

Telecom Update: March 2020

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The report details about the ARPU trend in the Indian telecom industry and throws light on the critical AGR issue and the payments associated with it.

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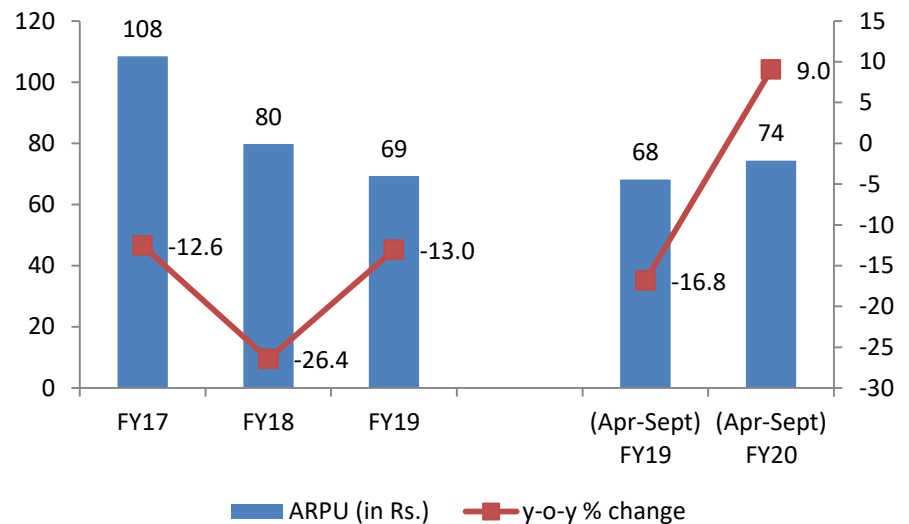
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Trend in industry ARPU

The telecom industry’s Average Revenue per User (ARPU) has been on a declining trend in the past 3 years from FY17 to FY19. It fell on a y-o-y basis in each of the quarters during these 3 years except for the June 2016 quarter where it remained flat. The scenario nevertheless saw an improvement after a gap of 3 years as the ARPU averaged 9% higher to Rs.74 during April-September 2019.

Chart 1: Trend in industry ARPU (in Rs.)



Source: TRAI, CMIE

This ARPU though is much lower than the average ARPU of Rs.124 during FY16 when Reliance Jio had not entered the telecom market. The industry is believed to have maintained the upward ARPU trend in Q3FY20 as telcos had hiked tariffs up to 40% for its prepaid users from the month of December 2019 onwards. The impact of the rate hike though will be seen entirely in Q4FY20. **Thus the industry ARPU is expected to go up by 12%-14% to Rs.78 to Rs.79 during FY20.**

Even while the industry ARPU is expected to improve going ahead, the challenge for industry will remain on AGR front. In fact, the prime reason that prompted the hike in prices was the acceptance of new definition of AGR by the Supreme Court in October 2019.

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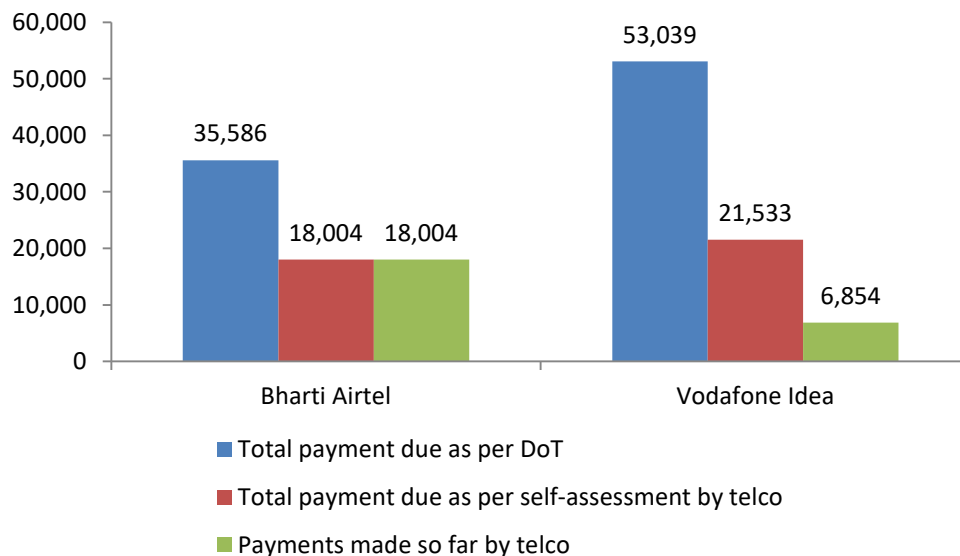
The AGR issue

The AGR issue started on 24 October 2019 with the Supreme Court supporting the DoT’s definition of AGR for telecom industry. The DoT said that the AGR should comprise dividends, handset sales, rent and profit from the sale of scrap, besides revenue from services. The telcos however demanded that the definition should be restricted to only core telecom services. The issue with respect to definition of AGR dates back to year 2005. The telecom companies have to pay license fee and spectrum usage charges (SUCs) to the government. These charges are certain percentage of the telcos’ revenues and higher revenues of telcos implies more payment of license fees and SUC. As per the current norms, the telecom companies pay 8% of the adjusted gross revenues as license fee and 3-5% of the adjusted gross revenues as spectrum usage charges.

Resultantly, the incumbent telcos were asked to pay around Rs.1.33 lakh crore to the government (Rs.92,000 crore as license fees and Rs.41,000 crore as SUC.) This payment includes principal, interest and penalties and the telcos were given 3 months’ time to make the payments by 23 January 2020. Post this announcement, the two large incumbents posted significant losses in the September 2019 quarter as they accounted for these charges as exceptional items in their respective results. Also, both the telcos mentioned about their concerns to run the business.

Subsequently in November 2019, the DoT provided an option to the telecom companies to defer payment of the spectrum auction installments due for 2020-21 & 2021-22, either for one or both years. These deferred amounts will be spread equally in the remaining installments to be paid by telcos. Interest as stipulated while auctioning of the concerned spectrum will however be charged so that NPV is protected. However, the announcement did not provide much relief to the telcos. With no major assistance given by the government, the incumbents defaulted on the timeline of 23 January and pinned their hopes on self-assessment of AGR liabilities as directed by DoT. Post assessment, the liabilities estimated by the government and the incumbents had a huge difference as shown in the chart below.

Chart 2: Stock of AGR payments of the large incumbents (in Rs. Crore)



Source: Respective companies’ press release

Note: Total payment due as per DoT includes outstanding SUC dues as on October 2019 and provisional license fee as per demand up to July 2019. Self-assessment for Bharti Airtel is for the period FY 2006-07 onwards up to December 2019 and interest thereon up to February 2020 and self-assessment for Vodafone Idea includes principal for the period FY 2006-07 to FY 2018-19 and interest up to February 2020.

The DoT estimated Rs.35,586 crore as dues for Bharti Airtel and the company on self-assessment claimed the dues at Rs.18,004 crore for which it has made the entire payment. The payment estimates by DoT for Vodafone Idea were at Rs.53,039 crore. However Vodafone Idea claimed their dues at Rs.21,533 crore. Of this, the company made payment of Rs.6,854 crore. Thus it can be seen that both the companies' self-assessment dues were quite lower than the claims of DoT which gave rise to another dispute. While Bharti Airtel's self-assessment amount was about 50% lower than the DoT's claims, Vodafone-Idea's self-assessment number was around 60% less than the claims made by DoT.

Considering stress in the industry and various pleas of the incumbents, the DoT proposed to the SC that the telcos be allowed to make the payment of license and spectrum dues in a staggered manner over a period of 20 years with an annual interest rate of 8%. However, this proposal was straight away rejected by the SC on 18 March 2020. The SC also mentioned that no self-assessment of AGR dues will be allowed and the telcos will have to make the payments as per the judgement given by the SC on 24 October 2019. **After this decision, the incumbents continue to face headwinds and will stand at the same position as they were when the new definition of AGR was accepted.**

Given the critical situation of the industry, the government's ambition to launch 5G in India in near future looks challenging. The incumbents that are battling the tough situation of AGR payments are likely to move at a slow pace with their investment plans towards 5G with the current low level of ARPU. The average ARPU now stands at Rs.74 (during April-September 2019) compared to that of Rs.124 in FY16 when the industry was getting 4G ready. Also, the reserve price suggested by TRAI for bands that could be used for deployment of 5G technology did not find much support from the industry due to its higher price.

Concluding remarks

- The industry is believed to have maintained the upward ARPU trend in Q3FY20 as telcos had hiked tariffs up to 40% for its prepaid users from the month of December 2019 onwards. The impact of the rate hike though will be seen entirely in Q4FY20. The industry ARPU is expected to go up by 12%-14% to Rs.78 to Rs.79 during FY20.
- Even while the industry ARPU is expected to improve going ahead, the challenge for industry will remain on AGR front.
- The government's ambition to launch 5G in India in near future looks challenging as the industry finds no respite with the AGR issue, the low ARPU level scenario and financial difficulties that hinders the pace of investments by incumbents towards 5G.

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