

Equities

2 November 2011 | 8 pages

Infosys Ltd (INFY.BO)

Model Update

- We raise our estimates on Infosys for FY12E-FY14E by ~2-3% as we factor in Q2FY12 results and make small changes to volume/pricing/cost/tax assumptions. We also raise our multiple to 19x (from 18x earlier) as we believe that a decent Q2 and a good guidance for Q3 does call for some rerating for the stock (our target multiple now implies ~5% discount to TCS, which has demonstrated quarters of good performance). However, given limited upside to our target price, we maintain our Neutral rating.

- Company Update
- Target Price Change
- Estimate Change

Neutral	2
Price (02 Nov 11)	Rs2,835.50
Target price	Rs2,890.00
	<i>from Rs2,650.00</i>
Expected share price return	1.9%
Expected dividend yield	1.5%
Expected total return	3.4%
Market Cap	Rs1,620,118M
	US\$32,879M

Price Performance (RIC: INFY.BO, BB: INFO IN)



Statistical Abstract

Year to	Net Profit	Diluted EPS	EPS growth	P/E	P/B	ROE	Yield
31 Mar	(RsM)	(Rs)	(%)	(x)	(x)	(%)	(%)
2010A	62,660	109.31	4.7	25.9	7.0	30.3	0.9
2011A	68,230	119.42	9.2	23.7	5.9	27.1	2.1
2012E	82,335	144.10	20.7	19.7	5.0	27.6	1.5
2013E	91,229	159.66	10.8	17.8	4.2	25.6	1.7
2014E	99,054	173.35	8.6	16.4	3.5	23.5	1.8

Source: Powered by dataCentral

Surendra Goyal, CFA

See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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Fiscal year end 31-Mar	2010	2011	2012E	2013E	2014E
Valuation Ratios					
P/E adjusted (x)	25.9	23.7	19.7	17.8	16.4
EV/EBITDA adjusted (x)	19.0	16.2	13.2	11.5	10.3
P/BV (x)	7.0	5.9	5.0	4.2	3.5
Dividend yield (%)	0.9	2.1	1.5	1.7	1.8
Per Share Data (Rs)					
EPS adjusted	109.31	119.42	144.10	159.66	173.35
EPS reported	109.31	119.42	144.10	159.66	173.35
BVPS	403.77	477.91	566.86	678.53	799.90
DPS	25.00	60.00	43.00	48.00	52.00
Profit & Loss (RsM)					
Net sales	227,420	275,010	336,981	380,159	422,057
Operating expenses	-157,860	-193,990	-240,046	-272,800	-307,785
EBIT	69,560	81,020	96,935	107,359	114,272
Net interest expense	9,910	12,110	17,628	17,746	20,965
Non-operating/exceptionals	0	0	0	0	0
Pre-tax profit	79,470	93,130	114,563	125,105	135,237
Tax	-16,810	-24,900	-32,227	-33,876	-36,184
Extraord./Min.Int./Pref.div.	0	0	0	0	0
Reported net income	62,660	68,230	82,335	91,229	99,054
Adjusted earnings	62,660	68,230	82,335	91,229	99,054
Adjusted EBITDA	78,610	89,560	106,826	118,895	127,004
Growth Rates (%)					
Sales	4.8	20.9	22.5	12.8	11.0
EBIT adjusted	8.1	16.5	19.6	10.8	6.4
EBITDA adjusted	9.3	13.9	19.3	11.3	6.8
EPS adjusted	4.7	9.2	20.7	10.8	8.6
Cash Flow (RsM)					
Operating cash flow	57,270	55,150	69,072	81,330	86,418
Depreciation/amortization	9,050	8,540	9,891	11,536	12,732
Net working capital	-1,470	-120	-4,827	-3,689	-4,402
Investing cash flow	-9,060	-3,430	-18,677	-17,619	-21,103
Capital expenditure	-9,060	-3,430	-18,677	-17,619	-21,103
Acquisitions/disposals	0	0	0	0	0
Financing cash flow	-12,390	-24,820	-34,675	-27,425	-29,711
Borrowings	2,320	870	-3,190	0	0
Dividends paid	-14,294	-34,271	-24,568	-27,425	-29,711
Change in cash	35,820	26,900	15,720	36,286	35,604
Balance Sheet (RsM)					
Total assets	277,360	312,630	370,797	437,974	513,897
Cash & cash equivalent	105,560	168,100	199,468	253,500	310,069
Accounts receivable	34,940	46,530	58,972	64,627	71,750
Net fixed assets	53,550	48,440	57,226	63,308	71,680
Total liabilities	46,870	39,600	46,917	50,290	56,870
Accounts payable	23,430	35,530	45,781	49,064	55,552
Total Debt	0	0	0	0	0
Shareholders' funds	230,490	273,030	323,880	387,684	457,027
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	34.6	32.6	31.7	31.3	30.1
ROE adjusted	30.3	27.1	27.6	25.6	23.5
ROIC adjusted	62.0	67.4	73.8	74.0	70.6
Net debt to equity	-45.8	-61.6	-61.6	-65.4	-67.8
Total debt to capital	0.0	0.0	0.0	0.0	0.0

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Infosys Ltd

Company description

Infosys is the second-largest Indian IT services company with more than 140,000 professionals, and is a leader in the offshore services space. Infosys provides business consulting, application development & maintenance and engineering services to over 600 clients across verticals such as Banking, Financial Services, Insurance, Retail, Manufacturing and Utilities in the Americas, Europe and Asia Pacific. Infosys also sells a core banking application, Finacle, which is used by leading banks in India, the Middle East, Africa and Europe. Its subsidiary, Infosys BPO, is a provider of BPO services.

Investment strategy

We rate Infosys shares Neutral (2). We are positive on the company's fundamentals. Offshore IT outsourcing has become a mainstream option, and we think that scale and scalability, along with an ability to move up the value chain, are key criteria for successful offshore vendors. In this respect, Infosys appears well positioned and continues to do well given its strong branding and industry leading sales force. We expect Infosys to deliver a revenue CAGR of ~16% (\$terms) and an earnings CAGR of ~15% for FY11-13E. Unlike other high-growth firms in other industries, Infosys continues to generate solid FCF and its RoE of ~25-30% remains well above its cost of capital. However, it faces some challenges: (a) the last few quarters have been weaker than peers; (b) results of the shift in strategy (with more transformational and non-linear work) have yet to play out; and (c) expectations remain elevated post the decent quarterly guidance, which will likely prevent any meaningful upgrades from a stock perspective.

Valuation

Our Rs2,890 target price for Infosys is based on 19x Sep'12E EPS. This is close to the mid-point of the last 3-year trading band of 10-25x 12-month forward earnings and factors in deceleration in growth and macro overhang. Our estimates continue to assume a certain PE premium to the market; this is justified, in our view, given the strong FCF and ROIC for Infosys vs. the overall market. We believe PE remains the most appropriate valuation measure given Infosys' profitability record and higher earnings visibility.

Risks

The key downside risks to our investment thesis on Infosys are: (1) any significant appreciation of the rupee against the USD/EUR/GBP; (2) pressure on billing rates; and (3) a prolonged slowdown in the US economy. Key upside risks that could cause shares to exceed our target price include: (1) a sharp recovery in the US/Global economy; and (2) any significant depreciation of the rupee against the USD/EUR/GBP.

If any of these risk factors has a greater downside impact than we anticipate, the share price will likely have difficulty attaining our target price. Conversely, if the impact of any of these upside risks is greater than we anticipate, the stock could exceed our target price.

Appendix A-1

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Infosys Ltd (INFY.BO) Ratings and Target Price History Fundamental Research

Analyst: Surendra Goyal, CFA

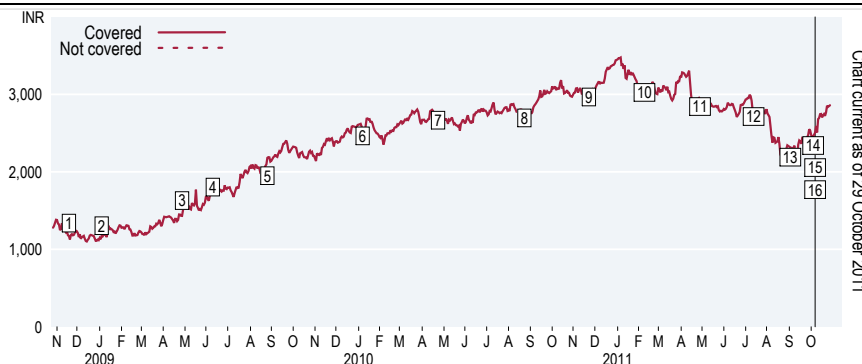


Chart current as of 29 October 2011

	Date	Rating	Target Price	Closing Price
1	19-Nov-08	1M	*1,420.00	1,172.00
2	4-Jan-09	1M	*1,350.00	1,130.95
3	28-Apr-09	*1L	*1,650.00	1,431.55
4	10-Jun-09	1L	*2,060.00	1,803.25
5	26-Aug-09	*2L	*2,290.00	2,181.35
6	7-Jan-10	2L	*2,785.00	2,525.25

	Date	Rating	Target Price	Closing Price
7	23-Apr-10	2L	*2,935.00	2,728.10
8	24-Aug-10	2L	*3,065.00	2,765.50
9	23-Nov-10	2L	*3,220.00	3,013.30
10	9-Feb-11	2L	*3,430.00	3,127.00
11	28-Apr-11	2L	*3,230.00	2,931.55
12	13-Jul-11	2L	*3,125.00	2,784.20

	Date	Rating	Target Price	Closing Price
13	2-Sep-11	2L	*2,570.00	2,315.55
14	5-Oct-11	2L	*2,650.00	2,454.30
15	7-Oct-11	Stock rating system changed		
16	7-Oct-11	*2	2,650.00	2,507.05

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Infosys Ltd (INFY.BO) Ratings and Target Price History Best Ideas Research Relative Call (3 Month)

Analyst: Surendra Goyal, CFA

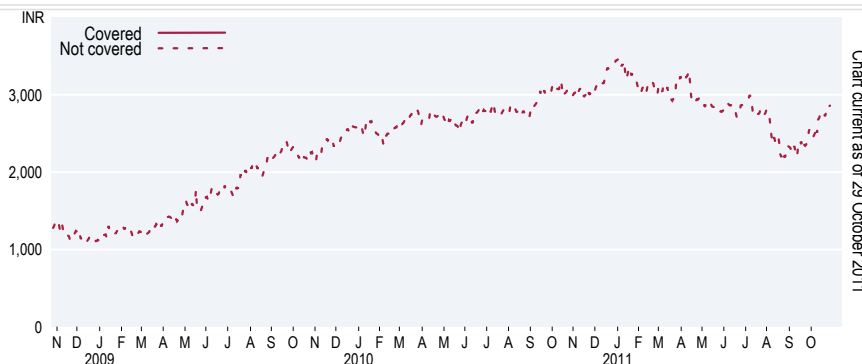


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