

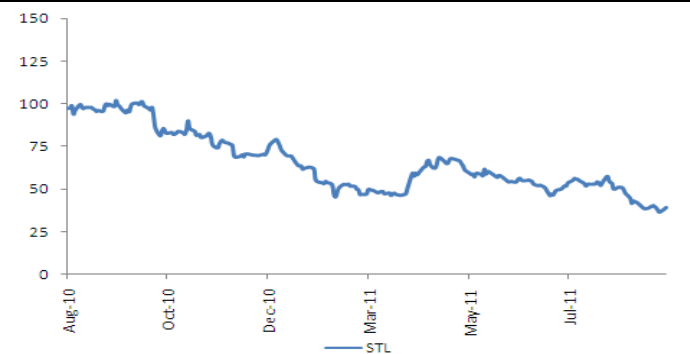
**Initiating Coverage**
**Sterlite Technologies Ltd.**

Recommendation	BUY
CMP (02/09/2011)	Rs. 39
Target Price	Rs. 53
Sector	Power & Telecom

**Stock Details**

BSE Code	532374
NSE Code	STRTECH
Bloomberg Code	SOTL IN
Market Cap (Rs. Crs)	1542
Free Float (%)	45.27
52- wk HI/Lo(Rs)	104-36
Avg. volume (Monthly)	243394
Face Value(Rs)	2
Dividend (FY 11)	25%
Shares o/s (Crs)	39.29

Relative Performance	1Mth	3Mth	1Yr
<b>Sterlite Tech</b>	-21.6%	-27.4%	-59.7%
<b>Sensex</b>	-8.3%	-8.5%	-7.5%


**Shareholding Pattern 30/06/2011**

Promoters Holding	54.7%
Institutional (Incl. FII)	13.8%
Corporate Bodies	6.1%
Public & others	25.4%

Sunil Jain, VP- Equity Research (022-39268196)  
[sunil.jain@nirmalbang.com](mailto:sunil.jain@nirmalbang.com)  
 Amish Pansuria, Research Analyst (022-39268174)  
[amish.pansuria@nirmalbang.com](mailto:amish.pansuria@nirmalbang.com)

**Big is getting Bigger!**

Sterlite Technologies Ltd (STL) is India's only fully integrated optical fiber manufacturer and the fifth-largest globally. The company is also the third-largest global manufacturer of power conductors and is a leader in the local market with 25% market share.

**Investment Rationale**
**Massive Capacity Expansion – leader in its businesses**

The company has embarked on a capacity expansion for its power conductors and optical fiber business units. In the power conductor segment, it has increased capacity from 75000 Mtpa in FY07 to 160000 Mtpa in FY10 and is further expanding to 200000 Mtpa by FY12. This would make STL the world's largest integrated manufacturer of power conductors. In the optical fiber segment, the company is increasing its capacity to 20 mn kms from its current 12 mn kms. This would make STL among the largest global manufacturers of optical fibers by FY12. The impact of these expansions will be seen in FY13.

**Independent Power Transmission Projects – long term benefits**

STL has ventured into bidding for independent power transmission projects and has won a BOOM project of East North Interconnection mega transmission whereby it will get fixed revenues every year. This would provide additional revenue stream after 3-5 years. This project has achieved financial closure and is on schedule. The company has 2 other BOOM projects under this portfolio for which it is targeting the financial closure in FY12.

**Huge Global Optic Fiber Demand – well set to benefit**

In 2010, the global demand for optical fiber cable reached 182 mn fiber-km and this is expected to cross 200 mn fiber-km in 2011 on the back of developed country's efforts to build FTTx networks. Chinese demand saw a flat growth in the previous year. This year, however, all the 3 telecom operators in China together have come up with investment plans of US\$ 50 billion for building 3G mobile network and construction of FTTx networks. Sterlite has formed a JV with a Chinese firm with 75% ownership and is in a very good position to capture this demand.

**Valuation & Recommendation**

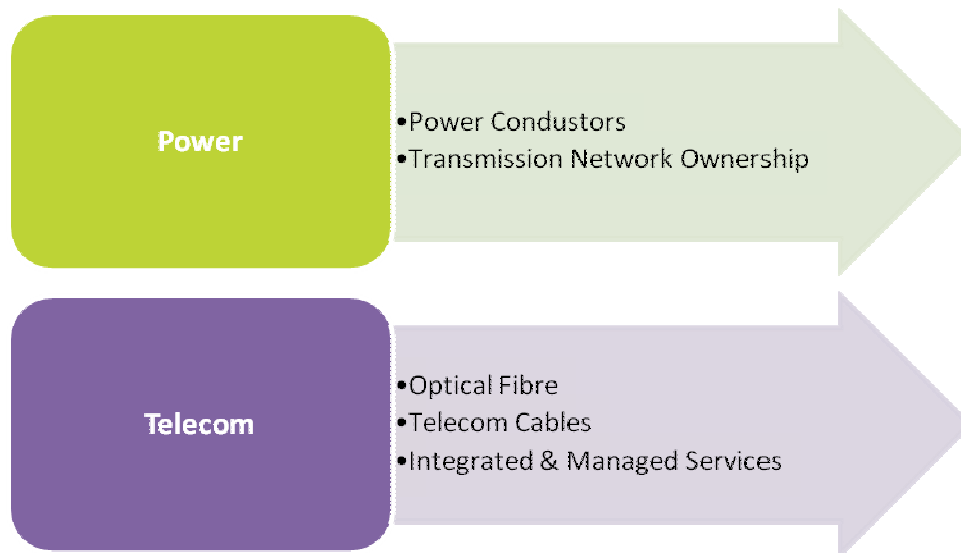
STL is a leader in the areas of its operations and the end user industries – Power and Telecom are seeing robust growth.

We expect revenues to grow by 22% to Rs.2762 cr and PAT to move up by 14% to Rs.160 cr in FY12E. At CMP, the stock is trading at 9.6x of FY12E EPS of Rs.4.08. We assign a multiple of 13x to its FY12E EPS to arrive at price target of Rs.53 and assign a BUY recommendation on the stock.

Year	Net Sales	Growth %	EBITDA	Margin %	Adj PAT	Margin %	EPS	PE	P/Bv
FY10A	2431	6.2	381	15.7	246	10.1	7.3	5.3	1.4
FY11A	2262	-7.0	265	11.7	140	6.2	3.9	10.0	1.5
FY12E	2762	22.1	322	11.7	160	5.8	4.1	9.6	1.2

**COMPANY PROFILE**

Sterlite Technologies (STL) is a leading global provider of transmission solutions for the power and telecom industries. It is among the Top 3 global manufacturers of power conductors and among the Top 5 global manufacturers of optical fibers and cables. It is India's only fully integrated optical fiber manufacturer. The company is a leader in the local market with 25% market share. Its business can be classified into two major segments — power transmission which contributed 71% to net revenues and telecom products and solutions segment, which contributed the rest in FY11.



The company manufactures and supplies optical fibers, fiber optic cables, copper telecom cables, structured data cables and ADSL2+ modems. It also deals in power transmission conductors and aluminum and alloy rods. It offers telecom integration and managed services.

The company has a global presence with clients in over 55 countries in Asia Pacific, Africa, Europe and North America. Almost 28% of its sales come from International business.

To strengthen its presence in China, STL recently formed a JV with a Chinese company, Jiangsu Tongguang Communication Co Ltd; STL holds a 75 per cent stake in the JV. This JV is setting up a manufacturing facility for 4 mn km of cables in China, and is expected to become operational by September 2012.

## INDUSTRY

### Power

Investment in the power T&D sector in 12<sup>th</sup> five-year plan is estimated at Rs 240,000 cr providing an opportunity of Rs. 552 cr in the conductor segment

#### Domestic Market

The Government of India has an ambitious mission of 'POWER FOR ALL BY 2012'. Power requirement will double by 2020 to 400,000 MW. To cater to this growing energy requirement, investments in new generation facilities are inevitable. The investments in generation have to be supported with equal if not more investments to build a robust transmission and distribution (T&D) network.

After a decade of underinvestment in the transmission and distribution space, the 11th and 12th Plans are more progressive for this segment. This is evident from the fact that the share of expenditure on T&D in the 11th Plan and 12th Plans is 51% and 56.4%, respectively, as compared to the 44.2% share in the 10th Plan. Transmission capex in the 11th plan has increased to Rs. 140,000 cr from Rs. 98,300 cr in the 10th plan. The bulk of the investments in the transmission segment are being done by PGCIL (40%) and SEBs, while the private sector constitutes only a small proportion. Based on preliminary estimates, transmission spending is expected to increase to Rs. 240,000 cr (up by 71%) in the 12th plan.

In the 12<sup>th</sup> Plan PGCIL plans to spend Rs. 120,000 cr for :

- Enhancing the capacity of the interregional transmission grid from 37,000 MVA to 75,000 MVA.
- Building a High Capacity Transmission Corridor (HCTC) for Rs. 49,630 cr (60% of this will be spent on transmission lines)

State Electricity Boards (SEBs) have also started investing in setting up as well as upgrading their T&D infrastructure. As per the preliminary estimates of the 12<sup>th</sup> Plan, SEBs are expected to spend Rs. 100,000 cr on their T&D infrastructure.

#### Global Power transmission Market

There is renewed momentum in T&D infrastructure build up in some of the developed parts of the world. The usual life of a transmission line is around 30-35 years. Many of these developed nations are now nearing the end of T&D infrastructure and many state and national transmission utilities in these countries are now planning investments to upgrade or set up new grids. The renewable energy installations are also demanding new T&D infrastructure to evacuate power from the new generating stations.

USA: The American Reinvestment and Recovery Act of 2009 is facilitating a US\$ 11 billion investment in the T&D grid.

Russia: Ministry of Energy has estimated an investment of US\$ 385 billion for its power grids over the next 10 years.

China: US\$ 28 billion investment in its power grid by 2015.

Mexico: US\$ 10 billion investment in the T&D sector by 2018.

Middle East & Africa: According to IEA ~US\$ 77 bn of investments would be required in the T&D sector of Middle East over a period of 2008-2015. Similarly, investments worth ~US\$ 63 bn are expected to be invested in building up the T&D infrastructure in Africa, over the same period.

Global electricity sector investment is anticipated to reach US\$ 10 Trillion by 2030. More than US\$ 5 trillion will be used to invest in transmission and distribution networks.

**STL is India's largest and fifth largest globally in optical fiber production and is in a good position to capture the global demand for fiber optic.**

### Telecom

#### **Domestic Market**

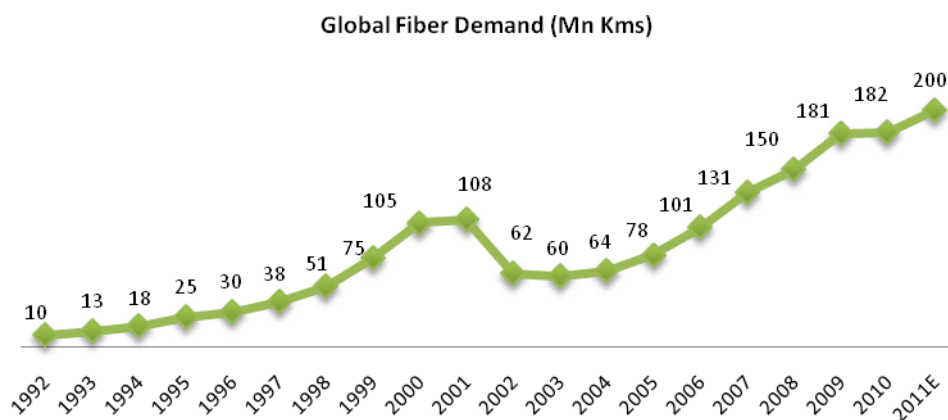
India is the second largest telecom market with 585mn wireless subscribers. However, the penetration levels are still about 50% of the enormous potential available. Government of India has intensified its efforts to roll out broadband and 3G services in the semi-urban and rural areas. We believe that the India market with the highest number of wireless subscribers is also at an inflection point of growth and should witness good growth in fiber deployments in the next 2-3 years as the bandwidth demand increases riding on the data ridden 3G technology.

Demand will be fuelled by the 3G rollout that is underway in the country. The other area where the demand will come from is the government. There are three major projects: fiber to the village project, which is being driven by the Ministry of IT, then there is the spectrum release of defense sector and there is a national knowledge network.

#### **Global Market**

As per CRU estimates, global demand for optical fiber is expected to cross 200 million kms in 2011. And the demand in the first half of the year was already close to 100 million kms, represents a growth of about 5% over 2010.

The demand for fiber optic cable in other advanced economies like USA, Japan, Germany, and Netherlands is also rising due to their efforts to build Fiber-to-the-Node and Fiber-to-the-Home (FTTH) networks.



Source: Company & NB Research

Chinese demand which constitutes almost 40% of the world demand for optical fiber saw a flat growth in the previous year. These fears have been dispelled with all three telecom operators in China coming out with investment plans of about US\$ 50 billion for those servicing the 3G mobile network upgrades.

Sterlite being qualified and certified by all three major Chinese operators for fiber supplies, which is a very positive development and with the recent joint venture in China, which should start operating in FY13, will be in much stronger position to capture the demand in the coming years.

**STL would become world's largest integrated manufacturer of power conductors.**

#### INVESTMENT RATIONALE

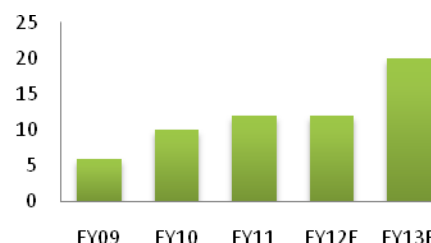
##### Capacity Expansion would make STL a leader

In the power conductor segment, STL is increasing capacity from 160000 MT to 200000 MT. This would make STL the world's largest integrated manufacturer of power conductors. In the optical fiber segment, the company is increasing its capacity to 20 mn km. The company is on track to complete all plant & machine installations by the end of FY12 towards its 20 mn km capacity. STL would be positioned amongst the Top 3 manufacturers' globally. This increase in capacities would bring benefits of economies of scale and add cushion towards the margin pressure prevailing in the industry. The full impact of this capacity expansion will be visible only in FY13.

Power Conductors (MT)



Optical Fiber (Mn Kms)



Source: Company & NB Research

##### Independent Power Transmission Projects – long term benefits

Sterlite has ventured into bidding for independent power transmission projects, which includes evacuation of power from the generation stations, strengthening of the grid and transmission of power from pooling stations to the other grid stations and load centers. In this space, STL has won a Build, Own, Operate and Manage (BOOM) project of Ultra Mega Power transmission project of two 400kV double circuit lines of ~430Km in India. The transmission lines would be commissioned within 3 years and the company would maintain them for a minimum time frame of 22 years. This would provide additional revenue stream after 3-5 years. The financial closure of this project is done.

The second and third project of transmission scheme involves establishment of 765 KV Single Circuit Lines; Vadodara-Dhule-Aurangabad and Indore-Bhopal-Jabalpur. The project involves a total line length of about 1,000 km and the set up of two 1500 MVA substations at Dhule and Bhopal. The project would be commissioned within 36 months and the Company would operate and maintain the transmission system for a minimum tenure of 35 years thereafter. The financial closure for these projects is expected in FY12.

##### Huge Global Optic Fiber Demand – well set to benefit

China has been the main driver in the market globally at more than 40% of all world demand. It was expected that the demand for fiber optic cable will slowdown in China at the end of 2010, but latest data shows that demand has continued to remain robust. The demand in China was propelled by network operators' efforts to improve connectivity and to cater to demand arising from 3G/4G usage. The demand for fiber optic cable in other advanced economies like USA, Japan, Germany, and Netherlands is also rising due to their efforts to build Fiber to-the-Node and Fiber-to-the-Home (FTTH) networks. This combination will drive demand globally for fiber optic cable in 2011 to 200 mn km. The growth in the market in 2012 will come from Western Europe and North America. Strong demand globally, is breaking away from the business cycle in the USA and Western Europe– since demand is now being driven by FTTH/FTTC. There is also additional demand

**Returns from the Independent Power Transmission Project would start coming in from FY14 onwards.**

in emerging markets, and new optical fiber lines are being planned in Russia, Brazil, Bangladesh and Uzbekistan.

### Order Book Expansion gives revenue visibility

The strong order book of Rs.2400 cr (1.06x its FY11 revenues) at the end of Q1FY12 gives good revenue visibility for the coming year. The order backlog in power segment is Rs.1800 cr and the balance is from the telecom segment.

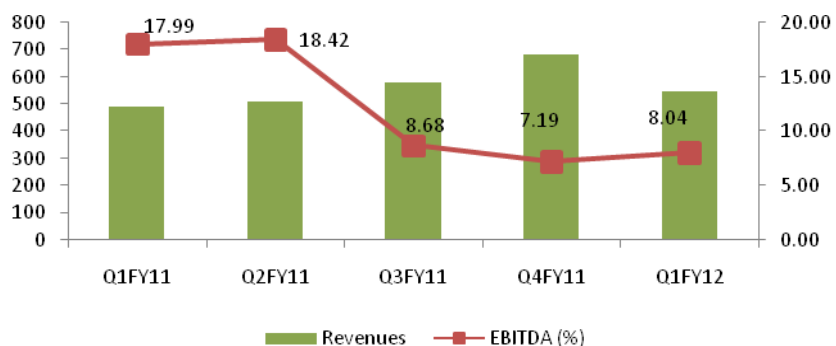


Order book expanded 9% sequentially in Q1FY12. PGCIL is expected to release orders of 275000 MT of conductors (against 225000 MT in the corresponding previous year), bulk of which would come in the H2FY12. STL with its leadership position in the power conductors market in India stands to benefit from this.

### Revenues and Margins to improve

Order flows for power conductors which are released by PGCIL were muted in 9MFY11, which lead to de-growth in revenues by 7% in FY11. Margins were affected due to execution of low margin orders which were accepted during recession period. EBITDA for the Power Conductors business fell from an average of Rs. 10000-12000/MT to below Rs. 4000/MT in Q1FY12.

PGCIL released major orders in Q4FY11 which would be executable over a 12-18 month time period. STL bagged orders worth Rs. 1150 cr during Q4FY11 (~Rs. 800 cr worth orders from PGCIL). Execution of these orders will help improvement in margins going forward and the full impact of margin expansion would be seen in the Q3 & Q4FY12 results. EBITDA Margins are expected to be ~11.7-12% in FY12E. We expect the revenues of the company to improve by 22% to Rs 2762 cr in FY12E.



Source: Company & NB Research

### Risks

- **High Dependence of PGCIL Contracts**  
PGCIL contributed almost 30% of STL's FY11 revenues. This high reliance on PGCIL is risky for the company.
- **Execution of BOOM project**  
ROE could be affected if there is any overrun in capex and increased debt costs.
- **Competition in the Conductor Business**  
Domestic Conductor market is flooded with new entrants. This could result in further pressure on margins for the company.

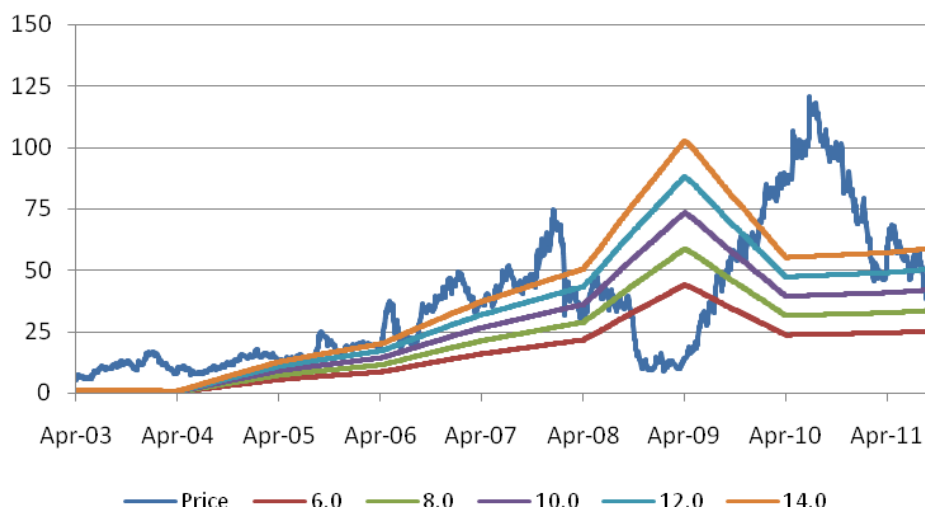
**We assign a Target PE of 13x to the stock**

### Valuation & Recommendation

STL is a leader in the areas of its operations and the end user industries – Power and Telecom are seeing robust growth. This demand is expected to remain positive in the coming years. Concerns like margin pressure would be tackled by the company by reducing the manufacturing expenses with the economies of scale it enjoys.

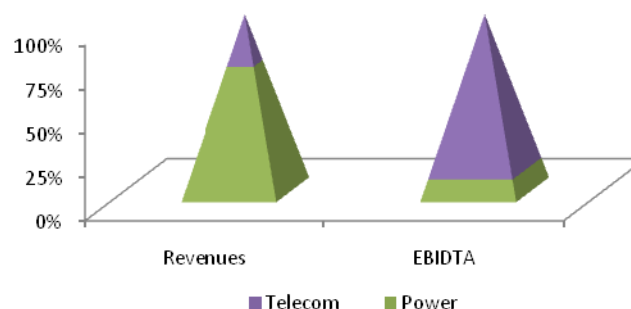
We expect the revenues to grow by 22% to Rs.2762 cr and PAT to move up by 14% to Rs.160 cr. At CMP, the stock is trading at 9.6x of FY12E EPS of Rs.4.08. We assign a 13x to the stock and arrive at price target of Rs.53 and assign a BUY recommendation on the stock.

### Forward PE Band



**Q1FY12 Result Update**

- STL reported disappointing results during the quarter wherein revenues grew by 11% YoY to Rs.547 cr. This was on the back of 16% YoY growth in the conductors segment at Rs.394 cr. Telecom revenues remained flat at Rs. 153 cr.
- EBIDTA margins dropped significantly to 5.5% due to execution of low margin projects in the conductor segment. Margins in the Conductor segment were mere 0.9% while that in telecom segment were 17%.



- PAT was lower by 49% YoY at Rs.5.23 cr. This was mainly due to lower revenues and higher interest costs.
- Order book stands at Rs.2400 cr which was a rise of 9% sequentially. PGCIL has announced to release orders of 275000 MT in the H2FY12 against 225000 MT in the previous year.

Financials	Q1FY12	Q1FY11	YoY %	Q4FY11	QoQ%
<b>Revenues - Net</b>	547.3	491.8	11%	682.2	-20%
<b>EBITDA</b>	30.2	83.0	-64%	49.0	-38%
<i>EBIDTA Margin</i>	5.5%	16.9%		7.2%	
Interest	21.9	7.1	207%	18.2	20%
<b>EBDT</b>	8.3	75.9	-89%	30.8	-73%
Depreciation	14.6	13.1	12%	15.8	-7%
Other Income	13.8	5.5	152%	0.1	19614%
<b>PBT</b>	7.5	68.3	-89%	15.1	-50%
Tax	2.3	12.7	-82%	4.8	-52%
PAT	5.2	55.6	-91%	10.3	-49%
<b>EPS</b>	0.13	1.42	-91%	0.3	-49%

Source: Company

**Initiating Coverage**

**Sterlite Technologies Ltd.**

**Financials**

Profitability (Rs. In Cr)	FY09A	FY10A	FY11A	FY12E
<b>Y/E - March</b>				
<b>Revenues - Net</b>	<b>2289.2</b>	<b>2431.6</b>	<b>2262.6</b>	<b>2762.3</b>
% change	35.8%	6.2%	-7.0%	22.1%
<b>EBITDA</b>	<b>234.2</b>	<b>381.0</b>	<b>265.6</b>	<b>322.4</b>
% change in EBITDA	17.4%	62.7%	-30.3%	21.4%
Interest	53.2	38.1	47.4	58.2
<b>EBDT</b>	<b>180.9</b>	<b>342.8</b>	<b>218.2</b>	<b>264.1</b>
Depreciation	42.5	48.3	56.0	63.9
Other Income	3.7	22.9	16.0	15.0
Extraordinary(ForexGain/Loss)	-34.8	0.0	0.0	0.0
<b>PBT</b>	<b>107.3</b>	<b>317.5</b>	<b>178.2</b>	<b>215.3</b>
Tax	19.3	71.4	37.7	54.9
PAT	88.0	246.1	140.5	160.4
<b>Adj. PAT</b>	<b>116.8</b>	<b>246.1</b>	<b>140.5</b>	<b>160.4</b>
Shares o/s ( No. in Cr.)	32.4	33.5	39.3	39.3
<b>Adj Diluted EPS</b>	<b>3.6</b>	<b>7.3</b>	<b>3.9</b>	<b>4.1</b>
Cash EPS	4.0	8.8	5.0	5.7
DPS (%)	25%	25%	25%	25%
Quarterly (Rs. In Cr)	Sep.10	Dec-10	Mar-11	Jun-11
<b>Revenue</b>	<b>509.44</b>	<b>579.11</b>	<b>682.23</b>	<b>547.33</b>
<b>EBITDA</b>	<b>90.56</b>	<b>43.08</b>	<b>48.98</b>	<b>30.19</b>
Interest	9.22	12.85	18.22	21.85
<b>EBDT</b>	<b>81.34</b>	<b>30.23</b>	<b>30.76</b>	<b>8.34</b>
Dep	13.34	13.84	15.75	14.63
Other Inc.	3.27	7.16	0.07	13.80
Extraordinary	0.00	0.00	0.00	0.00
<b>PBT</b>	<b>71.27</b>	<b>23.55</b>	<b>15.08</b>	<b>7.51</b>
Tax	13.72	6.88	4.88	2.28
<b>PAT</b>	<b>57.55</b>	<b>16.67</b>	<b>10.20</b>	<b>5.23</b>
EPS (Rs.)	1.62	0.47	0.26	0.13
Operational Ratio	FY09A	FY10A	FY11A	FY12E
EBITDA margin (%)	10.2%	15.7%	11.7%	11.7%
Adj PAT margin (%)	5.1%	10.1%	6.2%	5.8%
Adj EPS Growth (%)	23.3%	110.6%	-42.9%	14.1%
Price Earnings (x)	10.9	5.3	10.0	9.6
Book Value (Rs.)	19.0	27.2	26.3	31.9
ROE (%)	20.1%	32.0%	14.4%	14.0%
ROCE (%)	13.3%	28.4%	14.8%	15.2%
Debt Equity Ratio	0.8	0.4	0.6	0.4
Price / Book Value (x)	2.1	1.4	1.5	1.2
EV / Sales	0.8	0.7	1.0	0.8
EV / EBITDA	7.6	4.4	8.1	6.5

Source: Company, NB Research

Financial Health (Rs. In Cr)	FY09E	FY10A	FY11A	FY12E
<b>Y / E - March</b>				
Share Capital	32.3	71.1	71.3	78.6
Warrant/ ESOP	5.26	31.02	30.10	6.05
Reserves & Surplus	583.4	813.9	934.5	1174.5
Misc. Exp (not w/o)	0.0	0.0	0.0	0.0
<b>Net Worth</b>	<b>620.9</b>	<b>916.0</b>	<b>1035.9</b>	<b>1259.1</b>
Total Loans	496.6	358.2	619.8	544.8
Deferred Tax Liabilities	56.0	60.2	66.0	74.6
<b>Total Liabilities</b>	<b>1173.5</b>	<b>1334.4</b>	<b>1721.7</b>	<b>1878.5</b>
<b>Net Fixed Assets</b>	<b>656.7</b>	<b>683.4</b>	<b>866.9</b>	<b>1002.3</b>
<b>Investments</b>	<b>92.0</b>	<b>106.1</b>	<b>108.8</b>	<b>133.8</b>
Current Assets	925.3	1166.3	1538.3	1479.3
Current liability & Provision	500.5	621.4	792.4	736.9
<b>Working Capital</b>	<b>424.8</b>	<b>544.8</b>	<b>745.9</b>	<b>742.4</b>
<b>Total Assets</b>	<b>1173.5</b>	<b>1334.4</b>	<b>1721.7</b>	<b>1878.5</b>
Cash Flow (Rs. In Cr)	FY09E	FY10A	FY11A	FY12E
<b>Operating</b>				
Operating Income	234.2	381.0	265.6	322.4
Change in WC	238.7	11.8	-280.7	-14.1
Other Adjustment	-3.4	-11.0	5.3	0.0
<b>CF from Operation</b>	<b>469.5</b>	<b>381.7</b>	<b>-9.7</b>	<b>308.3</b>
<b>Investment</b>				
Capex	-132.5	-64.0	-244.9	-199.2
Other Investment	-86.0	-14.1	-2.7	-25.0
<b>Total Investment</b>	<b>-218.5</b>	<b>-78.1</b>	<b>-247.6</b>	<b>-224.2</b>
<b>Financing</b>				
Dividend Paid	-9.4	-20.8	-23.0	-22.6
Share Capital	0.0	6.6	0.2	7.3
Premium / Reserve	0.7	63.3	2.2	78.2
Borrowing	-166.6	-138.4	261.6	-75.0
Other Income	3.7	22.9	16.0	15.0
Other	-34.8	0.0	0.0	0.0
Interest	-53.2	-38.1	-47.4	-58.2
Tax Paid	-2.6	-67.2	-31.8	-46.3
<b>Total Financing</b>	<b>-262.2</b>	<b>-171.8</b>	<b>177.7</b>	<b>-101.6</b>
Net Chg. in Cash	-11.2	131.8	-79.6	-17.6
Cash at beginning	89.1	77.9	209.7	130.1
Cash at end	77.9	209.7	130.1	112.5

**Note**

**Disclaimer**

This Document has been prepared by Nirmal Bang Research (Nirmal Bang Securities PVT LTD).The information, analysis and estimates contained herein are based on Nirmal Bang Research assessment and have been obtained from sources believed to be reliable. *This document is meant for the use of the intended recipient only. This document, at best, represents Nirmal Bang Research opinion and is meant for general information only. Nirmal Bang Research, its directors, officers or employees shall not in anyway be responsible for the contents stated herein. Nirmal Bang Research expressly disclaims any and all liabilities that may arise from information, errors or omissions in this connection. This document is not to be considered as an offer to sell or a solicitation to buy any securities. Nirmal Bang Research, its affiliates and their employees may from time to time hold positions in securities referred to herein. Nirmal Bang Research or its affiliates may from time to time solicit from or perform investment banking or other services for any company mentioned in this document.*