

HCL Technologies Limited



HCL Technologies Limited.
Modest Performance; business model shifts to subscription drags P&P contribution

 CMP Target Potential Upside
INR 1,102 INR 1,391 26.2%

 Market Cap (INR Mn) Recommendation
INR 2,989,916 BUY

 Sector
Internet Software & Services
Synopsis:

HCL Technologies Limited (HCLT) Q4FY22 performance was lower than with our estimate and posted a soft quarter, dollar revenue witnessed a meagre growth by 0.5% QoQ, impacted by a steep decline in the P&P business. Revenue guidance of 12-14% CC (vs. 12.7% CC in FY22) implies a 2.4-3.2% CQGR, supported by USD 8.2bn net-new TCV signings and P&P base impact, but without any contribution from mega deals. Services business grew by 5%, crossing a milestone of USD 10bn in FY22 (CQGR of ~5.2% for 3 consecutive quarters). Products and Platforms (P&P) business optically declined seasonally at a higher-than-expected rate of 24% QoQ. Underlying metrics are extremely healthy with record headcount addition, steady progression of clients across higher size buckets and lower-than-peer attrition. Proactive investments in digital competencies, especially on data, cloud and experience did impact margins but have improved the durability of growth. Our target price of INR 1,391 is based on 21.5x Mar-24E EPS with EPS CAGR of 15.3% over FY22-24E.

MARKET DATA

Shares outs (Mn)	2,714
Mkt Cap (INR Mn)	2,989,916
52 Wk H/L (INR)	1377/891.25
Volume Avg (3m K)	3955.5
Face Value (INR)	2
Bloomberg Code	HCLT:IN

KEY FINANCIALS

(INR Mn)	Q4FY22A	Q3FY22A	Q4FY21A	QoQ	YoY	KRChoksey Est.	Variance (%)
USD Revenue	2,993	2,977	2,696	0.5%	11.0%	3,024	-1.0%
Revenue	2,25,970	2,23,310	1,96,577	1.2%	15.0%	2,27,231	-0.6%
EBIT	40,690	42,572	40,039	-4.4%	1.6%	40,910	-0.5%
PAT	35,930	34,421	29,867	4.4%	20.3%	32,976	9.0%
OPM (%)	18.0%	19.1%	20.4%	-106	-236	18.0%	0
NPM(%)	15.9%	15.4%	15.2%	49	71	14.5%	139

Source: Company, KRChoksey Research

SHARE PRICE PERFORMANCE

IT services excel; P&P business: challenges ahead

HCLT posted a soft quarter, dollar revenue witnessed a meagre growth by 0.5% QoQ, impacted by a steep decline in the P&P business. Revenue guidance of 12-14% CC (vs. 12.7% CC in FY22) implies a 2.4-3.2% CQGR, supported by USD 8.2bn net-new TCV signings and P&P base impact, but without any contribution from mega deals. As per HCLT, except the seasonal impact in 1QFY23, services business will continue to see good momentum while the P&P business would remain volatile in the near term and the decline in P&P business in FY22 (down 1.3% CC terms YoY) is largely due to shift from lumpy license sales to a subscription model and also due to discontinuation of certain products. Revenue growth guidance for FY23E is expected to hover around 12-14% in CC terms, on the back of accelerated investments in geo expansion/pricing lever in mode-2, 31% rise in FY22 deal annual contract value (ACV) and strong commentary on pipeline aiding growth visibility, P&P recovery in the medium term, with increase in subscription and support composition (currently 67% of P&P revenue) as well as growing services cross-sell (10% of services pipeline from product client base);

Strong deal wins to drive growth across geographies

HCLT booked net-new TCV of USD 2.2bn, which included six large services deals, and FY22 TCV growth was 14%. Within verticals, telecom M&E, manufacturing, and life-sciences & healthcare led the growth. Deal wins are continuing with smaller/faster deal cycles, especially in front-office transformation, talent supply gaps among clients leading to extension of outsourcing deals with enhanced scope and cloud transformation. The company has announced a fair number of deals in Europe geography. Net additions were robust at 11,100 in Q4 (~40k in FY22), taking the headcount to 208k, supported by 23k fresher adds in FY22. Clients billing more than USD 20mn, USD 50mn and USD 100mn increased by 8, 1 and 1 on sequential basis.

EBIT margin guidance band to 18-20%

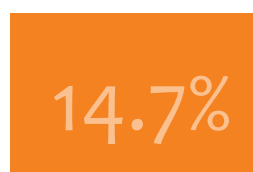
In Q4FY22, the company registered EBIT margin of 18% which is lower by 106 bps QoQ, impacted by the P&P business seasonality and offset by better services margin. Management has reduced margin guidance to the lower end of the 18-20% range for FY23, factoring in salary hikes and higher discretionary spends. As of now, management finds no significant difference in client spending behavior and indicated only a marginal impact due to the adverse macro-economic situation.

MARKET INFO

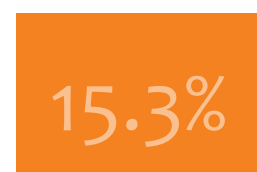
SENSEX	57,197
NIFTY	17,172

SHARE HOLDING PATTERN (%)

Particulars	Mar-22	Dec-21	Sep-21
Promoters	60.7	60.3	60.3
FIIIs	19	20.3	22.3
DIIIs	14.7	13.7	12.47
Others	5.6	5.7	4.9
Total	100	100	100



Revenue CAGR between FY22 and FY24E



PAT CAGR between FY22 and FY24E

HCL Technologies Limited.

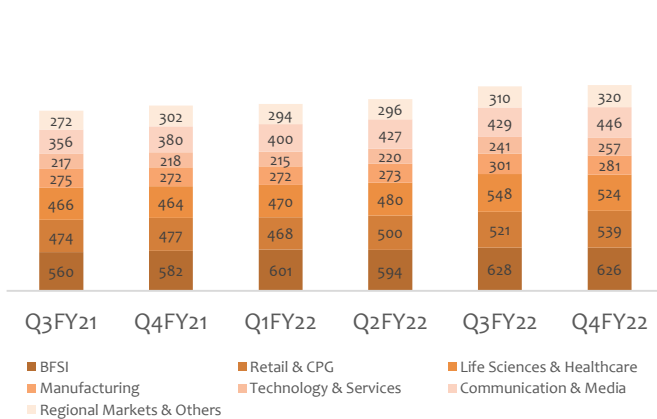
Key Concall Highlights:

(i) The P&P business declined by 24% CC QoQ due to seasonality and was worse than the high teen decline that was guided for by HCLT at the beginning of the quarter (ii) Q4FY22 EBIT margin at 18% contracted by 106bps QoQ and indicates that services business margin improved by 85bps (65bps due to recovery of seasonal leaves impact and 20bps on account of operational efficiencies), which was offset by a decline in the P&P segment margin (iii) Net new bookings came in at USD 2.26bn v/s USD 2.135bn in 3QFY22, but declined by 27% YoY, as expected, due a very large base. The total TCV at USD 8.3bn for FY22 grew by 14% YoY and ACV grew by 27% YoY. 10 large deals were signed in Q4FY22 (6 in Services and 4 in products business) (iv) HCLT has launched 2 new 5G applications in Q4FY22 to help mobile network operators optimize client experience and reduce energy consumption (v) Life Sciences & Healthcare, which grew by 18.5% YoY on the back of rapid growth in remote patient monitoring, which involves devices like BP monitors, pulse oximeters etc (vi) Manufacturing segment grew by 16.6% YoY, backed by its new framework, Envision, to help next-generation enterprises by deploying cutting-edge solutions

Valuation and view

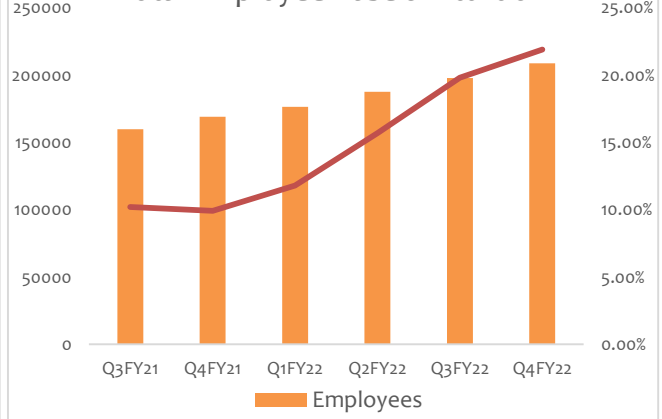
HCLT is currently trading at a valuation with a P/E multiple of 19.7x/17.1x on FY23E/FY24E earnings. HCLT has reported strong growth on the back of accelerated investments in geo expansion/pricing lever in mode-2, rise in FY22 deal (ACV) and strong commentary on pipeline, P&P recovery in the medium term, with an increase in subscription/support composition as well as growing cross-sell services. Hence we are maintaining our target price of INR 1,391 per share with a P/E multiple of 21.5x to the FY24 estimated EPS of INR 64.6, an upside of 26.2% over the CMP. Accordingly, we upgrade our rating to “BUY” rating to the stock.

Vertical-wise Revenue Contribution (USD Mn)



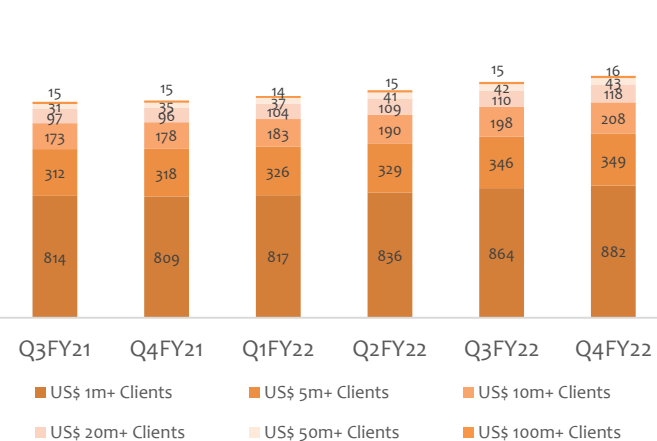
Source: Company, KRChoksey Research

Total Employee Base & Attrition



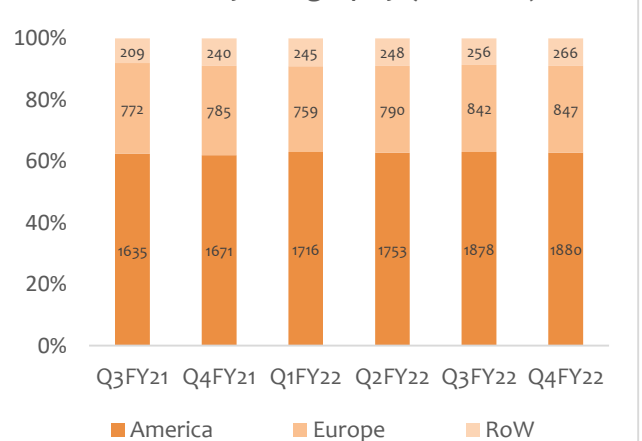
Source: Company, KRChoksey Research

Client Contribution



Source: Company, KRChoksey Research

Revenue by Geography (USD Mn)



Source: Company, KRChoksey Research

HCL Technologies Limited.

KEY FINANCIALS

Exhibit 1: Balance Sheet

Particulars (INR Mn)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Property, Plant and Equipment	46,538	52,701	58,440	56,420	42,637	41,970	43,261
Right-of-use Asset	0	0	26240	23920	23920	23920	23920
CWIP	5,310	5,310	4,000	3,210	3,210	3,210	3,210
Intangible Assets	1,44,057	1,76,950	2,94,210	2,91,500	2,91,500	2,91,500	2,91,500
Other non current assets	37,675	52,940	64,640	68,160	68,160	68,160	68,160
Investments	5,222	3,900	380	470	470	470	470
Total non current assets	2,38,801	2,91,800	4,47,910	4,43,680	4,29,897	4,29,230	4,30,521
Cash & equivalent	74205	91710	83850	137170	197919	227761	280098
Accounts receivable (Net)	96,394	1,17,060	1,41,340	1,36,630	1,51,858	1,72,145	1,90,805
Unbilled revenue	26,181	29,040	36,380	38,620	55,830	61,480	70,871
Investment securities, available for sale	23,572	22,200	69,880	67,730	67,730	67,730	67,730
Other current assets	25,198	37,160	52,800	50,370	50,370	50,370	50,370
Total current assets	2,45,550	2,97,170	3,84,250	4,30,520	5,23,707	5,79,485	6,59,874
Total Assets	4,84,351	5,88,970	8,32,160	8,74,200	9,53,604	10,08,715	10,90,395
Equity Share Capital	2,803	2,751	5,426	5,427	5,427	5,427	8,141
Other Equity	3,65,365	4,14,949	5,11,434	6,09,633	6,80,457	7,44,541	8,13,869
Equity Attributable to Owners of the Company	3,68,168	4,17,700	5,16,860	6,15,060	6,85,885	7,49,968	8,22,010
Non controlling Interest	0	4,540	5,280	5,850	5,850	5,850	5,850
Total Equity	3,68,168	4,22,240	5,22,140	6,20,910	6,91,735	7,55,818	8,27,860
Operating Lease Liability	0	0	24,720	22,670	22,670	22,670	22,670
Other liabilities	12,669	15,390	25,490	26,820	26,820	26,820	26,820
Borrowings	4,371	39,860	50,920	39,070	35,163	31,256	31,256
Total non current liabilities	17,040	55,250	1,01,130	88,560	84,653	80,746	80,746
Trade Payables	17,887	18,028	15,816	24,275	23,409	22,111	24,346
Current portion of capital lease obligations	444	1,067	1,639	1,877	1,877	1,877	1,877
Short term loans	1,717	11,262	21,096	824	12,658	8,438	8,438
Accrued employee costs	20,672	27,933	29,931	41,339	39,743	35,327	35,327
Deferred revenues	6,645	10,664	25,378	31,940	34,538	38,034	42,156
Income Tax Liabilities	6,822	9,377	10,089	13,347	13,862	15,235	18,514
Other current liabilities	44,957	33,149	1,04,940	51,129	51,129	51,129	51,129
Total Current Liabilities	99,143	1,11,480	2,08,890	1,64,730	1,77,216	1,72,152	1,81,789
Total liabilities	4,84,351	5,88,970	8,32,160	8,74,200	9,53,604	10,08,715	10,90,395

Source: Company, KRChoksey Research

HCL Technologies Limited.

KEY FINANCIALS

Exhibit 2: Profit & Loss Statement

Particulars (INR Mn)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Revenue	5,05,700	6,04,270	7,06,780	7,53,790	8,56,510	9,77,760	11,25,959
Employee Cost	3,32,370	3,83,160	4,40,180	4,45,910	5,27,600	5,86,701	6,57,491
SG&A and Other Cost	58,930	81,100	99,660	1,07,310	1,23,610	1,46,664	1,80,153
EBITDA	1,14,400	1,40,010	1,66,940	2,00,570	2,05,300	2,44,395	2,88,314
Depreciation	14,530	21,470	28,410	39,850	43,260	57,245	71,027
EBIT	99,870	1,18,540	1,38,530	1,60,720	1,62,040	1,87,149	2,17,287
Other income, net	11,796	9,463	5,429	9,407	7,470	8,171	8,410
Finance costs	696	1,743	3,649	2,837	2,840	2,989	3,118
Pre-tax Income	1,10,970	1,26,260	1,40,310	1,67,290	1,66,670	1,92,331	2,22,579
Income tax expense	23,160	24,810	29,380	36,630	34,280	40,390	46,742
Net profit Before EI & MI	87,810	1,01,450	1,10,930	1,30,660	1,32,390	1,51,942	1,75,837
Minority Interest, MI	10	220	310	560	560	560	560
Net profit Before MI	87,800	1,01,230	1,10,620	1,30,100	1,31,830	1,51,382	1,75,277
Diluted EPS (INR)	63.81	73.58	40.76	47.94	48.58	55.79	64.59
Shares in Million	1,402	1,376	2,714	2,714	2,714	2,714	2,714

Source: Company, KRChoksey Research

Exhibit 3: Free Cash Flow Analysis

Particulars (INR Mn)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Net Cash Generated From Operations	91,061	1,25,952	1,71,190	1,72,852	1,86,971	2,13,011	2,50,641
Net Cash Flow from/(used in) Investing Activities	-27,195	-41,576	-41,020	-37,940	-32,605	-53,857	-67,654
Net Cash Flow from Financing Activities	2,330	47,703	33,670	-30,791	7,927	-8,126	2,714
Others	82,543	75,815	1,63,024	69,190	1,01,544	1,21,186	1,33,363
Net Inc/Dec in cash equivalents	-16,347	56,264	816	34,931	60,749	29,842	52,338
Opening Balance	1,52,019	1,35,672	1,91,937	1,92,753	1,37,170	1,97,919	2,27,761
Closing Balance Cash and Cash Equivalents	1,35,672	1,91,937	1,92,753	2,27,684	1,97,919	2,27,761	2,80,098

Source: Company, KRChoksey Research

Exhibit 4: Ratio Analysis

Key Ratio	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
EBIT Margin (%)	19.7%	19.6%	19.6%	21.3%	18.9%	19.1%	19.3%
Tax rate (%)	20.9%	19.6%	20.9%	21.9%	20.6%	21.0%	21.0%
Net Profit Margin (%)	17.4%	16.8%	15.7%	16.5%	15.4%	15.5%	15.6%
RoE (%)	25.0%	25.8%	23.7%	22.0%	20.3%	21.0%	21.8%
RoCE (%)	22.1%	22.6%	20.7%	20.2%	18.6%	19.4%	20.4%
EV/EBITDA (x)	20.8	17.1	14.2	11.5	11.0	9.1	7.5
EPS (INR per share)	32.4	73.6	40.8	47.9	48.6	55.8	64.6

Source: Company, KRChoksey Research

HCL Technologies Limited.

HCL Technologies Limited				Rating Legend (Expected over a 12-month period)	
Date	CMP (INR)	TP(INR)	Recommendation	Our Rating	Upside
22-Apr-22	1102	1391	BUY	Buy	More than 15%
17-Jan-22	1268	1391	ACCUMULATE	Accumulate	5% – 15%
14-Oct-21	1251	1391	ACCUMULATE	Hold	0 – 5%
				Reduce	-5% – 0
				Sell	Less than – 5%

ANALYST CERTIFICATION:

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KR Choksey Shares and Securities Pvt. Ltd

Registered Office:

1102, Stock Exchange Tower, Dalal Street, Fort, Mumbai – 400 001.

Phone: +91-22-6633 5000; Fax: +91-22-6633 8060.

Corporate Office:

ABHISHEK, 5th Floor, Link Road, Andheri (W), Mumbai – 400 053.

Phone: +91-22-6696 5555; Fax: +91-22-6691 9576.