

27 April 2024

India | Equity Research | Q4FY24 results review

HCL Technologies

Technology

Exactly in-line Q4; weaker-than-estimated FY25 guidance

HCLT reported revenue growth and EBIT margin in line with our estimates. IT and business services grew 4% QoQ CC and Engineering R&D was down 1.6%. Software business was down 18.5% QoQ CC on seasonal weakness. Geography-wise growth was led by North America, at 4.2%. TCV was robust at USD 2.29bn, with 13 out of 21 large deal wins originating from services. However, FY25 growth guidance of 3–5% was lower than our/ Street's estimate of 4–7%. This guidance includes a soft Q1FY25 impacted by offshore transition in large contact and a soft Q2FY25 impacted by State Street JV divestiture. This implies a weak CQGR of -0.2% to +0.6% QoQ through FY25. Factoring this in, we reduce FY25E/26E EPS by 3–7%. We value HCLT on an SoTP-basis – Services (IT and ER&D) at 20x and Products at 16x on FY26E EPS to arrive at a TP of INR 1,330. Retain **REDUCE** on soft H1FY25 and unexciting EBIT margin guidance of 18–19%.

In-line growth and margin; weak seasonality impacts margin

HCLT reported 0.3% QoQ CC revenue growth, in line with our/Street's estimates. Growth was led by services business, up 3% QoQ, while the product and platform business reported 18.5% QoQ decline on weak seasonality. EBIT margin, at 17.6%, declined 220bps, was precisely in-line with our estimate, but overshot Street's estimate of a 140bps decline. Services business margin at 17.1% declined 70bps QoQ. Growth was led by cloud transformation and cybersecurity. Focus is on subscription and supporting revenues. Americas grew 4.2% QoQ, followed by Europe growing 2.3% while RoW declined 5.9% in CC. BFSI led growth with 3% growth amid macro uncertainty, along with manufacturing that was up 5%. TMT was up 22% QoQ as the Verizon deal's revenues came through.

Guidance implies weak CQGR; weak start to FY25

FY25 is expected to be the year of consolidation in terms of both demand and supply, with more investments in AI driving productivity gains. HCLT guided for 3% to 5% YoY cc revenue growth for FY25, tad lower than Street/our expectations of ~4–7% and guidance of 3–5% CC for the services business. This implies a weak CQGR of -0.2% to 0.6% through FY25. HCLT announced a very weak Q1FY25 of -2% QoQ CC growth. Guidance includes impact from State Street divestment. FY25E EBIT margin guidance range is 18–19%. Revenue contribution from ASAP and State Street divestment are offsetting factors in HCLT's FY25 revenue guidance.

Financial Summary

Y/E March (INR mn)	FY23A	FY24A	FY25E	FY26E
Net Revenue	10,14,560	10,99,130	11,54,681	12,57,394
EBITDA	2,26,290	2,45,710	2,53,457	2,88,107
EBITDA %	22.3	22.4	22.0	22.9
Net Profit	1,48,460	1,59,590	1,61,955	1,85,457
EPS (Rs)	54.8	58.9	59.8	68.5
EPS % Chg YoY	10.0	7.4	1.5	14.5
P/E (x)	26.9	25.0	24.6	21.5
EV/EBITDA (x)	17.2	15.7	14.5	12.7
RoCE (%)	20.8	21.9	21.4	23.6
RoE (%)	23.3	23.9	23.3	25.6

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Market Data

Market Cap (INR)	4,000bn
Market Cap (USD)	48,008mn
Bloomberg Code	HCLT IN
Reuters Code	HCLT.BO
52-week Range (INR)	1,697 /1,048
Free Float (%)	39.0
ADTV-3M (mn) (USD)	57.0

Price Performance (%)	3m	6m	12m
Absolute	(4.9)	19.7	38.3
Relative to Sensex	(9.2)	2.9	16.0

Earnings Revisions (%)	FY25E	FY26E
USD Revenue	(3.8)	(4.8)
EBIT	(6.2)	(1.8)
EPS	(7.5)	(3.3)

Previous Reports

14-01-2024: [Q3FY24 results review](#)

13-10-2023: [Q2FY24 results review](#)

Deal pipeline healthy, though discretionary demand still soft

HCLT reported large deal bookings of USD 2.29bn (up 18% QoQ). The company only calls out net new deal wins. Deal bookings were strong. It won 13 large deals in services and 8 in products business. This includes manufacturing deal from Europe and US, HLS deal from Japan, and a product deal in marketing from US. HCLT has also bagged a Unica platform deal from SBI.

Discretionary spends are still under pressure. Demand is driven by cost optimisation; in transformation, it is led by cloud engineering (finops), ERP modernisation, data modernisation, cybersecurity, and advanced analytics. ER&D business is also growing well. Deal pipeline is healthy and management expects to deliver healthy bookings in FY25.

Margins precisely in-line with our estimates; impacted by weak products and platforms seasonality

EBIT margin came in at 17.6% (-210 bps QoQ) led by ~156bps QoQ headwinds due to seasonal weakness in the products business (segmental margin came down from 32.9% in Q3FY24 to 21.2% in Q4). The company retained its EBIT margin guidance of 18–19% for FY25; however, aspirational margin range is still 19–20%. There will be some impact on margin in Q3FY25 from Verizon deal.

LTM attrition declined by 40bps QoQ to 12.4%. HCLT has considerably improved in managing attrition, which is at just 12.8% versus normalised pre-covid level attrition of ~15–16%. Employee headcount increased 0.7% YoY with net addition of ~2.7k employees.

Gen AI

HCLT is working on several Gen AI POCs and deals, but the size of the deals remains sub- USD 10mn. A few notable Gen AI projects the company is working on are: 1) Product validation and sustenance with Gen AI. 2) A US-based telco selecting for automating data pipeline for sales and marketing team. AI deals are coming at the cost of rest of IT services deals. Gen AI has maximum scope in efficiency in software development; hence, is helping HCLT gain market share.

Other highlights

- Services business growth was supported by Telecommunications, Media, Publishing & Entertainment (up 21.6% QoQ) vertical on the back of the Verizon deal.
- FY24 revenue grew 5.4% YoY USD. EBIT margin 18.2% was down 70bps YoY, lying within the guided range of 18-19% for FY24. Digital now constitutes 37.3% of revenue in FY24. Annual bookings stood at USD9.75bn with 73 large deals.
- Employee stats are partially different from industry trend of headcount reduction with net addition of 2,725 people QoQ.
- FCFF was up 27.7% YoY. Services grew 5.5% YoY in CC and software was up. The company is integrating ER&D business with IT services.
- OCF/Ni stood at 143%.
- 3096 freshers were added QoQ.
- DSO was down 6 days from 67 in Dec to 61 in Q4.
- INR18/sh worth of dividend was announced in Q4FY24.

Key management changes

Kalyan Kumar: From Chief Product Officer of Software Business to Chief Technology Officer. Vijay Guntur: President of ER&D to Chief of Technology. Harish Sriram Hariharan: From leading asset-heavy industries with engineering services to leading engineering services business and delivery.

Upside Risks: 1) Faster-than-expected recovery in discretionary spends; 2) strong growth in high margin products business leading to improvement in margins; and 3) market share gains in vendor consolidation deals.

Exhibit 1: Q4FY24 actuals vs estimates

(INR bn)	Q4FY24	Q3FY24	QoQ	Q4FY23	YoY	Q4FY24E I-Sec	vs. our estimates	Cons	vs. Cons
CC growth	0.3%	6.0%		-1.2%		5.0%	-473 bps	4.8%	-450 bps
Sales (USD m)	3,430	3,415	0.4%	3,235	6.0%	3,370	1.8%	3,372	1.7%
USD/INR	83.3	83.3	0.0%	82.2	1.3%	83.3		83.3	
Sales (INR bn)	285	284	0.2%	266	7.1%	281	1.5%	281	1.5%
EBIT	50	56	-10.5%	48	3.9%	54	-6.5%	52.5	-4.3%
EBIT Margin	17.6%	19.7%	-211 bps	18.2%	-55 bps	19.1%	-152 bps	18.7%	-107 bps
Reported PAT	40	44	-8.0%	40	0.5%	42	-5.6%	41.2	-2.9%
EPS	14.7	16.0	-8.0%	14.7	0.3%	15.6	-5.6%	15.2	-3.0%

Source: I-Sec research, Company data

Exhibit 2: HCLT – change in estimates

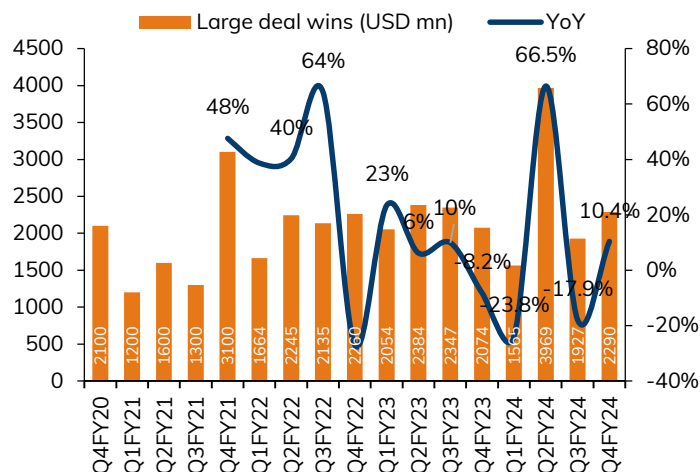
	New		Old		New vs Old	
	FY25E	FY26E	FY25E	FY26E	FY25E	FY26E
Revenues (USD mn)	13,829	14,969	14,380	15,717	-3.8%	-4.8%
Revenue growth YoY CC	4.2%	8.2%	9.2%	9.3%	-500bps	-110bps
Revenue growth YoY USD	4.2%	8.2%	8.9%	9.3%	-470bps	-110bps
USD/INR	83.5	84.0	83.5	84.0	0.0%	0.0%
INR bn						
Revenues	1,155	1,257	1,201	1,320	(3.8)	(4.8)
EBIT	208	238	221	243	(6.2)	(1.8)
EBIT margin	18.0%	18.9%	18.4%	18.4%	-50bps	60bps
EPS (INR/share)	59.7	68.3	64.5	70.7	-7.5%	-3.3%

Source: Company data, I-Sec research

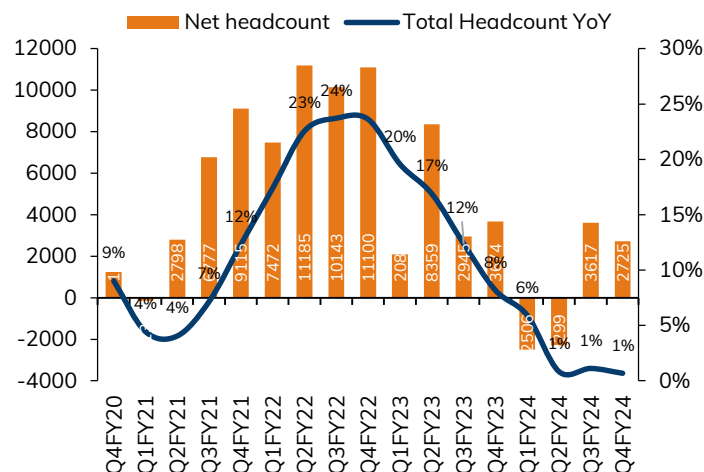
Exhibit 3: Incremental revenue as proportion of large deal TCV has come off in FY24, likely due to leakage in existing book of business and increase in average deal size of TCV

HCLT (USD bn)	FY21	FY22	FY23	FY24	FY25E
Net new large deal TCV	7.2	8.3	8.9	9.8	
Revenue	10.2	11.5	12.6	13.3	13.8
Incremental revenue	0.24	1.31	1.10	0.68	0.56
Incremental revenues as % of previous FY new large deal TCV		18%	13%	8%	6%

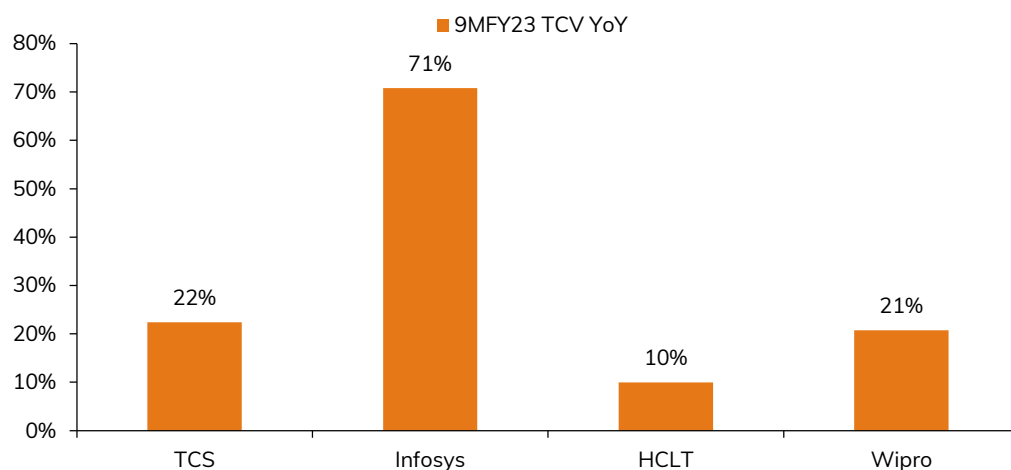
Source: I-Sec research, Company data

Exhibit 4: Large deal TCV is up 10.4% YoY

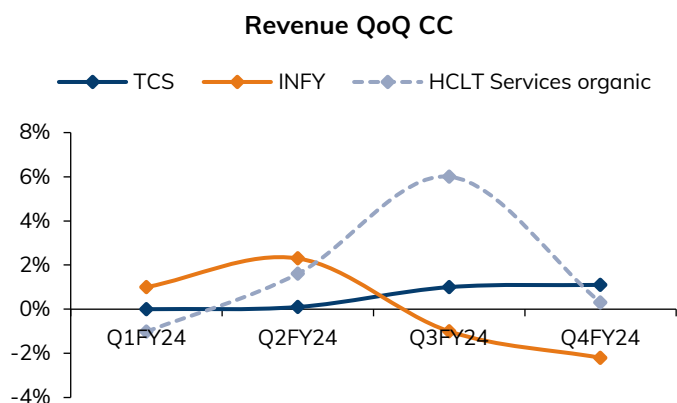
Source: I-Sec research, Company data

Exhibit 5: Headcount is up 1% YoY

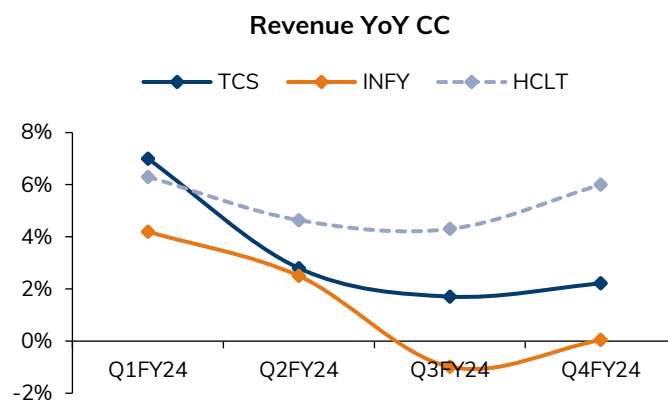
Source: I-Sec research, Company data

Exhibit 6: HCLT 9MFY23 TCV growth lower than tier-1 peers

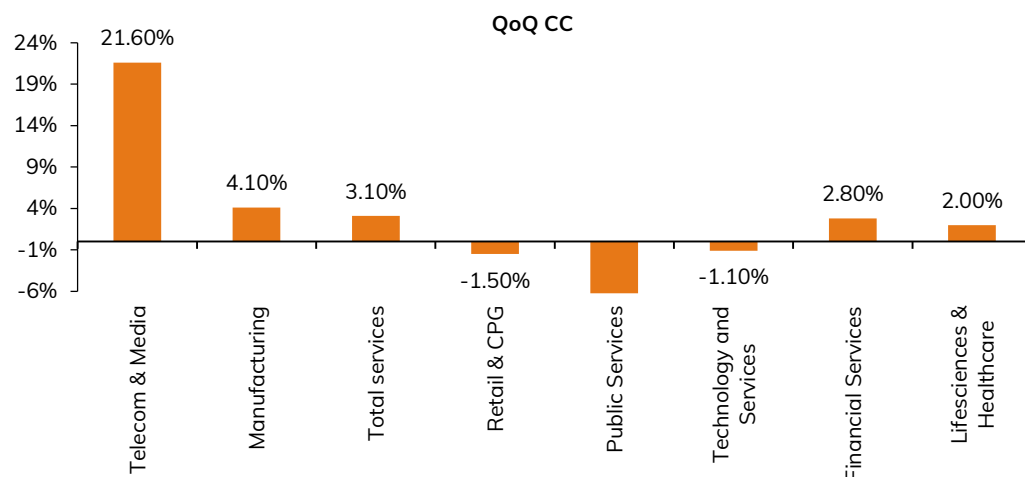
Source: I-Sec research, Company data, Note: TCS and Wipro report total order bookings, Infosys reports large deal bookings (>USD 50 mn deals) and HCLT reports net new large deal bookings

Exhibit 7: HCLT QoQ growth impacted by weak seasonality

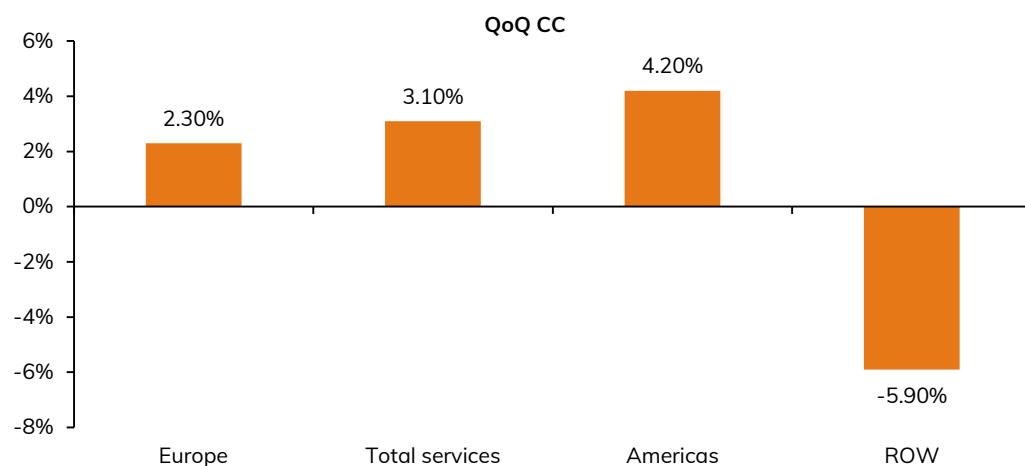
Source: I-Sec research, Company data

Exhibit 8: HCLT YoY growth lies ahead of peers

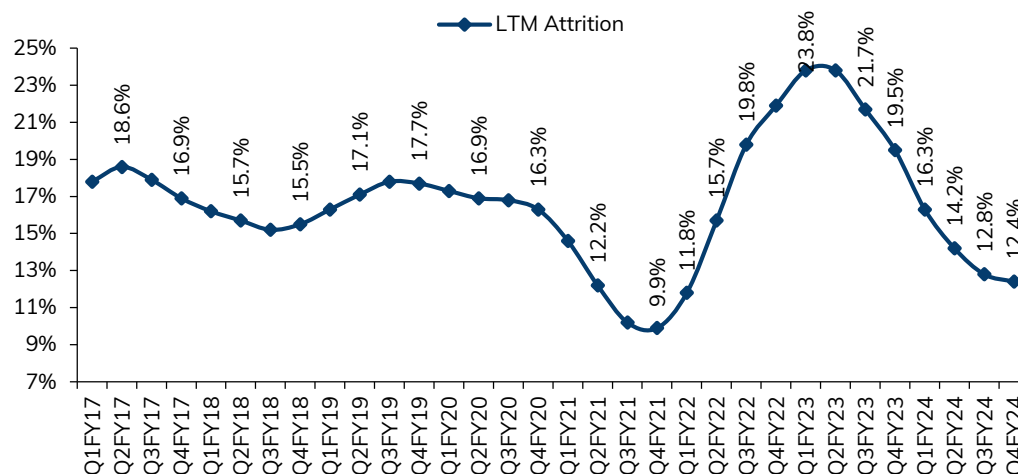
Source: I-Sec research, Company data

Exhibit 9: Sequential growth led by Telecom (catalysed by Verizon deal) and Manufacturing


Source: I-Sec research, Company data

Exhibit 10: Healthy sequential growth in America (led by Verizon deal) and Europe


Source: I-Sec research, Company data

Exhibit 11: Attrition at ~12.4%, well below normalised pre-covid levels of ~15-16%


Source: I-Sec research, Company data

Exhibit 12: Revenue growth across service lines

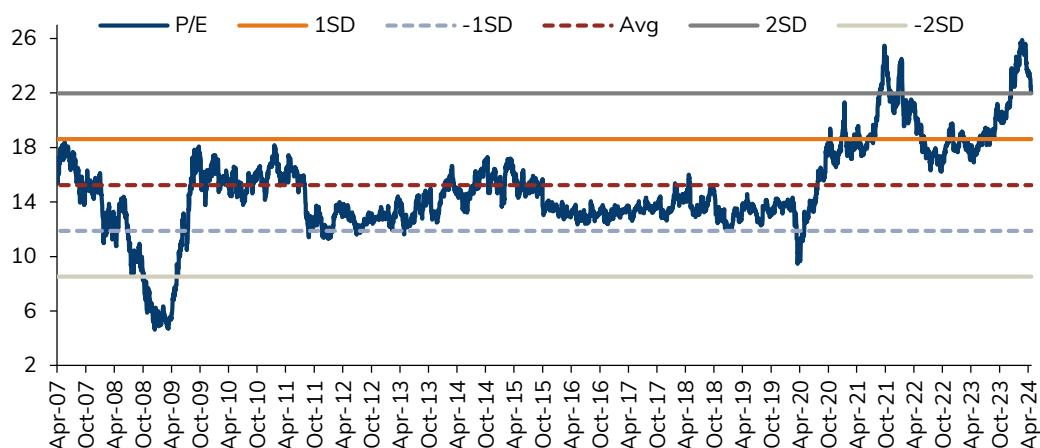
Revenue YoY CC	FY20	FY21	FY22	FY23	FY24	FY25E	FY26E
IT Services	12.70%	-0.60%	14.50%	15.60%	6.20%	4.26%	8.13%
ER&D	12.80%	-4.90%	16.80%	16.80%	1.60%	4.59%	9.29%
Products	60.50%	20.50%	-1.30%	1.80%	2.14%	3.21%	5.18%
Overall Revenue	16.7%	1.1%	12.7%	13.7%	5.0%	4.2%	8.2%

Source: I-Sec research, Company data

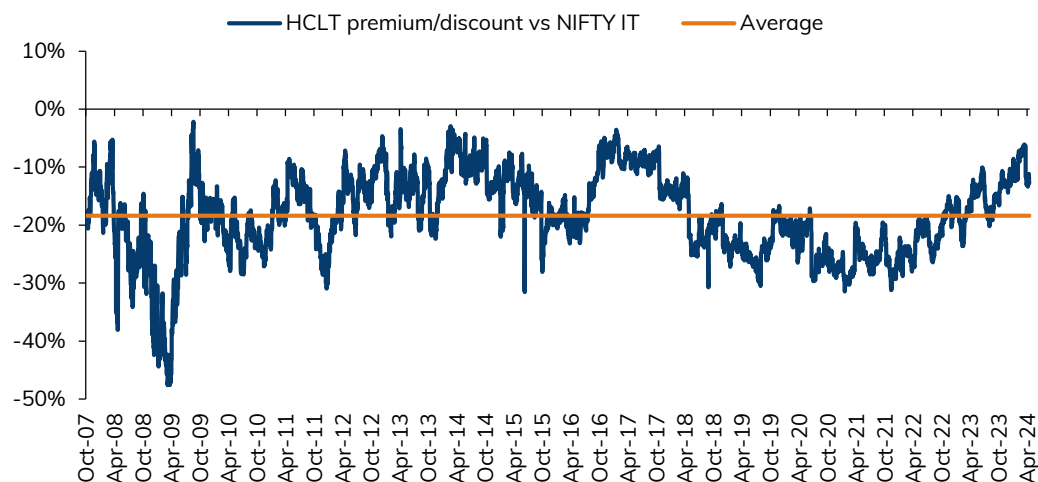
Exhibit 13: RoIC is steadily improving

LTM ROIC	Q4FY22	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24	Q3FY24	Q4FY24
HCLT Services	37.5%	36.4%	36.2%	37.4%	37.3%	38.0%	39.4%	40.1%	41.6%
HCL Software	14.2%	14.1%	14.3%	14.3%	15.5%	15.9%	16.2%	16.6%	16.5%
Consol HCLT	28.9%	28.5%	28.7%	29.8%	30.4%	31.1%	32.2%	32.8%	33.8%

Source: I-Sec research, Company data

Exhibit 14: HCLT trading at 22x (two-year forward P/E), in-line with its avg. +2SD of 22x

Source:

Exhibit 15: HCLT trading at ~13% discount to NIFTY IT vs. average discount of 18%

Source: I-Sec research, Company data

Exhibit 16: Valuation methodology**HCLT valuation: SoTP****Services Business**

FY26 EPS (INR)	58
Target multiple (x)	20

Products Business

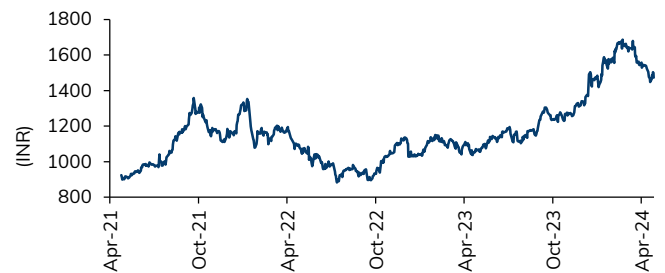
FY26 EPS (INR)	10
Target multiple (x)	16
Target Price (INR)	1,330

Source: I-Sec research, Company data

Exhibit 17: Shareholding pattern

%	Sep'23	Dec'23	Mar'24
Promoters	60.8	60.8	60.8
Institutional investors	34.3	34.6	34.6
MFs and other	8.3	8.3	8.0
Banks/ FIs	0.8	0.0	0.0
Insurance Cos.	6.4	6.0	6.0
FII	18.8	20.3	20.6
Others	4.9	4.6	4.6

Source: Bloomberg

Exhibit 18: Price chart

Source: Bloomberg

Financial Summary

Exhibit 19: Profit & Loss

(INR mn, year ending March)

	FY23A	FY24A	FY25E	FY26E
Net Sales (US\$ mn)	12,586	13,270	13,829	14,969
Net Sales (INR mn)	10,14,560	10,99,130	11,54,681	12,57,394
Operating Expense	7,88,270	8,53,420	9,01,224	9,69,287
EBITDA	2,26,290	2,45,710	2,53,457	2,88,107
EBITDA Margin (%)	22.3	22.4	22.0	22.9
Depreciation & Amortization	41,440	41,730	45,777	49,876
EBIT	1,84,850	2,03,980	2,07,681	2,38,231
Interest expenditure	3,530	1,470	900	889
Other Non-operating Income	13,560	9,650	12,077	13,277
Recurring PBT	1,94,880	2,12,160	2,18,858	2,50,618
Profit / (Loss) from Associates	-	-	-	-
Less: Taxes	46,420	52,570	56,903	65,161
PAT	1,48,460	1,59,590	1,61,955	1,85,457
Less: Minority Interest	20	-	(40)	(40)
Net Income (Reported)	1,48,460	1,59,590	1,61,955	1,85,457
Extraordinaries (Net)	-	-	-	-
Recurring Net Income	1,48,480	1,59,590	1,61,915	1,85,417

Source Company data, I-Sec research

Exhibit 20: Balance sheet

(INR mn, year ending March)

	FY23A	FY24A	FY25E	FY26E
Total Current Assets	4,81,920	5,22,880	5,71,406	6,21,118
of which cash & cash eqv.	90,650	94,560	2,68,353	2,85,220
Total Current Liabilities & Provisions	1,93,200	2,27,260	2,34,300	2,59,694
Net Current Assets	2,88,720	2,95,620	3,37,106	3,61,425
Investments	58,730	79,830	79,830	79,830
Net Fixed Assets	54,110	49,670	53,670	57,670
ROU Assets	23,370	39,900	-	-
Capital Work-in-Progress	-	-	-	-
Goodwill	-	-	-	-
Other assets	34,350	22,560	22,560	22,560
Deferred Tax assets	12,520	10,310	-	-
Total Assets	7,40,910	7,70,510	7,65,786	7,94,105
Liabilities				
Borrowings	42,220	22,230	22,230	22,230
Deferred Tax Liability	1,610	7,710	-	-
provisions	13,150	16,120	-	-
other Liabilities	29,950	41,740	34,440	34,440
Minority Interest	(70)	80	-	-
Equity Share Capital	5,430	-	-	-
Reserves & Surplus*	-	-	-	-
Total Net Worth	6,54,050	6,82,630	7,09,116	7,37,435
Total Liabilities	7,40,910	7,70,510	7,65,786	7,94,105

Source Company data, I-Sec research

Exhibit 21: Quarterly trend

(INR mn, year ending March)

	Jun-23	Sep-23	Dec-23	Mar-24
Net Sales	2,62,960	2,66,720	2,84,460	2,84,990
% growth (YOY)	(1.2)	1.4	6.7	0.2
EBIT	44,600	49,340	56,150	50,240
Margin %	17.0	18.5	19.7	17.6
Other Income	2,360	1,940	2,590	2,510
Adjusted Net Profit	35,340	38,320	43,500	40,000

Source Company data, I-Sec research

Exhibit 22: Cashflow statement

(INR mn, year ending March)

	FY23A	FY24A	FY25E	FY26E
CFO before WC changes	2,27,200	2,42,040	2,53,417	2,88,067
CFO after WC changes	2,16,980	2,01,360	3,85,724	2,80,615
Capital Commitments	(23,670)	(57,330)	(9,877)	(53,876)
Free Cashflow	2,03,760	2,06,120	3,38,698	2,69,331
Other investing cashflow	(15,640)	18,900	21,488	12,387
Cashflow from Investing Activities	(39,310)	(38,430)	11,611	(41,489)
Issue of Share Capital	-	12,392	(80)	-
Interest Cost	(800)	-	-	-
Inc (Dec) in Borrowings	(18,480)	1,120	-	-
Cash flow from Financing Activities	(1,55,230)	(1,06,450)	(1,66,640)	(1,57,098)
Dividend paid	(1,29,950)	(1,40,822)	(1,35,430)	(1,57,098)
Others	(6,000)	20,860	(31,130)	-
Chg. in Cash & Bank balance	(14,450)	3,910	1,73,793	16,868
Closing cash & balance	90,650	94,560	2,68,353	2,85,220

Source Company data, I-Sec research

Exhibit 23: Key ratios

(Year ending March)

	FY23A	FY24A	FY25E	FY26E
Per Share Data (INR)				
Reported EPS	54.8	58.9	59.8	68.5
Diluted EPS	54.8	58.9	59.8	68.5
Cash EPS	70.2	74.3	76.7	86.9
Dividend per share (DPS)	48.0	52.0	50.0	58.0
Book Value per share (BV)	241.6	252.1	261.8	272.3
Dividend Payout (%)	87.5	88.2	83.6	84.7
Growth (%)				
Net Sales	18.5	8.3	5.1	8.9
EBITDA	10.2	8.6	3.2	13.7
EPS	10.0	7.4	1.5	14.5
Valuation Ratios (x)				
P/E	26.9	25.0	24.6	21.5
P/CEPS	21.0	19.8	19.2	17.0
P/BV	6.1	5.8	5.6	5.4
EV / EBITDA	17.2	15.7	14.5	12.7
P/S	3.9	3.6	3.5	3.2
Dividend Yield (%)	3.3	3.5	3.4	3.9
Operating Ratios				
EBITDA Margins (%)	22.3	22.4	22.0	22.9
EBIT Margins (%)	18.2	18.2	18.0	18.9
Effective Tax Rate (%)	23.8	24.8	26.0	26.0
Net Profit Margins (%)	14.6	14.5	14.0	14.7
Inventory Turnover Days	0.7	-	-	-
Fixed Asset Turnover (x)	18.2	21.2	22.3	22.6
Receivables Days	63.0	64.8	62.5	61.5
Payables Days	-	-	-	-
Working Capital Days	-	-	-	-
Net Debt / EBITDA (x)	(2.5)	(3.4)	(6.9)	(6.7)
Profitability Ratios				
RoCE (%)	20.8	21.9	21.4	23.6
RoIC (%)	27.0	29.3	38.9	43.4
RoNW (%)	23.3	23.9	23.3	25.6

Source Company data, I-Sec research

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