

October 15, 2024

Q2FY25 Result Update

Change in Estimates | Target | Reco

Change in Estimates

	Current		Previous	
	FY26E	FY27E	FY26E	FY27E
Rating	BUY		BUY	
Target Price	2,130		2,080	
Sales (Rs. m)	1,305	1,468	1,298	1,460
% Chng.	0.5	0.5		
EBITDA (Rs. m)	311	355	308	352
% Chng.	0.9	0.8		
EPS (Rs.)	72.0	83.0	71.3	82.3
% Chng.	1.0	0.9		

Key Financials - Consolidated

Y/e Mar	FY24	FY25E	FY26E	FY27E
Sales (Rs. bn)	1,099	1,174	1,305	1,468
EBITDA (Rs. bn)	259	273	311	355
Margin (%)	23.5	23.3	23.8	24.2
PAT (Rs. bn)	157	173	195	225
EPS (Rs.)	58.0	63.9	72.0	83.0
Gr. (%)	5.7	10.1	12.8	15.3
DPS (Rs.)	52.0	57.5	64.8	74.7
Yield (%)	2.8	3.1	3.5	4.0
RoE (%)	23.5	25.1	27.5	30.8
RoCE (%)	21.7	22.4	25.4	28.6
EV/Sales (x)	4.3	4.1	3.7	3.2
EV/EBITDA (x)	18.5	17.5	15.3	13.4
PE (x)	32.0	29.1	25.8	22.4
P/BV (x)	7.4	7.2	7.0	6.8

Key Data

HCLT.BO | HCLT IN

52-W High / Low	Rs.1,866 / Rs.1,212
Sensex / Nifty	81,973 / 25,128
Market Cap	Rs.5,036bn / \$ 59,914m
Shares Outstanding	2,714m
3M Avg. Daily Value	Rs.5106.2m

Shareholding Pattern (%)

Promoter's	61.02
Foreign	18.45
Domestic Institution	15.79
Public & Others	4.74
Promoter Pledge (Rs bn)	-

Stock Performance (%)

	1M	6M	12M
Absolute	2.4	22.0	47.8
Relative	3.5	10.5	19.5

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Strong performance, but painted blurry outlook

Quick Pointers:

- Strong H1 narrows lower-end of the guidance from 3-5% to 3.5-5%, further de-risking to achieve growth at the up-end of the band
- TCV wins normalizes to comfort band of US\$ 2bn in Q2

HCLT reported overall strong results in Q2 with revenue, EBIT & PAT coming ahead of our & consensus estimates. Revenue came at US\$3.44 bn, up 1.6% QoQ CC (PLe 1.1% QoQ CC & consensus est. 0.6% QoQ CC). IT Services, ER&D & Software business grew by 1.8%, 1.1% & 1.4% QoQ CC respectively. In IT Services, the growth was broad based across geographies & verticals (FS grew excluding the JV divesture) with a healthy mix of cost optimization, transformation & discretionary spends. EBIT margin in Q2 increased by 150 bps (PLe of 80 bps & consensus est. of 90 bps) to 18.6% due to lower marketing spends & strong software business. The deal TCV was also steady at US\$ 2.2 bn vs US\$ 1.96 bn in Q1 with healthy pipeline.

After a Q1 trough, the recovery in Q2 was broad-based across verticals despite the revenue loss through JV divestment, which impacted FS vertical growth (flat QoQ). The growth was predominantly driven by the IT service business, while ER&D business growth was soft in Q2 and impacted by the continued weakness in Automotive and Aerospace segments. The strong uptick in the P&P business was a little surprising, which was led by product innovation and investments in new features, which have started gaining traction among its existing accounts. Despite the fact, the management maintained a sign of caution to its P&P business due to its nature of being volatile and maintained its aspiration to achieve mid-single digit growth in the medium-term. Although Q2 maintained a balanced growth on both discretionary and non-discretionary spends, the management painted cautious outlook predominantly on the macro headwinds and geo-political tension. Otherwise, the broad-based momentum within IT service should continue in the coming quarters. Based on the revised guidance, the ask rate for the rest of FY25 would be (0.7%-2.6% CC QoQ), which we believe is achievable led by improvement in deal TCV and constructive recovery. We are baking in revenue growth of 5.1% YoY CC (4.8% earlier) in FY25 and broadly keeping FY26/FY27 revenue estimates unchanged (9.8%/11.1% CC).

Margin performance was also strong in Q2 across its business mix that partly aided by lower SG&A seasonality in Q2, however the compensation revision cycle in H2 would keep the margins under pressure. Additionally, the continued fresher hiring would keep the utilization under check and provide lesser room for margin improvement. We are passing on some Q2 margin beat to full year FY25 and baking in 18.3% EBIT margin (earlier 18.1%), while keeping FY26/FY27 margin estimates broadly unchanged (18.9/19.4%).

Valuations and outlook: Given its defensive business mix and resilient vertical portfolio, HCLT is well positioned to capture the boarder market theme and participate in the critical aspects of enterprise operations. We are baking in USD revenue/Earnings CAGR of 9.3%/12.8% between FY24-27E. The stock is currently trading at 25x/22x FY26E/FY27E. We maintain "BUY" on HCL Tech assigning PE of 25x to FY27E with a target price of Rs. 2,130.

Strong performance, beating estimates on all front

- USD rev of 3.45b, up 1.6% QoQ in CC (up 2.4% QoQ reported), above our (+1.1% CC) and median consensus est. (+0.6% CC)
- Services business up 1.6% QoQ in CC, with IT services (up 1.8% QoQ in CC) and ER&D (up 1.1% QoQ in CC).
- HCL Software (P&P) was up 1.4% QoQ CC and up 9.4% YoY CC
- **Q2 new Deal TCV normalised to earlier run-rate of \$2.2bn vs Q1 low base at \$1.96bn**
- Broad-based growth across verticals, except FS (muted QoQ) all other verticals grew sequentially, while NA and Europe reported 1.0% and 4.3% QoQ growth, respectively
- **With improved revenue growth in Q2, the company has narrowed lowed-end of the guidance band by 50bps to 3.5-5% CC YoY (vs earlier 3-5% CC). EBIT margin guidance kept intact at 18.0-19.0%**
- **Q2 EBIT margin saw an improvement of 150bps to 18.6%, against our and consensus estimated improvement of 80 bps and 90bps QoQ, respectively**
- Services EBIT margin up 110bps QoQ, while P&P was up 500 bps QoQ
- **Net employees count declined by 780 QoQ and added 2.9k freshers during the quarter, Attrition at 12.9%, up 10bp QoQ**
- Reported PAT of Rs. 42.4b, flat QoQ/10.5% YoY, vs our estimates of Rs42.6b. Muted QoQ PAT due to lower other income
- The Board declared a dividend of Rs12/share
- FCF/NM at 119% on LTM basis

Concall Highlights

- The management mentioned that growth in Q2 was broad based across segments, geographies & verticals.
- ER&D segment reported growth after two successive quarters of decline. The management however mentioned that the demand is weak in auto (Europe region) & aerospace sub-segments. They also mentioned that auto segment weakness is likely to continue in Q3.
- In Software business segment the company mentioned that strong growth in seasonally weak quarter was due to the investment in sales & integration of sales team. They also mentioned that it on path of its 3 year strategic plan for its software business and expects it continue to grow in mid-single digit annually.

- In IT services, the growth was broad based across geographies & verticals except FS, which was flat in Q2. However, FS segment excluding the impact of State Street JV divesture reported growth on sequential basis. Management noted that the automotive sub-segment within the manufacturing sector is facing challenges due to client-specific issues. They further mentioned that some of the large clients are either cancelling the projects or postponing the same. They further mentioned that the demand of SAP transformation is strong in manufacturing segment which is offsetting the weakness in auto clients.
- The management mentioned that it would implement wage hike in H2. They also indicated that the wage hike would impact margins by approximately 65-80 basis points in Q3 and 60-70 basis points in Q4. Overall, employees in India will receive an average wage increase of approximately 7%, with top performers receiving raises in the range of 12-15%.
- On demand front, management noted continued traction in transformation and discretionary spending. Q2 revenue growth was driven by both cost efficiency and transformation programs. They further mentioned that they expect the demand recovery to continue however indicated caution due to the escalation in geo-political conflicts. The management also mentioned that they expect furloughs similar to last year in H2FY25.
- On Gen AI, the management mentioned that demand for Gen AI remains strong & it will be growth driver for them future. The also mentioned that they have continue to win Gen AI deals and most of the new deals have Gen AI function embedded in them. The company's generative AI initiatives, such as Gen AI Force, Gen AI Foundry, and AI labs, are gaining traction, with 25 modules in Gen AI Force moving to the adoption stage.
- HCLT overall EBIT margin improved by 110 bps sequentially with ~55 bps contribution from software segment. The management mentioned that remaining improvement was due to lower marketing spends in Q2 (seasonally high spends in Q1) in Services business & currency benefits.
- Top 5/10/20 clients revenue grew by 8.7%/5%/4.8% respectively.
- Guidance: HCLT increased its revenue guidance by 50 bps at lower end and it now guiding for revenue growth of 3.5-5% in CC terms at both company level & Services business. HCLT maintained the EBIT margin guidance of 18-19%.
- Net employees during the quarter declined by 780 to 218.6k. HCLT in Q2 added 2.9k freshers & LTM attrition increased marginally to 12.9% (10 bps increase)

Exhibit 1: 2QFY25 Results: USD revenues grew 2.4% QoQ, EBIT margin increased by 150bps QoQ

Consolidated (Rs bn)	2QFY25	1QFY25	QoQ gr. (%)	2QFY24	YoY gr. (%)	H1FY25	H1FY24	YoY gr. (%)
IT Services Revenue (USD mn)	3,445	3,364	2.4	3,225	6.8	6,809	6,425	6.0
Overall Revenue (Rs bn)	289	281	2.9	267	8.2	569	530	7.5
Gross Profit	101	97	3.9	97	4.3	198	190	3.9
Gross Margin (%)	34.9	34.5	40bps	36.2	-130bps	34.7	35.9	-120bps
SG&A and Other Costs	37.0	39.0	-5.0	37.2	-0.3	76.0	77	-1.1
% of Rev	12.8	13.9	-110bps	13.9	-110bps	13.4	14.5	-120bps
EBITDA	64	58	9.9	59	7.2	122	113	7.3
EBIT Margin (%)	22.1	20.7	140bps	22.3	-20bps	21.4	21.4	0bps
Depreciation	10	10	1	10	-0.3	20	19	3.5
% of Rev	3.5	3.6	-10bps	3.8	-30bps	3.5	3.7	-10bps
EBIT	54	48	11.8	49	8.7	102	94	8.1
EBIT Margin (%)	18.6	17.1	150bps	18.5	10bps	17.8	17.7	10bps
Other Income (net)	3	9	-64.4	2	67.5	12	4	187.7
PBT	57	57	-0.4	51	10.9	114	98.2	16.0
Tax	15	14	0.1	13	12.0	29	25	17.8
Effective tax rate (%)	25.5	25.4	10bps	25.3	20bps	25.4	25.0	40bps
Adjusted PAT	42	43	-0.5	38	10.5	85	74	15.4
Exceptional items	0	0	NA	0	NA	0	0	NA
Reported PAT	42	43	-0.5	38	10.5	85	74	15.4
Reported EPS (Rs)	15.6	15.7	-0.6	14.2	10.3	31	27	15.2

Source: Company, PL

Exhibit 2: Broad based Regional growth (%)

Geographies	Contr. To rev. (%)	QoQ Gr. (%)
Americas	65.1	1.0
Europe	28.4	4.3
RoW	6.5	9.1

Source: Company, PL

Exhibit 3: Broad based Vertical Growth (%)

Verticals	Contr. To rev. (%)	QoQ Gr. (%)
Financial Services	20.5	0.0
Manufacturing	19.5	2.9
Technology	13.1	3.2
Life Sciences & Healthcare	16.0	3.1
Telecom MP&E	12.1	1.6
Retail & CPG	9.6	4.6
Public Services	9.2	3.5

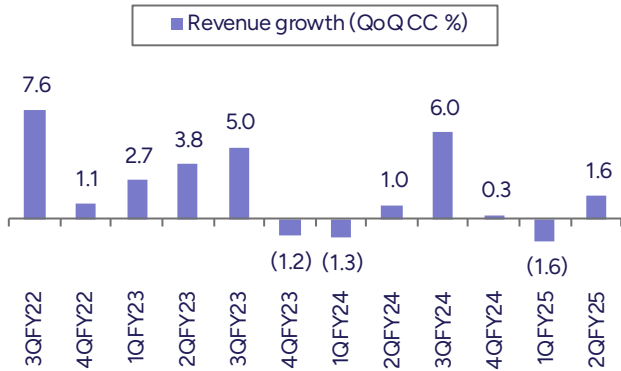
Source: Company, PL

Exhibit 4: Key Performance Indicator

	3QFY23	4QFY23	1QFY24	2QFY24	3QFY24	4QFY24	1QFY25	2QFY25	FY24	FY25E
Revenue (QoQ CC %)	5.0	-1.2	-1.3	1.0	6.0	0.3	-1.6	1.6	5.0	5.1
Margins										
Gross Margin	37.4	36.5	35.6	36.2	36.7	35.0	34.5	34.9	35.9	35.4
EBIT Margin	19.6	18.2	17.0	18.5	19.7	17.6	17.1	18.6	18.2	18.3
Net Margin	15.3	15.0	13.4	14.4	15.3	14.0	15.2	14.7	14.3	14.8
b										
Headcount (k)	222	226	223	221	225	227	219	219	227	-
Attrition (%)	21.7	19.5	16.3	14.2	12.8	12.4	12.8	12.9	12.4	-

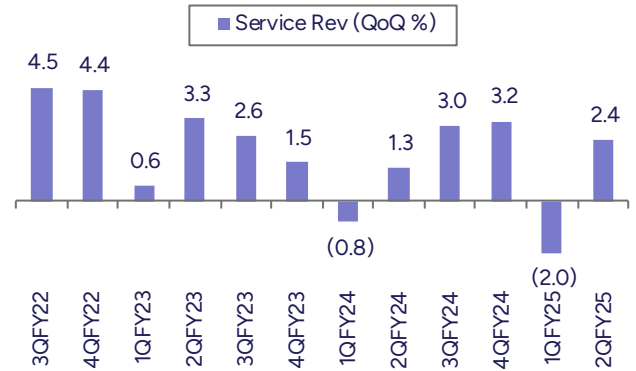
Source: Company, PL

Exhibit 5: Revenue growth QoQ % CC



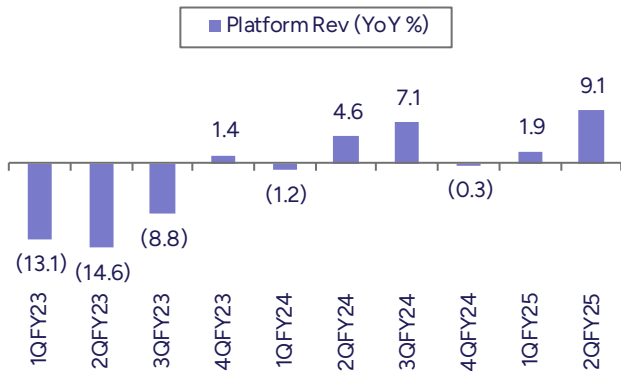
Source: Company, PL

Exhibit 6: Services business (IT & ER&D) revenue growth %



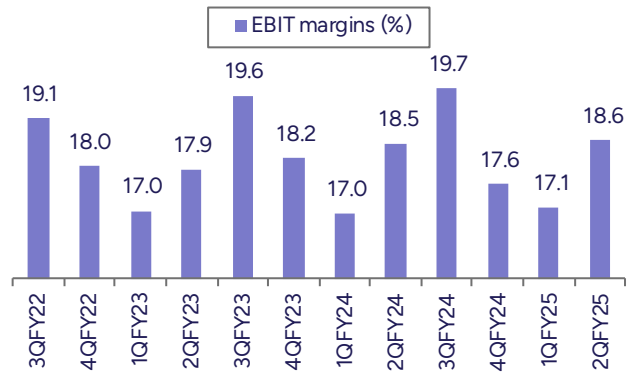
Source: Company, PL

Exhibit 7: Strong P&P revenue growth %



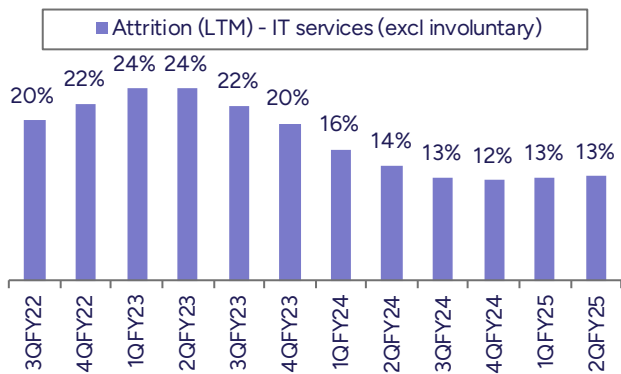
Source: Company, PL

Exhibit 8: EBIT margin increased in Q2 %



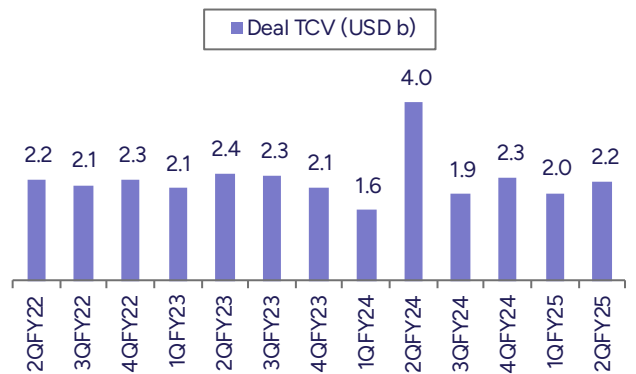
Source: Company, PL

Exhibit 9: Steady Attrition %



Source: Company, PL

Exhibit 10: Healthy deal TCV (USD bn)



Source: Company, PL

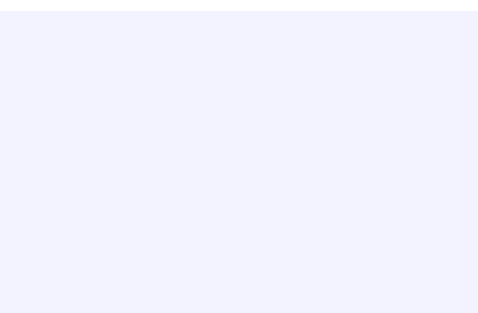
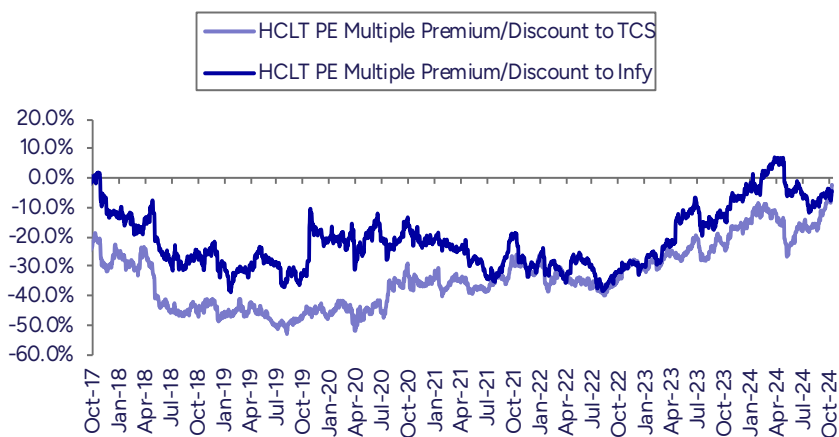


Exhibit 11: Operating Metrics

Consolidated (Rs bn)	3QFY22	4QFY22	1QFY23	2QFY23	3QFY23	4QFY23	1QFY24	2QFY24	3QFY24	4QFY24	1QFY25	2QFY25
Service Line wise (%)												
IT and Business Services	70.6	73.4	72.8	73.6	71.7	73.8	74.7	74.6	71.7	74.4	74.5	74.6
Engineering and R&D Services	15.9	16.4	16.6	17.0	16.6	16.1	15.4	16.0	16.4	16.1	15.9	15.8
Products and Platform	13.5	10.3	10.6	9.4	11.7	10.1	9.9	9.4	11.9	9.5	9.6	9.6
Vertical wise (%)												
BFSI	21.4	21.6	21.1	20.6	19.9	21.2	22.6	22.6	21.7	21.6	21.0	20.5
Manufacturing	17.5	18.0	18.3	18.3	18.3	19.0	19.0	19.0	20.1	20.4	19.4	19.5
Technology & Services	18.4	17.5	15.4	15.4	15.4	14.4	14.4	14.4	12.8	12.3	13.0	13.1
Retail & CPG	10.8	9.8	9.4	9.2	8.9	9.0	9.1	9.6	9.6	9.1	9.4	9.6
Telecom MP&E	8.4	9.0	9.2	9.2	9.4	8.8	7.6	8.0	9.7	11.5	12.2	12.1
Life Sciences	16.1	16.2	16.4	16.5	17.1	17.5	17.5	17.5	16.4	16.3	15.9	16.0
Public Services	10.3	10.5	10.2	10.2	10.2	10.2	10.0	9.9	9.7	8.8	9.1	9.2
Geography wise (%)												
US	63.4	63.1	63.1	64.8	63.5	63.8	64.5	64.5	64.5	65.2	66.0	65.1
Europe	28.7	28.7	28.6	27.5	29.1	28.9	28.7	28.5	29.0	28.9	27.9	28.4
ROW	7.9	8.2	8.3	7.7	7.4	7.3	6.8	7.0	6.4	5.9	6.1	6.5
Client wise (%)												
Top 5 clients	12.2	11.6	11.2	10.7	10.3	10.1	9.8	9.8	9.8	10.4	11.4	12.1
Top 10 clients	20.3	19.8	19.4	18.8	18.2	17.7	17.2	17.2	17.7	18.8	19.6	20.1
Top 20 clients	29.4	29.1	28.9	28.6	28.2	27.8	27.2	27.3	28.0	29.0	30.1	30.8

Source: Company, PL

Exhibit 12: HCLT 1-yr fwd PE premium/discount against TCS/Infy



Source: Company, PL

Financials

Income Statement (Rs m)

Y/e Mar	FY24	FY25E	FY26E	FY27E
Net Revenues	1,099	1,174	1,305	1,468
YoY gr. (%)	8.3	6.8	11.1	12.5
Employee Cost	705	759	833	932
Gross Profit	394	415	471	536
Margin (%)	35.9	35.4	36.1	36.5
Employee Cost	-	-	-	-
Other Expenses	-	-	-	-
EBITDA	259	273	311	355
YoY gr. (%)	6.6	5.7	13.8	14.2
Margin (%)	23.5	23.3	23.8	24.2
Depreciation and Amortization	42	42	47	53
EBIT	200	215	247	285
Margin (%)	18.2	18.3	18.9	19.4
Net Interest	-	-	-	-
Other Income	9	18	12	13
Profit Before Tax	210	233	259	298
Margin (%)	19.1	19.8	19.8	20.3
Total Tax	53	59	63	73
Effective tax rate (%)	25.1	25.5	24.5	24.5
Profit after tax	157	173	195	225
Minority interest	0	0	0	0
Share Profit from Associate	-	-	-	-
Adjusted PAT	157	173	195	225
YoY gr. (%)	5.7	10.3	12.8	15.3
Margin (%)	14.3	14.8	15.0	15.3
Extra Ord. Income / (Exp)	-	-	-	-
Reported PAT	157	173	195	225
YoY gr. (%)	5.7	10.3	12.8	15.3
Margin (%)	14.3	14.8	15.0	15.3
Other Comprehensive Income	-	-	-	-
Total Comprehensive Income	157	173	195	225
Equity Shares O/s (bn)	3	3	3	3
EPS (Rs)	58.0	63.9	72.0	83.0

Source: Company Data, PL Research

Balance Sheet Abstract (Rs m)

Y/e Mar	FY24	FY25E	FY26E	FY27E
Non-Current Assets				
Gross Block	643	688	737	793
Tangibles	370	415	465	520
Intangibles	273	273	273	273
Acc: Dep / Amortization	291	333	380	433
Tangibles	291	333	380	433
Intangibles	-	-	-	-
Net fixed assets	352	354	357	360
Tangibles	79	82	84	87
Intangibles	273	273	273	273
Capital Work In Progress	-	-	-	-
Goodwill	-	-	-	-
Non-Current Investments	1	1	1	1
Net Deferred tax assets	-	-	-	-
Other Non-Current Assets	52	52	54	56
Current Assets				
Investments	177	177	177	177
Inventories	-	-	-	-
Trade receivables	255	270	298	332
Cash & Bank Balance	95	102	110	122
Other Current Assets	66	71	79	88
Total Assets	998	1,027	1,075	1,136
Equity				
Equity Share Capital	5	5	5	5
Other Equity	677	695	714	737
Total Networkth	683	700	720	742
Non-Current Liabilities				
Long Term borrowings	22	22	22	22
Provisions	-	-	-	-
Other non current liabilities	66	68	73	79
Current Liabilities				
ST Debt / Current of LT Debt	1	1	1	1
Trade payables	59	59	63	70
Other current liabilities	168	177	197	222
Total Equity & Liabilities	998	1,027	1,075	1,136

Source: Company Data, PL Research

Cash Flow (Rs m)

Y/e Mar	FY24	FY25E	FY26E	FY27E
PBT	210	173	195	225
Add. Depreciation	42	42	47	53
Add. Interest	-	-	-	-
Less Financial Other Income	9	18	12	13
Add. Other	(50)	-	-	-
Op. profit before WC changes	201	215	242	278
Net Changes-WC	23	(8)	(9)	(8)
Direct tax	-	-	-	-
Net cash from Op. activities	224	208	234	270
Capital expenditures	(31)	(45)	(50)	(56)
Interest / Dividend Income	-	-	-	-
Others	(37)	-	-	-
Net Cash from Invt. activities	(67)	(45)	(50)	(56)
Issue of share cap. / premium	-	-	-	-
Debt changes	(2)	-	-	-
Dividend paid	(141)	(156)	(176)	(203)
Interest paid	-	-	-	-
Others	(12)	-	-	-
Net cash from Fin. activities	(155)	(156)	(176)	(203)
Net change in cash	3	7	8	12
Free Cash Flow	214	163	184	214

Source: Company Data, PL Research

Quarterly Financials (Rs m)

Y/e Mar	Q3FY24	Q4FY24	Q1FY25	Q2FY25
Net Revenue	284	285	281	289
YoY gr. (%)	6.7	0.2	(1.6)	2.9
Raw Material Expenses	180	185	184	188
Gross Profit	104	100	97	101
Margin (%)	36.7	35.0	34.5	34.9
EBITDA	72	65	62	68
YoY gr. (%)	-	-	-	-
Margin (%)	25.2	23.0	22.1	23.4
Depreciation / Depletion	11	11	10	10
EBIT	56	50	48	54
Margin (%)	19.7	17.6	17.1	18.6
Net Interest	-	-	-	-
Other Income	3	3	9	3
Profit before Tax	59	53	57	57
Margin (%)	20.6	18.5	20.3	19.7
Total Tax	15	13	14	15
Effective tax rate (%)	25.9	24.2	25.4	25.5
Profit after Tax	44	40	43	42
Minority interest	-	-	-	-
Share Profit from Associates	-	-	-	-
Adjusted PAT	44	40	43	42
YoY gr. (%)	13.5	(8.4)	6.8	(0.5)
Margin (%)	15.3	14.0	15.2	14.7
Extra Ord. Income / (Exp)	-	-	-	-
Reported PAT	44	40	43	42
YoY gr. (%)	13.5	(8.4)	6.8	(0.5)
Margin (%)	15.3	14.0	15.2	14.7
Other Comprehensive Income	-	-	-	-
Total Comprehensive Income	44	40	43	42
Avg. Shares O/s (m)	3	3	3	3
EPS (Rs)	16.1	14.7	15.7	15.6

Source: Company Data, PL Research

Key Financial Metrics

Y/e Mar	FY24	FY25E	FY26E	FY27E
Per Share(Rs)				
EPS	58.0	63.9	72.0	83.0
CEPS	73.4	79.4	89.3	102.5
BVPS	252.1	258.1	265.3	273.6
FCF	79.1	60.1	67.9	79.1
DPS	52.0	57.5	64.8	74.7
Return Ratio(%)				
RoCE	21.7	22.4	25.4	28.6
ROIC	22.3	22.8	24.9	26.7
RoE	23.5	25.1	27.5	30.8
Balance Sheet				
Net Debt : Equity (x)	(0.4)	(0.4)	(0.4)	(0.4)
Net Working Capital (Days)	65	66	66	65
Valuation(x)				
PER	32.0	29.1	25.8	22.4
P/B	7.4	7.2	7.0	6.8
P/CEPS	25.3	23.4	20.8	18.1
EV/EBITDA	18.5	17.5	15.3	13.4
EV/Sales	4.3	4.1	3.7	3.2
Dividend Yield (%)	2.8	3.1	3.5	4.0

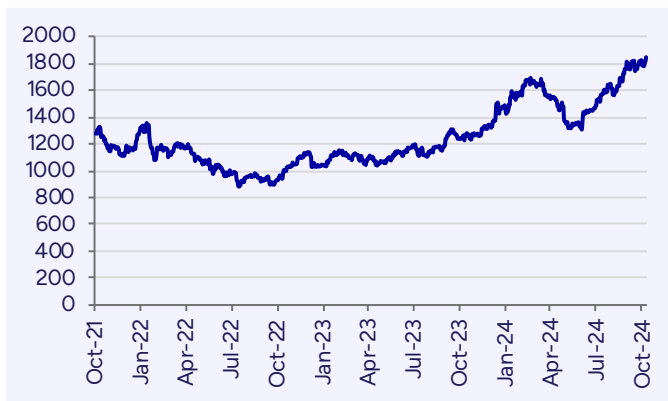
Source: Company Data, PL Research

Key Operating Metrics

Y/e Mar	FY24	FY25E	FY26E	FY27E
Revenue (USD mn)	13,270	14,014	15,477	17,308

Source: Company Data, PL Research

Price Chart



Recommendation History

No.	Date	Rating	TP (Rs.)	Share Price (Rs.)
1	03-Oct-24	BUY	2,080	1,817
2	14-Jul-24	BUY	1,790	1,560
3	02-Jul-24	BUY	1,680	1,469
4	28-Apr-24	Accumulate	1,550	1,474

Analyst Coverage Universe

Sr. No.	Company Name	Rating	TP (Rs)	Share Price (Rs)
1	Cyient	Accumulate	2,120	1,914
2	HCL Technologies	BUY	2,080	1,817
3	Infosys	BUY	2,180	1,904
4	LTIMindtree	BUY	7,200	6,273
5	Mphasis	Hold	3,020	3,016
6	Persistent Systems	Accumulate	5,770	5,488
7	Tata Consultancy Services	BUY	4,920	4,227
8	Tech Mahindra	Accumulate	1,720	1,625
9	Wipro	Accumulate	580	547

PL's Recommendation Nomenclature (Absolute Performance)

Buy	: > 15%
Accumulate	: 5% to 15%
Hold	: +5% to -5%
Reduce	: -5% to -15%
Sell	: < -15%
Not Rated (NR)	: No specific call on the stock
Under Review (UR)	: Rating likely to change shortly

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