Industry Focus

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Indian Wireless

Towerco Deals Provide Reliable Benchmarks, Vindicate Pricing

- **EV/Tower of US$160-170k the norm** – This is based on the recent Bharti Inf private equity deal and the sale of Spice's 875 towers. These benchmarks are based on projected Mar-08E tower count, i.e. 64k for Infratel (including 42% contribution to Indus). This equates to EV/IC of 2.2x based on avg. capex of $75k.

- **Unlocking for Bharti is significant** – The mid-point of US$10-12.5bn EV indicates Rs220/share (Mar-08), higher than our base case of Rs170/share, therefore providing a cushion against any value depletion from the core business. Though regulatory concerns have had greater influence on the stock, we remain positive as potential compromise and/or litigation related delays appear likely. The existing players' scale would also pose a steep asking rate to the potential new entrants. Besides, Bharti continues to trade at a discount to RCOM and Idea.

- **More reliable indicator of rental trends** – New norms are ~30% lower than RTIL's US$225-230k/tower and EV/IC of 3.0x. As we noted previously, the difference is a function of higher capex recovery (11-13% per tenant) assumed by RTIL vs. a more tenable 7.5-8.0% factored in the recent deals (Bharti/Spice). This in a way vindicates our stance on sustainable rental pricing in India.

- **More towerco deals** – TTSL has also put its 11,000 towers on the block, with the third-party towercos as front runners, in our view. Meanwhile, we are positively surprised by the respectable tenancy of these tower assets. Spice's 875 towers have an average tenancy of 1.69x, TTSL is reported at ~ 1.5x. This indicates potential upside for our assumptions, say 2.5x for Indus.

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Figure 1. Statistical Abstract

		M Cap	Price	P/E (x)		EV/EBITDA (x)	
Company name	Rating	US$M	1/3/2008	FY08E	FY09E	FY08E	FY09E
Bharti	1L	45,536	943	26.1	20.2	16.0	11.8
RCOM	2L	38,658	737	27.9	22.2	18.8	13.5
Idea	2L	8,870	135	32.8	27.1	17.3	13.0
Spice	1M	1,139	65	NM	61.1	21.8	14.7

Source: Citi Investment Research estimates

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

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Bharti Infratel Mar-09 EV at US$10-12.5bn

In a recent private equity transaction (PE), investors agreed to invest US$1bn to be converted into equity in Mar-09. The range of EV will be based on actual financial performance in FY09, subject to a floor and cap of US$10.0bn and US$12.5bn, respectively. We note that the range of EV/Tower in the recent transactions (including the Spice's sale of its 875 towers) was US$160-170k. This not only is a more realistic indicator of towerco valuations, but also the evolving rental pricing (capex recovery of 7.5-8.0%). For Bharti, we depict three scenarios.

1. The base case Mar-08 EV of US$7.9bn (Rs170/share) is based on DCF, but with more conservative assumptions, i.e. tenancy of 2.5x and capex recovery of ~7% per tenant. Please note that the base case working was before the Indus announcement and is hence more conservative.

2. We run separate DCF tables with more aggressive assumptions vs. the base case, i.e. tenancy of 2.5x for Indus and 3.25x for Infratel and capex recovery of 7.5-8.0% per tenant. Please note that resultant estimated value of Bharti Infratel, i.e. 42% of Indus + 100% of Infratel EV, is in line with the Mar-08 EV established in the recent PE round (US$10.5bn). This provides confidence in our assumptions. Please refer to the tables below on Indus and Infratel DCF for more details.

3. In the private equity round, for calculating EV/Tower we have discounted back the mid point of the Mar-09 EV range (say US$11.5bn) by one year to Mar-08.

Figure 2. Towerco Valuation Comparison

	Equity value (US$m)	EV (US$m)	Tower Count (Mar-08)	EV/Tower (US$)
Bharti Infratel (Citi base case)	na	7,872	64,000	123,000
Bharti Infratel (post-Indus)	na	10,366	64,000	161,961
Bharti Infratel (PE round)	na	10,455	64,000	163,352
RTIL	6,750	8,475	37,000	229,054
Spice	na	150	875	171,429

Source: Citi Investment Research

We detail the financial model of our EV estimation for Indus and Bharti Infratel (residual 20k towers) below.

Figure 3. Indus Towerco DCF Valuation

Rs m	FY08E	FY09E	FY10E	FY11E	FY12E	FY13E	FY14E	FY15E	FY16E
Owned towers (nos)	90,000	119,684	136,277	152,130	162,450	171,823	175,341	175,972	176,775
Rental per tenant per month (Rs)	50,000	43,000	42,000	39,000	37,000	36,000	35,000	34,000	33,000
Average tenancy	1.25	1.50	1.75	2.00	2.10	2.20	2.30	2.40	2.50
Tower rental revenues (Rs m)	67,500	92,636	120,196	142,394	151,469	163,300	169,380	172,312	175,007
EBITDA (Rs m)	25,380	38,060	59,689	76,674	83,240	91,135	95,736	98,404	100,762
EBITDA (%)	38%	41%	50%	54%	55%	56%	57%	57%	58%
Implied RoA	9.4%	10.6%	14.6%	16.8%	17.1%	17.7%	18.2%	18.6%	19.0%
Implied Payback (years)	10.6	9.4	6.8	6.0	5.9	5.7	5.5	5.4	5.3
Total capex (Rs m)	142,337	86,223	60,549	59,825	44,653	42,737	26,019	17,673	18,246
FCF (Rs m)	(119,624)	(51,850)	(6,178)	10,730	33,274	42,599	63,646	74,526	63,957
Terminal Value (Rs m)	947,513								
NPV (Rs m)	521,579								
NPV (US$m)	13,039								

Source: Citi Investment Research estimates

Figure 4. Bharti Infratel DCF Valuation

Rs m	FY08E	FY09E	FY10E	FY11E	FY12E	FY13E	FY14E	FY15E	FY16E
Owned towers (nos)	26,000	32,803	36,605	40,238	42,603	44,751	45,557	45,702	45,886
Rental per tenant per month (Rs)	50,000	42,000	36,000	30,000	30,000	30,000	30,000	30,000	30,000
Average tenancy	1.25	1.60	2.25	3.00	3.00	3.10	3.20	3.25	3.25
Tower rental revenues (Rs m)	19,500	26,452	35,580	43,457	46,011	49,942	52,482	53,471	53,687
EBITDA (Rs m)	7,332	11,494	19,327	26,074	28,118	31,147	33,348	34,276	34,414
EBITDA (%)	38%	43%	54%	60%	61%	62%	64%	64%	64%
Implied RoA	9.4%	11.7%	17.6%	21.6%	22.0%	23.2%	24.4%	25.0%	25.0%
Implied Payback (years)	10.6	8.6	5.7	4.6	4.5	4.3	4.1	4.0	4.0
Total capex (Rs m)	37,446	20,122	14,359	14,194	10,717	10,278	6,447	4,534	4,665
FCF (Rs m)	(31,168)	(10,020)	2,968	9,520	14,965	18,189	24,035	26,815	21,205
Terminal Value (Rs m)	314,147								
NPV (Rs m)	195,558								
NPV (US$m)	4,889								

Source: Citi Investment Research estimates

Valuations and Risks

Bharti Airtel (BRTI.BO - Rs943.30; 1L)

Valuation

Our 12-month forward target price of Rs1,200 is based on Sep-08 core DCF of Rs1,010 and a towerco option value of Rs170. The DCF is based on a WACC of 10.7%, a terminal growth rate of 4% and beta of 0.9. 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 FY09-10E. Our target price (net of towerco value) represents a FY09E P/E of 21.5x, P/CEPS of 14.2x and EV/EBITDA of 12.5x.

Risks

Our quantitative risk-rating system, which tracks 260-day share price volatility, rates Bharti shares 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) SingTel's strategic shareholding leaves us comfortable with execution issues and initiatives. Risks that could prevent the stock from reaching our target price include competition-led tariff pressures, un-remunerative capex, overall market downside, and slower-than-expected execution of the tower-sharing initiative.

Reliance Communications (RLCM.BO - Rs737.00; 2L)

Valuation

Our 12-month forward target price of Rs835 is based on a core business fair value of Rs650, a GSM option value of Rs115, a net towerco value of Rs50 and Flag's potential value unlocking at Rs20. We usually value Indian wireless plays on DCF given the back-ended nature of profits and cash flow. For RCOM, however, we use EV/EBITDA. Our 12-month core business value of Rs650 is based on 11.9x FY09E EV/EBITDA, a 5% discount to Bharti's implied target multiple (ex- towerco). Higher-than-average earnings growth (CAGR of 37% over FY07-10E) and the low sensitivity of wireless demand to interest rates should continue to support premium valuations for the sector, in our view.

Risks

Our risk-rating system, which tracks 260-day share price volatility, assigns a High Risk rating to RCOM, but we believe Low Risk 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 risks that are typical of newly listed companies. Besides, growth in the telecoms sector gives visibility to RCOM's prospects. Downside risks to our target price include smaller-than-expected market share, lower-than-anticipated operating leverage (especially in FY07) due to handset subsidies, cost-overruns n GSM overlay, regulatory and competition risks, un-remunerative capex and delays in the ongoing re-organization and more telecom-related paper.

IDEA Cellular (IDEA.BO - Rs134.50; 2L)

Valuation

We have set our 12-month target price at Rs140 based on Sep-08E DCF of Rs127 and an M&A premium of 10%. Though new spectrum norms dilute the M&A appeal, we believe that the substantial private-equity holding (30%) and spectrum/coverage will still appeal to new entrants as they may not get spectrum post the Government's approval for dual technology. We prefer DCF as our primary valuation methodology due to the back-ended nature of free cash flows given the new circle roll-outs. Our DCF assumes a WACC of 10.8% at a target debt to capital of 50.0% and terminal growth rate of 4.0% (similar to Bharti). Our DCF is based on explicit forecasts for FY07-16E with a terminal year EBITDA margin at 41.1% (~500bps below Bharti) and capex/sales of ~8% (in line with Bharti). The DCF value implies an EV/EBITDA of 12.3x, broadly in line with Bharti's target multiples (for the ex-towerco portion of Rs1,010), which is supported by Idea's higher growth rates notwithstanding Idea's smaller size and relatively less established track record.

Risks

Our quantitative risk-rating system assigns a default Speculative rating to Idea shares due its trading history of less than 12 months. We see a Low Risk rating as more appropriate due to the higher visibility of Indian wireless growth, Idea's reasonably competitive position, strong parentage and lower financial leverage post-IPO. Operationally, the downside risks facing Idea are slightly higher than its more established peers given the roll-out in new circles. Project cost over-runs, delays in spectrum allocation and hence commercial launches could affect the value accretion opportunity in new circles. Any of these factors could prevent the shares from reaching our target price. Upside risks to our estimates and target price would include higher-than-expected industry trends in subscriber additions and MOUs. An acquisition bid for Idea from potential new entrants at a significant premium to existing valuations would also present upside risk to our valuations.

Spice Communications (SPCM.BO - Rs64.90; 1M)

Valuation

Our target price of Rs70 is based on a 15% M&A premium to our core business DCF of Rs60 (as on Dec-08). We prefer DCF as our primary valuation methodology due to the back-ended nature of free cash flows, in the context of coverage ramp-up, especially in Karnataka. Our DCF assumes a WACC of 11% at a target debt to capital of 50.0% and terminal growth rate of 4.0% (similar to Bharti). Our DCF is based on explicit forecasts for CY07-16E with a terminal year EBITDA margin at 35% (~600bps below Idea) and capex/sales of ~7% (in line with Bharti). The target price implies a CY08E EV/EBITDA of 14.1x (which is 5% premium on pro-rata basis to Bharti's FY09 target ex-towerco), which we believe is supported by significantly higher prospective EBITDA growth rates for Spice. Though Spice rebuffed the moves by Idea pre-IPO, we believe that M&A potential exists in the medium term as access to 900MHz spectrum and its small footprint makes it a good and probably the only M&A candidate, especially with recent relaxation of M&A norms. If the new TRAI spectrum norms are accepted, the opportunity to enter new circles could also justify a premium to the DCF based on its existing two circles.

Risks

Our quantitative risk-rating system assigns a default Speculative rating to Spice shares due its trading history of less than 12 months. We see a Medium Risk rating as more appropriate due to the higher visibility of Indian wireless growth, strong parentage (Telekom Malaysia) and lower financial leverage post-IPO. Spice accumulated significant losses in the past resulting in negative net worth prior to the IPO. It previously defaulted on payments to vendors and debenture holders due to lack of adequate funds and has had qualifications from auditors with respect to its ability to continue operations in absence of access to long-term funds. Going forward, operationally, the risks facing Spice are slightly higher than its more established peers given its smaller scale. Lower-than-expected tenancy in third-party towers and higher capex requirements to increase coverage may depress return parameters. Its equipment sourcing contract with Spice Mobiles Pvt. Ltd, a group company, has transfer pricing risks as there is lack of clarity on the rationale and cost-plus billing terms. While new circle roll-outs are possible if new spectrum norms are accepted by the DoT (as and when the Defence Department releases spectrum), it will be constrained by management bandwidth and may require a fresh equity infusion. These risk factors could impede the stock from reaching our target price.

Appendix A-1

Analyst Certification

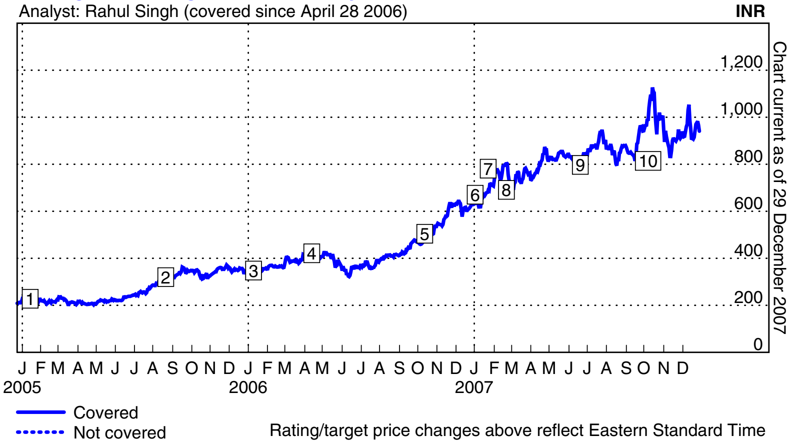
Each research analyst(s), strategist(s) or research associate(s) responsible for the preparation and content of all or any identified portion of this research report hereby certifies that, with respect to each issuer or security or any identified portion of the report with respect to an issuer or security that the research analyst, strategist or research associate covers in this research report, all of the views expressed by that research analyst, strategist or research associate in this research report accurately reflect their personal views about those issuer(s) or securities. Each research analyst(s), strategist(s) or research associate(s) also certify that no part of their compensation was, is, or will be, directly or indirectly, related to the specific recommendation(s) or view(s) expressed by that research analyst, strategist or research associate in this research report.

IMPORTANT DISCLOSURES

Bharti Airtel (BRTI.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Rahul Singh (covered since April 28 2006)



Rating/target price changes above reflect Eastern Standard Time

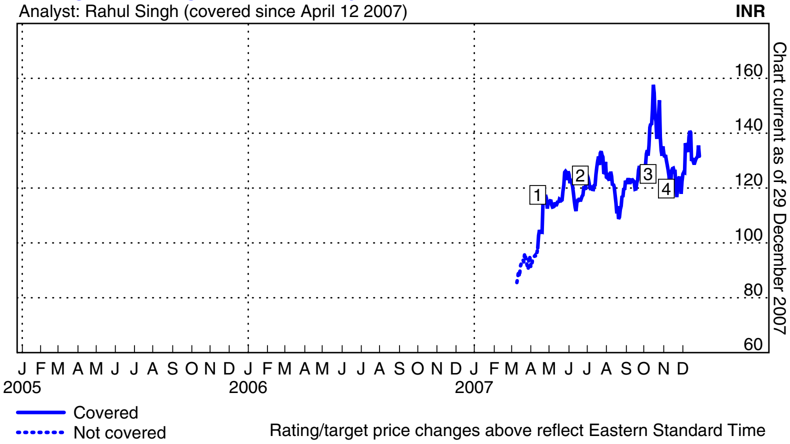
#	Date	Rating	Target Price	Closing Price
1:	14 Jan 05	*1M	*260.00	210.30
2:	22 Aug 05	1M	*400.00	306.10
3:	10 Jan 06	1M	*450.00	339.25
4:	13 Apr 06	1M	*500.00	395.95
5:	12 Oct 06	*1L	*600.00	475.65
6:	2 Jan 07	1L	*750.00	633.00
7:	23 Jan 07	1L	*800.00	689.15
8:	21 Feb 07	1L	*960.00	806.30
9:	20 Jun 07	1L	*1,050.00	824.65
10:	8 Oct 07	1L	*1,200.00	984.80

*Indicates change.

IDEA Cellular (IDEA.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Rahul Singh (covered since April 12 2007)



Rating/target price changes above reflect Eastern Standard Time

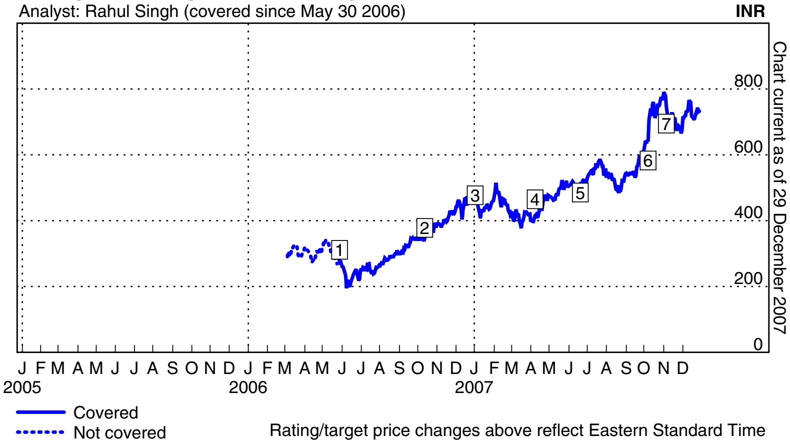
#	Date	Rating	Target Price	Closing Price
1:	12 Apr 07	1L	112.00	98.15
2:	20 Jun 07	1L	*140.00	115.15
3:	8 Oct 07	1L	*155.00	131.80
4:	6 Nov 07	*2L	*140.00	130.10

*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
3:	2 Jan 07	1M	*570.00	470.75
4:	9 Apr 07	1M	*510.00	415.60
5:	20 Jun 07	1M	*600.00	505.90
6:	8 Oct 07	*1L	*750.00	640.90
7:	6 Nov 07	*2L	*835.00	745.40

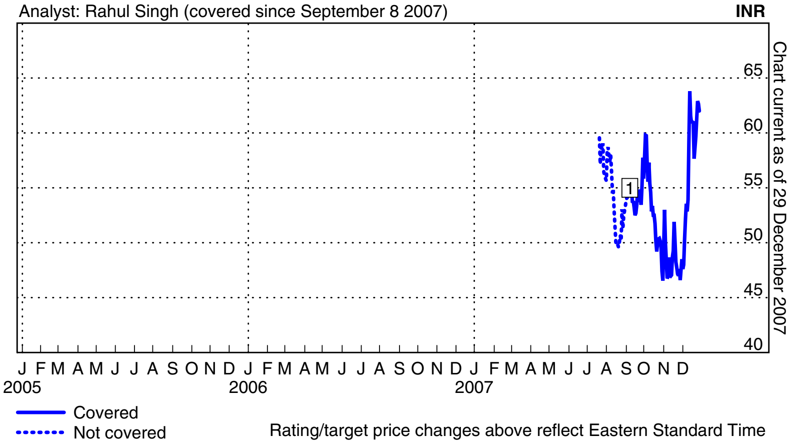
*Indicates change.

Rating/target price changes above reflect Eastern Standard Time

Spice Communications (SPCM.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Rahul Singh (covered since September 8 2007)



#	Date	Rating	Target Price	Closing Price
1:	7 Sep 07	1M	70.00	54.95

*Indicates change.

Rating/target price changes above reflect Eastern Standard Time

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