Q4FY17 Earnings Call Speech – May 29th 2017 @ 4 pm

Gurdeep Singh

Good Afternoon and welcome to Q4 FY17's earnings conference call. I have with me the senior management team of Reliance Communications. On behalf of us all, I thank you for joining this call.

On May 27th, 2017, our Board of Directors adopted the results for the fourth quarter FY17 ending March 31, 2017. The Media Statement, Quarterly Report and the Results have been uploaded on our web site and I trust you had a chance to go through the same.

During the last quarter, **sector's operational and financial performance has seen continuing severe adverse impact due to free offers, disruptive pricing and hyper competition.** The entire industry has trended down this quarter and the revenue, EBITDA and profitability for all players have been affected. For the first time in over 20 years, the sector has registered de-growth in revenues, leading to a reduction in the Government's share in revenues, sharp drop in operating margins, accompanied by increased interest costs arising from a staggering industry debt burden, and higher depreciation and amortisation charges as a result of higher spectrum purchase costs.

Steep declines in profitability and / or net losses have been reported for the past two quarters by all telecom operators in the country without exception, and a couple of operators have shut down their entire operations in the country. **This sector situation needs urgent requisite corrective policy initiatives by the Government and regulators to infuse operational and financial health.**

In this backdrop, our key financial & operational highlights for the quarter are:

- Consolidated revenues stood at Rs. 4,524 crore, down 8.1%, and EBITDA at Rs. 1,083 crore, down 10.2%, compared to the trailing quarter, in line with industry trends.

- The EBITDA margin declined to 24%, compared to 24.5% in the trailing quarter.

- Indian operations' revenues and EBITDA stood at Rs. 3,916 crore and Rs. 908 crore respectively; while Global revenues and EBITDA were Rs. 988 crore and Rs. 175 crore respectively.

- Total MOU was at 105.6 billion, up 3.4% Q-o-Q and our 3G/4G data subscribers' base stood at 20.8 Mn.

Financial highlights for the full year FY 17 are:

- Consolidated revenues stood at Rs. 19,949 crore, down 10.8%, on account of free offers, disruptive pricing and unprecedented competitive intensity in the industry; the impact of complete shutdown of RCOM's CDMA operations during 1st Half FY17; and full year impact of moving to higher cost ICR arrangements in 5 circles consequent upon end of the validity period of 900 MHz spectrum held by the Company.

- The Company suffered a net loss of Rs. 1,285 crore for the year, compared to a net profit of Rs. 660 crore in the previous year, owing to the drop in revenues, decline in EBITDA margin for the year from 34.2% to 27%, and increase in interest costs.

This is the first year since inception, when RCOM has incurred a net loss during the year, having shown steady financial and operational performance during last 10 years of its operations. Last two quarters during FY17 have been totally unprecedented and unanticipated by any operator, and have resulted in deep stress in the sector.

<u>Let me now talk about the current situation in the sector:</u>

The vitality of telecom sector is not only a critical pre-requisite for the growth of the Indian economy, but also for the execution of 'Digital India' vision, wherein a healthy and operationally efficient telecom industry is an absolute necessity.

The **current stress in the telecom sector** is a matter of grave concern not only for the industry players but also for the financial sector, regulators and the Government. This is a massive disruptive situation and no other sector in Indian economy has seen such an unsettling operating scenario. Even globally, in any telecom market, such disruption has not been experienced by the operators. In the current situation, viability and sustainability of the industry is at risk.

The sector's free cashflows are at highly negative levels and there is a huge deficit in the servicing of the fixed payments and deferred spectrum liabilities through sector EBITDA. High level of total sector liabilities of around Rs 7.5 lac crore would be unsustainably burdensome if the sector's current operating pressures continue.

The telecom industry has been urging the government to initiate requisite policy actions urgently to improve the sector's health. Based on the pleas by the industry bodies, the Ministry of Communications has set up an **Inter-Ministerial Group (IMG)** to look at the current sector situation and suggest policy solutions. We welcome the formation of IMG and hope that a Corrective Policy Framework would be put in place very soon.

It is critical that the government relooks at all the policy driven components of the industry's cost structure. Some of the key recommendations by the industry as well as TRAI to the government include revamping of methodology for estimation of Adjusted Gross Revenue for levying License Fees and Spectrum Usage Charges, lowering of levies in form of License Fees and Spectrum Usage Charges, increased moratorium and duration of installments for payment of deferred spectrum obligations, and formulating a financing package for the sector. Also in this changing scenario of ARPU led tariff plans rather than per minute/per GB tariff plans, per minute Interconnect Usage Charges itself, let alone a staggering rate of 14 paise, should be reviewed and scrapped by the Government.

The Key Point is that remedial policy actions and financing package is critically needed to infuse operational viability in the sector.

Current perspective about the telecom industry trends:

The data consumption has exponentially grown over last few quarters. A mature smartphone user in India is expected to consume far higher data per month than global averages. The data usage will continue to grow with adoption of smartphones and thus the quantum of 4G deployed spectrum and network capacity will be critical to serve this growth. RCOM is well positioned to operate in this market, with access to a nationwide, state-of-the-art 4G LTE network. Our comparative 4G business advantages were not visible in the last quarter till March due to free offers in the market, but since April we have started seeing upsurge in data consumption as a matter of fact, our May data consumption trends show a 2X jump over March.

Key takeaway about the trends is that data capacity and seamless execution of date-led strategy are crucial for incremental market shares.

Let me now spend some time to share with you the key developments at RCOM and how RCOM is trying to achieve best possible business execution in these challenging times.

RCOM, with its well planned business and corporate strategies, is managing its business execution in the best possible manner in the current industry situation.

In wireless business, we have been following a **dual-pillar strategy with a strong focus on execution.**

- Our **asset light strategy** for 4G services – our customers have access to a readymade pan-India network and we did not and do not have to incur any major capex for network rollout.

- We were the first player among the existing operators to switch over from a tariff led pricing strategy to an **ARPU led pricing strategy.** We have been offering a full bouquet of ARPU led products.

  As part of our data led strategy, we have launched smart acquisition products offering generous quantities of 4G data to our prepaid customers.

  1. One of these products offers 1 GB of 4G data everyday per month along with all voice calls priced at 25 paisa per minute, at an aggressive price of Rs. 96 per month. This product thus offers best-in-class voice tariff to 4G customers who have high STD usage.
  2. The other product offers 70 GB of 4G data at a price of Rs.149. At an effective price of Rs.2 per GB of 4G data, this is one of the most competitive data offers in the industry. In this plan off-net calls are priced at 1 paisa per second whether calls are local or national.

We have also launched **new post-paid plans** targeted to acquire high value Voice & 4G Data customers. All the plans offer unlimited calling on any network. Rentals start at Rs 299 which offers 6 GB 4G data and is targeted towards mass market customers hooked on to the social media, while Rs 499 plan offering 15 GB data is targeted towards customers whose usage extend beyond social media to downloading of music/videos and Rs 699 plan which offers 30 GB data targeting the heavy users who might like to use the phone as a Hotspot as well.

These innovative plans are helping us in managing the churn better and also enabling us to acquire post-paid and corporate customers in the 4G LTE business.

VOLTE is the technology for the future and as our plan of future-proofing the business, we expect to introduce **our VOLTE offering in next few quarters.**

During Q4, we have also been executing various revenue and cost driven operational measures:

A. Revenue driven operational measures

- Targeting acquisition of the primary SIM customers by focusing on postpaid acquisition
    - ~10% of incremental acquisitions are now on postpaid, and we hope to increase this to 20% over the next two quarters.
    - ~25% of our incremental revenue is through postpaid customers.
- Offering attractive 4G offers to customers on own network with 4G handsets but not currently using 4G.
- Improving customer retention by proactively offering best-fit plans
- Turning existing customers into partners through a customer referral program
    - A good number of incremental postpaid acquisitions are being contributed by the referral program.
    - By this program we are not only adding "filtered" i.e. better quality customers, we are also strengthening our bonds with the corresponding existing customers.

Concurrently we have been cautious in the "new" customer acquisition race. We have done this consciously, as we would like to prune the multi-SIM category and have been focusing our energies on deepening and widening our post-paid and corporate customer base by leveraging our pan-India 4G network.

We are also having focused **content partnerships** with Hungama, EROS Now, Saregama, Shemaroo, OnMobile, Opera and others. These partnerships allow us to offer all round entertainment like Music, Videos, Games, Llive TV streaming, Sports, Utility tools etc. These offerings continuously increase our customers' delight and thereby help in our data usage. Additionally, to improving the 4G device penetration and getting more smartphone customers on board we have tied up with financial services companies to offer **financing options** to our buyers for purchasing smartphones. We are driving sale of handsets through our own shopping portal as well. We are happy to see that a lot of customers have shown interest in buying smartphones through these financing schemes and are converting to use our gold standard 4G services.

B. Cost driven operational measures

We have reorganized and regrouped our operational departments and teams. We have dismantled the legacy circle based organization structure. This was a legacy structure arising out of the "circle" being the basis for issue of "licenses". **We have transitioned to a FMCG like organization** where all backend activities have been centralized to maximize economics of scale. The role of the decentralized field units now is to have a single-minded focus on generating sales. Concurrently, we have automated and digitized our processes e.g. e-KYC is being used extensively. We have created "apps" ecosystem (Instacare for customers and Channelcare for the retail channel) to ensure higher efficiency at lower cost. With all the above, we have **improved our "teeth to tail ratio**" significantly.

Our Key message is that RCOM is fully geared on best possible execution of its business operations.

I will now like to update you on the deleveraging strategy and corporate transactions.

RCOM launched a comprehensive programme of all-round strategic transformation in the year 2015, with emphasis on industry consolidation, an asset light business model, future sustainability, and cost efficiencies. The programme is now at the final stages of completion.

- **SSTL's consolidation into RCOM:** The proposed merger of SSTL's wireless operations with RCOM, marking the 1st in-country consolidation in the Indian telecom industry, is expected to be completed in June, 2017 with receipt of DoT approvals. The merger will add highly valuable 30 MHz of 850 band spectrum in 8 key circles, and will extend validity of spectrum in these circles for an additional period of 12 years, till 2033.

- **Spectrum trading and sharing deal with Jio**: Our 850 MHz spectrum trading and sharing arrangements with Reliance Jio have been fully implemented, and are now operational for the past over 6 months. This unique arrangement has enabled RCOM to deliver access and connectivity to a world class, nationwide 4G LTE network to millions of valued customers, with minimal capex and considerably lower operating costs.

- **Consolidation of RCOM's wireless business with Aircel:** The proposed consolidation of RCOM's wireless business with Aircel will place the merged wireless entity among the top 3 ranking operators in 12 important circles, and among the top 4 operators in India on the basis of customer base and revenues.

  The combined entity will enjoy substantial benefits of scale, and capex and opex synergies with an estimated NPV of ~Rs. 20,000 crore. As part of this transaction, RCOM's overall debt will reduce by Rs 14,000 crore, together with transfer of liability for spectrum instalments of an additional approx. Rs. 6,000 crore.

  We have received approvals from the Stock Exchanges, Securities and Exchange Board of India's (SEBI) and Competition Commission of India (CCI). The demerger and merger Scheme has been filed in the National Company Law Tribunal (NCLT). Approvals from the shareholders of both RCOM and Aircel have been duly received in the NCLT convened meeting during April 2017. The lenders' and other requisite consents are expected to be received in the next few months.

- **Monetisation of Tower Assets:** The proposed transaction for sale of the tower infrastructure owned by the Company to Brookfield has received requisite approvals from CCI. The business demerger and transfer scheme has been filed with the NCLT. Shareholders' approvals have been received in the NCLT convened meeting during April 2017, and lenders' and other consents are expected in the next few months.

RCOM will receive an upfront cash payment of Rs. 11,000 crore from the proposed transaction and the same will be fully utilised for reduction of debt. RCOM will also receive 49% future economic upside in the Towers business.

Upon completion of the Aircel merger and sale of the Tower business, RCOM's debt will stand reduced by approx. Rs 25,000 crore and the Company will hold highly valuable strategic stakes of 50% in the Aircel JV and 49% future economic upside in the towers business, providing future monetisation opportunities for significant further deleveraging.

Post these transactions, remaining substantially lower debt in RCOM would be serviced through RCOM's existing high growth and higher margin businesses in the domestic enterprise segment, Data Centers, optical fibre and international business in GCX. All these businesses have higher stability of revenues and stickier customer base with minimal churn.

Further deleveraging through monetization of our prime real estate properties at Delhi and Navi Mumbai would be achieved.

Liability Management: Post signing of binding documents for the Aircel and Brookfield transactions, RCOM has formally advised all its lenders that it will be making repayment of an aggregate amount of Rs 25,000 crore from the proceeds of these two transactions, on or before 30th September 2017. The said amount will cover not only all scheduled repayments, but also include substantial pre-payments to all lenders on a pro-rata basis.

RCOM is presently engaged in discussions with its lenders to obtain their requisite consents for the two transactions and to refinance scheduled instalments falling due in the interim period up to 30th September, 2017, to facilitate expeditious closing of both transactions in the best interests of all stakeholders. Based on the large number of approvals already received for the two transactions and continuing good progress for the balance, RCOM expects to meet its all debt repayment obligations in line with these plans, and substantially reduce its overall debt.

RCOM has been working steadfastly on execution of its well-planned, future-proof, all-round strategic transformation strategy since last two years. Had the hyper competitive disruptive situation not happened during last two quarters, RCOM would have been in a far better operating and financial situation due to its forward-looking planning. **Clearly, this has been a totally unexpected development and we urge all our stakeholders to appreciate the current situation and support the current transformational phase of the Company, which would usher RCOM into a very solid and sustainable position.**

I will now request Bill to give you an update on the developments in the Enterprise and GCX businesses.

Bill Barney

RCOM's Enterprise and GCX business continues to show steady performance while gaining visibility across key markets globally.

Here are some highlights of our Achievements in Q4:

- We completed significant Network upgrades and enhancements in Q4 across our global network infrastructure, with 1.75 Tbps added on subsea and 1.1 Tbps added on backhauls.

- GCX signed a partnership with vScaler to enable direct access to vScaler's cloud services platform via GCX's CLOUD X Fusion, delivering next generation application specific Cloud services to consumers and enterprises on a global scale. The collaboration leverages on GCX's core assets which include a global network with data centers connected in key hubs, and a leading ecosystem of on-net Clouds and providers as well as on vScaler's cloud platform powered by OpenStack, a leading open source IaaS provider. The joining of the two platforms will enable customers to simplify and accelerate their strategic deployments of cloud by allowing them to provision full HPC-on-Demand clusters, Big Data analytics, accelerated GPU compute (for Machine Learning), tiered and accelerated storage platforms via CLOUD X Fusion, from Global Cloud Xchange.

- We initiated Reliance Branch Connect launch—India's first 4G Enterprise VPN Solution. This 4G last mile for MPLS VPN with pan-India reach offers bandwidth options up to 2 Mbps; simple deployment with usage based plans; and bandwidth throttling to avoid bill shocks. Pre-launch orders received for about 1500 MPLS spoke locations from marquee enterprise customers across India.

- GCX won “Excellence in Connectivity for Data Centers” award at the inaugural Datacloud Asia in Singapore on 23rd February 2017. In addition, CEO Bill Barney (that’s me) was honored with “Data Center Industry Achievement Award” in recognition of contributions to the Data Center Industry. Broadgroup’s inaugural Datacloud Asia Awards showcased innovation and recognized new sectors in Data Center and Cloud. The winners were chosen by an independent panel of Judges from across Asia and the US, with the objective of recognizing excellence in data centers, cloud services and operations.

Now I would like to hand over back to Gurdeep to summarise:

Gurdeep Singh

To Summarise:

1. Sector’s operational and financial performance has seen continuing severe adverse impact due to free offers, disruptive pricing and hyper competition. This sector situation needs urgent requisite corrective policy initiatives by the Government and regulators to infuse operational and financial health.

2. RCOM is moving ahead steadfastly with the focused execution of business and strategically transformational corporate transactions. **RCOM is in final stages of completing its Aircel merger and tower transactions which would deleverage our balance sheet substantially.**

3. RCOM is intensely focused on executing its 4G data led strategy riding on access to the Pan-India state-of-the-art network.

4. RCOM, post completion of transactions, would emerge a stronger player, with solid operating businesses of high-margin domestic enterprise segment, Data Centers, optical fibre and international business in GCX**.** **Additionally, RCOM will hold valuable strategic stakes of 50% in wireless JV and 49% future economic upside in the tower business.**

Thank You. Over to operator for the Q&A.