Emkay Research

28th August'2008

Infosys Technologies

Event Update

Wait on demand pickup continues

HOLD

Price	Target Price
Rs1,708	Rs 1836
Sensex	14,297

Price Performance

(%)	1M	3M	6M	12M
Absolute	11	(9)	6	(9)
Rel. to Sensex	11	4	32	(5)

Source: Capitaline

Stock Details

Sector	IT Services
Reuters	INFY.BO
Bloomberg	INFO@IN
Equity Capital(Rs mn)	2862
Face Value(Rs)	5
52 Week H/L	2,140/1,212
Market Cap(Rs bn//US$ mn)	978/22,385
Daily Avg Volume (No of shares)	2170323
Daily Avg Turnover (US$)	86.2

Shareholding Pattern (%)

(31st March'08')	
Promoters	16.5
FII/NRI	55.5
Institutions	7.1
Private Corp.	2.9
Public	18.0

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Event: Infosys Analyst Meet'08: No demand pickup still

Infosys Analyst Meet'08 did little to throw any positive news/comments on demand acceleration/pick up. On the positive side, company remains confident on meeting FY09 guidance of 19-21% growth in revenues ***(though remained non committal whether it would live up to 'material beat' precedence).*** Besides the company indicated that it had not witnessed any significant project deferrals at its clients end as well as pricing discipline has stood until now. On the flip side, Infy management acknowledged that deal signings continued to take longer, disconcerting in our view given that sooner than later it ***could lead to intense scramble for locking in revenues/volumes for FY10 and thus could disrupt the prevalent discipline on pricing.*** We believe that if deal signings do not pick up over the next 2 months (near peak for next year's budgeting cycle), ***the offshore space could once again head into CY09 in a similar precarious demand/volume state as was seen in CY08***. The company also played down the unexpected 23% decline in top client revenues during Q1FY09 and expects growth to rebound from Q2FY09. We remain neutral on the sector borne from both delay in demand pickup further supported by somber campus hiring displayed by the vendors till date *(for details refer to our note dated 18th August'08,* ***IT Services: 'Hiring continues to be somber'****)*. Thus ***despite Infosys valuations appearing cheap at <15xFY10E earnings, scope for absolute out performance might be limited given increasing risks to the estimates itself. (for valuation charts please refer to Pg 3)*** Maintain 'HOLD' on Infy with a price target of Rs 1836.

Deal signings continue to take longer

Infosys management indicated that in the backdrop of the worsening environment, clients continued to exercise caution with deal signings still showing no signs of pickup. On the positive side, the company sees little risk to achieving FY09 revenue growth target of 19-21% but failed to commit on maintaining the 'material beat' precedence. Further the company indicates that pricing discipline has held on across the offshore space until now. As well, Infosys has not witnessed any material project delays/deferrals at clients unlike two other peers. However we are worried that deal signings are not showing any signs of a pickup as a prolonged delay on this front, could eventually lead to aggressive scramble to lock in revenues/volumes for FY10 ***(and that could disrupt the prevalent pricing discipline).***

Top client expected to rebound in Q2FY09

Infosys management played down investor concerns on the top client performance during Q1FY09 ***(top client declined by ~22% sequentially after a superlative ~12.5% CQGR ramp up through FY08, see top client performance in the table below).*** The vertical head indicated that the ramp down in top client revenues was slightly unexpected and much ahead of Infy's internal estimates. The company expects some form of a rebound in the top client contribution of revenues from Q2FY09 onwards, though rules out the significant sequential acceleration witnessed during FY08.

(In US$ mn)	Q3FY07	Q4FY07	Q1FY08	Q2FY08	Q3FY08	Q4FY08	Q1FY09
Top client rev	56.6	73.4	79.8	80.7	103.0	117.6	91.2
QoQ growth%	*15.0%*	*29.7%*	*8.7%*	*1.1%*	*27.6%*	*14.2%*	*-22.4%*

Source: Company, Emkay Research

Even in the telecom space, Infy sees prolonged negotiations on deals forced by the overall jitteriness caused by fears of spread of worsening macro environment across geographies.

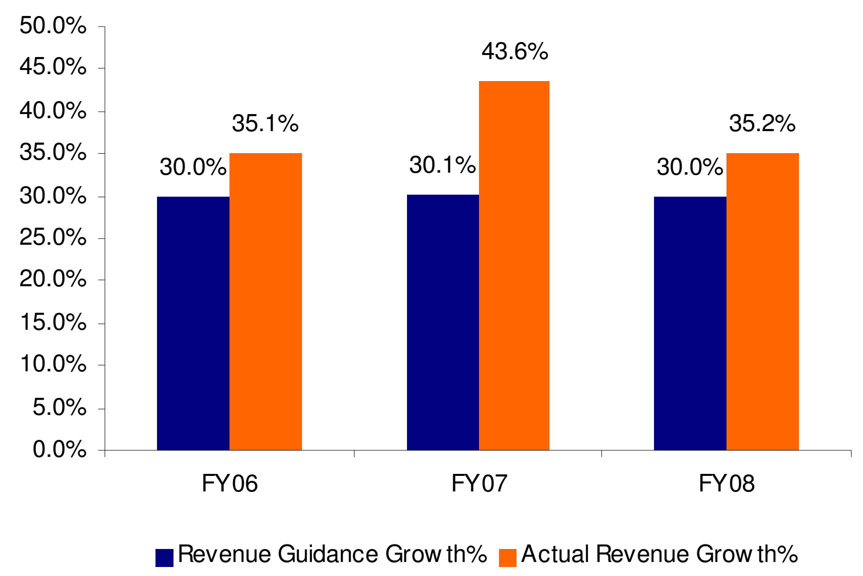
Axon; Margin accretion opportunities; take time to play out

Although Infosys management was unwilling to talk much on the Axon acquisition, Infosys remains confident about it's improved capabilities on the SAP side post the move. We highlight that Infosys has lagged materially behind peers on SAP headcount ***(Infosys SAP headcount at ~2,100 V/s Satyam at ~5,000 and TCS at ~4,000)*** and Axon gives it the much needed booster in ERP/ Europe. However the Axon acquisition comes with it's own set of challenges in the form of (1) retaining key personnel, (2) a marquee client roaster albeit high client concentration ***(Revenues/client beyond Top 10 at only ~US$ 3,00,000)*** and (3) margin expansion at Axon (Axon's EBIT margins at ~15% V/s Infosys's EBIT margins at ~27.8%).

Remain 'Neutral' on the sector; Wait on demand revival continues

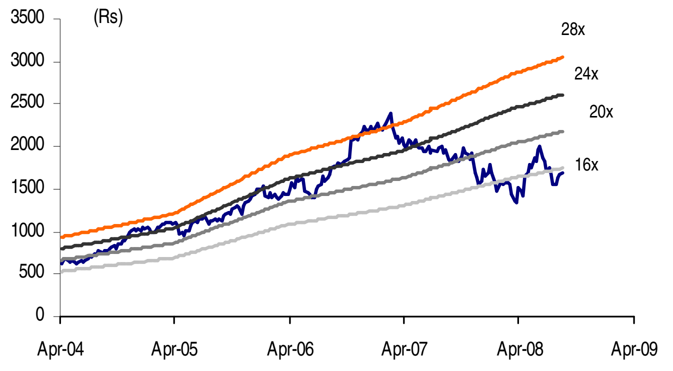
We believe that the prolonged delay in deal signings is disconcerting and see demand acceleration is taking longer than earlier expectations. We are worried as the wait on demand pickup could then lead to a mad rush to lock in business/volumes for FY10 and thus could disrupt the discipline displayed on pricing hitherto. For Infosys, we point out that although valuations might appear cheap at <15xFY10E earnings of Rs 117.3, the downside risks to FY10 estimates continue to rise. We remain 'Neutral' on the sector. Maintain 'HOLD' on Infosys with a price target of Rs 1836.

Scope for 'material US$ guidance beat' during FY09 might be limited

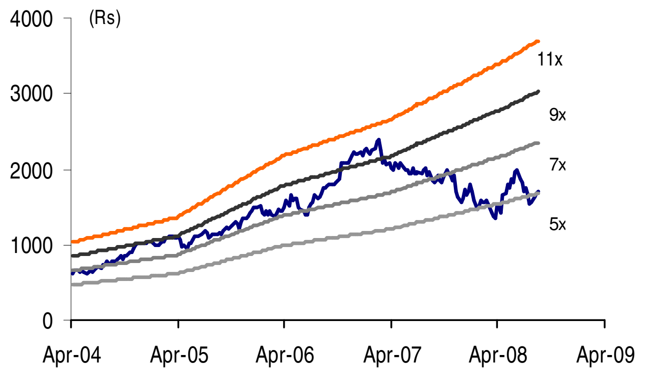


Source: Company, Emkay Research

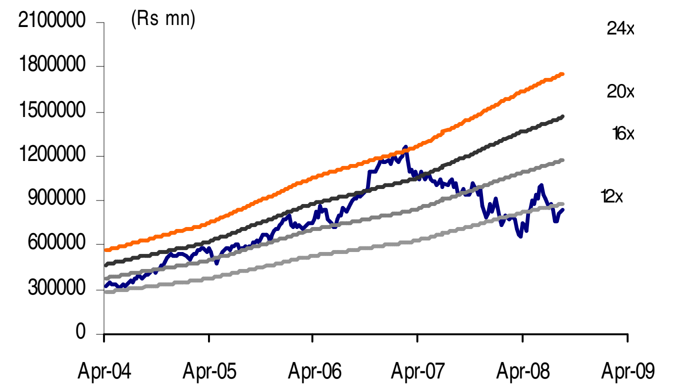
1 year forward P/E Bands



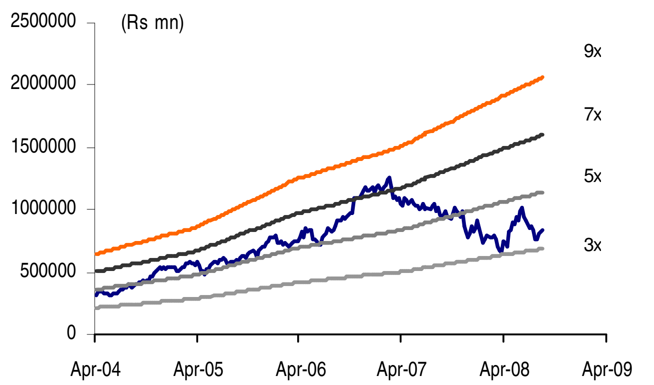
1 year forward P/BV



1 year forward EV/EBITDA



1 year forward EV/Sales



Financials

Income Statement

Y/E, Mar (Rs. m)	FY07	FY08	FY09E	FY10E
Net Sales	138,930	166,920	211,923	255,864
Growth (%)		20	27	21
Total Expenditure	(95,020)	(114,540)	(144,116)	(174,566)
Growth (%)		21	26	21
EBIDTA	43,910	52,380	67,807	81,297
Growth (%)		19	29	20
EBIDTA %	31.6	31.4	32.0	31.8
Other Income	3,760	7,040	7,375	9,221
Depreciation	(5,140)	(5,980)	(7,180)	(8,443)
EBIT	**42,530**	**53,440**	**68,002**	**82,074**
Interest				
EBT	**42,530**	**53,440**	**68,002**	**82,074**
Tax	(3,860)	(6,850)	(9,310)	(14,773)
EAT	**38,560**	**46,590**	**58,692**	**67,301**
Growth (%)		21	26	15
EAT (%)	27.8	27.9	27.7	26.3

Balance Sheet

Y/E, Mar (Rs. m)	FY07	FY08	FY09E	FY10E
Equity share capital	2,860	2,860	2,860	2,860
Reserves & surplus	109,690	135,090	172,962	216,642
Minority Interest	40	-	-	-
Networth	**112,590**	**137,950**	**175,821**	**219,502**
Secured Loans	-	-	-	-
Unsecured Loans	-	-	-	-
Loan Funds	**-**	**-**	**-**	**-**
Total Liabilities	**112,590**	**137,950**	**175,821**	**219,502**
Goodwill				
Gross Block	46,420	54,390	69,935	84,435
Less: Depreciation	18,360	19,860	27,040	35,483
Net block	**28,060**	**34,530**	**42,895**	**48,952**
Capital WIP	**9,650**	**13,240**	**18,000**	**20,000**
Investment	**-**	**-**	**-**	**-**
Current Assets	**95,460**	**130,900**	**166,502**	**213,081**
Inventories	-	-	-	-
Sundry debtors	24,360	32,970	40,643	47,668
Cash & bank balance	58,710	69,500	92,976	126,730
Loans & advances	12,140	27,710	31,353	37,153
Other current assets	250	720	1,530	1,530
Current Liab & Prov	**21,500**	**41,910**	**52,836**	**63,791**
Current liabilities	14,690	19,120	23,805	28,741
Provisions	6,810	22,790	29,031	35,050
Net current assets	**73,960**	**88,990**	**113,667**	**149,290**
Misc exps	**-**	**-**	**-**	**-**
Deferred Tax	**920**	**1,190**	**1,260**	**1,260**
Total Assets	**112,590**	**137,950**	**175,821**	**219,502**

Cash Flow	FY07	FY08	FY09E	FY10E
Net Profit after Tax	38,560	46,590	58,692	67,301
Add : Depreciation	5,140	5,980	7,180	8,443
Add : Misc exp w/off				
Net changes in WC	**(33,830)**	**(14,560)**	**(23,867)**	**(35,623)**
Operational Cash Flows	**23,000**	**43,531**	**58,602**	**63,912**
Capital expenditure	**(20,590)**	**(16,040)**	**(20,305)**	**(16,500)**
Investments	14,600	(940)	(1,620)	-
Investing Cash Flows	**(5,990)**	**(16,980)**	**(21,925)**	**(16,500)**
Borrowings	-	-	-	-
dividend paid	(7,510)	(22,251)	(20,599)	(23,621)
Issue of shares	15,670	6,530	7,398	9,963
Share Premium		-	-	-
Financing Cash Flows	**7,410**	**(15,761)**	**(13,201)**	**(13,657)**
changes in cash	**24,420**	**10,790**	**23,477**	**33,754**
Opening balance	**34,290**	**58,710**	**69,500**	**92,976**
Closing balance	**58,710**	**69,500**	**92,976**	**126,730**

Key ratios	FY07	FY08	FY09E	FY10E
EPS (Rs)	67.6	81.3	102.3	117.3
CEPS (Rs)	76.7	91.7	114.8	132.1
Book Value Per Share (Rs)	197.5	240.6	306.5	382.7
Dividend Per Share (Rs)	11.4	33.2	30.7	35.2
Valuations Ratios (x)				
PER	25.2	21.0	16.7	14.6
P/CEPS	24.5	20.5	16.4	14.2
P/BV	8.6	7.1	5.6	4.5
EV/EBIDTA	20.9	17.3	13.0	10.5
EV/Sales	6.6	5.4	4.2	3.3
M-Cap/sales	7.7	6.4	5.1	4.2
Profitability Ratios (%)				
RoCE	37.3	34.0	33.3	32.1
RoNW	42.2	37.2	37.4	34.0
EBITDA Margin	31.6	31.4	32.0	31.8
EBIT Margins	30.6	32.0	32.1	32.1
Net Profit Margin	27.8	27.9	27.7	26.3

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