

2G auction fails; Spectrum price could be lowered

The much awaited 2G spectrum auction in 1800MHz band ended in just two days (total 14 clock rounds), with DoT managing to sell only 102 out of 176 available blocks and garnering merely Rs94bn, as against the targeted amount of Rs400bn.

2G auction finds either no bidders or bids at base price only: Circles, like Mumbai, Delhi, Karnataka and Rajasthan, did not receive any bids at all. Combined reserve price of these 4 circles was Rs17.7bn per block, which is about 50% of the pan-India reserve price. In other circles, the winning bids were at base price, except for Bihar, where it was 9% higher than base price.

Idea buys spectrum in all 7 circles: Idea managed to buy spectrum in all the 7 circles where the Supreme Court had cancelled its licence for a consideration of Rs19.6bn. Idea also bought an additional spectrum block in the Bihar and West Bengal circles for Rs723mn, resulting in total outgo of Rs20.3bn.

Selective buying by Bharti & Vodafone and new entrants: Bharti bought only one block of spectrum for Rs87mn in Assam, whereas Vodafone bought extra spectrum in 14 circles (see Exhibit 1). Among new operators, Telenor and Videocon secured spectrum in six circles each for a total Rs40.2bn and Rs22.2bn.

DoT could approach TRAI for lowering base price: Media reports indicate that DoT is likely to approach TRAI for taking a relook, and possibly making a downward revision to the base reserve price for 2G spectrum. The failure of 2G auction has created various issues as there is now (1) no market determined price for GSM spectrum in four circles (2) no market determined price for CDMA spectrum in any of the circles (3) No demand at current base price, as not all available blocks were sold in any of the circles (except Bihar) and (4) no fair method to arrive at the price for re-farming in 900Mhz, excess spectrum, and spectrum "liberalisation".

Downward revision of 2G spectrum pricing to benefit industry: We believe any re-pricing of 2G spectrum will be positive for the industry, which is already suffering from stretched balance sheets, limited pricing flexibility and low payoffs from 3G/4G investments. Since pricing for the 2G auction was meant to act as a benchmark for deciding the pricing for all other spectrums (like re-farming of 900MHz band, penalty of excess spectrum beyond 6.2MHz, conversion of allotted spectrum to "liberalised" spectrum, and license renewal cost), any downward revision will have a positive cascading effect on all aspects of spectrum pricing.

Valuation: We believe the failure of 2G auction has resulted in current reserve price (Rs35bn per block pan-India) becoming a price ceiling for spectrum, rather than a price floor. Any lowering of 2G spectrum price will benefit Bharti and Idea, as the impact on their balance sheet will reduce, due to decline in future payoffs for license renewals, spectrum re-farming, and excess spectrum penalty. Bharti trades at 7x FY13 EV/EBITDA; maintain Add with a TP of Rs305. Idea trades at 6.6x FY13 EV/EBITDA, maintain Add with TP of Rs90.

Peer valuation

(Rs bn)

Company	CMP (Rs)	Net sales			EBITDA			Net profit			EV/EBITDA (X)		P/E (X)		Rating
		FY13E	FY14E	FY15E	FY13E	FY14E	FY15E	FY13E	FY14E	FY15E	FY13E	FY14E	FY13E	FY14E	
Bharti	283.0	804.4	902.0	1,006.7	252.3	299.2	348.1	37.3	65.6	85.0	7.1	6.0	28.8	16.4	ADD
Idea	92.2	219.3	251.5	283.5	58.6	70.5	80.2	9.7	13.9	17.0	7.4	6.2	31.5	22.3	ADD

Source: BRICS Research

Exhibit 1: 2G spectrum auction

(Rs mn)

Circle	Reserve price/Block	Final winning price	Total Blocks sold	Winners	Remarks
Bihar	425	464	11	Idea (1), Videocon (4), Vodafone (2), Telenor (4)	Winning price at 9.2% premium to base price
AP	2,869	2,869	4	Telenor (4)	Winner at base price only
Assam	87	87	7	Bharti (1), Idea (4), Vodafone (2)	Winner at base price only
Gujarat	2,248	2,248	8	Telenor (4), Videocon (4)	Winner at base price only
H.P.	78	78	1	Vodafone (1)	Winner at base price only
Haryana	465	465	6	Vodafone (2), Videocon (4)	Winner at base price only
J&K	63	63	6	Vodafone (2), Idea (4)	Winner at base price only
Kerala	653	653	1	Vodafone (1)	Winner at base price only
Kolkata	1,137	1,137	4	Idea (4)	Winner at base price only
M.P.	540	540	6	Vodafone (2), Videocon (4)	Winner at base price only
Maharashtra	2,628	2,628	5	Telenor (4), Vodafone (1)	Winner at base price only
North East	88	88	6	Idea (4), Vodafone (2)	Winner at base price only
Orissa	203	203	6	Idea (4), Vodafone (2)	Winner at base price only
Punjab	673	673	1	Vodafone (1)	Winner at base price only
Tamil Nadu	3,061	3,061	4	Idea (4)	Winner at base price only
UP-East	762	762	9	Videocon (4), Vodafone (1), Telenor (4)	Winner at base price only
UP-West	1,074	1,074	10	Videocon (4), Vodafone (2), Telenor (4)	Winner at base price only
West Bengal	258	258	7	Idea (5), Vodafone (2)	Winner at base price only
Delhi	6,931		0		No bidder
Mumbai	6,785		0		No bidder
Karnataka	3,301		0		No bidder
Rajasthan	671		0		No bidder

Source: DoT, BRICS Research

BRICS RECOMMENDATION SCALE

BUY:	More than 15% upside
ADD:	Upside up to 15% (between 0% and 15%)
REDUCE:	Downside up to 15% (between 0% and -15%)
SELL:	More than 15% downside

Head Office: Sadhana House, 1st Floor, 570, P. B. Marg, Behind Mahindra Tower,
Worli, Mumbai - 400 018. Tel: (91-22) 6636 0000

Disclaimer: This Report/Document has been prepared solely for your information. All reasonable care has been taken to ensure that the information contained herein is not misleading or untrue at the time of publication, but we make no representation as to its accuracy or completeness. All information is for private use of the person to whom it is provided and is not for public distribution and without any liability whatsoever on the part of BRICS Securities Limited, any associated company, or employee thereof (hereinafter collectively referred to as BRICS). This Report/Document shall not be copied, printed, distributed or re-distributed to any person. If you are not the intended recipient of this Report/Document, you should immediately send it to the sender. Nothing contained herein should be construed as an offer to buy or sell or a solicitation of an offer to buy or sell. The value of any investment may fall as well as rise. Past performance is no guide to the future. The rate of exchange between currencies may cause value of investment to increase or diminish; consequently investors may not get back full value of their original investment.

BRICS shall not be liable for any direct or indirect losses arising from action initiated by you on the basis of information provided in this Report/Document and BRICS accepts no responsibility for statements made or any other source of information received by you and you would be doing so at your own risk.

This Report/Document is not directed or intended for distribution to or use by any person or entity who is a US citizen or person resident in US or who is a citizen/resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject BRICS to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to a certain category of investors. Persons in whose possession this presentation may come are required to inform themselves of and to observe such restrictions.