

Institutional Equities
 India Research

Infosys
QUARTERLY REVIEW

 Bloomberg: INFO IN
 Reuters: INFY.BO

HOLD

Results & Guidance Disappoint – Downgrade to HOLD

Infosys' results disappointed on the back of a miss in the quarter on both, revenue growth (-1.9% QoQ) as well as guidance/outlook for FY13. The FY13 USD revenue guidance of 8-10% YoY growth fell short of our and consensus expectations. The guidance for Q1FY13 suggests 0-1% sequential growth. The results and the guidance will likely re-fuel fresh debate on "structural issues" with the Company. Hence, while we have lowered our target price to Rs. 2,550 per share, we downgrade our recommendation on the stock to "HOLD" from "BUY".

- Quarter Details:** Pricing declined 1.3% QoQ on constant currency basis. While the attrition recorded at 14.7% and net addition stood at 4,906 (vs. 3,266 in Q3) with lateral addition recorded at 4,727 (vs. 3,863 in Q3). Utilisation (including trainees) was lower at 67.2% (vs. 69.9% in Q3). US saw a strong decline of 4% (in constant currency terms), while the FSI declined 5%. We believe that the players like HCL Tech/Cognizant and others could win deals, making it difficult for Infosys to get deals at premium pricing. Cash and equivalents stood at US\$4.1bn in Q4.
- Disappointing USD Guidance for FY13:** Infosys guided to 8-10% YoY revenue growth for FY13 (vs. our expectation of 11-14%). After a revenue decline of 1.9% in Q4FY12 and flattish revenue guidance for Q1FY13, Infosys will have to deliver revenue CQGR of 4.8% over Q2-Q3-Q4FY13, which looks stretched. Its performance is volatile and Management's ability to predict this performance has become less accurate in the face of poor visibility in macro environment. We expect this to continue for some time, casting continued pressure on the stock.

Outlook & Valuation

We lower our earnings estimates for Infosys by 6.3% and 8.6% for FY13E & FY14E, respectively to factor in lower revenue growth trajectory. We have reduced our target to Rs. 2,550 (vs. Rs. 3,100 projected earlier), implying 15.5x average of for FY13E & FY14E EPS of Rs. 164 (vs. 18.5x forward earnings projected earlier) to account in for increased macro concerns.

Risks

- Higher exposure to Consulting/Package Implementation compared to peers
- Lower-than-expected demand ramp-up in key areas like the US.

Exhibit 1: Key Financials

Y/E Mar (Rs. mn)	FY10	FY11	FY12	FY13E	FY14E
Operating Income	227,420	275,010	337,340	371,805	418,055
EBITDA	78,610	89,680	107,160	114,382	129,886
Adjusted PAT/Net	62,090	68,350	83,160	89,661	99,010
EPS	108.2	119.0	144.8	156.1	172.3
ROCE	38.2	38.0	40.9	36.7	33.8
ROE	30.1	27.9	29.1	26.0	24.0
P/E	22.2	20.2	16.6	15.4	13.9

Source: Company, Karvy Institutional Research

Recommendation

CMP:	Rs2,396
Target Price:	Rs2,550
Previous Target Price	Rs3,100
Upside (%)	6.4%

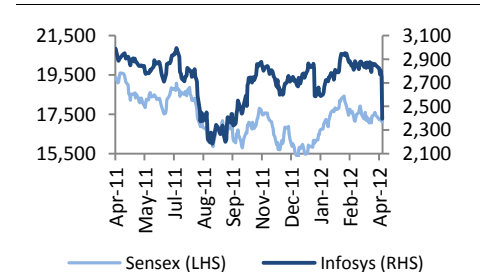
Stock Information

Market Cap. (Rs bn / US\$ mn)	1,376/26,717
52-week High/Low (Rs)	3,317/2,162
3m ADV (Rs mn /US\$ mn)	3,369/65.4
Beta	0.9
Sensex/ Nifty	17,095/5,207
Share outstanding (mn)	574

Stock Performance (%)

	1M	3M	12M	YTD
Absolute	(16.1)	-(7.3)	(27.5)	(13.4)
Rel. to Sensex	(12.7)	(12.4)	(16.5)	(21.7)

Performance



Source: Capitaline, Karvy Institutional Research

Earnings Revision

(%)	FY13E	FY14E
Sales	↓ 4.2	↓ 6.4
EBITDA	↓ 6.0	↓ 6.1
PAT	↓ 6.3	↓ 8.6

Source: Company, Karvy Institutional Research

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Results review

Infosys registered a lower-than-expected performance in Q4FY12. Its revenue in USD terms dipped 1.9% QoQ to US\$1,771 mn vs. a guided flattish revenue growth. Its margin declined by 110 bps sequentially mainly due to lower utilization and INR appreciation. The Company guided to 8-10% USD revenue growth in FY13E with a flat revenue growth for Q1FY13E, which in our view is disappointing. EPS for FY13E is seen at Rs. 158-161.

Revenue Analysis

Infosys' revenue stood at Rs. 88.5 bn in Q4FY12, which is 3.5% lower than our estimate. The average INR-USD conversion rate for the quarter was 50. In USD terms, its revenue declined 1.9% QoQ to US\$1,771 mn in the quarter under review.

- Sequential revenue decline of 1.9% included a volume decline of 0.6% (1.3% onsite volume growth and 0.3% offshore volume growth QoQ) and a blended pricing decline of 1.3% in constant currency terms.
- Infosys added 4,906 employees (net) to take the total employee base to 149,994. Laterals added this quarter stood at 4,727.
- The proportion of fixed price contracts was at 39.4% in Q4FY12, as against 40.9% in Q3FY12.
- EBITDA margin decreased by 110 bps owing to INR depreciation. Margin headwinds – like lower utilization (including trainees) which was lower at 67.2% in Q4FY12 (vs. 69.9% in Q3FY12) – was cushioned by lower SG&A spend.

Non-Operating Items

Other Income: Infosys' other income was higher than our estimate. Forex gain for the quarter stood at Rs. 600 mn.

Effective Tax Rate: The tax rate was 29.8% (vs. our expectation of 28.6%)

Dilution: ESOP conversion was in line with our estimate.

Net Profit Growth

Net profit was in-line with our expectation helped by higher-than-expected other income.

Disappointing Guidance

Infosys guided to 8-10% YoY revenue growth for FY13 (vs. our expectation of 11-14%). After a revenue decline of 1.9% in Q4FY12 and flattish revenue guidance for Q1FY13, Infosys will have to deliver revenue CQGR of 4.8% over Q2-Q3-Q4FY13, which looks stretched. Its performance is volatile and Management's ability to predict this performance has become less accurate in the face of poor visibility in macro environment. We expect this to continue for some time, casting continued pressure on the stock.

Exhibit 1: Quarterly details

Rs mn	4Q11	1Q12	2Q12	3Q12	4Q12
Revenues	72,500	74,850	80,990	92,980	88,520
Growth (YoY, %)	22.0	20.8	16.6	30.8	22.1
Growth (QoQ, %)	2.0	3.2	8.2	14.8	(4.8)
- Operating costs	49,260	53,100	55,830	61,630	59,620
EBITDA	23,240	21,750	25,160	31,350	28,900
EBITDA margin (%)	32.1	29.1	31.1	33.7	32.6
Growth (YoY, %)	14.9	10.9	8.7	32.7	24.4
Growth (QoQ, %)	(1.7)	(6.4)	15.7	24.6	(7.8)
- Interest expense	-	-	-	-	-
- Depreciation	2,220	2,230	2,350	2,360	2,430
+ Other income. net (incl forex)	4,150	4,430	3,870	4,220	6,520
PBT	25,170	23,950	26,680	33,210	32,990
- Taxes	6,990	6,730	7,620	9,490	9,830
Effective tax rate (%)	27.8	28.1	28.6	28.6	29.8
PAT	18,180	17,220	19,060	23,720	23,160
- Minority interests	-	-	-	-	-
Consolidated PAT	18,180	17,220	19,060	23,720	23,160
Net margin (%)	25.1	23.0	23.5	25.5	26.2
Growth (YoY, %)	16.6	15.7	9.7	33.3	27.4
Growth (QoQ, %)	2.1	(5.3)	10.7	24.4	(2.4)
Reported profits	18,180	17,220	19,060	23,720	23,160

Source: Company

Exhibit 2: Change in estimates

(Rs mn)	FY13E			FY14E		
	Old	New	Change (%)	Old	New	Change (%)
Revenue (US\$ mn)	7,960	7,607	(4.4)	9,301	8,620	(7.3)
Revenue	388,028	371,805	(4.2)	446,430	418,055	(6.4)
EBITDA margin (%)	31.3	30.8	(50)bps	31.0	31.1	10bps
EPS (Rs)	166.6	156.1	(6.3)	188.6	172.3	(8.6)

Source: Company, Karvy Institutional Research

Exhibit 3: Profit & Loss statement (Consolidated)

Rs mn	FY10	FY11	FY12	FY13E	FY14E
Revenues	227,420	275,010	337,340	371,805	418,055
Growth (%)	4.8	20.9	22.7	10.2	12.4
Avg. currency rate (Rs/\$)	47.4	45.5	48.1	48.9	48.5
Depreciation (%)	1.9	(4.0)	5.6	1.6	(0.8)
Employees (Nos)	113,796	130,820	149,994	163,038	187,494
Growth (%)	8.5	15.0	14.7	8.7	15.0
Software engineers (Nos)	97,984	116,208	133,092	141,843	169,682
% of total employees	86.1	88.8	88.7	87.0	90.5
Revenue/ S/W employee (US\$ 000)	51.4	56.4	56.3	55.3	55.3
Growth (%)	(6.2)	9.8	(0.2)	(1.6)	-
Expenses	148,810	185,330	230,180	257,423	288,169
As % of revenue	65.4	67.4	68.2	69.2	68.9
Employee cost	119,360	148,640	183,400	205,320	231,066
As % of revenue	52.5	54.0	54.4	55.2	55.3
Cost / Employee (Rs 000)	1,091.8	1,215.3	1,306.2	1,311.8	1,318.4
Wage inflation (%)	(5.0)	11.3	7.5	0.4	0.5
Other costs	29,450	36,690	46,780	52,103	57,103
As % of revenue	12.9	13.3	13.9	14.0	13.7
EBITDA	78,610	89,680	107,160	114,382	129,886
EBITDA margin (%)	34.6	32.6	31.8	30.8	31.1
Depreciation	9,050	8,540	9,370	10,883	11,758
Other income	9,340	12,110	19,040	22,784	21,322
PBT	78,900	93,250	116,830	126,283	139,451
Tax	16,810	24,900	33,670	36,622	40,441
Effective tax rate (%)	21.3	26.7	28.8	29.0	29.0
PAT	62,090	68,350	83,160	89,661	99,010

Source: Company, Karvy Institutional Research

Exhibit 4: Balance sheet (Consolidated)

Rs mn	FY10	FY11	FY12	FY13E	FY14E
Equity	2,860	2,860	2,860	2,860	2,860
Reserves	227,630	256,900	308,484	374,627	445,400
Capital employed	230,490	259,760	311,344	377,487	448,260
Fixed assets	53,550	57,600	54,090	55,707	56,449
Investments	37,120	1,440	15,430	15,430	15,430
Deferred tax assets	2,000	3,210	3,160	3,160	3,160
Cash	105,560	150,950	182,644	244,376	309,081
Working capital	32,260	46,560	56,020	58,814	64,140
Capital employed	230,490	259,760	311,344	377,487	448,260

Source: Company, Karvy Institutional Research

Exhibit 5: Cash flow statement (Consolidated)

Rs mn	FY10	FY11	FY12	FY13E	FY14E
PAT	62,090	68,350	83,160	89,661	99,010
+ non-cash expense	8,310	7,330	9,420	10,883	11,758
Cash profit	70,400	75,680	92,580	100,544	110,768
- Increase/(decrease) in WC	1,470	14,300	9,460	2,794	5,326
Operating cash flow	68,930	61,380	83,120	97,750	105,442
- Capex	9,060	12,590	5,860	12,500	12,500
Free cash flow	59,870	48,790	77,260	85,250	92,942
+ Equity raised	2,030	890	0	(0)	0
+ Debt raised	-	-	-	-	-
- Investments	37,120	(35,680)	13,990	-	-
- Dividend paid	16,740	39,970	31,576	23,518	28,237
- Misc. expense	(570)	-	-	-	-
Net change in cash	8,610	45,390	31,694	61,732	64,705
Opening cash	96,950	105,560	150,950	182,644	244,376
Closing cash	105,560	150,950	182,644	244,376	309,081

Source: Company, Karvy Institutional Research

Exhibit 6: RoCE/RoE analysis

	FY10	FY11	FY12	FY13E	FY14E
EBIT/Sales (%)	34.7	33.9	34.6	34.0	33.4
Sales/Avg CE (x)	1.1	1.1	1.2	1.1	1.0
EBIT/ Avg. CE (RoCE) (%)	38.2	38.0	40.9	36.7	33.8
Avg. CE/Avg. Equity (x)	1.0	1.0	1.0	1.0	1.0
PBT/EBIT (x)	1.0	1.0	1.0	1.0	1.0
PAT/PBT (x)	0.8	0.7	0.7	0.7	0.7
Cons.PAT/PAT (x)	1.0	1.0	1.0	1.0	1.0
PAT/Avg. Equity (RoE) (%)	30.1	27.9	29.1	26.0	24.0

Source: Company, Karvy Institutional Research

Exhibit 7: Key ratios

	FY10	FY11	FY12	FY13E	FY14E
Diluted shares (Nos mn)	574	574	574	574	575
FDEPS (Rs)	108.2	119.0	144.8	156.1	172.3
CEPS (Rs)	124.0	133.9	161.1	175.1	192.8
BV (Rs)	401.7	452.4	542.2	657.3	780.1
P/E (x)	22.2	20.2	16.6	15.4	13.9
P/C (x)	19.4	17.9	14.9	13.7	12.5
P/B (x)	6.0	5.3	4.4	3.7	3.1
EV/Sales (x)	5.6	4.5	3.5	3.0	2.6
EV/EBITDA (x)	16.2	13.7	11.1	9.9	8.2
Net gearing (%)	(62.4)	(59.4)	(64.3)	(69.4)	(72.9)
Working capital T/O (Days)	51.8	61.8	60.6	57.7	56.0
Dividend yield (%)	1.0	2.5	2.0	1.5	1.7

Source: Company, Karvy Institutional Research

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Stock Ratings	Absolute Returns
Buy	> 15%
Hold	5-15%
Sell	< 5%

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