

Idea-Vodafone Merger-Post Merger integration

Shivani Soni

JIMS,sector-5,RohiniDelhi-110085

Abstract:

This research work focuses on the merger deal which happened between Telecommunication companies Idea cellular and Vodafone India. The deal was officially announced on 20th March 2017 for total of \$23 billion. This merged created a combined entity which had an enterprise value of \$23.2 billion. The merger changed the market dynamics entirely and Idea-Vodafone became market leader with maximum number of subscribers and left Airtel on second position. Airtel was the market leader in Indian telecom market for 15 years consecutively with 320 million subscribers by 2017. The merger deal took place due to various reasons but major reason behind this deal was entry of reliance Jio.

With this research paper, I tried to explain what led to these mega telecom companies to merge with their competitor and what impact this merger had on Indian telecom market. I have also laid down all the essential details regarding the deal and explained the rationale behind the merger.

With this study, I have drawn a conclusion on Vodafone-Idea merger and also provided recommendation to telecom companies which might go for mergers and acquisitions later in the coming years.

Keywords: IDEA, VODAFONE, MERGER POST MERGER ANALYSIS

I. INTRODUCTION

Telecommunication was a booming sector till 2016, market had ample of players and subscribers were distributed among those players. Companies competing at that pint of time were Airtel, Idea, Vodafone, Reliance communications, BSNL, Telenor, MTS, Airtel, and MTNL. In September 2016, Events took a turn when Reliance Jio entered the telecom market with the investment of \$25 billion in 4G services in India. Jio offered free voice calls and internet services at prices below the prevailing market price. With Predatory pricing strategy Jio managed to take the 100 million subscribers as well as gained 6 percent of the market share.

Reliance Jio was taking subscribers from other market players with its market strategy and was creating adverse situations for them. Due to loss of subscribers, telecom companies started mounting losses and ended up taking heavy debt. Increased competition and worsening market situations made other

players also started following Jio's path and reduced their prices as well. Companies such Telenor, MTS, Airtel, and MTNL planned to exit the telecom industry for survival as they could not slash their prices below prevailing prices and some even planned for business combinations.

This situation resulted in concentrating the market, as by the end of 2017, almost 90% of India's wireless market was being controlled by five companies i.e. Airtel, Vodafone, Idea, Reliance Jio, and BSNL. Companies with large subscribers and huge capital structure also started having losses and ended up planning new strategies for survival in the market. Two most affected companies Idea and Vodafone came together to fight Jio in the market. Before Reliance Jio entered the market, Idea Cellular Limited had the third largest subscriber base in India whereas Vodafone India was the second largest player of the Indian Telecom Industry in terms of subscriber base. It wasn't only the monetary losses, Idea and

Vodafone were constantly losing their subscribers as well as market share. This led to the management of both the companies to rethink their business model and to formulate strategies for their survival.

The merger was officially and jointly announced by Idea and Vodafone on March 20th, 2017 of US \$ 23 billion to become world's second-largest company. The entire process of merger took 24 months to complete and on September 2020 Vodafone-Idea rebranded itself as VI. This merger did not only create a telecom giant, but it also had implications for the industry as well as consumers and it pushed more merger moves in the telecom sector.

Overview of the companies

IDEA: The company Idea Cellular Ltd was formed in the year 1995 to provide telecommunication services with the name of Birla Communications Ltd. The company started providing services in Gujrat and Maharashtra after obtaining the license from DOT in the same year. Later the name of the company was changed from Birla communications to Birla AT&T communication as both the companies entered a joint venture in 1997. Following this, three years later company again merged with Tata cellular to capture the larger market share. In the same year company was rebranded as Idea Cellular. Later in the years Idea cellular acquired companies such as Swinder Singh Satara & Company Ltd, Escotel Mobile Communications Ltd. In the year 2006, Tata took out its shareholding from Idea cellular and applied for a new license to DOT and Idea Cellular became the part of the Aditya Birla group. By the year 2016, Idea Cellular became third largest telecommunication service provider with huge subscriber base.

VODAFONE:

History of Vodafone India dates back in the year 1994, a joint venture between Hutchison Whampoa and the Max Group obtained license from DOT to provide telecommunication services in Mumbai circle. The company was with the name of Hutchison Max Telecom Ltd. (HMTL). It

started providing services in Maharashtra state within Mumbai circle with the name of Max Touch. Later HMTL was rebranded as Hutchison Essar Limited (HEL). In 2006, Vodafone acquired Essar Spacotel — A subsidiary of Essar Group and expanded its services in other states of India.

With large network distribution and quality services, HEL started targeting high end Indian customers for its postpaid services and ended up capturing huge market share. In 2007, the company announced to sell 67% of the shareholding and loan interest for \$11.1 billion to Vodafone Group PLC. The acquisition of HEL by Vodafone was completed in May, 2007. The company also faced controversy over this merger as they were prosecuted for tax dispute of \$2.5 billion with Indian income tax department. In 2011, when government announced 100% FDI in telecom sector, Vodafone PLC bought out ESSAR's shareholding and established full control over its operation. At the time of merger with Idea cellular was announced the company had 28 million subscribers pan India.

Overview of the Telecom industry:

Indian telecom sector has been crucial part in growth of GDP in the country. As growth of telecommunication and internet services is correlated to GDP growth in any country, and in India growth in telecom sector has been exemplary. The market was expected to see the growth of 10% annually and to be valued at \$103 billion in the year 2020. Contribution of Telecom sector in 2019 was 6.5% and expected to cross 10% by 2025. The subscriber base of internet services is expected to reach 829 million by the end of year 2021.

Currently India ranks second in the world in terms of subscriber base of 1,173.83 million as on December 31, 2020. The gross revenue in the FY 2021 first quarter stood at US\$ 9.35 billion. Considering the reach of telecommunication services in rural parts of India, 500 million new internet users will add on to the customer base over the next five years. As per reports of TRAI. In India every subscriber was using 11 GB data per month on an average in the year 2020. Government policies and initiatives has played crucial role in growth of telecom sector in the country. Specifically, 100% FDI and easier norms have made the telecom sector fastest growing sector as well as top employment generator in India. Back in 2016, telecom market had top six companies

having large market shares. Those companies were Airtel, Vodafone, Idea, Aircel, Reliance Communication, and BSNL and Airtel was the market leader with the market share of 24.3% followed by Vodafone and Idea.

Telecom services started in India back in 1995, which enabled wireless communication through paper. This had brought evolution in long distance communication. The first telecom service via mobile started on 15th august, 1995 in capital city of India Delhi and on the same day internet was introduced to the common public. In 1997, Government decided to set up a policy maker and regulatory body named Telecom Regulation Authority of India (TRAI). In 2000, Department of telecommunication started providing license to private players after government's decision to liberalize the norms for license obtaining process.

CONCEPTUAL BACKGROUND:

A Merger takes place between two companies willing to undertake an agreement to incorporate a single company and operate together with combined capital structure and assets, there are various reasons for merger to take place. Major reason for merger to occur is expand market share, increase capital, Increased investment capacity, business diversification, technological collaborations. During merger, management make sure to create value for shareholders and safeguard their rights. Merger can be of two type, horizontal mergers, and vertical mergers.

Merger usually takes place to fulfill certain objectives and both the party to a merger needs to provide congruence at those objectives to conclude a merger deal. After management's decision, shareholder's approval is taken, and merger deal further proceeds. The merger which took place between Idea and Vodafone was a horizontal as both the companies belonged to the same sector. Also, as per deal specifics, it as merger of equals, as both the companies decided to have a equal shareholding rights in the merged entity. In this merger both the decided to merge their capital, debts and assets as well as sold off some of the assets in order to pay the spectrum fee to the DOT.

Earlier it was decided by Idea and Vodafone decided that both the brands will continue to

operate under their ongoing brand names. However, in September 2020, they rebranded themselves as "VI" Vodafone Idea Limited became a Pan-Indian integrated GSM operator providing 2G, 3G & 4G mobile services under brand names of Vodafone and Idea. Vodafone Idea merger created a wave across telecom industry of India. It was a strong reaction to the competition of Reliance Jio and Airtel. This gave way to a string of mergers and acquisitions by the rival companies to hold their position in the telecom sector. The merger also leads to a conversion of multiple telecom service provider industry into a three-fold competition between Vodafone-Idea Ltd, Airtel and Reliance Jio.

NOVELTY OF THE RESEARCH:

This research was done with the intention to analyse the post-merger effects on the company as well as industry. This study tries to gauge management's perspective at the time of the merger and analyses the fact if the objectives of the merger have been achieved or not. Majority of the research done so far on this topic only specify the reasons of the merger and doesn't elaborate objectives. This study is unique as it also comprises the impact the market had after the merger was announced and what is the current dynamics of telecom industry in India.

STATEMENT OF PROBLEM:

Entry of newplayer with mega capital investment changed the market dynamics so quickly that many companies couldn't even plan out their survival. Some decided to merge with one of the competitors to be able to survive the wave of predatory pricing which were washing out all the telecom companies. The purpose of this study was to find the impact of IDEA-VODAFONE merger on the market and analyse the post-merger scenario of the company.

OBJECTIVES OF THE RESEARCH:

The objective is to analyze top emerging mutual fund schemes by:

1. To examine the merger between Vodafone and Idea and the specifics of their deal.
2. To analyze the impact of the merger on the Indian Telecom industry.
3. To Study the financial performance of Vodafone-Idea post-merger

RESEARCH METHODOLOGY:

The Indian telecom sector is going through a transforming phase now-a-days, telecom operators are going for mergers and acquisitions to survive in the industry and many players have even existed the market due to cut-throat competition and heavy losses. Vodafone-Idea merger requires through study and analysis because this merger created a stir in the market and forced other market players to merge with big companies. This research project compiles the data for analyzing the Vodafone-Idea merger from 2016 to 2019. All the data has been extracted from the company's audited financial reports.

Research design:

In this study, analytical and descriptive methodology, which is based on the collection of facts and information, compare, analyze and interpret them to find solid conclusions have been used.

Sources of data collection:

Here in this Research Project Secondary Data is used data which are taken from published sources of

- Wikipedia
- Money Control
- Company Website
- News articles
- Published research papers

Data analysis - tools/techniques:

- Financial modelling
- Determination of financial performance post-merger
- Business Valuation and synergy calculation

Limitation of the study:

The study is based purely on secondary data which are taken from financial statements of the merging companies and from analytical reports available on therefore, there can be certain difference in conclusion in the reports available online.

Data analysis and interpretation:

The deal highlights:

The US\$ 23 billion merger deal between Idea and Vodafone, was post completed in August 2018, post its announcement in 2017. The deal was agreed upon in such a manner that both the companies get the equal shares in the new merged entity. As the agreement, Vodafone PLC combined its Indian subsidiary Vodafone India with Birla group's Idea cellular with the swap ratio of 1:1, that means for every share held by the shareholder of Idea and Vodafone will get the one share of the merged company. On the completion of the deal, Vodafone ended up with 45.1% shareholding whereas Idea received 26% shareholding. Later Idea acquired 4.9% shares from Vodafone for ₹3.9 billion. Also, Idea has the right to acquire 9.5% shares from Vodafone over the next four years from the date of official announcement.

In case Idea cellular fails to acquire 9.5% shareholding, then Vodafone will be obliged to sell those shareholdings in open market to achieve equalization. But Vodafone cannot exercise voting right over those 9.5% shares till equalization is achieved and it is to be exercised jointly by Idea and Vodafone. However, Vodafone has more financial rights in the merged entity as CFO was nominated by Vodafone, but CEO & COO was nominated and appointed jointly by Vodafone and Idea. Mr. Kumar Mangalam Birla was appointed chairman of the merged entity jointly by Vodafone and Idea. It was also agreed upon between the parties that profit from sale of towers will be used to reduce the debt component in capital structure over the next four years. With this merger deal, both the companies' combined 300 million customer base, 41% revenue market share and 35% market share.

At the time of merger, Vodafone and Idea's enterprise value stood at ₹828 billion and ₹722 billion respectively. Until the merger was completed both the companies operated separately under their own brand name.

Annualized	Idea	Vodafone	Idea + Vodafone	Idea + Vodafone + Synergy (Annualised)
Revenue	187,869	225,796	413,665	744,596
EBITDA	59,143	66,273	125,417	260,609
EBITDA margin	31%	29%	30.30%	35%
EBIT	20,409	16,005	36,414	82,602
EBIT Margin (%)	11%	7%	9%	11%
Net Debt	559,277	576,800	1,136,077	1,136,077
Market Cap	396,088	396,088	792,177	792,177
EV	955,366	972,888	1,928,254	1,928,254
Total Assets	735,625	848,297	1,583,922	1,267,137
EV/EBITDA	8.1	7.3	7.7	7.4
Net Debt to EBITDA	4.7	4.4	4.5	4.4
ROCE (post tax)	4%	3%	3%	9%
Share price	110	110	110	110
No of shares	3601	3601	7202	7202

Table:1 Synergy calculation:

Findings:

- Idea and Vodafone pre-merger financials show revenue synergy of almost double of what their individual revenues combined.
- Estimated Enterprise value of the merged company arrived at 1,928,254.

Major change in ROCE (return on capital employed) can be seen due to merger it may go up to 9%.

- Share prices are assumed to be constant to arrive at the share-holding structure as per deal.

Details	IDEA	VODAFONE	Idea Integrated with Vodafone
Revenue	187	225	412
EBITDA	59	66	125
EBITDA (Margin) (% years)	30.89%	29.08%	30%
Net Credit	527	552	1,079
Net / EBITDA Debt ratio	4.62	4.25	4.42
Capex	75	79	154
Total investment of Spectrum	617	788	1,405

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Table: 2 Collection of funds

Findings:

The consolidated business will be able to make money from the sale of the Tower, 11.5% of Indus Towers Stake Sales and four-year partnership profits which will help the company reduce Net Debt / EBITDA to 3. While Vodafone also holds a 42% stake in Indus Towers, that is not included in the transaction perimeter.

	FY-2019 Q3	FY 2019 Q2	Changes (Rs.)	Change (%)
Sales Turnover	11751.60	7663.50	4101.30	53.52%
Operating Expenses	10614.7	7202.2	3412.5	47.57%
EBITDA	1136.90	461.40	675.50	146.40%
PAT	8735.40	-5016.10	-28.30	-0.56%
Equity share capital	8735.40	8735.10	0.30	00.00%
EPS	-5.73	-5.69	-0.04	-0.62%
EBITDA margin	9.67%	6.02%		3.64%
PAT margin	-42.88%	-65.45%		22.58%

Table:3 Financial performance of Vodafone-Idea post-merger

The merger of Vodafone Idea with Idea cellular was completed on August 31, 2018.

Findings:

To analyse the financial performance of the sample case during post-merger period it has been observed that company's turnover during post-merger quarter 3 went by 53.52%.

EBITDA increased from 461 crore in Q2FY19 to 1136.90 crore in Q3FY19.

EBITDA margin increased from 6.02% to 9.67% during the same period. There has been a decline in profit after tax by -0.56% on account of high finance cost, integration cost, and mobile tower exit charges.

Further notwithstanding the losses incurred by the company, it is said to raise Rs11000 crore from Vodafone group and Aditya Birla group and infuse the total Rs 25000 in the firm to ensure that company has sufficient balance sheet flexibility to successfully execute its strategy.

Particulars	Idea	Vodafone-idea post-merger	post Aditya group acquisition on merger from Vodafone
Promoters Idea	42.45%	21.10%	26.00%
Promoters Vodafone	-	50.30%	45.40%
Public	57.55%	28.60%	28.60%
Total	100.00%	100.00%	100.00%

Table 4: Shareholding pattern analysis

Rationale behind the merger:

One of the major reason due to which this merger took place was survival in the adverse market situations. Reliance Jio had made it difficult for already existing players to survive without implementing newer strategies to sustain in the market. Vodafone and Idea also gained several other benefits as well such as increased customer base, annual operating cost saving was estimated around ₹140 billion however NPV of the total saving is estimated to be ₹70 billion.

The merged entity became market leader and removed Airtel of its position as a market leader for 15 years. The company has larger network distribution and infrastructure than any other telecom company. The merged entity has both the customer base of urban and semi urban population of the company as Idea had strong presence in rural areas and Vodafone had strong presence in urban areas. Both the merging companies also estimated to create value for their shareholders in the long term and increase its market value. With this merger, competing with other players was easier for Vodafone-idea.

Merger conditions:

The merger agreement also had a clause of break-fee of ₹3.3 billion in case any parties back out from fulfilling their obligation towards merger deal, they will be obligated to pay the break free to the aggrieved party. The approval to the merger deal was given by Department of telecommunication on the condition that the merging companies were required to pay upfront payment of ₹3.3 billion on account of one-time spectrum fee which was owed by Idea cellular and Vodafone. This payment was part in cash and part in bank guarantee.

Impact of merger:

This merger has caused more mergers and acquisitions of other telecom companies. The market dynamics has completely changed now, few companies are ruling the sector as newer players had to exit due to extreme adverse market condition and competition. Customer will have lessor options now and will have to adhere to the prices fixed by the market players. Large number of subscriber base in India has made India the fastest growing telecom market and with the merging of huge telecom players it will help the telecom sector grow.

After this merger many other companies also took the merger option to survive. The assets of Telenor India and Reliance Communication were bought by Bharti Airtel. Also, Tata Teleservices customers started migrating to the Airtel network under an Intra Circle Roaming (ICR) arrangement. Various initiatives have been taken by the merger entity like renewal of price due to destructive entry of Reliance Jio which caused some serious imbalance.

This merger deal led to overcoming the debt of Idea Cellular and Vodafone India and large sum of credit was infused in the telecom sector. Impact of merger could be observed in various service providers in terms of quality of service in telecom sector. This impact could also be observed on the savings, synergies, and the spectrum in rapid growth. Cost and capex synergies were created for both companies. The major cost and capex synergies would be around network infrastructure, savings in energy costs, operational efficiencies, service centers, lower maintenance expenses. The merger has reduced the operation cost incurred to about 60% of the total cost which will aid in improving the quality and performance of the service provided by the company.

CONCLUSION:

Reliance Jio is the threat to most of the companies in telecommunication industry and to survive in this cutthroat competition mergers and acquisitions is seen taking place in industry. In the present case of Vodafone-idea it can be said that Synergy benefits would gradually be achieved in coming years which will result in higher profits and leverage is expected to reduce hence resulting in value addition to shareholder. Post-merger, there were no gain to public shareholders, it used to be a loss-making company amounting a loss of ₹5.3 billion in the December quarter of 2016. The merger between Idea and Vodafone will make them a top player in the long run.

If we look at the other side of the coin as well, not very long ago, India had a booming telecom sector, with number of telecom operators fighting for market share. But in 2016, Reliance Jio entered the sector which rock-bottom tariffs. A predatory pricing war started and ended up making several companies to exist the market. Therefore, it will not be wrong to say that market dynamics have changed a lot and competition level is not the same and telecom sector is being controlled by three major players.

In conclusion it can be said that People who are using Idea and Vodafone are now getting better network coverage in cities and towns post-merger. Consumers can expect more diverse services and access to newer and smarter technology like VoLTE, Digital wallets, and internet of things after the merger.

The merger between Idea and Vodafone India has made them a leading player in the Indian telecom sector. As per the benefits that arise from management synergies is ₹670 billion for cost and capital expenditure ₹140 billion operating expenses by the 4th year. It also decreased the debt on the Vodafone Idea Ltd with sale of Towers Assets. The merger will also lead to cost savings and asset monetization opportunities aiding financial performance. The big question to be answered is whether the company will be able to monetize the surplus spectrum and able to stream the money towards newer technologies and better services.

To be able to gain something out of this huge telecom merger Vodafone-Idea, need to develop new strategies to increase their number of subscribers in the market thereby increasing their

net revenue while keeping the debt to minimum. The big advantage to the promoters of Aditya group is that the consolidated with Vodafone in this pricing war with Reliance Jio and Airtel at the same time have rights to gradually increase the stake in stages to become equal partners. According to the current circumstances, there is little to no gain to the public shareholders, and they can only hope that they will be benefited with the merger in the long term.

Keeping in the view of the Current scenario of Indian telecom sector, it will not be prudent for any new player to enter the market. Thus, if a company wants to survive in this sector in the long run, it should have either of these two, huge capital investment or business combinations.

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