November 14, 2019

Sterlite Technologies Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
ST Commercial Paper	450.0	450.0	[ICRA]A1+ reaffirmed
LT Non Convertible Debenture Programme	300.0	300.0	[ICRA]AA(Stable) reaffirmed;
LT Fund based- Working Capital Facilities	790.0	705.0	[[ICRA]AA(Stable) reaffirmed;
LT Fund based-Term Loan	300.0	168.0	[ICRA]AA(Stable) reaffirmed;
ST Non-fund based Facilities	2885.0	2885.0	[ICRA]A1+
LT/ST Interchangeable facilities#	(2885.0)	(2885.0)	[ICRA]AA(Stable)/[ICRA]A1+ reaffirmed;
LT/ST Unallocated	0.0	217.00	[ICRA]AA(Stable)/[ICRA]A1+ reaffirmed;
Total	**4725.0**	**4725.0**	

**Instrument details are provided in Annexure-1*

Rationale

The rating reaffirmation reflects the strong market position of STL in the domestic market and geographically diversified revenue mix. ICRA notes that STL is among the few completely backward integrated players globally with preform manufacturing capabilities, aiding healthy operating margins when compared to other domestic players and a few global players. Being present across the entire spectrum of telecom products starting from preform manufacturing to software products for network integration, STL's clientele spans across all these segments and many countries, lending favourable diversification in client profile. To improve the company's presence in the software segment and further diversify its clientele, STL acquired Impact Data Solutions (IDS), a European cloud infrastructure development company in September 2019, at a total cost of Rs.105 crore. IDS acquisition will help STL in gaining further traction in European market as well as entry into few larger cloud service providers. The ratings are also supported by the strong order book of Rs. 8,137 crore as of September 2019 lending healthy revenue visibility for the next two fiscals. However, it is to be noted that a sizeable portion of these orders are in the services segment and hence there will be elongation of working capital cycle leading to stretched debtors. In services segment, the counterparties are largely domestic government agencies. Any delay in receipts from the counterparties could impact the company's liquidity position and it remains a key rating monitorable. The company primarily relies on back to back contracts with suppliers to match cashflow timings with revenue receipts, thereby containing working capital intensity below 20%.

STL's average realisations in the product segment moderated in H1FY2020, due to decline in optical fibre prices globally , on account of supply overhang amid slowdown in capex by Chinese telecom service providers. There will be some pressure on realizations and STL's product division's profit margins over the next few quarters. The ratings remain constrained by intense competition in the market with presence of large scaled global players with diversified manufacturing base.

Key rating drivers and their description

Credit strengths

Market leader in the domestic Optical Fiber (OF) and Optical Fiber Cable (OFC) market; increasing market share in export markets as well - STL is the leader in the Indian OF and OFC market with market share of ~45%, as per the management. The company is the only fully backward integrated player in India with capability to manufacture glass preforms from silica and the same provides cost competitiveness and hence results in healthy operating margin. STL's revenue mix is fairly diversified across geographies with Europe (24%) and India (64%) accounting for bulk of product revenue, followed by China (4%). The company has been increasing its presence in the export markets with a global market share of ~7%, as per the management. Recent acquisition of Metallurgica Bresciana (MB) and IDS will further help in increasing traction in European market.

Favourable long-term outlook with sizeable investments required to meet projected bandwidth requirement globally- Several markets switched to 5G following the introduction of new 5G-compatible smartphones during CY2019. As 5G devices increasingly become available and more service providers launch 5G, over 10 million 5G subscriptions are projected worldwide by the end of 2019.5G networks would require denser optical fibres with low latency. The deployment of optical fibres would increase with introduction of 5G, increasing demand prospects for optical fibre manufacturers globally. While there is supply overhang issue in the near term, overall outlook for OF/OFC remain favourable over the long term due to increasing digitization as well as higher bandwidth requirement.

Diversified customer base in the domestic and international markets- The company's product profile spans from preforms to network integration software products. STL has reputed clientele across countries and for different products, ranging from telcos, government agencies, private organizations and cloud companies.

Credit challenges

Reduction in OF and OFC realisations due to supply overhang will pressurise profitability; persisting low offtake from China could impact realisations going forward- OF realisations dropped in the international market because of supply overhang, as China which alone accounted for about half of global OF production witnessed reduction in demand. While long-term contracts remained largely unaffected due to annual reset of prices, spot market sales were impacted. The company derived ~20% of its total sales from the OF spot market. STL's realisations dropped by 6% in Q1FY2020 in the product segment. Given expected decline in global OF demand during CY2019, the overall realization is likely to remain suppressed over the next 2-3 quarters. Hence, there will be some pressure on STL's product division margin over the next few quarters.

Increase in share of services business could elongate working capital cycle; High leverage (TOL/TNW), as incremental working capital is largely funded from extended credit period by suppliers- Revenues from the services segment increased, contributing to 30.7% revenues in FY2019, on the back of order wins in the domestic market from various government agencies. Execution timeline for these contracts could range between 6 months to 1.5 years; and revenues and payments would be realized on a milestone basis. This may lead to elongation of working capital cycle. The company has entered into back to back contracts with suppliers to match timing of cashflows, thereby arresting deterioration working capital intensity. Any delay in payment receipts from the counterparties, in future, will have bearing on the company's liquidity profile as well as leverage indicators.

Intense competition from large sized global players - The company derived ~35% of the revenue in FY2019 from the export markets where large sized global players have established presence. Though the company enjoys cost competitive manufacturing, the stiff competition limits the pricing flexibility of the company. The company is focusing on organic and inorganic route to gain traction in new geographies and value added services and mitigate pricing pressure in relatively commoditized OF/OFC segment.

Liquidity position: Adequate

The company's liquidity profile is adequate, supported by cash & liquid investments to tune of Rs 300 crore along with undrawn bank lines of Rs 250-300 crore maintained on consistent basis. STL is expected to generate cash profits more than Rs 700 crore in FY2020, which should be sufficient debt repayment obligation of Rs 326.5 crore during current fiscal. Company's ability to restrict slippages in receivable recovery, especially from the government agencies/counterparties, remain crucial to maintain adequate liquidity.

Rating sensitivities

Positive triggers – Substantial improvement in scale of operations along with improvement in capital structure and coverage indicators, with TD/OPBIDTA below 1.0x and TOL/TNW below 1.5x on sustained basis.

Negative triggers –Substantial decline in operating profitability due to global supply demand mismatch, which could result in operating margin sliding below 15%; large debt funded investments thereby deteriorating capital structure, such that Net debt/ OPBDITA exceeds 2.0x or TOL/TNW exceeds 3.0x on sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology
Parent/Group Support	NA
Consolidation/Standalone	Consolidated financial statement

About the company

Sterlite Technologies Limited, formerly Sterlite Optical Technologies Limited (SOTL), was established in July 2001 after the demerger of the telecom division of Sterlite Industries Ltd (SIL). In July 2006, STL acquired the transmission line business of SIL to foray into the power transmission cables business. STL has grown over the years to become the largest OF and OFC manufacturer in the country. The company has sizeable presence in export markets as well with an established presence in global optical fiber market.

In May 2015, the management announced demerger of Telecom and Power businesses of the company to create two separate entities, which was completed in May 2016. In September 2015, STL acquired Elitecore Technologies Private Limited which was a telecom billing software company. After the aforementioned demerger, STL continues to operate as a telecom player offering products and solutions for optical fibers, fiber optic cables, data cables, system integration, telecom billing software and FTTH services.

The company has a 75:25 joint venture with Jiangsu Tongguang Communication Co Ltd in China for manufacturing of OF and another 58:42 joint venture with Conduspar Condutores Eletricos Limitada fir manufacturing of OFC in Brazil. Also, in July 2018, the company acquired an Italian OFC manufacturer, Metallurgica Bresciana S.p.A., for a consideration of Euro 47 million which was primarily funded by Euro debt. The company later acquired Impact Data Solutions, a European cloud infrastructure developer, in September 2019 at a total cost of GBP 12 million. The acquisitions are primarily focused towards gaining entry into new region/customer or improve value added products/services.

ICRA has consolidated the operational and the financial profiles of STL, its subsidiaries and joint ventures for the analysis. The company on a consolidated basis has an OF manufacturing capacity of 30 mfkm and an OFC capacity of 18 mfkm.

In FY2019, the company reported a net profit of Rs. 577.8 crore on an operating income of Rs. 5087.3 crore compared to a net profit of Rs. 364.1 crore on an operating income of Rs. 3205.5 crore in the previous year.

Key financial indicators (audited)

	Consolidated	
	FY2018	FY2019
Operating Income (Rs. crore)	3205.5	5,087.3
PAT (Rs. crore)	364.1	577.8
OPBDIT/OI (%)	23.4%	22.2%
RoCE (%)	30.2%	34.7%
Total Outside Liabilities/Tangible Net Worth (times)	2.0	2.9
Total Debt/OPBDIT (times)	1.6	1.8
Interest Coverage (times)	7.2	10.7
DSCR	3.7	4.6

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2020)				Rating History for the Past 3 Years		
		Type	Amount Rated	Amount Outstanding	Rating	FY2019	FY2018	FY2017
					14-Nov-2019	24-Aug-2018	22-Mar-2018	20-Dec-2017
1	ST Commercial Paper	Short-term	450.0	450.0	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
2	LT Non Convertible Debenture Programme	Long-term	300.0	300.0	[ICRA]AA(Stable)	[ICRA]AA(Stable)	[ICRA]AA-(Positive)	[ICRA]AA-(Positive)
3	LT Fund based-Working Capital Facilities	Long-term	705.0		[ICRA]AA(Stable)	[ICRA]AA(Stable)	[ICRA]AA-(Positive)	[ICRA]AA-(Positive)
4	LT Fund based-Term Loan	Long-term	168.0	168.0	[ICRA]AA(Stable)	[ICRA]AA(Stable)	[ICRA]AA-(Positive)	[ICRA]AA-(Positive)
5	ST Non-fund based Facilities	Short-term	2885.0		[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
6	LT/ST Interchangeable facilities#	Long-term/ Short-term	(2885.0)		[ICRA]AA(Stable)/ [ICRA]A1+	[ICRA]AA(Stable)/ [ICRA]A1+	[ICRA]AA-(Positive)/ [ICRA]A1+	[ICRA]AA-(Positive)/ [ICRA]A1+
	LT/ST Unallocated	Long-term/ Short-term	217.00		[ICRA]AA(Stable)/ [ICRA]A1+	[ICRA]AA(Stable)/ [ICRA]A1+	[ICRA]AA-(Positive)/ [ICRA]A1+	[ICRA]AA-(Positive)/ [ICRA]A1+

Amount in Rs. crore

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website click here

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	CP	NA	NA	7-365 days	450	[ICRA]A1+
INE089C07D75	NCD	23-Mar-17	8.45%	March 2021	75	[ICRA]AA(Stable)
INE089C07083	NCD	23-Mar-17	8.45%	March 2021	75	[ICRA]AA(Stable)
INE089C07091	NCD	27-Mar-18	8.7%	March 2023	150	[ICRA]AA(Stable)
NA	Working Capital Facilities				705	[ICRA]AA(Stable)
	Term Loan	Jan 2014	9.1%	March 2024	168	[ICRA]AA(Stable)
NA	NFB Facilities				2885	[ICRA]A1+
NA	Interchangeable facilities#				(2885)	[ICRA]AA(Stable)/ [ICRA]A1+
NA	Unallocated				217.0	[ICRA]AA(Stable)/ [ICRA]A1+

Source: Sterlite Technologies Limited

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Jiangsu Sterlite and Tonguang Fiber Company	75%	Equity method
Sterlite Conduspar Industrial Limitada	100.00%	Line by line
Metallurgica Bresciana S.p.A	100.00%	Line by line
Maharashtra Transmission Communication Infrastructure Limited	70.49%	Equity method
Speedon network Limited	100.0%	Line by line
Sterlite Telesystems Limited	100.0%	Line by line
Elitecore Technologies (Mauritius) Limited	100.0%	Line by line
Elitecore Technologies Sdn Bhd.	100.0%	Line by line
Sterlite Global Ventures (Mauritius) Limited	100.0%	Line by line
Sterlite Technologies UK Ventures Limited	100.0%	Line by line
Sterlite Tech Holding Inc	100.0%	Line by line
Sterlite Technologies Inc	100.0%	Line by line
Sterlite Technologies S.p.A.	100.0%	Line by line
Sterlite Innovative Solutions Limited	100.0%	Line by line
Sterlite Tech Connectivity Solutions Limited	100.0%	Line by line
Sterlite (Shanghai) Trading Co. Limited	100.0%	Line by line

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About ICRA Limited:

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