

Telecoms, Media & Technology  
 Telecoms  
 Equity – India

## Indian Telecoms

More spectrum likely, change in reserve price unlikely

- ▶ **Spectrum reserve price unlikely to be revised downwards**
- ▶ **Don't expect meaningful participation from incumbent telcos, RIL participation debatable**
- ▶ **Retain OW on Bharti and TP of INR406**

**More spectrum but no change to reserve price.** We believe there may not be significant changes to the auction reserve price. However, we expect the regulator to make more spectrum available for auction. TRAI clarifications have already suggested more spectrum being made available. In our view, an average c10Mhz of 2G spectrum could be made available.

**Likely bidders.** We expect Idea (seven impacted circles only) and Uninor (selective participation) to participate in spectrum auctions and don't expect meaningful participation from Bharti and Vodafone, as bidding intensity could adversely impact license renewal payouts. Separately, Bharti may add more BWA spectrum, in our view, given that 700MHz auctions look delayed and Reliance Industries' (RIL IN, N, TP INR800) BWA launch is getting more visible.

**RIL factor.** We believe that data remains core to its strategy and it doesn't seem to be in a hurry to provide voice and likely to focus on VOIP (via existing spectrum), in our view. That said, it may need spectrum for a fall back (as an interim voice solution). While upcoming auctions could be an option, there are other alternatives available as well such as M&A and as such its participation in the upcoming auctions remains a matter of debate. We believe RIL may benefit most from procuring 900/700MHz and re-farming of 900MHz spectrum will be positive for RIL. In the interim, RIL is likely to offer data cards, similar to what Bharti is doing. Key for RIL will be ability to arrive at mechanisms to provide dense coverage in a cost effective manner given the in-building penetration issues with 2,300MHz spectrum.

**Impact on tariffs.** As there is no immediate increase in costs for incumbents like Bharti, Vodafone, Tata, and RCOM; we see fewer possibilities for immediate headline rate hikes. However, minute discounting is likely to ease as costs for both Uninor and Idea input costs are likely to rise and as both of them have been most aggressive on special tariff vouchers (reduction in discounts could improve voice realizations by c5% easily).

**Stock implications.** Bharti is our preferred pick in the sector with target price of INR406. The recent bump up in India capex suggests that Bharti is closing network gaps/increasing population coverage and allows it to play the minute game. We believe this not only allows Bharti to gain minute market share but also increases in revenue market share. We value Bharti using a blend of SOTP-based DCF analysis and PE. The key downside risk would be spectrum re-farming as it will be significantly disruptive for the telco.

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## Bharti may add more BWA spectrum

Qualcomm has spectrum holding in four circles, which account for 22% of total mobile revenues (these circles account for 18% of total Bharti revenues) and have no overlap with Bharti's BWA presence. In our 23 April note, [Recovery driven by Voice](#), we highlighted that Bharti's purchase of the BWA spectrum of Qualcomm (reported by Reuters, Bharti in talks for stake in Qualcomm India unit-May 16, 2012) would be linked to RIL's rollout and timing of the 700MHz auctions. With the 700MHz auctions delayed (if we go by the recent TRAI recommendations) and RIL's 4G launch likely by the end of this year, it makes sense for Bharti to procure additional BWA spectrum in the metros of Mumbai and Delhi. We note that both Mumbai and Delhi are at 150% mobile penetration suggesting incremental growth driver in these markets is data only.

Separately as and when, government incentivises data growth, BWA players may benefit and Bharti may gain. To sum it up, we are of the view that purchase of Qualcomm spectrum would allow Bharti to mitigate risks from any possible disruption by RIL's 4G launch in addition to add the data card revenue stream and address the residential broadband space where telemedia business cannot reach. We believe Bharti with its 900/1,800 spectrum and mobile coverage in metros may be better off than RIL, in terms of providing voice fall back and providing residential broadband. In terms of payout, we believe except for Bharti there may not be many buyers of this spectrum from Qualcomm, and with Bharti having a presence in four markets with LTE already, the opportunity is more viable for Bharti than others. In our view, payout to obtain this spectrum may not be more than 1.1x-1.3x of the price paid by Qualcomm to obtain this spectrum. We believe the key rationale for Qualcomm to purchase this spectrum was to encourage adoption to LTE by all service providers, which procured BWA spectrum and, in our view, this is in place.

Figure 1: Qualcomm's BWA spectrum

Circles	Spectrum (MHz)	Contribution to Bharti's Revenue	Price Paid (USDm)	Premium/ Discount to BWA pan India Average	Discount to 3G auction price in the same circle
Haryana	10	1%	24	0.2x	0.3x
Kerala	10	2%	52	0.4x	0.4x
Delhi	10	10%	448	3.8x	0.3x
Mumbai	10	4%	459	3.9x	0.4x

Source: TRAI

Figure 3 : Spectrum available for refarming

	Available spectrum in 1800 MHz band	Spectrum Required for Auction( MHz)	Spectrum available for refarming( MHz)	Spectrum required for refarming including PSUs ( MHz)	Balance Spectrum (MHz)
Andhra Pradesh	37.0	13.0	24.0	16.2	7.8
Gujarat	22.0	13.0	9.0	18.4	-9.4
Karnataka	33.8	13.0	20.8	16.2	4.6
Maharashtra	28.0	13.0	15.0	16.4	-1.4
Tamil Nadu	47.4	13.0	34.4	10.4	24.0
Haryana	26.4	13.0	13.4	16.6	-3.2
Kerala	45.6	13.0	32.6	16.6	16.0
Madhya Pradesh	35.6	13.0	22.6	16.6	6.0
Punjab	19.0	13.0	6.0	21.8	-15.8
Rajasthan	3.2	13.0	-9.8	18.4	-28.2
U.P. (East)	17.6	13.0	4.6	10.2	-5.6
U.P. (West)	21.4	13.0	8.4	10.4	-2.0
West Bengal	21.6	13.0	8.6	10.6	-2.0
Assam	25.8	13.0	12.8	10.4	2.4
Bihar	13.2	13.0	0.2	10.4	-10.2
Himachal Pradesh	19.6	13.0	6.6	16.6	-10.0
J&K	15.2	13.0	2.2	8.0	-5.8
North East	29.0	13.0	16.0	13.0	3.0
Orissa	40.0	13.0	27.0	10.4	16.6
Delhi	18.4	13.0	5.4	22.2	-16.8
Kolkata	40.6	13.0	27.6	16.4	11.2
Mumbai	20.6	13.0	7.6	22.2	-14.6

Source: TRAI

Figure 4: License Renewal Timeline

	Bharti	Vodafone	Idea
Andhra Pradesh	2015	2021	2015
Gujarat	2021	2015	2015
Karnataka	2016	2021	2016
Maharashtra	2021	2015	2015
Tamil Nadu	2014	2015	
Haryana	2021	2015	2015
Kerala	2021	2015	2015
Madhya Pradesh	2021	2027	2015
Punjab	2015	2021	2016
Rajasthan	2016	2015	2021
U.P. (East)	2024	2015	2021
U.P. (West)	2021	2024	2015
West Bengal	2024	2024	
Assam	2024	2026	
Bihar	2024	2026	2026
Himachal Pradesh	2015	2026	2021
J&K	2024	2026	
North East	2025	2026	
Orissa	2024	2026	
Delhi	2014	2014	2021
Kolkata	2014	2014	
Mumbai	2021	2014	2026

Source: TRAI, Cells in Pink indicate 1,800 Mhz, in Grey indicate 900Mhz

Figure 5: Spectrum in various bands

	700 Mhz	2100 Mhz	2300 Mhz
AP	30	0	20
Gujarat	30	0	20
Karnataka	30	0	20
Maharashtra	30	0	20
Tamil Nadu	30	0	0
Haryana	30	0	10
Kerala	30	0	20
M.P.	30	0	20
Punjab	30	0	0
Rajasthan	30	0	0
UP - East	30	0	0
UP - West	30	0	0
West Bengal	30	0	0
Assam	30	0	20
Bihar	30	0	20
H.P.	30	0	20
J&K	30	0	20
North East	30	0	20
Orissa	30	0	20
Delhi	30	0	20
Kolkata	30	0	0
Mumbai	30	0	20
Total	660	0	290

Source: TRAI

Figure 6: Likely bidders in upcoming 2G auction

	Uninor	Idea	Bharti/ Vodafone	Tata (assuming they bid in markets they are getting traction)	RIL	Price/ Mhz (USD)	Price/Mhz/Pop (USD)
Andhra Pradesh	5	0	May bid	1.25	Its participation	59	0.8
Gujarat	5	0	selectively.		remains	47	0.9
Karnataka	5	0		1.25	debatable in our	68	1.3
Maharashtra	5	0		1.25	view and we	54	0.7
Tamil Nadu	5	5			believe they may	63	1.0
Haryana	0	0		1.25	be interested in	10	0.5
Kerala	5	0			lower spectrum	14	0.4
Madhya Pradesh	0	0			such as 900/700	11	0.2
Punjab	0	0			Mhz	14	0.6
Rajasthan	0	0				14	0.2
U.P. (East)	5	0				16	0.2
U.P. (West)	5	0				22	0.2
West Bengal	5	5				5	0.1
Assam	0	5				2	0.1
Bihar	5	0				9	0.1
Himachal Pradesh	0	0				2	0.3
J&K	0	5				1	0.1
North East	0	5				2	0.2
Orissa	5	5				4	0.1
Delhi	0	0		1.25		143	10.4
Kolkata	5	5		1.25		24	3.0
Mumbai	5	0		1.25		140	7.0
Estimated Amount payable (USDm)	2,629	507		445			

Source: HSBC

## Bharti: valuation and risks

We have an Overweight rating on Bharti with a target price of INR406. We value Bharti using a blend of SOTP-based DCF analysis and PE. Our valuation has two components: India and the Africa operations. We value the tower division along with the India business, which we value on a mix of equally weighted PE and DCF. For our DCF analysis, we assume a WACC of 12% and a cost of equity of 13% (cost of debt 10.5%) to arrive at a value of INR602 per share. For the purpose of our PE methodology, we use a PE of 16x and apply this to our FY13e EPS to arrive at a fair value INR294 per share. Our target price includes a negative adjustment for the TRAI recommendations of INR48; however, we see a small chance of these recommendations being accepted in the current format. We value the Africa business through DCF methodology assuming WACC of c13% to arrive at a value of -INR16 per share. Under our research model, for stocks without a volatility indicator, the Neutral band is 5ppts above and below the hurdle rate for Indian stocks of 11%. At the time we set our target price, it implied a potential return that was above the Neutral band; therefore, we rate the stock Overweight Potential return equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated. Key downside risks include re-farming of spectrum in 900 MHz band and revision of termination charges. Key catalysts include faster-than-estimated margin improvement in Africa and an accelerated enrolment of subscribers for 3G services.

Figure 7: Bharti Target Price Computation

(INR)	assumptions	value per share (INR)
India business	PE and DCF method	469
Africa business	DCF	-16
Adjustment for TRAI recommendations		-48
Target price		406

Source: HSBC

# Disclosure appendix

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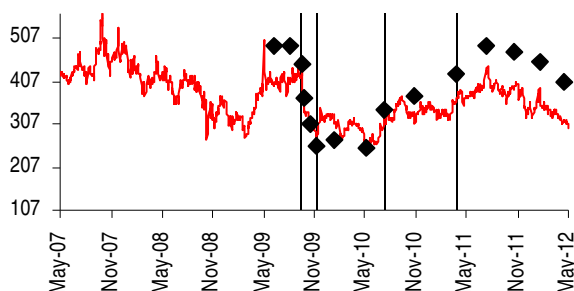
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Bharti Airtel (BRTI.BO) Share Price performance INR Vs HSBC rating history



Source: HSBC

Recommendation & price target history

From	To	Date
Overweight (V)	Neutral (V)	30 September 2009
Neutral (V)	Underweight (V)	24 November 2009
Underweight (V)	Neutral (V)	26 July 2010
Neutral (V)	Overweight	12 April 2011
Target Price	Value	Date
Price 1	488.50	22 June 2009
Price 2	488.50	18 August 2009
Price 3	448.00	30 September 2009
Price 4	368.00	07 October 2009
Price 5	305.00	01 November 2009
Price 6	254.00	24 November 2009
Price 7	270.00	24 January 2010
Price 8	250.00	20 May 2010
Price 9	341.00	26 July 2010
Price 10	370.00	08 November 2010
Price 11	425.00	12 April 2011
Price 12	488.00	25 July 2011
Price 13	475.00	04 November 2011
Price 14	451.00	08 February 2012
Price 15	406.00	02 May 2012

Source: HSBC

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BHARTI AIRTEL	BRTI.NS	297.55	16-May-2012	2,6,7

Source: HSBC

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