

IPO NOTE

Share Data

Issue size (Upper band)	283.3 mn shares
Issue size (Lower band)	326.9 mn shares
Price band	Rs. 65-75
Issue opens	February 12, 2007
Issue closes	February 15, 2007

Pre-issue shareholding pattern (%)

Promoters	65.8
Investors & Others	34.2

Post-issue shareholding pattern (%)

(Upper band)

Promoter & Family	58.6
Public & Others	41.4

Post-issue shareholding pattern (%)

(Lower band)

Promoter & Family	57.7
Public & Others	42.3

Objects of the issue

(Rs. mn)	Gross amount	Invested till 31 Dec. 06	1 Jan. 07- Mar. 07	2007-08	To be financed through issue
Building & expanding network in new circles*	15,711	6,003	1,456	8,252	9,708
Entry fee & capex for NLD operations	833	25	-	808	808
Rollout of services in Mumbai	6,470	-	647	5,823	6,470
Redemption of preference shares	7,567	-	7,567	-	7,567
Issue expenses	825	-	825	-	825
Total	31,406	6,028	10,495	14,883	25,378

*Himachal Pradesh, Rajasthan and UP (East).

Idea

Not Rated

Price: Rs. 65-75

BSE Index: 14478

7th February 2007

About the company

Idea Cellular Ltd. is a leading telecom service provider (GSM-based mobile services) currently present in 11 circles and has a licence to operate in 2 more circles (Mumbai and Bihar). It has received NLD licence and has applied for licences to operate in the remaining circles to have a pan-India footprint. It intends to raise money through IPO mainly to fund network rollout, expansion and maintenance.

Issue details

No. of shares (mn)	at Rs. 65	at Rs. 75	No. of shares (Mn)	at Rs. 65	at Rs. 75
Equity prior to the issue	2,309.5	2,309.5	Employees	7.7	6.7
Fresh issue	326.9	283.3	Public		
Equity after the issue	2,636.5	2,592.9	QIB	191.5	166.0
IPO as % of post issue capital	12	11	Non-Institutional	31.9	27.7
Market cap. (Rs. bn)	171.4	168.5	Retail portion	95.8	83.0
Green-shoe option	49.0	42.5	Total issue	326.9	283.3

The company intends to raise Rs. 21,250 mn via the IPO with a green-shoe option to raise further Rs. 3,185 mn. The company has done a pre-IPO placement to the promoters for Rs. 3,750 mn at Rs. 75, the upper price band of the IPO.

The company intends to utilise the majority of the proceeds towards increasing coverage in the 3 new circles of Himachal Pradesh, Rajasthan and UP (E) where it started operations in past 3-4 months and rolling out network in Mumbai where it has received licence recently. 483 preference shares of Rs. 10 mn each were issued in FY02, FY03 and FY04 with a tenure of 10 years, redeemable on March 20, 2007 or August 3, 2007. The amount of Rs. 7,567 mn is calculated assuming redemption on March 28, 2007.

Means of finance (Rs. mn)

Pre-IPO placement	3,750
Issue proceeds	21,250
Internal accruals	378
Total	25,378

Background

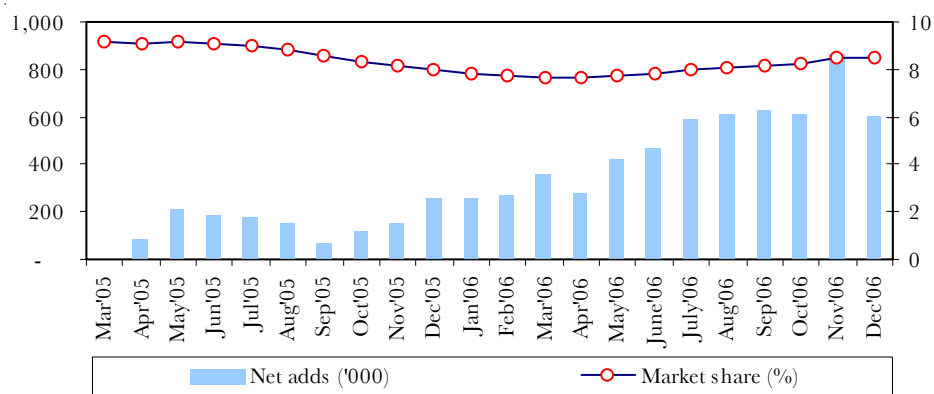
Although, Idea Cellular has operations in 11 circles (out of a total of 23 circles), it intends to have a pan-India presence and has applied for the remaining licences.

Overview of circles

	Mobile penetration (%)	No. of operators	Idea ranking	Market share (%)
Established circles				
Haryana	15.8	6	1	20.3
Maharashtra	10.3	6	1	23.0
UP (W)	10.4	6	1	21.2
Madhya Pradesh	7.0	6	2	21.4
Andhra Pradesh	14.8	6	4	13.5
Gujarat	18.5	6	3	16.0
Kerala	20.5	6	3	20.5
Delhi	71.1	7	5	11.5
New circles				
Himachal Pradesh	17.2	6	6	1.0
Rajasthan	10.4	7	6	2.5
UP (E)	7.2	6	6	2.3
New licence				
Bihar	4.5	5	–	–
Mumbai	58.8	7	–	–

Given below are the subscribers added by Idea per month and the market share as a % of the total mobile subscriber base. As can be seen, the lower net adds have resulted in loss in market share which can be ascribed to the management problem related to the JV partners – Birla and Tata. Both the net adds and market share have improved in past 6 months post resolution of the dispute with Birlas buying out Tata stake.

Idea – Subscribers



History

Year	Events	Number of operating circles
1995	Incorporated as Birla Communications	0
	Obtains licence for Gujarat and Maharashtra	0
1996	Changed name to Birla AT&T following JV between Grasim and AT&T	0
1997	Commenced operations in Gujarat and Maharashtra	2
2000	Merged with Tata Cellular acquiring Andhra Pradesh circle	3
2001	Acquired RPG cellular and hence MP circle	4
	Name changed to Birla Tata AT&T Ltd.	4
2001	Acquired Delhi licence	4
2002	Name changed to Idea Cellular, starts Delhi operations	5
2004	Acquired Escotel and hence Haryana, Kerala and UP (W)	8
2005	AT&T exits, equity split between Tata & Birla	8
2006	Tata exits, selling its stake to Birla	11
	Starts operation in 3 circles – HP, Rajasthan and UP (E)	11
	Obtains licence for Mumbai and Bihar	11

Shareholding changes

What initially started as a landmark event in telecom industry with 3 major players – Birla, Tata and AT&T joining hands to form Idea (all 3 having equal stake), ended up in a divorce with AT&T leaving in 2005 and Tata in 2006. When AT&T exited in September 2005, it sold its entire stake (33%) equally to the then JV partners, Birla and Tata at Rs. 17.77 per share. Tata sold its entire holding (approx. 50%) to Birla (AB Nuvo and Birla TMT) at a price of Rs. 40.50 in 2006. Since then, the promoter company Birla TMT has sold approximately 33% of the pre-IPO capital to a clutch of foreign investors included in the institutional investors list below. The sale was done at a price of Rs. 41.50 per share.

Shareholding pattern (%)

(%)	Pre Issue	Post Issue (Rs. 65)	Post Issue (Rs. 75)
Promoters	65.8	57.7	58.6
AB Nuvo Ltd.	36.3	31.8	32.3
Birla TMT	12.3	10.8	10.9
Hindalco	9.9	8.7	8.8
Grasim	7.4	6.5	6.6
Institutional investors	30.2	26.5	26.9
P5 Asia Investments (Mauritius)	14.3	12.5	12.7
Citigroup Global Markets (Mauritius)	5.9	5.2	5.3
Wagner Ltd.	4.4	3.8	3.9
Monet Ltd.	3.9	3.4	3.5
Nomad structure	0.9	0.8	0.8
Sequoia Capital	0.8	0.7	0.7
Others	4.0	15.9	14.4
Public	0.0	12.4	10.9
Others	4.0	3.5	3.5

Operational performance

Operational metrics	FY04	FY05	FY06	6MFY07	9MFY07
Subscriber base ('000s)	2,733	5,070	7,366	10,359	12,442
% market share	10.8	9.2	7.7	8.2	8.5
% prepaid	80.3	75.7	81.8	86.1	88.0
Churn (%)					
Prepaid	6.7	8.2	6.4	4.6	4.3
Post paid	4.6	4.4	5.3	4.7	4.6
Blended	6.2	7.3	6.2	4.6	4.3
MoU (Mins.)					
Pre paid	199	185	224	283	297
Post paid	583	463	523	657	683
Blended	279	248	289	343	353
ARPU (Rs.)					
Pre paid	381	307	304	283	279
Post paid	1,149	779	707	685	679
Blended	541	414	391	348	338

The company has been able to reduce the churn rate (i.e. % of subscribers leaving the operator) substantially and enhance MoU while increasing its market share. The fall in ARPUs is an industry wide phenomenon and with the introduction of services in new circles, we feel that ARPUs are bound to fall more.

Industry comparison (Dec.'06)

Operational metrics	Bharti Airtel	Reliance Com	Hutch Essar*	Idea Cellular
Market share (%)	21.8	20.5	15.9	8.5
Pre-paid (%)	87.1	82.9	84.1	88
Churn (%)	4.6	1.8	5.1	4.3
ARPU (Rs.)	427	328	420	279
MoU (min.)	467	454	406	297
RPM (Rs./min.)	0.91	0.72	1.03	0.94

*For the quarter ending September 2006.

Comparing with the leading telecom players, Idea lags behind in terms of ARPU and MoU. However, as RPM (revenue per minute) is at par with Bharti Airtel and Hutch Essar, the effective tariffs are not too low. In order to gain market share in the new circles, it might have to undertake predatory pricing or promotional offers (Subscriber acquisition & servicing costs have gone up from 8.7% of revenue in FY05 to 11% in FY06 and 12.6% in 9MFY07). Also, initially the subscribers (new users) have generally low usage (hence lower ARPU and MoU), the operating metrics are not likely to improve.

Comparison – Key financials (CY06)

(Rs. mn)	Bharti Airtel	Reliance Com	Hutch Essar*	Idea cellular
Revenue-mobile	123,146	98,784	92,274	39,137
Revenue-non mobile	41,985	36,233	–	–
EBITDA margin (%)-mobile	36.9	36.3	33.1	34.4
EBITDA margin (%)-non-mobile	49.9	42.4	NA	NA

*Estimated figures.

Despite the fact that all the other 3 players in the table above have substantially higher subscriber base and presence (hence better economies of scale) and better subscriber base (in terms of ARPU), the operating margins of Idea are not too low.

Outlook and Valuations

We have tried to compare Idea's valuations with Bharti Airtel and Reliance Com on EV (Mobile)/subscriber basis.

Valuation – Mobile business

	Bharti Airtel	Reliance Com	Idea (Rs 65)	Idea (Rs 75)
EV (Mobile)/subscriber (Rs.)	40,706	28,111	16,812	18,669
EV (Mobile)/sales (Mobile) (CY06)	10.6	8.5	5.3	5.9
Market price (Rs.)	771	489	65	75
Number of shares (mn)	1,895	2,045	2,636	2,593
Net debt (Rs. mn), Dec '06	48,133	14,806	37,811	37,811
EV (Rs. mn)-total	1,509,178	1,014,811	209,181	232,276
Subtract EV(non-mobile)	207,644	172,028	–	–
EV (Mobile) (Rs. mn)	1,301,534	842,783	209,181	232,276
Sales (CY06)-Mobile	123,146	98,784	39,137	39,137
Mobile subscriber base (mn) at Dec '06	31.97	29.98	12.44	12.44

We have obtained EV for mobile business by subtracting the EV for non-mobile business from total EV. To arrive at EV (non-mobile), we have given a premium of 20% and 25% to EV/sales of VSNL given the significant captive demand for the carrier services (NLD & ILD) and ability to service corporate clients with a bouquet of services becoming their one-stop-shop for telecom related needs.

Valuation – Non-mobile business

	Bharti Airtel	Reliance Com	VSNL
EV (non-mobile)/Sales (non-mobile)	5.0	4.8	4.0
Market price (Rs.)	771	489	489
Number of shares (mn)	1,895	2,045	285
Net debt (Rs. mn), Dec '06	48,133	14,806	15,553
EV (Rs. mn)-non mobile	207,644	172,028	154,918
Sales (CY06)-Non-mobile	41,985	36,233	39,155

As can be seen that Idea Cellular is at a significant discount to Bharti Airtel (>50% discount) and Reliance Com (~35% discount) on EV/subscriber basis. We feel that such high discount is not justified.

Also, given the growth opportunities available for Indian telecom players due to the low teledensity of ~17%, the current subscriber adds are likely to accelerate further. There is enough room for growth even for a late entrant like Idea. What remains to be seen is how fast will Idea be able to gain subscribers in the new circles along with existing circles while not compromising on margins. Acquisition of NLD licence will help further increase margins. We feel this IPO is a good opportunity to enter the Indian telecom market at a significant discount.

Financials

Balance Sheet

(Rs. mn)	FY02	FY03	FY04	FY05	FY06	9MFY07
Fixed assets	25,307	28,106	28,866	35,975	38,769	54,593
Gross block	16,341	22,546	25,775	40,632	47,934	63,053
Less: Depreciation	(3,459)	(5,340)	(7,478)	(16,437)	(20,831)	(24,930)
Net block	12,881	17,206	18,297	24,195	27,103	38,124
Intangible assets	9,388	10,470	9,669	10,825	9,934	11,905
CWIP	3,038	430	900	954	1,731	4,564
Goodwill on consolidation	4,300	4,336	4,469	11,605	11,605	11,605
Investments	0	17	450	–	–	950
Net deferred tax asset	–	–	–	–	–	3
Current assets	3,021	2,623	3,395	5,569	5,987	8,161
Inventories	51	78	97	176	114	182
Sundry debtors	705	701	837	1,514	1,308	1,629
Cash & bank balance	430	413	962	1,772	1,493	1,947
Other current assets	132	117	270	514	678	628
Loans & advances	1,703	1,314	1,229	1,594	2,394	3,774
Total assets	32,628	35,082	37,180	53,149	56,360	75,311
Debt	18,875	21,611	23,716	36,939	32,856	39,759
Secured loans	13,772	9,137	15,064	22,431	15,709	35,361
Unsecured loans	5,103	12,474	8,652	14,507	17,147	4,397
Current liabilities	4,445	3,962	4,945	7,020	12,313	20,939
Net worth	9,308	9,509	8,519	9,190	11,191	14,614
Share capital	20,167	25,265	27,425	27,425	27,425	27,425
Advance against share capital	2,925	1,140	–	–	–	–
Reserve & surplus	998	998	998	998	998	1,499
Misc. expenses	–	–	–	–	–	(13)
Profit/(Loss)	(14,782)	(17,895)	(19,905)	(19,234)	(17,233)	(14,298)

Profit & Loss A/c

(Rs. mn)	FY03	FY04	FY05	FY06	9MFY07
Income	9,403	12,966	22,557	29,655	30,580
Service revenue	9,403	12,965	22,464	29,489	30,416
Sale of trading goods	0	1	93	166	164
Operating expenses	6,968	9,210	14,347	18,981	20,306
Cost of trading goods	0	1	84	76	61
Personnel expenses	627	789	1,457	1,781	1,913
Network operating expenses	1,259	1,604	2,488	3,158	3,599
Licence & spectrum	1,233	1,619	2,187	3,020	3,076
Roaming & access charges	1,565	2,426	3,823	4,963	5,085
Subscriber acquisition & servicing	774	1,272	1,961	3,272	3,855
Advertising & business promotion exp.	376	685	1,048	1,253	1,404
Administration & other expenses	1,133	813	1,301	1,457	1,313
PBIDT	2,436	3,756	8,210	10,674	10,274
Margin (%)	25.9	29.0	36.4	36.0	33.6
Other income	107	163	171	244	139
Depreciation	1,969	2,205	3,420	4,451	4,154
Amortisation of intangibles	805	844	1,007	1,044	803
Amortisation of miscellaneous exp.	269	267	–	–	–
Financial charges	2,525	2,961	3,189	3,225	2,317
PBT	(3,026)	(2,358)	765	2,198	3,139
Tax	1	1	–	80	41
Current tax	1	1	–	34	89
Deferred tax	–	–	–	–	(3)
FBT	–	–	–	47	44
MAT credit	–	–	–	–	(89)
PAT	(3,028)	(2,359)	765	2,118	3,098
Prior period adjustments	(1)	(5)	(6)	–	–
Exceptional items (refund from DOT)	813	–	–	–	–
Net profit after exceptional items	(2,216)	(2,364)	759	2,118	3,098
Adjustments on A/c of :	(897)	355	(88)	(117)	(83)
Impact on material adjustment & prior period items	(864)	(3)	(93)	(92)	(83)
Impact on changes in A/c policies	(34)	357	5	(25)	–
Profit after adjustment	(3,113)	(2,009)	671	2,001	3,016
EPS annualised* (Rs.)	(1.7)	(1.2)	0.1	0.7	1.2

*Above EPS is stated after subtracting the unpaid preference share dividend if any.

Cash Flow Statement

(Rs. mn)	FY03	FY04	FY05	FY06	9MFY07
PAT after adjustment	(3,113)	(2,009)	671	2,001	3,016
Adjusted for:					
Depreciation, amortisation	2,685	2,959	4,422	5,520	4,957
Interest charges	2,499	2,695	3,189	3,225	2,317
Profit on sale of investments	(5)	(2)	(2)	(10)	(20)
Provision for bad & doubtful debts	443	214	239	307	268
Provision for gratuity etc.	8	23	118	83	36
Provision for FBT	–	–	–	47	44
Prov for tax	–	1	–	34	(3)
Dividend income	–	(1)	–	–	–
Interest received	(20)	(18)	(53)	(27)	(17)
(Profit)/loss on sale of FA	165	20	1	0	4
Operating profit before WC changes	2,660	3,881	8,586	11,178	10,600
Changes in CA & CL	458	(2,056)	(771)	1,693	1,240
(Inc.)/dec. in sundry debtors	(405)	(648)	(556)	(27)	(441)
(Inc.)/dec. in inventories	(27)	(19)	(60)	61	(68)
(Inc.)/dec. in Other CA	(17)	(15)	(251)	(164)	(99)
(Inc.)/dec. in loans & advances	391	(2,952)	4	(403)	(1,982)
Inc./(dec.) in CL	517	1,578	91	2,225	3,829
Tax paid (FBT & TDS)	–	(63)	(62)	(94)	(56)
Net cash from operations	3,119	1,762	7,752	12,777	11,784
Cash from investing activities	(6,753)	(4,258)	(7,363)	(5,221)	(15,876)
Purchase of FA (CWIP)	(6,741)	(3,779)	(5,449)	(5,293)	(14,869)
Investment in subsidiaries	(38)	(133)	(2,600)	–	–
Proceeds from sale of FA	19	74	121	34	6
Advance for purchase of equity/licences	–	–	–	–	(100)
Sale/(purchase) of other investments	(17)	(433)	510	–	(930)
Interest & dividend received	24	13	54	37	17
Cash flow from financing activities	3,618	3,045	(310)	(7,835)	4,544
Proceeds from issue of share cap.	2,180	1,021	–	0	–
Advance rcvd against share cap.	1,141	–	–	0	–
Proceeds from long-term borrowings	–	12,539	1,489	1,001	35,361
Repayment of long-term borrowings	(2,283)	(3,535)	(1,254)	(9,722)	(15,690)
Proceeds from short-term loan	5,019	–	14,300	19,847	14,664
Repayment of short-term loan	–	(4,419)	(10,928)	(15,210)	(27,459)
Short-term loan from/to subsidiary & others	–	(155)	(665)	(377)	(13)
Interest paid	(2,439)	(2,406)	(3,252)	(3,375)	(2,320)
Net inc./(dec.) in cash	(17)	549	79	(279)	452

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