

Company Flash

11 March 2008 | 7 pages

Jet Airways (JET.BO)

Citi India Conference 2008: Day 1 Takeaways

- Conference takeaways** — Jet Airways spoke with investors at the Citi India Investor Conference 2008. Here are some of the highlights of that presentation
- Domestic outlook** — Near-term outlook remains challenging, as supply overhang persists. Management forecasts 15-18% growth in seat capacity in FY09, and expects the demand-supply mismatch to rectify itself over the next fiscal year. Longer term demand growth is forecast at 2-2.5x GDP growth.
- Substantial improvement in international operations profitability by FY10E** — Management stated that international operations were expected to become profitable on a sustainable basis by FY10 – as all new routes to the US, the Middle East and HK would have matured by then. Sub-optimal utilization of aircraft should also improve, improving EBITDAR margin to 20-22%.
- Fund raising** — The promoter is expected to dilute his stake to 70% from c80%. These proceeds would then be deployed to fund the promoter's contribution to the \$400m rights issue that is targeted for 1Q FY09. Subsequent to that, Jet might raise another \$400m in equity offerings. Target debt-equity is forecast at ~2.5x (currently ~5x).
- JetLite update** — All 24 aircraft will be operational from early FY09. The airline is expected to break even in FY09. The airline will be consolidated in Jet's operations from FY09. JetLite also has rights to fly internationally (*see page 2 for more takeaways*).

Sell/Medium Risk	3M
Price (11 Mar 08)	Rs630.85
Target price	Rs765.00
Expected share price return	21.3%
Expected dividend yield	1.3%
Expected total return	22.5%
Market Cap	Rs135,164M US\$3,346M

Price Performance (RIC: JET.BO, BB: JETIN IN)



Statistical Abstract

Year to	Net Profit (RsM)	Diluted EPS (Rs)	EPS growth (%)	P/E (x)	P/B (x)	ROE (%)	Yield (%)
31 Mar							
2006A	2,240	25.94	-39.7	24.3	2.4	10.4	1.0
2007A	-1,414	-16.38	-163.1	nm	2.4	-6.2	1.0
2008E	-5,968	-69.13	na	-9.1	2.7	-28.0	1.0
2009E	-2,766	-25.87	62.6	nm	1.8	-9.5	1.0
2010E	4,876	45.61	276.3	13.8	1.4	11.5	1.3

Source: Powered by dataCentral

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See Appendix A-1 for Analyst Certification and important disclosures.

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- **Fleet Expansion:** Management stated that the first round of expansion is almost complete, with only 4 of 30 aircraft to be delivered by Oct 08. Next round of expansion will require \$700-800m capex from FY10 onwards for purchase of 10 aircraft. The company plans to use 4:1 debt/equity mix for funding the capex requirement. The company is also looking at investors for placing 10% promoter stake before the rights issue to part fund the rights issue promoter funding requirement.

Jet Airways

Company description

Jet Airways is one of India's leading domestic airlines with around 22% market share (around 31% including Jet Lite). Long the leader in the domestic market, it has scaled up its international operations and now flies to several international destinations in the Asia Pacific region, as also to Europe. It plans to enter the North American market in FY08, and, subject to regulatory approval, the Middle East markets too. Jet has an aggressive fleet expansion plan, and it plans to increase its fleet to 97 planes at end FY11, from 61 planes at end FY07.

Investment strategy

We rate Jet Airways Sell/Medium Risk (3M) with a target price of Rs765. Jet is one of India's leading airlines with a market share of around 22% and arguably the best brand and service orientation. In the past, the domestic aviation sector grew at a sedate 6% and was characterized by low levels of competition and high airfares, accompanied by high costs due to regulation. But the situation has changed over the past few years. Economic growth and liberalization have stimulated demand for air travel, and the sector has been averaging growth of over 25% over the past few years. Given the strong base effect over the past few years, we expect growth rates to moderate over the medium term. Deregulation has also resulted in a substantial increase in seat capacity, which we estimate to grow at a CAGR of at least 20-22% over FY08E-10E. The industry has come full circle, with consolidation commencing among key players. Given the supply overhang, the benefits of consolidation are yet to be reflected - we believe that airline P&Ls will remain under pressure unless they meaningfully scale back capacity induction. A rapidly consolidating industry should also discourage the entry of new players in the industry. It should also help the domestic market to return to profitability over the next 2 years. The profitability of Jet's international operations is forecast to improve significantly, especially as routes mature over an 18-24 month period. We forecast profitability to improve substantially over FY09-10E, driven by expectations of relatively stable yields and declining costs /ASK.

Valuation

Airlines are trading plays – given the cyclical nature of their business, high operational and financial leverage and an earnings profile that is excessively volatile and sensitive to macro variables like oil prices and currency

movements. Given the excessive volatility in earnings of airlines, we prefer to utilize a more stable metric to value airlines. The price-to-book metric is a good fall-back measure for airlines, especially in times of distress, but it is not so appropriate for Jet Airways, which is entering a high growth phase, and wherein industry conditions (in the domestic market) are improving. We could also use a DCF valuation but as India is a high growth market and new players are entering a transition phase, predicting cash flows over a longer term is quite difficult in our view. Hence we stick to our preferred method of EV/EBITDAR. While Jet arguably has superior growth opportunities to most of the global full service carriers, but Jet has still to demonstrate its ability to deliver robust and consistent earnings over time, and strong sustainable market share in the face of aggressive competition. Nevertheless, Jet's market position within the domestic market is fairly well entrenched, and its international operations are proceeding at a satisfactory pace. We value Jet by rolling forward our EV/EBITDAR multiple to FY10E as we believe that FY09E is a transition year for Jet with the launch of new international routes. We retain our multiple of 7x as we roll forward. We accordingly assign a target price of Rs765 to Jet Airways.

Risks

Our Medium Risk rating on Jet Airways is in line with the risk ratings on peers in our regional coverage universe. We believe that Jet merits a Medium risk rating, given: a) the competitive scenario in the domestic market; b) its international operations are still at a relatively embryonic phase and should take at least 2-3 years to stabilize; and c) turnaround of the Air Sahara acquisition. Key upside risks to our recommendation and target price are: a) Faster than anticipated capacity rationalization in the domestic airline industry; b) A sustained decline in ATF prices; c) Faster than anticipated ramp up, and greater than forecast profitability of international operations; and d) Rapid restructuring and turnaround of Jet Lite.

Appendix A-1

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Jet Airways (JET.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Jamshed Dadabhojy (covered since March 1 2006)



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