



Tulip Telecom

STOCK INFO.	BLOOMBERG
BSE Sensex: 20,310	TTSL IN
	REUTERS CODE
S&P CNX: 6,122	TULP.BO

15 November 2010

Buy

Rs179

Previous Recommendation: Buy

Equity Shares (m)	145.0
52-Week Range (Rs)	214/158
1,6,12 Rel. Perf. (%)	0/-20/-26
M.Cap. (Rs b)	26.0
M.Cap. (US\$ b)	0.6

YEAR	NET SALES	PAT	EPS	EPS	P/E	P/BV	ROE	ROCE	EV/	EV/
END	(RS M)	(RS M)	(RS)	GROWTH (%)	(X)	(X)	(%)	(%)	SALES	EBITDA
3/09A	16,144	2,505	14.7	35.3	12.1	4.5	44.5	17.8	2.1	10.0
3/10A	19,664	2,755	17.0	15.0	10.6	3.1	34.2	16.4	1.7	6.5
3/11E	24,123	3,323	20.5	20.6	8.8	2.4	30.8	16.3	1.5	5.4
3/12E	29,941	4,457	27.4	34.1	6.5	1.8	31.0	18.1	1.1	3.9

- **Operating performance broadly in line:** Tulip Telecom's 2QFY11 operating performance was broadly in line. Revenue increased 19.1% YoY and 11.4% QoQ to Rs5.85b (est of Rs5.77b). EBITDA grew 28.8% YoY and 15.3% QoQ to Rs1.63b (est of Rs1.59b). EBITDA margin has expanded due to 1) shift in the revenue mix from wireless to fibre, 2) bulk purchase of bandwidth and 3) economies of scale. Reported PAT increased by 50.8% YoY and 21.7% QoQ to Rs781m (1.6% above est). Net capex of ~Rs1.2b incurred during 2QFY11 (Rs2.4b in 2HFY11) is in line with the FY11 guidance of Rs4.5b.
- **Fiber constituted 30-35% of order input in 2QFY11; contribution to increase going forward:** Fiber constituted 30-35% of the order input for 2QFY11. Tulip has guided that 2/3rd of it revenue will come from fiber by FY12. Tulip has laid 6,000 kms of intra-city fiber for 'last mile' across 300 cities.
- **Net debt up by ~Rs2b on investment in Qualcomm BWA venture:** Net debt increased by Rs2.05b QoQ (~21% QoQ) to Rs11.6b. During the quarter, Tulip invested ~Rs1.4b for a 13% stake in the Qualcomm's BWA venture. Qualcomm had won BWA spectrum in four circles - Delhi, Mumbai, Haryana, and Kerala. Net debt/equity increased from 0.96x in 1QFY11 to 1.08x in 2QFY11. Net debt/annualised EBITDA is at 1.8x (vs 1.7x in 1QFY11).
- **Estimates unchanged; 27% EPS CAGR; maintain Buy:** Given in line 2QFY11 results, our estimates are largely unchanged. We expect an EPS CAGR of ~27% over FY10-12E. The stock trades at 8.8x FY11 EPS of Rs20.5 (~5.4x EV/EBITDA) and 6.5x FY12 EPS of Rs27.4 (3.9x EV/EBITDA). Maintain **Buy** with a target of Rs250.

QUARTERLY PERFORMANCE (CONSOLIDATED)

Y/E MARCH	FY10				FY11				(RS MILLION)	
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE	FY10	FY11E
Gross Revenue	4,429	4,910	5,009	5,307	5,252	5,850	6,256	6,765	19,664	24,123
YoY Growth (%)	33.2	27.7	15.0	15.0	18.6	19.1	24.9	27.5	21.8	22.7
QoQ Growth (%)	-4.0	10.9	2.0	5.9	-1.0	11.4	6.9	8.1		
Total Operating Expenses	3,343	3,642	3,659	3,762	3,834	4,217	4,447	4,772	14,409	17,270
EBITDA	1,086	1,268	1,350	1,545	1,417	1,634	1,809	1,993	5,255	6,853
YoY Growth (%)	66.0	56.5	48.0	56.0	30.5	28.8	34.0	29.0	56.1	30.4
QoQ Growth (%)	9.6	16.8	6.5	14.4	-8.3	15.3	10.7	10.2		
Margin (%)	24.5	25.8	27.0	29.1	27.0	27.9	28.9	29.5	26.7	28.4
Net Finance Costs	158	187	186	185	185	190	218	237	716	829
Non-Operating Income	271	37	104	57	-13	14	50	61	468	111
Depreciation & Amortization	353	436	409	155	375	420	445	466	1,353	1,705
Profit before Tax	846	682	858	1,262	844	1,038	1,196	1,352	3,654	4,430
Income Tax Expense / (Income)	96	164	172	467	203	258	297	350	899	1,108
Reported Net Profit / (Loss)	750	518	686	795	642	781	900	1,001	2,755	3,323
YoY Growth (%)	63.2	3.2	41.0	-24.8	-14.5	50.8	31.1	25.9	10.0	20.6
QoQ Growth (%)	-29.0	-31.0	32.6	15.9	-19.3	21.7	15.2	11.3		
Margin (%)	16.9	10.5	13.7	15.0	12.2	13.3	14.4	14.8	14.0	13.8

E: MOSL Estimates

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Operating performance broadly in line

- Tulip Telecom reported strong 2QFY11 with PAT up 51% YoY and 22% QoQ to Rs781m (est of Rs768m).
- Revenue increased 19.1% YoY and 11.4% QoQ to Rs5.85b (est of Rs5.77b) led by strong performance in fiber as well as wireless segments.
- EBITDA grew 28.8% YoY and 15.3% QoQ to Rs1.63b (est of Rs1.59b).
- EBITDA margin increased to 27.9%, up 210bp YoY and 93bp QoQ (vs est of 27.5%).
- The company has been enhancing fiber 'last mile' reach in major towns/cities; Tulip's intra-city fiber network spans over 6,000 km.
- Tulip has procured APDRP projects in Uttar Pradesh, Gujarat, Uttarakhand and Punjab having cumulative project value of ~Rs2b over 3-5 years.
- Tulip has a diversified client base of 1,800 spread over 2,000 locations.

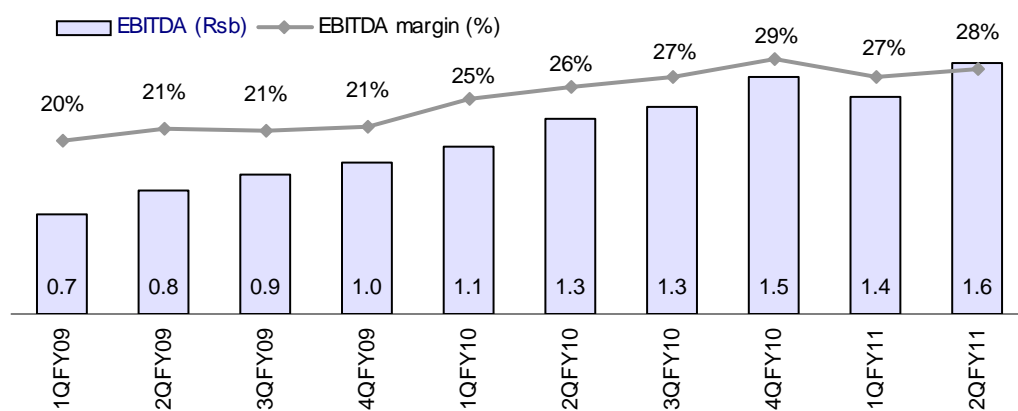
Net debt up by ~Rs2b to ~Rs11.6b on investment in Qualcomm BWA venture

- Net debt increased by Rs2.05b QoQ (~21% QoQ) to Rs11.6b.
- During the quarter, Tulip invested ~Rs1.4b for a 13% stake in the Qualcomm's BWA venture.
- Qualcomm had won BWA spectrum in four circles - Delhi, Mumbai, Haryana, and Kerala.
- Net debt/equity increased from 0.96x in 1QFY11 to 1.08x in 2QFY11.
- Net debt/annualised EBITDA is at 1.8x (vs 1.7x in 1QFY11).

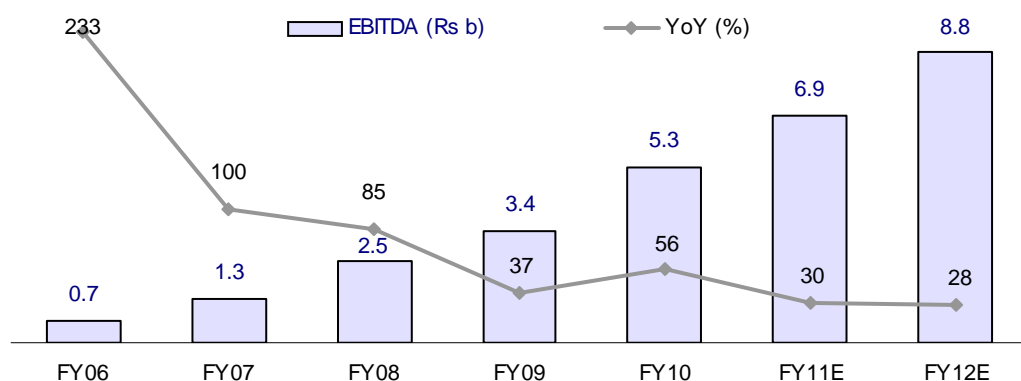
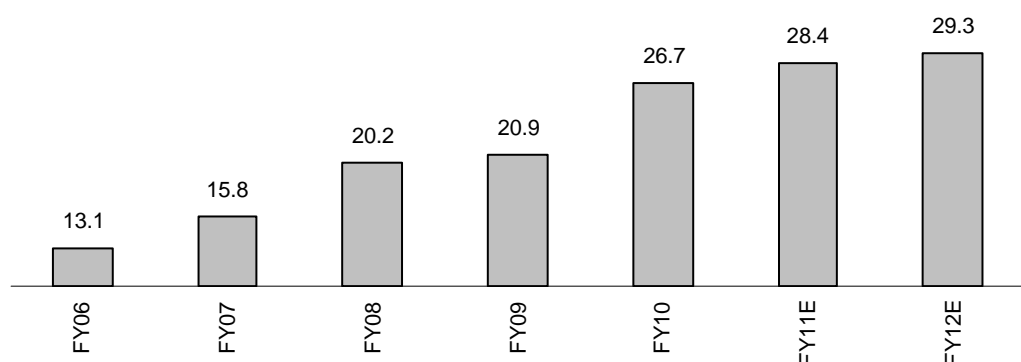
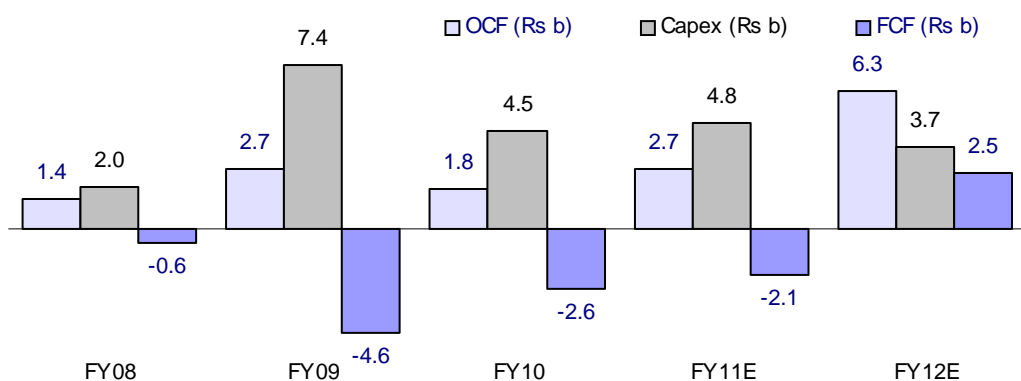
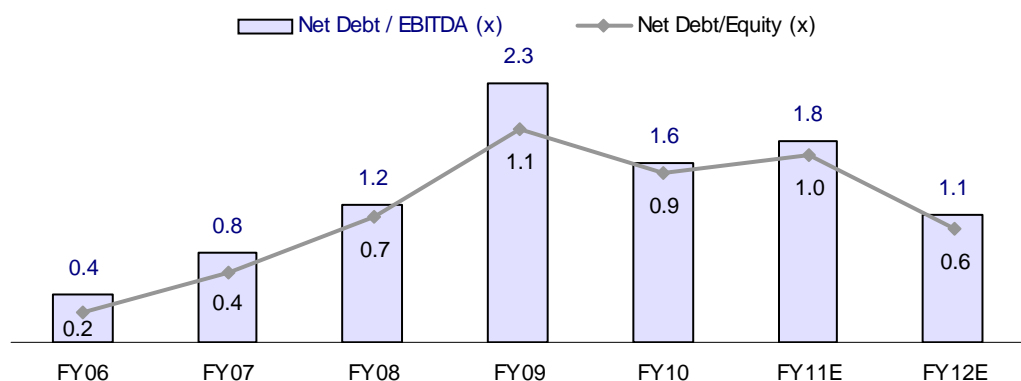
Estimates unchanged; 27% EPS CAGR; maintain Buy

Given in line 2QFY11 results, our estimates are largely unchanged. We expect an EPS CAGR of ~27% over FY10-12E. The stock trades at 8.8x FY11 EPS of Rs20.5 (~5.4x EV/EBITDA) and 6.5x FY12 EPS of Rs27.4 (3.9x EV/EBITDA). Maintain Buy with a target of Rs250.

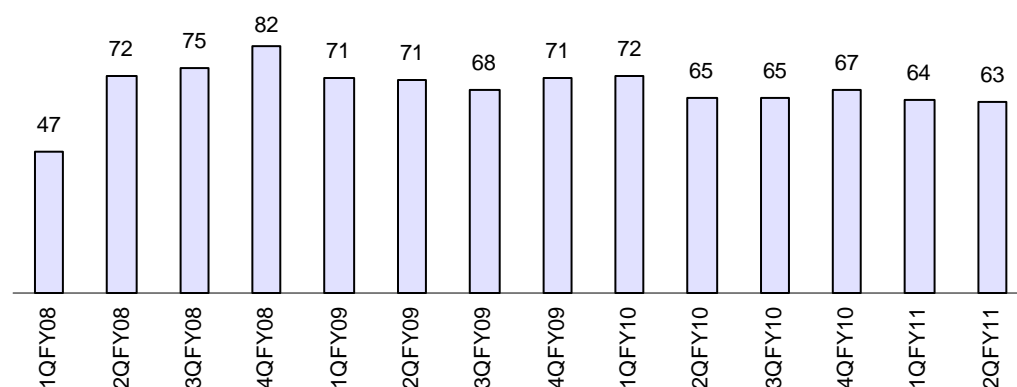
Tulip: Quarterly EBITDA and EBITDA margin



Source: Company/MOSL

FY10-12 EBITDA CAGR of 29%**EBITDA margin likely to improve further (%)****We expect FCF inflection in FY12****Leverage expected to climb down**

Source: Company/MOSL

RM cost declining (% of revenue)

Source: Company/MOSL

Highlights from 2QFY11 earnings call:

- Tulip has won R-APDRP projects in Uttar Pradesh, Gujarat, Uttarakhand and Punjab having cumulative project value of ~Rs2b over 3-5 years; Tulip is confident of winning similar projects for other states in India by end of FY11.
- Capex guidance is Rs4.5b for FY11 and Rs4b for FY12; capex as % of cash accruals is expected to decline in FY12.
- Forex gain amounting to ~Rs110m has been adjusted in the gross block in line with Tulip's accounting policy (changed in 1QFY11).
- Qualcomm would exit its BWA venture at a suitable time and invite telecom operators to partner. Tulip has an option to exit the BWA venture along with Qualcomm. It will evaluate the proposal at the time of Qualcomm's exit.
- Wireless last mile business will continue to record growth despite increasing fiber contribution; there are potential opportunities in the rural areas (especially from the government) which can be catered to using the wireless last mile.
- The increase in debtor days was on account of new product offerings (focussing on fiber). The management is conscious of the increase and is confident of driving it down in future.
- Network integration constitutes less than 10% of revenue.

TULIP TELECOM: SUMMARY OF ESTIMATE CHANGE (RS B)

	FY11E	FY12E
Revenue (Rs b)		
Old	23.8	29.6
New/Actual	24.1	29.9
Change (%)	1.1	1.1
EBITDA (Rs b)		
Old	6.7	8.7
New/Actual	6.9	8.8
Change (%)	2.4	1.2
Net Profit (Rs b)		
Old	3.3	4.5
New/Actual	3.3	4.5
Change (%)	1.4	-0.5
Diluted EPS (Rs)		
Old	20.2	27.6
New/Actual	20.5	27.4
Change (%)	1.4	-0.5
Depreciation (Rs b)		
Old	1.7	2.1
New/Actual	1.7	2.1
Change (%)	3.2	2.4
Net finance cost (Rs b)		
Old	0.8	0.8
New/Actual	0.8	0.8
Change (%)	-1.1	10.7
EBITDA margin (%)		
Old	28.1	29.3
New/Actual	28.4	29.3
Change (bp)	35	1
Tax rate (%)		
Old	24.0	25.0
New/Actual	25.0	25.0
Change (bp)	100	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. Tulip has an outstanding track record, having scaled up to a dominant ~30% market share in the largest and fastest growing VPN segment within five years. Tulip has network presence in ~2,000 cities and a client base of ~1,800.

Key investment argument

- Tulip has laid 6,000 kms 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; Contribution to revenues by fiber is expected to increase to ~70% by FY12.
- Growth in wireless connectivity and increased traction from fiber rollout should support ~23% CAGR in revenue and ~27% CAGR in EPS during FY10-12E.
- 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.

Recent developments

- Tulip has been awarded R-APDRP (Restructured - Accelerated Power Development Reforms Program) projects in UP, Gujarat, Uttarakhand and Punjab with a combined order value of Rs2b over 3-5 years.
- The company has also been awarded an order for managed services for Gujarat SWAN (State Wide Area Network) valued at Rs250m for a period of 3-5 years.
- Tulip has acquired a 13% stake in Qualcomm's BWA venture for a consideration of ~Rs1.4b
- FCC license obtained in USA (serving as a landing station abroad) would enable the company to provide data connectivity to Indian clients to USA.
- Tulip is setting up 6 POPs (Point Of Presence) for ILD (International Long Distance) services - one each in West coast & East coast of USA, one in London, one in Singapore and two in India which will act as gateways. The capex incurred on this project would be ~Rs150m.

Valuation and view

- Given in line 2QFY11 results, our estimates are largely unchanged.
- We expect an EPS CAGR of ~27% over FY10-12E.
- The stock trades at 8.8x FY11 EPS of Rs20.5 (~5.3x EV/EBITDA) and 6.5x FY12 EPS of Rs27.4 (3.9x EV/EBITDA). Maintain **Buy** with a target of Rs250.

Comparative valuations

		Tulip	Bharti	Idea
P/E (x)	FY11E	8.8	17.3	37.9
	FY12E	6.5	14.0	26.0
EV/EBITDA (x)	FY11E	5.4	8.4	9.6
	FY12E	3.9	6.4	6.9
EV/Sales (x)	FY11E	1.5	2.9	2.3
	FY12E	1.1	2.3	1.9
P/BV (x)	FY11E	2.4	2.2	1.9
	FY12E	1.8	1.9	1.8

Shareholding Pattern (%)

	Sep-10	Jun-10	Sep-09
Promoter	69.0	69.0	69.0
Domestic Inst	2.0	1.4	2.0
Foreign	21.1	25.1	23.0
Others	7.9	4.6	6.1

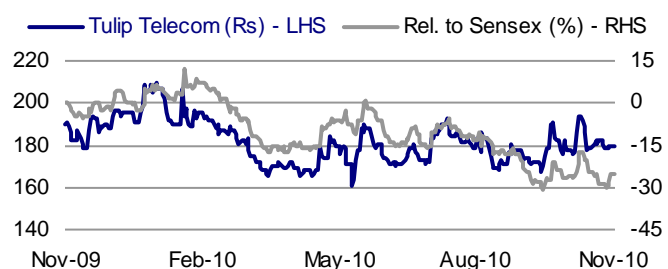
EPS: MOSL forecast v/s consensus (Rs)

	MOSL Forecast	Consensus Forecast	Variation (%)
FY11	20.5	20.1	2.2
FY12	27.4	24.4	12.2

Target Price and Recommendation

Current Price (Rs)	Target Price (Rs)	Upside (%)	Reco.
179	250	39.7	Buy

Stock performance (1 year)



Financials and Valuation

INCOME STATEMENT		(Rs Million)			
Y/E MARCH	2009	2010	2011E	2012E	
Revenues	16,144	19,664	24,123	29,941	
Change (%)	32.7	21.8	22.7	24.1	
Total Expenses	12,777	14,409	17,270	21,178	
EBITDA	3,367	5,255	6,853	8,763	
% of Gross Sales	20.9	26.7	28.4	29.3	
Change (%)	37.1	56.1	30.4	27.9	
Depn. & Amortization	414	1,353	1,705	2,114	
EBIT	2,953	3,902	5,148	6,649	
Net Interest	462	716	829	837	
PBT	2,835	3,654	4,430	5,942	
Tax	330	899	1,108	1,486	
Rate (%)	11.6	24.6	25.0	25.0	
Adjusted PAT	2,505	2,755	3,323	4,457	
Change (%)	33.9	10.0	20.6	34.1	
PAT after EO	2,505	2,755	3,323	4,457	

BALANCE SHEET		(Rs Million)			
Y/E MARCH	2009	2010	2011E	2012E	
Share Capital	290	290	290	290	
Additional Paid up Capital	831	831	831	831	
Reserves	5,694	8,155	11,206	15,299	
Net Worth	6,815	9,276	12,327	16,420	
Loans	11,224	11,886	13,806	12,423	
Other Liabilities	9	29	29	29	
Capital Employed	18,049	21,191	26,163	28,872	
Gross Block	13,209	15,443	20,284	23,807	
Less : Depreciation	1,061	2,414	4,119	6,233	
Net Block	12,148	13,030	16,165	17,574	
Curr. Assets	8,722	10,973	12,809	14,803	
Inventories	916	688	844	1,047	
Debtors	3,242	5,302	8,456	9,446	
Cash & Bank Balance	3,470	3,456	1,500	2,500	
Other Current Assets	1,094	1,527	2,009	1,809	
Curr. Liab. & Prov.	2,822	2,812	2,812	3,505	
Net Curr. Assets	5,901	8,161	9,997	11,298	
Appl. of Funds	18,049	21,191	26,162	28,872	

E: MGLSL Estimates

RATIOS					
Y/E MARCH	2009	2010	2011E	2012E	
Basic (Rs)					
EPS	14.7	17.0	20.5	27.4	
Cash EPS	17.2	25.3	30.9	40.4	
Book Value	40.1	57.1	75.9	101.1	
DPS	0.8	1.7	1.7	2.2	
Payout % (Incl.Div.Taxes)	5.4	9.9	8.2	8.2	
Valuation (x)					
P/E	12.1	10.6	8.8	6.5	
Cash P/E	10.4	7.1	5.8	4.4	
EV/EBITDA	10.0	6.5	5.4	3.9	
EV/Sales	2.1	1.7	1.5	1.1	
Price/Book Value	4.5	3.1	2.4	1.8	
Dividend Yield (%)	0.4	0.9	0.9	1.3	
Profitability Ratios (%)					
RoE	44.5	34.2	30.8	31.0	
RoCE	17.8	16.4	16.3	18.1	
Turnover Ratios					
Debtors (Days)	73	98	128	115	
Asset Turnover (x)	1.46	1.22	1.18	1.25	
Leverage Ratio					
Debt/Equity Ratio(x)	1.6	1.3	1.1	0.8	

CASH FLOW STATEMENT		(Rs Million)			
Y/E MARCH	2009	2010	2011E	2012E	
Op.Profit(Loss) bef Tax	3,367	5,255	6,853	8,763	
Other Income	344	468	111	130	
Interest Paid	-462	-716	-829	-837	
Direct Taxes Paid	-330	-879	-1,108	-1,486	
(Inc)/Dec in Wkg. Cap.	-172	-2,279	-2,310	-301	
CF from Op.Activity	2,747	1,848	2,718	6,270	
(inc)/Dec in FA + C/WIP	-7,365	-2,234	-4,841	-3,523	
(Pur)/Sale of Investments	0	-18	-1,482	0	
CF from Inv.Activity	-7,365	-2,253	-6,322	-3,523	
Issue of Shares	0	0	0	0	
Inc/(Dec) in Debt	2,286	661	1,921	-1,383	
Other Financing Activities	-137	-273	-273	-366	
CF from Fin.Activity	2,151	390	1,649	-1,747	
Incl(Dec) in Cash	-2,468	-14	-1,956	1,000	
Add: Opening Balance	5,938	3,470	3,456	1,500	
Closing Balance	3,470	3,455	1,500	2,500	



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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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