

Good set of numbers followed by improving profitability, revival in growth and major new deals, to boost investor confidence as corporate governance issues fade away

Current	Previous
CMP: Rs 773	Rating
Rating: Accumulate	Accumulate
Target: Rs 869	Target: Rs 911

(NR-Not Rated)

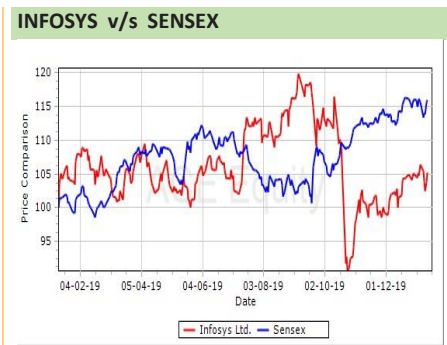
Stock Info	
INDEX	IT
BSE	500209
NSE	INFOSYSTCH
Bloomberg	INFO IN
Reuters	INFY.BO
Sector	Information Technology
Face Value (Rs)	5
Equity Capital (Rs Mn)	21210
Mkt Cap (Rs Mn)	3,143,938
52w H/L (Rs)	847 / 615
Avg Weekly Vol (BSE+NSE)	9,457,290

Shareholding Pattern	%
(As on Jan, 2020)	
Promoters	13.2
Public & Others	86.4

Source: NSE, Arihant Research

Stock Performance (%)	3m	6m	12m
INFOSYS	-5.7	3.0	8.6
SENSEX	9.8	7.9	15.2

Source: ACE Equity, Arihant Research



Source: ACE Equity, Arihant Research

Infosys reported good set of numbers in Q3FY20, mostly in line with our estimate. Consolidated revenue stood at Rs 230,920 mn, slightly above our estimate of Rs 227,369 mn, registering +7.9% YoY/+2.0% QoQ growth. Consolidated EBIT stood at Rs 50,640 mn, registering +4.8% YoY/+3.1% QoQ growth. EBIT margin expanded 22bps QoQ, though on YoY basis margin suffered a decline of 64bps. Consolidated PAT saw growth of 23.5% YoY to Rs 44,570 mn, higher than our estimate of Rs 42,063 mn on account of adoption of low corporate tax rates. The IT major's digital segment's revenue is seen growing continuously as each quarter passes by. We maintain our recommendation of ACCUMULATE rating on the stock with a revised target price of Rs 869.

Q3FY20 Highlights

- Revenue in constant currency (CC) terms during the quarter grew +9.5% YoY/+1.0% QoQ to \$ 3,243 mn. Digital revenues grew 40.8% YoY in CC terms to US\$ 1,318 mn. Digital revenue share as percentage of total revenue increased to 40.6% in Q3FY20 against 38.3% in Q2FY20 and 31.5% in Q3FY19.
- On a segmental basis, communication segment saw mild increase in growth of 20.6% YoY respectively in CC terms for the quarter, while life sciences, manufacturing and Hi-Tech segments witnessed growth of 17.7%, 12.2% & 11.8% YoY growth.
- Number of active clients increased to 1,384 in Q3FY20 against 1,364 in Q2FY20 and 1,251 in Q3FY19. Client concentration to revenue fell further with top client contribution down to 3.0% (3.4% in Q3 FY19) and top 10 clients contribution to 18.9% (19.2% YoY) in Q3FY20.

Valuations

Infosys management has raised its constant currency (CC) revenue guidance to 10-10.5% for FY20E, against 9-10% last quarter, which is mostly in line with our estimate. As the share of high margin digital business keeps getting better, Infosys maintained its operating margin guidance at 21-23% for FY20E. At CMP of Rs 773, Infosys is trading at a P/E of 21.2x and 18.9x its FY20E and FY21E earnings respectively.

Despite good Q3FY20 results, the company remains under the shadow of corporate governance allegations. Hence, we reduce the FY21E multiple at 20.0x FY21E earnings against 21.5x FY21E earlier to arrive at a price of Rs 869 per share, which gives 12.4% upside maintaining our rating at Accumulate.

Financial Performance

YE March (Rs Mn)	Net Sales	EBIT	Adj. PAT	Adj. EPS (Rs)	EBIT Margin %	RoE (%)	Adj. P/E (x)
FY18	705,220	171,480	161,470	35.8	24.3	24.9	22.8
FY19	826,750	188,800	161,250	37.0	22.8	24.8	22.0
FY20E	899,058	195,995	167,696	39.5	21.8	24.1	20.6
FY21E	988,963	217,572	184,231	43.4	22.0	24.5	18.8

Source: Companv. Arihant Research

Rs Mn (Consolidated)	Q3FY20	Q2FY20	Q3FY19	Q-o-Q	Y-o-Y
Net Revenue	2,30,920	2,26,290	2,14,000	2.0%	7.9%
Cost of Sales	1,53,730	1,50,790	1,40,160	1.9%	9.7%
Gross Profit	77,190	75,500	73,840	2.2%	4.5%
S&M and Admin. Expenses	26,550	26,380	25,540	0.6%	4.0%
EBIT	50,640	49,120	48,300	3.1%	4.8%
EBIT margin %	21.9%	21.7%	22.6%	22bps	-64bps
Other Income	8,270	6,260	7,530	32.1%	9.8%
Adjustments	-420	-420	-4,510	NA	NA
PBT	58,490	54,960	51,320	6.4%	14.0%
Tax Expense	13,830	14,590	15,220	-5.2%	-9.1%
Effective tax rate %	23.6%	26.5%	29.7%	-290bps	-601bps
Reported PAT	44,660	40,370	36,100	10.6%	23.7%
MI & Associates	-90	-180	-10	NA	NA
Consolidated PAT	44,570	40,190	36,090	10.9%	23.5%
Adjusted PAT	44,570	40,190	36,090	10.9%	23.5%
Adj PAT Margin %	19.3%	17.8%	16.9%	154bps	244bps
EPS (Rs)	10.5	9.5	8.3	11.1%	26.6%
Adj EPS (Rs)	10.5	9.4	8.3	11.2%	26.7%

Post Result Conference Call Highlights

- The company's North American business in financial services saw sequential growth with large deals signed worth USD 1.8 bn. The management remains skeptical on the business outlook front for the foreseeable future as business and trade headwinds across Europe and Americas continues to remain sluggish.
- The retail and financial services growth remained muted for the quarter in low single digits while the communications and life sciences segment grew by higher double-digits.
- Higher margin for digital business is driving the company's revenue mix shift towards data & analytics, SAAS, security and IoT with large deals signed to the tune of USD 1.8 bn during the quarter.
- The company also provided separate clarification on the probe regarding executive misconduct of the company stating that the audit committee did not find any evidence of financial impropriety or executive mismanagement.
- The management has checked the attrition rate of the company bringing it down to 19.6% from last quarter's 21.7%. This is beneficial in the long-run as the operational expenses along with the training costs needed to be contained.
- The management showed confidence for better outlook for their business on account of long term partnerships with several key clients, e.g. Telenet chose Infosys to provide service for next 5 years, to provide end-to-end IT infrastructure to Siemen's renewable subsidiary, etc.

Profit & Loss Statement (Consolidated)

Particulars (Rs Mn)	FY18	FY19	FY20E	FY21E
Income	7,05,220	8,26,750	8,99,058	9,88,963
Software development expenses	4,31,910	5,38,670	5,99,671	6,52,716
Gross Profit	2,73,310	2,88,080	2,99,386	3,36,248
Sales and development expenses	43,540	44,730	44,953	54,393
General and administrative expenses	58,290	54,550	40,458	44,503
Depreciation & Amortisation	18,620	20,635	17,981	19,779
EBIT	1,71,480	1,88,800	1,95,995	2,17,572
EBIT Margin (%)	24.3	22.8	21.8	22.0
Finance Cost (Lease expense)	0	0	1,600	1,600
Other Income	33,110	28,820	29,200	29,669
PBT	2,03,410	2,10,410	2,23,595	2,45,641
Tax	42,410	56,310	55,899	61,410
PAT	1,61,000	1,54,100	1,67,696	1,84,231
Adjusted PAT	1,61,470	1,61,250	1,67,696	1,84,231
Growth (%)	12.5%	-0.1%	4.0%	9.9%
Adjusted EPS	35.8	37.0	39.5	43.4

Source: Company, Arianth Research

Balance Sheet (Consolidated)

Particulars (Rs Mn)	FY18	FY19	FY20E	FY21E
Shareholder's Funds				
Share Capital	10,880	21,700	21,210	21,210
Reserves & Surplus	6,38,350	6,27,780	6,75,819	7,31,088
Net Worth	6,49,230	6,49,480	6,97,029	7,52,298
Minority Interest	10	580	580	580
Total Non Current Liabilities	8,610	-2,780	8,900	8,900
Total Current Liabilities	1,41,050	1,86,380	1,46,538	1,24,135
Total Liabilities	7,98,891	8,33,660	8,53,047	8,85,913
Net Block	1,25,740	1,57,100	1,88,567	2,23,181
Capital Work-in-Progress	16,060	13,880	13,880	13,880
Total Non Current Assets	2,98,730	3,04,880	3,31,546	3,66,169
Cash and bank balance	1,98,710	1,95,680	1,80,327	1,70,575
Total Current Assets	5,00,161	5,28,780	5,21,501	5,19,744
Total Assets	7,98,891	8,33,660	8,53,047	8,85,913

Source: Company, Arianth Research

Arihant Research DeskEmail: research@arihantcapital.com

Tel. : 022-42254800

Head Office

#1011, Solitaire Corporate Park ,
 Building No. 10, 1st Floor,
 Andheri Ghatkopar Link Road
 Chakala, Andheri (E).
 Mumbai – 400093
 Tel: (91-22) 42254800
 Fax: (91-22) 42254880

Registered Office

Arihant House
 E-5 RatlamKothi
 Indore - 452003, (M.P.)
 Tel: (91-731) 3016100
 Fax: (91-731) 3016199

Stock Rating Scale**Absolute Return**

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

Research**Analyst****Contact****Website****Email Id****Registration No.**

INH000002764

SMS: 'Arihant' to 56677

www.arihantcapital.comresearch@arihantcapital.com

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Arihant Capital Markets Ltd.

1011, Solitaire Corporate park, Building No. 10, 1st Floor,
 Andheri Ghatkopar Link Road Chakala, Andheri (E)
 Tel. 022-42254800 Fax. 022-42254880