

Recovery on track; H1FY24 to be muted...

About the stock: Sterlite Technologies (STL) is a leading telecommunication infrastructure player with offerings in optical fibre (OF) and optical fibre cables (OFC), hyper-scale network design and deployment & network software.

Q4FY23: Recovery continued with product segment driving profitability.

- Revenues came in at ₹ 1872 crore, up 18.3% YoY, driven by product segment. The product segment grew 40% YoY to ₹ 1486 crore while services declined ~24% YoY to ₹ 382 crore
- EBITDA at ₹ 256 crore, was up 1.8x YoY, with margins at 13.7% (up 790 bps YoY, 76 bps QoQ) largely in line with expectations, driven by revenues mix as product segment has superior margins. Product had a margin of 20.3% vs. ~20.3% in Q3
- PAT of ₹ 65 crore vs. loss in base quarter. Adjusted PAT was ₹ 82 crore

What should investors do? STL share price has grown ~19% over last five years.

- STL is uniquely positioned to benefit from 5G/ FTTH deployment cycle both domestically and globally. The company will likely see healthy earnings momentum in the medium term ahead (notwithstanding muted H1FY24) ahead. Thus, we maintain **BUY** rating on the stock

Target Price and Valuation: We value STL at ₹ 200, at 15x FY25 P/E.

Key triggers for future price performance:

- Demand offtake from expanded and overall fibre/cable pricing trajectory. We bake in ~12% overall revenue CAGR over FY23-25, with products segment revenues growth being higher, while services to remain muted.
- Improvement in leverage, which has gone up due to expansion and stretched working capital in services business
- Improving optical interconnect attach rate to aid margins

Alternate Stock Idea: Apart from STL, in our coverage we like Bharti Airtel.

- A play on favourable industry structure and superior digital play
- BUY with target price of ₹ 925

Key Financial Summary

(Year-end March)	FY20	FY21	FY22	FY23	5 yr CAGR (FY18-23)	FY24E	FY25E	2 yr CAGR (FY23-25E)
Net Sales (₹ crore)	5,154.4	4,825.2	5,754.3	6,926.0	16.7	7,870.2	8,654.3	11.8
EBITDA (₹ crore)	1,069.3	810.7	534.8	891.0	3.5	1,221.4	1,384.7	24.7
Net Profit (₹ crore)	433.9	275.5	62.0	141.0	(15.9)	435.4	539.0	95.5
EPS (₹)	10.8	6.9	1.6	3.5		10.9	13.6	
P/E (x)	14.4	22.3	99.6	43.8		14.2	11.4	
Price / Book (x)	3.3	3.1	3.2	3.0		2.5	2.2	
RoE (%)	25.0	14.0	8.3	11.7		17.6	18.9	
RoCE (%)	20.9	12.9	5.7	12.0		16.8	19.0	
		-6.4%	19.3%	20.4%		13.6%	10.0%	

Source: Company, ICICI Direct Research



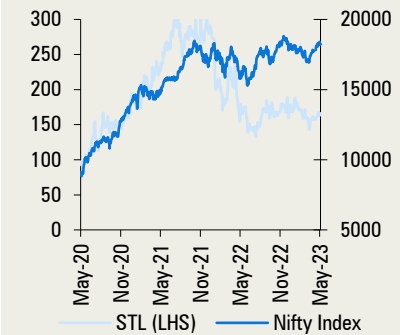
Particulars

Particular	Amount
Market Capitalization (₹ crore)	6,169
Total Debt (FY23) (₹ crore)	3,667
Cash & Inv (FY23) (₹ crore)	547
EV (₹ crore)	8,139
52 week H/L (₹)	193/ 129
Equity capital (₹ crore)	80
Face value (₹)	2

Shareholding pattern

	Jun-22	Sep-22	Dec-22	Mar-23
Promoters	54.2	54.1	54.1	54.1
DII	7.2	3.8	2.9	2.1
FII	6.0	7.9	7.9	8.0
Other	32.6	34.2	35.2	35.9

Price Chart



Key risk

- Continued leverage
- Sustained demand softness

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Key business highlights

Product segment to drive revenue growth...

STL's market share (ex-China) grew to ~12% in FY23 vs. ~9% in FY22 (albeit stable QoQ), led by increase in OFC market share in Americas during the year. The company operates in the optical product segment, which has a healthy 20%+ margin while newly focused interconnect products margins are at ~30%. The company has also reiterated that, going ahead, growth should be driven by growing OFC volumes (increasing market share, increasing optical Interconnect attach rate and developing new products) and consolidating the services business (by focusing on profitable growth and reducing working capital). **We bake in revenues CAGR of ~12% in FY22-25E driven by continued robust capacity utilisation in the product segment amid muted services business. We build in margins to recovery to 16% in FY25 with improving interconnect attach rate (interconnect product as a percentage of cable revenues). The company aims to increase it from 10% currently to 40% in the medium term, improve its margins in services (led by project mix) and also turn breakeven in new digital business.**

Strong order book; margins to improve in services ahead...

The order book was at ~₹ 11052 crore, of which O&M portion was 24%. Order book mix was telcos at 60%, citizen networks/government at 18% and enterprises at 18%. The company is targeting selective order intake in India in the India private segment. **Its medium-term target is to reach services margins of ~8% by FY24 end vs. ~4% currently as it expects to be profitable in UK with execution ramp up by H1FY24 along with completion of legacy projects.**

Other highlights

- **Demerger of product and services:** The company informed that services business would be demerged to "STL Networks Ltd". Pursuant to demerger, STL Networks' shareholding will mirror STL and its shares will be publicly listed. The objective is to pursue growth without constraint. The process will take nine to 12 months
- **Demand:** Global OFC demand is expected to grow at 4.4% CAGR over CY22-25 from 534 mn fkm to 607 mn fkm while North America and India are expected to grow at 11.5/8% CAGR during the same period
- **North America to be muted in H1:** The inventory build-up in North America may delay growth as some carriers will draw down their inventories first before new ordering begins. There is also shortage of trained labour & therefore need for connectorised solutions. **The company, thus, believes H1FY24 could be muted but expects sustained demand from H2 onwards.**
- **Capex:** Capex in FY23 was ~₹ 400 crore. It guided for ₹ 350-400 crore for FY24 (largely for interconnect and optical business and some maintenance)
- **Key order wins in Q4:** a) Long distance & intracity fibre rollout for leading telco, b) long distance fibre roll out along with optical fibre cables and optical connectivity solutions for leading telco, c) multi-million-dollar orders with a European telecom player for optical fibre cable, d) multi-million-dollar orders for optical fibre cable from North America and e) multi-million-dollar orders for optical fibre cable & optical connectivity from APAC
- **Net debt:** Net debt was at ~₹ 3120 crore vs. ₹ 3400 crore in Q3. It expects to release working capital with completion in certain projects. Led by cash flow generation, it aims to reduce debt by ₹ 200 crore in FY24. FY24 net debt to EBITDA target is less than 2.5x
- **Rights issue:** The company has decided on ₹ 500 crore as rights issue likely to improve capital structure. The issue is likely to be undertaken based on right market conditions

STL is uniquely positioned to benefit from 5G/ FTTH deployment cycle both domestically and globally. The company will likely see healthy earnings momentum in the medium term ahead (notwithstanding muted H1FY24) ahead. Thus, we maintain BUY and assign at target price of ₹ 200, valuing the company at 15x FY25E P/E.

Exhibit 1: Variance Table

	Q4FY23	Q4FY23E	Q4FY22	Q3FY23	YoY (%)	QoQ (%)	Comments
Revenue	1,872.0	1,851.6	1,582.0	1,882.0	18.3	-0.5	The product segment grew by 40% YoY to ₹ 1486 crore, while services declined by ~24% YoY% QoQ to ₹ 382 crore
Other Income	24.0	4.0	31.0	9.0	-22.6	166.7	
Cost of raw material	812.0	814.7	986.0	842.0	-17.6	-3.6	
Purchase of traded goods	1.0	0.0	0.0	0.0	NA	NA	
Employee Expenses	262.0	259.2	237.0	253.0	10.5	3.6	
(Increase) / decrease in inventories	29.0	64.8	-161.0	75.0	-118.0	-61.3	
Other Expenses	512.0	453.6	429.0	469.0	19.3	9.2	
EBITDA	256.0	259.2	91.0	243.0	181.3	5.3	
EBITDA Margin (%)	13.7	14.0	5.8	12.9	792 bps	76 bps	Margins expansion driven by revenues mix as product segment has superior margins
Depreciation	78.0	83.0	92.0	78.0	-15.2	0.0	
Interest	89.0	86.7	69.0	78.0	29.0	14.1	
Total Tax	34.0	23.6	-11.0	23.0			
PAT	65.0	75.0	-23.0	50.0	LP	30.0	

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

(₹ Crore)	FY24E			FY25E			Comments
	Old	New	% Change	Old	New	% Change	
Revenue	8,195.8	7,870.2	-4.0	8,985.4	8,654.3	-3.7	Realign estimates
EBITDA	1,270.7	1,221.4	-3.9	1,437.7	1,384.7	-3.7	
EBITDA Margin (%)	15.5	15.5	1 bps	16.0	16.0	0 bps	
PAT	479.9	435.4	-9.3	587.2	539.0	-8.2	
EPS (₹)	12.1	10.9	-9.3	14.8	13.6	-8.2	

Source: Company, ICICI Direct Research

Financial Summary

Exhibit 3: Profit & loss statement (₹ crore)				
(Year-end March)	FY22	FY23	FY24E	FY25E
Total operating Income	5,754.3	6,926.0	7,870.2	8,654.3
Growth (%)	19.3	20.4	13.6	10.0
Cost of raw materials	2,864.6	3,299.0	3,658.1	3,981.0
Employee Expenses	870.7	912.0	1,180.5	1,298.1
Administrative Expenses	1,484.2	1,824.0	1,810.1	1,990.5
Total Operating Expenditure	5,219.4	6,035.0	6,648.8	7,269.6
EBITDA	534.8	891.0	1,221.4	1,384.7
Growth (%)	-34.0	66.6	37.1	13.4
Depreciation	325.5	309.0	330.5	363.5
Interest	241.4	311.0	354.2	346.7
Other Income	59.3	41.0	28.0	30.0
Exceptional Items	(30.2)	104.0	-	-
PBT	57.4	208.0	564.7	704.5
Minority Interest	(14.6)	(13.0)	(12.0)	(12.0)
Profit from Associates	4.7	4.0	5.0	5.0
Total Tax	14.7	84.0	146.2	182.5
PAT	62.0	141.0	435.4	539.0
Growth (%)	-77.5	127.6	208.8	23.8
EPS (₹)	1.6	3.5	10.9	13.6

Source: Company, ICICI Direct Research,

Exhibit 4: Cash flow statement (₹ crore)				
(Year-end March)	FY22	FY23	FY24E	FY25E
Profit after Tax	62.0	141.0	435.4	539.0
Add: Depreciation	325.5	309.0	330.5	363.5
Add: Interest paid	241.4	311.0	354.2	346.7
(Inc)/dec in Current Assets	-410.3	-189.7	-638.6	-528.2
Inc/(dec) in CL and Provisions	228.6	-254.1	390.2	324.0
Others	0.0	0.0	0.0	0.0
CF from operating activities	447.1	317.2	871.7	1,045.0
(Inc)/dec in Investments	211.1	-43.9	0.0	0.0
(Inc)/dec in Fixed Assets	-400.8	-274.6	-350.0	-200.0
Others	-102.1	22.7	0.0	0.0
CF from investing activities	-291.8	-295.7	-350.0	-200.0
Issue/(Buy back) of Equity	0.2	0.1	0.0	0.0
Inc/Dec in Minority Interest	-12.4	-81.7	-4.0	0.0
Issue of Preference Shares	0.0	0.0	0.0	0.0
Inc/(Dec) in loan funds	472.3	355.6	-200.0	-100.0
Interest paid	-241.4	-311.0	-354.2	-346.7
Others	-121.1	-7.1	-59.2	-159.1
CF from financing activities	97.7	-44.0	-617.4	-605.8
Net Cash flow	253.0	-22.6	-95.7	239.2
Opening Cash	276.6	529.6	507.0	411.4
Closing Cash	530	507	411	651

Source: Company, ICICI Direct Research

Exhibit 5: Balance Sheet (₹ crore)				
(Year-end March)	FY22	FY23	FY24E	FY25E
Liabilities				
Equity Capital	79.6	79.7	79.7	79.7
Reserve and Surplus	1,877.1	2,011.0	2,387.3	2,767.2
Total Shareholders funds	1,956.7	2,090.7	2,467.0	2,846.9
Total Debt	3,311.4	3,667.0	3,467.0	3,367.0
Others	656.8	468.0	464.0	464.0
Total Liabilities	5,924.9	6,225.7	6,397.9	6,677.9
Assets				
Gross Block	5,095.4	5,495.4	5,845.4	6,045.4
Less: Acc Depreciation	2,053.4	2,474.4	2,805.0	3,168.4
Net Block	3,042.0	3,021.0	3,040.5	2,877.0
Capital WIP	142.4	129.0	129.0	129.0
Goodwill	296.0	225.0	225.0	225.0
Total Fixed Assets	3,480.4	3,375.0	3,394.5	3,231.0
Investments	388.2	361.0	361.0	361.0
Inventory	920.2	832.0	948.7	1,043.3
Debtors	1,706.5	1,822.0	2,070.0	2,276.2
Loans and Advances	131.6	132.0	150.0	164.9
Other Current Assets	1,715.1	1,877.0	2,132.9	2,345.4
Cash	529.6	507.0	411.4	650.6
Total Current Assets	5,002.9	5,170.0	5,712.9	6,480.4
Creditors	2,420.0	2,152.0	2,445.4	2,689.0
Provisions	25.3	66.0	75.0	82.5
Other current liabilities	670.8	644.0	731.8	804.7
Total Current Liabilities	3,116.1	2,862.0	3,252.2	3,576.2
Net Current Assets	1,886.8	2,308.0	2,460.8	2,904.2
Other non current assets	169.5	181.7	181.7	181.7
Application of Funds	5,924.9	6,225.7	6,397.9	6,677.9

Source: Company, ICICI Direct Research

Exhibit 6: Key ratios				
(Year-end March)	FY22	FY23	FY24E	FY25E
Per share data (₹)				
EPS	1.6	3.5	10.9	13.6
Cash EPS	9.7	11.3	19.3	22.7
BV	49.2	52.6	62.0	71.6
DPS	2.0	1.0	4.0	4.0
Cash Per Share	51.6	62.2	70.5	79.7
Operating Ratios (%)				
EBITDA Margin	9.3	12.9	15.5	16.0
EBIT Margin	3.6	8.4	11.3	11.8
PAT Margin	2.8	3.5	5.5	6.2
Inventory days	58.4	43.8	44.0	44.0
Debtor days	108.2	96.0	96.0	96.0
Creditor days	153.5	113.4	113.4	113.4
Return Ratios (%)				
RoE	8.3	11.7	17.6	18.9
RoCE	5.7	12.0	16.8	19.0
RoIC	4.1	10.5	15.1	16.9
Valuation Ratios (x)				
P/E	100.8	44.3	14.3	11.6
EV / EBITDA	16.9	10.5	7.6	6.4
EV / Net Sales	1.6	1.4	1.2	1.0
Market Cap / Sales	1.1	0.9	0.8	0.7
Price to Book Value	3.2	3.0	2.5	2.2
Solvency Ratios				
Net Debt/EBITDA	3.0	5.2	3.5	2.5
Net Debt / Equity	1.2	1.4	1.5	1.2
Current Ratio	2.1	1.8	2.1	2.1
Quick Ratio	1.8	1.5	1.7	1.7

Source: Company, ICICI Direct Research

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Sell: <-15%



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