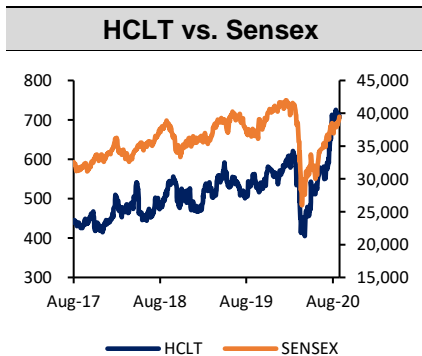


Target: Rs.886
CMP Rs.704 (13.5x FY23 P/E)
BUY

Index Details	
Sensex	39,106
Nifty	11,532
Industry	IT / ITES

Scrip Details	
Mkt Cap (Rs Cr)	1,91,042
O/S Share (Cr)	271.4
3 M Avg Vol (000)	365.6
52 Wk H/L (Rs)	729/376
Div Yield (%)	0.85
FVPS (Rs)	2.0

Shareholding Pattern	
Shareholder	%
Promoters	60.33
Institutional	35.63
Public	4.04
Total	100.00



Over the period FY16-FY20, HCL Technologies (HCLT) delivered robust double-digit USD revenue growth of 12.4% CAGR (INR revenue CAGR of 14.6%) despite the fact that its peers were posting slower growth. And it did experience a slowdown in Q1FY21 (QoQ decline of 7.4%), the order pipeline and energetic client engagements are suggestive of growth coming back. The management enthused by these recent developments has guided for 1.5-2.5% QoQ constant currency growth for the rest of FY21 and margins are expected in the range of 19.5%-20.5%.

We expect USD revenues to grow at a CAGR of 6.8% to \$12,104 mn (Rs.91,682 cr, 9.1% CAGR) by FY23. Over the same period, EBITDA and net profit are estimated to grow at a CAGR of 9.1% and 6.3% to \$3,047 Mn (Rs.23,079 cr, 10.1% CAGR) and \$1,867 Mn (Rs.14,140 cr, 8.6% CAGR), respectively. With strong profitability, return ratios RoE & ROIC are expected to improve by 21 bps & 237 bps to 21.8% & 27.4% respectively. Given the comfortable cash position, we anticipate strong pay-outs to shareholders over the forecast period.

We are optimistic given:

- The increased focus on cost take out programs, akin to the global financial crisis, to boost demand for IT & business services (ITBS). Cost takeout programs would mean increased focus on
 - Offshoring
 - Automation
 - Cloud adoption
 - Digital services

HCLT with a Q1FY21 revenue share of 70% from ITBS and an integrated stack is expected to be a big beneficiary of this cost take out trend.

- The fledgling, M&A fuelled Products and Platforms vertical (14% of Q1FY21 revenue) has completed 1 year of acquisition of the 7 IBM service line products. These horizontal products are not aligned with any particular vertical. Being in areas of security, marketing, automation, commerce, etc., and already a sticky part of the original systems of embedded customers are least impacted by the external economic environment.

Key Financials (in ₹ crores)

	Sales	EBITDA	Net Profit	EBITDA Margin (%)	Net Margin (%)	EPS ₹	BV ₹	RoE (%)	RoIC (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)
FY19	60,427	13,926	10,120	23.0	16.7	37.3	152.4	24.5	26.8	18.9	4.6	13.3
FY20	70,676	17,316	11,054	24.5	15.6	40.7	188.9	21.6	25.0	17.3	3.7	10.7
FY21E	76,255	19,658	11,723	25.8	15.4	43.2	212.1	20.4	26.3	16.3	3.3	9.2
FY22E	83,881	20,884	12,687	24.9	15.1	46.8	228.9	20.4	25.6	15.1	3.1	8.6
FY23E	91,682	23,079	14,140	25.2	15.4	52.1	238.5	21.8	27.4	13.5	3.0	7.8

This suite of products under the erstwhile ownership of IBM suffered from lack of investments. On assuming, ownership HCLT's R&D team has made considerable investments in product upgrades, refreshes and maintenance. This has resulted in renewed interest among existing clients leading to newer revenue streams and AMC renewals.

Prior to the acquisition of this product suite, HCLT had net cash of US \$1.13 bn (as on 31st Mar 2019). In the June quarter, the last of the instalments towards this purchase was paid out. Even after \$856 mn of the balance pay-out the cash & investments stand at \$1.38 bn and is testimony to the fact that these products are delivering an IRR of 15%+ (post tax).

Although this quarter the segment had witnessed a 2% revenue degrowth, given the strong growth outlook, we expect this segment to continue to do well. With segment EBIT contribution of about 30% we expect the corporate level EBIT to improve well beyond 20%.

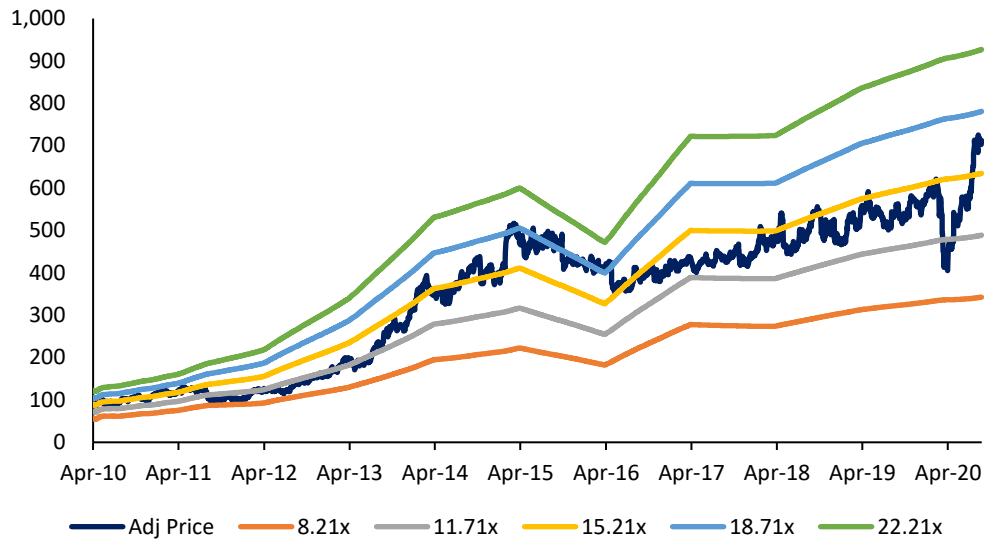
- The Engineering & R&D segment (16% of Q1FY21 revenue) has a higher discretionary component than the other two pieces. With customer focus on cost control and new product development and other initiatives on the back burner, this segment performance is expected to remain muted in the near term. However, we expect this this segment to be a strong revenue growth driver in the long term given the plethora of new technologies and product / services that are expected to be launched with the onset of 5G.

With a complete asset stack for products and services, HCLT has a strong digital foundation to address the emerging technical needs of clients and staying relevant. Apart from migration to cloud, the company has identified business analytics, IoT, cyber security and digital process outsourcing as the future growth engines.

Over the last 4 years, HCLT has spent a mammoth \$3.5 bn on acquisitions. With net cash & investments of \$1.38 bn (as on 30th Jun 2020), HCLT has a sizeable war chest for acquiring growth businesses, especially in the SAAS and the product space.

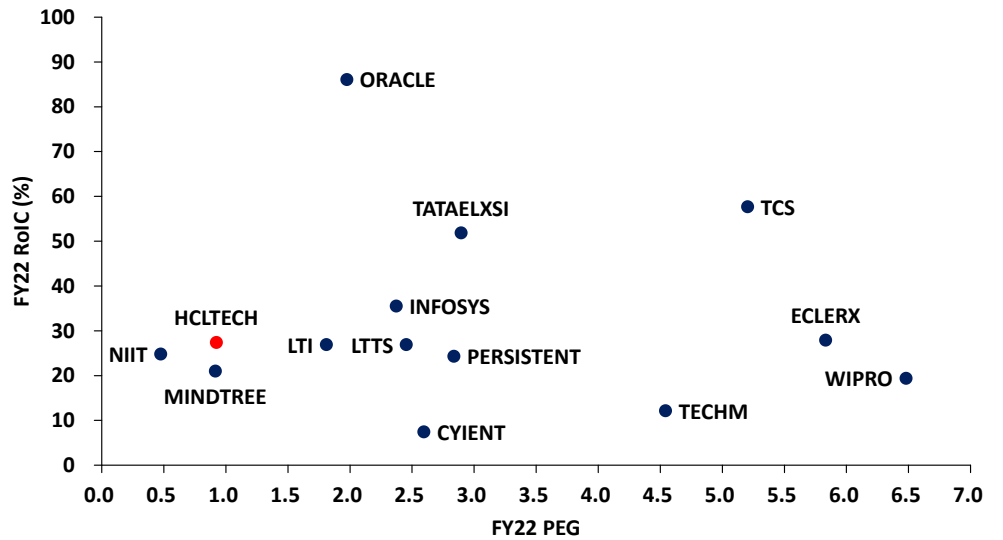
This carefully carved out acquisition strategy has ensured that HCLT has not only grown ahead of its peers in constant currency terms but also been able to narrow down the margin gap significantly. This should eventually lead to better return ratios and rerating of its valuation multiple. We initiate coverage on HCLT with a Buy for a 24-month PT of Rs.886 (17X FY23).

1 year forward P/E band chart



Source: Ventura Research

IT peer comparison

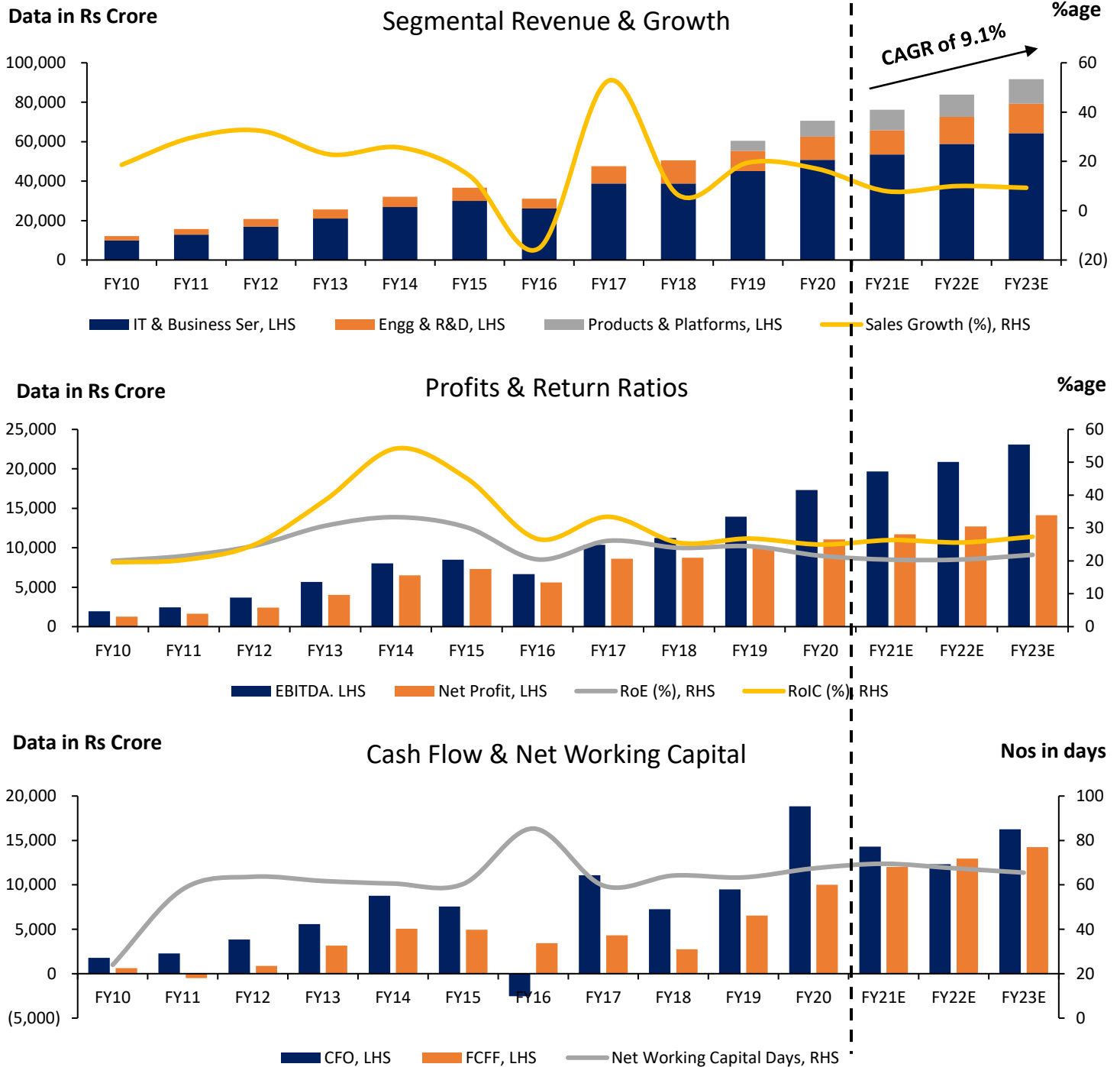


Source: Ventura Research

Lower dividend payout deteriorated the return ratios. But consistent inorganic expansion is expected to sustain top-line and bottom-line growth in future

Story of HCLT in pictorial format

Performance charts of HCLT



Source: Company reports & Ventura Research

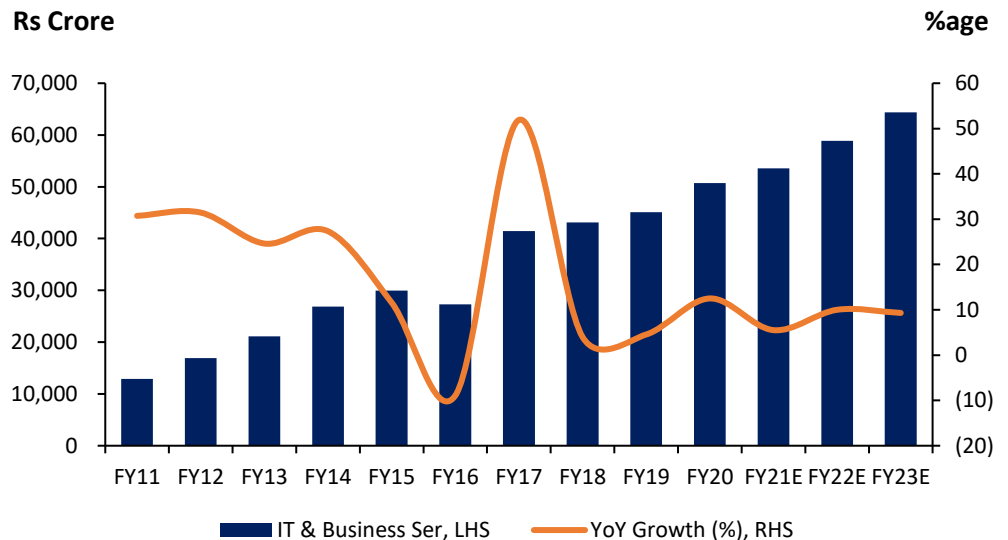
Business Segments

Business Segments	Q1FY21 revenue contribution	Services offered
IT & Business Services	70%	Provides a comprehensive portfolio of IT & Business Services (Application, Infrastructure and Digital Process Operations) and Digital transformation services enabled by Digital and Analytics, IoTWORKSTM, Cloud native and Cybersecurity solutions including products developed within these businesses.
Engineering and R&D Services	16%	Provides comprehensive engineering services and solutions across software, embedded, mechanical, VLSI and platform engineering that support the end to end lifecycle of products – both hardware and software across diverse industries including products developed within this business.
Products & Platforms	14%	Includes standalone product businesses that provide modernized software products to global clients for their technology and industry specific requirements.

Source: Company Reports & Ventura Research

IT & Business Services – A one-stop-shop solution for clients

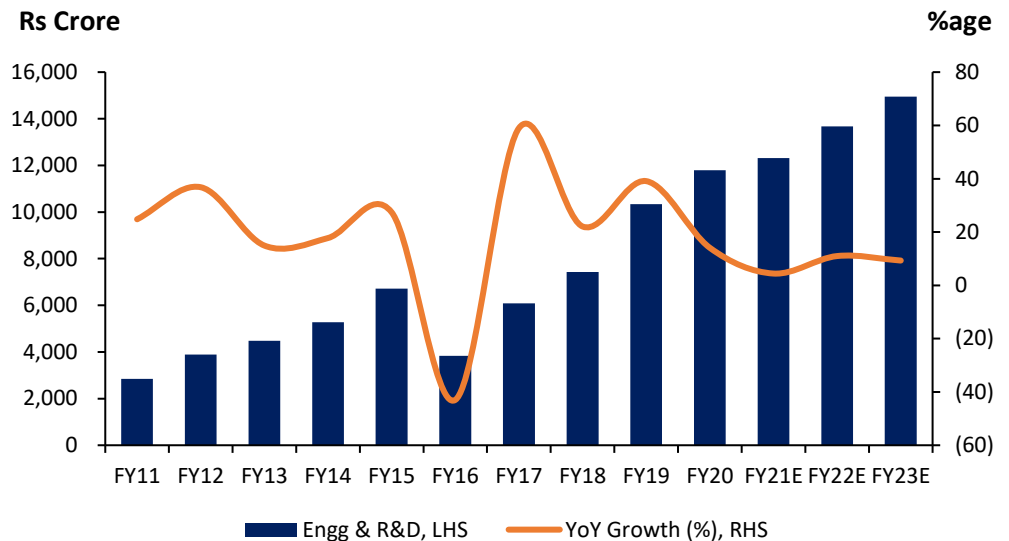
Global IT spends are not growing significantly and IT companies growing on market share gains and acquisitions. HCLT is gaining market share by providing end-to-end solutions to their clients and always open for acquisitions



Source: Company Reports & Ventura Research

Engineering and R&D – World’s 3rd largest business ERD unit

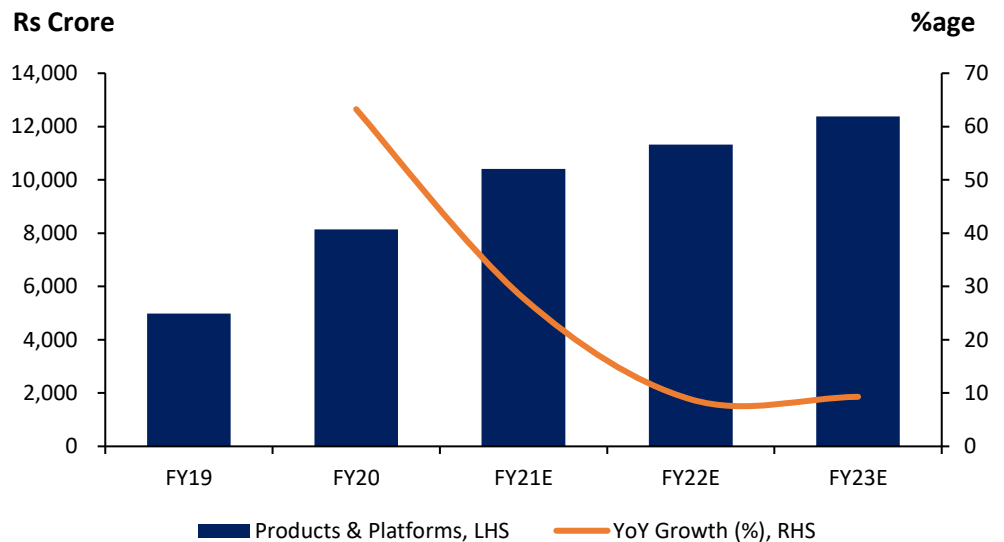
HCLT’s ER&D space is the world’s 3rd largest (largest by employee base). Rising demand for automation and platform engineering to reduce cost in manufacturing, infrastructure and other heavy industries, which has opened opportunities for this segment



Source: World Gold Council, Company Reports & Ventura Research

Products & Platforms – IBM products improved the presence

Most Indian IT companies are only in the IT solutions and services business, while very few are in IT products development. HCLT entered in this business in FY19 and with the acquisition of IBM products, it emerged strongly



Source: Company Reports & Ventura Research

Effective cash utilization for better business growth

HCLT kept its dividend pay-out lower than its peers and used that cash to propel its business performance and product diversification. This resulted in a revenue CAGR of 14.0% during FY15-20, while EBITDA and net profit grew at a CAGR of 15.4% and 8.6% respectively. This is superior to that its peers –

- **Tata Consultancy Services:** Revenue / EBITDA / Net Profit CAGR of 10.6% / 11.5% / 10.3% respectively and average dividend pay-out ratio of 46.8%
- **Infosys:** Revenue / EBITDA / Net Profit CAGR of 11.2% / 7.9% / 6.0% respectively and average dividend pay-out ratio of 49.3%
- **Wipro:** Revenue / EBITDA / Net Profit CAGR of 5.4% / 3.7% / 2.3% respectively and average dividend pay-out ratio of 8.1%.

Cash flow utilization

Cash Flow Utilization	FY16	FY17	FY18	FY19	FY20
HCL Technologies Ltd					
Cash Flow from Operations	Rs.3,154 Cr	Rs.6,995 Cr	Rs.6,339 Cr	Rs.8,676 Cr	Rs.13,359 Cr
Acquisitions	Volvo IT (\$138 Mn) PowerObjects (\$46 Mn) Geometric (\$188 Mn) C2SiS (\$10 Mn)	Butler America (\$85 Mn)	UrbanFulfillment (\$30 Mn) ETL Factory (£7.0 Mn)	H&D Int (€30 Mn) Actian Corp (\$330 Mn) Strong Bridge (\$45 Mn)	IBM Products (\$1.8 Bn) Sankalp Semi (\$25 Mn)
Buyback			Rs.3,500 Cr	Rs.4,000 Cr	
Dividend Payout Ratio (%)	40.28	39.74	19.13	10.71	12.27
Tata Consultancy Services Ltd					
Cash Flow from Operations	Rs.19,109 Cr	Rs.25,223 Cr	Rs.25,067 Cr	Rs.28,593 Cr	Rs.32,369 Cr
Acquisitions			Transamerica (\$2.0 Bn)	BridgePoint (\$1.5 Bn)	
Buyback			Rs.16,000 Cr	Rs.16,000 Cr	
Dividend Payout Ratio (%)	37.14	39.15	37.84	37.42	82.31
Infosys Ltd					
Cash Flow from Operations	Rs.10,028 Cr	Rs.11,531 Cr	Rs.13,218 Cr	Rs.14,841 Cr	Rs.17,003 Cr
Acquisitions	Skava (\$120 Mn) Noha Consul (\$70 Mn)		SkyTree (\$21 Mn) Brilliant Basics (£7.5 Mn)	Fluidio Oy (€65 Mn) WongDoody (\$75 Mn)	Stater NV (€128 Mn) Simplus (\$250 Mn)
Buyback			Rs.13,046 Cr	Rs.813 Cr	Rs.7,478 Cr
Dividend Payout Ratio (%)	41.13	41.05	59.05	60.52	44.71
Wipro Ltd					
Cash Flow from Operations	Rs.7,887 Cr	Rs.9,277 Cr	Rs.8,423 Cr	Rs.11,632 Cr	Rs.10,064 Cr
Acquisitions				Unza (\$246 Mn) LD Waxson (\$144 Mn) Zhongshan	Rational Int (\$52 Mn)
Buyback		Rs.2,500 Cr	Rs.11,031 Cr		Rs.10,531 Cr
Dividend Payout Ratio (%)	16.64	5.72	5.65	6.70	5.88

Source: Company Reports

Key management personnel

Key Person	Designation	Description
Mr Shiv Nadar	Founder & Chief Strategy Officer	Shiv Nadar is the Founder of HCL Enterprise, a \$9.9 billion global organization with over 150,000 professionals operating from 49 countries. He is also the Chief Strategy Officer of HCL Technologies, a group company and India's third largest IT services organization.
Mrs Roshni Nadar Malhotra	Chairperson	Roshni Nadar Malhotra is the CEO and Executive Director of the \$9.9 billion HCL Corporation, responsible for providing strategic guidance to the organization. She is also the Chairperson on the Board of HCL Technologies, a leading global technology organization with a market capitalization of \$20.5 billion, and the Chairperson of its CSR Committee.
Mr C Vijayakumar	President & CEO	Vijay is a graduate in Electrical & Electronics Engineering from P.S.G. College of Technology, Tamil Nadu, India, and lives in New York in the USA. He joined HCL nearly 25 years back as a member of the core team that designed and implemented India's first ever fully automated trading network at the National Stock Exchange.
Mr Prateek Aggarwal	CFO	Prateek is a graduate in commerce from SRCC, Delhi, and holds an MBA degree from IIM, Calcutta. He has also completed an M&A course from The University of Chicago Booth School of Business. His past experience includes working with organizations like Hindustan Unilever and GECIS, among others. After his stint from 2005-2008, Prateek re-joined HCL Technologies in 2012 and has held several leadership roles over the past six years. In the past couple of years, Prateek has played a pivotal role in shaping HCL's Mode 3 strategy and scaling our Products & Platforms business, as well as leading M&A pursuits from financial and legal angles.

Source: Company Reports

Financial Statements

Figures are in Rs Cr	FY19	FY20	FY21E	FY22E	FY23E		FY19	FY20	FY21E	FY22E	FY23E
Income Statement						Per Share Data (Rs)					
Net Revenue (USD Million)	8,632	9,936	10,067	11,074	12,104	Adjusted EPS	37.3	40.7	43.2	46.8	52.1
YoY Growth (%)	10.1	15.1	1.3	10.0	9.3	Adjusted Cash EPS	44.9	53.3	59.1	63.4	69.7
Net Revenue	60,427	70,676	76,255	83,881	91,682	Dividend Yield (%)	0.6	0.9	2.8	4.3	6.0
YoY Growth (%)	19.5	17.0	7.9	10.0	9.3	Dividend Per Share	4.0	6.0	20.0	30.0	42.5
Total Expenditure	46,501	53,360	56,597	62,997	68,602	FCFF Yield (%)	3.4	5.2	6.3	6.8	7.5
YoY Growth (%)	18.3	14.8	6.1	11.3	8.9	Adjusted Book Value per Share	152.4	188.9	212.1	228.9	238.5
EBITDA	13,926	17,316	19,658	20,884	23,079	Debt Burden					
Margin (%)	23.0	24.5	25.8	24.9	25.2	Total Debt to Equity	0.1	0.1	0.1	0.1	0.1
Depreciation	2,073	3,420	4,301	4,515	4,766	Net Debt to Equity	(0.1)	(0.1)	(0.2)	(0.2)	(0.2)
Depreciation to Gross Block (%)	6.7	7.4	8.9	8.8	8.7	Net Debt to EBITDA	(0.4)	(0.4)	(0.7)	(0.6)	(0.6)
EBIT	11,853	13,896	15,357	16,369	18,313	Return Ratios					
Margin (%)	19.6	19.7	20.1	19.5	20.0	Return on Equity (%)	24.5	21.6	20.4	20.4	21.8
Other Income	943	589	602	858	826	Return on Capital Employed (%)	23.0	21.4	20.3	20.0	21.5
Finance Cost	174	505	533	533	533	Return on Invested Capital (%)	26.8	25.0	26.3	25.6	27.4
Interest Coverage	68.1	27.5	28.8	30.7	34.3	Working Capital					
PBT	12,622	13,980	15,425	16,693	18,605	Receivable Days	71	73	75	74	73
Margin (%)	20.9	19.8	20.2	19.9	20.3	Inventory Days	1	0	1	1	1
Tax	2,502	2,923	3,702	4,006	4,465	Payable Days	8	6	6	7	8
Tax Rate (%)	19.8	20.9	24.0	24.0	24.0	Net Working Capital Days	63	67	70	68	66
PAT	10,120	11,057	11,723	12,687	14,140	Valuation Ratios					
Margin (%)	16.7	15.6	15.4	15.1	15.4	P/E	18.9	17.3	16.3	15.1	13.5
Min Int/Share of Associates	0	(3)	0	0	0	P/BV	4.6	3.7	3.3	3.1	3.0
Net Profit	10,120	11,054	11,723	12,687	14,140	EV/EBITDA	13.3	10.7	9.2	8.6	7.8
Margin (%)	16.7	15.6	15.4	15.1	15.4	EV/Sales	3.1	2.6	2.4	2.1	2.0
Balance Sheet						Cash Flow Statement					
Share Capital	271	543	543	543	543	Profit Before Tax	12,622	13,980	15,425	16,693	18,605
Total Reserves	41,095	50,724	57,020	61,566	64,172	Adjustments	(1,520)	212	4,048	622	3,059
Shareholders' Fund	41,366	51,267	57,563	62,109	64,715	Change in Working Capital	(1,599)	(2,564)	(1,464)	(992)	(940)
Minority Interest	103	154	154	154	154	Less: Tax Paid	(2,502)	(2,923)	(3,702)	(4,006)	(4,465)
Long Term Borrowing	2,977	2,848	2,500	2,250	2,000	Cash Flow from Operations	7,001	8,705	14,307	12,317	16,259
Long Term Lease Liability	0	2,179	2,179	2,179	2,179	Net Capital Expenditure	(3,434)	(1,829)	(2,500)	(3,000)	(3,500)
Deferred Tax Liability	(2,229)	(2,230)	(2,230)	(2,230)	(2,230)	Change in Investment Activities	2,473	(8,634)	(2,881)	(369)	(378)
Other Non Current Liabilities	783	1,593	1,593	1,500	1,400	Cash Flow from Investing	(961)	(10,463)	(5,381)	(3,369)	(3,878)
Long Term Provisions	821	1,048	1,137	1,248	1,358	Change in Borrowings	3,321	992	(693)	(750)	(750)
Total Liabilities	43,821	56,859	62,896	67,210	69,577	Buyback of Shares	(4,012)	0	0	0	0
Gross Block	30,730	46,104	48,604	51,604	55,104	Dividend & DDT	(1,321)	(1,625)	(5,427)	(8,141)	(11,533)
Less: Accumulated Depreciation	7,842	11,262	15,563	20,079	24,845	Less: Finance Cost	(174)	(505)	(533)	(533)	(533)
Net Block	22,888	34,842	33,041	31,525	30,259	Cash Flow from Financing	(2,186)	(1,138)	(6,654)	(9,424)	(12,816)
Right of use assets	0	2,648	2,648	2,648	2,648	Net Cash Flow	3,854	(2,896)	2,272	(477)	(435)
Capital Work in Progress	235	400	0	0	0	Opening Cash Balance	4,018	7,872	4,976	7,248	6,771
Non Current Investments	85	77	77	77	77	Closing Cash Balance	7,872	4,976	7,248	6,771	6,336
Long Term Loans & Advances	543	0	0	0	0						
Other Non Current Assets	2,647	4,202	4,534	4,987	5,451						
Net Current Assets	17,423	14,690	22,597	27,973	31,142						
Total Assets	43,821	56,859	62,896	67,210	69,577						

Source: Company Reports & Ventura Research

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