

## UPDATE

### LARGE CAP

#### Share Data

Reuters code	HCLT.BO
Bloomberg code	HCLT IN
Market cap. (US\$ mn)	4,967
6M avg. daily turnover (US\$ mn)	9.9
Issued shares (mn)	673
Target price (Rs)	400

#### Performance (%) 1M 3M 12M

Absolute	3	7	180
Relative	4	6	65

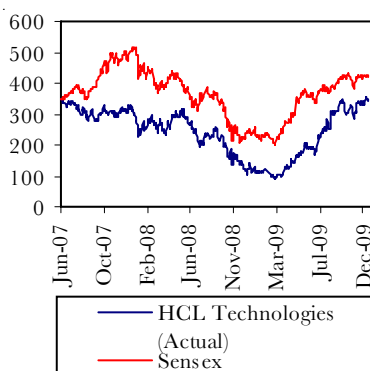
#### Valuation Ratios

Yr to 30 Jun	FY10E	FY11E
EPS (Rs)	17.1	26.1
+/- (%)	(4.9)	53.1
PER (x)	20.2	13.2
PBV (x)	3.5	3.0
Dividend/Yield (%)	1.2	1.7
EV/Sales (x)	2.0	1.7
EV/EBITDA (x)	9.5	8.4

#### Major shareholders (%)

Promoters	69
FII's	19
MF's	2
BFSI's	3
Public & Others	8

#### Relative performance



## HCL Technologies

Maintain Outperformer

Price: Rs 344

BSE Index: 16,913

17 December 2009

**“Increasing number of large deal wins adding to revenue visibility”**

In the last few months, HCL Technologies (HCLT) has had a huge success in multiple large deal wins. Its acquired company, Axon, which specialises in SAP consulting and implementation, did not perform up to expectations in FY09; but things seem to be improving at Axon now, with new deals in SAP coming HCLT’s way. Two recent deal wins of GSK Pharma and Sahara Oil Company, involve a large component of SAP implementation and consulting and are a testimony to HCLT’s increasing traction in SAP. The recent deal wins in pharma, utilities, media publishing will also help HCLT to diversify away from the otherwise traditional, BFSI market. HCLT has also been witnessing good traction in its Infrastructure services space, which grew by 15% in 1QFY10 and 19% in the previous quarter. Also, the management is looking at increasing share in the Oracle space. Thus, we believe HCL Tech’s Blue Ocean strategy is paying off well in diversifying into newer sub verticals and newer practices. Appended on page 2 is the list of recent deal wins and strategic alliances of HCLT.

With improving revenue visibility from increasing number of deal wins, we increase our earnings estimates for HCLT. We are revising our revenue growth assumptions and expect HCLT to clock revenue growth of 13% in USD in FY11. Earlier, we expected incremental revenue of ~US\$ 288 mn to flow in FY11, but we now expect an incremental revenue flow of ~US\$ 350 mn, majorly due to ramp-up in the large deals. Our revenue for FY11 at US\$ 2.9 bn, implies a CQGR of 3.2% in FY11. Also, HCL Tech is adopting aggressive cost rationalisation measures to counter margin challenges and we expect margins in FY11 to be in the broad range of 20.3%, 50 bps decline from FY10. Thus, our earnings get revised upwards by 6% for FY11 and now expect an EPS of Rs 26.1 versus our earlier estimate of Rs 24.6.

At our revised earnings, HCLT is trading at 13x FY11, which is at a huge discount to most of its other large cap peers; Infosys is trading at 22x our FY11 earnings estimates, implying HCLT’s valuation discount of ~40%. We believe such a huge discount is not warranted, given improving revenue visibility at HCL Tech. We have given a target multiple discount of 30% to HCLT versus Infosys and revise our target price of HCLT to Rs 400. We maintain Outperformer on HCL Tech and it is one of our preferred picks in the large cap space. Risks remain execution slippages around large deals and a weaker Balance sheet with goodwill and intangibles at ~35% of balance sheet size and DSO at 90 days as of September 2009 quarter.

## Recent deal wins and strategic alliances of HCLT

Date	Deal	Details	Deal size	No. of Years
16 Dec 09	GlaxoSmithKline	HCLT secured a 5 year deal from GlaxoSmithKline for system integration, SAP implementation and IT consulting services. The size of the deal has not been disclosed but we believe the deal to be a multi million dollar deal spread over five years.	Not disclosed, but expect it to be sizeable	5
08 Dec 09	News International	HCL Tech secured a 5-year deal from News International worth multi million pounds for infrastructure management and transformation engagement. HCLT will manage News International's datacenters and network environments along with strategically transforming them.	Not disclosed, multi million pounds	5
03 Dec 09	Sahara Petroleum Services Company	HCL Tech has entered into a SAP implementation engagement with Sahara Petroleum Services Company (SAPESCO)	Not disclosed	
24 Nov 09	Savvion partnership	HCLT has formed a strategic partnership with Savvion to extend its service focus in the Business Process Management (BPM) for financial services, media and publishing, entertainment, government and retail verticals.	Strategic partnership	
23 Nov 09	Equitable Life	The contract will start in March 2011 and will deliver substantial cost benefits to Equitable Life's policy holders through the transfer of core processing and support activities required to run its closed book of business. HCLT will be providing an end to end solution including policy administration, finance, actuarial services, IT operational support and call center services.	US\$ 200 mn	
18 Nov 09	Ubiquiti	HCL Technologies and Ubiquiti have formed a partnership to provide automated warranty solutions to automotive manufacturers. Ubiquiti will leverage HCLT's comprehensive Warranty Decision Support solution to help manufacturers automate the numerous analysis, alerting, data mining and reporting processes associated with warranty and repair data.	Strategic partnership	
04 Nov 09	iLumen	The alliance will help banks to improve data security and relationship management with reduced costs.	Strategic partnership	
17 Sep 09	Energy Future Holdings (EFH)	HCLT will manage EFH's IT Infrastructure landscape comprising data centre, voice and data networks and end-user computing services.	US\$ 80 mn	5
17 Sep 09	Oncor signs five year IT Infrastructure Management	HCL Tech has entered into a five year Transformational IT Infrastructure Management engagement with Oncor to connect and support Oncor's corporate functions, grid management operations and numerous community-based field service centers located throughout Oncor's service area.	US\$ 33 mn	5
1 Sep 09	Fortis Healthcare	Outsourced operations to manage 250 ambulances through GPRS and Wireless connectivity	Not disclosed	3
26 Aug 09	Optimotion	HCL Tech with this partnership will provide various practices such as SAP, Oracle and services such as business transformation, RIM, BPO, ADM, testing and so on. This partnership will enable HCL Tech to provide IT services to New Zealand Government and enterprise customers coupled with Optimotions' local expertise	Strategic partnership	–

## Income Statement

Yr end 30 Jun (Rs mn)	FY08	FY09	FY10E	FY11E
<b>Net sales</b>	<b>75,999</b>	<b>106,083</b>	<b>123,437</b>	<b>141,879</b>
<i>Growth (%)</i>	26.0	39.6	16.4	14.9
Operating expenses	(60,341)	(83,613)	(97,823)	(113,048)
Operating profit	15,658	22,470	25,615	28,831
<b>EBITDA</b>	<b>15,658</b>	<b>22,470</b>	<b>25,615</b>	<b>28,831</b>
<i>Growth (%)</i>	26.2	43.5	14.0	12.6
Depreciation	(3,001)	(4,494)	(5,330)	(5,508)
Other income	(974)	(3,457)	(6,142)	(1,487)
<b>EBIT</b>	<b>11,683</b>	<b>14,519</b>	<b>14,142</b>	<b>21,836</b>
Pre-tax profit (before non-recurring)	11,683	14,519	14,142	21,836
Pre-tax profit (after non-recurring)	11,683	14,519	14,142	21,836
Tax (current + deferred)	(1,272)	(2,543)	(2,699)	(4,321)
Net profit (before Minority Interest, Pref. Dividend, etc.)	10,411	11,976	11,444	17,515
Minority interests	(18)	34	(4)	(4)
Reported PAT	10,393	12,010	11,440	17,511
<b>Adjusted net profit</b>	<b>10,393</b>	<b>12,010</b>	<b>11,440</b>	<b>17,511</b>
<i>Growth (%)</i>	(17.4)	15.6	(4.7)	53.1

## Balance Sheet

Yr end 30 Jun (Rs mn)	FY08	FY09	FY10E	FY11E
Cash & marketable sec.	24,540	18,994	20,939	25,448
Other current assets	27,616	37,782	49,979	64,533
Investments	221	369	369	369
Net fixed assets	22,905	61,186	61,797	62,253
Other non-current assets	5,064	8,608	15,495	24,792
<b>Total assets</b>	<b>80,346</b>	<b>126,939</b>	<b>148,579</b>	<b>177,395</b>
Current liabilities	21,874	32,675	45,813	60,095
Total debt	447	30,012	28,989	28,989
Other non-current liabilities	5,785	7,393	8,610	10,332
<b>Total liabilities</b>	<b>28,107</b>	<b>70,080</b>	<b>83,411</b>	<b>99,416</b>
Share capital	1,427	1,597	1,597	1,597
Reserves & surplus	50,755	55,246	63,550	76,358
<b>Shareholders' funds</b>	<b>52,183</b>	<b>56,843</b>	<b>65,147</b>	<b>77,955</b>
Minorities interests	57	16	20	24
<b>Total equity &amp; liabilities</b>	<b>80,346</b>	<b>126,939</b>	<b>148,579</b>	<b>177,395</b>
<b>Capital employed</b>	<b>58,471</b>	<b>94,264</b>	<b>102,766</b>	<b>117,300</b>

## Cash Flow Statement

Yr end 30 Jun (Rs mn)	FY08	FY09	FY10E	FY11E
Pre-tax profit	11,683	14,519	14,142	21,836
Depreciation	3,001	3,567	4,093	4,755
Change in working capital	4,430	(1,302)	(4,729)	(7,847)
Total tax paid	(1,272)	(2,543)	(2,699)	(4,321)
<b>Cash flow from oper. (a)</b>	<b>17,842</b>	<b>14,241</b>	<b>10,808</b>	<b>14,423</b>
Capital expenditure	(7,597)	(42,527)	(4,704)	(5,211)
Change in investments	(720)	4,946	0	0
Others	247	678	0	0
<b>Cash flow from inv. (b)</b>	<b>(8,069)</b>	<b>(36,902)</b>	<b>(4,704)</b>	<b>(5,211)</b>
<b>Free cash flow (a+b)</b>	<b>9,772</b>	<b>(22,661)</b>	<b>6,104</b>	<b>9,212</b>
Equity raised/(repaid)	2,630	3,816	0	0
Debt raised/(repaid)	(237)	29,565	(1,024)	0
Dividend (incl. tax)	(5,976)	(5,479)	(3,135)	(4,703)
Others	(6,406)	(7,352)	0	0
<b>Cash flow from fin. (c)</b>	<b>(9,990)</b>	<b>20,550</b>	<b>(4,159)</b>	<b>(4,703)</b>
<b>Net change in cash (a+b+c)</b>	<b>(217)</b>	<b>(2,111)</b>	<b>1,945</b>	<b>4,509</b>

## Key Ratios

Yr end 30 Jun (%)	FY08	FY09	FY10E	FY11E
Adjusted EPS (Rs)	15.6	18.0	17.1	26.1
Growth	(17.5)	14.8	(4.9)	53.1
Book NAV/share (Rs)	78.6	85.0	97.3	116.4
Dividend/share (Rs)	9.0	7.0	4.0	6.0
Dividend payout ratio	57.5	45.6	27.4	26.9
Tax	10.9	17.5	19.1	19.8
EBITDA margin	20.6	21.2	20.8	20.3
EBIT margin	15.4	13.7	11.5	15.4
RoCE	21.2	19.0	14.4	19.8
Net debt/Equity	(46.1)	19.4	12.4	4.5

## Valuations

Yr end 30 Jun (x)	FY08	FY09	FY10E	FY11E
PER	22.0	19.2	20.2	13.2
PCE	17.1	14.0	13.8	10.0
Price/Book	4.4	4.1	3.5	3.0
Yield (%)	2.6	2.0	1.2	1.7
EV/Net sales	3.2	2.3	2.0	1.7
EV/EBITDA	15.5	10.8	9.5	8.4

## Du Pont Analysis – ROE

Yr end 30 Jun (x)	FY08	FY09	FY10E	FY11E
Net margin (%)	13.7	11.3	9.3	12.3
Asset turnover	1.1	1.0	0.9	0.9
Leverage factor	1.4	1.9	2.3	2.3
Return on equity (%)	20.3	22.0	18.7	24.5

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**Analyst Declaration:** We, Shradha Agrawal & Ritesh Khanna, hereby certify that the views expressed in this report accurately reflect our personal views about the subject securities and issuers. We also certify that no part of our compensation was, is, or will be, directly or indirectly, related to the specific recommendation or view expressed in this report.

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1. **BUY:** Potential upside of > +25% (absolute returns)
  2. **OUTPERFORMER:** 0 to +25%
  3. **UNDERPERFORMER:** 0 to -25%
  4. **SELL:** Potential downside of < -25% (absolute returns)
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