

Established in 1981, Infosys Ltd. is amongst the global leaders in consulting, technology, and outsourcing and next-generation services. It has market offerings spanning across more than 50 countries and 20+ industries. As in March 2015, the company had revenues worth ₹53,319 crore. It has a workforce of 176,000+ people. Globally, it has ~85 sales and marketing offices and 100 development centers.

Investment Rationale

☞ Riding high on reprioritisation to reclaim bellwether status

Banking upon the structural and cultural transformations that Infosys Ltd. (Infosys) is undergoing, it has reiterated its pledge to regain its bellwether status by FY19. In order to achieve this, the company has resorted to a 'Renew & New' strategy whereby CEO Vishal Sikka is preparing the company to set pace with its peers in the continually varying global IT software services space. Under this new combat methodology; Infosys is focusing on transitioning its current resources to adapt to technological changes and also adding onto the exclusivity of its services via acquisitions, training programs and need based talent acquisition. Owing to this, we expect revenue of the company to grow at a CAGR of ~9% during FY15-17E.

☞ Infosys' focus on acquisitions paves way for exclusive service offerings

Infosys is stressing on aggressive acquisitions to help its clients bring new digital experiences to their customers through IP-led technology offerings, new automation tools and unparalleled skill & expertise in these new emerging areas. This will help Infosys to stay competitive in market.

☞ Improving headcount provide high revenue visibility

Over last five years, Infosys' realisations have grown from ₹0.26 per employee to ₹0.37 per employee registering a CAGR of 9.4% as the headcount has registered 7.7% CAGR over FY11-FY15 even as the utilisation has declined. As per the recent pace of growth, we estimate the head counts to reach 189,987 in FY16E from the current levels of 176,187 henceforth translating into higher revenue even if we estimate the realisations to remain at the level of ₹0.38.

☞ Repeat clients: Vital for revenue growth

The company owes a huge chunk of its revenue to its repeat clients. Over last five years this has been varying between 95-98%. Its legacy clients have been with the company for more than 15 years. Moreover, its top 15 clients account for ~1/4th of the total business. Hence, retaining clients is an important factor in determining the company's revenue growth.

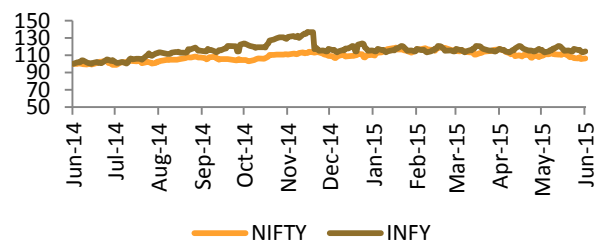
Market Data

Rating	BUY
CMP (₹)	995
Target (₹)	1,167
Potential Upside	~17%
Duration	Long Term
Face Value (₹)	5.0
52 week H/L (₹)	1,167/792.2
Adj. all time High (₹)	1,168
Decline from 52WH (%)	14.7
Rise from 52WL (%)	25.6
Beta	0.8
Mkt. Cap (₹cr)	2,27,656.0
EV (₹cr)	1,97,289.0

Fiscal Year Ended

Y/E	FY14A	FY15A	FY16E	FY17E
Revenue (₹cr)	50,133.0	53,319.0	58,297.5	63,740.9
EBITDA (₹cr)	13,378.0	14,849.0	16,059.6	17,362.2
Net Profit (₹cr)	10,648.0	12,330.0	13,731.5	15,273.6
EPS (₹)	186.2	107.8	60.0	66.8
P/E (x)	5.3	9.2	16.6	14.9
P/BV (x)	1.2	2.1	3.9	3.6
EV/EBITDA (x)	15.1	13.3	11.4	10.5
ROCE (%)	30.7	31.4	32.5	33.4
ROE (%)	22.4	22.5	23.3	24.1

One year relative price chart



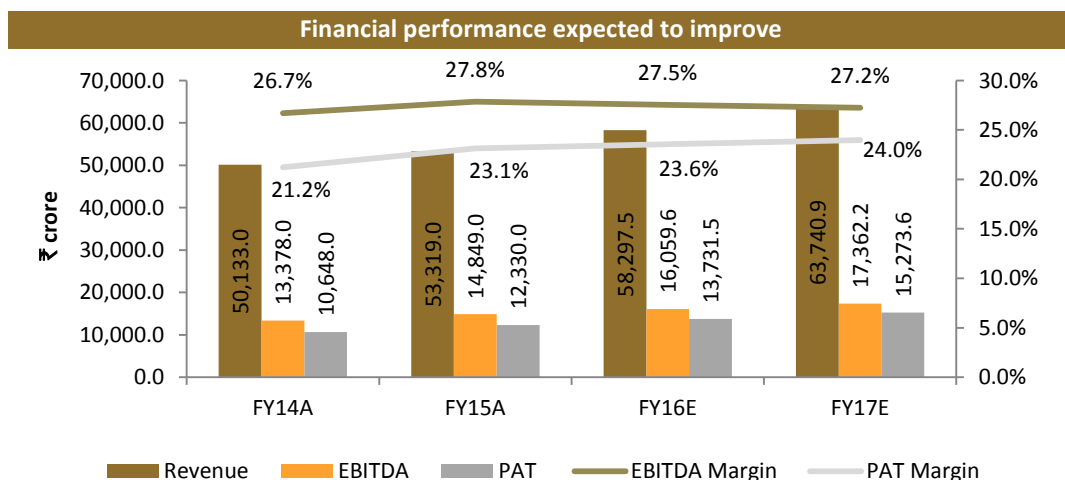
Shareholding Pattern	Mar 15	Dec14	Diff.
Promoters	13.1	13.1	0.0
FII	38.0	41.6	(3.6)
DII	15.1	15.3	(0.2)
Others	33.9	30.1	3.8

Infosys Ltd. enjoys the stature of a global leader in consulting, technology, and outsourcing and next-generation services.

Infosys: Striving to attain its bellwether status

Established in 1981, Infosys Ltd. is amongst the global leaders in consulting, technology, and outsourcing and next-generation services. It has market offerings spanning across more than 50 countries and 20+ industries. As in March 2015, the company had revenues worth ₹53,319 crore. It has a workforce of 176,000+ people. Globally, it has ~85 sales and marketing offices and 100 development centers. Infosys' major services include Application Management, Application Outsourcing, Business Applications, Business Process Outsourcing, Cloud, Digital, Engineering, Infrastructure Management, Management Consulting, Enterprise Mobility and Testing. Infosys provides enterprises with strategic insights on what lies ahead. It aids enterprises transform and thrive in a changing world through strategic consulting and the co-creation of breakthrough solutions, including those in mobility, sustainability, big data and cloud computing.

In the near future, the company's goal is to split its revenue streams more equally. This requires growth in the area of innovation in particular cloud computing and the proposed Intellectual Property Management System (IPMS) to safeguard intellectual assets and mitigate risks of Intellectual Property Rights violation. As a part of its US\$ 20-bn by 2020 target, Infosys wants about US\$16.5 bn of its revenue to be generated from its primary outsourcing business, US\$2 bn from newer services such as analytics and cloud, and US\$1.5 bn from acquisitions.



'Renew & New': Infosys' innovative mantra

With Vishal Sikka's arrival on board, the company has resorted to an evolving business model of 'Renew & New' to stand out of competition. The company's 'Renew & New' strategy is based on harnessing existing technologies and leveraging on analytics and next-gen technologies such as Artificial Intelligence and cloud computing in order to make services more accessible, approachable and reliable.

Under the process so far, the company has embarked on training of 12,300 employees in the design thinking discipline; conducted a 21-day training programme on artificial intelligence by Stuart Russell, a computer science professor at Berkley University and 1,200 people have been trained; besides, it acquired Panaya and Skava to help clients bring new digital experiences to their customers through IP-led technology offerings, new automation tools and unparalleled expertise in these areas.

Infosys' dual strategy 'Renew & New' emphasises upon increasing the competitiveness of its service lines by leveraging automation, machine learning and artificial intelligence.

Company's efficiency in maintaining and attaining clients aids the revenue growth.

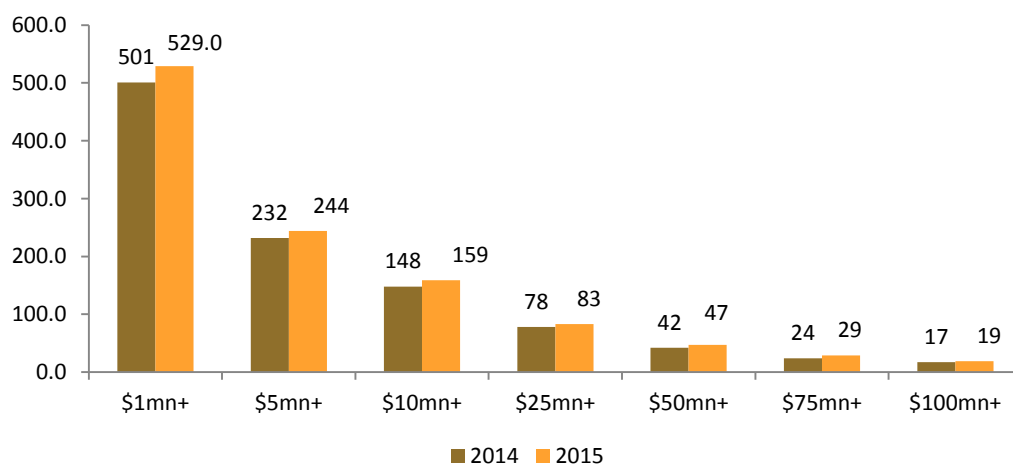
Moreover, the company has re-shuffled the top-management roping in executives to address area-specific concerns; it has identified 100 senior consulting partners, to be made co-leads for monitoring top 200 accounts. The CEO himself has identified the top 15 crucial accounts to manage personally. The company is sprucing up the capabilities of its core banking software Finacle in order to facilitate transactions using mobile banking and digital currencies like Bitcoin and Ripple.

Banking upon the aforementioned actions, the company has set forth a challenging target of US\$20 bn revenue by 2020 and the management anticipates that about US\$16.5 bn would come from renewing the existing business, a result of design thinking, innovation culture and zero distance coming into every project. **We believe that in a highly capricious and demanding tech industry, various aspects of the demand-supply scenario boil down to a single phenomenon that is addressing the need based behavior of the customers with pre-emptive models. However, for the benefits from the transitional process to materialise in a pecuniary form, the company's revenues must grow at ~10% FY16 onwards.**

Transitioning client matrix to aid growth

Over FY10-15, the company has seen a CAGR of 11.8% in its new client base growing from 338 to 529. It has witnessed a CAGR of ~16% in its client base contributing over US\$ 100 mn of revenues and 12.5% and 12.1% in its client base contributing over US\$ 50 mn and US\$ 10 mn respectively. At the end of FY15 the total active clients with Infosys were 950 which is ~11% CAGR from FY10. In Q4FY15 alone, the company added 52 accounts, taking the total accounts addition to 221 in FY15. The company derived 97.8% of its business from its repeat businesses alone. **We believe that company's efficiency in retaining and attaining clients will further aid its revenue growth by revitalizing its utilisation levels.**

Category-wise client base count



Q4FY15 revenues affected adversely due to cross currency headwinds

Infosys delivered subdued numbers on a sequential basis while recovering in its performance on a YoY basis in Q4FY15. The company reported a consolidated top-line of ₹13,411 crore, declining 2.8% QoQ, while it grew by 4.2% YoY. The decline in revenue sequentially was mainly due to cross currency headwinds impacting the pricing scenario. Onsite pricing declined by 2.5% QoQ, while offshore pricing fell by 4.1% QoQ.

Infosys delivered subdued numbers on sequential basis, while recovering its performance on a YoY basis in Q4FY15. The top-line was reported at ₹13,411 crore, declining 2.8% QoQ while grew by 4.2% YoY.

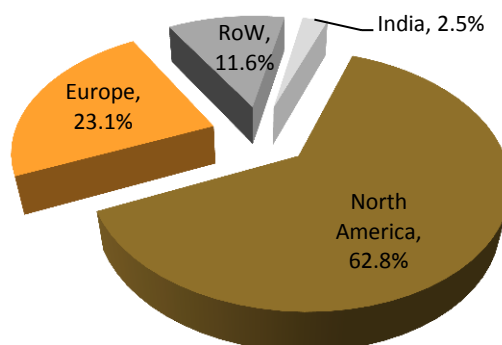
Volume growth stood at 0.8% QoQ with onsite volumes up 2.1% QoQ and offshore volumes up by 0.4% QoQ. Utilization levels de-grew 290 bps QoQ & 10 bps YoY to 72.8%. The management is however confident of sustaining the utilisation levels at 80-83% levels.

Geographically, the company posted decline in revenue from across the segments. Revenues from North America, Europe, India and RoW declined 0.7% QoQ, 6.1% QoQ, 4.1% QoQ and 5.7% QoQ respectively.

As per the service offerings, revenue from Application development de-grew 6.6% QoQ, registering the second consecutive quarter of decline, while, application maintenance revenue declined 1.7% QoQ, testing services was down 4.8% QoQ, infrastructure management services was lower by 3.8% QoQ, business process management fell by 4.5% QoQ, which offset the growth in revenue from products, platforms & solutions by 5.8% QoQ. Meanwhile, pricing pressures in infrastructure management-oriented, rebid deals have intensified.

The EBITDA of the company declined by 6.5% sequentially reported at ₹3,449 crore due to lower utilisation rate (decreasing 290 bps QoQ) and higher SG&A expenses (increasing 8.7% QoQ). As a result, the consolidated PAT decreased by 4.7% on QoQ basis to ₹3,097 crore as operating profits declined and the effective tax rate increased from 28% to 28.5%.

Geography-wise revenue contribution



FY15 numbers: Tad short of management guidance

Infosys logged out of FY15 with a rather disappointing growth of 6.4% in its consolidated top-line against the management's guidance of ~8% growth. The shortfall in achieving the growth rate was primarily due to decline of 10% in software product revenues (contributing ~3.5% to the total revenue) largely due to challenges associated with its product Finacle, its core banking software. The software product revenues of Infosys stood at ₹1,653 crore in FY15 as against ₹1,828 crore in FY14, revealing a decline of 9.5%. Other drags during the year were pricing pressure, slow spend in key verticals like energy and telecom and delays in project implementation. On the margins front, the company registered 120 bps increase in its EBITDA margin with EBITDA growing 11% in FY15 at ₹14,849 crore. In line with better operational performance coupled with lower depreciation and higher other income pushed the bottom-line, which grew by 15.8% and stood at ₹12,329 crore.

Going forward, the company has set forth revenue growth guidance at 6.2-8.2% in the dollar terms (10-12% in the constant currency terms). We believe that the management's strategy of streamlining the existing processes and inducing structural changes to explore newer areas of growth will affect the top-line positively. As per our estimates, the revenue growth can be anywhere between 9%-9.5% by FY16E.

The company has set forth revenue growth guidance at 6.2-8.2% in the dollar terms (10-12% in the constant currency terms) for FY16E.

Infosys is trying to bring about exclusivity in its service offerings via acquisitions and providing incubation to start-ups.

Increasing headcount: key to improving revenue

On a consolidated basis, the headcount for the company increased to 176,187 in FY15 from 160,405 in FY14. Owing to this the utilisation levels (excluding trainees) of the company increased from 77.4% in FY14 to 80.6% in FY15. According to the management, higher utilisation level is a key driver for the company's margin expansion as it indicates higher realised revenue per employee and could stay in the range of 80-83%. However for Infosys the realisations have grown even as the utilisation levels have shown huge fluctuations. Over last five years, the realisations have grown from ₹0.26 per employee to ₹0.37 per employee registering a CAGR of 9.4% as the headcount has registered 7.7% CAGR over FY11-FY15. And going by this growth rate we believe that the company will be able to increase its revenue even if the realisation levels hover around ₹0.38 level.

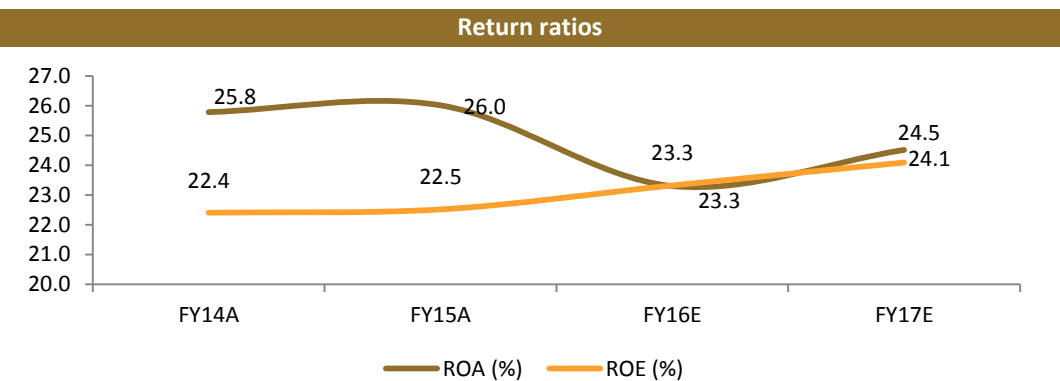
Acquisitions and funding start-ups pave way for exclusive service offerings

In Q4FY15, Infosys acquired automation technology firm Panaya. This is focused to strengthen the company's dual strategy of 'Renew and New' by increasing the competitiveness of its current service lines by leveraging automation, machine learning and artificial intelligence. Further, in early Q1FY16, it took-over Skava to help its clients bring new digital experiences to their customers through IP-led technology offerings, new automation tools and unparalleled skill and expertise in these new emerging areas.

Moreover, the company recently set up a fund to aid start-ups so that it can pick up innovative ideas and bring them to a mass scale. It entered into an agreement to invest US\$2 mn in Airviz, to acquire a minority stake. Airviz is a personal air quality monitoring startup and spin-off from Carnegie Mellon University. This investment will be made from the US\$500-mn innovation fund that the company had set up for investing in new technologies. We believe that the aforementioned actions will strengthen Infosys' competitive position. The company intends to achieve US\$1.5 bn of revenue via acquisition route as a part of its 'Five Year Vision'.

Key risks

- Currency fluctuations adversely affect the revenues generated outside India
- Client concentration is a major concern of the company as a small chunk of clients contributes significantly to the revenue
- Any unsuccessful acquisition or strategic investments that do not fructify can pose risk for the company
- Wage pressure and acquiring talent outside India can curb margins



Balance Sheet (Consolidated)

Y/E (₹cr)	FY14A	FY15A	FY16E	FY17E
Share Capital	286.0	572.0	1,144.0	1,144.0
Reserve and surplus	47,244.0	54,763.0	57,740.9	62,261.0
Net Worth	47,530.0	54,763.0	58,884.9	63,405.0
Other Long term Liabilities	323.0	46.0	44.1	42.3
Deferred tax liabilities	64.0	160.0	291.4	530.8
Current Liabilities	9,138.0	11,383.0	23,324.7	23,289.7
Total Equity & Liabilities	57,055.0	66,352.0	82,545.2	87,267.8
Fixed Assets	8,229.0	9,763.0	9,402.0	9,054.3
Long term loans and advances	2,157.0	3,091.0	3,252.0	3,421.4
Deferred Tax Assets	656.0	537.0	595.3	660.0
Non- Current Investments	1,252.0	1,438.0	1,438.0	1,438.0
Other non-current assets	1,742.0	4,327.0	5,109.6	6,033.8
Current Assets	43,019.0	47,196.0	62,748.2	66,660.2
Total Assets	57,055.0	66,352.0	82,545.2	87,267.8

Profit & Loss Account (Consolidated)

Y/E (₹cr)	FY14A	FY15A	FY16E	FY17E
Net Sales	50,133.0	53,319.0	58,297.5	63,740.9
Cost of Goods sold	30,804.0	31,866.0	34,841.4	38,094.6
Gross Profit	19,329.0	21,453.0	23,456.1	25,646.3
Expenses	5,951.0	6,604.0	7,396.5	8,284.1
EBITDA	13,378.0	14,849.0	16,059.6	17,362.2
Other Income	2,669.0	3,427.0	4,112.4	4,934.9
Depreciation	1,337.0	1,017.0	940.2	905.4
EBIT	14,710.0	17,259.0	19,231.8	21,391.7
Profit Before Tax	14,710.0	17,259.0	19,231.8	21,391.7
Tax	4,062.0	4,929.0	5,500.3	6,118.0
Share of associates	0.0	(1.0)	0.0	0.0
Net Profit	10,648.0	12,330.0	13,731.5	15,273.6

Key Ratios (Consolidated)

Y/E	FY14A	FY15A	FY16E	FY17E
EBITDA Margin (%)	26.7	27.8	27.5	27.2
EBIT Margin (%)	29.3	32.4	82.0	83.4
NPM (%)	21.2	23.1	23.6	24.0
ROCE (%)	30.7	31.4	32.5	33.4
ROE (%)	22.4	22.5	23.3	24.1
EPS (₹)	186.2	107.8	60.0	66.8
P/E (x)	5.3	9.2	16.6	14.9
BVPS (₹)	830.9	478.7	257.4	277.1
P/BVPS (x)	1.2	2.1	3.9	3.6
EV/Net Sales (x)	4.0	3.7	3.2	2.9
EV/EBITDA (x)	15.1	13.3	11.4	10.5

Valuation and view

Infosys intends to gain its status as the bellwether stock in coming few years. It has set forth a 'Five Year Vision' of reaching revenues worth US\$ 20 bn by 2020. To retain the confidence of the investors in its earnings visibility, the company is focusing on transforming its legacy business model to segmented and more specific model assigning need based solutions applying cloud computing, artificial intelligence and leveraging on capacities arising from exclusivity of new and old companies via funding and acquisitions. We expect the company's effort to provide it an edge against competition.

At a current market price (CMP) of ₹995, the stock trades at a P/E of 16.6x FY16E and 14.9x FY17E. We recommend 'BUY' with a target price of ₹1,167, which implies potential upside of ~17% to the CMP from long term perspective.

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Contact Us:

Funds India

H.M Center, Second Floor, 29,
Nungambakkam High Road, Nungambakkam,
Chennai - 600 034.

T: +91 7667 166 166

Email: contact@fundsindia.com