

# Sterlite Technologies Ltd - BUY

## Robust performance

Sterlite Technologies Ltd (STL) reported strong topline performance during Q1 FY20 with consolidated revenue growing 63% yoy (to Rs.14.3 bn) driven by higher traction in both, products and services businesses. However, the improving contribution from relatively lower margin services business has translated into some moderation of operating profit growth (up 32% yoy). The Order book remained at elevated levels of Rs.98.5bn (~2x FY19 revenues). Currently, the company is in-expansion mode wherein large part of its optic fiber (OF) capacity is getting commissioned in-phases (to reach total 50mn fkm capacity), which will aid faster execution of elevated order book position. In the global markets, the optic fiber prices have come off sharply from the highs, but the margins for STL have been relatively stable with its negligible presence in spot market. With the services business now forming bigger portion of the overall business, operating margins are likely to stabilize at 18-20% levels over the next couple of years.

Going forward, STL is significantly banking on the increasing demand for high-speed data across the globe. The strengthening of network with fiber is therefore critical. Additionally, projects like Governments BharatNet and smart city development are adding to the demand. With the increased capacity in place and integrated business model, STL is better placed than some of its peers. The increasing penetration in services and software segment has enhanced the industry size multifold. We assign a Buy on the stock with the target price of Rs.193 (10x FY21 EPS).

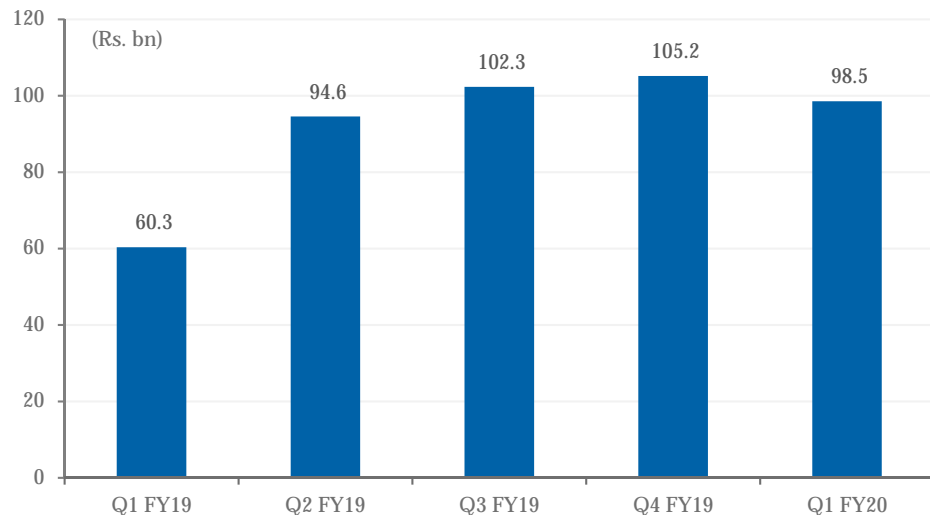
<b>CMP (Rs) 163</b>		<b>12-mts Target (Rs) 193</b>	<b>Upside 18%</b>
<b>Stock data</b> (As on July 18, 2019)		<b>Sector: Diversified</b>	
Sensex:	38,897	<b>Stock performance</b> 	
52 Week h/l (Rs)	399/144		
Market cap (Rs mn)	65,616		
Enterprise value (Rs mn)	76,660		
6m Avg t/o (Rs mn):	525.3		
FV (Rs):	2		
Div yield (%):	2.1		
Bloomberg code:	SOTL IN		
BSE code:	532374		
NSE code:	STRTECH		
<b>Shareholding pattern</b> (As of Mar'19 end)			
Promoter	53.8%		
FII+DII	16.8%		
Others	29.4%		

## Exhibit 1: Result table (Consolidated)

Y/e 31 Mar (Rs mn)	Q1 FY20	Q1 FY19	yoy(%)	Q4 FY19	qoq (%)
<b>Revenue</b>	<b>14,320</b>	<b>8,769</b>	<b>63.3</b>	<b>17,912</b>	<b>(20.1)</b>
<b>Operating Profit</b>	<b>3,234</b>	<b>2,449</b>	<b>32.1</b>	<b>3,151</b>	<b>2.6</b>
OPM (%)	22.6	27.9	-534 bps	17.6	499 bps
Other Income	87	73	20.6	132	(33.8)
Depreciation	(683)	(448)	52.6	(498)	37.3
Interest	(463)	(231)	100.8	(307)	50.9
Exceptional item	(13)	(10)	33.7	(25)	(47.0)
PBT	2,162	1,833	17.9	2,453	(11.9)
Tax	(733)	(548)	33.7	(822)	(10.7)
<b>PAT</b>	<b>1,429</b>	<b>1,285</b>	<b>11.2</b>	<b>1,632</b>	<b>(12.4)</b>
Minority Interest	(15)	(78)	(80.8)	20	-
<b>Reported PAT</b>	<b>1,414</b>	<b>1,207</b>	<b>17.1</b>	<b>1,652</b>	<b>(14.4)</b>

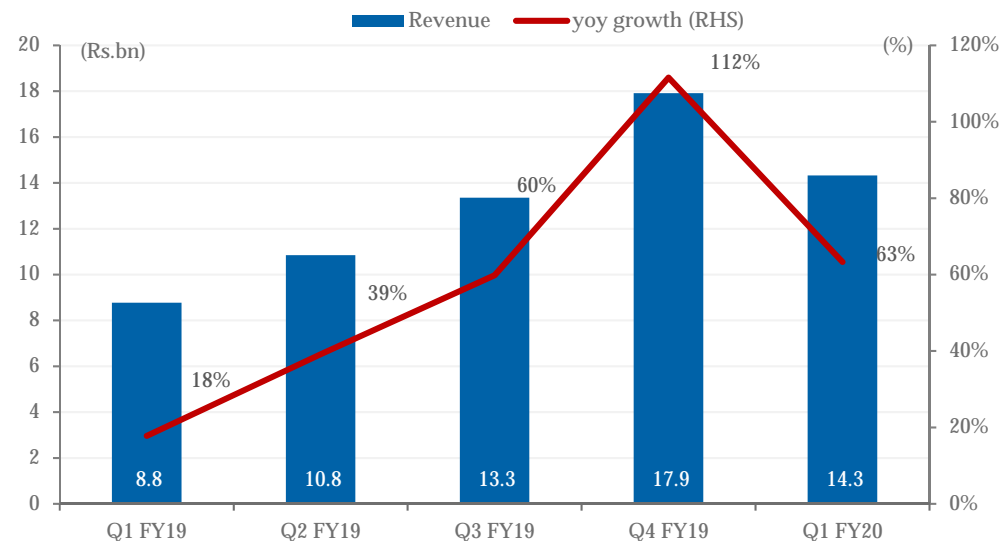
Source: Company, YES Sec – Research

### Exhibit 2: Order book provides near-term revenue visibility



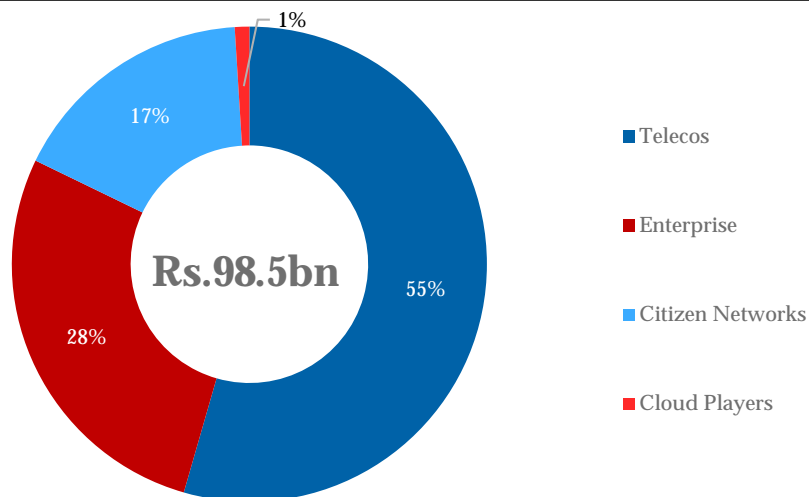
Source: Company, YES Sec – Research

### Exhibit 4: Revenue improving sharply over past one year



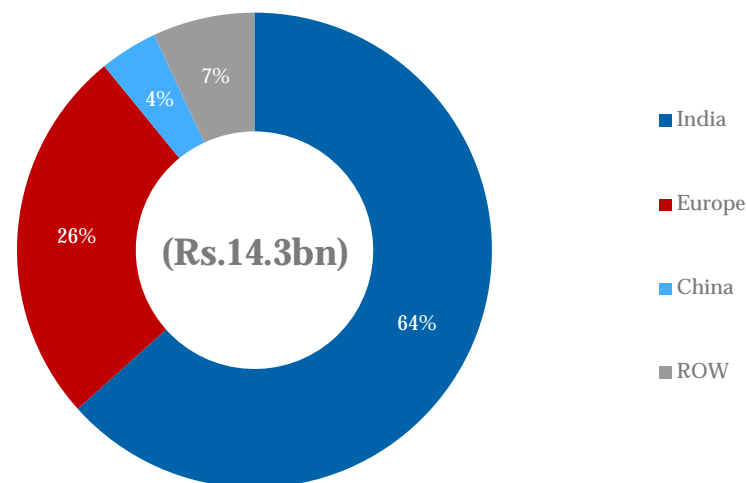
Source: Company, YES Sec – Research

### Exhibit 3: Telcos drive the order book with 55% share



Source: Company, YES Sec – Research

### Exhibit 5: India and Europe drive overall revenues



Source: Company, YES Sec – Research

## CONFERENCE CALL HIGHLIGHTS

- ✓ The revenues from product segment stood at ~70% during Q1 FY20 with balance being contributed from the services and software business.
- ✓ Backed by long-term contract, Optic Fiber realization for the company remained robust in the range of US\$ 7-8/fkm. (vis-à-vis US\$ 4/fkm in the spot market). The company doesn't expect immediate impact of lower spot-market prices to its fiber business with longer-term contracts in place.
- ✓ Operating margin during Q1 FY20 remained at a healthy level of ~23%. However, the management has retained its FY20 margin guidance of 18-20% owing to higher contribution from comparatively lower margin services business going forward.
- ✓ Order book for the company continued to remain strong at Rs.98.5bn providing strong revenue visibility in the near-term. Broadly, order book mix between products and services business stood at ~57% and ~43% respectively.
- ✓ The large-part of fiber capacity expansion program is at completion stage. The company expects revenue contribution from the newer-facilities to start from Q3 FY20 onwards. Currently, the company continues to run at existing capacity of 30 mn fkm.
- ✓ The cable capacity expansion program is on track (18 mn fkm being increased to 33 mn fkm). The same is likely to be completed by mid CY20.
- ✓ The company has delivered the complex design for the Navy's pan-India communication network. The project is being delivered at multiple locations throughout the country and is on schedule.

- ✓ The net debt at the end of Q1 FY20 stood at Rs. 19.8bn (~up 2.5bn qoq) owing to the higher capex being incurred for fiber and cable capacity expansion. Also, the higher share of services segment demand higher working capital investment. D/E is likely to be ~1x.
- ✓ The company has guided for Rs.5.5bn of Capex during FY20E.

### Exhibit 6: Financial Summary (Consolidated)

Y/e 31 Mar (Rs m)	FY18	FY19	FY20E	FY21E
Revenues	31,771	50,873	63,591	75,037
yoy growth (%)	29.7	60.1	25.0	18.0
Operating profit	7,494	11,272	12,233	14,186
OPM (%)	23.6	22.2	19.2	18.9
Reported PAT	3,343	5,628	6,550	7,813
Adjusted PAT	3,387	5,703	6,550	7,813
yoy growth (%)	66.0	68.3	16.4	19.3
EPS (Rs)	8.3	14.0	16.3	19.4
P/E (x)	19.6	11.7	10.0	8.4
EV/EBITDA (x)	9.8	7.2	6.7	5.4
Debt/Equity (x)	0.9	1.1	0.8	0.6
RoE (%)	32.5	38.9	33.4	31.1

Source: Company, YES Sec – Research

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**BUY > 15%**

**ADD 5% to 15%**

**HOLD -15% to +5%**

**SELL > - 15%**

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