

## Company Flash

25 April 2007 | 6 pages

# IDEA Cellular (IDEA.BO)

## Buy: 4QFY07 - Wireless Growth Accentuated by Other Income

- Results in-line** — Idea Cellular's 4QFY07 EBITDA at Rs4,360m was in-line with expectations on the back of strong revenue growth and modest margin gains. Net profit at Rs1,934m was, however, significantly ahead of expectations due to high other income and lower-than-expected depreciation.
- Wireless growth on track** — Wireless revenue growth at 14.1% qoq (est.) was robust, higher than in the immediate past. EBITDA margins at 33.3% improved by 30bps qoq, after adjusting for certain flexible-pay provisions that inflated staff costs in 3QFY07. Management indicated EBITDA margins in 8-old circles at 38.7%.
- KPIs under control despite new rollouts**— ARPUs declined only 2% qoq as the new launches did not have an adverse impact, implying rational pricing. The decline in rev/min was also moderate (Rs0.87 to Rs0.82), mainly on account of roaming tariff cuts.
- Captive NLD profitability, a small surprise** — NLD revenues of Rs603m with an EBIT of Rs126 was a small surprise, but mainly on account of captive traffic being carried on leased lines. At this stage, therefore, it is more a tool to save costs rather than a full-fledged business model. Management indicated they will take a final decision on NLD business model by 1QFY08.
- Surplus cash led to high other income** — 4QFY07 other income at Rs.326.4m was higher than expected on account of treasury gains due to the surplus cash on from the IPO, and would trend down as it gets deployed in the rollout.

<b>Buy/Low Risk</b>	<b>1L</b>
Price (25 Apr 07)	Rs115.95
Target price	Rs112.00
Expected share price return	-3.4%
Expected dividend yield	0.0%
<b>Expected total return</b>	<b>-3.4%</b>
Market Cap	Rs300,642M US\$7,376M

**Figure 1. Statistical abstract**

	EBITDA	Net Profit	FD EPS	EPS Growth	P/E	EV/EBITDA	Price/CEPS
	(Rs m)	(Rs m)	(Rs)	(%)	(x)	(x)	(x)
2005P	8,210	760	0.1	na	na	na	na
2006P	10,674	2,118	0.7	na	na	na	na
2007E	14,635	4,229	1.6	119%	72.0	22.7	27.5
2008E	21,873	6,631	2.5	54%	46.7	16.0	17.7
2009E	29,762	9,379	3.6	41%	33.0	12.1	13.1

Source: Citigroup Investment Research

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Figure 2. Financial statement

Rs.m	Jun-06	Sep-06	Dec-06 (est.)	Mar-07	FY07
Service Revenue	8,939.9	10,013.0	11,463.3	13,084.2	43,664.0
<i>qoq growth (%)</i>	<i>9.4</i>	<i>12.0</i>	<i>14.5</i>	<i>14.1</i>	<i>NA</i>
Sales of Trading Goods	62.4	83.0	18.4	-	-
Total Income	9,002.2	10,096.0	11,481.6	13,084.2	43,664.0
Cost of Trading Goods	(20.0)	(28.0)	(13.4)	0	(51.7)
Personnel Expenditure	(554.0)	(600.0)	(759.0)	(684.7)	(2,597.7)
Network Operating Exp	(1,045.0)	(1,144.0)	(1,410.2)	(1,680.0)	(5,279.2)
License & WPC Charges	(909.0)	(995.0)	(1,172.1)	(1,410.9)	(4,487.0)
Access & Interconnect Charges	(1,513.0)	(1,622.0)	(1,949.6)	(2,202.5)	(7,287.1)
Subscriber Acquisition & Servicing & Advertisement & Business Promotion Exp	(1,536.0)	(1,736.0)	(1,985.5)	(2,179.2)	(7,437.7)
Administration & Other Exp	(395.0)	(432.0)	(486.5)	(564.0)	(1,887.1)
Total Opex	(5,972.0)	(6,557.0)	(7,777.2)	(8,721.3)	(29,027.5)
Impact of Restatement	4.0	(3.0)	0	0	0
Restated Total Opex	(5,976.0)	(6,554.0)	(7,777.2)	(8,721.3)	(29,027.5)
EBITDA	3,026.2	3,542.0	3,704.4	4,362.9	14,636.5
<i>Margin %</i>	<i>33.6%</i>	<i>35.1%</i>	<i>32.3%</i>	<i>33.3%</i>	<i>33.5%</i>
Depreciation & Amortisation	(1,456.4)	(1,700.0)	(1,800.5)	(1,761.3)	(6,718.2)
EBIT	1,569.9	1,842.0	1,903.9	2,601.60	7,918.30
Interest & Financing Charges	(737.1)	(774.0)	(805.4)	(974.7)	(3,291.2)
Other Income	19	11	108.9	326.4	465.3
PBT	851.8	1,079.0	1,207.4	1,953.3	5,092.4
Tax	(4.0)	(6.0)	(30.7)	(19.1)	(59.8)
PAT	847.7	1,073.0	1,176.7	1,934.2	5,032.6
<i>PAT Margin %</i>	<i>9.4</i>	<i>10.6</i>	<i>10.2</i>	<i>14.8</i>	<i>11.5</i>

Source: Citigroup Investment Research, Company reports

Figure 3. Quarterly KPIs

	Mar-06	Jun-06	Sep-06	Dec-06	Mar-07
ARPU	381	362	335	322	317
MOU	302	342	344	369	387
Revenue per min	1.26	1.06	0.98	0.87	0.82
Subscribers ('000)	7,366	8,535	10,362	12,442	14,010
Pre-paid as % of total	82%	84%	86%	88%	89%
Total MOU (mn min)	7,008	8,097	9,736	12,629	15,469
Post-paid churn %	5.5%	4.7%	4.8%	4.4%	4.2%
Pre-paid churn %	6.3%	5.3%	4.3%	3.6%	4.2%

Source: Company reports

Unexpectedly high other income and lower depreciation charges aid the bottom line

Figure 4. Operating results in-line with expectations

Rs.m	Estimates	Actual	% difference
Sales	12,800	13,084	2.2
EBITDA	4,362	4,363	0.0
PAT	1,131	1,934	71.0

Source: Citigroup Investment Research, Company reports

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## IDEA Cellular

### Company description

Idea Cellular, a pure play wireless provider, is the fifth-largest cellular operator in India. It has licenses to provide cellular-phone services in 13 of the 23-telecom circles in India and has an active presence in 11 of them. The company listed on the Indian bourses in March 2007 and is part of the Aditya Birla Group.

### Investment thesis

We rate Idea as Buy/Low Risk. Continued robust wireless market expansion and Idea's ability to regain its growth potential post its restructuring and full control by Aditya Birla Group are the key factors to our investment argument. The company's IPO provided sufficient funding flexibility to pursue its growth plans. Idea's strong competitive position and comparable operational parameters provide us sufficient comfort in management's ability to execute its plans. Given the spectrum issues facing potential new entrants, Idea should remain relatively unconstrained for the next 12-18 months. As a result, we estimate an earnings CAGR of 47.7% over FY07-09E, well ahead of its peers and more than double that of the broader market. From an industry perspective, we believe that low revenue yields and moderate EBITDA margins leave little room for disruptive pricing. Additionally, most regulatory concerns are now addressed and potentially costly 3G auctions cannot derail it from its growth path, in our view

### Valuation

We have set our 12-month target price at Rs112 based on Mar-08E DCF, which we think is an appropriate method due to the back-ended nature of free cash flows given the new circle roll-outs. Our DCF assumes a WACC of 10.8% at a target debt to capital of 50.0% and terminal growth rate of 4.0% (similar to Bharti). Our DCF is based on explicit forecasts for FY07-16E with a terminal year EBITDA margin at 37.1% (~200bps below Bharti) and capex/sales of ~10% (in line with Bharti). The target price implies an EV/EBITDA of 11.6x, a slight premium to Bharti's target multiples (for the ex-towerco portion of Rs800), which we believe is supported by (1) higher EBITDA growth rates for Idea; (2) liquidity overflow from Bharti's foreign limit constraints; and (3) M&A possibilities in the long run given Idea's good fit for the potential suitors.

### Risks

Our quantitative risk rating system assigns a default Speculative Risk rating to Idea due its trading history of less than 12 months. We believe, however, that a Low Risk rating is more appropriate due to the higher visibility of Indian wireless growth, Idea's reasonably competitive position, strong parentage and the reduction of financial leverage post-IPO. Operationally, the risks facing Idea are slightly higher than its more established peers on account of the roll out in new circles. Project cost over-runs, delays in spectrum allocation and hence commercial launches could affect the value accretion opportunity in the new circles. Idea will also face competition from the established players in the new circles and market share gains may be lower than expected. Idea will incur higher capex requirements in the new circles due to the coverage compulsions, which may depress return parameters in the initial years. Any rollout plans beyond 13 circles may also require a fresh equity infusion. These risk factors could impede the stock from reaching our target price.

## Appendix A-1

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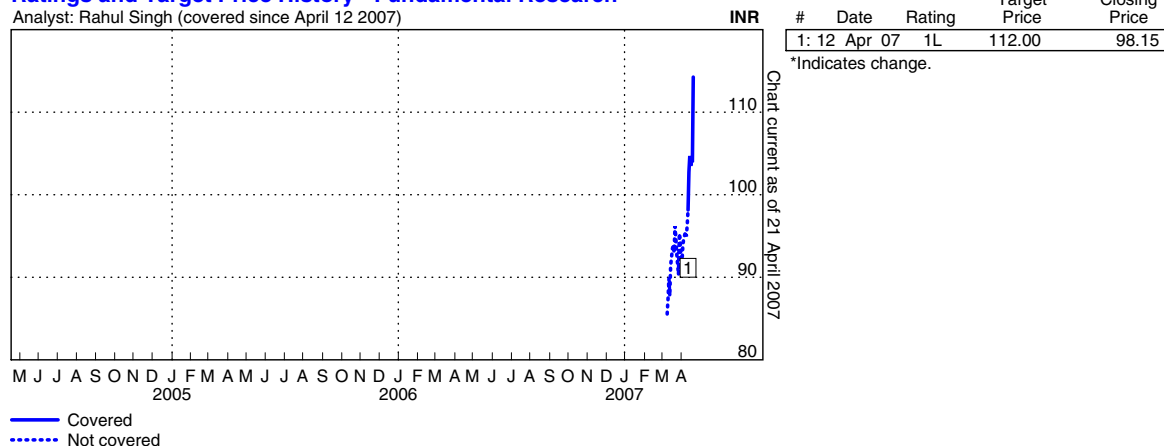
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Analyst: Rahul Singh (covered since April 12 2007)



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