ICRA

April 07, 2017

Reliance Communications Limited

Instruments*	Amount Rated (Rs. crore)	Rating Action
Non-Convertible Debenture (NCD) Programme	5,000	Downgraded to [ICRA]BBB; removed from watch and negative outlook assigned
Long-term Fund-based/Non-fund Based Limits	28,116	Downgraded to [ICRA]BBB; removed from watch and negative outlook assigned
Short-term Fund based/Non-fund Based Limits	7,314	Downgraded to [ICRA]A3+; removed from watch
Commercial Paper (CP) Programme	2,000	Downgraded to [ICRA]A3+; removed from watch

**Instrument details are provided in Annexure-1*

Rating Action

ICRA has downgraded the long-term rating to [ICRA]BBB (pronounced as ICRA triple B) from [ICRA]BBB+ (pronounced as ICRA triple B plus) for the Rs. 5,000 crore[1] Non-Convertible Debenture (NCD) Programme and the Rs. 28,116 crore Long-Term Fund Based/Non-Fund Based Limits (including unallocated limits) of Reliance Communications Limited (RCom)[†]. ICRA has also assigned Negative outlook to the long term rating. ICRA has also downgraded the short-term rating to [ICRA]A3+ (pronounced as ICRA A three plus) from [ICRA]A2+ (pronounced as ICRA A two plus) for the Rs. 7,314 crore Short-term Fund-based/Non-fund Based Limits (including unallocated limits) and the Rs. 2,000 crore Commercial Paper Programme of RCom. The ratings have been removed from rating watch.

ICRA has taken a consolidated view of the RCom Group (referred to as “the Group”) including Reliance Telecom Limited (RTL) and Reliance Infratel Limited (RITL).

Rationale

The revision in the Group’s ratings takes into consideration steady decline in its revenues and profitability over last few quarters. During Q3FY2017 company has reported 10% y-o-y and 4% q-o-q decline in its revenues and 38% y-o-y and 22% q-o-q decline in its Earnings before Interest Tax and Depreciation (EBITDA), resulting into net loss for the Group. The company has also reported decline in its Rate per Minute (RPM) to Rs. 0.40 in Q3FY2017 from Rs. 0.45 in Q2FY2017. For 9MFY17, the revenues declined by 6% yoy and EBITDA declined by 24%, translating into EBITDA margin compression from 34.4% to 27.9%. The pressures on revenue generation and profitability emanate from increased competitive intensity and pricing pressures in the industry especially following the launch of services by Reliance Jio Infocomm Limited (RJio); the ban on use of specified bank notes in November 2016 (demonetisation) and shutdown of Code Division Multiple Access (CDMA) operations by the Group. Further the Group’s capital structure continues to remain stretched. The Group’s debt, stood elevated at Rs. 44,586 crore as on December 31, 2016, impacted by the depreciation in the Indian rupee, given that around 50% of the loans are foreign currency denominated; and addition of spectrum related payouts. In

[1] 1 crore = 100 lakhs = 10 million
[†] For complete rating scale and definitions, please refer to ICRA's Website www.icra.in or other ICRA Rating Publications

the past the Group has been refinancing its debt maturities and continues to remain exposed to refinancing risks, given the sizeable repayments in the near to medium term. High debt coupled with decline in profitability has resulted in deterioration in its debt coverage metrics with its Gross Debt/EBITDA weakening to 7.76 times (annualised) as on 9MFY2017 end from 6.68 times as on FY2016 end.

The Group is undertaking three transactions – a) to merge Sistema Shyam TeleServices Limited's (SSTL) India wireless business with itself, b) to merge its wireless operations with that of Aircel Limited (Aircel) which is expected to give scale and synergy benefits and c) to offload its tower business to Brookfield Infrastructure group. Both (b) and (c) transactions entail transfer/reduction of debt along with concomitant transfer of revenue and EBITDA. For these transactions, the Group is in the process of obtaining necessary approvals, of which it has already received some approvals. ICRA has taken note of the investigations into acquisition of Aircel by Maxis Communications Berhad (MCB) in 2006, wherein the honourable Supreme Court of India (SC) is hearing petitions filed by certain quarters, and also the fact that the underlying proceedings brought against the shareholder of Aircel was dismissed by the special 2G Court on February 2, 2017.

On consummation of these transactions, the residual entity will be left with lower quantum of debt. However, the debt coverage metrics of the residual entity are expected to remain subdued based on expected cash generation in the residual entity. In addition the timely execution of company's plan to monetise real estate assets at expected valuations would be critical to achieve its deleveraging target.

Nevertheless, the ratings continue to factor in the Group's sizeable spectrum holding across bands, spectrum-sharing arrangement with RJio, the Group's established position as an integrated service provider with its presence spanning wireless services, wire-line services, enterprise connectivity solutions, domestic and international long distance segments, and direct-to-home (DTH) pay television services; the operational strengths it derives from its pan-India network; and its healthy telecom customer base (87.7 million subscribers as on end-December 2016).

The negative outlook is on account of likely continued pressures on the Group's performance and uncertainty on the debt servicing ability of the residual entity should the proposed transactions conclude. The industry pricing pressures are not expected to reduce in the near term and these remain heightened for RCom Group given its moderate market positioning (Revenue Market Share of 2.8% for Q3FY2017 which has reduced from 4.3% in Q3FY2016). ICRA will closely monitor the ongoing developments and the Group's initiatives to improve its operational performance and will take further rating action accordingly.

Key rating drivers

Credit Strengths

- Healthy telecom subscriber base (87.7 million as on December 31, 2016) and pan-India telecom operations.
- Healthy spectrum holding with sizeable spectrum in 800 MHz band which is best suited to provide high speed 4G data services.
- The non voice revenue continues to show steady growth. The proportion of non voice revenue to total telecom revenue improved to 39% in Q3FY2017 from 36% in Q2FY2017.
- Moderate capital expenditure plans going forward given the infrastructure sharing arrangement with Reliance Jio Infocomm Limited (RJio).
- No major spectrum expiry in the near to medium term. Limited regulatory payouts as compared to those to be incurred by its competitors

Credit Weakness

- Persisting high debt levels; the debt protection metrics have further deteriorated with increase in debt and weakening of its profitability. Its Debt/EBITDA has increased to 7.76 times (annualised) as on 9MFY2017 end from 6.68 times as on FY2016 end.
- Significant pressure on realizations owing to competitive pressures, resulting in decline in profitability during Q3FY2017.
- Heightened competitive intensity with the launch of services by RJio. While there has been a consolidation in the industry following spectrum trading, competitive intensity has not reduced with presence of sizeable players. This has prevented the industry participants to improve voice and data realizations
- Vulnerability to fluctuation in foreign exchange rate remains as significant proportion (50%) of the debt is still USD denominated whereas majority of internal accrual generation is rupee denominated.
- Weak subscriber quality and modest market position– with Revenue Market Share of 2.8% for Q3FY2017 and subscriber market share of 7.7% for Q3FY2017.

Description of key rating drivers highlighted above:

The Group has a pan-India network and an established position in the Indian telecom industry (87.7 mn subscribers as on December 31, 2016). It has healthy spectrum holding with sizeable spectrum in 800 MHz band which is best suited to provide high speed 4G data services. The Group earlier was providing CDMA services on this band, however now it has shut down its CDMA services and is offering 4G services on this band. Further the Group has entered into a comprehensive infrastructure sharing arrangement with RJio with reciprocal access to the newly laid network of RJio. This would limit the upfront capex of Group while enabling it to offer 4G services. In addition the group is present across segments like wireless services, wire-line services, enterprise connectivity solutions, domestic and international long distance segments, and direct-to-home (DTH) pay television services.

The group has also witnessed healthy uptake in its non voice revenues over last few quarters. The proportion of non voice revenue to total telecom revenue has improved to 39% in Q3FY2017 from 36% in Q2FY2017. Further with the merger of Sistema Shyam Telesevices Limited's (SSTL) wireless operations, Group has secured spectrum for a longer period of time and consequently it does not face any major spectrum/license expiry in the near to medium term. Given the healthy spectrum portfolio it did not have to bid aggressively for spectrum in the recent auctions and hence it faces limited regulatory payouts as compared to its competitors.

However the Group has witnessed pressure on its revenue growth and profitability amid the challenging environment and heightened competitive intensity post the launch of free voice and data services by RJio. Further the shutdown of its CDMA services and demonetisation has also exerted pressure on its revenue. During Q3FY2017 group has reported decline of 10% y-o-y and 4% q-o-q in its revenues and decline of 38% y-o-y and 22% q-o-q in its Earnings before Interest Tax and Depreciation (EBITDA). The group has also reported decline in its Rate per Minute (RPM) to Rs. 0.40 in Q3FY2017 from Rs. 0.45 in Q2FY2017.

Further the financial profile of the group is characterised by sizeable debt levels which along with modest EBIDTA has led to muted debt-coverage metrics. Moreover the company faces sizeable debt repayments in the near term whereas its internal accrual generation is insufficient to meet the repayment obligations. Accordingly the company has been refinancing its debt maturities and continues to remain exposed to the refinancing risks. The high proportion of foreign currency debt also exposes the company to risk of adverse movement in exchange rates.

In addition the Group is involved in re-organisation of its business wherein its wireless operations are getting merged into that of Aircel and its tower business is being acquired by Brookfield Infrastructure group. Both the deals aim at debt reduction; however the debt coverage metrics of the residual operations are expected to remain stretched.

Analytical approach:

While arriving at the rating, has taken a consolidated view of the RCom Group (referred to as “the Group”) including Reliance Telecom Limited (RTL) and Reliance Infratel Limited (RITL).

Links to applicable Criteria

Rating Methodology for Mobile Service Providers

About the Company:

Reliance Communications Limited, founded by the late Shri Dhirubhai H. Ambani (1932-2002), is the flagship company of the Reliance Group. RCom is among India’s largest integrated telecommunications service providers and ranked 6th based on subscriber market share. RCom’s corporate clientele includes over 39,000 Indian and multinational corporations, including small and medium enterprises, and over 290 global, regional and domestic carriers.

RCom has established a pan-India, next generation, integrated (wireless and wire-line), convergent (voice, data and video) digital network that is capable of supporting services spanning the entire communications value chain, covering over 21,000 cities and towns and over 400,000 villages. RCom also owns and operates next generation IP-enabled connectivity infrastructure, comprising over 260,000 km of fibre optic cable systems in India, the USA, Europe, the Middle East and the Asia-Pacific region.

Status of non-cooperation with previous CRA: Not Applicable.

Any other information: Not Applicable.

Rating History for last three years:

Table: Rating History

S. No.	Name of Instrument	Current Rating					Chronology of Rating History for the past 3 years		
		Type	**Rated amount (Rs. Crores)**	**Month - year & rating**	**Month - year & rating**	**Month - year & rating**	**Month - year & Rating in FY2016**	**Month - year & Rating in FY2015**	**Month - year & Rating in FY2014**
				April 2017	**Sep 2016**	**Jun 2016**	-	**March 2015**	**Sep 2013**
1	Non-Convertible Debenture (NCD) Programme	Long term	5,000	[ICRA]BBB (Negative)	[ICRA]BBB+ &	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Negative)	[ICRA]BBB+ (Negative)	[ICRA]BBB+ (Negative)
2	Long-term Fund-based/Non-fund Based Limits	Long term	28,116	[ICRA]BBB (Negative)	[ICRA]BBB+ &	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Negative)	[ICRA]BBB+ (Negative)	[ICRA]BBB+ (Negative)
3	Short-term Fund based/Non-fund Based Limits	Short term	7,314	[ICRA]A3+	[ICRA]A2+ &	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+
4	Commercial Paper (CP) Programme	Short term	2,000	[ICRA]A3+	[ICRA]A2+ &	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+

Complexity level of the rated instrument:

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1

Details of Instruments

Name of the instrument	Date of issuance	Coupon rate	Maturity Date	Size of the issue (Rs. Cr)	Current Rating and Outlook
Non-Convertible Debenture (NCD) Programme	March 2009	11.20%	March 2019	3,000	[ICRA]BBB(Negative)
Non-Convertible Debenture (NCD) Programme	Feb 2012	11.25%	Feb 2019	2000	[ICRA]BBB(Negative)
LT FB Limits (Term Loans)	March 2013	~11%-12%	March 2020	8,658	[ICRA]BBB(Negative)
LT NFB Limits	-	-	-	6,582	[ICRA]BBB(Negative)
LT Unallocated Limits	-	-	-	12,876	[ICRA]BBB(Negative)
ST FB Limits	-	-	-	3,365	[ICRA]A3+
ST Unallocated Limits	-	-	-	3,949	[ICRA]A3+
Commercial Paper (CP) Programme	Not placed	-	-	2,000	[ICRA]A3+

Source: Reliance Communication Limited

Name and Contact Details of the Rating Analyst(s):

Mr. Anjan Ghosh
+91 22 6114 3407
aghosh@icraindia.com

Mr. Harsh Jagnani
+91 124 4545 394
harshj@icraindia.com

Mr. Sachin Sachdeva
+91 124 4545 307
Sachin.sachdeva@icraindia.com

Name and Contact Details of Relationship Contacts:

Mr. L Shivakumar
+91 22 61143406
shivakumar@icraindia.com

About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

For more information, visit **www.icra.in**

Registered Office
ICRA Limited
1105, Kailash Building, 11th Floor, 26, Kasturba Gandhi Marg, New Delhi 110001
Tel: +91-11-23357940-50, Fax: +91-11-23357014

Corporate Office
Mr. Vivek Mathur
Mobile: +**91 9871221122**
Email: vivek@icraindia.com

Building No. 8, 2nd Floor, Tower A, DLF Cyber City, Phase II, Gurgaon 122002
Ph: +91-124-4545310 (D), 4545300 / 4545800 (B) Fax; +91- 124-4050424

Mumbai **Mr. L. Shivakumar** Mobile: +**91 9821086490** Email: shivakumar@icraindia.com 3rd Floor, Electric Mansion Appasaheb Marathe Marg, Prabhadevi Mumbai—400025, Board : +91-22-61796300; Fax: +91-22-24331390	**Kolkata** **Mr. Jayanta Roy** Mobile: **+91 9903394664** Email: jayanta@icraindia.com A-10 & 11, 3rd Floor, FMC Fortuna 234/3A, A.J.C. Bose Road Kolkata—700020 Tel +91-33-22876617/8839 22800008/22831411, Fax +91-33-22870728
Chennai **Mr. Jayanta Chatterjee** Mobile: +**91 9845022459** Email: jayantac@icraindia.com 5th Floor, Karumuttu Centre 634 Anna Salai, Nandanam Chennai—600035 Tel: +91-44-45964300; Fax: +91-44 24343663	**Bangalore** **Mr. Jayanta Chatterjee** Mobile: +**91 9845022459** Email: jayantac@icraindia.com 'The Millenia' Tower B, Unit No. 1004,10th Floor, Level 2 12-14, 1 & 2, Murphy Road, Bangalore 560 008 Tel: +91-80-43326400; Fax: +91-80-43326409
Ahmedabad **Mr. L. Shivakumar** Mobile: +**91 9821086490** Email: shivakumar@icraindia.com 907 & 908 Sakar -II, Ellisbridge, Ahmedabad- 380006 Tel: +91-79-26585049, 26585494, 26584924; Fax: +91-79-25569231	**Pune** **Mr. L. Shivakumar** Mobile: +**91 9821086490** Email: shivakumar@icraindia.com 5A, 5th Floor, Symphony, S.No. 210, CTS 3202, Range Hills Road, Shivajinagar,Pune-411 020 Tel: + 91-20-25561194-25560196; Fax: +91-20- 25561231
Hyderabad **Mr. Jayanta Chatterjee** Mobile: +**91 9845022459** Email: jayantac@icraindia.com 4th Floor, Shobhan, 6-3-927/A&B. Somajiguda, Raj Bhavan Road, Hyderabad—500083 Tel:- +91-40-40676500	