NARNOLIA
Advance Strategy Simple Solutions
SEBI Registered Portfolio Manager

# HCLTECH

*"Retain confidence"*

**"BUY"**
22nd Apr' 14

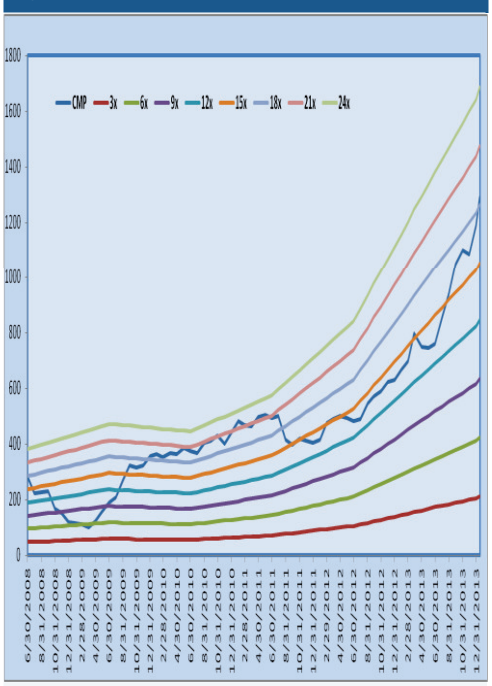
| Result update | Buy |
|---|---|
| CMP | 1435 |
| Target Price | 1650 |
| Previous Target Price | 1194 |
| Upside | 15% |
| Change from Previous | 38.2% |

| Market Data | |
|---|---|
| BSE Code | 532281 |
| NSE Symbol | HCLTECH |
| 52wk Range H/L | 1589/674 |
| Mkt Capital (Rs Crores) | 100383 |
| Average Daily Volume | 1193062 |
| Nifty | 6818 |

| Stock Performance | | | |
|---|---|---|---|
| | 1M | 1yr | YTD |
| Absolute | 2 | 95 | 149.1 |
| Rel. to Nifty | -3.2 | 17.9 | 131 |

| Share Holding Pattern-% | Current | 2QFY14 | 1QFY14 |
|---|---|---|---|
| **Promoters** | 61.69 | 61.75 | 61.84 |
| **FII** | 28.59 | 28.05 | 26.01 |
| **DII** | 3.69 | 4.20 | 5.70 |
| **Others** | 6.03 | 6 | 6.45 |

**1 year forward P/E**




***Strong show, while proved its consistency to maintain its margin at 26.7% mark;***

Following the successive 11th quarter, again company witnessed better growth in 3QFY14 . For 3QFY14, HCL Tech witnessed 3.9% (QoQ) sales growth in USD term and 2%(QoQ) in INR term led by better operating performance across all verticals and geographies. Dollar revenue growth of the company was far better than its peers Infosys and TCS that have reported at 0.38% de growth and 1.9% growth, respectively. PAT grew by 8.6%(QoQ).

**The company continues to lead the industry in profitable growth and margin expansion, having reported 56% growth in Net Income on Yearly basis. Management is confident to focus on vendor consolidation, application consolidation and cost control activities to maintain its growth story.**

**Stable Margin:** During the quarter, company's EBITDA margin ramped up by 70bps to 26.7% and good thing is, company has been able to maintain its range of 25-26% for its margin. PAT margin improved by 120bps to 19.5%, sequentially.

**Segmental Performance:** Infrastructure Services (contributes 34% of sales) continued to lead with growth at 4.1%, and Enterprise Application Services (contributes 17% of sales) up by 2.6% followed by Custom Application Services (contributes 16% of sales) at 1%. While, Engineering/ R&D Services down by 1% (QoQ) and BPO services (contributes 5% of sales) was unchanged.

**Mixed performance across verticals:** HCL Tech says financial services business grew 6.8% and manufacturing & Retail growth was at 1% on(QoQ) basis. While growth from Healthcare and Other services declined by 1% and 24% respectively.

**Healthy deal pipeline:** Healthy deal pipeline: During the quarter, HCL Tech reported an addition of 12 transformational deals in the US and Europe. HCL Tech has added two clients each in USD 50 million and USD 30 million categories. Its USD 100 million plus clients increased to 6 from 5 and USD 50 million clients rose to 14 from 13 year-on-year. Its USD 10 million clients jumped to 109 from 98 but USD 5 million clients declined to 183 from 187 Y-o-Y. These wins have been in the momentum markets of manufacturing and Financial Services as well as the emerging momentum markets of life sciences &

**View and Valuation:** HCL tech's decent level of utilization, focused on cost control and utilization of new market opportunities through vendor's consolidation would provide a new shape to the company in near future. On performance front, it continues to be bullish on the rebid market and bullish on short-term to medium term, momentum on deals pipeline also looking robust.

**Considering the increasing discretionary spends across the geographies like US and Europe, we expect healthy earnings performance ahead. At a CMP of Rs 1435, stock trades at 14.7x of FY15E earnings, We retain BUY on the stock with a target price of Rs1650.**

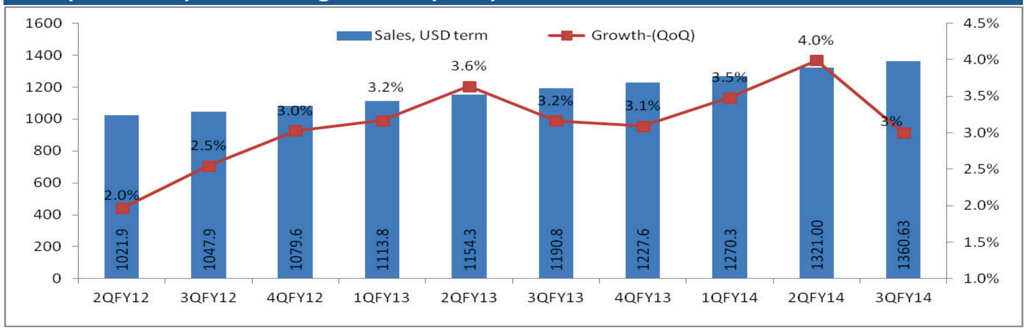
**Financials** Rs, Crore

| | 3QFY14 | 2QFY14 | (QoQ)-% | 3QFY13 | (YoY)-% |
|---|---|---|---|---|---|
| Revenue | 8349 | 8184 | **2.0** | 6424.6 | **30.0** |
| EBITDA | 2232 | 2125 | **5.0** | 1439.2 | **55.1** |
| PAT | 1624 | 1495 | **8.6** | 1039.7 | **56.2** |
| EBITDA Margin | 26.7% | 26.0% | **70bps** | 22.4% | **430bps** |
| PAT Margin | 19.5% | 18.3% | **120bps** | 16.2% | **320bps** |

**(Source: Company/Eastwind)**

# HCLTECH

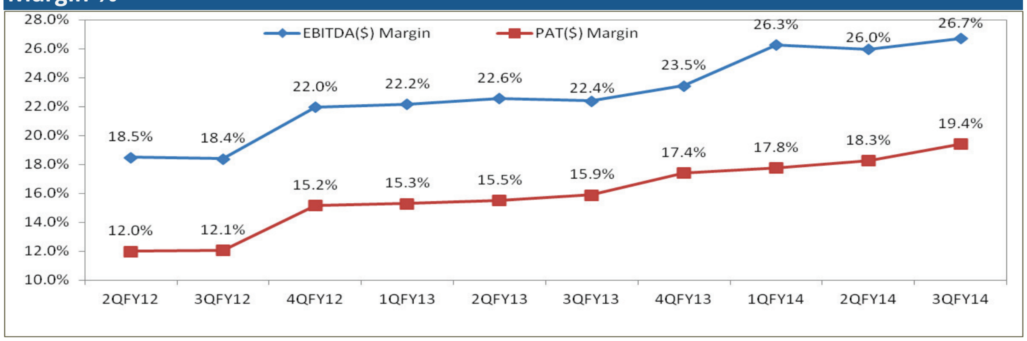
## Sales(USD term) and Sales growth-%(QoQ)




**(Source: Company/Eastwind)**

**In dollar terms, the revenues grew by 3% QoQ to USD 1360.63mn and net profit grew by 9.4% QoQ to USD 264.2mn.**

## Margin-%




**(Source: Company/Eastwind)**

**Tha company expects to maintain EBIT margin at 20-21% in medium term.**

## Clients Metrics

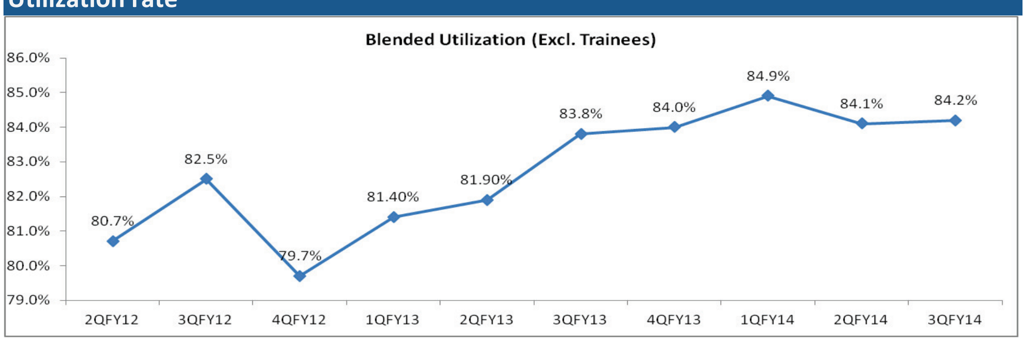
**Clients Contribution**

| | 2QFY12 | 3QFY12 | 4QFY12 | 1QFY13 | 2QFY13 | 3QFY13 | 4QFY13 | 1QFY14 | 2QFY14 | 3QFY14 |
|---|---|---|---|---|---|---|---|---|---|---|
| Top 5 Clients | 15.8% | 16.0% | 16.4% | 16.2% | 15.7% | 15.4% | 15.4% | 15.1% | 14.8% | 15.0% |
| Top 10 Clients | 24.2% | 24.3% | 24.7% | 24.5% | 24.2% | 24.0% | 23.8% | 23.8% | 23.8% | 24.1% |
| Top 20 Clients | 33.9% | 33.9% | 34.1% | 33.6% | 33.3% | 32.8% | 33.0% | 33.2% | 33.6% | 34.2% |

## Employee Metrics

| Head counts | 2QFY12 | 3QFY12 | 4QFY12 | 1QFY13 | 2QFY13 | 3QFY13 | 4QFY13 | 1QFY14 | 2QFY14 | 3QFY14 |
|---|---|---|---|---|---|---|---|---|---|---|
| No of Employee | 72055 | 72474 | 74675 | 75621 | 75226 | 74226 | 74912 | 87196 | 88332 | 90190 |
| Gross Addition | 4931 | 3303 | 5274 | 4479 | 3291 | 2933 | 4316 | 8061 | 7593 | 8291 |
| Attrition | 15.7% | 15.0% | 14.0% | 13.6% | 13.6% | 14.2% | 14.9% | 16.10% | 16.6% | 16.90% |

## Utilization rate




**(Source: Company/Eastwind)**

**Utilization stable at 84.2%. Further, it's Utilization are at decent levels, indicated can still derive more efficiency .**

# HCLTECH

## Key facts from Con-Call

The company is expecting to catch up more deal from US and Europe because of better demand environment ahead. Clients are looking vendor's consolidation, and company will try to turn this opportunity into deal.

The company expects to see EBIT margin at a range of 20-21% in near term. The wage hike is spread over two quarters or rather more than two quarters. Q4 margin could be impact be 30bps.

Digital systems integration, ALT ASM and infrastructure management services continue to drive the deal win momentum.

Focus on generating higher free cash flow continued during the quarter with free cash flow as percentage of EBITDA reaching 73%, up from 61% in the corresponding period last year.

## Financials;

| Rs, Cr | FY10 | FY11 | FY12 | FY13 | FY14E | FY15E |
|---|---|---|---|---|---|---|
| Net Sales-USD | 2704.6 | 3545.3 | 4151.5 | 4686.5 | 5387.7 | 6324.0 |
| Net Sales | 12136.3 | 15730.3 | 20830.6 | 25581.1 | 32999.6 | 38260.1 |
| Raw Materials Cost | 443.6 | 522.1 | 612.0 | 959.3 | 990.0 | 1147.8 |
| Employee Cost | 6253.7 | 8589.6 | 11104.6 | 12574.2 | 16334.8 | 19130.1 |
| Operation and other expenses | 3498.5 | 4163.2 | 5418.8 | 6386.4 | 7259.9 | 8608.5 |
| Total Expenses | 10195.7 | 13274.9 | 17135.3 | 19919.9 | 24584.7 | 28886.4 |
| EBITDA | 1940.6 | 2455.4 | 3695.2 | 5661.2 | 8414.9 | 9373.7 |
| Depreciation | 418.1 | 459.7 | 549.2 | 636.8 | 741.4 | 870.3 |
| Other Income | 154.1 | 299.7 | 206.5 | 306.6 | 486.0 | 594.0 |
| EBIT | 1522.5 | 1995.7 | 3146.0 | 5024.4 | 7673.5 | 8503.5 |
| Interest Cost | 204.1 | 142.6 | 142.6 | 105.6 | 79.2 | 59.4 |
| PBT | 1472.4 | 2152.8 | 3209.8 | 5225.4 | 8080.3 | 9038.0 |
| Tax | 213.4 | 488.5 | 782.7 | 1225.3 | 1834.2 | 2214.3 |
| PAT | 1259.0 | 1664.3 | 2427.1 | 4000.1 | 6246.1 | 6823.7 |
| **Growth-%** | | | | | | |
| Sales-USD | 24.1% | 31.1% | 17.1% | 12.9% | 15.0% | 17.4% |
| Sales | 18.6% | 29.6% | 32.4% | 22.8% | 29.0% | 15.9% |
| EBITDA | 5.9% | 26.5% | 50.5% | 53.2% | 48.6% | 11.4% |
| PAT | -4.6% | 32.2% | 45.8% | 64.8% | 56.1% | 9.2% |
| **Margin -%** | | | | | | |
| EBITDA | 16.0% | 15.6% | 17.7% | 22.1% | 25.5% | 24.5% |
| EBIT | 12.5% | 12.7% | 15.1% | 19.6% | 23.3% | 22.2% |
| PAT | 10.4% | 10.6% | 11.7% | 15.6% | 18.9% | 17.8% |
| **Expenses on Sales-%** | | | | | | |
| Employee Cost | 51.5% | 54.6% | 53.3% | 49.2% | 49.5% | 50.0% |
| RM Cost | 3.7% | 3.3% | 2.9% | 3.8% | 3.0% | 3.0% |
| Operation and other expenses | 28.8% | 26.5% | 26.0% | 25.0% | 22.0% | 22.5% |
| Tax rate | 14.5% | 22.7% | 24.4% | 23.4% | 22.7% | 24.5% |
| **Valuation** | | | | | | |
| CMP | 364.9 | 493.5 | 490.0 | 759.5 | 1435.0 | 1435.0 |
| No of Share | 67.9 | 68.9 | 69.3 | 69.6 | 69.6 | 69.6 |
| NW | 6288.8 | 7653.0 | 9837.9 | 13164.0 | 18269.9 | 23953.5 |
| EPS | 18.5 | 24.2 | 35.0 | 57.5 | 89.7 | 98.0 |
| BVPS | 92.6 | 111.1 | 141.9 | 189.1 | 262.5 | 344.1 |
| RoE-% | 20.0% | 21.7% | 24.7% | 30.4% | 34.2% | 28.5% |
| Dividend Payout ratio-% | 25.0% | 31.5% | 33.1% | 20.2% | 18.3% | 16.7% |
| P/BV | 3.9 | 4.4 | 3.5 | 4.0 | 5.5 | 4.2 |
| P/E | 19.7 | 20.4 | 14.0 | 13.2 | 16.0 | 14.6 |

(Source: Company/Eastwind)