

January 14, 2025

## On expected lines; likely soft Q4 outlook weighs....

**About the stock:** HCL Technologies (HCLTech) is a global technology company, employing 2,20,000+ people across 60 countries, delivering industry-leading capabilities centered around digital, engineering, cloud and AI, powered by a broad portfolio of technology services and products.

**Q3FY25 Performance:** HCL Tech reported revenue of US\$3,533 mn, up 3.8% QoQ & 4.1% YoY in CC terms. The EBIT margins came in at 19.5%, up ~90 bps QoQ/ down 20 bps YoY. IT services margins contracted by ~22 bps owing to tailwinds from productivity gains (100 bps) & forex gains (18 bps) which were offset by wage hike (-80 bps), furloughs (-40 bps) and HPE CTG acquisition (-20 bps).

### Investment Rationale

- Shift towards shorter duration deals to aid faster revenue conversion:** Management highlighted a shift in client spending pattern towards shorter duration deals and found longer deals taking more time to close. This has resulted in a robust annual contract value (ACV) growth of 9% QoQ and 23% YoY which shall aid in faster revenue conversion and support growth in the medium term. However, key monitorable would be improvement in TCv growth and the resolution of delay in discretionary spend based deal closures.
- Revenue growth outlook improved on the back of HPE CTG acquisition:** The company reported broadly in line numbers with the street estimates, driven by its software segment (+18.7% QoQ), which continued to anchor their quarterly performance. The lower end of its FY25 revenue guidance is revised upwards to 4.5-5% YoY in CC terms (bulk of which, i.e., ~50 bps, is HPE CTG acquisition induced), the organic growth outlook for FY25 remains unchanged. The implied organic growth for IT Services is now in the range of -1.6% to +0.6% QoQ in CC terms, implying a soft Q4 exit owing to ramp-down/reduction of a large /mega deal, delay in discretionary deal closures, and impact from the HPE CTG acquisition. **We believe the company's rupee revenue will grow at CAGR of 8.4% between FY24-27E, compared to CAGR of 12.7% between FY19-24.**
- Margins continue to remain in the comfort range of 18-19%:** The margins are expected to be within the previously guided margin band of 18-19%, going ahead. The company expects impact of ~50-60 bps in Q4 owing to wage hikes and residual impact from the increased amortisation for HPE CTG asset acquisition next quarter. Nonetheless, given the various operating levers in place we expect the margins in the guided band to be achievable. **Thus, we bake in EBIT margins of 18.5%/18.7%/19.2% in FY25E/26E/27E.**

### Rating and Target Price

- We expect earnings growth of ~10.4% over FY24-27. Nonetheless, we await FY26 outlook commentary ahead.
- We continue to maintain **HOLD** rating on the stock, valuing it at **target price of ₹ 1,870; at 24x P/E on FY27E EPS (vs. ₹1,840 earlier).**

### Key Financial Summary

Key Financials	FY22	FY23	FY24	5 year CAGR (FY19-24)	FY25E	FY26E	FY27E	3 year CAGR FY(24-27E)
Net Sales	85,651	1,01,456	1,09,913	12.7	1,17,015	1,27,988	1,39,841	8.4
EBITDA	20,041	22,628	24,200	11.6	25,759	28,541	31,884	9.6
Margins (%)	23.4	22.3	22.0		22.0	22.3	22.8	
Net Profit	13,516	14,851	15,702	5.8	17,385	18,787	21,100	10.4
EPS (₹)	49.8	54.8	57.9		64.1	69.2	77.8	
P/E	36.3	33.1	31.3		28.3	26.1	23.3	
RoNW (%)	21.8	22.7	23.0		24.2	24.9	26.5	
RoCE (%)	24.2	27.1	27.2		29.1	30.1	32.3	

Source: Company, ICICI Direct Research



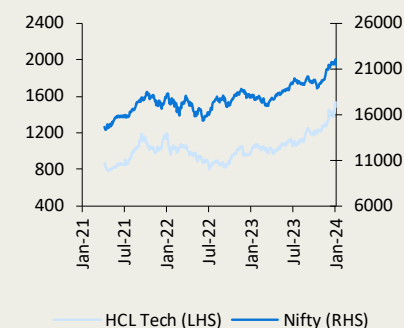
### Particulars

Particular	Amount
Market Cap (₹ Crore)	4,91,173
Total Debt (₹ Crore)	2,223
CC&E (₹ Crore)	27,193
EV (₹ Crore)	4,66,203
52 week H/L	2012 / 1235
Equity capital	543.0
Face value (₹)	2.0

### Shareholding pattern

	Dec-23	Mar-24	Jun-24	Sep-24
Promoters	60.8	60.8	60.8	60.8
FII	19.4	19.6	18.5	18.7
DII	15.2	15.0	15.8	15.8
Public	4.6	4.6	5.0	4.7

### Price Chart



### Key risks

- Lack of longer duration deals to backfill for large & mega deals being completed/ramped down;
- Better than expected growth

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## Performance highlights and Outlook

- Revenue Performance:** HCL Tech reported revenue of US\$3,533 mn, up 2.5% QoQ & up 3.5% YoY (in CC terms up 3.8% QoQ & 4.1% YoY). In rupee terms it reported revenue of ₹29,890 crore, up 3.6% QoQ & 5.1% YoY. Sequential growth was led by the software segment which grew 18.7% QoQ in CC terms. The IT services and ER&D business reported a growth of 1.5% and 5.4% QoQ in CC terms respectively.
- Margin Performance:** Margins in the quarter came in at 19.5%, up 90 bps QoQ. However, IT & Business Services and ER&D margins contracted by ~22 bps wherein the productivity gains from their margin improvement plan (Project Ascend) of 100 bps & forex gains of 18 bps were offset by wage hike impact of 80 bps, 40 bps from furloughs and 20 bps from the HPE CTG acquisition including integration expense. The PAT margin came at 15.4%, up 80 bps sequentially.
- Geography performance:** Geography wise all geographies grew on a YoY basis in CC terms with Americas (65.5% of mix), ROW (6.3% of mix) and Europe (28.2% of mix) reporting a growth of 6.2%, 2.9% and 2.6% respectively.
- Segment Performance:** Segment wise on YoY basis in CC terms, growth was led by TMPE (12.3% of mix), Retail & CPG (10.6% of mix) and Tech & Services (13.3% of mix) which grew by 33.1%, 17.2%, & 7.6% respectively while Public Services (8.9% of mix), Financial Services (20.3% of mix) & Life Sciences & Healthcare (15.5% of the mix) declined by 4.6%, 1.4% & 1.1% respectively.
  - Telecom & Media:** Reported a growth of 33.1% YoY in CC terms. This growth was attributed to the closing of HPE-CTG acquisition and consequent contribution of one month revenue from the business.
  - Retail & CPG:** Reported a growth of 17.1% YoY in CC terms. The management stated that the growth was broad based and was attributed to one of a large project which has come to an end. Overall pipeline for this vertical is healthy.
  - Manufacturing:** As per the management, the segment excl. automotive is progressing well. It expects automotive continues to remain a challenge for one or two more quarters.
  - BFSI & Technology:** The growth in tech and financial services is in line with the company's commentary and is witnessing increasing spending from clients, as per the management.
- Deal Wins:** Recorded a weak deal TCV at US\$2.1 bn, down 6% QoQ. The management mentioned that small deal wins are growing stronger than the large deal wins coupled with shorter deal cycles. Notably, ACV pipeline on a YoY basis has grown 23% and sequentially it is up 9%.
- Revenue and Margin Guidance/Aspiration:** The management has stated that Q4FY25 is expected to be a soft quarter and provided a guidance of organic revenue growth for IT services to be between -1.3% to 0.6%. The company has further guided that the usual seasonality will play out during 1QFY26E due to annual productivity passed on to clients as part of earlier large engagements and residual impact of large deal ramp down. The lower end of the revenue and services growth guidance for FY25 is revised upwards to 4.5-5% (vs 3.5-5% earlier), bulk of which, i.e., ~50 bps, is HPE CTG acquisition induced. The EBIT margin guidance maintained in the range of 18-19%.
- Attrition & Employee addition:** The headcount increased by 2,134 employees bringing the total employee headcount to 2,20,755. The attrition further inched up by 30 bps to YoY to 13.2%.
- Dividend:** The company declared an interim dividend of ₹12 per share and a special dividend of ₹6 per share. That brings their 12 months payout at ₹60 per share effectively distributing 95.2% of their net income.

**Exhibit 1: Quarter Performance**

	Q3FY25	Q3FY24	YoY (%)	Q2FY25	QoQ (%)	Comments
Revenue (US\$ mn)	353	342	3.5	345	2.5	In CC terms, revenue expanded by 3.8% QoQ and grew by 4.1% YoY
Revenue (₹ crore)	29,890	28,446	5.1	28,862	3.6	In CC terms, Software business reported growth of 18.7% QoQ while IT services and ER&D revenue grew by 1.5% & 5.4% QoQ
Cost of sales (including employee expenses)	19,661	18,416	6.8	19,184	2.5	
Gross Margin	10,229	10,030	2.0	9,678	5.7	
Gross margin (%)	34.2	35.3	-104 bps	33.5	69 bps	
Selling & marketing costs	3,369	3,272	3.0	3,309	1.8	
EBITDA	6,860	6,758	1.5	6,369	7.7	
EBITDA Margin (%)	23.0	23.8	-81 bps	22.1	88 bps	
Depreciation	1,039	1,143	-9.1	1,007	3.2	
EBIT	5,821	5,615	3.7	5,362	8.6	
EBIT Margin (%)	19.5	19.7	-26 bps	18.6	90 bps	IT services margin contracted by ~22 bps owing to productivity gains (100 bps) & forex gains (18 bps) which were offset by wage hike (-80 bps), furloughs (-40 bps) and HPE CTG acquisition (-20 bps)
Other income	311	259	20.1	325	-4.3	
PBT	6,132	5,874	4.4	5,687	7.8	
Tax paid	1,538	1,523	1.0	1,450	6.1	
PAT	4,591	4,350	5.5	4,235	8.4	

Source: Company, ICICI Direct Research

## Financial Summary

Exhibit 2: Profit and loss statement					₹ crore
Year-end March	FY24	FY25E	FY26E	FY27E	
<b>Total operating Income</b>	<b>1,09,913</b>	<b>1,17,015</b>	<b>1,27,988</b>	<b>1,39,841</b>	
Growth (%)	8.3	6.5	9.4	9.3	
Direct costs	72,125	77,703	84,728	92,015	
S,G&A expenses	13,588	13,553	14,719	15,942	
Total Operating Expenditure	85,713	91,256	99,447	1,07,957	
<b>EBITDA</b>	<b>24,200</b>	<b>25,759</b>	<b>28,541</b>	<b>31,884</b>	
Growth (%)	6.9	6.4	10.8	11.7	
Depreciation	4,173	4,131	4,551	4,971	
Amortisation	-	-	-	-	
Net Other Income	940	1,684	1,142	1,312	
PBT	20,967	23,311	25,132	28,224	
Forex adjustments	-	-	-	-	
Total Tax	5,257	5,917	6,333	7,113	
<b>PAT</b>	<b>15,702</b>	<b>17,385</b>	<b>18,787</b>	<b>21,100</b>	
Growth (%)	5.7	10.7	8.1	12.3	
EPS (₹)	57.9	64.1	69.2	77.8	
EPS (₹)	57.9	64.1	69.2	77.8	

Source: Company, ICICI Direct Research

Exhibit 3: Cash flow statement					₹ crore
Year-end March	FY24	FY25E	FY26E	FY27E	
PBT	20,967	23,311	25,132	28,224	
Depreciation & Amortisation	4,173	4,131	4,551	4,971	
(Inc)/dec in Current Assets	472	(2,077)	(3,208)	(3,466)	
Inc/(dec) in CL and Provisions	1,833	1,573	2,430	2,624	
Taxes paid	(4,212)	(5,917)	(6,333)	(7,113)	
<b>CF from Op. Activities</b>	<b>22,448</b>	<b>19,328</b>	<b>21,417</b>	<b>23,918</b>	
(Inc)/dec in Investments	(3,669)	1,684	1,142	1,312	
(Inc)/dec in Fixed Assets	(1,016)	(2,340)	(2,560)	(2,797)	
CF from Inv activities	(6,723)	(656)	(1,418)	(1,485)	
Issue/(Buy back) of Equity	-	-	-	-	
Inc/(dec) in loan funds	(181)	(500)	(500)	(500)	
Dividend paid & dividend tax	(14,073)	(13,908)	(15,029)	(16,880)	
Inc/(dec) in debentures	-	-	-	-	
Others	(1,212)	-	-	-	
<b>CF from Financing</b>	<b>(15,464)</b>	<b>(14,408)</b>	<b>(15,529)</b>	<b>(17,380)</b>	
Net Cash flow	261	4,264	4,470	5,053	
Exchange difference	130	-	-	-	
Opening Cash	9,065	9,456	13,720	18,190	
<b>Closing Cash</b>	<b>9,456</b>	<b>13,720</b>	<b>18,190</b>	<b>23,244</b>	

Source: Company, ICICI Direct Research

Exhibit 4: Balance Sheet					₹ crore
Year-end March	FY24	FY25E	FY26E	FY27E	
<b>Liabilities</b>					
Equity Capital	543	543	543	543	
Reserve and Surplus	67,720	71,197	74,954	79,174	
Total Shareholders funds	68,263	71,740	75,497	79,717	
Total Debt	2,223	1,723	1,223	723	
Other liabilities+Provisions	6,557	6,661	6,822	6,996	
Minority Interest / Others	8	8	8	8	
<b>Total Liabilities</b>	<b>77,051</b>	<b>80,132</b>	<b>83,550</b>	<b>87,444</b>	
<b>Assets</b>					
Net Block+ CWIP	7,909	7,151	6,297	5,365	
Intangible assets+ Goodwill	27,262	26,229	25,091	23,848	
Investments	94	94	94	94	
Liquid investments	7,043	7,043	7,043	7,043	
Inventory	185	197	215	235	
Debtors	19,483	20,742	22,687	24,788	
Loans and Advances	795	846	926	1,011	
Other Current Assets	11,675	12,429	13,595	14,854	
Cash & Bank	20,150	24,414	28,884	33,938	
Total Current Assets	59,331	65,672	73,350	81,870	
Total Current Liabilities	22,726	24,194	26,463	28,914	
Net Current Assets	36,605	41,477	46,887	52,956	
Other non current assets	5,181	5,181	5,181	5,181	
<b>Application of Funds</b>	<b>77,051</b>	<b>80,132</b>	<b>83,550</b>	<b>87,444</b>	

Source: Company, ICICI Direct Research

Exhibit 5: Key ratios				
Year-end March	FY24	FY25E	FY26E	FY27E
<b>Per share data (₹)</b>				
EPS	57.9	64.1	69.2	77.8
Cash EPS	73.2	79.3	86.0	96.1
BV	251.6	264.4	278.2	293.8
DPS	46.3	51.3	55.4	62.2
Cash Per Share	74.3	90.0	106.4	125.1
<b>Operating Ratios (%)</b>				
EBIT Margin	18.2	18.5	18.7	19.2
PBT Margin	19.1	19.9	19.6	20.2
PAT Margin	14.3	14.9	14.7	15.1
Debtor days	65	65	65	65
<b>Return Ratios (%)</b>				
RoE	23.0	24.2	24.9	26.5
RoCE	27.2	29.1	30.1	32.3
RoIC	40.2	44.4	50.4	57.9
<b>Valuation Ratios (x)</b>				
P/E	31.3	28.3	26.1	23.3
EV / EBITDA	19.3	17.9	16.0	14.1
EV / Net Sales	4.2	3.9	3.6	3.2
Market Cap / Sales	4.5	4.2	3.8	3.5
Price to Book Value	7.2	6.8	6.5	6.2
<b>Solvency Ratios</b>				
Debt/EBITDA	0.1	0.1	0.0	0.0
Debt/EBITDA	0.1	0.1	0.0	0.0
Current Ratio	1.4	1.4	1.4	1.4
Quick Ratio	1.4	1.4	1.4	1.4

Source: Company, ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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