

BUY

TP: Rs 1,190 | ▲ 25%

HCL TECHNOLOGIES

| IT Services

| 23 April 2021

Q4 in line; deal wins gain momentum

HCL Tech (HCLT) reported 3% QoQ dollar revenue growth in Q4FY21, in line with our estimate. EBIT margin stood at 20.4%, down 250bps QoQ. Management has guided for double-digit topline growth in FY22 and margins in the 19-21% range. We keep FY22/FY23 EPS estimates largely unchanged. Rolling valuations over, we have a new Mar'22 TP of Rs 1,190 (vs. Rs 1,150) based on an unchanged P/E of 18.8x. The company's healthy deal wins and cloud/infrastructure expertise offer good midterm growth visibility. BUY.

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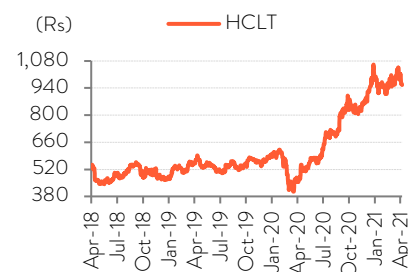
Robust in-line performance: Q4 revenue grew 3% USD/2.5% CC QoQ, in line with our estimate of 3% USD/2.4% CC. Growth was driven by the Mode-1 and 2 businesses which grew 3.7% and 6.2% QoQ, USD respectively. Demand has risen for digital, cloud, products and platforms. Among verticals, energy and utilities, life sciences and BFSI led the way. Five of seven verticals posted positive USD growth. EBIT margin was at a 20.4% (21% est.), down 250bps QoQ due to salary hikes, seasonality and fresher hiring. A one-off milestone bonus-related expense of ~Rs 5.8bn saw reported PAT decline 40% QoQ.

Healthy FY22 guidance: Management has guided for double-digit revenue growth in FY22, in line with our estimates. EBIT margin is guided to be in the range of 19-21%. HCLT registered a record 19 deal wins vs. 13 in Q3FY21 and 14 in Q4FY20. Most are mid-sized deals spanning 3-5 years. The pipeline for products and platforms also remains strong.

Maintain BUY: We remain positive on HCLT given continued strength of its Mode-2 and Mode-3 businesses which have performed well despite Covid-19, strong deal wins and stable margins. We expect 13.6%/10.2% USD growth for FY22/FY23 and EBIT margin in the range of 21.5-22%.

Ticker/Price	HCLT IN/Rs 956
Market cap	US\$ 34.6bn
Shares o/s	2,713mn
3M ADV	US\$ 77.5mn
52wk high/low	Rs 1,067/Rs 465
Promoter/FPI/DII	60%/27%/13%

Source: NSE

STOCK PERFORMANCE

Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21P	FY22E	FY23E
Total revenue (Rs mn)	604,280	706,780	753,790	884,469	997,050
EBITDA (Rs mn)	140,020	166,930	200,560	239,573	270,762
Adj. net profit (Rs mn)	99,757	110,940	130,660	148,833	171,734
Adj. EPS (Rs)	36.7	40.9	48.1	54.8	63.3
Adj. EPS growth (%)	16.3	11.5	17.8	13.9	15.4
Adj. ROAE (%)	25.2	23.5	22.9	22.6	23.1
Adj. P/E (x)	26.1	23.4	19.8	17.4	15.1
EV/EBITDA (x)	18.4	15.4	12.9	10.8	9.2

Source: Company, BOBCAPS Research | P – Provisional

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Other highlights

- HCLT will be investing in expanding into near-shore locations such as Brazil, Mexico, Spain, South Korea and Canada in FY22. Appointment of geographical sales leadership will also be a part of the investment.
- ER&D services growth remained weak due to the pandemic's impact on the automobile and aerospace subsegments.
- ~16,800 employees were hired in Q4FY21.
- Interim dividend of Rs 6/sh was announced for the quarter.

FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q4FY21	Q4FY20	YoY (%)	Q3FY21	QoQ (%)	FY21	FY20	YoY (%)
Revenues (US\$ mn)	2,696	2,543	6.0	2,617	3.0	10,175	9,936	2.4
Revenue	196,420	185,900	5.7	193,020	1.8	753,790	706,780	6.7
Operating Expenditure	145,450	138,700	4.9	138,600	4.9	553,230	539,850	2.5
Cost of revenues	117,400	111,510	5.3	111,950	4.9	445,920	443,080	0.6
as % of sales	59.8	60.0	-	58.0	-	59.2	62.7	-
SG&A expenses	28,050	27,190	3.2	26,650	5.3	107,310	96,770	10.9
as % of sales	14.3	14.6	-	13.8	-	14.2	13.7	-
EBITDA	50,970	47,200	8.0	54,420	(6.3)	200,560	166,930	20.1
Depreciation	11,170	8,390	-	10,270	-	39,850	28,400	40.3
EBIT	39,800	38,810	2.6	44,150	(9.9)	160,710	138,530	16.0
Other Income	1,900	(130)	-	1,270	-	6,570	1,780	269.1
PBT	41,700	38,680	7.8	45,420	(8.2)	167,280	140,310	19.2
Total Tax	11,910	7,070	-	5,440	-	36,630	29,380	24.7
Adjusted PAT	29,790	31,610	(5.8)	39,980	(25.5)	130,650	110,930	17.8
(Profit)/loss from JV's/Ass/MI	(170)	(80)	-	(160)	-	(570)	(320)	-
APAT after MI	29,620	31,530	(6.1)	39,820	(25.6)	130,080	110,620	17.6
Extra ordinary items	5750	0	-	0	-	5,750	0	-
Reported PAT	23,870	31,530	(24.3)	39,820	(40.1)	135,830	110,620	22.8
Reported EPS	10.9	11.6	(6.1)	14.7	(25.6)	48	41	17.6
Margins (%)			(bps)		(bps)			(bps)
EBITDA	25.9	24.6	130	28.2	(220)	26.6	23.6	300
EBIT	20.4	20.2	-	22.9	(250)	21.3	19.6	170
EBT	21.2	20.6	60	23.5	(230)	22.2	19.9	230
PAT	15.1	16.8	(170)	20.6	(560)	17.3	15.7	160
Effective Tax rate	28.6	18.5	1,010	12.0	1,660	21.9	20.9	100

Source: BOBCAPS Research, Company

FIG 2 – OPERATING METRICS

(in US\$ terms)	Q4FY21 (% Contri. to revenue)	Growth	
		QoQ (%)	YoY (%)
Revenue by Business Segment			
Mode 1	61.4	3.7	0.0
Mode 2	23.4	6.2	29.2
Mode 3	15.2	(3.9)	2.6
Revenue by Geography			
US	62.0	2.2	3.7
Europe	29.1	1.6	7.5
Asia Pacific	8.9	14.6	20.9
Revenue by Service Offering			
IT and Business Services	71.9	5.2	8.0
Engineering and R&D Services	15.1	0.4	(1.8)
Products & Platforms	13.0	(5.0)	5.2
Revenues by Industry			
BFSI	21.6	4.0	8.5
Retail	10.1	(0.9)	5.0
Media, Publishing & Entertainment	8.1	0.6	3.4
Life Sciences	14.1	6.8	19.6
Energy Utilities -Public Sector	11.2	11.0	7.9
Manufacturing	17.7	0.8	(9.4)
Technology Services	17.2	(0.4)	12.5
Client Contribution to Revenue			
Top 5	13.2	0.7	(8.2)
Top 10	20.9	2.5	(1.9)
Top 20	30.8	2.7	(0.9)
Employee Metrics			
	Q4FY21	Q3FY21	Q4FY20
Total Employees	168,977	159,682	150,423
Gross Addition	16,878	12,422	10,278
Net Addition	9,295	6,597	1,250
Revenues by Contract Type (%)			
Time & material	32.3	31.6	31.7
Fixed Price	67.7	68.4	68.3

Source: BOBCAPS Research

Valuation methodology

We keep FY22/FY23 EPS estimates broadly unchanged. On rollover, we move to a revised Mar'22 target price of Rs 1,190 (from Rs 1,150), set at an unchanged one-year forward P/E multiple of 18.8x. Our target price pencils in HCLT's strong margin guidance for FY22 and its commitment towards enhancing the Mode-2 and 3 portfolios (which command higher margins).

Reiterate BUY as we see relatively strong near-to-mid-term growth visibility for the company on the back of its growing Mode-2 software business (23% of revenue), healthy large-deal wins (19 contracts won in Q4FY21), and IMS heritage that offers unique positioning to leverage the cloud migration opportunity being accelerated by the pandemic.

FIG 3 – REVISED ESTIMATES

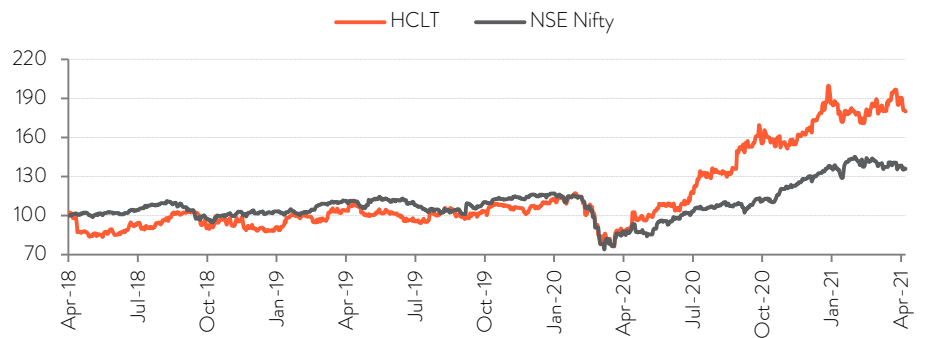
(Rs mn)	FY22E			FY23E		
	Old	New	Chg (%)	Old	New	Chg (%)
Revenues (US\$ mn)	11,330	11,559	2.0	12,399	12,741	2.8
YoY growth (%)	11.4	13.6	-	9.4	10.2	-
Revenues	866,906	884,469	2.0	967,129	997,050	3.1
EBITDA	232,633	239,573	3.0	261,409	270,762	3.6
EBITDA margin (%)	26.8	27.1	-	27.0	27.2	-
EBIT margin (%)	21.6	21.8	-	22.1	22.2	-
Net profits	149,993	148,833	(0.8)	171,473	171,734	0.2
EPS (Rs)	55.3	54.8	(0.8)	63.2	63.3	0.2

Source: BOBCAPS Research

FIG 4 – PEER COMPARISON

Company	Rating	Target Price (Rs)	US\$ revenue CAGR FY21-23E (%)	EPS (Rs)		ROE (%)		Target PE (x)
				FY22E	FY23E	FY22E	FY23E	
TCS	BUY	3,780	17.2	118	135	44	41	28.0
INFO	ADD	1,540	13.1	56	59	30	30	26.0
HCLT	BUY	1,190	11.9	55	63	23	23	18.8
TECHM	BUY	1,130	15.1	64	76	21	23	15.7
LTI	BUY	4,740	20.1	136	161	33	33	30.4
MPHL	REDUCE	1,550	14.4	81	96	22	24	16.9
MTCL	ADD	2,180	14.4	89	93	31	28	23.4
PSYS	SELL	1,260	12.8	57	68	16	17	19.2
COFORGE	BUY	3,350	24.2	121	154	24	25	22.0

Source: BOBCAPS Research

FIG 5 – RELATIVE STOCK PERFORMANCE

Source: NSE

Key risks

Downside risks to our estimates include:

- above-expected revenue contraction in IMS due to automation,
- above-expected HCL Software client attrition,
- an inability to renew existing contracts, and
- adverse currency movement.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21P	FY22E	FY23E
Total revenue	604,280	706,780	753,790	884,469	997,050
EBITDA	140,020	166,930	200,560	239,573	270,762
Depreciation	21,480	28,400	39,850	46,624	49,440
EBIT	118,540	138,530	160,710	192,949	221,323
Net interest income/(expenses)	(1,693)	0	0	0	0
Other income/(expenses)	7,720	1,790	6,580	2,883	6,139
Exceptional items	0	0	0	0	0
EBT	124,567	140,320	167,290	195,833	227,462
Income taxes	24,810	29,380	36,630	47,000	55,728
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
Reported net profit	99,757	110,940	130,660	148,833	171,734
Adjustments	0	0	0	0	0
Adjusted net profit	99,757	110,940	130,660	148,833	171,734

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21P	FY22E	FY23E
Accounts payables	0	0	0	0	0
Other current liabilities	126,860	259,090	217,050	309,564	348,967
Provisions	0	0	0	17,689	19,941
Debt funds	39,860	50,930	39,070	39,070	39,070
Other liabilities	4,540	5,280	5,850	5,850	5,850
Equity capital	2,812	2,812	2,812	2,812	2,812
Reserves & surplus	414,888	514,048	612,248	689,463	778,558
Shareholders' fund	422,240	522,140	620,910	698,125	787,220
Total liabilities and equities	588,960	832,160	877,030	1,064,448	1,195,198
Cash and cash eq.	59,290	48,430	65,150	201,281	298,181
Accounts receivables	146,100	177,720	175,250	218,088	245,848
Inventories	0	0	0	0	0
Other current assets	37,160	79,030	74,290	88,447	99,705
Investments	58,520	105,680	140,220	168,264	185,090
Net fixed assets	132,396	62,440	62,450	34,955	5,080
CWIP	0	0	0	0	0
Intangible assets	102,564	294,210	291,500	291,500	291,500
Deferred tax assets, net	0	0	0	0	0
Other assets	52,930	64,650	68,170	61,913	69,793
Total assets	588,960	832,160	877,030	1,064,448	1,195,198

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21P	FY22E	FY23E
Net income + Depreciation	120,740	139,340	170,510	195,457	221,173
Interest expenses	(4,480)	(1,790)	(6,580)	(2,883)	(6,139)
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(24,660)	47,020	(38,350)	59,466	(5,243)
Other operating cash flows	(1,936)	(40,905)	(47,246)	0	0
Cash flow from operations	89,664	143,665	78,334	252,039	209,791
Capital expenditures	(34,340)	(150,090)	(39,860)	(19,129)	(19,564)
Change in investments	5,200	47,160	34,540	28,044	16,826
Other investing cash flows	(3,604)	1,790	6,580	(53,206)	(27,514)
Cash flow from investing	(32,744)	(101,140)	1,260	(44,290)	(30,252)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	36,230	0	0	0	0
Interest expenses	(39,860)	0	0	0	0
Dividends paid	(10,990)	(53,384)	(62,874)	(71,618)	(82,638)
Other financing cash flows	0	0	0	0	0
Cash flow from financing	(14,620)	(53,384)	(62,874)	(71,618)	(82,638)
Changes in cash and cash eq.	42,300	(10,859)	16,720	136,130	96,901
Closing cash and cash eq.	59,290	48,430	65,151	201,281	298,181

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21P	FY22E	FY23E
Reported EPS	36.7	40.9	48.1	54.8	63.3
Adjusted EPS	36.7	40.9	48.1	54.8	63.3
Dividend per share	14.7	16.4	19.3	21.9	25.3
Book value per share	155.2	192.4	228.8	257.3	290.1

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21P	FY22E	FY23E
EV/Sales	4.3	3.6	3.4	2.9	2.5
EV/EBITDA	18.4	15.4	12.9	10.8	9.2
Adjusted P/E	26.1	23.4	19.8	17.4	15.1
P/BV	6.2	5.0	4.2	3.7	3.3

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21P	FY22E	FY23E
Tax burden (Net profit/PBT)	80.1	79.1	78.1	76.0	75.5
Interest burden (PBT/EBIT)	105.1	101.3	104.1	101.5	102.8
EBIT margin (EBIT/Revenue)	19.6	19.6	21.3	21.8	22.2
Asset turnover (Revenue/Avg TA)	112.6	99.5	88.2	91.1	88.2
Leverage (Avg TA/Avg Equity)	1.4	1.5	1.5	1.5	1.5
Adjusted ROAE	25.2	23.5	22.9	22.6	23.1

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21P	FY22E	FY23E
YoY growth (%)					
Revenue	19.5	17.0	6.7	17.3	12.7
EBITDA	22.4	19.2	20.1	19.5	13.0
Adjusted EPS	16.3	11.5	17.8	13.9	15.4
Profitability & Return ratios (%)					
EBITDA margin	23.2	23.6	26.6	27.1	27.2
EBIT margin	19.6	19.6	21.3	21.8	22.2
Adjusted profit margin	16.5	15.7	17.3	16.8	17.2
Adjusted ROAE	25.2	23.5	22.9	22.6	23.1
ROCE	24.9	23.4	22.2	25.7	31.1
Working capital days (days)					
Receivables	81	84	85	81	85
Inventory	0	0	0	0	0
Payables	92	130	157	149	165
Ratios (x)					
Gross asset turnover	4.8	7.3	12.1	18.2	49.8
Current ratio	2.3	1.4	1.8	1.7	1.9
Net interest coverage ratio	NA	NA	NA	NA	NA
Adjusted debt/equity	0.0	0.0	0.0	(0.2)	(0.3)

Source: Company, BOBCAPS Research

Disclaimer

Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

ADD – Expected return from >+5% to +15%

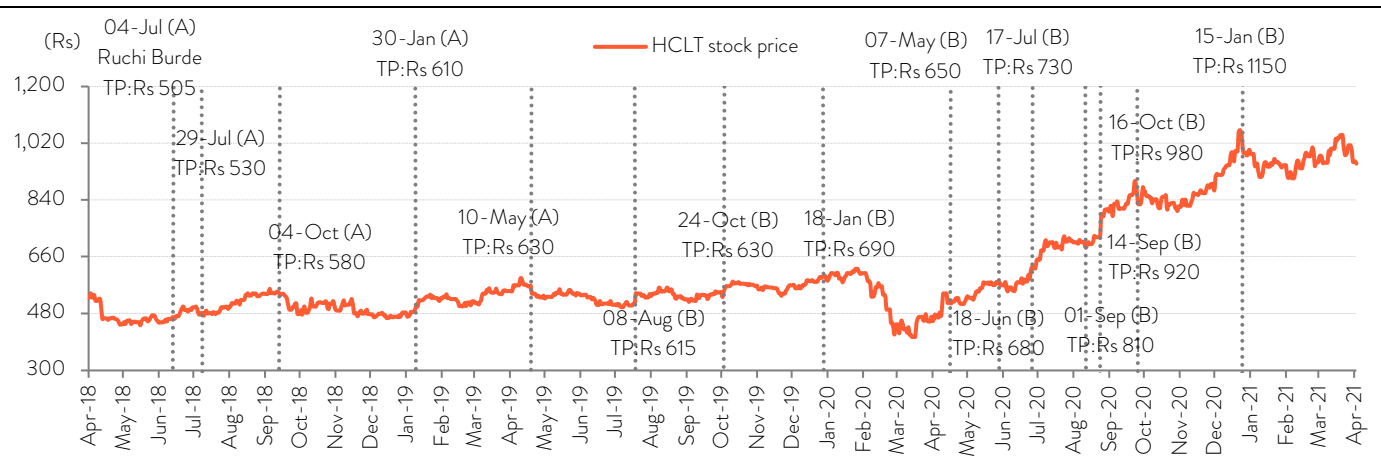
REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

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RATINGS AND TARGET PRICE (3-YEAR HISTORY): HCL TECHNOLOGIES (HCLT IN)



B – Buy, A – Add, R – Reduce, S – Sell

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