

**Sector: Telecom**

Sensex:	16,502
CMP (Rs):	98
Target price (Rs):	110
Upside (%):	12.2
52 Week h/l (Rs):	104/52
Market cap (Rscr) :	32,390
6m Avg vol ('000Nos):	6,579
No of o/s shares (mn):	3,305
FV (Rs):	10
Bloomberg code:	IDEA IN
Reuters code:	IDEA.BO
BSE code:	532822
NSE code:	IDEA

Closing price as on 12 Sep, 2011

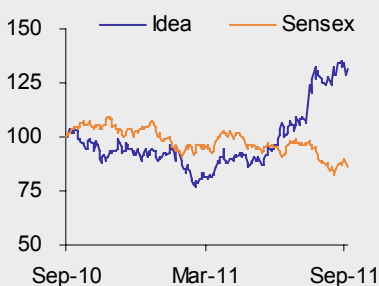
**Shareholding pattern**

<b>June ' 11</b>	<b>(%)</b>
Promoters	46.0
Institutions	18.1
Non promoter corp hold	0.5
Public & others	35.4

**Performance rel. to sensx**

(%)	<b>1m</b>	<b>3m</b>	<b>1yr</b>
Idea	6.6	45.1	38.6
Bharti	1.3	12.7	21.6
Rcom	(2.8)	(3.9)	(39.7)

**Share price trend**



**Idea shares Bharti's optimism on tariffs, eventual end to hyper competitive phase**

Idea Cellular FY11 annual report shares Bharti's optimism on an eventual end to hyper competitive phase and return of pricing power to operators. Subsequent news flow on 2G rate hikes by telcos suggests the optimism is not misplaced. Annual report also reiterates key positives of what is the only listed pure wireless operator-revenue growth >2x the industry rate, high quality sub base and rising revenue market share (RMS) over FY09-11.

**Competition has taken its toll on margins, RoE**

A crowded field with 14 players implied GSM incumbents continued to struggle in FY11; Idea reported ~13% drop in realized rate/min to 40.6p through Q4 FY10 to Q4 FY11, worse than Bharti's 8% decline. Both EBIT and PAT margins fell to lowest level in at least 6 years, which expectedly kept RoE, RoCE at mid-single digit levels. Excluding the ~Rs58bn in 3G fees and capitalized ~Rs4.1bn in related interest cost, capex/sales declined 8ppts to 24%.

**Impressive working capital mgmt bolsters operating CF**

Idea continues to impress on operating efficiency as it runs a tight ship over its working capital cycle. Negative working cycle further expanded to 69 days helped by decline in loans and advances and increase in creditor days, thereby boosting operating CF to Rs61bn.

**Valuations still leave room for upside: retain BUY**

Idea has put in a stellar performance over the past 1 year, outperforming the Sensex by ~39%. Optimism on the stock has been driven by perceived stability in voice tariffs; in fact, Idea has reportedly hiked rates in select circles although we would watch for impact, if any, on traffic growth.

The stock currently trades at 6.6x FY13 EV/EBIDTA which is much below its historic 1-yr fwd average. Based on FY11 actual numbers, we tweak our revenue/PAT estimates for FY12/13 but retain BUY with a revised 9-mth TP of Rs110.

**Financial highlights**

Y/e 31 Mar (Rs m)	FY10	FY11	FY12E	FY13E
Revenues	123,979	154,384	193,744	229,245
yoy growth (%)	22.4	24.5	25.5	18.3
Operating profit	33,580	37,258	49,211	59,604
OPM (%)	27.1	24.1	25.4	26.0
Pre-exceptional PAT	7,071	7,878	7,485	14,175
Reported PAT	9,540	8,987	7,485	14,175
yoy growth (%)	8.2	(5.8)	(16.7)	89.4
EPS (Rs)	2.9	2.7	2.3	4.3
P/E (x)	33.9	36.0	43.2	22.8
P/BV (x)	2.7	2.6	2.5	2.2
EV/EBITDA (x)	11.9	11.8	8.4	6.6
Debt/Equity (x)	0.7	1.0	0.9	0.7
ROE (%)	5.5	6.5	5.9	10.3
ROCE (%)	6.3	6.0	8.5	11.7

Source: Company, India Infoline Research

**Research Analyst**

**Bhavesh Gandhi**

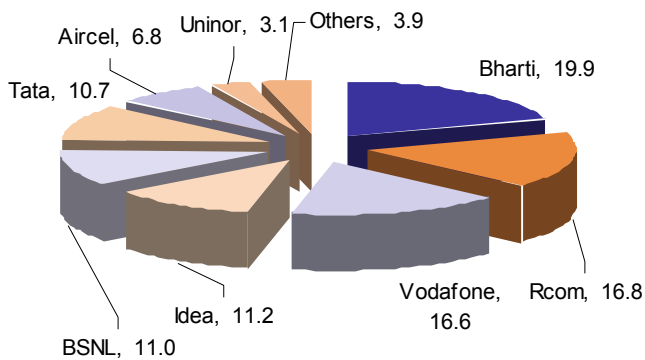
research@indiainfoline.com

**Idea appears optimistic on end of hyper competitive phase, return of pricing power**

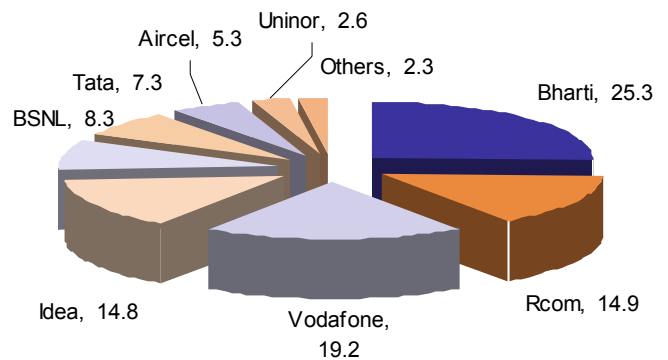
*Idea, like Bharti, remains optimistic on an eventual end of the hyper competitive phase and return of pricing power to operators*

Idea has expressed optimism that it is poised to reap benefits once the hyper competitive phase draws to its 'inevitable close' and pricing power returns to operators. Subsequent news flow on voice tariff hikes by incumbent players indicates that such optimism is not misplaced. FY11 saw Idea consolidate its position in 13 established circles and calibrated investment in 9 new circles. Annual report reiterates key competitive strengths namely, leader in ratio of active to reported subscribers and rising revenue market share (gain of 210bps over FY09-11).

**Reported subscriber market share, June '11**

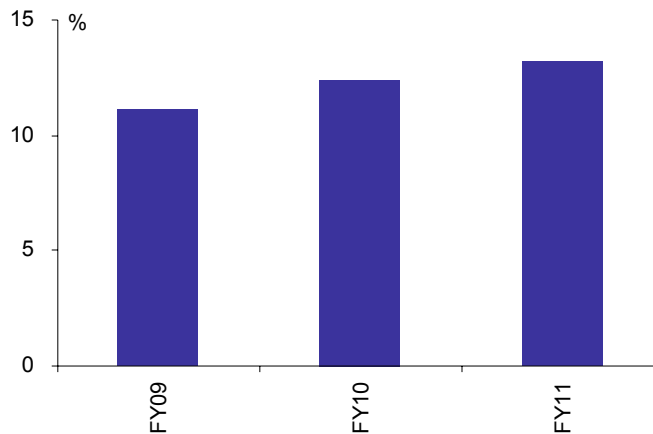


**VLR (active) sub market share, Jun '11**



Source: Company, India Infoline Research

**Idea has made impressive gains in RMS**



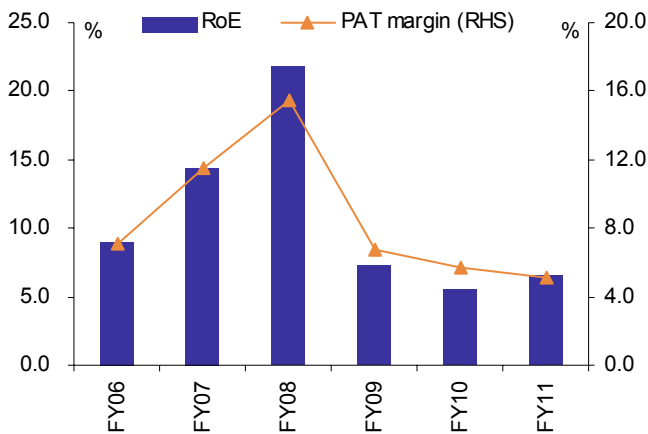
Source: Company, India Infoline Research

**Competition has taken its toll on margins, RoE**

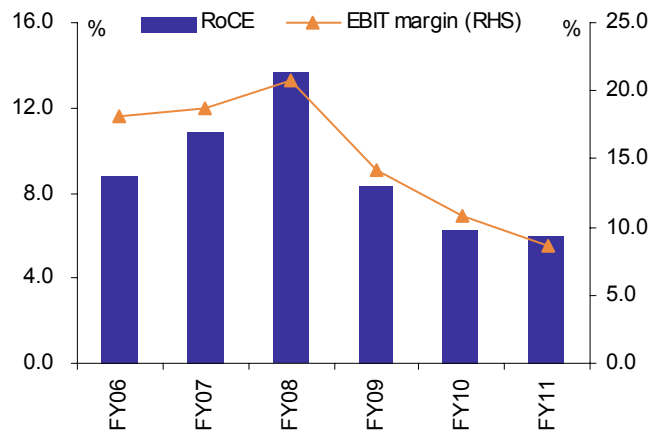
A crowded field continues to take its toll on profitability margins and return ratios. Idea saw ~13% decline in its realized rate/min through Q4 FY10 to Q4 FY11. Consequently, operating margin as well as profitability ratios-EBIT, PAT were dragged lower in FY11. Both RoE and RoCE remain stuck at the single digit levels as was seen in previous two years.

*Idea FY11 profitability margins stood at lowest level since at least FY06*

**PAT margin at lowest level since at least FY06...**



**...so was EBIT margin, impacting return ratios**

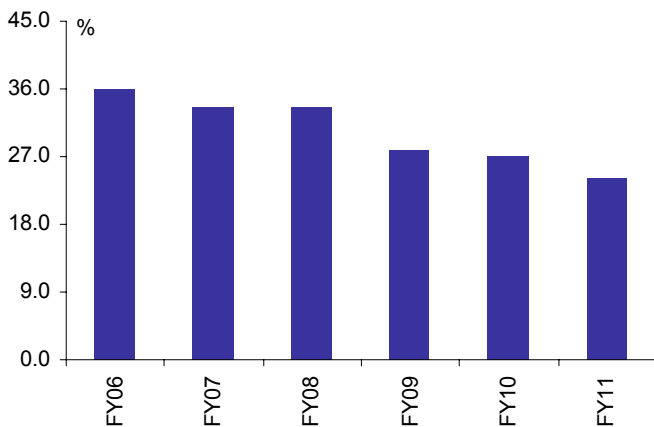


**Ramp up in N/w opex but SG&A costs stable in three years**

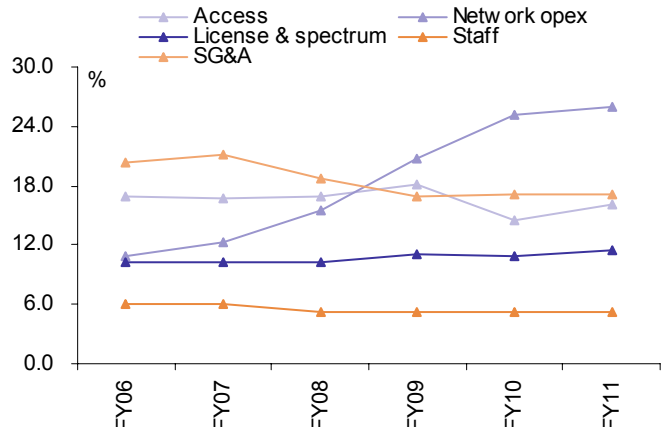
Idea has significantly ramped up network opex by nearly 10 ppts over the past three years as it has gradually completed pan India roll out. At the same time, it has managed to keep SG&A costs under impressive control over the same period. FY11 operating margin was pulled down by increased access charges and higher license fees.

*Network opex has been significantly ramped up in the past three years*

**Trend in operating margin**



**Trend in key costs: network opex has been scaled up**



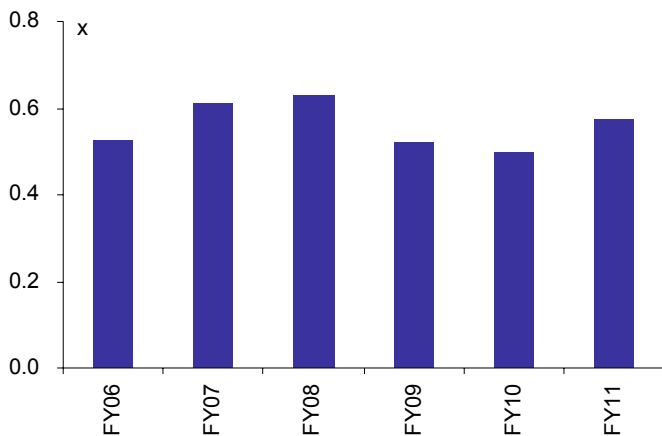
Source: Company, India Infoline Research

**Upfront 3G fee payment depresses asset turnover**

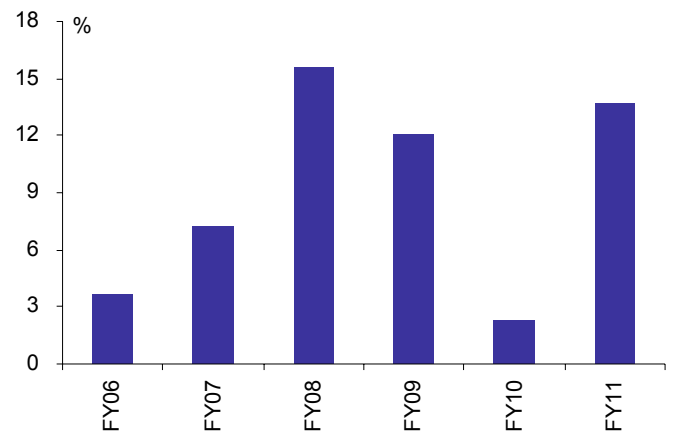
*Idea carried ~Rs62bn in 3G related intangible assets which depressed reported improvement in asset turnover*

Idea carried a total of ~Rs62bn in 3G intangible assets (Rs58bn 3G fees+Rs4.1bn interest capitalized thereon). However, Idea launched 3G services only towards the end of year and so if one removes these assets (in absence of any commensurate revenues), adjusted asset turnover would have shown an even better improvement.

**Asset turnover would have been higher but for upfront 3G fees**

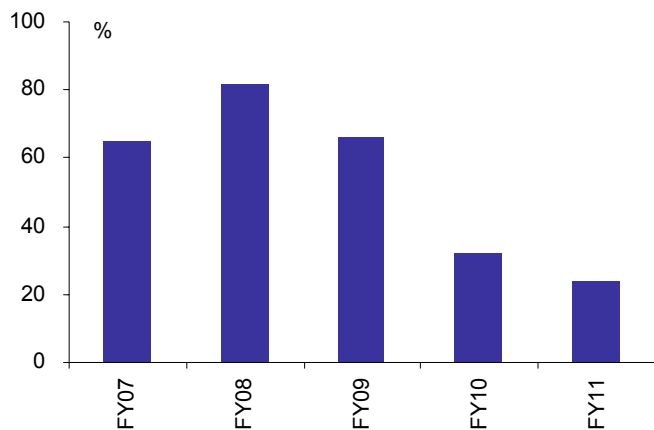


**CWIP as % of gross block**

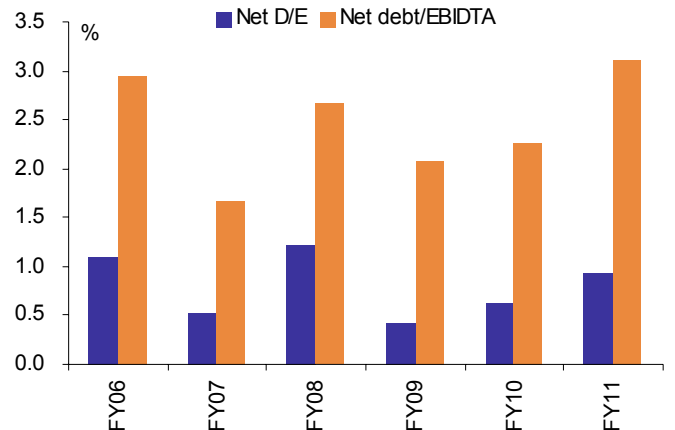


Source: Company, India Infoline Research

**Capex\*/sales ratio moderated further in FY11**



**Leverage inched up on 3G related borrowings**



Source: Company, India Infoline Research

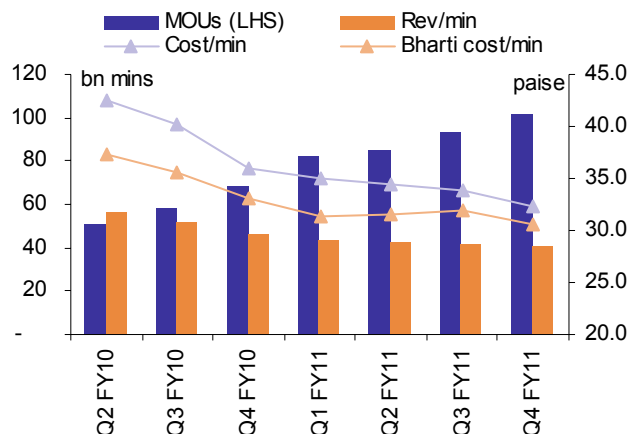
\*Capex excludes 3G fees and capitalized interests costs thereon

Idea's efficient operations has led to narrowing cost/min differential wrt Bharti

### Idea has narrowed cost/min differential wrt Bharti

Idea has over the past few quarters narrowed the cost/min differential wrt Bharti as operations gain scale and costs have been held under tight leash. Although, rev/min has fallen ~21% in the past 5 quarters, cost/min (standalone) too has declined 19%. From a 5.2p/min difference in Q2 FY10, Idea has closed the gap with Bharti to just 1.8p in Q4 FY11.

### Narrowing cost/min differential wrt Bharti



Source: Company, India Infoline Research

Decline in loans and advances days outstanding and increase in creditor days bolstered operating CF in FY11

### Working cap cycle bolsters operating CF

An indication of Idea's robust execution record has been its ability to run a tight ship wrt its working capital cycle. Loans and advances outstanding declined from 84 days to 49 days while payment cycle to creditors was stretched further to 89 days. Consequently, the positive contribution from operating cycle helped lower current ratio to 0.6x from 0.9x in FY10.

### Trend in operating cycle

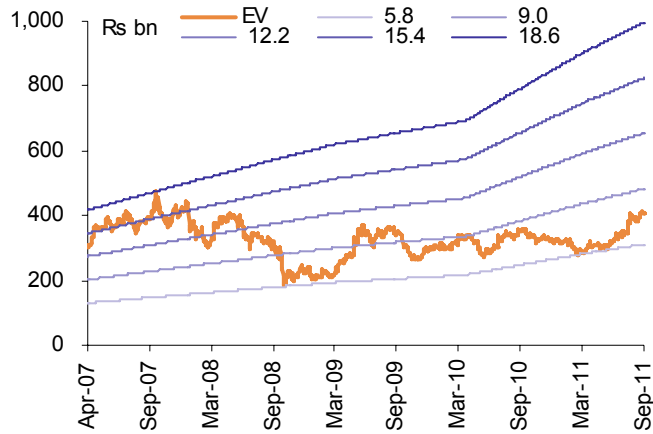
WC days	FY06	FY07	FY08	FY09	FY10	FY11
Inventories	1	1	1	2	2	2
Debtors	16	13	11	13	14	11
Loans & advances	37	40	45	67	84	49
Creditors	104	135	96	94	71	89
Other curr lia	44	41	47	46	42	38
Provisions	3	5	4	6	7	4
<b>Total WC days</b>	<b>(97)</b>	<b>(126)</b>	<b>(90)</b>	<b>(63)</b>	<b>(20)</b>	<b>(69)</b>

Source: Company, India Infoline Research

### Key annual report highlights

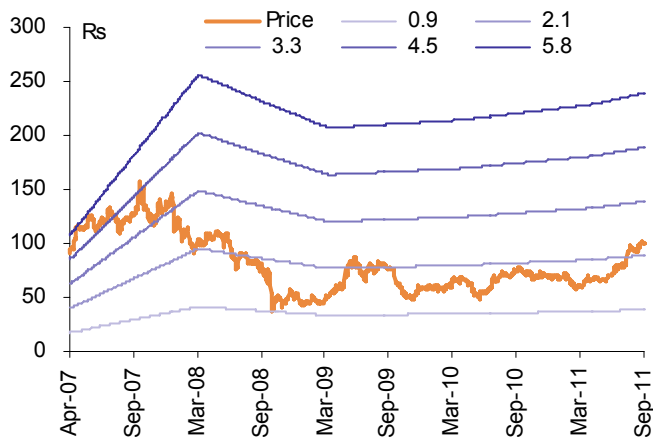
- ⊕ Idea increased its **RMS to 13.2%** from **12.4%** in previous year; it leads in **ratio of active to reported subscribers at ~93%** and was the biggest net gainer in number portability in FY11
- ⊕ Idea shares Bharti's optimism on an eventual end to the hyper competitive phase and return of pricing power to operators
- ⊕ Forays into mobile banking with 'Idea MyCash' pilot facility to provide basic banking services like money transfer using mobile platform in alliance with Axis Bank
- ⊕ **13 established** circles accounted for **89%** of revenues while their RMS stood at **17.7%**
- ⊕ Idea still owns >9,000 towers with tenancy of 1.54, apart from the demerged 11,094 towers under IRU arrangement with Indus
- ⊕ Won 3G spectrum in 11 circles which account for **76%** of its revenue base and has entered into bilateral roaming agreements with leading operators for Mumbai, Delhi Bihar, Karnataka, Kolkata and TN (inc Chennai)
- ⊕ About 60% of Idea subscribers use GPRS/EDGE handsets but only 10% are active users of wireless data services-a potential target market for the company
- ⊕ Realized **rate/min** fell **12.9%** through Q4 FY10 to Q4 FY11 but operational efficiencies ensured cost/min too fell **10.6%** to 32.6p
- ⊕ FY11 capex stood at **Rs99bn** including ~Rs58bn on 3G fees and Rs4.1bn in capitalized interest costs related to 3G debt
- ⊕ **Accumulated losses** of **Rs5bn** including those of the Spice Communications were wiped off in FY11
- ⊕ In Jul' 11, Delhi HC **reaffirmed the amalgamation of Spice** with the company in response to an application filed by DoT in March for recall of its order dated Feb' 10 sanctioning the scheme; However, the judgment transferred and vested unto the DoT, the six licenses granted to erstwhile Spice along with the spectrum (including the two operational licenses for Punjab & Karnataka), till the permission of DoT is granted for transfer thereof upon an application from Idea to that effect
- ⊕ Idea then filed an appeal before the Appellate Bench of the Delhi HC, challenging the above judgment. Through interim orders, Appellate Bench has directed DoT to (1) Accept the license fee without prejudice, as Idea continues to operate the licenses for Punjab & Karnataka granted to erstwhile Spice and 2) To maintain status quo in relation to the two operating licenses and no coercive steps in relation to any demand pertaining to the four non operating licenses, till the next hearing
- ⊕ Idea has not been given clearance for commercial use of the allotted 3G spectrum band in Punjab which compelled the company to approach TDSAT; TDSAT directed Idea to approach it again, if required, upon the final disposal of the Spice amalgamation issue by the Appellate Bench of Delhi HC

**Idea trades below historic 1-yr fwd EV/EBIDTA average...**



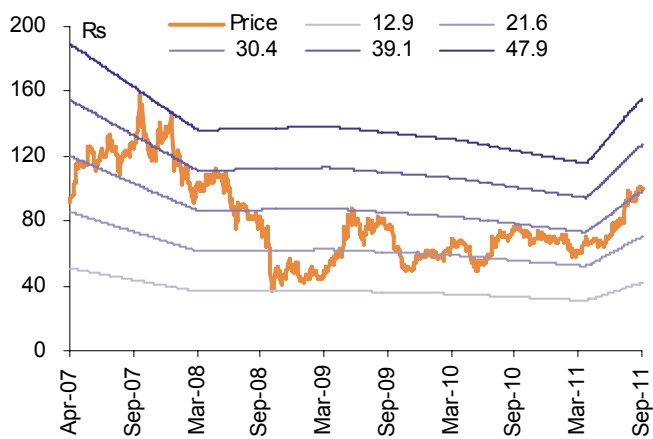
Source: Company, India Infoline Research

**...as well as P/BV**



Source: Company, India Infoline Research

**PE valuation bounces back to historic average**



Source: Company, India Infoline Research

*Idea has outperformed the Sensex by 39% but we believe current valuation still leaves room for upside*

**Valuations still leave room for upside: maintain BUY**

Idea has outperformed the Sensex by ~39% over the past 1 year on the back of likely stability in voice tariffs as well a lack of disruptive pricing of 3G plans. Regulatory uncertainty in terms of excess spectrum charge, spectrum renewal is also likely to be addressed in the new telecom policy. Meanwhile Idea, along with Bharti, has reportedly increased tariffs in select circles although the impact may be felt over the next 1 year; however, we would watch out for any volume impact of the same.

The stock trades at 6.6x FY13 EV/EBIDTA, much below its historic 1-yr fwd average. While the stock has put in a stellar performance, we believe current valuation still leaves room for upside. Based on FY11 actual numbers, we tweak our revenue/ PAT estimates for FY12/13 but retain BUY with a revised 9-mth TP of Rs110 (earlier Rs105).



## Financials

### Income statement

Y/e 31 Mar (Rs m)	FY10	FY11	FY12E	FY13E
Revenue	123,979	154,384	193,744	229,245
<b>Op.profit</b>	<b>33,580</b>	<b>37,258</b>	<b>49,211</b>	<b>59,604</b>
Dep & Amort	(20,149)	(23,973)	(28,018)	(30,208)
Interest exp	(5,215)	(4,515)	(10,593)	(9,243)
Other income	70	89	94	99
<b>PBT</b>	<b>8,286</b>	<b>8,860</b>	<b>10,693</b>	<b>20,250</b>
Taxes	(1,214)	(982)	(3,208)	(6,075)
<b>Adj. profit</b>	<b>7,071</b>	<b>7,878</b>	<b>7,485</b>	<b>14,175</b>
Extra items	2,468	1,109	-	-
<b>Net profit</b>	<b>9,540</b>	<b>8,987</b>	<b>7,485</b>	<b>14,175</b>

### Balance sheet

Y/e 31 Mar (Rs m)	FY10	FY11	FY12E	FY13E
Equity capital	32,998	33,033	33,033	33,033
ESOPS	445	478	478	478
Reserves	85,299	89,469	96,954	111,130
<b>Net worth</b>	<b>118,761</b>	<b>122,999</b>	<b>130,484</b>	<b>144,660</b>
Debt	78,593	120,705	117,705	102,705
Def.tax lia	2,142	3,099	3,254	3,417
<b>Total liabilities</b>	<b>199,496</b>	<b>246,803</b>	<b>251,443</b>	<b>250,781</b>
Fixed assets	170,937	212,465	197,732	201,769
Intangible assets	16,267	48,912	45,267	41,621
Investments	11,304	10,200	10,200	10,200
<b>Net working cap</b>	<b>(4,050)</b>	<b>(24,774)</b>	<b>(1,755)</b>	<b>(2,809)</b>
Inventories	536	659	1,062	1,256
Sundry debtors	4,656	4,789	6,900	8,165
Cash	2,900	4,577	28,793	33,337
Other curr assets	28,538	20,532	29,062	34,387
Sundry creditors	(24,134)	(37,682)	(44,057)	(52,130)
Other current lia	(16,545)	(17,650)	(23,515)	(27,823)
Misc.exp	5,038	-	-	-
<b>Total assets</b>	<b>199,496</b>	<b>246,803</b>	<b>251,443</b>	<b>250,781</b>

### Cash flow statement

Y/e 31 Mar (Rs m)	FY10	FY11	FY12E	FY13E
Profit before tax	8,286	8,860	10,693	20,250
Dep & Amort	20,149	23,973	28,018	30,208
Misc.exp w/o	226	5,038	-	-
Def.tax lia	1,012	957	155	163
Tax paid	(1,214)	(982)	(3,208)	(6,075)
Working cap Δ	(10,590)	22,401	1,197	5,597
Other op items	2,468	1,109	-	-
Operating CF	20,336	61,356	36,855	50,144
Capital exp	(18,224)	(98,146)	(9,639)	(30,600)
<b>Free cash flow</b>	<b>2,112</b>	<b>(36,790)</b>	<b>27,216</b>	<b>19,544</b>
Equity raised	(28,695)	(4,749)	-	-
Investments	9,148	1,104	-	-
Debt fin/disp	(10,529)	42,112	(3,000)	(15,000)
<b>Net Δ in cash</b>	<b>(27,964)</b>	<b>1,677</b>	<b>24,216</b>	<b>4,544</b>

### Key ratios

Y/e 31 Mar	FY10	FY11	FY12E	FY13E
<b>Growth matrix (%)</b>				
Revenue growth	22.4	24.5	25.5	18.3
Op profit growth	19.4	11.0	32.1	21.1
EBIT growth	(5.8)	(0.9)	59.2	38.6
Net profit growth	8.2	(5.8)	(16.7)	89.4

### Profitability ratios (%)

	FY10	FY11	FY12E	FY13E
OPM	27.1	24.1	25.4	26.0
EBIT margin	10.9	8.7	11.0	12.9
Net profit margin	5.7	5.1	3.9	6.2
RoCE	6.3	6.0	8.5	11.7
RoNW	5.5	6.5	5.9	10.3
RoA	2.8	2.9	2.4	4.4

### Per share ratios

	FY10	FY11	FY12E	FY13E
EPS	2.1	2.4	2.3	4.3
Cash EPS	7.6	8.9	9.6	12.3
Book value per share	36.0	37.2	39.5	43.8

### Valuation ratios (x)

	FY10	FY11	FY12E	FY13E
P/E	33.9	36.0	43.2	22.8
P/BV	2.7	2.6	2.5	2.2
M Cap/Sales	2.6	2.1	1.7	1.4
EV/EBIDTA	11.9	11.8	8.4	6.6

### Payout (%)

	FY10	FY11	FY12E	FY13E
Tax payout	14.7	11.1	30.0	30.0

### Liquidity ratios

	FY10	FY11	FY12E	FY13E
Debtor days	14	11	13	13
Inventory days	2	2	2	2
Creditor days	71	89	83	83

### Leverage ratios

	FY10	FY11	FY12E	FY13E
Interest coverage	2.6	3.0	2.0	3.2
Net debt / equity	0.6	0.9	0.7	0.5
Net debt / op. profit	2.3	3.1	1.8	1.2

### Du-Pont Analysis

Y/e 31 Mar (Rs m)	FY10	FY11	FY12E	FY13E
Tax burden (x)	0.85	0.89	0.70	0.70
Interest burden (x)	0.61	0.66	0.50	0.69
EBIT margin (x)	0.11	0.09	0.11	0.13
Asset turnover (x)	0.50	0.57	0.62	0.71
Financial leverage (x)	1.95	2.23	2.46	2.37

RoE (%)	FY10	FY11	FY12E	FY13E
	<b>5.5</b>	<b>6.5</b>	<b>5.9</b>	<b>10.3</b>

**In the year 2011 itself, we have received two reputed awards for being the Best Broker in India.**

## 'Best Equity Broker of the Year' – Bloomberg UTV, 2011

IIFL was awarded the 'Best Equity Broker of the Year' at the recently held Bloomberg UTV Financial Leadership Award, 2011. The award presented by the Hon'ble Finance Minister of India, Shri Pranab Mukherjee. The Bloomberg UTV Financial Leadership Awards acknowledge the extraordinary contribution of India's financial leaders and visionaries from January 2010 to January 2011.

## 'Best Broker in India' – Finance Asia, 2011

IIFL has been awarded the 'Best Broker in India' by Finance Asia. The award is the result of Finance Asia's annual quest for the best financial services firms across Asia, which culminated in the Country Awards 2011

## Other awards



### Recommendation parameters for fundamental reports:

**Buy** – Absolute return of over +10%

**Market Performer** – Absolute return between -10% to +10%

**Sell** – Absolute return below -10%

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