Tanla Solutions Limited

February 21, 2020

Ratings

Facilities	Amount (Rs. crore)	Ratings[1]	Rating Action
Long-term Bank Facilities	50.00 (enhanced from 0.10)	**CARE A; Stable (Single A; Outlook: Stable)**	**Removed from Credit watch with developing implications; Rating revised from CARE A- (Single A Minus)**
Short –term Bank Facilities	0.25 (reduced from 79.90)	**CARE A1 (A One)**	**Removed from Credit watch with developing implications; Rating revised from CARE A2+ (A Two Plus)**
Total	**50.25 (Rupee fifty Crore and twenty five lakh only)**		

The ratings have been removed from credit watch with developing implications upon completion of the proposed acquisitions

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The revision in the ratings assigned to the bank facilities of Tanla Solutions Limited (Tanla) is backed by improved financial performance during FY19 (refers to the period April 01 to March 31), strong capital structure with robust debt coverage indicators and strong liquidity position. The revision also takes into account synergies and benefits derived from recent acquisitions and increase in income and accruals during 9MFY20.

The ratings also factors in strength from experienced promoters & management team, long track record of the operation, established market position in Application to Person (A2P) messaging segment with tie-up in place for providing service for majority of telecom players operating in India and minimal threat from alternative communication platforms like OTT players (Over-the-Top).

The ratings are, however, constrained by concentrated revenue profile and high technological obsolescence risk. The ratings also factor in net losses reported during 9MFY20.

Key Rating Sensitivities

Positive Factors:

- Deriving benefits from the recent acquisitions
- Increase in the EBIDTA margins beyond 15%

Negative Factors:

- Increase in the overall gearing of the company over and above 0.50x

Detailed description of the key rating drivers

Key Rating Strengths

Improved financial performance during FY19

During FY19, the revenue of TSL (Consol.) grew by 27.78%, y-o-y over FY18 and it registered total operating income of Rs.1013.61 crore at the back of increase in volume of A2P messaging services from existing customers on domestic hub and addition of marquee clients on International Long Distance (ILD) hub. A2P messaging is used as a common way of communication with subscribers/customers by Government bodies, Banking and Financial Institutions (BFSI), online retail merchants and business houses in India during last couple of years. The increasing demand for real-time information from the consumers led the businesses to adopt this technology to gain confidence of the customers that resulted in increase in volume of message traffic during the year.

The cost of services as a percentage of gross sales reduced in FY19 leading to improvement in the PBILDT margin by 238 bps to 10.85% in FY19 from 8.47% in FY18. In line with improvement in the PBILDT margin, PAT margin of the company also improved from 2.41% in FY18 to 2.94% in FY19.

[1] *Complete definition of the ratings assigned are available at www.careratings.com and other CARE publications.*

On standalone basis, the company reported total operating income of Rs.818.50 crore in FY19 (FY18: Rs.693.46 crore) with PBILDT of Rs.93.71 crore (FY18: Rs.54.06 crore) and PAT of Rs. 17.08 crore (FY18: Rs. 13.09 crore).

Increase in income and accruals during 9MFY20 albeit net losses

During 9MFY20 (Published), the company reported total operating income of Rs.1429.43 crore (9MFY19: Rs.692.79 crore) with PBILDT of Rs.133.41 crore (9MFY19: Rs.75.20 crore). During 9MFY20, the company has provided for accelerated depreciation. As per the Telecom Commercial Communications Customer Preference Regulations (TCCCPR), 2018, voice and text communications should be provided using block chain technology. New technology and cloudification of services has resulted in a need for re-assessment of useful life of technology assets leading to additional provision of accelerated depreciation amounting to Rs. 219.55 crore in 9MFY20 which resulted in net loss of Rs. 122.04 crore during 9MFY20. However, company reported cash profits of Rs. 128.91 crore in 9MFY20 as against Rs. 75.77 crore in 9MFY19.
On standalone basis, during 9MFY20; company reported a TOI of Rs. 827.65 crore with a PBILDT of Rs. 96.97 crore and PAT of Rs. (141.04 crore).

Synergy from acquisition of Karix, Unicel and Gamooga

<u>Karix Mobile Private Limited (Karix)</u>

TSL has completed its acquisition process of Karix Mobile Private Limited and it's wholly owned subsidiary Unicel from GSO Capital Partners, a Blackstone Company. Karix is a leading business cloud communications provider with reach to over 1,500 enterprise clients in various industries across the country. With this transaction, the combined company envisages to be one of India's leading enterprise cloud communications providers with marquee customers in banking, insurance, automotive, DTH, retail, consumer products, e-commerce, m-commerce, and the government.

<u>Gamooga Softtech Private Limited (Gamooga):</u>

Gamooga is a big data and AI driven omni-channel marketing automation platform which enables businesses personally engage with their users across channels including email, SMS, voice, website, apps and other leading channels. Gamooga is a Marketing Automation Service Provider for B2C companies. It is expected to help TSL in developing tools for market research based on AI and various analysis.

Experienced promoters and professional management with long track record of operations

TSL has been promoted by Mr. Uday Kumar Reddy, the Chairman & Managing Director of the company. He is a management graduate with more than two decades of experience in Information Technology and Telecom Sector. He enabled the company transition from a products-based solution provider to one of the largest publicly traded Mobile Value Added Services (VAS) software companies, specializing in wireless data services for mobile messaging and billing. The company is also supported by other directors and experienced management team. The company has recently on-boarded 4 Independent Directors and 1 non-executive director.

Established market position in Application to Person (A2P) messaging segment with tie-up in place for providing service for majority of telecom players operating in India

TSL operates in majorly two segments; Mobile VAS (Value Added Services) (which consists of messaging, e-commerce and e-payments) & Software and Property Development. Over the years, the company has established itself with major telecom operators and content aggregators. As a part of cloud offering, TSL continues to provide A2P messaging services while Voice has been added during FY17.
TSL signed up contract with Airtel and Idea during FY17 for their 'Fastrack' platform where Tanla has SMSC connectivity to route messages. TSL has already contracts in place with BSNL for their 'Fastrack' platform and is in negotiation for deploying the platform with other Telcos like MTNL. Tanla launched Trubloq, World's first block chain enabled commercial communications stack that empowers individual mobile subscribers to truly own, control and manage commercial communications on Feb 26, 2019 at Mobile World Congress (MWC), Barcelona to comply with the new TRAI regulation (TCCCPR 2018). Trubloq will also enable businesses to build trusted relationships with their consumers. Tanla has tied up with 6 telecom operators viz., Airtel, Vodafone Idea, BSNL, Videocon, MTNL & TATA to launch Trubloq. TSL would be the first company to comply with the TRAI regulations and adopt the block chain technology with the launch of Turbloq.

Strong net worth and capital structure with robust debt coverage indicators
The financial position of the company is strong backed by networth of Rs. 725.54 crore as on March 31, 2019 and Rs. 758.48 crore as on September 30, 2019 respectively coupled with nominal debt. On a consolidated basis, the overall gearing of the company was 0.08x as on March 31, 2019 and 0.07x as on September 30, 2019. Low gearing and strong net worth support the financial flexibility and provide cushion in case of business downturns and adverse conditions. Debt levels of the company were low at Rs. 59.88 crore as on March 31, 2019. Strong cash accruals of Rs. 105.84 crore in FY19 (Rs. 69.19 crore in FY18) with low debt levels have resulted in strong debt coverage indicators. Total Debt to GCA stood at 0.57 times for FY19 while PBILDT interest coverage was 74.55 times for FY19.

Minimal threat from alternative communication platforms like OTT players (Over-the-Top)
The OTT (Over-the-Top) services changed the way of communication in a broader sense and people have gradually shifted from P2P (Person to Person) messaging to OTT communication which uses the internet on the smartphone of the subscriber rather than using the service provider's network, directly. Users find OTT platform based applications like WhatsApp, Facebook messenger, Skype, Hike, etc. a cheaper way of communication than using P2P messaging which directly uses the mobile network, charged at a higher tariff rate. Hence, there had been a potential threat to the revenue of the company from P2P segment. However, the A2P segment is indirectly benefitted from OTT services. The OTT services require two-factor authentication which is a current standard layer of security e.g. creating an account requires SMS verification. While OTT may have replaced P2P SMS, it is also helping A2P SMS flourish as it acts as an indirect driver of A2P growth, which has helped SMS to become a defined channel for brand/business communications. Hence, the threat is expected to be minimal in A2P SMS segment and it will be a strong channel for brand and business communications to reach consumers directly.

Stable industry outlook
According to World Bank, global economy growth is projected to soften to 2.9% in 2019, amid rising downside risks in the coming months and with the Indian IT industry being largely export driven, any adverse changes in the global macro-environment is bound to have an impact on its revenues. Increasing restrictions on H-1B visas in the US and rising cost of delivering on-site services shall impact margins in FY20.

Key Rating Weaknesses
High concentration of revenue in A2P messaging segment
VAS is the major business segment and continues to contribute about 96%-97% of the total revenue for past three years. The revenue contribution from Mobile VAS segment is around 96%-100% during FY18 – FY19.

Technological obsolescence risk
The OTT (Over-the-Top) services changed the way of communication in a broader sense and people has gradually shifted from P2P (Person to Person) messaging to OTT communication which uses the internet on the smartphone of the subscriber rather using the service providers network, directly. The A2P segment is indirectly benefitted from OTT services. Due to dynamic nature of technological innovation, the A2P business is exposed to obsolescence risk with better alternative mode of communication between enterprises and customers.

Liquidity: Strong
Liquidity is marked by strong accruals against negligible repayment obligations and liquid funds to the tune of Rs. 155.03 crore as on March 31, 2019. Its unutilized bank lines are more than adequate to meet its incremental working capital needs over the next one year. Average working capital utilization was low at around 0.5% for the 12 months ended in Nov. 2019. Further, the company had liquid funds to the tune of Rs. 202.30 crore as on Dec. 31, 2019.

Analytical approach: Consolidated
CARE has taken a consolidated view on TSL and its subsidiaries/associate/JV as all the entities have synergies in operations, exhibit cash flow fungibility, are owned and managed by common promoters. TSL along with its subsidiaries is engaged in the similar business activity with the subsidiaries set up to cater to different markets/regions.

Subsidiaries:
Tanla Mobile Asia Pacific Pte Ltd., Singapore
Tanla Corporation Pvt Ltd, India
Capitalsiri Investments Pvt Ltd., India
Karix Mobile Private Limited (From April 10, 2019)
Unicel Technologies Private Limited (From April 10, 2019)
Gamooga Softech Private Limited (From October 24, 2019)
Tanla Digital Labs Private Limited (From December 18, 2019)
Joint Venture:
TZ Mobile Private Limited., India (TSL holds 50%)
Associate:
Jengatron Gaming India Pvt Ltd., India (TSL holds 30%)

Applicable Criteria
Criteria on assigning 'outlook' and 'credit watch' to Credit Ratings
CARE's Policy on Default Recognition
Criteria for Short Term Instruments
CARE's methodology for Service Sector Companies
Financial ratios – Non-Financial Sector
Rating Methodology: Consolidation and Factoring Linkages in ratings

About the Company
Tanla Solutions Limited (TSL), incorporated on July 28th, 1995 has been promoted by Mr. Uday Kumar Reddy. TSL has its headquarters and development facilities in Hyderabad, India and serves global customer base through its 3 subsidiaries, one JV with Zed Worldwide Holdings S.L. Spain and one associate.
The company provides a range of services which includes product development and implementation in wireless communication industry, aggregator services and off-shore development services. The services can be classified into three major categories viz. Mobile Messaging [majorly into Application-to-Person (A2P)], Mobile Commerce and Mobile payments.
TSL has established relationship with major Telecom Operators in India viz. Airtel, Vodafone, IDEA, and with Original Equipment Manufacturers (OEM). TSL has deployed a solution namely "Fastrack", a messaging hub platform which performs immediate delivery of messages without relying on the system's 'Store & Forward' capacity and speed and it has a capability to handle from 20 to 2000 SMS TPS (Transaction Per Second) with advanced routing facilities. Fastrack is deployed at the core operator network across the country with leading telecom operators to deliver messages to all the mobile subscribers across all telecom operators.

Brief Financials (Rs. crore) – Consol.	FY18 (A)	FY19 (A)
Total operating income	793.23	1013.61
PBILDT	67.17	109.99
PAT	19.11	29.82
Overall gearing (times)	0.00	0.08
Interest coverage (times)	182.23	223.06

A: Audited

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History for last three years: Please refer Annexure-2

Covenants of rated instrument / facility: *Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3*

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based - LT-Cash Credit	-	-	-	50.00	CARE A; Stable
Non-fund-based - ST-Bank Guarantees	-	-	-	0.25	CARE A1

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017
1.	Fund-based - LT-Cash Credit	LT	50.00	CARE A; Stable	1)CARE A- (Under Credit watch with Developing Implications) (11-Sep-19) 2)CARE A- (Under Credit watch with Developing Implications) (02-Apr-19)	1)CARE A- (Under Credit watch with Developing Implications) (27-Aug-18)	1)CARE A-; Stable (08-Jan-18) 2)CARE A-; Stable (05-Apr-17)	-
2.	Non-fund-based - ST-Bank Guarantees	ST	0.25	CARE A1	1)CARE A2+ (Under Credit watch with Developing Implications) (11-Sep-19) 2)CARE A2+ (Under Credit watch with Developing Implications) (02-Apr-19)	1)CARE A2+ (Under Credit watch with Developing Implications) (27-Aug-18)	1)CARE A2+ (08-Jan-18) 2)CARE A2+ (05-Apr-17)	-

Annexure-3: Detailed explanation of covenants of the rated instrument / facilities - NA

Note on complexity levels of the rated instrument: *CARE has classified instruments rated by it on the basis of complexity. This classification is available at www.careratings.com. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

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About CARE Ratings:
CARE Ratings commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). CARE Ratings is proud of its rightful place in the Indian capital market built around investor confidence. CARE Ratings provides the entire spectrum of credit rating that helps the corporates to raise capital for their various requirements and assists the investors to form an informed investment decision based on the credit risk and their own risk-return expectations. Our rating and grading service offerings leverage our domain and analytical expertise backed by the methodologies congruent with the international best practices.

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