With a robust, upgraded mobile network in place, Reliance Communications (RCOM) rolled out its 3G services in December 2010. It was only the second private telecom operator to do so. The other was TATA DOCOMO. To make good its investment of Rs 85.85 billion for 3G licences in 13 circles, including Delhi and Mumbai, RCOM first introduced the service in Delhi, Mumbai, Kolkata and Chandigarh. On offer was a base speed of 21 Mbps, which allowed video calling, mobile TV, video streaming and other applications on a variety of mobile and personal computing devices.

This time, RCOM did not play its usual tariff card. Offering competitive tariffs, it focused mainly on improving the user experience in the hope of attracting subscribers eventually to more data-intensive plans that would be remunerative for the operator. RCOM believes that data content, innovation and network clarity will help increase ARPUs, which plain voice services are no longer able to shore up.

“With the rollout of 3G services, non-voice revenues for the industry should increase from the current 12-13 per cent to over 30 per cent in the years to come. We should be at that level,” stated Syed Safawi, chief executive officer of RCOM’s wireless business, at a media briefing.

For now, RCOM is busy rolling out services in the other circles it has 3G licences for. In April 2011, it became the first operator to launch 3G services in 24 locations in the Northeast. According to company officials, nearly Rs 5 billion has been invested to improve the quality of the network in this region.

“3G is the next stage in the evolution of GSM. With 3G handset penetration being upward of 20 per cent in Mumbai and Delhi currently, we are expecting all 3G handset owners to migrate to the 3G network. This goes hand in hand with our vision to launch the second telecom revolution in India and takes us closer to the vision of a wire-free nation,” Safawi noted.

Making a success of 3G is important for RCOM, as it is for all other service providers who have invested heavily in procuring 3G spectrum. With margins under severe pressure in this intensely competitive sector, RCOM’s focus on 3G and high speed internet makes sense to enable it to derive as much profit as it can from the spectrum it has.

Rough patch

Operational focus is also what the company needs at this point. RCOM, the flagship company of Anil Ambani's conglomerate, has been going through particularly rough weather of late.

In June 2010, for instance, it had announced a deal wherein its tower business was to be merged with GTL Infrastructure to create the world's largest independent telecom tower company with an enterprise value of Rs 500 billion and 80,000 towers. However, after several rounds of negotiation, the talks floundered and the deal had to be called off.

Thereafter, all RCOM's efforts, including talks with the Emirates Telecommunications Corporation to sell 26 per cent stake in Reliance Infratel (its tower business) to cut its bruising debt load, hit the buffers. In November 2010, HSBC downgraded RCOM to "underweight" from "neutral" as it believed that it would be increasingly difficult for RCOM to monetise its tower assets.

At the close of the year, the company found itself in the thick of controversy over its role in the 2G spectrum scam. The report of the Comptroller and Auditor General (CAG), which resulted in the resignation of then minister for communications A. Raja, also stated that Reliance Telecom was an initial shareholder in Swan Telecom, which was awarded licences in 13 circles in 2008. Reliance reportedly held 9.81 per cent equity (10.79 million shares) in Swan. This cross-holding indiscretion made Swan ineligible for a 2G licence; however, the company's application was not disqualified. In fact, it was allowed to resubmit its form in December 2007 with appropriate revisions in the shareholding pattern. Pointing to these anomalies, the CAG report termed Swan Telecom a "front company" of Reliance Telecom and doubted the latter's "intention".

RCOM has refuted any involvement in the 2G spectrum scam. According to a company statement, Reliance Telecom, RCOM or any Reliance ADA Group (R-ADAG) individual or affiliate never held a single share in Swan Telecom at the time of the grant of the 2G licence in January 2008 or at any time thereafter.

However, the controversy continues to rage with several RCOM officials undergoing CBI interrogation. The CBI has asked for a probe into the company's operations from 2001 to 2007 as directed by the Supreme Court. Two preliminary enquiries have been registered by the CBI on the issue of dual spectrum allocation and on RCOM (and other telecom companies) pledging spectrum licences for bank loans. The outcome of these investigations will be known as the year advances.

Taking stock

Controversies notwithstanding, RCOM remains the second largest telecom operator in the country with 135.71 million subscribers as of March 2011. It trails only Bharti airtel, which has 162.2 million subscribers. RCOM joined the 100 million mobile subscriber club (after Bharti airtel) in March 2010 to become the world's fourth largest, single-country mobile service operator. In the same month, it launched the largest and most aggressive broadband internet service under the brand name Reliance Netconnect Broadband Plus. Thereafter, it focused entirely on rolling out 3G services.

Leveraging the economic wisdom that costs can determine the sway of the market, RCOM trailblazed its way into the sector in 2003 with its game-changing Monsoon Hungama offer. It offered a phone and a connection for as little as Rs 500. This kicked off an industry trend in tariff undercutting, leading eventually to some of the lowest telecom tariffs in the world.

Today, RCOM delivers a full range of telecom services, including mobile and fixed line telephony, national and international long distance services, broadband and data services as well as a basket of value-added services (VAS) and applications. It has been valued as one of the world's top 10 telecom companies. It has a corporate clientele of 2,100 Indian and multinational companies, apart from 800 global carriers that use its network.

The company has, over the years, invested significantly in infrastructure rollout, which it intends to leverage in the future for bigger gains. RCOM currently owns and operates one of the world's largest next-generation IP-enabled connectivity infrastructures, with 200,000 km of optic fibre cable systems covering India, the US, Europe, the Middle East and the Asia Pacific.

Originally a CDMA operator, RCOM, in 2009, launched GSM services across the country. The network rollout was the largest and possibly the quickest initiative undertaken by any company till then. It was completed six months ahead of schedule and was true to RCOM's low-price-point strategy, backed by strong marketing initiatives.

Funding issues

While RCOM's network buildout efforts paid off, bringing in users in millions, it also consequently imposed a huge debt burden on the company. In fact, paying off the heavy debt is RCOM's biggest challenge today. The company's GSM business involved an investment of over $2 billion. On top of that, it spent $1.9 billion on 3G spectrum in 2010. The heavy capex resulted in net debt, which mounted from Rs 189 billion in end-2009 to Rs 324 billion by end-2010. Though the financial results for 2010-11 and the quarter ended March 2011 are yet to be declared, net profits are expected to continue to slide.

"The company's debt-equity ratio has reached an alarming level," observes Sridhar Pai, chief executive officer, Tonse Telecom. The company needs funds to reduce its debt and expand its operations. Company officials are evaluating various fund-raising options including selling off 26 per cent stake in RCOM, Reliance Infratel and Reliance Globalcom (its global business subsidiary).

RCOM is also tightening its spending. Its capital expenditure for 2010-11 and the next two years will be contained at about Rs 30 billion, which is significantly lower than the Rs 350 billion it spent in the past three financial years.

Meanwhile, it got a bit of a breather in March 2011, when it signed a $1.93 billion 10-year syndicated loan agreement with the China Development Bank (CDB). According to company officials, this will translate into an annual interest cost saving of over Rs 5 billion. The loan would be fully underwritten by the CDB and funded by a syndicate of Chinese banks and financial institutions including the CDB, RCOM noted in a media statement. The drawdown of the loan would go towards paying the mobile spectrum fees and buying telecom equipment.

Further, RCOM has redeemed all its outstanding foreign currency convertible bonds (FCCBs) worth Rs 22.5 billion, which were due for conversion in May 2011. The FCCBs, which were issued in May 2006, have been redeemed at a premium of 25.84 per cent, and the payments made on the due date for the bonds. If the FCCBs had come into conversion, the company would have had to allot 27,413,085 equity shares of Rs 5 each. Analysts say this has been a good move by the company as there will be few chances of conversion at the current share price. In May 2006, the average share price of the company was around Rs 310 per share; however, on May 10, 2011, the price was down to Rs 90.60.

Analyst view

The company's financial problems are temporary, believe most industry observers. "RCOM has deep pockets and is a strong player with a very unorthodox style of functioning. It regularly cuts corners to reduce operational expenses," notes Dr Mahesh Uppal, director, ComFirst.

RCOM's edge is in its nationwide presence. "It has built one of the most extensive and comprehensive networks in the country, including both active and passive infrastructure. It has been able to put together not only the core network but also enabling infrastructure, which includes passive infrastructure as well as a metro Ethernet and ITZ6 backbone. The company has around 200,000 buildings connected with optic fibre, which is more than any other operator. It is one of the few operators in the country with a global vision. RCOM is reaping the benefits of building the most equipped and largest backbone and access network in India," notes Pai.

An astute operator with a go-to-market confidence, RCOM as a brand has stayed relevant by innovating and keeping the buzz alive. However, the aggression and the ambitions are on the back burner these days. The 2G spectrum issue and the company's alleged involvement in it has had an adverse effect on its image. This is evident in the hit the company's share prices have taken, a cause of serious concern for RCOM. "As long as the perception that the company is involved in irregular activities remains, it will impact its standing in the industry. The effect of this on users will be less immediate, but will be far more serious on the share market and can impact future funding for the company," says Uppal.

Customer service is another issue. "In terms of sales, there is a huge push and we see a lot of aggressive marketing and in-your-face branding. But when it comes to after-sales support, the company is hugely lacking. Moreover, its recovery cell often bothers long-term subscribers with regard to billing dues," says Pai.

"Also, the company has adopted some wrong strategies. It has, for example, shifted its focus from Wi-Max to LTE. It should not have invested in Telsima as its top equipment vendor. An operator should never invest in a technology company," adds Pai.

On the 3G front, RCOM has an edge as it has a presence in both the GSM and CDMA markets. Analysts believe that this is a plus against rival GSM players as it can offer both data cards and dongles. However, RCOM does not have a very high proportion of lucrative customers, which could adversely affect the uptake of its 3G services. The company entered the market late and targeted the low-income segment. It managed to garner a huge subscriber base but ARPUs remained low with the brand positioned as a low-segment product. In offering 3G particularly, "RCOM will have to differentiate its voice services from data services and try to get better quality and higher paying subscribers," Uppal observes.

Currently, RCOM is facing competition on both the 3G and 2G fronts. Unless some rapid remedies are put in place with respect to revenues, the going can get tough.

Recent initiatives and the way forward

Going forward, RCOM's 3G strategy and the extent to which the company will leverage its existing network will play an important role. RCOM claims that its 3G network is connected to an IP backhaul in order to provide maximum download speeds and minimum latency. The operator intends to play on this and get high-ARPU subscribers.

In order to make the service popular, soon after rolling out 3G services, RCOM launched a new mobile data portal, R World, powered by Motricity, a mobile data service and solution provider. The R World platform enables features like content aggregation, single sign-on, news feeds and social networking capabilities.

To deliver rich content to its subscribers, RCOM has also entered into several alliances. It has partnered with Ericsson and Facebook for 3G applications, with Nokia for Ovi Life Tools, with Universal Music for international and local music content, and with Apalya for mobile TV.

In an attempt to do away with its less lucrative businesses, RCOM decided to exit from its PCO and fixed wireless phone business in February 2011. The decision came in view of the low margins and inefficient utilisation of precious spectrum. The resources that have been freed in the process will be assigned to more profitable areas such as data and VAS enhancement. As a part of its VAS initiative, the operator has launched mobile banking services in association with the State Bank of India (SBI). Its mobile banking services include such services as balance enquiry, mini statement, funds transfer and cheque book issuance. Subscribers do not need GPRS or internet access to avail of these services; they do, however, need to have an active current or savings account with SBI.

In another innovative step, RCOM is offering special UMTS SIM cards for security m-commerce transactions, which is the second most popular 3G application after music downloads.

On the rural telephony front, RCOM, in March 2011, launched a rural VAS initiative called Behtar Zindagi in partnership with Handygo Technologies, a VAS solution provider. The service is focused on rural subscriber needs and provides day-to-day information on health, education, finance, weather, mandi rates, livestock, agriculture, fisheries, etc. The service is available for Rs 30 for 30 days.

In January 2011, the operator launched a JVcompany, Kribhco Reliance Kisan Limited (KRSL), in partnership with cooperative society Kribhco. The JV's main focus will be to catalyse teledensity growth and offer state-of-the-art telecom products and services to rural subscribers. KRSL will create a distribution model to cover 72 per cent of the rural population through its network of over 25,000 cooperatives, 6,300 member cooperatives and 60 Krishi Seva Kendras spread across the country.

Going forward, the operator's thrust areas will be data services and entertainment through the mobile platform as it has a significant presence in the entertainment market.

In all, RCOM clearly comes through as a smart operator. It is going through a rough patch but, as Uppal says, "It is a long-term player and despite the scam setback, it will emerge from the ashes because the company knows how important the telecom sector is for the group. I do not see it exiting in the near future."