

Current Reco	: HOLD
Previous Reco	: BUY
CMP	: INR923
Target Price	: INR 915
Potential Return	: -1%

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Market data

Sensex	:	31,525
Sector	:	IT
Market Cap (INRbn)	:	2,120.7
Market Cap (USDbn)	:	33.060
O/S Shares (m)	:	2,296.9
52-wk HI/LO (INR)	:	1083/884
Avg Daily Vol ('000)	:	5,369
Bloomberg	:	INFO IN

Source: Bloomberg

Valuation

	FY17	FY18e	FY19e
EPS (INR)	62.8	64.2	65.4
P/E(x)	14.7	14.4	14.1
P/BV(x)	3.1	2.8	2.6
EV/EBITDA(x)	10.1	8.9	8.6
Dividend yield (%)	2.8	3.3	3.4

Source: Bloomberg

Returns (%)

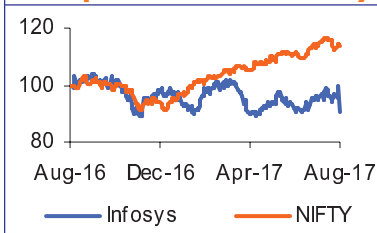
	1m	3m	6m	12m
Absolute	(6)	(4)	(8)	(10)
Relative	(6)	(7)	(17)	(20)

Source: Company, Antique

Shareholding pattern

Promoters	:	13%
Public	:	87%
Others	:	0%

Source: Bloomberg

Price performance vs Nifty

Source: Bloomberg, Indexed to 100

COMPANY UPDATE

Infosys Limited

Leadership vacuum to be detrimental in medium term; difficult to fill Dr. Sikka's shoes

In a dramatic turn of events Dr. Vishal Sikka resigned as MD & CEO of Infosys. Dr Sikka has attributed his resignation to the constant distractions, negativity and increasingly personal attacks. In our view, this is significantly negative for the company. Under Dr. Sikka's leadership Infosys had reversed the trend of revenue under-performance against Industry and had performed well on most operational parameters. It may be noted that prior to Sikka's tenure, Infosys had significantly under-performed industry growth rates. It is still perplexing to us that why would the CEO resign if he has the full support of the board and did the board do enough to give comfort to Dr. Sikka and provide a conducive working environment.

With Sikka's exit, we see downside risk to our revenue growth and margin estimates for FY18/19. IT services industry is passing through one of the most fundamental transitions and any sort of leadership flux at this moment can have serious medium term implications. Immediate impact would be witnessed in deal win rate coming down and Infosys ceding revenue market share in CY18. Given the circumstances of Dr. Sikka's exit, and despite the full support of the board, we believe that the company may find it difficult to attract the best of the external talent for CEO role. Infosys board needs to come with a concrete plan to isolate the next management team from a recurrence of the current events. We also note that the dispute between board and the founders is far from over. Prospects of class action law suits and in the worst case even SEC probe is possible. All this will take away eye from business and execution.

We revise down our FY18/19 EPS estimates by 1%/7% respectively driven by 1%/2.5% USD revenue cut and 120bps cut in FY19 EBIT margin to 23%. We revise TP to INR915 based on 14x FY19 EPS and downgrade rating to HOLD. We believe that leadership churn and the resultant growth slowdown will result in stock trading at the lower end of its historical range.

Dr. Sikka's exit: Leadership churn a big risk

Dr. Sikka's exit was the biggest risk and with this becoming an eventuality, the company faces a big challenge of filling the leadership vacuum. Dr. Sikka had guided the company well at a time when the industry is undergoing a metamorphosis towards newer technologies. Under Dr. Sikka's guidance the company was able to add 25 new services which comprised 8.3% of revenues in FY17. Dr. Sikka's strategic initiatives had just started bearing results and with his exit there could be delay in getting the desired results.

Strategy rethink may happen

The Co-Chairman of the Board, Mr. Ravi Venkatesan did allude that the company will not backtrack on the strategic roadmap laid by Dr. Sikka. However, we believe the new incoming CEO would like to have his own strategy for the company which could be different from the one followed by Dr. Sikka. This strategy shift would result in company trailing the peer group in adopting the emerging technologies.

Back flip on strategy could be detrimental

The cornerstone of Dr. Sikka's strategy has been the focus on newer technologies and automation of traditional services. With an external CEO unlikely, company may come back to operational efficiency paradigm. This shift from new technology to operational efficiency paradigm may prove to be detrimental for the company.

Underperformance could make a comeback

Given the uncertainty around new leader we believe the company could return to the era of underperformance (FY12-15) where the company lagged peers in revenue growth and margin performance. We have pruned our revenue growth to 7%/5.5% from 8% earlier for FY18/FY19 each.

Board room battle: no signs of abating

Despite Dr. Sikka's exit the Board room battle is far from over. If one has to go by the recent press release wherein the Board has laid the blame on Mr. Murthy for Dr. Sikka's exit, we believe this tussle between the Board and Mr. Murthy will take time to settle.

External CEO almost ruled out

Given the circumstances of Sikka's exit and a public perception of interference from a set of external shareholders, we believe Infosys may find it difficult to attract quality external talent. In this context Infosys may be in a worse off condition than in 2014, when they hired Dr. Sikka as CEO.

Class action law suits likely

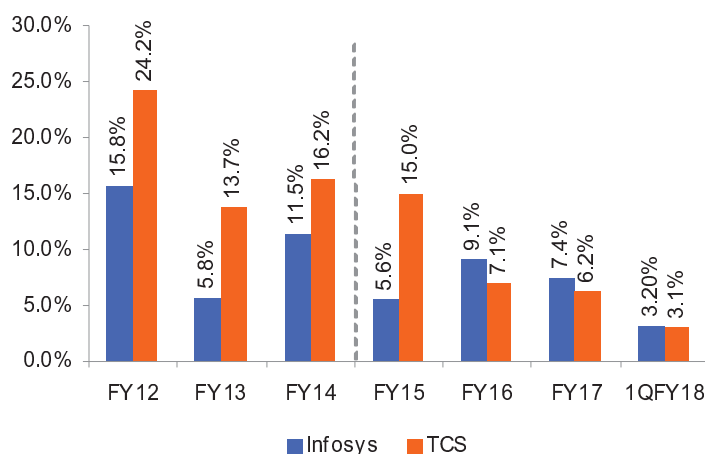
A lot of questions have been raised on the functioning of the board by the founders and by anonymous complaints recently. While the Board and management have been given clean chit by external investigations class action suits and SEC probe may also happen. This can further slowdown the focus on running the business efficiently.

Buyback may not be enough

Infosys board has approved share buy-back of 113mn shares (4.9% of the equity) at a price of INR1,150 (25% premium to CMP of 923). The total buyback amount is INR130bn and the buyback will be through a tender offer route. Buyback would require share-holders approval and the entire process may take 4-6 months. While the buyback amount is meaningful, stock impact may be limited as investors will be concerned on the leadership churn.

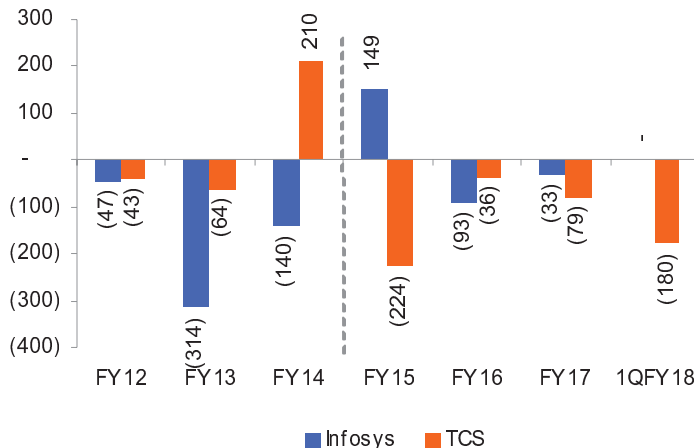
Infosys reversed the underperformance to TCS under Dr. Sikka's CEO tenure (FY15-1QFY18) on both revenue and margin front

Revenue growth better than TCS in FY16 and FY17



Source: Companies, Antique

EBIT margin change (bps) better than TCS since FY15



Source: Companies, Antique

Financials

Profit and Loss Account

Year-ended March 31	FY15	FY16	FY17	FY18e	FY19e
Net Revenue	533,190	624,410	684,850	709,242	760,874
Op. Expenses	384,180	453,630	498,800	517,377	565,705
EBITDA	149,010	170,780	186,050	191,865	195,169
Depreciation	10,690	14,590	17,030	18,242	19,857
EBIT	138,320	156,190	169,020	173,623	175,312
Other income	34,270	31,250	30,790	32,190	35,309
Reported PBT	172,590	187,440	199,810	205,813	210,621
Tax	49,290	52,520	55,980	59,113	61,080
Reported PAT	123,300	134,920	143,830	146,699	149,541
Net Profit	123,300	134,920	143,830	146,699	149,541
Adjusted PAT	123,300	134,920	143,830	146,699	149,541
Adjusted EPS (INR)	53.9	59.0	62.8	64.2	65.4

Balance sheet (INRm)

Year-ended March 31	FY15	FY16	FY17	FY18e	FY19e
Share Capital	5,720	11,440	11,440	11,440	11,440
Reserves & Surplus	541,910	606,350	678,380	742,134	805,324
Networth	547,630	617,790	689,820	753,574	816,764
Capital Employed	547,630	617,790	689,820	753,574	816,764
Gross Fixed Assets	164,420	189,660	210,730	239,730	269,730
Accumulated Depreciation	66,790	74,510	85,810	102,888	121,969
Net Fixed Assets	97,630	115,150	124,920	136,842	147,761
Goodwill	30,910	37,640	36,520	36,520	36,520
Investments	22,190	18,860	163,520	28,000	28,000
Non Current Investments	22,190	18,860	163,520	28,000	28,000
Current Assets, Loans & Adv.	512,790	582,240	508,590	696,001	752,205
Debtors	125,580	143,590	159,700	171,400	183,878
Cash & Bank balance	303,670	326,970	226,250	399,491	440,217
Loans & advances and others	83,540	111,680	122,640	125,110	128,110
Current Liabilities & Prov	115,890	136,100	143,730	143,789	147,721
Liabilities	12,360	17,550	17,580	15,300	15,300
Provisions	103,530	118,550	126,150	128,489	132,421
Net Current Assets	396,900	446,140	364,860	552,212	604,483
Application of Funds	547,630	617,790	689,820	753,574	816,764

Per share data

Year-ended March 31	FY15	FY16	FY17	FY18e	FY19e
No. of shares (m)	2,286	2,286	2,286	2,286	2,286
Diluted no. of shares (m)	2,286	2,286	2,286	2,286	2,286
BVPS (INR)	239.6	270.3	301.8	329.7	357.4
CEPS (INR)	58.6	65.4	70.4	72.2	74.1
DPS (INR)	22.4	24.5	25.8	30.2	31.4

Source: Company Antique

Cash Flow Statement

Year-ended March 31	FY15	FY16	FY17	FY18e	FY19e
PBT	172,590	187,440	199,810	205,813	210,621
Depreciation & amortisation	10,690	14,590	17,030	18,242	19,857
Interest expense					
(Inc)/Dec in working capital	(11,310)	(22,540)	(19,440)	(14,112)	(11,545)
Tax paid	(47,890)	(58,660)	(56,530)	(59,113)	(61,080)
Less: Interest/Div. Income Received	(2,920)	(1,760)	(3,480)	-	-
Other operating Cash Flow	4,780	3,530	2,320	-	-
CF from operating activities	107,520	122,430	140,630	150,830	157,853
Capital expenditure	(35,290)	(34,700)	(27,960)	(30,164)	(30,776)
Inc/(Dec) in investments	22,580	5,330	(142,110)	135,520	-
Add: Interest/Dividend Income Received	(80)	(750)	270	-	-
CF from investing activities	(12,790)	(30,120)	(169,800)	105,356	(30,776)
Dividend Paid	(49,350)	(68,130)	(69,390)	(82,945)	(86,351)
Others					
CF from financing activities	(49,350)	(68,130)	(69,390)	(82,945)	(86,351)
Net cash flow	45,380	24,180	(98,560)	173,241	40,726
Opening balance	256,950	302,330	326,510	227,950	401,191
Closing balance	302,330	326,510	227,950	401,191	441,917

Growth Indicators (%)

Year-ended March 31	FY15	FY16	FY17	FY18e	FY19e
Revenue(%)	6.4	17.1	9.7	3.6	7.3
EBITDA(%)	9.3	14.6	8.9	3.1	1.7
Adj PAT(%)	15.8	9.4	6.6	2.0	1.9
Adj EPS(%)	15.8	9.4	6.4	2.2	1.9

Valuation (x)

Year-ended March 31	FY15	FY16	FY17	FY18e	FY19e
P/E	17.1	15.6	14.7	14.4	14.1
P/BV	3.9	3.4	3.1	2.8	2.6
EV/EBITDA	12.1	10.4	10.1	8.9	8.6
EV/Sales	3.4	2.9	2.8	2.4	2.2
Dividend Yield (%)	2.4	2.7	2.8	3.3	3.4

Financial Ratios

Year-ended March 31	FY15	FY16	FY17	FY18e	FY19e
RoE (%)	24.1	23.2	22.0	20.3	19.0
RoCE (%)	33.7	32.2	30.6	28.5	26.8
Asset/T.O (x)	1.2	1.2	1.3	1.2	1.1
Net Debt/Equity (x)	(0.6)	(0.5)	(0.3)	(0.5)	(0.5)

Margins (%)

Year-ended March 31	FY15	FY16	FY17	FY18e	FY19e
EBITDA Margin(%)	27.9	27.4	27.2	27.1	25.7
EBIT Margin(%)	25.9	25.0	24.7	24.5	23.0
PAT Margin(%)	21.7	20.6	20.1	19.8	18.8

Source: Company Antique