Tanla Solutions Limited

September 11, 2019

Ratings

Facilities	**Amount (Rs. crore)**	**Rating[1]**	**Rating Action**
Long-term Bank Facilities	0.10	**CARE A-; (Single A Minus) (Credit watch with developing implications)**	Continues on credit watch with developing implications
Short-term Bank Facilities	79.90	**CARE A2+ (A Two Plus) (Credit watch with developing implications)**	Continues on credit watch with developing implications
Total Facilities	**80.00 (Rupees Eighty crore only)**		

Details of instruments/facilities in Annexure-1

CARE continues to place the ratings assigned to the bank facilities of Tanla Solutions Limited (Tanla) on 'Credit watch with developing implications' consequent to announcement made on August 20, 2018 by Tanla Solutions Limited entering into a definitive agreement to acquire 100% of Karix Mobile Private Limited (Karix) and its wholly owned subsidiary Unicel Technologies Private Limited (Unicel) from GSO Capital Partners, a Blackstone Company, at an enterprise value of Rs.340 crore on a cash cum stock transaction. Further, the proposed acquisition of 100% stake of Gamooga Softtech Private Limited (Gamooga) at an enterprise value of Rs. 48.45 crore on a cash cum stock transaction and proposed scheme of Amalgamation of Karix (Wholly owned subsidiary of Tanla Corporation Private Limited) and Unicel (Step-down subsidiary) with Tanla Corporation Private Limited (Wholly owned subsidiary of TSL) subsequent to necessary approvals from NCLT upon filing the draft scheme of amalgamation shall be a key rating monitorable.

CARE is in the process of evaluating the impact of the above developments on the credit quality of Tanla Solutions Limited and would take a view on the rating when the exact implications of the above are clear.

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of Tanla Solutions Limited draws strength from the 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, strong financial position with absence of debt in the books of accounts and adequate free cash balance, growing scale of operation with increased volume of A2P business segment resulting in growth in revenue in FY18 (refers to the period from April 1 to March 31) and FY19, improved liquidity profile and capitalization of assets under development. The ratings are, however, constrained by declining trend in profitability margin since last three years with change in revenue mix, concentrated revenue profile and high technological obsolescence risk.

The ability of the company to improve its profitability while managing the expanding scale, derive benefits from capitalized intangible assets and manage the intense competition are the key rating sensitivities.

Detailed description of the key rating drivers

Experienced Promoters and 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 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.

Diversified product portfolio; albeit high revenue concentration from messaging segment

TSL operates in majorly in two segments; Mobile VAS (Value Added Services) (which consists of messaging, e-commerce and e-payments) & Software development and Property Development. VAS is the major business segment and continues to contribute about 96%-97% for past three years. As a part of cloud offering TSL continues to provide A2P messaging services while Voice has been added during FY17. The revenue contribution from Mobile VAS segment is around 96%-100% during FY18 and 9MFY18. TSL also has additional revenue source through property development. TSL under its subsidiary Tanla Corporation Private Limited (Erstwhile Mufithumb Corporation Private Limited) has huge land bank of 6.8 acres in Hyderabad.

Increase in total operating income during FY18

During FY18, the revenue of TSL grew by 36.40%, y-o-y over FY17 and it registered total operating income of Rs.793.23 crore

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

as against Rs.581.54 crore in FY17 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. During 9MFY19 (Un-audited), the company reported total operating income of Rs.692.79 crore (9MFY18: Rs.584.42 crore) with PBILDT of Rs.75.21 crore (9MFY18: Rs.50.11 crore) and PAT of Rs.20.08 crore (9MFY18: Rs.22.81 crore).

Increase in total operating income, profits and accruals during FY19 (Consol.)

During FY19, the revenue of TSL on a consolidated basis grew by 27.40%, y-o-y over FY18 and it registered total operating income of Rs.1014.58 crore as against Rs.796.37 crore in FY18 with a PBILDT of Rs. 107.33 crore and a PAT of Rs. 29.82 crore. Gross Cash Accruals also increased notably to Rs. 103.75 crore for FY19 as against Rs. 69.20 crore for FY18.

With respect to the increased revenue, of which Rs. 171 Crore (equivalent to 22%) is attributable to an increase in price per message in overseas and domestic markets and Rs. 41 Crore equivalent to 5% was achieved due to enhanced volumes. Price per message increased due to a sudden dip in supply pursuant to closure of two of the largest telcos in the domestic market.

Comfortable financial position with significant improvement in operating cycle and improved liquidity position

The financial position is strong as the company does not have any debt in the books. The liquidity position of the company further improved in FY18 and FY19 with reduction in inventory days on account of selling up of all unsold plots during the year. TSL provides 2-3 months of credit period to their customers along with timely escalations to receive payment within the credit period provided. The operating cycle improved significantly and was comfortable at 2 days vis-à-vis 6 days during FY17. The working capital requirement is primarily funded through the cash flows from operations, hence the company has negligible bank borrowings. Also, the closing cash balance as on March 31, 2018 remained at Rs.160.20 crore as against Rs.123.52 crore as on March 31, 2017. Closing cash balance stood comfortable at Rs. 151.76 crore as on March 31, 2019 on a consolidated basis (excl. margin money deposits).

Synergy from acquisition of Karix Mobile Private Limited

Tanla has entered into a definitive agreement to acquire 100% of Karix Mobile Private Limited (Karix) and its 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 will 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. The share purchase agreement between Tanla and Banyan Investments Ltd, Mauritius, (a GSO Company) for acquisition of Karix Mobile Pvt Ltd, by Tanla, was executed on August 20th, 2018. However, the closure of this acquisition is pending due to regulatory approvals.

Synergy from acquisition of Gamooga Softtech Private Limited

Tanla will be entering into a share purchase agreement to acquire 100% of Gamooga Softtech Private Limited (Gamooga-leading BIG DATA, AI driven customer data and marketing automation platform). Gamooga is a Marketing Automation Service Provider for B2C companies. Gamooga Operates from Hyderabad and serves about 40+ enterprise clients and reported an annual revenue of Rs. 5.70 crore as per the financials as on March 31, 2018. The acquisition of Karix and Gamooga is expected to position TSL as an end to end solution provider for global enterprises incl. its existing clients to solve every imaginary use case and problem of customer experience.

This apart, TSL have approved the draft scheme of Amalgamation of Karix Mobile Private Limited(Wholly Owned Subsidiary of TCPL post share transfer) and Unicel Technologies Private Limited (Step-down subsidiary)with Tanla Corporation Private Limited (Wholly owned subsidiary of TSL) to be filed at the National Company Law Tribunal, Hyderabad bench, for necessary approvals.

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.

High concentration of revenue in A2P messaging segment
TSL operates in majorly in two segments; Mobile VAS (Value Added Services) (which consists of messaging, e-commerce and e-payments) & Software development and Property Development. VAS is the major business segment and continues to contribute about 96%-100% for past three years. As a part of cloud offering TSL continues to provide A2P messaging services while Voice has been added during FY18 and 9MFY19. TSL remains exposed to revenue concentration risk.

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.

Declining trend in profitability margins
The A2P business being lower margin segment, the cost of service which majorly comprises individual cost paid to mobile carriers for providing connectivity and content providers for providing content has increased in FY18 coupled with exit from certain segments of the mobile payments vertical resulted in shrinkage of PBILDT margin by 162 bps to 8.47% in FY18 from 10.09% in FY17. However, PAT level deteriorated significantly by 463 bps from 7.04% in FY17 to 2.41% in FY18 due to significant decline in depreciation during FY17 primarily on account of reassessment of useful life of the assets thereby resulting in a saving in depreciation.

Analytical approach: Consolidated
TSL, the Holding company, operates through 3 subsidiaries,) one JV with Zed Worldwide Holdings S.L. Spain and one associate. TSL along with its subsidiaries, JVs and associates are engaged in the similar business activity and enjoy both financial and operational linkages.
Entities being consolidated are:
Tanla Solutions Limited India (Holding Company)
Tanla Mobile Asia Pacific Pte Limited (Singapore Wholly-owned subsidiary)
Tanla Corporation Private Limited (India: Wholly-owned subsidiary)
Capitalsiri Investments Private Limited (India: Wholly-owned subsidiary)
TZ Mobile Private Limited (India: Joint Venture with ZED Worldwide Holdings S.L. Spain)
Jengatron Gaming Private Limited (India: Associate)

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
CARE's Methodology for Factoring of Linkages in Ratings

About the Company
Tanla Solutions Ltd (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 subsidiaries located in Dubai and Singapore. The company provides a range of services which includes product development and implementation in the 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. Apart from telecom operations, TSL is also engaged in property development through its subsidiary Tanla Corporation Private Limited (Erstwhile Mufithumb Pvt Ltd) which has a land bank of 6.8 acres in Vattinagulapally, near financial district of Hyderabad.

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

Consolidated:

Brief Financials (Rs. crore)	FY18 (A)	FY19 (A)
Total operating income	793.23	1014.58
PBILDT	67.17	107.33
PAT	19.11	29.82
Overall gearing (times)	0.00	0.08
Interest coverage (times)	182.23	335.40

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable.

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

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-Bank Overdraft	-	-	-	0.10	CARE A- (Under Credit watch with Developing Implications)
Non-fund-based - ST-Bank Guarantees	-	-	-	79.90	CARE A2+ (Under Credit watch with Developing Implications)

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 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016
1.	Fund-based - LT-Bank Overdraft	LT	0.10	CARE A- (Under Credit watch with Developing Implications)	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)	-	1)CARE A- (29-Jul-15)
2.	Non-fund-based - ST-Bank Guarantees	ST	79.90	CARE A2+ (Under Credit watch with Developing Implications)	1)CARE A2+ (Under Credit watch with Developing Implications) (27-Aug-18)	1)CARE A2+ (08-Jan-18) 2)CARE A2+ (05-Apr-17)	-	1)CARE A2+ (29-Jul-15)

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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