

May 31, 2011

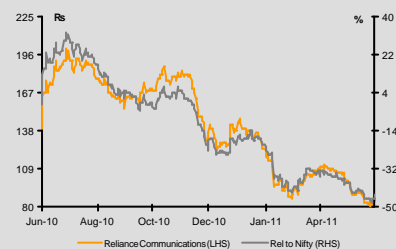
Reco	Previous Reco
Reduce	Reduce
CMP	Target Price
Rs88	Rs85
EPS change FY12E/13E (%)	-24.2/-22.4
Target Price change (%)	NA
Sensex	18,232
Nifty	5,473

Price Performance

(%)	1M	3M	6M	12M
Absolute	(12)	(0)	(31)	(41)
Rel. to Nifty	(7)	(2)	(26)	(45)

Source: Bloomberg

Relative Price Chart



Source: Bloomberg

Stock Details

Sector	Telecommunications
Bloomberg	RCOM@IN
Equity Capital (Rs mn)	10320
Face Value(Rs)	5
No of shares o/s (mn)	2064
52 Week H/L	205/75
Market Cap (Rs bn/USD mn)	181/4,016
Daily Avg Volume (No of sh)	4880078
Daily Avg Turnover (US\$m)	10.7

Shareholding Pattern (%)

	Mar-11	Dec-10	Sep-10
Promoters	67.9	67.9	67.7
FII/NRI	9.5	9.7	9.7
Institutions	9.0	9.1	9.2
Private Corp	2.0	2.1	2.2
Public	11.7	11.3	11.2

Source: Capitaline

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- Change in accounting policy to include IRU sales of 25.5bn led to spike in revenues. Ex-IRU revenue, topline improved by just 1.3% qoq. Mobility revenue was up 3.3% qoq
- ARPU fell 3.5% QoQ to Rs107 purely on MOU decline as RPM remains stable. Wireless traffic improved 3.2% on the back of paid minutes coming on network
- Net profit slumps to Rs1.7bn declining 64.9% qoq, led by lower margins across the business segments. Capex guidance at 15bn for FY12E, positive for peers
- Maintain our REDUCE rating with target price of Rs85
Valuations at 5.6x and 4.7x EV/EBIDTA for FY12E and FY13E respectively

Change in accounting policy boots Rev. & EBITDA but PAT takes a hit

The key thing in the Q4FY11 was the change in accounting policy for charging IRU sales from straight line method to recognizing upfront. Revenues at Rs74.7bn (including IRU sales of Rs25.5bn) improved 53.6% qoq. Mobility revenue at Rs41.9bn was up 3.3% qoq. It is betting high on the data usage with the higher spectrum availability post erosion of free mins. EBITDA Ex-IRU sales declined 23.1% qoq to Rs11.7bn (below our estimate of Rs15.9bn), due to margin pressure across the business segments. Due to network expansion network operating exp expanded 22.7% QoQ. PAT of Rs1.7bn declined 64.9% qoq, lowest in last four years.

Capex guidance at Rs15.0bn – positive for peers

The company has guided for Rs15.0bn capex for FY12E. The lower capex is primarily attributed to the balance sheet constraint. With the huge debt on the balance sheet and impending FCCB redemption in FY12E leaves limited scope of further fund raising for additional capex. However, it comes as a positive for its peers (Bharti, Idea in listed space) in the industry as there would be limited competitive intensity.

EPS est. cut by 24.2%/22.4% for FY12E/13E

Considering the increased pressure on margins and higher depreciation as the company has not yet started charging for 3G spectrum, we have cut EPS estimate by 24.2%/ 22.4% for FY12E/13E. The company would also charge premium paid for redemption of FCCB in Q1FY12E, which would escalate interest cost in FY12E. We believe the margin pressure would continue for current fiscal as company is still reducing free minutes on network and due to higher network operating expense pertaining to 3G expansion.

Maintain REDUCE with target price of Rs85

We maintain our REDUCE rating on the stock with target price of Rs85. At CMP of Rs88, the stock trades at 5.6x and 4.7x EV/EBIDTA and 17.6x and 12.6x our revised EPS for FY12E and FY13E respectively. High debt on books remains prime risk especially given the pressure on profitability of the company. Nevertheless, stake sale in tower business would key trigger for the stock in near term.

Financial Snapshot

Rs Mn

Y/E	Net Sales	EBITDA (Core)	EBITDA (%)	PAT (Rs)	EPS (Rs)	EPS %chg	ROE (%)	P/E	EV/EBITDA	P/BV
FY10	214964	71852	33.4	44554	21.6	-27.3	5.7	4.1	6.6	0.4
FY11P	224304	84042	37.5	11400	5.5	-74.3	2.1	15.9	6.5	0.4
FY12E	220790	70034	31.7	10337	5.0	-9.8	2.4	17.6	7.3	0.4
FY13E	235915	77093	32.7	14436	7.0	39.7	3.3	12.6	6.1	0.4

EPS by 24.2% / 22.4% for FY12E / 13E

	FY11P	FY12E			FY13E		
		Old	New	Chg %	Old	New	Chg %
Revenues	22430.4	21,496.7	22079.0	2.7	23,546.7	23591.5	0.2
EBIDTA	8404.2	6,967.7	7003.4	0.5	8,264.3	7709.3	(6.7)
EBIDTA %	37.5	32.4	31.7	-69 bps	35.1	32.7	-242 bps
PAT	1145.4	1364.5	1033.7	(24.2)	1861.1	1443.6	(22.4)
EPS	5.5	6.6	5.0	(24.2)	9.0	7.0	(22.4)

Wireless business performance

	3Q10	4Q10	1Q11	2Q11	3Q11	4Q11	QoQ %
Revenues	40,225	40,900	41,528	41,613	40,644	41,978	3.3
EBIDTA	12,550	11,815	11,989	12,101	11,792	11,490	-2.6
EBIDTA %	31.2	28.9	28.9	29.1	29.0	27.4	-164bps
Subs ('000)	93,796	102,422	110,806	117,337	125,652	135,718	8.0
ARPU (Rs)	149	139	130	122	111	107	-3.6
MOU (mins)	330	318	295	276	251	241	-4.0
RPM (Re)	0.45	0.44	0.44	0.44	0.44	0.44	0.0
Minutes (bn)	89.1	93.6	94.4	94.5	91.5	94.5	3.3

Quarterly financials

Particulars	Q4FY10	Q1FY11	Q2FY11	Q3FY11	Q4FY11	YoY (%)	QoQ (%)	YTD'11	YTD'10	YoY (%)
Wireless	40,900	41,528	41,613	40,644	41,978	2.6	3.3	165,763	169,156	(2.0)
Global	20,278	18,137	18,391	19,233	44,758	120.7	132.7	100,519	81,583	23.2
Broadband	6,798	6,763	6,617	6,184	6,906	1.6	11.7	26,470	28,385	(6.7)
Others	1,833	2,941	3,031	1,716	-378			7,310	5,437	
Total gross Sales	69,809	69,369	69,652	67,777	93,264	33.6	37.6	300,062	284,561	5.4
Inter-segmental elimination	19894	18684	19422	19127	18524	(6.9)	(3.2)	75756.7	68418.5	10.7
Net Sales	49,915	50,685	50,230	48,650	74,740	49.7	53.6	224,305	216,143	3.8
Network Operating	15251.0	13078.7	13813.0	12493.0	15331.0	0.5	22.7	54,716	61,734	(11.4)
as % of sales	30.6	25.8	27.5	25.7	20.5			24.4	28.6	
Employee Expenses	3396.0	3535.0	3596.4	3558.4	4067.0	19.8	14.3	14,757	15,001	(1.6)
as % of sales	6.8	7.0	7.2	7.3	5.4			6.6	6.9	
Access Charge	6293.5	6610.3	6571.7	6639.6	6654.6	5.7	0.2	26,476	21,377	23.9
as % of sales	12.6	13.0	13.1	13.6	8.9			11.8	9.9	
License Fee	2668.1	3101.8	3033.3	2829.9	2606.7	(2.3)	(7.9)	11,572	11,451	1.1
as % of sales	5.3	6.1	6.0	5.8	3.5			5.2	5.3	
Administrative expenses	7300.0	8445.8	7574.0	7840.0	8881.0	21.7	13.3	32,741	34,071	(3.9)
as % of sales	14.6	16.7	15.1	16.1	11.9			14.6	15.8	
Total operating expenditure	34909	34772	34588	33361	37540	7.5	12.5	140261	143634	(2.3)
EBITDA	15006.7	15913.4	15641.5	15289	37200	147.9	143.3	84,044	72,509	15.9
Depreciation	10847.0	9647.7	9553.0	10337.7	35500.0	227.3	243.4	65038.4	37465.6	73.6
EBIT	4159.7	6265.7	6088.5	4951.3	1699.8	(59.1)	(65.7)	19005	35043	(45.8)
Other Income	1011.7	407.0	953.1	1391.1	4021.6	-	-	6772.8	6359.0	6.5
Interest	-8134.0	6396.7	2797.0	1296.3	2234.0	(127.5)	72.3	12724.0	-9861.5	(229.0)
Business restructuring exp.	15.0	0.0	0.0	0.0	-123.0			-123.0	375.1	
PBT	13290.4	276.0	4244.6	5046.1	3610.4	(72.8)	(28.5)	13177.1	50888.3	(74.1)
Tax	1923.0	-718.6	-660.9	-213.7	1711.0	(11.0)	(900.7)	117.8	4453.6	(97.4)
PAT before MI	11367.4	994.6	4905.5	5259.8	1899.4	(83.3)	(63.9)	13059.3	46434.7	(71.9)
MI	-826.0	489.1	447.0	454.2	112.4			1502.7	1371.1	9.6
Profit from Associates	0.0	3.4	0.8	-3.0	-99.8			-98.5	-23.0	328.3
PAT	12193.4	508.9	4459.3	4802.6	1687.2	(86.2)	(64.9)	11458.1	45040.6	(74.6)

Margins (%)					bps chg	bps chg			bps chg	
EBIDTA	30.1	31.4	31.1	31.4	49.8	1,971	1835	37.5	33.5	392
EBIT	8.3	12.4	12.1	10.2	2.3	(606)	-790	8.5	16.2	(774)
EBT	26.6	0.5	8.5	10.4	4.8	(2,180)	-554	5.9	23.5	(1,767)
PAT	22.8	2.0	9.8	10.8	2.5	(2,023)	-827	5.8	21.5	(1,566)
ETR	14.5	(260.4)	(15.6)	(4.2)	47.4	3,292	5163	0.9	8.8	(786)

Financials

Profit & Loss

Y/E, Mar (Rs. mn)	FY10	FY11P	FY12E	FY13E
Net Sales	214,964	224,304	220,790	235,915
<i>Growth (%)</i>	-3.4	4.3	-1.6	6.9
Employee cost	15,001	14,757	16,951	18,270
Marketing expenses	35,328	32,741	35,251	35,739
Access charge	21,377	26,476	27,601	28,848
Network operating charge	59,955	54,716	58,952	63,465
License fee	11,451	11,572	12,000	12,501
Total operating expenditure	143,112	140,261	150,756	158,822
EBITDA	71,852	84,042	70,034	77,093
<i>Growth (%)</i>	-16.4	17.0	-16.7	10.1
Depreciation	55,705	65,039	47,394	51,235
Other non-operating expenses	-17,865	-67	0	0
EBIT	34,012	19,071	22,640	25,858
<i>EBIT margin (%)</i>	15.8	8.5	10.3	11.0
Other Income	6,359	6,773	4,000	2,800
Interest expenses	-9,862	12,724	13,285	10,006
PBT	50,233	13,120	13,355	18,652
Tax	4,454	118	1,870	2,611
<i>Effective tax rate (%)</i>	8.9	0.9	14.0	14.0
PAT before MI	45,779	13,002	11,485	16,040
Share of MI and Associates	1,224	1,602	1,149	1,604
Adjusted PAT	44,554	11,400	10,337	14,436

Cash Flow Statement

Y/E, Mar (Rs. mn)	FY10	FY11P	FY12E	FY13E
PBT	43,836	6,302	9,355	15,852
Depreciation	55,705	65,039	47,394	51,235
Interest	-9,862	12,724	13,285	10,006
Other Non-Cash items	-18,891	-1,108	-1,207	-1,207
Chg in working cap	3,465	-6,212	46,548	-1,372
Tax paid	-4,454	-118	-1,870	-2,611
Operating Cashflow	69,800	76,626	113,505	71,902
Capital expenditure	-41,194	-115,850	-15,000	-30,000
Free Cash Flow	28,606	-39,224	98,505	41,902
Other income	6,359	6,773	4,000	2,800
Investments	54,016	-99	0	0
Investing Cashflow	19,181	-109,176	-11,000	-27,200
Equity Capital Raised	0	0	0	0
Loans Taken / (Repaid)	-94,472	75,527	-35,000	-40,000
Interest Paid	9,862	-12,724	-13,285	-10,006
Dividend paid (incl tax)	0	0	0	0
Financing Cashflow	-84,611	62,803	-48,285	-50,006
Net chg in cash	4,370	30,253	54,220	-5,304
Opening cash position	17,625	21,995	52,248	106,468
Closing cash position	21,995	52,248	106,468	101,164

Balance Sheet

Y/E, Mar (Rs. mn)	FY10	FY11P	FY12E	FY13E
Equity share capital	10,320	10,320	10,320	10,320
Reserves & surplus	440,097	450,343	459,472	472,701
Net worth	450,417	460,663	469,793	483,021
Minority Interest	6,549	8,052	9,200	10,804
Loan Funds	297,150	372,677	337,677	297,677
Net deferred tax liability	281	281	281	281
Total Liabilities	754,397	841,673	816,951	791,784
Gross Block	786,653	964,060	989,060	1,019,060
Less: Depreciation	190,668	255,707	303,101	354,336
Net block	595,985	708,353	685,959	664,724
Capital work in progress	116,557	55,000	45,000	45,000
Investment	93,824	93,824	93,824	93,824
Current Assets	135,383	204,184	265,604	274,635
Inventories	5,446	5,615	6,483	7,737
Sundry debtors	33,117	52,918	58,385	61,835
Cash & bank balance	21,995	52,248	106,468	101,164
Loans & advances	54,098	67,026	63,240	68,872
Other current assets	20,726	26,377	31,028	35,028
Current lia & Prov	187,351	219,688	273,436	286,399
Current liabilities	147,085	172,471	214,668	224,845
Provisions	40,267	47,217	58,769	61,555
Net current assets	-51,969	-15,504	-7,832	-11,764
Total Assets	754,397	841,673	816,951	791,784

Ratios

Y/E, Mar	FY10	FY11P	FY12E	FY13E
Profitability (%)				
Core EBITDA Margin	33.4	37.5	31.7	32.7
Net Margin	6.8	8.4	8.8	9.4
ROCE	2.9	3.2	3.2	3.6
ROE	5.7	2.1	2.4	3.3
Per Share Data (Rs)				
EPS (adjusted)				21.6
CEPS	30.7	36.2	28.5	32.6
BVPS	221.4	227.1	232.1	239.3
DPS	0.8	0.5	0.5	0.5
Valuations (x)				
PER	4.1	15.9	17.6	12.6
P/CEPS	2.9	2.4	3.1	2.7
P/BV	0.4	0.4	0.4	0.4
EV / Sales	2.2	2.4	2.3	2.0
EV / EBITDA	6.6	6.5	7.3	6.1
Dividend Yield (%)	1.0	0.6	0.6	0.6
Gearing Ratio (x)				
Net Debt/ Equity	0.6	0.7	0.5	0.4
Net Debt/EBITDA	4.1	4.4	4.8	3.9

Recommendation History: Reliance Communications – RCOM IN

Date	Reports	Reco	CMP	Target
15/02/2011	Reliance Communication Q3FY11 Result Update	Reduce	97	85
19/11/2010	Reliance Communication Q2FY11 Result Update	Reduce	154	135
16/08/2010	Reliance Communication Q1FY11 Result Update	Hold	168	180
28/06/2010	Reliance Communication Event Update	Accumulate	201	228

Recent Research Reports

Date	Reports	Reco	CMP	Target
30/05/2011	Jagran Prakashan Q4FY11 Result Update	Buy	120	149
23/05/2011	LMW Q4FY11 Result Update	Accumulate	2,126	2,535
19/05/2011	DB Corp Q4FY11 Result Update	Hold	240	271
18/05/2011	HT Media Q4FY11 Result Update	Buy	156	183

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