RELIANCE COMMUNICATIONS LIMITED

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Transcript of Earnings Conference Call for the Quarter ended September 30, 2014

Conducted at 1.30 pm IST on November 17, 2014

Moderator:

Thank you for standing by and welcome to Reliance Communications' global earnings conference call on the Reliance Audio Conferencing platform.

This is Mamta, the moderator for this conference.

At this time, all the participants are in listen-only mode. There will be a presentation followed by a question and answer session at which time if you wish to ask a question, please press *1 on your telephone. Please be advised, this conference is being recorded today.

Today, we have the senior management team from Reliance Communications namely Mr. Vinod Sawhny (CEO – Reliance Communications), Mr. Gurdeep Singh (CEO – Wireless business), Mr. Bill Barney (CEO - GCX), Mr. Deepak Khanna (CEO – Enterprise business), Mr. Punit Garg (CEO – Carrier business), Mr. Manikantan Iyer (CFO – Reliance Communications), Mr. Rory Cole (CFO – GCX) and Mr. Anil Ladha (Head – Investor Relations).

The call will begin with some key observations by the management followed by a question and answer session. I must remind you that the overview and discussions today may include some forward-looking statements that must be viewed in conjunction with the risks that the company faces.

I hand over the call now to Mr. Vinod Sawhny. Thank you.

Vinod Sawhny:

Thanks, Mamta. Good afternoon and welcome to our second quarter 2015 earnings conference call. I have with me the senior management team of Reliance Communications. On behalf of us all, thank you for joining the call.

On Friday, November 14th, 2014, our Board of Directors adopted the results for the second quarter of the financial year 2014-15 ending September 30, 2014.

The Media Statement, Quarterly Report and the Results have been uploaded on our web site and I trust you have had a chance to go through the same.

To begin with, I would want to take you through the key financial & operational highlights for the quarter:

- **PAT:** Profit After Tax for the quarter stands at Rs. 153 Crore, a healthy sequential increase of 16.3%. In Q2 FY14, there was an accounting write back of Rs. 441 Crore due to Provision for Business Restructuring; hence, on a Y-o-Y basis the numbers are not directly comparable.

- **Revenue & EBITDA:** Q2 revenue stands at Rs. 5,403 Crore and EBITDA at Rs. 1,827 Crore, down ~2% from Q1, which is in line with the industry peer group and on account of seasonal factors.

- **EBIDTA margin:** Q2 EBITDA margin of 33.8% is amongst the highest in the industry, with strong contribution from both India and Global businesses.

- **Free Cash Flow:** RCOM generated operational cash flow (EBITDA) of Rs. 1,827 Crore in Q2, paid net finance charges of Rs. 670 Crore and invested Rs. 302 Crore on capex during the quarter. It remains free cash flow (FCF) positive and this is expected to continue

- **RPM & ARPU**: In Q2, overall RPM has sequentially increased to 44.4 paisa from 43.8 paisa; an improvement of 1.4%. ARPU for the quarter is Rs.137, up by 0.7 % on a sequential basis. We have improved RPM with tariff hikes, strong focus on paid & profitable minutes, and increase in data usage.

- **Data Subs & Traffic:** Total data traffic at 65,778 million MB for Q2, up 19% Q-o-Q and 75% Y-o-Y. Our data growth has been impressive - overall data customer base has grown by 3.8% Q-o-Q to 29.7 million; and 3G customers have increased 16.2% Q-o-Q to 15.1 million.

Here I would like to take this opportunity to spend some time on the potential of mobile data and how RCOM is geared to capture the upcoming growth.

Enormous untapped potential exists in mobile data to drive future growth:

While mobile internet users in India are growing at a rapid clip, less than a quarter of the nearly 810 million mobile subscribers are internet users. Smartphone shipments have crossed 5 million a month and set to more than double each year. Therefore, there is enormous headroom for growth. With data contribution still way below that of other growth markets, we believe that the sector is still in the initial phase of the data led growth curve.

RCOM is well poised to participate and lead in this future growth with all key enabling elements in place – excellent data network, strong device proposition, & strong ongoing traction in the data ecosystem supported by superior customer experience.

Strengthening of our network proposition:

RCOM continues to invest to bring superior network experience to all its customers. We have launched our Rev B services in 5 cities - Chennai, Bangalore, Mumbai, Pune and Hyderabad, which will enable our customers to access data speeds up to 14.7 Mbps. This service on the 800 MHz spectrum band provides the best indoor coverage, and is carried on our 100 Mbps backhaul ensuring the lowest latency and superior customer experience. We have expanded our 3G footprint to 18 circles.

Strengthening of our product & device proposition:

The pillars of our data strategy revolve around contracting more smartphone customers, getting non-data users into the data fold and move the existing data users up the consumption ladder. This is being done through a slew of targeted CLM initiatives.

- We offer free social networking on various 2G and 3G plans wherein customers get free access to WhatsApp and Facebook, especially targeted at the youth segment.
- In course of the quarter, we partnered Samsung in the launch of their flagship tablet series - Tab S.
- Our smartphone portfolio has been expanded to 20+ across brands and price-points from just 4 a year back, riding on the evolution of dual technology chipsets.
- We have gained significant traction in our smartphone bundled plans across the entire spectrum of entry level to high end devices across retail and corporate customers

Significant focus on enhancing customer experience:

- RCOM has recently embarked upon an initiative to launch 350 full service franchised retail outlets offering full gamut of services to our customers and also innovative self-care options. In the next four months, we will expand our reach to 1,000+ franchisee owned franchisee operated retail outlets.
- We also saw significant increase in the adoption of the Reliance Instacare App (over 5.3L downloads) with a high proportion of users utilizing payment and recharge features.
- RCOM is set to launch an exclusive and revolutionary Twitter based self-care service, which is the first initiative in Asia and only second in the world by any Telecom operator. This unique service allows subscriber to pay/recharge online, check latest offerings and account details and buy product & services through Twitter.

Thus, our concerted data strategy execution across consumer segments has begun to show results with 3G data subs having grown 16.1% to touch 15.1 Million subscribers. Additionally, our data usage per customer, already the highest in the industry, has further grown by 12.9% Q-o-Q.

Having said that - Voice, however shall continue to remain important:

The days of hyper competition in the industry with enormous pressure on voice tariffs are clearly behind us. Voice still constitutes~85% of overall industry revenues and with the new regime of stable voice rates, revenue & margin visibility for operators shall continue to improve.

Now, I would like to share our views on the regulatory environment and other key updates this quarter:

1. **The latest TRAI recommendations if executed spell a host of positives for the sector but pricing needs to be relooked:**

   Very recently, TRAI has come out with recommendations on the "Valuation and Reserve Price of Spectrum for Licenses expiring in 2015-2016". Some key positives that we would want to highlight are:

   - The regulator has recommended a clear road map for the availability of spectrum which will immensely help operators in their medium to long term network planning.
   - TRAI has indicated that currently, inadequate spectrum supply is a big constraint for quality of service to consumers and overall sector growth.

   We fully endorse the above views and feel that shortage of spectrum in the impending auction may lead to artificially high bidding levels and resultant unviable clearing prices for the auctioned spectrum would be very sub-optimal for the industry.

   However, TRAI's recommended increases in reserve prices in both 900MHz & 1800 MHz despite recent auction discovered prices being available, run contrary to the above. Also, in our opinion, the different evaluation methodologies used by TRAI fail to take into account circle specific economic parameters and thus have resulted in exaggerated valuations especially for B&C category circles. Our stand is as below:

   - Reduction in reserve prices particularly in B&C category circles

- No auction till adequate spectrum is made available across all bands simultaneously – 800MHz, 900MHz, 1800MHz & 2100 MHz

7 Reliance Telecom circles are up for renewal in 2015. Most of the other RCOM circles will come up for renewal only in 2021. The cost burden for renewals would be relatively lower for RCOM because all renewal circles are category B (2) & category C (5) circles. Further, all these circles have 5MHz of spectrum each in 800 & 2100 MHz bands beyond the spectrum up for renewal. Hence, adequate spectrum exists to ensure full range of voice & data services to our customers.

2. Clarity on spectrum trading guidelines is critical for the long term health of the sector:

Spectrum is the most valuable asset in an operator's balance sheet and a clear trading policy will allow operators to use this asset efficiently to provide better quality communication infrastructure. It is a critical need of the telecom industry that in the current optimistic economic scenario (with stable government, revived investment sentiment), spectrum availability and spectrum trading policies are given requisite impetus for urgent implementation. In the recent ministerial pronouncements, it has been indicated that the policy on Spectrum trading will be in place by end of this year. We welcome this initiative and also look forward to the government coming out with a clear roadmap on the spectrum availability to allow operators to plan the future growth and to fulfill the objectives of "Digital India".

3. The government's aggressive implementation of the "Digital India" vision will help unlock significant opportunities for the telecom sector:

The vision of Digital India is centered on 3 key areas – Digital Infrastructure as a utility to every citizen, digital empowerment of citizens and governance & services on demand. These translate into the expansion of Broadband connectivity at village level, improved access to services through IT & Mobile enabled platforms, and greater transparency in Government processes. The government has stressed the need for a telecom-led revolution to fully leverage its potential.

Going forward, we expect this to manifest into sizeable opportunities for the sector in the following areas: high speed internet connectivity, hosting & cloud services, mobile commerce, and smart applications to name a few.

Now, I shall share some other key developments in our India operations.

Having delved in the key developments and strategies in the Consumer space, let us take a look at important developments in the India Enterprise & Carrier businesses:

1. **ICT adoption by SMEs & demand for cloud services in India are key drivers for the Enterprise segment:**

In the past few years, the enterprise market has evolved in terms of its requirements and composition. Small and medium enterprises (SMEs) are now emerging as a key focus area for operators as they increasingly adopting ICT solutions to drive operational and capex efficiencies. Further, unlike large enterprises, SMEs have negligible in-house IT capabilities and are thus dependent on service providers for their security, communications and IT requirements. Numbering over 48 million and employing over 40% of India's workforce, they represent a tremendous opportunity as they increasingly board the ICT bandwagon. We expect the rising SME demand coupled with increasing appetite for enterprise mobility applications & cloud services to drive double digit growth in this segment. RCOM is a leader in the enterprise space and continues to expand its coverage and service offerings.

2. Strong performance in the India Enterprise business:

Our India Enterprise business continues to be on the growth track through strengthened engagement with marquee customers & acquisition of new logos. The future growth of the telecom addressable enterprise business will be driven by SMEs, uptake in non-traditional geographies & penetration of new products and services

- We cater to over 850 of the top 1000 large enterprises & nearly 50,000 medium and small enterprises across the country. In the last quarter, we continued our business expansion into tier 2 and 3 cities.
- We are among the market leaders in MPLS & Internet services.
- Reliance IDC is one of the largest players in the country with 10 data centers across India and 1.1 Million Sq. Ft of data center space.
- We made a strategic shift in our business model by moving up the value chain, from pure co-location services to managed services & cloud play- IaaS, SaaS & PaaS, in order to address the changing trends in the Enterprise space. RCOM aims to become the leading cloud services provider in India, leveraging its Data Center competencies.
- We are also developing on Data Protection as a Service offering—DPaaS for short—that would offer storage, archival and disaster recovery for Enterprise data.

  In the third quarter, we shall continue to focus on enhancing our market share in MPLS, Internet and cloud services through product & service innovation, geography expansion & ecosystem collaboration.

3. Strong performance in the Carrier business

- We had another great quarter of performance in our NLD & ILD businesses where we signed sizeable contracts with marquee Indian and international clients with a major focus on recurring revenue deals and monetizing assets.

- We have made good progress on intra circle fiber delivery to Reliance Jio and all NLD fiber (Inter-Circle) deliveries will be completed in this Financial Year.

The outlook for Q3 remains fairly positive with focus on Infra sales monetization & additional revenues from hubbing.

Now let us take a look at important developments in our Global operations:

In another sign of investor confidence in RCOM, Global Cloud Xchange successfully debuted in the Global Capital Market by raising USD 350 million fixed rate notes maturing in 2019.The demand in overseas markets was very strong. USD 250 million is being used to refinance the existing bank loan facility entered into by Reliance Globalcom B.V., and the rest of the proceeds are being used for Capex and general corporate purposes.

In Q2, we invested in future growth of the GCX global network by

- Initiating the process of a PCX cable between Japan & the USA as well as an ICX cable between India and Singapore. The completion of these two systems will allow us to span the globe with our own subsea cable systems.
- Adding 100G capacity to our global IP backbone taking the total capacity to 800G.
- We built a unique cloud platform 'Cloud X' and deployed two cloud nodes in Silicon Valley & Hong Kong with London installation underway. 20 nodes shall be completed by mid-2015. We have established a robust prospect funnel for the same.
- Our new enterprise-class Cloud switching structure is deployed across the world's largest private subsea cable system to enable automated deployment of cloud services –a market first.

GCX expects sustained growth in the coming quarters leveraging on our enhanced network capability, broadened suite of existing products and services and new opportunities across our Cloud platform.

Some other key updates for the quarter are:

1. RCOM's participation in the "Jan Dhan Yojna"

RCOM is one of the first telecom service providers to be ready to participate in the Government of India's "Jan Dhan Yojna" with its USSD platform-based mobile banking services to enable banking transactions for its customers. Financial inclusion is a national priority and we are proud to launch this platform which can offer basic financial services even in areas that are beyond the reach of traditional banking.

2. RCOM is aggressively pursuing de-leveraging initiatives

RCOM is in the process of driving various initiatives to deleverage its balance sheet. The company, as you are aware had raised Rs. 6,100 Crore through India's largest QIP offering in the previous quarter. Our net debt has been brought down to Rs. 36,334 Crore which helped lower interest burden. Apart from this we are in the process of securitization of tower receivables, selling non-core assets, and monetization of real estate assets as well. We have already begun to strengthen our balance sheet and we expect to see further improvements flow from the stated initiatives over the next few quarters.

In conclusion, I would like to reiterate the following:

- TRAI's recent recommendations on spectrum roadmap are a step in the right direction; however, the pricing recommendations are counter-productive and need to be relooked.
- Implementation of spectrum trading policies will significantly improve the quality of services for consumers.
- RCOM expects renewed thrust on telecom sector in the backdrop of the government's ambitious "Digital India" vision.
- RCOM continues to innovate through differentiated products and services with a focus on expanding data revenue base and enhancing user experience for both voice & data customers.
- RCOM continues to be a leader in the Indian enterprise space across IDC, Internet & MPLS.

- RCOM maintains its market leadership in the NLD & ILD segments and is focused on asset monetization & expansion of new revenue streams.
- RCOM continues to invest in partnerships & infrastructure growth in both in its India enterprise & global operations to deliver cloud offerings.
- RCOM is actively working on various initiatives to improve operating metrics, to de-leverage the balance sheet and achieve enhancement of shareholders' value.

Thank you. And I would now like to hand you back for the Q&As.

Operator:

Sure sir. First in line we have question from Mr. Kunal Vora from BNP Paribas, you may go ahead.

Kunal Vora:

Thanks for the opportunity sir. First question is on your network investment. 2G and 3G side for the last few quarters has been constant. Is there a plan to increase capex or you are happy with the current level, considering data volumes are growing fairly fast? That's one.

Second is on the strategy for the 800 MHz spectrum going forward. Would you recommend auction of additional 850 MHz spectrum and would you like to increase your holding in that spectrum band? And also, once there is a benchmark for liberalizing 850 MHz spectrum, would you like to liberalize your spectrum holding and launch LTE on it in the next two, three years? That's about it.

Gurdeep Singh:

Thanks, Kunal, Gurdeep here. Firstly, on the Capex guidance, our Capex guidance continues to be about Rs. 1,500 crore for the year. And you would recollect, a little over Rs. 300 crore is what we invested in the last quarter. So it's in line with our guidance. Having said that, you would recollect that we had invested upfront into the 3G infrastructure, when we rolled out the fiber optic network which is crucial for a seamless data delivery, way back when we rolled out our 3G services.

We currently have networks in 3G at various levels of utilization and we see that capacity and coverage today is sufficient enough for us to drive the next level of growth. We are carefully watching the smartphone penetration. As it moves to the Tier B and Tier C towns, it will help us take the network expansion further. So, till such time, our Capex guidance continues to be in the similar region.

Kunal Vora:

In terms of number of sites – just a follow-up there, in terms of number of sites, like you're at 11,000, while the GSM incumbents are well above 25,000 now. So, is there a coverage mismatch and doesn't it hurt your investment?

Gurdeep Singh:

Kunal, it doesn't, because you've got to see the mix of the circles that the other operators have versus us. We have three large metro circles, which don't have an expansion capacity beyond 100%, so which is your Mumbai, Delhi and Kolkata. And balance of it, most of them, barring MP, CG and Bihar, are C circles, and hence, given the smartphone penetration in those areas, we are well covered. 3G is a business different than 2G. I mean, here you cannot take network ahead of smartphones. Well, you can, that could be a one strategy, but it is purely dependent on devices on the network. So, we need to move hand-in-hand with the smartphone penetration, likely investment and the likely period of that returns.

Second question on spectrum; 800 MHz is a valuable spectrum. We are currently using it for rendering Rev A and the Rev B services. As you've heard little while ago, we have upgraded many of the cities to Rev B to deliver 14.7 Mbps. Some of our competitors have given up the spectrum in the CDMA space, giving us an ample opportunity to be the lead player in the dongle business, which continues to be our core thrust. Going forward, as we look forward to the liberalized spectrum in the same space, 850-megahertz, when it is liberalized, is a very formidable in-building spectrum for rendering LTE services. We are absolutely open to liberalizing the spectrum as and when we see the ecosystem developing and we believe that the market will be right for the LTE products and services.

Kunal Vora:

Just one follow-up there. So how do you see the 850 MHz LTE ecosystem right now? Do you think it's still some time away before it becomes mainstream and assuming that you want to do LTE, what proportion of your existing revenue would go away?

Gurdeep Singh:

Well, to give you a little bit of background on the 850 MHz LTE, I think whole of Korea is on LTE. There are other major players too; including now AT&T going into the 850 MHz LTE and I just heard the other day that Vodafone in Australia has gone Pan Australia 850 MHz LTE. So I think it is about time that the ecosystem is developing and we believe it's still maybe one to two years away when we have a fully ready ecosystem where we can take it to the mid level consumers.

And at this moment, there are only little over 250 million Indians who use Internet. I think the basic market to come for Internet for both 2G and 3G, with 3G being less than 10% usage on the population, it is still five-fold than the market that we are serving. So there is enough and more for us to drive penetration, affordability, adoptability in 2G and 3G to make good use of the current spectrum that we have.

Kunal Vora:

Okay. Thank you, sir. My questions are answered. I'll come back later if I have anything else.

Gurdeep Singh:

Thank you.

Operator:

Thank you Sir. Next question comes from Mr. Srinivas Rao from Deutsche Bank. You may go ahead.

Srinivas Rao:

Sir, thank you very much. I have two questions. First is on your operating side, which you have been suggesting for the last couple of quarters that your focus is on paid minutes and cutback on the so called free and promotional minutes. Your revenue growth obviously is trailing your peers. When can we see the drag of CDMA revenues to end so that revenue growth can move closer to the peers? Secondly, could you help us understand, I mean just from a finance perspective as to how much money has come in into the company as a result of the QIP, and where is it reflecting in the cash flow statement?

Gurdeep Singh:

Okay, let me answer the first one right away. In terms of the revenue performance growth, as I mentioned last time that our consistent endeavor has been to improve paid and profitable minutes. Over the last three or four quarters, we have considerably attempted to change our revenue mix and customer mix by bringing very unique products like 3G@2G, then One India One Roaming, and now social networking is freely bundled with our data Internet plan. I think all of this is helping us to acquire postpaid customers, corporate and SME customers and also in 3G circles, become one of the preferred ones on the MNP.

The contribution by the growth engine of the company, GSM and the Internet business has now moved up to a little over 72%. The pure-play CDMA voice is now less than 28%. But the good news in CDMA is that which we said last time also that we are moving towards a near stop bleed and I think in the last two months, we have now observed a kind of flat voice revenue on the CDMA.

It has happened because of two reasons. One, we have sharpened our focus on the segment. We believe the bundled sales are a great excitement for the CDMA community. We today sell – nearly 15% of our sales are bundled sales versus 5% same quarter in the previous year. Second, there are over 20 smartphones now in CDMA, which is helping our customers upgrade and those who really vouch by the quality and the experience on the CDMA, are more than happy to stay put in the CDMA network.

I think as we go forward, all the chipsets and I've been saying this in the past, are becoming universal chipset. They are only software locked and depending on the country and the bands operating, the handset makers will operate or open those codes for every band to be workable on the phone. I think there has been a hue and cry by all telecom operators across the world, because we cannot limit the consumer choice of purchase of a handset to a particular band, to a particular operator and that's immensely helping us as we're moving forward.

We believe that in a year's time from now when we speak same quarter next year, probably the universality of the chipset would have come down to a $60 phone and that will truly demolish the boundary between CDMA and GSM. It will be technology-agnostic phones, which will help us expand that market.

We do not see, in the next couple of quarters, a growth in line with the market growth in the CDMA voice business, but our GSM and Internet revenue business will certainly continue to beat the market growth. Hence, comfortably one can assume that wireless business in totality will deliver mark-to-market performance now and going forward in the coming quarters.

Srinivas Rao:

Thanks Gurdeep. This is really helpful.

Gurdeep Singh:

Thank you.

Manikantan Iyer:

Yes, Srinivas, on the QIP front, the Company received Rs. 4,808 crore from the QIP proceeds and a preferential allotment of Rs. 650 crore, totaling to Rs. 5,458 crore during this quarter and the same has been reflected as a part of cash flow from financing activities in the cash flow statement.

Srinivas Rao:

But the cash flow from financing statement only shows an inflow of Rs. 2,133 crore.

Manikantan Iyer:

That’s right, because what is reflected here is the – summarized financial cash flow statement. Maybe we can take it offline and give you the breakup.

Srinivas Rao:

Okay. Sure. No problem. Thank you.

Operator:

Thank you. Next question comes from Mr. Rajiv Sharma from HSBC. You may go ahead.

Rajiv Sharma:

Hi, thanks for the opportunity. Just one question. I missed out; I think you made some comments on this. How do you want to use your 850 MHz spectrum going forward and will you be looking at adding 850 to your existing 850 MHz spectrum?

Gurdeep Singh:

Rajiv – thanks for your question. Well, I said that, currently 800 MHz CDMA is being used for CDMA 1x, Rev A and Rev B services. When you liberalize that spectrum, it's a great spectrum to launch HSPA or LTE services. And as I said a little while ago that we're keeping a close watch on the ecosystem, which is fast evolving in 850 LTE and we will look at maybe as a sample case, one or two circles maybe in the next financial year to be ahead of the curve, learn the nuances of LTE and then take it to the market by the circle, by the geography where we see the larger returns.

Rajiv Sharma:

Okay. And there were some initial comments made on spectrum trading getting permitted and RCOM is excited about that getting permitted. So, can you help us understand how you plan to benefit from spectrum trading?

Gurdeep Singh:

Rajiv, spectrum is a scarce commodity as far as we are concerned. You know world over what kind of block sizes of these spectrums are auctioned. And hence, any spectrum trading guidelines are helpful and useful, because you don't have to rush to the auctioneer all the time to buy the spectrum and it helps to optimize the use of spectrum. There could be some circles, some areas, lying idle with some operator where they're not making good use as far as monetization of the spectrum is concern. It's easier to trade the tranche over 1 MHz to beef up your spectrum. You can get into unrepresented areas; you can augment capacity without having to wait.

Rajiv Sharma:

Gurdeep, which band would you like to benefit with spectrum trading? Will it be the 3G or it will be the 850 MHz?

Gurdeep Singh:

This is a bit hypothetical at this moment, but I'm saying that, trading only gives you more options than only outright 5 MHz chunk of buying. So it's a good trade-off analysis to keep the tranches of that purchase. We would be open to any band.

Rajiv Sharma:

And why do you think this 850 MHz auction is, both in terms of format and reserve price, taking so much time, what is delaying this auction? And do you think it is possible that the February auctions are only 900 MHz renewal and there is no 800 MHz spectrum auction along with that?

Gurdeep Singh:

Rajiv, as you may be aware that in a rare move all the four telco CEOs, we came together and wrote this memo to the Honorable Minister with a copy to the Honorable Prime Minister, urging them to put all the spectrum across the bands of 800 MHz, 900 MHz, 1800 MHz, 2100 MHz into one basket and do a one big bang auction so that the operators can make choicest decisions. Spectrum can then discover its true price rather than a predatory pricing. We certainly support all spectrum bands put together for an auction.

Rajiv Sharma:

And what's your stance on the MVNO, because it could be positive for you as it could allow you to leverage your excess capacity in GSM. But the market is already fragmented with nine players. So what's your stance on MVNO?

Gurdeep Singh:

We always support something which is good for the customers. If MVNO can help bring niche marketing and niche positioning that will certainly help consumers make little more elaborate choices, but yes, I do buy your point that there is already a hyper-competitive – not a hyper, but semi-hyper competitive stage in the market, but market at the ground is kind of taking an organic consolidation in anyway. See, MVNOs the world over, have entered only when the pricing was to be disrupted. I think we've entered into the phase of consumer experience and superlative services. And I think that's where probably the MVNOs will struggle hard to put their act together.

Rajiv Sharma:

My last question Gurdeep is, RCOM has lot of 3G spectrum in Delhi and Mumbai, means 5 MHz each. But the data penetration or subscriber base is more with the incumbents. So, what is preventing RCOM to get very aggressive on this unused capacity in 3G and be more disruptive in terms of tariffs and what's your view overall on data rates?

Gurdeep Singh:

Thanks for reminding me that we have a lot of spectrum, 5 MHz, in Delhi. Well, Rajiv it is not. 5 MHz spectrum is just about sufficient for a start-up service. Yes, we are one of three operators in Bombay and Delhi.

How do you measure the success? I mean, you measure the success by the fact that – we cannot do anything about the traditional subscriber base, but when we go and attack the traditional subscriber base of the incumbents with the very innovative products, we are doing many things; 3G@2G rates, One India One Roaming, contract zero plans, which are peace of mind plans, social networking bundled with data, which are quite differentiated and we believe are difficult to replicate by the incumbents. They help us at the MNP front.

So if you look at Delhi and Mumbai, we are already MNP positive by value by far. This is contrary to what our position was a year ago. So I would say it is working. B, you also measure your success in terms of what corporate and SME you are winning, and I think we've made a tremendous stride in that aspect.

Data as a world, you've got to be calibrating between the price and the quality of service that you deliver. You won't get too many consumers just because you have very disruptive prices and a very average or below average consumer experience. This is an area where you need to constantly invest, provide superlative experience and balance the two. And I think the efforts that we're making are in the similar direction and we are happy with the outcome of our effort so far.

Third, the acquisition front, you measure by what kind of a smartphones you get on network. So I'm happy to state that nearly 29% of the new smartphones coming into the market in Delhi and Bombay come to our network. So that shows that our strategy is at work and we are consistently changing the mix of our bucket of consumers in Delhi and Bombay.

Rajiv Sharma:

And do you think entry of Reliance Jio will put pressure on data rates?

Gurdeep Singh:

Well, I just said a little while ago that only 250 million Indians use Internet, there should typically be over a billion. The market to come for Internet is four times more than the market that we serve. There is enough and more room for everyone to be in this market. LTE is the next level of service. Unless you discover a mass market price for the device that goes down to the last mile customer, this is not a disruptive service. So if it is going to be at a niche level, at the top level, maybe initially with a dongle play, that is something that we will counter to when it comes to. Till such time the launch is a hypothetical question.

Rajiv Sharma:

Thanks. Thanks a lot and all the best for coming quarters. It is very helpful.

Gurdeep Singh:

Thank you.

Operator:

Thank you, sir. Next question comes from Mr. Jitendra Tokas from Citigroup. You may go ahead please.

Jitendra Tokas:

Hi. Thank you for the opportunity. Could you tell me when you will be recognizing the revenues from the intercity fiber deal?

Gurdeep Singh:

Well, as we said in the past also that we have a deal at three levels, the intercity fiber, intra-city fiber and the towers. We are in the process of delivering them. We have been delivering and it is fair to assume that we have been receiving the accruals against some of the deliveries that we have made. Given a very high confidential nature of the contracts that we have with Jio, we are sorry, unable to disclose the exact amount at this moment, because this will then lead to, surely analyzing about the possible date of the launch of the Jio. However, as I said to the channels this morning as well, we hope to conclude the delivery in near future.

Jitendra Tokas:

Okay. And just one more question, please. Are there any one-off in this quarter?

Gurdeep Singh:

Not of any significance.

Jitendra Tokas:

All right, okay. Thank you so much.

Gurdeep Singh:

Yeah. Are you referring this more to do with what we did in the Q2 of the previous year, which is the PBR write-back?

Jitendra Tokas:

No. Just any other one-offs, which may be there, that's all.

Manikantan Iyer:

No, no, nothing significant.

Jitendra Tokas:

Okay. All right. Thank you.

Operator:

Thank you, sir. Next question comes from Mr. Sunil Tirumalai from Credit Suisse. You may go ahead.

Sunil Tirumalai:

Hi. Thank you for the opportunity. Most of my questions have been answered. I just had two. One is on the finance cost, what is the outlook? I mean, how should we look at it going forward? And secondly, on the tax rates please. Thank you.

Gurdeep Singh:

I'll just answer the first one and my colleague, Mani, will answer the second. The net finance charge or the cost, we said that on an annualized basis, because of our QIP and its reflection in the books will have an impact of about Rs. 500 crore savings on an annualized basis.

Manikantan Iyer:

On the tax front, can you be elaborate what exactly you're looking for on the tax rate?

Sunil Tirumalai:

I just wanted to understand for the rest of this year and for next year what kind of tax rate outlook we should have?

Manikantan Iyer:

As far as tax is concerned, we are going through that 80IA exemption and I should not give guidance for the future, but at present, there is no tax liability which is required to be recognized.

Sunil Tirumalai:

Okay. Thank you.

Operator:

Thank you, sir. Next question comes from Mr. Rahul Singh from Standard Chartered. You may go ahead.

Rahul Singh:

Yeah, hi, good afternoon. I had two questions on balance sheet and one business-related question. So firstly, on the balance sheet, there's been some increase in loans and advances of almost about Rs. 2,000 crore on a Q-o-Q basis. What exactly is that on account of, as it is quite a sharp increase? And other question on the balance sheet is the capital work in progress, which has been steady at Rs. 3,000 odd crore, but just wanted to understand the nature of that number, because it's quite high in relation to your normal recurring Capex. So if I can get answers to these questions then I'll ask the other question.

Anil Ladha:

The loans and advances have increased about Rs. 1,900-odd-crore during the quarter. Some of the constituents for this increase include advances to suppliers, TDS deductions, and unbilled revenues.

Rahul Singh:

Okay.

Manikantan Iyer:

Yeah. On the CWIP, currently our CWIP consists of the projects which are in pipeline and closing out. In the coming two quarters, some of these will be capitalized in our books.

Rahul Singh:

So these are in the global operations?

Manikantan Iyer:

It is both, Indian and global.

Rahul Singh:

Okay, because in the Indian – in the normal, if your Capex is so low that this number – there are no long gestation projects in telecom, apart from Global operations.

Manikantan Iyer:

Yeah, no long gestations. You are aware that we are implementing a strategic contract, and other contracts are also on the pipeline. There are Capex, but it will be with an overall guidance of Rs. 1,500 crore, which has been stated.

Rahul Singh:

Okay. Thanks. And on the business, my question was on the data revenues. So if one looks at the data tariff, the implied data tariff on a per MB basis, it's been declining, while traffic has been growing in line with the industry, the revenue growth has not been in line with the industry. So just wanted to understand the data revenue versus traffic kind of dichotomy, especially relative to the peers?

Gurdeep Singh:

Fundamentally, as a company philosophy we are offering 3G at 2G rates, and we're very clear that with less than 10% of the consumer base is using 3G, there is more to drive penetration and adoption, and we have been doing lot of activities to induce customers and get them on to board and shift them from 2G to 3G. I'm happy to tell you, as of now, nearly 85% of our 3G handset owners in the network service areas use 3G. It's only been because of our services like 3G@2G. Having said that, we continue to have the highest usage per subscriber, about 752 MB, which continues to reflect our quality and the mix for the customers that we have on the network.

Rahul Singh:

Okay. Thanks a lot.

Operator:

Thank you, sir. Next question comes from Amruta Pabalkar from Morgan Stanley. You may go ahead.

Amruta Pabalkar:

Thanks for the opportunity. I have two questions, one on your data center and enterprise business, where do we see exactly revenues on India front? If it is others, why has there been a decline for last two sequential quarters? And secondly on the Global business front, when do we see the revenues inch-up going forward? Thank you.

Manikantan Iyer:

The data center and Enterprise business is a part of the non-voice segment, and not a part of the 'others' segment. Secondly, there is no decline in those two businesses. If you have a business question, Punit can take it up.

Rory Cole:

On the Global data side, let me share some information. As you know, one of our big components of our business relates to indefeasible right of use contracts. These varies somewhat over the season, for example, the second quarter is traditionally our weakest quarter because of the long summer break in our Middle East market and also our European and U.S. markets. So that tends to be our weakest quarter from an IRU perspective. We still expect significant growth in Q3 and Q4 Q-o-Q in that segment. So you should see somewhere between $15 million and $20 million increase in our business in those subsequent quarters. Just for reference, Q2 will always be the weakest over that period because of the summer break. A lot of our customers have year-end spending requirements that run on the fiscal year, which they do in Q3.

Amruta Pabalkar:

Right. Thank you. Just to confirm on the India bit, so the data center Enterprise business would fall under your non-voice segment, as well as the data business on the wireless segment, am I right?

Manikantan Iyer:

Correct.

Amruta Pabalkar:

And could you just elaborate on how is the industry flavor in terms of growth and how do you see yourself placed in this kind of segment in terms of market share or any broad guideline in the segment?

Punit Garg:

When you look at the market share data, which has been tracked by different analysts, whether it is Gartner or IDC or Forrester, they all seem to be different. There are five players in Indian market, with two new players trying to enter this space, because that's an open place.

RCOM easily, if you look at the overall market, has a market share of around 25%-26% among all the players. And the difference between number one, number two, or number three player won't be significant. Its a few points difference between any two players, because all are between 20% to 25%, and the remaining, share the rest of the pie. I think what is important for us is that we are present in the 900 corporates among the top 1,000 corporates. And we are betting on Tier 2, Tier 3 cities, especially, looking forward at the vision of Prime Minister for 100 Smart Cities. We are helping in terms of putting the infrastructure in place, in terms of all the services required over there, making it available, and growing the industry. Tier 2 and Tier 3 typically have all the SME industry and that's what Vinod said in his conversation or speech earlier.

And I think when you look at the next 100 cities, apart from the top 27 cities, we expect that there would be a CAGR of 25% to 30% growth in next three years and we believe that we will have a major share in that market. We have already started getting that and we will get more and more in the coming quarters.

Vinod Sawhny:

I just want to add a small point to what Punit just mentioned. Typically, our entire leadership around the enterprise space is driven on three specific pillars that we are pursuing this particular year. One is, expanding into Tier 2, Tier 3. The second is there's disproportionate focus that we're doing in the SME segment. And the third is trying to move out of low margin co-location business into high margin cloud business. And this we're doing both on the India side as well as on the Global side and the initial responses have been extremely encouraging.

Amruta Pabalkar:

Thank you, sir.

Operator

Thank you, ma'am. Next question comes from Priya Rohira from Axis Capital. You may go ahead.

Priya Rohira:

Yeah. Thanks. Most of my questions have been answered. I just need answer for one question and a follow-upon what Punit mentioned. You mentioned in the enterprise segment, you're focusing more on the high-margin cloud business. Would it suffice to say that this is currently still in the investment phase or with the suboptimal margins? And because of the investments you would be making could we see the margin inch up in the Globalcom also because of this initiative?

Punit Garg:

We started the cloud business journey two years ago in terms of building the platform. This mostly happens in a collaborative approach. To give you an example here, if you have to offer the SAP Disaster Recovery Service, SAP comes and setup the Disaster Recovery Platform in your data center, which include the hardware and the software. We get into a revenue share model in terms of providing that service to all the SAP users, so they don't have to build a backup datacenter or backup servers to provide that service. It is always ready, always-on service which we provide.

So it is not Capex intensive, it's not Opex intensive, but it is all about the infrastructure which we have already built, how do we monetize that and I think that's what we are doing in Global as well as here. Because in Global, along with our landing positions and Meet-me rooms, we have plenty of co-location space available, which we are leveraging for this high margin service. And similarly, in India, in our 10 data centers, which we have been talking about, we have given a portion of that for the cloud computing service. Whatever I will sell for the co-location, let's say, if it gives me $100, in the cloud computing service, the same space would give me $1,000. So it's a 10x return which you get on the same space by utilizing the same power and the space.

Priya Rohira:

Sure. So what would be the utilization of your data center right now in case if it's possible to share?

Punit Garg:

Currently, among the nine data centers which are operational, we have 650,000 square feet of space. The tenth data center, which is coming-up shortly, will roughly double the existing capacity. On 650,000 square feet, we're almost at 90% of utilization and the balance 10% is going to be used for existing customer expansion as well as the cloud computing. For the new data centers, we have done the deals and I would say that by the time it is launched in next 6-7 months, we would be sold almost like 40% to 50% of the space.

Priya Rohira:

Sure. That's helpful. And one question on the India wireless business, given the fact that now we're moving to a positive trajectory of the subscriber additions and also the transition from CDMA to GSM, would we say that we are behind this curve and you should only see growth kicking in from here-on?

Gurdeep Singh:

Sorry, Priya, can you just repeat your question please?

Priya Rohira:

Gurdeep, my question relates more to the fact that whatever we had seen the deceleration because of the CDMA to GSM transition, which should be completely behind us and now hereon we should only see growth. I mean as also reflected by subs additions in this quarter?

Gurdeep Singh:

Yes, exactly. I mean I did kind of mention that in the last quarter that we are nearing that flattening situation. And I'm glad to inform that we have achieved that. August and September have been near flat on the CDMA voice business. Data has always been growing. And going forward, as I said, we don't expect it to start suddenly growing 3% or 4% quarter-on-quarter, we would be happy to see this flattening continue at least for a quarter and then get into, at least, a growth in the range of 1% or 2%. Having said that, 72% of the business is GSM and Internet, it's still growing or beating the market quarter-on-quarter basis. If you put the two together as a math, we should be able to deliver mark to market performance in near future.

Priya Rohira:

Okay. That’s helpful, Gurdeep. Thank you so much.

Gurdeep Singh:

Pleasure.

Priya Rohira:

And wish you all the best.

Gurdeep Singh:

Thank you.

Operator:

Thank you, ma’am. Next question comes from Mr. Sanjay Chawla from JM Financial. You may go ahead.

Sanjay Chawla:

Hi. Good afternoon. Thank you for the call. I have three questions. First is could you give us the average cost of debt at the gross level in terms of interest expense over gross debt that you will have? That's the first question. Secondly, just a follow-up to your loans and advances increase. You mentioned TDS on receivable is one of the factors, can you just elaborate on that? And also did you mention unbilled revenue increase is also a reason for the surge in the loans and advances, just a clarification on that front, please? Third, is on your mobile – on the data growth, you’ve shown very strong data growth and I think the terabytes that you are carrying now is almost similar to what Bharti is carrying. So congratulations on that. Could you give us a broad sense of the data traffic mix in terms of dongles versus handsets?

Anil Ladha:

The average cost of debt at present is around 6.7%.

Sanjay Chawla:

This is in terms of gross interest expense over gross debt?

Manikantan Iyer:

The cost is bundled cost of the Indian and foreign currency loans, that is around 6.7%. Any further breakup we will be happy to share separately.

Sanjay Chawla:

Sure.

Manikantan Iyer:

And the second question on TDS front, you are aware that 30th November is the last date for filing returns. It's an aggressive step taken by the company to collect all the TDS certificates. More than a couple of hundred crore has been collected and which is reflecting in the balance sheet as of September 30. Once the TDS is collected it moves from debtors to loans and advances. So at the end of September 30, you see higher loans and advances and at the same time a reduction in debtors. Other than that, there was an advance that has been paid during this quarter for ongoing projects.

Sanjay Chawla:

Is this in the nature of a service tax or something else?

Manikantan Iyer:

It is TDS, tax deducted at source on payment receivables. It has been done at the end of the period. Previously we used to get the TDS certificate from the customers, if you remember, on a month-on-month basis. Now the government, since last year, has stated that a yearly certificate has to be issued. All our Enterprise customers and Carrier customers, and our big customers have deducted the tax and provided the certificates as of June end to be enclosed along with our return. So that particular amount which was lying in the debtors now stands reduced in our balance sheet. As I mentioned, this is a yearly exercise, so you will see a high figure.

Sanjay Chawla:

Okay. Did you mention unbilled revenues are also a reason for this?

Manikantan Iyer:

There will always be some services unbilled in this segment. Maybe a small portion must have gone up on that unbilled revenue. Unbilled revenue is always part of loans and advances.

Sanjay Chawla:

Okay.

Manikantan Iyer:

Yeah.

Gurdeep Singh:

Coming to your last question on the data revenue growth, data traffic growth, it's a mix of dongle and mobile Internet revenue. We normally don't share the breakup between the two, but having said that, I must let you know that in dongle business we are the leader, in terms of subscriber base, usage and the quality of customers that we have. And as we upgrade more and more cities to Revision B, which is 14.7 Mbps, which in-building delivers better speed than 3G. We believe that we will be able to take up the data growth even higher, have more subscribers and continue to change our portfolio and the revenue mix and the customer mix of the company.

Sanjay Chawla:

Okay. Thank you and all the best.

Gurdeep Singh:

Thank you.

Manikantan Iyer:

Thanks, Sanjay.

Operator:

Thank you, sir. Next we have follow-up question from Mr. Srinivas Rao from Deutsche Bank. You may go ahead.

Srinivas Rao:

Thank you very much Sir. I just have two questions. On the Global Cloud Xchange, you mentioned the two cables are in the process of getting constructed. You said one is a PCX cable, right? That's between?

Bill Barney:

You're right, this is Bill Barney here. Yeah, PCX runs from the Northern United States, particular in State of Washington to Japan, and then the ICX cable runs from Mumbai to Singapore.

Srinivas Rao:

Understood. Second question is on the Capex guidance provided. The cost of the cable built is part of the Capex or is the cable is being built in some kind of a consortium? And thirdly, I think GCX did raise some money sometime back. Is that also part of the consolidated debt being reported by the company?

Bill Barney:

Yes, both cables are built as consortiums. We are spending about one quarter of the Capex. The Capex will actually be spent over FY2016 and FY2017. So you'll see very little Capex spent in this year and most of the payments on both cables are back-end loaded into 2016 and 2017.

Manikantan Iyer:

The gross debt figure includes the GCX bond issue.

Srinivas Rao:

Thanks. This is helpful. Thank you so much.

Operator:

Thank you, sir. Next we have follow-up question from Mr. Kunal Vora from BNP Paribas.

Kunal Vora:

Yeah, thanks for the opportunity again. My question is again on the 850 MHz spectrum. How strategic is it for RCOM going forward? You're looking to sell various assets to deleverage the balance sheet. Could 850 MHz spectrum be one of them? Assuming trading is allowed, and spectrum liberalization happens at a reasonable price, would you be open to sell 850 MHz spectrum? That's one. And second one is, how different is the data realization in CDMA and GSM, if you can share some insights there?

Gurdeep Singh:

Okay, two things. Let me answer your first question on the 800 MHz CDMA spectrum.

We truly believe that we have one of the best spectrum holdings in 800 MHz CDMA currently, which when liberalized and upgraded, becomes 850 MHz LTE. I think it is a no-brainer for all of us to agree that sub-1 GHz spectrum is always the most valuable spectrum. Now, with more and more countries adopting and migrating to 850 MHz LTE, I think the ecosystem will evolve much faster than we expect and we believe we are sitting on a spectrum that will drive the next wave of growth for RCOM. Hence, the question of trading or selling off of that spectrum does not arise at all.

Secondly, in terms of data realization, the fact that most of the data consumed on CDMA is on dongles, particularly in Rev A and Rev B, and when you move to Rev B, your quality upgrades multi-fold, hence giving you the ability to get even more quality customers on your network and swing and churn large corporates to your side. Given that as a background, the data realizations in the CDMA dongle business is more attractive than that of 3G and it will continue to be so and even may grow higher in the future as the quality of service will fetch the price for itself.

Kunal Vora:

Okay. Thank you very much Sir.

Gurdeep Singh:

Thank you. With pleasure.

Operator:

Thank you, sir. At this time, there are no further questions from the participants. I would like to hand over the floor back to Mr. Vinod Sawhny. Over to you, sir.

Vinod Sawhny:

Well, thank you very much. I mean, before I end, let me once again repeat here or underscore that we continue to be encouraged by the buoyant data growth and our strength on this front across our consumer, as well as our enterprise businesses. And let me assure you that we will continue to improve the metrics for RCOM on the back of increased pragmatism on the regulatory front. Right, till we meet again, thank you very much everybody.

Gurdeep Singh:

Thank you everyone for being on the call.

Manikantan Iyer:

Thank you.

Operator:

Thank you, sir. That does conclude our conference for today. Thank you for participating on Reliance Conference Bridge. You may all disconnect now.