

## Strong performance; healthy outlook...

Tata Communication reported a better-than-expected performance on the operating front led by superior revenues and margins in the data segment. The topline was at ₹ 4403 crore, up 5.6% YoY, 0.1% QoQ, led by superior data revenues (forming ~82% of revenues) that grew 9.9% YoY. **EBITDA came in at ₹ 1042 crore, up 26.2% YoY, with margins at 23.7% (up 385 bps YoY) driven by strong data margins of 27.1% (up 450 bps YoY), aided by structural cost efficiency (likely to remain) of ~₹ 100 crore (including moving of employee base in India) and Covid-19 led benefits (savings in travel costs, lower SG&A costs and concession from the government from international entities).** The company reported a PAT of ₹ 257.8 crore, up ~2.4x YoY.

## Strategic growth plans paint a healthy future ahead

The company has laid down a strategic direction for growth with steps such as deeper engagement with key clients, cleaner structure, automation in processes and greater ownership of customer outcomes. Tata Communication intends to transform into a solution platform and has launched *Secure Connected Digital Experience (SCDX)*, a platform based solution for digital experience for its enterprise customers. **Its medium term financial targets include (1) double-digit EBITDA growth led by double digit data revenue growth, continued cost optimisation, (2) RoCE of 20% in the next three years and (3) healthier balance sheet with significant reduction.**

## Data segment margin witnesses upward shift

A turnaround in growth services was visible with a second consecutive quarter of double digit margins along with a healthy trajectory in traditional services driving profitability. **The funnel addition has been highest in the last two years across all portfolios including network transformation and unified collaboration. The company expects the same to get converted into an order book and then revenues, over the next couple of quarter.** We bake in 8.8% revenue CAGR in FY20-22E in the overall data segment, largely driven by traction in growth and innovation services. We expect data margins to expand to 25.4% in FY22 vs. 19.3% in FY20, driven by enhanced growth segment margin trajectory and structural cost control measures.

## Valuation & Outlook

The consistent performance of the data segment is impressive with step up in margins led by scale & cost initiatives. The rising internet traffic and work from home (WFH) are structurally positive for the company. We revise our EBITDA estimates upwards by ~20% and ~14% for FY21 and FY22, respectively. The company's strategic growth plan, focused approach and consistent improvement in data segment warrant a multiple re-rating, a part of which is visible in the price run up. We believe continued performance and deleveraging possibilities bode well for the company. Thus, we upgrade to **BUY** (vs. HOLD earlier) with a revised SoTP target price of ₹ 880/share.

### TATA COMMUNICATIONS

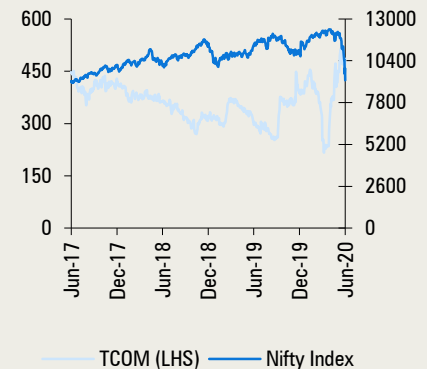
#### Particulars

Particulars	Amount
Market Capitalization	₹21652.9 Crore
Total Debt (FY 20)	₹10746 Crore
Cash (FY 20)	₹909.1 Crore
EV	₹33182.3 Crore
52 week H/L	760/ 200
Equity capital (₹crore)	285.0
Face value (₹)	10.0

#### Key Highlights

- EBITDA margin at 23.7% (up 385 bps YoY) driven by superior data margins of 27.1% (up 450 bps YoY)
- Upgrade from HOLD to BUY rating, valuing at ₹ 880/share on SoTP basis

#### Price Chart



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#### Key Financial Summary

(₹Crore)	FY18	FY19	FY20	FY21E	FY22E	CAGR (FY19-22E)
Net Sales	16,650.8	16,525.0	17,068.0	17,937.5	19,014.8	5.5
EBITDA	2,291.4	2,744.9	3,289.0	3,978.5	4,335.4	14.8
Adjusted PAT	46.9	(232.2)	283.9	800.4	1,006.5	88.3
Adjusted P/E (x)	461.7	NM	76.3	27.1	21.5	
Price / Book (x)	43.4	NM	NM	NM	NM	
Adjusted EPS (₹)	1.6	(8.1)	10.0	28.1	35.3	
EV/EBITDA (x)	12.7	11.1	10.1	7.9	6.8	
RoCE (%)	5.9	5.4	7.8	12.7	15.7	
RoE (%)	9.4	NM	NM	NM	NM	

Exhibit 1: Variance Analysis

	Q1FY21	Q1FY21E	Q1FY20	Q4FY20	YoY (%)	QoQ (%)	Comments
Revenue	4,402.9	4,375.8	4,168.6	4,397.9	5.6	0.1	The data revenues (forming ~82% of the revenues) grew by 10% YoY vs. our expectations of 9.4% growth.
Other Income	14.7	25.0	8.8	37.3	66.7	-33.0	
Employee Expenses	762.4	798.6	768.7	792.2	-0.8	0.8	
Administrative Expenses	857.4	1,028.3	865.9	1,048.2	-1.0	-1.9	
Network costs	1,741.3	1,693.4	1,708.4	1,688.6	1.9	0.3	
Raw Material Expense	0.0	0.0	0.0	0.0	0.0	0.0	
EBITDA	1,041.8	855.5	825.6	868.8	26.2	-1.5	The beat at EBITDA levels were on account of superior data margins of 27% (up 450 bps YoY) and much higher than expectations of 22.6%.
EBITDA Margin (%)	23.7	19.6	19.8	19.8	385 bps	390 bps	
Depreciation	589.9	580.0	552.2	686.7	6.8	-14.1	
Interest	116.3	121.7	115.7	123.2	0.5	-5.6	
Exceptional Items	10.5	0.0	6.5	378.1	0.0	0.0	
Total Tax	81.2	80.5	85.2	-9.8	-4.7	-925.3	
PAT	257.8	96.8	76.6	-275.0	236.5	-193.7	The beat at operating levels percolated to PAT
Total Minutes (in billion)	5.4	5.5	5.4	5.5	0.0	-1.8	
GDS Revenues	3,604	3,587	3,278	3,595	9.9	0.2	

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

(₹Crore)	FY21E			FY22E		
	Old	New	% Change	Old	New	% Change
Revenue	17,726.7	17,937.5	1.2	18,668.1	19,014.8	1.9
EBITDA	3,326.0	3,978.5	19.6	3,808.3	4,335.4	13.8
EBITDA Margin (%)	18.8	22.2	342 bps	20.4	22.8	240 bps
PAT	350.0	793.3	126.7	536.9	1,006.5	87.5
EPS (₹)	12.3	27.8	126.7	18.8	35.3	87.4

Source: Company, ICICI Direct Research

## Business Highlights

### Voice business:

- Revenue for the quarter came in at ₹ 799 crore, down 10.2% YoY and 0.5% QoQ, on account of a decline in voice minutes despite firm realisations for the quarter. We note that a decline in revenue was lower on account of higher usage due to lockdown. Voice overall volume came in at 5.2 billion (bn) minutes, a decline of 18.8% YoY, 3.7% QoQ. Realisations, on the other hand, were up 10.5% YoY (up 3.4% QoQ) to ₹ 1.54/minute on account of better destination mix
- Voice margins for the quarter came in at 8.4%, down 160 bps YoY as base quarter margins were aided by one-time settlement benefit

### Data business

- Revenue grew 9.9% YoY, 0.2% QoQ at ₹ 3604 crore, driven by strong momentum in growth segment and continued traction in traditional segment. Sequential revenue growth was flat due to slowdown in TCTSL, TCPSL and one-time bump up in rental revenue in Q4 **enterprise segment (63% of revenues) grew 11.7% YoY while service providers/carriers revenues were up 7% YoY**
- EBITDA was at ₹ 975 crore with a margin of 27.1%. EBITDA has grown 32.4% YoY, 18.4% QoQ. EBITDA margins expanded 450 bps YoY and 410 bps QoQ, driven by cost efficiencies and lower costs due to lockdown

### Traditional data services

- Revenue for the quarter was up 7.8% YoY, 1.5% QoQ at ₹ 2229 crore. Within this portfolio, the company witnessed a strong uptick in bandwidth usage due to lockdown
- Reported EBITDA came in at ₹ 941 crore, witnessing growth of 18.5% YoY and 15.8% sequential growth with a margin of 42.2%, up 370 bps YoY on the back of cost efficiency costs due to lockdown

### Growth services:

- Revenue for the quarter came in at ₹ 923 crore, up 20.2% YoY, 7.9% QoQ, driven by new deals and surge in conferencing traffic. UCC revenues grew 34.4% QoQ on the back of increased usage of collaboration tools in lockdown. Media services, however, were affected by cancellation of sporting events
- EBITDA for the quarter came in at ₹ 115 crore, witnessing 451% YoY and 15.5% QoQ growth, on account of operating leverage. EBITDA margins have expanded by 80 bps QoQ to 12.4%, recording double-digit margins for a second consecutive quarter. **The company expects margins to remain robust in the long term given the scale and cost efficiencies**

### Transformation services:

- Revenue (net of inter-segmental eliminations) grew 10.9% YoY, declined 10.2% QoQ to ₹ 333 crore. The sequential decline was owing to loss of revenues due to termination of onerous contract
- EBITDA loss for the quarter was lower at ₹ 3 crore (vs ₹ 16 crore loss in Q4) as the company has been able to shed the onerous customer contract. **The company expects it to hit profitability in FY22**

Payment solutions:

- Revenue came in at ₹ 52 crore, down 41.3% YoY, 36.3% QoQ, affected by lockdown as the company witnessed a drop in average daily transactions to 56 in Q1FY21 from 84 in Q4FY20. As a result of the same, EBITDA loss was ₹ 4 crore vs ₹ 22 crore EBITDA in Q4

Other highlights:

- Capex for the quarter was at ₹ 371 crore vs. ₹ 340 crore in Q4. FCF was ₹ 224 crore. **The company guided for similar to FY20 capex levels (~1596 crore) capex levels for FY21. Net debt was at ₹ 9008 crore, decline of ₹ 168 crore QoQ, driven by healthy FCF.** Net debt to EBITDA on TTM basis is 2.6x (vs. 2.8 in FY20)
- Covid-19 impact:** The company expects work from home (WFH) to be a key medium term trigger for organisations to upgrade their digitisation experience. However, some segments like media vertical remained impacted but is likely to ramp up with resumption of sporting events. Furthermore, there have been some delays in execution of new orders due to delay in procurement of equipment from OEMs. On the costs front, **Covid-19 led benefits include savings in travel costs, lower SG&A costs and concession from the government from international entities cumulating to ₹ 50-60 crore, during the quarter**

Valuations

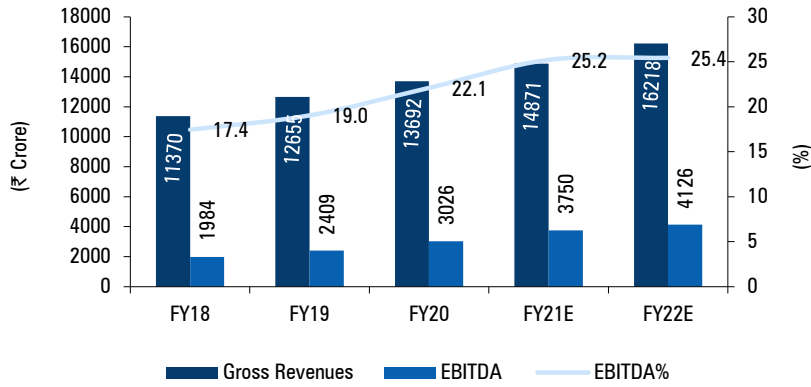
Exhibit 3: Valuations

Particulars	FY22 EBITDA (₹Crore)	EV/EBITDA (x)	Amount (₹Crore)
GVS Business Enterprise Value	209.8	3.0	640
GDS Business Enterprise Value (incl. Rent)	4,125.6	8.0	33,199
Data Centre - 26% stake (based on STT Tele deal valuation)			816
Less: Net Debt (incl. Lease Liability)	-	-	8,028
Less:AGR liability	-	-	1,541
Equity Value of the business	-	-	25,086
No. of equity shares outstanding (Crore)	-	-	28.5
Target Price	-	-	880

Source: Company, ICICI Direct Research

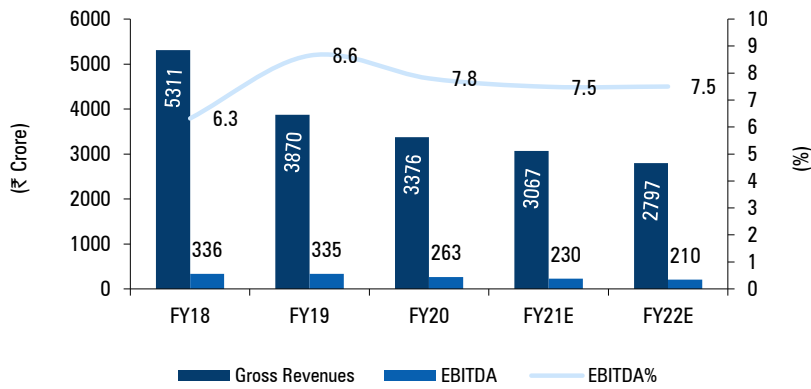
## Financial story in charts

Exhibit 4: Global data services operating performance



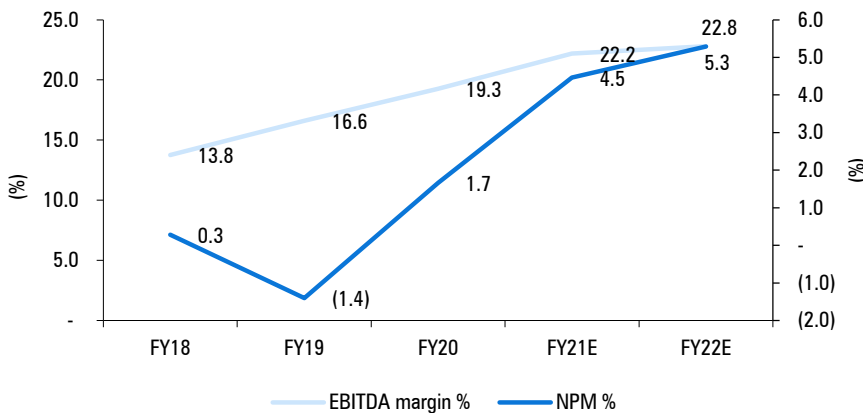
Source: Company, ICICI Direct Research

Exhibit 5: Global voice services operating performance



Source: Company, ICICI Direct Research

Exhibit 6: EBITDA and NPM margins trend



Source: Company, ICICI Direct Research

## Financial summary

Exhibit 7: Profit and loss statement				
	₹ crore			
(Year-end March)	FY19	FY20	FY21E	FY22E
<b>Total operating income</b>	<b>16525.0</b>	<b>17068.0</b>	<b>17937.5</b>	<b>19014.8</b>
Growth (%)	(0.8)	3.3	5.1	6.0
Employee Expenses	2959.7	3039.1	3130.6	3327.6
Network costs	7162.0	6777.6	7155.2	7472.8
Administrative Expenses	3658.4	3962.3	3673.2	3879.0
Other Expenses	0.0	0.0	0.0	0.0
Total Operating Expenditure	13780.1	13779.0	13959.0	14679.4
<b>EBITDA</b>	<b>2744.9</b>	<b>3289.0</b>	<b>3978.5</b>	<b>4335.4</b>
Growth (%)	19.8	19.8	21.0	9.0
Depreciation	2067.6	2357.7	2376.7	2395.9
Interest	396.6	470.7	479.8	470.7
Other Income	60.3	69.7	59.7	60.0
Exceptional Items	-2.2	390.6	10.5	0.0
PBT	343.2	139.7	1171.2	1528.8
Minority Interest	1.9	1.1	1.8	2.0
PAT from Associates	-150.3	2.2	-2.0	-2.0
Total Tax	273.3	226.7	374.1	518.3
<b>PAT</b>	<b>-82.4</b>	<b>-86.0</b>	<b>793.3</b>	<b>1006.5</b>
Growth (%)	NM	4.4	-1022.9	26.9
<b>Adjusted PAT</b>	<b>-232.2</b>	<b>283.9</b>	<b>800.4</b>	<b>1006.5</b>
Growth (%)	NM	NM	181.9	25.7
<b>EPS (₹)</b>	<b>-2.9</b>	<b>-3.0</b>	<b>27.8</b>	<b>35.3</b>

Source: Company, ICICI Direct Research

Exhibit 9: Balance sheet				
	₹ crore			
(Year-end March)	FY19	FY20	FY21E	FY22E
<b>Liabilities</b>				
Equity Capital	285.0	285.0	285.0	285.0
Preference Share Capital	0.0	0.0	0.0	0.0
Reserve and Surplus	-466.8	-1,563.4	-870.1	36.4
Total Shareholders funds	-181.8	-1,278.4	-585.1	321.4
Total Debt	10,274.3	10,746.0	10,346.0	9,086.2
Others	3,441.2	4,996.6	4,757.1	4,520.0
<b>Total Liabilities</b>	<b>13,533.7</b>	<b>14,464.2</b>	<b>14,518.0</b>	<b>13,927.7</b>
<b>Assets</b>				
Gross Block	34,741.8	36,977.0	38,577.0	40,177.0
Less: Acc Depreciation	23,475.6	25,833.4	28,210.1	30,605.9
Net Block	11,266.1	11,143.6	10,366.9	9,571.1
Capital WIP	298.3	286.0	286.0	286.0
Total Fixed Assets	11,564.5	11,429.6	10,652.9	9,857.0
Investments	1,491.3	1,563.1	1,613.1	1,663.1
Goodwill on Consolidation	86.3	91.8	91.8	91.8
Inventory	76.6	73.0	76.7	81.3
Debtors	2,968.5	3,228.9	3,390.9	3,594.6
Loans and Advances	238.7	259.6	272.8	271.9
Other Current Assets	690.6	929.6	977.0	1,035.6
Cash	852.1	909.1	1,855.4	2,271.3
Total Current Assets	4,826.5	5,400.2	6,572.8	7,254.7
Creditors	3,688.5	3,845.0	4,040.9	4,283.6
Provisions	601.6	726.0	763.0	849.3
Other current liabilities	2,188.9	3,126.3	3,285.5	3,482.9
Total Current Liabilities	6,479.1	7,697.3	8,089.4	8,615.7
Net Current Assets	-1,652.6	-2,297.1	-1,516.6	-1,361.0
Other non current assets	2,044.3	3,676.8	3,676.8	3,676.8
<b>Application of Funds</b>	<b>13,533.7</b>	<b>14,464.2</b>	<b>14,518.0</b>	<b>13,927.7</b>

Source: Company, ICICI Direct Research

Exhibit 8: Cash flow statement				
	₹ crore			
(Year-end March)	FY19	FY20E	FY21E	FY22E
Profit after Tax	-82.4	-86.0	793.3	1006.5
Add: Depreciation	2067.6	2357.7	2376.7	2395.9
Add: Interest Paid	396.6	470.7	479.8	470.7
(Inc)/dec in Current Assets	-328.5	-516.6	-226.4	-266.0
Inc/(dec) in CL and Provisions	-156.3	1218.2	392.1	526.3
Others	0.0	0.0	0.0	0.0
<b>CF from operating activities</b>	<b>1897.0</b>	<b>3444.1</b>	<b>3815.6</b>	<b>4133.4</b>
(Inc)/dec in Investments	-241.1	-71.8	-50.0	-50.0
(Inc)/dec in Fixed Assets	-2315.2	-2222.9	-1600.0	-1600.0
Others	-76.0	-82.7	-239.5	-237.0
<b>CF from investing activities</b>	<b>-2632.3</b>	<b>-2377.4</b>	<b>-1889.5</b>	<b>-1887.0</b>
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0
Inc/(dec) in loan funds	1287.1	471.7	-400.0	-1259.8
Less: Interest Paid	-396.6	-470.7	-479.8	-470.7
Less: Dividend and dividend tax	-152.6	-135.7	0.0	0.0
Others	-446.1	-874.9	-100.0	-100.0
<b>CF from financing activities</b>	<b>291.8</b>	<b>-1009.6</b>	<b>-979.8</b>	<b>-1830.5</b>
Net Cash flow	-443.5	57.0	946.3	415.9
Opening Cash	1295.6	852.1	909.1	1855.4
<b>Closing Cash</b>	<b>852.1</b>	<b>909.1</b>	<b>1855.4</b>	<b>2271.3</b>

Source: Company, ICICI Direct Research

Exhibit 10: Key ratios				
(Year-end March)	FY19	FY20	FY21E	FY22E
<b>Per share data (₹)</b>				
EPS	-2.9	-3.0	27.8	35.3
Adj. EPS	-8.1	10.0	28.1	35.3
BV	-6.4	-44.9	-20.5	11.3
DPS	5.4	4.8	0.0	0.0
Cash Per Share	29.9	31.9	65.1	79.7
<b>Operating Ratios (%)</b>				
EBITDA Margin	16.6	19.3	22.2	22.8
PBT / Total Operating income	4.1	5.5	8.9	10.2
PAT Margin	-1.4	1.7	4.5	5.3
Inventory days	1.7	1.6	1.6	1.6
Debtor days	65.6	69.0	69.0	69.0
Creditor days	81.5	82.2	82.2	82.2
<b>Return Ratios (%)</b>				
RoE	127.7	-22.2	-136.8	313.1
RoCE	5.4	7.8	12.7	15.7
RoIC	5.7	7.8	14.3	18.6
<b>Valuation Ratios (x)</b>				
P/E	-262.9	-251.9	27.3	21.5
EV / EBITDA	11.1	10.1	7.9	6.8
EV / Net Sales	1.8	1.9	1.8	1.6
Market Cap / Sales	1.3	1.3	1.2	1.1
Price to Book Value	-119.1	-16.9	-37.0	67.4
<b>Solvency Ratios</b>				
Debt/EBITDA	3.7	3.3	2.6	2.1
Debt / Equity	-56.5	-8.4	-17.7	28.3
Current Ratio	0.9	1.0	1.0	1.0
Quick Ratio	0.9	1.0	1.0	1.0

Source: Company, ICICI Direct Research

**Exhibit 11: ICICI Direct Coverage ( Telecom)**

Sector / Company	CMP (₹)	TP (₹)	Rating	M Cap (₹Cr)	EPS (₹)			P/E (x)			EV/EBITDA (x)			RoCE (%)			RoE (%)		
					FY20	FY21E	FY22E	FY20	FY21E	FY22E	FY20	FY21E	FY22E	FY20	FY21E	FY21E	FY20	FY21E	FY21E
Bharti Airtel	555	700	Buy	302,704	-59.0	-24.7	11.2	NM	NM	49.5	11.5	9.8	7.8	3.5	6.9	9.2	-4.7	4.2	11.3
Bharti Infratel	192	180	Hold	35,531	17.8	16.7	17.4	10.8	11.5	11.1	5.7	5.6	5.3	18.1	19.8	21.7	24.4	23.7	25.5
Vodafone Idea	8	UR	UR	24,138	-25.7	-7.5	-7.5	NM	NM	NM	9.5	8.1	7.0	-5.7	-4.7	-4.3	NM	NM	NM
Sterlite Tech	122	125	Reduce	4,901	10.8	8.1	11.4	11.3	15.0	10.7	6.4	7.7	5.9	27.8	20.9	15.8	33.0	25.1	15.8
Tata Comm	760	880	Buy	21,653	-3.0	27.8	35.3	NM	27.3	21.5	9.4	7.4	6.4	7.8	12.7	15.7	-22.2	NM	NM

Source: Company, ICICI Direct Research

## RATING RATIONALE

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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