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A Case on Vodafone – Idea Merger

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CASE STUDIES

INTRODUCTION

Mergers provide a way for businesses to pool expertise and resources to boost productivity and profit. For small business owners, a merger or acquisition can offer a way to cash in on an innovative product or service. On the other hand, mergers can introduce a variety of risks, such as differences in company cultures and loss of key personnel, which can cause performance to fall short of expectations. The telecom industry is going through a consolidation phase with many players looking for a merger. In a world where there is an increasing need of communication and social networking, Vodafone, due to its technical competence and innovation, is quickly becoming a preferred choice in many countries.

ORIGIN AND BACKGROUND

The revolutionary idea of cellular boom began when Racal Electronics plc and Millicom Inc. partnered in 1984 to offer mobile telephone services. This was the beginning of the Vodafone brand. Over the next few years, the ownership structures and the names changed a few times as the company grew. Vodafone Group plc had been finally established as an independent company in 1991.The name Vodafone is a portmanteau of voice data phone. Through the 90s, Vodafone acquired few companies and expanded across the stretch of United Kingdom. It consolidated its position and kept growing at a steady rate. In 1997, the company rebranded itself with the ‘speech mark’ logo that is its unique identity today.

The company later saw some major mergers. In 1999, it merged with AirTouch Communications to form the world's largest mobile telephony company. Vodafone entered India in 2007 and by 2011, acquired a controlling stake in Vodafone India. In 2014, Vodafone had acquired 100% stake in its Indian operations. Vodafone is known for its many firsts. It made the first International roaming call, and it was also the first to offer internet access on the move with Vodafone Live. Various other innovations like Vodafone Money Transfer service m-pesa have been very successful. Today, it has more than 400 million subscribers worldwide. Throughout its history, Vodafone has remained committed to offering the best services to its customers. It runs on a philosophy of 'Power to You' which means the company strives to empower the customer by offering various services tailored to match his needs. The company always strives to innovate and bring out new offerings to its customers.

Idea Cellular Infrastructure Services is a wholly owned subsidiary of Idea Cellular which maintains the tower assets and network infrastructures. During its inception in 1995, Aditya Birla Group, Tata Group and AT&T Wireless each held one-third equity in the company. Following AT&T Wireless' merger with Cingular Wireless in 2004, Cingular decided to sell its 32.9% stake in Idea. This stake was bought by the remaining two stakeholders equally. Tata forayed into the cellular market with its own subsidiary, Tata Indicom, a CDMA-based mobile provider and in April 2006, Aditya Birla Group announced the acquisition of the 48.18% stake held by Tata Group at INR 40.51 a share amounting to INR 44.06 billion with 15% of the stake acquired by Aditya Birla Nuvo and the remaining by Birla TMT holdings Private Ltd. both AV Birla family owned companies. Malaysia based Axiata bought a 19.96% stake in the company in 2009.Britain's Vodafone Group will merge its Indian subsidiary with local rival Idea Cellular within two years, creating a new market leader that will be better equipped to negotiate a brutal new price war.

A MERGER IS A PERFECT MATCH

Vodafone will own 45.1% in the combined entity after transferring 4.9% to the promoters of Idea Cellular for Rs 3,874 crore in cash post the merger. Kumar Mangalam Birla and other promoters of Idea Group will hold 26% and the rest will be owned by the public, said the statement.

Prior to completion of the transaction, Vodafone and Idea intend to sell their standalone tower assets and Idea's 11.15% stake in Indus Towers to reduce leverage in the combined company. Vodafone will also explore strategic options for its 42% stake in Indus Towers; potential options include either a partial or a full disposal. The Idea stock, which had jumped over 15% in early trade, was down 8% at Rs99.45 on the BSE at 10.36 am, as investors booked profits. The merger ratio is based Idea's price at Rs 72.5 a unit. The companies added that the implied enterprise value is Rs 828 billion or $12.4 billion for Vodafone India and Rs 722 billion or US$10.8 billion for Idea, excluding its stake in Indus Towers, valuing Vodafone India at 6.4x EV/LTM EBITDA and Idea excluding its stake in Indus Towers at 6.3x EV/LTM EBITDA.

Vodafone will contribute Rs 2,500 crore ($369 million) more net debt than Idea, upon closure of the merger. Based on Idea's net debt of Rs 52,700 crore at December end, Vodafone would contribute Rs 55,200 crore of net debt to the merged entity. “This landmark combination will enable the Aditya Birla Group to create a high quality digital infrastructure that will transition the Indian population towards a digital lifestyle and make the Government’s Digital India vision a reality," said Aditya Birla Group Chairman, Kumar Mangalam Birla. He added that Idea and Vodafone will together create a very valuable company given our complementary strengths.

Vodafone Group Chief Executive, Vittorio Colao said, "The combined company will have the scale required to ensure sustainable consumer choice in a competitive market and to expand new technologies – such as mobile money services – that have the potential to transform daily life for every Indian." "We look forward to working with the Aditya Birla Group to create value for all stakeholders.” The merger should be completed within 24 months, which is in 2018, subject to approvals from shareholders, creditors, stock exchanges, SEBI, the telecom department and Competition Commission of India. The merger is not subject to approval from Vodafone Group's shareholders. The pact also has a break-fee of Rs 3,300 crore (US$500 million) that would become payable under certain circumstances.

A SWOT ANALYSIS OF IDEA AND VODAFONE MERGER

Strengths	**Weaknesses**
• Cost advantages from proprietary know how • Patents • Influential brand names • Fast networking process • Accessible distribution network	• Lack of patent protection • Deprived of access to main distribution channels • Weak brand name • Poor customer reputation • High cost structure

Opportunities	Threats
• Technologies innovations • Elimination of trade barriers • An untapped market need	• Consumers shift to different brand • Arrival of substitutes • Strict regulations • Growing trade barriers

SYNERGIES FOR LONG TERM

The merger is expected to bring in capex and opex synergies in the form of lower infrastructure costs, network consolidation and cost efficiencies in information technology. The initial years would entail integration costs, estimated by the management at Rs.13,300 crore. Total cost synergies of Rs.14,000 crore on annual basis, are expected to flow in only from the fourth year after the merger. Hence, cost savings/synergies, which hold the key to future earnings, are expected to come in only in later years.

The October 2016 spectrum auction has left the telecom players saddled with heavy debt. The intense price war after the entry of Reliance Jio, led to a drop in revenues in the last two quarters. Idea's revenue declined by 3.8 per cent y-o-y in the December quarter while Vodafone's revenue declined by 1.9 per cent.

The net debt of the combined entity is pegged at about Rs.1.07 lakh crore.

The merger could face regulatory challenges on account of excess spectrum and revenue market share of over 50 per cent in some circles.

The litigation cases of the companies involved, particularly the tax struggle of Vodafone, could delay the closure of deal.

CONCLUSION

It will leverage customer affinity for Vodafone and Idea brands, that have combined consumer base of about 390 million, it will create substantial cost and capex synergies for both companies - an estimated net present value of around US$10 billion after integration costs and spectrum liberalization payments, with estimated run-rate savings of US$2.1 billion on an annual basis by the fourth year post completion. Operating cost savings represent 60% of the expected run-rate savings.

Vodafone Group’s consistent rise to the top despite all the struggles and challenges has become a very inspiring story. From a small telecom company in Newbury, Vodafone had beaten the odds and has become the third largest mobile communications company in a span of 30 years. The journey of becoming one of the most valuable brands in the world, Vodafone’s story has lessons everybody can learn from, especially if they want to succeed and achieve great things.

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