Company Flash

12 November 2008 | 8 pages

Jet Airways (JET.BO)

Is there an Investor Waiting in the Wings? NO

- **What's new?** — Press reports (ET, Mint) indicate Jet is negotiating to sell a 10% equity stake to Temasek Holdings for consideration of Rs2.5bn. The company is also reportedly raising debt funds of Rs10bn from Abu Dhabi-based Mubadala Development Corporation to help fund working capital requirements.

- **Management denies this development** — Management has indicated these talks are speculative, and that the company has no plans to infuse equity or debt (from Mubadala). However, management has said that Jet plans to raise fresh debt funds to meet its working capital requirements.

- **What are Jet's funding requirements?** — We forecast Jet's cash losses at Rs31.3bn (over FY09E-10E) (after interest payments, but before principal repayments of c.US$280m). The company is trying to curb operational losses through various initiatives – cutting loss-making flights, reducing ticket commissions, etc. The biggest positive is the sharp fall in crude oil prices (<$60 vs. our FY10/11 estimates of $75/bbl). If crude prices continue to decline, there could be a substantial positive upside to our current numbers.

- **Capital structure remains adverse** — Mgmt indicated that P&L concerns could abate, especially if crude prices continue to decline significantly. Investor concerns on the balance sheet will continue, given the eroded networth and the high leverage. We reiterate our Sell (3H) rating; our discomfort stems from the fact that operating cash flows are fully utilised to meet debt servicing requirements. A balance sheet restructuring will be required to ensure that operating profits flow through to net profits.

Sell/High Risk	3H
Price (12 Nov 08)	Rs199.00
Target price	Rs167.00
Expected share price return	-16.1%
Expected dividend yield	1.5%
Expected total return	**-14.6%**
Market Cap	Rs17,180M US$362M

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

Statistical Abstract

Year to 31 Mar	Net Profit (RsM)	Diluted EPS (Rs)	EPS growth (%)	P/E (x)	P/B (x)	ROE (%)	Yield (%)
2007A	-1,414	-16.38	-163.1	-12.1	0.8	-6.2	3.0
2008A	-11,263	-130.46	na	-1.5	0.4	-34.7	3.0
2009E	-12,833	-148.65	-13.9	-1.3	0.5	-33.7	1.5
2010E	-14,330	-165.99	-11.7	-1.2	0.6	-46.9	1.5
2011E	-10,514	-121.78	26.6	-1.6	1.0	-47.4	1.5

Source: Powered by dataCentral

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

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Fiscal year end 31-Mar	2007	2008	2009E	2010E	2011E
Valuation Ratios					
P/E adjusted (x)	-12.1	-1.5	-1.3	-1.2	-1.6
EV/EBITDA adjusted (x)	16.1	nm	-11.4	nm	89.4
P/BV (x)	0.8	0.4	0.5	0.6	1.0
Dividend yield (%)	3.0	3.0	1.5	1.5	1.5
Per Share Data (Rs)					
EPS adjusted	-16.38	-130.46	-148.65	-165.99	-121.78
EPS reported	-16.38	-130.46	-254.74	-165.99	-121.78
BVPS	259.14	492.99	389.65	318.09	195.84
DPS	6.00	6.00	3.00	3.00	3.00
Profit & Loss (RsM)					
Net sales	70,578	102,456	129,512	114,825	124,338
Operating expenses	-71,098	-112,095	-150,187	-126,866	-131,325
EBIT	**-520**	**-9,639**	**-20,674**	**-12,040**	**-6,987**
Net interest expense	-2,402	-5,225	-7,579	-7,627	-7,592
Non-operating/exceptionals	3,435	6,757	6,032	11,834	910
Pre-tax profit	**514**	**-8,107**	**-22,221**	**-7,833**	**-13,668**
Tax	-234	1,568	4,444	1,958	3,417
Extraord./Min.Int./Pref.div.	-1,694	-4,723	-4,215	-8,455	-262
Reported net income	**-1,414**	**-11,263**	**-21,992**	**-14,330**	**-10,514**
Adjusted earnings	-1,414	-11,263	-12,833	-14,330	-10,514
Adjusted EBITDA	3,621	-1,621	-12,217	-3,924	1,591
Growth Rates (%)					
Sales	24.0	45.2	26.4	-11.3	8.3
EBIT adjusted	-110.0	nm	-114.5	41.8	42.0
EBITDA adjusted	-61.0	-144.8	-653.7	67.9	140.5
EPS adjusted	-163.1	-696.5	-13.9	-11.7	26.6
Cash Flow (RsM)					
Operating cash flow	**7,279**	**14,716**	**4,204**	**-2,900**	**-2,200**
Depreciation/amortization	4,141	8,018	8,458	8,116	8,577
Net working capital	2,755	14,946	4,365	-5,141	-526
Investing cash flow	**-27,997**	**-107,389**	**-14,632**	**10,125**	**-3,250**
Capital expenditure	-29,180	-107,975	-200	-200	-3,250
Acquisitions/disposals	1,183	586	-14,432	10,325	0
Financing cash flow	**10,641**	**87,165**	**9,269**	**-7,225**	**5,450**
Borrowings	11,607	61,490	8,520	-6,922	5,753
Dividends paid	-606	-606	-303	-303	-303
Change in cash	**-10,076**	**-5,508**	**-1,159**	**0**	**0**
Balance Sheet (RsM)					
Total assets	**107,254**	**215,570**	**218,981**	**199,994**	**196,855**
Cash & cash equivalent	10,966	9,584	4,500	4,500	4,500
Accounts receivable	6,039	13,990	15,967	14,157	15,329
Net fixed assets	72,920	172,877	178,954	160,713	155,386
Total liabilities	**84,882**	**173,010**	**185,343**	**172,533**	**179,948**
Accounts payable	7,498	20,354	25,397	20,838	21,640
Total Debt	60,563	122,053	130,573	123,651	129,404
Shareholders' funds	**22,373**	**42,560**	**33,639**	**27,461**	**16,907**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	5.1	-1.6	-9.4	-3.4	1.3
ROE adjusted	-6.2	-34.7	-33.7	-46.9	-47.4
ROIC adjusted	-1.1	-6.7	-9.9	-6.4	-2.4
Net debt to equity	221.7	264.3	374.8	433.9	738.8
Total debt to capital	73.0	74.1	79.5	81.8	88.4

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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, US, Europe and Middle East. Jet has an aggressive fleet expansion plan, and it plans to increase its fleet to 89 planes at end FY10, from 81 planes at end FY08.

Investment strategy

We rate Jet Airways Sell/High Risk (3H) with a target price of Rs167. 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 and slowing economy we expect decline in demand over the next 12-18 months. Deregulation has also resulted in a substantial increase in seat capacity, which we estimate to taper off significantly over the next two years. The industry has come full circle, with consolidation commencing among key players. Given the supply overhang and challenging global environment, the benefits of consolidation are yet to be reflected - we believe that airline P&Ls will remain under pressure unless they aggressively scale back capacity induction. A rapidly consolidating industry should also discourage the entry of new players in the industry. We expect domestic operations to face significant pressure on profitability due to sharp depreciation in rupee vs. dollar, slowing passenger demand and intense competitive environment. We expect Jet's international operations will be better placed than domestic operations due to less competition and lower fuel prices.

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. Our preferred method for valuing Jet was EV/EBITDAR but we believe earnings are rendered futile in this challenging environment. Our target price of Rs167 is based on replacement cost methodology which is a slight deviation from our earlier method of a simple average of 2 methodologies - current equity value (based on residual cost) and 1 year forward price / book of 1x. Our estimates of plane prices are based our European aviation analyst Andrew Light’s view on expected decline in asset prices in this challenging environment. We also note that if asset prices would fall by further 10% from our current estimates then Jet’s equity value would be negative implying Jet won’t be able to service its debt and long term liabilities even if sells its assets.

Risks

Our High Risk rating on Jet Airways is in line with our quantitative risk rating system, which tracks 260-day share price volatility. We believe that Jet merits a High 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 another 12-18 months to stabilize; and c) its highly leveraged balance sheet. 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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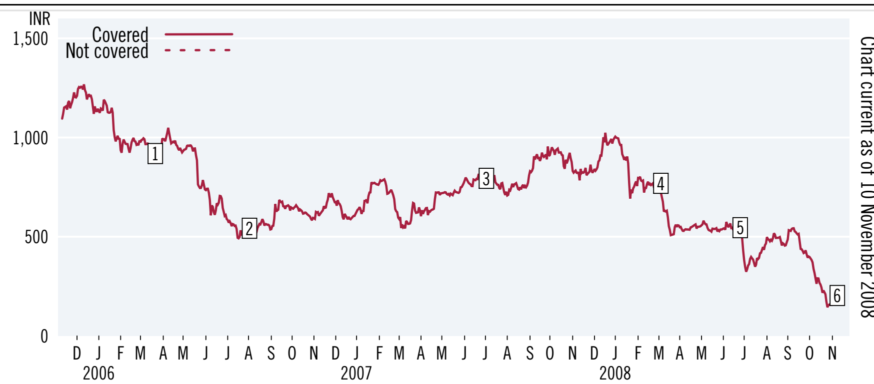
Jet Airways (JET.BO)

Ratings and Target Price History
Fundamental Research

Analyst: Jamshed Dadabhoy
Covered since March 1 2006



	Date	Rating	Target Price	Closing Price
1	22-Mar-06	*2H	*1,127.00	919.15
2	2-Aug-06	*3H	*390.00	526.85
3	3-Jul-07	*3M	*716.00	801.85
4	5-Mar-08	3M	*765.00	721.95
5	25-Jun-08	3M	*440.00	543.95
6	10-Nov-08	*3H	*167.00	202.20

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

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