HCL Technologies Ltd.

SAMCO THE WEALTHY HABIT

New opportunities emerging due to COVID-19 along with strong execution capabilities and impressive valuations make HCL Technologies a compelling investment

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Recommendation : **Buy on dips**

Date : 07th Jan 2021
Current Price Range : Rs 970-1000
Outlook : **Long term Strong Upside**
Investment Period : 5 years

Long term

Positives

Value Accretive for Minority Shareholders: A healthy 5-year average ROE of 25% and an average dividend payout ratio of 25% make this Company extremely attractive from a shareholder's perspective. Additionally, it continues to be undervalued among peers with a PE of 21x against industry PE of 32.7x, despite strong returns. Therefore, the stock price is expected to catch-up with earnings going forward.

Deal Levers to Drive Momentum: HCL Tech won 15 transformational deals in Q2FY21 and showed excellent 20% QoQ growth in terms of deal wins which has accelerated growth momentum for the company. Infact, its order pipeline has seen a significant rise on a QoQ basis as technology takes priority for companies globally. Q1FY21 also showed a 40% jump in order wins and HCL Tech with its sound capabilities is expected to seize more opportunities while garnering a strong topline.

Strong Business Tailwinds: Mode 2 digital and mode 3 product business segments currently contribute to 36.7% of revenue. With exposure to new age technologies, these segments outperformed during the pandemic which led to EBIT margins of 18.5% and 28.7% respectively in Q2FY21. In order to improve the service mix, the company is focusing on additional investments through various acquisitions in these segments. This provides HCL Tech an edge among IT players amidst a wave of digital adoption.

Strategic Collaborations: With over a 100 collaborations with companies including a broad alliance with Google Cloud to strengthen its go-to-market strategy and an acquisition of Australia-based DWS Ltd to capture business in Australia and NZ, will help the Company acquire niche capabilities across verticals which will further fuel growth.

Qualities of a Multibagger: HCL Tech has a track record of excellence with a CAGR growth of 21% in sales in the past 10 years, PAT CAGR of 25%, Stock price CAGR of 23% and average OPMs of over 20% in the same period. In the technology pack, this is a gem of a stock for long term investors to compound wealth.

Risks

Margin Pressures: While impressive, HCL Tech's operating margins continue to lag the tech biggies such as Infosys and TCS which are in the range of 27-30%. Moreover, HCL Tech's attrition rate is still higher compared to its peers. Also, any issues in integration through acquisitions during implementation/ scale up could lead to further deterioration of these metrics.

Employee Cost Pressure: 33% of HCL Tech's employees in the US are visa dependent. New regulations entail a substantial increase in wages as visas come in for renewal which could have an impact on employee costs going ahead. Some impact of this is expected to be seen in FY21 to some extent.

Risk from USD depreciation: HCL Tech has benefitted from dollar's appreciation as majority of its revenue (63%) is from the US. With the expectation of the dollar to continue its downward journey vis-à-vis other emerging currencies, this company is expected to be on a back foot.

Quick Stock Analysis