"HCL Technologies Limited Q4FY'21 Earnings Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to the Q4 FY'21 Earnings Conference Call of HCL Technologies Limited. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Sanjay Mendiratta, Head, Investor Relations. Thank you and over to you sir.

Sanjay Mendiratta: Thank you. Good morning and good evening, everyone. Apologies for the delayed start. And a very warm welcome to HCL Technologies Q4 and Annual Fiscal '21 Earnings Call. Trust you all are safe and healthy.

We have with us today Mr. C. Vijayakumar -- President and CEO, HCL Technologies; Mr. Prateek Aggarwal -- Chief Financial Officer; Mr. Apparao -- Chief Human Resources Officer along with the broader leadership team to discuss the performance of the company during the quarter and the annuals too followed by the Q&A.

In the course of this call, certain statements that will be made are forward-looking, which involve a number of risks, uncertainties, assumptions and other factors that could cause actual results to differ materially from those in such forward-looking statements. All forward-looking statements made herein are based on information presently available to the management, and the company does not undertake to update any forward-looking statements that may be made in the course of this call. In this regard, please do review the Safe Harbor statement in the formal "Investor Release" document and all the factors that can cause the difference. Over to you, CVK. Thank you.

C. Vijayakumar: Yeah. thank you, Sanjay. Good morning and good evening to everyone. Apologies for the delayed start. Thank you for joining us today. I hope all of you are doing well. Hope you are safe and good health. At HCL, we continue to strengthen our business continuity program. It's already in high gear across the country and we are extending every possible healthcare and well-being support to all our employees and their families.

With that, let me get started with the overall performance for the quarter and for the financial year. As you would have seen, our revenues grew 2.5% constant currency in Q4, and if you look at the full year, revenue grew 1.1% in constant currency, delivering $10.175 billion which is a 2.4% year-on-year growth. Our EBIT margin was down by 8.3% sequentially. It came in at 20.4% which is a 2.5% points below the previous quarter margin. And similarly, the net income reduced by 24.1% sequentially. There is a detail walk for the EBIT and net income which Prateek will walk you through in the subsequent slides. Our overall EBIT performance year-on-year was 11.7% growth. Year-on-year net income growth is 13.2%. We delivered one of our highest EBIT performance which is 21.4%, which is ~180 basis points increase from the previous year. Of course, all of this exclude the one-time milestone bonus paid in Q4, amounting to about $100 million.

Just moving on, just to provide you an overview of the business performance. As you saw, we had positive revenue growth, double-digit EBIT and net income growth in FY'21 in spite of COVID-related headwinds in the first quarter, some of that continued in the second quarter.

Our Mode-3 which is the digitization-led revenue all the new services as well as our products and platform Mode-3 revenue grew in double digits, Mode-2 in high teens and Mode-3 in low teens growth.

Our growth was very well balanced across verticals in all the geographies. What is very notable is there is very strong and diversified growth in the services business. And the strong pickup in Q4 in the IT and Business Services is led by our great success in digital transformation deals, which is application modernization, vertical-led operating model transformation deals, analytics, cloud migration, cyber security and digital workplace deals.

Our application services, which also includes a lot of application modernization work delivered one of its highest quarter-on-quarter growths in this quarter.

Our engineering services continues to deliver decent growth YoY as well, some of it is impacted due to the COVID impact in some of the segments in which we are present, like auto and aero segments.

Products and platform continues to exceed expectations and is performing well above the business case. There is a certain segment of products, which we see strong potential and healthy pipeline. And we are going to continue to invest in those products to ensure the medium to long term growth is assured. We've had good deal closures in the products and platforms business. The pipeline creation through the HCL channel is also strong, almost 20% of the pipeline of the total business is coming through the HCL services channel.

We're also very happy to announce that we had the highest client satisfaction Index, which was done through a third-party firm, which we do every year, this is the 11th year running, and Net Promoter Score came on top of the previous high that we achieved in FY'20.

This gives you the year-on-year performance and the quarter-on-quarter performance in constant currency. As you can see, IT and Business Services delivered 4.4% growth. Of course, there is about 25 million of revenue, which is from the acquisition of DWS in Australia, which is also embedded in that, but even excluding that very smart growth.

From our engineering services perspective, we had a modest growth of 0.7%. But again, we see good traction and the subsequent quarters the outlook remains very positive.

And products and platform, quarter-on-quarter is not so relevant in this business, but year-on-year perspective delivered a 20.5% growth.

And engineering services declined 5% year-on-year, largely due to the asset-heavy industries that we have and we do believe the growth in that segment has already bottomed out and we should see good uptick moving forward.

In terms of the overall business, we had a record net new booking of $3.1 billion in Q4 and total booking in FY'21 of $7.3 billion. This is all net new booking. This does not include renewals or rate card deals that we have signed, which was also very significant in the quarter and through the year. The $3.1 billion booking in Q4 was led by 19 large deals. And what's very heartening is these deals are across the segments, like we had eight deals in manufacturing, four in financial services, three large deals in life sciences and healthcare, two in consumer goods and two in tech. And it is also quite well spread between Americas and Europe; 13 in Americas and six in Europe.

Also, it's worthwhile to highlight most of these deals are with Fortune 500 or global 500 companies, where there is significant headroom for growth, paving the way for a very strong, long-term growing relationships. Our strategy during the mid of the last financial year, given that the demand environment had really become very strong, we consciously participated selectively in deals that aligns with the long-term value creation and the results are absolutely very, very heartening that we had a well-diversified, very high quality clients. Of course, a lot of digital spend. And this is going to be a good outcome in the long run and we're very happy to note that.

Several deals won. One large deal, probably the larger this quarter was a Europe-based global energy and utility company which is carving out of its parent. We are setting up a Greenfield digital foundation and establishing an independent IT organization and support to enable their continued business transformation.

One of the largest deals that we signed in our engineering and R&D segment was from a global technology company, where we had chosen as a strategic product engineering partner to drive innovation that would steer growth of these products and customer advocacy for their clients.

In Germany, we signed with one of the world's leading consumer goods company for the workplace as a service across all clients service support levels across the global locations and environments. Here, consumer experience enabled through automation and AI was a significant theme.

Similarly, in the US, financial services firm, we signed an integrated engagement encompassing application management, application development, and the digital foundation and cloud migration, primarily to transform the clients wealth management business on the application landscape.

A US-based telecom company again expanded its relationship with a digital transformation being the areas of water management, client experience, secure payments, etc., which is again modernizing applications and migrating more and more workloads to cloud.

We also recently announced a deal with UD Trucks, which is a Japanese automotive manufacturing company. This is again a carve-out. We're into an IT transformation, spanning digital foundation, application development, modernization and digital workplace services.

So this is just a small set of deals among the 19-deals that we signed. We have a very detailed list of all the deals in the “Investor Release”, almost 17 of the 19-deals are highlighted there.

Looking ahead, based on the record booking and the broad-based pipeline, the pipeline as they exist of FY'21 is the highest. So even though we had very high booking, a lot of it is what replenished with a qualified pipeline, which is slightly higher than what it was at the end of the previous quarter. This augurs very well for the growth in the near-term. And a lot of it is driven by our mode-2 services. We do believe our mode-2 service revenue and mode-1 service revenue should be equal in the medium-term. That's the aspirational goal that we are working towards. And for this purpose, we will continue to invest in expanding and investments and solutioning and engineering capabilities in our Mode-2 services, especially there are several new areas in the digital engineering space, which is 5G industry 4.0 data engineering and softwarization and several high growth verticals which offer a lot of opportunities for our engineering services. In the current market environment, semiconductor, software, automotive are some of the areas where we want to expand.

We also launched what we call as “HCL Cloud Smart” to address the $300 billion services opportunity related to cloud. Here, while we have very strong ecosystem partnerships and dedicated business units, Cloud Smart is overarching offering, helping accelerating and maximizing business value from cloud in alignment with the industry needs and the specific organizational goals and unique client situations. We want to take advantage of the massive opportunity that is playing out in the cloud space. And this offering really brings together our IP services, our engineering services, our hyper scalar partnerships, and the industry IP that we have in several segments, as well as some of the offerings from our products and platforms segment.

We're also launching “HCL Now”, which is really the SaaS version of all the products that we have on the HCL software side. And this is again a very exciting launch and we are seeing a lot of interest in our customers to adopt the cloud version of some of the products that we have SaaSified in the recent past.

All of this is helping us strengthen our partnerships with hyper scalers because they're looking for industry solutions to be coming in from the partners like us. And our investments here are very well aligned with what we want to accomplish.

In terms of geographies, we believe there are additional geographies where we are seeing growing demand and a significant adoption of the global delivery model. While we have made investments, we have a country model which is strongly present in these geographies, we think this is the time to double down on some of the sales and marketing investments in geographies like Germany, France, Canada, Australia, and Japan. While we are seeing very good traction, we think the market opportunity is much bigger. So we are going to invest more in these adjacent countries where we want to build our business.

We're also looking at expanding into some emerging markets to address some of the IT demands in countries like Brazil, Mexico, South Korea and Spain. Some of these countries already have a country manager appointed and we plan to expand our teams in these locations. We are also increasing investments from a geographic leadership and sales teams in some of these geographies.

On the products and platforms, the business stands validated by better-than-expected performance in FY'21. As I said, we are well ahead of our business case as an overall portfolio of all the investments that we make and we see further opportunities to grow this business.

There are two segments that are clearly emerging. There is a segment which has got strong growth potential. About 75% of our products and platforms business has got a very strong growth characteristics and that is where we are investing which should help us deliver double-digit growth in the 75% of the products portfolio in the medium-term. The remaining 25% is more of a sustained portfolio, where we want to sustain these products, optimize profitability, while it would decline in a double-digit manner in the medium-to-long term, while there could be a little more decline in this 25% in the current year, which is FY'22 because there are a couple of products which we have consciously taken a decision to discontinue.

We see a demand for talent is very strong. And the adoption of remote work requires a complete rethinking or I would say a zero-based approach to talent access and delivery models. We put several special programs in place to enable hiring, grooming talent, etc., and also led by increased offshoring for which we are not only depending on India, we are looking at additional locations with Sri Lanka, Vietnam, Philippines, where we believe we will significantly scale up in this year and in the next three years. We are continuing to expand on some of the local near shore centers in US, Continental Europe and Australia. These are small nodal centers which will help create the right mindshare for us and attract local talent. We already have strong presence in US and Continental Europe, but there are a few more locations where we propose to invest.

We plan to hire over 15,000 entry level hires during the year. And this is spread across India, US, Europe, Australia, Sri Lanka and Vietnam.

In terms of “Outlook”, while we had very strong booking, and we are exiting with a reasonably good exit momentum, we expect to grow in double digits in constant currency, and our operating margins we expect it to be from 19% to 21%. The reason why we provided a double-digit growth, rather than giving a range, you should look at this as a floor for our growth. A lot of bookings that we have done, there is certain amount of execution that needs to happen, which needs to be planned out. And we want to focus a little more on booking and the metrics around booking, and we will provide you continuous visibility of booking, we are very comfortable with a net new booking TCV to be announced in the coming quarters, we will fine tune it to make it more complete, including renewals, and even some amount of rate card deals. So that's where we want the organization to focus. And we want to provide a floor of what the growth expectations will be.

And from a margin perspective, as you would have noticed, we used to give a range of 1%, now we've given a range of 2%. When we did the planning, we did assume some amount of travel and transport spend would come back. While that is big thing, but given the current scenario, maybe that may not happen. However, we want to give ourselves a little bit of elbow room for all the investments that I talked about. Because this is not the time to maximize profits, I think the market opportunity is very strong, and we want to do everything possible to capture the market opportunity, and that is the rationale for a 2% guidance range.

With that, I would request "Prateek to provide a little more Financial Details."

Prateek Aggarwal: Thank you, CVK. So, let me walk you through the slides. So I'll just go through the numbers. So the EBITDA we clocked during the quarter was $603 million, which is 22.4%. As you can see, it is a reduction on a quarter-to-quarter basis, which I will walk you through the details. And by the way, these are numbers, which are the published numbers on the next page, just as a quick glance, are the numbers adjusted without the impact of milestone bonus. Let me go ahead with this one instead of the previous one because this is more relevant to my mind. This milestone bonus was a one-time bonus we paid to the employees 10-days of salary to commemorate achievement of the 10 billion milestone. So without that, EBITDA is at $703 million which is 26.1%, which is still a drop of 215 basis points on a quarter-to-quarter basis and I will give you the walk for that. On a net income basis, we came in at $410 million, which is EPS of Rs.47.9. On an annual basis, we did $10.175 billion and EBITDA of 26.7 and net income of 1.76 billion, resulting in that EPS of the same Rs.47.9.

This is the walk on a quarter-to-quarter basis on EBITDA margin. And as you can see, there are basically four factors here. Wage impact is we had the second quarter impact of all those senior members of the team and some other parts of the group, the total for the quarter was 16 basis points.

And the seasonal decline in revenue for P&P is basically a seasonality factor, I have a further page coming up explaining this in slightly more detail, it's a seasonal decline, which is contributing 73 basis points.

And the third factor here is really the large number of fresher hiring that we have done and as you can imagine, they are not billable immediately, and it takes kind of a quarter in some parts of our business a little more to make them productive and billable. So that has contributed about 61 basis points and freshers and other investments. And FOREX fluctuations took away another 21 basis points. So that is how the 215 basis points is really comprised of.

Looking at the "Cash Flow Summary." I'll just focus on the FY'21 while the Q4 numbers are given here in FY'20, are also given here for comparison. I think the numbers to focus on for the year are $2.176 billion of cash profits. Cash profits is nothing but OCF before the working capital changes, that's also the same cash profit translates to cash EPS that we have been publishing for quite some time now. On operating cash flow, we delivered 2.6 billion for the year, mind you, this is after the $100 million that we paid out for the milestone bonus. So if we were to exclude that from here as well, the number is actually 2.7 billion. And then when I remove the CAPEX from that, the free cash flow is at 2.34, and we have been clocking at $2.4 billion in the last few quarters on a LTM basis. And if I add the 100 million back, again, here it is 2.44 billion. And if you look at whichever yardstick you might want to measure, as a percentage of net income, or as a percentage of EBITDA, these are very, very healthy numbers for anybody. $2.8 billion is the cash on the balance sheet at a gross level. And after removing the borrowings of 534, it's about $2.3 billion.

Moving on to “P&P.” I said I have additional page. We have said this 20 times in the last, I don't know five or 10 quarters, it's got its own seasonality, and here you can see both for FY'20 and for FY'21 how the numbers have been. FY'21 Q1 obviously there was more contribution from acquisition of those seven products that we did at the end of June 2019, so, that is the reason for this growth to be so high. But even if you leave that out, I think the important point to note is that even after that, the growth has been very good, looking at constant currency of 16%, 9% and 3% sequentially … sequentially meaning on a year-on-year basis. And even for this quarter, it is a growth of 3.3%, 5.4% on a reported basis in constant currency 3.3%. And that is really the right number to look at. For the whole year, of course, it came in at 20.5%. There was a small impairment charge that we took for one of the products that was under one of the IP partnerships that we did, a small charge of about $16 million on an annual basis, it means 60 basis points on a quarterly basis. Now, out of the 20-odd product groups that we have either acquired or done by partnerships on, this is one of the products out of those 20 which have seen impairment after several years, as we approach June of 2021, it will be five years completion of this new business that we started in June 2016 with the very first day. To my mind, that's a small thing and happens once in a while.

The other notable thing during the quarter was the DWS acquisition, which we consummated on 5th of January. And those numbers have been sort of consolidated in this quarter. And as far as purchase price allocation is concerned, this table gives you the purchase price. If you add the $120 million equivalent that we paid for the shares, and the borrowings of close to $30 million, so the total enterprise value was about $150 million. And this is how the assets came in and the rest is of course.

This is the last thing that I want to talk about the tax line item. And this has been a bit of a surprise during the quarter because the Finance Minister in the Finance Bill went out and took away the benefit of depreciation that was available so far. And that was the law so far that goodwill was depreciable. And we had obviously baked that into our calculations. And we were taking the benefit of that as far as tax books is concerned. But in this quarter, the FM came and withdrew it from a retrospective effect from 1st April 2020. So while we got the benefit for one year FY'20, but for the FY'21, right from day zero of FY'21, we had to sort of write-back that benefit that we were taking. So, that has been the reason why the tax expense has gone up during the quarter and that is just looking at the US GAAP books. If you look at IndAS books, there is a big amount of close to $160 million, which is a complete one-time non-cash kind of a deferred tax liability that we have had to undertake, put it in the books there, which is not a liability payable to anybody at any point in time, but that is what IndAS and IFRS dictated. So, it has also caused a large difference or $160 million between the net income as per US GAAP, which did not try to get this silly entry actually. But under the IndAS literature, we tried our level best to see how we could have avoided this because this really is not reflecting the reality. But at the end of the day, this is what it is, and this is what we had to provide for in the IndAS books only, not under US GAAP. And my last page is reconciliation, I will come to that in a second. This is just a quick recap of the bond issuance that we did. We finally got ourselves two ratings, one by S&P which you are aware of, and we also got Fitch to rate us, both of us rated as A-minus with a stable outlook. And that is one of the highest credit ratings and the highest rated issuers out in the international debt capital markets. We raised about $500 million for a period of five years and this is listed on Singapore Stock Exchange. We did get very a fine pricing, as you can see from the data provided here.

This is the last page I was talking about. This is basically a reconciliation of the US GAAP in rupees crores versus the IndAS. And the key highlighted blue bars are what you need to focus on, or rather four, revenues, there is no difference at all, it is the same Rs. 75,000 odd crores. But in the EBITDA, as you can see, there is a difference of Rs. 790 crores which is coming entirely from how IndAS treats on the leasing charges versus US GAAP. So, as you can see, the IndAS EBITDA is always about 1 percentage point higher, which is this 719, it is kind of slightly lower than 1% at this point in time.

EBIT then kind of more or less matches up because the same reversal happens at the depreciation level. And then there are some other small items which make the reconciliation, but the big item this time with this Rs. 1,174 crores which I spoke about a few minutes back, and that is really causing the big difference of 1,290. And this is really the bulk of the difference being caused because of that deferred tax liability that we had to create under IndAS standard.

That is all I had. And over to you moderator for Q&A.

Moderator: Thank you very much. We will now begin with a question-and-answer session. The first question is from the line of Ankur Rudra from JP Morgan. Please go ahead.

Ankur Rudra: Thank you for the detailed presentation and the increased disclosure this time. CVK, could you give us a sense of how this order book you have had this time, how does the spread look? Is there any one or two very large these which skews the mix or is it evenly spread? And also, as an additional question, thanks for your commentary, can you give us a sense of your participation rates and application and division range have gone up significantly in the last year or so.

C. Vijayakumar: Ankur, as I said, it is very well balanced the 19 deals, there are two deals with the $250 million dollars plus, and several $100 million and $50 million plus kind of deals are there. So, it is not concentrated with one mega deal, so that is also a good part, that is a broad-based momentum across multiple geographies with some sizable deals, which are very, very good from a long-term perspective for us. And in terms of duration, also, I do not see too much of variation, most of them are either three year or five-year deals, o there is not a seven year or 10-year deal in this. So, that is one perspective that I can provide.

In terms of the business line, of course, there are at least four deals which are integrated, which has the green infrastructure, digital foundation and application modernization and cloud migration kind of programs. Two carve outs, which is M&A kind of deals, one we already announced which is UD Trucks, and another one which is again the largest dealer for the quarter, which is again a Europe based utilities company. And that is also digital foundation and application modernization and cloud smart offering. And one of the largest deals for engineering services was again, product sustenance, it is more of a cost and trying to build more innovation and customer advocacy kind of deals. It is very well spread, high quality deals in very high-quality large clients. That is the best that I can share now, Ankur.

Prateek Aggarwal: Ankur, I just want to add and clarify, to avoid confusion, the M&A or carve out that CVK spoke about is at the customer end, not at our end.

Ankur Rudra: Understand. Thank you. I was just going to ask for a follow-up from there, clearly very strong bookings this time. And also, as you highlighted, the duration is not very high. So, we are looking at an exit rate of new deals booked this time. The guidance of double-digit growth or even at least a double-digit growth looks a bit light and easy to achieve. Are there any headwinds, for example, the net impact of the PNP decline that you alluded to, is that something you have baked into this guidance? Is that why you are not quantifying at a higher level than this?

C. Vijayakumar: Yes, I think from the services business, both IT business, services, and engineering services, we are seeing a very strong outlook. Products and platform, as I said, 75% of the products we feel confident of a strong growth, 25% there is a declining characteristics and we have retired a couple of products. So, at this point, we have penciled in a low single-digit type of growth in the PNP segment. That is how the numbers will pan out.

Ankur Rudra: Understood. And just last follow-up for Pratik. Pratik, the margins this quarter in PNP or Mode-3, was it largely the impairment charge? And if I take that out, on a Y-o-Y basis the margins are sort of flattish.

Prateek Aggarwal: Actually, Ankur, if you just do the math on a quarter-on-quarter basis also, the drop in the PNP margin is about $40 million. Out of which revenue is a seasonal decline, it is just seasonality, there is nothing more to be read into it, that's about $18 million odd. Impairment, as I discussed, is about $16 million, that comprises $34 million, leaving just a small increase of $6 million, which has been building the sales and marketing and other parts of the business. So, really not a separate.

Moderator: Thank you. The next question is from the line of Pankaj Kapoor from CLSA. Please go ahead.

Pankaj Kapoor: CVK, my first question is on the investments that you plan to do. So, I was just trying to figure out, are you looking at this as more of a one-time investment? Any quantification you have in mind that what could it be in terms of the scales? And from a medium-term margin outlook perspective then, does it mean that once this investment is done maybe, say, a year or two, we can go back on a higher margin trajectory?

C. Vijayakumar: Yes. So, I think we are looking at it, I talked about many areas of investments into geographies, and Mode-2 and talent and locations and all that, you should consider it like 100 basis points kind of an investment. And then, of course, I mean, while some of that investments have happened in the last three, four months, a little bit of that could be in the run rate, but from a full year perspective it will play out, it will magnify. And I think some of these geographies we are seeing strong momentum, as we kind of scale up revenues that will automatically pay for itself. So, I do not see this like a permanent thing. And there are certain geographies where we want to expand and they are not like random geographies, they are geographies where we are seeing a lot of traction, and there is good acceptance, we have some marquee clients where there is a great way to expand. I mean, if you take the next year or FY 2023, 2024, I think this should not really be a headwind from a margin perspective.

Pankaj Kapoor: Understood. And my second question is on the dividend that we declared. So, just wanted to have some broader thoughts on your capital allocation policy. Is there any kind of a thought process in terms of the way you are looking at it as a percentage of maybe profit or as a percentage of free cash flow? Like many of your peers have. And any thoughts around the mode that you may have in mind, do you think a dividend is a more preferred route or you will be open to exploring other options as well?

C. Vijayakumar: Prateek if you can take this.

Prateek Aggarwal: Sure. So, Pankaj, thanks for the cue on that one, I should have covered it without even the slides. So, as we mentioned, the dividend for this quarter declared is Rs. 16 per share one, and we have declared Rs. 2, Rs. 4 and Rs. 4 in the previous three quarters, so that takes it up a total of Rs. 26. The Rs. 16 really is broken into two parts, one is just like we gave employees 10 days of salary as a commemorative mark just to mark the milestone of $10 billion, we are doing the same with the shareholders, Rs. 10 per share as a marker of that milestone. The rest Rs. 6 is really the new benchmark that we are setting going forward instead of the Rs. 4 per quarter that we paid in the last two quarters, and before that we were paying Rs. 2 per quarter, so we have increased it now to Rs. 6 per quarter, and that is what we intend to carry on into the four quarters of the next year and beyond. And we will again look at it next year end as and when we get to that.

Pankaj Kapoor: Understood. And just one last small clarification, Prateek. Given the kind of adjustments that we have done on the tax side, any sense in terms of what kind of effective tax rate should we be looking at? Last quarter you had spoken about it going down to around 22% kind of a level, but now with these changes what is the new ETR that one should expect? Thank you.

Prateek Aggarwal: Yes, Pankaj. So, as ETR is concerned, our reported ETR for this year is 21.9%. But that does have the benefit we got for FY 2020 in this year. So, if we normalize it, it comes to about 22.5%, taking away the benefit of prior years. So, against that 22.5%, we expect next year to go up to 24.5%, give or take 50 basis points either which way. So, the range for next financial year 2022 should be from 24% to 25% odd. This is about 1 percentage point higher from the midpoint of what I had told all of you last quarter, I had mentioned 23.5%. And because it was still an interim kind of working, I kept a (+/-1%) on that. So, from that perspective, the range has changed from 22.5% to 24.5%, to now a narrower range of 24% to 25%.

Moderator: Thank you. Next question is from the line of Diviya Nagarajan from UBS. Please go ahead.

Diviya Nagarajan: CVK, I was curious about your earlier comment about not the time to maximize profits. And I am also trying to reconcile that with your 100 basis points of investment that you talked about. And kind of wondering what that comment really means if you could add some color to that. And what also happens to the operating leverage that you get in the business this year? There is also a currency tailwind that we are starting the year with. Could you just kind of lead us through where you are thinking about this, please?

C. Vijayakumar: Yes, definitely there is an operating leverage in some of our core geographies and some of the scaled-up areas of capabilities. But in the given circumstance, I do think expanding our presence outside some of our strong geographies, which is US, UK, Nordics, is a very good investment. And we are already seeing the success of that in France in Germany, a little more emphasis on a few more geographies. And some geographies where we really do not have a country sales presence, we are trying to expand this.

And the second element is on our engineering services. For a while we have a strong leadership position in engineering services. There is definitely significant shift in technology, which is what we are now calling as Mode-2 digital engineering services, very similar to how the other Mode-2 services helped us scale and create a significant mindshare and very good traction. Like now our application services led by our digital capabilities is really doing extremely well. We want to create those opportunities and give ourselves a little bit of elbow room to invest there. So, when I said it was not the time to maximize, I think it is really a reflection of there are opportunities and this will really help us deliver stronger growth in the mid to long-term. I hope that clarifies?

Diviya Nagarajan: Yes, thank you. And just as a quick follow-up, these investments, would you categories them or characterize them as preemptive, or would you characterize them as need of the hour?

C. Vijayakumar: See, most of them are proactive, except the talent related some of the investments we believe are addressing some of the emerging demands, I mean, refreshes are scaling up, including in different geographies. So, some of that creates upfront costs, which will get rationalized as we move forward.

Moderator: Thank you. The next question is from the line of Sudhir Guntupalli from ICICI Securities. Please go ahead.

Sudhir Guntupalli: Extension of the prior question on margin guidance. A normalized EBIT margin guidance band used to be 19.5% to 20.5% before acquisition of IBM products. With their integration we were expecting a step jump in overall EBIT. Then came in COVID which brought some of the transient tailwind state, offshoring, higher utilization, so on and so forth. We do acknowledge that some of these may be strictly ephemeral in nature and there may be a need for higher investments. However, if you look at margin guidance band of 19% to 21%, it is weaker than even pre-COVID and pre-IBM acquisition levels. So, how do we reconcile the profitability trajectory with these tailwinds related to IBM/COVID on one side and your guidance on the other side?

C. Vijayakumar: Yes, I think the right way to look at it is, see, the gross margin level continues to be good outcome. And there are some areas where we want to proactively invest, while a lot of saving related to the pandemic is sitting in our FY 2021 margins, in our planning we have already assumed a certain amount of travel, all of that. So, maybe some of them may not play out. But that added to the investments that we have planned, we start getting into a slightly broader range, which is also the industry practice, which gives us a little bit more elbow room to do all the right things that are required.

Sudhir Guntupalli: Sure, CVK. And just one follow-up, in one of the recent industry forums you made an interesting point about industry revenue potentially doubling over the next three to four years. HCL being one of the key leaders in the industry, we would have anticipated HCL to outgrow the industry or match the industry growth levels. But our growth guidance seems to be a little behind, so how do we read this disconnect? Are we being conservative at this juncture or is there a context to it?

C. Vijayakumar: Sudhir, I think you should interpret that comment. And as it was said, it is a long-term outlook for the industry, and it is an industry forum and I want to just leave it there.

Moderator: Thank you. The next question is from the line of Ashwin Mehta from Ambit Capital. Please go ahead.

Ashwin Mehta: CVK, you did talk about investments on the digital engineering services side in the ER&D piece. So, what is our mix as of now approximately between core engineering versus digital engineering? And in terms of our outlook for ER&D, would you think that will grow at company average? Or because of the fact that there is exposure to aero, auto, this might grow slower going into the next year as well?

C. Vijayakumar: We expect our engineering services to be growing at the company average services growth rate, for sure. And right now, the mix of digital engineering services is small. I do not have an exact quantification, maybe in a future opportunity to interact we will provide you a little more color. But definitely the potential in some of these areas are good. And we are already doing a lot of work in this area, it is just that there is little more attention, and a little more proactive investment will help us execute well as well as drive growth in the future, mid to long-term.

Ashwin Mehta: Okay, thanks. And just one clarification. So, in terms of the impairment that we have taken in the products and platforms space in this quarter, is the revenue impact of that kind of already there in our numbers? And secondly, out of the remaining portfolio of around 25% of the business where we are seeing declines, if that kind of taken care of in our expectation of, say, low single-digit growth in products and platform space for the next year?

C. Vijayakumar: Yes, Ashwin, that is all factored in, in our projections. And just to provide a little more context to this impairment, I mean, if we wanted to optimize cost and deliver more contribution margin on this, to avoid an impairment, we could have very well done that. But we do believe this is a very strong product, there is a very strong outlook. So, we decided to invest a little bit more, which is why the contribution margin comes down and which is resulting in an impairment. So, it is a conscious call. I mean, if we really wanted to avoid, we could have very well avoided it. But we think it is the right thing to do in our overall product portfolio perspective.

Ashwin Mehta: Okay. And just one last small one, in terms of the next year margin guidance, have we baked in any wage hikes for the next year?

C. Vijayakumar: Yes, of course, yes. We have a wage cycle which starts in July. And last year, there was a three-month delay, but this year we expect to provide them wage hikes as per the regular cycle, and that impact is factored in our P&L.

Moderator: Thank you. The next question is from the line of Ashish Chopra from Kotak Asset Management. Please go ahead.

Ashish Chopra: Just a couple of quick ones from my side, CVK. Firstly, with respect to the investment that you mentioned around digital engineering and perhaps some new geographies, how are you thinking about the build versus buy over here? And do you think that the inclination to maximize the time to market may be due to some acquisition period and it could be embedded in part in the margin guidance?

C. Vijayakumar: See, I think, for example, in countries, I mean, we are always looking for opportunities for acquisition to expand in some geographies where we want to, like Australia we did, we did a small one in Germany two years back, all of that is, at least Germany is definitely helping us in a significant way, for Australia it is early days. So, we look for opportunities, but sometimes these things do not happen in a time bound manner, so at least we are ensuring that we are doing all the right organic investments in these areas. And the same is true with some of the digital engineering, if we find the right assets, we will not hesitate to acquire. But obviously, some of them the valuations are high and our ability to kind of get all the right outcomes, but that also takes time. So, that way, I think we are better off doing organic investments and growing some of these areas where we already have capabilities, it is just a little more emphasis and a little more proactive build out to ensure we are able to address some of the demand.

Ashish Chopra: Got it. And just lastly from my side, in the past couple of years we have seen the fiscal year starting on a relatively softer note because of some of the productivity clauses coming in in the larger engagement. Do we expect a similar kind of trajectory and seasonality this time around as well? Or would it be a year where the seasonality would be more or less in the products, but service could be by and large the same?

C. Vijayakumar: I think there would be a little bit of that seasonality which will play out in Q1. But nothing out of the way, I would say.

Moderator: Thank you. Next question is from the line of Kawaljeet Saluja from Kotak. Please go ahead.

Kawaljeet Saluja: It seems that there have been plenty of questions on margins, so let me add one more to it. CVK, normally you expect companies to fund investments in service design, geographies to their normal operation. I mean, is there any specific reason why you have called this out? And is there in any sort of way an acknowledgement that you have under invested in the business overall, which is causing this additional investment into FY 2022? And if not, then normally investment signifies that once they start paying off, it leads to a material change in growth trajectory. So, just wanted your thoughts on what is really investment versus spending.

C. Vijayakumar: I think, Kawal, on the geography, I think every year we were trying to pick up a couple of geographies and focus on. And that is how we have always looked at three or four geographies we pick up as a three, four-year strategy. And that is how the whole Nordics we have kind of reached a very strong leadership position. Similarly, some other geographies like South Africa and things like that. And some of these geographies we started, and we are seeing good results, so we are stepping up the investments. That is how I should see. And obviously, every investment that we make, we feel accountable for delivering returns, but not necessarily like on the same year, we think if you take a two-to-three-year horizon, they will pay for itself, and they would kind of deliver company level profits in some of these geographies. So, on the capability side, we have very strongly invested in Mode-2, on the IT and business services. Maybe on digital engineering, maybe we could have done a little bit more in the past. But we still think the timing is right, we can do some of these things which will help us to get a little bit more market share. And some of this will definitely reflect in growth as we move forward.

Kawaljeet Saluja: Okay, thanks. CVK, the second question is on engineering services. I mean, this business segment has always been talked about as a huge opportunity. Post COVID, for some of the companies, globally as well as in India, there seems to be recovery in engineering services. But somehow for HCL Tech, the pickup seems to be a little bit tardy. Any reasons? And when we move to FY 2022, how should we look at this particular business segment performing?

C. Vijayakumar: Kawal, I think it is definitely bottomed out. I mean, as we had said earlier, the hi-tech and communication, even this year there was a positive growth, and the asset heavy industry is where we had a steeper decline, especially some accounts in office automation and aerospace. And we see that those things have bottomed out. And next quarter onwards we should see a good growth in engineering services. That is what our expectation is.

Moderator: Thank you. Ladies and gentlemen, that was the last question for today. I now hand the conference over to Mr. C. Vijayakumar for closing comments.

C. Vijayakumar: To close, thank you for joining. And we have delivered very well in a pandemic year, and we are doing all the right things for our business to continue to be an industry leading franchise. And we look forward to connecting with you in the coming quarters. And thank you for your interest and thank you for joining this call.

Moderator: Thank you. On behalf of HCL Technologies Limited, that concludes the conference call. Thank you for joining us, and you may now disconnect your lines.