

Infosys Ltd.

ADD

Choice

Cautious outlook for FY24E; Strong order book to drive growth

Infosys Ltd. reported Q2FY24 revenues at \$4,718mn (in-line with our estimates), up 2.3% QoQ and 2.5% YoY in constant currency terms while in USD terms, reported revenue was up 2.2% QoQ and 3.6% YoY. INR revenue for Q2FY24 stood at INR389.9bn, up 2.8% QoQ and 6.7% YoY. Q2FY24 order book stood strong at \$7.7bn, up 185% YoY. PAT for the quarter came at INR62.1bn (+3.2% YoY) with EPS at INR15.01.

- **Conservative revenue guidance for FY24E:** Revenue growth was led Life sciences, Manufacturing and Retail segments with an increase of 18.4%, 12.6% and 9.2% YoY respectively. Among client geographies, Europe's revenue grew by 5.4% YoY, India's by 2.6% in CC terms, and North America's by 1% YoY in CC terms. Since the global market is uncertain, management is unsure of the recovery of demand. The management has cut its revenue guidance to 1-2.5% cc growth for FY24E. Management mentioned that there are constraints in payment, mortgages and investment banking in BFSI vertical. Operating in an environment where digital transformation initiatives and discretionary spending are limited, results in slower decision-making processes, which, in turn, is affecting Infosys's overall business volumes.
- **Robust deal wins and adoption of Topaz:** In Q2, Infosys secured a total of 21 large deals, which included 4 mega-deals. The combined total contract value (TCV) of these large deals amounted to \$7.7bn, with an impressive 48% representing net new business. These deals were distributed across various sectors, with 6 in Retail, 5 in Manufacturing, 4 in Telecom, 3 in Financial services, 2 in Life sciences, and 1 each in Technology and the URS vertical. The adoption of Topaz, a generative AI capability set, is proving to be valuable for the company. Interest in Gen-AI is on the rise, and clients are actively considering Topaz solutions to modernize their enterprises, as well as to refactor, reengineer, and deploy code.
- **Margins to remain range bound:** In Q2, the operating margins reached 21.2%, marking a sequential increase of 40bps, which brings the H1 margins to 21%. The sequential increase in operating margins can be attributed to various factors i.e. 0.5% improvement from cost optimization benefits, which includes high utilization and pricing adjustments; 0.3% boost from one-time revenue events and 0.1% contribution from UP (User Productivity) depreciation. However, these gains were partially offset by a 0.5% increase in costs related to third-party expenses, salaries, and other items. The management has guided for a comfortable operating margin band of 20-22% for FY24E, focusing on cost optimization.
- **Valuation:** Significant large deal wins lay a robust foundation for the company's future growth. The increasing adoption of the Generative AI solution, Topaz, is playing a crucial role in delivering consistent value and expanding market presence. Major deal wins and focus on cost optimization boosts confidence in the long-term growth prospects. We have introduced FY26E and expect Revenue/EBIT/PAT to grow at a CAGR of 6.2%/10.1%/9.7% respectively over FY23-FY26E. We maintain our **ADD** rating with a revised target price of INR1,655 implying a PE of 24x (unchanged) on FY26E EPS of INR76.9.

Financial Snapshot

Year end: March	FY22	FY23	FY24E	FY25E	FY26E
Revenue (USD Mn.)	16,310	18,208	18,824	20,130	21,834
Revenue (INR Mn.)	12,16,410	14,67,670	15,57,036	16,86,499	18,51,235
Gross Profit (INR Mn.)	4,14,000	4,41,120	4,67,881	5,14,631	5,70,256
EBIT (INR Mn.)	2,80,150	3,11,080	3,29,757	3,67,948	4,14,846
EBIT Margin (%)	23.0	21.2	21.2	21.8	22.4
EPS (INR)	52.5	57.6	60.9	68.9	76.9

Source: Company, CEBPL

Oct 13, 2023

CMP (Rs.)	1,465
Target Price (Rs.)	1,655
Potential Upside (%)	13.0

Company Info

BB Code	INFO IN EQUITY
ISIN	INE009A01021
Face Value (Rs.)	5.0
52 Week High (Rs.)	1,672.4
52 Week Low (Rs.)	1,215.4
Mkt Cap (Rs Bn.)	6,078.4
Mkt Cap (\$ Bn.)	73.2
Shares o/s (Mn.)/Float(%)	4,150.1/ 86
FY23 EPS (Rs.)	57.6
FY26E EPS (Rs.)	76.9

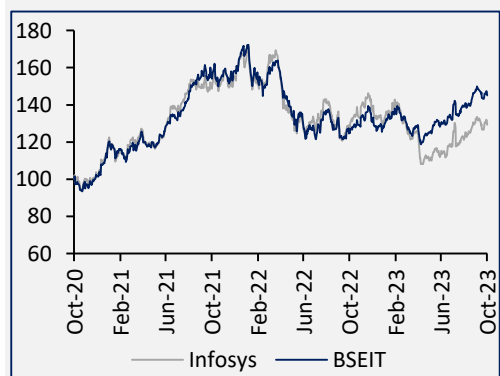
Shareholding Pattern (%)

	Jun-23	Mar-23	Dec-22
Promoters	14.94	15.14	15.11
FII's	33.44	35.09	36.29
DII's	34.58	33.59	32.50
Public	17.04	16.18	16.10

Relative Performance (%)

YTD	3Y	2Y	1Y
BSE IT	45.2	(5.8)	15.7
Infosys	29.3	(13.1)	2.5

Rebased Price Performance



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Sequential Operating Performance

	1QFY23	2QFY23	3QFY23	4QFY23	1QFY24	2QFY24
Income Statement						
Revenues (USD Mn.)	4,444	4,555	4,659	4,554	4,617	4,718
Revenues (INR Mn.)	3,44,700	3,65,380	3,83,180	3,74,410	3,79,330	3,89,940
Gross Profit (INR mn.)	1,01,010	1,11,260	1,17,570	1,11,280	1,13,080	1,17,370
Gross Margin (%)	29.3	30.5	30.7	29.7	29.8	30.1
EBIT (INR mn.)	69,700	79,390	83,220	78,770	78,910	82,740
EBIT Margin (%)	20.2	21.7	21.7	21.0	20.8	21.2
PAT (INR mn.)	53,600	60,210	65,860	61,280	59,450	62,120
Basic EPS (INR)	12.78	14.35	15.71	14.79	14.37	15.01
Operating Metrics						
Revenues - Geography (%)						
North America	61.8	62.5	62.0	61.0	60.8	61.1
Europe	25.0	24.7	25.8	27.0	26.8	26.5
India	2.6	2.9	2.4	2.6	2.7	2.8
ROW	10.6	9.9	9.8	9.4	9.7	9.6
Total	100.0	100.0	100.0	100.0	100.0	100.0
Revenues -Industry (%)						
Financial Services	30.6	30.5	29.3	28.9	28.1	27.5
Retail	14.5	14.2	14.3	14.8	14.5	15.2
Communication	13.0	12.3	12.3	11.8	11.7	11.4
Energy, Utilities, Resources and Services	12.4	12.3	13.0	12.9	12.9	12.7
Manufacturing	12.1	12.8	13.3	13.5	14.1	14.3
Hi Tech	8.2	8.2	8.1	8.0	8.1	7.8
Life Sciences	6.5	6.7	7.0	7.2	7.2	7.8
Others	2.7	3.0	2.7	2.9	3.4	3.3
Total	100.0	100.0	100.0	100.0	100.0	100.0
Employee Metrics						
Total Headcount	3,35,186	3,45,218	3,46,845	3,43,234	3,36,294	3,28,764
Attrition Rate LTM (%)	28.4	27.1	24.3	20.9	17.3	14.6
Utilization - incl trainees (%)	77.6	76.6	77.1	76.9	78.9	80.4
Effort Split (%)						
Onsite	24.3	24.4	24.5	24.6	24.7	24.6
Offshore	75.7	75.6	75.5	75.4	75.3	75.4
Total	100.0	100.0	100.0	100.0	100.0	100.0

Source: Company, CEBPL

CEBPL Estimates vs Actual for Q2FY24

Infosys (INR Mn.)	Q2FY24	Q2FY23	YoY(%)	Q1FY24	QoQ (%)	CEBPL Est.	Dev. (%)
Revenues (\$ mn.)	4,718	4,555	3.6	4,617	2.2	4,671	1.0
Revenues	3,89,940	3,65,380	6.7	3,79,330	2.8	3,83,988	1.6
Employee Cost	2,72,570	2,54,120	7.3	2,66,250	2.4		
Gross Profit (INR mn.)	1,17,370	1,11,260	5.5	1,13,080	3.8	1,14,534	2.5
Gross Margin (%)	30.1	30.5	(35) bps	29.8	29 bps	29.8	27 bps
Other costs	22,970	21,580	6.4	22,440	2.4		
Depreciation	11,660	10,290	13.3	11,730	(0.6)		
EBIT (INR mn.)	82,740	79,390	4.2	78,910	4.9	81,813	1.1
EBIT Margin (%)	21.2	21.7	(51) bps	20.8	42 bps	21.3	(9) bps
Other Income	6,320	5,180	22.0	5,610	12.7		
Interest	1,380	660	109.1	900	53.3		
PBT (INR mn.)	87,680	83,910	4.5	83,620	4.9		
Tax	25,530	23,650	7.9	24,170	5.6		
Adj. PAT (INR mn.)	62,120	60,210	3.2	59,450	4.5	64,387	(3.5)
Basic EPS (INR)	15.0	14.4	4.6	14.4	4.5	15.6	(3.6)

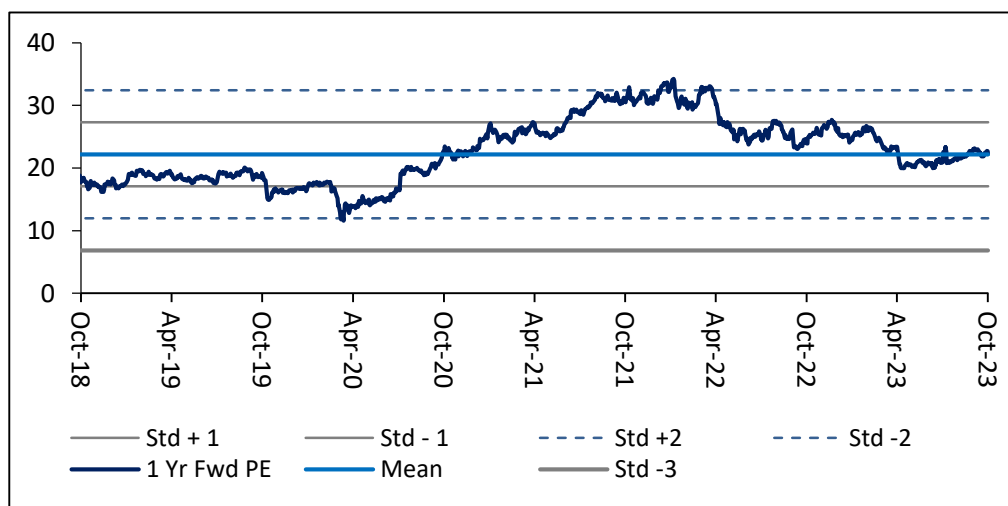
Source: Company, CEBPL

Change in estimates

Income Statement (INR Mn.)	FY24E			FY25E			FY26E
	Old	New	Dev. (%)	Old	New	Dev. (%)	New
Revenues (USD Mn.)	18,824	18,824	(0.0)	20,478	20,130	(1.7)	21,834
Revenues	15,51,288	15,57,036	0.4	17,00,626	16,86,499	(0.8)	18,51,235
Gross Profit Margin (%)	30.0	30.0	4 bps	30.9	30.5	(41) bps	30.8
EBIT	3,30,176	3,29,757	(0.1)	3,73,144	3,67,948	(1.4)	4,14,846
EBIT Margin (%)	21.3	21.2	(11) bps	21.9	21.8	(12) bps	22.4
EPS	61.9	60.9	(1.7)	70.5	68.9	(2.2)	76.9

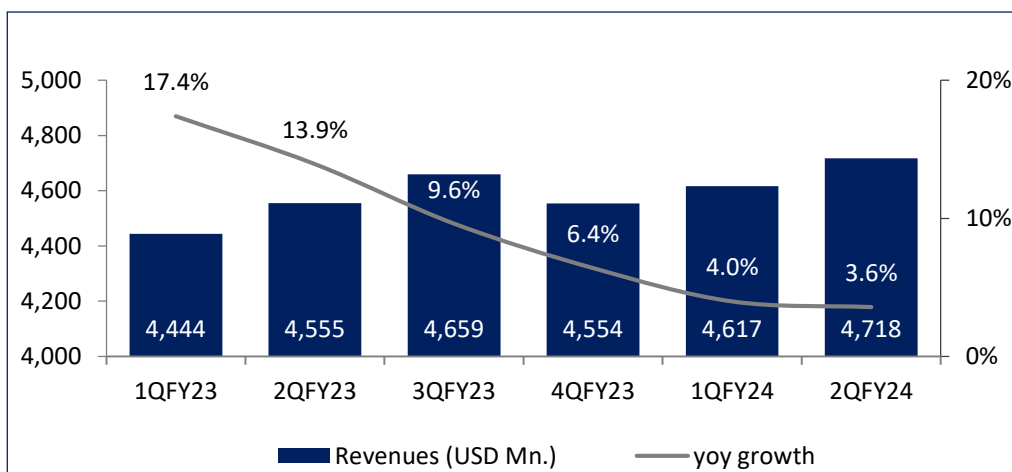
Source: Company, CEBPL

Historical 1 Yr Fwd PE Band



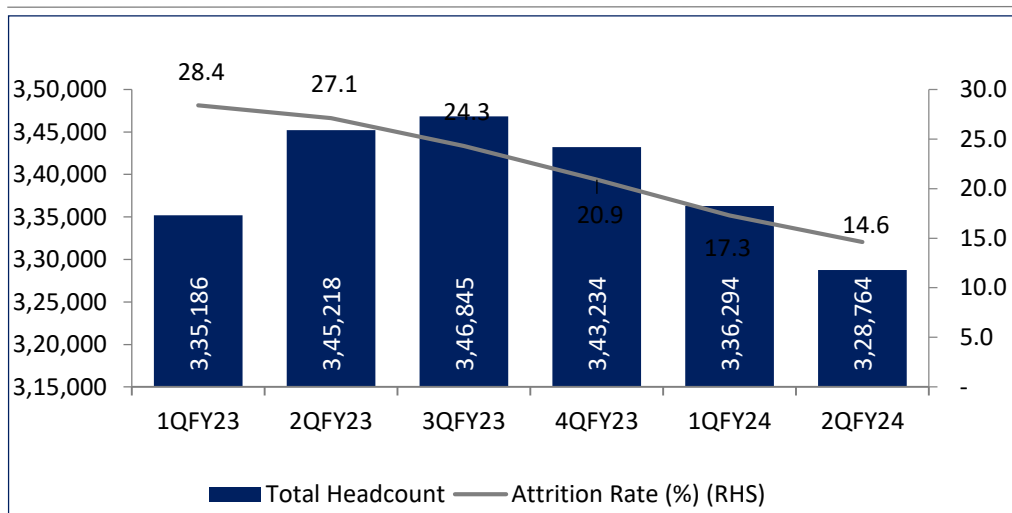
Source: Company, CEBPL

Slower revenue momentum



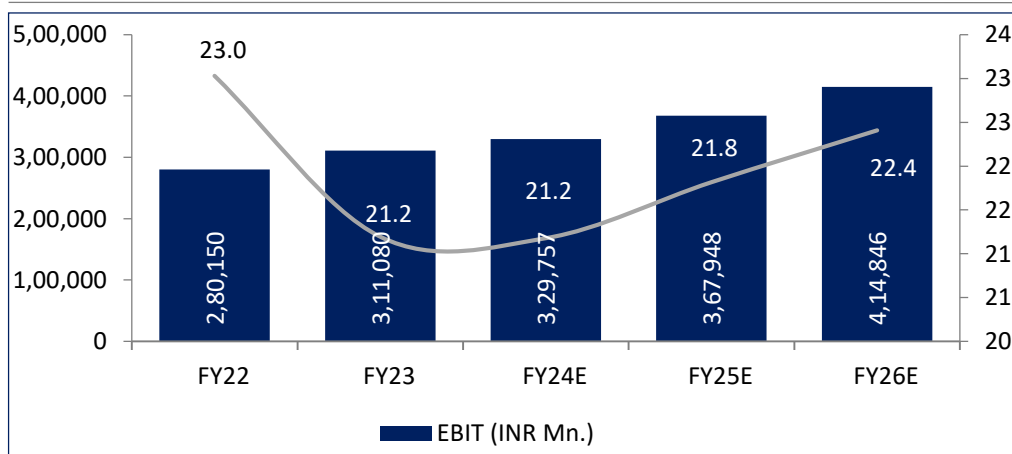
Source: Company, CEBPL

Negative net addition this quarter signaling excess capacity; Attrition is trending lower



Source: Company, CEBPL

Lower utilization levels dragging margins



Source: Company, CEBPL

Management Call - Highlights

- The growth in Q2 was affected by reduced spending from certain major clients. However, this impact was partially mitigated by the implementation of large deals in areas such as cost optimization and vendor consolidation, which contributed positively to our performance.
- During the quarter, the free cash flow was strong, totaling \$670mn, and the conversion of this free cash flow to net profit for Q2 was also strong, with a robust rate of 89%.
- The company maintains a cautious yet optimistic outlook for the medium term. This outlook is influenced by the ongoing shift to cloud technologies, primarily driven by the rising demand for real-time insights and analytics. Challenges persist in the communication sector, compounded by growing operational expenditure (OpEx) pressures and the risk of inflation.
- Infosys' recent agreement with Liberty Global reaffirms its position as a leader in collaborating with clients to deliver substantial cost savings and innovative solutions for transforming their business landscape. Clients in the EURS (Europe, Russia, and CIS) region are currently adopting a conservative approach to discretionary spending, and this trend is expected to persist throughout the year.
- In the energy sector, spending remains cautious due to the economic slowdown, with a strong emphasis on reducing costs and achieving a return on investment (ROI). Utilities, particularly in North America, are feeling the strain of high interest rates, leading to delays in capital-intensive projects.
- The financial services sector continues to face uncertainty, particularly in areas such as mortgages, asset management, investment banking, as well as in cards and payments. These segments are encountering various challenges and fluctuations.
- In the September quarter, the attrition rate decreased to 14.9 percent, while the headcount was reduced by 7,530 employees. The total headcount in Q2FY24 is now 3,28,764, compared to 3,36,294 in the previous quarter.
- Infosys has recently introduced the Infosys Cobalt Airline Cloud (ICAC), a groundbreaking industry-specific cloud solution tailored for commercial airlines. This innovative offering is designed to facilitate and expedite the digital transformation efforts of airline companies.
- Infosys announced an interim dividend of ₹18 per equity share during the declaration of its September quarter results. They have set October 25 as the record date, and the dividend is scheduled to be paid out on November 6.

Financial Summary (Consolidated in INR Mn.)

Income Statement (INR Mn.)	FY22	FY23	FY24E	FY25E	FY26E
Revenue (USD Mn.)	16,310	18,208	18,824	20,130	21,834
Revenue	12,16,410	14,67,670	15,57,036	16,86,499	18,51,235
Gross profit	4,14,000	4,41,120	4,67,881	5,14,631	5,70,256
EBITDA	3,14,920	3,53,330	3,76,780	4,18,543	4,70,383
Depreciation	34,770	42,250	47,023	50,595	55,537
EBIT	2,80,150	3,11,080	3,29,757	3,67,948	4,14,846
Other income	22,950	24,980	24,929	28,452	27,378
Interest expense	2,000	2,840	4,643	5,059	5,554
Reported PAT	2,21,110	2,40,950	2,51,902	2,85,349	3,18,402
EPS	52.5	57.6	60.9	68.9	76.9

Balance Sheet (INR Mn.)	FY22	FY23	FY24E	FY25E	FY26E
Tangible fixed assets	1,83,140	2,05,160	2,79,145	3,37,924	3,85,039
Goodwill & intangible assets	79,020	89,970	89,970	89,970	89,970
Investments	2,03,240	2,23,150	2,38,556	2,63,976	2,93,209
Cash & Cash equivalents	1,74,720	1,21,730	1,61,341	1,92,346	2,19,016
Other non-current assets	1,08,330	1,00,160	1,00,160	1,00,160	1,00,160
Other current assets	4,30,400	5,17,990	5,12,876	5,16,725	5,41,435
Total assets	11,78,850	12,58,160	13,82,048	15,01,101	16,28,830
Shareholder's funds	7,53,500	7,54,070	8,55,011	9,69,481	10,97,209
Minority interest	3,860	3,880	3,880	3,880	3,880
Borrowings	54,740	82,990	82,990	82,990	82,990
Other non-current liabilities	39,440	37,780	37,780	37,780	37,780
Other current liabilities	3,27,310	3,79,440	4,02,386	4,06,971	4,06,971
Total equity & liabilities	11,78,850	12,58,160	13,82,048	15,01,101	16,28,830

Cash Flows (INR Mn.)	FY22	FY23	FY24E	FY25E	FY26E
Cash flows from Operations	3,14,970	3,12,610	3,06,880	3,13,616	3,27,772
Cash flows from Investing	(64,160)	(12,090)	(93,260)	(98,316)	(89,501)
Cash flows from financing	(2,46,420)	(2,66,950)	(40,073)	(22,418)	(42,744)

Ratio Analysis	FY22	FY23	FY24E	FY25E	FY26E
Growth Ratios (%)					
Revenues	21.1	20.7	6.1	8.3	9.8
Gross Profit	18.1	6.6	6.1	10.0	10.8
EBITDA	12.9	12.2	6.6	11.1	12.4
EBIT	13.8	11.0	6.0	11.6	12.7
Margin Ratios (%)					
Gross Profit Margin	34.0	30.1	30.0	30.5	30.8
EBITDA Margin	25.9	24.1	24.2	24.8	25.4
EBIT Margin	23.0	21.2	21.2	21.8	22.4
Profitability (%)					
Return on equity	28.8	31.8	33.3	33.3	32.7
Return on invested capital	34.5	36.8	34.0	34.1	34.2
Return on capital employed	25.6	27.2	25.5	25.7	25.8
Valuation					
OCF / Net profit (%)	108.0	93.2	82.9	72.9	65.9
EV / EBITDA (x)	19.7	17.5	16.6	14.9	13.1
Book Value per share (x)	179.0	180.4	206.6	234.3	265.1
Free Cash flow yield (%)	4.6	4.9	3.4	3.8	4.2

Source: Company, CEBPL

Historical recommendations and target price: Infosys Limited



Infosys Ltd.

1.	16-01-2022	Add,	Target Price 1,513
2.	25-04-2022	Add,	Target Price 1,243
3.	13-07-2022	Outperform,	Target Price 1,257
4.	13-10-2022	Outperform,	Target Price 1,238
5.	10-01-2023	Add,	Target Price 1,207
6.	21-04-2023	Outperform,	Target Price 1,670
7.	21-07-2023	Add,	Target Price 1,570
8.	25-09-2023	Add,	Target Price 1,690
9.	13-10-2023	Add,	Target Price 1,655

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ADD	The security is expected to generate greater than 5% to less than 15% returns over the next 12 months
NEUTRAL	The security expected to show downside or upside returns by 5% over the next 12 months
REDUCE	The security expected to show less than -5% to greater than -15% over the next 12 months
UNDERPERFORM	The security is expected to generate returns in excess of -15% over the next 12 months

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