

Healthy growth on benign base; traction key ahead!

Sterlite Tech's (STL) performance for Q4FY21 was a mixed bag with a slight topline beat but lower-than-expected margins. Revenues came in at ₹ 1475 crore, up 27.1% YoY. We note that growth is on a benign base as Q4FY20 had 35% YoY decline. Product and services were in the ratio of 55:45. EBITDA came in at ₹ 256.5 crore, up 18.7% YoY, driven by topline growth. Reported EBITDA margins came in at 17.4% (vs. our estimate of 18.1%), down 123 bps YoY, given the higher employee and other expenses. PAT at ₹ 124.4 crore, up 54.9% YoY, was higher than expected, aided by lower depreciation and higher other income.

Management expects growth momentum to continue

STL has indicated that OFC capacity utilisations are at 100%. It also said that optical fibre demand has revived by investments in digital infrastructure. Globally, OFC industry volumes in 2021 are likely to grow ~6% YoY. STL perceives that unprecedented decade of digital network creation is on the anvil. **The company has also maintained that, going ahead, growth should be driven by growing OFC volumes, optical interconnect business, scaling up SI business (both domestically and going global) and building access solution business.** We bake in revenues CAGR of ~26.6% in FY21-23E. We expect FY22 revenues to witness a spurt (up ~37% YoY) driven by improved capacity utilisation as well as continued traction in solutions based business, with FY23 revenue growth at ~17%YoY. We build in margins of 18% for FY22E and FY23E, based on management guidance of margin band of 17-18% (earlier guidance 18-20%).

Order book stays healthy...

The order book was at ₹ 10754 crore (vs. ₹ 10737 crore in Q3), of which O&M portion was 25%. STL expects outstanding order execution worth ₹ 5470 crore in FY22 and remaining in FY23 and thereafter. The open participation funnel remained strong at ₹ 11500 crore. The order inflows traction has been encouraging with key order wins in Q4 such as a) strategic partnership with Openreach to help build its new UK full fibre network, b) multi-million-dollar digital partnership transformation for a leading north African Telco and c) a large-scale deal with a leading UAE Telco for Opticonn solution to advance its 4G, 5G and FTTx network infrastructure.

Valuation & Outlook

The revenue growth recovery, albeit on a benign base, is positive. The FCF of ₹ 86 crore in FY21 was utilised in inorganic expansion (₹ 266 crore), buyback and dividends (totalling ₹ 240 crore), resulting in increase of ₹ 440 crore of net debt at ₹ 2410 crore with net debt/EBITDA at 3x. We would await improvement in leverage, better capital allocation and pricing improvement before turning constructive. We maintain **HOLD**, with a revised target price of ₹ 240/share (earlier ₹ 200/share).

Key Financial Summary

(Year-end March)	FY19	FY20	FY21E	FY22E	FY23E	CAGR (FY21-23E)
Net Sales (₹ crore)	5,087.3	5,154.4	4,825.2	6,592.7	7,734.8	26.6
EBITDA (₹ crore)	1,127.2	1,069.3	810.7	1,186.7	1,392.3	31.1
Net Profit (₹ crore)	562.8	433.9	275.5	541.7	628.1	51.0
EPS (₹)	14.0	10.8	6.9	13.7	15.8	
P/E (x)	16.6	21.6	33.5	17.0	14.7	
Price / Book (x)	5.4	4.9	4.6	4.0	3.4	
EV/EBITDA (x)	9.7	10.5	14.3	10.0	8.4	
RoE (%)	33.0	25.0	14.0	23.7	23.4	
RoCE (%)	27.8	20.9	12.9	18.6	20.7	

Source: Company, ICICI Direct Research



Particulars

Particular	Amount
Market Capitalization (₹ crore)	9,218.1
Total Debt (FY21) (₹ crore)	2,839.7
Cash & Inv (FY21) (₹ crore)	429.3
EV (₹ crore)	11,188.5
52 week H/L (₹)	249/ 86
Equity capital (₹ crore)	79.3
Face value (₹)	2.0

Key Highlights

- STL has maintained that going ahead growth should be driven by growing OFC volumes, optical interconnect business, scaling up SI business (both domestically and going global) and building access solution business.
- We maintain HOLD, valuing it at revised target price of ₹ 240/share (vs. ₹ 200/share, earlier). Our target price implies 8.5x FY23E EV/EBITDA and 15x FY23E P/E)

Key risks to our call

- Faster than expected pricing recovery could lead to better than expected earnings and further multiples rerating
- Continued higher leverage could stall the earnings growth trajectory

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Exhibit 1: Variance Analysis

	Q4FY21	Q4FY21E	Q4FY20	Q3FY21	YoY (%)	QoQ (%)	Comments
Revenue	1,475.0	1,451.6	1,160.1	1,314.4	27.1	12.2	The topline growth was largely on benign base and pick up in OFC segment
Other Income	16.5	9.0	10.4	7.7	58.2	115.0	
Cost of raw material	854.1	653.2	516.0	698.4	65.5	22.3	
Purchase of traded goods	0.0	14.5	0.4	0.0	NA	NA	
Employee Expenses	179.1	166.9	152.0	164.3	17.8	9.0	
(Increase) / decrease in inventories	-117.8	21.8	22.7	-35.4	-620.0	232.6	
Other Expenses	303.2	332.4	253.0	257.1	19.9	17.9	
EBITDA	256.5	262.7	216.0	230.1	18.7	11.5	
EBITDA Margin (%)	17.4	18.1	18.6	17.5	-123 bps	-11 bps	
Depreciation	61.2	70.8	76.8	68.2	-20.3	-10.2	
Interest	53.4	49.2	59.3	49.8	-10.0	7.2	
Total Tax	50.3	38.2	13.1	33.3	283.7	51.4	
PAT	124.4	114.1	80.3	86.6	54.9	43.6	PAT beat was due to lower depreciation and higher other income

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

(₹ Crore)	FY22E			FY23E			Comments
	Old	New	% Change	Old	New	% Change	
Revenue	6,500.9	6,592.7	1.4	7,734.8	7,734.8	0.0	Realign after management commentary and Q4 results
EBITDA	1,236.8	1,186.7	-4.1	1,471.6	1,392.3	-5.4	
EBITDA Margin (%)	19.0	18.0	-103 bps	19.0	18.0	-103 bps	We have lowered the margins as per management commentary
PAT	464.4	541.7	16.6	597.0	628.1	5.2	We lower the depreciation charge
EPS (₹)	11.7	13.7	16.6	15.1	15.8	5.2	

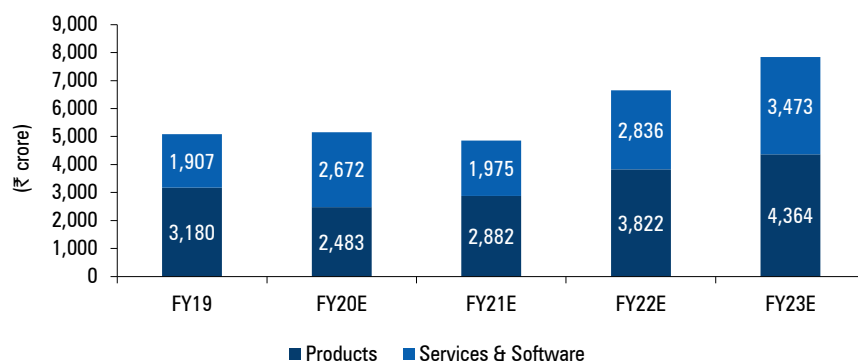
Source: Company, ICICI Direct Research

Business Highlights

- Global fibre demand:** For FY21, volumes for STL grew more than 35% despite a flat global industry. STL market share has grown 4x in the last five years i.e. from 1.3% in Q4FY16 to 5.1% in Q4FY21. As per management, OFC demand is expected to be at 565 mn fkm in 2023, to be driven by i) FTTH deployments and Bharat net in India, ii) carrier deployments in US, iii) buoyant FTTH deployments in Europe iv) deployments of 0.6 to 1mn 5G base stations in China
- Capacity expansion:** The cable capacity expansion plan (to 33 mn fkm from 18 mn fkm) is likely come on ground by June, 2021 and is on track in terms of costs and time. Currently, it is producing at annual run rate of 24 mn fkm in the cable division
- Witnesses investment in digital networks:** The management mentioned that last quarter they witnessed investments from i) telecom operators like Airtel (looking to invest in 30,000+ cell sites, fibre and FTTH rollout this year, China Telecom embarked on a US\$13 billion capex for CY21, out of which US\$6 bn was for 5G capex, ii) cloud companies, iii) large enterprises as well as from PE investments
- Order inflow & project status:** The order inflow traction has been encouraging with key order wins in Q4 such as: a) a three-year strategic collaboration with Openreach to provide millions of km of optical fibre cable to help connect UK with a full-fibre network, b) ~US\$100 million deals in the MEA region - for building future-ready digital networks, c) partnership with Airtel to build optical network across 10 circles. Project Varun (Indian Navy project) is 92% complete. Mahanet package A is 98% complete, while package B is 61% completed. Key new projects under execution are T-Fibre project (order size ₹ 1700-1800 crore), package A is 26% completed, while package B is 18% completed and fibre & FTTH rollout for large Indian telco is 41% complete
- Others**
 - Decline in depreciation owing to amortisation of Elitecore Goodwill, which is now fully amortised and Italian business had two quarter of depreciation accounted in Q3
 - Capex for FY22 is expected to be in the same range of FY21 i.e. in the range of ₹ 400-450 crore, out of which ₹ 60-65 crore would be maintenance capex. The management expects capex to taper down from FY23 downwards
 - STL is looking to bring down net working capital cycle days from 100 days currently to the range of 75-100 days

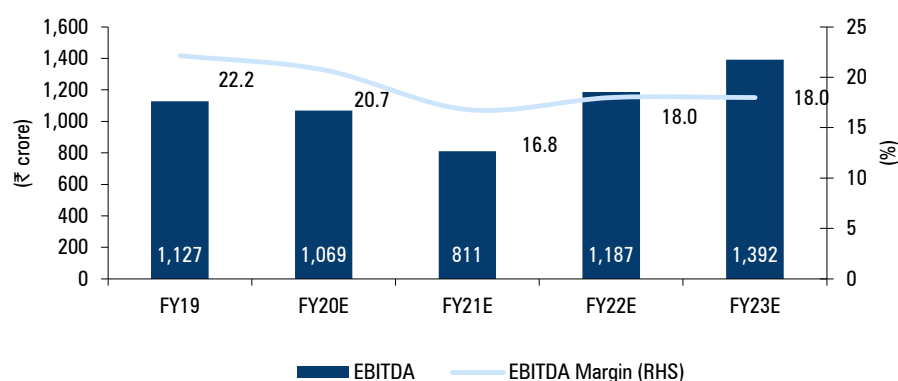
Financial story in charts

Exhibit 3: Topline growth trend



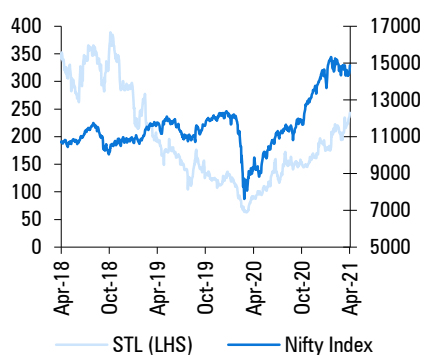
Source: Company, ICICI Direct Research

Exhibit 4: Margins to be in range of 17-18%



Source: Company, ICICI Direct Research

Exhibit 5: Price Performance



Source: Bloomberg, ICICI Direct Research

Financial summary

Exhibit 6: Profit and loss statement					₹ crore	
(Year-end March)	FY20	FY21	FY22E	FY23E		
Total operating Income	5,154.4	4,825.2	6,592.7	7,734.8		
Growth (%)	1.3	-6.4	36.6	17.3		
Cost of raw materials	2,467.5	2,394.9	3,329.3	3,906.1		
Employee Expenses	629.8	647.4	749.9	850.8		
Administrative Expenses	987.8	972.2	1,326.8	1,585.6		
Total Operating Expenditure	4,085.1	4,014.5	5,406.0	6,342.6		
EBITDA	1,069.3	810.7	1,186.7	1,392.3		
Growth (%)	-5.1	-24.2	46.4	17.3		
Depreciation	290.3	285.3	316.4	386.7		
Interest	221.0	203.0	264.1	289.0		
Other Income	34.3	43.0	45.0	50.0		
Exceptional Items	59.0	3.6	-	-		
PBT	533.3	361.8	651.1	766.6		
Minority Interest	(9.5)	(10.1)	5.0	5.0		
Profit from Associates	-	14.9	59.4	59.4		
Total Tax	108.9	111.3	163.8	192.9		
PAT	433.9	275.5	541.7	628.1		
Growth (%)	-22.9	-36.5	96.7	16.0		
EPS (₹)	10.8	6.9	13.7	15.8		

Source: Company, ICICI Direct Research

Exhibit 7: Cash flow statement					₹ crore	
(Year-end March)	FY20	FY21	FY22E	FY23E		
Profit after Tax	433.9	275.5	541.7	628.1		
Add: Depreciation	290.3	285.3	316.4	386.7		
Add: Interest paid	221.0	203.0	264.1	289.0		
(Inc)/dec in Current Assets	346.4	-720.7	-1,488.3	-961.8		
Inc/(dec) in CL and Provisions	203.7	385.5	1,057.5	683.4		
Others	0.0	0.0	0.0	0.0		
CF from operating activities	1,495.4	428.5	691.5	1,025.4		
(Inc)/dec in Investments	-197.9	30.1	50.0	50.0		
(Inc)/dec in Fixed Assets	-580.9	-323.8	-400.0	-300.0		
Others	-604.9	-106.8	-5.7	-6.3		
CF from investing activities	-1,383.6	-400.5	-355.7	-256.3		
Issue/(Buy back) of Equity	0.3	-1.5	0.0	0.0		
Inc/Dec in Minority Interest	7.8	-5.1	5.0	1.3		
Issue of Preference Shares	0.0	0.0	0.0	0.0		
Inc/(Dec) in loan funds	345.8	391.8	50.0	0.0		
Interest paid	-221.0	-203.0	-264.1	-289.0		
Others	-233.7	-206.4	-239.0	-239.0		
CF from financing activities	-100.9	-24.2	-448.1	-526.7		
Net Cash flow	10.9	3.8	-112.3	242.5		
Opening Cash	233.7	244.5	248.3	136.0		
Closing Cash	244.5	248.3	136.0	378.5		

Source: Company, ICICI Direct Research

Exhibit 8: Balance sheet					₹ crore	
(Year-end March)	FY20	FY21	FY22E	FY23E		
Liabilities						
Equity Capital	80.8	79.3	79.3	79.3		
Preference Share Capital	0.0	0.0	0.0	0.0		
Reserve and Surplus	1,839.0	1,908.1	2,210.8	2,600.0		
Total Shareholders funds	1,919.8	1,987.4	2,290.1	2,679.3		
Total Debt	2,448.0	2,839.7	2,889.7	2,889.7		
Others	461.7	650.7	655.7	656.9		
Total Liabilities	4,829.5	5,477.8	5,835.5	6,225.9		
Assets						
Gross Block	4,622.2	4,851.6	5,251.6	5,551.6		
Less: Acc Depreciation	1,684.4	1,969.7	2,286.1	2,672.9		
Net Block	2,937.8	2,881.9	2,965.5	2,878.7		
Capital WIP	132.8	227.2	227.2	227.2		
Goodwill	121.8	292.1	292.1	292.1		
Total Fixed Assets	3,192.4	3,401.2	3,484.8	3,398.0		
Investments	455.1	595.3	545.3	495.3		
Inventory	451.8	626.4	855.8	1,004.0		
Debtors	1,563.1	1,451.4	1,983.1	2,326.6		
Loans and Advances	51.5	33.8	46.2	54.2		
Other Current Assets	1,275.8	1,951.4	2,666.2	3,128.1		
Cash	244.5	248.4	136.0	378.5		
Total Current Assets	3,586.8	4,311.4	5,687.3	6,891.6		
Creditors	1,430.3	1,943.7	2,655.6	3,115.7		
Provisions	10.9	11.0	15.0	17.6		
Other current liabilities	1,060.1	932.2	1,273.7	1,494.4		
Total Current Liabilities	2,501.3	2,886.9	3,944.3	4,627.7		
Net Current Assets	1,085.5	1,424.5	1,743.0	2,263.9		
Other non current assets	96.5	56.9	62.5	68.8		
Application of Funds	4,829.5	5,477.8	5,835.5	6,225.9		

Source: Company, ICICI Direct Research

Exhibit 9: Key ratios					₹ crore	
(Year-end March)	FY20	FY21	FY22E	FY23E		
Per share data (₹)						
EPS	10.8	6.9	13.7	15.8		
Cash EPS	18.0	14.1	21.6	25.6		
BV	47.7	50.1	57.7	67.5		
DPS	4.2	4.2	6.0	6.0		
Cash Per Share	41.8	49.7	57.6	67.4		
Operating Ratios (%)						
EBITDA Margin	20.7	16.8	18.0	18.0		
EBIT Margin	15.1	10.9	13.2	13.0		
PAT Margin	9.3	5.8	8.2	8.1		
Inventory days	32.0	47.4	47.4	47.4		
Debtor days	110.7	109.8	109.8	109.8		
Creditor days	101.3	147.0	147.0	147.0		
Return Ratios (%)						
RoE	25.0	14.0	23.7	23.4		
RoCE	20.9	12.9	18.6	20.7		
RoIC	15.8	10.3	14.6	15.8		
Valuation Ratios (x)						
P/E	21.6	33.5	17.0	14.7		
EV / EBITDA	10.5	14.3	10.0	8.4		
EV / Net Sales	2.2	2.4	1.8	1.5		
Market Cap / Sales	1.8	1.9	1.4	1.2		
Price to Book Value	4.9	4.6	4.0	3.4		
Solvency Ratios						
Debt/EBITDA	1.9	2.3	3.5	2.4		
Net Debt / Equity	1.0	1.0	1.2	1.1		
Current Ratio	1.9	2.3	2.1	2.1		
Quick Ratio	1.6	2.0	1.8	1.8		

Source: Company, ICICI Direct Research

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