

# Bidding Over, Battle Begins

## The 3G verdicts are out. The three successful bidders for each of the 22 circles are now known. But who are the real winners? Joji Thomas Philip & Deepali Gupta delve deep into the auction strategies to decode the final outcome

### BHARTI AIRTEL DEFENDING ITS LEADERSHIP

HE IS the king of the hill. And he sure knows how to defend his turf. The thirteen 3G licences bagged by Suni Mittal-promoted Bharti Airtel cover 59% of India's cellular subscribers and 61% of revenues — this is the maximum 3G coverage any telecom operator has managed. Data released by sector regulator Trai reveal that regions where Bharti has bagged 3G spectrum contributes about 70% of its revenues. Put simply, Bharti Airtel has protected a big chunk of its 2G footprint.

Here's another way to look at how well Bharti has defended its fortress — in the nine circles where Bharti has lost the licence, its average revenue per user (ARPU) is 15-20% lower than the national ARPU. In other words, Bharti has defended its most lucrative markets. But there's one glitch — in these nine circles, Bharti is still among the top three. That position may now erode as customers may switch to rivals who have won 3G spectrum in these circles.

Industry watchers say its 3G bid is equivalent to six months of its revenues in these 13 zones — the lowest in the industry. Moreover, its total bid amount is only 12% of its current market cap, easily the least amongst all listed telecom companies who were successful in the auctions.

"On financing, Bharti is still best placed at 0.7x debt to Ebitda and 3x even after including the \$8.5bn raised for the ongoing Zain deal," point out security firm CLSA's analysts Deepti Chaturvedi and Surabh Mehrotra.

"In metro markets, about 10% subscribers account for about 35-40% of revenues. A large number of them would already have 3G-enabled handsets that will enable incumbents such as Bharti to quickly transition these subscribers to its 3G network. This will allow for a quick build-up of traffic on its 3G network and allow Bharti to extract the cost efficiencies of a 3G network," research analysts Srinivas Rao and Amyr Pirami at Deutsche Bank said in a note on Wednesday.

Bharti executives point out that large parts of its networks are already 3G-ready as the telco had begun upgrading its networks over the last 24-months — a step that will enable it to deploy 3G speedily and with minimum capex.

Revenues Defended:	70%
Market Covered:	61%
Total Bid as a percentage of Revenues:	35%
ARPU in winning circles:	Rs 245.8
ARPU in losing circles:	Rs 228.3
Amount bid per Rs 100 crore of revenue in winning circle:	Rs16.23 cr

### VODAFONE THE CHERRY PICKER

VODAFONE KNEW what it wanted and got it. It is not fretting about the rest. It has won only nine circles, while even smaller rivals like Aircel and Idea Cellular have won 13 and 11 respectively. But that is not such a bad thing. These nine circles cover 68% of its current 2G revenue base.

Vodafone has defended the best of its sweet spots. The company is among the top three by revenue in all nine circles that it won. India's second largest GSM operator by subscribers went hammer and tongs after high-revenue circles Delhi and Mumbai, and won. A score particularly in Delhi where it is fourth in terms of subscribers.

The company won spectrum in three metros, three 'A' class and three 'B' class circles. It stayed away from 'C' class circles that may have come cheaper, but had a lower revenue potential, said Samaresh Parida, director strategy, Vodafone Essar.

The nine circles account for 52% of total revenues for the sector. The company will be able to offer 3G services to around 57% of its customer base. The company will pay Rs11,618 crore for 3G spectrum in these circles that generate around double that revenue currently. The approximate average teledensity in the area was 77 mobile connections for every 100 potential cell phone users.

"We evaluated based on many parameters including cost per Mhz per person and penetration of 3G mobile handsets," Parida said. Average monthly revenue per user, a key measure of profitability, for circles it won 3G spectrum was Rs 244.2, while that for the circles it lost was Rs 162.3, as per an estimate by brokerage Edelweiss Capital.

Given the higher teledensity in the circles it has won spectrum, the spectrum cost per user will be lower. Analysts also said that in highly penetrated circles, quality of service is a big issue. With 3G spectrum, Vodafone will be able to improve service and accommodate more subscribers on its network. Parida has a different view.

"The business dynamics will change over the next three to five years. Share of revenue from data or value-added services will double in the mid-term." Around 11% of the company's revenue currently comes from value-added services. Vodafone has one of the highest value-added services revenue in the industry.

Revenues Defended:	68%
Market Covered:	52%
Total Bid as a percentage of Revenues:	50%
ARPU in winning circles:	Rs 244.2
ARPU in losing circles:	Rs 162.3
Amount bid per Rs 100 crore of revenue in winning circle:	Rs 17.89 cr

### AIRCEL CORRIDOR OF CERTAINTY

AIRCEL INDIA CEO GURDEEP Singh had a daunting task — he had to ensure that the service provider take its place with the biggies of Indian telecoms and yet not overbid. Aircel, 74% owned by Malaysia's Maxis, found the answer by adopting a strategy called Corridor of Contiguity, says Mr Singh.

"We went into the auctions with the aim of protecting our leadership in the circles we were strong, so we concentrated on circles like Tamil Nadu and the North-East. Once we had that, we looked for corridors of contiguity, where we went for all the southern circles (around Tamil Nadu) and Assam, West Bengal, Bihar and Orissa as these complete the North-East. Again, once we bid for J&K, we went for Punjab and UP (East) to open a new corridor," explained Mr Singh.

Aircel's strategy, which E&Y helped devise, has led to the telco emerging as the smartest bidder in the just concluded 3G auctions. Aircel has defended 93% of its revenues by bagging 3G in 13 circles — the highest amongst all telecom companies.

## Who Takes The Pole Position In The 3G Race

Contours of how 3G will shape the Indian telecom industry are starting to sharpen 24 hours after the utterly exhausting 34-day long spectrum auction process came to an end, and investment rationale of each player comes to light.

Not all winning bidders for each of the 22 circles will turn out to be winners. A dynamic and complex interplay of the current 2G footprint of each company, their new 3G coverage areas, the amount they will be paying as the winning bid, and the strength of their balance sheets to support funding will determine who makes the most of the 3G licences...and who suffers because of it.

There are three key metrics to watch out for. ET culled together these numbers for all the six key winners. First is 'revenues defended'. In their bidding strategies, telecom companies realised the importance of winning 3G licences in as many of the circles where they already had 2G operations.

This was of utmost importance — defend the markets they have already built and invested in. In circles where they have failed to do this, they are vulnerable to lose market share to the operators who now have 3G licences. The revenues defended metric indicates the percentage of their existing 2G markets each company has managed to protect by bagging 3G rights. (This is

measured in terms of revenues, not subscribers.)

The second metric is the percentage of the total addressable market each company has managed to cover. No company has managed to get a pan-India licence. Their real 3G reach is to be measured not by the number of circles they have won, but by the percentage of the total market (measured in revenues, not subscriber numbers) they have managed to cover.

The third is their total bid amounts expressed as a percentage of their current revenues. This will give a sense of the financial strain each company will come under as they service the licence payments.

This is crucial since the total 3G bids are far in excess of what the government had anticipated and what companies themselves had budgeted for. Bankers estimate the telecom companies had tied up Rs 35,000-40,000 crore from the banking system over a year ago. But with the total winning bids close to Rs 68,000 crore, telecom companies are likely to ask banks for top-ups.

Bankers say most companies have opted for bridge loans of a one-year tenure, hoping to raise external commercial borrowings (ECB). The Reserve Bank of India has allowed telecom operators to raise ECBs to fund their 3G rollouts. The following capsules on each of the six big winners unravel their bidding strategies and presents a clear picture of who the real winners are.



SUNIL MITTAL



VITTORIO COLAO



ANIL AMBANI



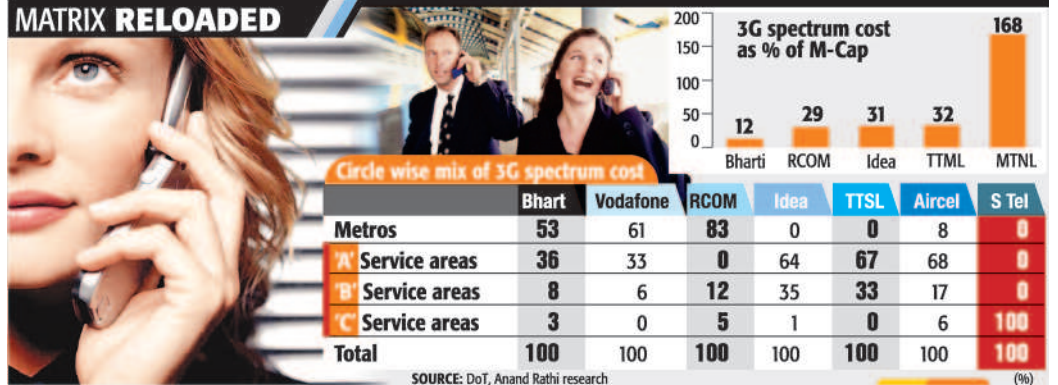
KUMAR MANGALAM BIRLA



RATAN TATA



GURDEEP SINGH



### RELIANCE COMM BIG CITY GAMBLE

RELIANCE COMMUNICATIONS went for the top and bottom circles in the value pyramid of service areas.

The company will spend 76% of its total investment in 3G spectrum on Mumbai and Delhi. In all it has bagged 13 circles for a price of Rs 8,585 crore compared with nine of Vodafone circles for Rs 11,618 crore.

Wins in Delhi and Mumbai give Reliance Communications an edge over its peers, because this may be its opportunity to catch up with Bharti and Vodafone — that lead in these mega-cities with a margin — and leave nine other operators in the circles far behind.

Because it started out with services based on CDMA technology, Reliance Communications lost out on customers that generate high revenue for service providers. The company's brand identity is also more immediately identified with low cost rather than luxury, which may change with 3G offerings, an analyst with an MNC brokerage said. Reliance Communications is also among the worst off in terms of funding. With net debt of Rs19,889 crore, the company debt to operating earnings for the just-ended financial year is 3.3. While the company has cash of around Rs 4,858 crore, not all of it can be deployed for spectrum, the analyst said.

"They will get the money, but it won't come cheap," said an analyst with a domestic brokerage. The company is also expected to bid aggressively for WiMax spectrum auction that will start soon, the analyst added.

The company did not respond to queries on how it plans to fund the purchase. The company is raising money through commercial paper according to a television report. Reliance Communications generates around 55% of its current revenue from the 13 circles it won spectrum in. These circles, broadly equivalent to states, account for around half the revenue of the Indian telecom sector's.

Average monthly revenue per user in the circles it won was Rs 119.9 compares with Rs 95.8 for the circles it lost, according to an estimate by brokerage Edelweiss.

The company's revenue must rise 33% to make its 3G spectrum viable, but if this helps it gain market share in Mumbai and Delhi this should be possible, analysts said.

Revenues Defended:	55%
Market Covered:	50%
Total Bid as a percentage of Revenues:	41%
ARPU in winning circles:	Rs 119.9
ARPU in losing circles:	Rs 95.8
Amount bid per Rs 100 crore of revenue in winning circle:	Rs 15.07 cr

### TATA TELE BIG MISSES

IT HAS won only nine circles and has managed to protect only 43% of its 2G revenue footprint. But Tata DoCoMo's president Deepak Gulati brushes aside the misses. Instead, he is happy to finally get rid of the late mover disadvantage the company was struggling with in the GSM space. He argues that the 3G auctions will enable his company to launch these services at the same time as that of other operators. "We were late entrants earlier (it was very late into the GSM party). Now, for the first time, we will launch simultaneously with other telcos," he said.

Still, the dismal numbers in Tata Tele's 3G scorecard are too obvious. With wins in only nine circles, the telco's 3G coverage of its 2G footprint is the lowest among the six successful bidders. These nine circles account for 44% of telecom sector's revenues — again the lowest amongst all leading operators.

"These figures are a comparison of the CDMA and GSM revenues, which does not present a correct picture. In the GSM space, our performance in the last one year since launch has been the best in the industry in terms of market share, rate per minute and brand," Gulati argued. But most analysts have termed the company's 3G bid a failure. "We did bid aggressively in Delhi and Mumbai and stepped aside after a point as we felt that winners' curse would be upon us if we continued," Gulati said.

Prior to the auctions, Tata Teleservices was touted to be amongst the most aggressive bidders, especially since 3G services have become synonymous with its JV partner — Japan NTT DoCoMo, which owns 26 per cent in the company. "They (DoCoMo) are basically the inventors of 3G," Gulati said. DoCoMo's experience of offering 3G services in Japan could help in faster and effective rollout. Yes... but Tata Tele will be rolling out 3G in less than half the addressable market.

Revenues Defended:	43%
Market Covered:	44%
Total Bid as a percentage of Revenues:	61%
ARPU in winning circles:	NA
ARPU in losing circles:	NA
Amount bid per Rs 100 crore of revenue in winning circle:	Rs 10.55 cr

### IDEA CELLULAR THE RURAL BET

IDEA CELLULAR lost the battle for Delhi and Mumbai, but won in 11 circles that contribute 81% of the company's revenues. These circles only account for 49% of the country's telecommunications market. But the strategy to buy into these fits with Idea's general philosophy. The company for long has been saying that the demand for value-added services and telephony is rising fastest in rural India, as the cell phones are the only mode of exposure to the world in these regions. GDP growth is leading to higher disposable income in these regions which will mostly be spent on mobile phone usage, chief executive Sanjeev Aga said a few months ago. Rural markets contribute over 40% of Idea's revenue.

The mobile service operator is not among the top three in any of the circles it lost. The mobile penetration in the circles it won is around 53%. The average monthly revenue per user in the circles it has won is at Rs 199 compared with Rs 146 in circles it lost.

The company also had its funding figured out before the bidding started. It has a line of credit for Rs 6,000 crore from a Swedish trade credit association which it can use for the purpose. It also has some leftover funds from sale of stake in subsidiary Aditya Birla Telecom to private equity player Providence. Idea will pay Rs 5,769 crore for its spectrum.

"Its bid is equivalent to six months of its revenues in those markets, and its average revenue market share in 3G markets is 21%, which augurs well from a payback perspective," said Deutsche Securities in a note to investors.

Revenues Defended:	81%
Market Covered:	49%
Total Bid as a percentage of Revenues:	41%
ARPU in winning circles:	Rs 198.9
ARPU in losing circles:	Rs 146
Amount bid per Rs 100 crore of revenue in winning circle:	Rs 9.62 cr

"Aircel has been the biggest positive surprise with 13 circle wins resulting in a payout of Rs 6,500 crore. Aircel management stated that the bidding strategy of Aircel was centred on the VAS potential of the circle apart from protecting the existing high-ARPU subscribers. The 13 circles where Aircel has won the 3G licence contribute 90% and 91% of the current subscriber and revenue base of Aircel," IDFC Securities's Charan Singh and Abhishek Gupta said in a note on Thursday.

Aircel has raised Rs 1,500 crore of debt from Standard Chartered for 3G. The company recently sold its tower business in a Rs 8500-crore deal.

These 13 circles also account for about 55% of India's telecom revenues, enabling it to occupy the second slot in this

parameter after Bharti Airtel. "We believe the company may possibly consider partnering with a foreign player in the future and, hence, bid aggressively covering 90% of its subscriber base," security research firm Edelweiss's analysts Ganesh Duvvuri and Devyani Javeri said in a note on Thursday.

At the same time, some industry officials also point out that Aircel would have to deliver quickly to relieve the pressure on its balance sheet as its 3G bid amount comes to over 130% of its current revenues, the highest among all telcos (except for MTNL). Besides, the bid amount is equivalent to 18 months of revenues from these circles, again the largest amongst all operators. Analysts also point out that if the 3G bid price were looked at based on the licence fee paid per existing subscriber, then Aircel had paid the highest — Rs 1,954 (\$42) per existing sub.

But Mr Singh, the CEO, is confident that the telco would be able to innovate smartly to circumvent these problems. His strategy: target the 90% of Indians whose first experience of the internet will be on the mobile phone. "If we can combine simple tariffs with innovative products and services, then we are confident that we can fill both the innovation and infrastructure gaps, thereby enhancing and changing the lives of our customers — that will be our unique model," he adds.