



Infosys Technologies

STOCK INFO. BLOOMBERG
BSE Sensex: 9,071 INFO IN
REUTERS CODE
S&P CNX: 2,745 INFY.BO

13 January 2009

Buy

Previous Recommendation: Buy

Rs1,230

		YEAR	NET SALES	PAT*	EPS	EPS	P/E	P/BV	ROE	ROCE	EV/	EV/
		END	(RS M)	(RS M)	(RS)	GR. (%)	(X)	(X)	(%)	(%)	SALES	EBITDA
Equity Shares (m)	572.5	3/07A	138,930	37,250	66.1	48.1	18.6	6.2	40.9	40.8	4.6	14.4
52-Week Range	2,017/1,040	3/08A	166,920	45,580	79.5	20.3	15.5	5.1	36.4	36.4	3.8	12.1
1,6,12 Rel. Perf. (%)	17/6/37	3/09E	216,684	57,970	101.1	27.1	12.2	4.1	37.2	37.2	2.9	8.7
M.Cap. (Rs b)	704.2	3/10E	222,651	58,979	102.7	1.6	12.0	3.3	30.5	30.5	2.7	8.5
M.Cap. (US\$ b)	14.4											

* 1:1 bonus in FY07, accordingly ratios are adjusted, PAT figures are adjusted PAT

- **US\$ revenue below expectations; EBITDA margin up 200bp:** Infosys reported dollar revenue degrowth of 3.7% QoQ to US\$1,171m. Dollar revenue in constant currency at US\$1,228m was above the upper end of guidance of US\$1,220m. EBITDA margin at 35.1% (up 200bp QoQ) was boosted by rupee depreciation and SGA leverage, while cross currency volatility and reduced utilization cast a negative pressure. Adjusted PAT grew 10.2% QoQ to Rs15.8b. Blended IT services volumes grew 2% QoQ and realization was down 1.8% QoQ (in constant currency).
- **FY09 US\$ revenue growth guidance revised to 12-13%:** Infosys has guided for FY09 dollar revenue at US\$4.67-4.71b (YoY growth of 11.8-12.8%) v/s earlier guidance of US\$4.72-4.81, implying a downgrade of 1-2%. In rupee terms, the revised guidance for FY09 is Rs215.5-217.6b, suggesting a 29-30% growth.
- **Sees competition cut billing rates:** Infosys sees some of its competitors (both MNC and Indian vendors) cut billing rates. It is dealing with pricing pressure by adopting a 'portfolio approach' - linking pricing and volumes. We read this as a willingness by the management to accept price cuts in contracts with higher assured volumes. Pricing in reported currency was down by 6.1% QoQ on a blended basis, while it was down 1.8% in constant currency.
- **Cutting FY10 EPS estimate to factor in rising pricing concerns:** We expect pricing to come under further pressure in the next few quarters. We revise our FY10 US\$ revenue growth estimates to 3.8% (v/s 4.4%) to factor in rising pricing concerns. We are cutting our FY10 EPS estimate to Rs102.7 v/s Rs105.4 earlier. Infosys trades at 12x FY10E EPS. We maintain our DCF-based target price of Rs1,347 (13x FY10E EPS). Maintain **Buy**.

QUARTERLY PERFORMANCE (Indian GAAP)

Y/E MARCH	(Rs Million)									
	FY08				FY09				FY08	FY09E
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4QE		
Revenues	37,730	41,060	42,710	45,420	48,540	54,180	57,860	56,104	166,920	216,684
Q-o-Q Change (%)	0.0	8.8	4.0	6.3	6.9	11.6	6.8	-3.0	20.1	29.8
Direct Expenses	21,690	22,310	23,250	24,820	27,540	28,910	30,750	31,317	92,070	118,517
SG&A	5,200	5,910	5,540	5,820	6,210	7,330	6,800	6,833	22,470	27,173
Operating Profit	10,840	12,840	13,920	14,780	14,790	17,940	20,310	17,955	52,380	70,995
Margins (%)	28.7	31.3	32.6	32.5	30.5	33.1	35.1	32.0	31.4	32.8
Other Income	2,530	1,540	1,580	1,390	1,170	660	380	2,160	7,040	4,370
Depreciation	1,440	1,440	1,530	1,570	1,690	1,770	1,870	2,132	5,980	7,462
PBT bef. Extra-ordinary	11,930	12,940	13,970	14,600	14,270	16,830	18,820	17,983	53,440	67,903
Provision for Tax	1,650	1,940	2,160	2,110	1,560	2,510	3,030	2,832	7,860	9,932
Rate (%)	13.8	15.0	15.5	14.5	10.9	14.9	16.1	15.8	14.7	14.6
PAT before EO	10,280	11,000	11,810	12,490	12,710	14,320	15,790	15,150	45,580	57,970
Q-o-Q Change (%)	0.9	7.0	7.4	5.8	1.8	12.7	10.3	-4.1	22.4	27.2
Extra-ordinary Items	510	0	500	0	310	0	620	0	1,010	930
PAT aft. Minority and EO	10,790	11,000	12,310	12,490	13,020	14,320	16,410	15,150	46,590	58,900
Q-o-Q Change (%)	-5.7	1.9	11.9	1.5	4.2	10.0	14.6	-7.7	20.8	26.4

E: MOSL Estimates

Infosys 3QFY09: US\$ revenue below expectations; EBITDA margin up 200bp

Infosys reported dollar revenue degrowth of 3.7% QoQ to US\$1,171m, marginally below our expectations of US\$1,177m. Dollar revenue in constant currency at US\$1,228m was above the upper end of guidance of US\$1,220m. Revenue in rupee terms was Rs57.9b, up 6.8% QoQ. EBITDA margin at 35.1% (up 200bp QoQ) was above our estimate of 33.1%. Rupee depreciation boosted margin by 470bp, while cross currency volatility and reduced utilization cast a negative pressure on margin by 100bp and 130bp respectively. S&M and G&A were down QoQ by 10% and 6% respectively. As a percentage of sales, SGA was down 180bp QoQ to 11.8%. The negative impact of pricing decline was offset by SGA leverage. Adjusted PAT (Rs620m tax reversal) grew 10.2% QoQ to Rs15.8b. Forex loss was reported at Rs2.2b v/s Rs1.3b in 2QFY09. Blended IT services volumes grew 2% QoQ, with onsite volumes declining 1% and offshore growing 3.3% QoQ. Blended realization was down 1.8% QoQ (in constant currency). Onsite realization in constant currency degrew 1.5%, while offshore degrew 0.2%.

FY09 US\$ revenue growth guidance revised to 12-13%; rupee EPS guidance maintained

Infosys has guided for FY09 dollar revenue at US\$4.67-4.71b (YoY growth of 11.8-12.8%) v/s earlier guidance of US\$4.72-4.81, implying a downgrade of 1-2%. EPS (adjusted for tax reversal) is revised downward by 1% to US\$2.2, implying YoY growth of 11.1%. In rupee terms, the revised guidance for FY09 is Rs215.5-217.6b suggesting a 29-30% growth. FY09 EPS guidance (adjusted for tax reversal) has been maintained at Rs101.3 (YoY growth of 27.6%) v/s earlier guidance of Rs100.5. New rupee guidance is at Re/US\$ of 48.71 v/s 46.97 earlier.

Management expects IT budgets for CY09 to be finalized around mid-February as against April for CY08. This could mean improved visibility in the near term, although the budgets are not expected to be sacrosanct and may be revisited if situation worsens.

GUIDANCE SUMMARY

	4Q	QOQ	FY09	YOY	FY09	YOY
	FY09	CHG. %	NEW	CHG. %	OLD	CHG. %
US\$ m Revenue Guidance						
Lower End	1,128	-3.7	4,670	11.8	4,720	13.1
Upper End	1,170	-0.1	4,710	12.8	4,810	15.2
INR M Revenue Guidance						
Lower End	54,940	-5.0	215,520	29.1	213,090	27.7
Upper End	56,990	-1.5	217,570	30.3	217,310	30.2
INR EPS Guidance	26.5	-4.0	101.3	27.6	100.5	26.6

EPS on adjusted basis

Source: Company, MOSL

Sees competition cut billing rates

Infosys sees some of its competitors (both MNC and Indian vendors) cut billing rates. The company is dealing with pricing pressure by adopting a 'portfolio approach' - linking pricing and volumes. We read this as a willingness by the management to accept price cuts in

contracts with higher assured volumes. Pricing in reported currency was down by 6.1% QoQ on a blended basis, while it was down 1.8% in constant currency. 4QFY09 guidance assumes flat pricing although the management expects worsening pricing scenario should macro environment deteriorate.

Hiring 27,000 employees vs 25,000 due to higher offer acceptance

Infosys has increased its FY09 hiring guidance by 2,000 to 27,000 employees. This is on account of (1) higher percentage of acceptance from campus offers than the past precedents and (2) employees in BPO joining in March. The increased hiring comes despite reduced attrition at 11.8% v/s 12.8% earlier. The company added 5,997 employees in 3QFY09 on a gross basis and 2,772 employees on a net basis. Management has confirmed that the company will honor its commitment of 20,000 campus offers for FY10 despite higher than expected joiners in FY09 and lower attrition.

Other result highlights

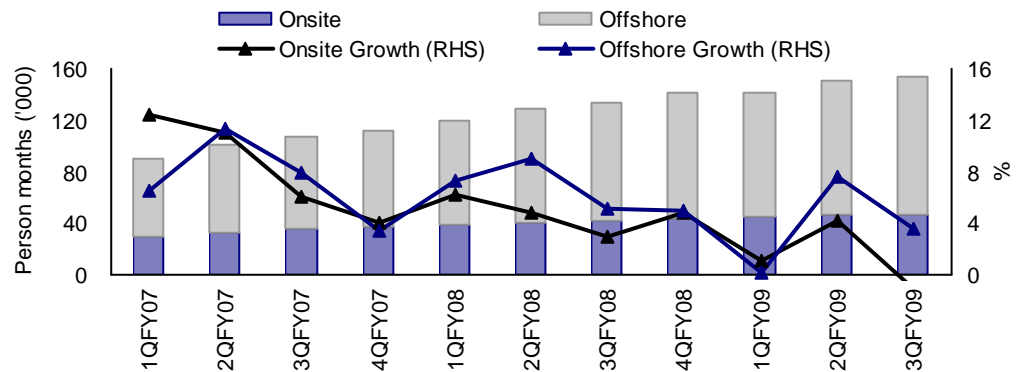
- ✂ Utilization including trainees at 68.5% was down 90bp QoQ, while utilization excluding trainees was up 80bp at 74.5%.
- ✂ Contribution from fixed price projects grew 220bp QoQ to 36.3% of revenue. This has been an industry-wide trend in the recent past, indicative of increasing bargaining power of the customer.
- ✂ Hedging position was at US\$576m v/s US\$932 at end of 2QFY09. We are surprised by Infosys' decision to lower hedge at the current Re/\$ rate of ~49. We are modelling a Re/US\$ rate of 45.6 for FY10.
- ✂ 3QFY09 North American revenue grew 1.1% QoQ and 1.5% in constant currency terms.
- ✂ Europe revenue declined 12.5% QoQ and 1.2% in constant currency terms, contributing 25.5% to revenue (v/s 28.1% in 2QFY09).
- ✂ 3QFY09 revenue from rest of the world declined 6.4% QoQ but grew 5.8% in constant currency terms.
- ✂ BFSI contributed 34.9% of revenue in 3QFY09 (v/s 33.4% in 2QFY09) and showed stronger growth of 1.0% QoQ; 4.1% in constant currency terms.
- ✂ Manufacturing contributed 19.6% of revenue in 3QFY09 (v/s 20.1% in 2QFY09) and declined 6.0% QoQ and 3.7% in constant currency terms due to sluggish demand in automobile, hi-tech, semi conductor verticals.
- ✂ Retail contributed 12.6% of revenue (v/s 12.1% in 2QFY09) and grew 0.3% QoQ (2.9% in constant currency terms).
- ✂ Telecom declined by 15.3% QoQ and 3.4% in constant currency.
- ✂ Top client (BT) degrew 21.5% during the quarter, predominantly due to 17% depreciation in GBP.
- ✂ Other verticals, which include Services, Transportation and Energy, grew 0.6% QoQ and 4.3% in constant currency terms.
- ✂ Revenue share of Financial Products group (Finnacle etc) was higher at 7.2% v/s 3.6% in 2QFY09, primarily from orders won in APAC and EMEA regions.

✍ Infrastructure management showed good traction with growth of 6.1% QoQ and contributed 6.5% to revenue v/s 5.9% in 2QFY09.

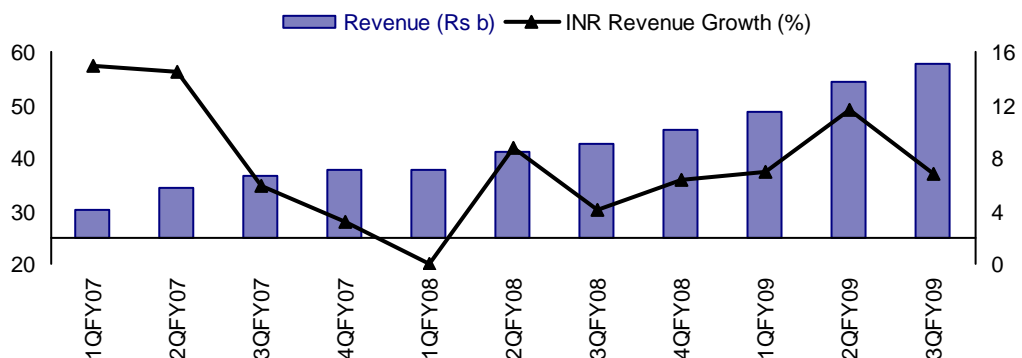
Valuation and view

This is the first time in the last three years when the management has stated pricing pressures are increasing, also reflected in the ~2% decline in constant currency realization. We note that in the last quarter, Infosys did not see major price re-negotiations, save a few ‘sporadic instances’. We expect pricing to come under further pressure in the next few quarters due to increased competition and deteriorating demand outlook before stabilizing in 2HFY10. We expect Infosys to largely maintain its EBITDA margins in the long run through its superior cost efficiencies, while some smaller players could be impacted significantly due to price war among the Tier I vendors, including MNC’s. We revise our FY10 US\$ revenue growth estimates marginally to 3.8% (v/s 4.4% earlier) to factor in rising pricing concerns. While we are maintaining our FY09 EPS at Rs101.1 (adjusted for tax reversal), we are cutting our FY10 EPS estimate to Rs102.7 v/s Rs105.4 earlier (based on an unchanged rupee rate assumption of Rs45.6/US\$). At our revised EPS, Infosys trades at 12x FY10E EPS. We maintain our DCF-based target price of Rs1,347 implying a P/E multiple of 13x FY10E EPS. Maintain **Buy**.

INCREASED OFFSHORING FOR COST REDUCTION

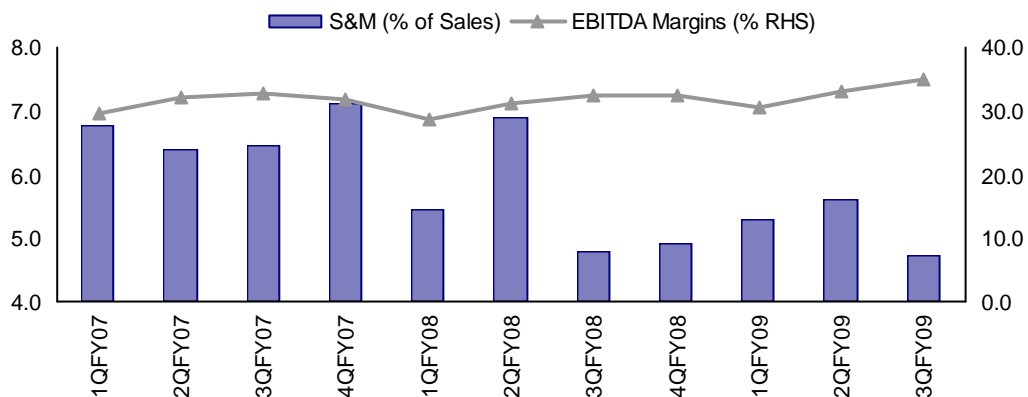


INR REVENUES BOOSTED BY RUPEE DEPRECIATION

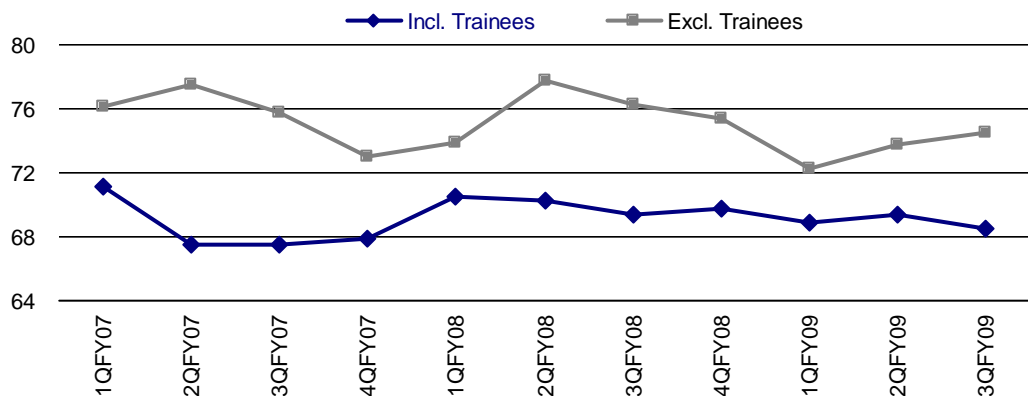


Source: Company/MOSL

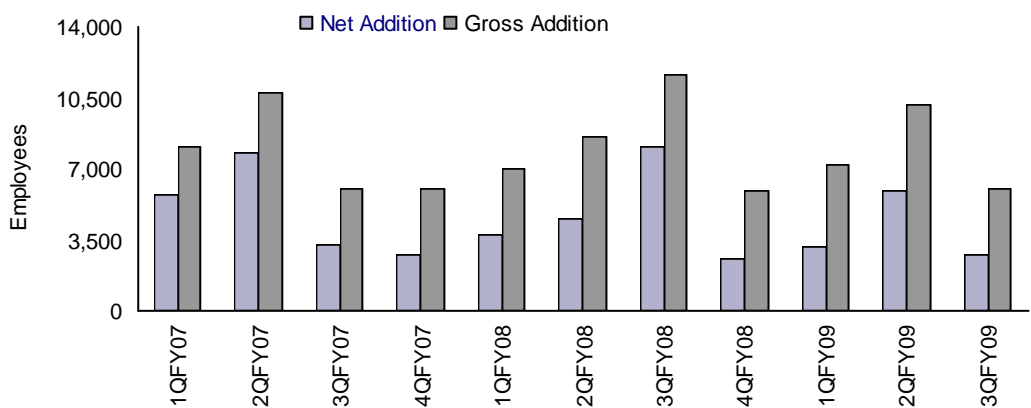
SGA LEVERAGE USED TO COUNTER MARGIN PRESSURE FROM PRICING DECLINE



UTILIZATION INCL. TRAINEES UNDER PRESSURE DUE TO LARGE HIRING (%)



HIGH GROSS ADDITION ON REVISED HIRING TARGET



Source: Company/MOSL

Infosys Technologies: an investment profile

Company description

Infosys is the second largest IT Services Company in India with revenue of around US\$4.7b and employing over 103,000 people. Infosys designs and delivers IT-enabled business solutions that help Global 2000 companies to win in a flat world. Infosys has 583 clients and global footprint in 23 countries and development centers in India, China, Australia, the UK, Canada and Japan. Its service offerings span business and technology consulting, ADM, SI, product engineering, IT infrastructure services and BPO.

Key investment arguments

- Most profitable among frontline Indian IT companies.
- Wide services offering profile and deep domain depth.

Key investment risks

- Uncertainties in the US financial markets and US economy slowing down in CY09, which could impact the IT spends of company's clients. US contributes around 64.5% of revenue.
- Across the board pricing pressure.

Recent developments

- AstraZeneca awarded Infosys Technologies Multi-Year, Multi-Million Dollar Global Services Deal.
- Infosys' solution won the Hitachi Data Systems Diamond Award for 'Best Virtualization Strategy'.

Valuation and view

- CAGR of 15% and 14% in revenue and profit respectively over FY08-FY10E.
- Valuations at 12.2x FY09E and 12x FY10E earnings.
- We maintain **Buy** with a price target of Rs1,347.

Sector view

- Global clients and service providers have made India as their base for IT-enabled solutions. India has ~5% share of global IT market. We are positive on the sector from a long term perspective.
- US economy slow down, lower BFSI IT spends, pricing pressures, sharper currency appreciation remain key concerns.
- We believe frontline Indian IT companies would be better placed to sail through the near term adversities mentioned above. Niche IT/ITeS services companies with strong business model are also likely to be better placed to face uncertainties in near term.

COMPARATIVE VALUATIONS

		INFOSYS	TCS	WIPRO
P/E (x)	FY09E	12.2	9.3	9.8
	FY10E	12.0	9.2	9.8
P/BV (x)	FY09E	4.1	3.2	2.2
	FY10E	3.3	2.6	1.9
EV/Sales (x)	FY09E	2.9	1.6	1.1
	FY10E	2.7	1.3	1.0
EV/EBITDA (x)	FY09E	8.7	6.3	5.4
	FY10E	8.5	5.5	5.1

SHAREHOLDING PATTERN (%)

	SEP-08	JUN-08	SEP-07
Promoter	16.5	16.5	16.5
Domestic Inst	8.4	7.9	6.5
Foreign	52.3	53.3	55.0
Others	22.8	22.3	22.0

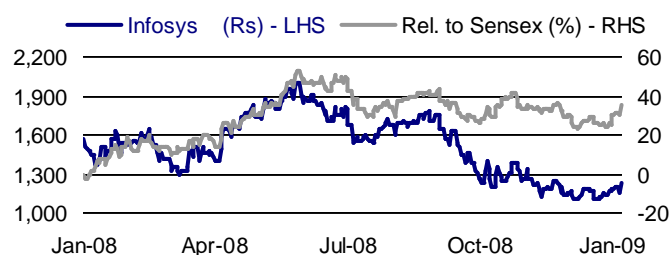
EPS: MOST FORECAST VS CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY09	101.1	101.6	-0.5
FY10	102.7	111.1	-7.5

TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
1,230	1,347	9.5	Buy

STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT		(RS MILLION)				
Y/E MARCH	2006	2007	2008	2009E	2010E	
Sales	95,216	138,930	166,920	216,684	222,651	
Change (%)	33.5	45.9	20.1	29.8	2.8	
Software Develop. Exp.	50,654	74,580	92,070	118,517	126,578	
Selling and Mktg. Exp.	6,005	9,290	9,160	11,137	11,126	
Administration Exp.	7,639	11,150	13,310	16,036	15,403	
EBITDA	30,918	43,910	52,380	70,995	69,544	
% of Net Sales	32.5	31.6	31.4	32.8	31.2	
Depreciation	4,371	5,140	5,980	7,462	7,624	
Other Income	1,396	3,700	7,040	4,370	10,005	
PBT	27,943	42,470	53,440	67,903	71,925	
Tax	3,132	5,110	7,860	9,932	12,947	
Rate (%)	112	12.0	14.7	14.6	18.0	
Minority Interest	210	110	0	0	0	
Adjusted PAT	24,601	37,250	45,580	57,970	58,979	
Extraordinary Items	18	-1,310	-1,010	-930	0	
Reported PAT	24,583	38,560	46,590	58,900	58,979	
Change (%)	30.0	56.9	20.8	26.4	0.1	

BALANCE SHEET		(RS MILLION)				
Y/E MARCH	2006	2007	2008	2009E	2010E	
Share Capital	1,380	2,860	2,859	2,868	2,876	
Share Premium	15,430	27,680	28,511	29,562	30,496	
Reserves	52,850	82,010	106,580	141,361	179,638	
Net Worth	69,660	112,550	137,950	173,790	213,010	
Minority Interest	680	40	0	0	0	
Loans	0	0	0	0	0	
Capital Employed	70,340	112,590	137,950	173,790	213,010	
Gross Block	29,830	46,420	54,390	66,390	81,390	
Less : Depreciation	13,280	18,360	19,860	27,322	34,946	
Net Block	16,550	28,060	34,530	39,068	46,444	
CWIP	5,710	9,650	13,240	12,000	15,000	
Investments	7,550	250	720	1,020	1,320	
Curr. Assets	63,990	96,130	131,370	161,062	195,089	
Debtors	16,080	24,360	32,970	41,831	43,570	
Cash & Bank Balance	34,290	58,710	69,500	85,167	111,409	
Loans & Advances	12,970	12,140	27,710	32,962	38,287	
Other Current Assets	650	920	1,190	1,104	1,823	
Current Liab. & Prov	23,460	21,500	41,910	39,360	44,842	
Creditors	7,320	11,540	16,240	15,817	15,903	
Other liabilities	2,020	3,150	2,880	4,574	3,085	
Provisions	14,120	6,810	22,790	18,969	25,854	
Net Current Assets	40,530	74,630	89,460	121,702	150,246	
Misc. Expenses	0	0	1	1	1	
Application of Funds	70,340	112,590	137,950	173,790	213,010	

E: MOSL Estimates

RATIOS *		(RS MILLION)				
Y/E MARCH	2006	2007	2008	2009E	2010E	
Basic (Rs)						
EPS	44.6	66.1	79.5	101.1	102.7	
Cash EPS	105.1	75.2	89.9	114.1	115.9	
Book Value	252.8	199.7	240.6	303.0	370.8	
DPS	22.5	11.5	33.2	35.9	30.8	
Payout %(Incl.Div.Taxes)	50.3	17.4	41.7	35.6	30.0	
Valuation (x)						
P/E		18.6	15.5	12.2	12.0	
Cash P/E		16.4	13.7	10.8	10.6	
EV/EBITDA		14.4	12.1	8.7	8.5	
EV/Sales		4.6	3.8	2.9	2.7	
Price/Book Value		6.2	5.1	4.1	3.3	
Dividend Yield (%)		0.9	2.7	2.9	2.5	
Profitability Ratios (%)						
RoE	40.4	40.9	36.4	37.2	30.5	
RoCE	40.2	40.8	36.4	37.2	30.5	
Turnover Ratios						
Debtors (Days)	56	53	63	63	70	
Fixed Asset Turnover (x)	6.6	6.4	5.6	6.0	5.4	
Leverage Ratio (x)						
Debt/Equity Ratio(x)	0.0	0.0	0.0	0.0	0.0	

* 1:1 bonus in FY07, accordingly ratios are adjusted

CASH FLOW STATEMENT		(RS MILLION)				
Y/E MARCH	2006	2007	2008	2009E	2010E	
CF from Operations	29,428	42,790	52,260	66,449	65,884	
Cash for Working Capital	3,549	-9,410	-3,770	-16,662	-1,582	
Net Operating CF	32,977	33,380	48,490	49,787	64,301	
Net Purchase of FA	-10,890	-20,590	-16,040	-10,760	-18,000	
Net Purchase of Invest.	4,558	7,300	-470	-300	-300	
Net Cash from Invest.	-6,332	-13,290	-16,510	-11,060	-18,300	
Proceeds from Equity & oth	6,010	11,840	1,060	1,059	942	
Proceeds from LT/STB	0	0	0	0	0	
Dividend Payments	-14,120	-7,510	-22,250	-24,120	-20,702	
Cash Flow from Fin.	-8,110	4,330	-21,190	-23,060	-19,759	
Net Cash Flow	18,535	24,420	10,790	15,666	26,242	
Opening Cash Balance	15,755	34,290	58,710	69,500	85,166	
Add: Net Cash	18,535	24,420	10,790	15,666	26,242	
Closing Cash Balance	34,290	58,710	69,500	85,166	111,409	



For more copies or other information, contact

Institutional: Navin Agarwal. **Retail:** Manish Shah

Phone: (91-22) 39825500 Fax: (91-22) 22885038. E-mail: inquire@motilaloswal.com

Motilal Oswal Securities Ltd, 3rd Floor, Hoechst House, Nariman Point, Mumbai 400 021

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1. Analyst ownership of the stock	No
2. Group/Directors ownership of the stock	No
3. Broking relationship with company covered	No
4. Investment Banking relationship with company covered	No

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