

July 13, 2022

RESULT REPORT Q1 FY23 | Sector: Information Technology

HCL Technologies Ltd

Weak operating margin but near to medium term outlook remains strong

Our view and valuation

Overall, the sequential revenue growth was inline with expectation; but the EBIT margin came much below estimates. The revenue growth is led by the Services segment (IT Services and ER&D), that continues to maintain growth momentum. The P&P Segment is expected to grow at mid single digit YoY. We expect revenue growth to be more predictable and robust going ahead as IT services contribution rises in revenue mix. Deal booking remains strong and that offers strong growth visibility for FY23. We expect it to maintain 18% + EBIT margin for FY23 led by improving employing pyramid, better utilization and positive operating leverage. Employee attrition should come in control over next few quarters. We expect revenue CAGR of 14.2% over FY22-24E, with average EBIT margin of 18.6%

Valuation remains attractive as it trades at PE of 14.7x on FY24E EPS. We maintain BUY Rating on the stock with revised target price of Rs 1,140/share at 18x on FY24E.

Result Highlights

- Reported revenue of Rs 234.6bn (up 3.8% QoQ in INR terms, up 1.1% QoQ in USD terms). The CC revenue growth for the quarter was 2.7%. In terms of segments, IT services grew 2.0% QoQ in cc terms, ER&D Services grew 3.7% QoQ in cc terms; while product and platform grew 5.1% QoQ in cc terms. Mode 2 segment continues to lead the growth momentum growing at 39.3% YoY in cc terms.
- Among verticals, the growth was led by Technology and Services (up 10.9% QoQ); Telecom, Media and Entertainment (up 4.3% QoQ)
- EBIT margin declined by 100 bps QoQ to 17% was due to productivity related commitments to clients, supply side constraints and Travel and Visa related costs.
- Reported strong deal win with TCv of new deal wins at \$2,054mn (up 23.4% YoY), with good mix of big and medium sized deals
- \$100mn clients increased by 3 YoY, \$50mn clients increased by 5 YoY
- Added 2089 employees during the quarter to reach 210,966 employees. LTM attrition increased by 190 bps QoQ to 23.8%.
- DSO increased by 4 days QoQ to 65 days.
- Net cash stands at \$1.7bn compared to \$2.4bn as of Q4FY22. Declared dividend of Rs 10/ share
- Maintained FY23E guidance with revenue growth for FY23 to be between 12-14% in cc terms; with EBIT Margin expected to be between 18-20%.

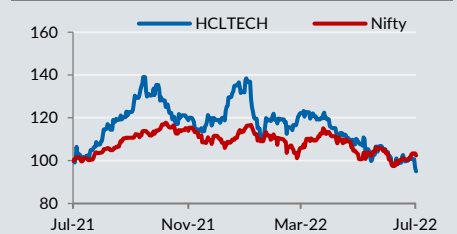
Rs mn	Actual	Estimate		% Variation	
		YES Sec	Consensus	YES Sec	Consensus
Sales	234,640	236,596	234,086	-0.8%	0.2%
EBITDA	49,750	51,621	52,889	-3.6%	-5.9%
EBITDA Margin (%)	21.20%	21.82%	22.59%	(62) bps	(139) bps
Adjusted PAT	32,830	32,704	33,222	0.4%	-1.2%

Reco	: BUY
CMP	: Rs 928
Target Price	: Rs 1,140
Potential Return	: +22.8%

Stock data (as on April 22, 2022)

Nifty	16,058
52 Week h/l (Rs)	1,378 / 924
Market cap (Rs/USD mn)	2,517,738 / 31,629
Outstanding Shares (mn)	2,714
6m Avg t/o (Rs mn):	4,099
Div yield (%):	4.8
Bloomberg code:	HCLT IN
NSE code:	HCLTECH

Stock performance



	1M	3M	1Y
Absolute return	-8.6%	-16.6%	-1.5%

Shareholding pattern (As of Mar'22 end)

Promoter	60.7%
FII+DII	33.7%
Others	5.4%

Δ in stance

(1-Yr)	New	Old
Rating	BUY	BUY
Target Price	1,140	1,407

Δ in earnings estimates

	FY22	FY23E	FY24E
EPS (New)	50.4	54.0	63.3
EPS (Old)	50.4	57.0	67.0
% change	NA	-5.2%	-5.5%

Financial Summary

(Rs mn)	FY22	FY23E	FY24E
Net Revenue	856,510	979,620	1,116,410
YoY Growth	13.6%	14.4%	14.0%
EBIDTA	201,920	219,856	259,170
YoY Growth	0.7%	8.9%	17.9%
PAT	135,150	146,648	171,805
YoY Growth	3.9%	8.5%	17.2%
ROE	22.2%	22.5%	23.8%
EPS	50	54	63
P/E	18.6	17.2	14.7
BV	228	252	281
P/BV	4.1	3.7	3.3

PIYUSH PANDEY
 Lead Analyst

piyush.pandey@ysil.in

+91 22 68850521



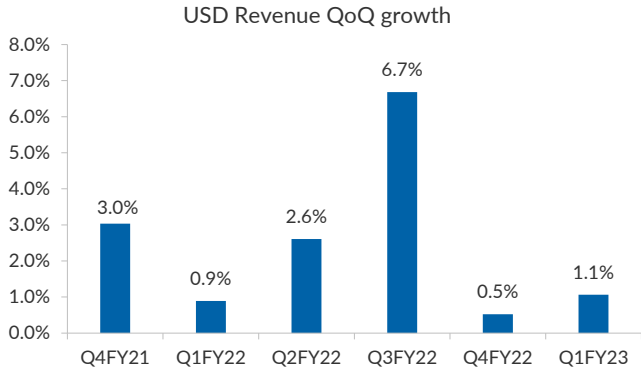
Exhibit 1: Quarterly snapshot:

Particulars (Rs mn)	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23	yoy %	qoq %	FY22	FY21	yoy %
Sales (\$ mn)	2,720	2,791	2,978	2,993	3,025	11.2	1.1	11,482	10,175	12.8
Sales	200,680	206,550	223,310	225,970	234,640	16.9	3.8	856,510	753,790	13.6
EBITDA	49,080	48,380	53,930	50,530	49,750	1.4	-1.5	201,920	200,560	0.7
EBITDA %	24.5	23.4	24.2	22.4	21.2	-325 bps	-116 bps	23.6	26.6	-303 bps
Depreciation	9,770	9,220	11,360	9,840	9,830	0.6	-0.1	40,190	39,850	0.9
EBIT	39,310	39,160	42,570	40,690	39,920	1.6	-1.9	161,730	160,710	0.6
EBIT Margin %	19.6	19.0	19.1	18.0	17.0	-258 bps	-99 bps	18.9	21.3	-244 bps
Other income	1530.0	1280.0	1000.0	1170.0	2630.0	71.9	124.8	8260.0	6440.0	28.3
PBT	41,250	41,230	44,300	43,210	43,370	5.1	0.4	169,990	167,150	1.7
Tax	8,940	8,460	9,820	7,210	10,560	18.1	46.5	34,430	36,630	-6.0
PAT	32,310	32,770	34,480	36,000	32,810	1.5	-8.9	135,560	130,520	3.9
Minority Interest	160	130	60	60	-20	-112.5	-133.3	410	440	-6.8
Net Income after MI	32,150	32,640	34,420	35,940	32,830	2.1	-8.7	135,150	130,080	3.9
NPM (%)	16.1	15.9	15.4	15.9	14.0	-212 bps	-195 bps	15.8	17.3	-149 bps

KEY CON-CALL HIGHLIGHTS

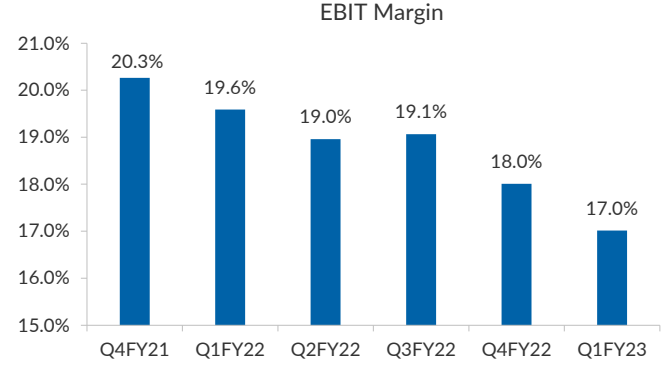
- Cloud migration and modernization continues to drive the growth of IT services.
- The operating margin should sequentially rise over next 2 quarters with some moderation in Q4.
- The decline in IT services margin was more than 100 bps QoQ, which got slightly offset by margin improvement in ER&D segment.
- Management expects that on account of margin levers related to utilization, pricing action, improvement in employee pyramid, and positive operating leverage, it should be able to manage lower level of 18-20% EBIT margin band for FY23.
- Expects to hire 30k-35k freshers for FY23.
- Not seeing any slowdown in demand environment as the deal pipeline remains near all time high.
- There has been some delay in realization of price increase discussions with clients.
- It has taken several HR related steps to control high attrition, which remains industry wide phenomena.

Exhibit 2: Sequential growth was along expectation



Source: Company, YES Sec

Exhibit 3: EBIT margin remains under pressure



Source: Company, YES Sec

FINANCIALS

Exhibit 4: Income Statement

Y/e March 31 (Rs mn)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Net sales	505,710	604,280	706,780	753,790	856,510	979,620	1,116,410
Operating expenses	(391,300)	(464,590)	(539,850)	(553,230)	(654,590)	(759,764)	(857,240)
EBITDA	114,410	139,690	166,930	200,560	201,920	219,856	259,170
Depreciation	(14,520)	(21,480)	(28,400)	(39,850)	(40,190)	(41,040)	(46,771)
EBIT	99,890	118,210	138,530	160,710	161,730	178,816	212,399
Other income	11,110	7,830	1,470	6,440	8,260	13,336	12,183
Finance cost	0	0	0	0	0	0	0
Profit before tax	111,000	126,040	140,000	167,150	169,990	192,152	224,582
Tax (current + deferred)	(23,170)	(24,810)	(29,380)	(36,630)	(34,430)	(45,524)	(52,777)
Reported Profit / (Loss)	87,830	101,230	110,620	130,080	135,150	146,648	171,805
Adjusted net profit	87,830	101,230	110,620	130,080	135,150	146,648	171,805

Exhibit 5: Balance Sheet

Y/e March 31 (Rs mn)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Share capital	2,780	2,710	5,430	5,430	5,430	5,430	5,430
Reserves & surplus	361,080	410,950	507,240	593,700	613,710	678,935	755,771
Shareholders' funds	363,860	413,660	512,670	599,130	619,140	684,365	761,201
Non-current liabilities	15,300	48,070	77,550	87,290	82,520	82,352	82,432
Long-term borrowings	3,380	29,770	28,480	38,280	39,230	37,269	35,405
Other non-current liabilities	11,920	18,300	49,070	49,010	43,290	45,084	47,027
Current liabilities	101,070	122,990	237,300	173,830	187,750	189,241	200,558
ST borrowings, Curr maturity	420	7,240	18,450	0	620	639	658
Other current liabilities	100,650	115,750	218,850	173,830	187,130	188,602	199,901
Total (Equity and Liabilities)	480,230	585,750	829,060	861,940	890,330	956,878	1,045,111
Non-current assets	234,650	288,530	444,860	431,430	409,920	439,578	455,078
Fixed assets (Net block)	122,740	140,620	217,360	202,650	177,890	191,747	205,029
Non-current Investments	3,030	850	770	890	1,030	1,030	1,030
Other non-current assets	106,530	143,510	226,730	227,890	231,000	246,801	249,019
Current assets	245,580	297,220	384,200	430,510	480,410	517,300	590,033
Cash & current investment	63,750	100,920	119,650	156,610	188,750	168,174	200,381

Y/e March 31 (Rs mn)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Other current assets	181,830	196,300	264,550	273,900	291,660	349,127	389,652
Total (Assets)	480,230	585,750	829,060	861,940	890,330	956,878	1,045,111
Total debt	3,800	37,010	46,930	38,280	39,850	37,907	36,063
Capital employed	379,580	470,000	610,210	688,110	703,200	768,276	845,210

Exhibit 6: Cash Flow Statement(Rs mn)

Y/e March 31 (Rs mn)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Profit before tax	111,000	126,040	140,000	167,150	169,990	192,152	224,582
Depreciation	14,520	21,480	28,400	39,850	40,190	41,040	46,771
Change in working capital	(32,953)	(1,740)	39,220	(53,660)	(4,190)	(56,342)	(29,638)
Total tax paid	(25,552)	(28,610)	(26,550)	(23,130)	(33,830)	(57,972)	(51,306)
Others	(5,700)	(6,020)	(1,610)	(5,980)	(4,980)	(10,056)	(8,903)
Cash flow from operations (a)	61,315	111,150	179,460	124,230	167,180	108,822	181,506
Capital expenditure	(44,207)	(39,360)	(105,140)	(25,140)	(15,430)	(54,897)	(60,053)
Change in investments	(14,801)	3,550	(47,610)	2,040	5,200	(3,120)	(3,275)
Others	3,568	(2,160)	(12,060)	3,840	4,070	8,041	6,686
Cash flow from investing (b)	(55,440)	(37,970)	(164,810)	(19,260)	(6,160)	(49,976)	(56,643)
Free cash flow (a+b)	5,875	73,180	14,650	104,970	161,020	58,847	124,863
Equity raised/(repaid)	(74)	(70)	2,720	0	0	0	0
Debt raised/(repaid)	(647)	33,210	9,920	(8,650)	1,570	(1,943)	(1,844)
Dividend (incl. tax)	(20,310)	(13,210)	(16,250)	(32,560)	(113,890)	(81,403)	(94,970)
Others	(35,103)	(54,570)	(40,000)	(24,640)	(11,220)	803	883
Cash flow from financing (c)	(56,134)	(34,640)	(43,610)	(65,850)	(123,540)	(82,542)	(95,931)
Net change in cash (a+b+c)	(50,258)	38,540	(28,960)	39,120	37,480	(23,696)	28,932

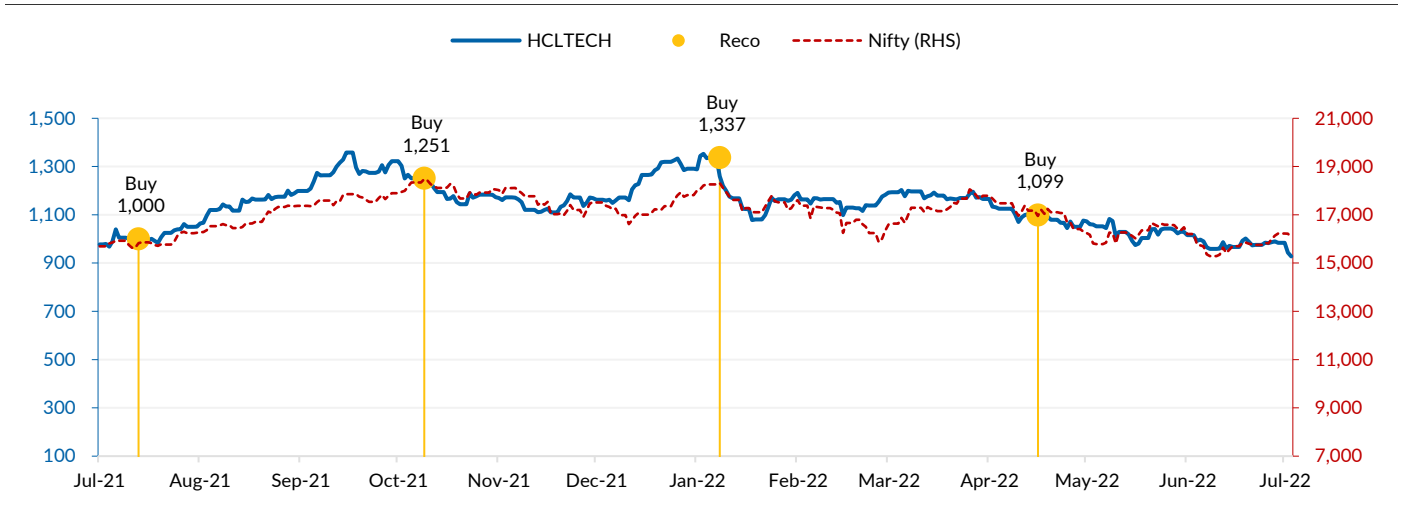
Exhibit 7: Ratio Analysis

Y/e March 31	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Growth(%)							
Revenue Growth	8.2	19.5	17.0	6.7	13.6	14.4	14.0
EBITDA Growth	11.0	22.1	19.5	20.1	0.7	8.9	17.9
EBIT Growth	5.4	18.3	17.2	16.0	0.6	10.6	18.8
Net Profit Growth	3.9	15.3	9.3	17.6	3.9	8.5	17.2
Profitability Ratios(%)							
EBITDA Margin	22.6	23.1	23.6	26.6	23.6	22.4	23.2
EBIT margin	19.8	19.6	19.6	21.3	18.9	18.3	19.0
Net Profit margin	17.4	16.8	15.7	17.3	15.8	15.0	15.4
RoA	21.3	22.2	19.6	19.0	18.5	19.4	21.2
RoE	25.3	26.0	23.9	23.4	22.2	22.5	23.8
RoCE	27.6	27.8	25.6	24.8	23.2	24.3	26.3
Liquidity Ratios							
Net debt/Equity (x)	-0.2	-0.2	-0.1	-0.2	-0.2	-0.2	-0.2
Current ratio (x)	2.4	2.4	1.6	2.5	2.6	2.7	2.9
Quick ratio (x)	2.4	2.4	1.6	2.5	2.6	2.7	2.9
Valuation Ratios							
PER(x)	NA	NA	NA	NA	18.6	17.2	14.7
PCE(x)	NA	NA	NA	NA	14.4	13.4	11.5
Price/Book(x)	NA	NA	NA	NA	4.1	3.7	3.3
EV/EBITDA(x)	NA	NA	NA	NA	11.7	10.9	9.1

Exhibit 8: Dupont Analysis

	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Net margin(%)	17.4	16.8	15.7	17.3	15.8	15.0	15.4
Asset turnover (x)	1.1	1.1	1.0	0.9	1.0	1.1	1.1
Leverage factor (x)	1.4	1.4	1.5	1.5	1.4	1.4	1.4
Return on Equity(%)	25.3	26.0	23.9	23.4	22.2	22.5	23.8

Recommendation Tracker



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Registered Address: 2nd Floor, North Side, YES BANK House, Off Western Express Highway, Santacruz East, Mumbai - 400 055, Maharashtra, India.

Correspondence Address: 4th Floor, AFL House, Lok Bharti Complex, Marol Maroshi Road, Andheri East, Mumbai - 400059, Maharashtra, India.

☎ +91 22 68850521 | ✉ research@ysil.in
Website: www.yesinvest.in

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ADD: Upside between 10% to 20% over 12 months

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