

Reliance Communications

3Q KPIs disappoint, cutting earnings, price target

- We cut FY11-13E earnings by 5-20% and price target to Rs110 (earlier Rs144) driven by lower traffic growth assumptions.
- Sub-par traffic growth in seasonally strong 3Q highlights challenges faced by RCOM in reviving traffic growth; discontinuation of free/PCO mins offers only partial explanation, in our view.
- Higher net debt coupled with cut in EBITDA results in accentuated impact on equity value.
- Maintain IN-LINE.

Traffic growth is the key challenge. RCOM's traffic decline of 3% qoq was much below industry peers' 5-8% qoq growth and belied a seasonally strong 3Q. Discontinuation of free/PCO mins would have added to the woes but unlikely to be the only reason, in our view. This highlights the challenges facing RCOM in reviving traffic growth without enjoying the flexibility to cut tariffs anymore.

Earnings cut. Despite stable tariffs FY12E onwards, we cut FY11-13E EBITDA by 2.5-6.2% and EPS by 5-20% to factor in lower minutes growth assumptions. FY11-13E CAGR of minutes stands reduced to 8% vs. 11% earlier.

Accentuated impact on equity value. We estimate Mar-11E net debt at Rs327bn (Rs312bn earlier) on the back of higher capex and slight deterioration in working capital in the last quarter. Though the earnings cut results in only a 9% reduction in EV (based on Mar-11 DCF), high leverage accentuates the impact on equity value resulting in cut in price target to Rs110 from Rs144.

Risks are balanced – New price target imputes EV/EBITDA of 7.7x FY12E, at a slight discount to Bharti/Idea. Upside risk from a strategic sale is balanced by potential downside from evolving "spectrum allocation & pricing" framework, which could constrain business model. We prefer Bharti and Idea in a stable pricing scenario.

IN-LINE (unchanged)

PRICE (as at 15 February 2011) PRICE TARGET

Rs101

Rs110

Bloomberg code
RCOM IN

Reuters code
RLCM.BO

Market cap
Rs211,354m (US\$4,646m)

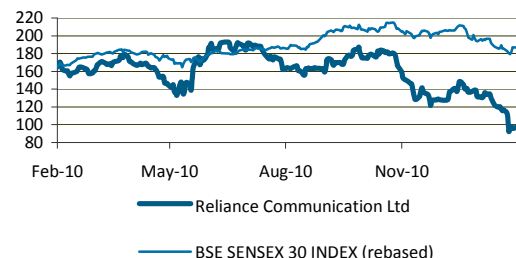
12 month range
Rs93 - 193

EPS est. change 2011E -4.8% 2012E -12.7%

Year end: March	FY10	FY11E	FY12E	FY13E
Sales (Rsm)	221,323	203,408	211,740	228,437
EBIT (Rsm)	40,740	25,413	29,984	37,075
EBITDA (Rsm)	78,205	66,124	72,513	81,044
Pretax profit (Rsm)	52,228	14,634	18,633	26,314
Earnings (Rsm) adjusted	47,774	14,487	17,329	23,156
Diluted EPS (Rs) adjusted	23.1	7.0	8.4	11.2
Diluted EPS growth (%) adj.	-22.3	-69.7	19.6	33.6
DPS (Rs)	1.50	1.00	1.00	1.50
EBITDA margin (%)	35.3	32.5	34.2	35.5
EBIT margin (%)	18.4	12.5	14.2	16.2
Net margin (%)	21.6	7.1	8.2	10.1
Div payout (%)	7.3	16.0	13.4	13.4
Book value/share (Rs)	210.1	215.1	221.5	230.3
Net debt/Equity (x)	0.6	0.7	0.7	0.6
Net debt/EBITDA (x)	3.2	5.0	4.4	3.6
ROE (%)	10.8	2.8	3.4	4.5
ROIC (%)	5.3	3.2	3.6	4.3
FCF (Rsm)	37,108	-67,213	16,038	37,735
EV/Sales (x)	2.1	2.6	2.5	2.2
EV/EBITDA (x)	5.8	8.1	7.4	6.3
PBR (x)	0.5	0.5	0.4	0.4
PER (x)	4.3	16.0	13.1	9.5
Dividend yield (%)	1.5	1.0	1.0	1.5

Source: Company, Standard Chartered Research estimates

Share price performance



Share price (%)	-1 mth	-3 mth	-12 mth
Ordinary shares	-26	-41	-43
Relative to Index	-23	-35	-49
Relative to Sector	-	-	-
Major shareholder	Promoters (67.9%)		
Free float	32%		
Average turnover (US\$)	16,924,289		

Source: Company, Bloomberg

Rahul Singh
rahul.singh@sc.com
+91 22 6755 9770

Saurav Anand
saurav.anand@sc.com
+91 22 6755 9777

**Fig 1: Earnings estimates revised downwards**

Year end: Mar	FY11E		FY12E		FY13E	
	Old	New	Old	New	Old	New
Wireless minutes (bn)	389.1	371.6	443.6	401.3	479.1	433.4
Rev/min (Rs)	0.43	0.44	0.40	0.42	0.40	0.42
ARPU (Rs)	120	116	102	97	97	91
Net revenues (Rsm)	212,828	203,408	227,530	211,740	247,948	228,437
EBITDA (Rsm)	67,791	66,124	75,015	72,513	86,378	81,044
PAT (Rsm)	15,225	14,487	19,845	17,329	29,185	23,156

Source: Company, Standard Chartered Research estimates

Fig 2: Quarterly results summary

(Rsm)	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10	QoQ (%)	YoY (%)
Net revenue	53,097	50,927	51,092	51,183	50,041	-2.2	-5.8
Access and IUC	-5,151	-5,905	-6,646	-6,534	-6,603	1.0	28.2
Other operating exp	-26,635	-25,947	-25,060	-24,983	-23,891	-4.4	-10.3
License fees	-3,186	-3,056	-3,066	-3,071	-3,002	-2.2	-5.8
EBITDA	18,125	16,019	16,320	16,595	16,680	0.5	-8.0
PBT	13,648	13,306	2,276	4,245	5,046	18.9	-63.0
PAT	11,645	11,383	2,995	4,906	5,260	7.2	-54.8

Source: Company

Fig 3: Wireless business snapshot

(Rsm)	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10	Remarks
Wireless revenue	40,225	40,900	41,528	41,613	40,644	Partly due to loss of revenue from wholesale/PCO segment
Net revenue	27,998	26,226	28,047	28,333	27,474	
EBITDA	12,545	11,815	11,989	12,101	11,792	Reduction in network opex helps maintain EBITDA margin
EBITDA margin (%)	31.2	28.9	28.9	29.1	29.0	
ARPU	149	139	130	122	111	
MoU	330	318	295	276	251	
Minutes of usage (bn min)	89.0	93.5	94.3	94.4	91.5	Decline due to loss of PCO minutes
Revenue per min (Rs)	0.45	0.44	0.44	0.44	0.44	Rev/min remains stable in-line with peers
EBITDA per min (Rs)	0.14	0.13	0.13	0.13	0.13	

Source: Company

Fig 4: Global business snapshot

(Rsm)	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10	Remarks
NLD mins (m)	13,643	16,086	15,265	16,383	16,569	
ILD mins (m)	2,823	2,656	3,123	3,753	4,084	
Global business revenue	19,818	20,278	18,137	18,391	19,233	Improvement in margins due to better utilisation of existing bandwidth
EBITDA	4,194	3,555	3,317	3,393	3,966	
EBITDA margin (%)	21.2	17.5	18.3	18.4	20.6	

Source: Company

Fig 5: Broadband business snapshot

(Rsm)	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10	Remarks
Broadband revenue	7,045	6,798	6,763	6,617	6,184	8% qoq decline in ARPU and slowdown in net adds led to sharp 7% qoq decline in revenues
EBITDA	2,755	2,526	2,477	2,481	2,267	
EBITDA margin (%)	39.1	37.2	36.6	37.5	36.7	
ARPL (Rs)	1642	1551	1534	1494	1377	

Source: Company

**Fig 6: DCF valuation**

(Rsm)	FY10	FY11E	FY12E	FY13E	FY14E	FY15E	FY16E
Operating EBIT	40,740	25,413	29,984	37,075	42,949	48,750	53,442
NOPAT	40,272	21,645	24,866	30,302	35,740	37,928	39,559
(Add) Depreciation	37,465	40,710	42,529	43,969	45,224	46,420	47,587
(Less) Capex	-42,191	-131,103	-35,569	-28,434	-27,353	-25,827	-26,007
Free cash flows	37,108	-67,213	16,038	37,735	54,214	58,668	62,055
NPV (explicit FCFs)	155,183						
NPV (terminal value)	398,873						
Firm value	554,056						
Net debt/(cash) (Rsm)	327,408						
Equity value	226,648						
Equity value per share (Rs)	110						
Base case 'g' (%)	3.0						
Base case WACC (%)	12.1						

Source: Company, Standard Chartered Research estimates

Fig 7: Income statement

Year to Mar (Rsm)	FY09	FY10	FY11E	FY12E	FY13E
Mobile	173,677	169,156	163,168	167,410	180,803
Global Business	67,761	81,583	75,316	73,920	73,234
Broadband	25,243	28,385	26,002	26,404	26,623
Others	10,098	11,796	14,155	18,402	23,922
Eliminations	-47,368	-68,418	-75,233	-74,395	-76,146
Total revenues	229,411	221,323	203,408	211,740	228,437
Reported EBITDA	92,875	78,205	66,124	72,513	81,044
EBITDA margins %	40.5	35.3	32.5	34.2	35.5
Mobile %	38.4	33.1	30.2	32.3	33.2
Global Business %	23.9	21.4	19.6	21.1	22.9
Broadband %	45.9	40.4	36.9	37.8	39.9
Others %	-12.7	-47.8	-36.6	-22.5	-13.9
Net Interest	7,867	11,863	-10,780	-11,351	-10,762
Depreciation & Amortisation	-39,388	-37,465	-40,710	-42,529	-43,969
PBT	61,354	52,228	14,634	18,633	26,314
Tax	123	-4,454	-146	-1,304	-3,158
PAT	61,477	47,774	14,487	17,329	23,156
EPS (Rs)	29.8	23.1	7.0	8.4	11.2

Source: Company, Standard Chartered Research estimates

**Fig 8: Balance Sheet**

Year end March (Rsm)	FY09	FY10	FY11E	FY12E	FY13E
Equity	10,320	10,320	10,320	10,320	10,320
Reserves and Surplus	412,483	423,286	433,602	446,758	464,968
Shareholders funds	422,803	433,606	443,922	457,078	475,288
Debt	391,623	297,154	377,154	327,154	297,154
Current Liabilities	159,718	147,085	141,098	123,758	122,827
Provisions	41,096	40,267	40,267	40,267	40,267
Minority	6,549	6,584	8,434	10,284	12,134
Total Liabilities	1,021,789	924,696	1,010,874	958,541	947,670
Fixed Assets	755,101	786,653	831,907	867,476	895,909
Accumulated Depreciation	-141,144	-190,671	-227,089	-265,325	-305,001
Net Fixed Assets	613,957	595,982	604,818	602,151	590,908
CWIP	113,096	116,557	116,557	116,557	116,557
Goodwill	52,215	49,976	49,976	49,976	49,976
Investments	2,762	1,199	1,199	1,199	1,199
Deferred tax assets	-281	-991	-991	-991	-991
Cash and cash equivalents	109,724	48,585	49,746	5,925	3,418
Current Assets	130,316	113,387	105,866	104,312	111,484
Inventories	5,427	5,446	5,000	5,000	5,000
Debtors	39,618	33,117	33,901	35,290	38,073
Other Current Assets	17,714	20,726	21,763	22,851	23,993
Loans & Advances	67,557	54,098	45,202	41,172	44,418
Total Assets	1,021,789	924,696	1,010,874	958,541	947,670

Source: Company, Standard Chartered Research estimates

Fig 9: Key Valuation metrics

Year to Mar	FY09	FY10	FY11E	FY12E	FY13E
YoY EPS Growth (%)	11.6	-23.7	-73.1	22.5	37.6
YoY EBITDA Growth (%)	13.3	-15.8	-15.4	9.7	11.8
P/E (x)	3.3	4.3	16.0	13.1	9.5
P/CEPS (x)	2.0	2.4	3.8	3.5	3.1
EV/EBITDA (x)	5.3	5.8	8.1	7.4	6.3
Price to book (x)	0.5	0.5	0.5	0.4	0.4
Price to sales (x)	0.9	0.9	1.0	1.0	0.9
Price to EBITDA	2.2	2.6	3.1	2.8	2.5
Price to FCFF (x)	-1.2	5.5	-3.0	12.6	5.4
FCFF yield (%)	-81.0	18.3	-33.2	7.9	18.7
FCFE yield (%)	-81.0	18.3	-38.6	2.3	13.3
Dividend yield (%)	1.0	1.5	1.0	1.0	1.5
Net debt/EBITDA	3.0	3.2	5.0	4.4	3.6
RoE (%)	14.5	10.8	2.8	3.4	4.5
RoIC (%)	7.5	5.3	3.2	3.6	4.3
Capex to sales (%)	111.4	19.1	64.5	16.8	12.4
Capex to EBITDA (%)	275.1	53.9	198.3	49.1	35.1
Depr to capex (%)	15.4	88.8	31.1	119.6	154.6

Source: Company, Standard Chartered Research estimates



Disclosures appendix

Global disclaimer

The information and opinions in this report were prepared by Standard Chartered Bank (Hong Kong) Limited, Standard Chartered Bank Singapore Branch, Standard Chartered Securities (India) Limited and/or one or more of its affiliates (together with its group of companies, "SCB") and the research analyst(s) named in this report. SCB makes no representation or warranty of any kind, express, implied or statutory regarding this document or any information contained or referred to in the document.

DISCLOSURES INCLUDING THOSE REQUIRED BY THE UNITED STATES

The research analysts responsible for the content of this research report certify that:

The view expressed and attributed to the research analyst or Analysts in the research report accurately reflect their personal opinion(s) about the subject securities and issuers and/or other subject matter as appropriate; and
 No part of his or her compensation and other benefits was, is or will be directly related to the specific recommendations or views contained in this research report. On a general basis, the efficacy of recommendations is a factor in the performance appraisals of analysts.
 Our ratings are under constant review.

Additional information with respect to any securities referred to herein will be available upon request.

THIS RESEARCH HAS NOT BEEN PRODUCED IN THE UNITED STATES.

Disclosures Appendix

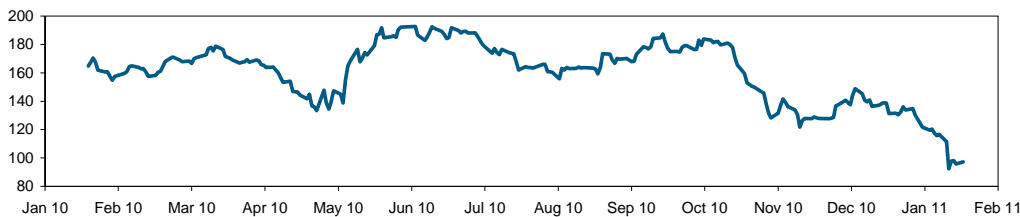
Where "disclosure date" appears below, this means the day prior to the report date. All share prices quoted are the closing price for the business day prior to the date of the report, unless otherwise stated.

Company Reliance Communication Ltd

As at the disclosure date, the following applies:

SCB and/or its affiliates have received compensation for the provision of investment banking or financial advisory services within the past one year

Reliance Communication Ltd - current rating is: IN-LINE



Source: FactSet prices / SCB ratings and price targets

Company Bharti Airtel Ltd

As at the disclosure date, the following applies:

SCB and/or its affiliates have received compensation for the provision of investment banking or financial advisory services within the past one year

Recommendation Distribution and Investment Banking Relationships

	% of covered companies currently assigned this rating	% of companies assigned this rating with which SCB has provided investment banking services over the past 12 months
OUTPERFORM	62.8%	14.0%
IN-LINE	28.4%	12.4%
UNDERPERFORM	8.8%	3.3%

Research Recommendation

Terminology	Definitions
OUTPERFORM (OP)	The total return on the security is expected to outperform the relevant market index by 5% or more over the next 12 months
IN-LINE (IL)	The total return on the security is not expected to outperform or underperform the relevant market index by 5% or more over the next 12 months
UNDERPERFORM (UP)	The total return on the security is expected to underperform the relevant market index by 5% or more over the next 12 months

SCB uses an investment horizon of 12 months for its price targets.



Country-Specific Disclosures

If you are receiving this document in any of the countries listed below, please note the following:

United Kingdom and European Economic Area: Standard Chartered Bank is authorised and regulated by the Financial Services Authority. This communication is not directed at Retail Clients in the European Economic Area as defined by Directive 2004/39/EC. Nothing in this document constitutes a personal recommendation or investment advice as defined by Directive 2004/39/EC.

Australia: The Australian Financial Services Licence for Standard Chartered Bank is Licence No: 246833 with the following Australian Registered Business Number (ARBN: 097571778). Australian investors should note that this document was prepared for wholesale investors only (as defined by Australian Corporations legislation).

Hong Kong: This document is being distributed in Hong Kong by, and is attributable to, Standard Chartered Bank (Hong Kong) Limited which is regulated by the Hong Kong Monetary Authority.

India: This document is being distributed in India by Standard Chartered Securities (India) Limited which is a SEBI registered broker and a member of the Bombay Stock Exchange Limited and The National Stock Exchange of India Limited.

Singapore: This document is being distributed in Singapore by Standard Chartered Bank Singapore Branch only to accredited investors, expert investors or institutional investors, as defined in the Securities and Futures Act, Chapter 289 of Singapore. Recipients in Singapore should contact Standard Chartered Bank Singapore Branch in relation to any matters arising from, or in connection with, this document.

United States: Except for any documents relating to foreign exchange, FX or global FX, Rates or Commodities, distribution of this document in the United States or to US persons is intended to be solely to major institutional investors as defined in Rule 15a-6(a)(2) under the US Securities Act of 1934. All US persons that receive this document by their acceptance thereof represent and agree that they are a major institutional investor and understand the risks involved in executing transactions in securities. Any US recipient of this document wanting additional information or to effect any transaction in any security or financial instrument mentioned herein, must do so by contacting a registered representative of Standard Chartered Securities (North America) Inc., 1 Madison Avenue, New York, N.Y. 10010, US, tel + 1 212 667 0700.

WE DO NOT OFFER OR SELL SECURITIES TO U.S. PERSONS UNLESS EITHER (A) THOSE SECURITIES ARE REGISTERED FOR SALE WITH THE U.S. SECURITIES AND EXCHANGE COMMISSION AND WITH ALL APPROPRIATE U.S. STATE AUTHORITIES; OR (B) THE SECURITIES OR THE SPECIFIC TRANSACTION QUALIFY FOR AN EXEMPTION UNDER THE U.S. FEDERAL AND STATE SECURITIES LAWS NOR DO WE OFFER OR SELL SECURITIES TO U.S. PERSONS UNLESS (i) WE, OUR AFFILIATED COMPANY AND THE APPROPRIATE PERSONNEL ARE PROPERLY REGISTERED OR LICENSED TO CONDUCT BUSINESS; OR (ii) WE, OUR AFFILIATED COMPANY AND THE APPROPRIATE PERSONNEL QUALIFY FOR EXEMPTIONS UNDER APPLICABLE U.S. FEDERAL AND STATE LAWS.

GENERAL DISCLAIMER

The information on this document is provided for information purposes only. It does not constitute any offer, recommendation or solicitation to any person to enter into any transaction or adopt any hedging, trading or investment strategy, nor does it constitute any prediction of likely future movements in rates or prices or any representation that any such future movements will not exceed those shown in any illustration. The stated price of the securities mentioned herein is as of the date indicated and is not any representation that any transaction can be effected at this price. While all reasonable care has been taken in preparing this document, no responsibility or liability is accepted for errors of fact or for any opinion expressed herein. The contents of this document may not be suitable for all investors as it has not been prepared with regard to the specific investment objectives or financial situation of any particular person. Any investments discussed may not be suitable for all investors. Users of this document should seek professional advice regarding the appropriateness of investing in any securities, financial instruments or investment strategies referred to in this document and should understand that statements regarding future prospects may not be realised. Opinions, forecasts, assumptions, estimates, derived valuations and price target(s) contained in this document are as of the date indicated and are subject to change at any time without prior notice.

The value and income of any of the securities or financial instruments mentioned in this document can fall as well as rise and an investor may get back less than invested. Future returns are not guaranteed, and a loss of original capital may be incurred. Foreign-currency denominated securities and financial instruments are subject to fluctuation in exchange rates that could have a positive or adverse effect on the value, price or income of such securities and financial instruments.

Past performance is not indicative of comparable future results and no representation or warranty is made regarding future performance. While we endeavour to update on a reasonable basis the information and opinions contained herein, there may be regulatory, compliance or other reasons that prevent us from doing so. Accordingly, information may be available to us which is not reflected in this material, and we may have acted upon or used the information prior to or immediately following its publication.

SCB is not a legal or tax adviser, and is not purporting to provide you with legal or tax advice. If you have any queries as to the legal or tax implications of any investment you should seek independent legal and/or tax advice.

SCB, and/or a connected company, may have a position in any of the securities, instruments or currencies mentioned in this document. SCB has in place policies and procedures and physical information walls between its Research Department and differing public and private business functions to help ensure confidential information, including 'inside' information is not publicly disclosed unless in line with its policies and procedures and the rules of its regulators. Data, opinions and other information appearing herein may have been obtained from public sources. SCB makes no representation or warranty as to the accuracy or completeness of such information obtained from public sources. You are advised to make your own independent judgment (with the advice of your professional advisers as necessary) with respect to any matter contained herein and not rely on this document as the basis for making any trading, hedging or investment decision.

SCB and/or any member of the SCB group of companies or its respective officers, directors, employee benefit programmes or employees, including persons involved in the preparation or issuance of this document may at any time, to the extent permitted by applicable law and/or regulation, be long or short any securities or financial instruments referred to in this document and on the website or have a material interest in any such securities or related investment, or may be the only market maker in relation to such investments, or provide, or have provided advice, investment banking or other services, to issuers of such investments. Within the last three years, SCB may also have acted as manager or co-manager for a public offering of securities of issuers referred to herein. SCB may have received or may expect to receive remuneration for investment banking services from companies mentioned herein.

SCB accepts no liability and will not be liable for any loss or damage arising directly or indirectly (including special, incidental, consequential, punitive or exemplary damages) from your use of this document, howsoever arising, and including any loss, damage or expense arising from, but not limited to, any defect, error, imperfection, fault, mistake or inaccuracy with this document, its contents or associated services, or due to any unavailability of the document or any part thereof or any contents or associated services.

This material is for the use of intended recipients only and the contents may not be reproduced, redistributed, or copied in whole or in part for any purpose without SCB's prior express consent. In any jurisdiction in which distribution to private/retail customers would require registration or licensing of the distributor which the distributor does not currently have, this document is intended solely for distribution to professional and institutional investors.

Copyright: Standard Chartered Bank 2011. Copyright in all materials, text, articles and information contained herein is the property of, and may only be reproduced with permission of an authorised signatory of, Standard Chartered Bank. Copyright in materials created by third parties and the rights under copyright of such parties are hereby acknowledged. Copyright in all other materials not belonging to third parties and copyright in these materials as a compilation vests and shall remain at all times copyright of Standard Chartered Bank and should not be reproduced or used except for business purposes on behalf of Standard Chartered Bank or save with the express prior written consent of an authorised signatory of Standard Chartered Bank. All rights reserved. © Standard Chartered Bank 2011.