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Nurturing Financial Excellence

IPO REPORT

**“Subscribe with Caution” to
Dinesh Engineers Ltd.**

Salient features of the IPO:

- Passive communication infrastructure provider **Dinesh Engineers Ltd. (DEL)** is planning to raise around Rs. 1.8bn through an IPO by offering 10mn share between the price range Rs. 183 - 185 per share.
- The IPO consists of only fresh issue. Net proceeds from the same would be largely utilized for the expansion of optical fiber cable (OFC) network under IP-1 license. Residual funds would be utilized towards general corporate purposes.

Key competitive strengths:

- Established optic fiber network in India
- Strong project management and execution capabilities
- Efficient business model
- Long standing customer relationships with strong repeat business

Risk and concerns:

- Slowdown in the telecommunication sector
- Adverse regulations
- Revenue concentration risk
- Poor capacity utilization in fiber leasing business
- Highly labor oriented operations
- Competition

Valuation & recommendation: There are no comparable listed companies in India that engage in the same line of business as the company. At the higher price band of Rs. 185 per share, DEL's share is valued at a P/E multiple of 11.8x (to its restated FY18 EPS of Rs. 15.6).

Below are few key observations of the issue: (For detailed valuation, refer to page 8 & 9 of the report)

- With rising urban and rural 4G penetration, there is increased demand of unlimited data bandwidth, which can only be resolved through the enhanced deployment of optic fibers. The proposed deployment of the 5G technology in future would also propel the demand of optic fibers. Thus to meet the increased demand, it is necessary to execute the existing and future 4G and 5G technology on OFC network. Prominent government support through policies like Digitalization and the new telecom policy i.e. "The National Digital Communications Policy, 2018" are also putting more emphasis on the increased fiber rollout. Currently, less than 25% of telecom towers are fiber-connected. Thus, there is an immense opportunity for growth for the entities engaged in the OFC network deployment.
- Incorporated in 2006, DEL is primarily engaged in executing optical fiber laying work for telecom operators (telco) and internet service providers (ISP) in India. It is the dominant player in the Western and Southern India, having present in 15+ telecom circle across 16 states
- In 2008, it was granted Infrastructure Provider (IP)-I License by the Department of Telecommunications (DoT), pursuant to which it has right to build, operate and manage wired network which can be used by the telcos and ISPs. Since 2011, the company has laid fiber network of around 9,500kms for the telcos under the vendor projects, which run across various states. As on 1st Apr. 2018, DEL had a vendor project order book of Rs. 4.2bn (i.e. 5,600kms optic fiber), which is to be executed in FY19. According to the management, with lower optic fiber penetration and increased penetration of mobile broadband, there would be sustainable growth in the vendor order book in future and the company is well placed to benefit from the same. Revenue from vendor contracts forms around 90% of the total revenue and has increased by 86.2% CAGR over FY15-18. EBITDA margin from this vertical is around 20-25%.
- Under fiber lease business, DEL has its own OFC network of around 7,500kms, which are leased to the telcos. DEL is witnessing increased demand of its fiber leasing business and can be demonstrated by the improving capacity utilization, which increased from 20% in FY15 to 32% in FY18. Over FY15-18, revenue from this business increased by 45.8% CAGR. Since there is minimal operating cost involved in leasing the fiber, the EBITDA margin from this business is around 85-90%.
- The vendor project order book, which the company is executing is in different geographical areas and is not overlapping with any of its existing OFC network. Also along with the vendor contract, DEL is parallelly putting its own OFC of 5,600kms capacity. Thus, this provides an increased geographical coverage and increased owned leased fiber capacity. The net proceeds from this IPO would be largely utilized for the expansion of this owned OFC network.
- On financial front, DEL has demonstrated robust performance. Over FY16-18, it reported a 57.2% CAGR rise in the consolidated operating revenue to Rs. 2,746.9mn in FY18. Consolidated EBITDA increased by 97.3% CAGR to Rs. 1,079.6mn in FY18. EBITDA margin expanded from 22.7% in FY16 to 35.7% in FY18. Reported PAT increased by 118.8% CAGR to Rs. 617mn in FY18. PAT margin expanded from 10.5% in FY16 to 20.4% in FY18. Cash flow from operations was positive over FY16-18 with an average annual cash flow of Rs. 343.8mn. Baring FY17, free cash flow was positive throughout the period and increased by 68.4% CAGR to Rs. 255.1mn in FY18. Average RoE was around 50% over FY16-18. Average RoCE was around 30% during the period.

On valuation front, at higher price band, the company is demanding a P/E valuation of 11.8x (to its restated FY18 EPS of Rs. 15.6). Considering the positive future outlook, strong financial performance and capacity expansion in the higher EBITDA margin segment, we feel the issue is attractively priced. However, considering the sustainability in the profitability margins, current turbulence in the equity market and listing in "T" category, we assign a **"Subscribe with Caution"** rating to the issue.

Recommendation	Subscribe with Caution
Price Band (Rs.)	Rs. 183 - 185 per Share
Face Value (Rs.)	Rs. 10
Shares for Fresh Issue (mn)	10mn Shares
Shares for OFS (mn)	Nil
Fresh Issue Size (Rs. mn)	Rs. 1,830 - 1,850mn
OFS Issue Size (Rs. mn)	N/A
Total Issue Size (Rs. mn)	Rs. 1,830 - 1,850mn
Bidding Date	28 th Sept. – 03 rd Oct. 2018
MCAP at Higher Price Band	Rs. 7,307.5mn
Enterprise Value at Higher Price Band	Rs. 7,583.1mn
Book Running Lead Manager	Hem Securities Ltd.
Registrar	Link Intime India Pvt. Ltd.
Sector/Industry	Other Telecom Services
Promoters	Mr. Dinesh Kollaiah Kargal & Mrs. Shashikala Dinesh Kargal

Pre and post - issue shareholding pattern		
	Pre – Issue	Post - Issue
Promoter and Promoter Group	100.00%	74.68%
Public	0.00%	25.32%
Total	100.00%	100.00%
Retail Application Money at Higher Cut-Off Price per Lot		
Number of Shares per Lot	80	
Application Money	Rs. 14,800 per Lot	
Analyst		
Rajnath Yadav		
Research Analyst (022 - 6707 9999; Ext: 912)		
Email: rajnath.yadav@choiceindia.com		

About the issue:

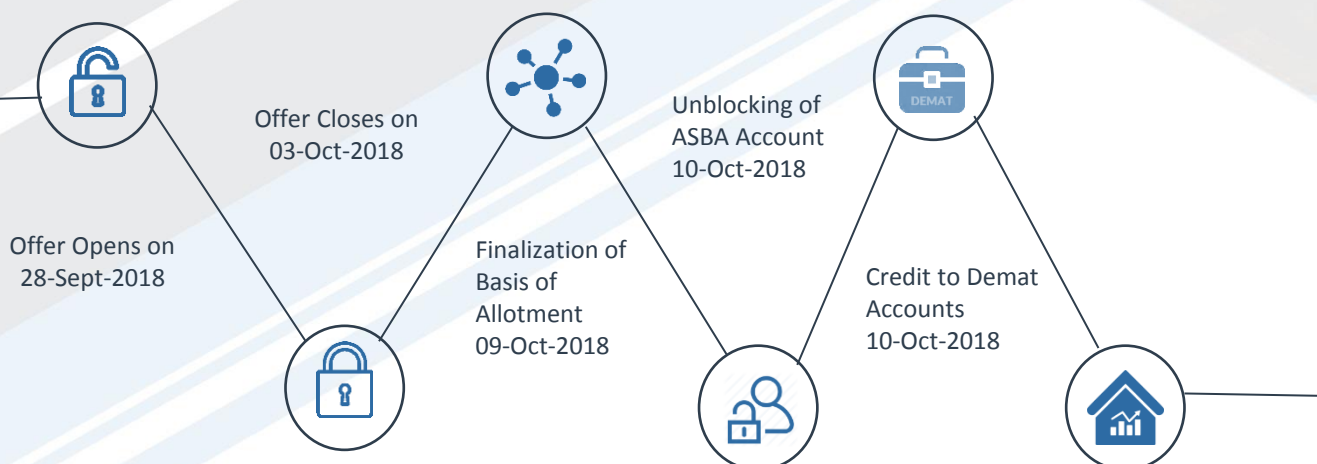
- DEL is coming up with an initial public offering (IPO) with 10mn shares (fresh issue: 10mn shares; OFS shares: nil) in offering. The offer represents around 25.32% of its post issue paid-up equity shares of the company. Total IPO size is Rs. 1,830 - 1,850mn.
- The issue will open on 28th Sept. 2018 and close on 03rd Oct. 2018.
- The issue is book building with a price band of Rs. 183 - 185 per share.
- The IPO consists of only fresh issue. Net proceeds from the same would be largely utilized for the expansion of optical fiber cable network under IP-1 license. Residual funds would be utilized towards general corporate purposes.
- 50% of the net issue shall be allocated on a proportionate basis to qualified institutional buyers, while rest 15% and 35% is reserved for non-institutional bidders and retail investors, respectively.
- Its promoter holds 100% stake in the company and post IPO this will come down to 74.68%. Public holding will increase from current nil to 25.32%.

Pre and Post Issue Shareholding Pattern (%)

	Pre Issue	Post Issue (at higher price band)
Promoter & Promoter Group (%)	100.00%	74.68%
Public (%)	0.00%	25.32%

Source: Company RHP

Indicative IPO Process Time Line:



Company Introduction:

DEL is a passive communication infrastructure provider in India focused on providing passive communication infrastructure services mainly to the telcos and ISPs. The company was incorporated in 2006 and through the next several years has executed the fiber laying work for many telcos. It has been licensed by the Department of Telecommunications with the Infrastructure Provider (IP)-I License, under which it can establish and maintain wired networks, duct space for the purpose to grant on lease or sale on IRU (indefeasible right of use) basis to the licensees of telcos, ISPs etc.

DEL's key expertise lies in the field of providing support services to telecom vendors which inter alia includes project management for laying of the duct and optic fiber cables, construction of basic transmission and telecom utilities, dark fiber leasing, optical fiber network construction, maintenance of duct and optic fiber & optical fiber project turnkey services to various telcos & broad band service operators across the states of India.

Since the receipt of the IP-I license, the company has created its own optic fiber network of around 7,500kms, which runs across the state of Rajasthan, Gujarat, Maharashtra, Goa, Karnataka, Andhra Pradesh and Telengana. Its wired network infrastructure solutions are used by telcos such as Bharti Airtel, BSNL, Reliance Jio, Vodafone, Idea, Tata Communication etc., which helps them inter-alia in increasing network's bandwidth, maximize existing network capacity, improve network performance and availability.

Since 2011, the company has laid fiber network of around 9,500kms for the telcos under the vendor projects, which run across the states of Maharashtra, Gujarat, Uttar Pradesh, Bihar, Karnataka, Andhra Pradesh, Chhattisgarh, Goa and Rajasthan. Apart from laying the network under the vendor project or own network, DEL is also engaged in the operations & maintenance activity of the fiber network and preventing the underground optic fiber therein from getting cut due to activities like road repairs, digging and expansion works by various authorities.

The growth and development of the company during the past years have been the result of its customer centric approach and core competence in the field of telecom infrastructure. DEL's main focus and vision is on providing the customers with the desired quality work within the given time frame. Based on the past records and experience in the field of laying the fiber for the telcos, Mahanagar Gas Ltd. has entrusted the company with the laying of its gas pipelines under the city of Mumbai. The gas pipeline laying work would helps it to diversify in the field of gas sector and will also open new business avenues. The work of laying the gas pipeline have been undertaken through outsourcing the same to the sub-contractors.

Some of the prominent clients of DEL includes telecom giants like Bharti Airtel Ltd., Idea Cellular, Vodafone, Tata Communications Ltd. etc. as well as ISP clients like Intech, D-vois SSV, Atria, Power Grid, Hathway, Sify etc. Apart from the above the company also has Mahanagar Gas Ltd. in its client list for gas pipeline work.

Business Operations: DEL's business operations can be briefly classified under the below mentioned three heads:

Project Execution for
Telecom Operators

Laying of fiber under
the IP-1 License and
then leasing or selling

Operations &
Maintenance (O&M) of
Telecom Network

Project execution for telcos (Vendor Projects): Project execution for telcos involves solely working for the telcos as contractors. Telco's based on their requirement notify the area where they require the fiber network. Once this area is notified the telcos assign the projects and their requirements to the company. On receiving the project, DEL initiates the work of procuring the right of way (RoW) permissions for the operators. On receiving the permission, it starts executing the projects. The fiber is laid in the allowable RoW limits from the center of the road and available land width. The depth of the trench and the protection material is based on the specifications given by the respective telco. The entire activity is done with the assistance of labour and/ or machinery. The activity is done simultaneously on multiple routes across the areas. Once the fiber laying is complete, the same is first tested by the project team and then acceptance testing is done by the telco for whom the project is executed. After such testing the network ,RoW documents are handed over to the telco.

Business Operations (Contd...):

Laying fiber under IP-I License (IP-I): Under the Infrastructure Providers Category I (IP-I) license, DEL can establish and maintain the assets such as dark fibers, RoW and duct space for the purpose to grant on lease/rent/sale on IRU basis to the licensees of telecom services providers and other vendors on mutually agreed terms and conditions. Under the IP-1 license, the company has developed its own network of around 7,500kms during the last five years. With its experience in telecom for the last decade, it understands the telecom market and the requirement of the telcos where they want the infrastructure to be built. The company identifies such strategic routes where the operators doesn't have their presence and build its network there. This network is then leased to telcos either by duct lease or by fiber lease. In some cases, where the telcos are unable to build network by their own on particular routes due to constraints like: high RoW challenges, overall project cost viability, local issues etc. they ask DEL to execute the route. In such case, the company executes the route either on own but the requisite permission for the route is on its name. Once the execution is completed the network is then leased to the telco.

For the projects executed under the IP-1 License, the right to use the network is given to the vendors on irrefutable basis for a specific period of time as agreed between the company and the vendors and the ultimate ownership of the network is with DEL.

Operations & maintenance (O&M) of telecom network: DEL also undertakes the O&M activity for the telecom operators and of the leased fiber maintained under IP-1 License. O&M activities involves deploying manpower and tools required for maintenance such as splicing machine, rodometre, OTDR machine etc. to monitor the route of the operator and preventing the underground optic fiber therein from getting damaged due to activities like road repairs, digging and expansion works by various authorities. For the fiber laid by it either as vendor project or on own account under IP-1 license, the company is preferred for the O&M for the same. The key focus under the O&M activity is the early identification of the faults and undertake the repair activities in a timely manner in order to minimize the network downtime.

Below are the segment-wise revenue details earned by DEL in past three fiscal:

Particulars	For the Period ended on		
	March 31, 2018	March 31, 2017	March 31, 2016
Revenue Breakup			
A. Telecom			
Vendor Projects / Contract Receipts	2713.24	1482.20	1099.41
IP 1 Leasing Income	274.80	178.58	105.48
B. Income From Mahanagar Gas Limited - Gas Pipeline	33.69	31.54	17.64
Total Revenue from Operations	3021.73	1692.32	1222.53
% of Revenue from Telecom	98.89%	98.13%	98.56%
% of Revenue from Mahanagar Gas Limited - Gas Pipeline	1.11%	1.87%	1.44%

Order Book: DEL's order book, as of any particular date, consists of the unexecuted portions of its outstanding orders, that is, the total contract value of the existing contracts secured by it, as reduced by the value of work executed and billed until the date of such order book. As of 01st Apr. 2018, the company's total order book was approximately Rs. 4,200mn.

Competition: The company operates in a competitive atmosphere specific to vendor projects executed for telcos. It faces competition from other optical fiber laying companies operating in the same geographies as it is operating. The competition depends on various factors, such as the total contract value, potential margins, the complexity, location of the project and risks relating to revenue generation. But DEL has an advantage over its competitors, as it has its own team of sub-contractors in various location across different states and the telecom operator get a single point of contact for coordination and understanding work progress details for different projects undertaken at different locations. While service quality, technical ability, performance record, experience, health and safety records and the availability of skilled personnel's are key factors in client decisions among competitors, however, price often becomes the main deciding factor while awarding of the projects.

Company Introduction (Contd...):

Financial performance: On account of 56.8% CAGR rise in the business from the telcos (i.e. vendor contracts), DEL reported 57.2% CAGR rise in the consolidated operating revenue over FY16-18 to Rs. 3,021.7mn in FY18. Vendor contracts contributed around 90% of the total revenue over the period. Other source of revenue i.e. fiber leasing reported a 61.4% CAGR rise in business during the period.

Operating expenditure, which included labor and sub-contract charges increased by 43.4% CAGR and formed around 58% of the revenue over FY16-18. Employee benefit and administrative & other expenses too increased by 50.6% and 65.5% CAGR. As a result total operating expenditure increased by 43.4% CAGR. Consolidated EBITDA increased by 97.3% CAGR to Rs. 1,079.6mn in FY18. EBITDA margin expanded from 22.7% in FY16 to 35.7% in FY18.

Depreciation & amortization charges increased by 35.2% CAGR, while finance cost was flat during the period. Other income increased by 55.9% CAGR, which can be primarily attributable to interest income. With almost stable tax rate, reported PAT increased by 118.8% CAGR to Rs. 617mn FY18. PAT margin expanded from 10.5% in FY16 to 20.4% in FY18.

Cash flow from operations was positive over FY16-18 with an average annual cash flow of Rs. 343.8mn. Baring FY17, free cash flow was positive throughout the period and increased by 68.4% CAGR to Rs. 255.1mn in FY18. Average RoE was around 50% over FY16-18. Average RoCE was around 30% during the period.

	FY16	FY17	FY18	CAGR (%)	Y-o-Y (%)
Revenue from Operations	1,222.5	1,692.3	3,021.7	57.2%	78.6%
EBITDA	277.5	456.7	1,079.6	97.3%	136.4%
Reported PAT	128.89	220.05	617.00	118.8%	180.4%
Restated Adjusted EPS	3.3	5.6	15.6	118.8%	180.4%
Cash Flow from Operating Activities	287.8	469.6	274.1	-2.4%	-41.6%
NOPLAT	141.0	234.0	627.1	110.9%	168.0%
FCF	89.9	(355.5)	255.1	68.4%	-171.8%
RoIC (%)	23.0%	20.1%	31.9%	886 bps	1,185 bps
Revenue Growth Rate (%)	140.2%	38.4%	78.6%		
EBITDA Growth Rate (%)	79.5%	64.6%	136.4%		
EBITDA Margin (%)	22.7%	27.0%	35.7%	1,303 bps	874 bps
EBIT Growth Rate (%)	89.9%	66.7%	169.0%		
EBIT Margin (%)	17.6%	21.2%	32.0%	1,435 bps	1,075 bps
Reported PAT Growth Rate (%)	85.6%	70.7%	180.4%		
Reported PAT Margin (%)	10.5%	13.0%	20.4%	988 bps	742 bps
Inventories Turnover Ratio (x)	45.5		17.3	-38.4%	
Trade Receivable Turnover Ratio (x)	5.1	4.7	4.7	-4.7%	-1.7%
Accounts Payable Turnover Ratio (x)	5.0	4.2	3.3	-18.0%	-19.5%
Fixed Asset Turnover Ratio (x)	2.2	2.4	2.6	10.0%	10.2%
Total Asset Turnover Ratio (x)	0.9	0.9	0.7	-9.1%	-15.4%
Current Ratio (x)	1.1	1.9	1.4	14.9%	-24.4%
Debt to Equity (x)	0.6	0.3	0.3	-34.2%	-13.1%
Net Debt (Rs.)	165.8	(9.4)	275.6	28.9%	
Net Debt to EBITDA (x)	0.6	(0.0)	0.3	-34.6%	
RoE (%)	44.5%	47.7%	57.0%	1,256 bps	935 bps
RoA (%)	9.2%	11.1%	14.8%	554 bps	365 bps
RoCE (%)	23.6%	24.2%	40.8%	1,721 bps	1,661 bps

Source: Company RHP



Competitive Strengths:

- Established optic fiber network in India
- Strong project management and execution capabilities
- Efficient business model
- Long standing customer relationships with strong repeat business
- Co-ordial relationship with suppliers and contractors

Business Strategy:

- Enhance the coverage of the optic fiber network
- Expand into business areas that create synergies with existing business
- Augment customer relationships
- Enhance project execution capabilities



Risk and Concerns:

- Slowdown in the telecommunication sector
- Adverse regulations
- Revenue concentration risk
- Poor capacity utilization in fiber leasing business
- Rise or volatility in raw material prices
- Highly labor oriented operations
- Competition

Peer Comparison and Valuation:

Company Name	Face Value (Rs.)	CMP (Rs.)	MCAP (Rs. mn)	EV (Rs. mn)	1M	3M	6M	1Y	Total Operating Revenue (Rs. mn)	EBITDA (Rs. mn)	PAT (Rs. mn)	EBITDA Margin (%)	PAT Margin (%)
Dinesh Engineers Ltd.	10	185	7,308	5,733					3,021.7	1,079.6	617.0	35.7%	20.4%
OnMobile Global Ltd.	10	40	4,202	2,354	-5.9%	3.7%	-7.8%	-29.1%	6,356.1	605.6	113.5	9.5%	1.8%
Uniinfo Telecom Services Ltd.	10	30	325	414	-10.6%	-27.6%	-43.3%		360.8	87.6	38.8	24.3%	10.7%
Average												16.9%	6.3%

Company Name	EPS (Rs.)	BVPS (Rs.)	DPS (Rs.)	Debt Equity Ratio	Fixed Asset Turnover Ratio	RoE (%)	RoCE (%)	P / E (x)	P / B (x)	EV / Sales (x)	EV / EBITDA (x)	MCAP / Sales (x)	Earnings Yield (%)	Order Book to Sales (x)
Dinesh Engineers Ltd.	15.6	74.2	0.0	0.1	2.6	21.0%	22.9%	11.8	2.5	1.9	5.3	2.4	8.4%	1.4
OnMobile Global Ltd.	1.1	54.6	1.7	0.0	11.1	2.0%	2.2%	37.0	0.7	0.4	3.9	0.7	2.7%	
Uniinfo Telecom Services Ltd.	3.6	30.3	0.0	0.3	13.2	12.0%	19.0%	8.4	1.0	1.1	4.7	0.9	11.9%	
Average				0.1	12.1	7.0%	10.6%	22.7	0.9	0.8	4.3	0.8	7.3%	0.0

Note: All financials is of FY18; Source: Choice Broking Research

There are no comparable listed companies in India that engage in the same line of business as the company. However, the above peers are considered as the proxy peers as they provide services to the telcos. At the higher price band of Rs. 185 per share, DEL's share is valued at a P/E multiple of 11.8x (to its restated FY18 EPS of Rs. 15.6).

Below are few key observations of the issue:

- Optical fiber is the primary communication media for broadband services. Optical fiber has the ability to carry virtually unlimited bandwidth provides, the most viable medium for carrying the digital signals. With rising urban and rural 4G penetration, there is increased demand of unlimited data bandwidth, which can be only resolved through the enhanced deployment of optic fibers. The proposed deployment of the 5G technology in future would also propel the demand of optic fibers. Thus to meet the increased demand, it is necessary to execute the existing and future 4G and 5G technology on OFC network. It is estimated that, 4G deployment would increase the optic fiber demand 4.5x times over 3G, while 5G deployment would increase the fiber demand 2x times over 4G.
- Prominent government support through policies like Digitalization and the new telecom policy i.e. "The National Digital Communications Policy, 2018" are also putting more emphasis on the increased fiber rollout. The government wants to get 60% of base stations fiberized, which will accelerate move towards 4G/5G and bring fixed-line broadband access to 50% of households. This is one of the key goals, as with 1.5mn kms OFC network, still less than 25% of telecom towers are fiber-connected. Thus, there is an immense opportunity for growth for the entities engaged in the OFC network deployment.
- Incorporated in 2006, DEL is primarily engaged in executing optical fiber laying work for telcos and ISPs in India. It is the dominant player in the Western and Southern India, having present in 15+ telecom circle across 16 states.
- In 2008, it was granted Infrastructure Provider (IP)-I License by the DoT, pursuant to which it has right to build, operate and manage wired network which can be used by the telcos and ISPs. Since 2011, the company has laid fiber network of around 9,500kms for the telcos under the vendor projects, which run across the states of Maharashtra, Gujarat, Uttar Pradesh, Bihar, Karnataka, Andhra Pradesh, Chhattisgarh, Goa and Rajasthan. Apart from laying the network, the company is also engaged in the operations & maintenance activity of the fiber network. As on 1st Apr. 2018, DEL had a vendor project order book of Rs. 4.2bn (i.e. 5,600kms optic fiber), which is to be executed in FY19. According to the management, with lower optic fiber penetration and increased penetration of mobile broadband, there would be sustainable growth in the vendor order book in future and the company is well placed to benefit from the same. Revenue from vendor contracts forms around 90% of the total revenue and has increased by 86.2% CAGR over FY15-18. EBITDA margin from this vertical is around 20-25%.

Peer Comparison and Valuation (Contd...):

- Under fiber lease business, DEL has its own OFC network of around 7,500kms, which runs across the state of Rajasthan, Gujarat, Maharashtra, Goa, Karnataka, Andhra Pradesh and Telengana. This wired network solutions are used by telcos such as Bharti Airtel, BSNL, Reliance Jio, Vodafone, Idea, Tata Communication etc., which helps them in increasing network's bandwidth, maximize existing network capacity, improve network performance and availability. Normally, the company enters into a 15 years lease agreement with the telcos and one year agreement with the ISPs. DEL is witnessing increased demand of its fiber leasing business and can be demonstrated by the improving capacity utilization, which increased from 20% in FY15 to 32% in FY18. Over FY15-18, revenue from this business increased by 45.8% CAGR. Since there is minimal operating cost involved in leasing the fiber network, the EBITDA margin from this business is around 85-90%.
- The vendor project order book, which the company is executing is in different geographical areas and is not overlapping with any of its existing OFC network. Also along with the vendor contract, DEL is parallelly putting its own OFC of 5,600kms capacity. Thus, this provides an increased geographical coverage and increased owned leased fiber capacity. The net proceeds from this IPO would be largely utilized for the expansion of this owned OFC network.
- On financial front, DEL has demonstrated robust performance. Over FY16-18, it reported a 57.2% CAGR rise in the consolidated operating revenue to Rs. 2,746.9mn in FY18. Consolidated EBITDA increased by 97.3% CAGR to Rs. 1,079.6mn in FY18. EBITDA margin expanded from 22.7% in FY16 to 35.7% in FY18. Reported PAT increased by 118.8% CAGR to Rs. 617mn in FY18. PAT margin expanded from 10.5% in FY16 to 20.4% in FY18. Cash flow from operations was positive over FY16-18 with an average annual cash flow of Rs. 343.8mn. Baring FY17, free cash flow was positive throughout the period and increased by 68.4% CAGR to Rs. 255.1mn in FY18. Average RoE was around 50% over FY16-18. Average RoCE was around 30% during the period.
- Based on our quick forecast. For FY19E, we are anticipating a top-line of Rs. 4,751.1mn (a growth of 57.2% over FY18) and an EPS of 19.5 per share (a growth of 25% over FY18). EBITDA and PAT margin are anticipated at 28.7% and 16.2%, respectively. In FY20E, we are expecting a 68.1% rise in the operating revenues to Rs. 7,985.1mn and an 89.2% rise in EPS to 36.9 per share. With dilution in the equity base, RoE would drop to 20.8% in FY19E as against 57% in FY18. However, this is expected to improve to 28.3% in FY20E.
- One of the key concerns for the company is its stretched receivables. In FY16, FY17 and FY18, the trade receivables were around 19.5%, 28.1% and 27.2% of the total revenue, respectively. Moreover, the top-five debtors represented 82.5%, 76.2% and 87.3% of the total outstanding debt, respectively, during the period. This demonstrates the stress in the telecom sector. Thus any delay or default in the payment from the customers would be negative for the company.

On valuation front, at higher price band, the company is demanding a P/E valuation of 11.8x (to its restated FY18 EPS of Rs. 15.6). Considering the positive future outlook, strong financial performance and capacity expansion in the higher EBITDA margin segment, we feel the issue is attractively priced. However, considering the sustainability in the profitability margins, current turbulence in the domestic equity market and listing in "T" category, we assign a **"Subscribe with Caution"** rating to the issue.

Financial Statements:

Consolidated Profit and Loss Statement (Rs. mn)

	FY16	FY17	FY18	CAGR over FY16 - 18 (%)	Annual Growth over FY17 (%)
Revenue from Contracts	1,117.1	1,513.7	2,746.9	56.8%	81.5%
Revenue from Leasing Fiber Capacity	105.5	178.6	274.8	61.4%	53.9%
Revenue from Operations	1,222.5	1,692.3	3,021.7	57.2%	78.6%
Operational Expenses	(749.6)	(1,036.4)	(1,541.0)	43.4%	48.7%
Cost of Raw Material Consumed / Purchase of Stock in Trade	(93.5)	(73.3)	(388.3)	103.7%	429.5%
Changes in Inventories of Raw Material and Work in Progress	(26.9)	0.0	175.0		
Employee Benefits Expenses	(38.1)	(68.9)	(86.4)	50.6%	25.5%
Administrative and Other Expenses	(37.0)	(57.1)	(101.4)	65.5%	77.6%
EBITDA	277.5	456.7	1,079.6	97.3%	136.4%
Depreciation and Amortization Expense	(61.8)	(97.3)	(112.9)	35.2%	16.1%
EBIT	215.6	359.4	966.7	111.7%	169.0%
Finance Costs	(20.7)	(27.8)	(19.9)	-1.9%	-28.6%
Other Income	2.5	6.8	6.1	55.9%	-11.0%
Exceptional Items	(0.4)	(0.4)	(1.7)	122.3%	311.9%
PBT	197.13	337.98	951.15	119.7%	181.4%
Tax Expenses	(68.2)	(117.9)	(334.2)	121.3%	183.3%
Reported PAT	128.89	220.05	617.00	118.8%	180.4%

Consolidated Balance Sheet Statement (Rs. mn)

	FY16	FY17	FY18	CAGR over FY16 - 18 (%)	Annual Growth over FY17 (%)
Equity Share Capital	2.5	2.5	295.0	986.3%	11700.0%
Other Equity	287.3	459.0	784.9	65.3%	71.0%
Minority Interest			2.1		
Long Term Borrowings	96.8	138.8	115.7	9.4%	-16.6%
Long Term Provisions	2.3	3.7	2.8	10.2%	-22.7%
Deferred Tax Liabilities (Net)	5.2	6.0	10.4	42.1%	72.8%
Other Non Current Liabilities (Lease Income Received in Advance)	518.9	874.2	1,156.9	49.3%	32.3%
Short Term Borrowings	78.4		167.0	46.0%	
Trade Payables	376.3	437.0	1,367.3	90.6%	212.9%
Other Current Financial Liabilities	14.5	11.3	19.2	14.9%	69.7%
Other Current Liabilities	14.9	41.9	53.4	89.5%	27.4%
Short Term Provisions	0.2	0.2	1.4	200.0%	513.6%
Current Tax Liabilities		5.8	203.3		3405.3%
Total Liabilities	1,397.2	1,980.4	4,179.4	73.0%	111.0%
Property, Plant and Equipment	500.2	677.5	689.8	17.4%	1.8%
Capital Work-in-Progress	64.6	35.6	462.3	167.5%	1197.2%
Intangible Assets	0.7	0.4	3.8	128.8%	855.0%
Non Current Trade Receivables	69.0	93.8	60.0	-6.8%	-36.1%
Non Current Investments	0.0	0.0	1.3	1035.8%	12800.0%
Non Current Financial Assets	115.6	163.6	293.4	59.3%	79.4%
Other Non Current Assets	116.5	59.9	47.7	-36.0%	-20.4%
Inventories			175.0		
Trade Receivables	238.2	475.8	821.0	85.7%	72.6%
Cash and Bank Balances	9.4	148.2	7.2	-12.5%	-95.2%
Current Loans	0.1	0.4	0.2	14.4%	-60.5%
Current Financial Assets (Unbilled Revenue)	243.4	281.9	1,503.6	148.5%	433.3%
Other Current Assets	39.5	43.2	114.2	70.1%	164.1%
Total Assets	1,397.2	1,980.4	4,179.4	73.0%	111.0%

Source: Company RHP

Financial Statements:

Consolidated Cash Flow Statement (Rs. mn)

Particulars (Rs. mn)	FY16	FY17	FY18	CAGR over FY16 - 18 (%)	Annual Growth over FY17 (%)
Cash Flow Before Working Capital Changes	277.5	456.1	1,080.7	0.97	1.37
Change in Working Capital	76.7	124.7	(673.8)		-6.40
Cash Flow from Operating Activities	287.8	469.6	274.1	-2.4%	-41.6%
Purchase of Property , Plant & Equipment	(230.5)	(279.8)	(128.7)	-25.3%	-54.0%
Cash Flow from Investing Activities	(267.7)	(238.6)	(551.8)	43.6%	131.3%
Cash Flow from Financing Activities	(43.8)	(100.3)	147.4		-247.0%
Net Cash Flow	(23.8)	130.8	(130.3)	134.2%	-199.6%
Opening Balance of Cash and Bank Balances	29.2	5.4	136.2	116.1%	2417.4%
Closing Balance of Cash and Bank Balances	5.4	136.2	5.9	4.2%	-95.7%

Consolidated Financial Ratios

Particulars (Rs. mn)	FY16	FY17	FY18
Revenue Growth Rate (%)	140.2%	38.4%	78.6%
EBITDA Growth Rate (%)	79.5%	64.6%	136.4%
EBITDA Margin (%)	22.7%	27.0%	35.7%
EBIT Growth Rate (%)	89.9%	66.7%	169.0%
EBIT Margin (%)	17.6%	21.2%	32.0%
Reported PAT Growth Rate (%)	85.6%	70.7%	180.4%
Reported PAT Margin (%)	10.5%	13.0%	20.4%

Liquidity Ratios

Current Ratio	1.1	1.9	1.4
Debt Equity Ratio	0.6	0.3	0.3
Net Debt to EBITDA	0.6	(0.0)	0.3

Turnover Ratios

Inventories Days	8.0		21.1
Debtor Days	71.1	77.0	78.3
Payable Days	(73.2)	(87.7)	(109.0)
Cash Conversion Cycle	5.9	(10.7)	(9.5)
Fixed Asset Turnover Ratio (x)	2.2	2.4	2.6
Total Asset Turnover Ratio (x)	0.9	0.9	0.7

Return Ratios

RoE (%)	44.5%	47.7%	57.0%
RoA (%)	9.2%	11.1%	14.8%
RoCE (%)	23.6%	24.2%	40.8%

Per Share Data

Restated Reported EPS (Rs.)	3.3	5.6	15.6
Restated DPS (Rs.)	0.8	1.0	0.0
Restated BVPS (Rs.)	7.3	11.7	27.4
Restated Operating Cash Flow Per Share (Rs.)	7.3	11.9	6.9
Restated Free Cash Flow Per Share (Rs.)	2.3	(9.0)	6.5
Dividend Payout Ratio	23.3%	18.2%	0.0%

Note: Ratios calculated on pre-issue data;

Source: Company RHP

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