

Margin beat; implied H2 growth disappoints

Information Technology ▶ Result Update ▶ **October 13, 2023**

TARGET PRICE (Rs): 1,680

Infosys reported mixed operating performance in Q2. Revenue grew 2.3% QoQ CC, ahead of our expectations; however, adjusting for higher pass-through and one-timers, it missed our estimates. Q2 revenue growth was impacted by spend reduction in some large clients, partially offset by ramp-ups of large deal wins in cost optimization and vendor consolidation. EBITM expanded 40bps QoQ to 21.2%, ahead of expectations, aided by the comprehensive margin expansion program launched last quarter. The company reported its highest-ever large deal TCV of USD7.7bn in Q2, where 48% of it was net new. Infosys has lowered its FY24 revenue growth guidance range to 1.0-2.5% CC YoY (earlier 1.0-3.5%), implying -1.9% to flat sequential growth in H2. Management attributed revenue guidance revision to weak discretionary spending, delay in decision making and slower ramp-up of large programs. Management has retained its EBITM guidance of 20-22% for FY24. We have cut FY24-26E EPS estimates by ~1%, factoring in Q2 performance and implied weak H2 outlook. We maintain BUY with a revised TP of Rs1,680 (earlier Rs1,700) at 23x Sep-25E EPS.

Infosys: Financial Snapshot (Consolidated)

Y/E March (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Revenue	12,16,410	14,67,670	15,46,496	17,11,440	19,04,467
EBITDA	3,14,920	3,51,310	3,68,184	4,16,572	4,66,350
Adj. PAT	2,21,110	2,40,950	2,45,557	2,84,839	3,20,996
Adj. EPS (Rs)	52.6	58.1	59.2	68.6	77.3
EBITDA margin (%)	25.9	23.9	23.8	24.3	24.5
EBITDA growth (%)	12.9	11.6	4.8	13.1	11.9
Adj. EPS growth (%)	15.8	10.5	1.9	16.0	12.7
RoE (%)	29.0	31.8	30.6	31.6	31.6
RoIC (%)	55.7	55.2	52.1	57.9	62.3
P/E (x)	27.9	25.2	24.8	21.4	18.9
EV/EBITDA (x)	18.4	16.4	15.5	13.4	11.8
P/B (x)	8.1	8.0	7.2	6.4	5.6
FCFF yield (%)	3.9	3.5	4.0	4.8	5.5

Source: Company, Emkay Research

Result Summary

Infosys' revenue grew 2.2% QoQ to USD4.72bn (2.3% QoQ/2.5% YoY in CC), above our estimate of USD4.6bn. Third-party items bought for service delivery expenses increased by 140bps QoQ, reflecting a jump in pass-through revenue, which supported revenue growth in addition to certain one-timers. EBITM expanded ~40bps QoQ to 21.2%, 20bps higher than our estimate of 21.0%. Margin expansion was aided by cost-optimization benefits comprising higher utilization and pricing (+50bps), revenue one-timers (+30bps) and rupee depreciation (+10bps), and it was offset by the increase in third-party costs along with salary-related and other costs (-50bps). Revenue growth in USD was led by Life Sciences (10.7% QoQ), Retail (7.1%), Manufacturing (3.6%), EURS (0.6%), while BFSI (flat), Communications (-0.4%), Hi-Tech (-1.6%) and Others (-0.8%) posted a weak performance. Among geographies, North America and Europe grew by 2.7% and 1.0% QoQ, respectively. Net headcount fell 2.2% QoQ. The company has announced an interim dividend of Rs18/share. **What we liked:** EBITM beat, strong deal intake and moderation in LTM attrition by 270bps QoQ to 14.6%. **What we did not like:** Weak implied growth in H2 and lower cash conversion (OCF/EBITDA at ~64%).

Earnings Call KTAs

i) Management suggested that weak discretionary spending, slower decision making and lower ramp-up of deals continue to weigh on revenue conversion. Strong large deal signings and pipeline position the company well for growth acceleration, once all macros stabilize. ii) Weakness persists in BFSI (mortgages, asset management, investment banking, and cards and payments), Communication, Hi-Tech, and parts of retail. Growth challenges in the communication sector continue, coupled with increasing OpEx pressures, risk of inflation, high interest rates, and supply-demand imbalances. EURS clients are taking a conservative approach to discretionary spending and the trend is likely to continue through the year. iii) Infosys signed 21 large deals in Q2, including 4 mega deals split across geographies (12 in America, 8 in Europe, and 1 in ROW) and verticals (6 in retail, 5 in manufacturing, 4 in Communications, 3 in Financial Services, 2 in Life Sciences, and 1 in EURS). iv) Large deals signed in Q2 are likely to contribute materially from the end of FY24 as deal ramp-ups will take some time. The deal pipeline remains healthy even after record deal closures, albeit a tad lower. v) The company has announced wage hikes w.e.f. November 1, 2023. vi) Utilization has improved to 81.8% from 81.1% QoQ, with more scope for improvement. vii) Infosys is currently working on over 90 Generative AI programs and has trained 57,000 employees on the same.

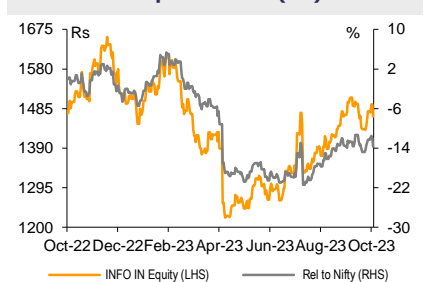
Target Price – 12M	Sep-24
Change in TP (%)	(1.2)
Current Reco.	BUY
Previous Reco.	BUY
Upside/(Downside) (%)	14.6
CMP (12-Oct-23) (Rs)	1,465.5

Stock Data	Ticker
52-week High (Rs)	1,673
52-week Low (Rs)	1,185
Shares outstanding (mn)	4,150.4
Market-cap (Rs bn)	6,082
Market-cap (USD mn)	73,066
Net-debt, FY24E (Rs mn)	-3,88,959
ADTV-3M (mn shares)	7
ADTV-3M (Rs mn)	9,866.8
ADTV-3M (USD mn)	118.5
Free float (%)	86.0
Nifty-50	19,794
INR/USD	83.2
Shareholding, Jun-23	
Promoters (%)	13.3
FPIs/MFs (%)	29.8/31.0

Price Performance

(%)	1M	3M	12M
Absolute	(2.4)	9.9	2.6
Rel. to Nifty	(1.4)	7.6	(11.3)

1-Year share price trend (Rs)



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Exhibit 1: Quarterly snapshot

(Rs mn)	Q2FY24	Q1FY24	QoQ chg.	Q2FY23	YoY chg.
Net sales (USD mn)	4,718	4,617	2.2%	4,555	3.6%
Net sales	3,89,940	3,79,330	2.8%	3,65,380	6.7%
Operating expenses	2,95,540	2,88,690		2,76,360	
EBITDA	94,400	90,640	4.1%	89,020	6.0%
Margins (%)	24.2	23.9	30	24.4	(20)
Depreciation	11660	11730		10290	
EBIT	82,740	78,910	4.9%	78,730	5.1%
Margins (%)	21.2	20.8	40	21.5	(30)
Interest received					
Other income (net)	4,940	4,710		5,180	
Pre-tax profit	87,680	83,620	4.9%	83,910	
Tax provided	25,530	24,170		23,650	
Profit after tax	62,150	59,450		60,260	
Emkay Net profit	62,120	59,450	4.5%	60,210	3.2%
EPS (Rs)	15.0	14.3	4.5%	14.3	4.6%

Source: Company, Emkay Research

Exhibit 2: Actuals vs. estimates

(Rs mn)	Actual	Estimate		Variation		Comment
		Emkay	Consensus	Emkay	Consensus	
Revenue (USD mn)	4,718	4,663	4,655	1.2%	1.4%	Revenue came ahead of our expectations partly due to higher pass-through revenue
Sales	3,89,940	3,85,178	3,84,220	1.2%	1.5%	
EBIT	82,740	80,704	81,070	2.5%	2.1%	
EBIT margin	21.2%	21.0%	21.1%	30 bps	10 bps	Margin beats estimates despite higher pass-through revenue
PAT	62,120	62,673	62,244	-0.9%	-0.2%	Net profit came a tad lower than estimates due to higher ETR

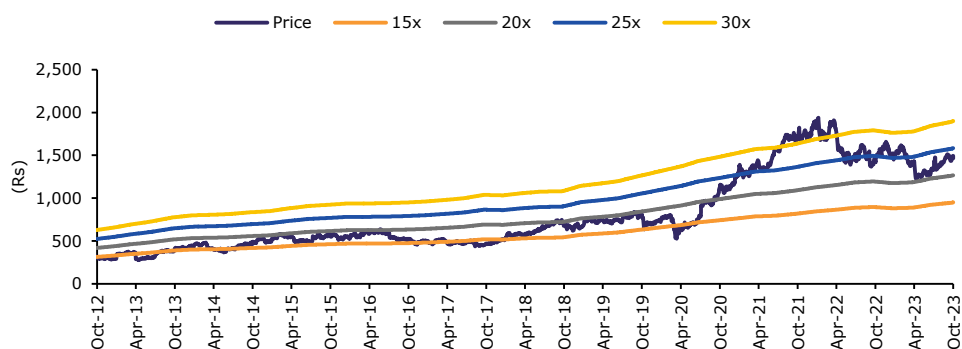
Source: Company, Bloomberg, Emkay Research

Exhibit 3: Changes in estimates

(Rs mn)	FY24E			FY25E			FY26E		
	Old	New	Change	Old	New	Change	Old	New	Change
Revenue (USD mn)	18,817	18,699	-0.6%	20,600	20,374	-1.1%	22,652	22,405	-1.1%
YoY growth	3.3%	2.7%		9.5%	9.0%		10.0%	10.0%	
Revenue	15,56,098	15,46,496	-0.6%	17,30,386	17,11,440	-1.1%	19,25,443	19,04,467	-1.1%
EBIT	3,22,791	3,21,292	-0.5%	3,67,913	3,65,220	-0.7%	4,14,060	4,09,307	-1.1%
EBIT margin	20.7	20.8		21.3	21.3		21.5	21.5	
Net profit	2,48,760	2,45,557	-1.3%	2,87,170	2,84,839	-0.8%	3,24,939	3,20,996	-1.2%
EPS (Rs)	59.9	59.2	-1.3%	69.2	68.6	-0.8%	78.3	77.3	-1.2%

Source: Company, Emkay Research

Exhibit 4: Infosys – One-year forward P/E



Source: Bloomberg, Emkay Research

Infosys: Consolidated Financials and Valuations

Profit and Loss					
Y/E March (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Revenue	12,16,410	14,67,670	15,46,496	17,11,440	19,04,467
Revenue growth (%)	21.1	20.7	5.4	10.7	11.3
EBITDA	3,14,920	3,51,310	3,68,184	4,16,572	4,66,350
EBITDA growth (%)	12.9	11.6	4.8	13.1	11.9
Depreciation & Amortization	34,770	42,250	46,892	51,352	57,043
EBIT	2,80,150	3,09,060	3,21,292	3,65,220	4,09,307
EBIT growth (%)	13.8	10.3	4.0	13.7	12.1
Other operating income	0	0	0	0	0
Other income	22,950	27,160	23,127	28,519	33,961
Financial expense	2,000	3,000	3,000	3,000	3,000
PBT	3,01,100	3,33,220	3,41,419	3,90,739	4,40,268
Extraordinary items	0	0	0	0	0
Taxes	79,640	92,140	95,632	1,05,499	1,18,872
Minority interest	(350)	(130)	(230)	(400)	(400)
Income from JV/Associates	0	0	0	0	0
Reported PAT	2,21,110	2,40,950	2,45,557	2,84,839	3,20,996
PAT growth (%)	14.3	9.0	1.9	16.0	12.7
Adjusted PAT	2,21,110	2,40,950	2,45,557	2,84,839	3,20,996
Diluted EPS (Rs)	52.6	58.1	59.2	68.6	77.3
Diluted EPS growth (%)	15.8	10.5	1.9	16.0	12.7
DPS (Rs)	31.0	34.0	38.0	42.5	47.5
Dividend payout (%)	59.0	58.5	64.2	61.9	61.4
EBITDA margin (%)	25.9	23.9	23.8	24.3	24.5
EBIT margin (%)	23.0	21.1	20.8	21.3	21.5
Effective tax rate (%)	26.4	27.7	28.0	27.0	27.0
NOPLAT (pre-IndAS)	2,06,051	2,23,601	2,31,298	2,66,610	2,98,794
Shares outstanding (mn)	4,205.6	4,148.6	4,150.2	4,150.2	4,150.2

Source: Company, Emkay Research

Cash Flows					
Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
PBT	3,01,100	3,33,220	3,41,419	3,90,739	4,40,268
Others (non-cash items)	36,490	49,840	46,662	50,952	56,643
Taxes paid	(76,120)	(87,940)	(95,632)	(1,05,499)	(1,18,872)
Change in NWC	(11,830)	(65,030)	(20,703)	(23,137)	(28,077)
Operating cash flow	2,49,640	2,30,220	2,71,746	3,13,054	3,49,962
Capital expenditure	(21,610)	(25,790)	(41,590)	(46,060)	(49,060)
Acquisition of business	(530)	(9,700)	0	0	0
Interest & dividend income	18,980	18,630	20,937	24,319	29,761
Investing cash flow	(74,950)	(17,640)	(41,590)	(46,060)	(49,060)
Equity raised/(repaid)	(1,09,960)	(1,18,110)	0	0	0
Debt raised/(repaid)	0	0	0	0	0
Payment of lease liabilities	(9,150)	(12,310)	0	0	0
Interest paid	0	0	0	0	0
Dividend paid (incl tax)	(1,27,310)	(1,36,530)	(1,57,707)	(1,76,383)	(1,97,134)
Others	(690)	1,380	0	0	0
Financing cash flow	(2,47,110)	(2,65,570)	(1,57,707)	(1,76,383)	(1,97,134)
Net chg in Cash	(72,420)	(52,990)	72,449	90,611	1,03,768
OCF	2,49,640	2,30,220	2,71,746	3,13,054	3,49,962
Adj. OCF (w/o NWC chg.)	2,61,470	2,95,250	2,92,449	3,36,191	3,78,039
FCFF	2,28,030	2,04,430	2,30,156	2,66,994	3,00,902
FCFE	2,45,010	2,20,060	2,48,092	2,88,313	3,27,664
OCF/EBITDA (%)	79.3	65.5	73.8	75.2	75.0
FCFE/PAT (%)	110.8	91.3	101.0	101.2	102.1
FCFF/NOPLAT (%)	110.7	91.4	99.5	100.1	100.7

Source: Company, Emkay Research

Balance Sheet					
Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Share capital	20,980	20,690	20,690	20,690	20,690
Reserves & Surplus	7,36,380	7,37,260	8,25,109	9,33,565	10,57,427
Net worth	7,57,360	7,57,950	8,45,799	9,54,255	10,78,117
Minority interests	0	0	0	0	0
Deferred tax liability (net)	(560)	(250)	(250)	(250)	(250)
Total debt	0	0	0	0	0
Total liabilities & equity	7,56,800	7,57,700	8,45,549	9,54,005	10,77,867
Net tangible fixed assets	1,30,750	1,33,460	1,23,918	1,17,339	1,12,205
Net intangible assets	17,070	17,490	14,017	10,562	5,942
Net ROU assets	48,230	68,820	76,002	80,744	82,516
Capital WIP	5,040	4,470	5,000	5,000	5,000
Goodwill	61,950	72,480	72,480	72,480	72,480
Investments [JV/Associates]	0	0	0	0	0
Cash & equivalents	3,77,960	3,16,510	3,88,959	4,79,569	5,83,337
Current assets (ex-cash)	5,25,730	6,32,480	6,69,147	7,29,143	8,00,183
Current Liab. & Prov.	4,09,930	4,88,010	5,03,974	5,40,832	5,83,796
NWC (ex-cash)	1,15,800	1,44,470	1,65,173	1,88,310	2,16,387
Total assets	7,56,800	7,57,700	8,45,549	9,54,005	10,77,867
Net debt	(3,77,960)	(3,16,510)	(3,88,959)	(4,79,569)	(5,83,337)
Capital employed	7,56,800	7,57,700	8,45,549	9,54,005	10,77,867
Invested capital	3,73,800	4,36,720	4,51,591	4,69,436	4,89,530
BVPS (Rs)	180.1	182.7	203.8	229.9	259.8
Net Debt/Equity (x)	(0.5)	(0.4)	(0.5)	(0.5)	(0.5)
Net Debt/EBITDA (x)	(1.2)	(0.9)	(1.1)	(1.2)	(1.3)
Interest coverage (x)	0.0	0.0	0.0	0.0	0.0
RoCE (%)	39.8	44.4	43.0	43.8	43.6

Source: Company, Emkay Research

Valuations and Key Ratios					
Y/E Mar	FY22	FY23	FY24E	FY25E	FY26E
P/E (x)	27.9	25.2	24.8	21.4	18.9
P/CE(x)	24.1	21.5	20.8	18.1	16.1
P/B (x)	8.1	8.0	7.2	6.4	5.6
EV/Sales (x)	4.8	3.9	3.7	3.3	2.9
EV/EBITDA (x)	18.4	16.4	15.5	13.4	11.8
EV/EBIT(x)	20.7	18.6	17.7	15.3	13.4
EV/IC (x)	15.5	13.2	12.6	11.9	11.2
FCFF yield (%)	3.9	3.5	4.0	4.8	5.5
FCFE yield (%)	4.0	3.6	4.1	4.7	5.4
Dividend yield (%)	2.1	2.3	2.6	2.9	3.2
DuPont-RoE split					
Net profit margin (%)	18.2	16.4	15.9	16.6	16.9
Total asset turnover (x)	1.6	1.9	1.9	1.9	1.9
Assets/Equity (x)	1.0	1.0	1.0	1.0	1.0
RoE (%)	29.0	31.8	30.6	31.6	31.6
DuPont-RoIC					
NOPLAT margin (%)	16.9	15.2	15.0	15.6	15.7
IC turnover (x)	3.3	3.6	3.5	3.7	4.0
RoIC (%)	55.7	55.2	52.1	57.9	62.3
Operating metrics					
Core NWC days	34.7	35.9	39.0	40.2	41.5
Total NWC days	34.7	35.9	39.0	40.2	41.5
Fixed asset turnover	2.7	3.0	2.9	3.0	3.0
Opex-to-revenue (%)	74.1	76.1	76.2	75.7	75.5

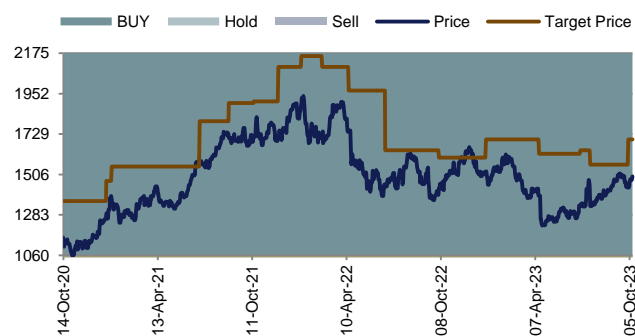
Source: Company, Emkay Research

RECOMMENDATION HISTORY - DETAILS

Date	CMP (INR)	TP (INR)	Rating	Analyst
02-Oct-23	1,435	1,700	Buy	Dipeshkumar Mehta
21-Jul-23	1,332	1,560	Buy	Dipeshkumar Mehta
02-Jul-23	1,336	1,640	Buy	Dipeshkumar Mehta
14-Apr-23	1,389	1,620	Buy	Dipeshkumar Mehta
01-Apr-23	1,428	1,700	Buy	Dipeshkumar Mehta
13-Jan-23	1,504	1,700	Buy	Dipeshkumar Mehta
02-Jan-23	1,524	1,700	Buy	Dipeshkumar Mehta
14-Oct-22	1,474	1,600	Buy	Dipeshkumar Mehta
04-Oct-22	1,429	1,600	Buy	Dipeshkumar Mehta
25-Jul-22	1,504	1,640	Buy	Dipeshkumar Mehta
23-Jun-22	1,452	1,640	Buy	Dipeshkumar Mehta
01-Jun-22	1,479	1,970	Buy	Dipeshkumar Mehta
14-Apr-22	1,749	1,970	Buy	Dipeshkumar Mehta
01-Apr-22	1,904	2,100	Buy	Dipeshkumar Mehta
22-Feb-22	1,734	2,100	Buy	Dipeshkumar Mehta
13-Jan-22	1,897	2,160	Buy	Dipeshkumar Mehta
01-Jan-22	1,888	2,100	Buy	Dipeshkumar Mehta
30-Nov-21	1,713	2,100	Buy	Dipeshkumar Mehta
14-Oct-21	1,716	1,910	Buy	Dipeshkumar Mehta
02-Oct-21	1,665	1,900	Buy	Dipeshkumar Mehta
27-Aug-21	1,709	1,900	Buy	Dipeshkumar Mehta
15-Jul-21	1,581	1,800	Buy	Dipeshkumar Mehta
02-Jul-21	1,568	1,800	Buy	Dipeshkumar Mehta
14-Apr-21	1,397	1,550	Buy	Dipeshkumar Mehta
05-Apr-21	1,410	1,550	Buy	Dipeshkumar Mehta
18-Mar-21	1,337	1,550	Buy	Dipeshkumar Mehta
14-Jan-21	1,371	1,550	Buy	Dipeshkumar Mehta
04-Jan-21	1,288	1,470	Buy	Dipeshkumar Mehta
18-Dec-20	1,190	1,360	Buy	Dipeshkumar Mehta
12-Nov-20	1,118	1,360	Buy	Dipeshkumar Mehta
14-Oct-20	1,137	1,360	Buy	Dipeshkumar Mehta

Source: Company, Emkay Research

RECOMMENDATION HISTORY - TREND



Source: Bloomberg, Company, Emkay Research

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