



Operation of Mobile Businesses of Three Companies – R.COM, MTS and AIRCEL - Under a new entity lead by Reliance Communications in 2015–A Study

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Abstract

Reliance Communications is India's foremost and truly integrated telecommunications service provider. The Company has a customer base of over 118 million, including over 2.6 million individual overseas retail customers. The telecom industry is at a stage where players are faced with high operational costs, be it energy, infrastructure, sales or distribution. Given this dynamic nature of the industry, it is inevitable for operators to consider such arrangements with each other to offer continued and seamless mobile services to customers. According to the deal the two companies will offer the 2G ICR advantage to its customers in some key circles, with the agreement being periodically expanded. Reliance is in merger with other partners to extend this privilege to its customers. As result of the demerger, SSTL will acquire and hold a 10% equity stake in RCOM. In addition, RCom will assume the liability to pay the DoT instalments for SSTL's spectrum, amounting to Rs. 392 crore per annum for the next 10 years. This Study aims at the implication and impact of recent merger of R.Com and Aircel.

Key words: Reliance Acquisition, merger of R.Com.&Aircel, Aircel merger scheme

Introduction

“The telecom industry is at a stage where players are faced with high operational costs, be it energy, infrastructure, sales or distribution. Given this dynamic nature of the industry, it is inevitable for operators to consider such arrangements with each other to offer continued and seamless mobile services to customers”

Reliance Communications and Aircel begun to combine their wireless telecom operations to create India's second largest mobile operator as intensifying competition fuels consolidation in a crowded market. A pact for 90-day exclusive talks has been initiated with Aircel's majority owner, Malaysia's Maxis Communications, and Sindy Securities

and Investments for the potential merger. The potential combination will exclude RCom's towers and optical fibre infrastructure, for which R.Com is proceeding with an asset sale.

Reliance Communications Limited

Reliance Communications Limited, founded by the late Shri Dhirubhai H Ambani (1932-2002), is the flagship company of the Reliance Group. The Reliance Group currently has a net worth in excess of Rs 91,500 crore (US \$15.3 billion), cash flows of Rs 10,200 crore (US \$1.7 billion) and net profit of Rs 4,700 crore (US\$ 0.8 billion).

Reliance Communications is India's foremost and truly integrated



telecommunications service provider. The Company has a customer base of over 118 million, including over 2.6 million individual overseas retail customers. Reliance Communications corporate clientele includes over 39,000 Indian and multinational corporations including small and medium enterprises and over 290 global, regional and domestic carriers.

Reliance Communications has established a pan-India, Next-Generation, integrated (wireless and wireline), convergent (voice, data and video) digital network that is capable of supporting best-in-class services spanning the entire communications value chain, covering over 21,000 cities and towns and over 400,000 villages. Reliance Communications owns and operates the world's largest next generation IP enabled connectivity infrastructure, comprising over 280,000 kilometers of fiber optic cable systems in India, USA, Europe, the Middle-East and the Asia-Pacific region.

SISTEMA

Sistema is the publicly-traded diversified holding company in Russia and the CIS. SISTEMA has its headquarters in Moscow, and operates a number of consumer service businesses in the areas of IT and telecoms — Mobile Tele Systems, Moscow City Telephone Network, Sky Link, MTS India and Established in 1993. This is a major shareholder of companies serving over 100 million customers in the sectors of telecommunications, high technology, radars and aerospace, banking, retail, mass-media, tourism and healthcare services.

Today Sistema is a large private investor operating in the real sector of the

Russian economy. Sistema's investment portfolio comprises stakes in predominantly Russian companies from various sectors of economy, including telecommunications, utilities, retail, high tech, pulp and paper, pharmaceuticals, healthcare, railway transportation, agriculture, finance, mass media, tourism, etc. Sistema is the controlling shareholder in most of its portfolio companies. Sistema's competencies focus on improvement of the operational efficiency of acquired assets through restructuring and attracting industry partners to enhance expertise and reduce financial risks.

SISTEMA's global depository receipts are listed under the symbol "SSA" on the London Stock Exchange (1 GDR is 20 ordinary shares) and the ordinary shares are listed under the symbol "AFKS" on the Moscow Exchange.

The Company reported revenues of RUB 164.0 billion for the second quarter of 2015, and total assets of RUB 1,175.7 billion as at June 30, 2015. Sistema's global depository receipts are listed under the symbol "SSA" on the London Stock Exchange. Sistema's ordinary shares are listed under the symbol "AFKS" on the Moscow Exchange. Website: www.sistema.com

MAXIS Communications

Maxis Berhad is a communications service provider in Malaysia. Headquartered in Kuala Lumpur, Malaysia, providing a variety of communication products, applications and value added services for consumers, large enterprises and small & medium business owners. Maxis launched Malaysia's first 4G LTE network on 1 January 2013. Maxis' high speed internet footprint is the largest in Malaysia, and



were the first to bring the iPhone, BlackBerry and the Samsung Galaxy line of smart phones to the Malaysian market. Through their partnership with Astro. Maxis now offers fibre internet packages bundled with entertainment, made available to customers at home and on mobile devices. They provide multi-channel customer service; customers are able to reach Maxis service representatives via telephone, web and social media platforms. Maxis Call Centre was awarded the 'Best of the Best' honour at the 2012 Customer Relationship Management and Contact Centre (CCAM) Annual Awards, being the only service provider that awards scholarships to children of their own post paid customers. Maxis uses the dialling prefixes of "012", "017", "014-2" and "011-2". The majority of the company's stake is owned by billionaire Ananda Krishnan, and the company has about 12.9 million subscribers as of the fourth quarter of 2013.

Products and services

As of May 2015, Maxis has 2G coverage of 95% on populated areas, 3G at 88%, 4G LTE at 59%, network modernisation at 81%. It is widely perceived that Maxis is best with network coverage and speed.

Maxis provides a variety of mobile communication products and services. They offer prepaid data plans, call plans and SMS plans, postpaid data plans, call plans and SMS plans, devices, wireless broadband, fibre internet, international roaming, MMS, WAP (over both GSM and GPRS) and residential fixed line services.

For business customers, Maxis offer cloud computing, data storage, machine-to-machine services, fixed high speed internet, VSAT services (satellite based

communications), call conferencing and a variety of mobile plans. Maxis also provide online games and a music store for its customers to download multimedia content.

Maxis' most popular service is its prepaid brand Hotlink, which currently serves over 9.5 million customers in Malaysia.

There are several high profile celebrities who have signed on as spokespersons for Maxis, including Siti Nurhaliza, the Malaysian reality television show Akademi Fantasia's contestants, along with Jessy Wong The Diva and Arthur the Brave and Fluffy. Maxis was the first company to launch LTE services in Malaysia on 1 January 2013, starting in the Klang Valley region. Maxis operates 2G GSM /GPRS/ EDGE, 3G WCDMA/HSPA+/DC-HSPA, 4G LTE networks.

Sindya Securities Investments Private Limited

Sindya Securities Investments Private Limited is a Private Company incorporated on 19 January 2006. It is classified as Indian Non-Government Company and is registered at Registrar of Companies, Chennai. Its authorized share capital is Rs. 500,000,000 and its paid up capital is Rs. 260,100,000. It is involved in Activities auxiliary to financial intermediation, except insurance and pension funding. [This Group includes activities involved in or closely related to financial intermediation other than insurance and pension funding but not themselves involving financial inter-mediation.

AIRCEL GROUP

The Aircel Group is a result of alliance between Maxis Communications Berhad of Malaysia (74% equity) and Sindya



Securities & Investments Private Limited (26% equity).

The Aircel Group, formed in 1994, offers affordable and outstanding mobile services to a vast subscriber base in India. Aircel has a vision of delighting its customers by giving them the respect they deserve. Our goal is to provide our customers with exemplary service and persistently look for new ways to surpass their expectations.

Aircel commenced operations in 1999. In our first decade of operations, we concentrated on building our foundations in the southern part of the country, and soon emerged as the regional market leaders. We worked hard and achieved that success by remaining focused on growth opportunities. Soon after our company began with its expansion in 2005 and has now set its sight on becoming a pan India operator. Our project pipeline is robust, allowing for sustainable long-term growth.

In addition to our leadership position in Tamil Nadu, Aircel met with extraordinary success in the Eastern frontier circles. We pride ourselves on customer satisfaction and managed to emerge as the market leaders in Assam and North Eastern states within 18 months of operations. During this period, our company gained a strong foothold in 10 circles, to provide better access to our customers. The company is present in all 23 telecom circles including Chennai, Tamil Nadu, Assam, North East, Orissa, Bihar, Jammu & Kashmir, Himachal Pradesh, West Bengal, Kolkata, Kerala, Andhra Pradesh, Karnataka, Delhi, UP(West), UP(East), Maharashtra & Goa, Mumbai, Haryana, Madhya Pradesh, Punjab, Gujarat and Rajasthan.

PRODUCTS AND SERVICES

Aircel offers its customers, services and products that are easy to understand and use. All offerings are stimulating and at the same time extremely unique as Aircel continues to re-invent itself constantly to deliver the best and most up-to-date services. The brand instils a feeling of pride, confidence and reliance among all stakeholders by anticipating their desires and fulfilling the same efficiently.

Aircel provides 3G service in Andhra Pradesh, Assam, Bihar & Jharkhand, Chennai, Jammu & Kashmir, Karnataka, Kerala, Kolkata, North East, Orissa, Punjab, Tamil Nadu, UP East and West Bengal.

Implication of merging

Reliance Communications and Aircel begun to combine their wireless telecom operations to create India's second largest mobile operator as intensifying competition fuels consolidation in a crowded market. A pact for 90-day exclusive talks has been initiated with Aircel's majority owner, Malaysia's Maxis Communications, and Sindy Securities and Investments for the potential merger. The potential combination will exclude RCom's towers and optical fibre infrastructure, for which R.Com is proceeding with an asset sale. The discussion are non-binding in nature. Any transaction will be subject to due diligence, definitive documentation and regulatory, shareholders' and other third party approvals. Hence, there is no certainty that any transaction will result."

In Dec, 2015 RCom entered a major pact to acquire the Indian business of Russia's Sistema, which operates under the 'MTS' brand, in a unique stock-cum-spectrum-fee payment deal.



RCom Aircel MTS wireless combo to benefit from substantial capex and opex synergies

As per the deal being negotiated, RCom shareholders will receive free listed shares in the combined wireless entity. This apart, the debt of Rs.10,000 crores will be transferred to the separate listed combined entity.

Impact of Merger

The merger will bring 9 million customers and around Rs 1,500 crore in revenues to RCom. It would also help RCom extend the validity of spectrum in 800/850 MHz band in eight circles, including Delhi and Kolkata, by 12 years from 2021 till 2033. Reliance Communications BSE -7.01 % (RCom), Aircel and Sistema (MTS) have begun initial talks for a three-way merger that could see the emergence of India's third largest telco by subscribers. In the first sign of sector consolidation, Reliance Communications last month agreed to buy Russian conglomerate Sistema's Indian mobile phone business in an all-stock deal. This month it agreed to sell its tower business to a group including TPG Capital Management LP to cut a heavy debt load. The Aircel talks exclude those assets. If the deal happens, RCom-Aircel-MTS wireless combo will have over 150 million customers in India and it will hold hold close to 20 percent of the total spectrum - highest in country - in virtually every band currently available to private players. This include the deal with MTS. Also, the monetisation of the tower and fiber assets will continue. Once these deals go through, RCom will become debt-free. According to the deal the two companies will offer the 2G ICR advantage to its customers in some key circles, with the agreement being periodically expanded. Reliance is in

merger with other partners to extend this privilege to its customers. They are already in advanced stages of talks with several operators across the country to put these agreements in place, A source from Gurdeep Singh, President and Chief Executive Officer (Wireless) Reliance Communications. Once in place, RCOM's 2G GSM customers will be able to roam seamlessly on all partner networks, free of any additional cost. "All agreements with existing telecom operators are likely to be completed by the end of the second quarter of the ongoing financial year.

"This agreement will expand RCOM's network footprint at no upfront cost—a 'pay as you use' model—and improve both service quality and operational efficiencies," Mr. Singh added.

The merger would create a company that holds roughly 20% of India's rapidly growing cell phone market, and help close the distance between it and much larger rivals **Bharti Airtel Ltd.** and **Vodafone Group PLC's** India unit. As of September 2015, Reliance had around 110 million subscribers while Aircel had around 84 million, according to the Telecom Regulatory Authority of India.

Asset sales and consolidation

The Anil Ambani-led group has been looking at both consolidation and asset sales aggressively. On 14 December, *Mint* reported that Reliance Group could seek to reduce debt by more than 40% through asset sales. Stake sales in its financial services businesses, along with plans to sell telecom towers, optical fibre, cement and road assets, could net the group more than Rs.50,000 crore. This is about 44% of the group's outstanding debt of Rs.1.14 trillion in September, 2015 according to Capitaline,



which provides financial and market data.

On 13 December, 2015 brokerage CLSA said R-Com's impending tower deal could lower its consolidated debt by a significant 60%. The operator had a debt of Rs.35,250 crore as on 30 September.

In addition to multiple infrastructure sharing deals with Reliance Jio (towers and fibre), R-Com is also finalizing a spectrum-sharing and trading deal with the company for its 800MHz spectrum, CLSA noted.

"Given that Reliance Jio has 5MHz of 800MHz in only two of the top-six industry ARPU (average revenue per unit) circles and nine of the 22 circles, this deal with R-Com is crucial as it would ensure a pan-India footprint on 800MHz thus boosting its 4G LTE services," CLSA said in the note. LTE, or long-term evolution, is a 4th-generation, high-speed technology standard.

"Reliance Jio deals are aiding to unlock R-Com asset values while the reciprocal benefits from sharing network and spectrum would lower capex requirement. Further proceeds from the spectrum sharing/trading deals would be used by R-Com to pay the Rs.7,000 crore liberalization fee for 800MHz spectrum and repay added debt, providing further upsides," the CLSA note added.

Shares of R-Com gained 2.39% to close at Rs.85.70 on the BSE, while the benchmark Sensex lost 0.56% to close at 25,590.65 points.

Reducing Debt

Both RCom and Aircel are saddled with high debt which must be retired before a merger can go ahead or even be considered, said bankers in the know. At last count, Aircel's debt stood at around

Rs 20,000 crore while RCom reported net debt of Rs 38,595 crore. Aircel is learnt to have very nearly closed a deal to sell its 4G airwaves in the 2300 Mhz band to Bharti Airtel BSE -4.85 % for around Rs 4,000 crore. The company has taken loans from its shareholders and these can be converted into equity. The spectrum sale and conversion of loan to equity will help Aircel reduce its debt to Rs 15,000 crore. RCom, on its part, according to sources, is on the verge of finding a buyer for its telecom towers. With the Viom Networks-American Tower deal finalised at an enterprise value of Rs 21,000 crore, the Anil Ambani company is hopeful of fetching close to Rs 20,000 crore for its 40,000 towers that come with a lease guarantee from Mukesh Ambani's Reliance Jio. The company is also hopeful of divesting a part or all of its overseas undersea cable arm, and use the funds to retire debt. As a result of these actions, the total debt of the two companies could fall to Rs 30,000 crore before the merger takes place, said one of the persons mentioned earlier.

Aircel has welcomed the move as it will be cost effective for both companies and they can focus on other areas to expand .

"The telecom industry is at a stage where players are faced with high operational costs, be it energy, infrastructure, sales or distribution. Given this dynamic nature of the industry, it is inevitable for operators to consider such arrangements with each other to offer continued and seamless mobile services to customers, soured from Aircel Chief Operating Officer Kaizad Heerjee.

Business Case

Aircel and RCom have operating profits of Rs 2,500 crore and over Rs 7,500 crore, respectively. Excluding the enterprise,



undersea cable and tower businesses, RCom's EBITDA (earnings before interest tax, depreciation and amortisation) from the mobility business is estimated to be Rs 3,000-3,500 crore.

Neither Aircel nor RCom, independently, are likely to achieve significantly higher profitability as competition grows. But the three-way merger will create the country's third-largest telco, behind Airtel and Vodafone, and enable the combined entity to leverage size and synergies to enhance profitability.

Mr Mikhail Shamolin, President and CEO of Sistema, intended that "The merger of SSSL and RCOM's telecom businesses is a milestone event. Despite the numerous challenges the sector faced in recent years, the combination of two leading data service providers is a clear sign of progress for the Indian telecom industry. They are confident that SSSL's entry into the equity capital of RCOM as a strategic investor will strengthen the competitive position of the combined company and provide subscribers with superior experience by fast tracking the growth of LTE technology in India.

Both RCom and Aircel operate their 2G GSM services on the 1800 Mhz band, which can also be used for offering 4G services after paying the government the auction-determined market price. The two also have 3G airwaves in the 2100 Mhz band.

The two companies already have infrastructure-sharing pacts which enable users to interchangeably use their networks. These pacts have also resulted in mutually opportunistic laying of networks and telecom tower footprint, which would mean a lesser effort to reduce duplication. If the Aircel deal goes through, Reliance Communications

shareholders will receive free shares in the new combined wireless entity, said a source with direct knowledge of the matter. Reliance Communications will continue to own its enterprise and undersea cable businesses.

With a debt of about \$6 billion, Reliance Communications is the most leveraged among listed Indian carriers. Unlisted Aircel is also battling a heavy debt burden, which rating agency ICRA said was about 185 billion rupees (\$2.8 billion) as of 2013. Prior to Closing of the Transaction, SSSL intends to pay off its existing debt. An appropriate payment / earn-out mechanism has been agreed in relation to disputed spectrum contiguity charges claimed by DoT. The combination of wireless businesses, through the demerger of SSSL wireless business into RCOM for stock consideration, will generate significant capex and opex synergies for mutual benefit.

The Indian data market is witnessing explosive growth, and SSSL's proven strengths in that space will further enhance RCOM's capabilities in delivering a superior experience to their valued customers. They are pleased that the addition of SSSL's valuable spectrum holdings in the 800 - 850 MHz band will strengthen RCOM's spectrum portfolio, and extend our ability to provide world class 4G LTE services to their customers in 8 important circles in the country till the year 2033.

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a strategic investor will strengthen the competitive position of the combined company and provide subscribers with superior experience by fast tracking the growth of LTE technology in India.

Moreover, they believe the completion of this transaction will serve as an example of growing business ties between Russia and India and encourage other investments between the two countries. This transaction underscores SSTL's track record in building the fastest-growing data services provider. This is an exciting new chapter for India's telecom industry and we look forward to leveraging our companies' combined experience for the development of LTE in India.

The Closing of the transaction, expected in the second quarter of 2016, is subject to customary conditions precedent, including inter alia applicable corporate, regulatory and other approvals.

Post Closing of the deal, minority investors of SSTL will be given an option to exchange their shares in SSTL with the pro-rata RCOM shares held by SSTL.

The merger will bring 9 million customers and around Rs 1,500 crore in revenues to RCom. It would also help RCom extend the validity of spectrum in 800/850 MHz band in eight circles, including Delhi and Kolkata, by 12 years from 2021 till 2033.

Following the development, the stock climbed 3.92 per cent to hit a high of Rs 78.20 on BSE. The decision by the RCom board has paved the way for the first major consolidation in the domestic telecom sector since 2009.

This is undoubtedly a very positive development. It has sent the right signals to global investors. M&A in any business

is a sign of maturity and this shows that the Indian telecom business and the regulations are maturing. This can be a game changer for R Comm going forward.

Prima facie the rating for the company will remain unaffected by the merger, but RCom will benefit, as it will have an additional 9 million data subscribers. It will have access to 850 megahertz spectrum, which is one of the most efficient waves in Indian circles. It will also enhance RCom's ability to make further arrangement of spectrum sharing and trading with Reliance Jio in future. The merger will help RCom launch its own 4G services later on. All in all.

The rating agency has BB - rating and 'stable outlook' on the telecom operator. As per the deal, SSTL will acquire 10 per cent equity in RCom, with the latter assuming the liability to pay the DoT installments for former's spectrum, amounting to Rs 392 crore per annum for the next 10 years. However, SSTL will bear the burden of its existing debt, RCom said in a filing to BSE. MTS has a debt of around Rs 3,800 crore. "The combination of our wireless businesses, through the demerger of SSTL wireless business into RCom for stock consideration, will generate significant capex and opex synergies for mutual benefit," said Gurdeep Singh, President and Chief Executive Officer — Consumer Business at RCom.

If the Aircel deal goes through, Reliance Communications shareholders will receive free shares in the new combined wireless entity, said a source with direct knowledge of the matter. Reliance Communications will continue to own its enterprise and undersea cable businesses. With a debt of about \$6 billion, Reliance Communications is the most leveraged among listed Indian carriers. Unlisted



Aircel is also battling a heavy debt burden, which rating agency ICRA said was about 185 billion rupees (\$2.8 billion) as of 2013.

Conclusion

It is definitely a step in the right direction as the industry has to move towards consolidation. It is difficult for so many telcos to survive in an extremely cut-throat environment with low ARPUs. Increasing competition will make life difficult for bottom four or five telecoms carriers, adding more such deals could be expected next year.

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The Reliance mobile phone business is India's fourth-biggest by customer numbers while Aircel ranks fifth. The combined business would surpass Vodafone's Indian operation as number two in the sector. India's telecoms market is the world's second-biggest behind China in terms of mobile phone subscriptions, but tough competition means low margins for the 10 carriers. In the first sign of sector consolidation, Reliance Communications agreed to buy Russian conglomerate Sistema's Indian mobile phone business in an all-stock deal. Next it agreed to sell its tower business to a group including TPG Capital Management LP to cut a heavy debt load. The Aircel talks exclude those assets.

Reliance Communications has a pact with Reliance Jio to share some airwaves. A deal with Aircel, majority owned by Malaysia's Maxis Communications, will

expand its access to 3G airwaves and add 4G capacity to its portfolio. Increasing competition will make life difficult for bottom four or five telecoms carriers, adding more such deals could be expected next year. Bharti Airtel Ltd is the current market leader. Reliance Communications' India operations that include its wireless business accounted for 82 percent of its revenue of about 47 billion Indian rupees (\$710 million) for the three months to September.

If the Aircel deal goes through, Reliance Communications shareholders will receive free shares in the new combined wireless entity, said a source with direct knowledge of the matter. Reliance Communications will continue to own its enterprise and undersea cable businesses.

With a debt of about \$6 billion, Reliance Communications is the most leveraged among listed Indian carriers. Unlisted Aircel is also battling a heavy debt burden, which rating agency ICRA said was about 185 billion rupees (\$2.8 billion) as of 2013. The discussions between R-Com and Aircel are non-binding and any transaction will be subject to due diligence, along with shareholders and other third-party approvals.

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