

## Idea Cellular Ltd

### Solid Q3 driven by traffic growth; ARPM decline moderates

**Strong revenue growth, margins flat:** Idea Cellular (Idea) reported revenues of Rs 39.5bn, up 8% QoQ and ahead of our expectations led by strong momentum in traffic growth (up 10% QoQ). Absolute consolidated EBITDA (Rs 9.5bn in Q3FY11) was also up 8% QoQ, in line with our expectations. Sales and marketing expenses increased sharply QoQ to 13.5% of sales (11% in Q2). Despite this, the consolidated EBITDA margin was flat QoQ at 24% as volume benefits helped lower network costs and Indus' margins continued to improve (+360bps QoQ). Net income at Rs 2.4bn came in ahead of expectations, with an increase of 35% QoQ, due to lower interest costs and depreciation. Capitalisation of 3G interest costs totalled Rs 1.2bn, inline with our estimates.

**ARPM decline minimal; traffic growth rebounds sharply:** MOUs were at 401 minutes, up 2% QoQ with robust traffic growth (up 10% QoQ) driven by favourable seasonality. Pressure on ARPMs (Rs 0.42) eased, with a decline of only 1% QoQ versus drops of 3%/5.4%/9% QoQ seen in Q2FY11/ Q1FY11/Q4FY10. ARPUs increased by Re 1 (0.6% QoQ) to Rs 168, helped by a lower-than-estimated ARPM decline. New circles continue to do well with revenue at Rs 3.9bn (up 17% QoQ) and EBITDA losses largely flat QoQ at Rs 1.4bn.

**FY11 capex guidance lowered:** 2G capex picked up this quarter to Rs 9.4bn (25% of sales); however, the management trimmed its capex guidance for the year to Rs 30bn (Rs 40bn earlier). The lower guidance is due to certain savings and also some spill-over of expenditure into FY12. Net debt stood at Rs 107bn, flat QoQ, implying a TTM net debt/EBITDA of 3x; cash for the quarter totalled Rs 5.2bn. Further, management commentary suggests that the impact of MNP will be marginal and that it is unlikely to be a game-changer for the sector.

**Takeaways:** Overall, this was a good performance from Idea with robust traffic growth and a lower-than-estimated ARPM decline. Further, growth in new circles remains strong with controlled EBITDA losses, flat for four quarters now. Additionally, the improving profitability in Indus is a positive. We maintain our positive stance on the sector and on Idea given our view that competitive pressures will continue to ease and policy framework will become supportive. Further, we do not expect any disruptive pricing leading to headline tariff cuts on the back of MNP. The stock is trading at 9x/7x FY11E/FY12E EBITDA. Maintain BUY.

#### Idea operating metrics

	3QFY10	4QFY10	1QFY11	2QFY11	3QFY11
<b>Subs (mn)</b>	52.3	63.8	68.9	74.2	81.8
Net adds (mn)	5.5	11.5	5.1	5.3	7.6
<b>ARPU (Rs)</b>	200	185	182	167	168
Q/Q (%)	(4)	(7)	(2)	(8)	1
Y/Y (%)	(25)	(27)	(22)	(20)	(16)
<b>MOU (mins)</b>	389	398	415	394	401
Q/Q (%)	4	2	4	(5)	2
Y/Y (%)	(6)	(1)	4	5	3
<b>ARPM (Rs/min)</b>	0.51	0.47	0.44	0.42	0.42
Q/Q (%)	(8)	(9)	(6)	(3)	(1)
Y/Y (%)	(20)	(27)	(25)	(24)	(19)
<b>Traffic (bn mins)</b>	57.8	68.3	82.3	84.8	93.5
Q/Q (%)	15	18	21	3	10
Y/Y (%)	44	54	69	69	62

Source: Company

#### Idea: Revenue by circle

(Rs bn)	3QFY10	4QFY10	1QFY11	2QFY11	3QFY11
<b>Revenues</b>					
Est. Circles	28.2	30.3	33.8	33.5	35.9
New Circles	2.4	2.8	3.1	3.4	4.0
<b>Q/Q Growth (%)</b>					
Est. Circles	4.2	7.2	11.8	(1.0)	7.3
New Circles	30.8	15.8	10.9	10.5	17.0
<b>EBITDA</b>					
Est. Circles	8.49	9.75	9.34	9.05	9.60
New Circles	(1.29)	(1.42)	(1.40)	(1.43)	(1.38)
<b>EBITDA Margin (%)</b>					
Est. Circles	30.1	32.2	27.6	27.0	26.7
New Circles	(54.0)	(51.5)	(45.7)	(42.2)	(34.9)

Source: Company

Idea will hold its Q3FY11 conference call on Tuesday, January 25, 2011, from 2:30-3:30PM IST. Dial in details: Primary access number +91-22-3065 0126, Secondary access number +91-22-6629 0339.

#### Idea quarterly review

Rs mn, year-end March	3QFY11	RCML Expected	Diff (%)	3QFY10	% Y/Y	2QFY11	% Q/Q
Revenue	39,556	38,888	1.7	33,478	18.2	36,592	8.1
Subscribers	81,800	79,596	2.8	63,800	28.2	74,200	10.2
ARPU	168.0	168.6	(0.3)	185.0	(9.4)	167.0	0.6
EBITDA	9,483	9,527	(0.5)	9,235	2.7	8,788	7.9
EBITDA margins	24%	24%	(0.5)	28%	(3.6)	24%	(0.0)
Net profit	2,431	2,184	11.3	2,666	(8.8)	1,798	35.2
EPS (LC)	0.74	0.66	11.3	0.81	(8.8)	0.54	35.2

Source: Company; RCML Research

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RCML: Voted amongst Top 4 most improved brokerages by Asia Money Poll 2010

RCML Research is also available on Bloomberg FTIS <GO> and Thomson First Call





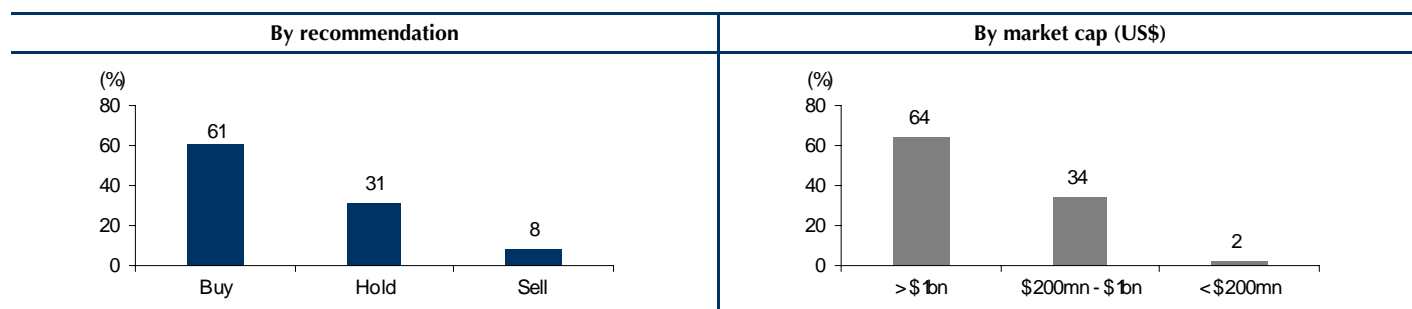
Fig 1 - Idea - Quarterly financials

Rs mn, year-end March	3QFY09	4QFY09	1QFY10	2QFY10	3QFY10	4QFY10	1QFY11	2QFY11	3QFY11
<b>Revenues (Rs Mn)</b>	<b>27,305</b>	<b>29,240</b>	<b>29,748</b>	<b>29,739</b>	<b>31,495</b>	<b>33,478</b>	<b>36,537</b>	<b>36,592</b>	<b>39,556</b>
Q/Q Growth (%)	18.8	7.1	1.7	(0.0)	5.9	6.3	9.1	0.2	8.1
Y/Y Growth (%)	59.9	48.2	36.9	29.3	15.3	14.5	22.8	23.0	25.6
<b>Interconnection &amp; access costs</b>	<b>(5,083)</b>	<b>(5,163)</b>	<b>(4,221)</b>	<b>(4,184)</b>	<b>(4,533)</b>	<b>(5,064)</b>	<b>(5,761)</b>	<b>(5,825)</b>	<b>(6,356)</b>
Q/Q Growth (%)	19.0	1.6	(18.2)	(0.9)	8.3	11.7	13.8	1.1	9.1
Y/Y Growth (%)	73.5	49.9	6.7	(2.0)	(10.8)	(1.9)	36.5	39.2	40.2
<b>License and spectrum fee</b>	<b>(2,983)</b>	<b>(3,239)</b>	<b>(3,369)</b>	<b>(3,320)</b>	<b>(3,452)</b>	<b>(3,328)</b>	<b>(4,242)</b>	<b>(4,178)</b>	<b>(4,529)</b>
Q/Q Growth (%)	16.1	8.6	4.0	(1.5)	4.0	(3.6)	27.5	(1.5)	8.4
Y/Y Growth (%)	71.8	64.8	37.7	29.1	15.7	2.7	25.9	25.8	31.2
<b>Network costs</b>	<b>(6,055)</b>	<b>(6,691)</b>	<b>(7,506)</b>	<b>(7,614)</b>	<b>(7,937)</b>	<b>(8,214)</b>	<b>(10,159)</b>	<b>(10,091)</b>	<b>(9,936)</b>
Q/Q Growth (%)	35.0	10.5	12.2	1.4	4.2	3.5	23.7	(0.7)	(1.5)
Y/Y Growth (%)	107.7	105.1	99.8	69.8	31.1	22.8	35.3	32.5	25.2
<b>Sales &amp; Marketing</b>	<b>(3,568)</b>	<b>(3,538)</b>	<b>(3,332)</b>	<b>(3,642)</b>	<b>(4,316)</b>	<b>(4,760)</b>	<b>(4,224)</b>	<b>(4,015)</b>	<b>(5,344)</b>
Q/Q Growth (%)	8.1	(0.8)	(5.8)	9.3	18.5	10.3	(11.3)	(5.0)	33.1
Y/Y Growth (%)	63.2	35.4	35.1	10.3	21.0	34.6	26.8	10.2	23.8
<b>G&amp;A</b>	<b>(1,190)</b>	<b>(1,106)</b>	<b>(1,287)</b>	<b>(1,220)</b>	<b>(1,332)</b>	<b>(1,320)</b>	<b>(1,552)</b>	<b>(1,541)</b>	<b>(1,837)</b>
Q/Q Growth (%)	16.9	(7.1)	16.3	(5.2)	9.2	(0.9)	17.6	(0.8)	19.2
Y/Y Growth (%)	73.1	21.2	38.5	19.8	11.9	19.3	20.6	26.3	37.9
<b>Employee costs</b>	<b>(1,457)</b>	<b>(1,450)</b>	<b>(1,446)</b>	<b>(1,663)</b>	<b>(1,784)</b>	<b>(1,558)</b>	<b>(1,715)</b>	<b>(2,155)</b>	<b>(2,072)</b>
Q/Q Growth (%)	10.2	(0.5)	(0.3)	15.0	7.3	(12.7)	10.1	25.7	(3.9)
Y/Y Growth (%)	52.7	57.8	41.5	25.7	22.4	7.4	18.6	29.6	16.1
<b>Total operating costs</b>	<b>(20,336)</b>	<b>(21,186)</b>	<b>(21,160)</b>	<b>(21,644)</b>	<b>(23,353)</b>	<b>(24,243)</b>	<b>(27,653)</b>	<b>(27,804)</b>	<b>(30,074)</b>
Q/Q Growth (%)	19.8	4.2	(0.1)	2.3	7.9	3.8	14.1	0.5	8.2
Y/Y Growth (%)	78.2	61.5	45.2	27.6	14.8	14.4	30.7	28.5	28.8
<b>EBITDA</b>	<b>6,969</b>	<b>8,054</b>	<b>8,588</b>	<b>8,095</b>	<b>8,141</b>	<b>9,235</b>	<b>8,884</b>	<b>8,788</b>	<b>9,483</b>
<b>EBITDA margin (%)</b>	25.5	27.5	28.9	27.2	25.9	27.6	24.3	24.0	24.0
Q/Q Growth (%)	15.7	15.6	6.6	(5.7)	0.6	13.4	(3.8)	(1.1)	7.9
Y/Y Growth (%)	22.9	21.9	20.0	34.4	16.8	14.7	3.4	8.6	16.5
<b>Profit before tax</b>	<b>2,164</b>	<b>2,740</b>	<b>3,175</b>	<b>2,558</b>	<b>2,073</b>	<b>2,947</b>	<b>2,087</b>	<b>1,940</b>	<b>2,616</b>
Q/Q Growth (%)	40.5	26.7	15.8	(19.4)	(19.0)	42.2	(29.2)	(7.0)	34.8
Y/Y Growth (%)	(17.9)	(6.5)	8.4	66.2	(4.2)	7.6	(34.3)	(24.2)	26.2
<b>Reported PAT</b>	<b>2,195</b>	<b>2,743</b>	<b>2,971</b>	<b>2,201</b>	<b>1,701</b>	<b>2,666</b>	<b>2,014</b>	<b>1,798</b>	<b>2,431</b>
Q/Q Growth (%)	52.3	25.0	8.3	(25.9)	(22.7)	56.7	(24.5)	(10.7)	35.2
Y/Y Growth (%)	(7.3)	(0.9)	12.9	52.8	(22.5)	(2.8)	(32.2)	(18.3)	42.9

Source: Company



### Coverage Profile



### Recommendation interpretation

Recommendation	Expected absolute returns (%) over 12 months
Buy	More than 15%
Hold	Between 15% and -5%
Sell	Less than -5%

Recommendation structure changed with effect from March 1, 2009

Expected absolute returns are based on share price at market close unless otherwise stated. Stock recommendations are based on absolute upside (downside) and have a 12-month horizon. Our target price represents the fair value of the stock based upon the analyst's discretion. We note that future price fluctuations could lead to a temporary mismatch between upside/downside for a stock and our recommendation.

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