

Tulip IT Services (TULITS)

RESULT UPDATE ✓

Current price Rs 980	Target price Rs 1230
Potential upside 25.5%	Time Frame 12 months

WHAT'S CHANGED...

PRICE TARGET.....	Rs 1230 from Rs 1185
EPS (FY08E).....	Rs 68.60 from Rs 63.95
EPS (FY09E).....	Rs 88.60 from Rs 80.65
RATING.....	Outperformer from Performer

OUTPERFORMER

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Tulip IT Services recorded strong results for Q3FY08 with a top line of Rs 333.13 crore (28.9% y-o-y growth and 50% q-o-q growth). Bottom line was Rs 54.09 crore (97% y-o-y growth and 37.08% q-o-q increase). The robust results were on the back of higher-than-expected revenue growth in IP/VPN. EBIDTA margin grew 71 bps and PAT margin were up 189 bps as the company get tax benefits in IP/VPN business. Based on the growth estimates, we are upgrading our target price to Rs 1230 and change our rating to outperformer.

Positive surprise from IP/VPN

The IP/VPN segment continued to post healthy numbers on back of higher-than-expected connects (93,711 against our estimates of 91,800) and a surprise 23.7% increase in ARPU from old customers that resulted in a top-line growth of 38.9% from this vertical. It also contributed more than 55% to total top-line, which helped in margin expansion of more than 71 bps. Going forward, we expect demand for wireless connectivity to remain robust. However, there might be some pressure on the ARPU as newer customers might require lesser bandwidth and competition catching up soon.

Network integration to grow at a steady rate

The legacy business of network integration grew 18.3% q-o-q and 6.7% y-o-y. These numbers are expected to increase in Q4 due to seasonality in the business. We also expect revenues from SWAN to accrue from Q1FY09 as Haryana is ready to be handed over to the state government and work is on for West Bengal and Assam. New business of data centres is expect to complement network integration business and could contribute significantly only post Q2FY09 as occupancy levels increase to above 30% (needed to breakeven).

Valuation

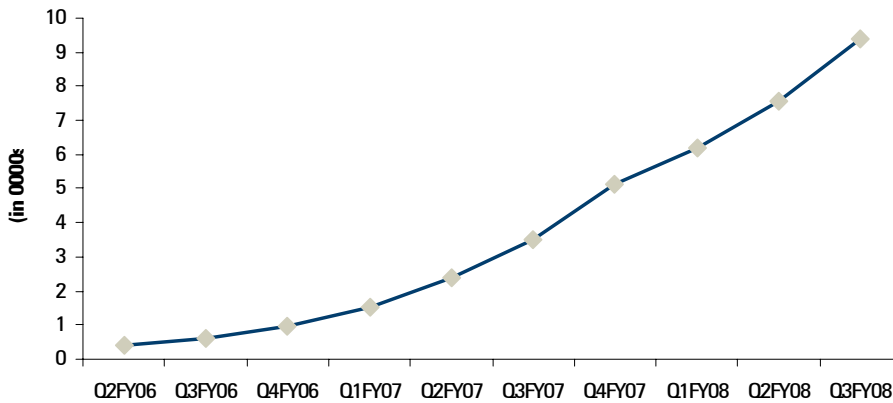
Tulip continued to show robust numbers and strong growth in the IP/VPN segment. On back of higher-than-expected connect and the surprise increase in ARPU, we are upgrading our estimates for both FY08 and FY09 and change our rating to outperformer. A SOTP valuation gives us a target price of Rs 1,230.

Key Financials

Year to March	Q3FY08	Q2FY08	% change	Q3FY07	% change (y-o-y)
Revenues	333.13	258.44	28.9	221.99	50
COGS	233.65	193.03	21.0	170.80	37
Employee expense	14.62	8.66	68.8	7.58	93
Other expenses	16.10	5.23	207.8	4.34	271
EBIDTA	68.76	51.52	33.5	39.27	75
EBIDTA margin (%)	20.6%	19.9%	3.5%	17.7%	17%
Other income	8.38	6.44	30.1	0.18	4555
Interest	6.57	6.11	7.5	3.81	72
Depreciation	12.43	10.72	16.0	5.72	117
PBT	58.14	41.13	41.3	29.92	94
Tax	4.04	4.05	-0.2	2.44	66
PAT	54.09	37.08	45.9	27.48	97

Source: Company, ICICIdirect Research

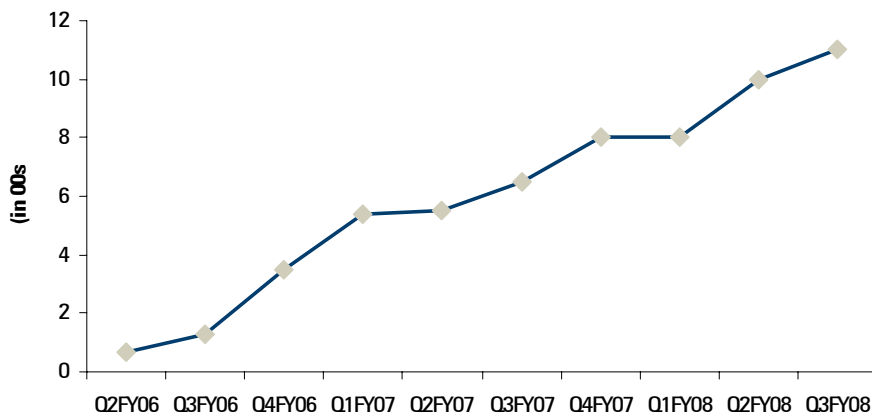
Exhibit 1: Steady increase in number of connects



We expect connects to increase from 93,811 in Q3FY08 to 167,700 in FY09

Source: Company, ICICIdirect Research

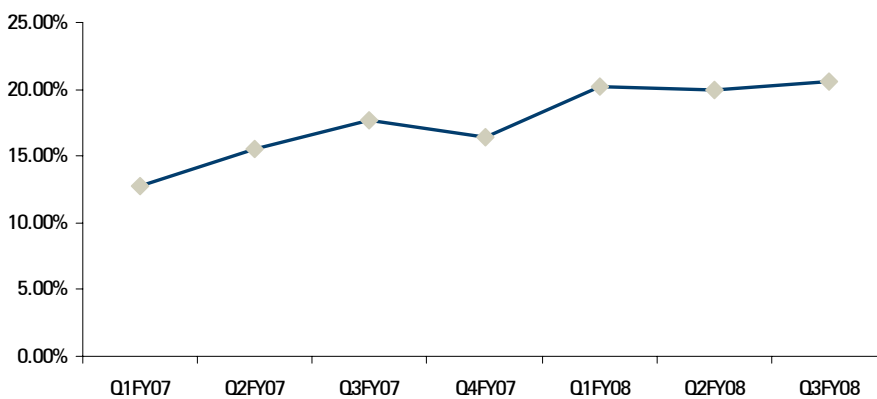
Exhibit 2: Steady increase in number of cities covered



Increasing the city penetration helps the company to bring in more clients

Source: Company, ICICIdirect Research

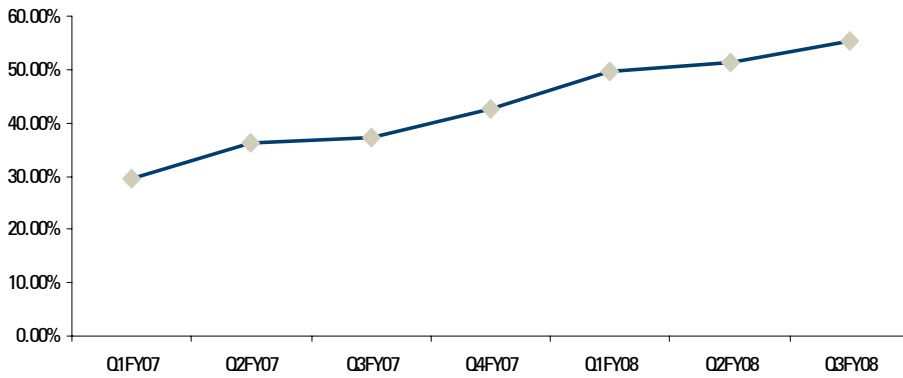
Exhibit 3: Expansion in EBIDTA margins on back of increase in IP/VPN share



IP/VPN having margins in range of 32% to increase blended EBIDTA margins above 20% range

Source: Company, ICICIdirect Research

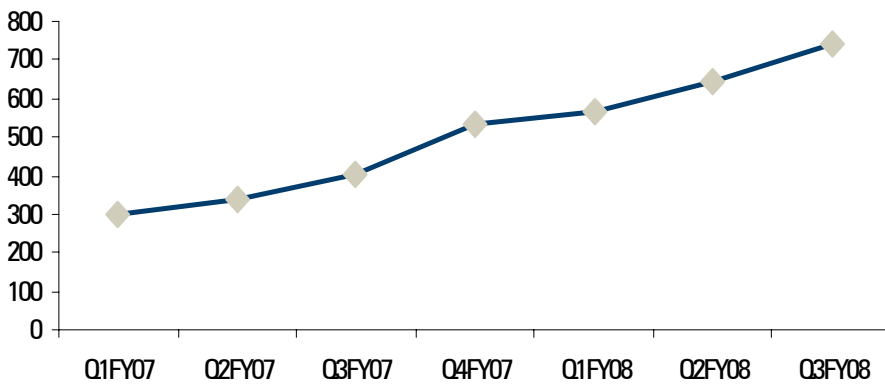
Exhibit 4: Contribution of IP/VPN increasing steadily



With increasing connects and higher realizations we expect IP/VPN to continue having above 50% contribution

Source: Company, ICICIdirect Research

Exhibit 5: Robust client addition



Source: Company, ICICIdirect Research

Exhibit 6: Data centres to complement network integration

City	Capacity (racks)	Area (sq ft)	
Delhi	450	8000	→ <i>Already operation with one large client</i>
Mumbai	2000	35000	
Bangalore	150	3000	
Chennai	150	3000	

We expect data centre to start contributing significantly only from FY10 as utilization increases

Source: Company, ICICIdirect Research

FINANCIAL SUMMARY

Profit and loss statement

	(Rs crore)			
(Year-end March)	FY06	FY07	FY08E	FY09E
Sales	508.17	840.79	1188.12	1367.34
% Growth	NA	65.45%	41.31%	15.08%
Op Profit	66.43	132.80	244.17	316.91
% Growth	NA	99.90%	83.86%	29.79%
Other Income	1.18	2.35	18.00	18.00
Depreciation	4.30	15.84	40.22	54.51
EBIT	62.14	116.96	203.95	262.39
% Growth	NA	88.24%	74.37%	28.66%
Interest	6.35	13.07	11.55	9.63
Profit before Tax	56.96	106.24	210.40	270.77
% Growth	NA	86.52%	98.03%	28.69%
Taxation	7.97	9.27	11.47	13.84
Net Profit	48.99	96.97	198.93	256.93
% Change YoY	NA	97.93%	105.15%	29.16%

Balance Sheet

	(Rs crore)			
(Year-end March)	FY06	FY07	FY08E	FY09E
Equity Share Capital	29.00	29.00	29.00	29.00
Reserves & Surplus	157.58	250.50	439.25	686.00
Secured Loans	75.58	141.60	125.50	100.00
Unsecured Loans	0.00	0.00	600.00	600.00
Deferred Tax Liability	0.19	0.80	0.00	0.00
Current Liabilities and Prov	45.40	61.21	82.17	96.54
Total Liabilities	307.75	483.11	1275.92	1511.53
Gross Block	80.02	250.03	517.74	705.34
Accumulated Depreciation	7.30	22.91	63.13	117.65
Net Block	72.72	227.12	454.61	587.69
Capital WIP	0.00	22.62	30.00	50.00
Investments	2.02	0.02	0.02	0.02
Cash	1.01	2.46	407.34	446.54
Inventories	26.25	20.52	76.53	82.74
Trade Recievables	145.68	139.78	220.34	251.63
Loans and Advances	14.24	36.50	53.00	58.83
Fixed Deposit Receipts	45.74	34.00	34.00	34.00
Misc Exp	0.07	0.06	0.06	0.06
Total Assets	307.74	483.09	1275.90	1511.51

Cash Flows

	(Rs crore)			
(Year-end March)	FY06	FY07	FY08E	FY09E
Profit after Tax	48.99	96.97	198.93	256.93
Depreciation	4.30	15.84	40.22	54.51
Cash Flow before WC Changes	51.96	116.16	238.35	311.44
Net Increase in Current Liabilities	5.13	15.81	20.96	14.37
Net Increase in Current Assets	-103.07	-10.63	-153.06	-43.33
Cash Flow after WC Changes	-45.98	121.34	106.24	282.48
Purchase of Fixed Assets	-57.40	-192.85	-275.10	-207.60
(Increase) / Decrease in Fixed Deposit Receipt	-37.32	11.74	0.00	0.00
(Increase) / Decrease in Investment	-2.00	2.00	0.00	0.00
Cash Flow from Investing Activities	-96.72	-179.11	-275.09	-207.60
Increase / (Decrease) in Secured Loans	51.82	66.01	-16.10	-25.50
Increase / (Decrease) in Equity Capital	-3.00	0.00	0.00	0.00
Increase / (Decrease) in Share Premium	97.80	0.00	0.00	0.00
Dividend Payment	-3.31	-6.79	-10.18	-10.18
Cash Flow from Financing Activities	143.32	59.23	573.73	-35.68
Op bal Cash & Cash equivalents	0.39	1.01	2.46	407.34
Closing Cash/ Cash Equivalent	1.01	2.46	407.34	446.54

Ratios

	FY06	FY07	FY08E	FY09E
EPS	16.89	33.44	68.60	88.60
Cash EPS	18.38	38.90	82.47	107.39
Book Value	64.34	96.38	161.46	246.55
Operating Profit Per Share	22.91	45.79	84.20	109.28
Operating Margin (%)	13.07%	15.79%	20.55%	23.18%
Net Profit Margin (%)	9.64%	11.53%	16.74%	18.79%
RONW	26.26%	34.69%	42.48%	35.93%
ROCE	23.70%	27.78%	34.35%	32.20%
Debt Equity	0.41	0.51	0.27	0.14
Fixed Assets Turnover Ratio	6.99	3.37	2.45	2.14
Enterprise Value	2914.56	2981.11	2560.14	2495.44
EV/EBIDTA	43.87	22.45	10.49	7.87
EV/Sales	5.74	3.55	2.15	1.83
Sales to Equity	2.72	3.01	2.54	1.91
Market Cap	2842.00	2842.00	2842.00	2842.00
Market Cap to sales	5.59	3.38	2.39	2.08
Price to Book Value	15.23	10.17	6.07	3.97
PE	58.01	29.31	14.29	11.06
Working Capital/Sales	0.37	0.20	0.60	0.57
Debtors Turnover Ratio	0.29	0.17	0.19	0.18
Cash to Absolute Liabilities	0.02	0.04	4.96	4.63
Debtors to Sales	0.29	0.17	0.19	0.18
Effective Tax Rate	13.99%	8.73%	5.45%	5.11%
Dividend Per Share	1.00	2.00	3.00	3.00
Dividend Yield (%)	0.10%	0.20%	0.31%	0.31%

RATING RATIONALE

ICICIDirect endeavours to provide objective opinions and recommendations. ICICIdirect assigns ratings to its stocks according to their notional target price vs current market price and then categorises them as Outperformer, Performer, Hold, and Underperformer. The performance horizon is 2 years unless specified and the notional target price is defined as the analysts' valuation for a stock.

Outperformer: 20% or more

Performer: Between 10% and 20%

Hold: \pm 10% return

Underperformer: -10% or more

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