

BSE Code: 500209

NSE Code: INFY

Reuters Code: INFY.NS

Bloomberg Code: INFO:IN

Innovation & automation to drive growth

Infosys is a global leader in consulting, technology, outsourcing and next-generation services, with a strong workforce of more than 194,000 employees. Infosys has a diversified geographical presence (in more than 50 countries) with 100 development centers located across India, APAC, the Americas & Europe.

Investment Rationale

☞ Traction in large deal wins; a confidence booster: Sustained momentum in client mining and large deal wins bolsters our confidence on the revenue visibility of the company. Infosys continues to witness momentum in large deal wins with the company witnessing 45% YoY increase in its total contract value (TCV) to USD 2.79 bn in FY16 when compared to USD 1.93 bn in FY15. Further, the company is investing heavily on business development and marketing to acquire new clients and mining its existing clients. This is clearly visible from continuous increase in its client base (CAGR of ~12% over FY11-16). We believe the company's deeper client penetration strategy and focus on creating industry specific solutions & platforms, development of IP led technologies and wide geographical footprint will provide further lever for growth.

☞ Focus on operational efficiency and productivity to offset pricing pressure: Owing to cost pressures there is structural shift towards digital technologies and automation in its traditionally manual areas of business. In order to offset the impact of pricing pressure, Infosys is bringing in operational efficiencies and productivity improvement and artificial intelligence especially in higher-end projects. The higher adoption of digital technology will enhance its pricing and thus aid in margin improvement. This will also provide scalability to its business.

☞ Strong balance sheet with healthy return ratios: Infosys has a strong balance sheet, resilient earnings and healthy cash & cash equivalent of Rs. 34,468 crores (as on 31st March 2016). With healthy operating cash flows and zero debt on its books, we expect the return ratios to stay healthy going forward. We expect ROE & ROCE to remain sturdy at 25.0% and 35.2% in FY18E. The free cashflows of the company is expected to increase to Rs. 10,815 Crores in FY18E. The company has good dividend track record with dividend payout (excluding special dividend) averaging more than 30% over the last 5 years, reflecting its efficient articulation of capital allocation philosophy.

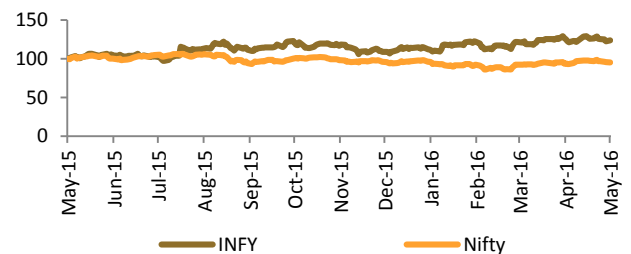
Valuation: Strong deal pipeline coupled with traction in large deal wins, focus on digitisation and automation would help Infosys to lead industry growth and would act as a margin lever ahead. We expect revenue and Adj. PAT to grow at a CAGR of 14.6% and 13.3% over FY16-18E. We initiate coverage on the stock with a BUY rating with a target price of Rs. 1,305 (FY18E P/E of 17x), implies a potential upside of 11% over the next 1 year.

Market Data

Rating	BUY
CMP (Rs.)	1,181
Target (Rs.)	1,305
Potential Upside	11%
Duration	Long Term
Face Value (Rs.)	5
52 week H/L (Rs.)	1,267.9/932.6
Adj. all time High (Rs.)	1,267.9
Decline from 52WH (%)	6.8
Rise from 52WL (%)	26.6
Beta	0.9
Mkt. Cap (Rs.Cr)	270,213

Fiscal Year Ended

Y/E	FY15	FY16	FY17E	FY18E
Revenue (Rs.Cr)	53,319	62,441	71,163	82,054
Adj. Net profit (Rs.Cr)	12,372	13,678	15,101	17,570
Adj. EPS (Rs.)	108.1	59.8	66.0	76.8
Adj. P/E (x)	21.8	19.8	17.9	15.4
P/BV (x)	5.3	4.7	4.1	3.6
ROE (%)	26.0	25.2	24.5	25.0

One year Price Chart

Shareholding Pattern

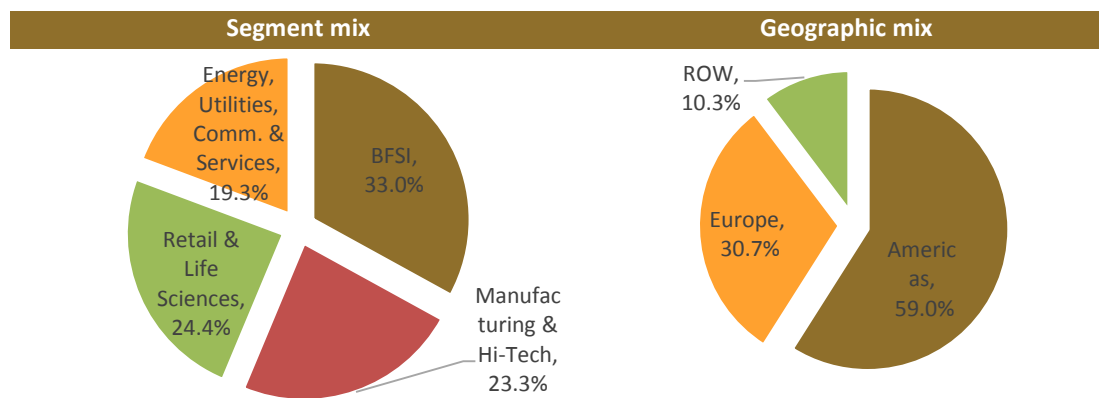
	Mar-16	Dec-15	Chg.
Promoters (%)	12.7	13.1	(0.4)
Public (%)	86.8	86.4	0.4
Others (%)	0.5	-	-

Infosys is India's second largest IT company, with a workforce of more than 194,000 employees.

NASSCOM expects Indian IT industry revenue to grow at a CAGR of 9.1% to touch USD 350 billion in 2025 (USD 300 bn by 2020).

Infosys Ltd: Business overview

Infosys is a global leader in consulting, technology, outsourcing and next-generation services. It provides services across application management, application outsourcing, business applications, business process outsourcing, cloud, digital, engineering, infrastructure management, management consulting, enterprise mobility, among others. The company caters to various industry segments that primarily include Financial Services and Insurance (FSI), Manufacturing (MFG), Energy & Utilities, Communication & Services (ECS), Retail, Consumer packaged goods & Logistics (RCL) and Life Sciences & Healthcare (LSH). Infosys has a diversified geographical presence with 100 development centers spread across India, APAC, the Americas & Europe, and servicing clients in more than 50 countries, thus de-risking its geographic presence. It has a strong workforce of more than 194,000 employees.



Source: Company, In-house research

Strong growth opportunities in IT sector bodes well for Infosys

Indian IT industry is now witnessing a significant shift from the earlier landscape of simple maintenance providers to full service players. Indian IT sector has grown at a CAGR of ~14% over FY11-15, of which revenue from exports witnessed a CAGR of 36%, while, the domestic revenue witnessed a negative CAGR of ~5%. National Association of Software and Services Companies (NASSCOM) expects Indian IT industry revenue to grow at a CAGR of 9.1% to touch USD 350 billion in 2025 (USD 300 bn by 2020). The growth will be driven by global digital disruption due to rise of SMAC (social, mobility, analytics, cloud), the Internet of Things (IoT) and robotics, among others. The growth in the domestic market for the IT sector will be driven by e-commerce growth, government initiatives like 'Digital India' and 'Make in India' programs (a USD 26 bn opportunity) and technology adoption by industries. Uptick in demand from the US will be a key driver for IT industry's software exports revenue growth. With Infosys having strong product domain knowledge and execution capabilities, we believe it is well placed to capitalise on strong growth opportunities for the company going ahead.

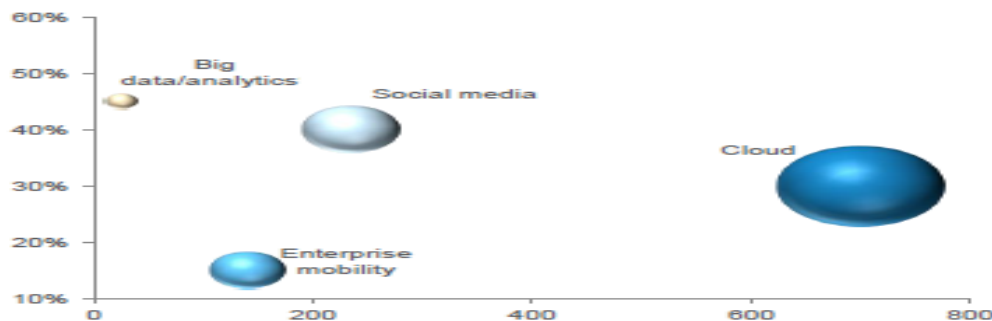
NASSCOM estimates SMAC revenues to account for c.20% of the total revenue of Indian IT companies in 2020, from current levels of less than 5%.

Banking big on digital

The growth of the IT companies will be driven by digital and new disruptive technologies like social, mobility, analytics and cloud (SMAC). NASSCOM estimates SMAC revenues to account for c.20% of the total revenue of Indian IT companies in 2020, from current levels of less than 5%. Infosys has already sensed the opportunity in this space and has made strong inroads into SMAC and digital transformation through inorganic route. In early FY16, Infosys acquired Kallidus Inc. (doing business as Skava). The acquisition of Skava helped the company to deliver new digital retail shopping experience to its large retail clients. The acquisition of Panaya enabled the company to provide higher-margin automation solutions to its clients. Further, to gain an edge in the digital space, the company will continue to invest in emerging mobile and digital technologies and big data analytics. This strategic move will aid the company in building strong relationship with clients and enhance its customer engagement. Besides, on the domestic market front, India's government focus on digital India initiative throws a rich opportunity for the IT players.

As Infosys is building strong capabilities in digital technology space across industries, we believe this move would augur well for the company. Besides, the company is betting big on funding start-ups which are focused on new-age technologies. Infosys has spent ~USD 29 million from its USD 500 million innovation fund that the company had set up for investing in new technologies. We believe the company's investments on newer technologies would help broaden its clients base as well as provides boost to its revenue.

SMAC leading the growth trend (USD bn)



Source: NASSCOM

Build deep and impactful client relationship

Infosys' client centric approach and high level of execution excellence continues to provide a high level of client satisfaction. This is clearly visible from its repeat business which is generating ~97% of its revenue. Infosys along with its subsidiaries have added 325 new clients in FY16, taking the total client base to 1,092 at the end of FY16. Further, to augment revenue share from existing clients, Infosys has outlined a strategy to engage with its clients on their large transformative programs, both in traditional IT areas as well as their new digital business initiatives. Further, it is broadening the set of end-to-end service offerings for its clients. Apart from mining its existing clients, the company is investing heavily on business development and marketing to acquire new clients.

The client addition remained robust as the company has added 325 new clients in FY16, taking the total client base to 1,092.

This is clearly visible from continuous increase in its client base (CAGR of ~12% over FY11-16). We believe the company's deeper client penetration strategy and focus on creating industry specific solutions & platforms, development of IP led technologies and wide geographical footprint will provide further lever for growth.

Clients matrix			
Clients	2014	2015	2016
1 mn dollar+	501	529	558
5 mn dollar+	232	244	268
10 mn dollar+	148	159	177
25 mn dollar+	78	83	88
50 mn dollar+	42	47	52
75 mn dollar+	24	29	31
100 mn dollar+	13	15	14
200 mn dollar+	3	4	6
300 mn dollar+	1	-	1

Source: Company, In-house research

Increased focus on automation to provide next leg of growth

The company has embarked on a strategy of increasing its emphasis on automation to improve productivity and reduce costs. Infosys has created a service differentiation platform named "Infosys Platform" which consists of Infosys Information Platform (IIP) and Infosys Automation Platform (IAP). These platforms are gaining fast traction with its clients as post the launch the company already having more than 220 engagements with IIP and 125+ engagements with IAP, post the launch of the platforms. Further, the acquisition of Panaya is enhancing its automation capabilities in packaged software offerings. The adoption of automation is yielding benefits with the company saving ~3,900 people's effort in FY16. With the company's focus on expanding the scope of automation through the implementation of L3 service offerings from L1 currently, we believe it would further improve operational efficiency. With the adoption of automation, the company is looking at 10-35% in cost savings. Besides, the company would utilize these savings to innovate and develop next-generation technologies. The company's Zero Distance programme is also driving innovation across projects as currently it has more than 8,000 Zero distance projects. The company's focus on automation and innovation will drive differentiation and provide company with a competitive moat.

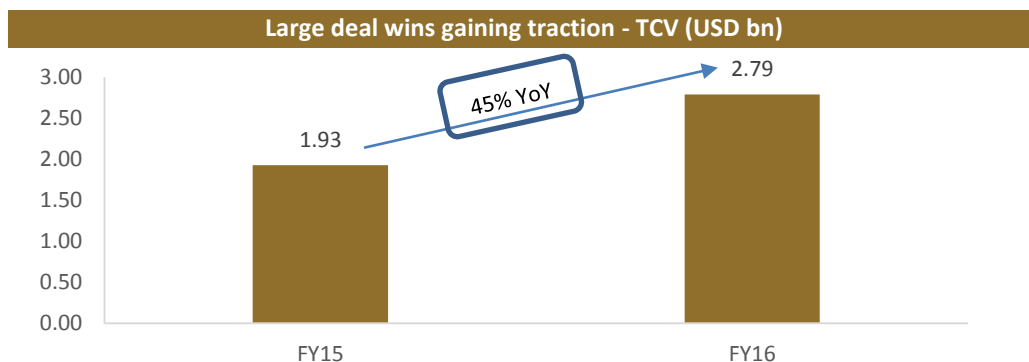
Strive to regain bellwether status

Infosys revenue has grown at a CAGR of ~18% over FY11-16. The management reiterated its strategy of achieving USD 20 bn in revenues with at least 30% operating margin by 2020 driven by its large deal pipeline coupled with continued client mining efforts and benefits accruing from realignment of organizational structure undertaken by the company in the recent past (to increase focus on expanding client relationships and innovation). The company's CEO & MD Vishal Sikka's increased participation in sales deals and incentivizing sales efforts have resulted Infosys in bagging large deal.

Infosys Information Platform (IIP) has completed more than 220+ engagements and that of Infosys Automation Platform (IAP) has 125+ engagements.

Large deal wins TCV rose 45% YoY in FY16 to USD 2.79 bn in as compared to USD 1.93 bn in FY15.

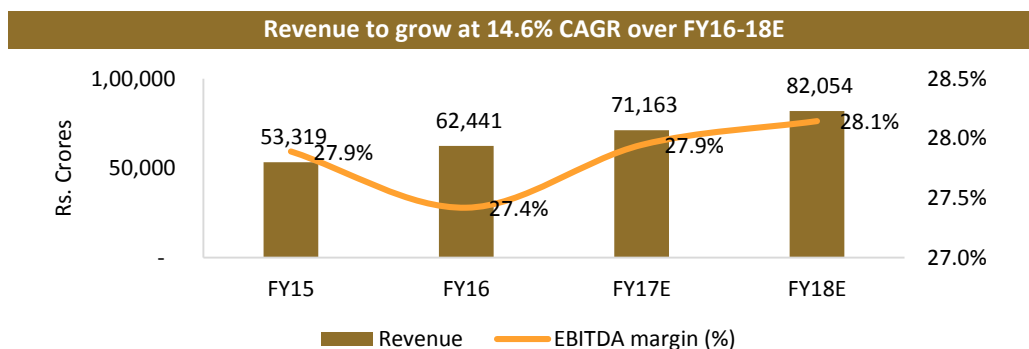
The company continues to witness strong momentum in large deal wins with 45% YoY increase to USD 2.79 bn in its total contract value (TCV) of large deal as compared to USD 1.93 bn in FY15. Further, the company is focusing more on design thinking, solutions in artificial intelligence and intellectual property led businesses that are expected to contribute at least 10% to its revenues going forward. Banking upon the aforementioned steps, we expect the company to regain its bellwether status. Meanwhile, the management remained optimistic of delivering industry leading growth in FY17. We expect Infosys to grow by 14% in FY17.



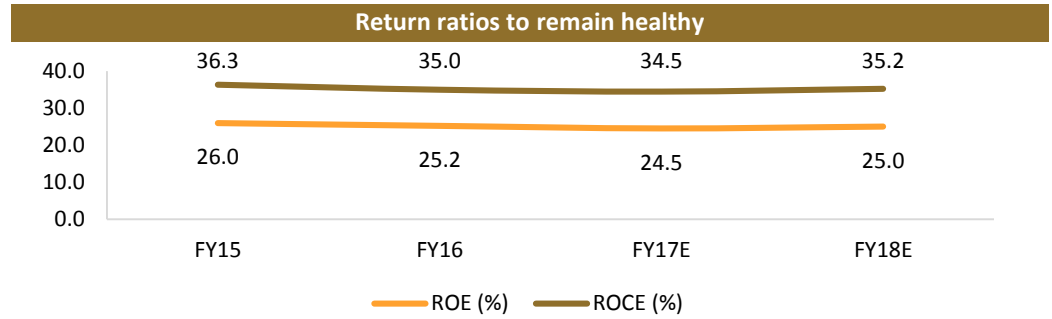
Source: Company, In-house research

Traction in large deal wins and cost optimisation initiatives to aid growth

The management has guided for robust revenue growth of 11.5%-13.5% in constant currency and 11.8%-13.8% in USD terms for FY17. Given strong guidance coupled with traction in large deal wins, we remain upbeat on the stock. As a result, we expect revenue to grow at a CAGR of 14.6% over FY16-18E. Despite pricing pressure in traditional services, we expect improvement in EBITDA margin on account of company's focus on digitisation and automation. We expect EBITDA margin to expand to 28.1% in FY18E from 27.4% in FY16. The net profit is projected to grow at a CAGR of 13.3% over FY16-18E. ROE & ROCE are likely to remain healthy at 25% and 35.2% in FY18E, respectively.



Source: Company, In-house research



Source: Company, In-house research

Key risks:

- Appreciation of INR against USD.
- Slowdown in global IT spend.
- Lower than expected improvement in margin.

Profit & Loss Account (Consolidated)

Y/E (Rs.Cr)	FY15	FY16	FY17E	FY18E
Total operating Income	53,319	62,441	71,163	82,054
Raw Material cost	-	-	-	-
Employee cost	29,802	34,418	38,997	44,965
Other operating expenses	8,646	10,903	12,279	13,994
EBITDA	14,871	17,120	19,887	23,095
Depreciation	1,017	1,266	1,644	1,801
EBIT	13,854	15,854	18,243	21,294
Interest cost	-	-	-	-
Other Income	3,430	3,128	3,027	3,454
Profit before tax	17,284	18,982	21,270	24,747
Tax	4,911	5,301	6,168	7,177
Profit after tax	12,373	13,681	15,101	17,570
Minority Interests	-	-	-	-
P/L from Associates	(1)	(3)	-	-
Adjusted PAT	12,372	13,678	15,101	17,570
E/o income / (Expense)	-	-	-	-
Reported PAT	12,372	13,678	15,101	17,570

Balance Sheet (Consolidated)

Y/E (Rs.Cr)	FY15	FY16	FY17E	FY18E
Paid up capital	572	1,144	1,144	1,144
Reserves and Surplus	50,164	56,682	64,409	73,868
Net worth	50,736	57,826	65,553	75,012
Minority Interest	-	-	-	-
Total Debt	-	-	-	-
Other non-current liabilities	50	126	139	152
Total liabilities	50,786	57,952	65,692	75,164
Net fixed assets	7,751	8,704	10,620	12,579
Capital WIP	776	960	960	960
Goodwill	3,595	4,476	4,476	4,476
Investments	2,270	1,892	1,892	1,892
Total Net Current Assets	30,867	34,489	39,623	46,757
-Net CA	500	1,792	2,354	3,332
-Cash	30,367	32,697	37,269	43,426
Deferred tax assets (Net)	536	533	533	533
Other non-current assets	4,991	6,898	7,588	7,967
Total assets	50,786	57,952	65,692	75,164

Cash Flow Statement (Consolidated)

Y/E (Rs.Cr)	FY15	FY16	FY17E	FY18E
Pre tax profit	17,283	18,979	21,270	24,747
Depreciation	1,017	1,266	1,644	1,801
Chg in Working Capital	(842)	(2,146)	(1,239)	(1,343)
Others	(2,354)	(2,371)	(3,027)	(3,454)
Tax paid	(6,751)	(5,865)	(6,168)	(7,177)
Cash flow from operating activities	8,353	9,863	12,480	14,575
Capital expenditure	(2,255)	(2,723)	(3,560)	(3,760)
Chg in investments	2,003	370	-	-
Other investing cashflow	1,251	1,633	3,027	3,454
Cash flow from investing activities	999	(720)	(533)	(306)
Equity raised/(repaid)	-	-	-	-
Debt raised/(repaid)	-	-	-	-
Dividend paid	(4,935)	(6,813)	(7,374)	(8,112)
Other financing activities	-	-	-	-
Cash flow from financing activities	4,935	(6,813)	(7,374)	(8,112)
Net chg in cash	4,417	2,330	4,572	6,156

Key Ratios (Consolidated)

Y/E	FY15	FY16	FY17E	FY18E
Valuation(x)				
P/E	21.8	19.8	17.9	15.4
EV/EBITDA	15.9	13.8	11.6	9.7
EV/Net Sales	4.4	3.8	3.2	2.7
P/B	5.3	4.7	4.1	3.6
Per share data (Rs.)				
EPS	108.1	59.8	66.0	76.8
DPS	44.7	24.3	26.8	29.5
BVPS	221.7	252.7	286.5	327.8
Growth (%)				
Net Sales	6.4	17.1	14.0	15.3
EBITDA	11.1	15.1	16.2	16.1
Net profit	16.1	10.6	10.4	16.3
Operating Ratios				
EBITDA Margin (%)	27.9	27.4	27.9	28.1
EBIT Margin (%)	26.0	25.4	25.6	26.0
PAT Margin (%)	23.2	21.9	21.2	21.4
Return Ratios (%)				
RoE	26.0	25.2	24.5	25.0
RoCE	36.3	35.0	34.5	35.2
Turnover Ratios (x)				
Sales/Total Assets	0.9	0.9	0.9	0.9
Sales/Working Capital	41.4	54.5	34.3	28.9
Liquidity and Solvency Ratios (x)				
Current Ratio	3.0	3.1	3.2	3.3
Interest Coverage Ratio	0.0	0.0	0.0	0.0
Debt/Equity	(0.6)	(0.6)	(0.6)	(0.6)

Rating criteria

Large Cap.	Return	Mid/Small Cap.	Return
Buy	More than equal to 10%	Buy	More than equal to 15%
Hold	Upside or downside is less than 10%	Accumulate*	Upside between 10% & 15%
Reduce	Less than equal to -10%	Hold	Between 0% & 10%
		Reduce/sell	Less than 0%

* To satisfy regulatory requirements, we attribute 'Accumulate' as Buy and 'Reduce' as Sell.

* Infosys is a large-cap company.

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