

#Industry » #Vodafone #Stock #SpectrumAuction2015 #RCom #Airtel

# Spectrum Auction: Cut-throat bidding leaves telecom scrips bleeding

*Investors worry about profitability of sector as bids top 94,000 crore*

Deepali Gupta | 10 March 2015, 8:55 AM IST

## Towering Troubles?

Govt is fast closing in on the record ₹1.06 lakh cr bagged from 2010 sale

Band	% of spectrum that is assured of getting sold	Assured revenues to govt
800	87 	2,037
900	100 	10,973
1800	64 	991
2100	76 	1,344
Total as of day 4		15,345

Source: Credit Suisse

**Cash outflow for renewing existing spectrum is already 56-83% above reserve prices**

The intense bidding seems to have taken a toll on telecom stocks

	Mar 3(₹)	Mar 9(₹)	%Fall
Bharti Airtel	348.95	343.55	-1.5
Idea Cellular	153.25	149.15	-2.7
RCom	66.25	62.90	-5.1
Sensex	29,593	28,844	-2.5



MUMBAI: Telecom companies raised their bids for airwaves to Rs 94,000 crore on Monday, closing in on 2010's record Rs 106,000 crore from spectrum sales, but investors and analysts expressed concerns about their future cash flow and profitability. "The marksituation being what it is, in the short to medium term, profitability and cash flows will take a hit. And margins will also

go down unless call rates are revised," said Hemant Joshi, partner at Deloitte Haskins & Sells.

Aggressive bidding by telecom companies, as they strive to protect existing airwaves in the 900 Mhz band, has seen licence renewal costs surge by more than 75% over the minimum price, according to brokerage CLSA. Reliance Communications, India's fourth-largest carrier, and No. 3 Idea Cellular - both of which have airwaves up for renewal in seven and nine circles, respectively - have underperformed the broader markets since the sale began on March 4, dropping 5.1% and 2.7%, respectively, at Monday's close. Shares of the Anil Ambani-run RCom slumped to a 52-week low of Rs 62.45. Market leader Bharti Airtel, which has the least at risk in the sale among the top four telcos since it has alternative bandwidth in most of its six renewal circles, has slipped 1.5%. To be sure, the benchmark Sensex has dropped 2.5% in the same period.

An executive at a leading telco said it would be wrong to attribute the slide in share prices of telecom companies just to the auctions. He pointed out that most stocks fell on Monday. But analysts said they had adopted a cautious attitude for the sector because of the high bids. "The ongoing spectrum auctions are continuing to beat market expectation on both pricing as well as demand for new spectrum. We remain cautious on the sector," Credit Suisse said in a note to clients. Raising call rates sufficiently to cover for the increased spectrum costs will be tough, given the existing competition as well as the impending entry of Mukesh Ambani-owned Reliance Jio Infocomm, also a major participant at the auctions, analysts noted.

## COMPETITIVE PRESSURES

A recent ET analysis revealed that for every Rs 100 crore more an operator spends on buying airwaves over the reserve price, its cost of hosting voice increases 0.8-1.5% per minute, which will need to be built into pricing. But competitive pressures on voice had in fact forced Idea to cut voice rates in the second quarter ended September 30, 2014, while Bharti Airtel and Vodafone have kept tariffs steady to avoid losing users. Bharti Airtel's CEO for India and South Asia Gopal Vittal told ET recently that call prices needed to be raised but that would happen over some years, not immediately after the auction.

At the end of day four (Saturday), intense bidding had pushed up costs just to buy back airwaves in the cost-efficient 900 Mhz band by 78% to Rs 22,740 crore for Idea, by 80% to Rs 6,110 crore for RCom, by 75% to Rs 14,180 crore for No. 2 ranked Vodafone India and by 74% to Rs 10,740 crore for Airtel, CLSA said in its report.

Credit Suisse noted that two of RCom's main circles, where it is fighting to keep its airwaves - Madhya Pradesh and Bihar - have seen renewal costs escalate by 75% and 172% over the reserve price, respectively. The two circles contribute 14.3% to its total revenue.

## POOR EBITDA

The ratio of debt to earnings before interest, tax, depreciation and amortisation (EBITDA) of Idea will rise to 3x because of spectrum-related costs, from about 1.1x now, according to ratings agency S&P. The ratio, however, will still be lower than that of most peers, excluding Bharti (about 2x).

"Reliance Communications' leverage will further increase to well above 5.5x from the already-high level of about 5x despite its lower spectrum outgo", because of the company's lower EBITDA, S&P said.

The agency expects Vodafone's leverage to rise to about 4x from about 3.5x now, but that's not of much worry thanks to parent Vodafone Group Plc. An analyst at a foreign brokerage said while the telcos won't face payment-related issues in the short term, the higher debt would hurt much-needed investment in 3G and 4G network rollouts, key to future growth. "What is more disturbing from an investor's standpoint is that all this debt for renewing airwaves won't add any revenue, and will directly hit the market cap."

## LITTLE ROOM TO BORROW

The analyst added that while the government mechanism allowing winners to pay 25% or 33% upfront depending on the airwaves band would provide shortterm relief, operators will have to show the overall winning amount due to the government as debt, which will mean their leeway to borrow more to support capex for network expansion will get restricted.

In 2014, Idea Cellular raised around Rs 4,800 crore and RCom raised more than Rs 6,000 crore, both via sale of shares. Bharti Airtel recently raised Rs 1,925 crore by selling shares in unit Bharti Infratel and has some room to sell more. Its challenge will be to balance what it spends and interest costs incurred given the continuing bleed in Africa.