Sterlite Technologies Limited Q1 FY25

Earnings Conference Call Transcript

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Chetan Wani: Ladies and gentlemen, good day and welcome to the STL's Q1 FY25 Earnings Conference Call. I am Chetan Wani, Head, Investor Relations at STL.

Today we are joined by Ankit Agarwal, Managing Director and CEO, Optical Networking Business, STL and Tushar Shroff, Group CFO, STL to walk us through the Q1 FY25 results and to take your questions.

Please note that all participant lines are in the listen only mode as of now, and there will be an opportunity for you to ask questions at the end of the presentation. You can also download a copy of the presentation from our website that is www.stl.tech. Please note that this call is being recorded.

Before we proceed with this call, I would like to add that some elements of today's presentation may be forward looking in nature and must be viewed in relation to the risks pertaining to the business. The Safe Harbor clauses indicated in the presentation also applies to this conference call.

I now hand over the call to Ankit Agarwal for opening remarks. Over to you Ankit.

Ankit Agarwal: Thank you Chetan. Good day everyone and thank you for joining us for our Q1 FY25 earnings conference call.

As we enter Q2 FY25, directionally our strategic priorities remain the same. On the Optical Networking Business, we shall continue to focus on driving growth by increasing OFC market share and connectivity attach rate. We will focus on rapidly building data centers suite of products to tap the huge potential in that space. We shall continue to also drive our technology and cost leadership in the optical business.

On the Global Services business we shall continue to build new capabilities for value added services. We shall stay focused on improving project mix to improve profitability, and we will work towards completing the demerger of our services business.

Lastly, in our STL digital business, we shall continue to scale the business to conscious investments in building new technology and domain capabilities while we keep our focus on maintaining our profitability.

STL has always endeavored to be a responsible leader and ensuring a connected and inclusive world. Through our various initiatives in education, women empowerment and health care, we have positively impacted millions of lives since FY19. To highlight some of these key initiatives, we started RoboEdge in 2023 with intention to power students with next gen skills and focus on robotics to enable career growth and we have been able to cover more than 11 schools and more than 3500 students have been benefited already. Next to the right is a Jeewan Jyoti program founded by Miss Jyoti Agarwal to empower underprivileged women by training them in various vocational skills to make them financially independent. So far more than 5000 women, artisans have been benefited from this program. We also started a hybrid healthcare program during COVID providing primary health care as well as tele health facilities to marginalized communities and rural parts of select districts of Maharashtra, we have impacted more than 1 million lives. To its left is afforestation and water pension program, where we are working with 26 Gram panchayats for creating or rebuilding 95 water structures. Our efforts have resulted in replenishment of 2.69 million cubic meters of water in Maharashtra. Under this project, we have created urban and rural forests by planting and maintaining more than three lakh plants and we will sincerely continue to drive such initiatives going forward.

On the ESG front, we are committed to our goal of being net zero emission organization by 2030. We present here some of the accomplishments on this front and to mention a few achievements since FY19. We have diverted more than 250,000 metric tons waste away from landfills. We have reduced emissions of more than 34,000 tons of carbon dioxide equivalent. We have recycled 860,000 cubic meter of water during this years. We are proud to share that we have even won more than 100 ESG awards for our work. We are the world's first optic fiber manufacturer launched externally verified eco label methodology when compared to standard products, these eco label products utilize approximately 52% less energy, carry 75% less global warming potential and use approximately 18% more recycled content and 25% more recycled packaging material. These products also reuse and recover almost 20% more waste and enhance the longevity of the network by nearly 13 years, thereby benefiting both the clients as well as the environment.

On the next few slides, let's talk about Optical Networking business and our specific efforts toward becoming the top three players in the optical connectivity business. Now as we reflect on FY24 in the last quarter, as per CRU latest estimates, OFC consumption for 2023 declined by 7% globally this was led by almost 12% decline in North America market. As we have shared previously, the inventory at multiple layers played a major role during this time. And sub optimal factory utilization was a trend across the industry. Despite a lower fresh demand during the last few quarters, we observed robust and continued fiber deployment resulting in healthy inventory digestion. Various Analysts' reports estimate steady demand improvement as well as demand scenario to stay robust for the medium and long term. As we look at the future projections from CRU, the medium term demand and the optical fiber cable volumes is expected to go up to 662 million fiber kilometers by 2028, up from 536 million fiber kilometers in 2023. Theis projects healthy 4.3% annual growth in global demand and a strong 7.1% growth in annual demand from 2023 to 2028 if we exclude China. The positive demand outlook by CRU along with our continued client commitments on increasing fiber deployment and steady STL order book additions is indicative of our recovery in the coming quarters.

Let us also look at a major technology trend, that is AI and its anticipated demand on fiber demand. As we discussed in previous earnings calls, AI and machine learning are gradually taking the center stage and swiftly blending in with all major mega technology trends, while data storage consumption and bandwidth requirements has spurred the demand for data centers over the last few years. 2023 will be remembered as the coming of age of AI. Chat GPT reached 100 million users worldwide in just two months, a goal that took Facebook four and a half years. Industry report suggests that two thirds of global network traffic shall involve AI by 2030. For the growth of AI and technologies to sustain and succeed, the technology backbone shall need massive amount of data center capacities to smoothly manage this data explosion. As we understand more, AI revolution is actually reshaping the data center designs and architecture. It's estimated that the overall optical connections and fiber requirements in AI data centers will be significantly higher than traditional CPU based data centers. If we look at some of the key layers in the data center architecture, typical optical connections in the AI data centers are estimated to be five times compared to traditional data centers and rack density may be as high as one and a half times. The fiber channels required to store in the storage layer is approximately estimated to be one and a half to two times of the traditional storage layers in traditional data centers. Overall network and connectivity may require as high as 18 times higher fiber content in the AI data centers. Overall data center capacity in the world is expected to grow at a rapid pace up until 2030 at least. In summary, in this era of the AI revolution, fiber shall need to be at the core of connectivity within and outside data centers. This fiber explosion within data centers and higher fiber requirements for data center interconnectivity presents a massive opportunity for a company like ours and have set an ambitious target that approximately 25% of our revenue should come from our data center suite of products in the medium term.

Apart from the AI driven investments that I just spoke about, globally, the fund infusion that we are seeing in 5G network creation FTTx deployments, as well as Cloud Data Center buildouts continue to be very strong. 5G remains one of the fastest growing technology in the world and tower fiberization is at the core of 5G not just in India, but also globally. 5G subscribers are expected to grow rapidly in the medium term across geographies, and we can expect 5G subscriber addition in North America, Western Europe and India to be robust all the way up to 2029. As per recent reports from Analysys Mason, the average fiberized mobile sites of towers in India stands 38% in 2024 which is expected to increase to 63% by 2029. With higher 5G subscribers and higher number of 5G towers, and higher fiberization requirements, 5G clearly is at the core of global expansion and should continue to drive demand for more optical fiber. FTTx connectivity, demand for homes and businesses globally remains strong as well. In the US alone, approximately 100 million homes await fibre to the home connections. Europe FTTx passes is expected to grow by 4% at least for the next five years. And India is expected to lead the global growth in FTTx installations, with 26% CAGR expected between 2023 and 2028. Data Center deployment is expected to continue attracting strong investments with data center capacity in North America projected to grow by more than 10% CAGR between 2024 and 2029. But Europe is expected to grow at 8.5% CAGR in 2027. In India, the existing data center capacity is expected to more than triple between now and 2028. As we saw previously, the data center connectivity requirements will continue to carry the demand for optical connectivity products. The demand outlook is also expected to be supported by other factors such as what we have witnessed in terms of improved telecom tariffs in India, especially between Airtel and Jio resulting in improved financial health and investment capability of the Indian telecom companies, the existing anti-dumping duty on Chinese products in India and Europe and overall industry shift from copper to fiber. On top of that, we also have the mega government projects such as the BEAD project in the US, BharatNet project in India and other such programs in Europe, Australia and other geographies, which will also overall increase the demand for optical connectivity products.

Coming specifically to the North America and the US region, at STL we are being optimistic on the demand in North America region. CRU has projected that the North American optical cable demand is expected to grow at approximately 13% CAGR till 2028. The fiber deployment in the region stayed strong at more than 9 million homes passed in 2023 alone and between 9-12 million incremental home passes additions are expected in the year 2024. The telecom and internet provider companies in North America have set aggressive ambitions on FTTx at home passes additions for the next two to three years. And have announced these targets publicly. For instance, AT&T in the very near term intends to add 19 million new homes, Lumen plans to add another 9 million homes, Frontier has already announced 5 million new homes to be passed. In addition, the government spending through BEAD and other programs shall only add to the fiber deployments planned by the private sector. As for the latest update, the program is progressing steadily asshowcased in thispage. Some analysts expect BEAD funding to begin by the start of 2024. All in all, it is estimated that in North America nearly as much fiber will be deployed in the next five to six years as has been deployed throughout history.

As a technology driven company for the past three decades, we have meticulously and passionately built capability across the optical fiber value chain. Our business and reason for existence is deeply rooted in fiber and technology has made the core of it right from creating Ultra Pure Glass Preform, State of the Art Optical Fiber Drawing, Optical fiber cable and most recently optical connectivity products, we are truly offering glass to gigabit connectivity. Our passion for innovation has driven us to solve industry challenges like attenuation, bend sensitivity, compatibility, duct space, labor availability, and the TCO reduction and created advanced fiber solutions that will support everything from immersive entertainment to Ad scale Gen AI experiences.

Some of our solutions are truly first in the world or sometimes first in India, such as India's first multi core fiber Multiverse which offers four times the capacity in the same fiber. Stellar fiber with superior bend in performance. We are amongst the first companies globally and amongst India's first to develop the world's slimmest fiber-miniaturized advanced fibers with diameters of 180 and 160 micron. We are also proud to share our progress on the IP portfolio, during Q1 FY25 our total IP patent portfolio increased to total of 715 patents, including filed and granted. We filed 32 new patents during this period and a record 24 patents were awarded to us in the US and India. We continue to push the boundaries and drive product innovations relentlessly to achieve many more firsts in the future as we move forward in our journey to become one of the top three optical networking companies globally.

Let us now reflect on a market share in optical connectivity rates. Basis CRU consumption data during H1 CY23 we had 8% market share on optical cable demand excluding China. Our Q1 CY24 market share however was observed at 6% amid challenging market demand environment. We believe that the market share shall normalize as a fresh demand steadily picks up and as we have also had intensified our efforts to regain our market share. We are happy to share that we recorded our highest ever optical connectivity attach rate during the last quarter at 23%. We are continuously working on new product developments and commercialization in optical connectivity space to further increase our attach rate.

Coming to the financial performance for the optical business in line with our guidance Q1 FY25 revenue stands at Rs.810 crores, which has marginally improved on quarter-on-quarter basis. EBITDA for the quarter stands at Rs.88 crores at 10.9% of revenues. EBITA margin reflects substantial improvement on Q-o-Q basis and stands low lower on Y-o-Y basis due to lower cable volumes. The Q-o-Q EBITDA improvement is indicative of success of various cost optimization measures undertaken by the company.

Having completed our capacity expansions are shared in previous discussions, we strategically located manufacturing assets and continued focus on cost structure optimization, product innovation and focus on data center product portfolio development as well as approval from tier one customers. We are very well positioned to capture the significant market share going forward and grow the business as the demand picks up.

Now let's discuss the progress in the Indian market and the growth of the global services business. In the global services business Q1 FY25 revenues stood at Rs.355 crores. Our selective order intake and execution focus has helped us achieve Q1 FY25 EBITDA of Rs.25 crores and EBITDA margin of 6.9%. We continue to build our capability towards value added services to improve our margin profile and reduce the fund involvement. On the project execution side, we have made substantial progress on all key projects during this quarter. Among major India public projects, our BharatNet project in state of the art Telangana is 69% complete including all packages. The data center project with PSU stands at 93% completion. Among the major India private projects fiber rollout for large Indian telco phase II is now 59% complete. Fiber rollout for a modern optical network for another private customer is 98% complete. With our extensive large project experience, we are well positioned to tap BharatNet phase III opportunities in the coming quarters.

Now let's discuss about STL digital business and their performance. In STL digital we are continuing the growth momentum. We are continuously working with new customers for growing our business in the US, Europe and India across technology and service verticals and observed a healthy fresh order flow during the last quarter. We are working with our 25 plus global customers and 40 plus active technology partners for business growth. We expect the future growth to be driven by robust order book of Rs.377 crores, healthy order pipeline and execution strength backed by the right team of leadership and consultants. In line with expectations and despite a tough industry environment, we achieved a quarter one FY25 revenue at Rs.71 crores displaying a growth on Y-o-Y basis. The EBITDA loss for Q1 FY25 stands at Rs.17 crores, the EBITDA loss is trending downwards on Y-o-Y basis and also suggests improved margins Q-o-Q basis.

I will now hand over to Tushar to talk through the financials.

Tushar Shroff: Thanks Ankit. Good day ladies and gentleman. In line with our guidance the consolidated Q1 revenue stands at Rs.1,218 crores showing improvement quarter-on-quarter basis. The Q1 EBITDA stands at Rs.93 crores and EBITDA margin stands at 7.6%. As guided our EBITDA margin has improved on quarter-on-quarter basis and for Q1 after the tax losses stands at Rs.47 crores, after the tax losses have reduced on quarter-on-quarter basis.

The new Order addition during the last quarter was robust with us securing the several large orders from marquee customers. We won the large long term orders from the leading UK telecom companies for optical interconnect and connectivity solutions. We secured large deals in Italy for optical fiber cable and specialty cable products. In India, we won large long term orders for fiber optic supply and deployment for a large private telecom operator. We also won large orders for our service business from an Indian public sector enterprise. On the back of global business our revenue mix was well diversified during Q1 FY25. We expect revenue mix to improve towards North America and Europe as the demand for optical products pick up in our global market.

We are happy to share that despite a significant order descoping, our open order book stands at Rs.9,883 crores at the end of Q1 FY25 backed by steady order wins. Our order book is well diversified across our customer segments and all of our businesses. We place before you an abridged version of reported numbers for your perusal. We are happy to share that the net debt has reduced by Rs. 769 crores from FY24.

With reference to global service demerger, we are progressing as planned on process of demerger. During the NCLT convened meeting on 10th July 2024 the scheme of demerger received 99.98% approval from the equity shareholders and 100% approval from the secured and unsecured creditors. The final NCLT approval are expected in indicative timeline of next three to four months and the resulting company is expected to get listed by the year end.

In summary, we have clear focus areas identified to drive business forward. In optical network business we shall target to drive the technology and cost leadership and pursue our ambition to be a global top three. We will increase the sales in our focused market to grow our optical network business and fill the volume gap. We will continue to increase optical connectivity business with a growth and attach rate with focus on rapidly building our data center product portfolio. In global service we will continue to focus on select project intake to improve the profitability and optimize the net fund involvement. In STL digital we will continue to scale the business and grow our revenue along with the focus on profitability.

With this now I hand over a call back to Chetan. Thank you.

Chetan Wani: Thank you, Tushar. Ladies and gentleman, we have come to the end of our presentation. And we shall now move to the Q&A session. We request you to keep your questions brief and limit the number of questions to maximum two so that the management can attend to maximum questions. The call is now open for Q&A

We will take the first question from the line of Nikhil Choudhary.Nikhil please go ahead and ask you a question.

Nikhil Choudhary: Hi and thanks for the opportunity. After a long time Ankit and Tushar we have seen first Q-o-Q growth. So, congratulations on that. But one thing here, the growth looks like it's driven by interconnect business where the attach rates jump from 11 to 23%. So basically, if you remove the interconnect part the core business was flattish or declined. So two questions here, first is how the demand is trending on the core business excluding interconnect and what's the outlook there. And second thing, what's the outlook on interconnect, after a long time it increased to 23%. Can it go further up?

Ankit Agarwal: Thank you Nikhil for your question. So, you have summarized it quite well. I think as we have been guiding, our focus markets continue to be US, Europe and India and as we have shared in the past, particularly in the US we had seen that it's been an interesting situation where on one side the inventories had been high but the deployment especially fibre to the home deployments have been very strong, in fact amongst the highest. So when I look at the market demand that I continue to be very positive about; it's triple play in terms of demand from the telecom operators, money coming in from private equity players into tier I and tier II service providers, as well as government funded projects, some from the past and BEAD which is expected to start coming in probably Q3, Q4 onwards, and then probably more significantly into next calendar year. So, from a demand perspective, definitely US and Europe will be our key drivers. I do also expect that in India, there will be continued focus on fibre to the home deployment, fibre to enterprise deployment as well as even when operators are talking about fixed wireless you will still need a fair bit of fiber connectivity which will be required up to that last 100-200 meters. So that's something that we do see principally a demand being positive. And then the fourth trigger and all of this will be the data center connectivity. As we just shared in one of our slides. We actually seeing a very interesting shift from so called regular data centers to DCs which are being built for more and more AI capability which will definitely require much more connectivity between the servers and the racks, etc. So, I would say principally we remain positive about the demand. We do see the inventory levels coming down, and certainly between next one to two quarters, this should result in improved demand for our optical cable products. On the connectivity part, principally I want to reiterate that we do endeavor to sell our cables and connectivity together as a solution. That's really where we believe we create value for our customers and then for STL, so that continues to be an endeavor. We continue to be focusing on our investments in building the technology, building the product portfolio, and also the IP. So I would say that this is something that we will continue to focus and prioritize but I wouldn't be able to give a specific guidance on connectivity. It will be both a function of how cable also steps up, and how we are able to win more orders both in Europe as well as in the US.

Nikhil Choudhary: Sure. Thank you for the detailed answer. Second and third are smaller question on the other two segments, services saw Q-o-Q jump but the margin did more or less in line with expectation but relatively higher than what we were thinking. So what should be a steady state margin in services and in the digital segment, despite of being lower base our revenue decline, high single digit on Q-o-Q basis. While I understand that our challenges in IT industry, still such a sharp decline was relatively higher. So those two are my final questions. Thank you.

Tushar Shroff: So Nikhil, with reference to the service business, steady state margin that we are expecting is in the range of 8-10% EBITDA margin, that is what we are targeting for this particular financial year. However, during this particular quarter, because it's a mix of the various orders which results into the margin. So there is a change in the mix, which has resulted in terms of the impact on the margin for this particular quarter but for overall financial year, we are looking at 8-10% in terms of sustainable EBITDA margin for this particular business. With respect to the digital business, yes this particular quarter because of the last couple of months and a couple of quarters, we have seen that the industry has witnessed slowdown in the IT sector, and which has also impacted us. However, we see this current financial year, we expect to grow this particular business over a period of time. So, overall we are targeting that we should be able to have at least 5-7% kind of growth in the digital business. That is what we are expecting.

Nikhil Choudhary: Sure. Understood. Thanks a lot and good luck for coming year.

Chetan Wani: Thanks Nikhil. We will take the next question from line of Balasubramaniam. Bala please go ahead.

Balasubramaniam: Good evening sir. Congratulations for Q-o-Q improvement. So, my first regarding BharatNet phase III and how much is the addressable market for us out of Rs.1,39,0000 crores and second question is there any delay in BEAD program due to political situation US

Ankit Agarwal: Thank you. Hi Bala. So one the current RFQ and opportunity right now from the spend perspective is Rs.65,000 crores. And I think it's important to remember that we would address this for 2-3 levels for us. It's an opportunity definitely on the services business, in terms of the entire deployment and then the materials. The second part would be supply of cables, both for our services requirements as well as other partners or players in the project. And then of course, the fiber itself to various cablers. So, this is something which is an opportunity across the board. I think it's a bit too early for me to share, we are in that phase where next 2-3 months where there will be more developments regarding this project. But certainly I would say there is a strong intent from the government to take this project forward and to make sure that the project is successful. In terms of the BEAD project, definitely there is a strong intent, the BEAD project was passed, which was bipartisan, so we don't see or expect any impact or slowdown of the BEAD project, particularly linked to the political situation. I would say that probably versus our own estimate earlier in this financial year to now we do see that the impact of BEAD ultimately to cable requirements, connectivity requirements, that probably got pushed out by 3-4 months or so.

Balasubramaniam: Got it. Sir we have lot of large deals in UK and India. So like what kind of environment levels for inventory reduction on global operator levels, and we when we can expect normal sees whether it's Q3 or Q4.

Ankit Agarwal: Yes, so as I said, we have been tracking this quite closely with our customers and also with their distributors. I would reiterate that the inventory topic that we have been talking about is largely a phenomenon in the US and probably to a smaller extent in Europe and UK. So I would say that what we are speaking about inventory, that is what we are seeing probably another one to two quarters more before we see the inventories are normalized. But I think when we talk about interest, RFQs or requirement requests coming up, I think that is moving in a good direction and the underlying demand of the market especially in the US, we continue to be bullish on for the next 4-5 years. As we shared is one of the slides we have won some good projects across UK, Europe that we've been talking about, which is both on the cable as well as connectivity. So as I said, our whole objective is to look at cable and connectivity together as a solution. And that's certainly something we are confident that the customer will see value in and will also be valuable to STL.

Balasubramaniam: Got it sir, my next question recording any improvement in OF and OFC prices and because our revenues majorly impacted by volumes. How much volumes have been dropped in this quarter, and we have seen some improvement on Q-o-Q basis it's because of realization side or increase in capacity utilization side.

Ankit Agarwal: I would say that overall, we won't be able to give specific volume details. But what I can share is that principally we've had, a flattish quarter in terms of volumes on the cable side but we've seen the positive growth on the connectivity side. So, I think that's how you should think about it. Definitely from a pricing perspective, again, I would say flattish to slight reduction. Again, that's also a function of where the mix of our sales has been. Our US sales has been on the lower side compared to Europe and India. So that has also reduced our overall realization at STL level. So as the US market improves as those exports increase, as well as what we produce locally there and we continue to sell to that extent our realization would improve again.

Balasubramaniam: Got it Sir. My final question, any kind of impact because of anti-dumping duty by European commission's because one of our competitors only exempted by European Commission's. So what kind of impact we can see not only for our company but the entire Indian market players.

Ankit Agarwal: Look, one I think it's important to remember that this is a provisional, so at least I can speak on behalf of STL. We are very confident on the merits of our case. We believe that with the right calculation levels, we do not believe there should be any case for anti-dumping and we are making all our representations with full effort. In terms of being prepared for it. I would say very confidently that we have one of the most advanced facilities for fiber optic cable in Italy, from where we can serve our European customers. We have invested in this facility significantly since we did the acquisition of Metallurgica a few years back, so we are very well set up to meet all our customer requirements with their lead times and product requirements. So from our perspective, meeting the customer requirements, we are very comfortable. In terms of the duty itself as I shared, we are definitely working on it. And to make sure that we put our full effort towards what is provisional duty currently. I won't be able to speak about rest of the industry, of course, different players have got different rates applied to them provisionally and I am sure the entire industry will work towards seeing how these can be removed or minimized.

Balasubramaniam: Got it, sir. Thank you.

Chetan Wani: We will take the next question from Advait. Please go ahead and ask you a question.

Advait: Sir congrats on a robust set of numbers. Just want to know how do you plan to structure your costs and is it across businesses and is the demerger a part of the cost restructuring.

Tushar Shroff: So, the way we have been looking at the cost structure is, overall we are looking at the fixed cost and we are attempting to see how we can optimize in terms of the fixed costs that we have, at the company level, whether in terms of manpower spent or in terms of other expenses or whether it's a logistic cost or whether it's a packaging material cost, all of that which are fixed in nature. We are trying to address all of that, by working with innovative solutions that we may be looking at, to find better way of managing the business. So, we are targeting to reduce fixed costs, at least to the extent of 4-5% on sustainable basis.

Advait: And this is across businesses.

Tushar Shroff: Yes, across the businesses.

Advait: And additionally, there is a Kavach, anti-collision opportunity in India, where the railways will be deploying 4G. So we just wanted to know if there's any kind of opportunity there for us.

Ankit Agarwal: I am familiar with the specific opportunity. We will definitely evaluate that and broadly I would make a view that not just BharatNet, there are multiple and very interesting opportunities for the services business. Just given the massive experience we have, whether it's on previous BharatNet projects, whether it's on system integration projects for the Indian Navy, Indian army. I think we are very well placed with our experience to capture some of the new opportunities that we are already starting to see in our pipeline.

Advait: Right Sir. Last question on the Italian plant we have, what is the capacity and how do you see that going up, if you can share.

Ankit Agarwal: I won't be able to comment on specific capacities but what I can share is that since we had acquired that facility, we have invested in scaling it up. And it's truly a world class facility. Now it's probably one of the largest facilities in Europe. So we are very well set up to cater to our customer requirements and certainly from a product portfolio perspective we are very well set up.

Advait: Thank you.

Chetan Wani: Thanks. We will take the next question from Sohan Joshi. Please go ahead.

Sohan Joshi: First question is with regards to the freight cost, the freight cost has increased by 2x almost across the geographies. So how are we impacted by this, I mean any impact on bottom line or the freight escalation enjoy the pass through status.

Tushar Shroff: So we have seen that the freight impact in our financials, what we have seen is that at least 2-3%, which we have seen that increase in the freight during this particular quarter, some part of the element is also with reference to the air freight that we had to incur to serve the customer better. It's a mix of the rate increase as well as in terms of the change of mix from air freight to sea freight that is also being impacted. But yes, in this quarter, we have seen a little bit of impact on the freight cost.

Sohan Joshi: So, going forward, are we planning to structure contracts in a way that henceforth you can pass on these costs to the customers because post COVID this has been a continuous issue, right.

Ankit Agarwal: Yes. I will break in two things, of course there is some element of this link to the Red Sea impact, and that has both caused some of the increase in costs as well as the insurance costs, lead times, travel transport times have gone up. So, I think that's anyone's guess by when those things normalize, but that is expected to normalize over the next few quarters. What we are doing in our own bases is, both just looking at how do we reduce our logistics costs, how do we reduce our container requirements itself, how do we become more efficient, at the same time, look at other types of contracts that we could do to minimize the costs, look at various routes. So that's the work we are doing. Typically our customers especially in our global customers, they typically want it on delivered basis, so it's up to us at STL to make sure that we can optimize our costs.

Sohan Joshi: Okay, my second question is with regards to the data center business, what growth run rate are we targeting. I mean, will it compensate to some extent toward declining volumes of OFC. Since internet companies are investing heavily in data center business, I presume the growth run rate will surpass every other business, right.

Ankit Agarwal: As I said, principally we definitely are very excited with the kind of opportunity we are seeing in the data center space. And as we said, because of this massive boom towards essentially generating AI. There is a direct implication into how data centers are getting structured and as a result of that need for fiber optics, cable and connectivity within the data center. So that flow is principally what we tried to share in through some of the slides. As a result of that we are looking at how do we increase our presence in this space. So that was essentially the message that we had shared and we have taken a target that 25% of revenue in the medium term should come by our sales to this sector. So, it was more something we wanted to share with our investors that strategically this is the direction we are excited about, this the direction we are leaning towards. It is not so much about you know bridging any gap it will take us some time to build a portfolio, get the technology get the IP and definitely we will update you probably quarter on quarter as we are progressing on that.

Sohan Joshi: Okay, thanks that is it from my side. All the best for the future quarters.

Chetan Wani: Thanks. We will take next question from Ketan Athavale. Please go ahead.

Ketan Athavale: Sir I wanted to know our margins which have been impacted since last few quarters, what are the factors contributing to that besides slowness in optical business? So that is the first question.

Tushar Shroff: So, if you see last three quarters our margins have been impacted mainly on ONB business, because of low capacity utilization that we have seen. Presently, since we have not been able to utilize all our facilities to the optimum level, which is impacting because of the higher fixed costs operating costs that we have not been able to leverage on, in terms of the fixed costs that we have. So that is impacting the overall the margin profile of ONB business.

Ketan Athavale: Okay, so by when can we see previous levels of margin and how do we expect the other expense to trend going forward?

Tushar Shroff: So, we expect US to pick up in next 1-2 quarters, that is what because the inventory levels are going down and as we see that US starts picking up, there are two advantages to it. One is that we will be able to utilize our US facility to the full extent, as well as for some of the non-BEAD requirements, we will be able to utilize our India facility. So, it has the two benefits one is fully utilizing the US facility as well as the India facility. So, which will help us in terms of taking a better utilization and which will improve the margin profile. However, in terms of the overall cost structure, as I have mentioned, in earlier question, that we are targeting to reduce it by at least to the extent of 4-5% on sustainable basis. That is over a period of time and that is what we will be looking at.

Ketan Athavale: Okay. And coming to BharatNet, so if my understanding is correct about 6000 maybe optical, 12,000 maybe EPC and the rest about 40,000 will be network equipment. So will we participate in that as well, can you clarify?

Ankit Agarwal: Just to clarify, as I said earlier, we have had extensive experience on phase I and phase II. Government is still issuing various clarifications on the terms of the tender, various conditions, various milestones, etc. So we continue evaluating in terms of making sure that the terms are something that make business sense for STL. So, from that perspective, it's too early for me to comment on what all will be our scope and what size will be. But clearly, as I said before, we will be focused both from the services business as well as from the optical business to make sure that we are a key participant in the project.

Ketan Athavale: Okay, and just last question. So in the balance sheet, you have an unallocated liability of a discontinued operations, so can you clarify what is it exactly.

Tushar Shroff: So these include bank borrowing of ~2360 Cr other trade and statutory liabilities and discontinued business related liabilities of approx. 15 crs. These are basically specific liabilities which are related to some of the discontinued business that we have, mainly on account of those contractual liabilities which is not due or disputed for some of the discontinued business that we have. So, over the last couple of years, we have discontinued some of the businesses where due to certain issues with the vendors we have not been able to close on those liabilities and since those are a disputed liability, which we have accrued in the financials, but still not been settled at this point in time.

Ketan Athavale: Okay. So by when can we expect it to go off balance sheet. These are contractual liabilities, right.

Tushar Shroff: These are some of the contractual liabilities but disputed for the service rendered by the some of the vendors that we have.

Ketan Athavale: By when can we expect them to go off balance sheet can you comment on that?

Tushar Shroff: It will depend on what kind of a settlement that we agree with our partner. So, if we are able to come to amicable settlement, then probably the liability may reduce or we will have settlement over a period time, but when we will be able to make the settlement with some of the partners that we have, that is an important aspect.

Ketan Athavale: Okay, got it. Thank you so much.

Chetan Wani: We will take the next question from Rohan Patel. Please go ahead

Rohan Patel: I just wanted to ask our margins have collapsed since the peak be achieved in 2018 and 2019, which was around 23% and 22% and which has fallen down to 8%. So, there is a drastic change. So, I am just new to this company, so can you explain what has happened?

Ankit Agarwal: Look, one probably if you are looking at the data from back then that would be a consolidation of optical business and largely the services business, which will be as one data point, and that will be a mix of profitability of probably at that time, some mix of optical business as well as some high margin services projects that we were executing at that time. Nevertheless, one time to if you also reflect as recent as couple of years ago, we had a very healthy optical business. We did north of Rs.5,000 crores plus and we had 20% EBITDA margin, which we demonstrated. This was essentially when we had a healthy factory utilization, which was for us typically north of 75-80%. And at that utilization, we are very comfortable to have industry leading margins at close to 20% plus. So, that is a little bit of history in brief. We are happy to have a separate conversation. Currently, our factory utilizations are lower, they are sub 50% and as the volumes pick up, especially in Europe and US and maybe to some extent more in India we are confident that structurally, this is a business that we can operate at 20% EBITDA margins.

Chetan Wani: Thank you, Rohan. We will take the next question from Saket.

Saket: Sir I joined a bit late sorry, if my questions are repetitive. Firstly for the interconnect part of the story. What have been our achievement for the last financial year and what are we looking forward for this year in terms of revenue and how is the market growing as per our expectation? If you could give some color on this?

Ankit Agarwal: Yes, sure. So, we did share some guidance. Of course, the number we have shared is 23% is the attach rate which is our highest ever so we are obviously quite excited about this, we are proud about it. At the same time, principally, this is a product that we believe creates value for customer as cable and connectivity together, it enables a lower cost per home pass, it enables faster deployment, lower requirement of trained manpower, so it has multiple benefits. One part to also remember particularly about the interconnect business, is that there is much more opportunity as more and more operators connect fiber to the home. When they go from home pass towards home connect that especially when there is specific more opportunity. In addition, what we also see is that as we start building our product portfolio, and also including building a product portfolio for the data center space, this is also an area of future growth for STL. So overall, I think it's something where we continue to invest, we continue to build a portfolio, we have had some good success in Europe and UK recently. We want to continue to grow both in Europe as well as US and we are also exploring other markets as well, to scale this up. And we are definitely looking at how do we provide a great solution for our customers. We provide a unique solution and we also building a lot of our own IP so that we can continue to scale this up in the future.

Saket: So just to brief it down what should be the revenue profile from this by that we can specifically give a broad number for the year.

Ankit Agarwal: We won't be able to give a guidance Saket for confidentiality reasons but I can at least share with you that we are confident that this is a business that should grow versus last year. We will not be able to give a guidance to a specific attach rate for the year. But definitely we are working very hard to ensure that we have a good attach rate and at the same time of course we also want to grow our cable business.

Saket: When we look at your numbers on Q-o-Q basis at least the EBITDA part of the story looks a bit encouraging, but again coming down the line to the finance cost part that also has been lowered for this quarter. So taking into account how the first quarter has been, where are we in terms of turning the tables and reporting better numbers, where are we in midst of that and what are the factors that are still pending as impediments for us back to our growth journey.

Ankit Agarwal: So, Saket what we have been sharing as a guidance and strategy that principally remains the same. We have been very clear in terms of our focus markets, Europe, US, India that remains the same. We do see some pretty interesting opportunities like the BEAD project in US, the BharatNet project in India, which can be additional tailwinds to the market. At the same time, we have been very focused on what is in our hands and in terms of our own cost efforts, that is something that Tushar spoke about. We have been driving in a very focused way last 12 months, we will continue to drive it to make sure that we are really at a very cutting edge in terms of cost competitiveness. And we will be looking very closely at every line item to make sure that we are cost competitive. So

I think as those efforts also continue to yield results, on the cost side as our factory utilization improves, and it goes back to 75-80% levels, probably in the next coming quarters, that is when you will really see that positive development. As we just shared on the previous question when we run at those kinds of utilization levels, we are confident of achieving the 20% EBITDA which we have demonstrated is as recent as a 1.5-2 years ago, so that is directionally what I can share now. We are confident that the market is moving in a better direction. We believe that our efforts on the costs will start yielding and will continue to yield results and really essentially as the volumes pick up of cable, as our connectivity attach rate continues to be maintained, we definitely feel positive about the future.

Saket: Thank you.

Chetan Wani: We will take the last question from Krunal. Please go ahead.

Krunal: Good evening. So, my question is on STL digital. We saw decline in revenue quarter on quarter. So just wanted to understand the reasons for the same and there is a change in top management in STL digital, so how does that affect our organization in that sense. So, if you can throw some light on that.

Ankit Agarwal: I will take the second question. Structurally, we have always driven the business as very focused business units. So, we have the optical business unit, we have our system integration business, and then we have STL digital business. So, we are very clear in terms of our three business units and we have very clear leadership and we drive it as P&L and also we do segmental reporting. So, we always structure with very strong leadership, very strong second line succession planning, all of that is how we drive our businesses. So equally when we had the exit of previous CEO for the digital business, very happy to share that Naveen Bolalingappa have stepped up. He is now taking over as the CEO for this business, and he has more than 20 plus years of experience in TCS and various other organizations. He has worked very closely with Raman and he really understands how we are going to drive this profitable growth going forward. So principally as a business, STL is very excited about the business. We have a strong leader in Naveen and we are very excited that through him we were able to deliver this profitable growth that we have committed.

Krunal: Got it. So just the EBITDA breakeven that we were targeting by year end. Does that still stay on?

Ankit Agarwal: Yes, for the digital business, yes that is directionally that we have also spoken about and now with Naveen coming on leadership, that's what he's driving as well.

Krunal: Got it. And the reason for the quarter and quarter decline in revenue there.

Tushar Shroff: So, the quarter on quarter is the impact of what we have seen in the industry as such, because last couple of quarters, industry is going through the volatile cycle and it has also impacted us. In terms of new orderbook which is going to impact us in terms of revenue, but we are confident that we should be able to revive our order book for the coming quarters and that should help us in terms of sustaining digital growth in this particular year.

Krunal: So what will be our order book now, you have shared the number last time also. So, can you share the number this time.

Tushar Shroff: It has been provided as a part of the presentation, so there has been little bit change in terms of the orderbook number that you may see as compared to the previous presentation. It's mainly impacted because of the way the revenue recognition happens in the IT sector which is gross to net and due to gross to net impact, we had to de scoop some of the order backlog. And that is one of the impact that you have seen in this particular quarter financials.

Krunal: Just one last clarification we had initiated a lot of cost cutting initiatives in the beginning of the last year. So has that impact been fully factored in in the quarterly costs or is there some more impact left.

Tushar Shroff: So we are continuously working on cost optimization, as I mentioned that we are looking at and if you see June 2023 numbers vis-a-vis June 2024 numbers that has been sustained reduction in terms of employee cost as well as in terms of other expenses. So, we continue to drive the cost optimization effort and as Ankit mentioned that is one of the levers that we are trying to see that how we can be a cost leader and in manufacturing our products. So from that perspective, this is a continuous journey for us in terms of optimizing the overall cost.

Krunal: Got it, great. Thank you so much.

Chetan Wani: Thanks Krunal. With this we come the end of the question and answer session and now I hand over the call back to Ankit for closing remarks.

Ankit Agarwal: I'd like to thank everyone for attending today's call and for showing interest in our company and all your questions. Despite the challenging market environment we have managed to make progress on our key strategic priorities and happy to share that we have also reduced our net debt by Rs.769 crores. Through our focus on customer centricity and cost leadership we have gained traction and order across the optical business, by delivering purpose engineering solution to our customer we have achieved highest ever connectivity attach rate of 23% as I mentioned earlier. We have identified AI data center as a future growth area and we are gearing up to make substantial impact in the emerging and exciting AI driven data centre segment. We continue to focus on all factors in our control including become lean and agile organization which Tushar just spoke about and driving technology leadership. We will continue to aggressively pursue business opportunity presented to us in our focus regions. Based on the strength of our hi-tech manufacturing, our innovation, our industry leading products and our amazing talent that we have. Lastly, we believe that we are well positioned to execute and deliver robust results and create shareholder value as demand normalizes. I hope we were able to address and clarify all your queries and comments. For any future questions and discussion do feel free to contact Investor Relations team which include myself and Tushar. We really look forward to continuing the conversation with you in the near future. Thank you. Jai Hind

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(This document has been edited to improve readability)