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MAHANAGAR TELEPHONE NIGAM LIMITED
RESEARCH

EQUITY RESEARCH | **January 08, 2008**

RESULTS REVIEW

Mahanagar Telephone Nigam Limited — Sell

Share Data

Market Cap	Rs. 124.58 bn
Price	Rs. 197.75
BSE Sensex	20,873.33
Reuters	MTNL.BO
Bloomberg	MTNL IN
Avg. Volume (52 Week)	0.89 mn
52-Week High/Low	Rs. 219.45/129
Shares Outstanding	630 mn

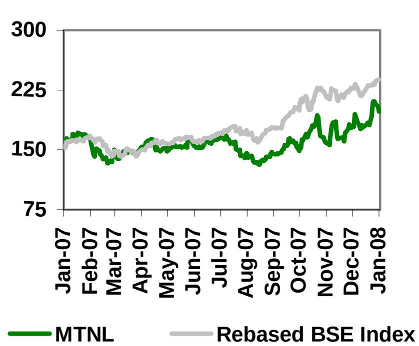
Valuation Ratios (Consolidated)

Year to 31 March	2008E	2009E
EPS (Rs.)	7.5	7.8
+/- (%)	(5.6)%	3.6%
PER (x)	26.4x	25.5x
EV/ Sales (x)	2.5x	2.5x
EV/ EBITDA (x)	14.1x	13.5x

Shareholding Pattern (%)

Promoters	56
FIIs	9
Institutions	25
Public & Others	10

Relative Performance



Core operations continue to disappoint

In Q2'08, Mahanagar Telephone Nigam Limited (MTNL) continued its weak performance, with net sales declining 1.7% yoy to Rs. 12 bn. The decrease was due to poor results reported by the wireline segment, partially offset by an improved performance across other segments. EBITDA margin dipped 59 bps yoy to 14.8% due to higher revenue sharing expenses and SG&A charges. Adj. net profit decreased 13.8% yoy to Rs. 947.8 mn due to a higher depreciation cost coupled with a rise in the effective tax rate.

In line with the expected decline in wireline subscriber base, coupled with a lower ARPU, the Company's net sales are estimated to decrease at a CAGR of 2.9% for FY07-FY09E. At the current price of Rs. 197.75, the stock is trading at a forward P/E of 26.4x FY08E and 25.5x FY09E. With operations restricted to two metropolises and an inability to scale outside the country, we maintain our Sell rating on the stock with a revised target price of Rs. 165 over a period of 12 months.

Result Highlights

During the quarter, net sales decreased 1.7% yoy to Rs. 12 bn primarily due to a reduction in the number of wireline subscribers. The Company's core operations, i.e. the Wireline segment, continued to register a decrease (down 12.3% yoy to Rs. 8.3 bn) owing to a decline in subscriber base coupled with lower average revenue per user (ARPU). However, the decline in overall net sales was somewhat arrested by an improved performance across all the other segments.

Key Figures (Standalone)

Quarterly Data	Q2'07	Q1'08	Q2'08	YoY%	QoQ%	H1'07	H1'08	YoY%
(Figures in Rs mn, except per share data)								
Net Sales	12,190	11,957	11,985	(1.7)%	0.2%	24,915	23,928	(4.0)%
EBITDA	1,877	2,617	1,775	(5.4)%	(32.2)%	4,604	4,184	(9.1)%
EBITDA Margins	*15.4%*	*21.9%*	*14.8%*			*18.5%*	*17.5%*	
(Subsribers in mn)								
GSM	2.3	2.6	2.8	21.0%	6.3%	2.3	2.8	21.0%
Basic cum WLL-F	3.8	3.8	3.7	(1.1)%	(0.9)%	3.8	3.7	(1.1)%
WLL-M	0.1	0.1	0.1	70.7%	12.5%	0.1	0.1	70.7%
Internet	1.6	1.8	1.8	15.5%	0.1%	1.6	1.8	15.5%
(ARPU in Rs. per month)								
GSM	251	208	281	12.1%	35.3%			
Fixed line	784	687	697	(11.1)%	1.4%			
Broadband	439	490	548	24.8%	11.8%			
Per Share Data (Rs.)								
Adj. EPS	1.7	1.8	1.5	(13.8)%	(14.5)%	3.6	3.1	(14.6)%

Segment Net Sales

Quarterly Data	Q2'07	Q1'08	Q2'08	YoY%	QoQ%
Basic Telephone	9,497	8,714	8,329	(12.3)%	(4.4)%
Cellular	1,825	2,028	2,294	25.7%	13.1%
WLL	171	213	229	33.9%	7.7%
Other Services	697	1,002	1,133	62.6%	13.1%
Total	**12,190**	**11,957**	**11,985**	(1.7)%	0.2%

Source: Company Data, Indiabulls Research

The share of the Cellular segment in the total sales improved 417 bps yoy to 19.1%. Moreover, the segment's sales increased 25.7% yoy to Rs. 2.3 bn led by a higher subscriber base and rise in ARPU. In addition, sales of the WLL and Other services (Broadband and Internet) rose by 33.9% yoy and 62.6% yoy, respectively. However, inspite of an improved performance by the Cellular and Broadband businesses, these segments are still not growing as aggressively as their peers.

Higher bandwidth charges shrink EBITDA margin further

EBITDA declined 5.4% yoy to Rs. 1.8 bn and margin reduced 59 bps to 14.8%. The decline in EBITDA margin was primarily due to higher revenue sharing expenses and SG&A charges. The rise in SG&A expenses (up 216 bps yoy to 21.2% of sales) was led by an increase in Internet bandwidth charges and provision for sundry debtors. However, the fall in margin was contained by lower employee remuneration (down 244 bps yoy to 35.7% of sales) owing to the one-time charge under the VRS scheme incurred during the corresponding quarter last year. Adj. net profit fell 13.8% yoy to Rs. 947.8 mn because of the rise in depreciation cost and a higher effective tax rate.

Key Events

- The Company made a bid to acquire the Sri-Lanka based fixed wireless operator, Suntel. The bid was submitted between the range of USD 100-120 mn, and if successful, MTNL would be able to add 0.3 mn subscribers to its total subscriber base.

Prospects

- MTNL plans to invest around Rs. 12.8 bn during the current fiscal year for expanding its services in Delhi. By undertaking this expansion, it plans to add 0.8 mn mobile subscribers to its already existing 1.2 mn user-base in Delhi.
- The Company might receive ILD as well as pan-India mobile license from the Department of Telecom (DoT). While the former will help it to route ILD calls from its own network instead of VSNL, the latter will expand its service reach beyond the two metropolises.

Key Risks

- The Company has surplus land and is planning to lease it out by way of a long term lease or revenue sharing arrangements. Unlocking of the land value can be a key risk to our rating.
- Receipt of ILD and pan-India license.
- Renewal of merger talks between MTNL and BSNL.

Outlook

Core operations on a decline

The Company continues to perform badly in the Wireline business. Though MTNL has tried to give value-added services such as broadband, IPTV, and virtual networking, none of them have been successful in arresting the declining trend of the Wireline business. The Company has even made an effort to scale up its cellular operations thereby registering a growth of 25.7% yoy during the quarter, but with presence in only two circles and pan-India players like Bharti Airtel Ltd and Reliance Communications growing aggressively, the chances of growth are further restricted.

We have upgraded our net sales estimate for FY09 by 8.5% to factor in the increased focus of the Company on the high value Cellular and Broadband operations. At the current price of Rs. 197.75, the stock is trading at a forward P/E of 26.4x FY08E and 25.5x FY09E. Based on our valuation, we reiterate our Sell rating on the stock with a revised target price of Rs. 165 over a period of 12 months. However, pan-India expansion or any development on the land front, can negatively affect our rating.

Key Figures (Consolidated)

Year to March	FY05	FY06	FY07	FY08E	FY09E	CAGR (%)
(Figures in Rs mn, except per share data)						(FY07-09E)
Net Sales	55,886	55,741	49,401	47,530	46,580	(2.9)%
EBITDA	13,644	8,544	8,726	8,284	8,664	(0.4)%
EBITDA Margins	*24.4%*	*15.3%*	*17.7%*	*17.4%*	*18.6%*	
(Subsribers in mn)						
GSM	0.9	1.9	2.7	3.2	3.5	
Basic cum WLL-F	4.1	3.9	3.8	3.6	3.4	
WLL-M	0.2	0.1	0.1	0.1	0.1	
Internet	1.0	1.4	1.8	2.0	2.1	
(ARPU in Rs. per month)						
GSM	398	287	204	215	210	
Fixed line	819	805	721	650	590	
Broadband	531	582	442	475	470	
Per Share Data (Rs.)						
Adj. EPS	15.1	9.6	7.9	7.5	7.8	(1.1)%
PER (x)	7.6x	19.1x	24.9x	26.4x	25.5x	

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