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Q4 FY07
Result Update

Reliance Communication

Outperformer

Rs 477

May 3, 2007

In Line

Company Details				Result Snapshot
Market Cap:	Rs 1,029,582m			
52-Week High/Low:	Rs 518 / 186			
Bloomberg Code:	RCOM@IN			
Reuters Code:	RLCM.BO / NS			
Shares O/s fully diluted:	2,158m			
Average Volume (3 months):	8.5m			
Price Performance				
(%)	1m	3m	12m	
Absolute	13.6	3.5	49.1	
Relative to Sensex	7.5	5.0	33.9	

Reliance Communications reported a 5% qoq rise in revenue to Rs 39.4bn, while the 80-bp margin expansion resulted in a 7% rise in EBITDA and 10.1% in PAT. In the verification process it switched off 5.6m subscribers but this did not hit revenue or profitability, as the de-activated customers had not generated any material revenue in Q3 FY07.

For FY07, revenue rose 35% to Rs 144.6bn, following a 39% jump in the subscriber base to 28m, while the OPM expansion of 1,600bp due to volumes led to a 125% growth in EBITDA and a 443% rise in PAT to Rs 31.6bn.

With accelerated capex plans for its CDMA and GSM networks (the present circles) and wider geographical coverage, the company is confident of reviving the growth rate in net additions. It is striving to maintain a 21-22% market share of incremental net additions in the next 12 months.

At the CMP, the stock trades at 23.5x FY08E earnings, which are expected to grow at 38% yoy on the back of a 75% yoy growth in the (truncated) subscriber base. We believe that the superior growth rates in the broader markets would be maintained, and rate the stock an **Outperformer**.

Q4 FY07 Result Overview

(Rs m)

Y/e March	Q4 FY07	Q4 FY06	YoY Gr. (%)	Q3 FY07	FY06	FY07	YoY Gr. (%)
Net Sales	39,369	29,700	32.6	37,553	107,664	144,683	34.4
Access Charges, License Fees	9,978	10,290	(3.0)	9,491	40,404	37,823	(6.4)
Network Opns Cost	4,424	3,350	32.1	4,165	15,346	16,738	9.1
Employee Cost	2,452	1,820	34.7	2,200	8,394	9,080	8.2
SG&A Expenses	6,164	3,820		6,426	18,167	23,833	
Total Expenditure	23,018	19,280	19.4	22,281	82,311	87,473	6.3
EBITDA	16,351	10,420	56.9	15,272	25,353	57,210	125.7
Margin (%)	41.5	35.1		40.7	23.5	39.5	
Other Income	-	-		-	1,391	-	
Depreciation	6,378	5,460	16.8	6,524	16,987	24,654	45.1
EBIT	9,973	4,960	101.1	8,747	9,757	32,557	233.7
Interest	(391)	420	(193.1)	(657)	3,215	7	(99.8)
PBT	10,364	4,540	128.3	9,404	6,542	32,549	397.5
Unusual or Infrequent Items	(27)	370		30	374	303	
PBT - Adjusted	10,391	4,170	149.2	9,374	6,168	32,246	422.8
Taxes	148	140	5.7	130	337	609	80.4
ETR (%)	1.4	3.4		1.4	5.5	1.9	
PAT	10,243	4,030	154.2	9,244	5,831	31,638	442.6

(Stock price as on April 30, 2007)



Highlights

Wireless

Wireless continued to lead growth in FY07, with 46% yoy revenue growth contributing 74% of the overall revenue and 70% to EBITDA. The subscriber base addition at 67% yoy (assuming 5.6m retained customers) was muted, compared to peers such as Bharti as further capex was delayed in the CDMA network. The EBITDA margin traction was on expected lines because of higher capacity utilisation of the present network with the EBITDA/min expanding to Rs 0.28 from Rs 0.26 in FY06.

Mobility Services

(Rs m)

Particulars	Q4 FY07	Q3 FY07	QoQ Gr (%)	FY06	FY07
Net Revenue	20,673	19,308	7.1	73,640	107,276
EBITDA	11,511	10,293	11.8	10,341	39,844
<i>EBITDA / Revenue (%)</i>	<i>38.8</i>	<i>37.4</i>		<i>36.4</i>	<i>37.1</i>
No. of Subscribers (m)	28.0	29.9	(6.7)	20.1	28.0
ARPU (Rs)	377	328	14.9	429	339
Traffic (m mins)	42,500	38,100	11.5	86,2147	143,786
<i>VAS as % of Mobile Revenue</i>	<i>6.3</i>	<i>6.3</i>		<i>6.2</i>	<i>6.3</i>

Source: Company Data, PL Research

Subscriber growth to pick up momentum

- Although the company plans to adopt the GSM platform as a long-term growth driver for its business depending on available spectrum, yet, not to miss any market opportunity, RComm has again begun investing in expanding the CDMA network and in widening population coverage. Against the \$500m invested in H1 FY07, it would invest almost \$900m on the wireless network in H2 FY07, primarily in CDMA as well as GSM in its present eight circles.

GSM - future plans

- RComm plans capex of \$450m in GSM, widening coverage and raising capacity three-fold. This would result in an additional 6m subscribers in the eight circles of the north-eastern states and Central India. By March 2008, in terms of net additions it expects to be on par with BSNL and Bharti in its present GSM circles.
- The other GSM expansion plans hinge on spectrum availability and allocation, which has been undecided for the past year. RComm had applied for spectrum in Feb.'06 and Jun.'06. Due to limited spectrum available, allocation (whenever it happens) might be decided on a "first-come first-served" basis but even that criterion has not been substantiated by anyone. The company expects a release of 20 MHz of spectrum by July 2007 in some parts of some circles.
- Overall, depending on spectrum allocation, in the next three or four years, it expects GSM to be the chief driver of subscriber growth and dominate the field, with 60% of its overall subscriber base in 2010.

GSM expansion; no impact on margins or competitiveness

- The company claims to have the lowest operating expense (opex) per subscriber, opex per minute and expects to maintain competitiveness regardless of investing in two technology platforms. It claims that the incremental opex in running both the platforms would not be substantial (\$12m-15m pa) as it would primarily entail higher fuel and power cost. Moreover, it has received attractive terms from equipment suppliers for its large GSM tender for its present expansion.

Passive infrastructure, unlocking value

Reliance Telecom Infrastructure, Ltd., was hived off in April 2007. Now with an arms-length relationship with the parent, it plans to unlock value for all its stakeholders through third-party rentals. With 20,000 new towers planned (capex \$1bn-1.2bn) as part of its widening coverage for its CDMA platform and expanding its GSM network, it would turn into a formidable player with 32,000 towers by end-FY08, next only to Bharti. As a first step, it is expected to raise resources based on its own balance-sheet strength. The parent plans to raise the money for expansion by divesting some (20-24%) of its holdings in the next two or three months.

Global

In Q4 FY07, revenue and margins were squeezed due to mounting competition on ILD volumes because of the aggressive launch of competing offers by peers, leading to a cut in tariffs. For the year, traction in volumes and higher capacity utilisation resulted in the OPM doubling to 24.8%, contributing 22% to the overall EBITDA.

Global Services

(Rs m)

Particulars	Q4 FY07	Q3 FY07	QoQ Gr (%)	FY06	FY07
Revenue	12,938	13,335	(3.7)	51,860	51,771
EBITDA	3,121	3,552	(12.1)	6,410	12,712
<i>EBITDA / Revenue (%)</i>	<i>24.1</i>	<i>26.6</i>	<i>-</i>	<i>12.4</i>	<i>24.8</i>

Source: Company Data, PL Research

FLAG, unlocking value through overseas listing

RComm plans capex of \$1.5bn for the N-G-N (next generation network) over the next three years, covering Asia, Africa, the Mediterranean and the Trans-Pacific markets. This project would make it the largest fully undersea cable-system operator, reaching 80% of the world's population, and would cater to the 50 largest telecoms markets (30 at present).

Funding is expected to be done by FLAG itself through the pre-sale agreements over capacity, through an IPO and through debt. The company expects data and storage needs would be the growth drivers. With tons of data transfer expected in entertainment content such as music and movies, the company expects a booming opportunity. It plans to list on overseas markets, diluting roughly a 24% stake. While it is very early to arrive at valuations, we expect it to report \$110m-120m in EBITDA in CY07. Further surprises could come in the form of some aggressive pre-sale agreements of NGN capacity.



Broadband

Broadband Services

(Rs m)

Particulars	Q4 FY07	Q3 FY07	QoQ Gr (%)	FY06	FY07
Revenue	3,299	3,161	4.3	5,130	11,442
EBITDA	1,611	1,486	8.4	770	5,192
<i>EBITDA / Revenue (%)</i>	<i>48.8</i>	<i>47.0</i>	-	<i>15.0</i>	<i>45.0</i>

Source: Company Data, PL Research

The enterprise market is \$1bn and growing at roughly 30%. RComm has a 50% market share in Internet Data Centre, 56% in Virtual Private Networks and 57% in Centrex Solutions. Broadband would help improve margins.

Capex plans and outlook

It plans to invest \$2.5bn in FY08; of this, \$400m would be on GSM networks, \$1.2bn on infrastructure and the rest on CDMA. The Q4 FY07 capex has picked up to almost \$600m (compared to \$400m in the previous quarter) due to the step-up in CDMA investments. The present D/E is only 0.2x.

Ahead, we expect a 33% CAGR in revenue, following a 55% rise in the number of subscribers, and 34% and 36% CAGRs in EBITDA and PAT respectively.

At the CMP of Rs 477, the stock trades at a P/E of 23.5x FY08E earnings and at an EV/EBIDTA of 12.6x FY08 estimates, based on the fully diluted equity. We retain an **Outperformer** rating on it.

Key Figures

Y/e March	FY06	FY07E	FY08E	FY09E
Revenues <i>(Rs m)</i>	107,664	144,683	178,824	240,070
EBITDA <i>(Rs m)</i>	25,353	57,210	79,911	100,107
<i>Margins (%)</i>	<i>23.5</i>	<i>39.5</i>	<i>40.7</i>	<i>41.7</i>
PAT <i>(Rs m)</i>	5,831	31,639	43,632	56,977
EPS <i>(Rs)</i>	2.9	14.7	20.2	26.4
PER <i>(x)</i>	167.3	32.5	23.5	18.1
EV / E <i>(x)</i>	41.1	18.4	12.6	10.0
EV / Sales <i>(x)</i>	9.7	7.3	5.1	4.0
<i>RoCE (%)</i>	<i>4.4</i>	<i>13.6</i>	<i>16.6</i>	<i>21.8</i>
<i>RoE (%)</i>	<i>5.0</i>	<i>18.5</i>	<i>18.6</i>	<i>21.1</i>

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