

October 20, 2010

Shashi Bhusan
shashibhusan@plindia.com
+91-22-66322300

Rating	BUY
Price	Rs439
Target Price	Rs500
Implied Upside	13.9%
Sensex	19,983

(Prices as on October 20, 2010)
Trading data

Market Cap. (Rs bn)	294.4
Shares o/s (m)	670.3
3M Avg. Daily value (Rs m)	458.7

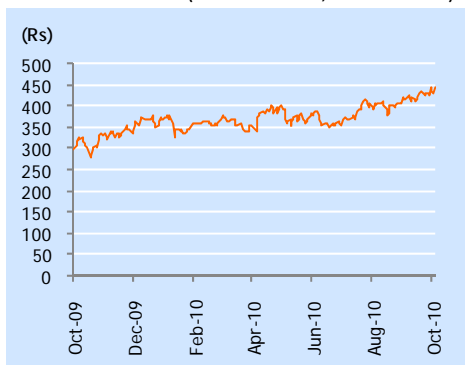
Major shareholders

Promoters	65.20%
Foreign	20.97%
Domestic Inst.	5.72%
Public & Other	8.11%

Stock Performance

(%)	1M	6M	12M
Absolute	4.8	25.9	45.6
Relative	2.8	1.3	10.5

Price Performance (RIC: HCLT.BO, BB: HCLT IN)



Source: Bloomberg

HCL Tech topped analyst estimates and reported revenue growth of 9.1% QoQ is US\$ terms for Q1FY11. We reiterate our “BUY” rating with a target price of Rs500.

- HCLT Q1FY11 results – Strong performance, beaten expectation:** HCLT revenue grew by 8.3% QoQ to Rs37.1bn for Q1FY11 (PLe Rs36.1bn, Cons: Rs35.6) in rupee term, whereas revenue in USD terms grew by 9.1% QoQ to \$804m. EBITDA margin eroded by 236bps QoQ to 16.3% due to currency and wage hike. The company reported EPS of Rs4.9, a de-growth of 1.6% QoQ due to Rs655m forex loss.
- Geography, Services and Verticals – Europe, Custom Application and Retail shines:** Revenue for AsiaPac and Europe grew by 20% and 18.4% QoQ respectively. In terms of services, custom application and IMS grew by 15.3% and 8.6% QoQ respectively. Retail and BFSI grew by 13.1% and 10.4% QoQ respectively ahead of its larger peer’s growth. All top 20 clients and non-top 20 clients contributed to the growth .
- Volume and pricing led the growth, attrition lowest among peers:** The pricing improved by 1.2% QoQ (onsite: 1.9%, offshore: 0.9%) whereas volume growth was 7.9% largely in-line with larger peers. The company added 8333 new employees for the quarters. They have added 48 new clients in Q1FY11.
- Valuation and Recommendation: Reiterate BUY, target price Rs500:** We may see stock giving an uptick movement on the back of strong result. We reiterate our “BUY” recommendation post Q1FY11 result with a target price of Rs500. We wait for the management commentary to get more input on demand pipeline

Key financials (Y/e June)	2009	2010	2011E	2012E
Revenues (Rs m)	106,301	125,650	150,480	181,826
Growth (%)	39.1	18.2	19.8	20.8
EBITDA (Rs m)	23,456	25,728	27,262	31,779
PAT (Rs m)	12,722	13,001	15,776	19,927
EPS (Rs)	19.0	19.4	23.5	29.7
Growth (%)	12.1	2.2	21.3	26.3
Net DPS (Rs)	10.7	4.7	6.1	6.1

Source: Company Data; PL Research

Profitability & Valuation	2009	2010	2011E	2012E
EBITDA margin (%)	22.1	20.5	18.1	17.5
RoE (%)	23.3	20.4	20.7	22.2
RoCE (%)	16.7	13.1	14.3	16.5
EV / sales (x)	3.0	2.5	2.0	1.6
EV / EBITDA (x)	13.6	12.3	11.3	9.3
PE (x)	23.1	22.6	18.7	14.8
P / BV (x)	5.2	4.2	3.6	3.0
Net dividend yield (%)	2.4	1.1	1.4	1.4

Source: Company Data; PL Research

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Growth ahead of expectation, margin erosion higher than expected (Rs m)

Y/e June	Q1FY11	Q4FY10	QoQ	Q1FY10	YoY	Cons(e)	PL(e)	Var VS PL (e)
Sales (\$ m)	804	737	9.1%	630.1	27.6%	NA	773.9	3.9%
Sales	37,081	34,254	8.3%	30,314	22.3%	35,621	36,100.1	2.7%
Operating Profit	6,033	6,381	-5.5%	6,888	-12.4%	6,129	6,173.1	-2.3%
<i>OPM</i>	<i>16.3%</i>	<i>18.6%</i>	<i>-236 bps</i>	<i>22.7%</i>	<i>-645 bps</i>	<i>17.2%</i>	<i>17.1%</i>	<i>-83 bps</i>
PBT	4,133	3,672	12.6%	3,903	5.9%	4,316	4,137.5	-0.1%
Tax	824	254	224.4%	702	17.4%	1,036	744.7	10.6%
<i>Tax Rate</i>	<i>19.9%</i>	<i>6.9%</i>	<i>1302 bps</i>	<i>18.0%</i>	<i>195 bps</i>	<i>24.0%</i>	<i>18.0%</i>	<i>194 bps</i>
PAT	3,365	3,418	-1.6%	3,200	5.2%	3,280	3,392.7	-0.8%
Forex Gain/Loss	(1348)	(1370)	-1.6%	(1,504)	-10.4%	NA	(500.0)	169.6%
PAT (excl forex adj. tax)	4,605	4,693	-1.9%	4,433	3.9%	NA	3,803	21.1%
EPS (Rs)	4.9	4.9	-1.6%	4.7	4.1%	4.8	4.95	-1.8%

Source: Company Data, Bloomberg, PL Research

Growth in Europe, a heartening sight

Geographic Split (\$ mn)	Q1FY11	Q4FY10	QoQ	Q1FY10	YoY
US	466.2	453.3	2.9%	369.9	26.0%
Europe	214.6	181.3	18.4%	182.7	17.4%
Asia Pacific	123.0	102.4	20.0%	77.5	58.7%
% Total					
US	58.0%	61.5%	-350 bps	58.7%	-70 bps
Europe	26.7%	24.6%	210 bps	29.0%	-230 bps
Asia Pacific	15.3%	13.9%	140 bps	12.3%	300 bps

Source: Company Data, PL Research

Custom Application and IMS – drive growth

Service Offering Split	Q1FY11	Q4FY10	QoQ	Q1FY10	YoY
Enterprise Application Services	174.4	163.6	6.6%	138.0	26.4%
Engineering and R&D Services	150.3	144.5	4.1%	117.8	27.6%
Custom Application (Industry Solutions)	251.6	218.2	15.3%	193.4	30.1%
Infrastructure Services	179.2	165.1	8.6%	122.2	46.6%
BPO Services	48.2	45.7	5.5%	58.6	-17.7%
% Total					
Enterprise Application Services	21.7%	22.2%	-50 bps	21.9%	-20 bps
Engineering and R&D Services	18.7%	19.6%	-90 bps	18.7%	0 bps
Custom Application (Industry Solutions)	31.3%	29.6%	170 bps	30.7%	60 bps
Infrastructure Services	22.3%	22.4%	-10 bps	19.4%	290 bps
BPO Services	6.0%	6.2%	-20 bps	9.3%	-330 bps

Source: Company Data, PL Research

Continue to drive towards FPP

Revenue by Contract Type	Q1FY11	Q4FY10	QoQ	Q1FY10	YoY
Time & Material	473.4	435.6	8.7%	378.1	25.2%
Fixed Price Projects	330.4	301.4	9.6%	252.0	31.1%
% of total Revenue					
Fixed Price Projects	41.1%	40.9%	20 bps	40.0%	110 bps
Time & Material	58.9%	59.1%	-20 bps	60.0%	-110 bps

Source: Company Data, PL Research

BFSI and Retail growth in-line with Infosys

Vertical Split	Q1FY11	Q4FY10	QoQ	Q1FY10	YoY
Financial Services	202.6	183.5	10.4%	165.7	22.2%
Hi-Tech - Manufacturing	218.6	201.2	8.7%	172.6	26.6%
Telecom	88.4	80.3	10.1%	81.9	7.9%
Retail	68.3	60.4	13.1%	44.1	54.9%
Media Publishing & Entertainment (MPE)	55.5	54.5	1.7%	42.8	29.4%
Life Sciences	67.5	60.4	11.7%	40.3	67.4%
Others	102.9	96.5	6.6%	82.5	24.6%
% of Total Revenue					
Financial Services	25.2%	24.9%	30 bps	26.3%	-110 bps
Hi-Tech - Manufacturing	27.2%	27.3%	-10 bps	27.4%	-20 bps
Telecom	11.0%	10.9%	10 bps	13.0%	-200 bps
Retail	8.5%	8.2%	30 bps	7.0%	150 bps
Media Publishing & Entertainment (MPE)	6.9%	7.4%	-50 bps	6.8%	10 bps
Life Sciences	8.4%	8.2%	20 bps	6.4%	200 bps
Others	12.8%	13.1%	-30 bps	13.1%	-30 bps

Source: Company Data, PL Research

Strong client addition across bucket

Number of million dollar clients LTM)	Q1FY11	Q4FY10	QoQ	Q1FY10	YoY
US\$ 100mn +	1	1	0.0%	1	0.0%
US\$ 50mn +	6	5	20.0%	4	50.0%
US\$ 40mn +	7	7	0.0%	7	0.0%
US\$ 30mn +	14	12	16.7%	9	55.6%
US\$ 20mn +	26	24	8.3%	20	30.0%
US\$ 10mn +	64	58	10.3%	45	42.2%
US\$ 5mn +	112	107	4.7%	94	19.1%
US\$ 1mn +	292	283	3.2%	264	10.6%

Source: Company Data, PL Research

**Growth across client segments**

Client Contribution to revenue (LTM)	Q1FY11	Q4FY10	QoQ	Q1FY10	YoY
Top 5 Clients	142.3	131.2	8.5%	119.7	18.8%
Top 10 Clients	208.2	191.6	8.6%	171.4	21.5%
Top 20 Clients	294.2	271.2	8.5%	240.1	22.5%
% of Total Revenue					
Top 5 Clients	17.7%	17.8%	-10 bps	19.0%	-130 bps
Top 10 Clients	25.9%	26.0%	-10 bps	27.2%	-130 bps
Top 20 Clients	36.6%	36.8%	-20 bps	38.1%	-150 bps
Number of Clients	426	408	4.4%	373	14.2%
New Client Relationship	48	51	-5.9%	28	71.4%
Accounting for > 5% of revenue	1	1	0.0%	1	0.0%

Source: Company Data, PL Research

Utilization - margin lever unutilized

Headcount	Q1FY11	Q4FY10	QoQ	Q1FY10	YoY
Utilization offshore (incl. trainees)	70.1%	72.9%	-280 bps	76.0%	-590 bps
Utilization offshore (excl. trainees)	74.1%	77.0%	-290 bps	77.9%	-380 bps
Utilization onsite	95.7%	95.2%	50 bps	97.2%	-150 bps
Efforts billed					
Efforts billed offshore	66396	61518	7.9%	51,167	29.8%
Efforts billed onsite	25609	23777	7.7%	19,950	28.4%
Total Billed Effort	92,005	85,295	7.9%	71,117	29.4%
Attrition LTM - IT Services					
Attrition LTM - IT Services	16.7%	15.7%	100 bps	12.8%	390 bps
Gross Addition					
Gross Addition	8333	8293	0.5%	2,612	219.0%
Net Addition					
Net Addition	5327	5409	-1.5%	665	701.1%
Gross Laterals Addition					
Gross Laterals Addition	5598	6854	-18.3%	1,671	235.0%

Source: Company Data, PL Research

IT Services - Marching ahead

Revenue	Q1FY11	Q4FY10	QoQ	Q1FY10	YoY
Offshore	315.1	286.5	10.0%	237.1	32.9%
Onsite	440.6	405.6	8.6%	334.2	31.8%
IT Services Revenue	755.7	692.1	9.2%	571.3	32.3%
% of total Revenue					
Offshore	41.7%	41.4%	30 bps	41.5%	20 bps
Onsite	58.3%	58.6%	-30 bps	58.5%	-20 bps

Source: Company Data, PL Research

**Billing rate witnessed uptick**

Billing Rate	Q1FY11	Q4FY10	QoQ	Q1FY10	YoY
Offshore	4,746	4,658	1.9%	4,634	2.4%
Onshore	17,204	17,057	0.9%	16,752	2.7%
Total	8,214	8,114	1.2%	8,033	2.2%

Source: Company Data, PL Research


Income Statement (Rs m)

Y/e June	2009	2010	2011E	2012E
Net Revenue	106,301	125,650	150,480	181,826
Raw Material Expenses	65,483	81,957	101,546	124,063
Gross Profit	40,818	43,693	48,934	57,762
Employee Cost	—	—	—	—
Other Expenses	17,362	17,965	21,672	25,983
EBITDA	23,456	25,728	27,262	31,779
Depr. & Amortization	4,493	5,009	6,882	7,949
Net Interest	—	—	—	—
Other Income	(3,671)	(5,302)	(155)	2,050
Profit before Tax	15,292	15,417	20,225	25,880
Total Tax	2,543	2,404	4,450	5,952
Profit after Tax	12,749	13,013	15,776	19,927
Ex-Od items / Min. Int.	27	12	—	—
Adj. PAT	12,722	13,001	15,776	19,927
Avg. Shares O/S (m)	670.3	670.3	670.3	670.3
EPS (Rs.)	19.0	19.4	23.5	29.7

Cash Flow Abstract (Rs m)

Y/e June	2009	2010	2011E	2012E
C/F from Operations	9,950	17,806	20,100	26,210
C/F from Investing	(33,898)	(11,824)	(7,524)	(8,728)
C/F from Financing	24,311	(5,499)	(4,076)	(10,076)
Inc. / Dec. in Cash	363	483	8,501	7,406
Opening Cash	3,840	4,203	4,686	13,187
Closing Cash	4,203	4,686	13,187	20,593
FCFF	21,333	7,540	18,873	24,755
FCFE	50,829	4,401	18,873	18,755

Key Financial Metrics

Y/e June	2009	2010	2011E	2012E
Growth				
Revenue (%)	39.1	18.2	19.8	20.8
EBITDA (%)	38.5	9.7	6.0	16.6
PAT (%)	12.8	2.2	21.3	26.3
EPS (%)	12.1	2.2	21.3	26.3
Profitability				
EBITDA Margin (%)	22.1	20.5	18.1	17.5
PAT Margin (%)	12.0	10.3	10.5	11.0
RoCE (%)	16.7	13.1	14.3	16.5
RoE (%)	23.3	20.4	20.7	22.2
Balance Sheet				
Net Debt : Equity	0.4	0.3	0.2	—
Net Wrkng Cap. (days)	—	—	—	—
Valuation				
PER (x)	23.1	22.6	18.7	14.8
P / B (x)	5.2	4.2	3.6	3.0
EV / EBITDA (x)	13.6	12.3	11.3	9.3
EV / Sales (x)	3.0	2.5	2.0	1.6
Earnings Quality				
Eff. Tax Rate	16.6	15.6	22.0	23.0
Other Inc / PBT	(24.0)	(34.4)	(0.8)	7.9
Eff. Depr. Rate (%)	28.3	27.1	34.9	37.6
FCFE / PAT	399.5	33.9	119.6	94.1

Source: Company Data, PL Research.

Balance Sheet Abstract (Rs m)

Y/e June	2009	2010	2011E	2012E
Shareholders Funds	56,846	70,352	81,775	97,626
Total Debt	29,771	26,632	26,632	20,632
Other Liabilities	7,650	7,402	7,402	7,402
Total Liabilities	94,267	104,386	115,809	125,660
Net Fixed Assets	15,862	18,486	19,713	21,168
Goodwill	45,325	43,122	42,260	41,583
Investments	370	707	707	707
Net Current Assets	24,102	32,431	43,489	52,562
<i>Cash & Equivalents</i>	<i>4,203</i>	<i>4,686</i>	<i>13,187</i>	<i>20,593</i>
<i>Other Current Assets</i>	<i>52,574</i>	<i>59,074</i>	<i>75,446</i>	<i>84,275</i>
<i>Current Liabilities</i>	<i>32,675</i>	<i>31,329</i>	<i>45,144</i>	<i>52,306</i>
Other Assets	8,608	9,640	9,640	9,640
Total Assets	94,267	104,386	115,809	125,660

Quarterly Financials (Rs m)

Y/e June	Q2FY10	Q3FY10	Q4FY10	Q1FY11
Net Revenue	30,325	30,757	34,254	37,081
EBITDA	6,386	6,073	6,381	6,034
<i>% of revenue</i>	<i>21.1</i>	<i>19.7</i>	<i>18.6</i>	<i>16.3</i>
Depr. & Amortization	974	928	1,011	1,064
Net Interest	—	—	—	—
Other Income	(1,390)	(767)	(1,578)	(650)
Profit before Tax	3,635	4,207	3,672	4,135
Total Tax	679	769	254	824
Profit after Tax	2,968	3,439	3,418	3,311
Adj. PAT	2,968	3,439	3,418	3,311

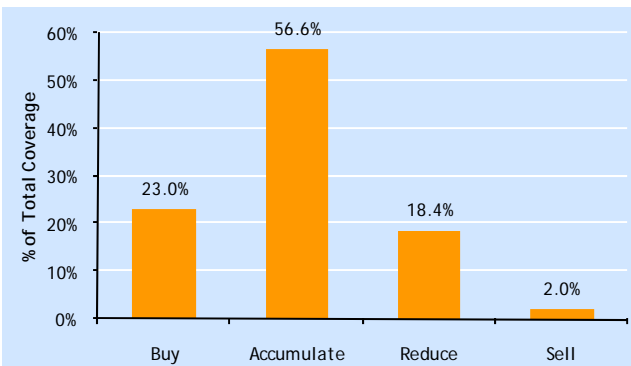
Source: Company Data, PL Research.

Prabhudas Lilladher Pvt. Ltd.

3rd Floor, Sadhana House, 570, P. B. Marg, Worli, Mumbai-400 018, India

Tel: (91 22) 6632 2222 Fax: (91 22) 6632 2209

Rating Distribution of Research Coverage



PL's Recommendation Nomenclature

BUY	: Over 15% Outperformance to Sensex over 12-months	Accumulate	: Outperformance to Sensex over 12-months
Reduce	: Underperformance to Sensex over 12-months	Sell	: Over 15% underperformance to Sensex over 12-months
Trading Buy	: Over 10% absolute upside in 1-month	Trading Sell	: Over 10% absolute decline in 1-month
Not Rated (NR)	: No specific call on the stock	Under Review (UR)	: Rating likely to change shortly

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