RESULT UPDATE

MID CAP

Tulip Telecom

Maintain Outperformer

Price: Rs 110 | **BSE Index: 17,749** | **10 February 2012**

Share Data

Reuters code	TULP.BO
Bloomberg code	TTSL IN
Market cap. (US$ mn)	337
6M avg. daily turnover (US$ mn)	0.9
Issued shares (mn)	145
Target price (Rs)	157

Performance (%)	1M	3M	12M
Absolute	3	(23)	(27)
Relative	(9)	(25)	(28)

Valuation ratios (Standalone)

Yr to 31 Mar	FY12E	FY13E
EPS (Rs)	22.1	23.7
+/- (%)	3.7	7.4
PER (x)	5.0	4.7
PBV (x)	1.1	1.0
Dividend/Yield (%)	1.5	1.5
EV/Sales (x)	1.2	1.2
EV/EBITDA (x)	4.3	4.0

Major shareholders (%)

Promoters	70
FIIs	19
MFs	2
Public & Others	10

3QFY12 Result – To re-rate once liquidity concern abate...

Tulip's (standalone) revenue and EBITDA were slightly below estimates; however, variance was higher at bottom line due to higher interest cost. The management attributed the moderation in revenue growth (in Data Connectivity segment) to challenging macro economic environment and has guided for similar trend in 4QFY12E and reduced its FY12E revenue growth guidance to 14-16% from earlier 18-20% earlier.

Top line grew by 13.9% YoY to Rs 6.9 bn (B&K: Rs 7.1 bn, up 17.6% YoY). EBITDA grew by 16.2% YoY to Rs 1.99 bn (B&K: Rs 2.04 bn), largely in line. However, EBITDA margins increased by 60 bps YoY to 29% (20 bps higher than our expectation of 28.8%) as increasing proportion of customers on fibre network continues to drive scale benefits (in terms of wholesale bandwidth procurement). PAT came in much lower than our expectations due to doubling of finance cost (led by both higher debt on increasing working capital requirements and increase in interest rates). PAT stood at Rs 784.8 mn, down 3.8% YoY (B&K: Rs 841.7 mn; up 3% YoY).

B&K's view

The tough macro-economic headwinds have started shadowing on corporate IT and telecom spends and its impact was visible on moderating growth at Tulip. FY12E growth guidance has been downward revised to 14-16% (from 18-20%) and visibility on FY13E remains low; however, Tulip is hopeful of delivering a 16-20% growth in the next fiscal. We have marginally downward revised our FY12E/FY13E revenue estimates by 2.8%/3.4% and correspondingly EBITDA gets downward revised by 2.7%/3.4%. The downward revision in earnings is marked at 6.2%/14.9% for FY12E/FY13E because of upward revision in interest costs as we begin to account for refinancing of FCCBs (currently zero coupon but Tulip might end up paying 7-8% on ECB financing).

Financial highlights

(Rs mn)	3QFY11	3QFY12	YoY (%)	2QFY12	QoQ (%)	FY11	YoY (%)	FY12E	YoY (%)	FY13E	YoY (%)
Net sales	6,026	6,865	13.9	7,029	(2.3)	23,507	19.6	27,246	15.9	31,508	15.6
EBITDA	1,715	1,992	16.2	2,048	(2.7)	6,653	26.6	7,869	18.3	9,167	16.5
EBITDA margin (%)	28.5	29.0	–	29.1	–	28.3	–	28.9	–	29.1	–
Depreciation	(441)	(526)	19.2	(495)	6.1	(1,705)	26.0	(2,062)	20.9	(2,457)	19.1
Other income	11	10	(9.0)	(26)	(140.1)	1	(96.7)	(16)	(1756.8)	40	(347.2)
Interest	(212)	(427)	101.6	(345)	23.7	(853)	19.1	(1,547)	81.4	(2,170)	40.3
PBT	1,073	1,050	(2.2)	1,181	(11.1)	4,096	27.4	4,243	3.6	4,579	7.9
Tax	(257)	(265)	3.0	(288)	(8.0)	(1,001)	11.3	(1,045)	4.4	(1,145)	9.5
PAT	816	785	(3.8)	893	(12.1)	3,085	33.8	3,197	3.7	3,434	7.4
PAT margin (%)	13.5	11.4	–	12.7	–	13.1	–	11.7	–	10.9	–
EPS (Rs)	5.6	5.4	(3.8)	6.2	(12.1)	21.3	33.8	22.1	3.7	23.7	7.4

Tulip's strategy of rising up the value chain and providing fiber connectivity along with enterprise data service is visible in improving margins. Its data center in Bangalore (commercially launched on 06 February 2011) will help to gain higher wallet share of the customer as it becomes a one-stop solution for both data connectivity and managed services. However, the near term concern on Tulip continues to be its ability to raise funds through the liquidity events (still awaiting sale of Qualcomm JV, stake sale in DC) or otherwise to repay its FCCBs and its rising working capital needs. We downward revise our valuation multiple and value Tulip at Rs 157 (downward revised from Rs 206), valuing it at 4.8x FY13E EV/ EBITDA, a 40% discount to Bharti's Indian operations FY13E target multiple. Maintain Outperformer. We are yet to incorporate data center financials in our model.

Con call highlights

- The management has witnessed deceleration in data connectivity orders due to which revenue growth has moderated. 4QFY12 would continue to see similar trend and FY12E revenue growth guidance has been reduced to 14-16%.
- On bandwidth prices, the management said that it is linked to voice rate which is expected to harden (122 licence cancellation by SC increases probability of rates hardening) and hence bandwidth prices are unlikely to go down from here.
- Out of the total Rs 9 bn funding for its Data Centre (TDC), Rs 2.3 bn was funded by Tulip. Of the remaining Rs 6.7 bn, Rs 5 bn is the external funding requirement and Rs 1.7 bn would be accrued from internal funds (in the third year of operations).
- For external fund the management has arranged Rs 2.5 bn through long-term credit lines and Rs 2.5 bn through mezzanine funding (limited time span is 3 years). The management is constantly in talks to raise equity for data center and mezzanine debt would be paid off once equity funds are raised.
- Data connectivity contributed 64% to total revenue of which 70% of revenue was recurring in nature.
- Fiber contribution to incremental connectivity orders stood at 83%.
- 3QFY12 capex stood at Rs 1.6 bn (Rs 1.15 bn for Tulip's current business and Rs 450 mn for data center); FY13E capex expected at Rs 4 bn and another Rs 2.25 bn capex will go towards TDC.
- The management has guided for 15-20% of data center order booking for FY12.
- Budgeted loss for data center was at US$ 10 mn, but now FY12E loss has been downward revised at US$ 3.5-4 mn. We believe that this revision is due to delayed start in data center operations (commenced operation in 4QFY12 against earlier guidance of 3QFY12).
- R-APRDP billing commenced in Uttar Pradesh and Gujarat.
- The management is in discussion with banks to raise funds to gear up for redemption of FCCB (in August 2012). The management believes that it would be able to arrange the funding by end of 4QFY12.
- Working capital requirement has increased over 9MFY12 as market conditions are challenging; however, the management expects to improve working capital position going forward.

- The BWA spectrum (JV with Qualcomm) sellout is pending due to on going issue of Tulip's licence fee payment in TDSAT; the sale will be done as soon as the issue is resolved.
- Mr Sanjay Jain resigned as the CEO to pursue other opportunities.

Revised estimates

(Rs mn)	FY12E			FY13E		
	Old	Revised	Change (%)	Old	Revised	Change (%)
Net sales	28,045	27,246	(2.8)	32,608	31,508	(3.4)
EBITDA	8,085	7,869	(2.7)	9,493	9,167	(3.4)
EBITDA margin (%)	28.8	28.9	–	29.1	29.1	–
Adjusted PAT	3,407	3,197	(6.2)	4,035	3,434	(14.9)
EPS (Rs)	23.5	22.1	(6.2)	27.8	23.7	(14.9)

Income Statement (Standalone)

Yr end 31 Mar (Rs mn)	FY10	FY11	FY12E	FY13E
Net sales	**19,651**	**23,507**	**27,246**	**31,508**
Growth (%)	*21.7*	*19.6*	*15.9*	*15.6*
Operating expenses	(14,396)	(16,853)	(19,377)	(22,341)
Operating profit	5,255	6,653	7,869	9,167
EBITDA	**5,255**	**6,653**	**7,869**	**9,167**
Growth (%)	*56.1*	*26.6*	*18.3*	*16.5*
Depreciation	(1,353)	(1,705)	(2,062)	(2,457)
Other income	30	1	(16)	40
EBIT	**3,932**	**4,949**	**5,790**	**6,750**
Interest paid	(716)	(853)	(1,547)	(2,170)
Pre-tax profit (before non-recurring)	3,216	4,096	4,243	4,579
Pre-tax profit (after non-recurring)	3,216	4,096	4,243	4,579
Tax (current + deferred)	(899)	(1,001)	(1,045)	(1,145)
Net profit (before Minority Interest, Pref. Dividend, etc.)	2,317	3,095	3,197	3,434
Prior period adjustments	(12)	(11)	–	–
Reported PAT	**2,305**	**3,085**	**3,197**	**3,434**
Adjusted net profit	**2,305**	**3,085**	**3,197**	**3,434**
Growth (%)	*(7.7)*	*33.8*	*3.7*	*7.4*

Balance Sheet (Standalone)

Yr end 31 Mar (Rs mn)	FY10	FY11	FY12E	FY13E
Cash and marketable sec.	3,470	2,498	2,498	2,498
Other current assets	7,567	9,883	14,849	15,717
Investments	–	3,782	3,782	3,782
Net fixed assets	13,297	16,521	19,489	21,032
Total assets	**24,334**	**32,684**	**40,618**	**43,028**
Current liabilities	2,838	2,938	3,232	3,555
Total debt	12,191	17,549	22,701	23,774
Other non-current liabilities	29	32	32	32
Total liabilities	15,059	20,519	25,965	27,361
Share capital	290	290	290	290
Reserves & surplus	8,989	11,875	14,364	15,377
Less: Misc. expenditure	(4)	(0)	(1)	–
Shareholders' funds	**9,275**	**12,165**	**14,653**	**15,667**
Total equity & liabilities	**24,334**	**32,684**	**40,618**	**43,028**
Capital employed	**21,495**	**29,745**	**37,385**	**39,473**

Cash Flow Statement (Standalone)

Yr end 31 Mar (Rs mn)	FY10	FY11	FY12E	FY13E
Pre-tax profit	3,216	4,096	4,243	4,579
Depreciation	1,353	1,705	2,062	2,457
Change in working capital	(2,297)	(2,216)	(4,673)	(545)
Total tax paid	(879)	(998)	(1,045)	(1,145)
Cash flow from oper. (a)	**1,393**	**2,587**	**587**	**5,347**
Capital expenditure	(2,501)	(4,930)	(5,030)	(4,000)
Change in investments	(0)	(3,782)	–	–
Others	–	3	(1)	1
Cash flow from inv. (b)	**(2,501)**	**(8,709)**	**(5,031)**	**(3,999)**
Free cash flow (a+b)	**(1,108)**	**(6,122)**	**(4,443)**	**1,348**
Equity raised/(repaid)	(12)	9	(0)	(0)
Debt raised/(repaid)	966	5,358	5,152	1,073
Dividend (incl. tax)	(407)	(271)	(271)	(271)
Others	(480)	–	–	–
Cash flow from fin. (c)	**67**	**5,096**	**4,882**	**802**
Net chg in cash (a+b+c)	**(1,041)**	**(1,026)**	**438**	**2,150**

Key Ratios (Standalone)

Yr end 31 Mar (%)	FY10	FY11	FY12E	FY13E
Adjusted EPS (Rs)	15.9	21.3	22.1	23.7
Growth	(7.7)	33.8	3.7	7.4
Book NAV/share (Rs)	64.0	83.9	101.1	108.1
Dividend/share (Rs)	1.6	1.6	1.6	1.6
Dividend payout ratio	11.8	8.8	8.5	7.9
Tax	28.0	24.4	24.6	25.0
EBITDA margin	26.7	28.3	28.9	29.1
EBIT margin	20.0	21.1	21.3	21.4
RoCE	20.0	19.3	17.2	17.6
Net debt/Equity	94.0	123.7	137.9	135.8

Valuations (Standalone)

Yr end 31 Mar (x)	FY10	FY11	FY12E	FY13E
PER	6.9	5.2	5.0	4.7
PCE	4.4	3.3	3.0	2.7
Price/Book	1.7	1.3	1.1	1.0
Yield (%)	1.5	1.5	1.5	1.5
EV/Net sales	1.2	1.2	1.2	1.2
EV/EBITDA	4.6	4.2	4.3	4.0

Du Pont Analysis – ROE (Standalone)

Yr end 31 Mar (x)	FY10	FY11	FY12E	FY13E
Net margin (%)	11.7	13.1	11.7	10.9
Asset turnover	0.9	0.8	0.7	0.8
Leverage factor	2.8	2.7	2.7	2.8
Return on equity (%)	28.9	28.8	23.8	22.7

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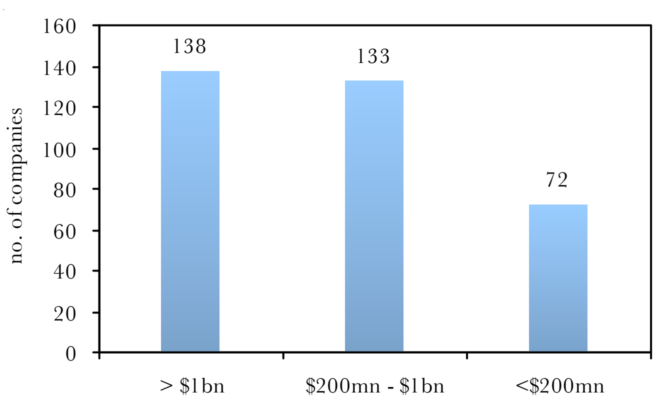
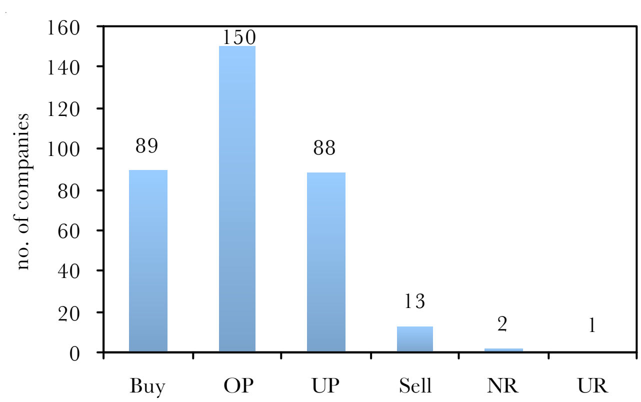
B&K Universe Profile

By Market Cap (US$ mn)



By Recommendation



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1. **BUY:** Potential upside of > +25% (absolute returns)
2. **OUTPERFORMER:** 0 to +25%
3. **UNDERPERFORMER:** 0 to -25%
4. **SELL:** Potential downside of < -25% (absolute returns)

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