

Infosys Technologies Ltd (Q4 FY08)

April 16, 2008

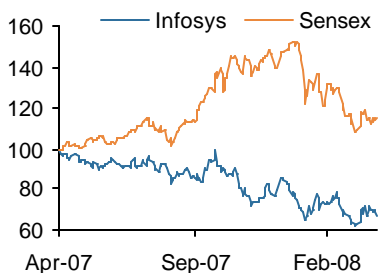
Stock data

Sensex:	16,154
CMP (Rs):	1,510
Target price (Rs):	1,341
Downside (%):	11.2
52 Week h/l (Rs):	2,140/1,212
Market cap (Rs cr)	86,372
6m Avg vol BSE&NSE ('000 nos):	1,811
No of o/s shares (mn):	572
FV (Rs):	5
Bloomberg code:	INFO IN
Reuters code:	INFY.BO
BSE code:	500209
NSE code:	INFOSYSTCH

Shareholding pattern

December 2007	(%)
Promoters	16.5
FII's	52.2
Indian institutions	7.0
Public & others	24.3

Share price trend



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- Rupee revenue growth of 6.3% qoq in Q4 FY08 was in line with expectations. Volume growth was modest at 4.9% qoq while pricing improvement was negligible.
- Slow growth was witnessed in the US region along with a material de-growth in banking and financial services segment.
- EBITDA margin was stable qoq at 32.5% aided by SG&A leverage, better subsidiary profitability, rupee depreciation and absence of one-time expenditure.
- Q4 FY08 net profit growth of 4.1% qoq, excluding the tax reversals, was marginally below expectations. Announcement of a special dividend of Rs20 and increase in payout policy is a positive surprise.
- Terming the business environment as challenging and imposing revenue loss risk, management guides for a weak Q1 FY09. However, FY09 guidance of 19-21% revenue growth and EPS of Rs92.3-93.9 is healthy.
- We believe that strong back-ended revenue growth expectation (Q2-Q4 FY09 CQGR 5.6-6.7%) and Re/\$ assumption of Rs40 are key risks in the guidance.
- Remain negative on Infosys with a price target of Rs1,341, implying 11% downside.

Result table

Period	Q3 FY08	Q4 FY08	QoQ	YoY
(Rs mn)	(₹)	(₹)	(%)	(%)
Net sales	42,710	45,420	6.3	20.4
Total Expenditure	(28,790)	(30,640)	6.4	19.0
EBITDA	13,920	14,780	6.2	23.5
EBITDA margin (%)	32.6	32.5	-	-
Depreciation	(1,530)	(1,570)	2.6	8.3
Interest	-	-	-	-
Other income	1,580	1,390	(12.0)	16.8
PBT	13,970	14,600	4.5	24.7
Tax	(2,160)	(2,310)	6.9	53.0
Pre-Exceptional PAT	11,810	12,290	4.1	20.5
Extraordinary items	500	200	-	-
Minority Interest	-	-	-	-
PAT	12,310	12,490	1.5	9.2
Number of shares (Mn)	572.0	572.0	-	-
EPS (Rs) – quarterly	21.5	21.8	1.5	9.2

Source: Company, India Infoline Research

Q4 FY08 revenue growth in-line with expectations; FY08 revenues meets guidance

Infosys delivered a 6.3% qoq rupee revenue growth in Q4 FY08 driven by a modest volume growth of 4.9%, negligible pricing improvement of 0.2% and rupee depreciation of 0.9%. FY08 revenue growth in dollar terms was 35% yoy comprising 27.6% volume growth and 5.2% pricing improvement while the rupee growth was significantly lower at 20.2% yoy, impacted by an 11% appreciation of the rupee.

Insignificant pricing improvement and lackluster growth in US and BFSI have been key negatives in Q4 FY08

The pricing improvement of a miniscule 0.2% qoq in Q4 FY08 was the smallest recorded in the last ten quarters. This might as well mean that any significant like-to-like pricing improvements would be difficult to come by going ahead as business environment becomes more challenging. Therefore, Infosys having secured a material 5% pricing improvement each in the last two years (FY07 and FY08), would be robbed off an important revenue growth and margin improvement lever in FY09. Revenues from the BFSI vertical declined 2% qoq due to a 3% de-growth in the banking and financial services component. Revenue growth in the US region remained subdued at 3.6% qoq for a second consecutive quarter. Management admitted about revenue growth challenges in the short-term.

Growth was driven by the Top client while it was broad-based across service lines and non-BFSI verticals

Revenues from the Top client of Infosys grew by robust 15.3% qoq thereby increasing its revenue share to 10.3%. Amongst verticals other than BFSI, company recorded strong double-digit growth in manufacturing, telecom and transportation segments. In case of services, system integration, engineering services, IMS, BPO, package implementation and consulting grew far ahead of the company. Low growth in the US was compensated by a 10.9% growth in other geographies.

EBITDA margin remained stable in Q4 FY08 and FY08

Infosys managed to maintain EBITDA margin in Q4 FY08 aided by SG&A leverage, improvement in subsidiary profitability, absence of one-time items (US\$8mn hit in Q3 FY08) and depreciation of the rupee. Net profitability of Infosys BPO improved from 11.4% to 13.2% on qoq basis while that of Infosys Australia improved materially from 14% to 21%. Offshore revenue share and utilization was stable qoq. For FY08, EBITDA margin at 31.4% was similar to FY07 levels despite an 11% appreciation of the rupee. This was due to significant pricing improvements, SG&A leverage, utilization improvement and offshore shift.

Net profit growth marginally below expectations for Q4 FY08; FY08 EPS guidance surpassed

Excluding the tax reversals (Rs200mn in Q4 FY08 and Rs500mn in Q3 FY08), net profit grew by 4.1% qoq. This growth was marginally below our expectations and was mainly impacted by sequentially lower other income. Infosys reported a net forex loss of ~Rs400mn during the quarter. For FY08, Infosys surpassed its EPS guidance of Rs81.1 by clocking Rs81.6.

Manpower hiring modest at just 3% of Q3 FY08 base; Attrition continues to decline

Manpower addition was subdued at 2,586, just 3% of Q3 FY08 base, due to weak near-term revenue growth outlook. Of the above, 900 people were added in the BPO segment. Attrition at 13.4% for the stand-alone company reflects continued improvement. In FY08, Infosys added net 18,946 and gross 33,177 employees.

Weak Q1 FY09 outlook reflects near-term growth pressures

Expressing concerns on near-term growth, Infosys guided for a flattish revenue growth of 0.6-0.9% qoq in Q1 FY09. Company expects salary increases of 4-5% onsite and 11-13% offshore, effective April 1st, 2008, to lead to an EBITDA margin decline of ~300bps qoq. As a result, the EPS is guided at Rs20.7 (pre tax-reversal), lower qoq by 3.4%.

FY09 guidance though healthy poses some noticeable risks

Despite giving a weak Q1 outlook, management has guided for a healthy 19-21% growth in rupee revenues and EPS of Rs92.3-93.9 in FY09. The guidance assumes a pick-up in revenue growth Q2 FY09 onwards (required Q2-Q4 COGR of 5.6-6.7%) along with a sharp improvement in the EBITDA margin. Full-year EBITDA margin is expected at ~31%. Company expects to hire 25,000 people on gross basis in FY09, which is in-line with the revenue guidance. Guidance has been given at a Re/\$ rate of Rs40. Given the current business environment and rupee outlook, we believe that strong back-ended growth assumption and stable currency assumption are key risks in the guidance.

Announcement of special dividend and increase in payout policy is a positive surprise

In a bid to enhance shareholders' returns, Infosys announced a final dividend of Rs7.25 and a special dividend (for achievement of US\$1bn in annual profits) of Rs20 per share taking the total dividend to Rs33.25 for FY08. Further, the company has increased the dividend payout policy to 30% of profits from earlier 20%. We believe that this is a positive step, given the high existing cash balance of ~US\$2bn, company's conservative approach towards acquisitions and its ability to generate sizeable cash flows every quarter.

Remain negative with a price target of Rs1,341, implying 11% downside.

We have downgraded EPS estimate for FY09 by 3.5% to Rs92.5 while maintaining our FY10 estimate at Rs100.6. Our FY09 EPS estimate is near the lower end of the guided band and reflects our belief that current guidance is not conservative and is exposed to risks from further deterioration in business conditions and rupee appreciation. We maintain SELL by lowering our one-year target price to Rs1,341 (14.5x FY09E EPS); implying 11% downside from current levels.

Projected financials

y/e Mar, Rs mn	FY06	FY07	FY08	FY09E	FY10E
Revenues	95,210	138,930	166,981	202,251	248,499
yoy growth (%)	33.5	45.9	20.2	21.1	22.9
EBITDA	30,911	43,910	52,441	63,004	75,280
EBITDA margin (%)	32.5	31.6	31.4	31.2	30.3
PAT	24,581	38,560	46,651	52,911	57,527
PAT	24,581	38,560	46,651	52,911	57,527
yoy growth (%)	30.0	56.9	21.0	13.4	8.7
EPS (Rs)	44.6	67.4	81.6	92.5	100.6
P/E (x)	33.9	22.4	18.5	16.3	15.0
P/BV (x)	11.9	7.7	6.2	4.9	4.0
EV/EBITDA (x)	25.4	18.3	14.6	11.9	9.6
ROE (%)	40.0	42.3	36.9	33.5	29.3
ROCE (%)	45.5	46.5	43.3	39.4	37.6

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