S Mobility Limited's Conference Call
February 18, 2013

Moderator

Ladies and gentlemen good day and welcome to the S Mobility Limited's conference call for the quarter ended December 31st 2012. As a reminder for the duration of this conference, all participants' lines will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during this conference call, please signal an operator by pressing * and then 0 on your touchtone telephone. Please note that this conference is being recorded. At this time, I would like to hand the conference over to Mr. Ravi Sathe of CDR India. Thank you and over to you Sir.

Ravi Sathe

Good afternoon everyone and thank you for joining us on S Mobility results conference call for the period ended December 31st, 2012. We have with us on the call the CFO of the company Mr. Subramanian Murali and R S Desikan, CEO of S Mobility. Before we begin I would like to add that some of the statements to be made in today's discussion may be forward looking in nature and a statement in this regard is available in the con-call invite which was emailed to you earlier. We will begin the call with the opening remarks from the management following which we will have the forum open for an interactive question and answer session. I would now like to invite Mr. R S Desikan to share with you some perspectives on the performance and developments of the company.

R. S. Desikan

Thank you Ravi. I have with me on this call Mr. Murali who is our Group CFO. We also have with us on the call Ozi Amanat who is the Chief Investment Officer at the group level that is for the holding company of S Mobility from the Singapore office. We are all from the corporate side. From the business side we have Mr. Ramakrishnan who is the CEO of the device business and Mr. Saket Agarwal who is the CEO of the VAS business supported by the CFOs of all the business, who are also on the call.

Let me begin by sharing a brief overview on the mobile handset space. There has been a gradual change where consumers are moving from 2G networks to 3G. All the operators have invested heavily for license fees and networks to promote 3G and therefore they are very keen that S Mobility promotes significant quantities of attractively priced 3G handsets. Our entire focus has shifted from 2G to 3G. In fact, within the power point presentation, you would have observed that the growth in the industry, in terms of value, is going to be driven by the 3G handsets rather than 2G handsets. In order to capitalize on this opportunity, we have lined up our entire supply chain and backend operations to support growth in 3G. We are well positioned in the market in terms of products, availability and distribution channels for the 3G revolution which is just around the corner. Simultaneously in terms of basic 2G products, ASPs have been declining from time to time. There is another aspect to the entire 3G paradigm which is while 2G handsets are being predominantly sold through Mom and Pop stores, the share of organized retail in 3G markets is much higher than that in 2G space. Fortunately S Mobility is not only into the device business alone but also in the retail space. Thus we are able to capture the growth in the retail segment also. During the quarter we have introduced several device models such as Mi-435, Mi-430 and others which have been very well received.

On the retail business, it has been a fairly tough business; with several challenges we have increased the total number of stores to almost 900. Like in any other retail chain, we do have a long tail with some of the stores where we are actually bleeding, so we are trying to restructure our retail business in such a way that some of the loss making stores are eliminated. At the same time, in order to capitalize on the 3G revolution, we started upgrading our stores to the 3G level, which we internally refer to as Version 2 stores. These provide a first hand user experience of handsets to the consumers. We believe that this approach is far better than the purchase experience at a normal Mom and Pop store. With regards to VAS, we have had certain regulatory challenges that still continue to exist. The domestic revenue has reduced in an absolute amount from quarter to quarter. In fact, the same thing happened last quarter as well. However, at the total VAS business level, we have managed to offset the drop in the domestic revenue by focusing on international markets. Our revenue from the international markets both in Africa, Latin America, South East Asia and the Indian subcontinent has managed to offset the drop in domestic revenues. I would now like to invite Mr. Murali to share with you the financials. Over to you, Murali.

S. Murali: Thank you Mr. Desikan. Thank you, for joining us today on the call to discuss S Mobility's financial and operational performance for the quarter ended December 2012. As Mr. Desikan mentioned, during the last few quarters, we have been in the midst of a strategic transformation in each of our businesses which has altered our offerings in this eco system. With regards to this, our performance during the quarter under review was rather subdued due to couple of reasons. Firstly, an unexpected poor festival season sale and certain one time provisions which impacted the reported profits. The negative impact however was offset, to an extent, by our focus on efficient growth by driving revenues and volumes, at the same time not compromising on margins. We continue to focus on better managing working capital cycles, build vendor relationships and reducing costs and overheads. For example our device business despite lower revenues, EBITDA as well as PAT was higher by over 1.5 times in the December quarter as compared to that in the September quarter. Our consolidated revenue for the quarter under review stood at Rs. 4,905 million and EBITDA stood at Rs. 55 million as against the loss before interest and depreciation and tax of Rs. 162 million in the corresponding period last year. This has been a significant turnaround. Reported loss after tax stood at Rs. 138 million as against a loss of Rs.179 million in the corresponding period last year. The loss incurred during the current quarter is mainly due to the impact of Rs. 132 million which was provisioning towards expected claims pertaining to previous periods. This is a one time charge which we have included. Our cash position continues to be strong. It stands at Rs. 1,727 million and it is important to note that this is after the FY12 dividend payout of 50% at Rs.1.50 per share which was paid out to the shareholders during the quarter under review. Let me now take you through some of the highlights of each business.

To begin with I would like to highlight the progress we made in our device business. S Mobility device division sold 1.5 million spice mobile handsets during the quarter indicating a 12% increase in volume year on year. Our S-branded handset's ASP stood at Rs. 1,119 which is an 8.5% reduction compared to the sequential quarter of September 12 indicating a downward trend in ASPs for the feature phone segment. While segment revenues are lower by 9% sequentially, gross margins improved by 600 basis points during the quarter. EBITDA margins have also improved due to cost rationalization and increase in gross margin. It is important to note that we have achieved a 46% overhead reduction in the 6 month period under review which is basically down from 20% of sales in H1FY12 to 13% in H1FY13. The Android based devices such as Stellar Pad and Stellar Virtuoso launched during the quarter have been very well received in the market. While we expect these handsets to further contribute to our revenues going forward, our focus on feature phone markets that comprises a major part of our portfolio share continues to remain strong.

Moving on to our company's retail business, we continue to focus on increasing the throughput in Spice Version 2 retail stores which has been established to enhance our brand visibility, ASPs and build on our brand loyalty. Today we have 846 Spice Hotspot stores out of which 24 are Version 2 stores. These 846 stores are spread across 147 cities in India. During the quarter under review we have actually witnessed a decline in the same store sales growth led by closure of unprofitable stores and unexpected slow festive season sales. Retail sales stood at Rs. 2,600 million down 16% sequentially. Gross margins have improved marginally by 110 basis points over September 2012, led by focus on retail sales and better realization. Retail ASPs stood at Rs. 5,814, increase of 12% sequentially and 20% year on year. This can be attributed to the increase in the share of Smartphones in our portfolio. Smartphone sales accounted for 67% by value and 28% by volume in the December 2012 quarter versus 55% by value and 22% by volume in the December 2011 quarter. ASPs for Smartphones stood at Rs. 13,804 during the quarter indicating an increase of 19% year on year and 1% quarter on quarter. This is testament to Mr. Desikan's point in his opening remarks with regards to the market moving towards Smartphones. We continue to gradually expand our presence across tier-1 cities and explore regional opportunities going forward. We are evaluating new business models around retail segments to further improve our performance and competitive positioning going forward.

On the VAS front, revenue growth has remained flat again primarily due to continued reduction in revenue share, related to the negative impact of TRAI regulatory directives. However revenue contribution from international operations and new product introductions have compensated for the close to 40% drop in domestic revenues. That is how revenues have remained flat despite a revenue drop from domestic operations. International revenues have shown a significant increase; they currently stand at 32% of total revenues versus 18% in December 2011 and 25% in September 2012. The increased contribution from international revenues is on account of aggressive expansion in emerging markets like Tanzania, Bangladesh, Zambia etc. Revenues from new products stood at 49% of total domestic VAS revenues versus 18% in quarter ended December 2011. We have increased our focus towards retail in mobile VAS retail, enterprise business, content monetization and mobile internet services. We expect these products to have great potential and believe that these will be the key growth drivers going forward. Developing more 3G or device-based VAS services through innovative products continue to be our focus. As most are aware, our margins were impacted on account of the minimum guarantee what we pay to the content providers and also due to certain one time provisions which we have taken during the quarter ended December 12 against expected claims for previous periods.

To sum up, we are in the midst of a challenging phase within this ecosystem and we are relentlessly working towards improving our profitability. We have achieved significant success in working capital management, cash to cash cycles, driving overheads down. We will continue to solidify our product portfolio and focus on account receivables, inventory, cash and overheads. We are optimistic on the developments in the Indian telecom system and I believe we are headed towards unlocking further value through prospects in this sector. This brings us to the end of our opening remarks and we would now be glad to take your suggestions and answer your queries.

Moderator Thank you Ladies and gentlemen we will now begin the question and answer session. Our first question is from Santosh Kathira of Merisis Capital. Please go ahead.

Santosh Kathira The Company seems to have done better than it has, compared to the last years. With regards to devices, ASPs have been reducing. It has declined from Q1 to Q2 and from Q2 to Q3. Is there anyway to account for and counter this trend? With most sales contributed by feature phones are we losing out on the Smartphone segment which is currently growing at a faster pace?

R. S. Desikan We have introduced a bulk of Smartphones towards the end of the quarter, during the month of December. Thus, you will see the full impact of the same through improving ASPs starting from the next quarter. Last quarter even though we did introduce some of the models, we could not capture the same for the entire three months' period.

Santosh Kathira I need clarity in the pricing of feature phones and Smartphones. Are the new phones introduced launched with a gradual pricing strategy? Are you are looking at an ASP of Rs. 5,000 for your Smartphones and is there a possibility that S Mobility launches the same at a price point of may be Rs. 4,000, so that you can start pushing your feature phone purchases into a slightly higher bracket?

T. M. Ramakrishan I will just brief you on the Smartphone strategy that we are into. Now there are two segments in the Smartphone. All Android phones are treated as Smartphones. We have 2G Android handsets which are very well accepted in the Indian market and 3G Android which are currently leading ASPs of Smartphones. Handsets that we have launched approximately cost Rs. 5,200. I expect 2G Androids to replace traditional touch phones completely. This means that 2G Android ASP will decrease to Rs. 2,500. Currently, ASPs of 3G Android stand at approximately Rs. 7,500 that will reduce to Rs. 6,000 in this quarter itself. You will see this moving. But then overall, the volumes for smart phones stood at 2% compared to 98% for feature phones. This trend is on its way to a major change where smartphone volumes will increase. Three months down the line we are looking at achieving 100,000 Smartphone sales per month. This way, we would see ASPs also growing.

Santosh Kathira Are we expecting to see the impact of this in the next 4-5 months for recently introduced handsets?

Ramakrishan Yes, the actual impact because we will see price dropping again in feature phones.

Santosh Kathira So cumulatively the impact would always be positive on the final ASP number?

T. M. Ramakrishan Yes.

Santosh Kathira Are there any intentions for the Spice group to go beyond India in the device business, i.e. distributing in other developing markets?

R. S. Desikan We do have a presence in places like Dubai and Africa where other divisions like VAS or retail are already established. We are certainly exploring the possibility. Our teams have been there; they have been scrutinizing the area. We are looking at opportunities there, but certainly if the opportunities are good, we will leverage it.

Santosh Kathira As far as I know, this time around the retail segment was a drag on the bottom-line and slightly on the top-line as well. I see that we are still going in the consolidation phase where we are trying to clean up our books and improve the working capital cycles as of now. In the past, we have had targets of reaching about 2,000-3,000 odd stores within the next couple of years. Are you looking at revising that based on a new strategy because in the last quarter we have increased the number of stores, but this time I believe there has been a decrease.

R. S. Desikan What we have realized is when you try to expand very aggressively invariably, it leads a long tail with lot of stores with negligible or even negative margins, even at the store level. If we have to return the adequate returns to our shareholders, it is our belief that instead of just establishing larger number of stores, we should look at the number of profitable stores. Secondly, the entire market is shifting from 2G to 3G, the stores also require some level of upgradation; which we have initiated already by establishing Version 2 stores. A customer who purchases a Rs.1,000 phone is different from a consumer who buys a Rs. 5,000-6,000 phone. He expects certain levels of demonstration before purchasing the device rather than just buying the box and walking away from the shop. It is essential to show how Android phones work. He would like to try out the internet or the video streaming and various other features. So we need to put in certain investment both in quality sales personnel as well as infrastructure with regards to the Version 2 stores. So, loss making stores are being shutdown and the Version 2 stores are being upgraded. So to that extent on the whole the number of stores may be reducing. Certainly it is a lengthy process and is expected to continue. But these initiatives are to solidify our foundation for long term stability of the business. We believe that in the long run this will enhance the overall value of the Company.

S. Murali To add to that, I believe when we talked about 2,500 stores over the last two years or over the last one year going forward, it was not an organic growth. We were always looking at inorganic opportunities as well, which we will continue to look at. We did not mention that we will grow to 2,500 stores organically. It is not possible to grow to 2,500 organically. Thus, we are continuing to look at inorganic opportunities. When it materializes, then the number of stores can increase. However, this is not entirely in our hands or under our control.

Santosh Kathira So, just coming back to a point about moving from 2G to 3G, now you come out with Hotspot 2.0, so in this case how do you compare the ASPs between your regular hotspots and the 2.0 versions?

R. S. Desikan ASPs at Version 2.0 stores will be certainly higher than regular ones because Smartphone contribution to revenues, while overall could be at about 67%, for Version 2 stores, it could be as high as 90%. So by virtue of the fact that Smartphones in general have got a higher ASP, the overall Version 2 ASPs are going to be much higher than the normal store ASPs.

Santosh Kathira The reason why I asked the question was that because there is a higher investment in Hotspots 2.0 version, the time taking to breakeven which is typically one year for simple Hotspot I am guessing would be slightly higher if the ASP was not proportionately increasing to the amount of investment that you have put in, so that is what I am trying to understand here. Will hotspot 2.0 Version 2 stores break-even within a year considering the higher ASPs as you mentioned?

R. S. Desikan No, what we are trying to do is instead of rushing with brand new Version 2 stores starting from scratch, we are trying to upgrade some of the existing stores into Version 2 stores which already have the advantage of good locations and neighborhood. By this process we are able to control the breakeven level. Instead of a green-field, it is like a brown-field expansion.

Santosh Kathira Regarding VAS business, Spice Digital seems to be right for inorganic growth in markets abroad. So are you looking at some acquisitions as of now?

R. S. Desikan In today's sectorial scenario, I believe it is easier and cheaper for us to grow organically rather than invest highly in acquisitions. Some of our competitors have initiated inorganic acquisitions at a very high cost. I am not sure whether that has really paid off.

Saket Agarwal Quite frankly, given the irrational valuations in the domestic VAS business, it did not make sense earlier. However, there is sanity coming in the picture. Inorganic growth for certain product lines would definitely be something that we are keen to focus on, specifically around mobile internet and mobile commerce which we are looking at aggressively currently. Now that most of the valuations are amenable for inorganic growth we are looking at the same.

R. S. Desikan But not in the voice business.

Saket Agarwal Not really.

Santosh Kathira You talked about moving into the 3G space and advanced VAS systems. Thus, I expect consolidation in the domestic markets. In terms of international markets, most of the peers have gone about setting up their base in those regions rather than buying services. Do you intend to start off organically abroad or is there any scope for inorganic growth abroad as well?

R. S. Desikan No, we already have a physical presence in many countries in Africa

Santosh Kathira You have presence in Latin America and I guess the market is different. Again, you have a different market in Argentina and even Peru. Are you looking at expanding there and in Africa inorganically or organically?

Saket Agarwal We put our own subsidiary in Africa three years back and during the initial couple of years it has been more about building the business. But off-late we are seeing enough traction and in a sense it is an organic-cum-inorganic method, where we have an equity partner who allows us to take care of the African market. For the rest of the markets, we are not investing heavily, building assets and then growing in the markets. We are using a partnership route, where we are partnering with local VAS companies to distribute the products and quite frankly the way we are progressing in the next couple of quarters we are already looking at 50% contribution coming from the international market. So we are pretty much on the track. So we do not find the need at this point in time to get into an inorganic expansion in international operations.

Santosh Kathira With regards to how sales have declined over the last festive season; can this be said of the entire mobile industry or is it specific to only retail and only to Spice? I would not want to name competitors, but are they also experiencing a similar slump?

R. S. Desikan In fact recently whether you have read, I believe it was stated in the Economic Times, I came across an article which stated that the last festive season has not really been that good for all the consumer durable companies. In fact there was another article in the latest India Today issue discussing how the consumer is actually holding back from splurging on consumer durable items. A 40% to 50% jump in revenue that we expected during Diwali which was even expected by companies like Samsung actually did not happen. So certainly there has been a general problem.

Moderator Thank you. The next question is from Paras Mehta of Goldman Sachs. Please go ahead.

Paras Mehta One question is on domestic VAS and the second is on the Version 2 stores. Firstly on VAS, by when do you expect the VAS revenues in India to start showing growth again and what are the key applications that you believe are likely to drive that?

R. S. Desikan In terms of domestic VAS revenues, it comprises of two parts – one is the traditional 2G VAS revenue which is voice based and the second is our new introductions. There are several new initiatives that we have taken trying to get into mobile VAS retail, enterprise business and mobile internet services and so on. These are all new initiatives that we have put in place, outside of the traditional voice based VAS services which we have been providing over time. So that is the area we are focusing on. We believe that the future is going to be dependent on new VAS that will compensate the negative effect of voice traffic.

Paras Mehta And what could be the key applications that you believe can drive that?

Saket Agarwal We have been reaching out to the consumer all these years with the traditional route via telecom operators. We realize that given the changing consumer behavior based on both the networks and the smartphones that are getting into the hands of the consumer and also the regulatory environment, it is important to reach out to consumers through alternative routes. Those alternative routes are direct to consumer through our retail channel. It could be through mobile internet product offerings which we are focusing with various App Stores. These are two new ways of reaching out to the consumer. The good news is that in the last couple of quarters, we have seen traction by way of which we have been able to compensate 40% drop in domestic Telco revenue by our new endeavors. I believe it is laying out well for us and it is only going to get better as phones are getting cheaper and smarter while networks are getting enhanced with 3G capability.

Paras Mehta Now the second question is with regards to Version 2 stores, what is your average cost of converting an existing store to a Version 2 store and currently if there are about 24 Version 2 stores out of 846 Spice retail outlets, what is the number of Version 2 stores expected by 2013?

S. Murali The average of cost of conversion of an existing store is around 20-25 lakhs per store. Given the experience which the new stores will provide and the live demo phones that we use, this is the kind of incremental CAPEX which we are looking at for new stores. With respect to the number of stores, I believe it is too early to give a new number in terms of how many new stores we will put up. We are in the process of working our retail strategy. With regards to how we want to expand further over the next 2 or 3 quarters; I believe we will evolve and I don’t believe I can commit any number at this point.

Paras Mehta Would you be able to provide any clarity on how many stores you will be able to convert in the next few months?

S. Murali I believe that is what I just mentioned because we have certain internal plans and it is bit early to share that.

Moderator Thank you our next question is from Srinivas Rao of Deutsche Bank. Please go ahead.

Srinivas Rao Firstly, when you talk of Smartphones does that necessarily also mean 3G enabled?

R. S. Desikan Currently we do have 2.5G as well as 3G, but we believe that going forward, our future focus or emphasis is going to be primarily on 3G enabled smartphones.

Srinivas Rao Sir right now as we speak when you give today by 67% by value is smartphone that is both 2.5 and 3G, is that correct?

R. S. Desikan That is correct because in fact almost in all our Hotspot retail stores we do sell Samsung and Nokia which also have 2.5 G as well as 3G. So we sell what the customer wants.

Srinivas Rao I am just trying to get to that appropriately we can understand the definition, that is all.

R. S. Desikan The difference is in our on device business, we are moving away from 2.5G; in terms of Spice handsets we will focus only on 3G, but in retail we will sell 2.5G handsets as well because the customer may want a Nokia or Samsung, and well will provide them with the same.

Srinivas Rao When you said 2.5G it will be EDGE and GPRS right?

R. S. Desikan You are right.

Srinivas Rao Just to clarify you said the 3G Android Price you expected to reduce to about Rs. 6,000 in the next 1-2 quarters, have I got that right?

T. M. Ramakrishan That is right. Not over 1-2 quarters, rather the coming quarter itself.

Srinivas Rao Will 2G Android ASPs come down to Rs. 2,500?

T. M. Ramakrishan Yes, between Rs. 2500 to Rs. 3,000

Srinivas Rao And right now it is at about Rs. 5,000?

T. M. Ramakrishan Right now both put together I can clarify it is Rs. 4,500 for 2G and Rs. 7,000 plus for 3G.

Srinivas Rao I wanted to check on your retail store strategy and whatever I have tracked over almost two years is that you have tried fairly hard I must say to make it a profitable venture. Unfortunately repeatedly when you focus on growth, it becomes challenging to generate profits and when you try and do the other way around the growth is challenging. So it seems to be an issue which is impacting the business. Firstly, do you actually believe that a retail handset model can work in India, given that the price of these kind of goods continue to reduce aggressively, literally quarter by quarter? Does the business have the opportunity to actually make money?

R. S. Desikan Let us just step back for a minute and look at the bigger picture. The total handset business in India is about Rs. 50,000-60,000 crores of which organized retail is just about 10% of the total. Let us say a little over Rs. 5,000 crore. 90% is flowing through Mom & Pop stores, and organized trade is just about Rs. 5,000 crores. Within Rs. 5,000 crores there are only two big players taking almost half of that revenue, one is us, one is our other major competitor and the others are primarily regional players who have got a footprint in certain parts of the country. Of course Croma is a slight exception. They have an all India footprint. However, it is not just only a pure play mobile handset retailer. They also sell everything from A to Z in electronics and electrical appliances and so on. So even though this is all India it is a slightly different business model. In our business model which is the neighborhood format, about 400-500 square feet multiple stores- they comprise 10% currently. However going forward, both Indian as well as international experience very clearly shows that as the smartphones percentage increases the share of organized trade is going to grow disproportionately to what it is today which means the Rs. 5,000 crore market of organized trade is going to grow much faster than the Mom & Pop store. That is where we see an opportunity.

Srinivas Rao As you would have seen even in US, the experience of companies like BestBuy, this whole issue where internet retailers tend to have an impact on pricing and in India you have companies like Flipkart which is gaining some traction attracting particularly 3G phone users who are fairly well informed buyers. Is that another source of potential competition from a pricing perspective for you?

R. S. Desikan If you can't beat them, join them. So we have joined them. We are our own online retail store.

Srinivas Rao Currently, is the pricing on your online store comparable to your normal store?

R. S. Desikan That is right.

Srinivas Rao Is that the model which is more workable? What percentage of sales will you make through your online stores?

R. S. Desikan Currently it is negligible. In terms of percentage, it may be less than 1%. But we have to be present in that segment; the only good news is when you talk about smartphones, you know you require more of touch and feel of the product than just ordering the box. While blindly ordering a box is a common phenomenon for 2G phones and is much easier. For a 3G phone, you would want to see the features and experience it. Therefore, we do believe that footfalls are required. Brick and mortar are still essential other than just online stores.

Srinivas Rao That brings me to the other question which is; the phone phenomenon what they call as showrooming where people come and test the phone at the brick and mortar retailers, basically end up buying from online retailers because of the pricing differential. I know this is not applicable for Spice branded handsets, but definitely for other handsets like Nokia or Samsung. Is this something that you are cognizant about? Do you see that happening in your stores, particularly the ones which you are converting into Version 2 where as you said people will get an opportunity to see live demo of handsets?

R. S. Desikan When they visit the store and then if they don't buy, we push sales through our online store there. Consumers are welcome to buy products from our own online stores. As long as they buy our products, it is fine with us. If a consumer wants to purchase a Spice phone, whether he buys it online or a physical store, it does not make a difference.

Srinivas Rao No, if he buys a Samsung Galaxy, he sees at your retail outlet and goes and buys it from let us say Flipkart, just is an example.

R. S. Desikan If he sees Galaxy at the Spice retail store and goes and buys it from Flipkart it is a problem but he can also buy a Galaxy from our own online retail. This option may become available in the near future. We are still to fine tune that business model but we are looking at different options on how to beat this issue.

Moderator Thank you. Our next question is from Samir Tulsiyan of JM Financial Please go ahead.

Samir Tulsiyan Firstly, if we are talking about the price points of 2G and 3G phones to come down to Rs. 2,500 and Rs. 6,000 in the coming quarter. What are the price points we are looking forward to for the Smartphones to really take off and what are the price points at which you expect tablets to take off? Secondly, what has been the impact of the recent TRAI regulations on the mobile VAS business and how much more impact is yet to be realized?

R. S. Desikan As far as VAS is concerned the revenue drop is primarily driven by various regulatory changes which TRAI is implementing through the operator. The other side of the equation is in many of these cases, in addition to a revenue sharing arrangement, we also have certain minimum guarantees which we have granted to the content owner almost 2 years back when we signed a 2 years contract. This primarily affected our performance in the last quarter and possibly in the current quarter, which is also causing a slight drop in the margins. Once the existing contract is over, hopefully we should have a better situation in terms of profitability. But as far as the revenue drop is concerned, Saket just explained the initiatives we have taken to offset the drop in revenue by the introduction of new innovative products in other areas. This is how we are managing our VAS business. If we observe a revenue drop, we compensate the negative effect via international expansion. So therefore as far as Spice Digital Limited is concerned, the total revenue is almost near flat even though domestic revenue has dropped by as much as 40%, because of the flexibility and innovation shown by our development team along with our international team. Thus, we have been able to maintain the overall revenue at the same level, despite a 40% drop, which in any normal industry would be very difficult to manage.

Samir Tulsiyan Going ahead, are we seeing a stable domestic business or are there any expected hurdles to overcome as far as the domestic business is concerned? Secondly, what is the minimum guarantee period required to overcome the same?

R. S. Desikan The minimum guarantee is almost over and the old contracts are running out in April.

Saket Agarwal While we see domestic revenues from telcos which will continue to slide, TRAI regulations have had multiple implications. It is not that TRAI rules have been implemented as yet in letter and in spirit. If those were to be implemented, then our industry would actually die which necessitates the acquisition of the customer only through a written consent over a fax, email or an SMS. Thus, we are talking about is self regulation by telecom operators. We have also been trying to implement methods to readdressing consumer grievances and provide refunds off late. While this continues to be in a certain state of flux, we got into creating alternate revenue streams which are not dependent on the operator, reaching out to the consumer directly through our initiatives in the retail front and mobile internet. Good news is that despite of significant fall in revenues from the telecom operator, equivalent to 40% last quarter, we could recover most of the negative impact through these initiatives where we are reaching to the consumer through alternate methods. We are concerned at the downfall of revenues from telecom operators, but we are confident as we have enough traction from other lines of business from the domestic front, though, not through telecom operators but directly reaching out to consumers. It will continue to be a challenging period till certain agreement is reached with regards to how VAS business is conducted in India.

Samir Tulsiyan The second question about the price points that we are looking at for Smartphones and tablets to take off.

T. M. Ramakrishan The pricing for tablets is going to reduce. This is primarily due to handset and PC manufacturers who are entering the same space apart from mobile operators who are also doing the same. Thus, we expect a cut throat competition from them too. As some may be aware, Acer is launching quad core, 10 inch products which are priced at less than Rs. 10,000. So the price is going to decline to that level and this is where the competition will exist. With regards to Android phones, it is not the price that is declining but technology which is growing and getting affordable a fast pace where you are able to purchase products at less than Rs. 10,000.

Samir Tulsiyan With regards to Smartphone prices, what would be the reduction from Rs. 2,500 and Rs. 6,000 levels?

T. M. Ramakrishan It can reduce. When feature phones were actually doing well, there were non-warranty products from Chinese companies that flooded the market and were doing extremely well. Now they have actually specialized in the Feature phone segment and will enter into the Smartphone segment because that is expected to be the main market. This is a change that will happen and they will also aid us in contributing to the growth in market.

R. S. Desikan It is not just the ASPs that are declining. Correspondingly, the volumes are also increasing, That is why the total market size is expected to grow from something like US$ 10 billion to 14 billion in value. With respect to the company's perspective, we are more concerned about the total value that we generate rather than focusing on ASPs alone. ASP is certainly an important aspect, but the total revenue that we generate and of course, our margins are of prime importance.

Samir Tulsiyan My concern was on the margin front only.

T. M. Ramakrishan I don't see margins dropping to that level because our raw material costs are also reaching a level to support the same. So I don't see a major concern in the margins.

Moderator As there are no further questions from the participants. I would now like to hand the floor back to the management for closing comments.

R. S. Desikan Ladies and gentlemen thank you for attending our quarterly conference call. If you have got anymore questions you are always welcome to contact Hetal who is our Investment Relations Manager.

Moderator Thank you very much sir. Ladies and gentlemen on behalf of S Mobility Limited, that concludes this conference call.