

Sterlite Technologies Ltd.**Rs 53****Worst is over!****BUY**

Sterlite Technologies Ltd (STL) posted Q3FY11 results which were below our expectations on margins front. STL registered top line of Rs 579 crore against our expectation of Rs 542 crore, de-growth of 33% y-o-y. However insufficient order inflows from PGCIL during the quarter and lower realisations led EBITDA and PAT margins to decline significantly by 460 bps and 555 bps respectively y-o-y (against our estimates of decline of 371bps and 219 bps).

- Net sales at Rs 579 crore (de-growth of 33% y-o-y and growth of 14% q-o-q)
- Employee expenses increased by ~39% y-o-y (+194bps as a % of sales) and other expenses declined by ~16% (in absolute terms) vs 346bps increase as a % of sales.
- EBITDA margins declined significantly by 460bps y-o-y and 1034bps q-o-q, largely on account of increase in cost and execution of lower margin orders.
- Interest expenses increased by ~46% y-o-y due to higher working capital financing cost (average interest rate @ ~8.5%, increase by 200bps).
- Effective tax rate gone up by 474 bps due to higher provisioning for MAT.
- PAT margins dropped substantially by 555bps y-o-y due to higher interest cost and tax rate.
- Order book declined by 21% to Rs 1,700 crore; Export orders- Rs 300 crore; Telecom-Rs 300 crore; Power-Rs 1,400 crore; L1 orders-Rs 600 crore not included above.

Is the worst over?

Our concern during Q2FY11 over delayed order inflows from PGCIL (which commands better margins with protection due to pass-through clause) continued over Q3FY11. However pick up in tendering for conductors from PGCIL is clearly seen with ~50% of total orders during 9MFY11 released in last 3 months. STL bagged ~29% of orders from PGCIL released for conductors in last 3 months. Orders for conductors during current period accounts for 75% of total ordering by PGCIL in FY10. Moreover PGCIL soon expected to start inviting bids for high capacity power transmission corridors (capex of Rs 58,000 crore).

On the Telecom front, we do not see any major concern with slowing demand from China (8% drop in 2010 vs 2009, consumes 42%) which is getting offset by increasing demand from non-Chinese markets (9% up in 2010 vs 2009, consumes 58%). Renewal of order from British Telecom for 2mn fkms can also be seen as positive reference for the company in global markets.

However we believe that increasing competition would force STL to bid more aggressively to maintain order inflows momentum which could dent its margins. Environmental concerns and land issues related with associated power plants may affect PGCIL tendering.

On the back of above, we believe that the worst is over for the company. However we expect that the recovery would not be sharp and contingent upon the order inflows from PGCIL and global demand for optical fiber. Consequently we have revised our estimates for FY11 and FY12 downwards pertaining to lower realisations and lower margins.

Guidance revised downwards, Change in Estimates and Valuations

In light of short term delay in order inflows from PGCIL, management has revised its EBITDA guidance for FY11 to Rs 300 cr vs Rs 400 crore earlier and Rs 400-500 crore for FY12. We have reduced our revenue estimates for FY11E and FY12E by 0.1% and 11% respectively while net profit estimates reduced by 25% and 15% for the same period. Consequently we have also revised our Target Price to Rs 96 with introducing valuation impact from UMTPP.

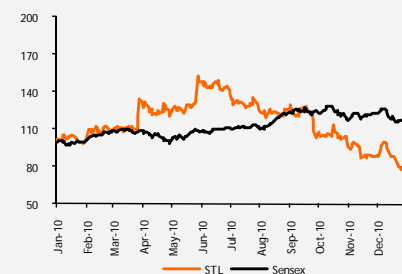
Price Outlook: Rs 96

Market Data	Feb 16 th , 2011
Shares outs (Cr)	35.6
Equity Cap (Rs Cr)	71.2
Mkt Cap (Rs Cr)	1,922
52 Wk H/L (Rs)	124.2/52.0
Avg Vol (1yr avg)	398,754
Face Value (Rs)	2
Bloomberg Code	SOTL IN

Market Info:

SENSEX	18,300
NIFTY	5,494

Price Performance:



Share Holding pattern (%) :

Particulars	Dec-10	Sep-10	Chg
Promoters	50.13	50.15	-0.02
FIIIs	3.28	3.81	-0.53
DIIIs	12.89	15.03	-2.14
Others	33.70	31.01	2.69
Total	100.0	100.0	

Source: BSE

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