

Idea CellularRs117
NEUTRAL

RESULT NOTE

Mkt Cap: Rs308bn; US\$7.5bn

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Result: Q4FY07

Comment: Lower salary and higher other income aids performance

Last report: 09 April 2007 (Price Rs95; Recommendation: Neutral)

Key financials

Year end 31 Mar (Rs m)	Net sales (Rs m)	% Change yoy	Net profit (Rs m)	EPS (Rs)	% Change yoy	PE (x)
2006	29,655	31.5	2,030	0.9	176.7	124.8
2007	43,664	47.2	5,033	1.9	107.1	60.3
2008E	67,117	53.7	8,006	3.0	56.5	38.5
2009E	89,964	34.0	9,311	3.5	16.3	33.1

Idea Cellular's (Idea) results were better than expected mainly on account of lower salary costs, lower depreciation and higher other income. The subscriber base grew by 15% qoq on average basis for the quarter and blended ARPU declined by 1.6% qoq. Revenues at Rs13.1b were higher than our Rs12.8b forecast due to higher level of ARPU. EBITDA margins expanded by 100bp qoq against our expectation of flat margins due to lower salary cost (5.2% of revenues – 6.6% in the previous quarter). Lower depreciation and higher other income at Rs326m (Rs109m in the previous quarter) boosted net profit to Rs1.9b (64% qoq). Though, the decline in salary cost (qoq) was explained due to certain one-time expenses in the previous quarter, there is lack of clarity on the lower depreciation reported by the company. We are building in the restated higher ARPU and raising our revenue forecast by 2% and 3.7% for FY08 and FY09 respectively, the lower depreciation has resulted in earnings revision of 5.6% and 8% for the two years. Consequently, our DCF-based target price has risen by 9.5% to Rs102. At 15.9x FY08 EBITDA and 12.8x FY09 EBITDA valuations remain expensive relative to Bharti and RCOM, we maintain Neutral rating.

KEY HIGHLIGHTS

□ Subscriber base grows by 15% qoq and ARPUs decline 1.6% qoq

Idea's subscriber base grew from 12.4m to 14m during the quarter. The company reported ARPU of Rs317 compared to Rs322 in the previous quarter, a decline of 1.6% qoq. The subscriber base grew 90% and ARPU declined 15% during FY07. During the year, Idea expanded its coverage to 4,432 population centers from 1,944 centers in FY06. It stated that by rolling out networks in all the circles, where it currently has license to operate, it would be able to cover 58% of the population.

Some Key metrics

- Subscriber base at 14m, prepaid subscriber base – 88.9%
- Postpaid churn - 4.2% (4.4% previous quarter) and prepaid churn – 4.2% (3.6% previous quarter)
- Blended APRU – Rs317 (Rs322 per quarter)
- Blended MOU – 387 minutes

- Revenue per minute – Rs0.82 (Rs0.87)
- Value-added services – 9% of revenues (9.2%)
- Employees – 5,532 (4,647)
- Cash and bank balances – Rs18b
- Total debt – Rs42.5b
- Capital expenditure – Rs28.9b in FY07 (US\$2b guided over the next two years)

□ **EBITDA margins increase by 100bp to 33.3%.**

Idea is rolling out its service in the 'new' circles of Himachal Pradesh, Uttar Pradesh (E) and Rajasthan. Hence, its network operating rose by 19% qoq to 12.8% of revenues. The EBITDA margins in its 'established' circles including Delhi, Maharashtra, Gujarat, Andhra Pradesh, Madhya Pradesh, Haryana, Kerala and Uttar Pradesh (W) stood at 38.7% and showed an increase of just 70bp over the same quarter last year. Idea's salary costs declined by 9.8% qoq as there were one-time expenses including leave encashment and additional flexible pay incurred in the previous quarter. Thus, salary costs declined from 6.6% of revenues to 5.2%. This aided EBITDA margin expansion of 100bp. Idea incurred losses of Rs330m at the operating level in its 'new' circle operations.

□ **PAT rises 64% qoq due to margin expansion, lower depreciation and higher other income**

Idea's EBITDA margins expanded by 100bp due to lower salary costs, thus EBITDA grew by 17.8% qoq but net profit grew by 64% qoq. Idea's depreciation and amortization charge decreased by 2.1% qoq and other income jumped to Rs326m compared to Rs109m in the previous quarter due to higher yield on the IPO money collected.

□ **Valuations and view**

Idea Cellular's (Idea) results were better than expected. While we expect the losses in its 'new' circle operations to increase as it expands coverage, the margin expansion in its 'established' circles has been lower than expected at just 20bp in FY07 over FY06 despite no tariff wars. Bharti's EBITDA margins for its mobile services have expanded by 100bp in 9MFY07. We expect margins to remain stable for the next couple of years due to continued roll out in new circles. Idea expects to launch services in Mumbai and Bihar circles by the end of 2007. It has applied for licenses in 12 other circles. We expect Idea's subscriber base to reach 30.5m by FY09 from the current 14m. We are raising our revenue forecast by 2% and 3.7% for FY08 and FY09 respectively, but the lower depreciation has resulted in earnings revision of 5.6% and 8% for the two years. Consequently, our DCF-based target price has risen by 9.5% to Rs102. At 15.9x FY08 EBITDA and 12.8x FY09 EBITDA valuations remain expensive relative to Bharti and RCOM, we maintain Neutral rating.

Quarterly results

Year to 31 March (Rs m)	Q4FY06	Q4FY07	FY07	FY08E
Income	8,557	13,084	43,664	67,117
Personnel expenses	489	685	2,598	3,557
Network operating expenses	813	1,680	5,279	8,741
License fees and WPC charges	842	1,411	4,487	7,249
Interconnect cost	1,355	2,203	7,287	11,074
SG&A	1,850	2,743	9,325	14,095
EBITDA	3,193	4,363	14,637	22,401
Depreciation and amortization	1,310	1,761	6,718	10,222
Net finance cost	790	975	3,291	4,160
Other income	102	326	465	150
PBT	1,194	1,953	5,093	8,169
Tax	26	19	60	163
PAT	1,168	1,934	5,033	8,006
Operating ratios (%)				
EBITDA margin	37.3	33.3	33.5	33.4
PAT margin	13.6	14.8	11.5	11.9
yoy growth (%)				
Income		52.9	47.2	53.7
EBITDA		36.7	37.1	53.0
PAT		65.6	137.7	59.1

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2. Neutral: Within 0-10% to Index
3. Underperformer: Less than 10% to Index

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