



Tulip Telecom

BSE SENSEX 18,415	S&P CNX 5,516	CMP: Rs164	TP: Rs210	Buy								
Bloomberg Equity Shares (m)	TTSL IN 145.0	YEAR	NET SALES	PAT	EPS	EPS	P/E	P/BY	ROE	ROCE	EV/	EV/
52-Week Range (Rs)	201/132	END	(RS M)	(RS M)	(RS)	GROWTH (%)	(X)	(X)	(%)	(%)	SALES	EBITDA
1,6,12 Rel. Perf. (%)	6/0/-17	3/10A	19,655	2,310	14.2	-3.5	11.5	2.9	28.7	14.0	1.7	6.2
M.Cap. (Rs b)	23.8	3/11A	23,511	3,064	18.9	32.7	8.7	2.2	28.6	14.0	1.6	5.7
M.Cap. (US\$ b)	0.5	3/12E	28,826	3,164	19.5	3.3	8.4	1.8	23.3	12.2	1.5	5.3
		3/13E	35,695	3,440	21.2	8.7	7.7	1.2	18.5	11.4	1.1	4.3

We are downgrading Tulip Telecom's FY12 and FY13 earnings by ~20% and lowering target price to Rs210 (Rs240 earlier) to factor in start-up EBITDA loss for data center business (partially developed facility acquired in Jan-11), and higher depreciation (for data center) and finance costs (for data centre as well as core business). We now expect 6% EPS CAGR over FY11-13 and incorporate acquired data center EBITDA break-even in FY13. Leverage remains relatively high with FY11 net debt/EBITDA at 2.3x.

Given the timing/valuation uncertainty we are not incorporating potential proceeds from stake sale in data centre business (process underway) or sale of stake in Qualcomm's BWA venture (invested Rs1.4b for 13% stake). However our valuation ratios (EV/EBITDA, EV/Sales) capture potential pay-out for redemption premium for outstanding FCCBs (premium of ~Rs1.9b; FCCB due Aug-12). Maintain **Buy** as valuations remain attractive at 8.4x FY12 diluted EPS of Rs19.5 and 5.3x EV/EBITDA. Our target price is based on DCF and implies FY13 P/E of ~10x and EV/EBITDA of 5.2x.

Operating performance (standalone) in line: During 4QFY11, Tulip consolidated its data center operations. Standalone revenue (up 20% YoY to Rs6.38b) and earnings (up 30% YoY to Rs855m) were in line with our estimates, led by strong performance in the fiber segment. The management has guided revenue growth of 20% and 50-75bp margin expansion in FY12. The company has guided capex of Rs7b including Rs2.5b towards data center business in FY12.

Key positives: (1) Increased traction from fiber (constituting 70-80% of new order inputs in 2HFY11) in data connectivity, (2) potential equity sale at the subsidiary level (expected to close in three months) can lower debt levels, (3) continued traction in government business can be an additional growth driver, and (4) potential sale of stake held in BWA venture at a premium.

Key concerns: (1) Potential delay in ramping up of acquired data center operations, (2) upward pressure on interest rates, (3) relatively high leverage, given continued capex and increase in working capital requirements, and (4) potential US\$42m additional liability for FCCB redemption due in August 2012.

Y/E MARCH	Quarterly Performance (Consolidated)								(Rs Million)	
	FY10				FY11				FY10	FY11
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q		
Gross Revenue	4,429	4,910	5,009	5,307	5,252	5,853	6,022	6,380	19,655	23,511
YoY Growth (%)	33.2	27.7	15.0	15.0	18.6	19.2	20.2	20.2	21.7	19.6
QoQ Growth (%)	-4.0	10.9	2.0	5.9	-1.0	11.4	2.9	5.9		
Total Operating Expenses	3,343	3,642	3,659	3,762	3,834	4,220	4,306	4,513	14,406	16,880
EBITDA	1,086	1,269	1,350	1,545	1,417	1,633	1,716	1,867	5,249	6,631
YoY Growth (%)	66.0	56.5	48.0	56.0	30.5	28.7	27.1	20.8	55.9	26.3
QoQ Growth (%)	9.6	16.8	6.4	14.4	-8.3	15.2	5.1	8.8		
Margin (%)	24.5	25.8	27.0	29.1	27.0	27.9	28.5	29.3	26.7	28.2
Net Finance Costs	158	187	186	185	185	190	212	267	716	853
Non-Operating Income	112	7	-9	-80	-13	14	11	-11	30	1
Depreciation & Amortization	353	436	409	155	375	420	441	479	1,353	1,714
Profit before Tax	687	653	746	1,125	844	1,038	1,075	1,111	3,210	4,065
Income Tax Expense / (Income)	96	164	172	467	203	258	257	283	899	1,001
Reported Net Profit / (Loss)	591	489	574	658	642	780	817	827	2,310	3,064
YoY Growth (%)	28.5	-2.6	17.9	-37.8	8.6	59.6	42.5	25.8	-7.8	32.6
QoQ Growth (%)	-44.1	-17.3	17.4	14.6	-2.5	21.6	4.8	1.2		
Margin (%)	13.3	10.0	11.5	12.4	12.2	13.3	13.6	13.0	11.8	13.0

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Operating performance (standalone) in line with estimates

- Tulip Telecom's PAT grew 30% YoY and 4.7% QoQ in 4QFY11 to Rs855m, in line with our estimate.
- Revenue increased 20.4% YoY and 6% QoQ to Rs6.38b (in line with our estimate), led by strong performance in fiber as well as wireless segments.
- EBITDA grew 22.1% YoY and 9.9% QoQ to Rs1.89b (v/s our estimate of Rs1.85b). EBITDA margin expanded 42bp YoY and 106bp QoQ to 29.6% (v/s our estimate of 29%).
- Capex for FY11 was Rs5.3b (capex/sales of 22%), higher than the company's guidance of Rs4.5b.
- Tulip has guided capex of Rs7b for FY12, including Rs2.5b towards the data center business.
- In 4QFY11, Tulip consolidated the recently acquired Bengaluru-based data centre operations (for a consideration of Rs2.3b). The acquired data center subsidiary reported EBITDA loss of Rs9m and is expected to be operational effective from August 2011.
- Tulip's intra-city, 6,000km fiber network spans over 300 cities in India, with 600+ customers. Over 80% of new orders in terms of revenue are now from fiber.
- Customer base remains diversified, with 1,800+ clients spread across more than 2,000 locations.

Net debt up 23% QoQ to Rs15.3b; net debt/annualized EBITDA increased to 2x

- Consolidated net debt increased by 23% QoQ to Rs15.3b due to data center acquisition (of Rs2.3b) and higher capex.
- Net debt/equity increased to 1.26x and net debt/EBITDA (annualized) to 2x. Net debt is likely to increase further given more investments required in data center business. Tulip plans to place equity stake in data center business to a financial/strategic investor.

Data center operations to be EPS accretive from FY14

- The acquired data center subsidiary reported EBITDA loss of Rs9m and is expected to be operational effective August 2011.
- Tulip expects to earn revenue of Rs10b, with ~50% EBITDA margin from data centers in 3-4 years.
- While we build in revenue of Rs319m in FY12 and Rs2.7b in FY13, we incorporate EBITDA loss of Rs287m in FY12 and positive EBITDA of Rs30m in FY13.
- Management expects to break even at EBITDA level in 2Q/3Q FY13.
- In FY14, we estimate revenue of Rs6.5b and EBITDA of Rs1.5b (EBITDA margin of 23%).
- We have modeled capex of ~Rs2.5b in FY12/13 and Rs1.1b in FY14 for the acquired data center.
- Our estimates are relatively conservative and will be under risk only if there is significant delay in the ramp-up.

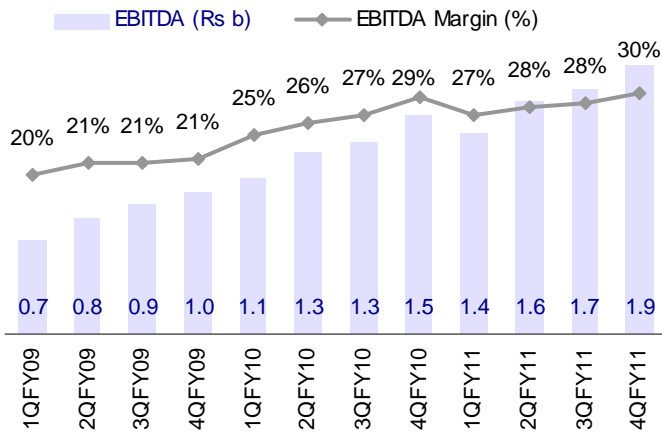
Downgrading earnings estimates by ~20% for FY12/13; revising target price to Rs210; maintain Buy

- We are downgrading Tulip Telecom's FY12 and FY13 earnings by ~20% and lowering target price to Rs210 (Rs240 earlier) to factor in start-up EBITDA loss for data center business (partially developed facility acquired in Jan-11), and higher depreciation (for data center) and finance costs (for data centre as well as core business).
- We now expect 6% EPS CAGR over FY11-13 and incorporate acquired data center EBITDA break-even in FY13.
- Leverage remains relatively high with FY11 net debt/EBITDA at 2.3x.
- Given the timing/valuation uncertainty we are not incorporating potential proceeds from stake sale in data centre business (process underway) or sale of stake in Qualcomm's BWA venture (invested Rs1.4b for 13% stake). However our valuation ratios (EV/EBITDA, EV/Sales) capture potential pay-out for redemption premium for outstanding FCCBs (premium of ~Rs1.9b; FCCB due Aug-12).
- Maintain **Buy** as valuations remain attractive at 8.4x FY12 diluted EPS of Rs19.5 and 5.3x EV/EBITDA. Our target price is based on DCF and implies FY13 P/E of ~10x and EV/EBITDA of 5.2x.

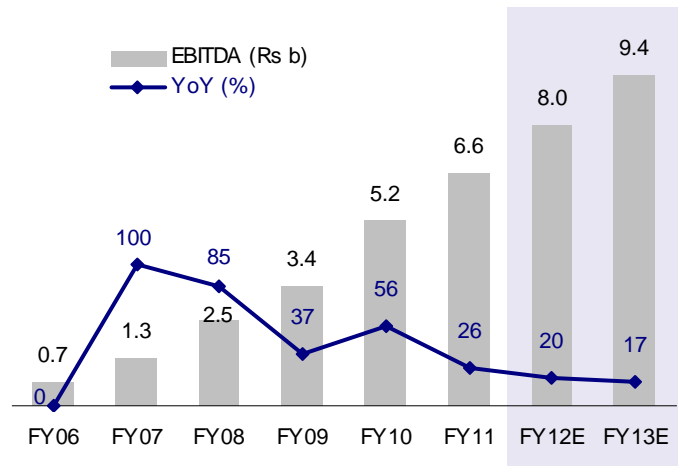
Highlights of 4QFY11 earnings call

- Continued focus on capturing higher customer wallet share through fiber, international business, and managed services (including data center ramp-up).
- Tulip plans to increase density/coverage of fiber in existing 300 cities to keep up pace with robust demand for fiber connectivity.
- Fiber now constitutes 70-80% of the new order input in data connectivity business.
- Management has guided ~20% revenue growth in FY12, driven by data connectivity (65-70%) and managed services; contribution of network integration would remain in single digits.
- Expects EBITDA margin to expand by 50-75bp in FY12.
- Increase in working capital during FY12 would be much lower than the ~Rs2b+ increase during last two years.
- Consolidated capex of ~Rs7b in FY12 (Rs4.5b for core business + Rs2.5b for data center).
- Interest costs to be under upward pressure, given recent increases in interest rates.
- Capex over-run in FY11 was largely due to laying of NLD (National Long Distance) fiber between Mumbai, Bangalore and Chennai (management expects a pay-back of two years on this investment).
- Data center operations should commence operations and start generating revenue by 2QFY12; Tulip expects to earn revenue of Rs10b, with ~50% margin from data centers in 3-4 years.
- Won R-APDRP (Restructured - Accelerated Power Development Reforms Program) project for the state of Andhra Pradesh for Rs320m spread over five years, taking cumulative project order value to Rs2.4b over 3-5 years for five states.
- The management expects equity sale in the data center subsidiary to materialize in three months, as the process is underway.

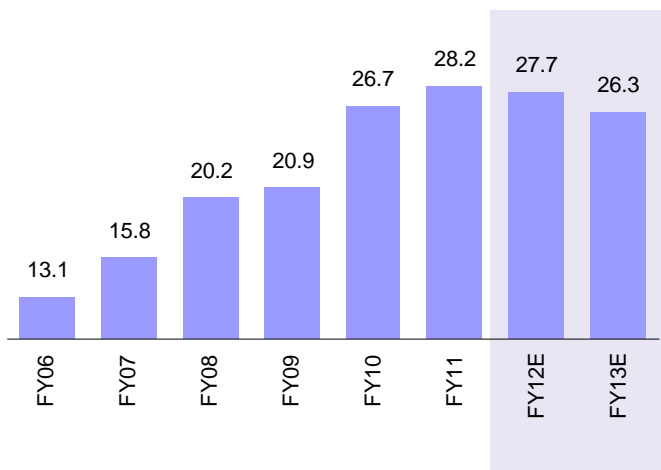
Quarterly EBITDA and margin



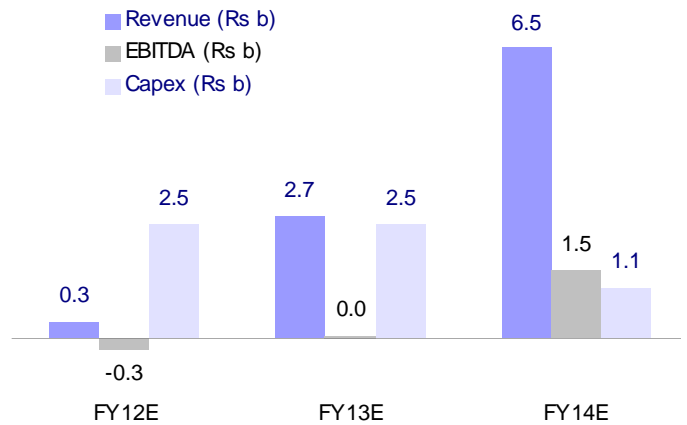
FY11-13E EBITDA CAGR of 19%



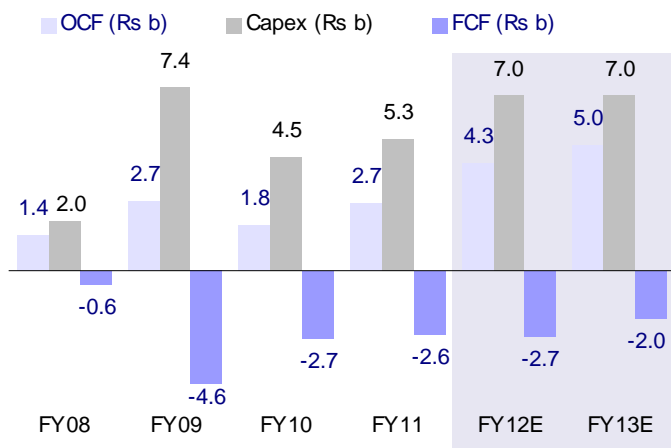
EBITDA margin expected at ~27%



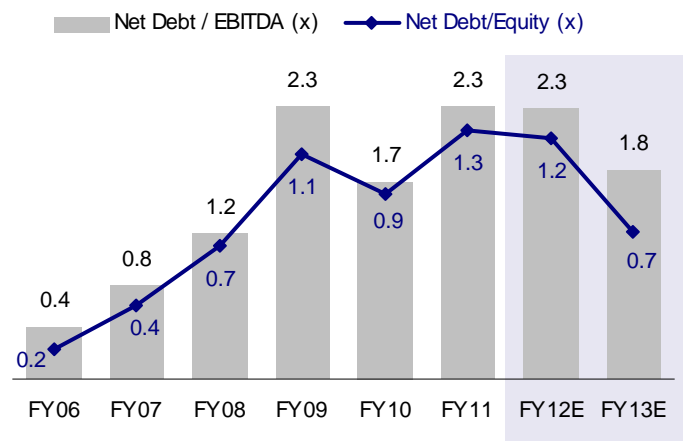
Data center operations expected to be EPS accretive from FY14



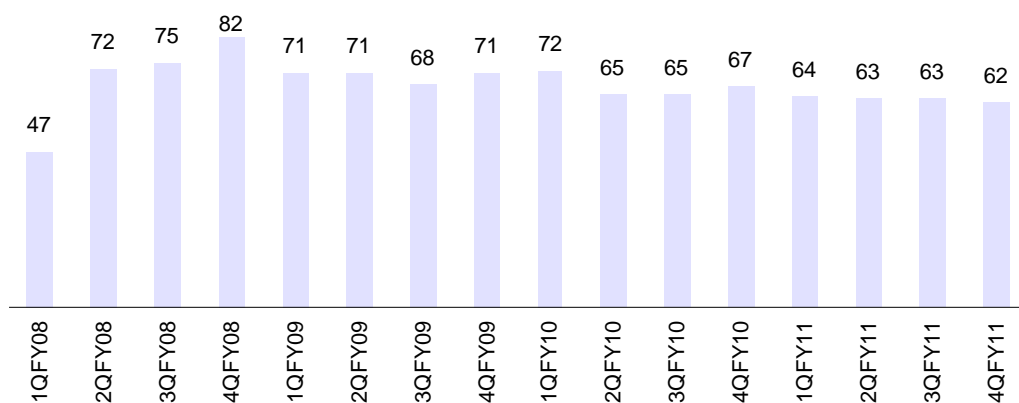
Data center capex to keep FCF negative in FY12/13



Leverage to remain high



Source: Company/MOSL

RM/Bandwidth cost declining (% of revenue)

Source: Company/MOSL

Tulip Telecom: Summary of estimate change

	FY11	FY12E	FY13E
Revenue (Rs b)			
Old	23.5	28.6	33.3
New/Actual	23.5	28.8	35.7
Change (%)	0.0	0.8	7.1
EBITDA (Rs b)			
Old	6.6	8.4	9.0
New/Actual	6.6	8.0	9.4
Change (%)	0.2	-4.3	4.6
Net Profit (Rs b)			
Old	3.1	4.0	4.3
New/Actual	3.1	3.2	3.4
Change (%)	-1.0	-21.0	-19.1
Diluted EPS (Rs)			
Old	19.0	24.7	26.2
New/Actual	18.9	19.5	21.2
Change (%)	-1.0	-21.0	-19.1
Depreciation (Rs b)			
Old	1.7	2.1	2.4
New/Actual	1.7	2.4	3.1
Change (%)	0.9	15.9	27.8
Net Finance Cost (Rs b)			
Old	0.9	1.0	1.0
New/Actual	0.9	1.4	1.8
Change (%)	-2.4	46.8	85.8
EBITDA Margin (%)			
Old	28.2	29.2	26.9
New/Actual	28.2	27.7	26.3
Change (bp)	5	-150	-64
Tax Rate (%)			
Old	24.2	25.0	25.0
New/Actual	24.6	25.0	25.0
Change (bp)	42	0	0

Source: Company/MOSL

Tulip Telecom: an investment profile

Company description

Tulip is a leading player in the Indian enterprise data segment, focused on providing connectivity to corporates, SMEs and government verticals. It has an outstanding track record, having scaled up to a dominant ~31% market share in the largest and fastest growing VPN segment within five years. Tulip is present in ~2,000 cities with a client base of ~1,800.

Key investment arguments

- Tulip has laid 6,000km of intra-city fiber for 'last mile' across 300 cities in the past 1.5 years; fiber reach is expected to expand to 600 cities in one year.
- Fiber rollout allows tapping high bandwidth connects, thereby capturing higher share of clients' requirement, increasing the addressable market by 5-6x and de-risking from competition; fiber constituted 70-80% of the new order inputs in data connectivity business in 2HFY11.
- Tulip has the deepest network coverage amongst the private operators with a presence in 2,000 cities.
- Growth in wireless connectivity and increased traction from fiber rollout should support 19-23% CAGR in revenue/EBITDA during FY11-13.
- The government vertical, which contributes <5% of revenue, is likely to be an additional growth driver.

Key investment risks

- Potential technology disruption.
- Scale differential v/s large telcos.
- Increased competition post allocation of BWA spectrum to rivals.

Comparative valuations

		Tulip	Bharti	Idea
P/E (x)	FY12E	8.4	18.1	29.4
	FY13E	7.7	13.8	15.2
EV/EBITDA (x)	FY12E	5.3	7.5	7.1
	FY13E	4.3	6.2	5.3
EV/Sales (x)	FY12E	1.5	2.7	1.8
	FY13E	1.1	2.3	1.5
P/BV (x)	FY12E	1.8	2.4	1.7
	FY13E	1.2	2.1	1.6

Shareholding Pattern (%)

	Dec-10	Sep-10	Dec-09
Promoter	69.0	69.0	69.0
Domestic Inst	1.9	2.0	1.6
Foreign	19.6	21.1	24.8
Others	9.6	7.9	4.6

Recent developments

- Tulip has acquired Bengaluru-based data center from SADA IT Parks Private Limited for Rs2.3b.
- Tulip has been awarded R-APDRP (Restructured - Accelerated Power Development Reforms Program) projects in UP, Gujarat, Uttarakhand, Andhra Pradesh and Punjab, with a combined order value of Rs2.4b over 3-5 years.
- Tulip has acquired a 13% stake in Qualcomm's BWA venture for a consideration of ~Rs1.4b.

Valuation and view

- We are downgrading Tulip Telecom's FY12 and FY13 earnings by ~20% and lowering target price to Rs210 (Rs240 earlier) to factor in start-up EBITDA loss for data center business. We now expect 6% EPS CAGR over FY11-13 and incorporate acquired data center EBITDA break-even in FY13.
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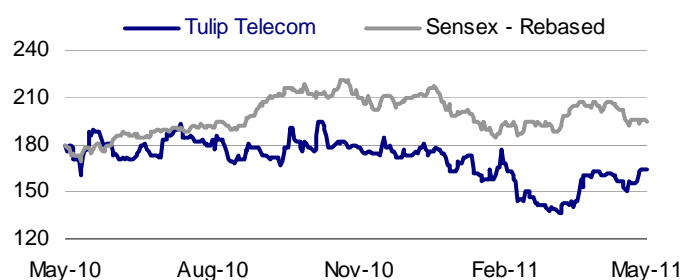
EPS: MOSL forecast v/s consensus (Rs)

	MOSL Forecast	Consensus Forecast	Variation (%)
FY12	19.5	22.6	-13.7
FY13	21.2	27.2	-22.0

Target price and recommendation

Current Price (Rs)	Target Price (Rs)	Upside (%)	Reco.
164	210	28.0	Buy

Stock performance (1 year)



Financials and Valuation

Income Statement		(Rs Million)				
Y/E March	2009	2010	2011	2012E	2013E	
Revenues	16,144	19,655	23,511	28,826	35,695	
Change (%)	32.7	21.7	19.6	22.6	23.8	
Total Expenses	12,777	14,406	16,880	20,838	26,310	
EBITDA	3,367	5,248	6,631	7,988	9,385	
% of Gross Sales	20.9	26.7	28.2	27.7	26.3	
Change (%)	37.1	55.9	26.3	20.5	17.5	
Depn. & Amortization	414	1,353	1,714	2,426	3,126	
EBIT	2,953	3,895	4,917	5,562	6,259	
Net Interest	462	716	853	1,433	1,800	
Other Income	344	30	1	90	128	
PBT	2,835	3,209	4,065	4,219	4,587	
Tax	330	899	1,001	1,055	1,147	
Rate (%)	11.6	28.0	24.6	25.0	25.0	
Adjusted PAT	2,505	2,310	3,064	3,164	3,440	
Change (%)	33.9	-7.8	32.7	3.3	8.7	
PAT after EO	2,505	2,310	3,064	3,164	3,440	

Balance Sheet		(Rs Million)				
Y/E March	2009	2010	2011	2012E	2013E	
Share Capital	290	290	290	290	325	
Additional Paid up Capital	831	831	831	831	4,743	
Reserves	5,694	8,157	11,003	13,896	17,065	
Net Worth	6,815	9,279	12,124	15,017	22,132	
Loans	11,224	12,191	17,769	21,738	21,536	
Other Liabilities	9	29	29	29	29	
Capital Employed	18,049	21,499	29,922	36,784	43,698	
Gross Block	13,209	15,711	23,104	30,104	37,104	
Less : Depreciation	1,061	2,414	4,128	6,554	9,680	
Net Block	12,148	13,297	18,976	23,550	27,424	
Curr. Assets	8,722	11,041	13,893	16,752	20,592	
Inventories	916	688	992	1,217	1,507	
Debtors	3,242	5,320	6,344	7,778	9,631	
Cash & Bank Balance	3,470	3,470	2,504	3,504	5,000	
Other Current Assets	1,094	1,562	4,054	4,254	4,454	
Curr. Liab. & Prov.	2,822	2,839	2,947	3,518	4,318	
Net Curr. Assets	5,901	8,202	10,946	13,234	16,274	
Appl. of Funds	18,049	21,499	29,922	36,784	43,698	

E: MOSL Estimates

Ratios						
Y/E March	2009	2010	2011	2012E	2013E	
Basic (Rs)						
EPS	14.7	14.2	18.9	19.5	21.2	
Cash EPS	17.2	22.5	29.4	34.4	40.4	
Book Value	40.1	57.1	74.6	92.4	136.2	
DPS	0.8	1.7	1.7	1.7	1.7	
Payout %(Incl.Div.Taxes)	5.4	11.8	8.9	8.6	7.9	
Valuation (x)						
P/E	11.1	11.5	8.7	8.4	7.7	
Cash P/E	9.5	7.3	5.6	4.8	4.1	
EV/EBITDA	9.4	6.2	5.7	5.3	4.3	
EV/Sales	2.0	1.7	1.6	1.5	1.1	
Price/Book Value	4.1	2.9	2.2	1.8	1.2	
Dividend Yield (%)	0.5	1.0	1.0	1.0	1.0	
Profitability Ratios (%)						
RoE	44.5	28.7	28.6	23.3	18.5	
RoCE	17.8	14.0	14.0	12.2	11.4	
Turnover Ratios						
Debtors (Days)	73	99	98	98	98	
Asset Turnover (x)	1.46	1.21	1.07	1.00	1.04	
Leverage Ratio						
Debt/Equity Ratio(x)	1.6	1.3	1.5	1.4	1.0	

Cash Flow Statement		(Rs Million)				
Y/E March	2009	2010	2011	2012E	2013E	
Op.Profit(Loss) bef Tax	3,367	5,248	6,631	7,988	9,385	
Other Income	344	30	1	90	128	
Interest Paid	-462	-716	-853	-1,433	-1,800	
Direct Taxes Paid	-330	-879	-1,001	-1,055	-1,147	
(Inc)/Dec in Wkg. Cap.	-172	-1,876	-2,108	-1,288	-1,543	
CF from Op.Activity	2,747	1,807	2,670	4,303	5,023	
(inc)/Dec in FA + CWIP	-7,365	-2,502	-7,393	-7,000	-7,000	
(Pur)/Sale of Investments	0	0	-1,550	0	0	
CF from Inv.Activity	-7,365	-2,502	-8,943	-7,000	-7,000	
Issue of Shares	0	0	0	0	3,946	
Inc/Dec in Debt	2,286	966	5,578	3,969	-202	
Dividends Paid	1	2	2	2	2	
Other Financing Activities	-137	-273	-273	-273	-273	
CF from Fin.Activity	2,151	695	5,307	3,698	3,473	
Inc/Dec in Cash	-2,468	0	-967	1,000	1,496	
Add: Opening Balance	5,938	3,470	3,470	2,504	3,504	
Closing Balance	3,470	3,470	2,504	3,504	5,000	



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Disclosure of Interest Statement

Tulip Telecom

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|---|----|
| 1. Analyst ownership of the stock | No |
| 2. Group/Directors ownership of the stock | No |
| 3. Broking relationship with company covered | No |
| 4. Investment Banking relationship with company covered | No |

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