



Telecom

BSE Sensex: 17,127

S&P CNX: 5,084

30 September 2009

We met Mr. Vsevolod Rozanov, President & CEO, Sistema Shyam Teleservices (SSTL) to get an update on the company's launch plans and outlook on the wireless sector from a new entrant's perspective.

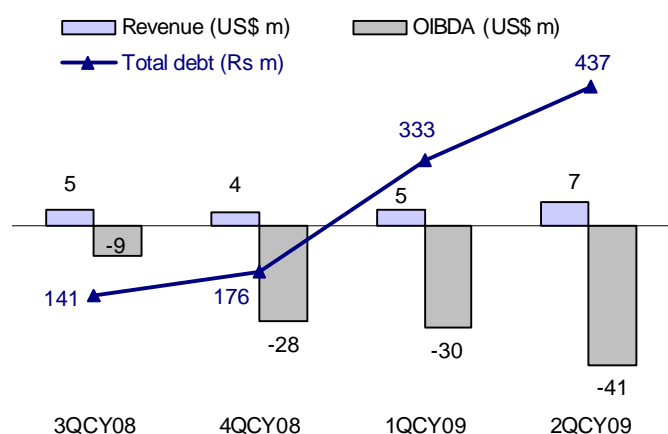
SSTL is a JV between Sistema (LSE: SSA; 73.7% stake) and Shyam Group (23.8% stake). Sistema is the largest public diversified corporation in Russia and the CIS. Sistema's telecom operation, branded MTS, is 8th largest globally (2nd in Europe) with ~100m subscribers. SSTL is a new entrant in the Indian wireless market with presence in six circles and subscriber base of 1.7m. SSTL is targeting a pan-India presence by 3QCY10.

Key takeaways:

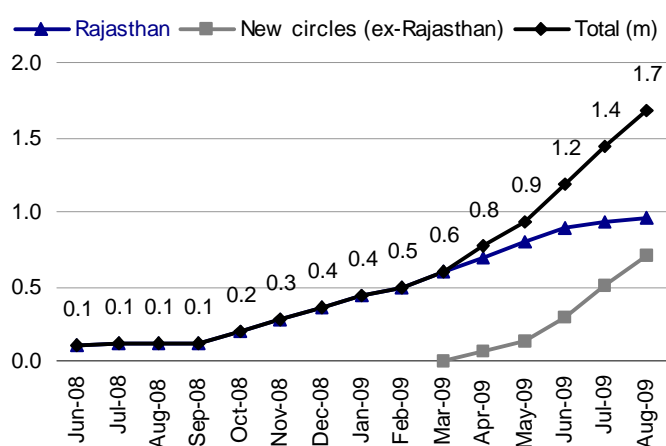
- ✦ **Bullish on growth:** SSTL believes that subscriber and market growth is sustainable given low penetration and high affordability. Significant slowdown in subscriber additions is unlikely until reported penetration reaches 60-80%.
- ✦ **Russian experience:** Mr. Rozanov cited MTS' Russian experience where wireless penetration has reached ~135%. Wireless ARPU (local currency) started to inch up once penetration reached 80-90%.
- ✦ **Majority (~80%) of new subscribers are "switches":** SSTL mentioned that ~80% of its subscriber additions are switches. It is competing largely in saturated urban market; population coverage at the launch has been ~50%.
- ✦ **EBITDA break-even in 3-3.5 years:** SSTL plans to invest ~US\$5.5b over next five years; US\$1.5b has been already invested. SSTL expects to reach EBITDA break-even in 3-3.5 years, with a subscriber base of 35-40m - assuming no significant decline in ARPU/RPM.
- ✦ **Cautious on investing:** SSTL is cautious on investing due to high competition, prospects of intra-circle roaming tie-ups, and technology advancements that can enhance capacity for less capital outlay.
- ✦ **Why CDMA:** Sistema is the only new entrant in India relying on CDMA technology. The management believes that CDMA is a superior choice for a late entrant given 1) technological superiority, 2) spectrum allocation in the 800MHz, and 3) untapped data potential.

Stable pricing critical for new entrants: We continue to believe that stable pricing remains critical for new entrants to achieve their break-even targets. However, short term disruptions are likely as new operators try to gain visibility in a highly competitive market. Maintain **Buy** on Bharti/RCom given attractive valuations and strong growth outlook.

SSTL: QUARTERLY FINANCIALS



SISTEMA SHYAM: SUBSCRIBER BASE (M)



OIBDA: Operating income before depreciation and amortization

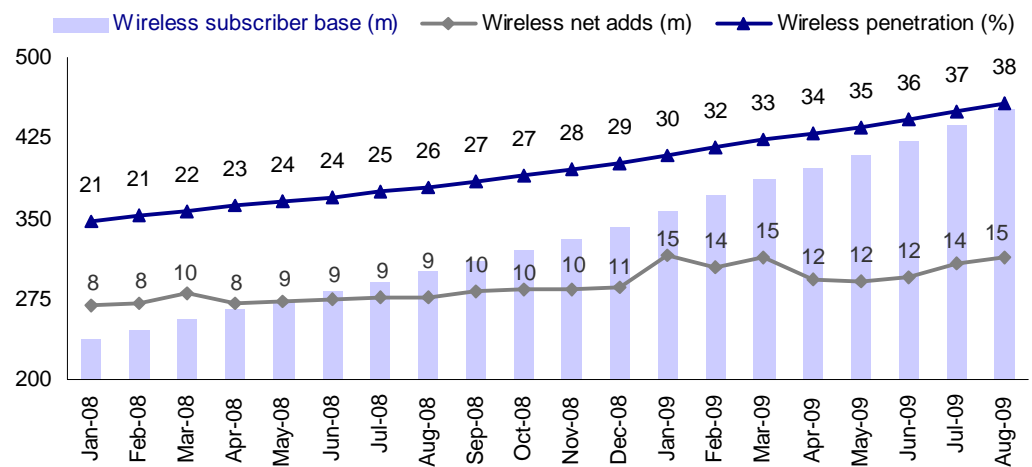
Source: DOT/MOSL

SSTL is a JV between Sistema (LSE: SSA; 73.7% stake) and Shyam Group (23.8% stake). Sistema is the largest public diversified corporation in Russia and the CIS, which manages fast growing companies operating in the consumer services sector. Sistema's telecom operation, branded as MTS, is the 8th largest globally (2nd in Europe) with ~100m subscribers. MTS (Bloomberg: MBT US, Mkt Cap: US\$19.2b, CMP: US\$48.3) had quarterly revenue of US\$2b and EBITDA of US\$0.95b during 2QCY09.

SSTL is a new entrant in the Indian wireless market with presence in six circles and subscriber base of 1.7m (0.4% subscriber share). SSTL is targeting a pan-India presence by 3QCY10. SSTL operates in India under the MTS brand name and has launched operations on a CDMA platform in Rajasthan, Tamil Nadu (including Chennai), Kolkata, West Bengal, Kerala, and Bihar. SSTL has spectrum in all 22 circles. SSTL's net monthly subscriber additions have accelerated to ~0.25m in over Jun-Aug'09, implying a net adds share of 1.5-2%.

Bullish on market growth: SSTL believes that subscriber and market growth in the Indian wireless sector is sustainable given low penetration levels, competition, and high affordability. Significant slowdown in subscriber additions is unlikely until reported penetration in India reaches 60-80%.

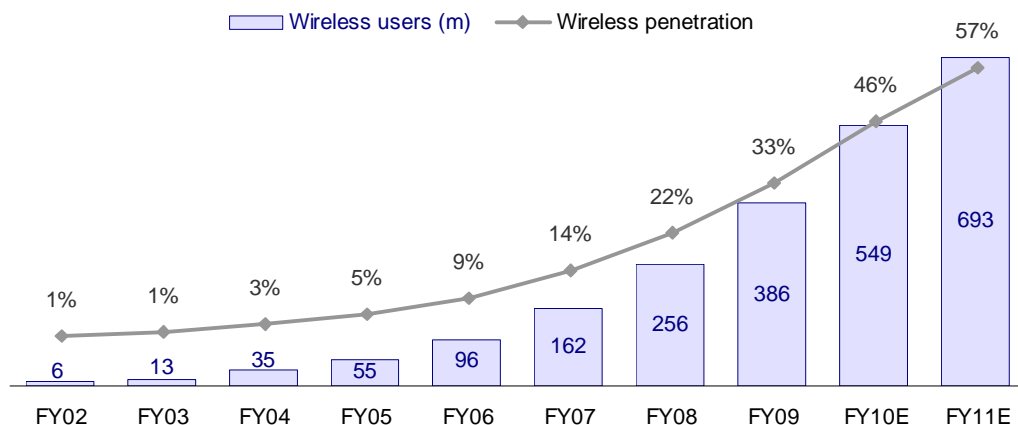
WIRELESS SUBSCRIBER BASE AND NET ADDITIONS (M)



Source: TRAI/MOSL

Reported wireless penetration overstated: SSTL management believes that wireless penetration in India (~38% on a reported basis) is overstated due to 1) rotational churn and dual SIM/handset usage which has accelerated post several new rollouts over the past one year, and 2) spectrum allocation being linked to subscribers which is a disincentive for operators to aggressively churn out dormant subscribers. Real wireless penetration in India could be 20-30% lower than reported i.e. 27-30%.

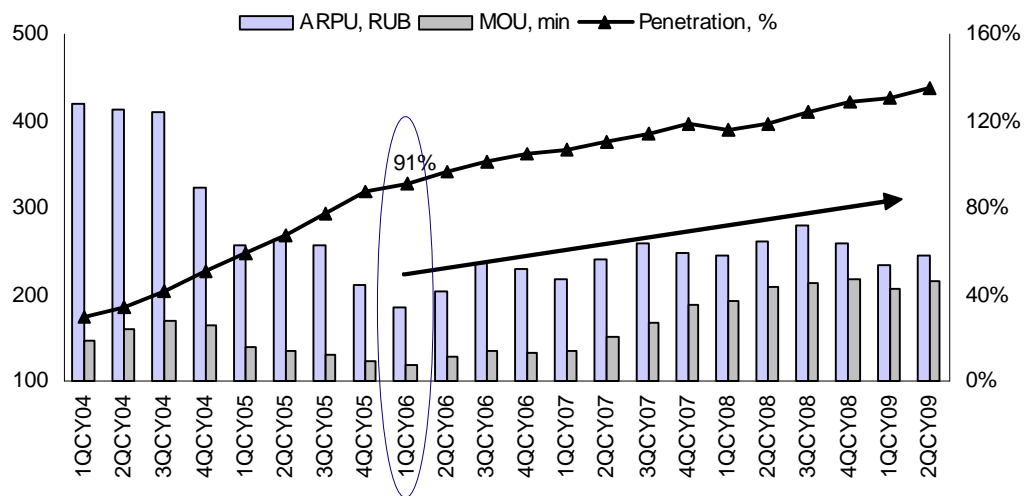
REPORTED WIRELESS PENETRATION TO REACH 57% BY FY11



Source: TRAI/MOSL

Russian experience: Mr. Rozanov cited MTS’ Russian experience where wireless penetration has reached ~135% and is still growing. Wireless ARPU (local currency) started to inch up once penetration reached 80-90%; similar trend of ARPU growth and stabilization is likely in India as well when penetration reaches 60%+.

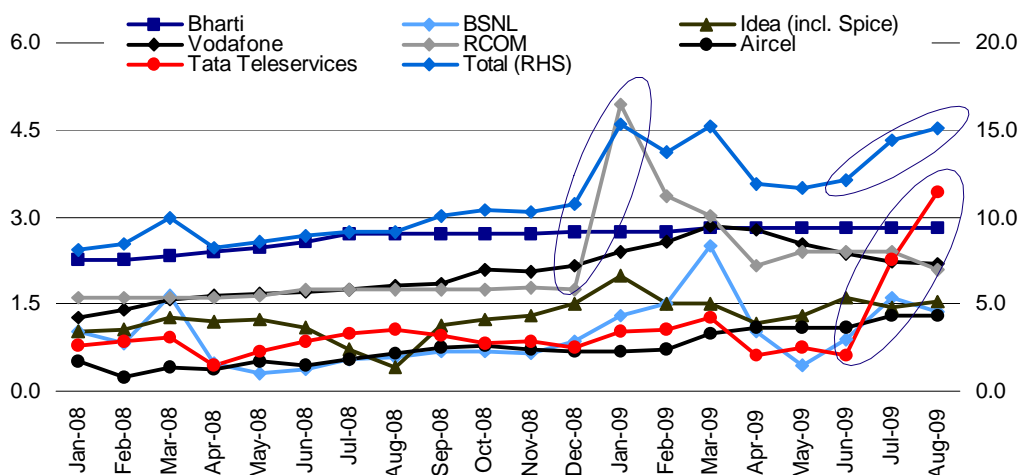
MTS RUSSIA: ARPU, MOU AND WIRELESS PENETRATION



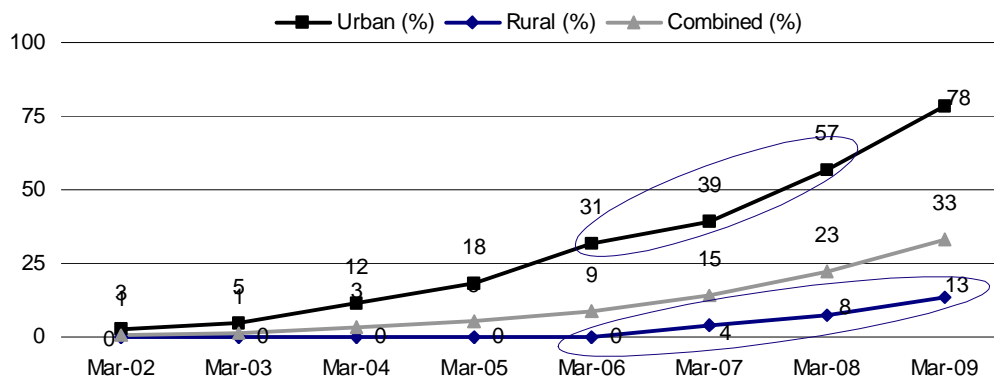
Source: MTS/MOSL

Majority (~80%) of new subscribers are “switches”: SSTL management mentioned that ~80% of its subscriber additions are switches – subscribers that are either churning out of other operators or using MTS as an additional phone. Most of the new entrants like Sistema prefer to launch in high ARPU, high penetration geographies in the initial phase, hence majority of subscribers are existing wireless subscribers of other operators. Population coverage in the circles during the launch has been ~50%, which implies that it is competing in relatively saturated urban markets.

OPERATOR WISE MONTHLY SUBSCRIBER ADDITIONS (M)



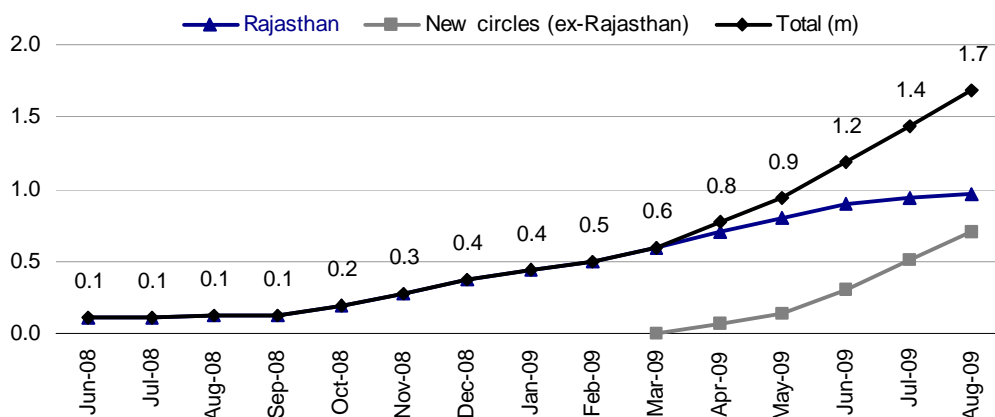
URBAN MARKET LARGELY SATURATED AT 80%+ REPORTED PENETRATION



Source: TRAI/MOSL

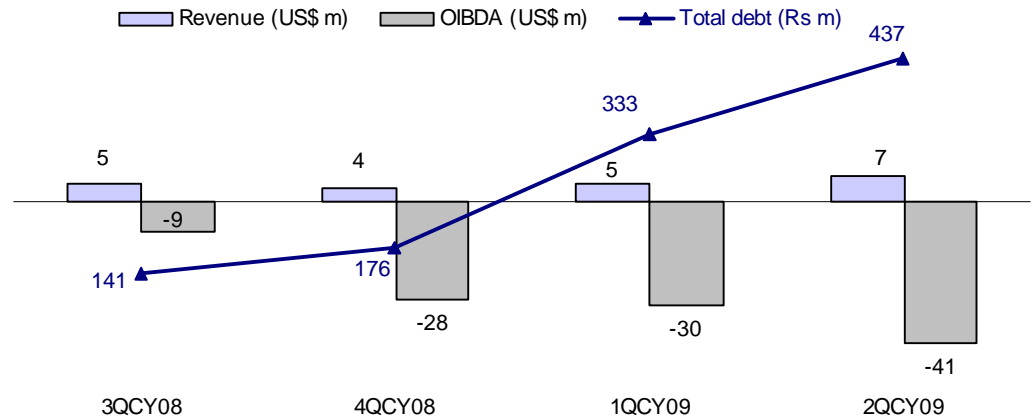
EBITDA break-even in 3-3.5 years; cautious on investing: As per its business plan, SSTL would invest US\$5.5b in India over next five years, of which US\$1.5b is already invested. At current ARPU/RPM levels, the company estimates that it will require a subscriber base of 35-40m to reach EBITDA breakeven, which is likely to take 3-3.5 years. SSTL has become relatively cautious on investing due to high competition, prospects of intra-circle roaming tie-ups, other technology advancements that can enhance capacity for less capital outlay.

SSTL: SUBSCRIBER BASE (M)

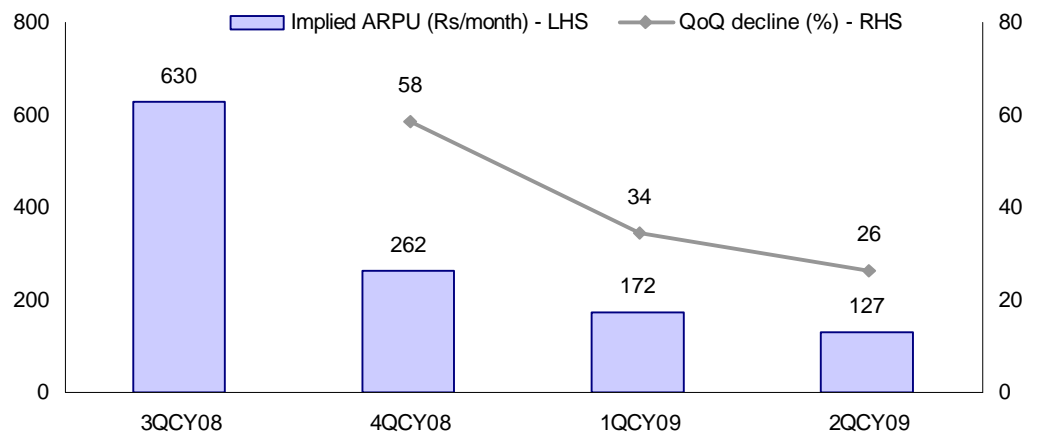


Source: TRAI/MOSL

SSTL: QUARTERLY FINANCIALS



SSTL: IMPLIED ARPU



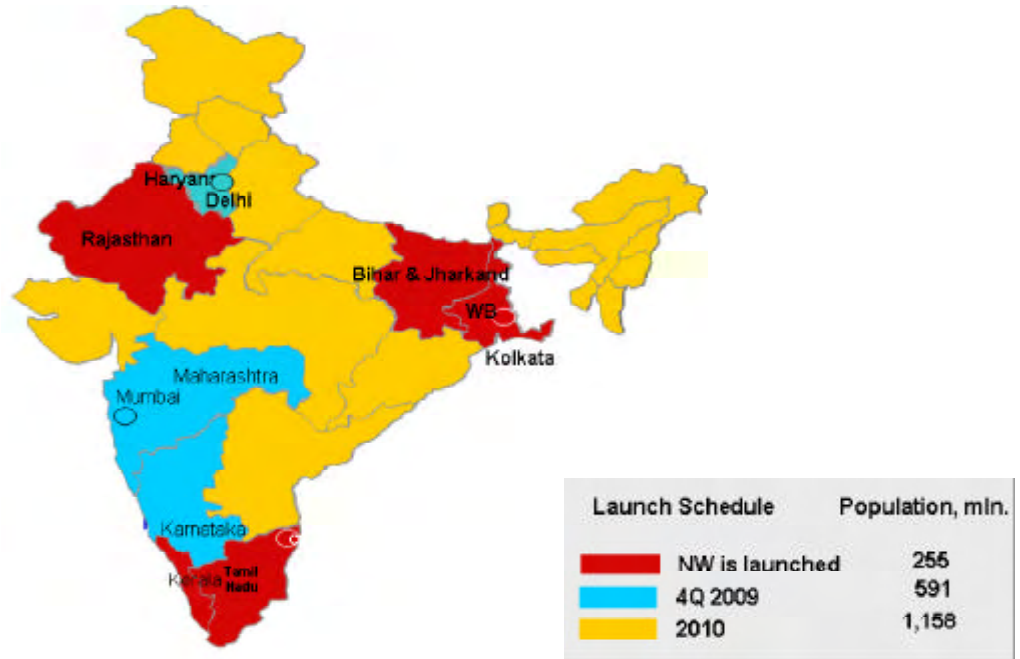
OIBOA: Operating income before depreciation and amortization

Source: Sistema/MOSL

Why CDMA: SSTL is the only company in India relying on CDMA technology while all other operators (including RCOM and Tata with huge CDMA user base) are focusing on GSM. SSTL management believes that CDMA is a superior choice for a late entrant in India given 1) technological superiority, 2) spectrum allocation in the 800MHz band vs 1800 MHz band for new GSM operators, and 3) untapped data revenue potential in the Indian market.

Pan-India presence by 3QCY10: SSTL plans to scale up to pan-India presence by 3QCY10. In the first phase, SSTL plans to set up ~18,000 BTS for pan-India coverage vs our estimate of 30,000-40,000 BTS required for a comparable coverage in GSM 1800. Huawei and ZTE are the primary vendors for active equipment while passive infrastructure is being leased (more than 90% on shared basis) by both, operator-backed and independent tower operators. SSTL has tied up with Samsung, LG & others apart from ZTE, Huawei for handset range. Other partners include IBM, Sitronics, AEGIS, Hindujas etc.

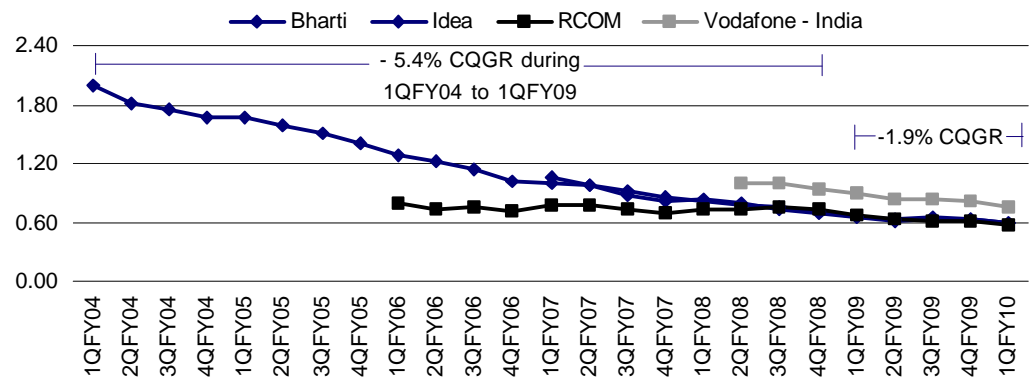
SSTL: LAUNCH PLAN



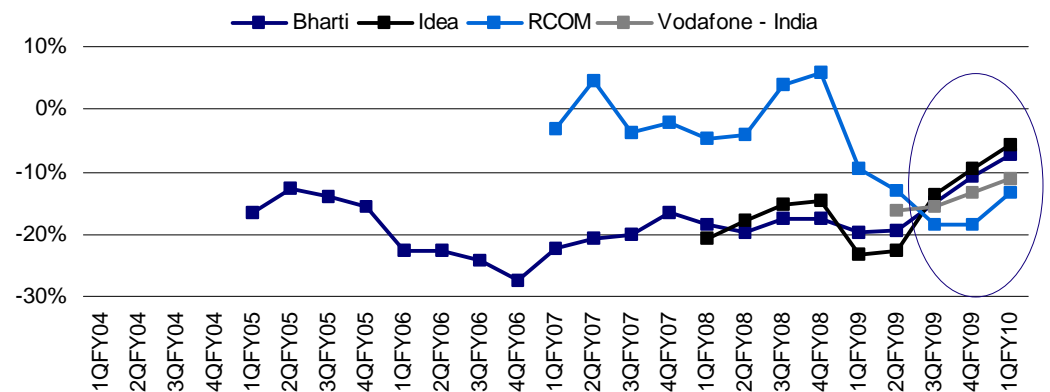
Source: Company/MOSL

Stable pricing critical for new entrants: We continue to believe that stable pricing remains critical for new entrants to achieve their break-even targets. However, short term disruptions are likely to continue as new operators try to break the clutter in a highly competitive wireless market.

TREND IN RPM OF MAJOR WIRELESS OPERATORS (-1.9% CQGR OVER PAST FOUR QUARTERS)



RPM DECLINE LOWER OVER PAST 2-3 QUARTERS DESPITE HIGHER COMPETITION (%)



Source: Company/MOSL

SSTL: Equity Structure

Sistema (LSE : SSA) – 73.71%

Shyam Group – 23.79%

Other – 2.5%

SSTL: Board of Directors

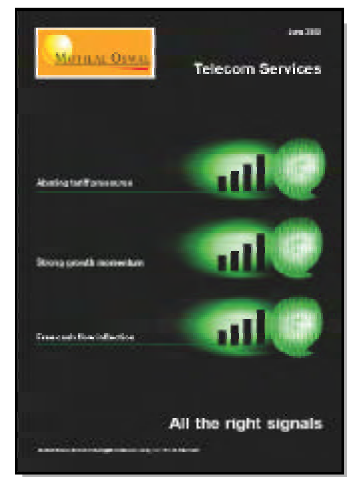
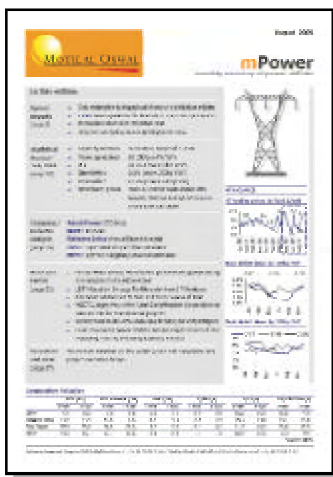
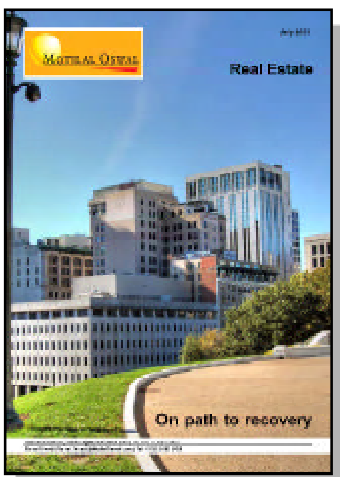
- ✍ Mr. Ron Sommer (Director & Chairman of The Board)
- ✍ Mr. Sergey Cheremin (Director & Deputy Chairman of The Board)
- ✍ Mr. Ajay Khanna (Director), MD, Shyam Group
- ✍ Mr. Alok Tandon (Director), MD, Shyam Group
- ✍ Mr. Madhukar (Independent Director)
- ✍ Mr. Mikhail Shamolin (Director), CEO, MTS Group
- ✍ Mr. Rajiv Mehrotra (Director), Chairman, Shyam Group
- ✍ Mr. Suman Sehgal (Independent Director)
- ✍ Mr. Vsevolod Rozanov (WTD), President & CEO, SSTL

SSTL: CIRCLE WISE SUBSCRIBER DETAILS

	JAN-09	FEB-09	MAR-09	APR-09	MAY-09	JUN-09	JUL-09	AUG-09
Sistema Subs (m)								
Rajasthan	0.43	0.50	0.60	0.70	0.80	0.89	0.93	0.97
Chennai	0.00	0.00	0.00	0.00	0.04	0.05	0.06	0.07
Kolkata	0.00	0.00	0.00	0.00	0.00	0.05	0.10	0.15
Tamil Nadu	0.00	0.00	0.00	0.05	0.07	0.12	0.17	0.21
Kerala	0.00	0.00	0.00	0.02	0.03	0.05	0.07	0.09
West Bengal	0.00	0.00	0.00	0.00	0.00	0.03	0.11	0.20
New circles (ex-Rajasthan)	0.00	0.00	0.00	0.07	0.14	0.30	0.51	0.71
Total (m)	0.43	0.50	0.60	0.77	0.94	1.19	1.44	1.68
Market subs (m)								
Rajasthan	20.9	21.7	22.4	23.2	24.0	24.9	25.9	26.9
Chennai	8.8	9.0	9.2	9.3	9.5	9.6	10.0	10.2
Kolkata	10.7	11.1	11.6	11.9	12.1	12.4	12.7	13.0
Tamil Nadu	24.9	26.1	27.4	28.2	29.0	30.0	31.5	32.9
Kerala	14.8	15.3	15.8	16.3	16.7	17.4	18.2	19.0
West Bengal	14.1	14.8	15.5	16.1	16.7	17.2	17.9	18.5
New circles (ex-Rajasthan)	73.3	76.3	79.5	81.8	84.0	86.6	90.2	93.5
Total (m)	94.2	98.0	101.9	105.0	108.0	111.5	116.1	120.4
Subscriber share (%)								
Rajasthan	2.1	2.3	2.7	3.0	3.3	3.6	3.6	3.6
Chennai	0.0	0.0	0.0	0.0	0.4	0.5	0.6	0.7
Kolkata	0.0	0.0	0.0	0.0	0.0	0.4	0.8	1.1
Tamil Nadu	0.0	0.0	0.0	0.2	0.2	0.4	0.5	0.6
Kerala	0.0	0.0	0.0	0.1	0.2	0.3	0.4	0.5
West Bengal	0.0	0.0	0.0	0.0	0.0	0.2	0.6	1.1
Total (%)	0.5	0.5	0.6	0.7	0.9	1.1	1.2	1.4
Sistema net adds (m)								
Rajasthan	0.07	0.06	0.10	0.10	0.10	0.09	0.04	0.03
Chennai	0.00	0.00	0.00	0.00	0.04	0.01	0.01	0.01
Kolkata	0.00	0.00	0.00	0.00	0.00	0.05	0.05	0.05
Tamil Nadu	0.00	0.00	0.00	0.05	0.01	0.05	0.05	0.04
Kerala	0.00	0.00	0.00	0.02	0.01	0.02	0.02	0.02
West Bengal	0.00	0.00	0.00	0.00	0.00	0.03	0.08	0.09
Total (m)	0.07	0.06	0.10	0.17	0.17	0.25	0.25	0.24
Market net adds (m)								
Rajasthan	1.34	0.77	0.74	0.77	0.80	0.95	0.98	0.98
Chennai	0.12	0.17	0.22	0.14	0.16	0.13	0.35	0.28
Kolkata	0.31	0.48	0.45	0.30	0.21	0.29	0.27	0.35
Tamil Nadu	0.83	1.21	1.22	0.83	0.81	0.95	1.52	1.40
Kerala	0.38	0.44	0.55	0.46	0.46	0.66	0.77	0.81
West Bengal	0.58	0.74	0.71	0.60	0.57	0.54	0.67	0.56
Total (m)	3.57	3.80	3.89	3.10	3.01	3.51	4.56	4.37
Net adds share (%)								
Rajasthan	5.1	8.3	13.6	12.9	12.3	9.8	4.4	3.4
Chennai	0.0	0.0	0.0	0.0	25.3	8.1	2.9	2.7
Kolkata	0.0	0.0	0.0	0.0	0.0	17.0	17.0	14.1
Tamil Nadu	0.0	0.0	0.0	6.6	1.7	5.6	3.1	2.7
Kerala	0.0	0.0	0.0	3.2	3.0	2.7	2.5	2.5
West Bengal	0.0	0.0	0.0	0.0	0.0	5.3	12.5	15.9
Total (%)	1.9	1.7	2.6	5.5	5.6	7.2	5.5	5.4

Source: TRAI

N O T E S



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