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Updates

Telecom: MNP—consumers now have a choice, investors don't

News Roundup

Corporate

- Indian watch major Titan Industries is setting up an assembly plant in Vietnam. The move is intended to provide the Tata-managed watch and jewellery company with better access to growth markets in South East Asia. (ET)
- Ranbaxy Laboratories has acquired a 27.35% stake in Zenotech Laboratories through bulk deals in the open market. (ET)
- DLF Ltd is acquiring the privately-held super luxury resorts and spa chain Singapore-based Amanresorts for around US\$250 mn. (BS)
- Kishore Biyani-promoted Future Group is set to launch a television channel, a bevy of specialised magazines, get into television production and bid for or acquire FM radio stations across the country. (BS)

Economic and political

- The Left conveyed to the UPA that it is willing to discuss an earlier Government proposal that would allow India to approach IAEA (International Atomic Energy Agency) on the condition that the safeguards agreement will not be confirmed until cleared by the Left-UPA committee on the nuclear deal. (Indian Express)
- British Prime Minister Gordon Brown in his maiden foreign policy speech has strongly backed New Delhi's claim for a permanent seat in the United Nations Security Council. (ET)
- The Government said a total investment of US\$6.5 bn is in the pipeline for the medical tourism industry in the country. (ET)

Source: ET = Economic Times, BS = Business Standard, FE = Financial Express, BL = Business Line.

EQUITY MARKETS

India	Change, %			
	13-Nov	1-day	1-mo	3-mo
Sensex	19,035	1.6	3.3	26.8
Nifty	5,695	1.4	4.9	30.2
Global/Regional indices				
Dow Jones	12,988	(0.4)	(7.8)	(1.9)
Nasdaq Composite	2,584	(1.7)	(7.9)	1.6
FTSE	6,312	(0.4)	(6.2)	1.5
Nikkie	15,127	(0.5)	(12.7)	(10.0)
Hang Seng	27,803	0.5	(3.6)	27.0
KOSPI	1,933	0.5	(4.6)	4.5
Value traded - India				
		Moving avg, Rs bn		
	13-Nov	1-mo	3-mo	
Cash (NSE+BSE)	235.5	300.8	225.1	
Derivatives (NSE)	567.7	904.2	488.7	
Deri. open interest	943.0	959.5	844.4	

Forex/money market

	Change, basis points			
	13-Nov	1-day	1-mo	3-mo
Rs/US\$	39.4	8	11	(114)
6mo fwd prem, %	0.7	(25)	71	24
10yr govt bond, %	8.0	4	6	2

Net investment (US\$mn)

	8-Nov	MTD	CYTD
FIs	(71)	(307)	16,980
MFs	(56)	(36)	142

Top movers -3mo basis

Best performers	Change, %			
	13-Nov	1-day	1-mo	3-mo
Neywell Lignite	203	4.3	89.1	161.1
Reliance Energy	1,854	1.9	13.3	146.1
Engineers India	912	1.7	58.3	99.2
MRF	7,549	1.4	85.5	93.7
Reliance Cap	2,035	1.1	12.0	81.1
Worst performers				
i-Flex	1,425	(0.1)	(21.1)	(31.5)
Punjab Tractors	196	5.2	(12.9)	(23.4)
Ingersoll Rand	282	(1.5)	(4.1)	(21.5)
Essel Propack	48	(0.4)	(18.1)	(20.2)
Polaris	105	2.9	(10.1)	(13.7)

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Telecom

Sector coverage view

Cautious

Company	Rating	Price, Rs	
		13-Nov	Target
Bharti	REDUCE	833	775
Rcom	SELL	707	550
Idea Cellular	SELL	121	110

MNP—consumers now have a choice, investors don't

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- **MNP introduction in metros by end-December 2008; in other circles, in a phased manner**
- **MNP could put pricing and sector profitability under significant pressure; the war may have already started**
- **Profitability of all operators to come under pressure but RCOM may be relatively better off**

We believe the telecom ministry's approval to introduce mobile number portability (MNP) in the country (in a phased manner starting with the metros) will likely put additional pressure on pricing, profitability and returns. The metros had 18% of the total wireless subscriber base in the country at end-September 2007 and accounted for 24% of the total adjusted gross revenues in the Jun'07 quarter. We also presume that the metros would have a larger proportion of high-usage, higher-profitability customers—the ideal target market for porting. We expect the introduction of MNP to change the competitive landscape in three ways—(1) higher spend on customer acquisition and retention; (2) greater emphasis on quality of service implying higher capex spend; and (3) pressure on tariffs due to 'new' (including RCOM) and extant operators using pricing aggressively to target high-ARPU customers of incumbents. We highlight that these policy changes are potentially negative for the incumbent GSM operators like Bharti, Idea and Vodafone-Essar while marginally positive for RCOM. We retain our cautious view of the Indian telecom sector. Our DCF-based 12-month target prices of Bharti, Idea and RCOM, respectively are Rs775, Rs110 and Rs550, respectively.

RCOM is in a better position versus others. We believe that the eventual implementation of MNP will be a large negative development for the sector, especially now that GSM spectrum allocation to 'new' players including RCOM looks more likely (see Exhibit 1 for the priority order of spectrum allocation of GSM spectrum). We expect RCOM to be in a relatively better position versus others under an MNP regime. RCOM can churn out extant GSM subscribers of incumbent operators under MNP while largely retaining its CDMA subscribers. A CDMA subscriber of RCOM will not be in a position to migrate to a GSM operator (technology compatibility issues), unless the subscriber changes the handset. Further, a CDMA subscriber would have limited options to migrate given fewer (two only) number of CDMA players.

MNP may take 12-15 months to implement. Global experience suggests that the MNP roll-out process has taken various countries at least 12 months once the methodology and cost-allocation basis are decided and agreed upon by the regulator and the telcos. We believe that MNP in India could be introduced as early as December 2008. The telecom ministry seems to have finalized upon a 'centralized database' approach for MNP implementation and press reports suggest that capex allocation would be on a proportionate (market share) basis.

The cost and capex for implementation of MNP would vary depending on the call routing method employed (see Exhibit 2 for the various routing methodologies employed for MNP globally). Direct routing of call ('All Call Query') involves higher set-up costs and capex but has lower operational costs. Pakistan implemented 'All Call Query' system at a capex of approximately US\$80 mn in March 2007 for 55.7 mn subscribers (each operator contributed US\$10-12 mn). Extrapolating this capex to India, it would cost US\$450-500 mn for implementation (based on FY2009E subs). On the other hand, the UK adopted onward routing which has lower upfront capex but higher administration costs. In UK, MNP implementation had upfront costs of US\$12 mn for 15 mn subs, assuming that the set-up costs remain the same, capex for Indian vendors could be US\$270 mn.

Metros the ideal test markets for MNP. We believe that the subscriber profile in the metros—high-usage (and highly profitable, see Exhibit 3) customers reluctant to lose their mobile numbers and quite high penetration—makes these markets ideal as test markets for the introduction of MNP in India. Their high subscriber and revenue share (18% and 24%, respectively) also makes them ideal turf for some interesting porting wars. We note that Bharti has the highest subscriber and revenue market share in the four metros. Exhibits 4, 5, and 6 depict the player-wise subscriber base as at end-September 2007, subscriber market share of operators, and Jun 2007 AGR details, respectively. In addition, we expect penetration levels in the metros at the time of the MNP launch to be around 40-80%, in line with global experience (see Exhibit 7).

MNP may work in India even if not successful globally. We expect MNP to be a success in India due to (1) the absence of long-term service contracts between service providers and subscribers and (2) price-sensitive nature of the market. We expect MNP to be negative for Bharti, Idea and Vodafone but positive for RCL. Global experience suggests that certain hygiene factors need to be in place for MNP to be successful including (1) low cost of port (2) time within which port, if accepted, should be low and (3) easy administrative procedures. We would refer readers to our report *Change is bad* dated October 4, 2007 for more details.

Implications for Indian telecom operators

India is different from other countries in that long-term service contracts and handset subsidies are virtually non-existent. The only other country which is similar to India is Finland, where the regulator does not allow handset bundling. After the introduction of MNP, the churn rate in Finland increased by >10 pps within a short time. ARPU for Telia Sonera, the largest operator in Finland, declined 16% within four quarters of the launch of MNP. Exhibit 8 discusses the Finland case in detail. We expect the impact on Indian players in the following ways:

- 1. Sales and marketing spend will go up.** We believe MNP will lead to higher sales expenses to acquire and retain customers. In addition, operators may be forced to invest in network and improve the quality of service. Further, telecom operators may enter into long-term service contracts by bundling or providing handset subsidies to subscribers.
- 2. Price competition will increase.** MNP would perhaps remove the last possible barrier to competition. In our view, price competition will likely intensify given that there is very little difference between service providers. Further, pricing will quickly settle around the lowest price offered by a service provider in a region. In fact, the likely entry of new players in most circles will likely mean additional pricing competition. This may have already started, in our view. Bharti recently cut the outgoing tariff for local call on its Rs999 plan to Rs1/min from Rs2/min. There is no change to the Rs495 plan but customers under the Rs495 plan can migrate to the new tariff plan by making a one-time payment of Rs504. Finally, as per press reports, RCOM may price its GSM plans significantly below current prices; however, this is contingent on it getting spectrum and will likely take time.

We note that India is a very price-sensitive market and subscribers would have no qualms about changing their service provider for a cheaper service as long as they can retain their numbers. Even without MNP, churn is quite high in India (prepaid and postpaid monthly churn for Bharti was 3.2% and 3.8%, respectively, in 2QFY08), which demonstrates either (1) dissatisfaction with service providers and/or (2) propensity to change operators based on relative pricing.

RCOM and Idea likely to get GSM spectrum assuming 20 Mhz spectrum is released by the defence department and TRAI's revised spectrum policy is accepted
New entrants and likely order of receipt of spectrum based on chronological order

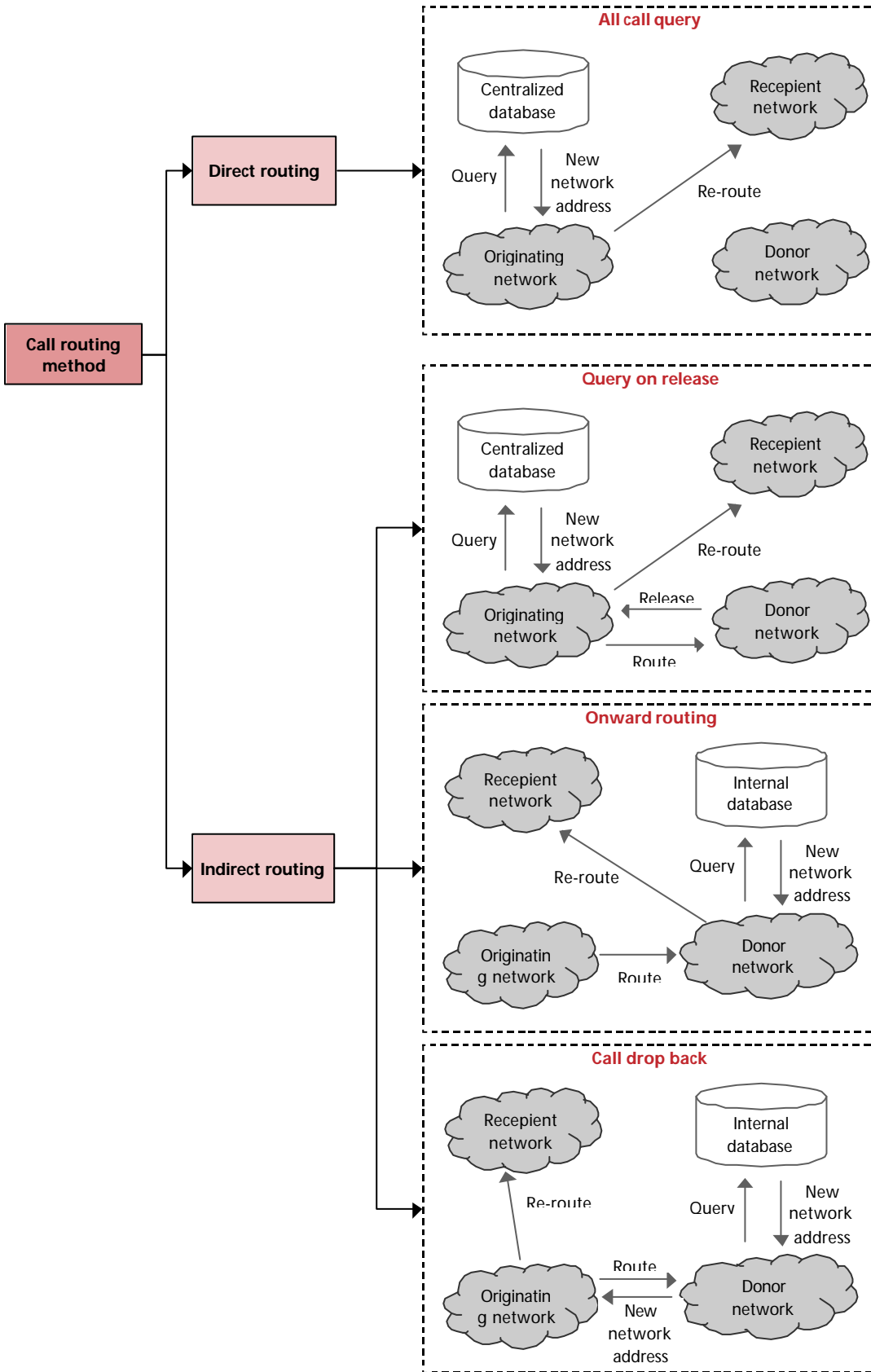
	Bharti	Reliance	BSNL/MTNL	VOD/Essar	Idea	TTSL	Aircel	Spice	Others
Metro									
Calcutta					2		1	3	
Chennai		2			1			3	
Delhi		2					1	3	
Mumbai		3			2		1	4	
Circle A									
Andhra Pradesh		2					1	3	
Gujarat		2					1	3	
Karnataka		2			2		1		
Maharashtra		2					1	3	
Tamil Nadu		2			1			3	
Circle B									
Haryana		2					1	3	
Kerala		2					1	3	
Madhya Pradesh				2			1	3	
Punjab		2			2		1		
Rajasthan		2					1	3	
Uttar Pradesh (east)		2					1	3	
Uttar Pradesh (west)		2					1	3	
West Bengal and A&N islands					2			3	1
Circle C									
Assam				1	3			4	2
Bihar				1	2			4	3
Himachal Pradesh				1				2	
North East				1	2			4	3
Orissa				1	2			4	3
J&K				1	2			3	

Existing operations
License acquired but spectrum not available
License applied for
Existing CDMA operations, GSM license received, spectrum awaited

Source: COAI, AUSPI, DOT, compiled by Kotak Institutional Equities.

Choice of call routing method determines the cost and complexity of MNP implementation

Schematic representation of various call routing methods used for MNP



Source: Kotak Institutional Equities.

Subscribers in metros are more profitable than in other circles

Circle-wise ARPU, MOU, and RPM, June 2007 quarter

	Postpaid	Prepaid	Blended
ARPU (Rs/sub/month)			
Metro	739	261	369
Circle A	664	244	295
Circle B	545	239	261
Circle C	594	274	307
All India	655	248	297
Metros vs national average (%)	12.8	5.2	24.2
MOU (min/sub/month)			
Metro	898	371	489
Circle A	1,097	411	493
Circle B	992	422	464
Circle C	978	373	435
All India	997	404	476
Metros vs national average (%)	(9.9)	(8.2)	2.7
RPM (Rs/min)			
Metro	0.82	0.70	0.75
Circle A	0.61	0.59	0.60
Circle B	0.55	0.57	0.56
Circle C	0.61	0.73	0.71
All India	0.66	0.61	0.62
Metros vs national average (%)	25.3	14.6	20.9

Note:

(a) ARPU and RPM are net of interconnection charges.

Source: TRAI reports, Kotak Institutional Equities.

Subscriber base of wireless operators in India

	Bharti	Reliance	BSNL	Hutch	IDEA	TTSL	Aircel	MTNL	Spice	BPL	Others	Total
Total subs - Sep 2007	48,876	36,324	30,303	35,658	18,672	14,919	8,039	2,878	3,482	1,153	125	200,428
Current mobile market share (%)	24.4%	18.1%	15.1%	17.8%	9.3%	7.4%	4.0%	1.4%	1.7%	0.6%	0.1%	100%
Circle-wise subscribers ('000)												
Metro												
Calcutta	1,410	1,450	777	1,573		774						5,984
Chennai	1,321	746	863	942		174	1,522					5,568
Delhi	3,546	1,968		2,905	1,779	2,162		1,306				13,667
Mumbai	2,138	2,177		2,901		1,041		1,571		1,153		10,982
Circle A												
Andhra Pradesh	4,755	3,098	2,014	2,028	2,511	1,564						15,970
Gujarat	2,016	2,077	1,606	5,068	2,100	572						13,439
Karnataka	5,606	2,025	1,671	2,270		679		1,283				13,534
Maharashtra	3,279	2,436	2,551	1,759	3,699	1,578						15,301
Tamil Nadu	2,975	2,197	2,105	2,012		357	3,940					13,586
Circle B												
Haryana	853	650	1,195	1,072	910	582						5,260
Kerala	1,297	1,645	2,060	1,454	2,170	422						9,049
Madhya Pradesh	2,107	3,024	1,419		2,205	452						9,207
Punjab	2,865	837	1,413	1,500		582		2,199			88	9,484
Rajasthan	2,736	1,360	2,219	2,219	651	992					37	10,212
Uttar Pradesh (east)	2,270	2,375	3,184	3,658	658	663						12,808
Uttar Pradesh (west)	1,277	1,765	1,710	2,252	1,943	933						9,880
West Bengal and A&N islands	1,397	1,484	1,097	2,045		420	348					6,790
Circle C												
Assam	725	656	566				866					2,814
Bihar	3,250	2,762	1,243			591	330					8,177
Himachal Pradesh	695	391	509		47	92	23					1,757
North East	344	242	487				475					1,548
Orissa	1,295	959	816			286	380					3,736
J&K	720		799				154					1,673

Source: COAI, AUSPI, Compiled by Kotak Institutional Equities.

Subscriber market share of telecom operators, Sep '07

Market share (%)	Bharti	Reliance	BSNL	Hutch	IDEA	TTSL	Aircel	MTNL	Spice	BPL	Total	Penetration (%)
Metros											Circle mkt share (%)	
Calcutta	23.6	24.2	13.0	26.3		12.9					3.0	34.8
Chennai	23.7	13.4	15.5	16.9		3.1	27.3				2.8	74.2
Delhi	25.9	14.4		21.3	13.0	15.8		9.6			6.8	65.7
Mumbai	19.5	19.8		26.4		9.5		14.3		10.5	5.5	48.5
Metros total	23.2	17.5	4.5	23.0	4.9	11.5	4.2	7.9	—	3.2	18.1	
Circle A												19.6
Andhra Pradesh	29.8	19.4	12.6	12.7	15.7	9.8					8.0	24.0
Gujarat	15.0	15.5	11.9	37.7	15.6	4.3					6.7	23.6
Karnataka	41.4	15.0	12.3	16.8		5.0		9.5			6.8	17.7
Maharashtra	21.4	15.9	16.7	11.5	24.2	10.3					7.6	22.6
Tamil Nadu	21.9	16.2	15.5	14.8		2.6	29.0				6.8	
Circle B												27.2
Haryana	16.2	12.4	22.7	20.4	17.3	11.1					2.6	26.7
Kerala	14.3	18.2	22.8	16.1	24.0	4.7					4.5	10.2
Madhya Pradesh	22.9	32.8	15.4		24.0	4.9					4.6	34.5
Punjab	30.2	8.8	14.9	15.8		6.1		23.2			4.7	16.1
Rajasthan	26.8	13.3	21.7	21.7	6.4	9.7					5.1	10.5
Uttar Pradesh (east)	17.7	18.5	24.9	28.6	5.1	5.2					6.4	13.7
Uttar Pradesh (west)	12.9	17.9	17.3	22.8	19.7	9.4					4.9	9.6
West Bengal and A&N islands	20.6	21.9	16.2	30.1		6.2	5.1				3.4	
Circle C												9.7
Assam	25.8	23.3	20.1				30.8				1.4	6.7
Bihar	39.7	33.8	15.2		7.2	4.0					4.1	26.6
Himachal Pradesh	39.6	22.2	28.9		2.7	5.3	1.3				0.9	11.1
North East	22.2	15.6	31.5				30.7				0.8	9.4
Orissa	34.7	25.7	21.8			7.6	10.2				1.9	14.8
J&K	43.0		47.8				9.2				0.8	-

Source: COAI, AUSPI, Compiled by Kotak Institutional Equities.

Metros accounted for 24% of the total adjusted gross revenues of the wireless operators in the June 2007 quarter

Circle	AGR (Rs mn)	% of total
Delhi	14,853	9.1
Mumbai	13,841	8.4
Chennai	5,532	3.4
Kolkata	4,714	2.9
Metros total	38,941	23.8
All India	163,807	100.0

Telecom operator wise AGR details, Jun '07

	Delhi		Mumbai		Chennai		Kolkata		Metros		All India	
	(Rs mn)	(%)	(Rs mn)	(%)	(Rs mn)	(%)	(Rs mn)	(%)	(Rs mn)	(%)	(Rs mn)	(%)
Bharti	5,675	38.2	3,263	23.6	1,954	35.3	1,170	24.8	12,062	31.0	49,054	29.9
Vodafone	3,157	21.3	4,133	29.9	780	14.1	1,384	29.4	9,454	24.3	28,158	17.2
RCOM	2,170	14.6	2,522	18.2	606	11.0	1,104	23.4	6,401	16.4	28,571	17.4
BSNL	—	—	—	—	790	14.3	530	11.2	1,320	3.4	22,291	13.6
Idea	1,467	9.9	—	—	—	—	—	—	1,467	3.8	12,849	7.8
TTSL	1,725	11.6	1,758	12.7	345	6.2	526	11.2	4,353	11.2	12,876	7.9
MTNL	661	4.4	1,023	7.4	—	—	—	—	1,684	4.3	1,684	1.0
Aircel	—	—	—	—	1,057	19.1	—	—	1,057	2.7	4,597	2.8
Spice	—	—	—	—	—	—	—	—	-	-	1,946	1.2
BPL	—	—	1,144	8.3	—	—	—	—	1,144	2.9	1,144	0.7
Others	—	—	—	—	—	—	—	—	-	-	638	0.4
Total	14,853	100.0	13,841	100.0	5,532	100.0	4,714	100.0	38,941	100.0	163,807	100.0

Source: TRAI, Kotak Institutional Equities.

MNP launch time and mobile penetration at the time of launch in various countries

Country	Year of launch	Mobile penetration at the time of launch
		(%)
Australia	Jun-01	57
Austria	Oct-04	97
Belgium	Sep-02	73
Canada	Mar-07	58
Denmark	Jul-01	65
Finland	Jul-03	89
France	Jun-03	64
Germany	Sep-02	71
Hong Kong	Mar-99	48
Ireland	Jul-03	83
Italy	Sep-02	91
Japan	Oct-06	74
Korea	Jan-04	70
Netherlands	Apr-99	27
Norway	Nov-01	82
Pakistan	Mar-07	33
Portugal	Jan-02	76
Singapore	Apr-97	16
Spain	Oct-00	58
Sweden	Sep-01	78
Switzerland	Mar-00	55
UK	Jan-99	51
US	Mar-03	51

Source: Industry sources, Kotak Institutional Equities.

Introduction of MNP saw a sharp increase in churn and substantial pricing pressure for the Finnish telecom operators

MNP case study: Finland

	Dec-03	Mar-04	Jun-04	Sep-04	Dec-04	Mar-05	Jun-05	Sep-05	Dec-05	
# of subscribers	4,749	4,789	4,829	4,891	4,950	5,066	5,128	5,209	5,292	
# of mobile number portings		381	300	211	321	564	366	319	215	
Portings as % of subs base		8.0	6.2	4.3	6.5	11.3	7.2	6.2	4.1	
Blended churn, leading operator (%)		20	37	31	22	26	34	29	25	18
Blended ARPU, leading operator (US\$/sub/month)		46	47	48	47	44	40	38	37	35
MOU, leading operator (min/sub/month)		164	236	249	258	267	265	285	278	281
RPM, leading operator (US cents)		28.2	20.0	19.1	18.4	16.4	15.0	13.3	13.1	12.6
EBITDA margin of the leading operator (%)		35.3	38.4	38.8	40.5	33.0	33.3	27.8	35.0	29.5

Note:

(1) MNP was launched in Finland in July 2003.

(2) Handset subsidy on 2G handsets is banned in Finland. 3G handset subsidies have been allowed since April 2006.

(3) Finland is among the few countries in the world where handset bundling is not allowed/ popular. This reflected in the high number of ports in Finland compared to other countries.

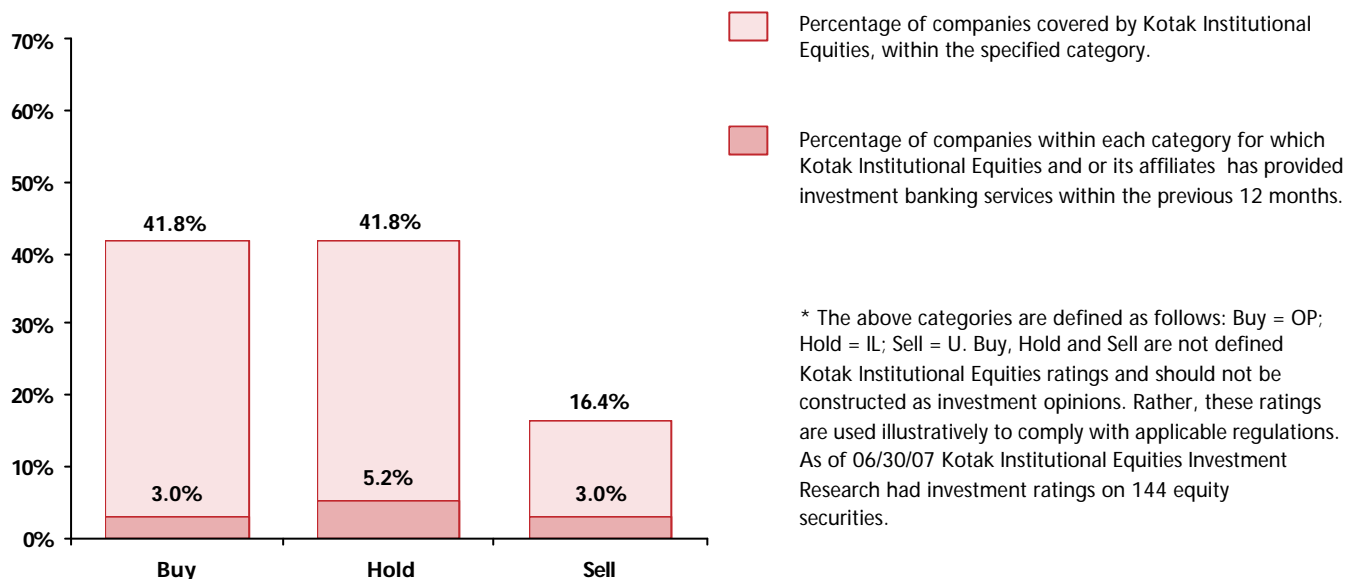
Increased churn led to severe pricing competition resulting in a sharp decline in revenue per minute (RPM) of the leading operator, TeliaSonera

Source: NUMPAC 2006, Telegeography, Kotak Institutional Equities.

"Each of the analysts named below hereby certifies that, with respect to each subject company and its securities for which the analyst is responsible in this report, (1) all of the views expressed in this report accurately reflect his or her personal views about the subject companies and securities, and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report: Kawaljeet Saluja."

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Distribution of ratings/investment banking relationships



* The above categories are defined as follows: Buy = OP; Hold = IL; Sell = U. Buy, Hold and Sell are not defined Kotak Institutional Equities ratings and should not be constructed as investment opinions. Rather, these ratings are used illustratively to comply with applicable regulations. As of 06/30/07 Kotak Institutional Equities Investment Research had investment ratings on 144 equity securities.

Source: Kotak Institutional Equities.

As of September 30, 2007

Ratings and other definitions/identifiers

New rating system

Definitions of ratings

BUY. We expect this stock to outperform the BSE Sensex by 10% over the next 12 months.

ADD. We expect this stock to outperform the BSE Sensex by 0-10% over the next 12 months.

REDUCE: We expect this stock to underperform the BSE Sensex by 0-10% over the next 12 months.

SELL: We expect this stock to underperform the BSE Sensex by more than 10% over the next 12 months.

Old rating system

Definitions of ratings

OP = Outperform. We expect this stock to outperform the BSE Sensex over the next 12 months.

IL = In-Line. We expect this stock to perform in line with the BSE Sensex over the next 12 months.

U = Underperform. We expect this stock to underperform the BSE Sensex over the next 12 months.

Our target price are also on 12-month horizon basis.

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Coverage view. The coverage view represents each analyst's overall fundamental outlook on the Sector. The coverage view will consist of one of the following designations: Attractive (A), Neutral (N), Cautious (C).

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