets	9,516	9,639	9,639	9,639
Cash	19,818	19,568	24,591	30,489
Current Investments	6,407	6,627	6,627	6,627
Trade receivables	13,142	14,827	16,363	17,918
Unbilled revenue	4,261	5,374	5,018	5,495
Prepayment & O.fin.assets	6,373	6,146	6,387	5,995
Other current assets	16	336	336	336
Total Current Assets	50,017	52,878	59,322	66,859
Trade payables	694	1,655	1,826	2,000
Unearned revenue	2,295	2,809	3,100	3,395
OCL & provisions	11,116	14,174	15,248	16,336
Total Current Liabilities	14,105	18,638	20,175	21,731
Net Current Assets	35,912	34,240	39,147	45,129
<b>Application of Funds</b>	<b>65,785</b>	<b>66,100</b>	<b>71,679</b>	<b>77,563</b>

Source: Company, ICICI Direct Research

Exhibit 18: Key ratios				
(Year-end March)	FY18	FY19	FY20E	FY21E
<b>Per share data (₹)</b>				
EPS	32.3	35.4	39.4	44.5
Cash EPS	36.5	40.0	45.9	51.6
BV	144	149	162	176
DPS	43.5	20.9	22.1	25.7
Cash Per Share	44	45	57	70
<b>Operating Ratios (%)</b>				
EBIT Margin	24.3	22.8	22.5	23.0
PBT Margin	28.7	25.4	25.8	26.5
PAT Margin	20.7	18.6	18.8	19.4
Debtor days	68	65	65	65
Unbilled revenue	20	21	21	19
Creditor days	4	7	7	7
<b>Return Ratios (%)</b>				
RoE	22.5	23.7	24.3	25.3
RoCE	30.9	32.9	32.8	34.2
RoIC	43.3	47.3	50.7	56.8
<b>Valuation Ratios (x)</b>				
P/E	24	22	20	17
EV / EBITDA	16	15	13	11
EV / Net Sales	4	4	3	3
Market Cap / Sales	5	4	4	3
Price to Book Value	5	5	5	4
<b>Solvency Ratios</b>				
Debt/EBITDA	-	-	-	-
Debt / Equity	-	-	-	-
Current Ratio	3	2	2	2
Quick Ratio	3	2	2	2

Source: Company, ICICI Direct Research

Exhibit 19: ICICI Direct coverage universe (IT)

Sector / Company	CMP			M Cap (₹ Cr)	EPS (₹)			P/E (x)			EV/EBITDA (x)			RoCE (%)			RoE (%)		
	(₹)	TP(₹)	Rating		FY18	FY19	FY20E	FY18	FY19	FY20E	FY18	FY19	FY20E	FY18	FY19	FY20E	FY18	FY19	FY20E
Cyient (INFENT)	546	620	Hold	6,530	36.0	42.4	46.6	16.1	13.7	12.4	10.3	9.1	7.5	21.4	21.4	20.7	17.3	18.7	18.1
Eclerx (ECLSER)	637	860	Reduce	3,532	72.9	60.0	63.1	12.7	15.5	14.7	8.0	9.1	9.2	28.2	21.5	24.8	24.1	16.5	18.9
Firstsource (FIRSOU)	51	60	Buy	3,502	4.8	5.4	5.9	10.7	9.4	8.6	8.8	7.2	6.2	13.0	14.0	15.7	13.9	13.9	13.8
HCL Tech (HCLTEC)	1,028	1,190	Hold	146,833	62.6	74.7	76.7	17.3	14.5	14.1	12.5	10.1	9.1	27.4	26.5	26.0	23.8	24.5	22.5
Infosys (INFTEC)	770	845	Hold	335,118	32.3	35.4	39.4	23.8	21.7	19.5	16.2	14.8	13.0	30.9	32.9	32.8	22.5	23.7	24.3
L&T Intotech (LTINFO)	1,607	1,940	Buy	29,148	64.7	87.3	94.6	26.0	19.2	17.7	23.2	14.3	12.3	36.0	40.4	36.4	28.8	31.0	27.8
NIIT Tech (NIITEC)	1,345	1,395	Hold	7,677	45.6	65.7	76.1	27.8	19.0	16.7	13.8	10.4	8.9	19.4	24.2	24.3	15.8	19.9	20.2
Persistent (PSYS)	620	650	Hold	5,119	40.5	44.0	48.7	15.8	14.6	13.2	9.1	7.1	6.4	19.8	20.5	20.5	15.2	15.0	14.9
TCS (TCS)	2,115	2,080	Hold	790,125	67.4	83.8	88.8	31.2	25.0	23.7	23.0	18.9	17.2	37.6	43.8	43.2	29.6	34.4	33.9
Tech M (TECMAH)	674	845	Hold	67,723	42.8	47.7	51.4	17.6	15.8	14.6	13.4	9.5	8.2	21.5	23.6	23.2	20.2	21.2	19.8
Wipro (WIPRO)	258	315	Buy	171,636	12.7	14.9	17.3	22.5	19.1	16.4	14.8	12.0	10.2	16.9	17.8	18.1	16.6	15.8	16.7

Source: Company, ICICI Direct Research

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Buy: > 15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: < -15%



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