

Idea Cellular | HOLD

Idea moots fund-raising to bring financial leverage under control

In a stock-exchange filing yesterday, Idea announced its Board would meet on 4th of January to consider equity-raising proposals. We believe fresh equity funding would allow Idea to better defend its revenues and market share (RMS) based on a hike in 4G/fibre capex, and/or help reduce its surging leverage ratio [net debt-to-EBITDA]. As of Sep-17, the pro-forma net debt of VI merge-co was INR 1106bn—implied LR being 6.6x based on TTM EBITDA. Even after incorporating INR 155bn of proceeds from tower-divestments (assuming sale of entire Indus holding by Idea), we estimate the LR would surge further to c.8x by Mar-18, well ahead of the 6.5x MCLR [Maximum Closing Leverage Ratio] agreed by principal shareholders of the two companies (i.e. ABG and Voda Plc).

We do not expect Aditya Birla Group [ABG] to dilute its stake in Idea; as such, equity-raising may happen through a rights issue and/or a preferential issue to ABG, in our view. Rights issue done at a significant discount would be dilutive to fair value, but we expect investors to focus on the positives of fund-raising. We retain our Hold rating on Idea shares, with a Mar-19 TP of INR 110.

- Fund raising proposal appears to be driven by merger conditions, and not so much by immediate cash crunch or any covenant breach:** We estimate Idea can fund its 2HFY18 capex from cash balance (INR 28bn as of end-2Q) plus OCF (INR 3-4bn per quarter). Further, anticipated proceeds from recent sale of towers (INR 40bn) to ATC should help bridge the negative FCF through 1HFY19; there are no significant repayments due in this period. Further, the company has indicated there are no restrictive covenants from lenders on any borrowings. As such, we think compliance with merger-conditions may be the primary factor driving the latest fund raising proposal.
- Leverage ratio likely to remain ahead of MCLR:** The merger agreement specifies an MCLR (net debt-to-LTM EBITDA) of 6.5x if the transaction closes by Mar-18, and an MCLR or 6.0x if closing is achieved by Sep-18 (i.e. 2QFY19). These conditions are not cast in stone and can be waived jointly by the co-promoters. However, even assuming a full sell-down of 11.15% Indus stake by Idea, we estimate total net debt of around INR 1000bn for the merge-co by Mar-18, implying LR of c.8x. To comply with Mar-18 MCLR, we estimate Idea would need to raise INR 86bn of fresh equity, which is unlikely in our view.
- Preferential issue of >INR 56bn would reduce free float below 25% post-merger:** Current free float of Idea stock (including c.20% owned by Axiata) is 57.6%, which would halve to 28.8% post merger. Thus, bringing down free-float to 25.0% requires 13.2% dilution [(1-25/28.8) X 100] or a 15.2% increase in equity base [28.8/25.0] or an issue of approx. 550mn shares on current equity base of 3.61bn Idea shares. Based on SEBI-rules, the preferential issue priced is INR 101.5/share today, which implies a maximum size of INR 56bn for preferential allotment of equity to ABG. As such, we expect equity raising to involve a rights issue and/or a preferential issue to the ABG.

Idea Cellular: Key consolidated financials [IND AS]

Year end Mar, INR mn	FY16	FY17	FY18E	FY19E	FY20E
Revenues	359,494	355,757	299,364	309,364	335,076
Revenue growth (%)	13.9	(1.0)	(15.9)	3.3	8.3
EBITDA	119,675	102,763	61,756	67,187	76,340
EBITDA growth (%)	10.7	(14.1)	(39.9)	8.8	13.6
Adj. PAT	23,065	(8,215)	(45,296)	(48,177)	(46,191)
EPS (Rs)	6.4	(2.3)	(12.5)	(13.3)	(12.8)
EPS growth (%)	(28)	(136)	NM	NM	NM
P/E (x)	15.7	NM	NM	NM	NM
EV/EBITDA (x)	6.7	8.1	12.50	12.3	11.7
P/B (x)	1.5	1.5	1.8	2.4	3.4
U-FCFF yield (%) [a]	(30.9)	(8.7)	(1.0)	(0.5)	0.5
RoAIC (%)	7.0	2.3	(2.0)	(1.9)	(1.2)

Source: Company, JM Financial. [a] Unlevered FCFF divided by EV.



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Recommendation and Price Target

Current Reco.	HOLD
Current Price Target (12M)	110
Upside/Downside)	9.2%

Key Data – IDEA IN

Current Market Price	INR101
Market cap (bn)	INR363.3/US\$5.7
Free Float	38%
Shares in issue (mn)	3,602.9
Diluted share (mn)	3,610.3
3-mon avg daily val (mn)	INR1,624.3/US\$25.6
52-week range	124/66
Sensex/Nifty	33,812/10,442
INR/US\$	63.5

Price Performance

%	1M	6M	12M
Absolute	8.0	18.1	34.4
Relative*	4.9	8.0	5.7

* To the BSE Sensex

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Exhibit 1. Maximum size of preferential issue to ABG for minimum 25% free float

Preferential issue price (INR) [a]	101.5
Number of shares issue (bn)	0.55
Total equity raised (INR bn)	55.6

Source: JM Financial. [a] As per SEBI formula.

Exhibit 2. Idea shareholding assuming preferential issue of shares to ABG (%)

	Current		Post-issue		Post merger	
	mn	(%)	mn	(%)	mn	(%)
Aditya Birla Group [ABG]	1.53	42.4	2.08	50.0	2.08	25.0
Voda Plc		0.0		0.0	4.15	50.0
Axiata	0.71	19.7	0.71	17.1	0.71	8.6
Public	1.37	37.9	1.37	32.9	1.37	16.4
Total	3.61	100.0	4.15	100.0	8.31	100.0
Free float	2.1	57.6	2.1	50.0	2.1	25.0

Source: Company, JM Financial.

Exhibit 3. Maximum Closing Leverage Ratio (MCLR) as per merger agreement

Transaction closure by	MCLR (x)
4QFY18	6.50
1QFY19	6.25
2QFY19	6.00
3QFY19	5.75
4QFY19	5.50

Source: https://www.sec.gov/Archives/edgar/data/839923/000110465917038355/a17-12473_1ex4d32.htm.

Financial Tables (Consolidated)

Income Statement						Balance Sheet					
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E	Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
Net Sales	359,494	355,757	299,364	309,364	335,076	Shareholders' Fund	235,505	247,322	202,376	154,200	108,008
Sales Growth	13.9%	-1.0%	-15.9%	3.3%	8.3%	Share Capital	36,005	36,053	36,103	36,103	36,103
Other Operating Income	0	0	0	0	0	Reserves & Surplus	199,500	211,269	166,273	118,096	71,905
Total Revenue	359,494	355,757	299,364	309,364	335,076	Preference Share Capital	0	0	0	0	0
Cost of Goods Sold/Op. Exp	180,939	189,922	176,251	176,434	190,781	Minority Interest	0	0	0	0	0
Personnel Cost	16,119	17,976	17,093	17,969	19,038	Total Loans	428,957	579,097	587,400	643,008	697,592
Other Expenses	42,761	45,096	44,264	47,773	48,917	Def. Tax Liab. / Assets (-)	19,539	13,587	-11,716	-38,486	-64,223
EBITDA	119,675	102,763	61,756	67,187	76,340	Total - Equity & Liab.	684,000	840,006	778,061	758,722	741,377
EBITDA Margin	33.3%	28.9%	20.6%	21.7%	22.8%	Net Fixed Assets	712,238	846,234	820,689	795,555	773,775
EBITDA Growth	10.7%	-14.1%	-39.9%	8.8%	13.6%	Gross Fixed Assets	259,554	325,871	384,431	448,525	515,901
Depn. & Amort.	62,561	78,272	84,802	89,228	91,156	Intangible Assets	493,854	604,488	574,988	542,729	510,612
EBIT	57,115	24,491	-23,045	-22,041	-14,817	Less: Depn. & Amort.	47,793	97,429	150,730	205,700	262,739
Other Income	2,131	3,069	469	123	207	Capital WIP	6,623	13,303	12,000	10,000	10,000
Finance Cost	20,962	40,411	50,537	55,433	59,759	Investments	21,491	14,872	14,349	13,177	11,918
PBT before Excep. & Forex	38,284	-12,851	-73,113	-77,351	-74,369	Current Assets	67,527	105,941	51,865	52,287	58,275
Excep. & Forex Inc./Loss(-)	0	0	0	0	0	Inventories	0	0	0	0	0
PBT	38,284	-12,851	-73,113	-77,351	-74,369	Sundry Debtors	0	0	0	0	0
Taxes	15,220	-4,635	-24,527	-25,855	-24,792	Cash & Bank Balances	20,996	49,825	2,285	994	4,518
Extraordinary Inc./Loss(-)	4,217	4,218	3,291	3,319	3,386	Loans & Advances	0	0	0	0	0
Assoc. Profit/Min. Int.(-)	0	0	0	0	0	Other Current Assets	46,531	56,116	49,580	51,294	53,757
Reported Net Profit	27,281	-3,997	-45,296	-48,177	-46,191	Current Liab. & Prov.	117,255	127,041	108,843	102,298	102,591
Adjusted Net Profit	23,065	-8,215	-45,296	-48,177	-46,191	Current Liabilities	0	0	0	0	0
Net Margin	6.4%	-2.3%	-15.1%	-15.6%	-13.8%	Provisions & Others	117,255	127,041	108,843	102,298	102,591
Diluted Share Cap. (mn)	3,600.5	3,605.3	3,610.3	3,610.3	3,610.3	Net Current Assets	-49,728	-21,100	-56,977	-50,010	-44,316
Diluted EPS (INR)	6.4	-2.3	-12.5	-13.3	-12.8	Total - Assets	684,000	840,006	778,061	758,722	741,377
Diluted EPS Growth	-27.8%	0.0%	0.0%	0.0%	0.0%						
Total Dividend + Tax	2,600	0	0	0	0						
Dividend Per Share (INR)	0.6	0.0	0.0	0.0	0.0						

Source: Company, JM Financial

Cash Flow Statement					
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
Profit before Tax	38,284	-12,851	-73,113	-77,351	-74,369
Depn. & Amort.	62,561	78,272	84,802	89,228	91,156
Net Interest Exp. / Inc. (-)	14,437	4,542	12,425	-123	-207
Inc (-) / Dec in WCap.	2,361	32,072	-9,810	-6,430	-279
Others	2,402	2,459	0	0	0
Taxes Paid	-8,611	-6,808	-776	-914	-946
Operating Cash Flow	111,434	97,685	13,527	4,410	15,356
Capex	-359,609	-211,730	-60,032	-65,009	-70,322
Free Cash Flow	-248,175	-114,044	-46,505	-60,599	-54,966
Inc (-) / Dec in Investments	205	209	0	0	0
Others	1,318	4,234	4,282	4,614	4,852
Investing Cash Flow	-358,086	-207,287	-55,750	-60,395	-65,470
Inc / Dec (-) in Capital	175	-4,453	50	0	0
Dividend + Tax thereon	-2,598	-2,599	-776	-914	-946
Inc / Dec (-) in Loans	139,266	145,483	-4,590	55,608	54,584
Others	0	0	0	0	0
Financing Cash Flow	136,843	138,430	-5,317	54,694	53,639
Inc / Dec (-) in Cash	-109,809	28,829	-47,540	-1,291	3,524
Opening Cash Balance	130,805	20,996	49,825	2,285	994
Closing Cash Balance	20,996	49,825	2,285	994	4,518

Source: Company, JM Financial

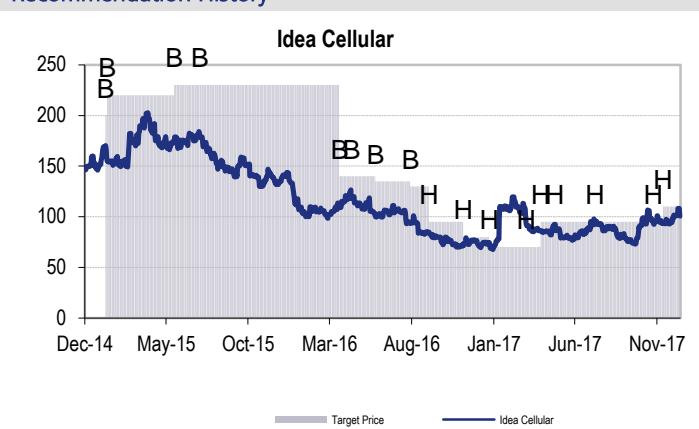
Dupont Analysis					
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
Net Margin	6.4%	-2.3%	-15.1%	-15.6%	-13.8%
Asset Turnover (x)	0.6	0.5	0.4	0.4	0.4
Leverage Factor (x)	2.6	3.2	3.6	4.3	5.7
RoE	9.9%	-3.4%	-20.1%	-27.0%	-35.2%
Key Ratios					
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
BV/Share (INR)	65.4	68.6	56.1	42.7	29.9
ROIC	7.0%	2.3%	-2.0%	-1.9%	-1.3%
ROE	9.9%	-3.4%	-20.1%	-27.0%	-35.2%
Net Debt/Equity (x)	1.7	2.1	2.9	4.2	6.4
P/E (x)	15.8	-44.3	-8.1	-7.6	-7.9
P/B (x)	1.5	1.5	1.8	2.4	3.4
EV/EBITDA (x)	6.7	8.1	12.50	12.3	11.7
EV/Sales (x)	2.1	2.5	3.2	3.3	3.2
Debtor days	0	0	0	0	0
Inventory days	0	0	0	0	0
Creditor days	0	0	0	0	0

Source: Company, JM Financial

History of Earnings Estimate and Target Price

Date	FY18E EPS (INR)	% Chg.	FY19E EPS (INR)	% Chg.	Target Price	% Chg.
27-Jan-15					200	
30-Jan-15					220	10.0
4-Jun-15					230	4.5
22-Jul-15					230	0.0
7-Apr-16	0.7				140	-39.1
13-Jun-16	1.6	128.6	2.8		135	-3.6
17-Aug-16	1.1	-31.3	2.0	-28.6	130	-3.7
21-Sep-16	-1.3	-218.2	0.2	-90.0	95	-26.9
24-Nov-16	-3.0	130.8	-1.9	-1050.0	80	-15.8
11-Jan-17	-6.0	100.0	-5.6	194.7	70	-12.5
17-Apr-17	-12.4	106.7	-8.9	58.9	95	35.7
13-May-17	-12.4	0.0	-8.9	0.0	95	0.0
27-Jul-17	-12.4	0.0	-8.9	0.0	95	0.0
13-Nov-17	-12.4	0.0	-8.9	0.0	95	0.0
1-Dec-17	-12.5	0.8	-13.3	49.4	110	15.8

Recommendation History



APPENDIX I

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