

17/12/2009

MF Global Company Update

# Bharti Airtel

| New Frontiers

TELECOM

BHARTI IN: **BUY**

RS 327

Media reports have indicated that Bharti Airtel plans to buy 70% in Warid Bangladesh and the deal is valued at US\$ 900mn. The deal is yet to be confirmed by the management. Our first thoughts on the deal are:

- » Considering US\$ 900mn is the EV of Warid Bangladesh, this translates to EV/sub of US\$ 321, which is much higher than Bharti's EV/sub at US\$ 210. Hence, the deal is expensive.
- » The competitive intensity in Bangladesh is much lower than India with the largest mobile operator (Grameen phone) having a subscriber market share of 43% and EBIDTA margins of 57% (Q3CY09). The Top-3 operators (Grameen, Axiata and Orascom) have 88% market share. Mobile teledensity stands at a mere 31%. Hence, the case for a fourth operator is very strong.
- » Tariffs in Bangladesh are higher and MoUs (minutes of usage) are lower than in India. This market presents immense opportunities for Bharti to scale up its business model based on low tariffs and high MoU.
- » Although Bangladesh has lower mobile penetration, operators cannot scale up their subscriber base similar to India. The government of Bangladesh imposes a SIM tax of 800 Taka (US\$ 12). This creates entry costs for subscribers. This aspect also reduces the instances of multiple SIM cards. Hence, revenue growth for the 4<sup>th</sup> and 5<sup>th</sup> placed operators will be slower.
- » We estimate Warid Bangladesh revenues for CY09 at ~US\$ 90mn and it may not be EBIDTA positive, considering its installed BTS base of 1750-1900.

We find acquisition of Warid Bangladesh structurally positive for Bharti, but not a significant driver for valuations as it will take at least two years for Bharti to gain traction in Bangladesh. Hence, we rate the deal Neutral. We currently have a Buy rating on the stock.

## VALUATION SUMMARY

Y/E MAR, RS MN	FY2008	FY2009	FY2010E	FY2011E	FY2012E
NET SALES	270,250	369,615	401,978	428,100	466,925
GROWTH, %	45.9	36.8	8.8	6.5	9.1
CORE EBIDTA	113,715	151,680	162,072	163,884	175,090
EBIDTA MARGIN, %	42.1	41.0	40.3	38.3	37.5
NET PROFIT	67,008	84,700	91,381	79,149	78,807
EPS, RS	17.7	22.3	24.1	20.9	20.8
EPS GROWTH, %	57.4	26.4	7.9	-13.4	-0.4
PER, X	18.5	14.7	13.6	15.7	15.8
EV/EBIDTA, X	11.3	8.6	8.3	8.2	7.6
EV/NET SALES, X	4.7	3.5	3.4	3.1	2.9
PRICE/BOOK VALUE, X	5.5	4.0	3.1	2.6	2.2
ROIC, %	34.4	32.6	21.7	15.4	13.1
ROE, %	37.0	31.5	25.7	18.1	15.3
DIVIDEND YIELD, %	0.0	0.0	0.7	0.0	0.0

Source: Company, MF Global India Research Estimates

## TARGET RS 365 (+12%)

### SECTOR RATING

OW	N	UW

### STOCK RATING

BUY	NEUTRAL	SELL
> 15%	-15% TO +15%	< -15%

### COMPANY DATA

O/S SHARES :	3797MN
MARKET CAP (RS) :	1237BN
MARKET CAP (USD) :	27BN
52 - WK HI/LO (RS) :	495 / 230
AVG. DAILY VOL. (3MTH) :	17MN
FACE VALUE (RS) :	5

### SHARE HOLDING PATTERN, %

PROMOTERS :	67.7
FII / NRI :	18.7
FI / MF :	8.2
NON PROMOTER CORP. HOLDINGS :	3.8
PUBLIC & OTHERS :	1.6

### PRICE PERFORMANCE, %

	1MTH	3MTH	1YR
ABS	8.1	-22.1	-12.2
REL TO BSE	8.8	-23.5	-81.7

### PRICE VS. SENSEX



Source: Bloomberg, MF Global India Research

## Bangladesh Telecom market

Bangladesh has 51mn subscribers. Bangladesh has a much higher market concentration as indicated by Hirschman Herfindahl Index (HHI), which is an indicator of competitive intensity. HHI indicates that Bangladesh has a much lower competitive intensity compared to India at 1630. We also see the market is particularly polarised with Grameen phone having a substantial lead in terms of market share over the other operators.

OPERATOR	SUBSCRIBERS (IN MN)	MARKET SHARE (%)	CONTRIBUTION TO HHI
GRAMEENPHONE	22.3	43.4	1882
AXIATA	11.0	21.4	457
ORASCOM	12.3	23.9	570
WARID	2.8	5.4	29
PBTL	2.0	3.9	15
TELETALK	1.1	2.1	4
<b>TOTAL</b>	<b>51.4</b>	<b>100.0</b>	<b>2958</b>

Source: BTRC

The largest operator in Bangladesh, which is Grameenphone, a JV of Telenor and Grameen Telecom, enjoys very high market share and EBITDA margins.

PARTICULARS ( US\$ MN)	YTD CY09 (3Q)
SUBSCRIPTION AND TRAFFIC	604
INTERCONNECT REVENUES	71
MOBILE REVENUES COMPANY'S SUBSCRIPTIONS	674
OTHER MOBILE REVENUES	2
TOTAL MOBILE REVENUES	676
NON-MOBILE REVENUES	7
TOTAL REVENUES <sup>1)</sup>	683
<sup>1)</sup> OF WHICH INTERNAL REVENUES	0
EBITDA BEFORE OTHER INCOME AND EXPENSES	400
OTHER INCOME AND EXPENSES	0
EBITDA	400
EBITDA MARGIN (%)	59
DEPRECIATION AND AMORTISATION <sup>1)</sup>	-173
IMPAIRMENT LOSSES <sup>2)</sup>	0
OPERATING PROFIT	226
OPERATING PROFIT MARGIN (%)	33.5
MOU	310
ARPU IN US \$	3.5
ARPU IN BANGLADESH TAKA	239

Source: Telenor

The high margins for Grameenphone is on account of high market and revenue share and low cost structure. We can clearly see that Grameenphone has much lower MoU and ARPU similar to Bharti (in Bangladesh Taka). Grameenphone has over ~10k BTS supporting 22mn subscribers. Hence, the subscribers per BTS for Grameenphone (2200) is much higher than Bharti (1000), resulting in a lower cost structure.

Hence, we believe that the Bangladesh market with a population of 160mn and teledensity of just 31% offers significant opportunities for a 4<sup>th</sup> operator.

#### RECOMMENDATION HISTORY

RECOMMENDATION	TARGET, RS	CMP, RS	DATE
BUY	365	292	3-NOV-09
BUY	395	359	7-OCT-09
BUY	490	443	23-SEP-09
BUY	455	435	31-AUG-09
BUY	455	408	24-JUL-09
BUY	415	405	26-MAY-09
BUY	415	375	4-MAY-09
BUY	375	294	12-MAR-09
BUY	400	320	23-JAN-09
BUY	400	325	3-NOV-08
BUY	465	399	24-JUL-08
NEUTRAL	465	422	22-MAY-08

## Financials

### INCOME STATEMENT

Y/E MAR, RS MN	FY2008	FY2009	FY2010E	FY2011E	FY2012E
NET SALES	270,250	369,615	401,978	428,100	466,925
GROWTH, %	45.9	36.8	8.8	6.5	9.1
OPERATING EXPENSES	-156,535	-217,935	-239,907	-264,216	-291,834
EBITDA	113,715	151,680	162,072	163,884	175,090
GROWTH, %	52.6	33.4	6.9	1.1	6.8
MARGIN, %	42.1	41.0	40.3	38.3	37.5
DEPRECIATION	-37,261	-47,581	-58,514	-69,649	-82,086
EBIT	76,454	104,099	103,557	94,235	93,004
GROWTH, %	55	36	-1	-9	-1
MARGIN, %	28	28	26	22	20
NET INTEREST AND OTHERS	82	-11,025	3,998	2,188	4,826
PRE-TAX PROFIT	76,536	93,074	107,555	96,423	97,830
TAX PROVIDED	-8,378	-6,615	-14,838	-15,804	-17,407
PROFIT AFTER TAX	68,158	86,459	92,718	80,619	80,424
MINORITY INTEREST	-1,150	-1,759	-1,336	-1,470	-1,617
MF NET PROFIT	67,008	84,700	91,381	79,149	78,807
GROWTH, %	57	26	8	-13	0
EXTRAORDINARY ITEMS: GAINS/(LOSSES)	0	0	0	1	1
UNADJ. SHARES (M)	3,796	3,796	3,796	3,796	3,796
WTD AVG SHARES (M)	3,796	3,796	3,796	3,796	3,796

### CASH FLOW

Y/E MAR, RS MN	FY2008	FY2009	FY2010E	FY2011E	FY2012E
PRE-TAX PROFIT	76,536	93,074	107,555	96,423	97,830
DEPRECIATION	37,261	47,581	58,514	69,649	82,086
CHG IN WORKING CAPITAL	25,105	27,636	23,640	11,376	-657
TOTAL TAX PAID	-6,678	-4,314	-18,827	-15,792	-17,407
OTHER OPERATING ACTIVITIES	-5,643	-4,491	-3,060	-4,168	-6,892
CASH FLOW FROM OPERATING ACTIVITIES	126,580	159,486	167,823	157,488	154,961
CAPITAL EXPENDITURE	-138,481	-142,361	-200,297	-160,297	-150,297
CHG IN INVESTMENTS	574	-733	3,055	4,461	6,892
CHG IN MARKETABLE SECURITIES	-46,082	10,160	17,826	11,537	-776
OTHER INVESTING ACTIVITIES	0	0	0	1	1
CASH FLOW FROM INVESTING ACTIVITIES	-183,989	-132,934	-179,416	-144,300	-144,182
FREE CASH FLOW	-57,408	26,552	-11,592	13,188	10,779
EQUITY RAISED/(REPAID)	14,937	1,149	1,699	-304	0
DEBT RAISED/(REPAID)	36,180	-23,723	36,186	-3,284	-3,284
DIVIDEND (INCL. TAX)	0	0	-8,268	0	0
OTHER FINANCING ACTIVITIES	5,605	389	-1,336	-1,470	-1,617
CASH FLOW FROM FINANCING ACTIVITIES	56,722	-22,184	28,280	-5,058	-4,901
NET CHG IN CASH	-687	4,367	16,688	8,130	5,878

## BALANCE SHEET

AS AT 31ST MAR, RS MN	FY2008	FY2009	FY2010E	FY2011E	FY2012E
CASH & BANK	6,777	11,145	27,833	35,971	41,866
MARKETABLE SECURITIES AT COST	48,086	37,925	20,099	8,562	9,338
DEBTORS	28,061	28,528	34,141	26,976	29,423
INVENTORY	1,142	963	1,652	1,759	1,919
LOANS & ADVANCES	346	15,122	15,122	15,122	15,122
OTHER CURRENT ASSETS	29,371	50,396	48,578	50,407	53,124
TOTAL CURRENT ASSETS	113,783	144,079	147,424	138,797	150,792
INVESTMENTS	108	128	128	128	128
GROSS FIXED ASSETS	438,799	584,226	784,523	944,820	1,095,118
LESS: DEPRECIATION	-112,844	-163,479	-221,993	-291,643	-373,729
NET FIXED ASSETS	325,955	420,747	562,530	653,178	721,389
OTHER NON-CURRENT ASSETS	32,143	37,296	37,296	37,284	37,284
<b>TOTAL ASSETS</b>	<b>471,988</b>	<b>602,249</b>	<b>747,377</b>	<b>829,386</b>	<b>909,593</b>
TOTAL CURRENT LIABILITIES	154,135	217,185	242,490	247,985	251,681
NON-CURRENT LIABILITIES	92,270	70,718	107,429	104,494	102,181
TOTAL LIABILITIES	246,405	287,903	349,919	352,479	353,862
PAID-UP CAPITAL	18,979	18,982	18,982	18,982	18,982
RESERVES & SURPLUS	206,603	295,363	378,476	457,625	536,432
SHAREHOLDERS' EQUITY	225,582	314,345	397,459	476,607	555,414
<b>TOTAL EQUITY &amp; LIABILITIES</b>	<b>471,988</b>	<b>602,249</b>	<b>747,377</b>	<b>829,386</b>	<b>909,593</b>

## PER-SHARE DATA

	FY2008	FY2009	FY2010E	FY2011E	FY2012E
MF EPS (INR)	17.7	22.3	24.1	20.9	20.8
GROWTH, %	57.4	26.4	7.9	-13.4	-0.4
BOOK NAV/SHARE (INR)	59.3	82.4	104.8	125.6	146.3
FDEPS (INR)	17.7	22.3	24.1	20.9	20.8
CEPS (INR)	27.5	34.8	39.5	39.2	42.4
CFPS (INR)	32.0	31.1	43.8	40.9	40.3
DPS (INR)	0.0	0.0	2.2	0.0	0.0

## FINANCIAL STRUCTURE

	FY2008	FY2009	FY2010E	FY2011E	FY2012E
TOTAL DEBT/EQUITY (%)	0.4	0.4	0.4	0.3	0.3
NET DEBT/EQUITY (%)	0.4	0.3	0.3	0.2	0.2

**PROFITABILITY, PRODUCTIVITY, LIQUIDITY AND VALUATION RATIOS**

	FY2008	FY2009	FY2010E	FY2011E	FY2012E
RETURN ON ASSETS (%)	18.3	16.6	14.3	10.6	9.5
RETURN ON EQUITY (%)	37.0	31.5	25.7	18.1	15.3
RETURN ON INVESTED CAPITAL (%)	34.4	32.6	21.7	15.4	13.1
ROIC/COST OF CAPITAL (X)	34.4	32.6	21.7	15.4	13.1
ROIC - COST OF CAPITAL (%)	22.2	20.4	9.4	3.1	0.7
RETURN ON CAPITAL EMPLOYED (%)	27.7	25.4	21.8	15.3	13.4
COST OF CAPITAL (%)	12.2	12.2	12.2	12.3	12.4
ROCE - COST OF CAPITAL (%)	15.6	13.2	9.5	3.0	1.0
ASSET TURNOVER (X)	1.4	1.2	1.0	0.8	0.8
SALES/TOTAL ASSETS (X)	0.7	0.7	0.6	0.5	0.5
SALES/NET FA (X)	1.0	1.0	0.8	0.7	0.7
WORKING CAPITAL/SALES (X)	-0.4	-0.3	-0.4	-0.4	-0.3
FIXED CAPITAL/SALES (X)	0.0	0.0	0.0	0.0	0.0
RECEIVABLE DAYS	37.9	28.2	31.0	23.0	23.0
INVENTORY DAYS	1.5	1.0	1.5	1.5	1.5
PAYABLE DAYS	43.7	31.4	58.6	56.7	56.0
CURRENT RATIO (X)	0.7	0.7	0.6	0.6	0.6
QUICK RATIO (X)	0.7	0.7	0.6	0.6	0.6
INTEREST COVER (X)	24.4	N/A	44.0	23.4	23.7
DIVIDEND COVER (X)			11.1		
PER (X)	18.5	14.7	13.6	15.7	15.8
PEG (X) - Y-O-Y GROWTH	0.3	0.6	1.7	-1.2	-36.5
PRICE/BOOK (X)	5.5	4.0	3.1	2.6	2.2
YIELD (%)	0.0	0.0	0.7	0.0	0.0
EV/NET SALES (X)	4.7	3.5	3.4	3.1	2.9
EV/EBITDA (X)	11.3	8.6	8.3	8.2	7.6
EV/EBIT (X)	16.8	12.6	13.0	14.3	14.4
EV/NOPLAT (X)	18.9	13.6	15.1	17.1	17.5
EV/CE	4.0	3.4	2.7	2.3	2.0
EV/IC (X)	6.5	4.4	3.3	2.6	2.3

Source: Company, MF Global India Research Estimates

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#### Rating Rationale

BUY and SELL recommendations are used to draw attention to stocks, which we believe are under-priced or over-priced by circa 15%, that is, price differential of +/- 15% between our price target and the market price. Stocks which do not achieve this price differential are NEUTRAL. Price targets are established in the context of a flat market.

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