Idea Cellular Ltd ---Maintain OUTPERFORM

Notes from the AIC: Maintains strong focus on ROI

EPS: ◄► TP: ◄►

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- Idea's CFO, Mr. Akshaya Moondra, presented at the AIC in Hong Kong on 26 March.
- The company's investments in new circles would not focus on top-line growth or market share, but would be more limited and focussed on profitability and returns. Idea clearly indicated that it does not expect to achieve market leadership in new circles.
- RCOM's GSM service launch has had limited impact and hence the company does not see any need to respond. The reduction in termination charges is also not expected to lead to price pressures.
- The company's FY3/10 capex remains at FY3/09 levels (Rs60 bn). Management indicated that it has access to adequate funds for the capex over the next three years.
- At current valuations, we find Idea attractively valued given its healthy financial position and near-term growth prospects. We retain our OUTPERFORM rating on the stock with a target price of Rs60.

Bbg/RIC	**IDEA IN / IDEA.BO**	**Price (25 Mar 09, Rs)**	**47.30**
Rating (prev. rating)	**O (O) [V]**	**TP (Rs) (prev. TP)**	**60.00 (60.00)**
Shares outstanding (mn)	3,100.10	Est. pot. % chg. to TP	27
Daily trad vol–6m avg (mn)	10.9	52-wk range (Rs)	111.75 - 36.90
Daily trad val–6m avg (US$ mn)	17.8	Mkt cap (Rs/US$ bn)	146.6/ 2.9

Free float (%)	43.0	**Performance**	**1M**	**3M**	**12M**
Major shareholders	Aditya Birla Group -	Absolute	(1.9)	(1.7)	(50.0)
	57%	Relative	(8.6)	(0.6)	(19.2)

Year	3/07A	3/08A	3/09E	3/10E	3/11E
Revenues (Rs mn)	43,500	67,200	97,616	138,621	163,729
EBITDA (Rs mn)	14,489	22,518	26,940	36,818	43,689
Net profit (Rs mn)	4,858	10,423	8,831	11,213	15,814
EPS (Rs)	2.12	3.96	3.08	3.40	4.80
- Change from prev. EPS (%)	n.a.	n.a.	0	0	0
- Consensus EPS (Rs)	n.a.	n.a.	3.04	3.62	6.90
EPS growth (%)	126.0	86.9	(22.3)	10.5	41.0
P/E (x)	22.3	11.9	15.4	13.9	9.9
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0
EV/EBITDA (x)	11.8	9.2	7.0	5.6	4.5
P/B (x)	5.0	3.5	1.2	0.9	0.8
ROE (%)	22.3	29.4	7.5	6.1	8.2
Net debt/equity (%)	112	170	35	32	27

Note 1: Idea cellular provides GSM based mobile telephony services in India.

New circle investments to remain ROI-focussed

Management clearly indicated that it is not looking for a market leadership position in new circles. Instead, the company would focus more on key areas in the new circles where it could justify ROI. The coverage could be selective as 1800 MHz spectrum weakens its competitive position versus the early entrants with 900 MHz spectrum.

The company continues to believe that it should break even in new circles in 24-27 months. We factor in a breakeven in 36 months in our models.

Market leadership in old circles

In nine circles where Idea has 900 MHz spectrum, the company is ranked top three in subscriber market share in all, except Karnataka. It recently got Karnataka circle through the Spice acquisition and believes that it could significantly strengthen its position in this circle too. Idea also expects to improve operating efficiencies in two Spice circles which could help margins.

RCOM's GSM launch has had limited impact

Management does not think that it needs to respond to the recent free minute scheme by RCOM. First, this scheme has had limited impact among Idea's core customers. Second, management believes that it could be rolled back by RCOM.

The company also indicated that it would be cautious in using pricing as an entry strategy in new circles, as it could have a negative impact on its established circles.

Negative on new entrants

New entrants have three disadvantages: a) late entry to market, b) spectrum allocation is in less-efficient 1800MHz frequency and c) a lack of proper organisation set-up and understanding of the Indian market. While tower sharing could reduce the initial capex needs for new operators, they need to give longer-term rental commitments to the tower operators.

FY3/10 capex to remain at FY09 levels

The deferment of launch in two circles should lead to FY3/09 capex of Rs55-60 bn (earlier expectations were Rs75 bn). This capex would spill over to FY3/10. FY3/10 capex should also remain in the same range of Rs55-60 bn (excluding 3G).

FY3/09 capex has been largely on old circles of Idea. FY3/10 capex is expected primarily to be in the new circles (including seven launches) and in improving efficiency of two Spice circles.

Views on 3G

Timing on 3G remains uncertain, but management hopes that it could still be completed in FY3/10.

Management indicated that initial 3G launch could be restricted to large cities due to: a) higher number of 3G handsets amongst existing subscribers, and b) greater requirement of capacity capex. Further, initial usage of 3G could be limited to voice with data services becoming a key driver only at a later stage.

Well funded with little need to raise further debt

Idea expects to end FY3/09 with Rs50 bn in cash (Rs35 bn net of short-term debt). The company also has access to further Rs10 bn of debt facilities.

Over the next three years, the company already has commitments of further US$2 bn in debt from lenders and should be able to generate US$1.5 bn in operating cash flows while having a cash outgo of around US$0.5 bn for debt servicing and repayments.

Companies Mentioned *(Price as of 25 Mar 09)*
Idea Cellular Ltd (IDEA.BO, Rs48.75, OUTPERFORM [V], TP Rs60.00, MARKET WEIGHT)

Disclosure Appendix

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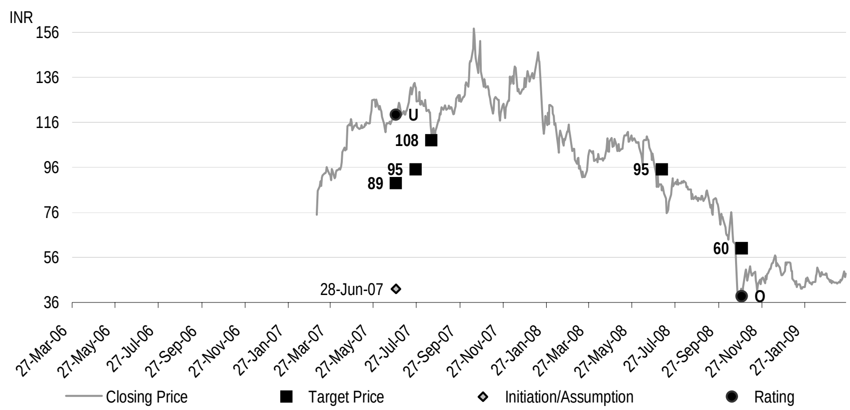
3-Year Price, Target Price and Rating Change History Chart for IDEA.BO

IDEA.BO Date	Closing Price (INR)	Target Price (INR)	Rating	Initiation/ Assumption
28-Jun-07	119.35	89	U	X
26-Jul-07	131.3	95		
17-Aug-07	110.75	108		
08-Jul-08	85.7	95		
29-Oct-08	38.75	60	O	



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Price Target: (12 months) for (IDEA.BO)

Method: Our 12-month target price of Rs60 for Idea Cellular Limited is based on discounted cash flow (DCF) analysis. We assume a weighted average cost of capital (WACC) of 12.5 and beta of 1.1. Our DCF model builds in negative cash flows for two years, followed by a period of strong cashflow growth till FY3/16, and a 2% terminal growth rate.

Risks: Risks to our 12-month target price of Rs60 for Idea are: 1) execution risk - Idea is entering new circles, where it is the sixth or seventh operator. If marketshare or margins are below our estimates or capex higher than our numbers, it could lead to a downside risk to our target price, 2) market risk - this would include the possibility of irrational competition from some players trying to gain market share, which could negatively impact margins and returns. 3) economic risk - a slowdown in the Indian economy could slow down subscriber additions. Our model assumes around 9 mn monthly net additions per month for FY09. 4) valuation risk - continuous pressure on telecom stocks or Indian market could keep the share performance weak

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