

July 13, 2022

Q1FY23 Result Update

☑ Change in Estimates | ☑ Target | ■ Reco

Change in Estimates

	Current		Previous	
	FY23E	FY24E	FY23E	FY24E
Rating	HOLD		HOLD	
Target Price	982		1,007	
Sales (Rs. m)	9,76,038	10,70,173	9,76,942	10,78,454
% Chng.	(0.1)	(0.8)		
EBITDA (Rs. m)	2,10,182	2,38,170	2,17,667	2,45,300
% Chng.	(3.4)	(2.9)		
EPS (Rs.)	49.8	57.7	52.5	59.3
% Chng.	(5.1)	(2.6)		

Key Financials - Consolidated

Y/e Mar	FY21	FY22	FY23E	FY24E
Sales (Rs. bn)	754	857	976	1,070
EBITDA (Rs. bn)	193	200	210	238
Margin (%)	25.6	23.4	21.5	22.3
PAT (Rs. bn)	124	135	135	156
EPS (Rs.)	45.8	49.8	49.8	57.7
Gr. (%)	12.3	8.8	0.0	15.9
DPS (Rs.)	26.0	44.0	20.0	12.0
Yield (%)	2.8	4.7	2.2	1.3
RoE (%)	22.0	21.9	20.8	21.1
RoCE (%)	25.1	24.6	24.8	24.7
EV/Sales (x)	3.1	2.8	2.4	2.1
EV/EBITDA (x)	12.2	11.8	11.2	9.5
PE (x)	20.3	18.6	18.6	16.1
P/BV (x)	4.1	4.1	3.7	3.1

Key Data

HCLT.BO | HCLT IN

52-W High / Low	Rs.1,378 / Rs.925
Sensex / Nifty	53,887 / 16,058
Market Cap	Rs.2,518bn/ \$ 31,629m
Shares Outstanding	2,714m
3M Avg. Daily Value	Rs.3453.13m

Shareholding Pattern (%)

Promoter's	60.95
Foreign	19.97
Domestic Institution	13.68
Public & Others	5.40
Promoter Pledge (Rs bn)	-

Stock Performance (%)

	1M	6M	12M
Absolute	(8.6)	(31.4)	(5.3)
Relative	(7.9)	(22.1)	(7.9)

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HCL Technologies (HCLT IN)

Rating: HOLD | CMP: Rs928 | TP: Rs982

Margin weakens further

Quick Pointers:

- Negative surprise - Sharp drop of 180bps QoQ in IT services margins.
- New deal TCV is \$2bn, 23.4% YoY, -9% QoQ and ACV is up by 17.9% YoY.
- Low headcount addition of ~2K, 1% QoQ.

HCLT reported largely in-line revenue of USD 3025 mn, +2.7% QoQ CC (PLe: 2.9%, Cons: 2.4%), +1.1% QoQ USD (PLe: 1%, Cons: 0.8%). Growth was led by Products (5.1% QoQ CC), followed by ER&D (3.7% QoQ CC). IT services growth was muted at 2% QoQ CC, as productivity benefits to be provided to clients kicked-in. EBIT margin declined by 100bps QoQ to 17% led by 180bps QoQ decline in IT services margin, due to higher talent costs amidst elevated levels and deal transition costs. Management has retained its margin guidance of 18-20% for FY23, but given headwinds from wage hikes spread across Q2 and Q3, we model EBIT margin at 17.5%/18% for FY23/24.

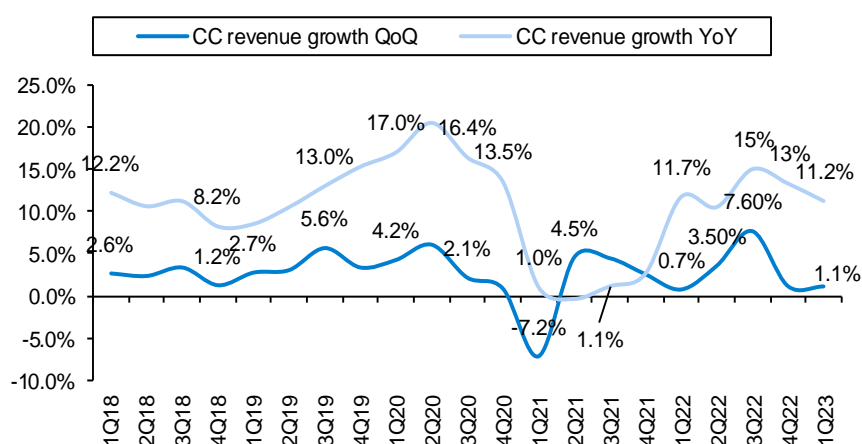
We cut EPS estimates by 5%/2.6% for FY23/24 due to cut in margin estimates. We continue to value HCLT on 17x FY24 EPS to arrive at TP of Rs. 982 (earlier: Rs. 1007). HCLT is currently trading at 19x/16x on FY23/24E EPS of INR 49.8/57.7 respectively with Revenue/EPS CAGR of 9.3%/7.6% over FY22-24E. Maintain 'HOLD'.

- **Sequential services (IT+ERD) revenue growth led by select few verticals:** IT services growth was led by Technology services (10.9% QoQ CC), TMT (4.3% QoQ CC) and Life Sciences & Healthcare (2.7% QoQ CC). Whereas other verticals - BFSI (0.8% QoQ CC) and Public Services (-0.2% QoQ CC) were flattish, Manufacturing declined 0.5% QoQ CC and Retail & CPG declined 1.4% QoQ CC. Growth was healthy in US (2.8% QoQ CC) and soft in Europe (1.6% QoQ CC).
- **Margins for FY23 likely to be below the guided range:** EBIT margin came at 17%, -100bps QoQ (PLe: 17.1%, Cons: 17.6%) led by 180bps QoQ decline in IT Services and 40bps QoQ drop in ERD segment. Margin was partially offset by increase of 340bps QoQ in Product business. Margin walk – 1) 100bps impact from higher outsourcing costs, 2) 150bps impact from retention and employee addition costs, 3) 35 bps from travel and visa costs partially offset by exchange gains of 40bps and weak seasonality was offset by operating efficiency.
- **Other concall takeaways:** 1) Management retained revenue guidance of 12-14% YoY CC due to healthy new deal TCV (\$2 bn, 23.4% YoY, -9% QoQ), close to record high pipeline and near term strength in demand, 2) Fresher addition target of 30K for FY23 intact, added ~6K freshers in Q1 and targets to add ~10K in Q2, 3) Attrition inched up to 23.8% (190bps QoQ) and is expected to taper off from Q3, 4) DSO increased to 65 days (vs 61 in Q1) led by delay in payments by certain clients, which are expected to be recovered in Q2, 5) Declared dividend of Rs. 10/share.

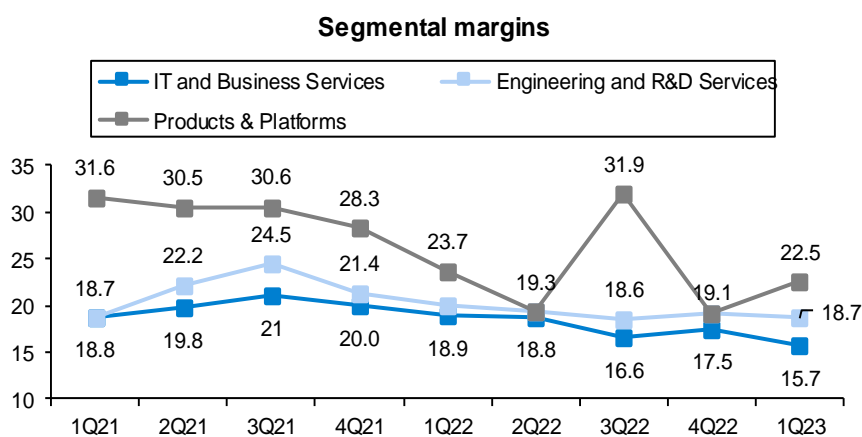
Exhibit 1: Q1FY23: Quick view on results

(Rs m)	1Q23	4Q22	QoQ gr.	1Q22	YoY gr.	PL(e)	Var VS PL(e)
Sales (\$ m)	3,025	2,993	1.1%	2,720	11.2%	3,024	0.0%
Sales	2,34,640	2,25,970	3.8%	2,00,680	16.9%	2,33,744	0.4%
EBIT Margin	49,750	50,530	-1.5%	49,080	1.4%	50,489	-1.5%
EBIT Margin	21.2%	22.4%	-116 bps	24.5%	-325 bps	22%	-40 bps
EBIT Margin	39,920	40,690	-1.9%	39,310	1.6%	39,970	-0.1%
EBIT Margin	17.0%	18.0%	-99 bps	19.6%	-258 bps	17.1%	-9 bps
Adjusted PAT	32,830	35,940	-8.7%	32,150	2.1%	32,373	1.4%
EPS	12.1	13.3	-8.6%	11.8	2.3%	11.94	1.5%

Source: Company, PL

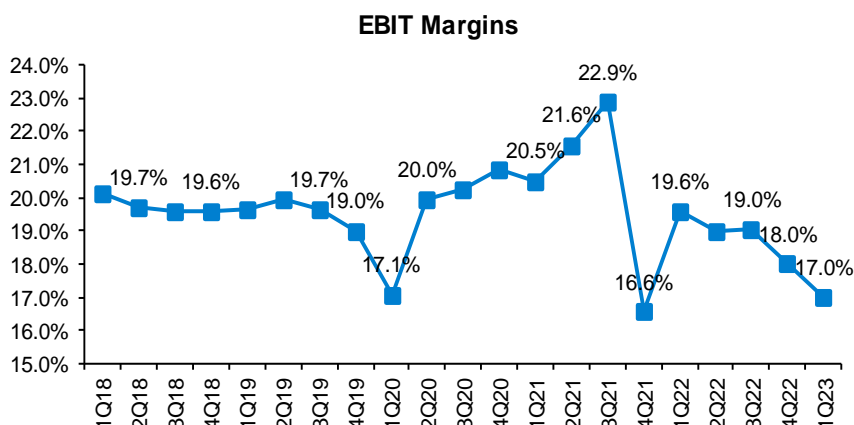
Exhibit 2: Soft QoQ growth since past two quarters


Source: Company, PL

Exhibit 3: Sharp decline in IT services margins


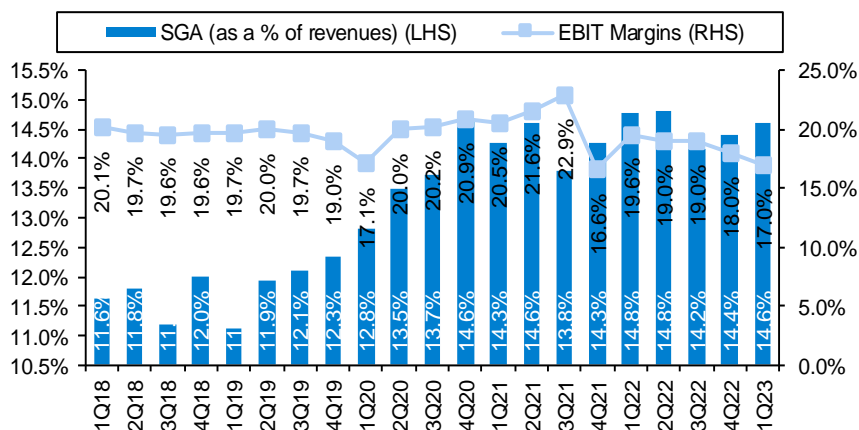
Source: Company, PL

Exhibit 4: Declining margin profile



Source: Company, PL

Exhibit 5: SGA expenses increased by 20bps QoQ

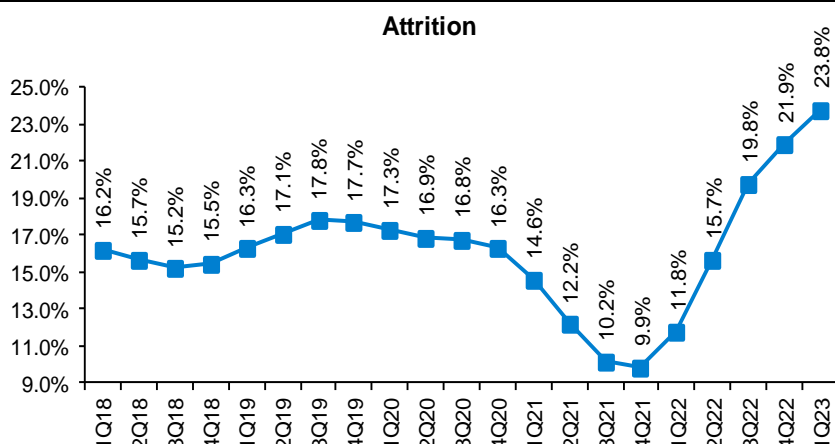


Source: Company, PL

Exhibit 6: Change in Estimates

Particulars	FY23E	FY24E
Revenue (US\$ m)		
New	12,616	13,720
Old	12,638	13,826
Change (%)	-0.2%	-0.8%
USD Revenue growth (%)	9.9%	8.8%
EBIT Margins (%)		
- New	17.5%	18.0%
- Old	18.0%	18.5%
Change (%)	-57 bps	-49 bps
EPS (Rs)		
- New	49.8	57.7
- Old	52.5	59.3
Change (%)	-5.1%	-2.6%

Source: Company, PL

Exhibit 7: Attrition rises sharply


Source: Company, PL

Exhibit 8: Geography-wise revenues

(US\$ m)	1Q23	4Q22	QoQ gr.	1Q22	YoY gr.
US	1,942.0	1,888.6	2.8%	1,707.7	13.7%
Europe	840.9	859.0	-2.1%	784.5	7.2%
Asia Pacific	242.0	266.4	-9.2%	227.4	6.4%
% Total					
US	64.2%	63.1%	110 bps	62.8%	141 bps
Europe	27.8%	28.7%	-90 bps	28.8%	-105 bps
Asia Pacific	8.0%	8.9%	-90 bps	8.4%	-36 bps

Source: Company, PL

Exhibit 9: Services Revenue growth led by Technology and Communication verticals and by US market

	Growth in CC		Contribution to revenues
	QoQ	YoY	
Total revenues	1.1	13.3	
Geographical split of revenues			
US	2.8	17.5	64.2
Europe	1.6	22.5	27.8
ROW	1.1	18.2	8.0
Vertical split of revenues			
Financial services	0.8	16.4	21.1
Manufacturing (new classification)	(0.5)	19.1	18.3
Telecom, media, publishing, entertainment	2.7	15.7	9.2
Retail & CPG	(0.2)	15.2	9.4
Public Services	(1.4)	5.8	10.2
Life sciences	4.3	29.2	16.4
Technology & Services	10.9	34.2	15.4
Service line split of revenues			
IT and Business Services	2.0	18.1	72.8
Engineering and R&D Services	3.7	23.0	16.6
Products & Platforms	5.1	(6.5)	10.6

Source: Company, PL

Exhibit 10: Client Metrics

Particulars	1Q23	4Q22	QoQ gr.	1Q22	YoY gr.
US\$100m	17	16	1	15	2
US\$50m	42	43	-1	35	7
US\$20m	127	118	9	96	31
US\$10m	218	208	10	178	40
US\$5m	353	349	4	318	35
US\$1m	880	882	-2	809	71
(US\$ m)					
Top 5 Clients	338.8	347.2	-2.4%	368.8	-8.1%
Top 6-10 Clients	248.0	245.4	1.1%	200.3	23.9%
Top 10 Clients	586.8	592.6	-1.0%	569.1	3.1%
Top 10-20 Clients	287.4	278.3	3.2%	267.9	7.3%
Top 20 Clients	874.2	871.0	0.4%	837.0	4.4%
Non-Top 20 Clients	2,150.7	2,122.0	1.4%	1,882.6	14.2%
% of Total Revenue					
Top 5 Clients	11.2%	11.6%	-40 bps	13.6%	-236 bps
Top 10 Clients	19.4%	19.8%	-40 bps	20.9%	-153 bps
Top 20 Clients	28.9%	29.1%	-20 bps	30.8%	-188 bps

Source: Company, PL

Financials

Income Statement (Rs m)

Y/e Mar	FY21	FY22	FY23E	FY24E
Net Revenues	7,53,790	8,56,510	9,76,038	10,70,173
YoY gr. (%)	6.6	13.6	14.0	9.6
Employee Cost	4,53,200	5,31,750	6,23,883	6,82,178
Gross Profit	3,00,590	3,24,760	3,52,155	3,87,995
Margin (%)	39.9	37.9	36.1	36.3
SG&A Expenses	-	-	-	-
Other Expenses	-	-	-	-
EBITDA	1,93,280	2,00,410	2,10,182	2,38,170
YoY gr. (%)	15.8	3.7	4.9	13.3
Margin (%)	25.6	23.4	21.5	22.3
Depreciation and Amortization	39,850	38,740	39,726	45,425
EBIT	1,53,430	1,61,670	1,70,457	1,92,745
Margin (%)	20.4	18.9	17.5	18.0
Net Interest	-	-	-	-
Other Income	6,570	8,560	6,920	6,100
Profit Before Tax	1,60,000	1,70,230	1,77,377	1,98,845
Margin (%)	21.2	19.9	18.2	18.6
Total Tax	35,100	34,580	42,534	42,526
Effective tax rate (%)	21.9	20.3	24.0	21.4
Profit after tax	1,24,900	1,35,650	1,34,843	1,56,319
Minority interest	570	490	(20)	-
Share Profit from Associate	-	-	-	-
Adjusted PAT	1,24,330	1,35,160	1,34,863	1,56,319
YoY gr. (%)	12.4	8.7	(0.2)	15.9
Margin (%)	16.5	15.8	13.8	14.6
Extra Ord. Income / (Exp)	-	-	-	-
Reported PAT	1,24,330	1,35,160	1,34,863	1,56,319
YoY gr. (%)	12.4	8.7	(0.2)	15.9
Margin (%)	16.5	15.8	13.8	14.6
Other Comprehensive Income	-	-	-	-
Total Comprehensive Income	1,24,330	1,35,160	1,34,863	1,56,319
Equity Shares O/s (m)	2,714	2,712	2,707	2,707
EPS (Rs)	45.8	49.8	49.8	57.7

Source: Company Data, PL Research

Balance Sheet Abstract (Rs m)

Y/e Mar	FY21	FY22	FY23E	FY24E
Non-Current Assets				
Gross Block	3,77,870	3,52,060	3,85,359	3,95,818
Tangibles	86,370	80,460	1,08,449	1,18,908
Intangibles	2,91,500	2,71,600	2,76,910	2,76,910
Acc: Dep / Amortization	-	-	-	-
Tangibles	-	-	-	-
Intangibles	-	-	-	-
Net fixed assets	3,77,870	3,52,060	3,85,359	3,95,818
Tangibles	86,370	80,460	1,08,449	1,18,908
Intangibles	2,91,500	2,71,600	2,76,910	2,76,910
Capital Work In Progress	-	-	-	-
Goodwill	-	-	-	-
Non-Current Investments	890	90	1,150	1,150
Net Deferred tax assets	-	-	-	-
Other Non-Current Assets	67,750	57,770	78,330	78,330
Current Assets				
Investments	-	-	-	-
Inventories	-	-	-	-
Trade receivables	1,75,250	2,06,710	2,35,319	2,58,014
Cash & Bank Balance	2,04,900	1,88,750	1,92,357	2,99,789
Other Current Assets	50,370	84,950	60,514	66,351
Total Assets	8,77,030	8,90,330	9,53,029	10,99,452
Equity				
Equity Share Capital	1,341	1,341	1,341	1,341
Other Equity	6,13,720	6,17,800	6,78,239	8,02,070
Total Networth	6,15,060	6,19,140	6,79,579	8,03,410
Non-Current Liabilities				
Long Term borrowings	39,070	39,230	39,230	39,230
Provisions	-	-	-	-
Other non current liabilities	49,500	43,290	39,042	42,807
Current Liabilities				
ST Debt / Current of LT Debt	-	-	-	-
Trade payables	1,67,550	1,87,750	1,95,208	2,14,035
Other current liabilities	-	-	-	-
Total Equity & Liabilities	8,77,030	8,90,330	9,53,029	10,99,452

Source: Company Data, PL Research

Cash Flow (Rs m)

Y/e Mar	FY21	FY22	FY23E	FY24E
PBT	1,60,000	1,70,230	1,77,377	1,98,845
Add. Depreciation	39,850	38,740	39,726	45,425
Add. Interest	-	-	-	-
Less Financial Other Income	6,570	8,560	6,920	6,100
Add. Other	-	-	-	-
Op. profit before WC changes	1,99,850	2,08,970	2,17,102	2,44,270
Net Changes-WC	(14,410)	(42,070)	(21,524)	(5,940)
Direct tax	(35,100)	(34,580)	(42,534)	(42,526)
Net cash from Op. activities	1,50,340	1,32,320	1,53,045	1,95,805
Capital expenditures	(61,070)	(12,930)	(73,024)	(55,885)
Interest / Dividend Income	-	-	-	-
Others	(120)	800	(1,060)	-
Net Cash from Invt. activities	(61,190)	(12,130)	(74,084)	(55,885)
Issue of share cap. / premium	-	-	-	-
Debt changes	(11,850)	160	-	-
Dividend paid	(83,608)	(1,19,286)	(54,147)	(32,488)
Interest paid	-	-	-	-
Others	57,478	(17,214)	(21,207)	-
Net cash from Fin. activities	(37,980)	(1,36,340)	(75,353)	(32,488)
Net change in cash	51,170	(16,150)	3,607	1,07,432
Free Cash Flow	89,270	1,19,390	80,020	1,39,920

Source: Company Data, PL Research

Key Financial Metrics

Y/e Mar	FY21	FY22	FY23E	FY24E
Per Share(Rs)				
EPS	45.8	49.8	49.8	57.7
CEPS	60.5	64.1	64.5	74.5
BVPS	226.7	228.3	251.0	296.8
FCF	32.9	44.0	29.6	51.7
DPS	26.0	44.0	20.0	12.0
Return Ratio(%)				
RoCE	25.1	24.6	24.8	24.7
ROIC	40.8	35.7	33.5	32.6
RoE	22.0	21.9	20.8	21.1
Balance Sheet				
Net Debt : Equity (x)	(0.3)	(0.2)	(0.2)	(0.3)
Debtor (Days)	85	88	88	88
Valuation(x)				
PER	20.3	18.6	18.6	16.1
P/B	4.1	4.1	3.7	3.1
P/CEPS	15.3	14.5	14.4	12.5
EV/EBITDA	12.2	11.8	11.2	9.5
EV/Sales	3.1	2.8	2.4	2.1
Dividend Yield (%)	2.8	4.7	2.2	1.3

Source: Company Data, PL Research

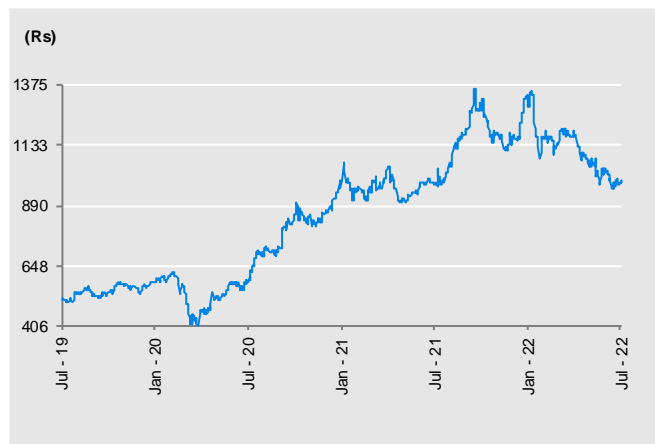
Quarterly Financials (Rs m)

Y/e Mar	Q2FY22	Q3FY22	Q4FY22	Q1FY23
Net Revenue	2,06,550	2,23,310	2,25,970	2,34,640
YoY gr. (%)	11.1	15.7	15.0	13.6
Raw Material Expenses	1,27,580	1,39,280	1,42,920	1,50,660
Gross Profit	78,970	84,030	83,050	83,980
Margin (%)	38.2	37.6	36.8	35.8
EBITDA	48,380	52,420	50,530	49,750
YoY gr. (%)	(2.3)	(3.7)	15.7	2.8
Margin (%)	23.4	23.5	22.4	21.2
Depreciation / Depletion	9,220	9,910	9,840	9,830
EBIT	39,160	42,510	40,690	39,920
Margin (%)	19.0	19.0	18.0	17.0
Net Interest	-	-	-	-
Other Income	2,070	2,030	2,520	3,450
Profit before Tax	41,230	44,540	43,210	43,370
Margin (%)	20.0	19.9	19.1	18.5
Total Tax	8,460	9,970	7,210	10,560
Effective tax rate (%)	20.5	22.4	16.7	24.3
Profit after Tax	32,770	34,570	36,000	32,810
Minority interest	130	140	60	(20)
Share Profit from Associates	-	-	-	-
Adjusted PAT	32,640	34,430	35,940	32,830
YoY gr. (%)	3.9	(13.5)	50.6	0.6
Margin (%)	15.8	15.4	15.9	14.0
Extra Ord. Income / (Exp)	-	-	-	-
Reported PAT	32,640	34,430	35,940	32,830
YoY gr. (%)	3.9	(13.5)	50.6	0.6
Margin (%)	15.8	15.4	15.9	14.0
Other Comprehensive Income	-	-	-	-
Total Comprehensive Income	32,640	34,430	35,940	32,830
Avg. Shares O/s (m)	2,714	2,713	2,709	2,709
EPS (Rs)	12.0	12.7	13.3	12.1

Source: Company Data, PL Research

Price Chart

Recommendation History



No.	Date	Rating	TP (Rs.)	Share Price (Rs.)
1	04-Jul-22	Hold	1,007	975
2	22-Apr-22	Accumulate	1,169	1,099
3	05-Apr-22	BUY	1,295	1,187
4	16-Jan-22	BUY	1,398	1,337
5	04-Jan-22	BUY	1,400	1,326
6	21-Dec-21	BUY	1,402	1,160
7	16-Oct-21	BUY	1,386	1,251
8	05-Oct-21	BUY	1,429	1,279
9	06-Aug-21	BUY	1,239	1,050
10	20-Jul-21	BUY	1,094	1,000

Analyst Coverage Universe

Sr. No.	Company Name	Rating	TP (Rs)	Share Price (Rs)
1	Affle (India)	BUY	1,342	1,009
2	Coforge	BUY	4,095	3,488
3	Cyient	Accumulate	798	761
4	HCL Technologies	Hold	1,007	975
5	Infosys	Accumulate	1,646	1,479
6	L&T Technology Services	Accumulate	3,247	2,986
7	Larsen & Toubro Infotech	Accumulate	4,184	4,001
8	Mindtree	Accumulate	3,121	2,891
9	Mphasis	Hold	2,421	2,241
10	Persistent Systems	Hold	3,490	3,329
11	Redington (India)	BUY	162	127
12	Sonata Software	Accumulate	694	655
13	Tata Consultancy Services	Accumulate	3,607	3,265
14	TeamLease Services	Accumulate	3,642	3,300
15	Tech Mahindra	Hold	1,065	1,011
16	Wipro	Hold	439	422
17	Zensar Technologies	Hold	279	270

PL's Recommendation Nomenclature (Absolute Performance)

Buy	: > 15%
Accumulate	: 5% to 15%
Hold	: +5% to -5%
Reduce	: -5% to -15%
Sell	: < -15%
Not Rated (NR)	: No specific call on the stock
Under Review (UR)	: Rating likely to change shortly

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