

Reliance Communication

Performance highlights

(₹ cr)	3QFY11	2QFY11	% chg(qoq)	3QFY11E	% Var
Net sales	4,865	5,023	(3.1)	5,301	(8.2)
EBITDA	1,529	1,564	(2.3)	1,665	(8.1)
EBITDA margin (%)	31.4	31.1	30bp	31.4	68bp
PAT	480	446	7.7	311	54.4

Source: Company, Angel Research

Poor revenue growth due to mixed KPIs in the wireless business: For 3QFY2011, RCOM reported consolidated revenue of ₹4,865cr, down 3.1% qoq. The decline was on the back of mixed KPIs in the wireless business. The wireless business witnessed a 2.3% decline in revenue to ₹4,064cr. This poor performance was on the back of MOU tumbling to 251mins (v/s 276mins in 2QFY2011); the decline in MOU was arrested to a great extent by robust subscriber growth of 7.1% qoq and held-up ARPM at ₹0.44/min. Thus, ARPU slipped by 8.8% qoq to ₹111 in 3QFY2011 from ₹122 in 2QFY2011.

EBITDA margin improvement: Overall EBITDA margin improved marginally by 30bp qoq to 31.4% due to better operational performance in its global business segment supporting the positive impact of held-up EPM in the wireless business.

Outlook and valuation: Going forward, we expect ARPM as well as MOU to stabilise. The GSM rollout is majorly completed and we expect it to aid the company's margins, as network operating expenditure would decline going forward. In addition to this, stabilising ARPM would aid margins. We expect RCOM's mobile business to report a 21% CAGR in its subscriber base over FY2010–12E and ARPM as well as MOU to stabilise going forward. **We recommend Neutral rating on the stock with a fair value of ₹106, valuing the stock at 6.1x FY2012E EV/EBITDA.**

Key financials (Consolidated, Indian GAAP)

Y/E March (₹ cr)	FY2009	FY2010	FY2011E	FY2012E
Net sales	22,242	21,614	21,126	23,101
% chg	18.1	(2.8)	(2.3)	9.3
Net profit	5,926	4,741	2,205	1,885
% chg	44.6	(20.0)	(53.5)	(14.5)
EBITDA margin (%)	38.6	33.5	33.9	33.7
EPS (₹)	24.4	23.0	10.4	9.1
P/E (x)	4.0	4.2	9.4	10.7
P/BV (x)	0.5	0.5	0.4	0.4
RoE (%)	16.6	11.1	5.0	4.1
RoCE (%)	6.7	22.8	20.7	20.5
EV/Sales (x)	2.6	2.3	2.4	2.0
EV/EBITDA (x)	6.7	6.8	7.0	5.9

Source: Company, Angel Research

NEUTRAL

CMP	₹97
Target Price	-

Investment Period	-
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Stock Info	
Sector	Telecom
Market Cap (₹ cr)	20,103
Beta	1.2
52 Week High / Low	205/90
Avg. Daily Volume	1550881
Face Value (₹)	5
BSE Sensex	18,202
Nifty	5,456
Reuters Code	RLCM.BO
Bloomberg Code	RCOM@IN

Shareholding Pattern (%)	
Promoters	67.9
MF / Banks / Indian FIs	9.1
FII / NRIs / OCBs	8.4
Indian Public / Others	14.6

Abs. (%)	3m	1yr	3yr
Sensex	(9.7)	12.7	0.5
Reliance Comm.	(42.7)	(42.5)	(528.0)

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Exhibit 1: 3QFY2011 – Financial performance (Consolidated, Indian GAAP)

(₹ cr)	3QFY11	2QFY11	% chg(qoq)	3QFY10	% chg (yoy)	9MFY11	9MFY10	% chg (yoy)
Net revenue	4,865	5,023	(3.1)	5,284	(7.9)	14,956	16,623	(10.0)
Operating Expenditure	3,336	3,459	(3.5)	3,497	(4.6)	10,272	10,873	(5.5)
EBITDA	1,529	1,564	(2.3)	1,786	(14.4)	4,684	5,750	(18.5)
Depreciation & Amortisation	1,034	955	8.2	833	24.1	2,954	2,662	11.0
EBIT	495	609	(18.7)	953	(48.1)	1,731	3,088	(44.0)
Interest Charges	130	280	(53.7)	(408)	(131.8)	849	(373)	(327.7)
Provision for business restructuring	-	-		22		-	36	
Other Income	139	95		26		275	535	
PBT	505	425	18.9	1,365	(63.0)	1,157	3,960	(70.8)
Income Tax	(21)	(66)	(67.7)	200	(110.7)	(159)	253	(163.0)
PAT	526	491	7.2	1,165	(54.8)	1,316	3,707	(64.5)
Share in earnings of associate	0	-		56		1	2	
Minority Interest	45	44.7		0.8		138.2	219.7	
Adj PAT	480	446	7.7	1,108	(56.7)	1,177	3,485	(66.2)
EPS	2.3	2.2	78.2	5.4	(56.6)	5.7	16.9	(66.2)
EBITDA margin (%)	31.4	31.1	30bp	33.8	(240)bp	31.3	34.6	(330)bp
EBIT margin (%)	10.2	12.1	(190)bp	18.0	(780)bp	11.6	18.6	(700)bp
PAT margin (%)	9.9	8.9	100bp	21.0	(1110)bp	7.9	21.0	(1310)bp

Source: Company, Angel Research

Poor revenue growth due to mixed KPIs in the wireless business

For 3QFY2011, RCOM reported consolidated revenue of ₹4,865cr, down 3.1% qoq. The flattish revenue growth was due to mixed KPIs in the wireless business.

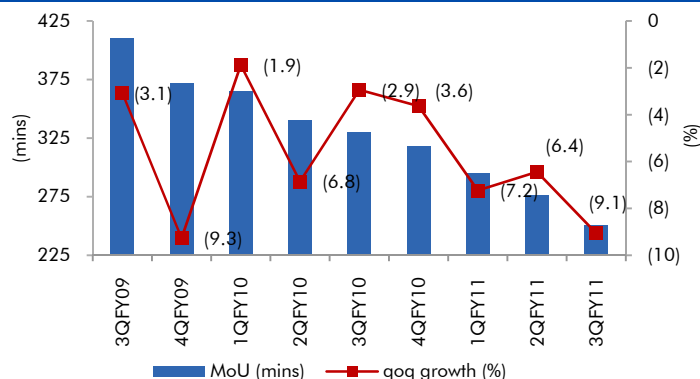
Exhibit 2: Revenue break-up (Business segment wise)

Business segment (₹ cr)	3QFY11	2QFY11	% chg (qoq)	3QFY10	% chg (yoy)
Wireless	4,064	4,161	(2.3)	4,023	1.0
Global	1,923	1,839	4.6	1,982	(3.0)
Broadband	618	662	(6.5)	705	(12.2)
Others	311	303	2.5	290	7.2
Eliminations	1,913	1,942	(1.5)	1,715	11.5
Net revenue	5,004	5,023	(0.4)	5,284	(5.3)

Source: Company, Angel Research

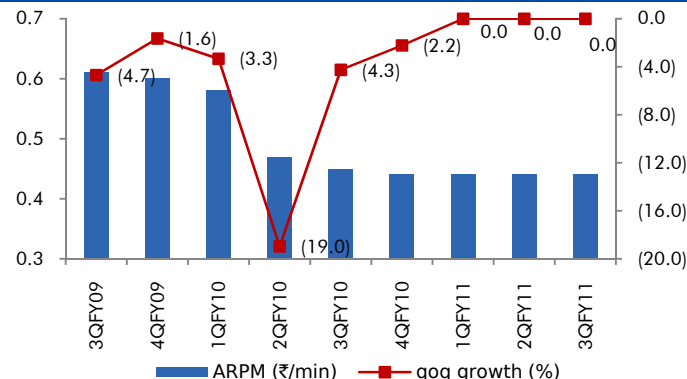
Wireless: The wireless business registered a 2.3% decline in revenue to ₹4,064cr. This poor performance was on the back of MOU tumbling to 251mins (v/s 276mins in 2QFY2011). The MOU decline was arrested to a great extent by robust subscriber growth of 7.1% qoq and held-up ARPM at ₹0.44/min. Thus, ARPU slipped by 8.8% qoq to ₹111 in 3QFY2011 from ₹122 in 2QFY2011.

Exhibit 3: Trend in MOU (qoq)



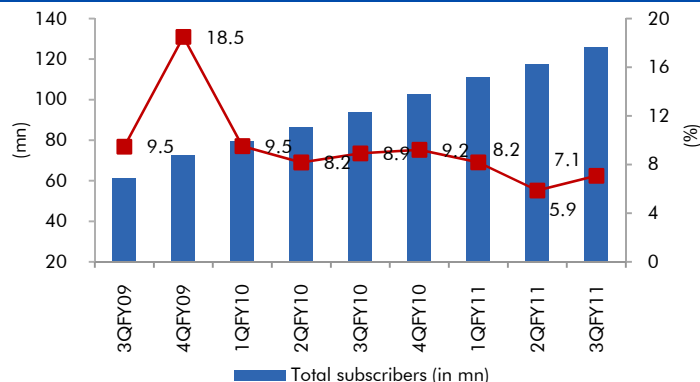
Source: Company, Angel Research

Exhibit 4: Trend in ARPM (qoq)



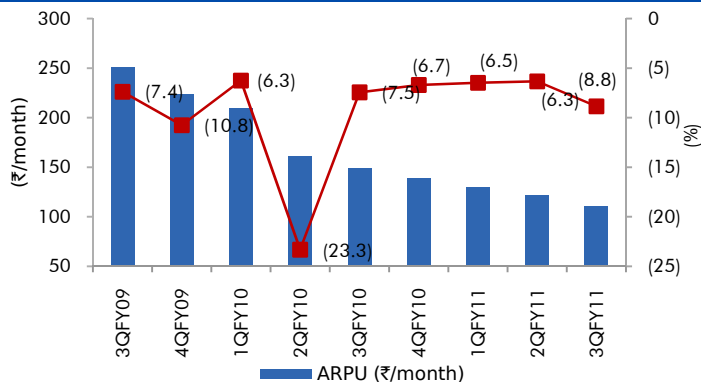
Source: Company, Angel Research

Exhibit 5: Trend in subscriber additions (qoq)



Source: Company, Angel Research

Exhibit 6: Trend in ARPU (qoq)



Source: Company, Angel Research

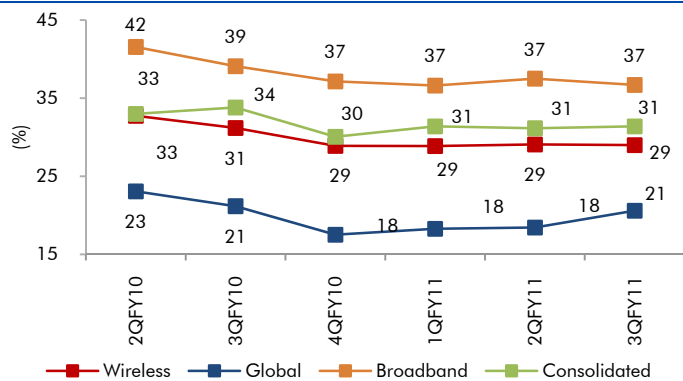
Global: The global business witnessed muted revenue growth of 4.6% qoq to ₹1,923cr, driven by decent qoq growth in ILD as well as NLD minutes of 8.8% and 1.1%, respectively. This was primarily because of a steep drop in realisations in each of the verticals.

Broadband: Revenue of the broadband business declined by 6.5% qoq to ₹618cr on the back of a 7.8% qoq fall in ARLP to ₹1,377, overshadowing the effect of healthy net additions of 26,000 lines in 3QFY2011.

EBITDA margin improvement

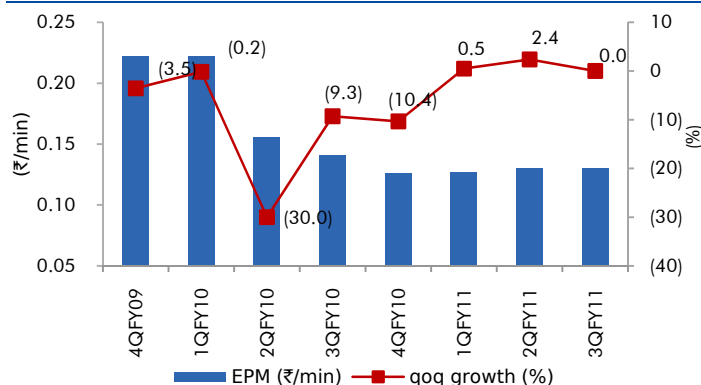
Overall EBITDA margin improved marginally by 30bp qoq to 31.4% due to better operational performance in its global business segment supporting the positive impact of held-up EPM in the wireless business.

Exhibit 7: Segment-wise EBITDA margin trend (qoq)



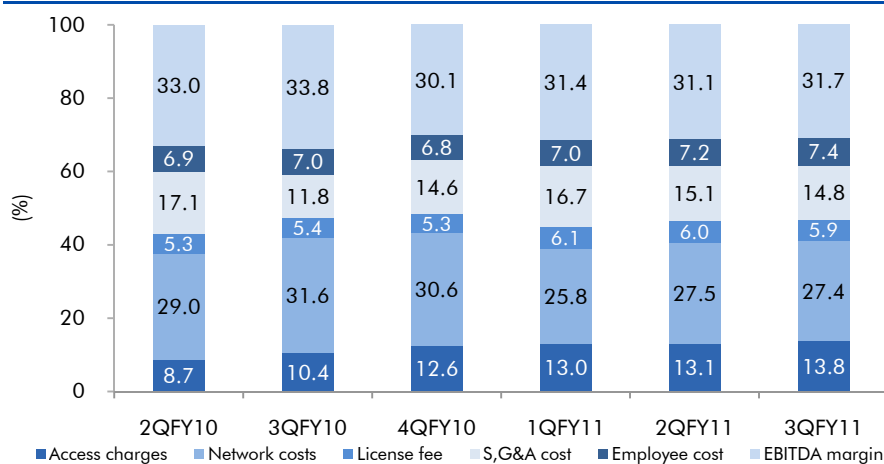
Source: Company, Angel Research

Exhibit 8: Trend in EPM (qoq)



Source: Company, Angel Research

Exhibit 9: Opex break-up



Source: Company, Angel Research

Recommendation rationale

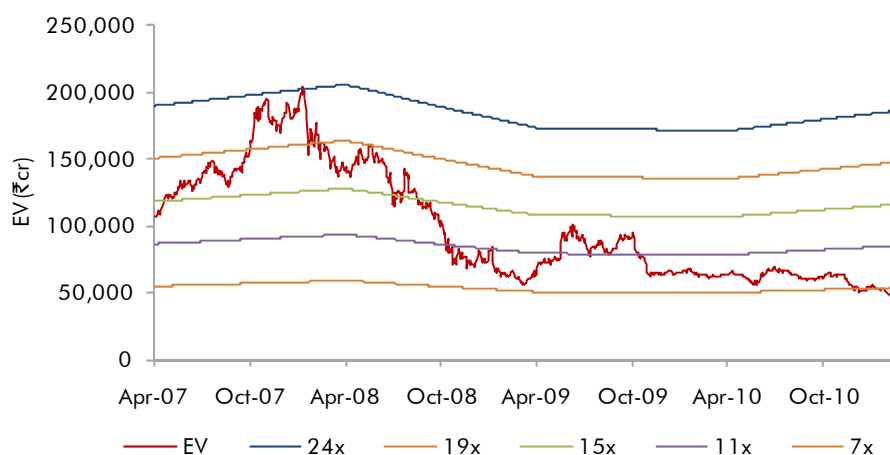
Stabilising ARPM and completion of GSM rollout: To aid margins

ARPM is now stabilising with the company managing to hold it up to ₹0.44/min in 3QFY2011. Also, most of the expenses related to the GSM rollout are through, which is further expected to accrue in margins going forward as promotion cost will settle down at current levels and network operating expenditure will likely decline. Hence, we expect margins to improve, expanding to 33.9% and 33.7% in FY2011E and FY2012E, respectively.

Outlook and valuation

We expect RCOM's mobile business to record a 21% CAGR in its subscriber base over FY2010–12E and ARPM as well as MOU to stabilise going forward. We recommend a Neutral rating on the stock with a fair value of ₹106, valuing the stock at 6.1x FY2012E EV/EBITDA.

Exhibit 10: One-year forward EV/EBITDA



Source: Company, Angel Research

Exhibit 11: Valuation

(₹ cr)	FY2012E
EBITDA	7,776
Target EV/EBITDA (x)	6.1
Target EV	47,434
Debt	30,300
Cash	4,727
Target mcap	21,861
Fair value (₹)	106

Source: Company, Angel Research

Exhibit 12: Change in estimates

Parameter (₹ cr)	FY2011E			FY2012E		
	Earlier estimates	Revised estimates	Variation (%)	Earlier estimates	Revised estimates	Variation (%)
Net revenue	20,861	21,126	1.3	23,131	23,101	(0.1)
EBITDA	6,654	7,166	7.7	7,695	7,776	1.1
Other income	276	345	25.0	200	200	-
PBT	1,581	2,315	46.4	2,354	2,435	3.5
Tax	(15)	(79)	425.3	330	341	3.3
PAT	1,426	2,205	54.7	1,822	1,885	3.5

Source: Company, Angel Research

Profit and loss account (Consolidated, Indian GAAP)

Y/E March (₹ cr)	FY2009	FY2010	FY2011E	FY2012E
Net sales	22,242	21,614	21,126	23,101
Network expenditure	4,364	6,173	5,467	5,917
<i>% of net sales</i>	19.6	28.6	25.9	25.6
License fee	1,187	1,145	1,232	1,402
<i>% of net sales</i>	5.3	5.3	5.8	6.1
Access charges	2,382	2,138	2,684	2,928
<i>% of net sales</i>	10.7	9.9	12.7	12.7
Other expenses	5,718	4,907	4,577	5,078
Total expenditure	13,650	14,363	13,960	15,325
<i>% of net sales</i>	61.4	66.5	66.1	66.3
EBITDA	8,592	7,250	7,166	7,776
<i>% of net sales</i>	38.6	33.5	33.9	33.7
Depreciation and amortisation	3,931	3,747	4,065	4,480
EBIT	4,661	3,504	3,101	3,296
Interest charges	(787)	(1,186)	1,132	1,061
Other Income, net	706	636	345	200
Profit Before Tax	6,154	5,326	2,315	2,435
Provision for Tax	(12)	445	(79)	341
<i>% of PBT</i>	(0.2)	8.4	(3.4)	14.0
PAT	6,166	4,880	2,394	2,094
Share in earnings of associate	2	(2)	0	-
Minority interest	242	137	188	209
Profit after minority interest	5,926	4,741	2,205	1,885
Fully diluted EPS (₹)	24.4	23.0	10.4	9.1

Balance sheet (Consolidated, Indian GAAP)

Y/E March (₹ cr)	FY2009	FY2010	FY2011E	FY2012E
Liabilities				
Share Capital	1,032	1,032	1,032	1,032
Reserves & Surplus	41,248	42,329	44,330	46,010
Total shareholders' funds	42,280	43,361	45,362	47,042
Minority Interest	655	658	760	800
Secured loans	3,000	3,000	3,000	3,000
Unsecured loans	36,162	26,715	29,300	27,300
Total Debt	39,162	29,715	32,300	30,300
Deferred Tax liability	28	99	99	99
Total Liabilities	82,126	73,834	78,521	78,241
Assets				
Gross Block - Fixed Assets	75,510	78,665	90,665	94,165
Accumulated Depreciation	14,114	19,067	23,132	27,612
Net Block	61,396	59,598	67,533	66,553
Capital Work-in-Progress	11,310	11,656	11,500	10,500
Goodwill	5,222	4,998	5,000	5,000
Investments	9,566	4,160	120	120
Current Assets				
Inventories	543	545	550	545
Sundry debtors	3,962	3,312	3,473	3,797
Cash and cash equivalents	1,683	819	2,347	4,727
Other Current Assets	1,771	2,073	1,818	2,176
Loans & Advances	6,756	5,410	5,282	5,775
Total Current Assets	14,714	12,157	13,469	17,021
Less:- Current Liab	15,972	14,708	15,298	16,794
Less:-Provisions	4,110	4,027	3,803	4,158
Net Current Assets	(5,367)	(6,578)	(5,632)	(3,932)
Total Assets	82,126	73,834	78,521	78,241

Cash flow statement (Consolidated, Indian GAAP)

Y/E March (₹ cr)	FY2009	FY2010	FY2011E	FY2012E
Pre-tax profit from operations	5,447	4,690	1,970	2,235
Depreciation	3,931	3,747	4,065	4,480
Pre tax cash from operations	9,379	8,436	6,035	6,715
Minority interest	240	139	188	209
Other income/prior period ad	706	636	345	200
Net cash from operations	9,845	8,933	6,192	6,706
Tax	12	(445)	79	(341)
Cash profits	9,858	8,488	6,271	6,365
(Inc)/Dec in				
Current assets	(3,328)	1,693	216	(1,171)
Current liabilities	4	(1,346)	366	1,851
Net trade working capital	(3,324)	347	582	680
Cashflow from operating activities	6,533	8,834	6,853	7,045
(Inc)/Dec in fixed assets	(24,324)	(2,295)	(11,844)	(2,500)
(Inc)/Dec in intangibles	(1,656)	224	(2)	-
(Inc)/Dec in deferred tax liability	(75)	71	(0)	-
(Inc)/Dec in investments	1,434	5,406	4,040	-
Cashflow from investing activities	(24,621)	3,406	(7,807)	(2,500)
Inc/(Dec) in debt	13,341	(9,447)	2,585	(2,000)
Inc/(Dec) in minority interest	(1,776)	3	102	40
Inc/(Dec) in equity/premium	7,521	(3,456)	(0)	-
Dividends	193	205	205	205
Cashflow from financing activities	18,892	(13,104)	2,482	(2,165)
Cash generated/(utilised)	805	(864)	1,528	2,381
Cash at start of the year	878	1,683	819	2,347
Cash at end of the year	1,683	819	2,347	4,727

Key ratios

Y/E March	FY2009	FY2010	FY2011E	FY2012E
Valuation ratio (x)				
P/E (on FDEPS)	4.0	4.2	9.4	10.7
P/CEPS	2.0	2.4	3.2	3.2
P/BVPS	0.5	0.5	0.4	0.4
Dividend yield	1.0%	1.0%	1.0%	1.0%
EV/Sales	2.6	2.3	2.4	2.0
EV/EBITDA	6.7	6.8	7.0	5.9
EV/Total assets	0.7	0.7	0.6	0.6
Per share data (₹)				
EPS	24.4	23.0	10.4	9.1
Cash EPS	47.8	41.1	30.4	30.8
Dividend	0.9	1.0	1.0	1.0
Book value	204.8	210.1	219.8	227.9
Dupont analysis				
Tax retention ratio (PAT/PBT)	1.0	0.9	1.0	0.8
Cost of debt (PBT/EBIT)	1.3	1.5	0.7	0.7
EBIT margin (EBIT/Sales)	0.2	0.2	0.1	0.1
Asset turnover ratio (Sales/Assets)	0.3	0.3	0.3	0.3
Leverage ratio (Assets/Equity)	1.9	1.7	1.7	1.7
Operating ROE	14.0	10.9	4.9	4.0
Return ratios (%)				
RoCE (pre-tax)	6.7	22.8	20.7	20.5
Angel RoIC	8.0	5.0	4.3	4.4
RoE	16.6	11.1	5.0	4.1
Turnover ratios (x)				
Asset turnover (fixed assets)	0.3	0.3	0.3	0.3
Receivables days	55	61	59	57
Payable days	422	390	392	382

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Disclosure of Interest Statement

Reliance Communication

1. Analyst ownership of the stock	No
2. Angel and its Group companies ownership of the stock	Yes
3. Angel and its Group companies' Directors ownership of the stock	No
4. Broking relationship with company covered	No

Note: We have not considered any Exposure below ₹1 lakh for Angel, its Group companies and Directors

Ratings (Returns):

Buy (> 15%)

Reduce (-5% to 15%)

Accumulate (5% to 15%)

Sell (< -15%)

Neutral (-5 to 5%)