Industry In-Depth

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Indian Wireless

Landscape A-Changing? Growth Potential Intact Though

- **Hutch or no Hutch, we remain bullish** – No matter how we look at HTIL, the big picture remains positive – If HTIL sells, 1) sale to an existing operator (e.g. RCOM) would likely bring consolidation – a welcome catalyst, in our view; 2) sale to an outsider (e.g. Vodafone) wouldn't change the competitive landscape either. We think any deal valuation would reflect the sector's strong growth.

- **Strong business; upgrading estimates** – With robust subscriber growth also driving strong growth in long distance, we are raising our estimates and target prices across the board for Indian wireless. Bharti remains our top pick and we continue to like RCOM, HTIL and TTML.

- **Hutch Essar (HE): no guts, no glory?** – Potential suitors include RelCom, Vodafone, Essar, Maxis, Orascom and private equity (separately or in tandem, according to media reports). Although HE is an attractive asset in one of the few the remaining wireless growth areas globally, key to the deal is valuation.

- **Best fit for RCOM and good for the sector** – With the least regulatory hurdles for RCOM, HE's good fit by footprint, and dissipating GSM spectrum and entry constraints, RCOM stands to gain the most from buying HE, in our view. Besides becoming the industry leader, RCOM could achieve cost savings and industry consolidation. Significant overpayment or a loss to Vodafone are risks, however.

- **Opportunity to Buy Bharti if Vodafone succeeds** – If Vodafone succeeds in acquiring Hutch Essar, it would have to exit its 10% stake in Bharti. We see any related stock weakness as a buying opportunity.

Rahul Singh[1]
+91-22-6631-9863
rahul.r.singh@citigroup.com

Anand Ramachandran, CFA[2]
Head of Asian Telecoms
+852-2501-2448
anand.ramachandran@citigroup.com

Supriya Gupte[1**]
supriya.gupte@citigroup.com

Figure 1. Indian Wireless – Valuation Comparisons

Company	RIC	Rating	Price (Rs) 1-Jan-07	Target Price (Rs)	PE (x) 06E/ FY07E	PE (x) 07E/ FY08E	EPS CAGR*	EV/EBITDA (x) 06E/ FY07E	EV/EBITDA (x) 07E/ FY08E	DY (%) 06E/ FY07E	DY (%) 07E/ FY08E
Bharti	BRTI.BO	1L	628.9	750.0	30.4	20.8	46.5%	16.8	11.8	0.3%	0.7%
Rel. Cns	RLCM.BO	1M	471.3	570.0	34.3	22.7	130.2%	18.2	12.6	0.4%	0.6%
HTIL	2332.HK	1M	19.6	24.0	209.2	62.6	NM	12.7	9.9	0.0%	0.0%
Regional Cellular Peers Avg					21.3	17.5		8.8	7.2	2.4%	2.7%
Regional Integrated Peers Avg					15.6	14.4		6.8	6.1	3.3%	3.6%

Note: year-end 31 March for Bharti and RCVL, 31 Dec for HTIL; *05-08E/FY06-FY09E EPS CAGR

Source: Company data, Citigroup Investment Research estimates

See page 48 for Analyst Certification and important disclosures.

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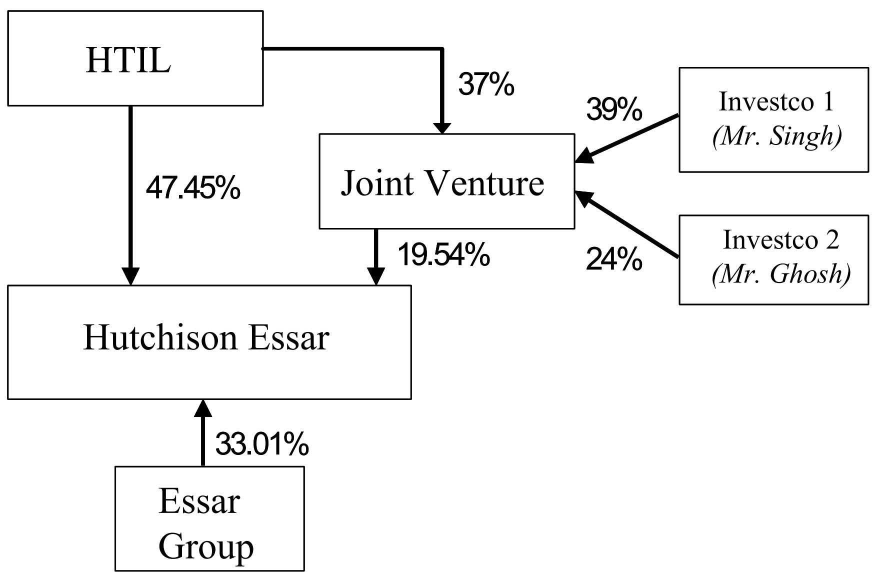
Dissecting a Potential HTIL Exit – We Remain Bullish

As outlined below, HTIL owns an effective 67% stake in Hutch Essar (this includes HTIL's rights to acquire 97% fully diluted share capital of both investment holding companies by Messrs Singh and Ghosh. We would not expect the consideration for these stakes to be material.

We are perplexed at this apparent inclination to exit India. What drives this? We think the lack of any improvement in relations with Essar coupled with the ability to perhaps realize significant valuation premiums both hold. Relations with Essar have always been blow-hot/ blow-cold, in our view. The BPL Mumbai dispute last year was the first public manifestation of the discord. We see the crux of the disagreements with Essar as the Essar Group wanting more control in shareholder changes at the HTIL level (Orascom holds a 19.3% stake and HWL has 49%). With this background, growth expectations for Indian wireless appear red-hot (as do valuations). If the requisite valuation premium is available – it is very possible that HTIL might exit.

Figure 2. Hutch Essar: Shareholding Structure



Source: Citigroup Investment Research

HTIL's exit could be positive at the margin

Potential suitors are many and include RelCom, Vodafone, Essar, Maxis, Orascom and private equity (separately or in tandem, according to media reports). We see RCOM and Vodafone as the front-runners in any bid to acquire HE.

- If RCOM wins: A successful acquisition would not only be positive for RCOM but would also improve sector dynamics, with the top three players controlling 80% of the market. It would also imply an earlier-than-expected round of consolidation in the sector. This would be positive at the margin given the fragmented market currently with most circles having 5-6 operators. Such a market structure would increase the probability of rational competitive behavior and would raise the bar for new entrants.

- **If Vodafone wins**: Acquisition of HE by Vodafone would not alter the market dynamics per se – i.e. the number of operators would stay the same. First, we think any deal valuation (with a control premium) could have a positive side effect on the valuations of listed stocks relative to Bharti and RCOM. Second, an acquisition at rich valuations would only increase the chances of Vodafone being rational (especially in the context of Vodafone's investment criteria) in future endeavors with regard to the asset, which again would be positive for the sector. This could also mean an acceleration in the industry's collaborative efforts vis-à-vis tower sharing, etc. Lastly, Vodafone would likely have to exit its 10% stake in Bharti. In our view, any overhang-related weakness in Bharti stock would be a buying opportunity.

Figure 3. Indian Wireless - Market Share by Circles (as at November 2006)

	Bharti	BSNL+MTNL	RCOM	Hutch-Essar	Tata Tele	Others	Total
Delhi	25.2%	11.3%	18.5%	20.1%	12.8%	12.1%	100.0%
Mumbai	18.4%	14.3%	22.4%	26.2%	6.9%	11.7%	100.0%
Chennai	22.5%	17.4%	16.1%	15.6%	3.5%	25.0%	100.0%
Calcutta	18.9%	12.4%	29.6%	26.5%	12.6%		100.0%
Maharashtra	20.2%	17.7%	20.3%	10.0%	7.4%	24.4%	100.0%
Gujarat	14.4%	10.4%	17.2%	37.5%	3.3%	17.1%	100.0%
A.P.	29.1%	15.2%	24.5%	12.2%	4.2%	14.8%	100.0%
Karnataka	35.3%	15.1%	17.1%	15.3%	10.6%	6.6%	100.0%
T.N.	17.5%	22.5%	18.0%	8.6%	6.6%	26.8%	100.0%
Kerala	12.3%	28.7%	21.3%	11.7%	5.3%	20.7%	100.0%
Punjab	34.0%	9.4%	10.0%	13.6%	8.2%	24.9%	100.0%
Haryana	20.9%	19.4%	14.1%	18.2%	5.7%	21.7%	100.0%
U.P.(W)	13.5%	18.0%	20.2%	19.3%	6.8%	22.3%	100.0%
U.P.(E)	14.1%	29.2%	21.6%	28.5%	5.0%	1.5%	100.0%
M.P.	16.9%	25.9%	35.2%		1.1%	20.9%	100.0%
Rajasthan	25.4%	19.2%	21.6%	20.4%	10.8%	2.6%	100.0%
W.B. & A & N	14.1%	21.7%	26.5%	22.9%	11.7%	3.0%	100.0%
H.P.	37.0%	25.7%	15.3%		21.3%	0.7%	100.0%
Bihar	33.3%	22.3%	37.6%		6.8%		100.0%
Orissa	29.4%	26.7%	28.6%		11.0%	4.3%	100.0%
J&K	45.0%	49.7%	0.0%			5.3%	100.0%
Assam	28.6%	25.5%	18.9%			27.0%	100.0%
N.E.	13.3%	59.2%	10.4%			17.1%	100.0%
Total	22.3%	18.7%	21.0%	16.4%	7.2%	5.7%	100.0%

Source: Cellular Operators Association of India (COAI) , Association of Unified Service Providers of India (AUSPI) , Citigroup Investment Research

Dissecting the suitors list

RCOM has the most to gain from acquiring Hutch Essar, in our view

RCOM's GSM presence has minimal overlap with Hutch's India footprint of 16 circles (see the figure below). We believe RCOM is likely to be among the strongest bidders (among the others: Vodafone, Maxis, Orascom and Essar) for the following reasons:

- RCOM has been increasingly unequivocal about its shift to GSM given affordability constraints in the CDMA eco-system, especially for a developing market.

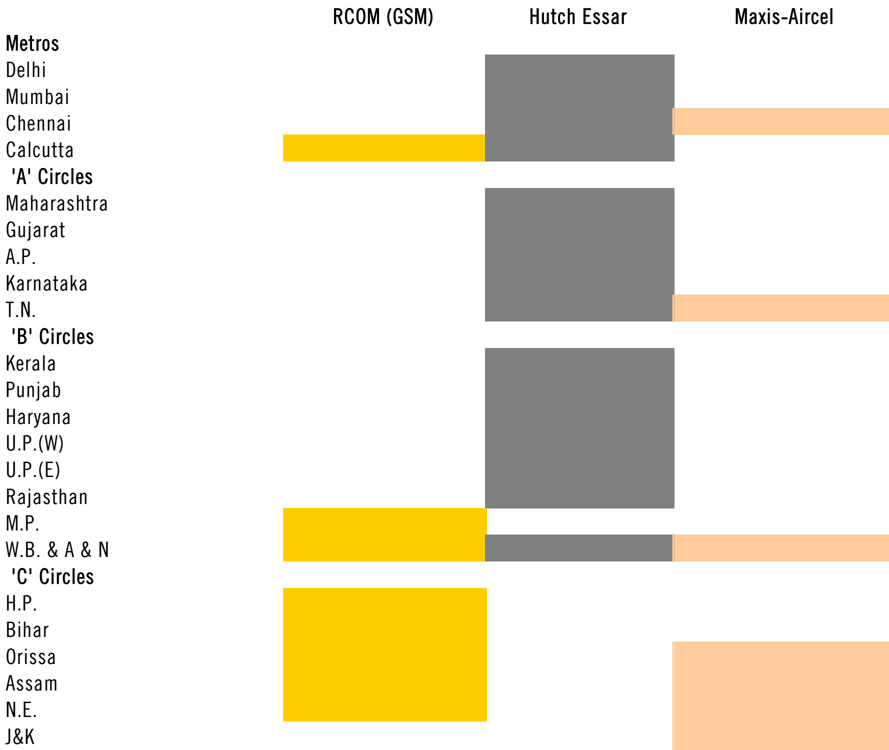
- Spectrum constraints for 2G services could delay RCOM's plans and prolong the period for which RCOM would have to settle for sub-optimal market share as a CDMA operator. Acquisition of an existing player therefore sidesteps the main hurdle. Besides, Hutch also has spectrum in the 900Mhz band in the majority of its circles, thereby providing an added incentive.

- Though integration efforts would come with challenges, offsets would include: a) reducing the time to market; and b) eliminating the risks accompanying greenfield GSM overlay and sub-optimal cost structures.

- 100% acquisition by RCOM would also not breach FDI norms, unlike for other suitors such as Vodafone, Maxis, Orascom, who might need a local partner.

- Lastly, acquisition of HE would make RCOM the market share leader with a 36.8% share compared with Bharti's 22%. This could open up possibilities of scale benefits for RCOM.

Figure 4. Footprint Matrix



Source: Citigroup Investment Research, Shaded portions represent circles of active presence

Vodafone – The next strongest bidder after RCOM

Vodafone has also confirmed its interest in Hutch-Essar. This is consistent with Vodafone's stated strategy of an opportunistic emerging market expansion; its balance sheet provides funding flexibility at 1.5x Debt/EBITDA. The hurdles faced by Vodafone, in our view, include the following:

- Exit of its 10% economic interest in Bharti Airtel;

- Compliance with the 74% FDI guideline that requires a local partner; and

- The need to allay investor concerns about over-valuation in its pursuit of growth markets, especially in the context of its investment criteria (IRR > Local WACC + 200bps).

While this would also entail a switch for Vodafone from its stake in #1 (Bharti) to the #4 operator (Hutch Essar), we do not see the issue as material given (1) it would get a majority stake opportunity in HE versus its existing minority stake in Bharti; and (2) the under-penetration and small difference in market share among the top four operators. We would also point out that HE's acquisition by RCOM might not be in Bharti's interest because it would create a clear market leader (with 36.8% market share). This raises the potential that Bharti might actually assist in Vodafone's cause – initially through the waiver of the non-compete clause in the case of Vodafone's exit from its 10% stake, and later through potential infrastructure sharing.

Others could join the fray too – Essar, a crucial hinge, in our view

- Essar: Never say never – Since Essar Group has the first right of refusal and has been visibly reluctant to play ball with potential suitors, it should not be ignored. Moreover, funding would be key to Essar's ambitions, especially if the control premium reaches 20% or more.

- Maxis-Aircel: Caught in two minds – Maxis-Aircel could also be an interested party (given their operations in just seven circles out of nine licenses so far), although we think it may not be as aggressive as RCOM, judging by its decision to pay the entry fee for 14 new circles last month. According to media reports, Maxis's relatively lower bid of US$13.5bn was previously rejected by Hutch.

- Orascom: Ground slipping beneath its feet – Orascom's intentions are unclear to us, although its 19% stake in HTIL makes it a potential buyer, especially given that Orascom's stake in HTIL (acquired in December 2005) was principally driven by its Hutch Essar exposure.

Merger guidelines imply minimal hurdles for RCOM

The Dot guidelines for intra-circle M&A prescribe the following:

- If, consequent to the merger under consideration, the number of operators in any circle/served market falls below three, the merger would not be allowed by the Competent Authority.

- Detailed examination by the Competent Authority indicates that if: (a) the market share of the merged entity is greater than 50%; and (b) the concentration ratio of the top two firms in a post-merged scenario is greater than or equal to 75%. If RCOM were to acquire HE, then the guidelines would be violated in three of the 16 overlapping circles vis-à-vis Calcutta, UP (East) and Gujarat. The guidelines, however, do not specify who the "Competent authority" is and what the remedial measures are in case the 50/75% criteria that is mentioned above were to be exceeded. Given the likely launch by new entrants in the sector – i.e. Maxis- Aircel, TM-Spice, etc., – we believe that the DoT may take a slightly more liberal approach on this issue. Furthermore, the market share calculation (see below) includes RCOM's FWTs, which might get excluded.

Figure 5. RCOM's Acquisition Plans May Face Some Scrutiny in 3 Circles

	Market Share of RCOM+Hutch	Market Share of (RCOM+Hutch) and next largest operator
Delhi	39%	64%
Mumbai	49%	67%
Chennai	32%	54%
Calcutta	56%	75%
Maharashtra	30%	55%
Gujarat	55%	72%
A.P.	37%	66%
Karnataka	32%	68%
T.N.	27%	49%
Kerala	33%	62%
Punjab	24%	57%
Haryana	32%	54%
U.P.(W)	39%	62%
U.P.(E)	50%	79%
Rajasthan	42%	67%
W.B. & A & N	49%	71%

Note: Markets shares based on Nov-06 subs numbers

Source: Citigroup Investment Research, COAI, AUSPI

- The spectrum of the merged entity would be capped at 15Mhz for Metro and A-category circles, and 12.4Mhz for Category B an C circles. The surplus spectrum would have to be returned. Given that most of the overlaps for RCOM are in its CDMA circles where the allocated spectrum is 2.5-5.0 MHz, RCOM would have to return spectrum in only three circles (see table below). Everything else remaining equal, this number (three in the case of RCOM) would be much lower if HE was to be acquired by an incumbent GSM operator.

Figure 6. Spectrum Regulations

	Spectrum allocated			Post-merger	Spectrum
All Figures in Mhz	RCOM	Hutch	Total	allowance	surrender reqd
Delhi	5.0	10.0	15.0	15.0	0
Mumbai	5.0	12.0	17.0	15.0	2
Chennai	5.0	8.0	13.0	15.0	0
Calcutta	11.2	8.0	19.2	15.0	4.2
Maharashtra	5.0	6.2	11.2	15.0	0
Gujarat	3.8	10.0	13.8	15.0	0
A.P.	5.0	8.0	13.0	15.0	0
Karnataka	5.0	8.0	13.0	15.0	0
T.N.	3.8	6.2	10.0	15.0	0
Kerala	3.8	6.2	10.0	12.4	0
Punjab	3.8	6.2	10.0	12.4	0
Haryana	3.8	6.2	10.0	12.4	0
U.P.(W)	3.8	6.2	10.0	12.4	0
U.P.(E)	5.0	8.0	13.0	12.4	0.6
Rajasthan	3.8	6.2	10.0	12.4	0
W.B. & A & N	10.0	4.4	14.4	12.4	2.0

Source: Citigroup Investment Research

Any deal would likely come with a significant control premium

Given Hutch's footprint and scale, lack of alternate acquisition targets, majority control on offer and Essar's apparent reluctance to play ball, the bid would have to be attractive. We believe that a control premium could be meaningful beyond the equity value of US$15bn, which is factored into our sum-of-the-parts valuation as well as the current market price.

Figure 7. Stake Value and Implied HE Valuations at Various Price Points

	100% equity value	Net debt	Firm Value	HTIL stake value	Implied EV/EBITDA		Implied P/E	
	(A) (US$m)	(B) (US$m)	(A+B) (US$m)	(HK$)	2007E	2008E	2007E	2008E
10% discount	13,528	2,185	15,713	14.78	14.3	10.5	23.5	16.6
5% discount	14,280	2,185	16,465	15.60	14.9	11.0	24.9	17.5
CIR base case	15,031	2,185	17,217	16.42	15.6	11.5	26.2	18.4
10% premium	16,535	2,185	18,720	18.06	17.0	12.5	28.8	20.3
20% premium	18,038	2,185	20,223	19.70	18.3	13.5	31.4	22.1
30% premium	19,541	2,185	21,726	21.35	19.7	14.5	34.0	24.0

Source: Citigroup Investment Research estimates

Hutch Essar acquisition: Implications for listed stocks

HTIL: Cash rich but little else...

We see three possible scenarios:

Scenario #1 (short term) – Premium bid expectations – most likely

We see this as a continued positive for the stock price for now. A 25% control premium on the stake value in HE leads us to our HK$24 target price.

Scenario #2 – No deal, status quo continues

The absence of a deal could result in short-term weakness as premium expectations evaporate but keeps longer term value accretion potential (in HE) intact. Still, based on our DCF calculation, we see equity value rising to US$15.8bn as of end-2008 (with potential upside bias on long distance business contributions and margin upside). HTIL's intention to sell (and the uneasy relationship with Essar) should sustain some M&A premium as well, in our view.

Scenario #3 – A successful sale for cash: Do you want to own a shell then?

HE is 80% of NAV, 50% of consolidated EBITDA and the crown jewel in the HTIL stable – its sale (for cash) would leave a cash-rich shell with mature (struggling for growth) businesses in Hong Kong and Israel, a weak business in Thailand and well delayed (yet to commence) start-ups in Indonesia and Vietnam. We also highlight Orascom's 19% stake in HTIL (acquired in December 2005), which we think came principally because of the Hutch Essar exposure. With that now having become one, the chances of Orascom selling out (into a strong post deal stock price) would be high as well, in our view. Should such a deal go through, we would need to evaluate our investment case for HTIL in a very different light.

We are reasonably sure other scenarios could emerge as the saga unfolds. Watch this space.

RCOM: If yes, a master stroke; if no, revert to Plan A

Complementary footprint and RCOM's increasingly unequivocal pro-GSM stance makes Hutch an ideal acquisition candidate for them, in our view. While a control premium is likely, we believe that it may be worth it for RCOM given the potential benefits including the following:

- Time to market for GSM rollout gets shortened considerably.
- RCOM + Hutch would have 36.8% market share of subscribers if the acquisition goes through, materially ahead of Bharti's 22.0% as of November 2006. While Indian wireless operators typically have EBITDA margins in the mid-30s irrespective of the scale, we expect some synergies in operating costs can be extracted, thus justifying the premium over current market valuations. For example, a control premium of, say, US$2-3bn could be justified if RCOM can extract savings of about ~US$200m (based on current 12-month forward EV/EBITDA of 12.5x), which is just 3% of combined RCOM-Hutch FY08E revenues.
- It could also reduce the risks associated with the alternate greenfield GSM rollout by RCOM, which could lead to sub-optimal cost structures (even if it is for a short while). This is assuming that the assimilation is smooth without the associated risks.

On the flip side, if Vodafone is successful in its bid for HE, it would be potentially negative for RCOM. Not only would RCOM then have to revert to the potentially risky GSM-overlay route, its rollout plans would be at the mercy of spectrum constraints. It would also be negative for the stock because RCOM's current valuations (EV/EBITDA of 12.7x FY08E and PER of 23.0x) are now at a 5-10% premium to Bharti's valuations in anticipation of a successful bid. While the competitive landscape does not change materially in the case of a Vodafone-Hutch deal, potential collaboration between Vodafone and Bharti could create some polarization in the market structure.

Bharti: Might lose leadership, but does it matter?

Though Bharti might lose its leadership position, we believe its execution and strategies will remain largely unaffected. If the merger goes through, the top three players would control almost 80% of the market, which could potentially alter the market dynamics – (1) It would improve the chances of continued rational behavior by the operators; and (2) it would make it more difficult for new entrants – vis-à-vis Maxis-Aircel, TM-Spice, etc.– to make significant inroads. This would thus be positive for Bharti. In addition, eventual valuations of the HE sale could have a rub-off impact on Bharti's valuations as well.

Business as usual on core operations

Continued momentum in subscriber additions (averaging ~6.5m in the past couple of months), accelerated coverage plans of all operators, and associated growth in long distance traffic provides greater visibility on growth being more front-ended (over next 3-4 years). Our new estimates reflect that even while broadly retaining our long-term (2016) penetration target of ~50%.

Figure 8. Revised Indian Wireless Subscriber Estimates

Year to 31 Mar	FY07E		FY08E		FY09E		FY10E		FY16E	
	OLD	NEW	OLD	NEW	OLD	NEW	OLD	NEW	OLD	NEW
Subscriber estimates ('000)	159,442	162,230	232,920	239,186	300,688	313,894	365,753	387,693	639,474	664,128
Population (Million)	1,130	1,130	1,147	1,147	1,164	1,164	1,182	1,182	1,292	1,292
Penetration (%)	14	14	20	21	26	27	31	33	49	51

Source: Citigroup Investment Research estimates

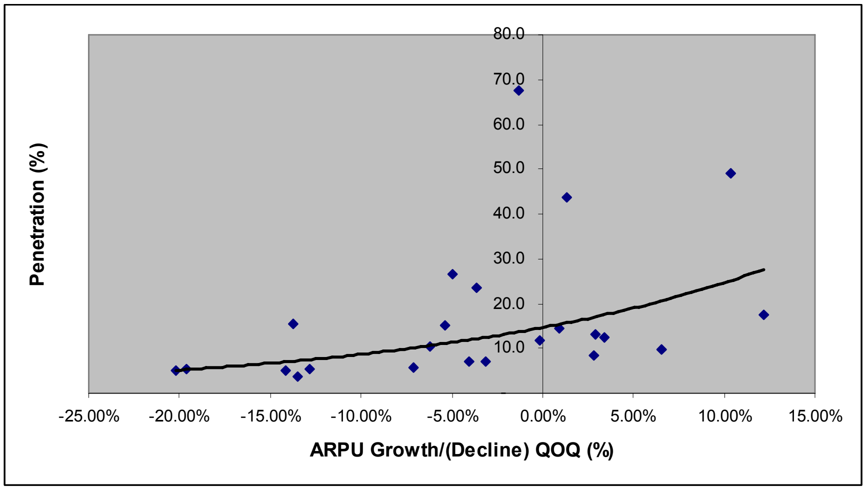
Apart from the 1HFY07 KPIs of the listed operators, there has been further evidence of increased mobile spending from the recently released 3Q06 ARPU data by COAI. Interestingly, the ARPU trends (see chart below) are loosely correlated with the respective penetration of the circle. It basically means that in circles with relatively higher penetration, the usage increase by the existing subscribers is more than negating the impact of lower usage by new subscribers. Also, given low fixed-line penetration in the country (~5%), wireless is fast becoming the preferred, and in some cases the only, mode of communication. This is also evident in the fact that after the metros, ARPU across A, B and C Category circles are fairly similar.

Figure 9. ARPU Declines Have Been Moderate

Circle Category	3Q06 ARPU (Rs)	QOQ (%)	Penetration (%)
Metro	419	1.36%	46.7
A	320	-4.53%	13.2
B	289	-1.72%	10.8
C	311	-9.79%	7.2

Source: COAI, Citigroup Investment Research

Figure 10. ARPU Trends Correlated With Penetration by Circle



Source: COAI, Citigroup Investment Research

Figure 11. Indian Telcos: KPI Comparisons

Blended ARPU (Rs)	2Q05	3Q05	4Q05	1Q06	2Q06	3Q06
Bharti	491	476	470	442	441	438
Hutch Essar	554	518	511	454	433	420
Reliance	403	421	413	379	379	354
Blended MOU (Mins)						
Bharti	383	388	411	431	441	451
Hutch Essar	351	369	385	378	392	406
Reliance	501	568	547	532	491	461
ARPM (Rs/Min)						
Bharti	1.31	1.25	1.17	1.04	1.01	0.98
Hutch Essar	1.58	1.40	1.33	1.20	1.10	1.03
Reliance	0.80	0.74	0.76	0.71	0.77	0.77
EBITDA Margins %						
Bharti	34.8	36.5	36.5	36.2	36.4	36.9
Hutch Essar	33.6	NA	31.3	NA	32.7	NA
Reliance	22.7	28.2	32.1	35.7	36.0	36.1

Source: Company Reports and Citigroup Investment Research

Raising estimates and target prices

Greater confidence in mobile spending and front-ended momentum in subscriber additions drives us to raise our estimates for Bharti and RCOM by 4-8% for FY08-09.

Figure 12. Our Estimate Changes on Bharti

Year to 31 Mar	New			Old		
Rs Mils	FY07E	FY08E	FY09E	FY07E	FY08E	FY09E
Revenues	190,423	266,355	331,571	180,802	246,460	302,099
EBITDA	72,984	104,376	131,761	70,366	97,375	120,886
EBITDA %	38.3	39.2	39.7	38.9	39.5	40.0
EBITDA upgrade (%)	3.7%	7.2%	9.0%	NA	NA	NA
Capex	102,484	108,906	92,947	98,295	98,498	81,673
EPS	20.69	30.30	37.47	20.21	28.10	34.44
EPS upgrade (%)	2.4%	7.8%	8.8%	NA	NA	NA

Source: Citigroup Investment Research Estimates

Figure 13. Our Estimate Changes on Reliance

Year to 31 Mar	New			Old		
Rs Mils	FY07E	FY08E	FY09E	FY07E	FY08E	FY09E
Revenues	154,280	202,235	242,295	152,726	194,123	231,154
EBITDA	57,231	82,645	108,215	56,826	79,870	103,828
EBITDA %	37.1	40.9	44.7	37.2	41.1	44.9
EBITDA upgrade (%)	0.7%	3.5%	4.2%	NA	NA	NA
Capex	70,656	75,336	73,967	67,902	75,604	69,885
EPS	13.74	20.75	28.76	13.04	19.59	27.57
EPS upgrade (%)	5.3%	5.9%	4.3%	NA	NA	NA

Source: Citigroup Investment Research Estimates

Figure 14. Our Estimate Changes on Hutchison Essar

Year to Dec	New				Old			
Rs Mils	2006E	2007E	2008E	2009E	2006E	2007E	2008E	2009E
Revenues	90,374	139,778	181,822	213,878	89,522	137,046	176,041	203,995
EBITDA	29,914	49,621	67,274	81,274	29,632	48,651	65,135	77,518
EBITDA Margin %	33.1%	35.5%	37.0%	38.0%	33.1%	35.5%	37.0%	38.0%
Capex	49,706	55,911	50,910	51,331	49,237	54,819	49,292	48,959

Source: Citigroup Investment Research estimates

Figure 15. Key Assumptions - Wireless

	FY06/CY05	FY07/CY06E	FY08/CY07E	FY09/CY08E
Subs (m)				
Bharti	19.6	37.1	55.0	70.8
Hutch	11.4	23.8	38.4	52.1
RCOM	17.3	29.1	42.0	54.7
Blended ARPU (Rs)				
Bharti	441	424	369	339
Hutch	522	425	363	328
RCOM	387	340	316	294
EBITDA % - wireless				
Bharti	36.6%	36.3%	37.6%	38.6%
Hutch	32.4%	33.1%	35.5%	37.0%
RCOM	30.3%	36.2%	36.9%	38.2%
Wireless Capex (Rs m)				
Bharti	43,048	75,504	81,273	70,485
Hutch	15,545	49,706	55,911	50,910
RCOM	NA	68,260	73,049	71,980
Capex to sales (%) - wireless only				
Bharti	53.3%	52.4%	39.9%	27.5%
Hutch	27.5%	55.0%	40.0%	28.0%
RCOM	NA	45.8%	37.3%	30.5%
Revenues – wireless (Rs m)				
Bharti	80,822	144,132	203,841	256,099
Hutch	56,630	90,374	139,778	181,822
RCOM	74,070	110,830	157,636	198,762
EBITDA – wireless (Rs m)				
Bharti	29,565	52,308	76,557	98,817
Hutch	18,339	29,914	49,621	67,274
RCOM	22,411	40,090	58,155	75,959

Source: Company Reports and Citigroup Investment Research estimates

Target prices raised to reflect roll forward and strategic premiums

We have also raised the target prices of all the Indian Wireless stocks under our coverage.

- Bharti: For Bharti, we are rolling forward our DCF to Mar-08, which gives us a 12-month target of Rs750 (from Rs600) on subscriber estimate revisions and higher growth forecast for long distance volumes. This is based on WACC of 10.8%, a terminal growth rate of 3.5%, Beta of 0.9 (implying a terminal EV/EBITDA multiple of 8.0x). Our new target price represents a FY09E EV/EBITDA of 11.0x, a PER of 20.0x and P/CEPS of 12.5x.

- Reliance: Our target price for RCOM is revised up to Rs570 (from Rs430) based on FY09E EV/EBITDA of 11.2x, P/CEPS of 12.0x and a PER of 19.6x. We expect RCOM multiples to continue to closely track Bharti's given the lack of headroom for foreign holdings in the latter. In addition, the risks associated with technology shift to GSM may get significantly mitigated in case RCOM makes a successful bid for HE, as well as according it a clear market leadership position.

- HTIL: We see the 67% stake in Hutch-Essar (HE) as for sale but at a price. A 25% control premium on the stake in our revised-up (on higher subs) US$15bn equity value for HE leads us to a new target price of HK$24. (1) Premium bid expectations – we think this is most likely and is a positive for now; (2) No deal means short-term weakness as (premium) hopes evaporate but keeps longer term value accretion potential (in HE) intact. (3) Sale for cash – this leaves a cash-rich entity with less attractive businesses that would warrant evaluation in a very different light, in our view.

We outline our valuation comparison of Bharti, RCOM and what is implied for HTIL (on our estimates) based on the current HTIL stock price. The same comparison (at our target prices) for the businesses is outlined in Figure 17 below.

Figure 16. Valuation Comparison at Current Prices: Hutch-Essar vs Bharti vs RCOM

	Implied Hutch-Essar Value (at HTIL HK$19.6)			Bharti (at current price Rs628.9)			RCOM (at current price Rs471.3)		
	2006E	2007E	2008E	2006E	2007E	2008E	2006E	2007E	2008E
P/E (x)	45.0	26.6	18.7	34.0	22.5	17.6	43.3	24.8	17.6
P/CE (x)	29.9	17.4	12.5	20.8	14.2	11.0	21.7	14.2	10.7
EV/EBITDA (x)	26.1	15.7	11.6	18.7	12.7	9.9	20.3	13.6	10.2
P/sales (x)	7.6	4.9	3.8	6.9	4.8	3.8	6.7	5.1	4.1
EV/sub (US$)	985	558	383	705	425	303	592	396	286

Note : Calendarized valuations for Bharti and RCVL; Prices as of 01 Jan 07

Source: Citigroup Investment Research estimates

Figure 17. Valuation Comparison at Target Prices: Hutch-Essar vs Bharti vs RCOM

	Implied Hutch-Essar Value (at DCF)			Bharti (at target price Rs750)			RCOM (at target price Rs570)		
	2006E	2007E	2008E	2006E	2007E	2008E	2006E	2007E	2008E
P/E (x)	56.8	33.6	23.7	40.5	26.9	21.0	52.3	30.0	21.3
P/CE (x)	37.8	22.0	15.8	24.8	16.9	13.2	26.2	17.2	12.9
EV/EBITDA (x)	32.2	19.4	14.3	22.2	15.1	11.7	24.4	16.3	12.2
P/sales (x)	9.6	6.2	4.8	8.2	5.7	4.5	8.1	6.1	5.0
EV/sub (US$)	1,214	688	472	837	505	360	711	473	341

Note : Calendarized valuations for Bharti and RCVL

Source: Citigroup Investment Research estimates

Figure 18. Regional Wireless Companies Valuation Comparison

Company	RIC	Price	Rating	PE (x)		Earnings CAGR	P/CEPS (x)		EV/EBITDA (x)		EBITDA CAGR	Dividend Yield (%)	
		1-Jan-07		06E/ FY07E	07E /FY08E	05-08E/ FY06-09E	06E/ FY07E	07E /FY08E	06E/ FY07E	07E /FY08E	05-08E/ FY06-09E	06E/ FY07E	07E /FY08E
AIS	ADVA.BK	Bt77.5	2M	13.5	11.8	2.2%	6.4	5.9	5.7	5.2	0.6%	8.1%	8.5%
Bharti	BRTI.BO	Rs628.85	1L	30.4	20.8	46.5%	18.7	13.1	16.8	11.8	45.3%	0.0%	0.3%
China Unicom	0762.HK	HK$11.4	1M	24.0	21.7	14.8%	5.0	4.8	5.1	4.5	5.5%	1.0%	1.0%
China Mobile	0941.HK	HK$67.2	2M	21.0	17.9	14.5%	10.0	8.9	8.0	6.9	14.1%	2.3%	2.5%
Digi	DSOM.KL	RM15.2	1L	17.2	13.7	23.6%	8.8	8.2	7.2	6.4	14.2%	5.8%	7.3%
FET	4904.TWO	NT$36.95	2L	10.9	10.9	-3.1%	5.5	5.6	4.9	4.7	-2.6%	8.4%	7.8%
Globe	GLO.PS	P1235	2L	13.0	11.9	19.9%	5.4	5.4	5.1	4.6	9.0%	4.0%	6.5%
Indosat	ISAT.JK	Rp6750	2M	24.3	22.5	7.0%	6.9	6.0	6.5	6.1	10.5%	2.2%	2.1%
KTF	032390.KS	W29750	3M	15.2	11.9	-1.0%	3.9	3.6	4.2	3.7	1.5%	3.9%	4.4%
LGT	032640.KQ	W9620	1M	7.2	6.1	22.9%	3.4	3.0	4.4	3.4	11.5%	0.0%	3.5%
Maxis	MXSC.KL	RM10.2	3L	13.6	15.2	1.3%	8.7	8.5	6.9	7.6	7.9%	7.1%	6.8%
MobileOne	MONE.SI	S$2.15	2L	13.0	13.0	0.6%	7.7	7.7	7.0	6.9	-0.4%	6.0%	7.0%
Rel. Cns	RLCM.BO	Rs471.3	1M	34.3	22.7	130.2%	18.5	13.2	18.2	12.6	63.4%	0.0%	0.4%
SKT	017670.KS	W222500	3M	11.8	10.8	-0.7%	5.7	5.4	5.1	4.7	2.0%	3.8%	4.7%
SmarTone	0315.HK	HK$8.06	3M	57.1	25.8	43.6%	5.9	5.3	3.6	2.9	4.2%	1.5%	1.2%
TAC	TACC.SI	US$4.3	3L	15.3	12.5	14.3%	6.3	5.3	6.7	6.1	7.1%	0.0%	0.0%
Tata Tele	TTML.BO	Rs19.15	1M	NM	582.9	NM	11.8	5.4	11.1	6.7	104.2%	0.0%	0.0%
Taiwan Mobile	3045.TW	NT$33.8	1L	10.4	11.7	-4.6%	6.8	7.3	5.9	5.7	-0.8%	7.7%	7.4%
Wtd. Avg				**21.3**	**17.5**		**10.2**	**8.7**	**8.8**	**7.2**		**2.4%**	**2.7%**
Median				**15.2**	**13.3**		**6.6**	**5.7**	**6.2**	**5.9**		**3.0%**	**4.0%**

Source: Company Reports and Citigroup Investment Research estimates

Figure 19. Asian Telecoms – Regional Integrated Valuations Comparison

Company	RIC	Price	Rating	PE(x)		Earning CAGR	P/CEPS(x)		EV/EBITDA (x)		EBITDA CAGR	Dividend Yield (%)	
		1-Jan-07		06E/ FY07E	07E/ FY08E	05-08E/ FY06-09E	06E/ FY07E	07E/ FY08E	06E/ FY07E	07E/ FY08E	05-08E/ FY06-09E	06E/ FY06E	07E/ FY07E
China Tel	0728.HK	HK$4.26	1L	15.7	15.2	5.3%	4.8	4.6	5.3	5.0	3.7%	1.9%	1.8%
China Netcom	0906.HK	HK$20.85	1M	13.0	12.5	3.2%	3.8	3.7	4.6	4.3	2.9%	2.7%	2.8%
Chunghwa	2412.TW	NT$60.6	1L	13.3	12.3	-0.5%	6.9	6.8	5.5	5.2	-1.1%	5.9%	7.1%
HTIL	2332.HK	HK$19.6	1M	209.2	62.6	NM	15.7	11.7	12.7	9.9	38.5%	0.0%	0.0%
KT	030200.KS	W46500	2L	11.7	10.7	6.4%	4.1	3.8	4.8	4.5	2.2%	4.4%	7.6%
MTNL	MTNL.BO	Rs142.85	3L	17.9	22.3	-22.6%	7.7	8.1	4.3	4.9	-9.7%	3.2%	2.8%
PCCW	0008.HK	HK$4.73	1M	14.5	13.6	11.8%	6.3	5.7	6.7	6.1	6.4%	4.1%	4.5%
PLDT	TEL.PS	P2550	1L	15.0	13.5	9.0%	7.6	8.3	6.6	6.0	6.2%	4.4%	5.2%
PT Telkom	TLKM.JK	Rp10100	1L	17.5	16.3	22.8%	9.7	8.5	6.5	5.7	18.3%	2.2%	3.6%
VSNL	VSNL.BO	Rs424.4	2M	20.8	19.2	11.0%	12.2	11.0	10.6	8.9	18.4%	1.1%	1.0%
Singapore Tel	STEL.SI	S$3.28	1L	17.8	15.1	8.3%	11.1	9.9	9.4	8.5	0.0%	4.6%	3.3%
StarHub	STAR.SI	S$2.63	1L	15.5	16.0	18.6%	9.6	9.2	9.5	8.5	12.3%	4.2%	4.9%
Telekom Mal	TLMM.KL	RM9.75	2L	16.6	13.6	20.0%	5.8	5.1	5.7	5.0	16.5%	4.7%	5.2%
Wtd Avg				**15.6**	**14.4**		**7.6**	**6.9**	**6.8**	**6.1**		**3.3%**	**3.6%**
Median				**15.7**	**15.1**		**7.3**	**7.5**	**6.1**	**5.4**		**3.6%**	**3.4%**

Source: Citigroup Investment Research estimates

Companies

Bharti Airtel Limited (BRTI.BO)

Organic Success

Buy/Low Risk	1L
Price (29 Dec 06)	Rs631.35
Target price	Rs750.00
from Rs600.00	
Expected share price return	18.8%
Expected dividend yield	0.3%
Expected total return	**19.1%**
Market Cap	Rs1,196,878M
	US$27,143M

Price Performance (RIC: BRTI.BO, BB: BHARTI IN)

Rahul Singh
+91-22-6631-9863
rahul.r.singh@citigroup.com

Anand Ramachandran, CFA
+852-2501-2448
anand.ramachandran@citigroup.com

Supriya Gupte
supriya.gupte@citigroup.com

- **Increasing estimates and target price** — Bharti's strong execution sets it apart from the rest, which should make it the biggest beneficiary of surging wireless penetration. Our earnings upgrade of 2.4%-8.8% over FY07-09E and target price upgrade to Rs750 reflects that, plus the expected commensurate benefits in its wholesale voice business.

- **Hutch sale should be positive, one way or another** — While there is a probability of losing the #1 status if Hutch goes to RCOM, we believe it will be offset by the benefits of earlier-than-expected consolidation. Early stage of penetration and less tangible benefits of market leadership (EBITDA margins consistent across operators in mid-30s) means Bharti may not miss much.

- **Will Vodafone's exit provide opportunities?** — Though Vodafone-Hutch deal will be a setback to consolidation, the inevitable control premium would have a ruboff impact on Bharti. The consequent unwinding of Vodafone's 10% stake in Bharti could provide further buying opportunities on any overhang related weakness, be it SingTel or investors seeking liquidity.

- **Top pick, but foreign premium poses technical constraints** — We roll forward our DCF to March-08 yielding our new target price. Bharti continues to be our top-pick in the region. Valuations adjusted for growth (EV/EBITDA of 11.8x FY08E) still look reasonable. The lack of headroom in the foreign limit (despite the hike in FDI cap) remains an irritant though to gain exposure.

Figure 20. Statistical Abstract

Year end March	Net Profit (Rs m)	EBITDA (Rs m)	P/E (x)	EV/EBITDA (x)
2005A	14,978	29,687	77.8	40.4
2006A	22,566	42,981	52.8	28.5
2007E	39,190	72,984	30.4	16.8
2008E	57,388	104,376	20.8	11.8
2009E	70,972	131,761	16.8	9.3

Source: Citigroup Investment Research estimates

Figure 21. Earnings Estimate Revisions

	Net Profit	EPS	% Change	EBITDA
2007E	**39,190**	**20.7**	**2.4**	**72,984**
Old	*38,272*	*20.2*		*70,366*
2008E	57,388	30.3	7.8	104,376
Old	*53,213*	*28.1*		*97,375*
2009E	70,972	37.5	8.8	131,761
Old	*65,224*	*34.4*		*120,886*

Source: Citigroup Investment Research estimates

Fiscal year end 31-Mar	2005	2006	2007E	2008E	2009E
Valuation Ratios					
P/E adjusted (x)	78.1	53.0	30.5	20.8	16.8
EV/EBITDA adjusted (x)	42.7	30.0	18.2	13.1	10.5
P/BV (x)	19.2	13.0	9.4	6.8	5.2
Dividend yield (%)	0.0	0.0	0.3	0.7	1.2
Per Share Data (Rs)					
EPS adjusted	8.08	11.92	20.69	30.30	37.47
EPS reported	8.08	11.92	20.69	30.30	37.47
BVPS	32.95	48.67	67.13	92.39	121.47
DPS	0.00	0.00	2.00	4.50	7.50
Profit & Loss (RsM)					
Net sales	80,028	116,215	191,606	267,562	332,802
Operating expenses	-61,305	-88,610	-143,121	-196,703	-243,559
EBIT	**18,723**	**27,605**	**48,485**	**70,859**	**89,243**
Net interest expense	-1,996	-2,512	-3,950	-3,343	-3,217
Non-operating/exceptionals	-124	272	0	0	0
Pre-tax profit	**16,604**	**25,365**	**44,534**	**67,515**	**86,026**
Tax	-1,528	-2,539	-5,344	-10,127	-15,055
Extraord./Min.Int./Pref.div.	-98	-260	0	0	0
Reported net income	**14,978**	**22,566**	**39,190**	**57,388**	**70,972**
Adjusted earnings	14,978	22,566	39,190	57,388	70,972
Adjusted EBITDA	29,687	42,981	72,984	104,376	131,761
Growth Rates (%)					
Sales	65.6	45.2	64.9	39.6	24.4
EBIT adjusted	129.1	47.4	75.6	46.1	25.9
EBITDA adjusted	89.8	44.8	69.8	43.0	26.2
EPS adjusted	195.1	47.4	73.7	46.4	23.7
Cash Flow (RsM)					
Operating cash flow	**32,583**	**48,320**	**107,775**	**114,610**	**122,570**
Depreciation/amortization	10,964	15,376	24,500	33,518	42,518
Net working capital	1,029	7,295	40,135	20,361	5,863
Investing cash flow	**-29,938**	**-54,095**	**-102,286**	**-108,569**	**-92,604**
Capital expenditure	-26,982	-57,309	-102,484	-108,906	-92,947
Acquisitions/disposals	-1,464	3,631	0	0	0
Financing cash flow	**-860**	**5,338**	**1,613**	**-10,218**	**-25,457**
Borrowings	-1,017	-806	10,000	3,000	-6,000
Dividends paid	0	0	-4,239	-9,538	-15,897
Change in cash	**1,784**	**-438**	**7,102**	**-4,177**	**4,509**
Balance Sheet (RsM)					
Total assets	**159,073**	**215,681**	**306,595**	**383,432**	**441,656**
Cash & cash equivalent	3,087	2,649	10,513	6,336	10,845
Accounts receivable	10,098	14,203	19,161	24,081	26,624
Net fixed assets	131,809	180,971	258,193	333,581	384,011
Total liabilities	**97,258**	**122,545**	**178,509**	**207,496**	**210,646**
Accounts payable	0	0	0	0	0
Total Debt	89,048	112,898	168,862	197,849	200,999
Shareholders' funds	**61,814**	**93,135**	**128,086**	**175,936**	**231,011**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	37.1	37.0	38.1	39.0	39.6
ROE adjusted	28.0	29.5	35.7	38.0	35.0
ROIC adjusted	13.1	13.9	17.2	18.2	18.5
Net debt to equity	139.1	118.4	123.6	108.9	82.3
Total debt to capital	59.0	54.8	56.9	52.9	46.5

For further data queries on Citigroup's full coverage universe please contact CIR Data Services Asia Pacific at CitiResearchDataServices@citigroup.com or +852-2501-2791

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Bharti's engine will continue to roll, Hutch or no Hutch

Bharti's execution track record and its edge in terms of managing growth has been remarkable, in our view. This also shows up in Bharti's relatively stable (yet rising) net adds vis-à-vis the industry. Bharti therefore looks better positioned to gain from upcoming wireless growth.

Figure 22. Our Estimate Changes on Bharti

Year to 31 Mar	New			Old		
Rs M	FY07E	FY08E	FY09E	FY07E	FY08E	FY09E
Revenues	190,423	266,355	331,571	180,802	246,460	302,099
EBITDA	72,984	104,376	131,761	70,366	97,375	120,886
EBITDA %	38.3	39.2	39.7	38.9	39.5	40.0
EBITDA upgrade (%)	3.7%	7.2%	9.0%	NA	NA	NA
Capex	102,484	108,906	92,947	98,295	98,498	81,673
EPS	20.69	30.30	37.47	20.21	28.10	34.44
EPS upgrade (%)	2.4%	7.8%	8.8%	NA	NA	NA

Source: Company Reports, Citigroup Investment Research Estimates

What does Hutch-Essar (HE) sale do to Bharti?

There are two likely scenarios:

1. RCOM acquires Bharti: While Bharti would lose its leadership status under this scenario, we don't think it matters too much. In any case, the scale benefits from leadership status have not been very apparent (with all operators having EBITDA margins in the mid-30s) partially on account of heavy upfronting of opex related to the rapid pace of rollout. Early stages of penetration also negates the leadership change to some extent, though admittedly, RCOM-Hutch's combined market share of ~38% would be clear of Bharti's present 22%.

2. Vodafone acquires Hutch: While negative for consolidation, Vodafone's entry is unlikely to alter competitive dynamics much. Infact, Vodafone's existing relationship with Bharti might result in increased collaboration between the two especially in the infrastructure sharing space. The control premium paid for the HE acquisition (say 20-25%) would also have a positive bearing on Bharti's valuations. Vodafone would also have to disengage from its 10% economic interest (5.6% direct and 4.4% indirect) in Bharti, which could provide further buying opportunities in case of any overhang related weakness.

Bharti Airtel Limited

Company description

Bharti Airtel, through its group companies, provides cellular-phone services in all the 23-telecom circles of India. The group also provides fixed-line phone services, broadband, long-distance and enterprise services. The company is listed on The Stock Exchange, Mumbai (BSE) and The National Stock Exchange of India Limited (NSE). The major shareholders are Bharti Telecom, SingTel and Vodafone.

Investment thesis

We rate Bharti as Buy/Low Risk (1L) with a target price of Rs750. We believe continued robust wireless market expansion and Bharti's ability to capture this growth profitably will be the recurring theme for the stock. We estimate an FY06-09E EPS CAGR of 46.5% or more than double that of the broader market. We believe that competitive pressures, though intense, will continue to be rational as low revenue yields and moderate EBITDA margins leave little room for disruptive pricing. Additionally, most regulatory concerns are behind us and 3G recommendations, though discomforting, cannot derail the growth path, in our view. The strategic shareholding of SingTel, which the company has increased over time, leaves us comfortable with execution issues and new initiatives (such as electronic recharge, vendor tie-ups or a One Alliance partnership). Combined with strong brand presence and a good corporate governance standard, Bharti appears a strong investment. The company has yet to realize the benefits of economies of scale, and we expect a slight strengthening of margins.

Valuation

Our 12-month forward target price of Rs750 (previously Rs600) is based on DCF, which suggests a fair value of Rs749 as of March 2008 (rolled forward from March 2007). This is based on WACC of 10.8%, terminal growth rate of 3.5% and beta of 0.9 (implying a terminal EV/EBITDA multiple of 8.0x). We prefer DCF as our primary valuation methodology because the wireless market will likely continue to see robust growth requiring upfront capex but should generate significant free cash beyond 2009-10. Our target price represents a FY09E P/E of 20.0x, P/CEPS of 12.5x and EV/EBITDA of 11.2x.

The imputed target PER of 25.0x FY08E is at 25% premium to the broad market PER (20.0 FY08E at the higher end of Citigroup's Sensex target of 16,000). This we believe is justified by above-average earnings growth (FY06-09E EBITDA CAGR of 45.3% and EPS CAGR of 46.5%), improved earnings visibility and relative insulation from macro risks (interest rates and political risks).

Risk

Our quantitative risk-rating system rates Bharti as Low Risk. We are comfortable attributing a Low Risk rating for the following reasons: (1) Bharti has a track record of profitability and execution; (2) the company's capex plans are fully funded; and (3) the strategic shareholding of SingTel and Vodafone leaves us comfortable with execution issues and initiatives. The risks that could prevent the stock from reaching our target price include competition-led tariff pressures, un-remunerative capex, overall market downside, and more telecom related paper entering the market.

Figure 23. Income Statement

Year to 31 Mar (Rs m)	2006	2007E	2008E	2009E
Mobile revenue	80,822	144,132	203,841	256,099
Infotel revenue	46,613	67,449	92,110	112,314
Total service revenue	113,724	190,423	266,355	331,571
Other revenue	1,160	1,183	1,207	1,231
Total Revenue	114,884	191,606	267,562	332,802
Access charges	(21,776)	(52,201)	(75,206)	(92,832)
Network operating	(11,729)	(21,525)	(29,765)	(37,148)
Cost of sales of goods	(1,169)	(1,785)	(1,931)	(2,069)
Personnel	(8,186)	(13,016)	(17,253)	(20,352)
SG&A	(19,146)	(32,118)	(42,118)	(52,331)
Intersegment elimination	-	21,158	29,595	36,841
Total Operating Expenses	(62,006)	(99,488)	(136,678)	(167,891)
EBITDA ex license fee	54,210	92,118	130,884	164,911
License fee	(11,228)	(19,133)	(26,507)	(33,150)
Adjusted EBITDA	42,981	72,984	104,376	131,761
Depreciation	(14,206)	(23,343)	(32,396)	(41,430)
Amortization	(1,170)	(1,157)	(1,122)	(1,088)
Net finance costs	(2,512)	(3,950)	(3,343)	(3,217)
PBT	25,365	44,534	67,515	86,026
Current tax	(1,773)	(5,344)	(10,127)	(15,055)
PAT	22,826	39,190	57,388	70,972
EPS (Rs)	11.9	20.7	30.3	37.5
Shares outstanding (MM)	1,894	1,894	1,894	1,894
Growth Y/Y (%)				
Revenues	43.6%	66.8%	39.6%	24.4%
EBITDA	44.8%	69.8%	43.0%	26.2%
EPS	47.4%	73.7%	46.4%	23.7%
DPS	NA	NA	125.0%	66.7%

Source: Company Reports and Citigroup Investment Research Estimates

Figure 24. Balance Sheet

Year to 31 Mar (Rs m)	2006	2007E	2008E	2009E
Net PP&E block	142,411	220,790	297,300	348,818
Investments	3,216	3,216	3,216	3,216
Deferred tax asset (net)	(1,946)	(1,946)	(1,946)	(1,946)
Inventories	381	1,253	1,958	2,701
Sundry debtors	14,203	19,161	24,081	26,624
Cash and bank balances	2,649	10,513	6,336	10,845
Other current assets, loans and advances	11,042	11,042	11,042	11,042
Total current assets	28,275	41,968	43,416	51,212
Current liabilities	78,396	124,360	150,346	159,496
Provisions	-	-	-	-
Total current liabilities	78,396	124,360	150,346	159,496
Net current assets	(50,121)	(82,391)	(106,930)	(108,285)
Total Assets	135,339	180,290	231,140	280,215
Share capital	18,939	18,939	18,939	18,939
Reserve and surplus	17,511	52,462	100,312	155,386
Shareholders equity	36,450	71,401	119,251	174,325
Secured loans	34,503	44,503	47,503	41,503
Minority interests	957	957	957	957
Total Liabilities	135,339	180,290	231,140	280,215

Source: Company Reports and Citigroup Investment Research Estimates

Figure 25. Cash Flow Statement

Year to 31 Mar (Rs m)	2006	2007E	2008E	2009E
Cash Flow from Operations	48,320	107,775	114,610	122,570
Capex	(57,309)	(102,484)	(108,906)	(92,947)
Cash Flow from other Investing Activies	(54,095)	(102,286)	(108,569)	(92,604)
Cash flow from Financing Activities	5,338	1,613	(10,218)	(25,457)
Change in cash	(438)	7,102	(4,177)	4,509
Beginning Cash	3,087	3,412	10,513	6,336
Closing cash	2,650	10,513	6,336	10,845

Note: Difference between 2006 Closing and 2007E Beginning Cash is on account of direct additions to equity.

Source: Company Reports and Citigroup Investment Research Estimates

Figure 26. Key Assumptions

Year to 31 Mar	2006	2007E	2008E	2009E
Wireless Subs (m)	19.58	37.07	55.00	70.80
% Prepaid Subscribers	83%	86%	87%	88%
ARPU prepaid (Rs)	326	337	290	264
ARPU postpaid (Rs)	899	912	889	876
MOU prepaid (Mins)	320	358	340	323
MOU postpaid (Mins)	740	784	792	808
Rev. per minute - prepaid (Rs)	1.02	0.94	0.85	0.82
Rev. per minute -postpaid (Rs)	1.22	1.16	1.12	1.08
Capex / Sales (%)	55%	54%	41%	28%

Source: Company Reports and Citigroup Investment Research Estimates

HTIL (2332.HK)

Buy/Medium Risk	**1M**
Price (01 Jan 07)	HK$19.60
Target price	HK$24.00
from HK$18.00	
Expected share price return	22.4%
Expected dividend yield	0.0%
Expected total return	**22.4%**
Market Cap	HK$93,271M
	US$11,991M

Price Performance (RIC: 2332.HK, BB: 2332 HK)

Anand Ramachandran, CFA
+852-2501-2448
anand.ramachandran@citigroup.com

Rahul Singh
+91-22-6631-9863
rahul.r.singh@citigroup.com

Raising Target Price; Building Up to the Next Hurrah?

- **Raising target price to HK$24** — We see the 67% stake in Hutch-Essar (HE) as being up for sale but it should come at a hefty price. A 25% control premium on the stake in our raised (on higher subs) US$15bn equity value for HE leads us to a new target price of HK$24.

- **Hutch-Essar stake for sale, but at what price?** On our raised subscriber forecasts and estimates, we now expect 100% equity value for HE at US$15bn (as of Dec-2007E, or US$13.4bn as of Dec-2006). We think that HTIL would rightly demand a hefty control premium. At our US$15bn valuation (100% equity value for HE), the 67% stake would be worth HK$16.42/HTIL share and would drive a HK$19.33/share NAV. The 25% control premium to the HE stake yields a target of HK$24 for HTIL.

- **Who's interested?** — Potential suitors are plentiful including Reliance Communications, Vodafone, Essar, Maxis, Orascom and private equity (either separately or in tandem, according to media reports). Although HE is an attractive asset in one of the few the remaining wireless growth areas globally, we believe key to the deal is who would step up to pay the requisite valuations?

- **Stock implications on three scenarios** — (1) Premium bid expectations – we think this is the likeliest scenario and is positive for now; (2) No deal would mean short-term weakness on evaporating hopes of a premium valuation but would keep intact the longer term value accretion potential in HE; (3) Sale for cash – this would leave a cash-rich entity with businesses that would look less attractive and warrant evaluation under a different light. Watch this space.

Figure 27. Statistical Abstract

Year to 31-Dec	EBITDA (HK$ m)	Net Profit (HK$ m)	P/E (x)	Div. Yld (%)
2004	4,154	(30)	NM	0.0%
2005	6,752	(768)	NM	0.0%
2006E	10,352	445	209.2	0.0%
2007E	13,693	1,487	62.6	0.0%
2008E	17,143	2,777	33.5	0.0%

Source: Citigroup Investment Research estimates

Figure 28. Earnings Revision

Year to 31-Dec	Net Profit (HK$ m)	EPS (HK$)	% Chg	EBITDA (HK$ m)
2006E	445	0.094	5.6	10,352
Prev	*422*	*0.089*		*10,303*
2007E	1,487	0.313	6.1	13,693
Prev	*1,402*	*0.295*		*13,522*
2008E	2,777	0.584	7.0	17,143
Prev	*2,595*	*0.546*		*16,765*

Source: Citigroup Investment Research estimates

Fiscal year end 31-Dec	2004	2005	2006E	2007E	2008E
Valuation Ratios					
P/E adjusted (x)	nm	nm	nm	62.6	33.5
EV/EBITDA adjusted (x)	25.4	16.9	12.4	10.1	8.3
P/BV (x)	6.4	5.8	4.6	4.0	3.4
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Per Share Data (HK$)					
EPS adjusted	-0.01	-0.17	0.09	0.31	0.58
EPS reported	-0.01	-0.17	0.09	0.31	0.58
BVPS	3.07	3.40	4.24	4.87	5.71
DPS	0.00	0.00	0.00	0.00	0.00
Profit & Loss (HK$M)					
Net sales	14,845	24,356	33,263	42,828	51,072
Operating expenses	-14,989	-22,273	-28,405	-35,591	-41,200
EBIT	**-144**	**2,083**	**4,858**	**7,237**	**9,872**
Net interest expense	-1,015	-1,604	-2,116	-2,699	-2,905
Non-operating/exceptionals	1,584	-195	0	0	0
Pre-tax profit	**425**	**284**	**2,741**	**4,538**	**6,967**
Tax	-185	-434	-861	-1,189	-1,528
Extraord./Min.Int./Pref.div.	-270	-618	-1,435	-1,862	-2,663
Reported net income	**-30**	**-768**	**445**	**1,487**	**2,777**
Adjusted earnings	-30	-768	445	1,487	2,777
Adjusted EBITDA	4,154	6,752	10,352	13,693	17,143
Growth Rates (%)					
Sales	46.9	64.1	36.6	28.8	19.2
EBIT adjusted	-151.8	1,546.5	133.2	49.0	36.4
EBITDA adjusted	14.5	62.5	53.3	32.3	25.2
EPS adjusted	86.0	-2,390.1	156.4	234.0	86.7
Cash Flow (HK$M)					
Operating cash flow	**2,244**	**5,277**	**9,873**	**11,003**	**13,939**
Depreciation/amortization	3,117	4,367	5,495	6,456	7,270
Net working capital	35	-500	-174	-241	-157
Investing cash flow	**-4,420**	**-9,762**	**-12,764**	**-14,148**	**-12,554**
Capital expenditure	-5,387	-4,046	-12,335	-13,841	-12,291
Acquisitions/disposals	1,647	-4,937	0	0	0
Financing cash flow	**2,285**	**4,819**	**3,130**	**3,838**	**1,309**
Borrowings	3,802	4,568	3,155	3,725	1,309
Dividends paid	0	0	0	0	0
Change in cash	**109**	**334**	**239**	**694**	**2,694**
Balance Sheet (HK$M)					
Total assets	**40,720**	**59,591**	**78,109**	**87,012**	**95,435**
Cash & cash equivalent	2,102	2,436	2,675	3,369	6,063
Accounts receivable	0	0	0	0	0
Net fixed assets	20,228	24,591	36,750	45,609	52,057
Total liabilities	**25,854**	**39,769**	**52,492**	**56,697**	**58,613**
Accounts payable	0	0	0	0	0
Total Debt	17,179	26,690	41,059	45,384	47,292
Shareholders' funds	**14,866**	**19,822**	**25,617**	**30,314**	**36,822**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	28.0	27.7	31.1	32.0	33.6
ROE adjusted	-0.8	-5.1	2.5	6.9	11.0
ROIC adjusted	-1.2	4.3	7.1	8.5	10.7
Net debt to equity	101.4	122.4	149.8	138.6	112.0
Total debt to capital	53.6	57.4	61.6	60.0	56.2

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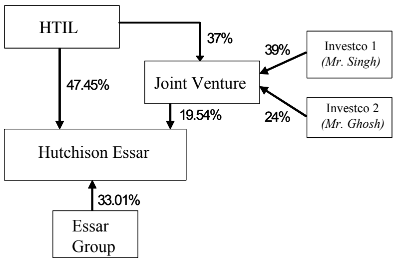
Hutch Essar stake for sale but at a (rich) price?

Figure 29. Hutch Essar: Shareholding Structure



Source: Company Reports and CIR estimates

As outlined in Figure 29, HTIL owns an effective 67% stake in Hutch Essar (this includes HTIL's rights to acquire 97% of the fully diluted share capital of both investment holding companies by Messrs Singh and Ghosh. We would not expect the consideration for these stakes to be material.

We are perplexed at this apparent inclination to exit India. What drives this? We think the lack of improvement in relations with Essar coupled with the inability to realize a significant valuation premium are factors. Relations with Essar have always been blow-hot/ blow-cold, in our view. The BPL Mumbai dispute last year was the first public manifestation of the discord. We see the crux of the disagreements with Essar as being that the Essar Group wants more control of shareholder changes at the HTIL level (where Orascom holds a 19.3% stake and HWL has 49%). With this background, growth expectations for Indian wireless are red hot (as are valuations). If the requisite valuation premium is available, we think it is very possible that HTIL would exit.

We have raised our estimates on HE modestly on higher subscriber growth expectations for the market (discussed in more detail in a subsequent section). On higher subscriber forecasts, we now expect 100% equity value for HE at US$15bn (as of Dec-2007E, or US$13.4bn as of Dec-2006). We think that HTIL would rightly demand a control premium as well.

Given the variety of numbers/ bids indicated in various press reports, we think it is useful to outline a sensitivity analysis of the implied HTIL stake value, NAV implications and valuations at various price points (see Figure 30). We highlight that our base case valuation (US$15bn for 100% equity) is an end-2007E estimate (12 months out versus US$13.4bn as of Dec-2006).

Figure 30. HTIL – Stake Value, Consequent NAV and Implied Valuations for HE at Various Price Points

	100% equity val (A) (US$m)	Net debt* (B) (US$m)	Firm Value (A+B, US$m)	HTIL stake value (HK$)	HTIL NAV (HK$) (other biz unchanged)	Implied EV/EBITDA for HE (x) 2007E	Implied EV/EBITDA for HE (x) 2008E	Implied P/E for HE (x) 2007E	Implied P/E for HE (x) 2008E
10% discount	13,528	2,185	15,713	14.78	17.69	14.3	10.5	23.5	16.6
5% discount	14,280	2,185	16,465	15.60	18.51	14.9	11.0	24.9	17.5
CIR base case	15,031	2,185	17,217	16.42	19.33	15.6	11.5	26.2	18.4
10% premium	16,535	2,185	18,720	18.06	20.97	17.0	12.5	28.8	20.3
20% premium	18,038	2,185	20,223	19.70	22.61	18.3	13.5	31.4	22.1
30% premium	19,541	2,185	21,726	21.35	24.25	19.7	14.5	34.0	24.0

*Net debt estimate as of Dec 2007E. Based on last reported accounts (1H06), net debt at HE was approximately HK$10.8bn (US$1.5bn) as of June 2006. We estimate net debt at US$1.8bn as of Dec 2006E (assuming total capex of US$1.1bn in 2006 versus US$517m for 1H06).

Source: Citigroup Investment Research estimates

Cough up the dough, anyone?

Potential suitors are many and include Reliance Communications (RLCM.BO - Rs469.90; 1M), Vodafone (VOD.L - £1.42; 2H), Essar, Maxis (MXSC.KL - RM10.20; 3L), Orascom (ORTE.CA - E£377.35; 1H) and private equity (separately or in tandem, according to media reports). Media reports (Dow Jones, Bloomberg, local newspapers) have been widespread with some reporting the following interests in HE:

- A grouping of Maxis and private equity partners reportedly had bid US$13.5bn, but this was rejected by HTIL.

- Reliance Communications (in tandem with private equity partners) is an interested bidder. Press reports have indicated an EV for HE at US$17-19bn. Other reports suggest Maxis would join the Reliance consortium.

- Press reports have indicated a minimum mark of US$14bn as set by HTIL as a selling level. It is not clear to us what this refers to exactly; a value for HTIL's 67% stake or a valuation for HE. Assuming this refers the value of the stake would imply a US$20.8bn (100% equity) valuation for HE or HK$22.7/share for HTIL's 67% stake.

- The Essar Group reportedly offered US$11bn for HTIL's 67% stake or HK$20.82/HTIL share. This would value Hutch Essar (100% equity) at US$16.4bn.

- Vodafone reportedly bid US$17-18bn. Other than expressing interest in the asset, however, Vodafone made no formal announcement about the bid. Another variation of this report was the Essar group and Vodafone would work in tandem. Vodafone would buy-out HTIL's 67% stake while Essar's stake would remain with the Indian partners for now but exit in a year's time through an IPO (with Vodafone guaranteeing exit at the price that HTIL's stake was bought out).

Although HE is an attractive asset in one of the few the remaining wireless growth areas globally, key to the deal, in our view, is who will step up to pay the requisite valuations? We believe R-Com and Vodafone are likely the two leading acquirer candidates. Crucially, however, because we believe Essar group has the first right of refusal to the HTIL stake, Essar group's view should be significant for any transaction as well.

We outline a valuation comparison of Bharti (BRTI.BO - Rs629.50; 1L) and RCVL and what is implied for Hutch-Essar on our estimates based on the current HTIL stock price (see Figure 31). The same comparison using our target price is outlined in Figure 32. On our calculations, the implied valuations for HE are already at a small premium to those for Bharti and RCVL.

Figure 31. Valuation Comparison at Current Prices: Hutch-Essar vs Bharti vs RCVL

	Implied Hutch-Essar Value (at HTIL HK$19.6)			Bharti (at current price Rs628.9)			RCVL (at current price Rs471.3)		
	2006E	2007E	2008E	2006E	2007E	2008E	2006E	2007E	2008E
P/E (x)	45.0	26.6	18.7	34.0	22.5	17.6	43.3	24.8	17.6
P/CE (x)	29.9	17.4	12.5	20.8	14.2	11.0	21.7	14.2	10.7
EV/EBITDA (x)	26.1	15.7	11.6	18.7	12.7	9.9	20.3	13.6	10.2
P/sales (x)	7.6	4.9	3.8	6.9	4.8	3.8	6.7	5.1	4.1
EV/sub (US$)	985	558	383	705	425	303	592	396	286

Note: Calendarized valuations for Bharti and RCVL; Prices as of 01 Jan 2007

Source: Citigroup Investment Research estimates

Figure 32. Valuation Comparison at our Target Prices: Hutch-Essar vs Bharti vs RCVL

	Implied Hutch-Essar Value (at DCF)			Bharti (at target price Rs750)			RCVL (at target price Rs570)		
	2006E	2007E	2008E	2006E	2007E	2008E	2006E	2007E	2008E
P/E (x)	56.8	33.6	23.7	40.5	26.9	21.0	52.3	30.0	21.3
P/CE (x)	37.8	22.0	15.8	24.8	16.9	13.2	26.2	17.2	12.9
EV/EBITDA (x)	32.2	19.4	14.3	22.2	15.1	11.7	24.4	16.3	12.2
P/sales (x)	9.6	6.2	4.8	8.2	5.7	4.5	8.1	6.1	5.0
EV/sub (US$)	1,214	688	472	837	505	360	711	473	341

Note : Calendarized valuations for Bharti and RCVL

Source: Citigroup Investment Research estimates

Implications for HTIL stock: Three scenarios

Scenario #1 (short term) – Premium bid expectations – most likely

We see this as a continued positive for the stock price for now. A 25% control premium on the stake value in HE leads us to our HK$24 target. Various sensitivities are outlined in the figure above.

Scenario #2 – No deal, status quo continues

The absence of a deal could see short-term weakness as premium expectations evaporate but keeps longer term value accretion potential (in HE) intact. Still based on our DCF, we see equity value rising to US$15.8bn as of end-2008 (with potential upside bias on long distance business contributions and margin upside). HTIL's intention to sell (and the uneasy relationship with Essar) should sustain some M&A premium as well.

Scenario #3 – A successful stake sale for cash: do you want to own a shell then?

HE is 80% of NAV, 50% of consolidated EBITDA and the crown jewel in the HTIL stable – its sale (for cash) would leave a cash-rich shell with mature (struggling for growth) businesses in Hong Kong and Israel, a weak business in Thailand and well delayed (yet to commence) start-ups in Indonesia and Vietnam. We also highlight Orascom's (ORTE.CA - E£377.35; 1H) 19% stake in HTIL (acquired in December 2005), which we think came principally because of the Hutch Essar exposure. Were that asset to be gone, the chances of Orascom selling out (into a strong post-deal stock price) would be high as well, in our view. All in all, we would need to evaluate our investment case for HTIL in a very different light should a deal go through.

We are reasonably sure more scenarios would emerge as the saga continues – watch this space.

Estimates up on higher numbers at India

We have revised up consolidated net profit estimates by 5.6% and 6.1% for 2006 and 2007 – our EBITDA estimates are up 0.5% and 1.3% for the two years. This is primarily on higher subscriber growth expectations at Hutch Essar – very little has changed otherwise. Changes to our HE estimates are outlined as Figure 33 below. We see two points of note:

Figure 33. Hutchison Essar Estimates Changes

	NOW				EARLIER			
Year to Dec	**2006E**	**2007E**	**2008E**	**2009E**	**2006E**	**2007E**	**2008E**	**2009E**
India - Wireless subs (m)	144.7	219.9	295.2	369.2	142.6	214.5	283.7	349.5
Wireless penetration (%)	12.8%	19.2%	25.4%	31.4%	12.7%	18.9%	24.6%	29.9%
Hutch Essar subs (m)	23.8	38.4	52.1	65.6	23.4	37.4	50.0	62.0
market share (%)	16.5%	17.4%	17.7%	17.8%	16.7%	17.6%	17.8%	17.9%
Hutch-Essar Financials								
Revenues (Rs Mils)	90,374	139,778	181,822	213,878	89,522	137,046	176,041	203,995
EBITDA (Rs Mils)	29,914	49,621	67,274	81,274	29,632	48,651	65,135	77,518
EBITDA Margin %	33.1%	35.5%	37.0%	38.0%	33.1%	35.5%	37.0%	38.0%
Capex (Rs Mills)	49,706	55,911	50,910	51,331	49,237	54,819	49,292	48,959

Source: Citigroup Investment Research estimates

- We incorporate SpaceTel circle rollout in 2Q/3Q 2007. We also do not incorporate any changes to revenues and margins from the long distance business (HE has received a letter of intent and could purchase capacity soon – US$200m was budgeted in 2006 capex for this). We could see revenue and margin benefits once HE starts to build up volumes (likely 2H07 onwards).

- What this also means is that Hutch Essar would likely have subscriber, revenue and margin acceleration forthcoming into 2007 and 2008. Subscriber and revenue would likely accelerate as roll-out into the seven new circles picks up steam. First half EBITDA margins were at 32.7% on clean-ups at (recently acquired) BPL circles. The start-ups (C-circle operations) would have some impact in 2007 but we see no reason why Hutch Essar should not approach 36-38% margins on a three-year view. On our current estimates, we estimate three-year (2006-09) EBITDA CAGR at 39.5% for Hutch Essar.

Higher NAV, higher target price on a premium to NAV

There are two changes to our NAV composition (now HK$19.33 versus HK$18 previously).

- At our raised US$15bn equity valuation for Hutch Essar, the 67% stake is worth HK$16.42/HTIL share (versus HK$15.24/share on a US$14bn valuation previously).

- A slightly higher Partner stock price would lead to a stake (52%) value of HK$1.38/share (versus HK$1.27 previously).

We see the 67% stake in Hutch-Essar as being up for sale but at a hefty price. A 25% control premium on the stake leads us to our new target price of HK$24 (HK$18 previously).

Figure 34. HTIL: Sum-of-the-Parts Valuation

	Tot eq. val (US$m)	HTIL stake (%)	Stake value (US$m)	Stake value (HK$m)	Value/ share (HK$)	Value/HTIL sh (HK$)
Partner Communications	1,616	52.5%	848	6,573	1.38	Listed, based on market price
HGCH, Hong Kong	1,122	100.0%	1,122	8,695	1.83	2007E end DCF estimate (WACC-10.0%; growth rate to perpetuity of 2.5%)
Mobile, Hong Kong	460	70.9%	326	2,529	0.53	2007E end DCF estimate (WACC-10.2%; growth rate to perpetuity of 2.5%)
Hutchison Essar (India)	15,031	67.0%	10,070	78,039	16.42	2007E end DCF estimate (WACC-11.4%; growth rate to perpetuity of 4.0%)
Hutch CAT Thailand	0	66.5%	0	0	0.00	Start-up operations, estimated FCF positive by 2007
Others (SL, Ghana, Vietnam, Indonesia)	0	50-100%	0	0	0.00	Small
Total value of equity stakes (1)			**12,366**	**95,837**	**20.17**	
HTIL debt to operating companies						
Parent debt to HTIL, HK	NA	NA	266	2,062	0.43	Loan, repayable on demand
Parent Level Net debt (end-06E)	NA	NA	-777	-6,046	-1.27	
Total value of debt (2)			**-511**	**-3,984**	**-0.84**	
Net asset value (1+2)			**11,855**	**91,853**	**19.33**	**4752.5m shares outstanding**

Source: Citigroup Investment Research estimates.

HTIL

Company description

HTIL is an international provider of telecoms services. It operates telecoms services in nine markets (Hong Kong, Macau, India, Indonesia, Israel, Sri Lanka, Thailand, Ghana and Vietnam), offering a range of telecom services, from mobile and fixed-line calls to 3G technology. The company was listed on the Stock Exchange of Hong Kong and ADRs were listed on the New York Stock Exchange in October 2004.

Investment thesis

Our rating on HTIL is Buy/Medium Risk (1M), with a sum-of-the-parts-driven target price of HK$24.0. In our view, the group's high-growth Indian assets (66.9% stake in Hutch-Essar) represent the single largest value driver at this stage. The group's recent M&A initiatives have led to the successful structuring of an all-India footprint. We believe this gives HTIL increased credibility as an alternative choice for exposure to the strong growth potential in the Indian wireless sector (our favorite wireless market in the region). Given HTIL's diverse range of assets (telecoms assets and operations in eight countries), we think NAV valuation better reflects the company's valuation than conventional metrics at this stage.

Valuation

Given the diverse range of assets in HTIL, we believe a sum-of-the-parts (SoP) analysis is best suited to value the company. There are three principal parts to our SoP analysis: Partner (Israel) is listed and thus provides the clearest and simplest indicator to the value of HTIL's stake; Hutch-Essar and the fixed-line and mobile businesses in Hong Kong are the three significant unlisted parts. We value these on a fundamental DCF basis and check their valuations based on peer group trading multiples; and outstanding shareholder loans to the operating companies. All in all, we estimate NAV at HK$19.33. In the short term, we see the 67% stake in Hutch-Essar (HE) as being available for sale but at a price. Bidding interest has been significant – consequently, we are assigning a 25% control premium on the stake, which leads to our target price of HK$24. Given majority holdings in all entities and no separately listed holdings other than Partner, we ascribe no holding-company discount, which leaves us with HK$24 as our target price.

Risk

Given HTIL's past loss-making status and imminent start-up businesses in Indonesia and Vietnam, we rate HTIL as Medium Risk rather the Low Risk that is indicated by our quantitative risk-rating system. The following risk factors could impede the stock from reaching our target price: HTIL has been loss-making and has high debt and off-balance-sheet liabilities; the company does not intend to pay dividends in the foreseeable future; competition is tough in its subsidiaries' markets (Hong Kong, India, Thailand and Israel); the 3G-business model in Hong Kong is still unproven and we see a large impact on profitability from 3G rollout costs and SACs in the medium term, though SAC amortization would boost reported numbers somewhat; and regulatory and policy restrictions in various markets. Continuing disagreements and disputes with the Essar group in India could also develop into a risk to Hutch Essar's growth prospects. Lastly, a potential sale of the Hutch Essar stake for cash would leave a cash-rich entity with less attractive businesses, which would warrant evaluation in a very different light, in our view.

Figure 35. HTIL – Consolidated Income Statement, 2004-2008E (HK$ Dollars in Millions)

Year to Dec	**2004**	**2005**	**2006E**	**2007E**	**2008E**
Hong Kong mobile (incl Macau)	3,714	3,837	3,953	4,071	4,085
Hong Kong fixed line	1,870	2,204	2,404	2,567	2,696
India	7,093	9,996	15,952	24,673	32,094
Thailand	1,219	1,045	1,043	1,040	1,101
Israel	-	6,612	9,152	9,247	9,244
Indonesia and Vietnam		-	30	429	970
Others	949	662	728	801	881
Total revenues	**14,845**	**24,356**	**33,263**	**42,828**	**51,072**
EBITDA - consolidated subsidiaries					
Hong Kong mobile (incl Macau)	362	769	1,334	1,303	1,341
Hong Kong fixed line	670	696	842	950	998
India	2,201	3,237	5,280	8,759	11,875
Thailand	(233)	(15)	125	208	297
Israel	-	1,981	3,020	3,237	3,235
Indonesia and Vietnam		-	(67)	(643)	(533)
Others	(27)	(218)	(182)	(120)	(70)
Total EBITDA - consol subsidiaries	**2,973**	**6,450**	**10,352**	**13,693**	**17,143**
% share of associates' EBITDA	1,181	302	-	-	-
EBITDA (incl associates)	**4,154**	**6,752**	**10,352**	**13,693**	**17,143**
Depr and amortization					
Hong Kong mobile (incl Macau)	(886)	(1,189)	(1,187)	(1,056)	(1,002)
Hong Kong fixed line	(476)	(618)	(594)	(575)	(554)
India	(857)	(797)	(1,359)	(2,392)	(3,214)
Thailand	(846)	(529)	(497)	(375)	(346)
Israel	-	(1,149)	(1,652)	(1,662)	(1,674)
Indonesia and Vietnam		-	(98)	(279)	(355)
Others	(52)	(85)	(107)	(115)	(125)
Total depr and amort	(3,117)	(4,367)	(5,495)	(6,456)	(7,270)
Associate depreciation	(428)	(216)	-	-	-
EBIT/Operating profit					
Hong Kong mobile (incl Macau)	(524)	(420)	147	247	339
Hong Kong fixed line	194	78	248	375	443
India	1,344	2,440	3,921	6,367	8,661
Thailand	(1,079)	(544)	(372)	(168)	(49)
Israel	-	832	1,368	1,574	1,562
Indonesia and Vietnam		-	(165)	(922)	(888)
Others	(79)	(303)	(289)	(236)	(195)
Total EBIT	**(144)**	**2,083**	**4,858**	**7,237**	**9,872**
Share of associate/JV earnings	338	86	-	-	-
Net interest expenses and others	(1,015)	(1,604)	(2,116)	(2,699)	(2,905)
Extraordinary profits/(losses)	1,246	(281)	-	-	-
Profit before taxes and MI	**425**	**284**	**2,741**	**4,538**	**6,967**
Current taxes	(105)	(229)	(319)	(557)	(773)
Deferred taxes	(80)	(205)	(542)	(631)	(755)
Profit after taxes	240	(150)	1,880	3,349	5,439
Minorities	(270)	(618)	(1,435)	(1,862)	(2,663)
Net profit to shareholders	**(30)**	**(768)**	**445**	**1,487**	**2,777**
EPS (HK$)	**(0.007)**	**(0.166)**	**0.094**	**0.313**	**0.584**
DPS (HK$)	-	-	-	-	-
Payout ratio (%)	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*

Source: Company data, Citigroup Investment Research estimates

Figure 36. HTIL – Consolidated Balance Sheet, 2004-2008E (HK Dollars in Millions)

Year to 31 Dec	2004	2005	2006E	2007E	2008E
Fixed Assets	20,228	24,591	36,750	45,609	52,057
Intangibles (incl G'will)	6,139	9,688	14,200	13,566	12,932
Deferred tax assets	844	918	10,497	10,507	10,479
Ass and JVs	1,846	2	1,417	1,417	1,417
Amts due from rel cos	-	-	-	-	-
Long term deposits	79	416	93	93	93
Other non-current assets	5,261	10,833	5,853	5,561	5,279
Cash and equivalents	2,102	2,436	2,675	3,369	6,063
Restricted cash	10	1	8	8	8
Other CA	4,211	10,706	6,616	6,882	7,106
Total CA	6,323	13,143	9,300	10,259	13,177
Total Assets	**40,720**	**59,591**	**78,109**	**87,012**	**95,435**
Bank Loans	12,281	7,677	2,308	2,309	2,310
Other loans	1,316	11	802	802	802
Debentures	247	2	212	212	212
Other CL	6,852	10,781	7,278	7,017	6,797
Total CL	20,696	18,471	10,600	10,339	10,121
Long term loans	3,582	19,002	37,949	42,273	44,181
Amts due to rel companies	-	-	-	-	-
Deferred tax liabilities	148	963	896	1,537	2,265
Pension obligations	-	-	215	215	215
Minority interests	1,036	3,652	5,466	7,159	9,664
Share Capital	1,125	1,188	1,188	1,188	1,188
Reserves	12,705	14,982	18,963	21,967	25,970
Exchange Reserve	-	-	-	-	-
Shareholders' funds	13,830	16,170	20,151	23,155	27,158
Total liabilities	**40,720**	**59,591**	**78,109**	**87,012**	**95,435**

Source: Company data, Citigroup Investment Research estimates

Figure 37. HTIL – Consolidated Cash Flow Statement, 2004-2008E (HK Dollars in Millions)

Year to Dec	2004	2005	2006E	2007E	2008E
Profit before taxation	425	284	2,741	4,538	6,967
Interest and other finance costs	1,015	1,604	2,116	2,699	2,905
Dep and amort	3,117	4,367	5,495	6,456	7,270
Depr and amort - associates	428	216	-	-	-
Operating profit before D&A	5,346	6,471	10,352	13,693	17,143
Share of associates oper profit bef D&A	(1,181)	(302)	-	-	-
Stake disposal gains	(1,300)	-	-	-	-
Int and other fin costs	(892)	(883)	(1,207)	(1,731)	(1,962)
Taxes paid	(82)	(217)	(319)	(557)	(773)
Change in working capital	35	(500)	(174)	(241)	(157)
Others	318	708	1,220	(160)	(311)
Operating cash flow	2,244	5,277	9,873	11,003	13,939
Capex	(5,387)	(4,046)	(12,335)	(13,841)	(12,291)
Stake acquisitions	1,647	(4,937)	-	-	-
Additions to sub acq costs	(728)	(650)	(429)	(307)	(263)
Others	48	(129)	-	-	-
Investing cash Flow	(4,420)	(9,762)	(12,764)	(14,148)	(12,554)
Equity issuance/ buybacks	-	-	-	-	-
Dividends	-	-	-	-	-
Debt increase/(decrease)	3,802	4,568	3,155	3,725	1,309
Amounts due to related cos	(1,513)	-	-	-	-
Others	(4)	251	(25)	113	-
Financing cash Flow	2,285	4,819	3,130	3,838	1,309
Incr/(Decr) in cash	109	334	239	694	2,694
Cash - YB	1,993	2,102	2,436	2,675	3,369
Cash - YE	2,102	2,436	2,675	3,369	6,063

Source: Company data, Citigroup Investment Research estimates

HTIL – Key Valuation Metrics

Year to 31 Dec	2004	2005	2006E	2007E	2008E
P/E (x)	NM	NM	209.2x	62.6x	33.5x
P/CEPS (x)	47.9x	23.4x	15.7x	11.7x	9.3x
EV/EBITDA (x)	31.2x	18.0x	12.7x	9.9x	7.8x
Price to book (x)	6.4x	5.8x	4.6x	4.0x	3.4x
Price to sales (x)	5.9x	3.8x	2.8x	2.2x	1.8x
Price to EBITDA (x)	26.6x	14.3x	9.0x	6.8x	5.4x
Price to FCF (x)	NM	NM	NM	NM	36.0x
FCF Yield (%)	NM	NM	NM	NM	2.8%
Dividend yield (%)	0.0%	0.0%	0.0%	0.0%	0.0%
EV/invested capital (x)	3.4x	2.7x	2.1x	1.9x	1.7x
Net debt/EBITDA (x)	4.55	3.71	3.71	3.07	2.41
Net debt/equity (%)	109.0%	150.0%	190.5%	181.4%	151.8%
Total debt to equity (%)	124.2%	165.1%	203.8%	196.0%	174.1%
Net debt to capital (%)	50.4%	55.0%	60.0%	58.1%	52.8%
Total debt to capital (%)	57.4%	60.6%	64.2%	62.7%	60.6%
EBITDA/interest expense (%)	2.9x	4.0x	4.9x	5.1x	5.9x
RoE	NM	NM	2.2%	6.4%	10.2%
RoIC	NM	NM	5.2%	7.4%	9.9%
RoIC-WACC	NM	NM	-4.8%	-2.6%	-0.1%
RoA	NM	3.5%	6.2%	8.3%	10.3%
Capex to sales (%)	36.3%	16.6%	37.1%	32.3%	24.1%
Capex to EBITDA (%)	181.2%	62.7%	119.1%	101.1%	71.7%

Source: Company data, Citigroup Investment Research estimates

Reliance Communications (RLCM.BO)

Buy: No Guts, No Glory

Buy/Medium Risk	1M
Price (02 Jan 07)	Rs469.90
Target price	Rs570.00
from Rs430.00	
Expected share price return	21.3%
Expected dividend yield	0.4%
Expected total return	21.7%
Market Cap	Rs960,765M
	US$21,779M

Price Performance (RIC: RLCM.BO, BB: RCOM IN)

- **Increasing estimates and target price** — Despite the constraints imposed by CDMA, subscriber adds have picked up in 2H FY07, but at the cost of ARPUs – as evident in 2Q FY07 KPIs. Our estimates for FY07-09 have been raised 4-6% to reflect accelerating subscriber adds and increased confidence in the wholesale voice business.

- **Hutch Essar (HE) acquisition could resolve many issues** — HE's assets fit in well with Reliance's increasingly unambiguous pro-GSM stance. Not only would it take RCOM to leadership position, but it would also obviate the potentially risky GSM overlay option and the associated spectrum constraints. Although potential cost benefits exist, which justify some control premium, risk of overpayment exists.

- **What if HE goes to another party** — HE's acquisition by, say, Vodafone, would mean RCOM would have to revert to GSM overlay, the economics of which depend on deals with vendors and the extent of infrastructure sharing. Parallel capex on both networks does create a risk of sub-optimality. Given RCOM's premium valuations, such an event could pose some downside risk.

- **Reiterating our Buy/Medium Risk rating** — We raise our target price for RCOM to Rs570 from Rs430 based on an EV/EBITDA of 11.2x FY09E, the imputed multiple at our DCF-based target price for Bharti. Potential clear leadership option associated with the Hutch opportunity and the lack of foreign headroom in Bharti could mean RCOM closely tracking Bharti's valuations.

Rahul Singh
+91-22-6631-9863
rahul.r.singh@citigroup.com

Anand Ramachandran, CFA
+852-2501-2448
anand.ramachandran@citigroup.com

Supriya Gupte
supriya.gupte@citigroup.com

Figure 38. Statistical Abstract

	Net Profit (RS. Mils)	P/E (x)	EV/EBITDA (x)	EBITDA (RS. Mils)
2006P	4,823	199.2	40.1	24,786
2007E	28,085	34.2	18.1	57,231
2008E	42,431	22.6	12.6	82,645
2009E	58,802	16.3	9.5	108,215

Source: Citigroup Investment Research estimates

Figure 39. Earnings Estimate Revision

	Net Profit	EPS	% Change	EBITDA
FY07E	**28,085**	**13.7**	**5.3**	**57,231**
Old	*26,662*	*13.0*		*56,826*
FY08E	42,431	20.8	5.9	82,645
Old	*40,060*	*19.6*		*79,870*
FY09E	58,802	28.8	4.3	108,215
Old	*56,375*	*27.57*		*103,828*

Source: Citigroup Investment Research estimates

Fiscal year end 31-Mar	2005	2006	2007E	2008E	2009E
Valuation Ratios					
P/E adjusted (x)	na	199.2	34.2	22.6	16.3
EV/EBITDA adjusted (x)	na	na	18.1	12.8	9.7
P/BV (x)	na	8.2	6.8	5.4	4.2
Dividend yield (%)	na	0.0	0.4	0.6	0.9
Per Share Data (Rs)					
EPS adjusted	na	2.36	13.74	20.75	28.76
EPS reported	na	2.36	13.74	20.75	28.76
BVPS	na	57.48	68.96	86.34	110.60
DPS	na	0.00	2.00	3.00	4.00
Profit & Loss (RsM)					
Net sales	na	112,884	154,280	202,235	242,295
Operating expenses	na	-105,085	-120,976	-150,086	-171,296
EBIT	**na**	**7,799**	**33,304**	**52,148**	**70,999**
Net interest expense	na	-2,649	-3,426	-5,003	-4,179
Non-operating/exceptionals	na	0	0	0	0
Pre-tax profit	**na**	**5,150**	**29,878**	**47,146**	**66,820**
Tax	na	-327	-1,793	-4,715	-8,018
Extraord./Min.Int./Pref.div.	na	0	0	0	0
Reported net income	**na**	**4,823**	**28,085**	**42,431**	**58,802**
Adjusted earnings	na	4,823	28,085	42,431	58,802
Adjusted EBITDA	na	24,786	57,231	82,645	108,215
Growth Rates (%)					
Sales	na	na	36.7	31.1	19.8
EBIT adjusted	na	na	327.0	56.6	36.1
EBITDA adjusted	na	na	130.9	44.4	30.9
EPS adjusted	na	na	482.3	51.1	38.6
Cash Flow (RsM)					
Operating cash flow	**na**	**21,810**	**33,796**	**85,767**	**103,158**
Depreciation/amortization	na	16,987	23,927	30,497	37,216
Net working capital	na	0	-21,643	7,836	2,962
Investing cash flow	**na**	**0**	**-69,351**	**-75,336**	**-73,967**
Capital expenditure	na	0	-69,351	-75,336	-73,967
Acquisitions/disposals	na	0	0	0	0
Financing cash flow	**na**	**0**	**14,474**	**-13,903**	**-15,380**
Borrowings	na	0	22,500	-2,000	-2,000
Dividends paid	na	0	-4,600	-6,901	-9,201
Change in cash	**na**	**21,810**	**-21,082**	**-3,472**	**13,812**
Balance Sheet (RsM)					
Total assets	**na**	**319,738**	**349,262**	**399,699**	**458,168**
Cash & cash equivalent	na	60,038	38,956	35,484	49,296
Accounts receivable	na	16,807	19,285	19,662	20,191
Net fixed assets	na	214,263	259,687	304,526	341,278
Total liabilities	**na**	**202,223**	**208,262**	**223,168**	**232,036**
Accounts payable	na	89,956	72,786	89,692	100,560
Total Debt	na	92,976	115,476	113,476	111,476
Shareholders' funds	**na**	**117,515**	**141,000**	**176,531**	**226,132**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	na	22.0	37.1	40.9	44.7
ROE adjusted	na	na	21.7	26.7	29.2
ROIC adjusted	na	na	15.5	18.5	21.6
Net debt to equity	na	28.0	54.3	44.2	27.5
Total debt to capital	na	44.2	45.0	39.1	33.0

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Hutch could be master stroke, otherwise revert to Plan A

Complementary footprint and RCOM's increasingly unequivocal pro-GSM stance make HE an ideal acquisition candidate for RCOM. While a control premium is likely, we believe that it may be worth it for RCOM given the benefits that can be derived.

- Time to market for GSM rollout would be shortened considerably.

- RCOM + Hutch would have a 36.8% market share of subscribers if the acquisition went through, much ahead of Bharti's 22.0% to date. While Indian wireless operators typically have EBITDA margins in the mid-30s irrespective of scale, we expect some synergies in operating costs that can be extracted, thus justifying the premium over current market valuations. For example, a control premium of say US$2-3bn could be justified if RCOM can extract savings of about ~US$200m (based on the current 12-month forward EV/EBITDA of 12.5x), which is just 3% of the combined RCOM-Hutch FY08E revenues.

- It could also reduce the risks associated with the alternative greenfield GSM rollout by RCOM, which could lead to sub-optimal cost structures (even if it is for a short while). This is of course assuming that the assimilation is smooth without any associated risks.

On the flip side, if Vodafone is successful in its bid for HE, it would be potentially negative for RCOM. Not only would RCOM then have to revert to the potentially risky GSM overlay route, its rollout plans would be at the mercy of spectrum constraints. It would also be negative for the stock as RCOM's current valuations (EV/EBITDA of 12.6x FY08E and P/E of 22.6x) are now at 5-10% premiums to Bharti's valuations in anticipation of a successful bid. While the competitive landscape would not change materially in case of a Vodafone-Hutch deal, potential collaboration between Vodafone and Bharti could create some polarization in the market structure.

Technologically challenged but running at full steam

RCOM's wireless business has done reasonably well given the constraints imposed by CDMA. While the bottlenecks might not go away completely in the immediate future, we think RCOM remains well positioned to capture growth given its wide and deep network as well as strong local brand.

Figure 40. Estimate Revisions

Year to 31 Mar	New			Old		
Rs m	FY07E	FY08E	FY09E	FY07E	FY08E	FY09E
Revenues	154,280	202,235	242,295	152,726	194,123	231,154
EBITDA	57,231	82,645	108,215	56,826	79,870	103,828
EBITDA %	37.1	40.9	44.7	37.2	41.1	44.9
EBITDA upgrade (%)	0.7%	3.5%	4.2%	NA	NA	NA
Capex	70,656	75,336	73,967	67,902	75,604	69,885
EPS	13.74	20.75	28.76	13.04	19.59	27.57
EPS upgrade (%)	5.3%	5.9%	4.3%	NA	NA	NA

Source: Company Reports and Citigroup Investment Research estimates

Figure 41. Segmental Forecasts (Rs m)

Profit & Loss	FY06	FY07E	FY08E	FY09E
Total Revenue	**112,884**	**154,280**	**202,235**	**242,295**
Wireless	74,070	110,830	157,636	198,762
Global Business	59,048	72,726	82,367	87,527
Broadband	5,128	11,735	15,990	20,414
EBITDA	**24,786**	**57,231**	**82,645**	**108,215**
Wireless	22,411	40,090	58,155	75,959
Global Business	5,922	13,446	18,102	22,657
Broadband	746	4,624	7,069	10,006
EBITDA Margin (%)	**22.0**	**37.1**	**40.9**	**44.7**
Wireless (%)	30.3	36.2	36.9	38.2
Global Business (%)	10.0	18.5	22.0	25.9
Broadband (%)	14.5	39.4	44.2	49.0

Source: Company Reports and Citigroup Investment Research estimates

Reliance Communications

Company description

RCVL is an integrated player in the Indian telecom sector. The company was listed on the Indian stock exchanges as part of the scheme of de-merger of Reliance Industries Ltd (RIL). It is the second-largest player in the mobile segment, has an 80,000km-long India-wide optic-fiber network and owns the FLAG submarine cable network. The company plans to launch IPTV and retail broadband in 2007. The business of RCVL is organized into three business units 1) Wireless, which includes a nationwide wireless network on CDMA and GSM; 2) Global Business comprising wholesale voice and data; and 3) Broadband business for both retail and enterprise.

Investment thesis

We rate RCOM as Buy/Medium Risk (1M) with a target price of Rs570. Continued expansion of the wireless market and RCOM's ability to capture market share profitably will, in our view, be the recurring theme for the stock. The wireless business has demonstrated higher operating leverage in the recent past and has maintained similar return parameters despite lower revenue yields. Competitive pressures, though intense, should continue to be rational. RCOM is also planning a GSM overlay on its existing CDMA network; while there is market rationale for this (GSM has lower-priced handsets), we think the economic rationale would be determined by the deal from vendors as well as the extent of infrastructure-sharing possible. Additionally, most regulatory concerns appear behind us, and news flow now is likely to be positive.

The company has yet to realize the benefits of full utilization of its network infrastructure (especially in broadband), and we expect significant strengthening of margins as traffic increases across segments. We thus expect RCOM to register an EBITDA CAGR of 63.4% for FY06-09E.

Valuation

In valuing Indian wireless plays, we use DCF as our primary methodology given the back-ended nature of profits and cash flow. In the case of RCOM, however, we use EV/EBITDA in the absence of a detailed balance sheet, which is awaiting reorganization.

RCOM's 12-month target price of Rs570 is based on 11.2x FY09E EV/EBITDA, similar to the implied target EV/EBITDA for Bharti based on our DCF estimate. RCOM's valuation multiples are likely to closely track Bharti's due to the liquidity overflow from the latter, notwithstanding the risk of technology transition. In addition, the risks associated with technology shift to GSM may get significantly mitigated in case RCOM makes a successful bid for HE, besides according it a clear market leadership. As a secondary valuation methodology, we apply a target P/E of 27.5x FY08E for a fair value of Rs570. We believe a premium to the Sensex's target 12-month forward P/E of 20.0x is justified given our projected earnings growth for RCOM of 51% yoy for FY08E and a 45% CAGR for FY07-09E against estimated market earnings growth of 25% for FY07E and 15% for FY08E.

Risk

Our quantitative risk-rating system, which tracks 260-day share price volatility, assigns a High Risk rating to RCOM, but we believe a Medium Risk rating is more appropriate. RCOM has been de-merged from Reliance Industries, and its shareholding at the time of listing mirrored the holding of RIL. The stock is therefore unlikely to have risk factors that are typical of newly listed companies that have more limited management and operating track records. Besides, growth in the telecom sector accords visibility to RCOM's prospects – characteristics that are similar to those of its peers. However, we believe its evolving financial history and risks pertaining to GSM overlay warrant a risk rating higher than that which we assign to Bharti (Low Risk).

Operationally, the risks facing RCOM are slightly higher than for Bharti due to the proposed technology shift. Also, RCOM's present CDMA-led business model leaves open the possibility of the re-emergence of handset subsidies, which the company has brought under control.

Downside risks to our target price include smaller-than-expected market share, lower-than-anticipated operating leverage (especially for FY07), cost-overruns in GSM overlay, regulatory and competition risks, un-remunerative capex, delays in the ongoing re-organization and more telecom-related paper entering the market.

Figure 42. Income Statement (Rs m)

Year to 31 March	FY06	FY07E	FY08E	FY09E
Total Revenue	**112,884**	**154,280**	**202,235**	**242,295**
Total Cost	(88,098)	(97,049)	(119,589)	(134,080)
Access & IUC	(31,012)	(66,040)	(80,001)	(90,143)
License Fees	(8,559)	(10,723)	(15,313)	(19,523)
Other Operating Exp	(48,527)	(61,297)	(78,034)	(88,822)
EBITDA	**24,786**	**57,231**	**82,645**	**108,215**
EBITDA Margin (%)	22.0	37.1	40.9	44.7
Net Interest	(2,649)	(3,426)	(5,003)	(4,179)
Depreciation & Amortization	(16,987)	(23,927)	(30,497)	(37,216)
PBT	5,150	29,878	47,146	66,820
Tax	(327)	(1,793)	(4,715)	(8,018)
PAT	4,823	28,085	42,431	58,802
No. of Shares	2,045	2,045	2,045	2,045
EPS	2.4	13.7	20.8	28.8
DPS	-	2.0	3.0	4.0

Source: Company Reports and Citigroup Investment Research estimates

Figure 43. Balance Sheet

As at 31 March	FY06	FY07E	FY08E	FY09E
Equity	10,223	10,223	10,223	10,223
Reserves and Surplus	107,292	130,777	166,308	215,909
Shareholders funds	117,515	141,000	176,531	226,132
Debt	92,976	115,476	113,476	111,476
Secured Loans	87,185	109,685	107,685	105,685
Unsecured Loans	5,791	5,791	5,791	5,791
Current Liabilities	89,956	72,786	89,692	100,560
Provisions	19,291	20,000	20,000	20,000
Total Liabilities	**319,738**	**349,262**	**399,699**	**458,168**
Fixed Assets	230,531	301,187	376,524	450,491
Accumulated Depreciation	(47,573)	(71,500)	(101,997)	(139,213)
Net Fixed Assets	182,958	229,687	274,526	311,278
CWIP	31,305	30,000	30,000	30,000
Investments	121	121	121	121
Cash	60,038	38,956	35,484	49,296
Current Assets	45,316	50,498	59,568	67,474
Inventories	4,076	4,500	5,000	5,500
Debtors	16,807	19,285	19,662	20,191
Other Current Assets	765	1,000	1,200	1,400
Loans & Advances	23,668	25,713	33,706	40,383
Total Assets	**319,738**	**349,262**	**399,699**	**458,168**

Source: Company Reports and Citigroup Investment Research estimates

Figure 44. Cash Flow Statement

Year to 31 Mar	FY07E	FY08E	FY09E
PAT	28,085	42,431	58,802
Add: Depreciation	23,927	30,497	37,216
Change in NWC	(21,643)	7,836	2,962
Add: Interest	3,426	5,003	4,179
Operating Cash Flow	33,796	85,767	103,158
Capex	69,351	75,336	73,967
Free Cash Flow	(35,556)	10,431	29,191
Cash flow into investments	(69,351)	(75,336)	(73,967)
Increase in debt	22,500	(2,000)	(2,000)
Increase in Equity	-	-	-
Less: Interest	(3,426)	(5,003)	(4,179)
Less: Dividend	(4,600)	(6,901)	(9,201)
Financial cash flow	14,474	(13,903)	(15,380)
Cash year begin	60,038	38,956	35,484
Cash generated	(21,082)	(3,472)	13,812
Cash year end	38,956	35,484	49,296

Source: Citigroup Investment Research estimates

Tata Teleservices (TTML.BO)

Buy/Medium Risk	1M
Price (02 Jan 07)	Rs19.35
Target price	Rs24.00
from Rs31.44	
Expected share price return	24.0%
Expected dividend yield	0.0%
Expected total return	**24.0%**
Market Cap	Rs35,014M
	US$794M

Price Performance (RIC: TTML.BO, BB: TTLS IN)

Rahul Singh
+91-22-6631-9863
rahul.r.singh@citigroup.com

Anand Ramachandran, CFA
+852-2501-2448
anand.ramachandran@citigroup.com

Supriya Gupte
supriya.gupte@citigroup.com

Buy: Laggard Catching Up Slowly

- **Earnings adjusted, new target price reflects higher dilution** — We lower our FY07-08E EBITDA (by 22-25%) based on lower-than-expected performance in 1HFY07 even though sub adds have witnessed acceleration in the 2H. Coupled with higher-than-expected dilution in rights issue (at 19%), we cut our target price to Rs24 (from Rs31.44) based on March-08 DCF.

- **Operational turnaround on course** — TTML has been getting its act together operationally with its share of net adds at 12% for the past six months. However, in the context of its lowest-in-the-industry tariffs, the cumulative share of 7% in Mumbai/Maharashtra remains sub-optimal and appears constrained by its CDMA network.

- **Returns could be back-ended though** — Given TTML's likely net breakeven in FY09, returns could be back-ended, especially in relation to its peers. We expect financial milestones to drive stock performance. Demonstration of operating leverage, which we expect to improve by 10% during FY07-09E, would be critical.

- **Corporate action could act as an external trigger** — We expect Tata Group to consolidate its telecom holdings relative to VSNL, TTSL and TTML for the next 12-18 months. The process could begin with Tata's option to buy out the government's remaining stake in VSNL (the call option for which expires in Feb-07). We think TTML (along with VSNL) offers a route to gain exposure to the consolidated entity.

Figure 45. Statistical Abstract

Year end March 31	Net Profit	EPS	Revenue	Revenue Growth	EBITDA	EV / EBITDA
(Rs m)	(Rs Mils.)	(Rs)	(Rs Mils.)	(%)	(Rs Mils.)	(x)
2006	(4,938)	(3.2)	10,951	35.6%	1,247	40.4
2007E	(2,830)	(1.6)	14,861	35.7%	3,044	18.3
2008E	(1,391)	(0.8)	18,370	23.6%	4,711	12.5
2009E	1	0.0	22,011	19.8%	6,741	9.0

Source: Citigroup Investment Research estimates and Company Reports

Fiscal year end 31-Mar	2005	2006	2007E	2008E	2009E
Valuation Ratios					
P/E adjusted (x)	-5.5	-6.0	-12.4	nm	nm
EV/EBITDA adjusted (x)	nm	43.7	18.3	12.1	8.7
P/BV (x)	1.7	1.7	1.6	1.6	1.6
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Per Share Data (Rs)					
EPS adjusted	-3.54	-3.25	-1.56	-0.77	0.00
EPS reported	-3.54	-3.25	-1.56	-0.77	0.00
BVPS	11.06	11.42	12.31	12.31	12.31
DPS	0.00	0.00	0.00	0.00	0.00
Profit & Loss (RsM)					
Net sales	8,075	10,951	14,861	18,370	22,011
Operating expenses	-11,906	-14,423	-16,329	-18,143	-20,287
EBIT	**-3,831**	**-3,472**	**-1,468**	**227**	**1,724**
Net interest expense	-1,447	-1,458	-1,362	-1,618	-1,723
Non-operating/exceptionals	0	0	0	0	0
Pre-tax profit	**-5,279**	**-4,930**	**-2,830**	**-1,391**	**1**
Tax	0	-9	0	0	0
Extraord./Min.Int./Pref.div.	0	0	0	0	0
Reported net income	**-5,279**	**-4,938**	**-2,830**	**-1,391**	**1**
Adjusted earnings	-5,279	-4,938	-2,830	-1,391	1
Adjusted EBITDA	-661	1,247	3,044	4,711	6,741
Growth Rates (%)					
Sales	35.1	35.6	35.7	23.6	19.8
EBIT adjusted	-159.1	9.4	57.7	115.5	658.5
EBITDA adjusted	-220.9	288.6	144.1	54.8	43.1
EPS adjusted	-84.7	8.3	51.8	50.9	100.1
Cash Flow (RsM)					
Operating cash flow	**5**	**926**	**724**	**2,803**	**4,275**
Depreciation/amortization	3,170	4,719	4,512	4,484	5,017
Net working capital	666	1,145	-957	-290	-743
Investing cash flow	**-4,410**	**-3,481**	**-5,550**	**-5,660**	**-4,992**
Capital expenditure	-4,338	-3,481	-5,550	-5,660	-4,992
Acquisitions/disposals	-72	0	0	0	0
Financing cash flow	**4,611**	**3,162**	**5,123**	**2,000**	**1,000**
Borrowings	5,616	2,290	1,000	2,000	1,000
Dividends paid	0	0	0	0	0
Change in cash	**206**	**606**	**297**	**-857**	**282**
Balance Sheet (RsM)					
Total assets	**45,513**	**49,998**	**56,262**	**58,996**	**60,315**
Cash & cash equivalent	820	274	1,724	867	1,150
Accounts receivable	1,423	1,558	2,270	2,807	3,363
Net fixed assets	24,924	24,366	25,039	26,215	26,191
Total liabilities	**29,027**	**32,640**	**33,993**	**36,726**	**38,045**
Accounts payable	10,198	11,521	11,874	12,608	12,927
Total Debt	18,828	21,119	22,119	24,119	25,119
Shareholders' funds	**16,487**	**17,358**	**22,270**	**22,270**	**22,270**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	-8.2	11.4	20.5	25.6	30.6
ROE adjusted	-33.3	-29.2	-14.3	-6.2	0.0
ROIC adjusted	-12.1	-9.6	-3.6	0.5	3.8
Net debt to equity	109.2	120.1	91.6	104.4	107.6
Total debt to capital	53.3	54.9	49.8	52.0	53.0

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Figure 46. Change in EPS Estimates

	2007E	2008E
Old	(1.64)	0.03
New	(1.56)	(0.77)

Source: CIR Estimates

Figure 47. Key Assumptions – TTML

	2006	2007E	2008E	2009E
Subscribers ('000)	**1,840**	**3,125**	**4,502**	**5,784**
Mobile	797	1,549	2,410	3,230
FWT	814	1,324	1,818	2,270
Fixed	229	252	274	285
ARPU (Rs)				
Mobile	340	255	204	184
FWT	621	559	503	478
Fixed	1615	1,421	1,279	1,215
Costs				
Marketing Cost / revenue (%)	16.8	13.6	11.6	10.2
Interconnect Cost/Rev. (%)	33.2	32.0	31.5	31.3
Balance Sheet				
Capex / Sales (%)	37.7	37.3	30.8	22.7
Net Debt	20,845	20,394	23,251	23,969

Source: Company Reports and Citigroup Investment Research estimates

Figure 48. Income Statement – TTML

Rs m	2006	2007E	2008E	2009E
Telecom Services	10,951	14,861	18,370	22,011
Interconnection/Access Costs	(3,639)	(4,756)	(5,787)	(6,889)
Network Operation Costs	(1,771)	(2,378)	(2,939)	(3,302)
Employee Costs	(486)	(573)	(630)	(681)
G&A expenses	(1,981)	(2,140)	(2,268)	(2,404)
Marketing and promotion	(1,844)	(2,028)	(2,130)	(2,236)
Total Expenditure	(9,721)	(11,874)	(13,754)	(15,512)
Operating Profit	1,231	2,987	4,616	6,499
Other Income	17	57	95	242
EBITDA	1,247	3,044	4,711	6,741
Financial Charges	(1,458)	(1,362)	(1,618)	(1,723)
Depreciation	(4,719)	(4,512)	(4,484)	(5,017)
PBT	(4,930)	(2,830)	(1,391)	1
Provision for Income Tax	(9)	-	-	-
PAT	(4,938)	(2,830)	(1,391)	1

Source: Company Reports and Citigroup Investment Research estimates

Figure 49. Balance Sheet – TTML

Rs m	2006	2007E	2008E	2009E
Cash and Bank Balances	274	1,724	867	1,150
Sundry Debtors	1,558	2,270	2,807	3,363
Loans and Advances	1,466	2,064	2,551	3,057
Current Assets	3,298	6,059	6,225	7,570
Net Block	22,615	23,289	24,464	24,440
CWIP	1,751	1,751	1,751	1,751
Profit and Loss Account	22,334	25,164	26,555	26,555
Total Assets	**49,998**	**56,262**	**58,996**	**60,315**
Share Capital	15,206	18,095	18,095	18,095
Advance against Equity	-	-	-	-
Reserves and Surplus	2,152	4,174	4,174	4,174
Shareholder's Capital	17,358	22,270	22,270	22,270
Total Loans	21,119	22,119	24,119	25,119
Current Liabilities and Provisions	11521.3	11874.39	12607.88	12926.79
Total Liabilities	**49,998**	**56,262**	**58,996**	**60,315**

Source: Company Reports and Citigroup Investment Research estimates

Tata Teleservices

Company description

Tata Tele (TTML) is part of Tata Group and provides telecommunication services in two of the most lucrative circles in India, Mumbai and Maharashtra. The company provides fixed line, CDMA-based mobile and fixed wireless services, and has 2.35m as on 30 September 2006. It was earlier called Hughes Tele, which was acquired by Tata Group in 2001-02. Tata Teleservices owns around 47% of the company, and provides similar services as TTML in 18 other circles.

Investment thesis

We rate the stock as Buy/Medium Risk (1M) and believe that TTML has done a reasonable job in getting its act together in the intensely competitive markets of Mumbai and Maharashtra. It has increased its coverage significantly, stepped up marketing, introduced innovative mobile products and garnered about 12% of the net adds in the last 6 months. Fixed wireless offtake has been surprisingly strong as TTML has been able to churn subscribers away from incumbents MTNL and BSNL with a sleek product and better customer service.

We believe TTML will turn PAT positive in FY09 after turning cash profit positive in 1Q07. We believe that the company offers a good entry point to tap the turnaround in business fundamentals given the recent underperformance. Our target price of Rs24 is based on DCF and multiple discount to its larger listed peers.

Valuation

We value Tata Tele using a DCF methodology given the back-end nature of its cash flow and profitability. Our March-08 DCF value comes to Rs24, which is our target price, on account of higher-than-expected dilution in the rights issue and near-term earnings adjustments (FY07-08E). For our calculations, we use explicit cash flow till FY16 and a terminal growth rate of 5%. We use a WACC of 12.0%, which factors in a risk-free rate of 8%, a risk premium of 6%, a beta of 0.9, a cost of debt of 7.5%, a debt / capital ratio of 15% and a marginal tax rate of 33.6%. We assume higher costs and equity for TTML than Bharti.

Alternatively, we value Tata Tele using a FY09E EV/EBITDA multiple of 10.1x, at a 10% discount to Bharti's imputed EV/EBITDA which translates into a fair value of Rs23. We believe that FY06 and FY07 multiples are not relevant as growth is at a nascent stage. We retain our Buy/Medium Risk (1M) rating on the stock.

Risk

Our quantitative risk-rating system, which tracks the share price volatility of the last 260 days, rates Tata Tele as Medium Risk. Disappointment on subscriber numbers and financials could be a negative trigger for the stock. Also, the company will require significant funds to expand and any plans that significantly dilute the share base would likely be received negatively by the market. Competition in Mumbai and Maharashtra is also likely to go up with BSNL setting up fresh capacity in these markets. If any of these factors has a greater impact than we expect, the stock could have difficulty achieving our target price.

Bharti – (BRTI.BO, Rs629, Buy/Low Risk)

Valuation

Our 12-month forward target price of Rs750 is based on DCF, which suggests a fair value of Rs749 as of March 2008 (rolled forward from March 2007). This is based on WACC of 10.8%, terminal growth rate of 3.5% and beta of 0.9 (implying a terminal EV/EBITDA multiple of 8.0x). We prefer DCF as our primary valuation methodology because the wireless market will likely continue to see robust growth requiring upfront capex but should generate significant free cash beyond 2009-10. Our target price represents a FY09E P/E of 20.0x, P/CEPS of 12.5x and EV/EBITDA of 11.2x.

The imputed target PER of 25.0x FY08E is at 25% premium to the broad market PER (20.0 FY08E at the higher end of Citigroup's Sensex target of 16,000). This we believe is justified by above-average earnings growth (FY06-09E EBITDA CAGR of 45.3% and EPS CAGR of 46.5%), improved earnings visibility and relative insulation from macro risks (interest rates and political risks).

Risk

Our quantitative risk-rating system rates Bharti as Low Risk. We are comfortable attributing a Low Risk rating for the following reasons: (1) Bharti has a track record of profitability and execution; (2) the company's capex plans are fully funded; and (3) the strategic shareholding of SingTel and Vodafone leaves us comfortable with execution issues and initiatives. The risks that could prevent the stock from reaching our target price include competition-led tariff pressures, un-remunerative capex, overall market downside, and more telecom related paper entering the market.

Analyst Certification Appendix A-1

We, Rahul Singh and Anand Ramachandran, CFA, research analysts and the authors of this report, hereby certify that all of the views expressed in this research report accurately reflect our personal views about any and all of the subject issuer(s) or securities. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

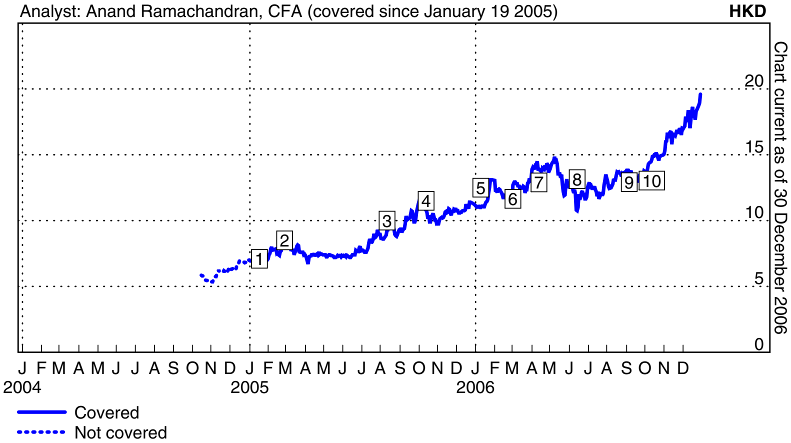
IMPORTANT DISCLOSURES

Hutchison Telecommunication Intl. (2332.HK)

Ratings and Target Price History - Fundamental Research

Analyst: Anand Ramachandran, CFA (covered since January 19 2005)

HKD



#	Date	Rating	Target Price	Closing Price
1:	18 Jan 05	1M	8.00	6.55
2:	28 Feb 05	*2M	*8.80	8.50
3:	11 Aug 05	2M	*10.00	9.30
4:	13 Oct 05	2M	*12.10	10.85
5:	10 Jan 06	2M	*12.50	11.00
6:	2 Mar 06	2M	*13.00	12.70
7:	13 Apr 06	2M	*16.00	13.90
8:	14 Jun 06	2M	*12.60	10.75
9:	6 Sep 06	2M	*15.90	13.72
10:	12 Oct 06	*1M	*18.00	14.64

*Indicates change.

Tata Teleservices (Maharashtra) Ltd (TTML.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Rahul Singh (covered since May 12 2006)

INR

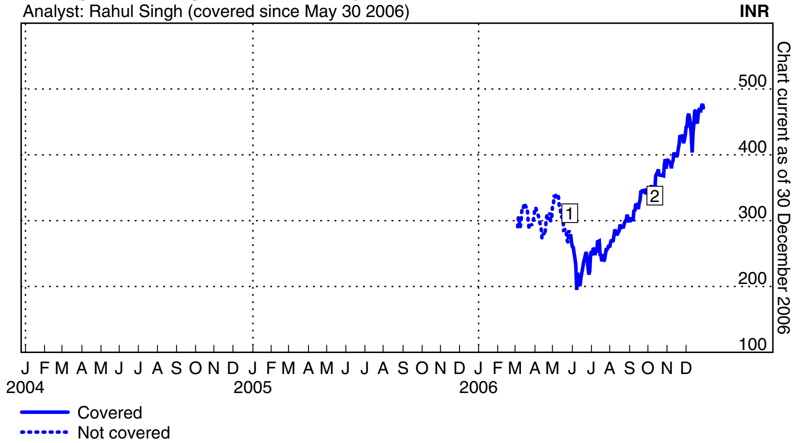
#	Date	Rating	Target Price	Closing Price
1:	10 Jan 06	2M	29.47	27.31
2:	13 Apr 06	*1M	*31.43	22.84

*Indicates change.

Reliance Communications (RLCM.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Rahul Singh (covered since May 30 2006)



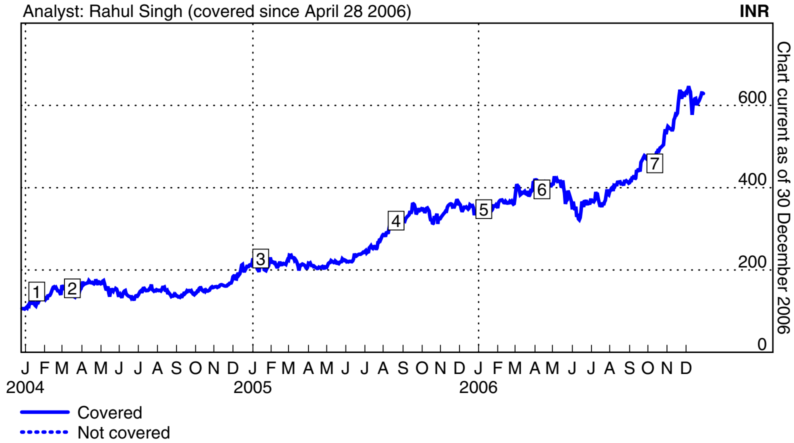
#	Date	Rating	Target Price	Closing Price
1:	29 May 06	1M	360.00	276.25
2:	12 Oct 06	1M	*430.00	345.95

*Indicates change.

Bharti Airtel Limited (BRTI.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Rahul Singh (covered since April 28 2006)



#	Date	Rating	Target Price	Closing Price
1:	20 Jan 04	1H	*160.00	118.40
2:	17 Mar 04	1H	*220.00	146.15
3:	14 Jan 05	*1M	*260.00	210.30
4:	22 Aug 05	1M	*400.00	306.10
5:	10 Jan 06	1M	*450.00	339.25
6:	13 Apr 06	1M	*500.00	395.95
7:	12 Oct 06	*1L	*600.00	475.65

*Indicates change.

Customers of the Firm in the United States can receive independent, third-party research on the company or companies covered in this report, at no cost to them, where such research is available. Customers can access this independent research at http://www.smithbarney.com (for retail clients) or http://www.citigroupgeo.com (for institutional clients) or can call (866) 836-9542 to request a copy of this research.

Rahul Singh holds a long position in the shares of Bharti Airtel Limited.

Citigroup Global Markets Inc. is acting as buyside advisor in the purchase of PCCW shares.

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