

Healthy performance continues....

Infosys reported healthy set of Q2FY21 numbers on the revenue and profitability front. Revenues increased 4.0% QoQ vs. our estimate of 3.3%. The company also reported healthy EBIT margin of 25.3% (vs. our estimate of 23.8%). Digital revenues increased 12.9% QoQ, 27.5% YoY and now account for 47.3% of overall revenues. The large deal pipeline increased 80.7% QoQ mainly due to addition of Vanguard deal. Further, Infosys has outperformed Tata Consultancy Service (TCS) in terms of revenue growth in YoY terms in which TCS' dollar revenues declined 1.7% YoY vs. Infosys, which increased by 3.2% YoY in Q2FY21. In terms of guidance, Infosys has revised its FY21E revenues guidance upwards from 0-2% YoY to 2-3% YoY & operating margin guidance to 23-24% from 21-23%.

Revenues to be driven by digital, large deal pipeline

Infosys, over the past few quarters, has executed well on the basis of healthy large deal wins and traction in digital. Going forward, we expect digital revenues to further witness healthy growth on the back of enterprise migrating to cloud. Further, the company is also winning large deals on back of automation, traction in consumer experience & data, core modernisation and cost take outs. In addition, we expect acceleration in vendor consolidation opportunities (which may pan out in subsequent quarters) and acquisition of captives to further drive revenues in coming years. Hence, we expect Infosys to register 9% CAGR in dollar revenues over FY20-23E.

Revenue improvement to drive margins

Margins in Q2FY21 improved 269 bps, mainly led by utilisation (80 bps QoQ), offshoring (80 bps QoQ), pricing (100 bps) partially offset by rupee appreciation and cross currency headwinds. The company will give wage hike to all its employees effective January 2021 and expects travel & change in mix to impact margins. However, we believe rationalisation of onsite pyramid, automation, lower subcontracting cost and improvement in revenues to offset the near-term margin headwinds. Hence, we expect the company to register EBIT margins near the upper end of guided range of 23-24% in FY21E. In addition, we expect the company to maintain 23.5% and 23.8% margins in FY22E and FY23E, respectively.

Valuation & Outlook

Infosys has consistently outperformed TCS over the past few quarters and also narrowed the margin gap between the two companies. In addition, healthy deal wins are expected to help the company make steady improvement in financials in coming quarters. Digital acceleration, large deal wins vendor consolidation and cost rationalisation remain key long term drivers. Further, Infosys has maintained healthy cash flow generation and has a consistent dividend payout policy. We remain positive on the stock and maintain our **BUY** rating on the stock with a target price of ₹ 1350/share.

Particulars

Particular	Amount
Market CAP (₹ Crore)	4,84,500.6
Total Debt	-
CC&E (₹ Crore)	23,304.0
EV (₹ Crore)	4,61,196.6
52 week H/L	1165 / 511
Equity capital	2,170.0
Face value	₹ 5

Key Highlights

- Large deal wins, vendor consolidation and acceleration in digital technologies remain key long term revenue drivers
- Expect margins to sustain above 23% in coming years
- Maintain BUY with revised target price of ₹ 1350/share (24x FY23E EPS)

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Key Financial Summary

₹ Crore	FY19	FY20	FY21E	FY22E	FY23E	CAGR (FY20-23E)
Net Sales	82,676	90,791	98,738	1,09,816	1,24,305	11.0%
EBITDA	20,890	22,279	26,857	29,321	33,562	14.6%
EBITDA Margins (%)	25.3	24.5	27.2	26.7	27.0	
Net Profit	15,411	16,595	19,541	20,928	24,016	
EPS (₹)	35.4	38.9	46.0	49.3	56.5	13.3%
P/E	32.1	29.2	24.7	23.1	20.1	
RoNW (%)	23.7	25.2	27.2	26.9	28.4	
RoCE (%)	32.9	30.8	33.5	33.3	35.3	

Source: Company, ICICI Direct Research

Exhibit 1: Variance Analysis

	Q2FY21	Q2FY21E	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	Comments
Revenue	24,570	24,312	22,629	8.6	23,665	3.8	The company reported 4.0% QoQ growth in dollar revenues led by healthy growth
Employee expenses	14,916	15,071	14,352	3.9	14,947	-0.2	
Gross Profit	9,654	9,241	8,277	16.6	8,718	10.7	
Gross margin (%)	39.3	38.0	36.6	271 bps	36.8	245 bps	
Selling & marketing	1,136	1,216	1,162	-2.2	1,146	-0.9	
G&A expenses	1,435	1,483	1,476	-2.8	1,451	-1.1	
EBITDA	7,083	6,542	5,639	25.6	6,121	15.7	
EBITDA Margin (%)	28.8	26.9	24.9	391 bps	25.9	296 bps	
Depreciation	855	756	727	17.6	756	13.1	
EBIT	6,228	5,786	4,912	26.8	5,365	16.1	
EBIT Margin (%)	25.3	23.8	21.7	364 bps	22.7	268 bps	EBIT margin improved led by utilisation (80 bps QoQ), offshoring (80 bps QoQ), pricing (100 bps) while improvement in SG&A was partially offset by rupee appreciation and
Other income	570	428	626	-8.9	475	20.0	
PBT	6,798	6,214	5,538	22.8	5,840	16.4	
Tax paid	1,892	1,542	1,459	29.7	1,520	24.5	
Reported PAT	4,851	4,609	4,019	20.7	4,233	14.6	Reported PAT came in above our estimate due to better performance at operating level and higher than expected other

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

	FY21E			FY22E			FY23E	Comments
	Old	New	% Change	Old	New	% Change		
(₹ Crore)							Introduced	
Revenue	96,237	98,738	2.6	1,05,637	1,09,816	4.0	1,24,305	Traction in digital technology and healthy deal pipeline prompt us to revised our revenue estimates upwards
EBIT	21,942	23,697	8.0	24,296	25,807	6.2	29,585	
EBIT Margin (%)	22.8	24.0	120 bps	23.0	23.5	50 bps	23.8	We have revised our margin estimates upwards considering strong execution in Q2FY21E and cost rationalisation
PAT	18,270	19,541	7.0	21,159	20,928	-1.1	24,016	
EPS (₹)	43.1	46.0	6.7	49.9	49.3	-1.2	56.5	

Source: Company, ICICI Direct Research

Conference Call Highlights

- **Revenue outlook:** The company's performance in the quarter was better than its peers. We believe the improved performance in the quarter was due to market share gains and ramp up of large deal wins. The company has indicated healthy traction in BFSI due to vanguard deal, cost take out opportunities in troubled sector, traction in cloud, vendor consolidation opportunities and market share gains. In addition, improved deal pipeline (15 large deal won in the quarter) is expected to drive company's revenues. We believe this has prompted Infosys to revise its guidance upwards from 0-2% YoY to 2-3% YoY in FY2E. The company has also done three acquisitions which might further add to company's topline
- **Other highlights:** The company highlighted a few pointers for better performance than peers like better client servicing, focus on large deals, higher market share gains, early adoption of WFM, pivoted to new ways of sales, focus on digital capability and localisation play. The company is seeing healthy traction in existing markets and sees vendor consolidation opportunities to moving slowly and can pan out in coming quarters
- **Margin trajectory:** Margins in Q2FY21 improved 269 bps, mainly led by utilisation (80 bps QoQ), offshoring (80 bps QoQ), pricing (100 bps) partially offset by rupee appreciation and cross currency headwinds. The company will give wage hike to all its employees effective January 2021 and expects travel and change in mix to impact margins. However, we believe that rationalisation of onsite pyramid, automation, lower subcontracting cost and improvement in revenues would offset the near-term margin headwinds. Hence, we expect the company to register EBIT margins near the upper end of guided range of 23-24% in FY21E. In addition, we expect the company to maintain 23.5% and 23.8% margins in FY22E and FY23E
- **TCV:** Large deal TCV was healthy with deal signings worth ~US\$3.14 billion in the quarter, up 80.7% QoQ. We believe the robust growth in deal pipeline was mainly led by US\$1.5 bn deal of Vanguard. Out of the total deal, 86% was net new. The company sees improved traction with cloud deals, cyber security and automation. The company won 15 large deals in the quarter while the deal won was broad based and across geographies. Eleven deals were in Americas, four in Europe and one in RoW
- **Digital story:** Digital continues to drive the growth of the company with 27.5% YoY growth and constituting 47.3% of revenues (vs. 38.3% in Q2FY20). Further, the company continues to see acceleration in digital technology like cyber security, cloud, data, experience and automation
- **Employee update:** There was a marginal addition of 975 employees taking employee strength to 240,208. Of the total employees hired 3000 were fresher and 2500 laterals. The company plans to hire 16500 freshers this year and 16000 next fiscal. Attrition at a consolidated level witnessed a reduction from 11.7% to 7.8%. With growth improving across sectors, this number could inch up in coming quarters. The company is planning to give wage hike to all its employees effective January 2021. Utilisation (ex-trainees) improved 240 bps sequentially to 83.6% in Q2FY21

Key Metrics

Exhibit 3: Geography-wise split

	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21
<u>Revenue by geography (%)</u>					
North America	61.4	61.3	61.6	61.5	60.7
Europe	24.1	24.4	24.4	24.0	24.3
India	2.7	2.8	2.6	2.9	3.0
ROW	11.8	11.5	11.4	11.6	12.0
<u>Growth QoQ in \$ terms (%)</u>					
North America	2.2	0.9	-0.9	-2.5	4.7
Europe	4.7	2.3	-1.4	-4.0	7.4
India	20.4	4.8	-8.5	8.9	9.8
ROW	-3.2	-1.5	-2.3	-0.7	9.8

Source: Company, ICICI Direct Research

Revenues growth was across geographies

Exhibit 4: Vertical-wise split

	% contribution to revenues Q2FY21	% contribution to revenues Q1FY21	Growth QoQ (%)
<u>Revenue by verticals (%)</u>			
Financial Services	32.0	31.5	7.8
Insurance			
Retail	14.9	14.3	10.6
Communication	12.6	13.4	-0.2
E&U	12.3	12.8	2.0
Manufacturing	9.1	9.5	1.7
Hi Tech	9.1	8.7	11.0
Life Sciences	6.8	6.7	7.7
Others	3.2	3.1	14.3

Source: Company, ICICI Direct Research

The company has seen growth across verticals except communication. The company sees cost take out opportunities in troubled verticals

Exhibit 5: Client & human resource matrix

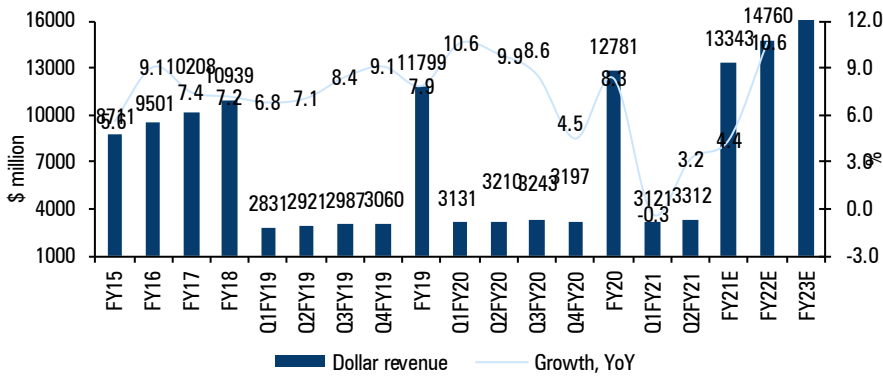
	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21
<u>Client metrics</u>					
5 Million \$ clients	693	705	718	729	745
25 Million \$ clients	228	232	234	236	242
50 Million \$ clients	61	61	61	60	60
100 Million \$ clients	27	28	28	25	30
<u>Headcount, Utilization & Attrition</u>					
Total Employees	236486	243454	242371	239233	240208
Utilization (Excluding trainees)	84.9	84.4	83.5	81.2	83.6
LTM Attrition	21.7	19.6	20.7	11.7	7.8

Source: Company, ICICI Direct Research

The company added five new clients in US\$100 million category and has seen lowest attrition. However, Infosys believes this could inch up with pick-up in demand

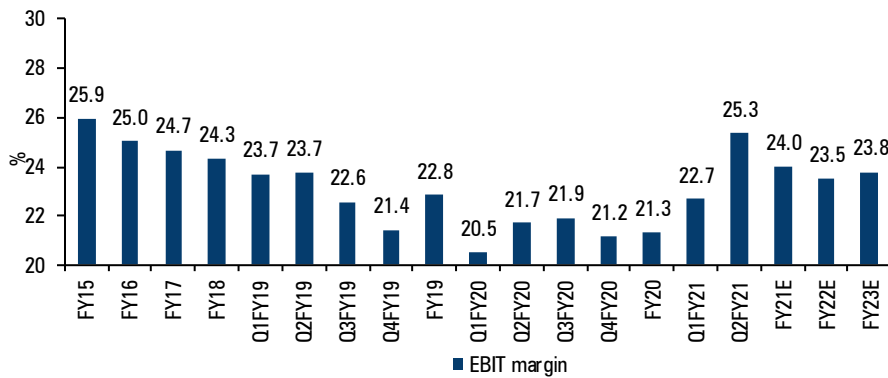
Financial story in charts

Exhibit 6: Dollar revenues to increase at a CAGR of 9% over FY20-23E



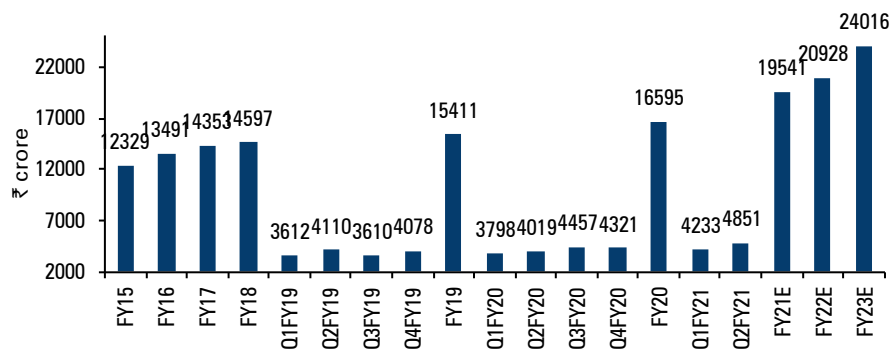
Source: Company, ICICI Direct Research

Exhibit 7: Change in margin estimates for FY21E & FY22E, introduced FY23E



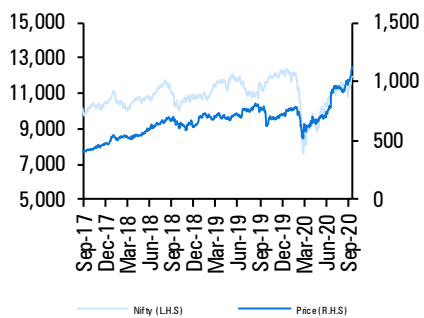
Source: Company, ICICI Direct Research

Exhibit 8: PAT trend



Source: Company, ICICI Direct Research

Exhibit 9: Three year price chart



Source: Company, ICICI Direct Research

Financial summary

Exhibit 10: Profit and loss statement				
	₹ crore			
(Year-end March)	FY20	FY21E	FY22E	FY23E
Total operating Income	90,791	98,738	1,09,816	1,24,305
Growth (%)	9.8	8.8	11.2	13.2
COGS (employee expenses)	57,827	61,020	68,196	76,820
Admin expenses	5,973	5,924	6,809	7,707
S&M expenses	4,712	4,937	5,491	6,215
Total Operating Expenditure	68,512	71,881	80,495	90,743
EBITDA	22,279	26,857	29,321	33,562
Growth (%)	6.7	20.5	9.2	14.5
Depreciation	2,905	3,160	3,514	3,978
Other Income	2,803	2,331	2,046	2,353
PBT	22,007	25,849	27,683	31,768
Total Tax	5,367	6,307	6,755	7,751
PAT	16,595	19,541	20,928	24,016
Growth (%)	7.7	17.8	7.1	14.8
EPS (₹)	38.9	46.0	49.3	56.5
Growth (%)	9.9	18.2	7.1	14.8

Source: Company, ICICI Direct Research

Exhibit 11: Cash flow statement				
	₹ crore			
(Year-end March)	FY20	FY21E	FY22E	FY23E
Profit after Tax	16,595	19,541	20,928	24,016
Add: Depreciation	2,905	3,160	3,514	3,978
(Inc)/dec in Current Assets	(3,357)	(2,730)	(3,808)	(4,980)
Inc/(dec) in CL and Provisions	1,419	1,439	2,007	2,626
Taxes paid	(4,550)	(6,307)	(6,755)	(7,751)
CF from operating activities	18,557	19,079	20,596	23,286
(Inc)/dec in Investments	(322)	2,331	2,046	2,353
(Inc)/dec in Fixed Assets	(3,307)	(3,000)	(3,000)	(3,000)
CF from investing activities	(1,793)	(669)	(954)	(647)
Dividend paid & dividend tax	(9,515)	(13,667)	(14,956)	(17,243)
Others	(27)	-	-	-
CF from financing activities	(17,591)	(13,667)	(14,956)	(17,243)
Net Cash flow	(827)	4,743	4,685	5,396
Exchange difference	(92)	-	-	-
Opening Cash	19,568	18,649	23,392	28,077
Closing Cash	18,649	23,392	28,077	33,474

Source: Company, ICICI Direct Research

Exhibit 12: Balance sheet				
	₹ crore			
(Year-end March)	FY20	FY21E	FY22E	FY23E
Equity Capital	2,122	2,122	2,122	2,122
Reserve and Surplus	63,722	69,596	75,568	82,341
Total Shareholders funds	65,844	71,718	77,690	84,463
Employee benefit obligation:	38	38	38	38
Debt	-	-	-	-
Deferred Tax Liability	968	968	968	968
Other non current liabilities	5,062	5,062	5,062	5,062
Total Liabilities	71,912	77,786	83,758	90,531
Assets				
Property, plant and equipme	17,867	17,707	17,193	16,216
Goodwill	5,286	5,286	5,286	5,286
Intangibles	1,900	1,900	1,900	1,900
Available for sale assets	4,137	4,137	4,137	4,137
Other assets	9,002	9,002	9,002	9,002
Cash	18,649	23,392	28,077	33,474
Current Investments	4,655	4,655	4,655	4,655
Trade receivables	18,487	20,103	22,359	25,308
Unbilled revenue	7,121	7,744	8,613	9,750
Prepayment & O.fin.assets	5,602	6,092	6,776	7,670
Other current assets	62	62	62	62
Total Current Assets	54,576	62,049	70,542	80,919
Trade payables	2,852	3,100	3,448	3,903
Unearned revenue	2,990	3,252	3,617	4,094
OCL & provisions	15,014	15,943	17,237	18,931
Total Current Liabilities	20,856	22,295	24,302	26,928
Net Current Assets	33,720	39,754	46,240	53,991
Application of Funds	71,912	77,786	83,758	90,531

Source: Company, ICICI Direct Research

Exhibit 13: Key ratios				
(Year-end March)	FY20	FY21E	FY22E	FY23E
Per share data (₹)				
EPS	38.9	45.9	49.2	56.4
Cash EPS	45.7	53.3	57.4	65.8
BV	154	169	183	198
DPS	22.3	32.1	35.1	40.5
Cash Per Share	44	55	66	79
Operating Ratios (%)				
EBIT Margin	21.3	24.0	23.5	23.8
PBT Margin	24.2	26.2	25.2	25.6
PAT Margin	18.3	19.8	19.1	19.3
Debtor days	74	74	74	74
Unbilled revenue	25	27	27	27
Creditor days	11	11	11	11
Return Ratios (%)				
RoE	25.2	27.2	26.9	28.4
RoCE	30.8	33.5	33.3	35.3
RoIC	39.9	47.6	50.6	56.5
Valuation Ratios (x)				
P/E	29.2	24.7	23.1	20.1
EV / EBITDA	20.7	17.0	15.4	13.3
EV / Net Sales	5.1	4.6	4.1	3.6
Market Cap / Sales	5.3	4.9	4.4	3.9
Price to Book Value	7.4	6.7	6.2	5.7
Solvency Ratios				
Debt/EBITDA	-	-	-	-
Debt / Equity	-	-	-	-
Current Ratio	2.1	2.1	2.1	2.1
Quick Ratio	2.1	2.1	2.1	2.1

Source: Company, ICICI Direct Research

Exhibit 14: ICICI Direct coverage universe (IT)

Company	Cmp (₹)	TP (₹)	Rating	Mcap (₹ Cr)	EPS (₹)			P/E (x)			RoCE (%)			RoE (%)		
					FY20	FY21E	FY22E	FY20	FY21E	FY22E	FY20	FY21E	FY22E	FY20	FY21E	FY22E
					HCL Tech (HCLTEC)	890	885	Hold	2,41,543	40.8	46.3	52.5	22	19	17	23.0
Infosys (INFTEC)	1,136	1,350	Buy	4,84,500	38.9	45.9	49.2	29	25	23	30.8	33.5	33.3	25.2	27.2	26.9
TCS (TCS)	280	3,300	Buy	10,54,345	86.2	87.2	103.8	3	3	3	43.5	44.5	49.0	37.5	37.1	42.3
Tech M (TECMAH)	849	765	Buy	82,054	45.9	44.0	51.0	19	19	17	19.1	16.4	17.4	18.5	16.0	16.7
Wipro (WIPRO)	350	435	Buy	2,00,109	16.6	18.1	19.8	21	19	18	19.3	21.0	22.4	17.4	18.6	19.9
Mindtree (MINCON)	1,553	1,160	Buy	25,586	38.3	51.8	60.3	41	30	26	23.0	26.6	27.4	20.0	22.9	23.3
LTI (LTINFC)	3,320	2,320	Hold	57,962	86.6	97.1	113.6	38	34	29	30.7	29.2	29.2	28.1	26.4	26.2
Coforge (NIITEC)	2,605	2,200	Buy	15,783	71.4	75.3	94.4	36	35	28	23.0	24.7	26.0	18.5	19.4	21.2
Infoedge (INFEDG)	3,747	3,555	Hold	48,184	26.8	27.8	33.4	140	135	112	18.0	10.6	12.0	13.5	7.9	8.9
Teamlease (TEASER)	2,342	2,205	Buy	4,010	20.5	48.2	62.8	114	49	37	15.0	12.7	14.1	6.5	12.9	14.5

Source: Company, ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: < -15%



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