

RESULT UPDATE

Bharti Airtel

Maintain Outperformer

Price: Rs 583

BSE Index: 8,779

22 January 2009

Share Data

Reuters code	BRTLBO
Bloomberg code	BHARTIIN
Market cap. (US\$ mn)	22,536
6M avg. daily turnover (US\$ mn)	80.4
Issued shares (mn)	1,898
Target price (Rs)	778

Performance (%)	1M	3M	12M
Absolute	(19)	(20)	(30)
Relative	(7)	(2)	41

Valuation Ratios

Yr to 31 Mar	FY09E	FY10E
EPS (Rs)	45.2	48.7
+/- (%)	28.0	7.8
PER (x)	12.9	12.0
PBV (x)	3.5	2.7
EV/Sales (x)	3.2	2.8
EV/EBITDA (x)	7.8	7.0

Major shareholders (%)

Promoters	67
FII's	23
MF's	3
BFST's	3
Public & Others	4

Financial highlights

(Rs mn)	2QFY09	3QFY09	QoQ (%)	2QFY08	YoY (%)	FY08	FY09E	YoY (%)	FY10E	YoY (%)
Net Sales	90,203	96,334	6.8	69,639	38.3	270,250	373,458	38.2	425,741	14.0
EBITDA	36,993	39,452	6.6	29,634	33.1	113,398	152,646	34.6	171,062	12.1
EBITDA Margin (%)	41.0	41.0	-	42.6	-	42.0	40.9	-	40.2	-
Other Income	274	239	(12.8)	643	(62.8)	2,739	988	(63.9)	1,450	46.8
Interest	5,741	1,904	(66.8)	810	135.1	2,341	10,467	347.1	3,390	(67.6)
Depreciation	11,549	12,704	10.0	10,377	22.4	37,260	47,543	27.6	61,445	29.2
PBT	19,724	24,629	24.9	19,032	29.4	76,536	95,624	24.9	107,677	12.6
Extraordinary income	(508)	(478)	(5.9)	(244)	95.9	(1,150)	(1,626)	41.4	(1,405)	(13.6)
Tax	(1,247)	2,558	(305.1)	1,564	63.6	8,378	8,162	(2.6)	13,747	68.4
Reported PAT	20,463	21,593	5.5	17,224	25.4	67,008	85,835	28.1	92,525	7.8
Adj. PAT	20,971	22,071	5.2	17,468	26.3	68,158	87,462	28.3	93,930	7.4
Adj. PAT margin (%)	23.2	22.9	-	25.1	-	25.2	23.4	-	22.1	-
EPS (Rs)	10.8	11.4	5.5	9.1	25.2	35.3	45.2	28.0	48.7	7.8

3QFY09 Result – In-line results, tariff decline remains a concern

Results are in line with our estimates. Topline increased by 6.8% QoQ, to Rs 96,334 mn. Strong subscriber additions, with a relatively lower decline in average revenue per user (compared to last quarter), supported this growth. The EBITDA margin is maintained at 41%. The forex loss for 3QFY09 is Rs 2,221 mn, against Rs 5,862 mn in 2QFY09. PAT increased to Rs 21,593 mn, a sequential growth rate of 5.5%. Capex is in line with FY09E guided figure of US\$ 3.5 bn.

Operationally, average revenue per user (ARPU) declined by 2.1% QoQ, to Rs 324. Minutes of Usage (MoU) also declined by 4% QoQ, to 505 minutes. 1,389 towers are added during the quarter, taking the total count to 61,355.

Because of its high population coverage (79%) and a strong brand, we expect the company to maintain its subscriber addition rate. However, we expect tariffs to decline at a faster pace in the coming years, because of an increased competition. Bharti Airtel, because of a high usage elasticity (increasing MoU with reducing tariffs), will be the least impacted one, among all the telcos. Still, the revenue growth is expected to come down. 3G auctions will increase the capex requirement, without significantly contributing to the financials.

On account of the change in tariff assumptions, we have reduced valuation for its core business to Rs 586 per share, from Rs 702 earlier. Bharti Infratel's share, to overall valuation, is maintained at Rs 192. The stock trades at 13x FY09E earnings and 12x FY10E earnings. Maintain Outperformer, with a target price of Rs 778.

Key highlights

- **EBITDA margin:** EBITDA margin remained flat, at 41%. We were anticipating a decline in the EBITDA margin. Reduction in access and interconnect costs negated the increase in network operation costs.

- **Segmental details:** Enterprise-Corporate segment showed a QoQ decline. This is because of a high base effect, as last quarter, Bharti finished several key projects and revenue booking was high. Details of DTH operation were not provided separately. For segment-wise result break-up, refer to Appendix 1.
- **Operational details:** ARPU declined by 2.1% QoQ, to Rs 324. Minutes of Usage (MoU) also declined by 4% QoQ, to 505 minutes. MoU declined because company discontinued certain free and discounted minutes. Another important operational aspect is reduction in churn rate, from 3.1% in 2QFY09, to 2.8% in 3QFY09. For detailed quarterly comparison of operational parameters, refer to Appendix 2.
- **Passive-infrastructure business:** 1,389 towers are added during the quarter, taking the total count to 61,355 (35,066 towers belong to Indus Towers). Tenancy ratio increased to 1.34, from 1.26 last quarter. Indus Towers has indigenously erected 10,433 towers during April to December 2008. In 4QFY09E, 35,066 towers will be transferred to Indus Towers and accordingly, joint venture accounting will be used.
- **Capex and debt:** Bharti Airtel incurred a capex of Rs 39 bn during the quarter. So far, in FY09E, the company had incurred a capex of Rs 111 bn, in line with the guided capex figure of US\$ 3.5 bn for FY09E. Net debt increased to Rs 65 bn, from Rs 51 bn last quarter. Net debt-to-equity ratio is at 0.22. Debt figure also includes Rs 33 bn worth fully and compulsorily convertible debentures, issued to foreign investors for their investments in Bharti Infratel.

Outlook

Balance sheet is robust and 3G funding is not a concern. However, 3G's commercial success remains doubtful. We expect its performance ratios to come down after the 3G implementation. Because of its high network coverage and a strong brand, we expect the company to maintain its subscriber addition rate. However, we expect tariffs to decline at a faster pace in the coming years, because of an increased competition. RCom's GSM launch has forced operators to slash the entry point rates for new subscribers. We expect the industry to witness further rounds of tariff cut, in order to grab market share. Bharti Airtel, because of a high usage elasticity (increasing MoU, with reducing tariffs), will be the least impacted one, among all the telcos. Still, the revenue growth is expected to come down.

New estimates

	ARPM (Rs/min)			ARPU (Rs/subs/month)			Total revenue (Rs mn)		
	Old	New	Change (%)	Old	New	Change (%)	Old	New	Change (%)
FY08	0.77	0.77	0.0	370	370	0.0	270,250	270,250	0.0
FY09E	0.61	0.61	0.0	329	318	(3.4)	372,758	373,458	0.2
FY10E	0.52	0.51	(2.6)	292	270	(7.4)	441,040	425,741	(3.5)
FY11E	0.47	0.44	(5.7)	269	239	(11.0)	475,493	443,447	(6.7)
FY12E	0.47	0.43	(7.9)	267	231	(13.3)	507,895	467,136	(8.0)

Assumption: We are not changing our revenue estimates for other segments.

Valuation

We have done DCF calculations to value its core business and its passive infrastructure business.

- 1. Core business:** Because of the change in tariff assumptions, valuation for its core business has reduced to Rs 586 per share, from Rs 702 earlier. We are maintaining our EBITDA margin estimates, which take into account tower rentals outgo (to its tower companies) and a negative impact of reducing tariffs.
- 2. Passive Infrastructure business:** We maintained the valuation of Indus Towers at Rs 706 bn. Bharti Infratel's 42% stake is valued at Rs 296 bn or Rs 156 per share. We value Bharti Infratel's operation in six circles (non-overlapping to Indus' operation) at Rs 109 bn or Rs 57 per share. Adjusting for 10% stake dilution to foreign investors, Bharti Infratel contributes Rs 192 to Bharti Airtel's valuation.

We maintain Outperformer rating for the stock, with a revised target price of Rs 778. At current price, the stock trades at 13x FY09E earnings and 12x FY10E earnings. Key risks to our Outperformer rating are:

- A higher than anticipated tariff decline.
- Over-bidding in 3G spectrum auctions.
- Pending regulatory issues like increase in 3G base reserve price, reducing termination charges, imposing one time fees for spectrum allocation over 6.2 MHz, etc.

Appendix 1: Segment-wise performance

(Rs mn)	3QFY09	2QFY09	QoQ (%)	3QFY08	YoY (%)
Mobile revenue	79,392	72,843	9.0	56,105	41.5
Contribution to service revenue (%)	82.4	80.8	–	80.6	–
EBITDA	24,963	22,009	13.4	22,887	9.1
EBITDA margin (%)	31.4	30.2	–	40.8	–
EBIT	18,403	15,728	17.0	15,345	19.9
EBIT margin (%)	23.2	21.6	–	27.4	–
Telemedia revenue	8,458	8,486	(0.3)	7,307	15.8
Contribution to service revenue (%)	8.8	9.4	–	10.5	–
EBITDA	3,531	3,696	(4.5)	3,173	11.3
EBITDA margin (%)	41.7	43.6	–	43.4	–
EBIT	1,969	2,270	(13.3)	1,592	23.7
EBIT margin (%)	23.3	26.7	–	21.8	–
Enterprise-Carriers revenue	17,733	17,002	4.3	11,346	56.3
Contribution to service revenue (%)	18.4	18.8	–	16.3	–
EBITDA	8,050	7,351	9.5	3,652	120.4
EBITDA margin (%)	45.4	43.2	–	32.2	–
EBIT	6,936	6,352	9.2	2,837	144.5
EBIT margin (%)	39.1	37.4	–	25.0	–
Enterprise-Corporate revenue	4,075	4,872	(16.4)	3,290	23.9
Contribution to service revenue (%)	4.2	5.4	–	4.7	–
EBITDA	1,749	2,018	(13.3)	1,377	27.0
EBITDA margin (%)	42.9	41.4	–	41.9	–
EBIT	1,323	1,619	(18.3)	1,215	8.9
EBIT margin (%)	32.5	33.2	–	36.9	–
Passive Infrastructure revenue	12,702	11,983	6.0	–	–
Contribution to service revenue (%)	13.2	13.3	–	–	–
EBITDA	4,258	3,991	6.7	–	–
EBITDA margin (%)	33.5	33.3	–	–	–
EBIT	436	1,185	(63.2)	–	–
EBIT margin (%)	3.4	9.9	–	–	–
Eliminations & Others-revenue	(26,026)	(24,983)	4.2	(8,409)	209.5
Contribution to service revenue (%)	(27.0)	(27.7)	–	(12.1)	–

Source: Company, B&K Research

Appendix 2: Operating metrics

Operating metrics	3QFY09	2QFY09	QoQ (%)	3QFY08	YoY (%)
Wireless					
Subs Base-period end (mn)	85.65	77.48	10.5	55.16	55.3
Market share-cop (%)	25.1	25.0	–	24.8	–
Net Adds market share (%)	25.9	28.5	–	25.7	–
SMS as % of mobile revenue	4.1	4.3	–	4.4	–
Non-voice as % of mobile revenue	9.5	10.0	–	9.3	–
prepaid % in net adds	99.6	98.4	–	95.4	–
Prepaid customer base (% of total subs)	93.5	92.9	–	91.0	–
Postpaid Churn (%)	1.2	1.4	–	1.8	–
Prepaid Churn (%)	2.9	3.2	–	3.9	–
Total minutes (mn min)	123,626	115,834	6.7	73,840	67.4
ARPU (Rs/subs/month)	324	331	(2.1)	358	(9.5)
MoU (min/subs/month)	505	526	(4.0)	474	6.5
ARPM (Rs/min)	0.64	0.63	2.0	0.76	(15.1)
EBITDA/subs/month (Rs/subs/month)	102	100	2.0	147	(30.4)
EBITDA/min (Rs/min)	0.20	0.19	6.3	0.31	(34.9)
Population coverage (%)	79	77	–	68	–
Passive infrastructure					
Tower base (Nos.)	61,355	59,966	2.3	–	–
Average monthly tower rentals (Nos.)	31,488	32,177	(2.1)	–	–
Tenancy ratio (x)	1.34	1.26	–	–	–
Broadband					
Subscribers (in '000s)	2,619	2,509	4.4	2178	20.2
ARPU (Rs/subs/month)	1,098	1,147	(4.3)	1140	(3.7)
DSL penetration (%)	37.9	36.7	–	34.5	–
Enterprise-Carrier					
Optical fiber length (RKms)	90,205	83,389	8.2	67138	34.4
NLD minutes on network (mn)	11,609	11,349	2.3	7,898	47.0
ILD minutes on network (mn)	2,603	2,284	14.0	1,591	63.6

Source: Company, B&K Research

Income Statement

Yr end 31 Mar (Rs mn)	FY07	FY08	FY09E	FY10E
Net sales	184,202	270,250	373,458	425,741
<i>Growth (%)</i>	<i>57.9</i>	<i>46.7</i>	<i>38.2</i>	<i>14.0</i>
Operating expenses	(109,858)	(156,852)	(220,812)	(254,679)
Operating profit	74,344	113,398	152,646	171,062
Other operating income	0	0	2640	150,006
EBITDA	74,344	113,398	152,646	171,062
<i>Growth (%)</i>	<i>79.1</i>	<i>52.5</i>	<i>34.6</i>	<i>12.1</i>
Depreciation	(26,190)	(37,260)	(47,543)	(61,445)
Other income	1,119	2,739	988	1,450
EBIT	49,272	78,877	106,091	111,067
Interest paid	(2,488)	(2,341)	(10,467)	(3,390)
Pre-tax profit	46,784	76,536	95,624	107,677
(before non-recurring items)				
Pre-tax profit	46,784	76,536	95,624	107,677
(after non-recurring items)				
Tax (current + deferred)	(5,680)	(8,378)	(8,162)	(13,747)
Net profit	41,103	68,158	87,462	93,930
Adjusted net profit	40,621	67,008	85,835	92,525
<i>Growth (%)</i>	<i>100.3</i>	<i>65.0</i>	<i>28.1</i>	<i>7.8</i>
Minority interests	(482)	(1,150)	(1,626)	(1,405)
Net income	40,621	67,008	85,835	92,525

Balance Sheet

Yr end 31 Mar (Rs mn)	FY07	FY08	FY09E	FY10E
Current assets	44,843	113,783	121,219	111,771
Investments	682	108	700	750
Net fixed assets	224,719	326,611	443,881	541,249
Other non-current assets	27,644	32,143	30,263	31,723
Total assets	297,888	472,644	596,063	685,493
Current liabilities	95,724	134,787	142,069	142,844
Total Debt	52,461	97,063	125,366	122,986
Other non-current liabilities	12,350	15,195	16,132	14,645
Total liabilities	160,534	247,045	283,567	280,475
Share capital	18,959	18,979	18,980	18,977
Reserves & surplus	116,594	198,063	284,960	377,485
Shareholders' funds	135,553	217,042	303,941	396,462
Minorities interests	1,801	8,556	8,556	8,556
Total equity & liabilities	297,888	472,644	596,063	685,493

Cash Flow Statement

Yr end 31 Mar (Rs mn)	FY07	FY08	FY09E	FY10E
Pre-tax profit	46,784	76,536	95,624	107,677
Depreciation	26,190	37,260	47,543	61,445
Chg in working capital	22,327	12,180	(3,608)	(10,044)
Total tax paid	(5,572)	(6,693)	(8,263)	(13,947)
Cash flow from oper. (a)	89,729	119,283	131,295	145,131
Capital expenditure	(93,626)	(139,151)	(164,301)	(164,059)
Chg in investments	530	(45,507)	11,542	20,580
Cash flow from inv. (b)	(93,095)	(184,659)	(152,759)	(143,479)
Free cash flow (a+b)	(3,366)	(65,375)	(21,463)	1,652
Equity raised/(repaid)	302	15,577	934	(3)
Chg in minorities	362	5,605	(1,626)	(1,405)
Debt raised/(repaid)	5,066	44,602	28,303	(2,380)
Other financing activities	501	27	129	0
Cash flow from fin. (c)	6,230	65,811	27,739	(3,788)
Net chg in cash (a+b+c)	2,864	436	6,276	(2,137)

Key Ratios

Yr end 31 Mar (%)	FY07	FY08	FY09E	FY10E
EPS (Rs)	21.4	35.3	45.2	48.7
EPS growth	98.1	64.8	28.0	7.8
EBITDA margin	40.4	42.0	40.9	40.2
EBIT margin	26.7	29.2	28.4	26.1
RoCE	27.8	29.2	26.8	22.3
Net debt/Equity	31.3	18.7	24.6	22.7

Valuations

Yr end 31 Mar (x)	FY07	FY08	FY09E	FY10E
PER	27.2	16.5	12.9	12.0
PCE	16.6	10.6	8.3	7.2
Price/Book	8.1	4.9	3.5	2.7
Yield (%)	0.0	0.0	0.0	0.0
EV/Net sales	6.2	4.3	3.2	2.8
EV/EBITDA	15.5	10.1	7.8	7.0

Du Pont Analysis – ROE

Yr end 31 Mar (x)	FY07	FY08	FY09E	FY10E
Net margin (%)	22.1	24.8	23.0	21.7
Asset turnover	0.7	0.7	0.7	0.7
Leverage factor	2.2	2.1	2.0	1.8
Return on equity (%)	35.2	36.9	31.9	25.8

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