

Equities

14 November 2011 | 8 pages

Jet Airways (JET.BO)

Alert: 2QFY12 - Conference Call Takeaways

- Competition remains intense** — On both international and domestic operations. Mgmt noted that on international routes, entry of the domestic LCCs on West Asian / SE Asian routes impacted yields slightly in 2Q (though these have recovered into 3Q). Within the domestic market, Air India's 'fare wars' impacted 2Q yields. Looking ahead, management notes that yields in Nov improved ~18-20% over Oct levels (in line with Sept yields) – this implies 3Q yields should improve ~14% Q/Q – impressive, but less than the typical 18-20% seasonal uptick witnessed in the past years.
- Debt levels steady, cash flows augmented by asset sales** — Management notes that currency translation-inflated debt by ~Rs10bn. Over the next 6 months, ~Rs15bn of debt has to be repaid, which will be partly funded through cash from the Godrej – BKC transaction (~US\$100m) and sale and lease back (US\$150-300m).
- Cost Restructuring: a long-term positive** — Management noted that it plans to cut costs (ex fuel) / ASK by 5-10% pa. Areas targeted are IT overheads, manpower expenses, better aircraft utilization, et al. We think this is a positive, and necessary, given that oil prices remain sticky, and cost structures of the aviation sector in India must reflect the 'new reality' – a price sensitive market, within which the corporate travel market has a far lower proportion today than 5 years ago (corporate segment accounts for ~33% of Jet's revenues – at the time of Jet's IPO it was estimated that ~80% of passenger travel was business related). One tangible improvement: that we highlight - fuel burn / block hour that's improved by ~10% in the past four years.
- Brand repositioning** — Management expects operations to be consolidated into two different formats: full service and low fare. Before it embarks on this initiative, it needs to reduce structural costs to ensure the low fare model is sustainable over the long term – we think this is critical given that 75% of seats offered by Jet are low cost now.
- Maintain Sell** — Jet is interestingly positioned – recent developments from a competitive perspective implies some relief for its full service business. However, we think oil and a depreciating rupee trump possible market share gains, for now. Longer term, we like management's focus on cost reduction initiatives as the business is realigned to the current demand environment.

Figure 1. Jet Airways – Statistical Abstract

Year to 31 Mar	Net Profit (RsM)	Diluted EPS (Rs)	EPS growth (%)	P/E (x)	P/B (x)	ROE (%)	Yield (%)
2010A	-6,028	-69.82	71.7	-3.7	1.3	-30.7	0.0
2011A	-2,682	-31.06	55.5	-8.4	1.4	-16.1	0.0
2012E	-9,477	-109.78	na	-2.4	2.9	-80.2	0.0
2013E	-1,807	-20.93	80.9	-12.4	3.8	-26.7	0.0
2014E	1,168	13.53	164.6	19.2	3.2	18.1	0.0

Source: Powered by dataCentral

Company Update

Sell/High Risk	3H
Price (14 Nov 11)	Rs259.75
Target price	Rs215.00
Expected share price return	-17.2%
Expected dividend yield	0.0%
Expected total return	-17.2%
Market Cap	Rs22,425M US\$448M

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



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Jet Airways

Valuation

Airlines are trading plays - given the cyclical nature of their business, high operational and financial leverage and an earnings profile that is excessively volatile and sensitive to macro variables like oil prices and currency movements. Given the excessive volatility in earnings of airlines, we prefer to utilize a more stable metric to value airlines. Our target price of Rs215 is based on 9x EV/EBITDAR on FY13 estimates. Our multiple of 9x pegs Jet at a significant premium to other LCC / regional growth carriers. Typically, in the past we've pegged Jet at a premium (of around 20-25%) to its regional peers; given more than 5-6 years of trading history, we now begin to peg the stock against its own trading history. Jet's average forward EV/EBITDAR since its IPO has been around 12x, excluding the 2 exceptional years of CY07-08 (these years were the confluence of the global financial crisis and the ramp-up in competition in the industry - we reckon they are somewhat exceptional and the collapse in earnings precipitated by both factors will not likely play out over the near term). Our fair-value multiple of 9x (which is a 25% discount to the 12x average) provides a sufficient buffer - in our view - to the risk that oil prices continue to remain elevated.

Risks

We assign a default High Risk rating to Jet Airways given that the stock is deemed to be relatively volatile by our quantitative risk-rating model (based on stock price movements in the past year) or that it has a trading history of less than 3 months. Our High Risk rating emanates from very high sensitivity of Jet Airways' earnings (and thus stock price) to macro environment, mainly oil prices and foreign exchange rates- both of which are inherently volatile. Key upside risks to our recommendation and target price are: a) Stronger-than-forecast yield growth in the domestic market could boost revenues / EBITDAR, b) a sustained decline in ATF prices (driven by a significant fall in global oil prices), c) Strong appreciation of the rupee vs. USD; and d) Legislative changes - FDI permitted for other foreign airlines and/or lower sales tax on aviation turbine fuel. Key downside risks that could result in stock falling below our target price include a) increased competitive intensity, marked by a pro-longed reduction in fares by other airline companies, could put pressure on yields, and b) sustained cost pressures due to high oil prices and a depreciating rupee against USD

Appendix A-1

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Jet Airways (JET.BO) Ratings and Target Price History Fundamental Research

Analyst: Jamshed Dadabhoy



	Date	Rating	Target Price	Closing Price
1	20-Aug-09	3H	*174.00	243.50
2	15-Feb-10	3H	*428.00	476.90
3	14-Dec-10	*3M	*696.00	771.90

	Date	Rating	Target Price	Closing Price
4	27-Sep-11	3M	*230.00	264.60
5	4-Oct-11	3M	*215.00	227.20
6	7-Oct-11	Stock rating system changed		

	Date	Rating	Target Price	Closing Price
7	7-Oct-11	*3H	215.00	232.50

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Jet Airways (JET.BO) Ratings and Target Price History Best Ideas Research Relative Call (3 Month)

Analyst: Jamshed Dadabhoy



	Date	Rating	Target Price	Closing Price
1	11-Feb-11	*ADD LP	-	457.25

	Date	Rating	Target Price	Closing Price
2	1-Mar-11	*REM LP	-	444.10

* Indicates change

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Data current as of 10 Oct 2011

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	45%	42%	37%	50%	43%	46%

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