

Bharti Airtel

STOCK INFO.	BLOOMBERG
BSE SENSEX: 10,930	BHARTI IN
	REUTERS CODE
S&P CNX: 3,196	BRTI.BO

12 July 2006

Buy

Previous Recommendation: Buy

Rs383

Equity Shares (m)	1,884.1
52-Week Range (Rs)	433/245
1,6,12 Rel. Perf. (%)	3/-2/-2
M.Cap. (Rs b)	721.2
M.Cap. (US\$ b)	15.6

YEAR	NET SALES	PAT	EPS	EPS	P/E	P/BV	ROE	ROCE	EV/	EV/
END	(RS M)	(RS M)	(RS)	GROWTH (%)	(X)	(X)	(%)	(%)	SALES	EBITDA
3/06A	116,631	22,584	12.0	48.3	31.9	7.9	29.5	21.6	6.6	17.7
3/07E	164,558	33,622	17.8	48.9	21.5	5.8	30.9	24.7	4.8	12.5
3/08E	206,367	44,382	23.6	32.0	16.3	4.3	30.0	25.1	3.8	9.6

The Indian Wireless Industry added 4.85m subscribers in June 2006 against 4.29m subscribers in May 2006. The growth was mainly led by CDMA operators while GSM additions were flat. Bharti, a GSM operator, added 1.21m subscribers in June 2006 compared with 1.18m additions in May 2006. The company further strengthened its leadership position in the overall wireless market. We maintain our positive stand on the stock.

CDMA operators gain market share

CDMA operators increased their market share at 28.15% in June 2006, aided by strong subscriber additions by Reliance Infocomm and Tata Tele Services (TTSL). Reliance's CDMA net additions jumped 68% MoM to 873,868. TTSL witnessed an increase of 29% MoM in CDMA net additions to 780,184 subscribers.

Subscriber additions by GSM operators flat

GSM operators added 3.19m subscribers in June 2006 against 3.17m subscribers in May 2006. While BSNL's additions were lower, Hutch and Idea's subscriber additions accelerated. BSNL's additions tumbled 29.5% MoM. It reported subscriber additions of 0.29m for June 2006 against 0.41m for May 2006, as it lost subscribers in Andhra Pradesh, Kerala, Haryana, Chennai and Punjab.

BSNL's subscriber additions have been volatile, primarily due to capacity constraints but the current slowdown may be result of network and quality of service issues. Hutch's net adds were up 10% MoM while Idea's net additions were up 12% MoM. Bharti added 1.21m subscribers for the month, thereby reporting the sixth consecutive month of 1m+ subscriber additions.

WIRELESS SUBSCRIBER ADDITIONS (ABSOLUTE NUMBERS)

	MAR-06	APR-06	MAY 06	JUN-06
Bharti	1,129,134	1,104,694	1,176,310	1,212,367
BSNL	1,097,863	426,944	415,195	292,774
Hutch	829,979	701,211	705,478	776,662
Idea	361,409	274,343	422,185	474,114
Aircel	147,505	218,923	194,234	173,946
MTNL	221,345	76,489	79,834	72,183
Spice	113137	51166	42977	27076
BPL	494	-29,970	-15,100	4,750
Reliance Tele.	103,905	105,865	145,993	160,885
Total GSM	4,004,771	2,929,665	3,167,106	3,194,757
Reliance CDMA	925,005	502,250	521,884	873,868
TTSL CDMA	457,689	514,150	604,822	780,184
Total CDMA	1,387,006	1,021,594	1,131,517	1,660,369
Total Wireless	5,391,777	3,951,259	4,298,623	4,855,126

MARKET SHARE (%)

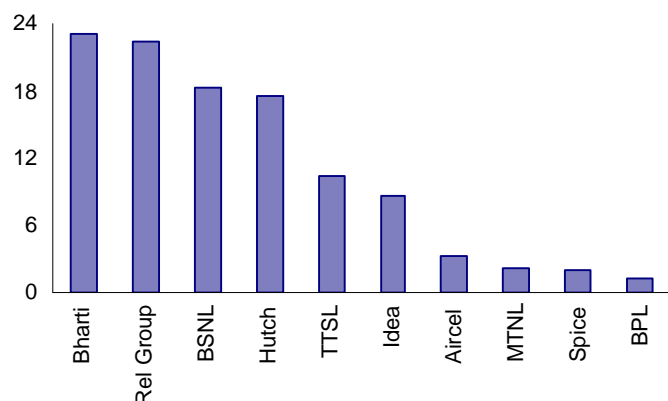
	MAR-06	APR-06	MAY 06	JUN-06
Bharti	20.4	20.7	20.9	21.1
BSNL	17.9	17.6	17.3	16.8
Hutch	16.0	16.1	16.1	16.1
Idea	7.7	7.6	7.7	7.8
Aircel	2.7	2.8	2.9	2.9
MTNL	2.0	2.0	2.0	2.0
Spice	2.0	2.0	1.9	1.9
BPL	1.4	1.3	1.2	1.2
Reliance Tele. (GSM)	2.0	2.0	2.1	2.1
Total GSM	72.0	72.1	72.1	71.9
Reliance CDMA (DM+FWP)	19.0	18.8	18.5	18.5
TTSL CDMA (DM+FWP)	8.8	9.0	9.2	9.5
Total CDMA	28.0	27.9	27.9	28.2
Total Wireless	100.0	100.0	100.0	100.0

Source: COAI, AUSPI

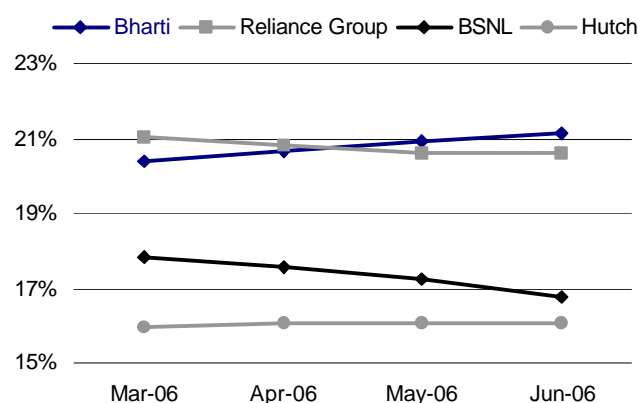
Note: 1. Since Reliance Infocomm has reported consolidated additions for both its FWP and digital mobile operations, we have consolidated numbers for other CDMA operators as well for meaningful comparison. 2. MTNL has not reported its CDMA subscriber additions for the month.

BHARTI RETAINS ITS LEADERSHIP POSITION

MARKET SHARE AS AT END-JUNE 2006 (%)



MARKET SHARE MOVEMENT OF TOP PLAYERS (%)



Source: COAI, AUSPI

Bharti maintains leadership

Bharti's market share increased from 20.9% in May 2006 to 21.1% in June 2006. We believe that the launch of FWP will enable Bharti to increase its market share further. Initially, the company plans to roll out the service in 88 cities and aggressively ramp up in 3,800 towns by August 2006. The capex for rolling out FWP services is likely to be minimal, as it will use its existing GSM network. There is no change in the capex guidance by company – it continues to be at US\$1.8-2b for FY07.

Bharti has been the most consistent operator in terms of subscriber additions. It is the only operator to report six consecutive months of 1m+ subscriber additions. We believe that the company's superior execution and innovative business model, which have enabled it to focus on subscriber acquisitions while outsourcing other functions to vendors, have been the primary drivers for its consistent performance. It plans to take its town coverage from 3,800 towns to 5,200 towns by the end of FY07. Further, its fixed line additions at 78k were extremely good.

Other large operators such as BSNL and Reliance Infocomm have been witnessing volatility in their subscriber additions. We believe that Bharti Airtel will continue to be the market leader, driven by its strong execution skills.

Valuation and view

We continue to be impressed with Bharti's subscriber additions. The company has been reporting additions in line with our estimates and ahead of market expectations. We note that additions for Bharti were impressive given the stringent verification norms.

We believe that Bharti will be able to sustain its premium over other operators because of its de-risked business model and management's ability to tap new areas of revenues and efficiency. We expect Bharti to report EPS of Rs17.8 in FY07 and Rs23.6 in FY08. The stock is currently trading at 21.5x FY07E EPS and 16.3x FY08E EPS. We reiterate **Buy** with a price target of Rs471 – an upside of 23%.

Bharti Airtel: an investment profile

Company description

Bharti Airtel, promoted by Sunil Bharti Mittal, is the largest cellular services provider in India with a subscriber base of more than 23m and a market share of over 21% of the overall cellular market. It is the first cellular services provider to have introduced the lowest denomination recharge coupon for prepaid subscribers and electronic recharge. It is also the most profitable cellular services provider and is managed by a very strong team of professionals. It is the only player to have a presence in all 23 circles in India.

Key investment arguments

- ☞ Leader in the fast growing Indian cellular market and enjoys scale advantage.
- ☞ Strong innovative management, the biggest differentiator.
- ☞ Most profitable cellular services provider.

Key investment risks

- ☞ Declining ARPU's could lead to lower operating margins.
- ☞ Being a listed company, can not be a price leader due to focus on profitability and hence is reactive to competitor's pricing.

Recent developments

- ☞ Introduced India's first Rs999 Lifetime prepaid card with a lifetime validity on 23 December 2005.
- ☞ Launched Easy Lifetime Prepaid.
- ☞ Launched Airtel Mega its Fixed wireless phone service

Valuation and view

- ☞ Revenue CAGR of 33% and earnings CAGR of 40% over FY06-08E. Valuations at 21.5x FY07E earnings and 16.3x FY08E earnings are attractive and at a discount to some similar sized peers in other fast growing industries, like TCS and Infosys.
- ☞ **Buy** with a target price of Rs471, an upside of 23% from current levels.

Sector view

- ☞ Rapid growth in mobile subscriber base enabling the cellular market to surpass that of fixed telephony.
- ☞ Industry is forecasting subscriber base would touch 200m by FY09 implying a 30% CAGR over the next 3 years. 200m subscriber target will be achieved by mid FY09 even if industry is able to maintain monthly addition of 4m subscribers per month against 5m average additions that industry has seen in 2006.
- ☞ Tariff cuts to be compensated by volume and cut in regulatory levies, resulting in decent margins and RoE.

COMPARATIVE VALUATIONS

		BHARTI	INFOSYS	TCS
P/E (x)	FY07E	21.5	26.0	25.0
	FY08E	16.3	21.7	20.3
P/BV (x)	FY07E	5.8	9.5	11.3
	FY08E	4.3	7.1	7.9
EV/Sales (x)	FY07E	4.8	6.5	6.9
	FY08E	3.8	4.9	5.1
EV/EBITDA (x)	FY07E	12.5	20.2	19.0
	FY08E	9.7	15.7	15.0

SHAREHOLDING PATTERN (%)

	MAR.06	DEC.05	MAR.05
Promoters	45.5	45.6	46.5
Domestic Institutions	3.9	3.7	2.9
FII's/FDI's	48.1	47.9	48.0
Others	2.5	2.8	2.6

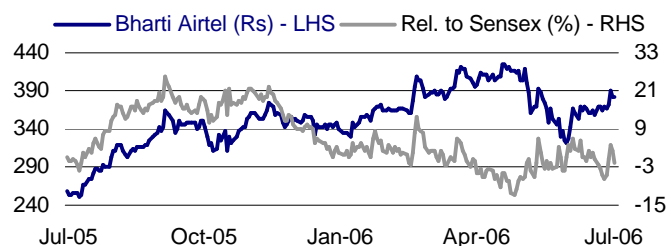
EPS: MOST FORECAST VS CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY07	17.8	17.9	-0.4
FY08	23.6	24.0	-1.8

TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
383	471	23.0	Buy

STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT					
(Rs Million)					
Y/E MARCH	2004	2005	2006	2007E	2008E
Revenues	48,320	80,028	116,631	164,558	206,367
Change (%)	64.0	65.6	45.7	41.1	25.4
Total Expenses	32,413	49,963	73,032	100,974	124,103
EBITDA	15,907	30,065	43,599	63,583	82,263
% of Gross sales	32.9	37.6	37.4	38.6	39.9
Depn. & Amortisation	7,733	11,341	15,830	20,846	25,916
EBIT	8,174	18,724	27,769	42,738	56,348
Net Interest	2,380	1,996	2,651	3,079	3,608
Other Income	182	-124	456	364	408
PBT	5,976	16,604	25,574	40,023	53,147
Tax	901	1,528	2,736	6,003	8,238
Rate (%)	15.1	9.2	10.7	15.0	15.5
Adjusted PAT	5,076	14,978	22,584	33,622	44,382
Change (%)	4.0	195.1	50.8	48.9	32.0
PAT after EO	5,376	14,978	22,584	33,622	44,382

BALANCE SHEET					
(Rs Million)					
Y/E MARCH	2004	2005	2006	2007E	2008E
Share Capital	18,534	18,534	18,939	18,939	18,939
Additional Paid up Capital	48,116	47,987	56,060	56,060	56,060
Reserves	-20,733	-5,455	16,894	50,683	95,166
Net Worth	45,916	61,065	91,893	125,682	170,165
Loans	45,723	49,040	47,395	68,710	69,339
Minority Interest	0	749	951	1,349	1,876
Other Liabilities	3,694	3,076	3,704	5,556	5,834
Deferred Tax Liability	1,127	1,183	1,945	1,945	1,945
Capital Employed	96,460	115,114	145,888	203,242	249,159
Gross Block	120,455	163,634	228,252	308,983	364,983
Less : Depreciation	20,484	31,825	47,655	68,501	94,417
Net Block	99,972	131,879	180,598	240,682	270,566
Intangible Fixed assets	36,388	39,211	38,200	34,380	33,349
Investments	158	671	692	554	996
Other Non-Current Assets	1,911	2,400	3,258	3,421	5,131
Curr. Assets	15,138	24,124	31,002	45,184	59,542
Inventories	317	545	381	431	451
Debtors	5,030	7,308	10,620	21,640	29,400
Cash & Bank Balance	1,305	3,256	2,838	3,754	6,544
Other current assets	8,486	13,015	17,163	19,358	23,147
Curr. Liab. & Prov.	20,719	43,959	69,662	86,599	87,077
Sundry Liabilities	17,460	40,486	64,879	81,099	81,301
Other Current Liabilities	3,259	3,473	4,783	5,500	5,775
Net Curr. Assets	-5,581	-19,835	-38,660	-41,415	-27,535
Appl. of Funds	96,461	115,114	145,888	203,242	249,159

E: MOST Estimates

RATIOS					
Y/E MARCH	2004	2005	2006	2007E	2008E
Basic (Rs)					
EPS	2.7	8.1	12.0	17.8	23.6
Cash EPS	7.1	14.2	20.3	28.8	37.1
Book Value	24.8	32.9	48.5	66.4	89.8
DPS	0.0	0.0	0.0	0.0	0.0
Payout %(Incl.Div.Taxes)	0.0	0.0	0.0	0.0	0.0
Valuation (x)					
P/E		47.4	31.9	21.5	16.3
Cash P/E		27.0	18.9	13.3	10.3
EV/EBITDA		25.2	17.7	12.5	9.6
EV/Sales		9.5	6.6	4.8	3.8
Price/Book Value		11.6	7.9	5.8	4.3
Dividend Yield (%)		0.0	0.0	1.0	1.0
Profitability Ratios (%)					
RoE	12.4	28.0	29.5	30.9	30.0
RoCE	9.8	17.6	21.6	24.7	25.1
Turnover Ratios					
Debtors (Days)	50	42	41	59	63
Asset Turnover (x)	0.3	0.4	0.4	0.4	0.5
Leverage Ratio					
Debt/Equity Ratio(x)	1.1	0.9	0.6	0.6	0.4

CASH FLOW STATEMENT					
(Rs Million)					
Y/E MARCH	2004	2005	2006	2007E	2008E
Op.Profit/(Loss) bef Tax	15,907	30,065	43,599	63,583	82,263
Other Income	182	-124	456	364	408
Interest Paid	-2,380	-1,996	-2,651	-3,079	-3,608
Direct Taxes Paid	-1,012	-1,472	-1,974	-6,003	-8,238
(Inc)/Dec in Wkg. Cap.	9,488	16,731	15,712	5,360	-11,259
CF from Op.Activity	22,186	43,205	55,142	60,225	59,566
(inc)/Dec in FA +CWIP	-39,684	-43,248	-64,549	-80,930	-55,800
(Pur)/Sale of Investments	1,939	-2,146	2,848	138	-1,706
CF from Inv.Activity	-37,745	-45,393	-61,701	-80,792	-57,506
Issue of Shares	-81	-129	8,073	0	0
Inc/(Dec) in Debt	15,994	3,317	-1,645	21,315	629
Other Financing Activities	346	951	-288	168	101
CF from Fin.Activity	16,259	4,139	6,141	21,483	730
Inc/(Dec) in Cash	700	1,951	-418	916	2,789
Add: Opening Balance	606	1,305	3,256	2,838	3,754
Closing Balance	1,305	3,256	2,837	3,754	6,544

E: MOST Estimates; All Financials as per US GAAP

N O T E S



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Bharti Airtel

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|---|-----|
| 1. Analyst ownership of the stock | No |
| 2. Group/Directors ownership of the stock | Yes |
| 3. Broking relationship with company covered | No |
| 4. Investment Banking relationship with company covered | No |

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