

Larsen & Toubro Infotech ACCUMULATE

Growth momentum sustains

Summary

Larsen & Toubro Infotech's (LTI) Q3FY19 revenue growth of 6.1% QoQ in CC beats our forecast. Further, EBIT margin of 19.1%, +20bps QoQ and EPS of Rs21.7, -6.4%/+31% QoQ/YoY was a beat to our forecast.

Digital solutions (37% of revenue) saw another quarter of strong growth +5.6%/+32.5% QoQ/YoY in US\$. LTI now has 63 Fortune 500 clients, 2 added in Q3FY19.

We factor Q3 result and raise FY19/20E EPS by 2.4%/1.9%. We now forecast FY18-20E revenue (US\$)/EPS CAGR of 17.2%/22%. We increase our TP to Rs1,925 (vs. Rs1,889) based on 20x FY20E. With a 7% upside, we downgrade LTI to ACCUMULATE from BUY.

Key Highlights and Investment Rationale

- Q3FY19 – Third consecutive quarter of 20%+ YoY growth in CC**
 - Revenue growth in CC was 6.1%/20.6% and in US\$ it was 5.6%/18.2% QoQ/YoY. Even after adjusting for the pass-through revenue in the manufacturing vertical in India, the revenue growth was strong at 4.6% QoQ in US\$.
 - Digital solutions maintained the growth momentum, up +5.6%/+32.5% QoQ/YoY.
 - Except for BFS (29.1% of revenue, +3% QoQ in CC) and others (4.6% of revenue, +3.3% QoQ) all the other verticals grew faster than the company growth QoQ.
 - Top 6-10/11-20 clients 14%/16% of revenue grew at 7.1%/7.6% QoQ in US\$ and non-top 20 (36% of revenue) grew at 9.3% QoQ. US\$5mn+ clients +3 QoQ to 47 and US\$20mn+ clients +1 QoQ to 15.
 - LTI is seeing client specific issues in its top-5 clients (25% of revenue, +0.6% QoQ).
 - Q3FY19 EBIT margin was at 19.1%, +20bps QoQ with operational efficiencies, and INR depreciation offsetting the impact of pass-through revenue (-30bps) and investments in large deals.
- Continue to expect LTI to maintain its sector outperformance in FY20E**

We believe that growth in top5-20 clients and non-top 20 clients should offset the impact of slower growth in top-5 clients. Our forecast factors softness in top-5 clients – US\$ revenue growth of 15.1% for FY20E vs. 19.3% for FY19E. Given the sector outperformance we believe that the stock deserves premium valuation and maintain our target PER of 20x FY20E at the top-end of its 1-yr forward PER band of 9.5x to 21.2x since its listing in 2016.

TP	Rs1,925	
CMP	Rs1,801	
Potential upside / downside	+7%	
Previous Rating	BUY	
V/s Consensus		
EPS (Rs)	FY19E	FY20E
IDBI Capital	88.7	96.3
Consensus	85.6	96.7
% difference	3.7	(0.4)

Shareholding Pattern (%)	
Promoters	74.8
FII	7.8
DII	7.0
Public	10.4

Price Performance (%)			
	-1m	-3m	-12m
Absolute	3.0	(1.3)	61.3
Rel to Sensex	2.7	(6.0)	57.5

Financial snapshot

Year	FY16	FY17	FY18	FY19E	FY20E
Revenue	58,464	65,009	73,064	94,471	108,781
EBITDA	10,248	12,302	11,875	19,259	21,603
EBITDA (%)	17.5	18.9	16.3	20.4	19.9
Adj. PAT	8,363	9,707	11,122	15,242	16,549
EPS (Rs)	49.1	56.9	64.7	88.7	96.3
EPS Growth (%)	4.4	15.8	13.7	37.0	8.6
PE (x)	36.7	31.7	27.8	20.3	18.7
Dividend Yield (%)	1.8	0.9	1.2	1.7	1.9
EV/EBITDA (x)	29.7	23.9	24.7	14.8	12.6
RoE (%)	40.3	36.8	31.8	35.3	31.6
RoCE (%)	40.0	42.1	31.2	44.0	40.2

Source: Company; IDBI Capital Research

Q3FY19 Result Review

Key Stock Data	
Bloomberg	LTI IN
Sector	IT
Shares o/s (mn)	172
Market cap. (Rs mn)	312,402
Market cap. (US\$ mn)	4,398
3-m daily average value (Rs mn)	1,775
52-week high / low	Rs1,990 / 1,078
Nifty / Sensex	36,387 / 10,907

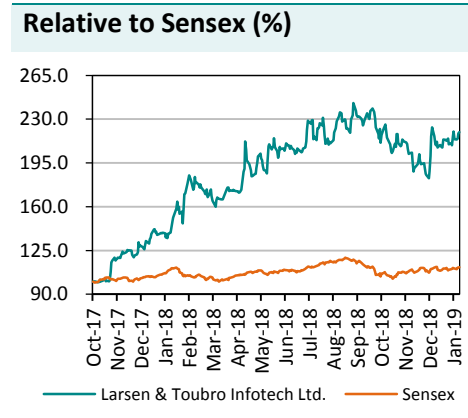


Exhibit 1: Financial snapshot

(Rs mn)

Year-end: March	Q3FY19	Q2FY19	QoQ (%)	Q3FY18	YoY (%)
Revenues (US\$ mn)	346.9	328.5	5.6	293.5	18.2
Revenues	24,729	23,312	6.1	18,837	31.3
COGS	15,776	15,225	3.6	12,218	29.1
Gross profit	8,953	8,087	10.7	6,619	35.3
SG&A	3,865	3,297	17.2	3,404	13.5
EBITDA	5,088	4,790	6.2	3,215	58.3
Depreciation & amortization	355	368	(3.5)	403	(11.9)
EBIT	4,733	4,422	7.0	2,812	68.3
Other income	290	944	(69.3)	883	(67.2)
PBT	5,023	5,366	(6.4)	3,695	35.9
Tax	1,268	1,363	(7.0)	866	46.4
Minority interest	0	2	n.m.	0	n.m.
Adjusted net profit	3,755	4,005	(6.2)	2,829	32.7
Exceptional items	0	0	n.m.	0	n.m.
Reported net profit	3,755	4,005	(6.2)	2,829	32.7
Recurring EPS (Rs)	21.7	23.1	(6.4)	16.5	31.4
As % of net revenue					
Gross profit	36.2	34.7		35.1	
SG&A	15.6	14.1		18.1	
EBITDA	20.6	20.5		17.1	
EBIT	19.1	19.0		14.9	
Reported net profit	15.2	17.2		15.0	
Tax rate	25.2	25.4		23.4	

Source: Company; IDBI Capital Research

Exhibit 2: Actual vs. estimates

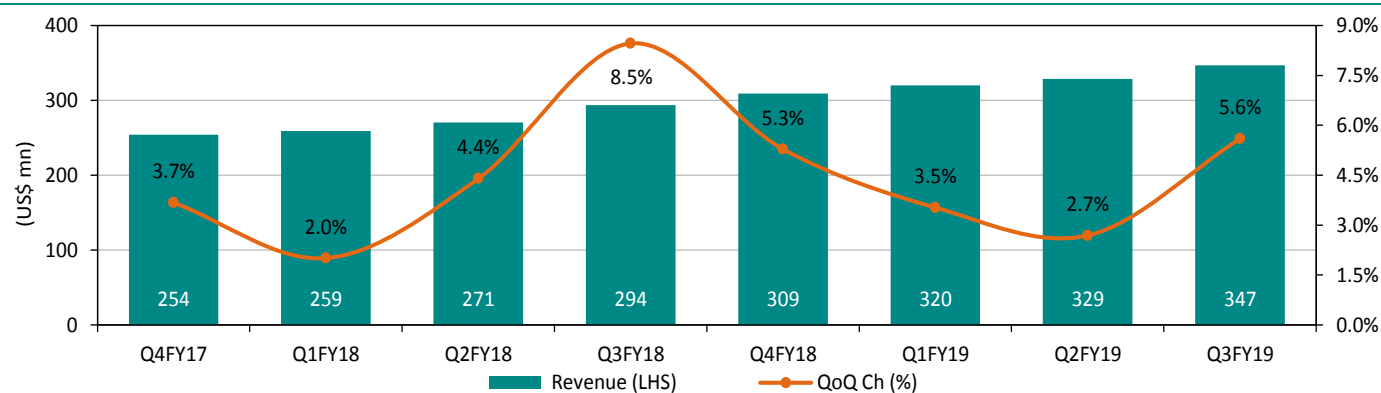
Year to March	Q3FY19	Q3FY19E	Variance (%)
Revenue (US\$ mn)	346.9	341.5	1.6
Revenue (Rs mn)	24,729	24,616	0.5
EBIT (Rs mn)	4,733	4,522	4.7
EBIT margin (%)	19.1	18.4	77bps
PAT (Rs mn)	3,755	3,426	9.6
PAT margin (%)	15.2	13.9	127bps
EPS (Rs)	21.7	19.8	9.4

Source: Company; IDBI Capital Research

Exhibit 3: Earnings Revision

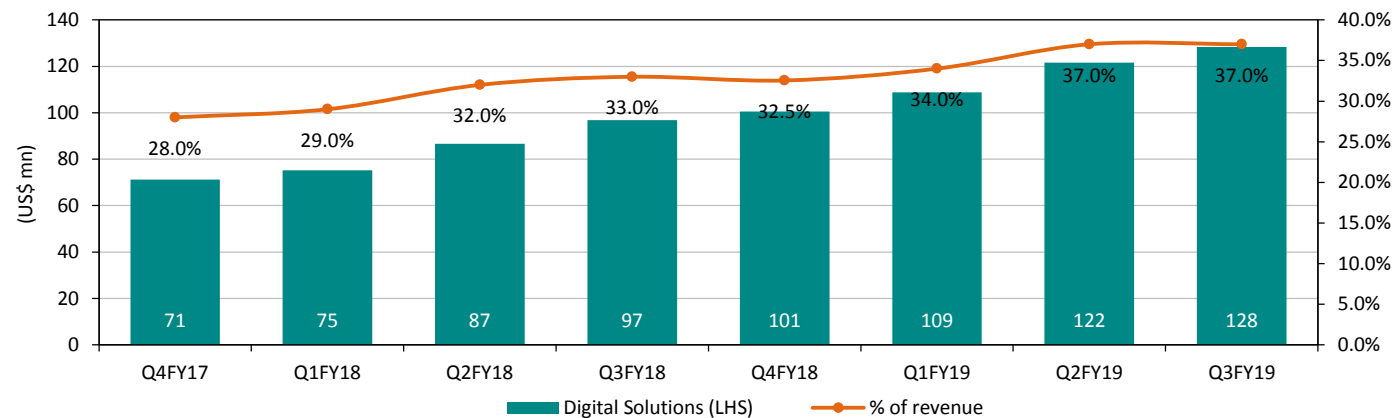
Year-end: March	FY19E		Chg (%)	FY20E		Chg (%)
	New	Old		New	Old	
Revenue (US\$ mn)	1,351	1,343	0.5	1,554	1,544	0.6
Revenue (Rs mn)	94,471	93,519	1.0	108,781	108,090	0.6
EBIT (Rs mn)	17,783	17,234	3.2	20,000	19,612	2.0
EBIT margin (%)	18.8	18.4	40bps	18.4	18.1	24bps
EPS (Rs)	88.7	86.6	2.4	96.3	94.5	1.9

Source: Company; IDBI Capital Research

Exhibit 4: Q3FY19 revenue was higher than our forecast


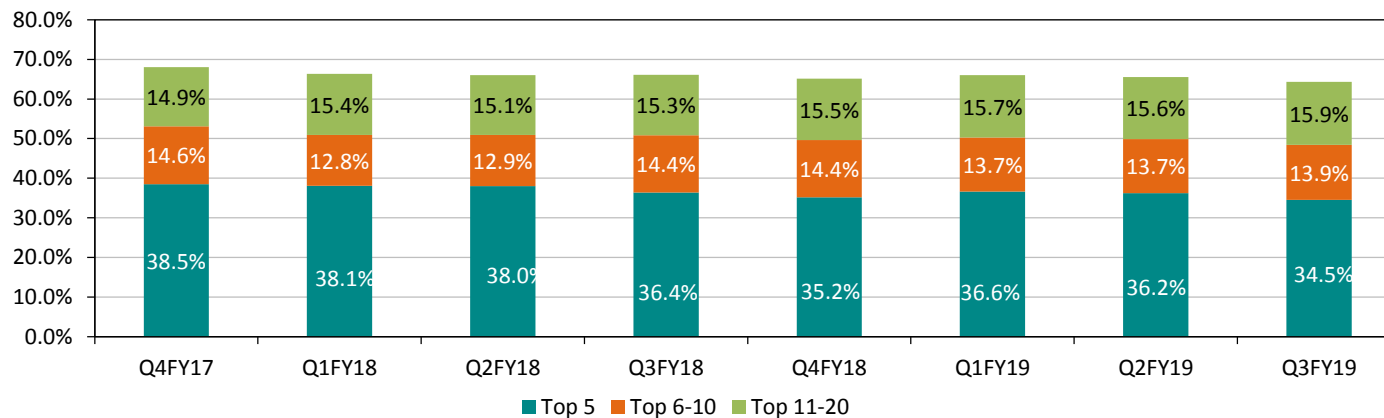
Source: Company; IDBI Capital Research

Exhibit 5: Digital solutions maintained the growth momentum



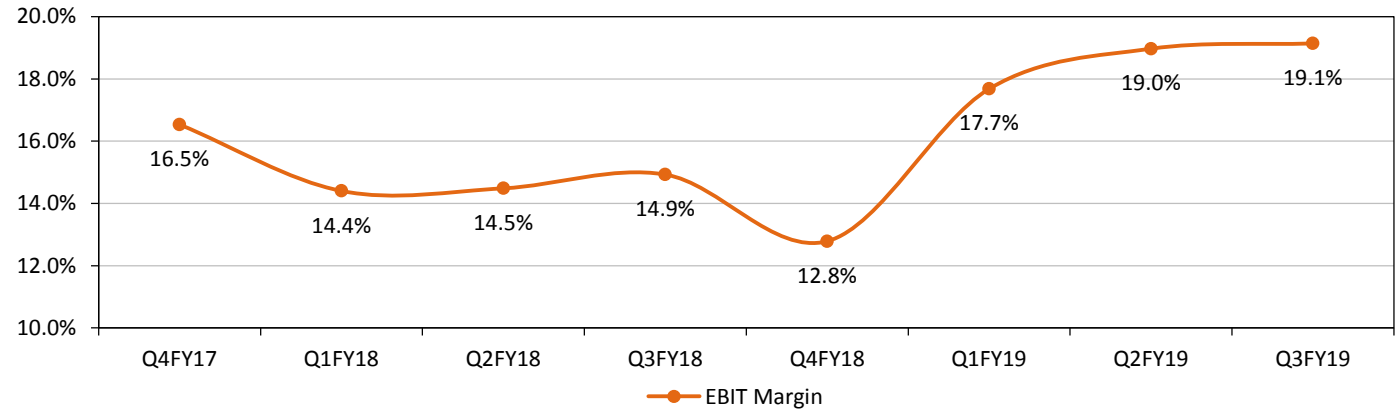
Source: Company; IDBI Capital Research

Exhibit 6: Q3FY19 growth was driven by non-top 5 clients



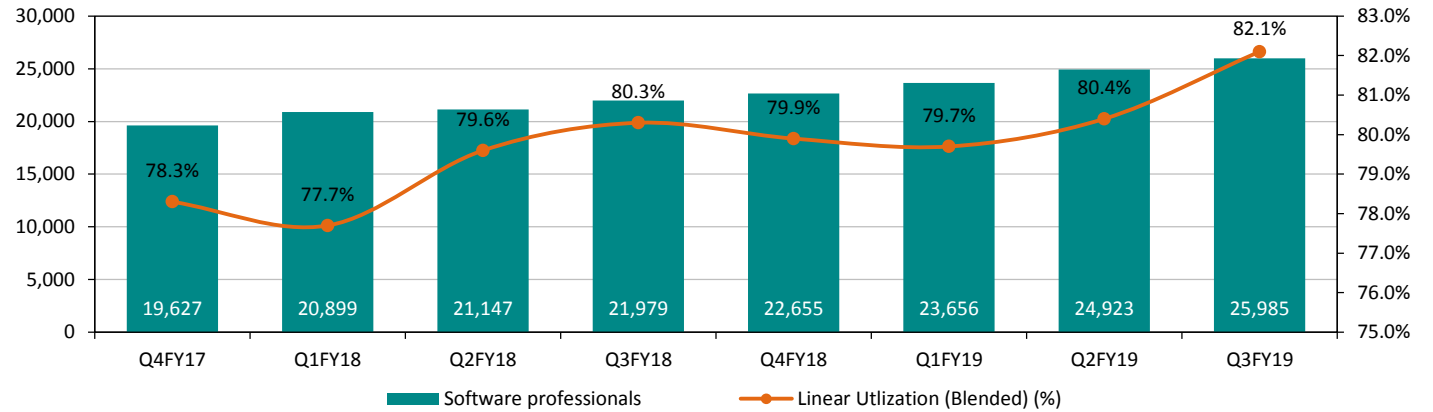
Source: Company; IDBI Capital Research

Exhibit 7: Q3FY19 EBIT margin was higher than our forecast



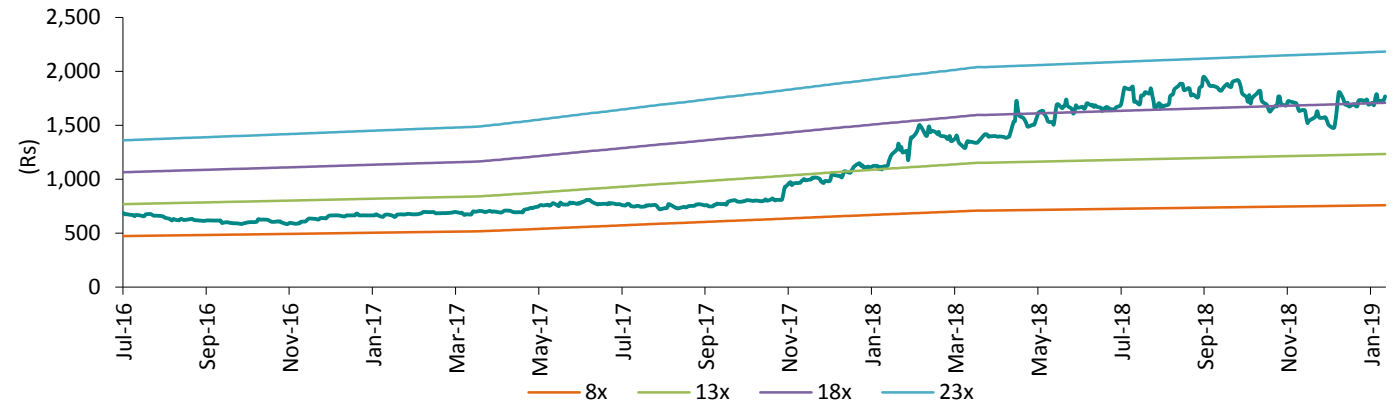
Source: Company; IDBI Capital Research

Exhibit 8: Utilisation saw an uptick in Q3FY19



Source: Company; IDBI Capital Research

Exhibit 9: One-year forward PER trend



Source: Company; IDBI Capital Research

Financial Summary

Profit & Loss Account

(Rs mn)

Year-end: March	FY17	FY18	FY19E	FY20E
Net sales	65,009	73,064	94,471	108,781
<i>growth (%)</i>	11.2	12.4	29.3	15.1
Operating expenses	(52,707)	(61,189)	(75,212)	(87,178)
EBITDA	12,302	11,875	19,259	21,603
<i>growth (%)</i>	20.0	(3.5)	62.2	12.2
Depreciation	(1,779)	(1,562)	(1,476)	(1,603)
EBIT	10,523	10,313	17,783	20,000
Interest paid	(32)	(158)	(103)	(80)
Other income	1,867	4,260	2,755	2,145
Pre-tax profit	12,358	14,415	20,435	22,065
Tax	(2,649)	(3,290)	(5,193)	(5,516)
<i>Effective tax rate (%)</i>	21.4	22.8	25.4	25.0
Minority Interest	(2.0)	(3.0)	(1.0)	-
Net profit	9,707	11,122	15,242	16,549
Adjusted net profit	9,707	11,122	15,242	16,549
<i>growth (%)</i>	16.1	14.6	37.0	8.6
<i>Shares o/s (mn nos)</i>	171	172	172	172

Cash Flow Statement

(Rs mn)

Year-end: March	FY17	FY18	FY19E	FY20E
Pre-tax profit	12,358	14,415	20,435	22,065
Depreciation	1,282	1,562	1,482	1,603
Tax paid	(1,947)	(4,716)	(5,193)	(5,516)
Chg in working capital	1,897	(6,096)	(119)	3,020
Other operating activities	1,228	5,353	(1,086)	(666)
Cash flow from operations (a)	14,818	10,518	15,520	20,505
Capital expenditure	(143)	(3,004)	(800)	(1,000)
Chg in investments	-	-	-	-
Other investing activities	-	-	-	-
Cash flow from investing (b)	(143)	(3,004)	(800)	(1,000)
Equity raised/(repaid)	0	1	-	-
Debt raised/(repaid)	(546)	-	-	-
Dividend (incl. tax)	(3,393)	(4,443)	(6,199)	(7,026)
Chg in minorities	1	2	-	-
Other financing activities	-	-	-	-
Cash flow from financing (c)	(3,938)	(4,439)	(6,199)	(7,026)
Net chg in cash (a+b+c)	10,737	3,075	8,521	12,480

Balance Sheet

(Rs mn)

Year-end: March	FY17	FY18	FY19E	FY20E
Net fixed assets	5,432	6,874	6,192	5,589
Investments	-	-	-	-
Other non-curr assets	3,469	2,189	2,847	3,278
Current assets	33,287	41,942	55,079	67,676
Inventories	-	-	-	-
Sundry Debtors	11,697	22,327	25,883	25,333
Cash and Bank	13,201	16,276	24,797	37,277
Loans and advances	3,665	2,214	2,847	3,278
Total assets	42,188	51,005	64,119	76,543
Shareholders' funds	31,443	38,598	47,640	57,163
Share capital	171	172	172	172
Reserves & surplus	31,272	38,426	47,469	56,992
Total Debt	-	-	-	-
Secured loans	-	-	-	-
Unsecured loans	-	-	-	-
Other liabilities	(1,263)	(2,689)	(2,689)	(2,689)
Curr Liab & prov	12,000	15,083	19,153	22,054
Current liabilities	10,365	11,918	15,271	17,584
Provisions	1,635	3,165	3,882	4,470
Total liabilities	10,737	12,394	16,464	19,365
Total equity & liabilities	42,188	51,005	64,119	76,543
Book Value (Rs)	184	225	277	333

Source: Company; IDBI Capital Research

Financial Ratios

Year-end: March	FY17	FY18	FY19E	FY20E
Adj. EPS (Rs)	56.9	64.7	88.7	96.3
Adj. EPS growth (%)	15.8	13.7	37.0	8.6
EBITDA margin (%)	18.9	16.3	20.4	19.9
Pre-tax margin (%)	19.0	19.7	21.6	20.3
ROE (%)	36.8	31.8	35.3	31.6
ROCE (%)	42.1	31.2	44.0	40.2
Turnover & Leverage ratios (x)				
Asset turnover (x)	1.8	1.6	1.6	1.5
Leverage factor (x)	1.3	1.3	1.3	1.3
Net margin (%)	14.9	15.2	16.1	15.2
Net Debt/Equity (x)	(0.4)	(0.4)	(0.5)	(0.7)
Working Capital & Liquidity ratio				
Inventory days	0	0	0	0
Receivable days	66	112	100	85
Payable days	23	25	25	25

Valuation

Year-end: March	FY17	FY18	FY19E	FY20E
P/E (x)	31.7	27.8	20.3	18.7
Price / Book value (x)	9.8	8.0	6.5	5.4
PCE (x)	26.8	24.4	18.5	17.1
EV / Net sales (x)	4.5	4.0	3.0	2.5
EV / EBITDA (x)	23.9	24.7	14.8	12.6
Dividend Yield (%)	0.9	1.2	1.7	1.9



Notes

Dealing	(91-22) 6836 1111	dealing@idbicapital.com
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Key to Ratings Stocks:

BUY: Absolute return of 15% and above; **ACCUMULATE:** 5% to 15%; **HOLD:** Upto ±5%; **REDUCE:** -5% to -15%; **SELL:** -15% and below.

IDBI Capital Markets & Securities Ltd.

Equity Research Desk

6th Floor, IDBI Tower, WTC Complex, Cufee Parade, Colaba, Mumbai – 400 005. Phones: (91-22) 2217 1700; Fax: (91-22) 2215 1787; Email: info@idbicapital.com

SEBI Registration: BSE & NSE (Cash & FO) – INZ000007237, NSDL – IN-DP-NSDL-12-96, Research – INH000002459, CIN – U65990MH1993GOI075578

Compliance Officer: Christina D’souza; Email: compliance@idbicapital.com; Telephone: (91-22) 2217 1907

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