

8 October 2012

CMP: Rs. 3.2

Industry: Telecom services

BSE group: B

Promoters

Videocon Group

Date of incorporation

1946

Registered office

Autocars Compound, Adalat Road,
Aurangabad 431005

Company website

www.connectzone.in

Caution: The company has lost 94.8% of its market value since December 2007. It has a negative net worth of minus Rs. 6989 mn. Its GSM license may be revoked by the Supreme Court and its market value may fall further.

Key Data (as on 1 Oct'12)

BSE	511116	ISIN	INE527B01012
Face Value	10.0	Mkt Cap (Rs. mn)	1928.6
Current P/E	negative	Current P/BV	negative
52 week high-low	5.48-2.70	30 day avg. daily trading volume (nos.)	22,095
Equity Capital (Rs mn)	6122.6	Networth (Rs mn)	-6988.9

Company business

The company provides landline, internet, leased line and mobile telephony (GSM and CDMA) services in the Punjab telecom circle.

The company was formerly part of the Himachal Futuristics Communications group, named HFCL Infotel and promoted by Anant Nahata. It started as a provider of landline services under the brand name 'Connect' in 2000. It launched CDMA services in 2007 under the brand name PING. It launched GSM operations in Punjab in 2010. The HFCL group held 36% in a joint-venture with the Videocon group under the name Datacom – this company had licenses in all circles except Punjab. As part of Videocon's buyout of HFCL's stake in Datacom (now Videocon Telecommunications) in August 2009, the ownership of HFCL Infotel was also transferred to the Videocon group at no additional consideration because the debt of HFCL was absorbed by the Videocon group. Post the change of management, the company is now named Quadrant Televentures.

The company's financial performance in FY12 is compared to peers in the table below:

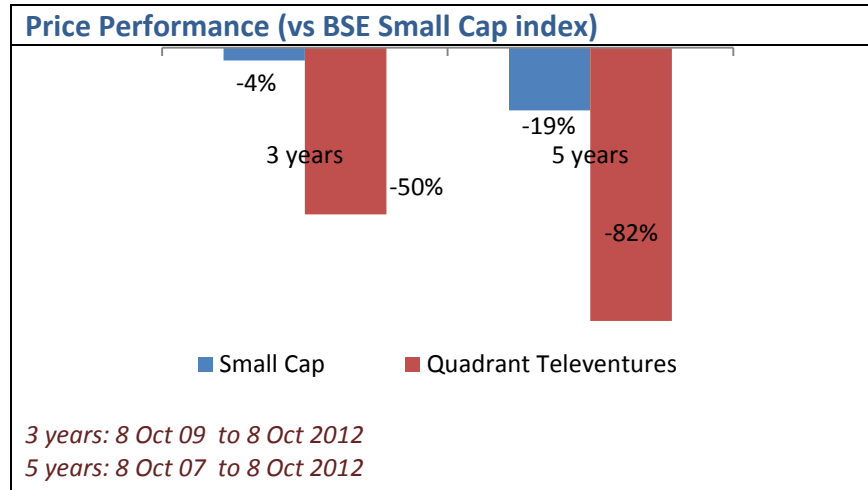
Financials - Standalone

FY12, Rs mn	Quadrant Televentures	Tata Teleservices	Tata Communications	MTNL
Total income	2828.9	25057.2	42683.9	36244.1
EBIDTA	(308.7)	5470.5	11645.9	-15999
EBIDTA margin	negative	21.8%	27.3%	negative
PAT	(1791.6)	(5175.5)	1713.4	(41097.8)
PAT margin	negative	negative	4.0%	negative
EPS	negative	negative	6.01	negative
Cash accruals	(589.9)	258.5	8784.2	(-26135.6)
Debt/EBIDTA (x)	negative	9.82	0.82	negative
Debt/Equity (x)	negative	negative	0.13	3.80
ROANW	-	negative	2.40%	negative
ROACE	negative	negative	4.80%	negative
P/E	negative	negative	26.3	negative
P/BV	Negative	negative	0.9	0.68

Source: Moneycontrol, Company

Write to us at:

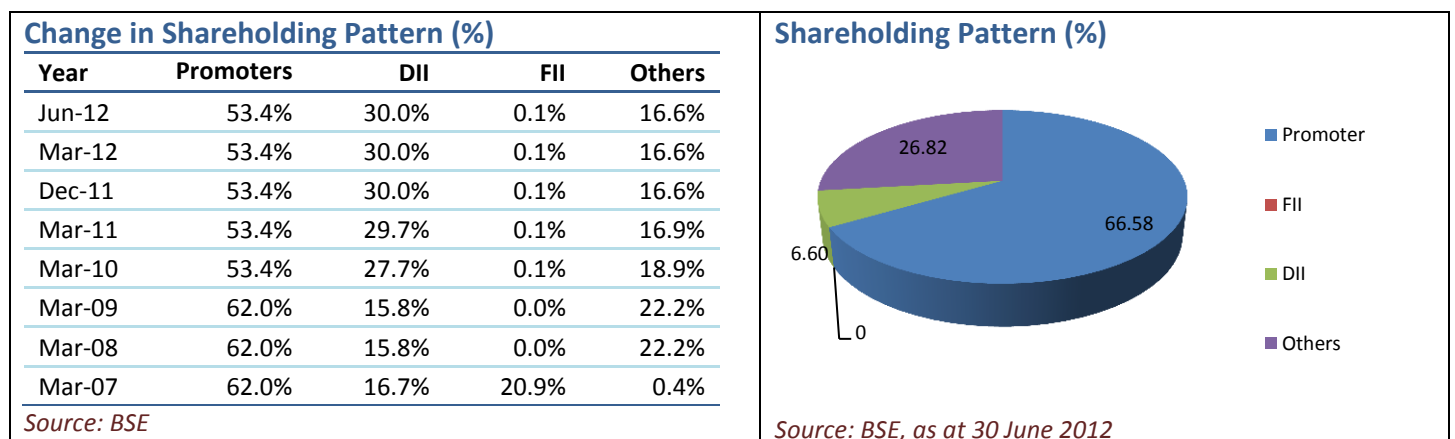
equity.research@outlook.com



Public Shareholders >1%

Sl. No.	Name of the Shareholder	No. of Shares held (mn)	Shares as % of Total No. of Shares
1	IDBI Bank Ltd	118.3	19.3
2	Oriental Bank of Commerce	23.0	3.8
3	Mantu Housing Projects Ltd	16.1	2.6
4	Oriental Bank of Commerce	21.0	3.4
5	Masitia Capital Services Ltd	13.0	2.1
6	ING Vysya Bank Ltd	11.9	1.9
7	Life Insurance Corporation of India	10.8	1.8
8	Moolsons Holdings Pvt Ltd	8.3	1.4
Total		222.3	36.3

Source: BSE



The equity held by lenders is on account of the conversion of their loans into shares, under a corporate debt restructuring scheme implemented with effect from FY10.

Company's brand fairly well-known in Punjab	Key strengths The company has an established presence in Punjab – it has a total subscriber base of 1.7 mn telephony customers, including 200,044 landline customers, 115,538 Broadband internet customers 27,768 CDMA mobile customers and 1.3 mn GSM mobile customers. The company's products are sold under the brand 'Connect' and the fact that the new management has continued to market the products under the same brand is testimony to the salience of the brand with customers.
Broadband services grow by 10%	Broadband internet services showed decent growth as the company's subscriber base in this segment increased by 10% to 200,044.
Change of management, raising the possibility of much-needed capital infusion	The company's net worth has been negative since FY07. The company's accumulated losses are Rs. 15,428 mn, while its debt has consistently been over Rs. 6000 mn for at least ten years. As discussed earlier, its ownership was transferred to the Videocon group at zero consideration in August 2009. The company urgently needs capital infusion to continue operations, and the Videocon group is better positioned to provide this capital infusion as compared to the erstwhile promoters of the company.
Competitive pressures in the business	Key concerns The mobile services industry is marked by intense competition, and the company faces pressures from bigger players such as Airtel, Vodafone, Idea Cellular and Reliance, among others. There are already eight players in the Punjab circle, and this company, given its financial weaknesses and market position, faces significant hurdles to increase its market share. The economics of the mobile phone industry are practically unsustainable for small players, and they will be the worst-affected by competition in the extremely price-sensitive Indian market. Given their inability to match their larger and well-funded competitors on prices, as well as new measures such as mobile number portability etc., this will drive market share away from small players towards larger players.
Financial position – company is in dire straits	The company underwent a corporate debt restructuring scheme in FY10, and loans were reduced from Rs. 7954 mn in FY09 to Rs. 7722 mn in FY10 (the lenders were given shares in the company). The company's debt stands at Rs. 6042 mn. However, given the accumulated losses of Rs. 15,428 mn and the negative equity of Rs. 6989 mn, the company is in urgent need of capital infusion.
Videocon's 2G licenses got cancelled this year	The contingent liabilities of the company add up to Rs. 852 mn, of which nearly Rs. 605 mn is on account of various disputes with BSNL. On 2 February 2012, as part of its investigation into the irregularities in the allocation of 2G spectrum, the Supreme court revoked 122 2G licenses of companies in various companies. The affected companies include Uninor (22 circles), Videocon (21 circles), Loop Telecom (21 circles), MTS (21 circles), Etisalat (15 circles), Idea Cellular (15 circles), S Tel (6 circles) and Tata Teleservices (3 circles). The spectrum is going to be re-auctioned and the prices are expected to be much higher (base price is expected to be Rs. 140 bn for 5 MHz pan India 2G license. For comparison, Swan Telecom acquired licenses in 13 circles at a price of Rs. 15 bn in 2008). Videocon's operations in Punjab are conducted through this company, whose license has not yet been revoked. The cancellation of Videocon's licenses doesn't affect the feasibility of continuing operations in Punjab, but it is bound to affect Videocon's operations adversely (Videocon does not have a 3G license either), and the prohibitive price of the newly auctioned spectrum may lead Videocon to exit the telecom business altogether.

The exit of the main promoter of the company will lead to folding up of the business, or sale of the business to a competitor. Given the current financial position of the company, it is unlikely that such a sale will generate any returns to shareholders of the company.

Company's own GSM license may be cancelled

The company, originally a CDMA operator, was granted GSM spectrum under a dual technology license. The Cellular Operators Association of India (COAI), a GSM lobby group, has filed a petition in the Supreme Court for revoking the GSM licenses granted to CDMA operators (including this company, Tata Teleservices, and Reliance Communications) under dual technology licenses. An adverse judgment would sound the death knell for the company.

Industry overview

Mobile subscriber base grows at 13%, 41.9 mn subscribers avail of mobile number portability (MNP) service

The Indian telecom market grew by 12.4 % to 951.34 mn subscribers as at March 31, 2012. At 919.17 mn wireless connections the growth in the mobile telephony market was around 13.0%. The share of private sector in total telephony was 87.01%. Overall teledensity is 78.66%. Urban tele-density is about 169.55% reflecting an oversupply of towers, whereas rural tele-density is at 39.22%. Broadband connections have also crossed 13.81 mn connections. The total number of GSM subscribers as of July 2012 was 671.95 mn. The total CDMA subscriber base was 247.4 mn in Jan 2012 representing 27.7% of India's subscriber base at that time.

The introduction of mobile number portability has led to significant churn in the market, with a total of 41.9 mn subscribers having submitted requests for changing their service providers as of March 2012.

Government Policies

National telecom policy 2012

The national telecom policy framed by the government in 2012 is aimed at achieving the following:

- To increase rural tele-density from current level of around 39% to 70% around 2017 and 100% by 2020.
- To provide affordable and reliable broadband services and reach 175 mn broadband connections by 2017 and 600 mn by 2020 at a minimum download speed of 2 Mbps.
- Promote domestic manufacturing of telecom equipment, so that it accounts for 80% of telecom sector demand by 2020.
- Simplify the licensing framework and move towards one license across the nation for services.
- Move towards full mobile number portability. Under the existing scheme, subscribers can retain their numbers only if they switch to service providers within the same circle.
- Move towards free national roaming.
- Make available an additional 300 MHz of spectrum by 2017 and another 200 MHz by 2020.
- Put in place a simplified merger and acquisition regime in the telecom services sector, while ensuring adequate competition.

The department of telecom (DoT) and Telecom Regulatory Authority of India (TRAI) are working out the legal framework for implementing these objectives.

Other policy developments include:

- 2 G spectrum auction will take place in December 2012. The base price has been fixed at Rs. 140 bn for a license of 5 MHz of pan-India spectrum.
- The government has also proposed a one-time license fee to be charged to mobile service providers holding GSM spectrum more than 4.4 Mhz and CDMA spectrum more than 2.5 Mhz. The fee is expected to be levied only on the additional spectrum and the amount is expected to be in line with the base price at the 2 G spectrum auction. This proposal has not been finalized.
- The government is trying to hold 4G spectrum auction by end of this year.

Company fundamentals

Migration towards GSM services in a highly competitive market

The company continued to migrate from CDMA to GSM services, and as a result, the CDMA subscriber base fell by 88% from 241,798 to 27,768. The GSM subscriber base increased by 7.6% to 1.32 mn. (the decrease in the number of CDMA subscribers – 214030 was more than the increase in the number of GSM subscribers 93732 and on the whole, the company lost subscribers). The Punjab circle is highly competitive, with seven other operators offering services including well-established operators like Airtel, Vodafone, Idea, Tata Docomo, Reliance apart from BSNL and Aircel.

The company has four revenue streams:

Earnings from broadband services to be hit by license fee imposed by DoT

- **Mobile telephony services:** Revenue from mobile telephony services increased 15.6% to Rs. 1704 mn.
- **Interconnection usage charge fees:** These are charged to other service providers for transferring a call to the company's network. Revenues from this stream increased 49.5% to Rs. 161.3 mn.
- **Infrastructure services:** This includes setting up and managing wireless and wired infrastructure, for corporate users. Revenue from infrastructure services increased by 6% to Rs. 48.8 mn.
- **Internet services:** Revenues from internet services increased by 22.7% to Rs. 898 mn.

During FY12, the company did not pay any license fee for providing internet services. Beginning July 2012, the DoT has imposed a license fee on all internet service providers – this will be computed as 4% of adjusted gross revenues (AGR). From FY14, onwards, this rate will be revised to 8% of AGR. This will impact the earnings of the company going forward.

Key financial indicators

The company's total income increased 18.7% to Rs. 2828 mn, driven by a 22.6% increase in revenue from internet services. The company's EBIDTA was minus Rs. 308.7 mn, an improvement over last year's EBIDTA of minus Rs. 727.8 mn. This was due to a reduction in marketing expenses from Rs. 402 mn to Rs. 203 mn. The company's PAT was minus Rs. 1791 mn this year as compared to last year's figure of minus Rs. 2236 mn. The company's debt this year remained at Rs. 6042.6 mn, and the net worth was negative at minus Rs. 6889 mn.

Quarterly results

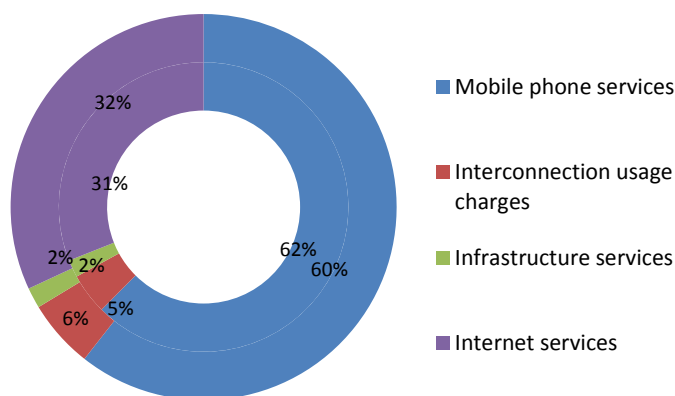
Particulars (Rs in mn)	Apr '12 to Jun '12	Apr '11 to Jun '11	% Change ¹	Jan '12 to Mar '12	% Change ²
Total income	796.9	713.3	12%	739.7	8%
Total expenditure	874.2	834.9	5%	733.1	19%
EBIDTA	(77.3)	(121.6)	-	6.6	-
PAT	(452.3)	(486.8)	-	(374.7)	-
EPS	(0.7)	(0.8)	-	(0.6)	-

¹ compared to corresponding quarter in the previous year

² sequential comparison

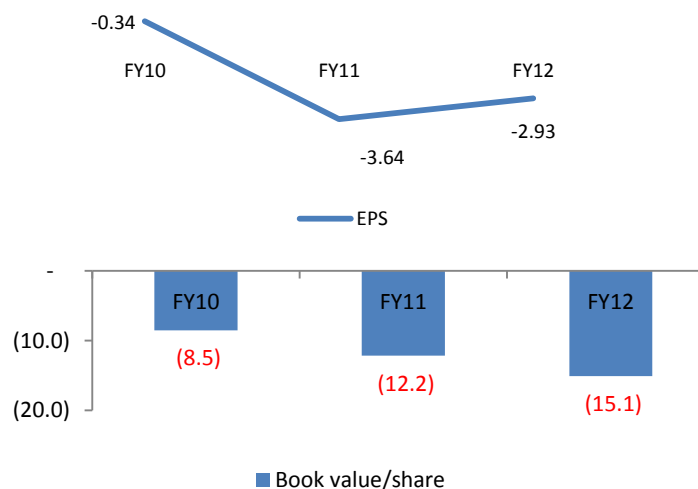
Ratios

Segment-wise contribution to total revenue

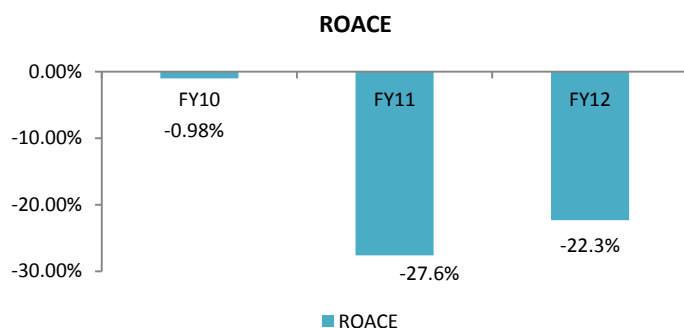


Inner ring represents FY11 data: total revenue was Rs. 2360.5 mn
Outer ring represents FY12 data: total revenue was Rs. 2813.0 mn

Key ratios

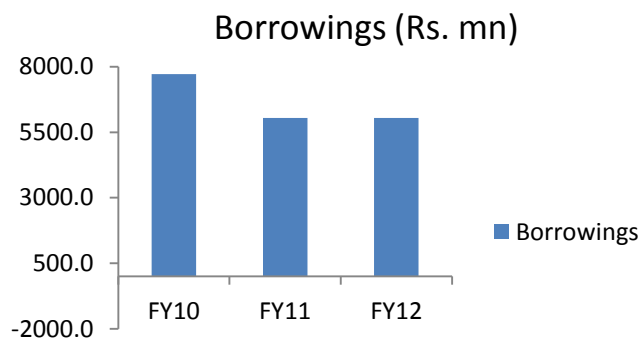


Profitability ratios



Return on net worth is not meaningful because the company's net worth has been negative since FY07

Borrowings



Debt/equity is not meaningful because the company's net worth has been negative since FY07.

Debt was 545 times EBIDTA in FY10. EBIDTA has been negative in subsequent years.

Financials

P&L (Rs. mn)	FY10	FY11	FY12
Total income	1978.2	2383.4	2828.9
EBIDTA	14.1	(727.8)	(308.7)
EBITDA Margin%	0.7%	negative	negative
Depreciation	799.8	1230.2	1201.7
EBIT	(785.6)	(1958.0)	(1510.4)
Interest	(704.2) ^[1]	278.7	281.2
PBT	(56.1)	(2236.7)	(1791.6)
Tax	nil	nil	nil
PAT	(56.1)	(2236.7)	(1791.6)
PAT Margin %	negative	negative	negative

^[1] Pursuant to the corporate debt restructuring scheme in FY10, the company's lenders were given equity shares and provision for interest worth Rs. 704.2 mn was reversed.

Valuation ratios	FY10	FY11	FY12
P/E	negative	negative	negative
P/BV	negative	negative	negative

Balance Sheet (Rs. mn)	FY10	FY11	FY12
Share Capital	6772.6	8371.1	8371.1
Reserves & Surplus	(11331.8)	(13568.4)	(15360.0)
Net worth	(4559.2)	(5197.4)	(6989.0)
Borrowings	7722.1	6044.1	6042.6
Current Liabilities & Provisions	4628.2	7554.9	8616.8
Total liabilities	7791.1	8401.6	7670.3
Net fixed assets	3736.1	4912.7	4544.8
Capital work in progress and intangibles	3399.6	2520.1	2059.5
Non-current investments	0.1	0.1	0.1
Current Assets	655.1	883.0	940.1
Other non-current assets	0.1	85.8	125.8
Total assets	7791.1	8401.6	7670.3

Cash Flow (Rs.mn)	FY10	FY11	FY12
PBT	-56.1	-2236.7	-1791.6
CF from Operations	447.5	2854.2	397.4
CF from Investments	-134.7	-2490.1	-308.0
CF from Financing	-301.9	-361.4	-90.7
Inc/(dec) in Cash	10.8	2.7	-1.3
Closing Balance	63.4	66.1	64.8

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