

Bharti Infratel Limited First Quarter Ended June 30, 2016 Earnings Conference Call

Conference Call Transcript

Event: Bharti Infratel Limited First Quarter Ended June 30, 2016 Earnings Call

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Bharti Infratel Limited First Quarter Ended June 30, 2016 Earnings Conference Call**CORPORATE PARTICIPANTS****Akhil Gupta**

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Chief Financial Officer - Bharti Infratel Limited

Devender Singh Rawat

Managing Director and CEO - Bharti Infratel Limited

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Citigroup - Mumbai

Vinay Jaising

Morgan Stanley - Mumbai

Sachin Salgaonkar

Bank of America - Mumbai

Sunil Tirumalai

Credit Suisse - Mumbai

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Deutsche Bank - Singapore

Vaibhav Goyal

SBI Life Insurance - Mumbai

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JM Financial - Mumbai

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Morgan Stanley - Mumbai

PRESENTATION**Kamaldeep - Moderator**

Good afternoon ladies and gentleman. I am Kamaldeep, the moderator for this conference. Welcome to the Bharti Infratel Limited First Quarter Ended June 30, 2016 Earnings Call. For the duration of the presentation, all participant lines will be in the listen-only mode. After the presentation, the question-and-answer session will be conducted for all the participants on this call. In case of a natural disaster, the conference call will be culminated post an announcement. Present with us on the call today is the senior leadership team of Bharti Infratel Limited. Before I hand over the call, I must remind you that the overview and discussions today may include certain forward-looking statements that must be viewed in conjunction with the risks that we face. I now hand over the call to our first speaker of the day Mr. Akhil Gupta. Thank you and over to you Sir!

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Akhil Gupta - Chairman - Bharti Infratel Limited

Thank you, my colleagues and I would like to welcome you all to the earning call for the first quarter ended June 30, 2016. You are all aware that telecommunications has a very crucial role to play for success of Digital India program being pursued by the Government of India. This is so because telecommunication is the only one which can provide networks for broadband connectivity to Internet across length and breadth of the country, to every town and village. And of course, in India, where fixed lines are less, the only way to do so is wireless.

Telecom networks, as you would know, already cover approximately 95% of population and 90% geography of India for voice, with over 500,000 towers and over a million base stations. However, for mobile broadband the penetration is still quite low, with 3G networks on only, at best, 40% to 50% of towers, and for 4G, where the rollout started only last year, it is significantly lower than that.

With investments of over \$50 billion by operators in spectrum over the last six years and perhaps more to come in the coming auctions, the operators are rapidly rolling out mobile broadband networks across the country. We expect that the voice coverage will be replicated for at least 3G within the next few years. This means that this should result into a significant rollout in the coming years. In addition, the operators have also now started rolling out 4G networks, which we expect over time to follow the same trend, as the 4G ecosystem grows.

The rollout for operators are also being complemented by very rapid growth in penetration of smartphones in India, which as per an Ericsson estimate, is likely to go from 13% in 2014 to 58% by 2020. IDC estimates India to overtake US to become the second largest smartphone market globally by, as early as, 2017.

The telecom industry is also witnessing a reasonable consolidation, which would result in the spectrum becoming available to operators who have the resources to roll out networks. The continuing rapid growth of data traffic and massive investments in spectrum, we expect the operators who will be the consolidators, to accelerate data network rollouts in years to come.

Let me point out two major developments during this quarter for us. The first is about a transition to Ind-AS accounting standard with effect from April 1, 2016. As per the Ind-AS, while the consolidation for JVs, other than controlled subsidiaries, is to be on equity accounting basis, we are also presenting in our quarterly report the consolidated results based on a pro forma consolidation, incorporating 42% proportionate consolidation of Indus Tower results, based on audited Ind-AS accounts. This would enable all our investors and stakeholders to have continuity of reporting of our performance, since right from our inception, we have been reporting consolidated results in this manner under IGAAP. We have also reworked all the earlier period financial results, which were hereto before made on the basis of Ind GAAP to Ind-AS for like-for-like comparison by you. Full details of the various salient features of transition to Ind-AS and the various reconciliations have been given in the quarterly report for your better understanding, but I would request our CFO, Pankaj Miglani, to separately talk about these for clarity.

The other major development during the quarter was the amendment to Master Service Agreement by Indus Towers and Bharti Infratel. You might recollect we had given a brief outline on the proposed changes during the earnings call for the last quarter on 27 April 2016. The gist of the amendments to the MSAs is as under.

Number one, the reason for amendments, as we had outlined during the last quarter earning call, the amendments in MSAs were carried out by us, because they were desirable in the context of addressing the following two major anomalies or concerns. First, the uncertainty regarding charges at the time of renewal of leases, which have repeatedly come up during our discussions with all the investors and two, the fact that there was a rate difference on sharing on same tower between a tenant who came earlier versus a late entrant, in as much as the earlier entrant had to pay a higher effective rental due to escalations over larger period of time vis-à-vis the later entrant. The gist of material amendments to counter these was, first, we introduced a rate card approach for the rates to be charged to the operators, whereby the rate card would go up by 2.5% each year on the commencement of each financial year. In other words, on April 1 of each year, the base rates would increase by 2.5% for all operators on a uniform basis.

Two, for all existing customers whose leases were expiring before March 31, 2022, an option was given on a non-discriminatory basis to extend the same till March 31, 2022 and in lieu, we offered certain concessions by way of rationalization of the existing escalation charges with a view to address the anomalies as above, but based on the principle that the overall effect along with amendment of rate cards for new sharing's would be NPV neutral to both.

Three, there were certain other minor amendments, for example, some amendment to encourage de-loadings on congested sites, to make room for additional sharing on such sites. The financial effect of such amendments, first of all, the overall effect of the above rationalization of approximately 15 crores a month on a consolidated basis would

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be neutralized by additional recovery on new sharing, due to rate card increases and the effect of change of accounting as per Ind-AS, since the revenue equalization would no longer be required. Accordingly, the overall financial impact for 2016-2017 itself on account of the MSA amendment and Ind-AS adoption would be immaterial vis-à-vis the IGAAP results as you have been seeing earlier.

Secondly, one concern had been on revenue per customer and I would like to while the details have been given in the quarterly report, let me just point out two facts. The revenue per customer per month as per the Indian GAAP for quarter four 2016 was 34,671 per month. As per Ind-AS, for the same period, that is quarter four 2016 that amount stands at 35,012, a slight improvement. Between Q4 2016 and Q1 2017, as per Ind-AS, the revenue per customer per month has a slight improvement from 35,012 to 35,039.

The overall effects of these changes are, number one, removal of uncertainty on renewals, as renewals will be like any new tenancy. Two, uniformity between charges paid by all operators for same kind of sharing on a tower, irrespective of the point of entry.

In summary, it is our belief that as leaders, we have carried out a very major transformation with respect to MSA construct on a permanent and long-lasting basis, which would result in win-win situation for all concerned, the towercos, as well as the customers and further strengthen the principle of non-discriminatory services to all our customers, a principle which I'm very proud, is the bedrock of our mandate.

Coming to the results, this quarter the total tower base stood at 89,352, witnessing a year-on-year growth of 3.4%, where the colocation growth was 6%. We ended the quarter with over 196,000 colocations with a Closing Sharing factor of 2.20 times.

The consolidated revenues for the quarter were at 3,211 crores, a year-on-year growth of 7%, while the EBITDA for the quarter at Rs.1408 crores showed a growth of 9% year-on-year.

The profit after-tax for the quarter was at Rs.756 crores, witnessing a 71% year-on-year growth. This did include a one-time reversal of a deferred tax of something about Rs.127 crores, which needs to be adjusted, which is a real gain, because that is the gain on our mark-to-market income on mutual funds which are more than three years and above. There is actually no tax. Therefore it's a reversal of the tax, which was already provided. I think Pankaj will perhaps talk a little more about that separately.

We are also pleased to note that on another major government of India initiative that is on Smart Cities, some implementations have now commenced with tenders floated by a few states for specific cities or areas. For example, for Bhopal principal areas and NDMC area in New Delhi. We have participated in the bid for Bhopal, of which the results are awaited. We expect other states to follow suit. These developments, we believe, augur well for infrastructure companies like ours. We also believe that with our resources and expertise, we would be in a pole position to exploit these new potentials.

In summary, we believe that in coming times the infrastructure requirement of telecom operators will increase to cater to the ever-increasing data demand across India. Our relationship with all the operators and our execution and management expertise will help us in further strengthening our leadership position. In addition, we would be closely watching developments on potential new business areas, like Smart Cities.

Thank you all. Pankaj, may I now request you to brief on the accounting changes from this quarter, before we open the floor for question-and-answers.

Pankaj Miglani - Chief Financial Officer - Bharti Infratel Limited

Thank you, Akhil. Good afternoon, friends. I will now talk about the Ind-AS changes. The Company has adopted the Ind-AS financials from April 1, 2016, with effective date of transitioning being April 1, 2015. The major changes are as follows. First, as per Ind-AS, the consolidation for joint venture has to be done on the basis of equity accounting. However, we are also presenting in our quarterly report the audited consolidated results, based on a pro forma consolidation, incorporating 42% proportionate share of Indus Towers, based on Ind-AS. This would enable all the investors to have continuity of reporting of our performance, since right from our inception we have been reporting under IGAAP. We have also reworked the earlier period financial results, which were hereto before made on the basis of Ind GAAP to Ind-AS for like-to-like comparison.

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The second change under Ind-AS, the annual escalations on revenue and costs are no longer equalized over the lease term. Hence the lease revenues and costs are recognized in P&L on actual basis, which means the revenue equalization and lease equalization are no longer recorded. Third, under IGAAP, investments are accounted for at cost or market price, whichever is lower. The gain on such investments was being recognized in the statement of profit and loss account only at the time of realization of profit. Under Ind-AS now, such financial instruments have been recorded at market value through profit and loss account. Accordingly, our mutual fund investments will be mark-to-market every quarter and the financial results will reflect the corresponding changes. In addition to these changes, in Section C we have detailed all other changes which have happened. Accordingly, we have made changes to our quarterly report too. The quarterly report is now segregated into four broad sections. In Section A, the company is providing audited financial information on pro forma basis as per Ind-AS accounting principles, but for consolidation which is happening on a line by line basis for joint venture. In Section B, we are representing the audited consolidated financial statements under Ind-AS, based on equity accounting for joint venture. In Section C, we have given the details on the key accounting changes, the impact of transitioning to Ind-AS and reconciliation.

The reconciliation statements, which we have disclosed are broadly categorized into five different items. So first is on IGAAP to Ind-AS balance sheet as on April 1, 2015, detailing all the changes what we have done. The second is net profit reconciliation between IGAAP and Ind-AS for last four quarters, as well as for the complete financial year 2016. The third is an IGAAP to Ind-AS profit and loss statement walk for financial year 2016. Fourth is IGAAP to Ind-AS balance sheet as on March 31, 2016. And the last one is profit and loss and a balance sheet walk from Ind-AS consolidated results using equity method, to pro forma consolidated results using proportionate consolidation. And Section D talks about the accounting policies, which have now been implemented, along with the glossary of the terms. We have tried to make the transition to Ind-AS smooth as possible and ensure continuity is maintained for the investors and analysts. However, we are open to any questions that you might have. Thank you very much and we will now open the floor for Q&A.

Kamaldeep - Moderator

Thank you very much Sir. We will now begin the question and answer interactive session for all the participants who are connected to the audio conference service from Airtel. Due to time constraints we would request if you could limit the number of questions to two enable more participation. Hence, management will take only two questions per participant to ensure maximum participation. Participants who wish to ask questions may please press * 1 on their touch tone enabled telephone keypad. On pressing * 1 participants will get a chance to presents their question on a first in line basis. To ask a question participants may please press * 1 now. The first question comes from Mr. Kunal Vora from BNP Paribas, Mumbai. Mr. Vora you may ask you question now.

Kunal Vora - BNP Paribas - Mumbai

Thanks for the opportunity. I have two questions. First is can you share your outlook for average rental per tenant going forward? It has been flattish over the last two, three years, but considering that we are moving to Ind-AS now, should we be expecting, excluding the impact of rental contract renewal, around 2.5% escalation going forward? And also can you help us quantify the impact of rental renewals. So there's two parts; 2.5% should be the normal increase, but will that be largely offset by the downward revision because of rental contract renewal? That is my first question.

Pankaj Miglani - Chief Financial Officer - Bharti Infratel Limited

Hi, Kunal, let me pick up the second question first. On rental renewal impact, Akhil in his speech has already broadly outlined the total impact which has happened, which is around 15 crores per month, which further gets offset on account of the higher realization what we will have, plus the transitioning the RE reversal, which would have happened on transitioning from IGAAP to Ind-AS. As far as the outlook on average rental per tenant is concerned, while we do not provide any specific guidance, on Ind-AS, because of this transitioning happening, we expect the rental per tenant to grow basis loadings and premiums and further offset by the tenancy offset, which will happen on account of higher tenancy. So we will not be giving you any specific amount per se.

Kunal Vora - BNP Paribas - Mumbai

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So the tenant who was like, say, paying 10 escalations, assuming he started at 30,000, gone to 37,500, what will be the new rental now, will it be 30,000 or will it be like say what is the new base now?

Akhil Gupta - Chairman - Bharti Infratel Limited

It would be frozen wherever he is, till his escalation catches up with the rate card, and that is what the effect of that 15 crores which I had mentioned, takes into account all that effect.

Kunal Vora - BNP Paribas - Mumbai

I will have to understand this better offline but the second question is on new tenant additions, they have slowed down during the quarter and I think there was an additional impact because of certain exits. Is the pain behind us now or can we expect some more impact on exits going forward?

Devender Singh Rawat - Managing Director and CEO - Bharti Infratel Limited

Hi, this is D.S. Rawat this side. We have had exits as you know from Videocon, which is one of the operators, which has sold its spectrum and that is what is primarily visible in the current numbers that you look there. Besides, of course, the operators' own focus in first quarter towards waiting for the spectrum auction that is round the corner too, in terms of their larger emphasis is primarily in building 3G, 4G networks is what we see from an operator standpoint today. Is the pain behind us, it is hard to say. We still think we are in a phase of consolidation of operators, but we believe this consolidation is positive in the long run for us and that is why we are actually seeing that as consolidation progresses, we might have few more operators, depending on the way this consolidation shapes up. You already are aware of the newspaper articles around Uninor, around discussions between RCom and Aircel. So, these are some things which are still in the works. But our belief is with this consolidation whatever entity that gets formed will definitely try to match up in terms of their coverage and reach with the leading operators, which is positive for us and overall it will improve the health of all the telecom operators.

Kunal Vora - BNP Paribas - Mumbai

Just one follow-up on this. So, for the tenants who exited over the last two, three quarters, I was looking at your Annual Report, you have about 2 crores of termination charges for contract cancellation in FY 2016, which was 20 crores in FY2015. How were the recoveries? Over the last two, three quarters whoever has exited, is it in litigation right now or have you been able to collect everything incrementally?

Devender Singh Rawat - Managing Director and CEO - Bharti Infratel Limited

So, these are progressive discussions that happen with the operators about exits that are going on. We continue to go ahead and seek our claim with them. With some, yes, there are litigations that are going on for the historical ones. For the new ones, we are trying to reach settlements and see that we get the corrections for the exits that have happened there.

Kunal Vora - BNP Paribas - Mumbai

Can you help us quantify what kind of number you might be able to collect on this?

Devender Singh Rawat - Managing Director and CEO - Bharti Infratel Limited

First, I think from again I just want to add this that from reporting in the financial numbers, we have not taken any of the exit numbers into our financial accounting. From accounting standpoint, on the day we collect this money is when we are going to recognize that as revenues too. We do not want to give guidance there. These are

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negotiations, one on one with operators. As I said, we reserve our rights in terms of going into our claims with these operators and for some of them we have sent some legal notices to see that we get our collections there.

Kunal Vora - BNP Paribas - Mumbai

Thank you Sir, my questions have been answered.

Kamaldeep - Moderator

Thank you Mr. Vora. The next question comes from Mr. Gaurav Malhotra from Citigroup, Mumbai. Mr. Malhotra you may ask your question now.

Gaurav Malhotra - Citigroup - Mumbai

Thanks for the opportunity. Just a couple of questions. One is on your base rental and if I just do that math versus the math for, say, American Towers, as well as Viom, what we see is that your rental seems to be almost at a 20%-25% premium to the competition. Now, part of the reason could be because of escalation etc. and 3G loading, but still the number seems to be on the higher side. So, any thoughts on that and a follow-up on that would be what would be the risk of churn happening, given that there is the renewals are coming along?

Devender Singh Rawat - Managing Director and CEO - Bharti Infratel Limited

So, again, let me take this, DS Rawat this side. As far as our market intelligence goes, firstly the information that we have is not in the public domain. So I cannot comment about that specific information. Our belief, yes, we are expensive, but that range is about 5% to 7% and not beyond that. On a total cost basis, we are cheaper than any other competitor, given our higher tenancy ratio, given our lower energy cost and the higher uptime that we provide. Those are the products that we work on in terms of differentiation towards the end customer. You rightly said, yes, we have got higher escalations. We have been in the business for a longer time, escalations have been building up with some of the operators too, and also higher loading, because the leading operators are working with us. So those could be the plausible reasons, as you rightly said. B, on churn, I have said this earlier that tower capacities are not truly fungible capacities. There is a certain degree of overlap with other tower companies. But in that sense, we do not foresee any risk of operators churning or migrating at the end of the contract too. C, I think what we have done by correcting the fundamental construct of this MSA going forward, we believe that the time when tenancies start to come up for renewal, the industry would have adopted this as a model and there would hardly be any incentive for anyone to actually look at migrating. And lastly, of course, there is a huge amount of disruption for an operator, besides the cost of course of shifting from one tower to another one. So we do not see that is going to have any material impact in terms of shifting from one operator to another unless, of course, the service qualities are terribly bad.

Gaurav Malhotra - Citigroup - Mumbai

Just one follow-up, is competition also, in your view, or if you can share, is also shifting to the kind of new rate card system which you and Indus have already shifted to?

Devender Singh Rawat - Managing Director and CEO - Bharti Infratel Limited

It's hard for me to comment about how competition is going to take this up, but I am sure they have similar challenges as we do. And we hope that they will embrace what we have taken as a step and we will be able to see value in that.

Kamaldeep - Moderator

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Thank you very much Mr. Malhotra. The next question comes from Mr. Vinay Jaising from Morgan Stanley, Mumbai. Mr. Jaising you may ask your question now.

Vinay Jaising - Morgan Stanley - Mumbai

Firstly, congratulations on this big move on the rate card. I have two questions. The first one is a little long and on the rate card. You mentioned that's applicable from April 1 of this year, so is it fair to assume whatever was available on March 31 of last year that has gone up by 2.5% already for new tenants and subsequent to this, should we assume that those operators who are tenants post 2022, even their rate card has gone up? That is my first question. Should I wait for my second, or should I ask it?

Akhil Gupta - Chairman - Bharti Infratel Limited

No, why do not we answer the first question. The construct, Vinay, is that the new rate card, obviously I can only put it to work for new tenancies or the new collocations, which customers seek. So these new rate card will be applicable there. And as far as the old ones are concerned that's where we said we have rationalized certain escalation charges, the impact of which was 15 crores a month. So the new rate card applies to all new collocations and it will apply henceforth to all new collocations for everyone.

Vinay Jaising - Morgan Stanley - Mumbai

So sir, is it fair to say that if earlier we were, let us say, at 30,000 till March, 31 for the new tenants, so now these new tenants which are 1,500 odd in number, they would be paying 30,000 times 1.025 already for this quarter? So the applicability has already happened?

Akhil Gupta - Chairman - Bharti Infratel Limited

I do not know where exactly from which date, but yes, broadly that's the construct.

Vinay Jaising - Morgan Stanley - Mumbai

So this year itself the growth has happened on the new rate card?

Akhil Gupta - Chairman - Bharti Infratel Limited

Yes.

Vinay Jaising - Morgan Stanley - Mumbai

Sir, secondly, you mentioned 2022, all those tenants who are existing and who are going to be coming up for renewal up to 2022, we would be freezing their rates till the new tenants go to that rate or till rationalization occur. Now how many tenants would that be of our total size of what we have existing?

Devender Singh Rawat - Managing Director and CEO - Bharti Infratel Limited

Hi Vinay, DS this side again. First, the rate card is going up by 2.5% for the base rate for all operators. Second, the freeze is an option that has been given to the operators to choose from. So you get a freeze provided you get an extension up to 2022. There could be operators, particularly the smaller lot, who could probably choose not to exercise this freeze. So it's a hard number to give right now to you. Depending on how all operators have signed up for this, we will be able to come back maybe and looking at internal numbers of what this means. And third, this is also a progressive number. A freeze for just one year for someone who has come as a tenant last year would

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probably bring him at par in the subsequent year with the rate card there too. So this is for each operator. Besides the headline rate card itself moving up by 2.5% every year, there is an option that has been given to all the operators on a non-discriminatory basis to choose from.

Vinay Jaising - Morgan Stanley - Mumbai

The reason I'm asking, and I'm sure my other colleagues will also be trying to gauge at is, how much is now the 2.5%, not for the new tenants which Akhil has already said, they will be applicable to higher rate. How much of them would be also coming up incrementally for growth that was why I was asking that. But I can wait for a quarter. The second question is on the longer term, what are you seeing as your incremental net adds for tenancies and how much is your loading as percentage of your monthly rentals today?

Devender Singh Rawat - Managing Director and CEO - Bharti Infratel Limited

So again, Vinay, we said we do not give guidance, but we are hopeful that with the spectrum auction and with this consolidation scenario behind, continuing data growth, we still think we will remain in the percentage growth that we have seen in the past. So, we do not see that fundamentally changing. We are happy with the data growth that's happening there. Consolidation, as we said, in the long run, we believe is very positive for us. So I would leave that there without making specific guidance on numbers going forward. We still think tower growth at low-single digit and tenancies at high-single digits is something that we'll look forward to as a growth for numbers there. Loading specific, I do not think we have given this in the public domain, so let me check with my CFO. I do not think it's in any of the numbers. So I would not be able to give you loading as a percentage of my overall revenue, but it's not a large amount of money, that's what I could put there. You can see that from revenue per tenant and revenue per tower numbers. And also, you know the GBT, RTT mix, so one could make a fair assumption. These numbers are not very large numbers.

Kamal Deep - Moderator

Thank you very much Mr. Singh. The next question comes from Mr. Sachin Salgaonkar from Bank of America, Mumbai. Mr. Salgaonkar you may ask your question now.

Sachin Salgaonkar - Bank of America - Mumbai

Thank you for the opportunity. My first question is, Akhil, you did mention that the freeze option is available on a non-discriminatory basis. So let's say, if I'm number one, number two and number three tenants on a tower, is that freeze option available to all of the tenants right now?

Akhil Gupta - Chairman - Bharti Infratel Limited

Yes, to everyone.

Sachin Salgaonkar - Bank of America - Mumbai

So, which means, let's say, Bharti, Vodafone, Idea, all of them say that from tomorrow onwards I want my rentals to be freed, and in return, obviously, they will get an extension, so is that a fair way to look at it?

Akhil Gupta - Chairman - Bharti Infratel Limited

That's a fair to look, except that the freeze is available till the escalations catch up with the rate card.

Sachin Salgaonkar - Bank of America - Mumbai

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And how do we know.

Akhil Gupta - Chairman - Bharti Infratel Limited

Thereafter the escalations, which is the new rate card, whatever is the rate will continue.

Sachin Salgaonkar - Bank of America - Mumbai

And what is the new rate card? So the way to look at it is, please help me understand that every tower has a different mix of guys who was coming at tower at different types. So, at what level will it catch up with rate card? It is perhaps possible that it is not possible for the number one guy to catch up with the rate card, unless and until he is given discounts. So in that scenario, are discounts the one option you guys are looking at?

Akhil Gupta - Chairman - Bharti Infratel Limited

Yes. As I mentioned, there is a rationalization of these escalation charges with does include some of those to equate it and to make it NPV neutral. But to answer your question, just to give you an example, if on a single tenant it was 30,750 in year one and 31,500 or 31,600 in year two, it cannot be generalized, because it depends on when this particular tenant come on the tower. So if somebody came in one year, it will catch up in one year itself. It will be frozen only for one year. If somebody came for four years, it will be caught up in four years and so on.

Sachin Salgaonkar - Bank of America - Mumbai

Akhil, the other thing you mentioned is there is no real impact on numbers on 2016-2017, but from what we said, we do see a decent amount of impact post FY 2019 and onwards, simply because of a lot of contracts are coming for renewal. So, is that the earnings would not be impacted after that, because on my calculation I do see a bit of an impact on those years?

Akhil Gupta - Chairman - Bharti Infratel Limited

Yes, I think it depends on what you want to see, because when they were to come up for renewal, the moot point and the open point would have been as to at what rate would the operators renew. Now, obviously at this point of time, in the absence of what we have done now, which makes it very clear that whatever is the rate card that is the expected rate at which renewals will take, it was like taking a new tenancy. But if under the earlier scheme the new tenancy was at the base rate of 30,000, the dispute would have been at what rate does it get renewed, so that one has now been completely settled.

Sachin Salgaonkar - Bank of America - Mumbai

Akhil, what really happens at a reset year, let's say, 2022, so what exactly happens as a sort of base rate card at that time. Is that 33,000?

Akhil Gupta - Chairman - Bharti Infratel Limited

2022, whatever is the base rate as per the rate card, there is no base rate now, there is a rate card, which applies every year. So whenever anybody's renewal comes up that is the rate card and that is the rate at which the renewal happens.

Sachin Salgaonkar - Bank of America - Mumbai

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Akhil, last question in this direction is, how should we look at your EBITDA margins? I mean, last call you did say that it's best to assume that they do not grow and have a flattish outlook. Is there a risk that the margins may go down at least in the interim till 2022, because of this structure, because of discounts and freezing of rentals?

Akhil Gupta - Chairman - Bharti Infratel Limited

You have already seen in this quarter whatever impact was there and as you can see, it's not material. So I would not say they will go up, I won't say they will go down. They could move a little bit, but in terms of materiality either way, it would be not there.

Sachin Salgaonkar - Bank of America - Mumbai

Got it thank you.

Kamaldeep - Moderator

Thank you very much Mr. Salgaonkar. The next question comes from Mr. Viral Shah from Credit Suisse, Mumbai. Mr. Shah you may ask your question now.

Sunil Tirumalai - Credit Suisse - Mumbai

This is Sunil from Credit Suisse. Sir, just going back again to the renewals, I think a lot of questions because it's something which it's important for us to understand. So firstly, is this a system that is applicable across both Infratel and Indus?

Akhil Gupta - Chairman - Bharti Infratel Limited

Yes.

Sunil Tirumalai - Credit Suisse - Mumbai

And so long-term focused incumbent operators who have contracts coming up for renewal up till 2022, we would expect across Infratel and Indus to have taken up this option as of April 1?

Akhil Gupta - Chairman - Bharti Infratel Limited

As you mentioned yourself, it is an option, so I cannot say. Likelihood is they will take, because they will get some benefit, but it's an option, they have to decide.

Sunil Tirumalai - Credit Suisse - Mumbai

And I would like to keep out the accounting change from an NPV discussion, because that's has no role to play in deciding whether a transaction is NPV neutral or not. Now you are in effect for a particular operator on a tower giving freeze on rentals for the next, let us say, four years, or like six years. And at the end of it, he will be transitioning to a base rate as of that date. Now clearly over the next six years you are giving away some value as per status quo, because you are not charging those renewals, I mean charging those escalations. So do you mean to say that at the end of it, he is going to jump up to a fairly high rate for you to get back the NPV?

Akhil Gupta - Chairman - Bharti Infratel Limited

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Well, I cannot give you the exact calculation NPV on this call, because that obviously is a very long thing. But all I can confirm is that without the impact of transition to Ind-AS on pure accounting format, it will be NPV neutral.

Sunil Tirumalai - Credit Suisse - Mumbai

I'm sorry, so without the accounting changes

Akhil Gupta - Chairman - Bharti Infratel Limited

The impact of the accounting change due to transition to Ind-AS, the NPV neutrality would apply.

Sunil Tirumalai - Credit Suisse - Mumbai

But is my understanding correct that to make it NPV neutral you have to see a fairly sharp jump in the rental for the operator at the end of 2022?

Akhil Gupta - Chairman - Bharti Infratel Limited

That is the scheme of this rate card. At the end of whenever anybody renews, whatever is the rate card that is supposed to apply. Not just 2022, but at any point of time. What fundamentally has been done is that any new tenancy which comes up, or a renewal which comes up will be equated now.

Sunil Tirumalai - Credit Suisse - Mumbai

And just hypothetically, let us say, a tenant a potential tenant walked up to you on March 31 of this year, versus say, walking up to you on April 1 of this year, what is the change in rate that you would have given?

Akhil Gupta - Chairman - Bharti Infratel Limited

2.5%, that's the rate card change.

Sunil Tirumalai - Credit Suisse - Mumbai

But this rate card was not existing on March 31, because it's a new system.

Akhil Gupta - Chairman - Bharti Infratel Limited

March 31 has already gone. Whoever had come, had come at the earlier rate.

Sunil Tirumalai - Credit Suisse - Mumbai

No, I just wanted to understand what is the continuity wise what is the change that would have happened for a new customer coming in?

Akhil Gupta - Chairman - Bharti Infratel Limited

We had 2.5% increase after April 1.

Bharti Infratel Limited First Quarter Ended June 30, 2016 Earnings Conference Call**Sunil Tirumalai - Credit Suisse - Mumbai**

And I see that moving on to other topics, I see that the employee base in Indus has been kind of rising sharply last few quarters. It went up earlier and for last two quarters it's kind of remained stable. What has driven that and that's also caused the employee cost to go up. I mean, should that stabilize going forward, what's happening over there?

Devender Singh Rawat - Managing Director and CEO - Bharti Infratel Limited

Indus had done some amount of in sourcing. They rely on a model where the partners do most for the field maintenance. There are some geographies where they had taken in some of these people on their own headcount and that's one of the reasons why you see that change. Also, in terms of government acquisition they had built up some teams given the call quality requirements, they were focusing on building some acquisition strength around acquiring government land. I think, and I do not know Akhil if you want to add on that. I think the hiring that was to be done, has already been done from their standpoint.

Akhil Gupta - Chairman - Bharti Infratel Limited

Yes, I think, as I recollect, they are evaluating the benefits of getting some of these people in sourced. So there will be some changes, but nothing which one needs to be bothered about. Because even if these numbers increase here, the expenditure on outsource will come down, so it will kind of compensate.

Sunil Tirumalai - Credit Suisse - Mumbai

And that would you have any outlook for what you see in terms of CapEx for the year?

Akhil Gupta - Chairman - Bharti Infratel Limited

Sorry, we do not give the outlook. In our business, the CapEx is based on the orders. And therefore, it's very dynamic. All I can give you the guidance is that if the demand was to jump 10 times, we are prepared for it.

Sunil Tirumalai - Credit Suisse - Mumbai

And sorry, if I may slip in one last question. The 15 crores, the difference that you're talking about in the new system, is that a number that's valid only for this year based on all the operators who have chosen the new option as of April 1, or is that a number that could go up depending on more guys coming in over time?

Akhil Gupta - Chairman - Bharti Infratel Limited

No. This will not be going up. This cannot go up. It will vanish over a period of time. But it would suffice to say that as far as now the accounts are concerned and going forward they're going to be on Ind-AS, whatever is the figure here, please treat it as a base, and this is how the business will grow in the normal course now.

Kamaldeep - Moderator

Thank you very much Sir. The next question comes from Mr. Srinivas Rao from Deutsche Bank, Singapore. Mr. Rao you may ask your question now.

Srinivas Rao - Deutsche Bank - Singapore

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My first question is on tenancy growth, which has kind of come off in the last couple of quarters and came at about 6% this quarter. And now, as you said, there have been some cancellations, which probably would have impacted. Ex of the smaller players, would it be fair to say that the tenancy demand from the larger incumbents or your larger customers has been stable? So that would be my first question.

Devender Singh Rawat - Managing Director and CEO - Bharti Infratel Limited

Srinivas, Rawat this side. I had mentioned in the previous question too that operators continue to roll out more aggressively on 3G, 4G and I also mentioned that there is a possible hold back of rollout on account of forthcoming spectrum auctions. Again, the big focus seems to be on data side and of course whatever sites needed for building in capacity and quality that they continue doing there too.

Srinivas Rao - Deutsche Bank - Singapore

My second question is on this rate card approach, which you have indicated and obviously it's also a good solution for the issues which you face. But a permanent 2.5% increase every year for I do not know for till what time basically means a pricing which is not linked to any demand-supply situation in the industry. Is that how we should think about it?

Akhil Gupta - Chairman - Bharti Infratel Limited

There is a permanent inflation in the world in most of the developing countries, which is permanent. So even under the previous method there is a 2.5% escalation on the same basis. Fundamentally there is no change as far as the increment or the increase is concerned.

Srinivas Rao - Deutsche Bank - Singapore

And just to clarify, this increase is I mean, there is no sunset clause to this, right? I mean this is what you would expect to take every year?

Akhil Gupta - Chairman - Bharti Infratel Limited

Yes.

Srinivas Rao - Deutsche Bank - Singapore

Thank you, I will come back for more questions Sir.

Kamaldeep - Moderator

Thank you very much Mr. Rao. The next question comes from Mr. Vaibhav Goyal, SBI Life Insurance Mumbai. Mr. Goyal you may ask your question now.

Vaibhav Goyal - SBI Life Insurance - Mumbai

Sir, two things. Still I'm not able to understand this NPV neutral part. And second thing when you said that on the loading part, there you have asked for decongestion. So how would that work and whether that will increase some tenancy there?

Akhil Gupta - Chairman - Bharti Infratel Limited

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No, let me clarify. As far as the NPV is concerned, obviously with this increase of rate and these are the same operators ultimately will also bring in the new business. So what we had calculated was that with this increase over the next say five years, versus that there should be NPV neutrality. So that is what the NPV neutral is about. On loading, we are not forcing anybody to de-load, we cannot under the contract, but we have made some changes to encourage them by using latest equipment, which is smaller in size or smaller in power rating to try and vacate some space, because by doing so, our chances of getting an additional tenant increases. So it's not that we are forcing anybody or somebody is under an obligation to de-load, but we are providing some incentive to people to de-load, so that we can bring in more and this is particularly true in case of sites in the big cities where there is big demand.

Vaibhav Goyal - SBI Life Insurance - Mumbai

So by any chance, the total number of tenancies which a tower can handle and with the loading part that reduces with all these things?

Devender Singh Rawat - Managing Director and CEO - Bharti Infratel Limited

Typical towers, we said there is a certain area of equipment that it can handle on top of the tower and given the space constraints, the amount of area that you can occupy on the floor, particularly on rooftops where there are constraints on area. With 2G, 3G, 4G kind of progressive technologies coming in, with fiber, more microwave coming in in-site, the operator requirement for this incremental loading is going up. So our idea is to see that we incentivize people to remove some equipment too. In some city sites, this could be limiting for growth of tenancies. And as Akhil said, mostly in the city areas where there is growth happening on account of 3G and 4G, so now there is an incentive for an operator to remove equipment. Earlier there was no incentive for an operator to take out and put new generation equipment or more compact equipment or reengineer his network. So, these are more technical solutions given to operators, so that it frees up space on the top of the tower, on the floor of the tower, and also in terms of power consumption there. So all three aspects together.

Vaibhav Goyal - SBI Life Insurance - Mumbai

Thanks, that is all.

Kamaldeep - Moderator

Thank you very much Mr. Goyal. The next question comes from Mr. Sanjay Chawla from JM Financial, Mumbai. Mr. Chawla you may ask your question now.

Sanjay Chawla - JM Financial - Mumbai

Good afternoon. Thank you for the call and also a fantastic set of disclosures. I wanted to clarify two things. This 150 million number that you have mentioned, the monthly impact, is it something, which is already reflecting, which means is this 45 crores impact already reflecting into first quarter and your revenues have been rebased according?

Akhil Gupta - Chairman - Bharti Infratel Limited

First of all, thank you very much Sanjay for complimenting my team on the disclosure, because as you know, it's extremely important for us that we come out with disclosures and complete details which are absolutely clear to our investors. So what I would request through you to all our other investors is, if you have any suggestions for making it more useful to you, please do come back to us. We are committed to making them as smooth and as understandable for you as possible. On the second one, yes, this 15 crores a month impact is already taken into the accounts here. And of course, as I'd mentioned in my speech, because of the Ind-AS primarily, the impact is going to be negligible.

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Sanjay Chawla - JM Financial - Mumbai

So revenues would have been if this adjustment to MSA had not been done, your sharing revenues would have been higher by 45 crores this quarter. Is that correct?

Akhil Gupta - Chairman - Bharti Infratel Limited

Yes, that's correct.

Sanjay Chawla - JM Financial - Mumbai

So, obviously this estimate of 15 crores per month, it assumes a certain percentage of your tenants have taken the option of getting their rentals.

Akhil Gupta - Chairman - Bharti Infratel Limited

We have assumed all of them will take.

Sanjay Chawla - JM Financial - Mumbai

So assuming all of them take, this is the maximum impact in terms of.

Akhil Gupta - Chairman - Bharti Infratel Limited

Yes.

Sanjay Chawla - JM Financial - Mumbai

So, this is essentially an adjustment to the historical escalation which we have done, right?

Akhil Gupta - Chairman - Bharti Infratel Limited

Because of freezing, some of this is what could have come. We are comparing this INR15 crores versus IndGAAP. So, what could have escalated is also into this account. I think from your point of view, what you I would recommend is what you should keep in mind is that this 15 crores a month, which we have said, which is 180 crores or so per year is the figure. This is not that it will increase.

Sanjay Chawla - JM Financial - Mumbai

So assuming whoever has to take will take it, based on that?

Akhil Gupta - Chairman - Bharti Infratel Limited

Yes, I am assuming that everybody will take it.

Sanjay Chawla - JM Financial - Mumbai

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And obviously, this I guess, this number 15 crore, so is this designed in such a way the historical escalation that you've kind of reduced the rental to that extent. Is it designed to ensure that all the rentals for all the tenants converge to your rate card by -- latest by FY22?

Akhil Gupta - Chairman - Bharti Infratel Limited

More or less, I would say. I cannot say 100%, but yes, practically all of them should converge by March 31, 2022. That's generally the plan.

Sanjay Chawla - JM Financial - Mumbai

And just the last thing, we are still seeing some tenancy losses and exits happening. Can you give us a sense in terms of more on an immediate basis, what kind of how many tenancies one should look at in terms of which are addressed? And particularly, I am looking to these operators like Videocon, of course, then Uninor and probably the Aircel, RCOM, from your point of view.

Devender Singh Rawat - Managing Director and CEO - Bharti Infratel Limited

Sanjay, we have said this earlier, 85% of our revenue is coming from the top three. We only see them becoming bigger in this consolidation scenario. So we do not see a large risk on account of this. Operator specific, you following them on the news there, Videocon has been taken in the last quarter. That's the number that you see there. Anything else that happens on these scenarios I have said, we expect that these people will actually redeploy a lot of that equipment that comes in from an expansion mode. So operator specific, we do not want to comment about specific operators there. But we have a very limited risk of this consolidation that is to come in from relative terms with as compared to other IP ones there. And as I said, we see this as a long-term positive too. We will give the resources in the hands of people who can use this for expansion and competing with the leaders, which is also where our towers are more suited for someone to roll out.

Sanjay Chawla - JM Financial - Mumbai

So, DS, can we at least assume that the circles where RCOM had to shut down and Videocon exit that is fully reflecting in the tenancy losses that you have reported so far?

Akhil Gupta - Chairman - Bharti Infratel Limited

Sanjay, I think it's not proper for us to be commenting on any individual customer of ours, because I would not like to disclose as to which operator, how many did they exit and so on so forth.

Sanjay Chawla - JM Financial - Mumbai

Thank you very much and all the best.

Kamaldeep - Moderator

Thank you very much Mr. Chawla. The last question comes from is Amruta Pabalkar from Morgan Stanley, Mumbai. Mr. Pabalkar you may ask your question now.

Amruta Pabalkar - Morgan Stanley - Mumbai

Thanks for the opportunity. I had a question on the core margins, which you commented some time back.

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Devender Singh Rawat - Managing Director and CEO - Bharti Infratel Limited

Amruta, this is D.S. Rawat. We cannot hear you properly, if you could just get closer to the mic, that will be a help.

Amruta Pabalkar - Morgan Stanley - Mumbai

Sorry. I had a question on the core margins, which you said would be largely flat going forward. Could you kindly tell us with tenancy and loading going up, why would not the core margins move to say 75% or 80% as your tenancy goes to 3x?

Pankaj Miglani - Chief Financial Officer - Bharti Infratel Limited

There are always some expenses involved whenever there is an increase in business, but I think DS can answer this better.

Devender Singh Rawat - Managing Director and CEO - Bharti Infratel Limited

So, first, I think, the tenancy ratio of 3, my guess is, the time we need there will probably have those kind of things. We have got a large base, you should look at that in terms of large base improvements on EBITDA margins will incremental EBITDA margins is going to have, and given the discount structure of higher tenancy rates coming in at a slightly lower rate is also something that kicks in. So, 70% to 75% at 3 tenancy ratios in theory, yes, it should be somewhere around those ranges.

Akhil Gupta - Chairman - Bharti Infratel Limited

But it's too far off, very hypothetical at this stage.

Amruta Pabalkar - Morgan Stanley - Mumbai

So, say, if you are inching up by around 0.2x every quarter, we should see some margin inch up of around 10 bps to 20 bps come in, very roughly, would that be a fair statement to make, if you were to go by that theory?

Pankaj Miglani - Chief Financial Officer - Bharti Infratel Limited

Do not look at that on a quarter-on-quarter basis. My view, if you do that comparison on year-on-year basis, you will see something hitting closer to the number that you have said there.

Akhil Gupta - Chairman - Bharti Infratel Limited

But I would strongly advise, Amruta, you and all other investors, I think the best is to assume that these margins are sustainable, which are good margins. And if something happens in terms of increased margin, I think treat that as a bonus.

Amruta Pabalkar - Morgan Stanley - Mumbai

Thank you Sir.

Kamaldeep - Moderator

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Thank you very much Ms. Pabalkar. I now hand over the call proceedings to Mr. D.S. Rawat for the final remarks.

Devender Singh Rawat - Managing Director and CEO - Bharti Infratel Limited

So thank you very much. As Akhil cited, the quarter saw two major developments, Ind-AS reporting and MSA amendments. We covered that in fair bit of detail today. The quarter saw consolidated revenues at 3,211 crores and net profit of 756 crores, a jump of 71% year-on-year. Leading operators continue to expand their 3G and 4G footprint by expansion of existing sites and the addition of sites. Overall, we expect this year to be a year of consolidation and data growth for the operators. Despite consolidation, we continue to see the demand for new towers remain in the range of 2% to 4%, while colocations to be in the range of 6% to 8%. We expect the positive momentum to continue with new spectrum auction, which is due in Q2 financial year 2017 and increased focus on full colocations as operator would want to improve service quality going ahead. During the quarter, we also we have also participated in Bhopal Smart City Tender and would be participating in other similar tenders. We are best placed to play a key role by building and sharing vital infrastructure solution with all customers on a non-discriminatory basis. We believe that we are fully geared to meet customer demands and capitalize on emerging opportunities. On behalf of entire Bharti Infratel team, I thank you all for your continued support and look forward to an exciting journey ahead of us. Thank you very much.

Kamal Deep - Moderator

Thank you Sir. Ladies and gentlemen, this concludes the conference call. You may now disconnect your lines. Thank you for connecting to audio conference service from Airtel and have a pleasant evening.