

BSE SENSEX
43,278

S&P CNX
12,631

Infosys

Stock Info

Bloomberg	INFO IN
Equity Shares (m)	4,572
M.Cap.(INRb)/(USDb)	4781.6 / 62.5
52-Week Range (INR)	1185 / 511
1, 6, 12 Rel. Per (%)	-6/26/51
12M Avg Val (INR M)	8927

Financials Snapshot (INR b)

Y/E Mar	2020	2021E	2022E
Sales	908	1,004	1,154
EBIT Margin (%)	21.3	24.4	25.0
PAT	166	194	229
EPS (INR)	38.9	45.7	54.1
EPS Gr. (%)	5.1	17.4	18.4
BV/Sh. (INR)	145	182	208

Ratios

RoE (%)	25.2	25.1	26.0
RoCE (%)	20.4	21.4	22.6
Payout (%)	44.9	45.5	45.5

Valuations

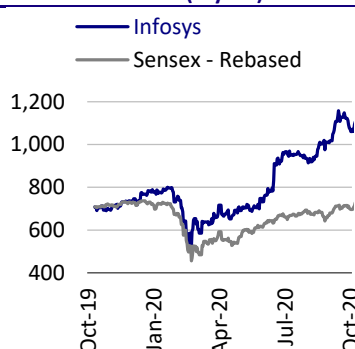
P/E (x)	28.9	24.6	20.8
P/BV (x)	7.8	6.2	5.4
EV/EBITDA (x)	23.0	17.1	14.6
Div Yield (%)	1.6	1.9	2.2

Shareholding pattern (%)

As On	Sep-20	Jun-20	Sep-19
Promoter	13.0	13.2	13.2
DII	25.0	25.4	22.8
FII	31.7	30.9	34.0
Others	30.4	30.5	30.1

FII Includes depository receipts

Stock Performance (1-year)



CMP: INR1,123

TP: INR1,355 (+21%)

Buy

Robust outlook on both growth and profitability

We attended Infosys (INFO)'s Analyst Day, wherein the management shared their views on the industry outlook and drivers for future revenue and margin expansion. Here are the key highlights from the meet:

- Overall, the commentary from Infosys was quite positive as the management expressed a) their confidence about returning to pre-COVID growth levels; b) scope for a further upside on operating margins; c) significant opportunity from the shift to cloud; d) acceleration in the deal pipeline since the pandemic.
- It further highlighted the ambition to eventually have 33% of the workforce operating flexibly/remotely, which should help lower capex and D&A expenses.
- At the board level, the Infosys chairman reiterated the board's confidence in the management and expressed the willingness to retain their position as long as necessary. This should mitigate any remnant concern related to the management and board's stability.
- Infosys' outlook for a large wave of technological investment is in line with our expectation. This should lead to a strong demand outlook for the IT Services industry in the medium term.

Cloud is now the key focus area

- Infosys sees cloud (hybrid, multi and poly cloud) as a USD500b enterprise investment opportunity and expects this to drive massive market opportunity in the migration and maintenance space.
- The management further highlighted its response through the launch of Infosys Cobalt, the first cloud brand in the IT Services market. It currently has 35K associates working in the space and 200+ solutions on Cobalt.

Margin expansion despite investment need

- INFY believes there is scope for margin expansion despite the continued need for investment in automation and digital capabilities.
- While it believes near-term factors such as wage delays and low travel expenses are reversible, it expects to drive margin improvement through a better business mix, continued pyramid optimization, higher automation, tighter management of sub-contractor cost, and increasing digital value-add.

Valuation and view

- We remain positive on Infosys and reiterate the stock as our top idea in the IT Services space. We continue to see Infosys as a key beneficiary of recovery in IT spends in FY22. We expect the company to deliver the best growth in the near-to-medium term in the large-cap space.
- Infosys should narrow the divergence in its valuation with TCS to 10%. On our estimates, the stock is currently trading at 21x FY22 EPS. We value the stock at 25x FY22E EPS (10% discount to TCS). Reiterate Buy.

Acceleration of existing tech trends

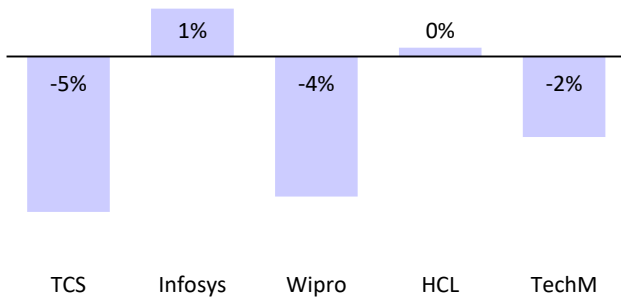
- Mr Nandan Nilekani highlighted seven key areas of technology spends, including 1) consumerization in user experience, 2) the adoption of Open Source technology, 3) cloud migration, 4) AI & analytics, 5) cybersecurity, 6) platforms, and 7) the modernization of the legacy system. The current pandemic has accelerated these trends; work that was expected to be done over several years has been compressed into several months.
- This is largely attributable to incumbent companies realizing that with the changing landscape, they have to be digitally agile to not only excel but also survive.
- This has led to resilience in client budgets. One of the key trends that have been accelerated is cloud adoption. This is driving massive market opportunity in the migration and maintenance space for IT service providers.

Business strategy

- To leverage underlying trends in the industry, Infosys has identified four key strategies: 1) scaling up digital capabilities, 2) focusing on deepening automation and AI, 3) continuing the re-skilling of employees, and 4) implementing higher localization.
- With resiliency in its strategy, INFO is poised for growth. The company has been continuously increasing the proportion of digital (47% of revenues), winning large deals, expanding existing accounts, and launching new logos.
- Furthermore, operational sustainability is also seen on account of higher localization. Currently, around 63% of the workforce in the US is local and over 50% is local in Europe, New Zealand, and Australia. Despite H1-B visa regulations expected to ease in the US, the company continues to expand localization and aims to reach 25k hiring by 2022.

Cloud adoption to be growth driver

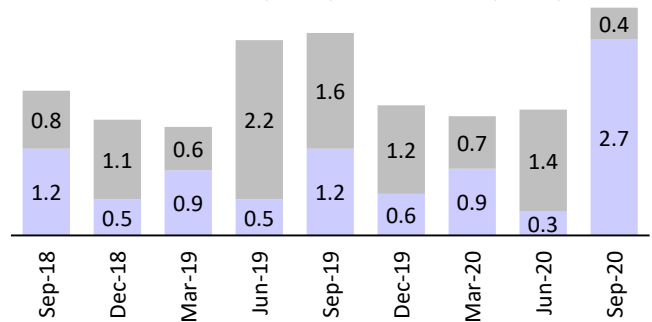
- Everything is shifting to digital. Digital revenues, constituting 47% of revenues, grew 25% in 2Q.
- Large deal momentum is very strong for the company. The company reported the biggest large-deal value in 2Q.
- The company is focusing on expanding its work with existing clients; it is opening new accounts by understanding what is relevant for them and how to help them in navigating the next.
- From the chairman to the management, all highlighted the opportunities presented by the cloud and the company's response capitalizing on this through the launch of Infosys Cobalt – the first cloud brand in the IT Services market. Infosys expects this to drive massive market opportunity in the migration and maintenance space, and highlighted that its 35k associates are focused in the space.
- The company posted positive YoY growth in 1Q/2QFY21. The management believes it is gaining market share as clients look to consolidate their positions.

Exhibit 1: Only company to drive positive growth in 1HFY21**USD Revenue Growth in 1HFY21 (YoY %)**

Source: Company, MOFSL

Exhibit 2: New deal wins were significantly larger

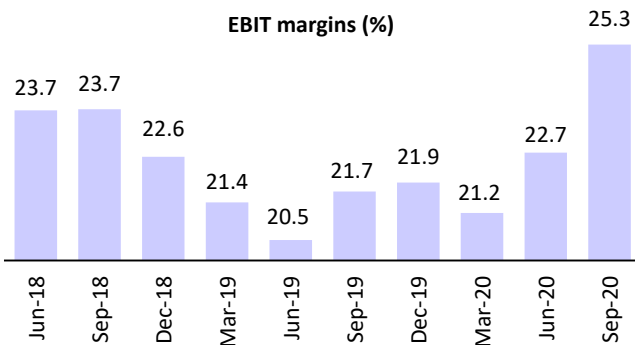
■ New deal wins (USD b) ■ Renewals (USD b)



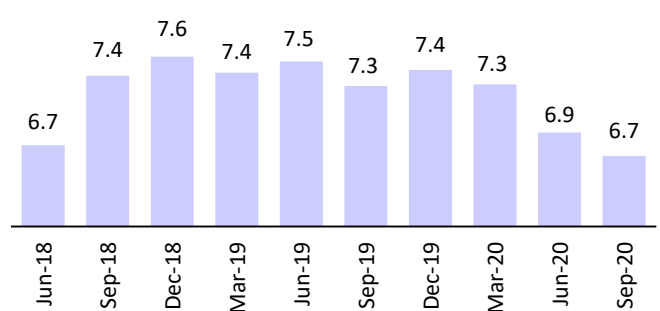
Source: Company, MOFSL

Margin expansion despite investment need

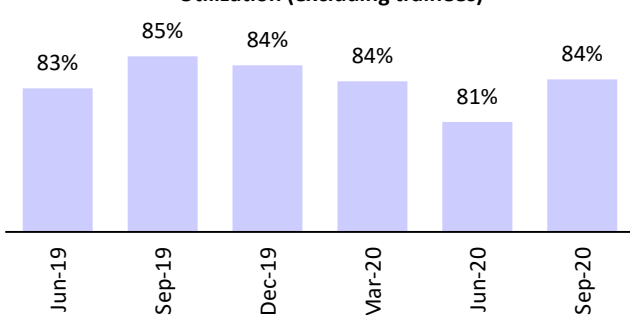
- The investment phase of the company is now behind, and all new investments are to be funded from the P&L. The company is looking to sustain margins in the near term and aims to expand the margin band going forward.
- Strategic cost levers such as automation, offshore mix, operating leverage, etc. have resulted in permanent cost savings for the company. Other costs such as travel and visa and facilities expenses are expected to return as the situation normalizes, but would not reach pre-COVID levels.
- Although future remote working is expected to aid margins significantly, this would be partly offset by increased spend on technology, security, and communication. However, net-net, the impact is beneficial for the industry.
- A clear set of margin drivers is in place, which would help sustain margins and expand them in the long run.

Exhibit 3: Margin expansion robust...**EBIT margins (%)**

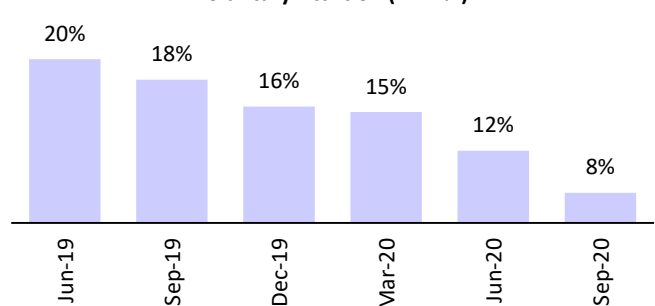
Source: Company, MOFSL

Exhibit 4: ...partly due to reduction in sub-con expenses...**Sub-con costs as % of sales**

Source: Company, MOFSL

Exhibit 5: ...increase in utilizations...**Utilization (excluding trainees)**

Source: Company, MOFSL

Exhibit 6: ...and reduction in attrition (lowest)**Voluntary Attrition (LTM %)**

Source: Company, MOFSL

Cash conversion and returns to shareholders

- Margin expansion, robust WC management, and lower capex have led to a robust increase in FCF generation for the company. It generated USD1.4b FCF in 1HFY21 (increase of 59% YoY).
- The company has consistent and increasing dividend payouts, ensuring at least 85% of FCF is returned to the shareholders.
- The company has returned 120% to its shareholders in the past three years.

Exhibit 7: Consistent and increasing dividend payouts...

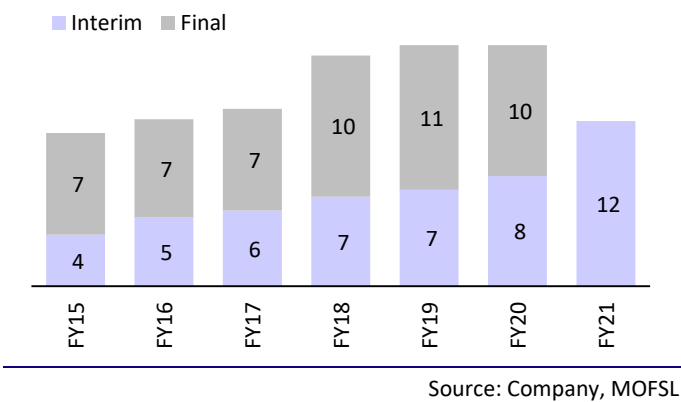
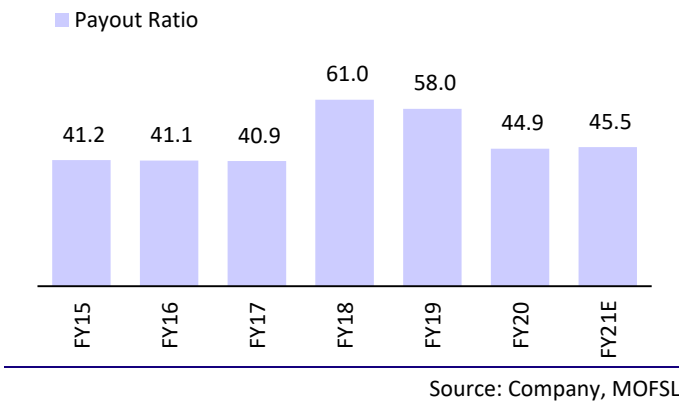


Exhibit 8: ...leading to healthy payout ratio



Financials and valuations

Income Statement							(INR b)	
Y/E March	2015	2016	2017	2018	2019	2020	2021E	2022E
Sales	533	624	685	705	827	908	1,004	1,154
Change (%)	6.4	17.1	9.7	3.0	17.2	9.8	10.6	14.9
Software Develop. Exp.	329	391	433	451	539	607	653	744
SGA expenses	66	77	83	82	99	107	107	121
EBITDA	149	171	186	190	209	223	278	327
% of Net Sales	27.9	27.4	27.2	27.0	25.3	24.5	27.7	28.3
Depreciation	11	15	17	19	20	29	33	38
Interest	0	0	0	0	0	0	0	0
Other Income	34	31	31	32	29	26	20	22
PBT	173	187	200	203	218	220	265	311
Tax	49	53	56	42	56	54	70	81
Rate (%)	28.6	28.0	28.0	20.9	25.9	24.4	26.6	26.0
Minority Interest	0	0	0	0	0	0	1	0
Adjusted PAT	123	135	144	161	161	166	194	229
Extraordinary Items	0	0	0	0	7	0	0	0
Reported PAT	123	135	144	161	154	166	194	229
Change (%)	11.2	9.4	6.6	11.9	-4.3	7.7	17.0	18.2

Balance Sheet							(INR b)	
Y/E March	2015	2016	2017	2018	2019	2020	2021E	2022E
Share Capital	6	11	11	11	22	21	21	21
Reserves	542	606	678	638	628	637	753	860
Net Worth	548	618	690	649	650	658	774	881
Capital Employed	550	622	693	658	661	719	839	946
Gross Block	164	175	258	261	311	414	461	544
Less : Depreciation	67	79	96	115	135	164	197	236
Net Block	129	153	161	146	176	251	263	309
Investments & Other Assets	63	84	135	153	143	131	162	162
Curr. Assets	472	517	537	500	529	546	632	727
Debtors	126	144	160	174	202	256	245	281
Cash & Bank Balance	312	328	326	262	262	233	326	375
Other Current Assets	34	46	51	64	65	57	61	71
Current Liab. & Prov	114	132	140	141	186	209	219	251
Net Current Assets	358	385	397	359	342	337	414	476
Application of Funds	550	622	693	658	661	719	839	946

Financials and valuations

Ratios

Y/E March	2015	2016	2017	2018	2019	2020	2021E	2022E
Basic (INR)								
EPS	27.0	29.5	31.5	35.7	37.1	38.9	45.7	54.1
Cash EPS	29.3	32.7	35.2	39.3	38.1	42.8	53.7	63.1
Book Value	119.8	135.1	150.9	142.0	142.2	144.7	182.5	207.8
DPS	11.1	12.1	12.9	21.8	21.5	17.5	20.8	24.6
Payout %	41.2	41.1	40.9	61.0	58.0	44.9	45.5	45.5
Valuation (x)								
P/E	41.7	38.1	35.7	31.5	30.3	28.9	24.6	20.8
Cash P/E	38.3	34.4	31.9	28.6	29.5	26.2	20.9	17.8
EV/EBITDA	34.5	30.1	27.6	27.0	24.6	23.0	17.1	14.6
EV/Sales	9.6	8.2	7.5	7.3	6.2	5.6	4.7	4.1
Price/Book Value	9.4	8.3	7.4	7.9	7.9	7.8	6.2	5.4
Dividend Yield (%)	1.0	1.1	1.1	1.9	1.9	1.6	1.9	2.2
Profitability Ratios (%)								
RoE	24.1	23.2	22.0	24.0	23.7	25.2	25.1	26.0
RoCE	19.2	19.2	18.5	20.1	21.2	20.4	21.4	22.6
Turnover Ratios								
Debtors (Days)	86	84	85	90	89	103	89	89
Fixed Asset Turnover (x)	4.1	4.1	4.2	4.8	4.7	3.6	3.8	3.7

Cash Flow Statement

(INR b)

Y/E March	2015	2016	2017	2018	2019	2020	2021E	2022E
CF from Operations	119	145	160	147	164	194	226	266
Cash for Working Capital	-11	-23	-19	-1	-6	-24	-17	-26
Net Operating CF	108	122	141	146	158	170	209	240
Net Purchase of FA	-22	-27	-28	-20	-24	-33	-37	-42
Free Cash Flow	85	95	113	126	134	137	173	198
Net Purchase of Invest.	10	-4	-145	51	9	31	9	9
Net Cash from Invest.	-13	-31	-173	31	-16	-2	-27	-33
Proceeds from Equity	0	0	0	0	0	0	0	0
Others	0	0	0	0	0	-6	0	0
Dividend Payments	-49	-68	-69	-205	-145	-95	-103	-122
Buyback of shares	0	0	0	0	0	-75	0	0
Cash Flow from Fin.	-49	-68	-69	-205	-145	-176	-103	-122
Net Cash Flow	45	23	-102	-28	-2	-8	79	85
Effect of forex on cash flow	-1	0	-1	0	0	-1	0	0
Opening Cash Bal.	260	304	327	226	198	196	186	265
Add: Net Cash	45	23	-102	-28	-2	-8	79	85
Closing Cash Bal.	305	327	225	198	196	186	265	351

Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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