

# Vodafone-Idea Merger: Ideating for Consolidation

## *Abstract*

Vodafone India and Idea has announced that they are merging together as a new entity. The announcement could lead to havoc in the market as Airtel which was on saddle and guarding the telecom market of India, will now play second fiddle to new-founded venture, thus paving way for radical changes in the structure of debt-ridden Indian Telecom Industry. The merger of two telecom giants is likely to unleash inundation of consolidation bids by other existing market players which are now eyeing on operational efficacy and profit enhancement by taking the leverage of integration. However experts believe that owing to the merger of the companies, operational integration and redundancy of manpower at same locations would put jobs at risk

## **Introduction**

On Monday i.e. March 20, 2017, Telecom Industry of India was taken by surprise as two major players Vodafone and Idea announced merger – which was all set to change the market dynamics and structure and subsequently to fashion nightmares to other players of the Telecom Industry - which has witnessed a massive growth since the advent of the new telecom policy in 1998.

The announcement of the merger which would continue in the form of integration till 2019, has not been made on the whims and fancies of the promoters of the merging companies, but is the offspring of concerted and deliberated moves and moots staged in the fag-end of the December, 2017

The industry which has been dubbed by telecom pundits as treasure-trove of revenue-unexplored, has amassed combined revenue of \$34 billion, total debt of Rs 4 Lakh Crores amidst cut-throat competition among 8 national level players. The average quarterly smartphone sales touches around 25 million units, the total subscriber base is around 1.189 billion.

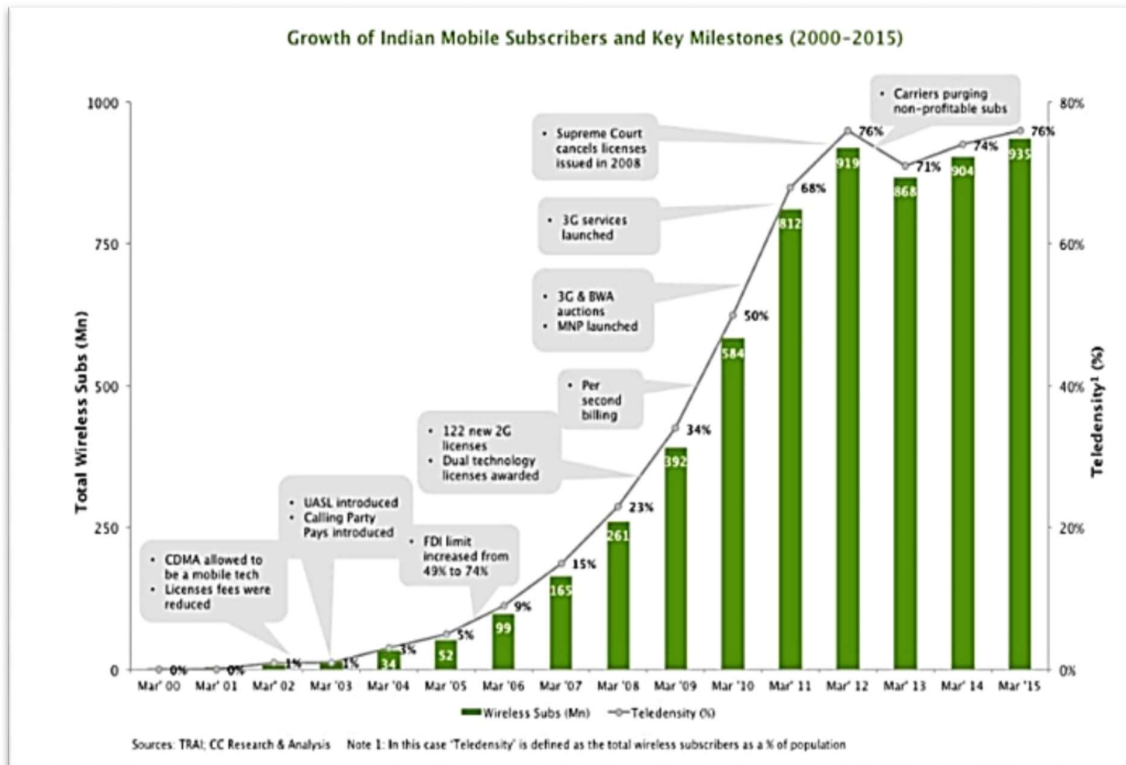
After producing a massive growth with a remarkable CAGR 117%, the industry has already started showing sign of consolidation, toeing the same line, recently Vodafone India had announced its merger with Idea Cellular with a combined subscriber base of 394 million, and a combined revenue of Rs 80,000 crore. This series of consolidation moves are having widespread repercussion on the market structure and market concentration which is duly linked to kind of pricing and its impact on competition. All companies in the industry are studying the implication of consolidation and how it is going to affect their operations. Which are already under tremendous pressure to maintain its EBIDTA margin. All major stakeholders are having their own perspective

on this consolidation .TRAI is examining its impact on tariff if any and Competition commission of India is examining the effect on market Structure and price.

### **Telecom Industry Overview**

The saga of Telecom Industry is by and large epitomized by the state controlled service operator –Department of Telecom until 2000 when market was regulated and department was corporatized as Bharat Sanchar Nigam Limited 15 September 2000 .

From miniscule 5 million subscriber base in 1999, India rushed to 227 million in subscriber base by the end of 2007 at the sideline of trigger created by reform policy of the government which facilitated private telecom operators to enter the market. However Transition from monopolistic market to competitive market led to need of regulatory body which was established and christened as Telecom regulatory Authority of India through TRAI Act. The Act envisaged not only the smooth telecom services and non-discrepant tariffs in India, but also mooted a regulated Telecom Policy regime In India. Bolstered by new Telecom regime and policy , new players like reliance communication , Idea , Vodafone , Tata teleservices entered the cellular service mobile market which unleashed cut-throat competition and intense rivalry among players. In 2003, on an average 1.5 million new subscribers were added to the existing consumer base. This has since increased to approximately 7 million per month in 2007. After the coming up of new operators the mobile tariff has reduced drastically. Coming to recent times India's smartphone penetration stood at 24% of total connections in 2015.



The average handset price for smartphones has been declining, with an entry-level 4G smartphone available for INR2,999. Prices are expected to further reduce helping drive data usage. The average data consumption has increased from 338MB/month in 2011 to 753 MB/month in 2015. Today India is the fastest growing telecom market. The technology evolution has been drastic starting from 2G services in 94-95, 3G services in 2010 and 4G by early 2016, India has witnessed a tremendous growth in terms of technological revolution the life cycle of technology has reduced drastically, which means operator has to be very alert in updating its existing technology anytime.

According to a report by leading research firm Market Research Store, the Indian telecommunication services market will likely grow by 10.3 per cent year-on-year to reach US\$ 103.9 billion by 2020. Further Ericsson Mobility Report India reckons that smartphone subscriptions in India would increase four-fold to 810 million users by 2021, It also expect smartphone traffic to grow seventeen-fold to 4.2 Exabytes (EB) per month by 2021.

**Current mobile operators**

Operator	Share
Vodafone	18.72
idea	17.17
Airtel	24.32
Jio	10.98
BSNL	8.8

Aircel	8.38
reliance communication	7.99
tata DoCoMo	5.17

## **Mergers in Indian Telecom Industry**

### **Idea acquires 80 % stakes in Spice**

Aditya Birla group's Idea Cellular bought BK Modi's Spice Communications for over Rs 2,700 crore and now the former owns more than 80 per cent equity in the latter which is now a subsidiary of the Mumbai-based telecom operator. Idea Cellular acquired the company from Modi Wellvest and Telekom Malaysia (TMI, now Axiata) in July 2008.

### **Telenor buys Unitech Wireless**

Telenor, a Norway-based international telecommunication service provider bought 49 per cent stake in Unitech Wireless the telecom arm of the realty firm, Unitech, in two tranches for Rs 2,380 crore. However the company had raised its stake to over 60 per cent, but like Etisalat, saw its joint venture's licenses cancelled by the Supreme Court in 2012. It has however stayed put in the Indian market, bought back licenses in some circles, took control of the joint venture after Unitech exited it. Telenor now owns 100 per cent of its Indian unit. The company had rebranded itself to Telenor India from Uninor.

### **Reliance Industries – Infotel merger**

Mukesh Ambani owned Reliance Industries bought 95 per cent stake in Infotel Broadband for Rs. 4,800 crore in June 2010. The company has already shaken the market by announcing its 4G plan. It is also offering cost-free unlimited voice call, and data offer to its users. The offer will end on 31st March and after that Jio will charge for data and voice calls. It has already introduced its entry-level Rs 149 plan for free data and voice calls which will come into power from 1st April 2017.

### **Reliance Communications – Aircel merger**

In the biggest consolidation deal in the telecom sector, Reliance Communications Ltd led by Anil Dhirubhai Ambani has announced its plan to merge with Aircel. If the merger comes through then the new entity will create a telecom operator ranked fourth by customer base and revenues and number three operator by revenues in 12 important circles. RCom and Maxis Communications Berhad (MCB) of Malaysia, which owns Aircel, will hold 50 per cent each in. The merged company will be one of India's largest private sector companies, with an asset base of over Rs 65,000 crore and net worth of Rs 35,000 crore (\$5.2 billion).

Source: <http://www.gizbot.com/telecom/news/top-mergers-acquisitions-indian-telecom-sector/articlecontent-pf70707-038300.html>

## **Vini, Vidi, Vinci: Reliance Jio**

The entry of Reliance Jio in the market in late 2016 drastically changed the hues and harmony of competition with its data service pricing as low as Rs. 51/GB data, and free voice call. Reliance's hunt for the market share, has opened new front of market warfare with competition soaring to new heights. Company offers huge benefits to its customers with unbelievably low prices and unlimited 4G data for 3 months on trial basis. Such unpatrolled moves forced other operators to reduced their 3G/4G data rates by up to 80 percent. Since the tariff has reduced due to entry of new player in the market, the existing players are finding it difficult to reach profit. Bharti Airtel Ltd has reported gloomy results, with revenues and operating profit declining by 5.3% and 9.5%, respectively, on a quarter-on-quarter basis in 2016-17. Free cash flow stood at Rs1.5 crore last quarter, down from Rs3,547 crore in the September quarter and Rs3,953 crore (ex-dividend receipts) in the June quarter. As per JM Financial Institutional Securities Ltd point out, Idea Cellular's debt levels have reached alarming proportions. "Given the recent auction spend (Rs12,800 crore) and near-term EBITDA collapse, Idea's financial leverage is set to touch alarming levels—net debt to cross Rs55,000 crore by Mar 2017.

## **Vodafone-Idea merger**

As Reliance Jio entered the Indian telecom market with bang, script of Merger story started being scribbled on the canvas of telecom industry. In a rollercoaster ride for all the major players, Reliance Jio armed and backed by **Reliance** Industries Limited (RIL),- a Fortune Global 500 company and India's second-most valuable company by market value -unleashed slew of freebies offers which transformed market from oligopolistic to hyper competitive, and almost strangled the survival for other companies. As of now, it seems that a complete merger would crown merged entity of Vodafone -Idea (Which are presently holding No.2 and No .3 position in the market respectively) on top of the telecom market and thus dethrone Bharti Airtel from the saddle. The combined subscriber base of the merged entity would be around 39 crore, which is significantly higher than Airtel's 27 crore and Jio's present status of 7.2 crore. It would have a revenue market share of nearly 40 per cent compared with Airtel's near-32 per cent.

## **Vodafone-Idea Merger Aftermath**

As the current price war is already getting tougher day by day, the merger will not only add fuel to the already alarming situation but is also likely to unbridle "consolidation spree". Rival companies like Reliance Communications, Tata Teleservices and Aircel are already in talks for merger. Airtel has bought India

operations of Telenor.(ET) . However there is also growing fear of consolidation converting into unholy cartelization which may invite the intervention of regulatory bodies like TRAI and CCI . The Telecom regulatory authority of India has come into force after the enactment of TRAI Act which posits its *main objectives as to provide a fair and transparent environment that promotes a level playing field and facilitates fair competition in the market.* TRAI regularly issues orders and directions on various subjects such as tariffs, interconnections, quality of service, Direct To Home (DTH) services and mobile number portability. As of now TRAI smelt no rat and has maintained Vodafone- Idea merger as a business issue and its interjections would be subject to arousal of any regulatory issue, if any.

Another regulator Competition Commission of India (CCI)- an apex body which looks after competition issues like Anti-competitive agreement , abuse of Dominant Position, has categorically cleared the merger on the ground that the merger is not creating competition concerns as the market is highly hyper competitive and tariff structure plummeting to extremely low level which rejects the probability of any kind of abuse of dominance issues.

### Share structure: pre- merger and post- merger

Pre-Merger		Post-Merger	
Operator	Share	Operator	Share
Vodafone	18.72	Vodafone +idea	35.89
Idea	17.17	Airtel	24.32
Airtel	24.32	Jio	10.98
Jio	10.98	BSNL	8.8
BSNL	8.8	Aircel	8.38
Aircel	8.38	Reliance communication	7.99
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(source : TRAI. 2016.)

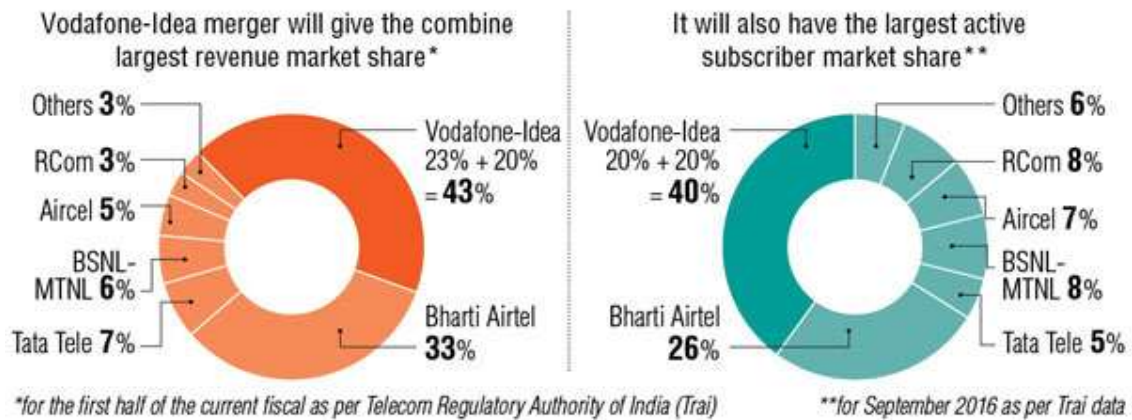
### What next

With new-found scenario, Indian Telecom Industry stands on the crossroad decked with imminent Consolidation Spree.“ What is happening in the Indian telecom market is what you should expect given the cost and revenue structure of the industry: very high upfront fixed costs combined with very low marginal cost of voice and data transmission and a market that is very price sensitive”, feels an expert at John Hopkins University . This implies that by merging, telecom companies can scale their services faster and combine staff and operations to reduce costs, giving them the wherewithal to offer lower prices on its services. However unfettered merger and acquisition bids could

also stir hornet's nest of monopolistic cartels making life of small players and even subscribers miserable. Pandemonium and prospects exuded by consolidation galore keep pundits and practitioners quizzing over what future of debt-ridden Indian telecom industry has stored in its womb.

### Exhibits-1

#### CREATING THE NO.1 PLAYER



### Exhibit-2

### Debt + Free Calls = Consolidation?

India's 11 carriers have more than \$62 billion of debt

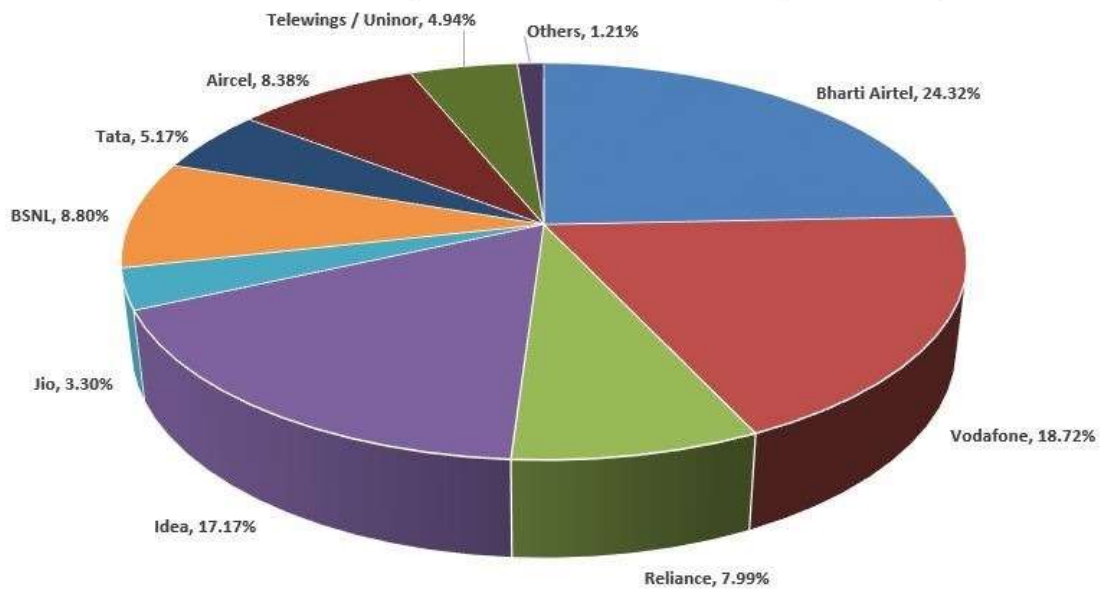
	Market Share (Percentage)	Debt (Billions of Rupees)
Airtel	24.32	974
Vodafone	18.72	354
Idea	17.17	364
BSNL	8.8	79
Aircel	8.38	121
Reliance Comm.	7.99	427
Tata Tele	5.17	303
Telenor	4.94	18
Reliance Jio	3.3	490
Sistema	0.6	34
MTNL	0.34	181.4

Source: Market share data from TRAI Oct. 2016 report; Debt from company filings

Bloomberg

### Exhibit-3

Indian Telecom Operator's Market Share ( Oct 2016)

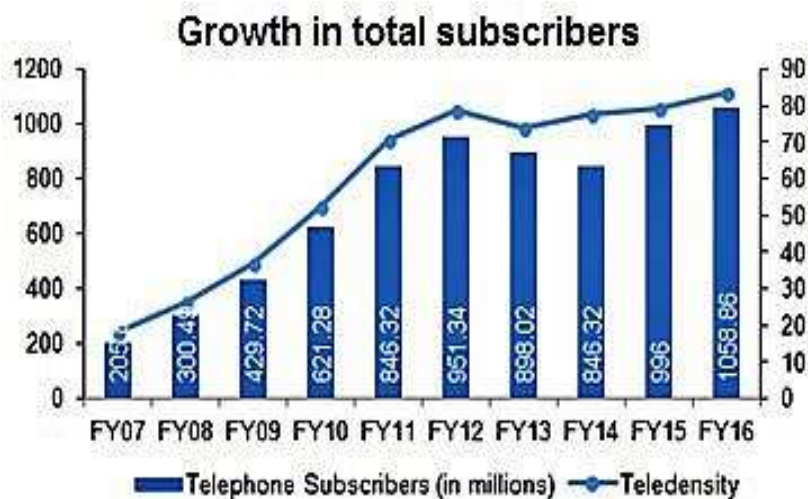


### Exhibits-4



Group Company wise % market share (Subscribers) - December 2016					
Sl. No.	Name of Company	Total Sub Figures	Additions in December 2016	% Market Share	% Growth over previous month
1	<u>Bharti Airtel</u>	26,58,52,605	25,02,355	32.82%	0.95%
2	Vodafone	20,46,86,924	18,95,229	25.27%	0.93%
3	Idea	19,05,17,876	28,39,426	23.52%	1.51%
4	<u>Aircel</u>	9,08,75,553	2,29,356	11.22%	0.25%
5	<u>Telenor</u>	5,44,69,499	7,18,049	6.72%	1.34%
6	MTNL	35,90,443	0	0.44%	0.00%
	All India	80,99,92,900	81,84,415		

### Exhibits-5



Source: Telecom Regulatory Authority of India, TechSci Research  
 Notes: CAGR - Compound Annual Growth Rate