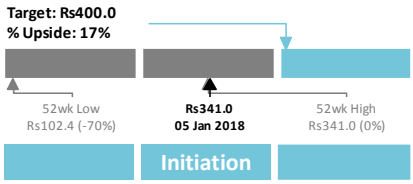
Sterlite Technologies (SOTL IN)

Target Price	Rs400.0
Current Price	Rs341.0
% Upside	17%

Global Optical Fiber Demand to Sustain High Growth

Technology Hardware
India
08 Jan 2018

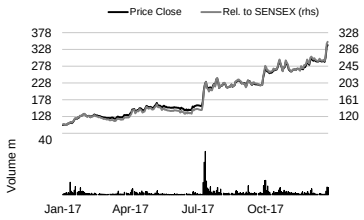
BUY



Basic Share Information

Market cap	Rs136.7b / US$2.16b
Daily traded value (3mth)	US$8.73m
Shares outstanding	407.0m
Free float	46%
Net debt-to-equity	96.4%
1 yr high	Rs341.0
1 yr low	Rs102.4
Foreign Shareholding	8%
Share price date	5 Jan 18

Price/Volume



Source: Bloomberg

	1mth	3mth	12mth
Absolute	23.3%	54.4%	229.2%
Absolute USD	25.3%	58.7%	252.9%
Relative to SENSEX	19.2%	46.3%	202.1%



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Direct Beneficiary of Exponential Growth in Data

Summary: We see Sterlite's optical fiber business (around 80% of FY3/17 revenues) as a beneficiary of ongoing accelerated spend by telecom operators across the world to manage fast growing data traffic. With high telco demand and a global capacity constraint, Sterlite is witnessing both an increase in optical fiber prices and longer-dated purchase contracts. In addition, Sterlite's presence among a small group of integrated suppliers has helped it keep costs under control and increase capacity. We expect Sterlite to report 32% revenue CAGR over FY3/18–20, benefitting from optical fiber capacity expansion (to 8% of global market share). Operating EBITDA margin should expand by 185bps during FY3/18–20 due to better utilization in optical fiber cable segment, leading to earnings CAGR of 42% over the same period. We also see potential upside to our estimates from Bharatnet (due to adoption of more advanced fiber) and optical fiber cable capacity expansion as local telco investment picks up. A 50% increase in Sterlite's optical fiber cable capacity would add 7% to our revenue CAGR estimate and 16% to our fair value estimate. We initiate on Sterlite Technologies with a BUY rating.

Target Price and Catalyst: Our target price of Rs400 is based on 28x our FY3/20 EPS estimate of Rs14.23. We see Phase 2 bidding in Bharatnet and order inflow from domestic telecom operators as potential catalysts for the shares.

Earnings: We forecast 32% revenue CAGR over FY3/18–20, on the back of capacity expansion in Sterlite's optical fiber segment and sustained growth in services and software verticals driven by a healthy order book of Rs38.0bn. We also expect a pickup in EBITDA margin for Sterlite Technologies over the next few years, which should lead to a 42% CAGR in net income for the company over the same period.

Valuation: Our target price of Rs400 is based on a PER of 28x applied to our FY3/20 EPS estimate. Our PER is one standard deviation above Sterlite Tech's median 12-month forward PER of the last two years, factoring in improved business environment. While the stock has delivered handsome returns in the last one year, we believe that it is still not completely factoring in the high double-digit growth over the next few years. Our comparable analysis of Sterlite's peer group suggests a global FY20 PER median of 14x, but at a much lower growth and OPM. Adjusting for growth, its global peer group is currently trading at a median 1.6x PEG versus Sterlite Tech at 0.8x. Our price target implies 17% potential upside from last close. We initiate coverage with a BUY rating. Main risks to our rating and target price are oversupply in global optical fiber market, a decline in China demand, delay in 5G rollout across major geographies, and a slackening of pace in 'Digital India' projects.

	Mar-16A	Mar-17A	Mar-18E	Mar-19E	Mar-20E	Trend
Total turnover (Rsm)	21,440	24,489	32,631	44,054	55,705	
Operating profit (Rsm)	3,336	3,597	5,218	7,308	9,715	
Pre-tax profit (Rsm)	2,250	2,574	4,076	5,899	8,322	
Net income to ord equity (Rsm)	1,537	2,014	2,607	4,154	5,792	
Net profit growth		31.0%	29.4%	59.4%	39.4%	
P/E (x)	89.24	68.51	53.25	33.42	23.96	
Adj EV/EBITDA (x)	32.73	29.65	21.65	15.90	12.11	
P/B (x)	18.18	15.68	13.26	10.57	7.76	
ROE	16.7%	24.6%	27.1%	35.2%	37.4%	
Dividend yield	0.2%	0.4%	0.6%	0.9%	0.6%	
EPS HTI New (Rs)	3.82	4.98	6.40	10.20	14.23	
Consensus EPS (Rs)	2.35	4.80	7.26	10.42	13.66	
HTI EPS vs Consensus	62.6%	3.7%	(11.8%)	(2.1%)	4.2%	

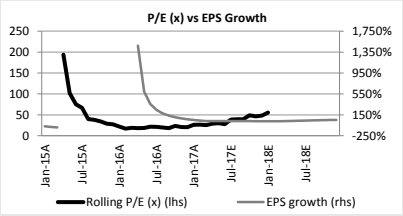
Source: Company data, Bloomberg, HTI estimates

Click here to download the working model

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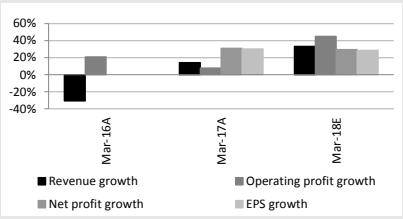
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Valuation



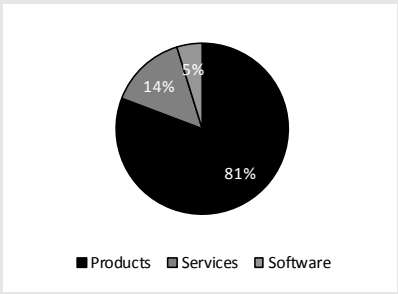
Source: Company data, Bloomberg, HTI estimates

Earnings Trends



Source: Company data, Bloomberg, HTI estimates

Sales Breakdown (FY3/17)



Source: Company data

Investment Thesis

BUY

➤ Sterlite's optical fiber business (80% of FY3/17 revenues) is benefitting from increased global telco spend to manage fast growing data traffic. With high telco demand and a global capacity constraint, Sterlite is witnessing both an increase in optical fiber prices and longer-dated purchase commitments.

➤ We expect Sterlite to report 32% revenue CAGR over FY3/18–20, benefitting from optical fiber capacity expansion (to 8% of global market share).

➤ We expect an operating EBITDA margin expansion of 185bps From FY3/17 levels to drive earnings CAGR of 42% over FY3/18–20.

➤ We also see potential upside to our estimates from Bharatnet (due to adoption of more advanced fiber) and optical fiber cable capacity expansion as local telco investment picks up.

➤ We expect Sterlite's ROE to improve from here on as high revenue growth with stable margins should lead to solid earnings growth over FY3/18–20 and hence improving return ratios. Thus, we forecast ROE to improve from 24.6% in FY3/17 to 37% in FY3/20.

Company Snapshot

Sterlite Technologies Limited manufactures and sells telecom products and solutions in India and internationally. It focuses on providing telecom products and solutions that include integrated optical fiber and other telecom products, such as fiber optical cables, copper telecom cables, structured data cables and access equipment, fiber connectivity and system integration solutions for telecom networks, OSS/BSS solutions, and billing and bandwidth management solutions to organizations. The company also engages in the service design, engineering, implementation, and maintenance of optical fiber cable networks. It also exports its products and services.

Key Investment Metrics

Revenue Growth

Low | Medium | **High**

We forecast 32% revenue CAGR over FY3/18–20. We expect this growth to come from expansion in optical fiber capacity and high demand for optical fiber cable business.

Profit Margins

Low | **Medium** | High

We expect pickup in EBITDA margin for Sterlite Technologies over the next few years due to better utilization in optical fiber cable business.

Shareholder Returns

Low | Medium | **High**

We expect Sterlite's ROE to improve from hereon as high revenue growth with pickup in EBITDA margin should lead to solid earnings growth over FY3/18–20 and hence improving return ratios. Thus, we forecast ROE to improve from 24.6% in FY3/17 to 37% in FY3/20.

Balance Sheet Risks

High | **Medium** | Low

Sterlite Technologies is engaged in a business which requires high capex to build capacity. Its net debt to equity for FY3/17 was 1 and the company's guidance is to maintain average net debt to equity around 1 over FY3/18–20.

Barriers to Entry

Low | Medium | **High**

Sterlite is one of the seven companies in the world, which makes optical fiber pre-form, which is essential to make Optical Fiber Cable. Thus barriers to entry in this business seem high.

International Exposure/Breakdown

High | Medium | Low

Sterlite Technologies derived 37% of its revenue in FY3/17 (24% in FY3/16) from international markets.

FX Exposure

High | **Medium** | Low

Sterlite Tech imports a majority of its raw material (41% of revenues in FY3/17), but also derived 36% of its revenues from outside India. The company hedges its FX exposure on a daily basis.

Corporate Governance

Low | Medium | **High**

Sterlite Technologies follows best practices in corporate governance. Non-executive directors comprised around 60% of the board. Moreover, independent directors comprise three-fourths of the audit committee members.

Our Model Assumptions

We forecast 32% revenue CAGR over FY3/18–20, which we expect to come from expansion in optical fiber capacity and high demand for optical fiber cable business

Profit & Loss (Rsm)	Mar-16A	Mar-17A	Mar-18E	Mar-19E	Mar-20E
Total turnover	21,440	24,489	32,631	44,054	55,705
Cost of sales	(9,608)	(9,984)	(13,368)	(18,268)	(23,183)
Gross profit	**11,832**	**14,505**	**19,263**	**25,785**	**32,521**
Total operating costs	(8,496)	(10,908)	(14,045)	(18,477)	(22,807)
Operating profit	**3,336**	**3,597**	**5,218**	**7,308**	**9,715**
Operating EBITDA	4,592	5,189	7,143	9,864	12,834
Depreciation and amortisation	**(1,256)**	**(1,592)**	**(1,925)**	**(2,555)**	**(3,119)**
Interest income		87	-	-	-
Interest expense	(1,086)	(1,110)	(1,142)	(1,410)	(1,393)
Pre-tax profit	**2,250**	**2,574**	**4,076**	**5,899**	**8,322**
Taxation	(652)	(397)	(1,269)	(1,545)	(2,330)
Minority interests	(61)	(163)	(200)	(200)	(200)
Net income to ord equity	**1,537**	**2,014**	**2,607**	**4,154**	**5,792**

Source: Company, HTI estimates

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We expect pickup in EBITDA margin for Sterlite Technologies over the next few years due to better utilization in optical fiber cable business

✓ Key P/L Takeaway

We forecast 32% net revenue CAGR over FY3/18–20 and a 42% net income CAGR over the same period helped by 185bps improvement in operating EBITDA margin

We forecast 32% revenue CAGR over FY3/18–20. We expect this growth to come from higher orders of Sterlite's optical fiber and optical fiber cable as demand would stay strong in the medium term with continuous infrastructure improvement by telecom companies with optical fiber networks and also from preparing infrastructure for 5G. We expect a pickup in OPM for Sterlite Technologies over the next few years as high revenue growth is supported by stable costs along with benefit from higher utilization of optical fiber cable business. We estimate a 185ps increase in operating EBITDA margin over our forecast period.

Our Model Assumptions

Sterlite enjoys decent cash balance but also has debt on its balance sheet as it is a capex heavy business

ROE should improve from hereon as high revenue growth with pick up in OPM should lead to solid net earnings growth over FY3/18–20 and hence improving return ratios; thus, we forecast ROE to improve from 24.6% in FY3/17 to 37.4% in FY3/20

Balance Sheet (Rsm)	Mar-16A	Mar-17A	Mar-18E	Mar-19E	Mar-20E
Total cash and equivalents	1,731	2,380	2,347	1,995	3,095
Inventories	2,053	3,335	3,113	4,254	5,399
Accounts receivable	7,084	6,867	8,940	12,069	15,262
Other current assets	1,489	2,146	2,696	3,530	4,463
Total current assets	**12,357**	**14,728**	**17,097**	**21,849**	**28,219**
Tangible fixed assets	11,663	12,580	13,655	16,600	17,980
Intangible assets	1,522	1,206	1,206	1,206	1,206
Total other assets	704	992	846	1,017	1,242
Total non-current assets	**13,888**	**14,779**	**15,707**	**18,822**	**20,428**
Total assets	**26,245**	**29,507**	**32,803**	**40,671**	**48,647**
Short-term debt	3,542	5,910	6,410	7,410	7,910
Accounts payable	3,722	4,486	5,128	7,007	8,892
Other current liabilities	4,764	3,695	3,682	4,013	4,354
Total current liabilities	**12,028**	**14,091**	**15,220**	**18,430**	**21,156**
Long-term debt	5,709	5,394	5,894	7,894	8,394
Other liabilities	650	769	769	769	769
Total non-current liabilities	**6,358**	**6,163**	**6,662**	**8,662**	**9,162**
Total liabilities	**18,387**	**20,254**	**21,883**	**27,092**	**30,318**
Common stocks	790	797	797	797	797
Retained earnings reserve	6,756	8,004	9,672	12,331	17,080
Shareholders' equity	**7,546**	**8,801**	**10,469**	**13,127**	**17,877**
Minority interests	312	452	452	452	452
Total equity	**7,859**	**9,253**	**10,921**	**13,579**	**18,329**
Total liabilities & shareholders' equity	**26,245**	**29,507**	**32,803**	**40,671**	**48,647**

Source: Company, HTI estimates

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✓ **Key B/S Takeaway**

With net debt to equity ratio of 1, we believe balance sheet risk is low

Sterlite Technologies is in a business which requires high capex to build capacity for the future and that has put pressure on its balance sheet in terms of high borrowings. Net debt to equity for FY3/17 was 1 and we expect average net debt to equity to remain 1 over FY3/18–20

Our Model Assumptions

We expect cash flow from operations to rise slower than OP due to high working capital over the same period

Free cash flow generation should be decent as high earnings growth is getting offset by incremental capex

Cash Flow (Rsm)	Mar-16A	Mar-17A	Mar-18E	Mar-19E	Mar-20E
Operating profit	**3,336**	**3,597**	**5,218**	**7,308**	**9,715**
Depreciation and amortisation	1,256	1,592	1,925	2,555	3,119
Changes in working capital	(2,545)	461	(1,481)	(3,068)	(3,166)
Other operating cash flow	(860)	(1,078)	(1,142)	(1,410)	(1,393)
Operating cash flow	**1,187**	**4,572**	**4,520**	**5,386**	**8,275**
Interest received	(123)	(119)	-	-	-
Interest paid	1,192	1,229	1,142	1,410	1,393
Tax paid	(487)	(763)	(1,269)	(1,545)	(2,330)
Cash flow from operations	**1,769**	**4,919**	**4,393**	**5,251**	**7,338**
Capex	(2,239)	(2,127)	(3,000)	(5,500)	(4,500)
Other investing cash flow	684	(196)	-	-	-
Cash flow from investing activities	**(1,555)**	**(2,323)**	**(3,000)**	**(5,500)**	**(4,500)**
Dividends paid to ordinary shareholders	(282)	(709)	(938)	(1,495)	(1,043)
Proceeds from issue of shares	2	6	-	-	-
Increase in debt	834	38	1,000	3,000	1,000
Other financing cash flow	(1,363)	(1,204)	(1,342)	(1,610)	(1,593)
Cash flow from financing activities	**(809)**	**(1,869)**	**(1,280)**	**(105)**	**(1,635)**
Cash at beginning of period	6,164	1,731	2,030	1,997	1,645
Total cash generated	**(4,433)**	**299**	**(33)**	**(352)**	**1,100**
Implied cash at end of period	**1,731**	**2,030**	**1,997**	**1,645**	**2,745**
Free cash flow	**(470)**	**2,792**	**1,393**	**(249)**	**2,838**

Source: Company, HTI estimates

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✓ Key Cash Flow Takeaway

Capex over next three years would likely offset high free cash flow which the business generates

We expect cash flow from operations to rise slower than OP due to high working capital over FY3/18–20. Sterlite has generated free cash flow of Rs2,792mn in FY3/17 and we expect it to moderate over FY3/18–19 due to incremental capex for capacity expansion.

Our Model Assumptions

Given the high net income CAGR of 42% over our forecast period, we see a PER of 24x on our FY3/20 EPS estimate as attractive

Per Share Data	Mar-16A	Mar-17A	Mar-18E	Mar-19E	Mar-20E
EPS (Rs)	3.82	4.98	6.40	10.20	14.23
FDEPS (Rs)	3.82	4.98	6.40	10.20	14.23
Revenue per share (Rs)	53.3	60.5	80.2	108.2	136.9
Operating EBITDA per share (Rs)	11.41	12.83	17.55	24.23	31.53
BVPS (Rs)	18.76	21.75	25.72	32.25	43.92
DPS (Rs)	0.60	1.50	1.92	3.06	2.13
Recurrent cash flow per share (Rs)	4.40	12.16	10.79	12.90	18.03
Shares in issue (million)	402.3	404.6	407.0	407.0	407.0
Year end adjusted shares in issue (m)	402.3	404.6	407.0	407.0	407.0
Key Ratios	**Mar-16A**	**Mar-17A**	**Mar-18E**	**Mar-19E**	**Mar-20E**
Valuation Measures					
P/Sales (x)	6.40	5.63	4.25	3.15	2.49
P/E (x)	89.24	68.51	53.25	33.42	23.96
P/CF (x)	77.57	28.05	31.59	26.43	18.92
P/B (x)	18.18	15.68	13.26	10.57	7.76
Adj EV/EBITDA (x)	32.73	29.65	21.65	15.90	12.11
Dividend yield	0.2%	0.4%	0.6%	0.9%	0.6%
Growth					
Revenue growth	(30.8%)	14.2%	33.3%	35.0%	26.4%
Operating profit growth	21.0%	7.8%	45.1%	40.1%	32.9%
Net profit growth		31.0%	29.4%	59.4%	39.4%
Margins					
Gross margin	55.2%	59.2%	59.0%	58.5%	58.4%
Operating EBITDA margin	21.4%	21.2%	21.9%	22.4%	23.0%
Operating margin	15.6%	14.7%	16.0%	16.6%	17.4%
Pretax profit margin	10.5%	10.5%	12.5%	13.4%	14.9%
Tax rate	29.0%	15.4%	31.1%	26.2%	28.0%
Net profit margin	7.2%	8.2%	8.0%	9.4%	10.4%
Key Ratios					
ROE	16.7%	24.6%	27.1%	35.2%	37.4%
ROA	2.8%	7.2%	8.4%	11.3%	13.0%
Capex/revenue	10.4%	8.7%	9.2%	12.5%	8.1%
Current ratio (x)	1.03	1.05	1.12	1.19	1.33
Creditor days	141.8	164.0	140.0	140.0	140.4
Debtor days	120.9	102.4	100.0	100.0	100.3
Inventory days	78.2	121.9	85.0	85.0	85.2
Sales/avg assets	0.39	0.88	1.05	1.20	1.25
Credit analysis					
EBITDA/interest paid (x)	(3.85)	(4.22)	(6.25)	(7.00)	(9.22)
OCF/interest paid (x)	(1.48)	(4.00)	(3.85)	(3.72)	(5.27)
Debt/EBITDA (x)	2.01	2.18	1.72	1.55	1.27
Debt/equity	117.7%	122.2%	112.7%	112.7%	89.0%
Net debt to equity	95.7%	96.4%	91.2%	98.0%	72.1%

Source: Company, HTI estimates

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✓ Key Driver Takeaway

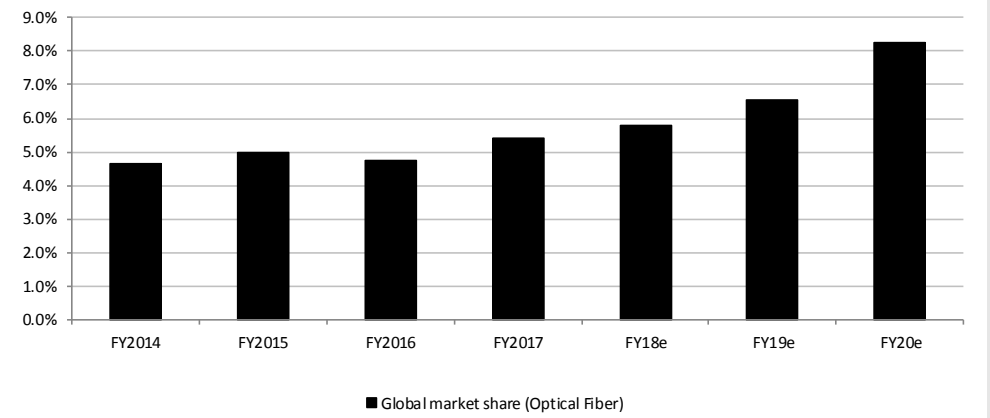
We forecast a CAGR for net income of 42% over FY3/18–20

We forecast 32% revenue CAGR over FY3/18–20. We expect this growth to come from higher orders of Sterlite's optical fiber and optical fiber cable as demand would stay strong in the medium term with continuous infrastructure improvement by telecom companies with optical fiber networks and also from preparing infrastructure for 5G. Sterlite should see a pickup in OPM over the next few years as high revenue is supported by stable costs; we estimate a 185bps increase in EBITDA margin over our forecast period.

Company Outline and Operational Review

Sterlite Technologies is the largest communication fiber manufacturer in India, with an annual optical fiber (OF) capacity of 30mn fKm (fiber Km) and optical fiber cable (OFC) capacity of 15mn fKm currently. The company sees itself as one of the few suppliers in the world to have a presence at all stages of the optical fiber cable manufacturing process, and is among the seven key suppliers of preform (a key intermediate product in the OFC manufacturing process) across the globe. In addition, Sterlite also offers system implementation and software sales to its core telco and public sector customers, benefitting from its visibility into their new spending decisions and preference for an integrated product and service contract. Sterlite Tech controls close to 6% of global capacity of optical fiber, and is in the middle of setting up a new factory which would add 20mn fKm/year to its optical fiber capacity and take its global market share to over 8%, according to our estimates.

Sterlite Technology Market Share - Optical Fiber (Global)



Source: Company data, CRU, HTI estimates

Direct Beneficiary of Exponential Growth in Data

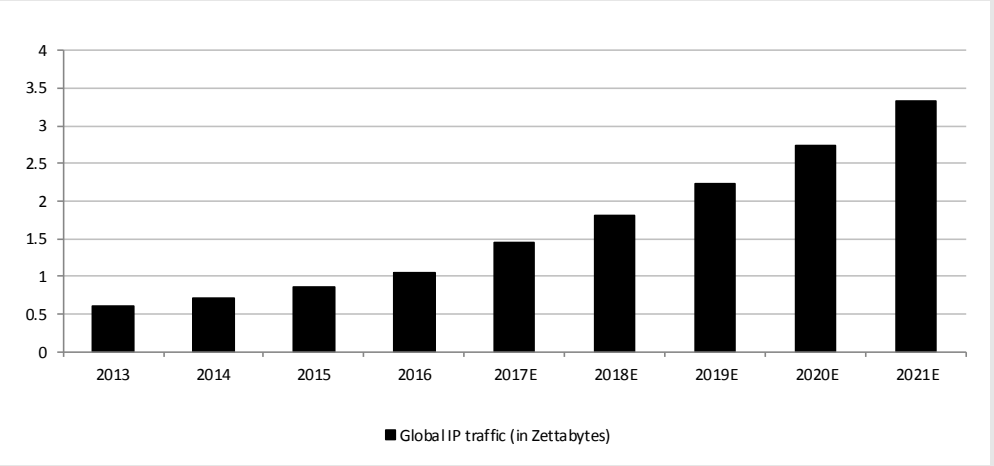
We see Sterlite's optical fiber business (80% of revenues in FY3/17) as one of the direct beneficiaries of the data explosion currently underway across the world. With rapid growth in data consumption, telecom operators across both developed and developing countries are scrambling to set up or expand their optical fiber cable capacity in backhaul, leading to a scarcity of the optical fiber over last 6–8 quarters. This scarcity has resulted in a) an increase in pricing of the optical fiber (spot prices have moved from close to US$7.0 per fKm in early 2015 to US$12.0 per fKm in June 2017, according to data from company and CRU monitor), and b) elongation of delivery contracts from a few months to multiple quarters or even years. We see both trends as positive for Sterlite Tech, as it is one of the small group of suppliers (including peers like Corning, YOFC, Prysmian, Shin-Etsu Chemical etc.) which operates across the value chain of optical fiber cable manufacturing and hence benefits from any mismatch in demand-supply of optical fiber.

Moreover, our estimates suggest that the company's recent plan to expand OF manufacturing capacity by two-thirds over the next two years should be absorbed by a fast growing end market, despite similar expansion by its peers. Finally, we see the demand of both OF and OFC in India picking up over the next few years due to demand from both telecom and Bharatnet project. Given Sterlite's dominant domestic market share, this should be positive for the growth – we project 32% revenue CAGR over the next three years.

High Speed Wireless and Wireline Connections to Drive Data Growth

According to Cisco VNI Index, global internet data traffic has seen very rapid growth over last few years, and is expected to continue for the foreseeable future, benefitting from higher data speeds across the world. We expect data usage to move up another notch as gradual 5G rollout happens across the world starting from 2019–20 onwards. According to the widely followed Cisco Systems (CSCO US) VNI index, global data demand should grow from 1 Zettabyte in 2016 to 3.34 Zettabytes in 2021, at a CAGR of 24% over the period.

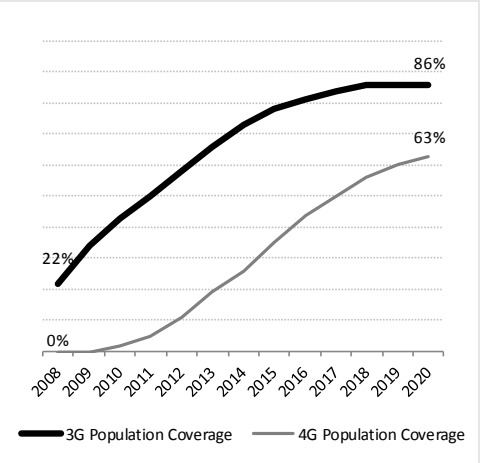
Global IP Traffic – 2013–21



Source: Cisco VNI Index

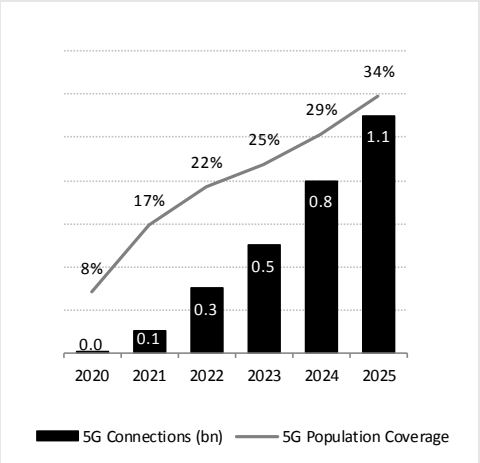
This data growth has been driven by a pickup in the 3G and 4G wireless connections over the last decade, with every increase in speed level leading to greater requirement for data from consumers. With telecom operators embarking on the rollout of 5G services with theoretical speed reaching gigabytes per second, the pace of data consumption should only grow going forward.

Global 3G and 4G Population Coverage



Source: GSMA Intelligence

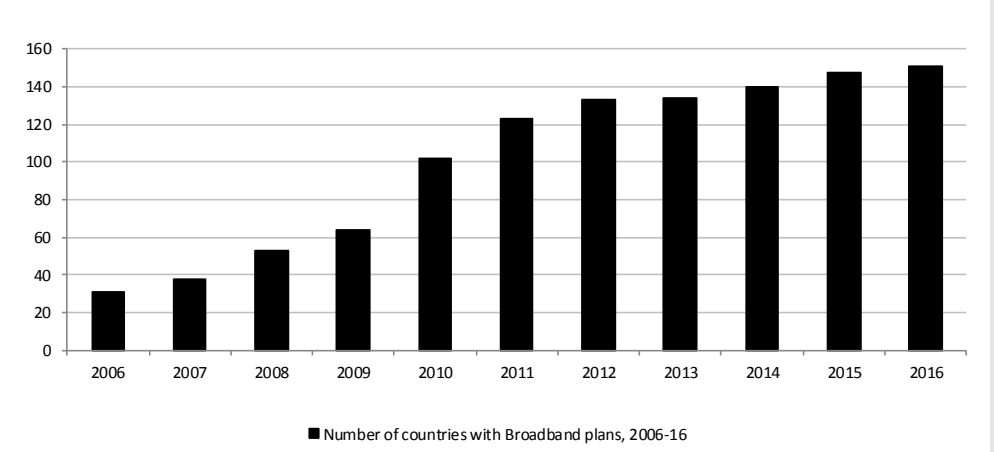
Global 5G Population Coverage and Adoption



Source: GSMA Intelligence

Countries across the world are aggressively expanding their adoption of broadband, with ITU data suggesting that over 150 countries now have either an official national broadband plan or a strategy to roll out one soon. We see this as an indicator of increased adoption of wired internet or FTTX (fiber to the premises) network.

Number of Countries with Broadband Plans, 2006-16



Source: ITU

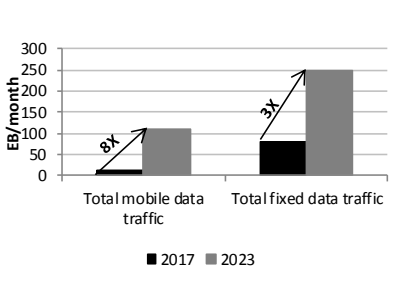
In addition, we see multiple levers for the data drivers across the globe over the next three to five years. While significant spending on 4G has already taken place in countries such as the US and China (leading to a slowdown in telecom spending), global data demand is likely to remain high. Key drivers of data demand include cloud services, datacenter interconnect (DCI) and 5G, all of which are likely to manifest as Internet of Things (IoT) capabilities.

Future Growth Drivers for Data Traffic

Optical Networking Growth Drivers	
Cloud Services	17% CAGR between 2013-2018 in Cloud services, creating huge bandwidth demand - Gartner
5G transition	5G expected to gain traction by 2020 - would require 1000x bandwidth per unit are (vs 50x required in 4G vs 3G) and pervasive fiber deployment
4K UHD video	Global IP video traffic to grow at a CAGR of 26% from 2016 to 2021, tripling in size - Cisco
Web-Scale network builds	Huge connected datacenter requirement from internet giants (Google, Facebook etc) to propel dedicated optical bandwidth and data consumption

Source: ADVA, Cisco VNI Index, Gartner

Data Traffic Growth between 2016–23



Source: Ericsson Mobility report (Nov-17)

According to Ericsson, the pick-up in both wireline and wireless internet would result in total data traffic reaching 360 Exabytes/month by 2023 (a 25% CAGR over 2017–23), with fixed data traffic accounting for 70% to the total data traffic.

Optical Fiber Best Positioned to Benefit from Data Demand

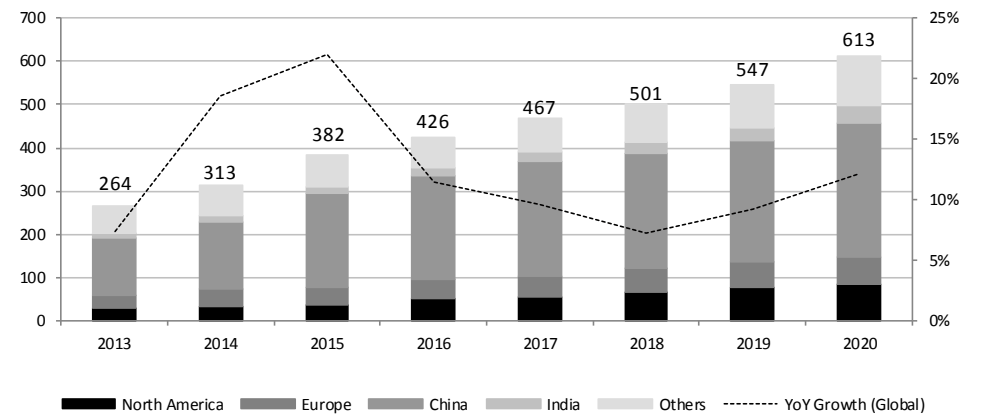
While the pick-up in data demand would play across multiple segments in hardware, software and internet sectors, we see fiber as a clear choice to transport data within the network of telecom operators. Our analysis of the industry suggests three key mediums to transport data on the telecom networks: a) Copper/DOCSIS (Data Over Cable Service Interface Specification), b) Microwave and c) Optical Fiber Cable. While microwave is easier to setup, it is most useful for relatively short distances. It is also susceptible to interference from buildings and cannot travel a long distance. Hence, most of the backhaul transmission of data in a mobile network happens over optical fiber cable. On the other hand, copper cable suffers from multiple shortcomings, including comparatively shorter lifespan, limited distance transportation without boosters, lower bandwidth and comparatively higher cost due to use of expensive copper. This has resulted in OFC being the preferred medium to transport bulk data across the world. Hence, we see OF as well placed to benefit from the increasing data demand due to a lack of clear alternative.

Optical Fiber Demand to Continue to Outpace Supply

Over the last two years, telecom operators (both wireless and fixed) across developed and developing countries ramped up consumption of optical fiber cable for capacity expansion in telecom network, in response to high data demand from consumers. According to International Cablemakers Federation (ICF), this resulted in a worldwide fiber shortage starting early 2016, which led to increase in optical fiber prices and elongation in delivery times from months into quarters.

Over the last 1.5 years, spot prices for OF have moved from close to US$7.0 per fKm to US$12.0 per fKm. On the other hand, larger vendors like Corning and Prysmian have started booking firm orders for 2018–19 delivery. While this scarcity has resulted in announcement of greenfield plants from manufacturers, we remain positive on the pricing scenario and do not expect a supply glut to develop in the market due to continued demand across the world.

Optical Fiber Cable Demand - Global (mn fKm)



Source: Company data, CRU, HTI estimates

Our optical fiber cable model suggest that OFC demand would increase by around 150mn fKm between 2017–20, primarily due to the demand from US and developing economies in the early years and China towards the later part of the period. On the other hand, industry reports indicate incremental supply between 100–150mn fKm coming over the next two years. Hence, we believe that the demand/supply situation over the next 2–3 years would at best stabilize. Given the current demand supply mismatch, this should continue to keep the end market favorable for the manufacturers, including Sterlite Tech.

While comments from optical fiber manufacturers signal a significant addition to their capacity, major announcement of network expansion by either companies or national entities should absorb additional supply.

Capacity Expansion Plans - Major Optical Fiber Manufacturers

Company	Capacity additions
Corning	Announced plans to spend $250mn to expand optical fiber capacity. Recieved order in Apr-17 worth $1bn from Verizon to supply 20mn fKm/yr for 3 years.
Sterlite Technologies	Setting up a Greenfield factory to increase its Optical Fiber capacity from 30mn fKm to 50mn fKm by June-2019, through an investment of Rs12bn (c.$185mn).
Furukawa Electric	Announced plans to nearly double its 2016 optical fiber manufacturing capacity by 2019 and to increase its optical fiber cable manufacturing capacity as well.
Shin-Etsu Chemical	Expanding global production capacity of optical fiber ingot (preform) by investing a total of ¥18 billion (c.$160mn).
Prysmian	3yr €250mn (c.$300mn) expansion plan to increase production capacity for fibre and cable. Recently received order from Verizon worth $300mn to supply optical fiber cable.

Source: Company data

Comments on Capex Plans from Major Customers

Country	Demand scenario
US	- Verizon has committed long term contracts with Corning and Prysmian for optical fiber cable and associated equipment worth $1.3bn over next three years, including over 75mn fKm of OFC - AT&T announced 5G evolution plan, with plan to reach 14mn locations (from 7mn currently) with 100% fiber networks by mid-2019
China	- China announced a 3-yr action plan for major constructions of information infrastructure in Jan-17, with 92 new information infrastructure projects, involving total investment amount of RMB1.2 trillion, during 2016 to 2018 - It is also expected to invest clsoe to $400bn in 5G deployment during 2020-30
Germany	- Germany is investing €100bn into national gigabit internet network, as part of common EU broadband targets for 2025 - EWE and Deutsche Telekom are planning a €2bn project to improve fiber-optic broadband provision in Germany, starting in mid-2018
India	- India is spending over $6bn to connect cities and villages across the country as part of BharatNet project, and has also announced plans on smart cities - Airtel has an ongoing plan to deploy 550k of OFC and is spending c.$4bn in FY18 to expand 4G mobile broadband network along with fibre connectivity and backhaul - Reliance Jio is in process to launch optical fibre based home broadband services under the name of 'Jio Fibre', and is currently testing the network along with trial offers in major cities.
Japan	- The first live 5G networks are expected to come on stream in parts of Tokyo and other select areas ahead of the 2020 Tokyo Olympics and Paralympics - Japanese Telecom cos to invest USD 46bn into delivering nationwide 5G coverage in 2023
South Korea	- South Korea will pump 1.6 trillion won (USD1.49b) through 2020 with local firms to build the (5G) in the country

Source: Company data, Media quotes

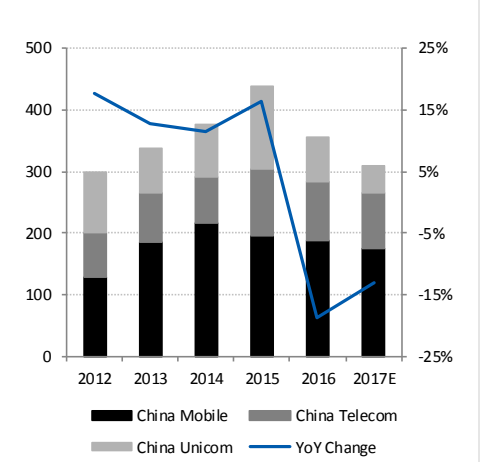
China Demand a Concern Among Investors, but Recent Trends not Ominous

China currently accounts for over 55% of OFC usage in the world, and is expected to consume over 260mn fKm in 2017. The country has gone through a major buildup over the last five years, consuming almost 900mn fKm of OFC by itself. This expansion has happened due to major deployment of both 4G (910mn users by July 2017) and mass FTTX deployment. This has given rise to the concern that a slowdown in consumption in the China would be negative for the demand side of the equation.

While we see a merit in the concern, we believe that the fear of a decline in consumption is exaggerated, as the country continues to spend to cater to data demand. According to YOFC management, demand for optical fiber in 2018 should remain at least at the same level as in 2017. Moreover, the country has recently launched a 3-year action plan for

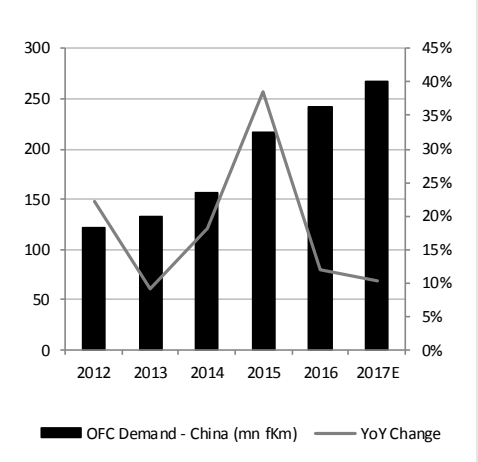
major constructions of information infrastructure, which should help maintain demand for OFC. Our analysis of the telecom spending in recent years indicates that while the telecom capex saw a major correction in 2016–17, the consumption of OFC remained in the positive territory. Despite this, we have assumed no growth in China in 2018 and only 5% in 2019 to keep our estimates conservative.

Telecom Capex in China



Source: Company data, HTI estimates

OFC Demand - China

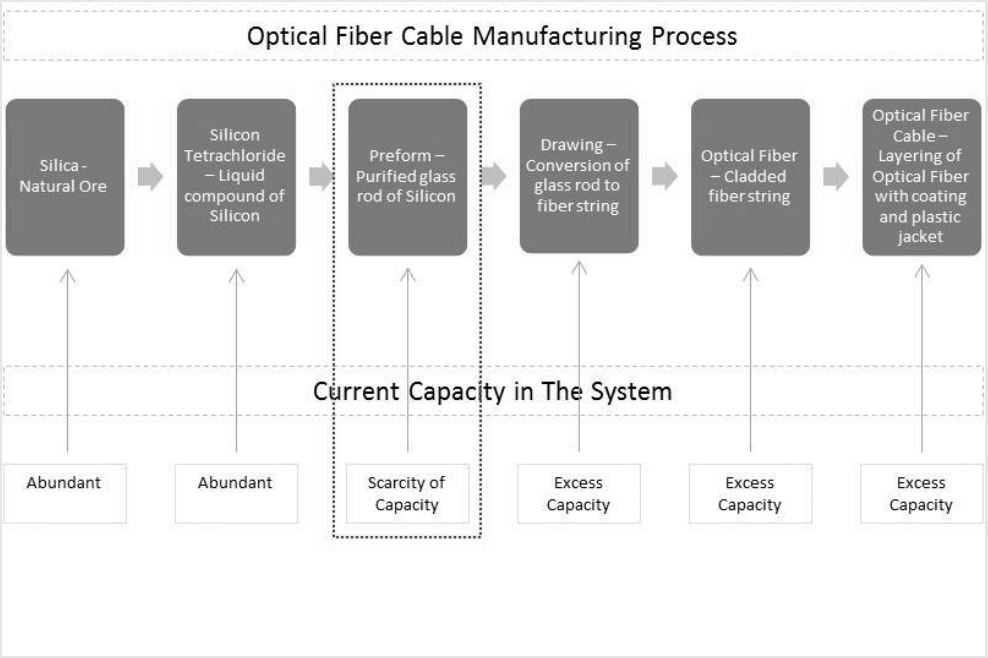


Source: Company data, CRU

Preform is the Main Bottleneck in the OFC Supply Chain

Our analysis of optical fiber industry suggests that the key bottleneck in increasing availability of OFC is preform, which is an interim product between raw silica and optical fiber. While there is sufficient capacity of raw material and excess capacity of drawing, cladding (made from plastics) and cabling processes, the preform stage is controlled by a group of 7–8 suppliers (including Corning, Sterlite Tech, Prysmian, Shin-Etsu Chemical etc.) which benefit from any mismatch in demand/supply of optical fiber.

Optical Fiber Manufacturing Process



Source: Company data, ICF, Wikipedia

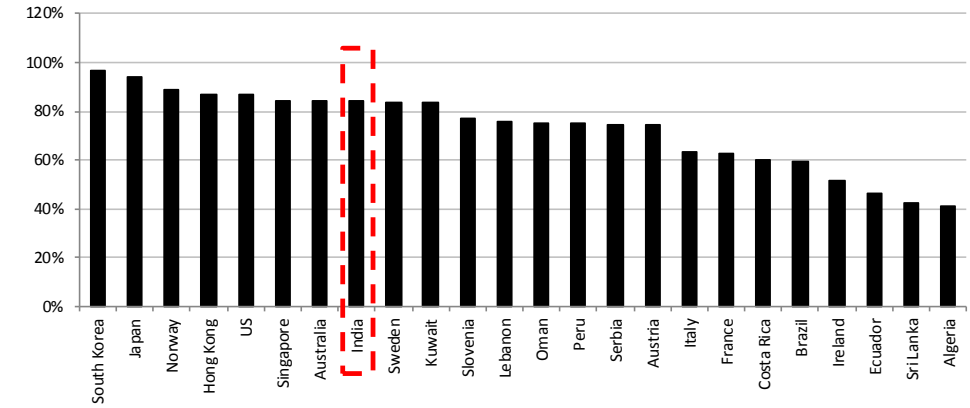
India Remains a Major Opportunity

India is the largest market for Sterlite Technologies and contributed over 63% of the company's revenues for in FY3/17. Within India, public sector (including PSUs) contributed 14% to direct revenues, while private sector was almost half of total revenues. Sterlite is the premium player in India for both optical fiber (40–45% market share) and optical fiber cable (30–40% market share). In addition, Sterlite also offers system implementation and software sales (20% of total revenues) to its core telco and public sector customers, benefitting from its visibility into their new spending decisions and preference for an integrated product and service contract.

Open Signal analysis of global LTE performance suggests that while India performed well on signal availability, it was at the bottom of the sample when it came to speed.

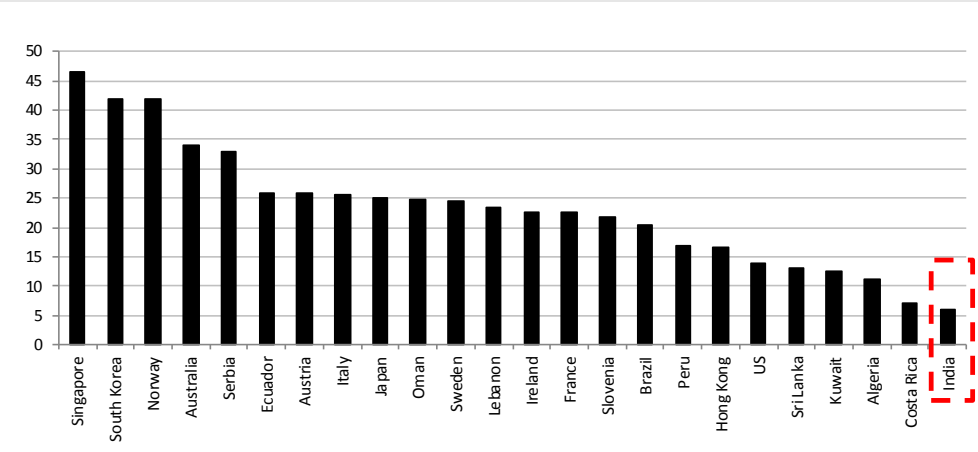
With an explosion in data happening in India over the last one year (monthly data consumption increasing by 9x YoY according to Internet Trends 2017 report), we see high potential for optical fiber deployment in the country. An increase in data flow through telecom networks is usually associated with a corresponding increase in the deployment of fiber across telecom towers owing to its capacity to handle very high volumes of data. But, most of the wireless data in India telco backhaul networks is still transported using microwave, which have limitations in terms of data capacity and distance. This has resulted in a reduction in speed and quality of wireless data transmission, as is evident in a comparison of LTE signals conducted by Open Signal, where India performed well on signal availability, but was at the bottom of the sample when it came to speed.

4G Availability Comparison



Source: OpenSignal State of LTE – Nov-17

4G Speed Comparison

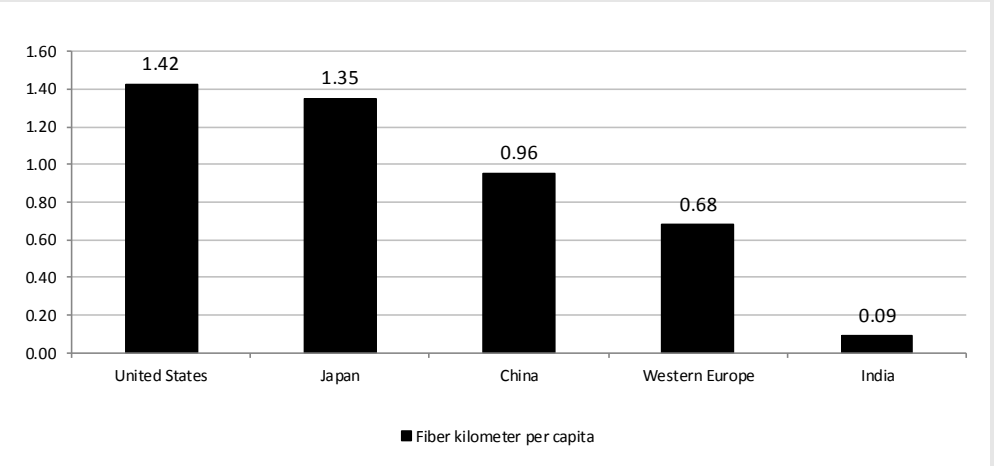


Source: OpenSignal State of LTE – Nov-17

Deloitte's analysis of Indian tower operators suggests that the fiberization of telecom towers is still around 20%. We see this penetration as sub-optimal and expect the telecom companies to spend heavily on fiber and accompanying optical network to catch up with demand. According to E&Y estimates, heavy data traffic in telecom networks requires fiberization of one in every two sites in India over the next three to four years. For reference, in 2013 China's spend was five times the corresponding spending on optical equipment by Indian telecoms last year, despite an equivalent data subscriber base.

Fiber deployment in India is still below 0.1km/capita, much below developing peers like China (around 1km/capita) and developed markets like US (1.4km/capita)

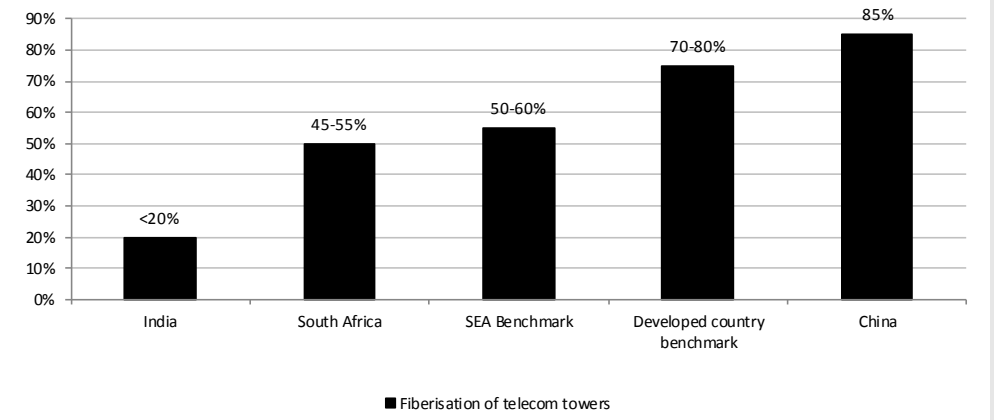
Fiber Kilometer Per Capita



Source: Company data, CRU

Fiberization of Telecom Towers – India versus ROW

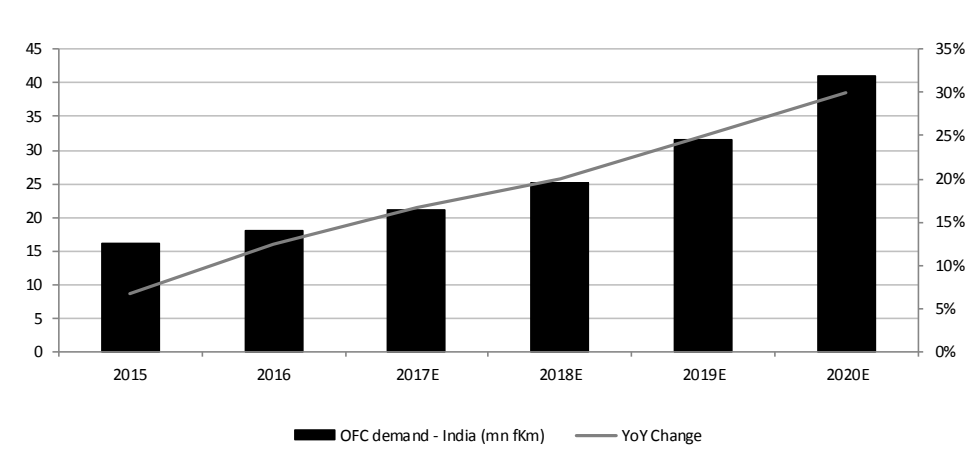
According to both Deloitte and E&Y estimates, fiber usage in telecom backhaul is still less than 20%, while microwave has a 50% share of India's backhaul networks



Source: Company data, Deloitte

This gap is now also being noticed by large telecom operators and industry experts, leading to investment in networks capable enough to handle the data traffic. We see this as a multi-year trend, with telecom operators continuously spending on upgrading their backhaul transport capacity to manage data traffic. We expect this to result in significant pick-up in growth of OFC in India, which should benefit Sterlite as it is the largest player in the domestic market and the only company which has preform manufacturing capability in India.

Optical Fiber Cable Demand - India (mn fKm)



Source: Company data, CRU, HTI estimates

Tapping Digital India Initiative through BharatNet

India's government launched its Digital India initiative in 2014, with the aim of connecting both rural and urban populations to greater information flow and government schemes. As part of this initiative, it launched the BharatNet program to connect all rural and urban district centers via high speed optical fiber links. One of the key requirements for supplying equipment for BharatNet is that it is designed, developed and manufactured in India. BharatNet aims to connect 250,000 Gram Panchayats (GP, local self-government bodies in villages or smaller towns in India) through 100 Mbps connectivity. The project is being implemented with the help of three central public sector undertakings (PSU), Bharat Sanchar Nigam Limited (unlisted), PowerGrid Corporation of India (PWGR IN) and Railtel India (unlisted), and monitored by an especially created entity, Bharat Broadband Network Limited (BBNL; unlisted).

BharatNet implementation is planned in three phases, with collaboration between central and state governments. The three phases of the BharatNet project are as follows.

- **Phase 1:** Under the first phase, 100,000 GPs are to be provided with broadband connectivity through underground optical fiber cables. This phase is already near completion, with supply of OFC done over the last two years. Commentary from Sterlite management suggests that it contributed close to 45% of total fiber in Phase 1, with a mix of direct and indirect sales.

- **Phase 2:** During this phase, a further 150,000 GPs are to be provided with broadband connectivity using a mix of underground fiber, fiber over power lines, radio and satellite media. According to industry report, the bidding for Phase 2 is expected to happen in early 2018. The total budget for implementation of Phase 2 is Rs187.9bn, about 1.7x the cost of Phase 1.

- **Phase 3:** In the third phase from 2018 to 2023, the network is to be expanded to urban centers, with fiber deployment between districts using a ring topology structure to provide greater redundancy.

BharatNet project is estimated by the government to be worth Rs421bn, and is likely to be completed only by 2023; according to government data, Phase 1 and 2 would require deployment of 1mn km of optical fiber cable, with 24–48 fibers per cable

Status of BharatNet - 17 December 2017

Description of Work	Status
OFC Pipe laid	2,56,582 Kms (1,12,464 GPs)
Optical Fibre laid	2,50,197 Kms (1,06,585 GPs)
Tenders Finalized	3334 Blocks / 1,24,757 GPs
Work Started	3268 Blocks / 1,22,219 GPs
Current Weekly performance of Optical Fibre laying	1964Kms
Current Weekly performance of OFC Pipe laying	839 Kms
Optical Fibre Cable Delivered on site	3,14,629 Kms
Service Ready GPs	87,836GPs

Source: bbni.nic.in

Upcoming Phase 2 Deployment Still Not Baked in Numbers

While Phase 1 optical fiber deployment for Bharatnet is already over, Phase 2 is expected to come out over next few months. While we do not expect Sterlite to win a big share of Phase 2 OFC bid (Phase 1 share of 15%) due to the presence of numerous smaller peers who only operate in the low margin OFC space, it should continue to dominate the more lucrative optical fiber space (45% share in Phase 1).

Moreover, while the Phase 1 opportunity in terms of volume was close to 7.5mn fKm (assuming 300k km of cable delivered in Phase 1), our analysis of government plans for Phase 2 suggests that the opportunity is over 3.5x for optical fiber manufacturers without taking into account the price increase which has happened in the last two years. This is primarily on account of a mixture of 2.3x in distance coverage as well as higher fiber count requirement per OFC in Phase 2 deployment.

BharatNet Phase 2 Opportunity Size

Phase 2 Opportunity Size	Value
Bharatnet phase 2 project size (Rs mn)	230,000
OFC order size (HTI estimate based on phase 1, Rs mn)	25,091
Total OFC to be deployed (in Km)	689,568
Total OFC to be deployed (HTI estimates, in mn fKm)	26.5
Revenue opportunity for Sterlite Tech (assuming 40% share, Rs mn)	11,704

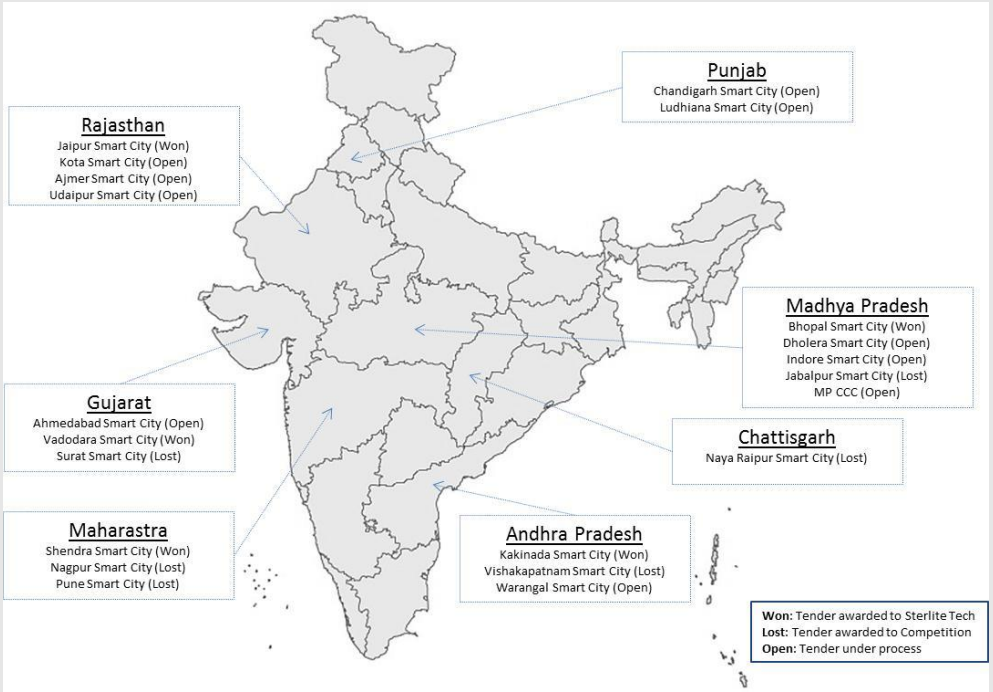
Source: bbni.nic.in

While we believe that a portion of this is already baked into the current valuation of Sterlite, primarily the distance to be covered and the higher fiber count is not into either the share price or our estimates, and can provide an additional upside on confirmation of technical specifications.

Smart City Opportunity in India Still Partially Tapped

The government of India launched its Smart Cities Mission (SCM) in 2015, where it envisioned applying digital solutions to infrastructure and services in selected cities. The services included in smart cities include intelligent transport management system, public Wifi, smart street lighting etc. Sterlite has participated in the SCM and secured 4 projects (implemented under its services business segment). While there is limited visibility of the timeline of ordering due to control being with local municipalities, this can act as incremental growth drivers for Sterlite Tech.

Smart City Opportunities



Source: Company data

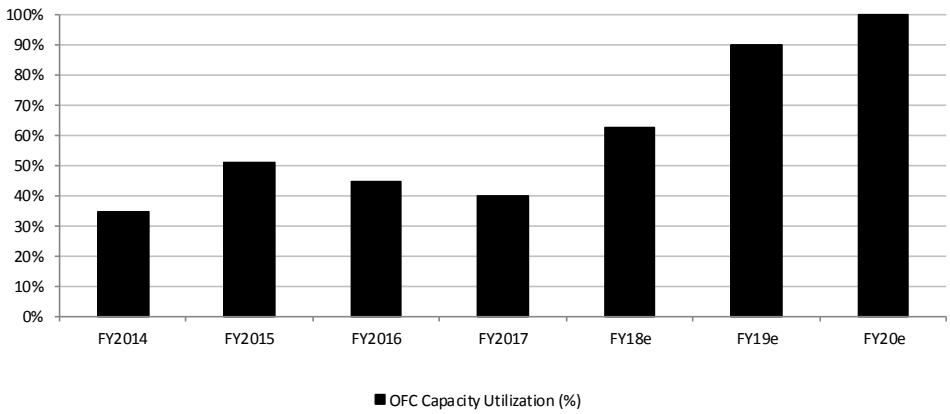
OFC Capacity Expansion on Higher India Demand Could Provide Further Upside

Sterlite has 15mn fKm of OFC capacity currently, compared to 30mn fKm of capacity, which would increase to 50mn fKm in 2 years. While the company is currently operating OF capacity at 100% utilization due to the high demand/supply gap in global markets, its OFC capacity is underutilized (60% utilization in Q2 FY3/18) due to its predominant dependence on low volume Indian market (30–40% market share in last 2 years).

We believe that there is a high likelihood of a change in this scenario in next 1–2 years, when a demand from Indian telcos and Bharatnet would come in and lead to a significant increase in overall size of the market. While we have currently not assumed any upside from this in our calculations for Sterlite and expect the company to reach 100% utilization in FY3/20 as per the guidance, we see this as an upside to both our estimates and target price.

For example, if we do a back of the envelop calculation of an increase of 50% in Sterlite's OFC capacity to 22.5mn fKm (55% of our current demand estimate for India) in FY3/20, our revenue CAGR for next three years increases by 7% and our target price increase by 16%.

OFC Capacity Utilization (%)

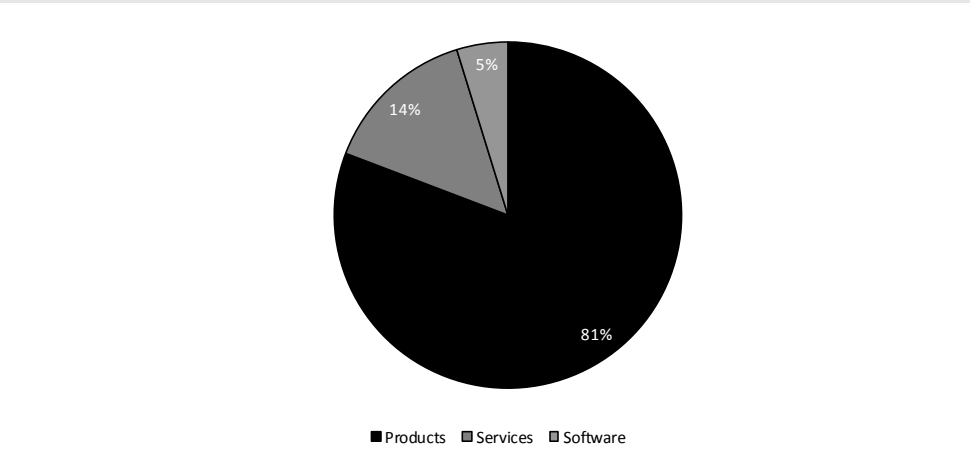


Source: Company data, HTI estimates

Business Overview

Sterlite Tech operates in three key business segments: a) optical fiber products (OF and OFC), b) services (telecom implementation and smart cities services) and c) software (Elitecore Technologies, acquired in September 2015, focused on telecom software). While a majority of Sterlite's revenue comes from optical fiber business (around 80% in FY3/17), services business is the larger of the other two segments.

Revenue Breakup – FY3/17



Source: Company data

In terms of profitability, optical fiber business is the most profitable with margins generally close to 30%, while optical fiber cable OPM are generally around 15–20% (depending on plant utilization). On the other hand, the services and software business of Sterlite have between 11–13% OPM, with aspiration to take them to 15% in a few years.

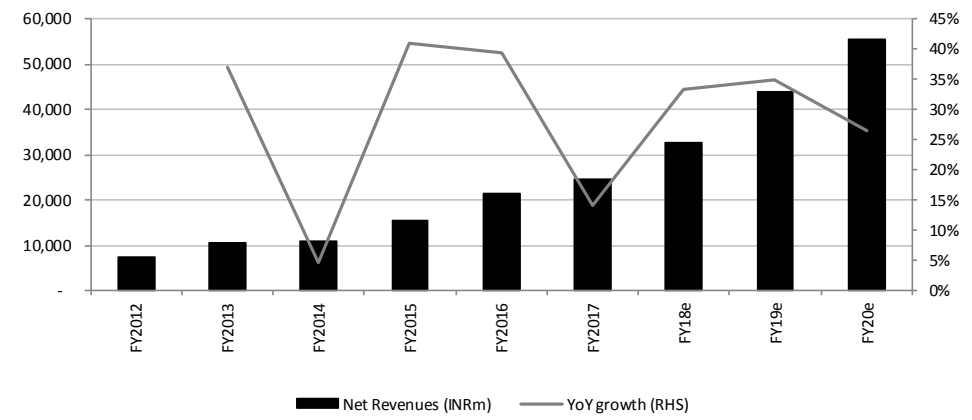
Within the optical fiber products business, we estimate optical fiber to contribute close to 60% of revenues and 67% of OPM due to its higher profitability. Sterlite Tech also has two subsidiaries (one each in China and Brazil), with its Chinese subsidiary (Jiangsu Sterlite and Tongguang Fiber Co. (unlisted) contributing 15% (as of FY3/17) to its product business revenues.

Sterlite Technology went through a demerger of its power business in mid-2016, and hence the company's detailed financials prior to FY3/16 are not comparable to current business.

Financials

We forecast 32% revenue CAGR over FY3/18–20. We expect this growth to come from higher than past orders of Sterlite's optical fiber and optical fiber cable business as we expect demand to stay strong due to higher demand from telecom companies. Moreover, we see sustained growth in Sterlite's services and software segments on the back of a healthy order book of Rs38.0bn and recent orders secured by Elitecore (unlisted) (including from BSNL (unlisted).

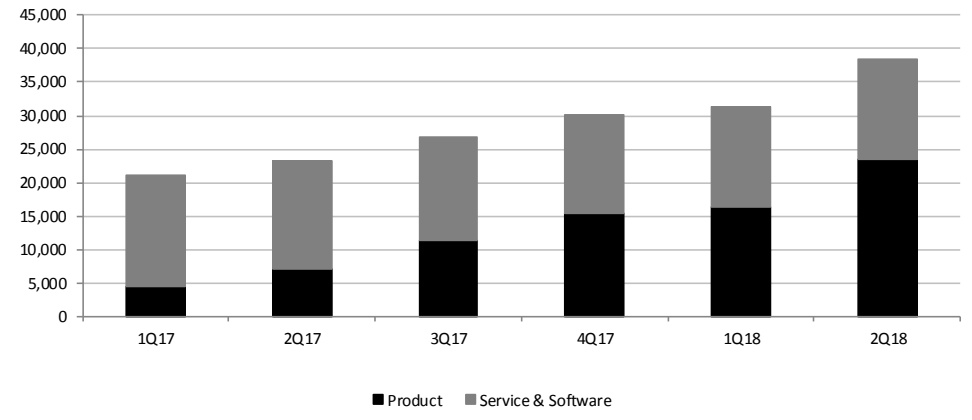
Revenue and Revenue Growth*



Source: Company data, HTI estimates, *Note: Revenue for FY12-15 are of Sterlite's Telecom business

Sterlite Technology has maintained a healthy order book (book to bill in Q2 FY3/18 of 1.6x FY3/17 revenues), with stable order book in services and software segment complemented by high growth in product segment (reflecting an increase in long duration deliveries of optical fiber).

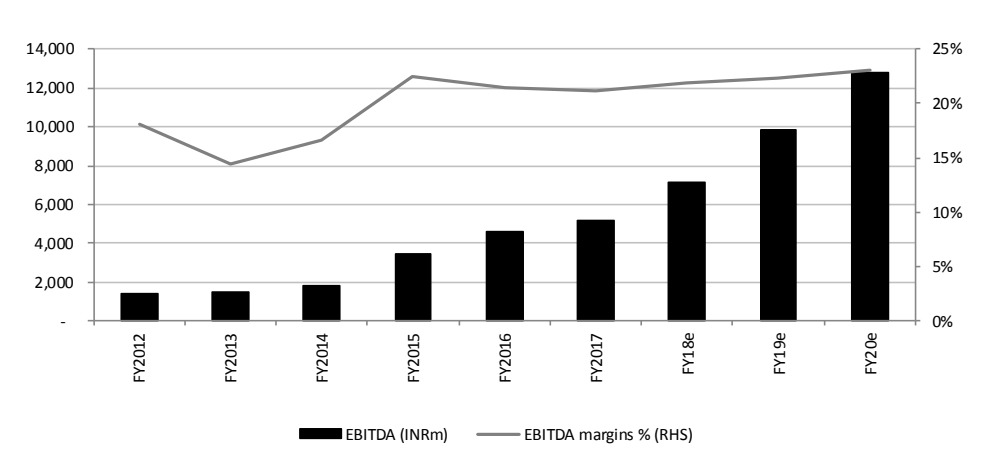
Sterlite Tech Order Book (Rs mn)



Source: Company data

We expect a pickup in OPM for Sterlite Technologies over the next few years as high revenue growth is supported by stable costs along with benefit from higher utilization of optical fiber cable business. We estimate 185bps increase in operating EBITDA margin over our forecast period.

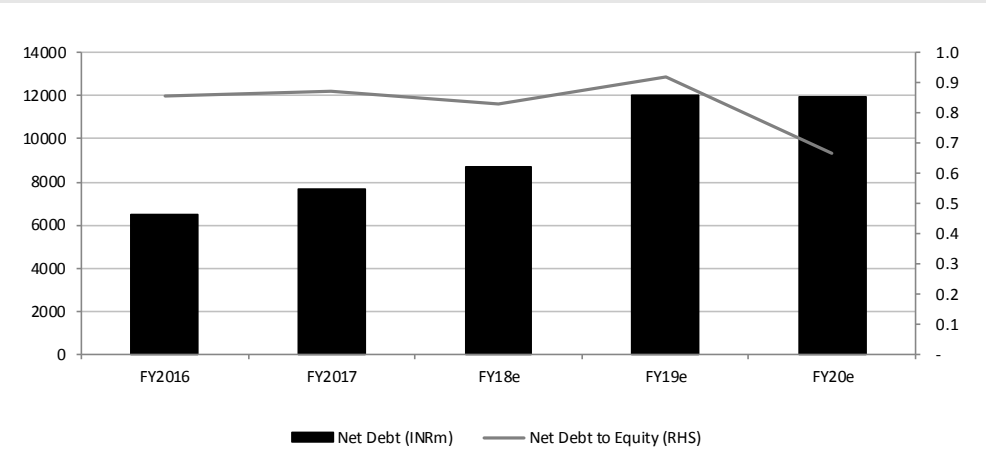
EBITDA margins*



Source: Company data, HTI estimates, *Note: EBITDA for FY12-15 are of Sterlite's Telecom business

Sterlite is currently doing optical fiber (OF) capacity expansion from current 28m fKM to 50m fKm by FY3/20. Management has guided for capex of Rs12bn over FY3/18–20. We expect this capex to be in a combination of incremental debt and internal accruals. But, due to high growth, Sterlite's cash generation would result in a decline of net debt and hence our net debt to equity is suppressed for the forecast period.

Net Debt to Equity

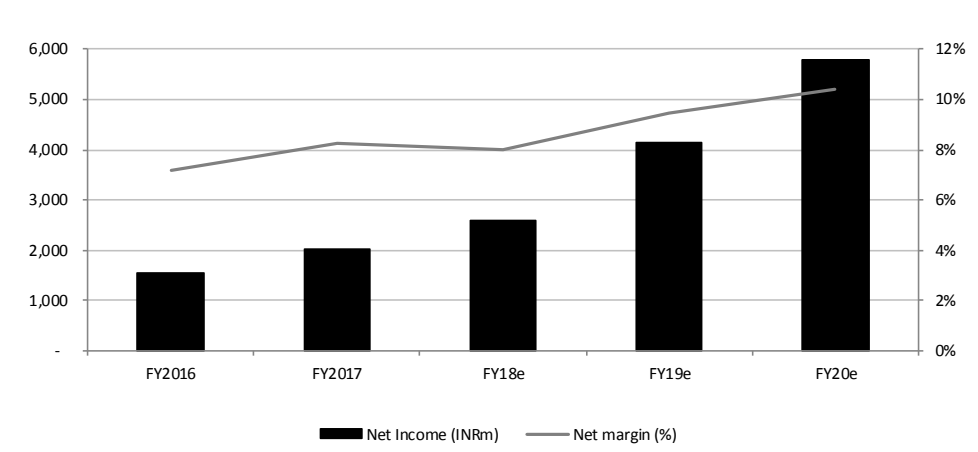


Source: Company data, HTI estimates

Net Income Target of FY3/20 Too Optimistic on Current Scenario

Sterlite Tech has provided a FY3/20 earnings target of US$100mn, highlighting the 3x growth in net income from FY3/17 earnings of Rs2bn (US$31mn). While we see strong growth in Sterlite Tech earnings over next three years (42% CAGR over FY3/18–20), we believe that the company would miss the guidance in the current scenario by about 14%. Our analysis suggests an FY3/20 base case net income of Rs5.7bn or US$88mn. While we see multiple upside scenarios for this number, we do not believe that the share price is factoring in the US$100mn guidance.

Sterlite Tech Net Income



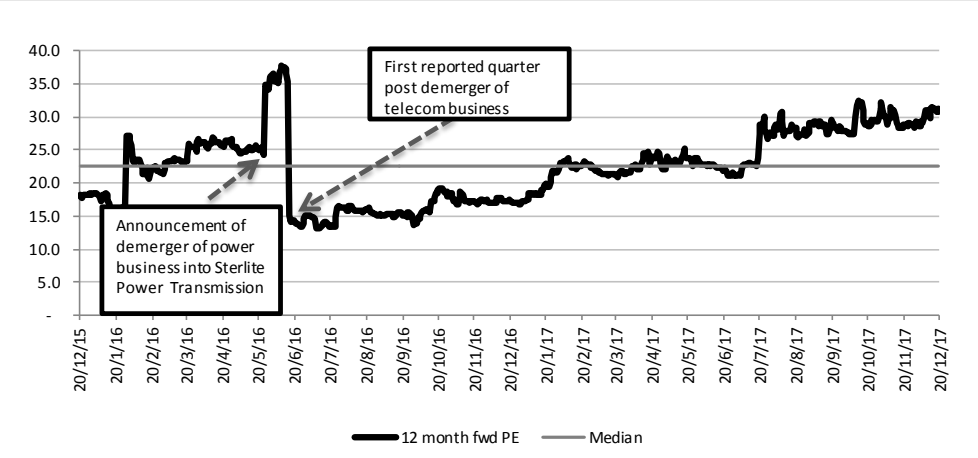
Source: Company data, HTI estimates

Valuations

Our target price of Rs400 is based on a PER of 28x applied to our FY3/20 EPS estimates, which is one standard deviation above its median 12-month forward PER of the last two years (primarily covering the ex-power business period) for the company to factor in improved business environment. While the stock has seen handsome returns in last one year, we believe that it is still not completely factoring in the high double-digit growth over the next three years. Our price target implies 17% upside from last close. We therefore initiate coverage with a BUY rating.

Our comparable analysis of Sterlite's global peer group suggests an FY20 PER median of 14x, but it is factoring in significantly lower growth and median EBITDA margin (12.8% versus Sterlite Tech's EBITDA margin estimate of 23.0%). We note that Sterlite Tech's global peer group is trading at a median 1.6x PEG ratio (PER to earnings growth) on Factset consensus estimate versus Sterlite Tech's PEG of 0.8x.

12-month forward PE chart



Source: Company data, Bloomberg

Risks to Our Rating and to the Attainment of Our Target Price

The following are the main risks to our BUY rating and our target price:

1) **Oversupply in global Optical Fiber market** – While we believe that demand in global market for optical fiber would be able to absorb the incremental supply over the next two years, lower demand than we currently expect would result in a reduction in realization in Sterlite's optical fiber business.

2) **China demand declining from current level** – China is the largest customer of optical fiber cable in the world and any decline in the market demand would negatively impact pricing of optical fiber.

3) **Delay in 5G rollout across major geographies** – 5G rollout from 2019–20 onwards would a big driver of telco spending on optical fiber. A delay in 5G rollout plan would negatively impact demand.

4) **Slackening of pace in Digital India projects –** Sterlite has benefitted from Digital India initiatives like Bharatnet and Smart Cities. A slowdown in ordering process would negatively impact revenue growth.

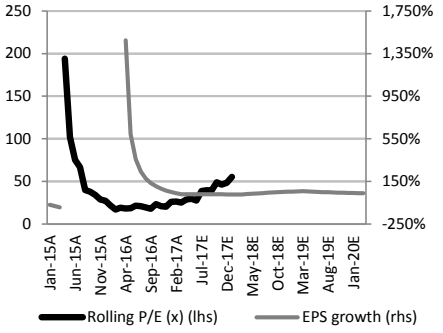
Peer Comparison Table as of 05 January 2018

Company	Price	Market Cap (USD Mn)	P/E (x)		EV/EBITDA(x)		Revenue growth (USD)		EBITDA Margin		PEG ratio
			2018E	2019E	2018E	2019E	2018E	2019E	2018E	2019E	2016-19E
Developed Market Peers											
Corning	$33.8	29,339	18.6	16.7	11.4	11.1	2.5%	6.2%	30.6%	29.6%	3.5
Prysmian S.p.A.	€ 28.3	7,425	16.1	13.8	9.3	8.4	4.8%	3.7%	9.8%	10.5%	1.6
Furukawa Electric Co.	¥5,900	3,682	13.5	11.3	8.3	7.4	4.3%	4.5%	8.2%	8.7%	1.6
Sumitomo Electric Industries	¥1,954	13,698	11.7	10.9	5.9	5.6	3.4%	2.9%	11.2%	11.5%	2.3
Fujikura Ltd	¥1,058	2,765	12.8	11.7	7.1	6.6	4.6%	1.1%	9.8%	10.4%	1.9
Shin-Etsu Chemical Co	¥12,175	46,464	19.7	17.8	8.6	7.9	7.3%	5.2%	32.9%	34.3%	2.2
Chinese Peers											
Yangtze Optical Fibre and Cable	HKD 37.9	1,702	14.6	12.9	11.7	10.2	15.2%	9.5%	16.2%	17.0%	0.7
Fiberhome	¥29.9	5,129	26.2	20.6	18.1	14.7	24.0%	23.0%	7.3%	7.4%	0.8
Jiangsu Hengtong Photoelectric	¥41.9	8,777	18.3	14.8	15.2	13.3	20.7%	14.9%	14.2%	14.1%	0.6
Sterlite Technologies	**INR 341**	**2,154**	**33.4**	**23.9**	**15.0**	**11.5**	**34.0%**	**26.4%**	**22.4%**	**23.0%**	**0.8**
Global Median			**17.2**	**14.3**	**10.3**	**9.3**	**6.1%**	**5.7%**	**12.7%**	**12.8%**	**1.6**

* Sterlite Technologies and its Japanese peers calculations on FY basis (CY17=FY18). The numbers represented here are for CY.

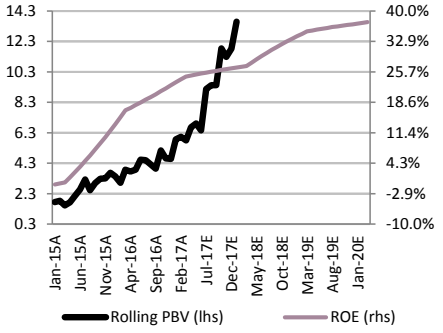
Source: Company data, Factset, HTI estimates

P/E (x) vs EPS Growth (%)



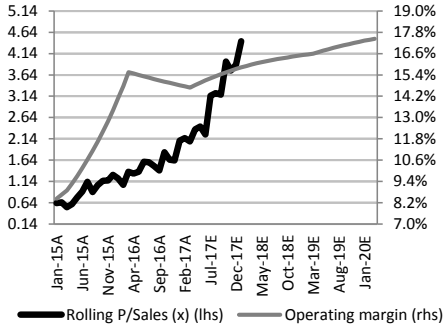
Source: Company data, Bloomberg, HTI estimates

P/B (x) vs ROE



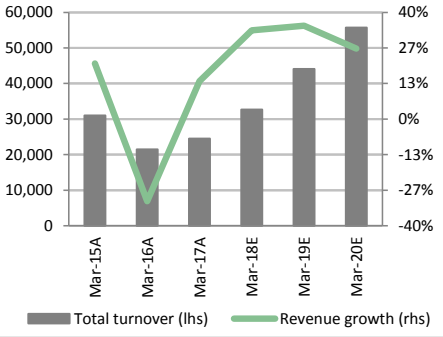
Source: Company data, Bloomberg, HTI estimates

PSR (x) vs OPM (%)



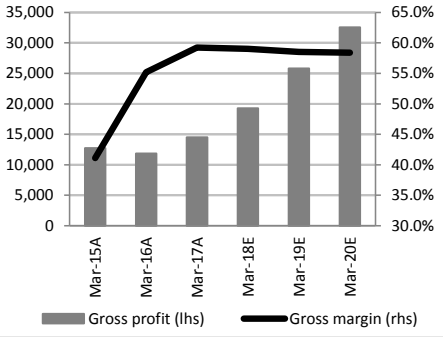
Source: Company data, Bloomberg, HTI estimates

Turnover and Growth



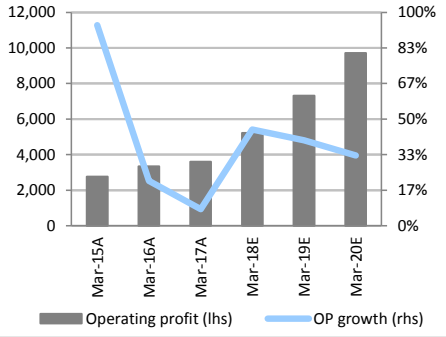
Source: Company data, Bloomberg, HTI estimates

Gross Profit and Margin



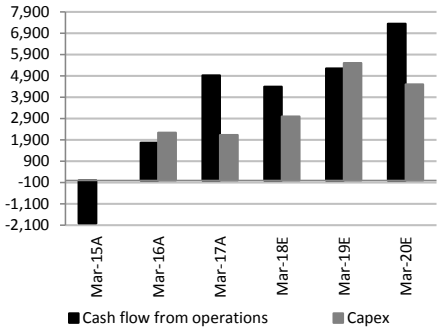
Source: Company data, Bloomberg, HTI estimates

Operating Profit and OP Growth



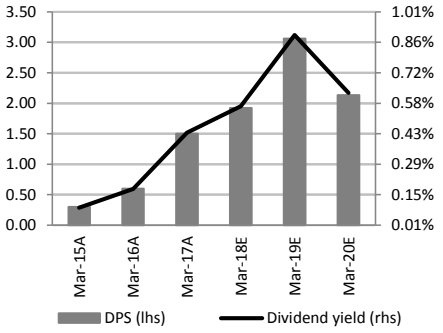
Source: Company data, Bloomberg, HTI estimates

CF from operations vs Capex (Rsm)



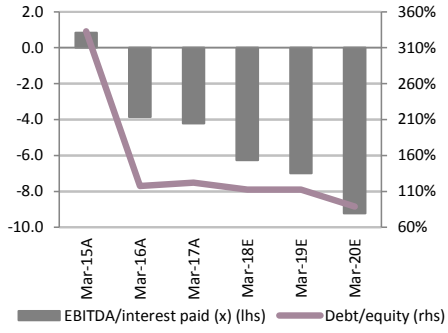
Source: Company data, Bloomberg, HTI estimates

Dividend Payout and Yield (Rs)



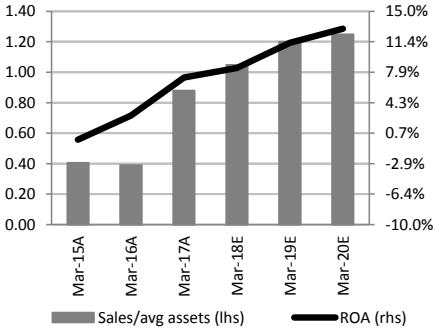
Source: Company data, Bloomberg, HTI estimates

Debt to Equity (%) and Interest Cover (x)



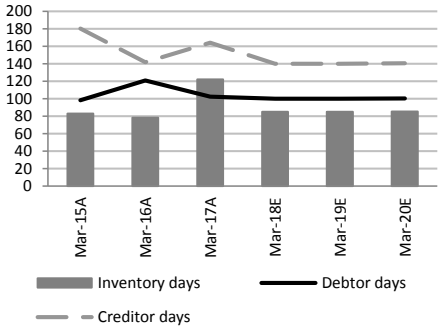
Source: Company data, Bloomberg, HTI estimates

ROA (%) and Asset Turnover (x)



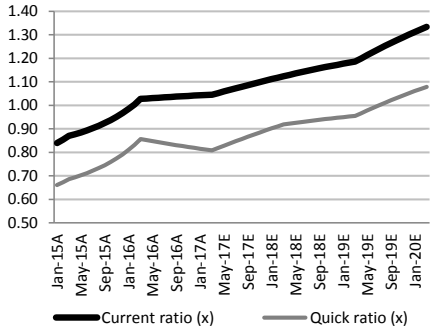
Source: Company data, Bloomberg, HTI estimates

Cash Operating Cycle



Source: Company data, Bloomberg, HTI estimates

Current Ratio (x) vs Quick Ratio (x)



Source: Company data, Bloomberg, HTI estimates

Revenue Growth

We forecast 32% revenue CAGR over FY3/18–20. We expect this growth to come from expansion in optical fiber capacity and high demand for optical fiber cable business.

Profit Margins

We expect pickup in EBITDA margin for Sterlite Technologies over the next few years due to better utilization in optical fiber cable business.

Shareholder Returns

We expect Sterlite's ROE to improve from hereon as high revenue growth with pickup in EBITDA margin should lead to solid earnings growth over FY3/18–20 and hence improving return ratios. Thus, we forecast ROE to improve from 24.6% in FY3/17 to 37% in FY3/20.

Balance Sheet Risks

Sterlite Technologies is engaged in a business which requires high capex to build capacity. Its net debt to equity for FY3/17 was 1 and the company's guidance is to maintain average net debt to equity around 1 over FY3/18–20.

✓ Key Takeaway

We see Sterlite's optical fiber business as a beneficiary of telecom operators' increased spends across the world to manage data traffic, which should help it report 32% revenue CAGR over FY3/18–20

Investment Thesis – Target Price – Share Price Catalysts

We see Sterlite's optical fiber business (80% of FY3/17 revenues) as a beneficiary of ongoing accelerated spend by telecom operators across the world to manage fast growing data traffic. With high telco demand and a global capacity constraint, Sterlite is witnessing both an increase in optical fiber prices and longer-dated purchase commitments. In addition, Sterlite's presence among a small group of integrated suppliers has helped it keep costs under control and increase capacity. We expect Sterlite to report 32% revenue CAGR over FY3/18–20, benefitting from optical fiber capacity expansion (to 8% of global market share). Operating EBITDA margin should expand by 185bps during FY3/18–20 due to better utilization in optical fiber cable segment, leading to earnings CAGR of 42% over the same period. We also see potential upside to our estimates from Bharatnet (due to adoption of more advanced fiber) and optical fiber cable capacity expansion as local telco investment picks up. Our target price of Rs400 is based on a PER of 28x applied to our FY3/20 EPS estimate of Rs14.23. We see Phase 2 bidding in Bharatnet and order inflow from domestic telecom operators as the biggest catalysts for shares.

APPENDIX

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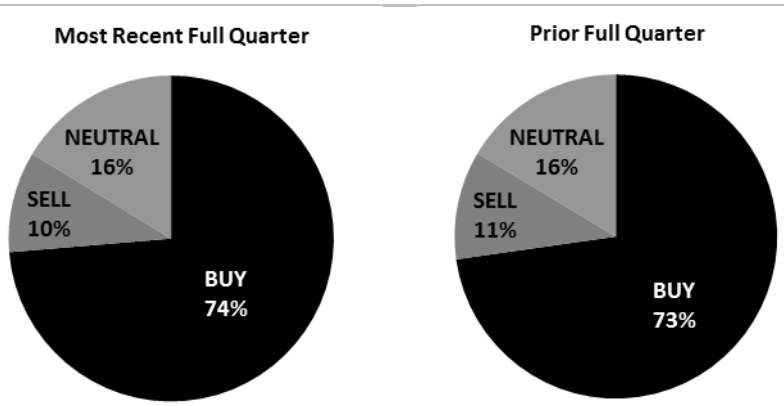
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Recommendation Chart



Date	Recommendation	Target (Rs)	Price (Rs)
2018-01-08			

Source: Company data Bloomberg, HTI estimates

Definitions for Key Investment Metrics

Business Growth

This is the metric which matches the top line in our report.

Business profit

This is the metric which best represents operating profit in our report

Shareholder Returns

Return on Equity

Balance Sheet Risk

Net Debt to Equity