

## 2QFY09 Result Update

CMP: INR 1,227

Target: INR 1,750

OUTPERFORMER

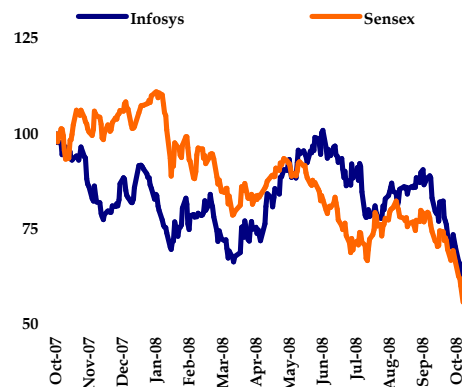
Sector View	CAUTIOUS
Company Risk	MEDIUM
BSE Sensex	10,529
S&P Nifty	3,280
BSE IT	2,584
<b>Bloomberg Consensus</b> (BUY/SELL/HOLD)	27 / 2 / 7
BSE Code	500209
NSE Code	INFOSYSTCH
Bloomberg Code	INFO IN
Reuters	INFY.BO
52 Wk High/Low (INR)	2,140 / 1,196
Equity (INR Mn)	2,863
Market Cap. (INR Mn)	702,093

### Shareholding Pattern (%)

Foreign	53.25
Institutions	7.90
Corporate	3.12
Promoters	16.51
Public & Others	19.22

Returns (%)	Abs Perf	Relative to	
		Sensex	BSE IT
1 Month	-29.86	-3.36	5.38
3 Months	-26.83	-4.99	7.04
1 Year	-37.92	6.12	7.87

### Relative Price Performance



Source: Comline Products

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Infosys reported revenues of USD 1,216 mn for 2QFY09, up 19%, in line with our expectations. Revenues in rupee terms remained little higher than our estimates due to better average rupee realization (Rs 44.5/USD as against our estimates of Rs 43.7/USD). Net profit in rupee terms is little higher than our expectations primarily due to rupee rate assumption. The company has revised FY09 USD guidance downwards by ~5% to reflect economic uncertainties and cross-currency headwinds (USD appreciation against major global currencies). Cross-currency negative impact and decline in volume assumptions contributed almost equally in downward revision of FY09 USD revenue guidance to 13.1-15.2%.

The revised FY09 guidance remained 2% lower than our expectations. However, considering turmoil in BFSI, sluggish global economy and drastic currency fluctuations, it appears to be satisfactory. We expect reasonable valuations, depreciating rupee and modest growth guidance, despite uncertainties over demand environment, client consolidation due to M&A, cases of bankruptcies, clients' indecisiveness over IT spending, would provide good support to the stock.

Infosys board has decided not to increase the bidding price for Axon from 600 pence per share. We welcome this move as in the current environment ~20x TTM earnings is expensive.

We have revised FY09E and FY10E EPS estimates down by ~2% and ~6% after factoring in H1FY09 results, change in exchange rate assumption, USD revenue growth estimates cut. We maintain Outperformer recommendation on the stock with a revised target price of Rs 1,750 at 16x FY10E earnings.

### Consolidated results for the quarter ended September 30, 2008

- ✓ Income was Rs 54,180 mn; 32% YoY%, 11.6% QoQ growth
- ✓ Profit after tax was Rs 14,320 mn; 30.2% YoY, 10% QoQ growth
- ✓ EPS increased to Rs 25; 29.9% YoY and 10% QoQ growth
- ✓ Interim dividend of Rs 10 per share (~67% yoy increase)

### Financial Summary

Descriptions	INR Mn	FY2006	FY2007	FY2008	FY2009E	FY2010E
Income		95,210	138,930	166,920	215,784	239,245
Operating Profit		30,910	43,910	52,380	69,375	75,601
Profit Before Tax		27,920	42,470	53,440	67,246	75,967
Profit After Tax		24,790	38,610	46,590	58,067	62,293
EPS (INR)		44.9	67.5	81.5	101.5	108.9
BVPS		126.2	196.8	241.2	316.4	393.1
P/E		27.3	18.2	15.1	12.1	11.3
Cash Balance		41,840	58,960	70,220	102,453	141,183

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## Key Highlights

- ✓ **Employee Addition:** Gross addition of 10,117 employees (net 5,927) during the quarter. The company guided 4,500 and 25,000 employee additions (at gross level) in Q3FY09 and FY09 respectively.
- ✓ **Client:** Top client grew by ~1.3% sequentially, accounted for 7.6% of total revenues. Top 10 clients accounted for 28% of the revenues this quarter with 2.1% sequential decline. Top 10 clients reported decline in absolute USD revenues for 2 quarters in row first time after ~7 years. USD 1+ mn clients remained at 325 despite addition of 40 new clients during the quarter. Top 2-5 clients declined by 3.5% sequentially.
- ✓ **Attrition:** During the quarter attrition rate declined by 80 bps to 12.8% on LTM basis
- ✓ **Margin Movement:** ~6% rupee depreciation and higher utilization resulted into improvement in margin by ~260 bps sequentially. The management indicated FY09 margin, factoring lower utilization in H2FY09, to remain broadly at the same level of FY08.
- ✓ **Pricing Environment:**
  - Onsite and offshore billing rate marginally improved by 0.6% and 0.1% respectively in Q2FY09, change in business mix (onsite- offshore) resulted into 0.3% decline in blended billing rate.
  - **Management Comment:** Management indicated pricing environment remain largely stable.
- ✓ **Guidance Assumption:** FY09 guidance assumed flat growth in 2HFY09. Improved performance of subsidiaries, SG & A leverage, favorable rupee and economies of scale would help to manage margin in the coming quarters. The management expects operating margin for FY09 would be within narrow range from FY08 levels of 31.4%, and net margin to be slightly lower considering higher effective tax rate, and higher dividend payout and thus lower non-operating income.
- ✓ **Tax Rate:** Tax rate return to normal rate of ~15% of PBT. Effective tax rate for FY09 is likely to be ~14% of PBT.
- ✓ **Subsidiary performance:** Depreciation of major global currency against USD impacted performance of subsidiaries for the quarter, although rupee remained favorable. We believe margin improvement of subsidiaries would help company to manage margins. Consulting subsidiary is likely to breakeven in FY09.

USD Mn	Sep-08	Jun-08	Mar-08	Dec-07	Sep-07	Jun-07
Revenue	128.8	132.0	127.5	119.0	108.0	101.2
Net Profit	9.3	8.0	16.0	11.0	5.0	11.9
NPM	7.2%	6.1%	12.5%	9.2%	4.6%	11.8%



### Positives from the result and management comments

- ✓ Q2 actual numbers are in-line with guidance – Q2 actual numbers (USD 1,216 mn) meets lower end of guidance (USD 1,215-1,225 mn), while constant currency (qoq) numbers (USD 1,236 mn) beat guidance
- ✓ Manufacturing continues to show good traction
- ✓ Company has added 40 new clients during the quarter, strong addition in BFSI segment gives pleasant surprise
- ✓ No change in employee hiring plan despite near-term challenges – suggests management confidence level and readiness to grab demand opportunities when situations start improving
- ✓ DSO decline to 60 days – Commendable in challenging environment
- ✓ Client consolidation on account of M&A – Impacted positively during the quarter

### Negatives from the results and management comments

- ✓ FY09 guidance revised downwards considering weakening demand and cross-currency fluctuations
- ✓ Worsening economic conditions
- ✓ Number of USD 1+ mn clients remain at 325 – difficulty in scaling up client account
- ✓ Number of USD 100+ mn clients decline to 5 from 6
- ✓ Clients indecisiveness over IT spending continues
- ✓ Utilization likely to decline in coming quarters – Hiring ahead of demand

### Valuation

Possibility of global economic slowdown, especially after large corporate failure and continued massive write-downs in financial sector, is increased in last few months and likely to last longer than earlier anticipated, which would impact the demand for IT and ITES. Clients' postponement/cancellation of IT projects, indecisiveness over IT spending and client consolidation due to M&A, bankruptcy remains key concerns. However, we believe current valuations also factor-in this worsening macro environment to large extent. The stock has outperformed broader markets by ~15% till date in CY08. Clients' indecisiveness over IT spending considering weakening business prospects, client consolidation due to M & A and clients going out of business remains a key concern.

Infosys and other IT stocks, considering their higher cash generation and favorable rupee, would derive strength from likely earnings slowdown in other sectors of the domestic economy on account of higher interest rates and rising input costs.

We have revised FY09E and FY10E EPS estimates down by ~2% and ~6% after factoring in H1FY09 results, change in exchange rate assumption of average Rupee/USD rate to 44.5 and 42 for FY09 and FY10 respectively, USD revenue growth estimates cut. We maintain Outperformer recommendation on the stock with a revised target price of Rs 1,750 at 16x FY10E earnings.



## 2QFY09 &amp; 1HFY09 Financial Results

Descriptions (INR Mn)	Q2FY09 Sep-08	Q1FY09 Jun-08	Q-o-Q Growth	Q2FY08 Sep-07	Y-o-Y Growth	H1FY09 Sep-08	H1FY08 Sep-07	Y-o-Y Growth
Income	54,180	48,540	11.6%	41,060	32.0%	102,720	78,790	30.4%
Software Development Expenses	28,910	27,540	5.0%	22,310	29.6%	56,450	44,000	28.3%
<b>Gross Profit</b>	<b>25,270</b>	<b>21,000</b>	<b>20.3%</b>	<b>18,750</b>	<b>34.8%</b>	<b>46,270</b>	<b>34,790</b>	<b>33.0%</b>
<i>GPM</i>	<i>46.6%</i>	<i>43.3%</i>		<i>45.7%</i>		<i>45.0%</i>	<i>44.2%</i>	
Selling & Distribution Expenses	3,030	2,570	17.9%	2,830	7.1%	5,600	4,880	14.8%
General & Administrative Expenses	4,300	3,640	18.1%	3,080	39.6%	7,940	6,230	27.4%
<b>Operating Profit</b>	<b>17,940</b>	<b>14,790</b>	<b>21.3%</b>	<b>12,840</b>	<b>39.7%</b>	<b>32,730</b>	<b>23,680</b>	<b>38.2%</b>
<i>OPM</i>	<i>33.1%</i>	<i>30.5%</i>		<i>31.3%</i>		<i>31.9%</i>	<i>30.1%</i>	
Depreciation	1,770	1,690	4.7%	1,440	22.9%	3,460	2,880	20.1%
<b>PBIT</b>	<b>16,170</b>	<b>13,100</b>	<b>23.4%</b>	<b>11,400</b>	<b>41.8%</b>	<b>29,270</b>	<b>20,800</b>	<b>40.7%</b>
<i>PBITM</i>	<i>29.8%</i>	<i>27.0%</i>		<i>27.8%</i>		<i>28.5%</i>	<i>26.4%</i>	
Other Income	660	1,170	-43.6%	1,540	-57.1%	1,830	4,070	-55.0%
<b>Net Profit Before Tax</b>	<b>16,830</b>	<b>14,270</b>	<b>17.9%</b>	<b>12,940</b>	<b>30.1%</b>	<b>31,100</b>	<b>24,870</b>	<b>25.1%</b>
<i>PBTM</i>	<i>31.1%</i>	<i>29.4%</i>		<i>31.5%</i>		<i>30.3%</i>	<i>31.6%</i>	
Provision for Taxation	2,510	1,250	100.8%	1,940	29.4%	3,760	3,080	22.1%
<b>Net Profit After Tax</b>	<b>14,320</b>	<b>13,020</b>	<b>10.0%</b>	<b>11,000</b>	<b>30.2%</b>	<b>27,340</b>	<b>21,790</b>	<b>25.5%</b>
<i>PATM</i>	<i>26.4%</i>	<i>26.8%</i>		<i>26.8%</i>		<i>26.6%</i>	<i>27.7%</i>	
Equity	2,862	2,862		2,856		2,862	2,856	
<b>EPS (INR)</b>	<b>25.0</b>	<b>22.7</b>	<b>10.0%</b>	<b>19.3</b>	<b>29.9%</b>	<b>47.8</b>	<b>38.1</b>	<b>25.2%</b>



## Revenue by Service Offering

Consulting & package implementation, Infrastructure management, and System Integration reported healthy growth

Revenue by service offering	As % of Revenue			Q-o-Q	Y-o-Y
	Sep-08	Jun-08	Sep-07	Growth	Growth
<b>ADM</b>	42.7%	43.4%	44.2%	3.6%	14.9%
Application Development	20.6%	21.4%	21.8%	1.3%	12.4%
Application Maintenance	22.1%	22.0%	22.4%	5.8%	17.4%
Business Process Management	6.0%	6.3%	5.2%	0.3%	37.3%
Consulting and Package Implementation	25.3%	23.7%	23.6%	12.4%	27.6%
Infrastructure Management	5.9%	5.7%	5.5%	9.0%	27.6%
Product Engineering Services	2.1%	2.2%	1.6%	0.5%	56.2%
System Integration	3.5%	3.1%	2.8%	18.9%	48.7%
Testing	7.0%	7.4%	7.8%	-0.4%	6.8%
Other Services	3.9%	4.3%	5.6%	-4.5%	-17.1%
<b>Total Services</b>	<b>96.4%</b>	<b>96.1%</b>	<b>96.3%</b>	<b>5.6%</b>	<b>19.1%</b>
Products	3.6%	3.9%	3.7%	-2.8%	15.8%
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>5.3%</b>	<b>19.0%</b>

## Revenue by Industry

Manufacturing, Energy & Utilities shows good traction

Industry / Vertical	As % of Revenues			Q-o-Q	Y-o-Y
	Sep-08	Jun-08	Sep-07	Growth	Growth
Insurance, Banking and Financial Services	33.4%	34.5%	36.5%	1.9%	8.9%
Manufacturing	20.1%	18.4%	13.9%	15.0%	72.1%
Retailing	12.1%	12.2%	12.5%	4.4%	15.2%
Telecom	19.0%	19.7%	20.6%	1.5%	9.7%
Energy & Utilities	5.5%	5.4%	5.3%	7.2%	23.5%
Transportation & Logistics	2.3%	2.4%	2.3%	0.9%	19.0%
Services	5.1%	5.5%	7.7%	-2.4%	-21.2%
Others	2.5%	1.9%	1.2%	38.5%	147.9%
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>5.3%</b>	<b>19.0%</b>

## Revenue by Geography

Europe continue to report healthy growth numbers

Geography	As % of Revenues			Q-o-Q	Y-o-Y
	Sep-08	Jun-08	Sep-07	Growth	Growth
North America	61.5%	62.6%	62.6%	3.4%	16.9%
Europe	28.1%	27.3%	27.4%	8.4%	22.0%
India	1.3%	1.3%	1.0%	5.3%	54.7%
Rest of the World	9.1%	8.8%	9.0%	8.9%	20.3%
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>		



## Clients Data

Clients	Sep-08	Jun-08	Sep-07
Number of Clients	586	567	520
Added during the quarter	40	49	48
Accounting for > 5% of revenue	1	1	1

### Client Concentration

Top client	7.6%	7.9%	7.9%
Top 5 clients	18.6%	19.9%	19.5%
Top 10 clients	28.0%	30.1%	29.9%
Repeat business	99.8%	99.6%	97.7%

### No. of clients with annual revenues > US\$ 1-mln

1-10 million US\$	231	234	218
10-30 million US\$	60	58	47
30-50 million US\$	14	15	14
50-100 million US\$	15	12	13
100+ million US\$	5	6	3

## Business Outlook

### ✓ Quarter ending December 31, 2008

- Income is expected to be in the range of Rs 55,190 million and Rs 57,300 million; YoY growth of 29.2% – 34.2%
- Earnings per share is expected to be Rs 26.63; YoY growth of 23.6%\*\*

### ✓ Fiscal year ending March 31, 2009

- Income is expected to be in the range of Rs 213,090 million and Rs 217,310 million; YoY growth of 27.7% – 30.2%
- Earnings per share\*\*\* is expected to be Rs 101.06; YoY growth of 24%

\*\* Including tax reversal of Rs 500 million for the quarter ended December 31, 2007. Excluding the tax reversal the YOY growth is expected to be 28.9%.

\*\*\* Including tax reversal of Rs 310 million in fiscal 2009 and Rs 1,210 million in fiscal 2008 respectively. Excluding the tax reversal the earnings per share is expected to be Rs.100.51 for the year ending March 31, 2009; YoY growth of 26.6%

Conversion 1 USD = Rs. 46.97



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