

TELECOM

MNP: Not a game changer, but margin dilutor

Mobile Number Portability (MNP) was rolled out in Haryana on November 25, 2010, and pan-India on January 20, 2011. In our earlier note, *MNP: Adding to operators' woes*, dated November 23, 2010, on the impact of MNP, we had indicated that market shares will not alter much, but margins could get impacted. Our analysis had indicated that Bharti Airtel's (Bharti) EBITDA would be eroded 3-10% just on account of revenue loss as customers 'down trade' on existing plans, without assuming any incremental cost for retaining customers. Our initial survey to ascertain the likely impact of MNP post its implementation leads us to believe that our early thesis has been ratified. We continue to believe that MNP may not be a game changer, as subscriber switching will be restricted between a few service providers, but it could impact margins as customers are offered more bang (minutes) for the buck.

■ New offers: Pay less for more

Bharti's and Vodafone Essar's (Vodafone) current offers in the Mumbai market seem to indicate that their postpaid ARPU could get diluted by about 35%. While Bharti is offering 15,000 seconds (250 minutes) talk time free for a rental of INR 249, Vodafone is offering 12,000 seconds (200 minutes). Idea Cellular (Idea), we believe, is the most aggressive, offering 400 minutes free talk time for a rental of INR 179 per month. It is interesting to note that Bharti is waiving off all charges (porting fee of INR 19, SIM card charge, and activation fee), while Idea is collecting INR 19 as porting fee and INR 99 for SIM card and activation. Our analysis indicates that an existing customer of Bharti and Vodafone will be able to maintain the outgoing talk time and yet spend 35% less with the new offers. This, we believe, could result in lower margins.

■ Corporate customers are price sensitive too

We surveyed three corporates, who together have close to 5,000 corporate connections with vendors like Vodafone, Bharti, and Tata Docomo. In Mumbai, we gather that Vodafone offers the best service and quality of network. Corporates seem reluctant to switch as there are limited options and, in any case, service providers match the best price offered in the market. Corporate customers lay emphasis on quality of network and billing and negotiate tariffs intermittently without any set lock-ins.

■ Edelweiss survey: Vodafone has 60% market share

An internal survey at Edelweiss Capital, primarily in Mumbai, revealed that 55% of those (82% with postpaid connections) surveyed indicated that they would switch operators once MNP is implemented. The most common reason behind the switch is perceived quality of network and high tariffs. Among the survey respondents, 60% had Vodafone connections.

■ Outlook: Margins at risk

The current offers indicate that the race for subscriber market share has been re-initiated and realisations are getting compromised. We maintain our cautious view on the sector as there are several uncertainties including the imminent new telecom policy and impact of MNP and 3G services. We maintain '**HOLD/SO**' on BHARTI, '**HOLD/SP**' on Idea, and '**REDUCE/SU**' on RCOM.

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■ Operators offering more bang for lower buck

As MNP was launched on January 20, 2011 pan-India, we visited the stores of Vodafone, Airtel, Idea, Reliance Communications (RCOM) and Tata Docomo to compare the schemes currently on offer, for postpaid customers. We restricted our study to postpaid schemes, as we believe this segment would be more sensitive to MNP and their revenue share is over 25% for operators. Vodafone is currently offering its existing subscribers a rental fee (INR 249 per month) waiver for two months, together with new plans. It is offering a plan with rental fee of INR 249 per month and free talk time of 12,000 seconds (200 minutes of local/domestic long distance). This, with a rental fee waiver for an existing subscriber, would impact Vodafone's ARPU and margins significantly. We estimate that Vodafone would earn 37% less ARPU than earlier, assuming MOU of the customer remains the same.

Bharti is offering a plan with rental fee of INR 249 and 15,000 seconds free talk time (250 minutes of local/domestic long distance). Surprisingly, Bharti is waiving off activation fee, SIM card charges as well as porting fees of INR 19. Idea is offering the most competitive plan in Mumbai for postpaid customers. It is currently offering 400 minutes free talk time for local calls, 200 minutes free talk time for domestic long distance calls for a monthly commitment of INR 179. Idea, though, is charging porting fees of INR 19 and activation fee of INR 99.

Table 1: Comparison of talk plans offered

	Idea	Bharti	Vodafone
Rental fees (INR/month)	179	249	249
Pulse rate	Minute	Second	Second
Free talk time – Local	400	15,000 (250 mins)	12,000 (200 mins)
Free talk time - Domestic long distance	200		
Local tariff (INR/minute)	0.5	0.6	0.6
Activation fees (INR)	99	0	0
Porting fees (INR)	19	0	0

Source: Company stores

Table 2: MNP impact - potential ARPU dilution due to the new talk plans on offer

		Bharti	Vodafone	Idea
Average GSM subscriber base for the industry in Mumbai for quarter ending Sep 2010 (mn)	(A)	18.4	18.4	18.4
Average proportion of postpaid GSM customer base in metros (%)	(B)	9.0	9.0	9.0
Average postpaid GSM subscriber base for the industry in Mumbai for quarter ending Sep 2010 (mn)	(C) = (A) * (B)	1.7	1.7	1.7
Assumed market share of GSM postpaid subscriber base in Mumbai for the individual operators (%)	(D)	25.0	50.0	5.0
Estimated postpaid subscriber base in Mumbai for individual operators (mn)	(E) = (C) * (D)	0.4	0.8	0.1
Average subscriber base in Mumbai for quarter ending Sep 2010 (mn)	(F)	3.2	5.4	1.8
Proportion of postpaid subscribers to total in Mumbai for the individual operators (%)	(G) = (E)/(F)	12.9	15.5	4.6
ARPU in Mumbai for the quarter ending Sep 2010 for individual operators (INR/month)	(H)	368	381	207
Current outgoing MOU of a postpaid customer in metros for the industry (minutes/month)	(I)	408	408	408
Current outgoing MOU of a prepaid customer in metros (minutes/month) for the industry	(J)	115	115	115
Ratio of outgoing MOU of a metro postpaid / prepaid customer for the industry	(K) = (I)/(J)	3.5	3.5	3.5
Calculated current ARPU in Mumbai of a postpaid subscriber for individual operators (INR)	(L)	982	970	658
Estimated current rental revenue in Mumbai of a postpaid subscriber (INR/month)	(M) = (L) * 31%	304	301	204
Current average postpaid revenue per outgoing minute in the metros for the industry (INR/minute)	(N)	1.08	1.08	1.08
Calculated average postpaid outgoing MOU (Minutes/month)	(O) = (L)/(N)	909	898	609
Fixed fee for postpaid currently on offer by individual operators (INR/month)	(P)	249	249	179
Free talktime being offered (minutes)	(Q)	250	300	400
Additional charged talk time assuming outgoing MOU of the postpaid customer remains the same as before (minutes)	(R) = (O) - (Q)	659	598	209
Rate per second on outgoing MOU currently on offer (INR)	(S)	0.01	0.01	0.01
Total call charges (INR/month)	(T) = (R) * (S)	396	359	104
Total ARPU (INR/month)	(U) = (P) + (T)	645	608	283
As % of existing ARPU from a postpaid customer in Mumbai	(V) = (U)/(L)	66	63	43

Source: TRAI, COAI, Company stores, Edelweiss research

In our initial analysis of the impact of MNP in our report (MNP: Adding to operators' woes, dated November 23, 2010), we had highlighted that although Bharti would not lose subscriber market share, its EBITDA could get impacted by 3-10%, as it would be able to retain customers at a lower 'negotiated pricing'. However, current plans on offer seem to suggest that Idea, as expected, is the most aggressive with monthly commitment from a postpaid customer being ~28% lower than Bharti and Vodafone, in Mumbai. Anecdotal

evidence (based on actions of colleagues, who have Loop, Vodafone, and Airtel in Edelweiss) seems to indicate that Idea plans are popular. This, in our view, could impact even the market share of incumbent operators.

Recent reports in the media, based on figures reported by the operators to DoT, indicate that although initial numbers are not significant, Idea seems to be the biggest gainer while Bharti seems to have seen no impact.

Table 3: Initial impact of MNP (Net subscriber gains/loss)

Operator	Net gainer from MNP
Idea	12,300
Vodafone	11,252
Bharti	94
Aircel	3,389
RCOM	(9,645)

Source: Business Standard

■ **Edelweiss survey: Vodafone has 60% market share**

We did an internal survey of Edelweiss employees to gauge subscriber preferences and, hence, the potential impact of MNP. The survey involved multiple choice questions pertaining to mobile usage, service issues and requirements. Nearly all the 300 respondents were from Mumbai and 82% were postpaid users. Majority use Vodafone (60%), followed by Airtel (22%), Loop Telecom (6%), and RCOM (6%). Around 55% of the survey respondents indicated that they would switch service providers post MNP. Given the fact that the user profile comprises largely high-end postpaid users, we think results of the survey provide some insights into the trends/requirements of the higher-end users relevant to MNP.

Chart 1: Mumbai – Nov '10 operator-wise subscribers

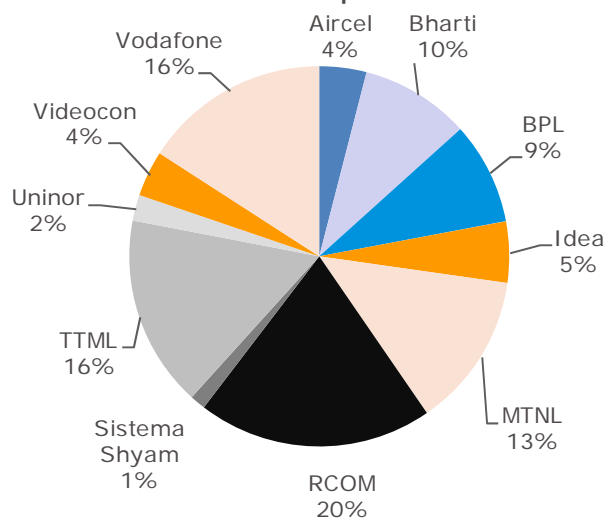
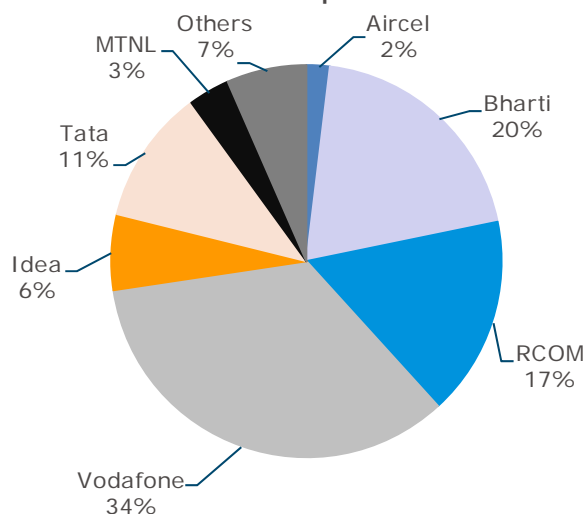
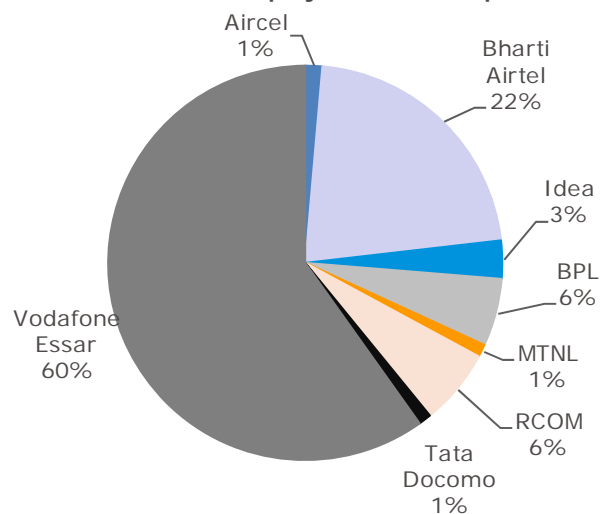
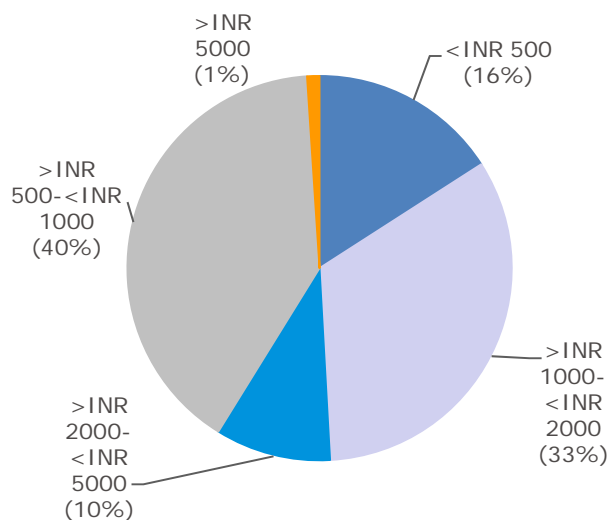


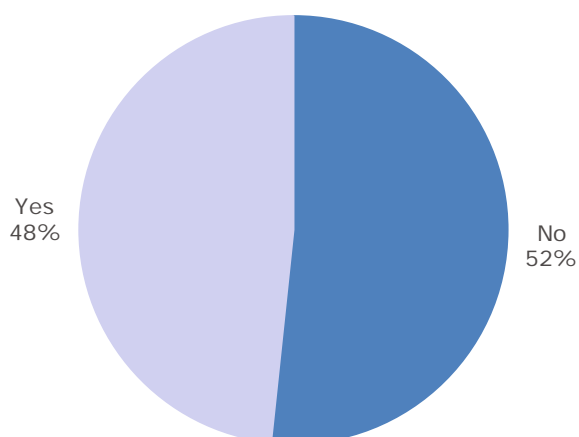
Chart 2: Mumbai – Q2FY11 operator-wise revenues



Source: TRAI

Chart 3: Edelweiss employees' current operator**Chart 4: ARPU of 84% users more than INR 500**

Source: Edelweiss research

Chart 5: 48% of the respondents owned >1 SIM

Source: Edelweiss research

Around 55% of the survey respondents indicated that they would switch service providers post MNP. Top reasons to switch operators were poor network quality (37%), high tariffs (25%) and poor quality of customer service (14%). As per TRAI data, industry postpaid tariff is ~80% higher than prepaid tariff – this could be a major cause for dissatisfaction among users, in our view.

Chart 6: 55% of respondents want to switch post MNP

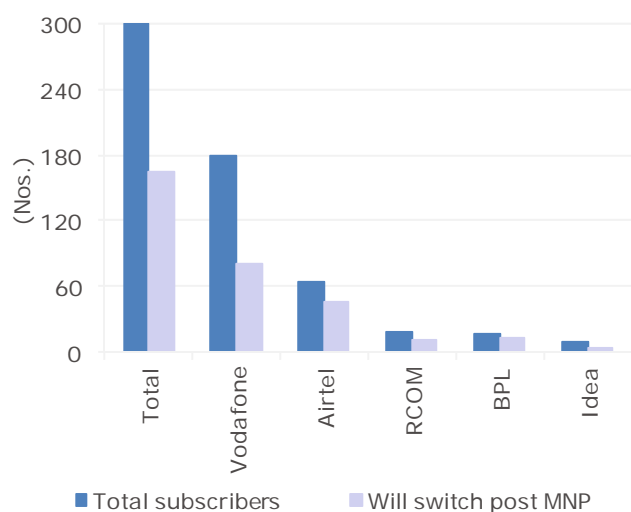
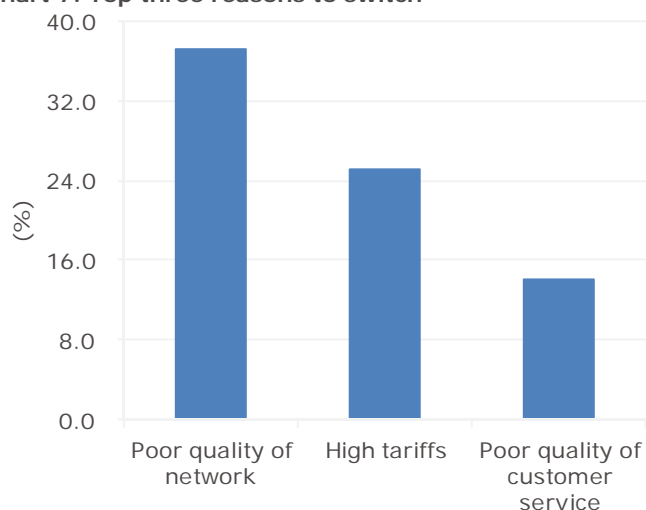


Chart 7: Top three reasons to switch



Source: Edelweiss research

We have further analysed the survey results for Vodafone and Airtel users, who comprised majority of our survey respondents. We believe these two operators command a high market share of the postpaid subscriber base in Mumbai. We highlight our key findings below:

Vodafone Essar (60% market share among respondents)

Vodafone is the third largest operator in Mumbai with a November 2010 subscriber market share of 16% and Q2FY11 revenue market share of 34%. Around 60% of our survey respondents are Vodafone users, of which, 91% are postpaid subscribers. High tariffs, followed by poor quality of network, emerged as top reasons for discontent among Vodafone users. Nearly 46% Vodafone users indicated that they would switch post MNP, citing: (1) higher tariffs (39%); (2) poor quality of network (33%); and (3) poor quality of customer service (14%) as the top three reasons. Bharti and Idea emerged as the top preferences to switch to, post MNP, among Vodafone users.

Chart 8: ARPU of 48% Vodafone users > INR 1,000

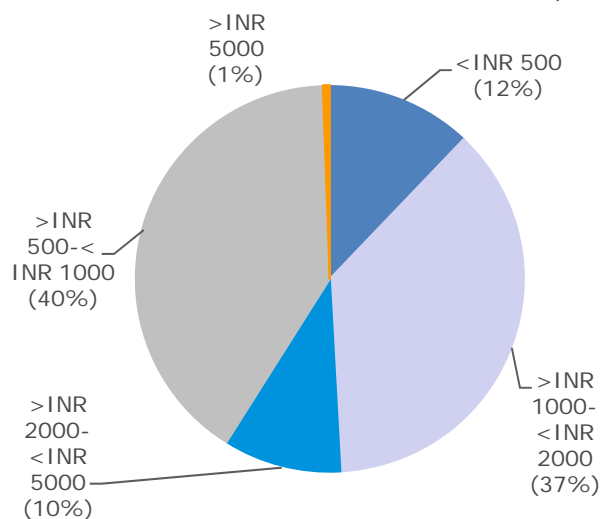
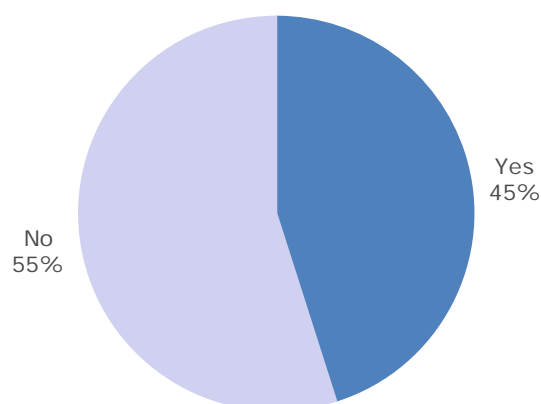


Chart 9: 45% of Vodafone users owned >1 SIM



Source: Edelweiss research

Chart 10: 46% respondents want to switch post MNP

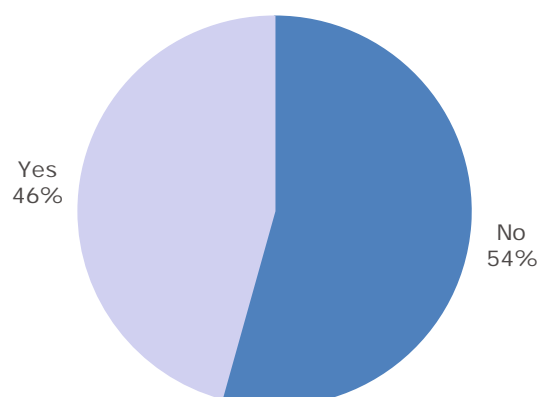
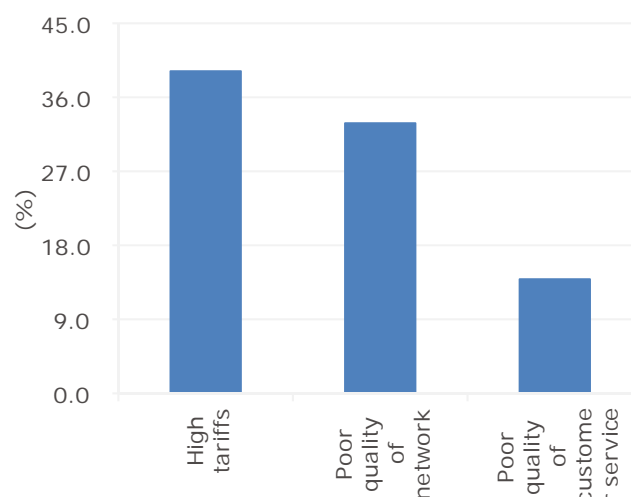


Chart 11: Top reasons to switch out from Vodafone



Source: Edelweiss research

Chart 12: Key gainers from Vodafone

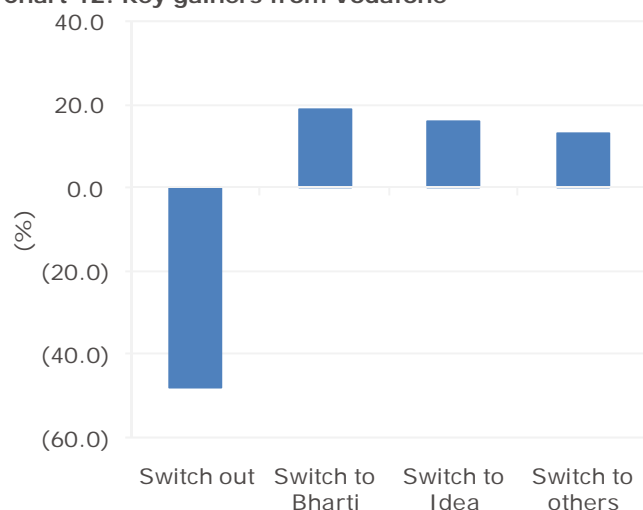
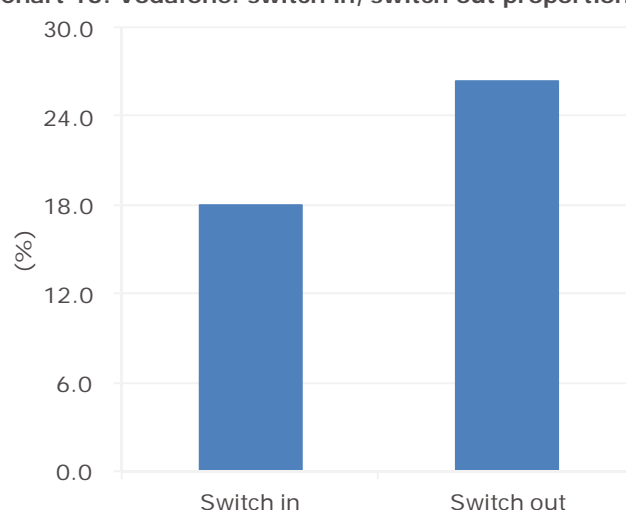


Chart 13: Vodafone: switch in, switch out proportion



Source: Edelweiss research

Bharti Airtel (22% market share among respondents)

Bharti is the fourth largest operator in Mumbai with a November 2010 subscriber market share of ~9% and Q2FY11 revenue market share of 20%. Around 22% of our survey respondents are Airtel users, of which, 71% are postpaid subscribers. Poor quality of network and customer service emerged as top reasons for discontent among Bharti users. About 71% of Bharti users indicated that they would switch post MNP, citing: (1) poor quality of network (38%), (2) poor quality of customer service (22%); and (3) high tariffs (11%) as the top three reasons. Vodafone and Idea emerged as the top preferences to switch to post MNP among Vodafone users.

Chart 14: ARPU of 40% Bharti users >INR 1,000

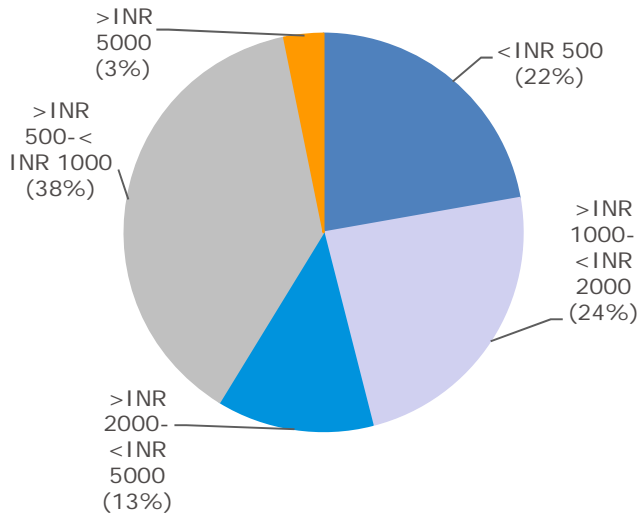


Chart 15: 52% of the Bharti users owned >1 SIM

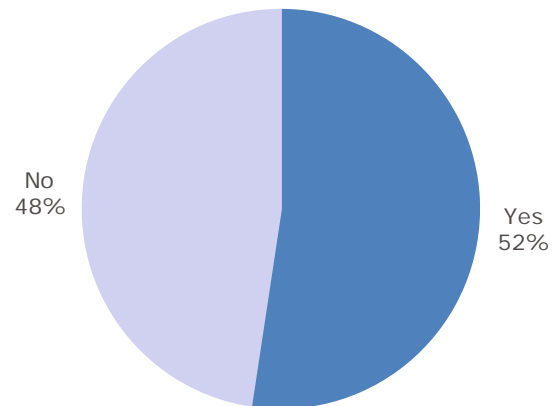


Chart 16: 71% respondents want to switch post MNP

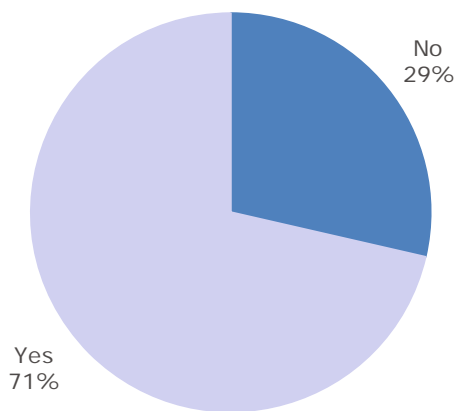


Chart 17: Top reasons to switch out from Bharti

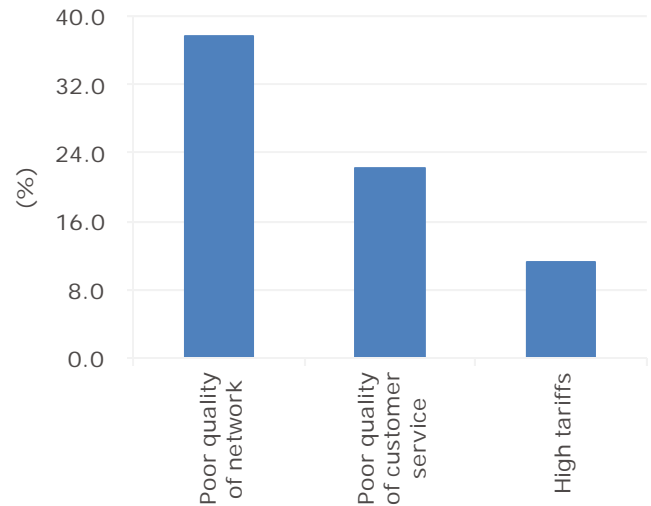


Chart 18: Key gainers from Bharti

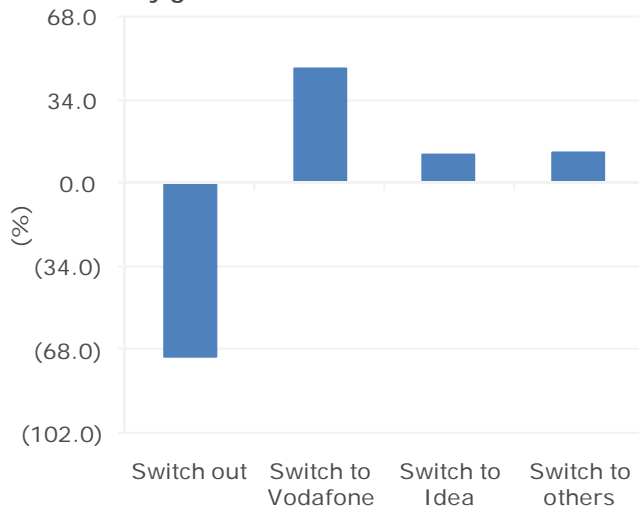
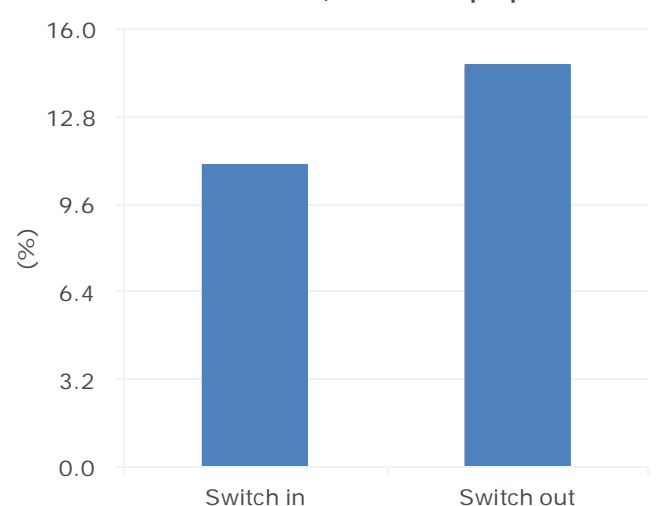


Chart 19: Bharti: switch in, switch out proportion



Source: Edelweiss research

■ Corporate customers too are price sensitive

We surveyed three corporates in the financial services and IT sectors in Mumbai. The companies surveyed were of various sizes, with the largest company having 4,000 corporate connections, another with 400 connections and the smallest with ~100 connections. While Vodafone and Airtel are the two preferred vendors, one of the corporates had Tata Docomo as its primary service provider for mobile connections given to employees. Key reasons cited for the preferred service providers were:

- Quality of network and international connectivity
- Quality of customer service

Surprisingly, all corporates indicated that they manage to get best pricing from their service providers and, hence, don't think tariff is a differentiator. One of the corporates surveyed mentioned that it negotiates with its service provider by bundling its telecom requirements. However, we were surprised that the other two corporates treat mobile and enterprise separately and there is no bundling or cross subsidy involved.

Also, all the corporates surveyed indicated that there was no price lock-in with their service provider and tariffs get revised whenever there is any discount offered in the market.

On the action plan, most corporates indicated that they have limited options as the choice is only between Vodafone and Airtel. As expected, most corporates would be using two service providers as quality of network differs depending on the locality.

It is surprising to note that corporates were not approached by competing service providers with any specific plans in the run up to and even after MNP implementation. Also, on 3G services there is limited activity that corporates have experienced from their service providers, indicating that there is still some time for 3G services to be launched in Mumbai. Corporate customers believe that MNP will not influence their decision for choosing a service provider; they, however, expect attractive schemes as far as 3G services are concerned. Within 3G services, it is mainly internet access which corporate customers believe will be of interest while video calling is not expected to be a key area of interest.

■ Net impact would be on margins

Our three-pronged approach to analyse the impact of MNP viz., (1) comparison of offers by visiting stores; (2) internal survey of Edelweiss employees; and (3) survey of corporates, suggests that MNP will not lead to any significant change in subscriber market share, but could negatively impact revenues and margins. Revenues could get impacted as customers 'down trade' on their existing plans. Margins are likely to get impacted given lower revenue/cell site, while the cost/cell site will be largely fixed and customer acquisition/retention costs will rise.

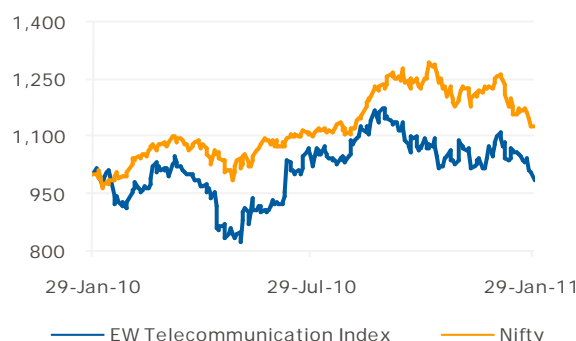
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Coverage group(s) of stocks by primary analyst(s): Telecom

Bharti Airtel, Idea Cellular, Reliance Communications and Tulip Telecom

EW indices



Distribution of Ratings / Market Cap

Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	116	45	12	176

* 3 stocks under review

	> 50bn	Between 10bn and 50 bn	< 10bn
Market Cap (INR)	110	53	13

Recent Research

Date	Company	Title	Price (INR)	Recos
25-Jan-11	Idea Cellular	Uncertainties still remain; Result Update	72	Hold
20-Jan-11	Spice Mobility	Retail telecom play; Visit Note	102	Not Rated
18-Jan-11	Tulip Telecom	Data centre acquisition: Long-term strategic fit; Event Update	169	Buy
15-Dec-10	Reliance Comm.	Syndicated loan financing from Chinese banks; EdelFlash		

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

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