

Infosys Technologies Ltd.

INR: 1,225

Reduction in Dollar Guidance

BUY



We have analyzed the results of Infosys post Q2FY09 results & our key findings are:

Q2FY09 Results – Key highlights

- **Depreciated rupee drove revenue growth-** Revenue increased 11.6% q-o-q to Rs 5,418 crore, driven mainly by the 5.9% depreciation of the rupee over last quarter, notably USD revenue grew 5.3% sequentially
- **Cross Currency impact** – USD revenue negatively impacted by 3% due to wider movement in EUR, GBP and AUD
- **Operating margins increased by 264 bps-** EBITDA grew strongly by 21.3% on back of depreciated rupee and Seasonal decline in employee expenses growth
- **Higher taxes impact PAT margins-** Higher effective tax rate at 14% in the reduce the margin to

Q2 FY09 Guidance

Particulars	Q3FY09	Initial FY09	Revised FY09
Revenue (US\$ mn)	1,198	5,010	4,765
Revision (%)			-4.9
Revenue (Rs cr)	5,625	21,450	21,520
Revision (%)			0.3
Rs /US\$ rate	46.97	43.04	46.97
Revision (%)			9.1
EPS (\$)	0.57	2.34	2.24
Revision (%)			-4.3
EPS (Rs)	26.63	101.06	101.06
Revision (%)			0.0

- **Cut USD guidance-** Conservative management culture, challenging macro environment and cross currency has compelled Infosys to reduce the USD revenue/EPS guidance by 5% each, still expecting 13-15% growth. For remaining 2 quarters, at the upper end of guidance, management expects 0.2% q-o-q growth and at the lower end of guidance 2.3% decline in growth. Investors would see this reduction as negative in uncertain times.

Our View

We continue to maintain POSITIVE view on the IT sector despite sharp underperformance to the market. We believe that offshoring of IT services will continue to grow. However, recent turmoil had raised pressure on medium term growth of Indian IT sector.

We are reducing our estimates and P/Es for Infosys taking into consideration the deteriorating external environment and reduction in USD guidance. Valuations looks attractive in recent sharp fall, however, at the same time there are no near term upside factors for the company as well Indian IT sector.

At the CMP of Rs 1,225, Infosys is trading at 13.4x its TTM earnings and 12.1x FY09E EPS of Rs 101.5. We maintain a BUY on the stock with a target price of Rs 1,625. At the target price the stock would be valued at 16.0x FY09E EPS of Rs101.5 and 13.7x FY10E EPS of Rs 118.0 implying an upside potential of 32.6%.

Price Outlook (INR): 1,625

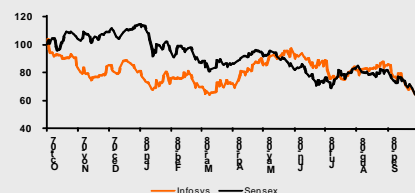
Market Data October, 10 2008

Shares outs (Cr)	286
Equity Cap	57.3
Mkt Cap (Rs. Cr)	70,123
52 Wk H/L (Rs)	2,140/1,196
Avg Vol (1yr avg)	3,38,359
Face Value (Rs)	5
Bloomberg Code	INFO IN

Market Info:

SENSEX - 10,528
NIFTY - 3,280

Price Performance



Share Holding Pattern (%)

Particulars	30/9	30/6	Chg (%)
Promoter	16.5	16.5	-0.1
Institution	41.5	40.5	2.4
Public	22.9	23.8	-4.0
ADR	19.1	19.2	-0.2
Total	100	100	

Source: BSE, KRC Research

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Strong revenue growth of 12.9% in Europe was impacted by cross currency

Infosys had Cash balances stood at Rs 7,821 crores (Rs 136/share)

Other key highlights

- While revenue guidance for Q3FY09 implies merely 3.8% growth y-o-y, Infosys has maintained its annual hiring guidance which points towards a decline in utilization rates, cross currency impact on revenue, or changes in pricing
- Hiring of 10,117 employees for 2Q09 was inline with seasonal trends. The company has hired 1,649 employees in the BPO segment while crossing the 100,000 milestone during 2Q09
- Strong revenue growth of 12.9% in Europe was impacted by cross currency headwinds to 8.3% q-o-q
- While the demand environment uncertainty has remained, Q209 revenue growth was partially supported by expansion of existing client relationships. Repeat business from customers increased to 99.8%
- Margins increased by 264 bps q-o-q – this was a net impact of rupee depreciation and decline in software expenses. In addition the accounting for wage hikes in Q1FY09 also positively impacted margins. In Q309, Infosys expects to maintain EBITDA margins in a narrow band (40-50bps of 32.6%)
- The company has won 5 deals in the Financial space as well as 5 deals in the Manufacturing space
- Amongst verticals, Telecom and Travel/Transportation revenue declined to 19.0% and 2.3% while manufacturing recorded increased to 20.1% of revenue. BFSI revenues contribution declined to 26.5%
- Amongst service lines, ADM revenue declined 3% q-o-q while ERP/Consulting saw marginal decline of 0.5% q-o-q. Infrastructure management saw 25% q-o-q growth and Product Engineering saw 24% q-o-q growth on low bases
- The company has hedges of US\$932m @ of Rs 46.97 and maintained its hedging policy of maintaining cover for the next two quarters
- Infosys had Cash balances stood at Rs 7,821 cores. The FY09 cash balance of the company is expected at Rs 8,893 cr (Rs 155/share). Receivable days were 60 as compared to 69 in 1QFY09.

Key financials

(Rs Cr)

	2Q08	1Q09	2Q09	QoQ	YoY	
Revenue (US\$ mn)	1,022	1,155	1,216	5.3%	18.9%	
Revenue	4,106	4,854	5,418	11.6%	32.0%	
S/W Development Expenses	2,231	2,754	2,891	5.0%	29.6%	
other expenses	591	621	733	18.0%	24.0%	
EBITDA	1,284	1,479	1,794	21.3%	39.7%	
EBITDA margin	31.3%	30.5%	33.1%	264 bps	184 bps	Supported by rupee depreciation
Depreciation & amortization	144	169	177	4.7%	22.9%	
EBIT	1,140	1,310	1,617	23.4%	41.8%	
EBIT margin	27.8%	27.0%	29.8%	286 bps	208 bps	
Other income	154	117	66	-43.6%	-57.1%	Lower other income due to losses on f/w contract. \$932mn hedges as on Q2 @ Rs 46.97/\$
Profit before tax	1,294	1,427	1,683	17.9%	30.1%	
Income tax	194	125	251	100.8%	29.4%	
Net Profit	1,100	1,302	1,432	10.0%	30.2%	
PAT margin	26.8%	26.8%	26.4%	-39 bps	-36 bps	Decline in PAT due to higher taxes and forex losses
EPS - basic	19.26	22.79	25.01	9.8%	29.9%	
EPS - fully diluted	19.19	22.71	24.98	10.0%	30.2%	

Revenue by verticals

	2Q08	3Q08	4Q08	1Q09	2Q09	
Geographic wise						
North America	62.6%	62.3%	60.7%	62.6%	61.5%	
Europe	27.4%	28.6%	29.3%	27.3%	28.1%	Increasing revenue from Europe
India	1.0%	1.2%	1.3%	1.3%	1.3%	
RoW	9.0%	7.9%	8.7%	8.8%	9.1%	
Service line wise						
Application development	21.8%	21.5%	21.8%	21.4%	20.6%	
Application maintenance	22.4%	24.8%	23.4%	22.0%	22.1%	
BPO	5.2%	5.9%	6.0%	6.3%	6.0%	
Consulting & PI	23.6%	24.0%	24.1%	23.7%	25.3%	Moving up into the value chain
Infrastructure Mgmt	5.5%	4.5%	4.6%	5.7%	5.9%	
Product Engg Services	1.6%	1.7%	1.8%	2.2%	2.1%	
System Integration	2.8%	2.7%	3.0%	3.1%	3.5%	
Testing Services	7.8%	7.4%	7.2%	7.4%	7.0%	
Others	5.6%	3.8%	4.4%	4.3%	3.9%	
Products	3.7%	3.7%	3.7%	3.9%	3.6%	
Vertical wise						
Insurance	7.7%	7.3%	7.0%	6.8%	6.9%	
Banking & FS	28.8%	29.5%	26.9%	27.7%	26.5%	Credit crisis takes its toll but in absolute term BFSI grew by 2% qoq
Manufacturing	13.9%	14.6%	16.4%	18.4%	20.1%	Maintaining last quarter growth
Retail	12.5%	12.0%	11.9%	12.2%	12.1%	
Telecom	20.6%	21.1%	22.5%	19.7%	19.0%	Problems with BT continue
Energy & Utilities	5.3%	5.2%	5.2%	5.4%	5.5%	
Transportation & Logistics	2.3%	2.4%	2.8%	2.4%	2.3%	
Services	7.7%	6.0%	5.5%	5.5%	5.1%	
Others	1.2%	1.9%	1.8%	1.9%	2.5%	

Project wise

Fixed Price	29.8%	32.8%	33.2%	32.8%	34.1%
T&M	70.2%	67.2%	66.8%	67.2%	65.9%

Employee Metrics

	2Q08	3Q08	4Q08	1Q09	2Q09	
IT and BPO professionals	75,313	83,011	85,013	87,816	93,624	
- Billable	66,743	75,345	79,494	82,368	83,412	
- Banking Business Unit	2,053	2,053	2,053	2,076	2,093	
- Trainees	6,517	5,613	3,466	3,372	8,119	
Sales & support	5,188	5,590	6,174	6,563	6,682	
Total employees	80,501	88,601	91,187	94,379	100,306	Crossed 100,000 milestone
Gross addition	8,543	11,683	5,947	7,182	10,117	Maintaining FY09 target of 25,000 and will recruit 4,500 more in Q3
Net addition	4,530	8,100	2,586	3,192	5,927	
Attrition % (TTM)	14.2%	13.7%	13.4%	13.6%	12.8%	Declining attrition implies lower training expenses
Utilization						
- including trainees	70.3%	69.4%	69.8%	68.9%	69.4%	
- excluding trainees	77.8%	76.3%	75.4%	72.2%	73.7%	Seasonal trend in utilization

Operational metrics

	2Q08	3Q08	4Q08	1Q09	2Q09	
Infosys consolidated						
Billed effort (person-months)	159,203	167,381	180,478	183,604	194,073	
- Onsite	40,936	42,190	44,220	44,680	46,526	
- Offshore	118,267	125,191	136,258	138,924	147,547	
Billed effort distribution (%)						
- Onsite	25.7%	25.2%	24.5%	24.3%	24.0%	Declining onsite contribution implies higher EBITDA margin
- Offshore	74.3%	74.8%	75.5%	75.7%	76.0%	
Revenue distribution (%)						
- Onsite	48.8%	47.8%	47.5%	47.5%	47.3%	
- Offshore	51.2%	52.2%	52.5%	52.5%	52.7%	
IT Services						
Billed effort distribution (person-months)	128,457	134,208	140,804	141,446	150,669	
- Onsite	40,740	41,974	43,999	44,477	46,314	
- Offshore	87,717	92,234	96,805	96,969	104,355	
Billed effort distribution (%)						
- Onsite	31.7%	31.3%	31.2%	31.4%	30.7%	
- Offshore	68.3%	68.7%	68.8%	68.6%	69.3%	
Revenue distribution (%)						
- Onsite	53.2%	52.6%	52.5%	52.7%	52.0%	
- Offshore	46.8%	47.4%	47.5%	47.3%	48.0%	
Volume growth	7.7%	4.5%	4.9%	0.5%	6.5%	
Q-o-Q Change in Billing Rates						
Onsite	2.95%	1.06%	-0.05%	0.02%	0.64%	Increase in billing in spite of lowering demand for IT services
Offshore	2.63%	1.34%	0.53%	-0.04%	0.06%	
Blended	2.78%	1.21%	0.26%	-0.01%	0.33%	

	2Q08	3Q08	4Q08	1Q09	2Q09	
Revenue by clients						
Active Clients	520	530	538	567	586	
Added during the period	48	47	40	49	40	Largest client additions in BFSI
No. of million dollar clients	295	305	310	325	325	
No. of 5mn+ dollar clients	122	128	141	146	151	
No. of 10mn+ dollar clients	77	81	89	91	94	
No. of 20mn+ dollar clients	44	45	47	53	56	
No. of 30mn+ dollar clients	30	30	32	33	34	
No. of 40mn+ dollar clients	22	22	22	25	26	
No. of 70mn+ dollar clients	11	12	13	16	12	
No. of 90mn+ dollar clients	9	9	10	12	8	
Revenue - top client	7.9%	9.5%	10.3%	7.9%	7.6%	
Revenue - top 5 client	19.5%	21.6%	22.0%	19.9%	18.6%	Top clients contributions declining
Revenue - top 10 client	29.9%	32.5%	32.0%	30.1%	28.0%	
Repeat Business	97.7%	96.3%	95.0%	99.6%	99.8%	
DSO - TTM (in days)	61	60	72	69	60	

Constant Currency Reporting

Geographical growth	Sequentially		Constant Currency		
	Q1 09	Q2 09	Q1 09	Q2 09	
North America	4.3%	3.3%	2.0%	3.4%	
Europe	-5.6%	8.3%	-1.5%	12.9%	Cross currency headwinds diminish sequential growth
RoW	1.8%	10.1%	-0.3%	15.9%	
Vertical wise	Sequentially		Constant Currency		
	Q1 09	Q2 09	Q1 09	Q2 09	
BFSI	2.8%	1.7%	2.9%	3.2%	
Manufacturing	13.3%	14.8%	12.1%	16.2%	
Retail	3.7%	4.5%	3.7%	5.5%	
Telecom	-11.20%	1.70%	-11.70%	5.80%	
Others	0.50%	7.10%	0.40%	8.40%	

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Other Stocks in the sector under our active coverage: IT

Infosys Technologies Ltd.	Rating Legend
	Our Rating Upside
	Strong Buy More than 25%
	Buy 15% - 25%
	Hold 10% - 15%
	Reduce Nil – 10%
	Sell Less than 0%

Date	Company	Type of Report	Recommendation	Reco. Price	Target
23 July 2008	Wipro	Result Update	Buy	395	463
22 July 2008	Satyam	Result Update	Buy	368	456
17 July 2008	TCS	Result Update	Hold	782	898

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