FIRST LIGHT

18 October 2021

RESEARCH

HCL Technologies | Target: Rs 1,440 | +15% | BUY

Product business a drag on performance

Daily macro indicators

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	1.54	(4bps)	20bps	81bps
India 10Y yield (%)	6.32	(1bps)	14bps	41bps
USD/INR	75.37	0.2	(2.6)	(2.8)
Brent Crude (US$/bbl)	83.18	(0.3)	14.1	92.0
Dow	34,378	0.0	(0.7)	20.6
Shanghai	3,562	0.4	(3.8)	6.6
Sensex	60,737	0.8	4.2	48.9
India FII (US$ mn)	**12-Oct**	**MTD**	**CYTD**	**FYTD**
FII-D	(12.6)	(273.1)	(198.1)	1,829.2
FII-E	33.8	134.4	8,664.4	1,338.0

Source: Bloomberg

SUMMARY

HCL Technologies

- Q2 a miss with subdued revenue growth of 2.6% QoQ USD due to 8.4% contraction in product business
- TCV strong at US$ 2.2bn, up 38% QoQ with 14 large deals. Weak product business profits capped EBIT margin at 19%
- We reduce FY22-FY24 EPS by 6-7% and set our TP at Rs 1,440 (Rs 1,530 earlier); retain BUY

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BUY
TP: Rs 1,440 | ⮝ 15%

HCL TECHNOLOGIES | Technology & Internet | 15 October 2021

Product business a drag on performance

- **Q2 a miss with subdued revenue growth of 2.6% QoQ USD due to 8.4% contraction in product business**
- **TCV strong at US$ 2.2bn, up 38% QoQ with 14 large deals. Weak product business profits capped EBIT margin at 19%**
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Growth underperforms: HCLT reported 3.5% QoQ CC revenue growth in Q2FY22, below our (5.5%) and street (5%) estimates. The product and platform (P&P) business disappointed with a revenue decline of 8% QoQ CC (8.4% USD) due to seasonality, whereas the services business (88% of revenue) clocked a strong uptick of 5.2% QoQ CC. Within services, ER&D was up 5.3% and IT & business services (ITBS) grew 4% QoQ USD. ER&D commentary was positive, similar to other peers as asset-heavy industries recovered after multiple Covid waves.

Pick-up in manufacturing and healthcare: Among verticals, growth was led by manufacturing/life-sciences & healthcare/technology services which grew 6.8%/ 6.8%/2% QoQ USD. BFSI disappointed (-1.1%) while retail and ENU were flattish.

Miss on margins: EBIT margin at 19% declined 60bps QoQ and missed our/street estimates owing to 430bps P&P margin contraction. Services business EBIT margin at 18.9% was flattish sequentially. Employee cost as a percentage of revenue increased 100bps QoQ as HCLT hired ~11k employees in Q2 to backfill attrition which skyrocketed to 15.7% from 11.8% in Q1FY22.

Deal wins remain strong: TCV was at US$ 2.2bn vs. US$ 1.7bn in Q1. HCLT bagged 14 new transformational deals in Q2 (including one large product-based contract) vs. 12 deals in Q1. The company saw significant wins from the telecom, BFSI, manufacturing, hi-tech and life-sciences verticals.

FY22 guidance largely intact; product business to remain flat: Management's FY22 outlook of double-digit CC revenue growth and 19-21% EBIT margin is unchanged. HCLT expects a strong Q3 as some deal slippages in Q2 are recouped. Growth in FY22 will hinge on ITBS as the product business is guided to grow only 0-1%.

Retain BUY: We cut EPS estimates to factor in lower growth and margins, translating to a new Sep'22 TP of Rs 1,440, based on an unchanged target P/E of 24.6x. Despite weakness in the product business, we retain BUY given the robust demand climate and strong traction in ITBS driven by cloud services and digital transformation.

Key changes

Target	Rating
▼	◀ ▶

Ticker/Price	HCLT IN/Rs 1,251
Market cap	US$ 45.1bn
Free float	38%
3M ADV	US$ 82.5mn
52wk high/low	Rs 1,378/Rs 800
Promoter/FPI/DII	60%/27%/13%

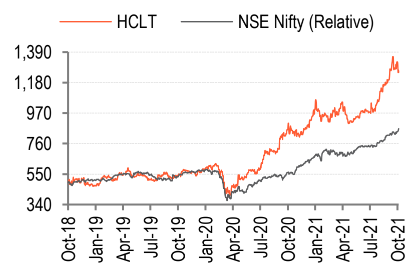
Source: NSE | Price as of 14 Oct 2021

Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	753,790	842,705	947,245
EBITDA (Rs mn)	200,560	206,350	240,395
Adj. net profit (Rs mn)	130,660	133,201	149,683
Adj. EPS (Rs)	48.1	49.1	55.2
Consensus EPS (Rs)	48.1	49.8	56.7
Adj. ROAE (%)	22.9	20.3	20.5
Adj. P/E (x)	26.0	25.5	22.7
EV/EBITDA (x)	16.9	16.4	13.8
Adj. EPS growth (%)	17.8	1.9	12.4

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

Disclaimer

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

BUY – Expected return >+15%

HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

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