



## Infosys Technologies

Evergreen

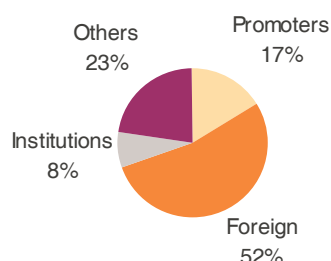
Price target revised to Rs1,655

Buy; CMP: Rs1,227

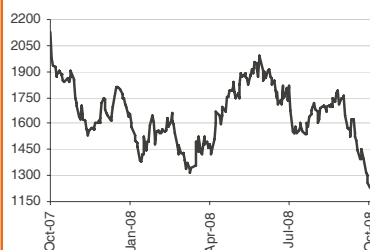
### Company details

Price target:	Rs1,655
Market cap:	Rs70,167 cr
52 week high/low:	Rs2140/1040
NSE volume: (No of shares)	19.5 lakh
BSE code:	500209
NSE code:	INFOSYSTCH
Sharekhan code:	INFOSYS
Free float: (No of shares)	47.8 cr

### Shareholding pattern



### Price chart



### Price performance

(%)	1m	3m	6m	12m
Absolute	-28.3	-27.8	-13.3	-36.3
Relative to Sensex	-5.5	-15.4	18.1	-2.9

### Result highlights

- The consolidated top line of Infosys Technologies (Infosys) grew by 11.6% quarter on quarter (qoq) and by 32% year on year (yoy) to Rs5,418 crore in Q2FY2009, boosted by the rupee's depreciation (a 6% contribution sequentially). In dollar terms, the revenues grew by 5.3% qoq driven by a 6.5% volume growth. The volume growth was partially offset by a drop in the billing rates (0.3% down sequentially) and cross-currency head wind. The billing rates declined due to a higher proportion of offshore revenues during the quarter.
- The operating profit margin (OPM) improved by 264 basis points to 33.1% in Q2FY2009 on account of the gains from wage hikes and visa charges (gains of 160 basis points and 80 basis point respectively, as these charges had been accounted for in Q1FY2009), and a favourable currency impact (250 basis points). This was partially offset by higher sales, general and administrative (SG&A) expenses (70 basis points). The gains from the wage hikes and visa charges were also partially reinvested in the business. Consequently, the operating profit increased by 21.3% qoq to Rs1,794 crore during the quarter.
- Infosys' adjusted net profit grew by 12.7% qoq to Rs1,432 crore in Q2FY2009. That is marginally above our expectation of Rs1,393 crore. The sequential growth in the net income was lower than that in the operating profit due to a higher

### Results table

Particulars	Q2FY09	Q2FY08	Q1FY09	% yoy	% qoq
<b>Total revenue</b>	<b>5418</b>	<b>4106</b>	<b>4854</b>	<b>32.0</b>	<b>11.6</b>
Software development expenses	2,891	2,231	2,754	29.6	5.0
<b>Gross profit</b>	<b>2527</b>	<b>1875</b>	<b>2100</b>	<b>34.8</b>	<b>20.3</b>
Selling and marketing expenses	303	283	257	7.1	17.9
General and administration expenses	430	308	364	39.6	18.1
Total expenditure	3624	2822	3375	28.4	7.4
<b>Operating profit</b>	<b>1794</b>	<b>1284</b>	<b>1479</b>	<b>39.7</b>	<b>21.3</b>
Non-operating income	66	154	117	-57.1	-43.6
Profit before depreciation and tax	1860	1438	1596	29.3	16.5
Depreciation/Amortisation	177	144	169	22.9	4.7
<b>Profit before tax</b>	<b>1683</b>	<b>1294</b>	<b>1427</b>	<b>30.1</b>	<b>17.9</b>
Provision for taxation	251	194	125	29.4	100.8
Profit after current tax	1432	1100	1302	30.2	10.0
RPAT	1432	1100	1302	30.2	10.0
<b>Adjusted PAT</b>	<b>1432</b>	<b>1100</b>	<b>1271</b>	<b>30.2</b>	<b>12.7</b>
Equity share capital (par value Rs5 each)	286	286	286		
Basic EPS (in Rs)	25.0	19.2	22.2		
GPM (%)	46.6	45.7	43.3		
OPM (%)	33.1	31.3	30.5		
PBT margin (%)	31.1	31.5	29.4		
NPM (%)	26.4	26.8	26.2		
Tax/PBT	14.9	15.0	8.8		

foreign exchange (forex) loss (Rs126 crore in Q2FY2009 vs Rs80 crore in Q1FY2009).

- ♦ Infosys has guided that its FY2009 revenues in dollar terms would grow by just 13-15% compared with the earlier guidance of a 19-21% revenue growth announced in Q1FY2009. The earnings growth guidance has also been downgraded to just 10.3% in dollar terms from 14.3-16.3% announced previously. The guidance has been downgraded because of cross-currency head wind and further weakening of the demand environment.
- ♦ Infosys has also maintained conservatism in its earnings guidance in rupee terms. Though the rupee depreciated by 6% during the quarter, the company has kept its earnings guidance in rupee terms at Rs101.1 per share.
- ♦ Infosys has also announced that it will not revise its bid upward for Axon Group and that is a positive for the company in view of the weakening demand environment.
- ♦ We have downgraded the revenue growth estimate in dollar terms to reflect the weakening business environment and cross-currency head wind. However, this has been offset by an upward revision in our exchange rate assumption. We have assumed an exchange rate of Rs45 each for FY2009 and for FY2010. Hence, we have marginally downgraded the earnings growth estimate by 0.2% and 1.3% for FY2009 and FY2010 respectively.
- ♦ At the current market price, the stock is trading at attractive valuations of 12.1x FY2009 earnings estimate and 11x FY2010 earnings estimate. We reiterate our Buy recommendation on the stock with a price target of Rs1,655 and time horizon of 12 months.

#### **Revenue guidance in dollar terms downgraded sharply**

Infosys' revenues in dollar terms are guided to grow by just 13-15% (USD4.71- 4.81 billion) in FY2009. The revenue guidance in dollar terms is down by 6% from the previously announced guidance of a 19-21% growth (USD4.97-5.05 billion). Out of the 6% decline, a 3% drop has been caused by cross-currency head wind and the remaining 3% decrease has been a result of the further weakening of the business environment.

The cross-currency head wind stemmed from the sharp appreciation in the US Dollar against the Australian Dollar, the euro and the Pound Sterling during the quarter. The revenue guidance for FY2009 in dollar terms implies a revenue growth of 5.1-9.6% in the second half of FY2008. This guidance also implies a flat revenue growth for the third and fourth quarters of FY2009. Hence, we believe

Infosys has been conservative in its guidance to reflect the challenging business environment and the company may actually exceed the guidance at the end of FY2009. However, we remain worried about the revenue growth in FY2010 given the significant delay in the decision-making process and ramp-up of the clients. In terms of earnings guidance for FY2009 in dollar terms, the earnings are expected to grow by just 10.3% in FY2009, down from the earlier guidance of a 14.3-16.3% growth.

In rupee terms, Infosys has guided that its revenues would grow at 27.7-30.2% (Rs21,309-21,731 crore) in FY2009, at a rate marginally higher than guided previously. The earnings guidance in rupee terms has been kept unchanged at Rs101.1 per share. The guidance has factored in an exchange rate of Rs46.97.

#### **No upward revision in Axon's bid**

Infosys has mentioned that it will not revise its bid upward for Axon Group and that is a positive for the company in view of the weakening demand environment. However, the management has mentioned that it may look for another acquisition that is of strategic fit. The company currently has cash & cash equivalent of USD1.9 billion.

#### **Hiring and client addition remained healthy**

Infosys was on schedule in terms of hiring. The company added over 10,000 employees during the quarter in line with its target. It is expected to hire 4,500 employees for the next quarter. The company has also maintained its hiring target of 25,000 employees for FY2009. In terms of client addition, the company added 40 clients during the quarter. Most of the clients were in the banking, financial services and insurance (BFSI) vertical. The deal flow also remained healthy during the quarter. The company currently has 12 deals in the pipeline. It won five transformational deals and five outsourcing deals during the second quarter. The average size of the transformational deals is more than USD30 million with three for Finacle product. As for the outsourcing deals, two deals are worth more than \$100 million, two are worth close to \$100 million and the remaining one is worth close to USD50 million.

#### **Subsidiaries' bottom line improved on sequential basis**

The subsidiaries have cumulatively reported a sequential decline of 2% in the top line to Rs128.8 crore for the quarter. The profit after tax (PAT) margin of Infosys BPO and Infosys Consulting improved significantly during the quarter. Infosys BPO's PAT margin improved to 15% in Q2FY2009 from 10% in Q1FY2009. On the other hand, Infosys Consulting's losses reduced to Rs1.1 crore from Rs2 crore in Q1FY2009. This led to a 16% sequential increase in the subsidiaries' profit to Rs9.3 crore.

## Performance of subsidiaries (\$ million)

Particulars	Q2FY09	Q2FY08	Q1FY09	% yoy	% qoq
<b>Revenues</b>					
Infosys BPO	72.6	53.0	73.0	36.9	-0.6
Infosys Australia	30.8	34.0	34.0	-9.3	-9.3
Infosys Consulting	17.7	16.0	18.0	10.4	-1.8
Infosys China	5.8	5.0	6.0	15.8	-3.5
Infosys Mexico	2.0	0.0	1.0	-	96.0
Total revenues	128.8	108.0	132.0	19.3	-2.4
<b>PAT</b>					
Infosys BPO	11.0	8.1	7.0	35.6	56.9
Infosys Australia	2.1	5.7	3.0	-63.5	-30.7
Infosys Consulting	-1.1	-0.8	-2	36.3	-
Infosys China	-1.9	-1.1	0	68.2	-
infosys mexico	-0.8	0.0	0	-	-
Total PAT	9.3	11.9	8.0	-22.0	16.0
<b>PAT margins (%)</b>					
Infosys BPO	15.1	15.3	9.6		
Infosys Australia	6.7	16.8	8.8		
Infosys Consulting	-6.2	-5.0	-11.1		
Infosys China	-32.0	-22.0	0		
infosys mexico	-42.9	0	0		
Total PAT margin	7.2	11.0	6.1		

## Other highlights

- Infosys has reported a healthy sequential growth of 8.3% in the European region for the quarter. However, the business environment has further deteriorated in Europe in the last two to four weeks.
- The management has also highlighted that it will continue to invest in the European region in order to achieve its aspiration for a revenue mix of 40% from North America, 40% from Europe and 20% from the rest of the world.
- The manufacturing vertical has also reported a healthy sequential growth of 14.8% for the quarter.
- For the BFSI vertical, the company has reported a 1.7% sequential growth. The recent consolidation in the BFSI vertical had a limited impact on Infosys as the company is an entrenched vendor at both ends.

- The attrition rate stood at 12.8% in Q2FY2009 compared with 13.6% in Q1FY2009.
- The hedge position at the end of the quarter stood at \$932 million compared with \$811 million at the end of Q1FY2009.
- The days sales outstanding (DSO) for the quarter stood at 60 days compared with 64 days at the end of Q1FY2009.

## Valuation

For Infosys, we have downgraded the revenue growth estimate in dollar terms to reflect the weakening business environment and cross-currency head wind. However, this has been offset by an upward revision in our exchange rate assumption. We have assumed an exchange rate of Rs45 each for FY2009 and for FY2010. Hence, we have marginally downgraded the earnings growth estimate by 0.2% and 1.3% for FY2009 and FY2010 respectively. At the current market price, the stock is trading at attractive valuations of 12.1x FY2009 earnings estimate and 11x FY2010 earnings estimate. We reiterate our Buy recommendation on the stock with a price target of Rs1,655 and time horizon of 12 months.

## Key financials

Particulars	FY06	FY07	FY08E	FY09E	FY10E
Net revenue (Rs cr)	9521	13893	16692	21643	24155
Net profit (Rs cr)	2458	3726	4659	5781	6311
No of shares (cr)	55.1	55.7	57.2	57.2	57.2
Adjusted EPS (Rs)	44.6	65.1	79.3	101.1	110.3
% yoy chg	30.4	46.0	21.8	27.4	9.2
PER	27.5	18.8	15.5	12.1	11.1
EV/EBIDTA	9.8	14.6	11.8	8.4	7.5
EV/Sales	3.2	4.6	3.7	2.7	2.4
RoCE (%)	39.7	37.7	38.7	37.7	33.9
RoNW (%)	35.3	34.3	33.8	32.4	28.5

The author doesn't hold any investment in any of the companies mentioned in the article.

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