

# HCL Technologies

## HOLD

Miss on all front

### Summary

HCL Technologies' (HCLT) revenue growth was below our estimates mainly led by underperformance of product business. The company's IT services revenues (88% of revenues) increased 5.2% QoQ partially offset by 8% QoQ decline in product revenues. Going forward, we expect the company to report healthy growth in IT services revenues (~12% YoY) in FY22 partially offset by flat growth in product business. Further, the company's aim to increase payout to 75% of net income for next 5 years is key positives. However, lower than expected revenue growth compared to industry and recent run up in price prompt us to maintain HOLD rating on the stock with a target price of Rs 1,355 (24x FY23 EPS).

### Key Highlights and Investment Rationale

#### Revenue growth guidance of double digit maintain for FY22

Revenue growth of 2.6%/11.3% QoQ/yoY in US\$ and +3.5%/10.5% in CC driven by strong growth across services portfolio led by digital business, engineering and cloud services. EBIT margin of 19% -60bps QoQ. Mode-2 solutions(25.8% of revenue) continued to lead the growth, +12.5%/36.3% QoQ/YoY in CC. Amongst verticals, growth was led by Lifesciences & Healthcare (15.3% of revenue) grew by 7%/20.1% QoQ/YoY in CC. US\$5100 mn+ clients increased by 1 QoQ to 15. LTM attrition increased to 15.7% vs 11.8% sequentially. HCLT secured 14 large deals during the quarter at US\$2.24bn up by 38% YoY. For FY22, HCLT reiterated its guidance for a double-digit revenue growth in CC, and EBIT margin guidance of 19% to 21%.

#### Cloud and app modernisation to drive revenue growth

HCLT is seeing acceleration in multi-year deal, cloud, cloud consulting, cloud migration, app modernisation. The company's tenure of deals has also increased to five years from three years. Apart from healthy deal wins, HCLT plans to invest in Australia, Canada, France, Germany, Japan and emerging markets like Brazil, Mexico, South Korea and Spain, which, we believe, bodes well for medium term revenue growth (as the company can tap existing customers to drive growth). This coupled with healthy deal pipeline; robust hiring and improvement in Europe prompt us to build in 11.1% CAGR growth in FY21-23E.

TP	Rs1,355
CMP	Rs1,251
Potential upside / downside	+8%
Previous Rating	HOLD

### V/s Consensus

EPS (Rs)	FY22E	FY23E
IDBI Capital	48.6	56.5
Consensus	49.7	56.9
% difference	(2.3)	(0.6)

### Shareholding Pattern (%)

Promoters	60.3
FII	23.2
DII	12.2
Public	5.3

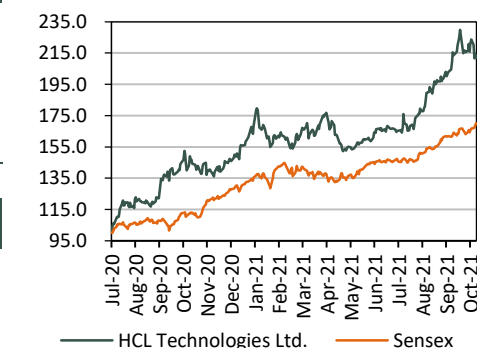
### Price Performance (%)

	-1m	-3m	-12m
Absolute	1.0	26.4	40.5
Rel to Sensex	(4.2)	10.5	(9.7)

### Key Stock Data

Bloomberg / Reuters	HCLT IN/ HCLT.BO
Sector	IT Services
Shares o/s (mn)	2,714
Market cap. (Rs mn)	3,394,524
Market cap. (US\$ mn)	45,105
3-m daily avg Trd value (Rs mn)	3,863.6
52-week high / low	Rs1,377 / 801
Sensex / Nifty	61,306 / 18,339

### Relative to Sensex (%)



### Financial snapshot

Year	FY19	FY20	FY21	FY22E	FY23E
Revenue	6,04,280	7,06,780	7,53,790	8,35,452	9,42,683
EBITDA	1,39,690	1,66,930	1,93,280	2,03,279	2,37,636
EBITDA (%)	23.1	23.6	25.6	24.3	25.2
Adj. PAT	1,01,230	1,09,252	1,24,340	1,31,923	1,53,209
EPS (Rs)	37.3	40.3	45.8	48.6	56.5
EPS Growth (%)	18.3	7.9	13.8	6.1	16.1
PE (x)	34.3	31.8	28.0	26.4	22.7
Dividend Yield (%)	0.3	0.5	2.0	2.8	3.1
EV/EBITDA (x)	24.4	20.4	17.4	16.4	13.9
RoE (%)	26.0	23.6	22.4	21.4	23.4
RoCE (%)	28.7	26.8	24.3	23.8	26.6

Source: IDBI Capital Research;

## Exhibit 1: Financial snapshot

(Rs mn)

Q2FY22 revenue growth of 3.5% QoQ in CC was below our forecast.

EBIT margin of 19% was at the lower end of the guided band.

Year-end: March	Q2FY22	Q1FY22	QoQ (%)	Q2FY21	YoY (%)
<b>Revenues (US\$ mn)</b>	<b>2,791</b>	<b>2,720</b>	<b>2.6</b>	<b>2,507</b>	<b>11.3</b>
<b>Revenues</b>	<b>2,06,550</b>	<b>2,00,680</b>	<b>2.9</b>	<b>1,85,940</b>	<b>11.1</b>
COGS	1,31,270	1,25,930	4.2	1,12,790	16.4
Gross profit	75,280	74,750	0.7	73,150	2.9
SG&A	26,900	25,670	4.8	23,640	13.8
<b>EBITDA</b>	<b>48,380</b>	<b>49,080</b>	<b>(1.4)</b>	<b>49,510</b>	<b>(2.3)</b>
Depreciation & amortization	9,220	9,770	(5.6)	9,350	(1.4)
<b>EBIT</b>	<b>39,160</b>	<b>39,310</b>	<b>(0.4)</b>	<b>40,160</b>	<b>(2.5)</b>
Other income	2,070	1,940	6.7	1,360	52.2
PBT	41,230	41,250	(0.0)	41,520	(0.7)
Tax	8,460	8,940	(5.4)	9,990	(15.3)
Minority interest	130	160	(18.8)	110	n.m.
<b>Reported net profit</b>	<b>32,640</b>	<b>32,150</b>	<b>1.5</b>	<b>31,420</b>	<b>3.9</b>
<b>Diluted EPS (Rs)</b>	<b>12.0</b>	<b>11.8</b>	<b>1.5</b>	<b>11.6</b>	<b>3.9</b>
<b>As % of net revenue</b>					
Gross profit	36.4	37.2		39.3	
SG&A	13.0	12.8		12.7	
EBITDA	23.4	24.5		26.6	
EBIT	19.0	19.6		21.6	
Reported net profit	15.8	16.0		16.9	
Tax rate	20.5	21.7		24.1	

Source: Company; IDBI Capital Research

**Exhibit 2: Earnings Revision**

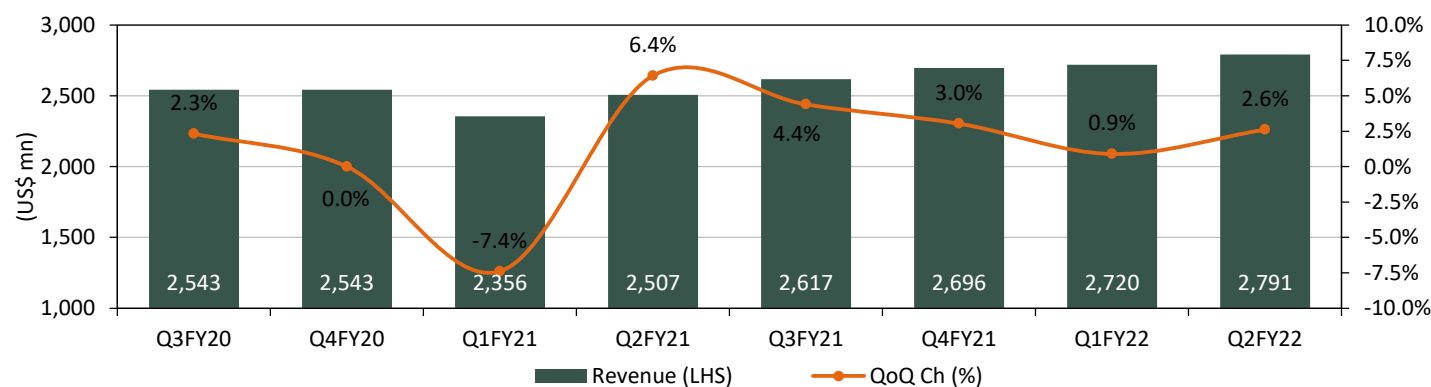
Year-end: March	FY22F			FY23F		
	New	Old	Chg (%)	New	Old	Chg (%)
Revenue (US\$ mn)	11,298	11,364	(0.6)	12,569	12,519	0.4
Revenue (Rs bn)	835.5	839.7	(0.5)	942.7	926.4	1.8
EBIT (Rs bn)	165.7	153.5	7.9	197.7	162.9	21.4
EBIT margin (%)	19.8	18.3	155bps	21.0	17.6	339bps
EPS (Rs)	48.6	44.5	9.3	56.5	47.0	20.1

Source: Company; IDBI Capital Research

**Exhibit 3: Actual vs. estimates**

Year to March	Q2FY22	Q2FY22E	Variance (%)
Revenue (US\$ mn)	2,791	2,824	(1.2)
Revenue (Rs mn)	206,550	208,369	(0.9)
EBIT (Rs mn)	39,160	38,561	1.6
EBIT margin (%)	19.0%	18.5%	45bps
PAT (Rs mn)	32,640	29,868	9.3
PAT margin (%)	15.8%	14.3%	147bps
EPS (Rs)	12.0	11.0	9.3

Source: Company; IDBI Capital Research

**Exhibit 4: Q2FY22 revenue growth was below our forecast**

Source: Company; IDBI Capital Research

**Exhibit 5: Growth in large clients**

Year-end: March	Q3FY20	Q4FY20	Q1FY21	Q2FY21	Q3FY21	Q4FY21	Q1FY22	Q2FY22
US\$100m +	15	15	15	14	15	15	14	15
US\$50m +	32	30	29	29	31	35	37	41
US\$20m +	94	96	93	91	97	96	104	109
US\$10m +	167	171	173	172	173	178	178	190
US\$5m +	302	308	320	317	312	318	326	329
US\$1m +	712	791	848	865	814	809	817	836

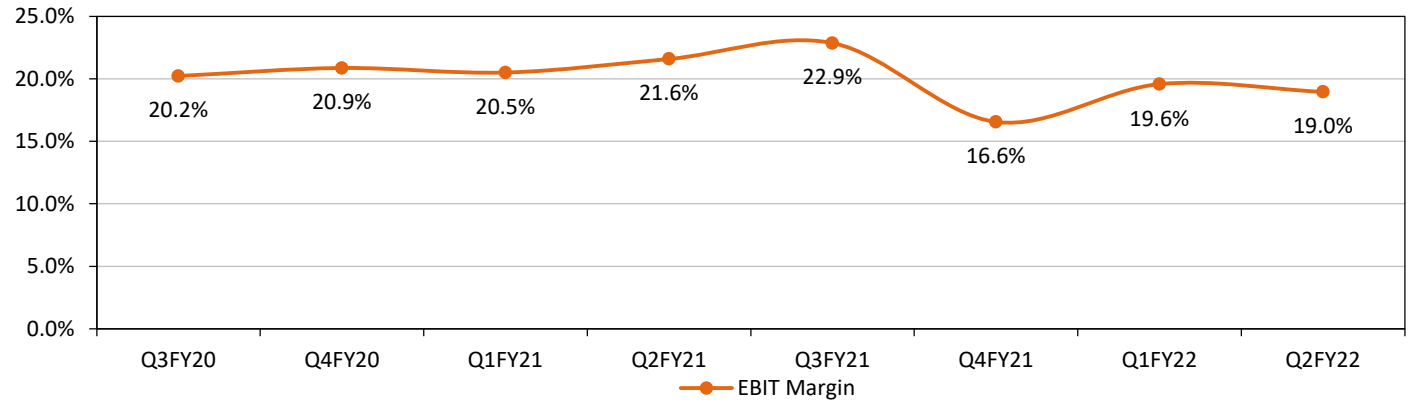
Source: Company; IDBI Capital Research

**Exhibit 6: Revenue growth across various segments (%)**

Parameters	% of revenue	QoQ CC growth	YoY CC growth
Overall revenue growth		3.5	10.5
<b>Geography</b>			
US	62.8	2.4	10.7
Europe	28.3	5.8	9.0
ROW	8.9	4.0	14.9
<b>Service-lines</b>			
IT and Business services	72.6	5.2	13.2
Engineering and R&D Services	15.7	5.4	12.7
Products and Platforms	11.7	(8.0)	(5.5)
<b>Verticals</b>			
Financial Services	21.3	0.4	6.3
Manufacturing	17.9	8.1	11.9
Technology & Services	17.2	2.6	10.8
Telecom & Media Publishing	7.9	3.0	3.6
Retail & CPG	9.8	0.9	13.4
Life science & Healthcare	15.3	7.0	20.1
Public Services	10.6	1.9	8.8
<b>Mode 1-2-3 solutions</b>			
Mode 1	60.9	2.8	6.1
Mode 2	25.8	12.5	36.3
Mode 3	13.3	(7.6)	(6.40)

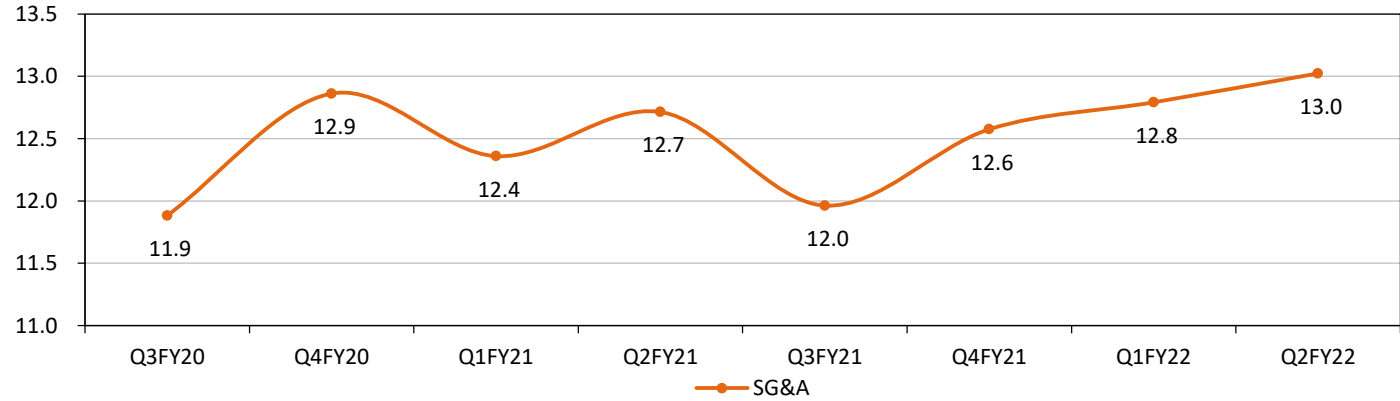
Source: Company; IDBI Capital Research

**Exhibit 7: Q2FY22 EBIT margin was at the lower end of guided band**



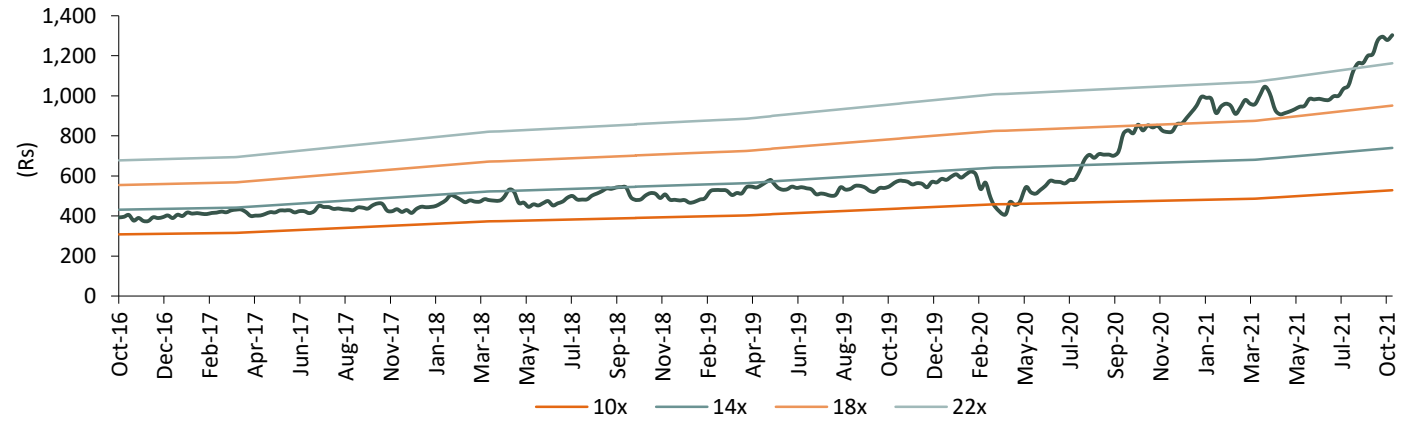
Source: Company; IDBI Capital Research

**Exhibit 8: SG&A saw a QoQ uptick**



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	FY20	FY21	FY22E	FY23E
<b>Net sales</b>	7,06,780	7,53,790	8,35,452	9,42,683
<i>Growth (%)</i>	17.0	6.7	10.8	12.8
Operating expenses	(5,39,850)	(5,60,510)	(6,32,173)	(7,05,047)
<b>EBITDA</b>	<b>1,66,930</b>	<b>1,93,280</b>	<b>2,03,279</b>	<b>2,37,636</b>
<i>Growth (%)</i>	19.5	15.8	5.2	16.9
Depreciation	(28,400)	(39,850)	(37,564)	(39,897)
<b>EBIT</b>	<b>1,38,530</b>	<b>1,53,430</b>	<b>1,65,715</b>	<b>1,97,739</b>
Other income	1,790	6,570	6,570	7,607
<b>Pre-tax profit</b>	<b>1,40,320</b>	<b>1,60,000</b>	<b>1,72,285</b>	<b>2,05,346</b>
Tax	(30,748)	(35,100)	(39,672)	(51,336)
<i>Effective tax rate (%)</i>	21.9	21.9	23.0	25.0
Minority Interest	(320.0)	(560.0)	(690.0)	(800.0)
<b>Net profit</b>	<b>1,09,252</b>	<b>1,24,340</b>	<b>1,31,923</b>	<b>1,53,209</b>
<b>Adjusted net profit</b>	<b>1,09,252</b>	<b>1,24,340</b>	<b>1,31,923</b>	<b>1,53,209</b>
<i>Growth (%)</i>	7.9	13.8	6.1	16.1
<i>Shares o/s (mn nos)</i>	2,714	2,714	2,714	2,714

### Cash Flow Statement

(Rs mn)

Year-end: March	FY20	FY21	FY22E	FY23E
Pre-tax profit	1,40,320	1,60,000	1,72,285	2,05,346
Depreciation	19,000	39,850	37,564	39,897
Tax paid	(30,758)	(23,140)	(39,672)	(51,336)
Chg in working capital	57,750	(54,560)	2,636	(11,394)
Other operating activities	(17,980)	32,445	(12,426)	(16,310)
<b>Cash flow from operations (a)</b>	<b>1,68,331</b>	<b>1,54,595</b>	<b>2,00,387</b>	<b>1,66,202</b>
Capital expenditure	(1,40,190)	(37,900)	(28,880)	(25,000)
Chg in investments	80	(120)	-	-
Other investing activities	-	-	-	-
<b>Cash flow from investing (b)</b>	<b>(1,40,110)</b>	<b>(38,020)</b>	<b>(28,880)</b>	<b>(25,000)</b>
Equity raised/(repaid)	2	-	-	-
Debt raised/(repaid)	9,920	(8,650)	-	-
Dividend (incl. tax)	(19,604)	(70,555)	(97,692)	(1,08,547)
Chg in minorities	190	(410)	-	-
Other financing activities	-	-	-	-
<b>Cash flow from financing (c)</b>	<b>(9,491)</b>	<b>(79,615)</b>	<b>(97,692)</b>	<b>(1,08,547)</b>
<b>Net chg in cash (a+b+c)</b>	<b>18,730</b>	<b>36,960</b>	<b>33,815</b>	<b>32,655</b>



**Balance Sheet**

(Rs mn)

Year-end: March	FY20	FY21	FY22E	FY23E
Net fixed assets	3,52,420	3,50,470	3,41,787	3,26,890
Investments	770	890	890	890
Other non-curr assets	66,700	68,260	75,534	85,229
<b>Current assets</b>	<b>3,86,000</b>	<b>4,30,510</b>	<b>4,95,737</b>	<b>5,78,682</b>
Inventories	910	940	1,144	1,291
Sundry Debtors	1,41,310	1,36,630	1,51,068	1,80,789
Cash and Bank	1,19,650	1,56,610	1,90,168	2,18,396
Loans and advances	34,220	48,410	54,934	61,985
<b>Total assets</b>	<b>8,05,890</b>	<b>8,50,130</b>	<b>9,13,948</b>	<b>9,91,690</b>
<b>Shareholders' funds</b>	<b>5,12,670</b>	<b>5,99,130</b>	<b>6,33,362</b>	<b>6,78,024</b>
Share capital	5,427	5,427	5,427	5,427
Reserves & surplus	5,07,243	5,93,703	6,27,934	6,72,597
<b>Total Debt</b>	<b>46,930</b>	<b>38,280</b>	<b>38,280</b>	<b>38,280</b>
Secured loans	-	-	-	-
Unsecured loans	46,930	38,280	38,280	38,280
Other liabilities	25,900	37,200	42,293	49,049
<b>Curr Liab &amp; prov</b>	<b>2,18,850</b>	<b>1,73,830</b>	<b>1,97,633</b>	<b>2,23,157</b>
Current liabilities	2,01,100	1,51,370	1,68,278	1,88,990
Provisions	17,750	22,460	29,354	34,167
<b>Total liabilities</b>	<b>2,91,680</b>	<b>2,49,310</b>	<b>2,78,206</b>	<b>3,10,486</b>
<b>Total equity &amp; liabilities</b>	<b>8,05,890</b>	<b>8,50,130</b>	<b>9,13,948</b>	<b>9,91,690</b>
<b>Book Value (Rs)</b>	<b>189</b>	<b>221</b>	<b>233</b>	<b>250</b>

Source: Company; IDBI Capital Research

**Financial Ratios**

Year-end: March	FY20	FY21	FY22E	FY23E
Adj. EPS (Rs)	40.3	45.8	48.6	56.5
Adj. EPS growth (%)	7.9	13.8	6.1	16.1
EBITDA margin (%)	23.6	25.6	24.3	25.2
Pre-tax margin (%)	19.9	21.2	20.6	21.8
ROE (%)	23.6	22.4	21.4	23.4
ROCE (%)	26.8	24.3	23.8	26.6
<b>Turnover &amp; Leverage ratios (x)</b>				
Asset turnover (x)	1.0	0.9	0.9	1.0
Leverage factor (x)	1.5	1.5	1.4	1.5
Net margin (%)	15.5	16.5	15.8	16.3
Net Debt/Equity (x)	(0.1)	(0.2)	(0.2)	(0.3)
<b>Working Capital &amp; Liquidity ratio</b>				
Inventory days	0	0	1	1
Receivable days	73	66	66	70
Payable days	8	11	11	11

**Valuation**

Year-end: March	FY20	FY21	FY22E	FY23E
P/E (x)	31.8	28.0	26.4	22.7
Price / Book value (x)	6.8	5.8	5.5	5.1
PCE (x)	25.3	21.2	20.5	18.0
EV / Net sales (x)	4.8	4.5	4.0	3.5
EV / EBITDA (x)	20.4	17.4	16.4	13.9
Dividend Yield (%)	0.5	2.0	2.8	3.1



# Notes

Dealing

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**Key to Ratings Stocks:****BUY:** 15%+; **HOLD:** -5% to 15%; **SELL:** -5% and below.**IDBI Capital Markets & Securities Ltd.****Equity Research Desk**

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