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REDUCE

NOMURA SINGAPORE LTD., SINGAPORE

RESULTS FIRST LOOK

A mixed 4Q, with accounting policy changes clouding underlying financial performance. Adjusted for one-time impact of accounting changes, total revenues grew 7% q-q, but EBITDA was down 5% on our estimates. Core wireless trends were below peers - revenue grew 3% q-q (vs ~4% for Bharti), but EBITDA was down 3% (vs 1% for Bharti) as margins fell 160bps to 27%. It is still transitioning from free minutes, with limited evidence of being a beneficiary of MNP/3G so far. Preliminary FY12F capex of INR15bn appears conservative and efforts are on to reduce net debt to EBITDA from ~4.9x now.

Price target: 120.0 INR

Price (30 May 2011): 87.55 INR

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More benefits from accounting changes, less from MNP/3G

- **Earnings vs. our Forecast:** **BELOW**

Likely Impact:

- **Earnings Estimates:** **NO CHANGE**
- **Dividend Estimates:** **NO CHANGE**
- **Price Target:** **NO CHANGE**
- **Long-term View:** **CONFIRMED**

ABOVE OR BELOW EXPECTATIONS? Underlying NPAT of INR2bn (adjusted for change in accounting policy) was below consensus expectations.

WHAT DOES THE RESULT MEAN?

- For 4Q, wireless trends were still below peers. Wireless revenue grew 3% q-q (vs 4% for Bharti), but EBITDA declined 3% (vs Bharti down 1% q-q) with a margin decline of 160bps to 27%. RCOM attributes this to higher subscriber acquisition efforts in this quarter. MNP, we understand, has not been a significant driver of gross adds, although RCOM maintains that postpaid/high-end prepaid still remains an opportunity. ARPUs and MoUs declined by 4% q-q each, but RPMs held steady at 44paisa, in line with its initiative of rationalizing on free minutes, which could be completed in another 2 quarters. It currently has 1.7mn 3G subscribers and around 9K towers are now 3G 'lit' (i.e., 20% of its 50K portfolio).

- Consolidated numbers were distorted given the impact of a change in accounting policy – i.e. in the Global (submarine cable) segment, RCOM has changed its revenue recognition to 'on activation of circuits' from 'straight line basis over the life of the contract'. Therefore revenue/ EBITDA/ depreciation on a consolidated basis were higher by around INR25bn each for the full year, with the full impact of this accounting change reflected in 4Q numbers. It is not clear to us as to what drove this change in policy, and this impact is expected to be one-time. Trends in the Global segment are expected to return to 'normal' in FY12.

- *Preliminarily* reversing the impact of accounting changes from 4Q numbers, underlying total revenues appear to have grown by 6.5% q-q in 4Q, helped by wireless and broadband, although EBITDA appears to have declined by 5% q-q with margins of 30%, on our estimates.

- Broadband trends were also mixed – revenue growth of 12% q-q was one of the strongest in several quarters, but margins declined 390bps q-q.

- For FY11, RCOM spent INR43bn in capex, including 3G (INR30bn guidance not including 3G). 3G capex is yet to be capitalized, and this will occur in FY12 – and hence the D&A impact from this will also kick in from FY12.

- Balance sheet gearing stood at 4.9x and RCOM is continuing to target gearing below 3x.

ANY CHANGE TO GUIDANCE? Preliminary capex is expected to be at INR15bn for FY12, which seems conservative to us.

LIKELY STOCK REACTION: Flattish.

CONFERENCE CALL TAKEAWAYS:

- RCOM has rolled out 3G in all the 13 circles in which the company has licenses (330 towns). The company now has 1.7mn 3G customers and ~9K towers. RCOM will look at uptake of 3G in smaller Towns before deciding on further investments.
- After 'realigning its products' or rather rebalancing its free minutes, RCOM intends to be focussed on both MoU growth and defending RPMs as its strategy in wireless. For the industry, management thinks that the decline in tariffs is behind and sees sustained levels of RPM going forward. Management feels that industry could consolidate to 5-6 players in the next 18-24 months.
- Capex guidance for the next year is at INR15bn and will be funded with internally generated cash. The company believes that high capex. investments are behind them and will continue to focus on data growth. RCOM targets to bring down the net debt/EBITDA ratio to sub-3 levels
- On MNP, management does not see it as a significant driver for gross adds or churn. The company will focus on postpaid and high-end prepaid segments and remain value driven.
- RCOM has taken actions on debt management to manage its high cost rupee loans. So far they have drawn INR 60bn from China Development bank for refinancing its ST rupee loan for 3G expenses.
- In its enterprise segment, RCOM has data centres spanning 450k sq feet in India; also has 9 data centres outside India.
- Management clarified that Hawk submarine system will be operational this quarter.

Valuation Methodology and Investment Risks: Our DCF-based price target of Rs120 is driven by a WACC of 10.9% and a terminal growth rate of 3%. Key upside risks to our investment view include lessening competitive activity and potential M&A transactions.

Note: Ratings and Price Targets are as of the date of the most recently published report (http://www.nomura.com/research) rather than the date of this email.

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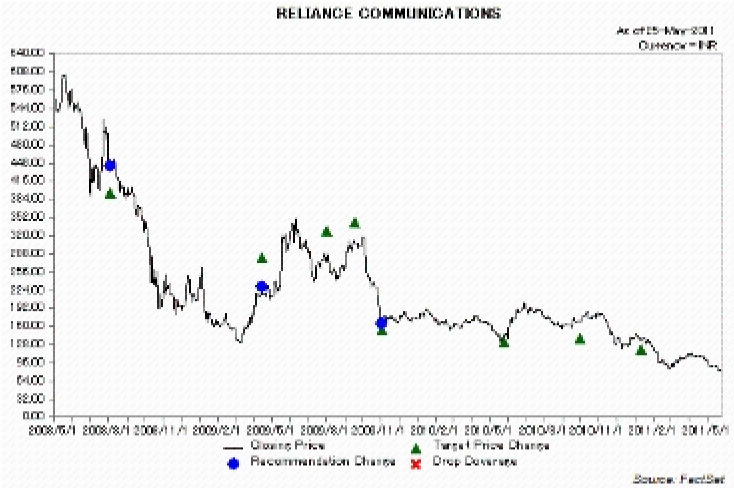
Issuer name	Ticker	Price	Price date	Stock rating	Disclosures
Reliance Communications	RCOM IN	87.55 INR	30 May 2011	Reduce	

Previous Rating

Issuer name	Previous Rating	Date of change
Reliance Communications	Buy	03 Nov 2009

Reliance Communications (RCOM IN) **87.55 INR (30 May 2011)** Reduce

Rating and target price chart (three year history)



Date	Rating	Target price	Closing price
11-Jan-2011		120.00	137.80
30-Sep-2010		140.00	168.25
26-May-2010		132.00	135.00
03-Nov-2009		154.00	165.90
03-Nov-2009	Reduce		165.90
18-Sep-2009		344.00	306.60
03-Aug-2009		329.00	289.90
15-Apr-2009		282.00	230.05
15-Apr-2009	Buy		230.05
05-Aug-2008		395.00	442.25
05-Aug-2008	Reduce		442.25

For explanation of ratings refer to the stock rating keys located after chart(s)

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