Equities

11 November 2011 | 13 pages

Jet Airways (JET.BO)

2QFY12: Results Reflect Impact of Adverse Macro Environment

- **Recurring loss at Rs 4.4bn slightly higher than estimates** — Operating revenue (ex-leasing income) at Rs ~31.9bn was 7% below our estimates, reflecting a ~250bps Q/Q decline in dom PLF. EBITDAR at ~Rs669m was ~19% below estimates- primarily a result of Rs 1.1bn EBITDAR loss in the domestic segment (vs CIRA est of Rs 443m). Reported loss was much higher at Rs 7.1bn, reflecting ~Rs 2.7bn of forex loss.
- **Domestic Operations: EBITDAR loss- first quarter post 2QFY10** — Overall domestic industry capacity grew 20%YoY, in line with pax growth. Jet's market share (ex-JetLite) dropped ~140bps YoY -reflecting increased competitive intensity. Total op revenue / RPK (including surcharge, baggage etc) dropped ~10% YoY, resulting in EBITDAR loss of ~Rs 1.1bn (Rs 2bn/Rs 1bn profits in 2QFY11 and 1QFY12 respectively).
- **International Operations: The silver lining**— While international departures rose a healthy 12%, ASKs rose ~10% YoY, reflecting an increase in short-haul flights. A slight (~2%) miss in revenue estimates was compensated for by a very strong EBITDAR margin of ~9% (+420bps QoQ; CIRA est: 2%). A steady PLF of ~81% and slightly better yields could not compensate for a ~52% growth in fuel costs (~10% YoY growth in block hours). A YoY margin drop of 1,100bps reflects the adverse macro environment for the industry rather than Jet's relative positioning.
- **JetLite** — Similar to Jet's (9W) domestic operations, JetLite's EBITDAR margins also slipped ~20ppt YoY, reflecting increased cost pressures. PLF was steady at ~75% but yields dropped ~13% YoY, resulting in an EBITDAR loss of ~Rs 419m. JetLite's market share increase by ~60bps YoY and QoQ as its share in Jet's overall domestic operations increased at the expense of overall consolidated yield.
- **Maintain Sell** — Outlook remains challenging for the sector, given sustained high crude oil prices and a depreciating INR. Cash generation through sale and lease-back income should enable Jet to ensure that debt levels don't burgeon past current levels (Rs 161bn). We remain sellers, given fairly challenging domestic conditions, and limited visibility on crude oil prices falling.

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	-3.6	1.3	-30.7	0.0
2011A	-2,682	-31.06	55.5	-8.1	1.4	-16.1	0.0
2012E	-9,477	-109.78	na	-2.3	2.8	-80.2	0.0
2013E	-1,807	-20.93	80.9	-12.1	3.7	-26.7	0.0
2014E	1,168	13.53	164.6	18.7	3.1	18.1	0.0

Source: Powered by dataCentral

■ Company Update

Sell/High Risk	3H
Price (11 Nov 11)	Rs253.00
Target price	Rs215.00
Expected share price return	-15.0%
Expected dividend yield	0.0%
Expected total return	**-15.0%**
Market Cap	Rs21,843M
	US$437M

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

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See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

Fiscal year end 31-Mar	2010	2011	2012E	2013E	2014E
Valuation Ratios					
P/E adjusted (x)	-3.6	-8.1	-2.3	-12.1	18.7
EV/EBITDA adjusted (x)	48.2	14.7	nm	13.6	8.7
P/BV (x)	1.3	1.4	2.8	3.7	3.1
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Per Share Data (Rs)					
EPS adjusted	-69.82	-31.06	-109.78	-20.93	13.53
EPS reported	-48.67	-9.94	-96.03	-20.93	13.53
BVPS	200.34	184.92	88.88	67.97	81.49
DPS	0.00	0.00	0.00	0.00	0.00
Profit & Loss (RsM)					
Net sales	111,587	140,110	156,611	165,898	183,365
Operating expenses	-117,831	-138,719	-165,007	-164,264	-176,730
EBIT	**-6,244**	**1,391**	**-8,396**	**1,634**	**6,635**
Net interest expense	-10,474	-10,858	-8,602	-8,098	-7,505
Non-operating/exceptionals	10,794	7,159	5,152	4,206	2,330
Pre-tax profit	**-5,924**	**-2,308**	**-11,847**	**-2,258**	**1,460**
Tax	-104	-374	2,369	452	-292
Extraord./Min.Int./Pref.div.	1,826	1,824	1,187	0	0
Reported net income	**-4,202**	**-858**	**-8,291**	**-1,807**	**1,168**
Adjusted earnings	-6,028	-2,682	-9,477	-1,807	1,168
Adjusted EBITDA	3,446	10,577	606	10,456	15,278
Growth Rates (%)					
Sales	-14.7	25.6	11.8	5.9	10.5
EBIT adjusted	64.5	122.3	-703.4	119.5	306.2
EBITDA adjusted	140.1	206.9	-94.3	nm	46.1
EPS adjusted	71.7	55.5	-253.4	80.9	164.6
Cash Flow (RsM)					
Operating cash flow	**8,871**	**9,480**	**7,714**	**6,571**	**11,671**
Depreciation/amortization	9,691	9,186	9,002	8,822	8,642
Net working capital	1,556	-1,008	6,152	-445	1,861
Investing cash flow	**11,842**	**-1,400**	**529**	**-100**	**-100**
Capital expenditure	-100	-100	-100	-100	-100
Acquisitions/disposals	11,942	-1,300	629	0	0
Financing cash flow	**-24,009**	**-6,473**	**-8,928**	**-6,571**	**-11,671**
Borrowings	-23,536	-6,000	-8,928	-6,572	-11,671
Dividends paid	0	0	0	0	0
Change in cash	**-3,297**	**1,607**	**-686**	**-100**	**-100**
Balance Sheet (RsM)					
Total assets	**206,674**	**203,947**	**191,138**	**183,079**	**176,281**
Cash & cash equivalent	8,264	6,772	5,000	5,000	5,000
Accounts receivable	8,765	10,254	12,014	11,817	13,062
Net fixed assets	166,611	158,924	149,094	140,271	131,629
Total liabilities	**189,378**	**187,983**	**183,464**	**177,211**	**169,245**
Accounts payable	21,807	21,580	27,673	25,410	27,488
Total Debt	142,804	136,804	127,876	121,304	109,633
Shareholders' funds	**17,296**	**15,964**	**7,673**	**5,867**	**7,035**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	3.1	7.5	0.4	6.3	8.3
ROE adjusted	-30.7	-16.1	-80.2	-26.7	18.1
ROIC adjusted	-3.8	0.7	-4.3	1.6	5.4
Net debt to equity	777.9	814.5	nm	nm	nm
Total debt to capital	89.2	89.6	94.3	95.4	94.0

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Significant margin erosion reflects challenging macro environment with sustained high crude oil prices and a sharply deprecating INR. That said, the company appears to have saved on overhead expenses

Figure 1. Jet Airways: 2QFY12 Results (Rs m)

	2QFY11	1QFY12	2QFY12	% Chg YoY	% Chg QoQ
Total operating revenues	**29,699**	**34,049**	**31,875**	**7.3%**	**-6.4%**
Employee Expenses	3,209	3,614	4,072	26.9%	12.7%
Fuel Cos	9,942	15,636	14,912	50.0%	-4.6%
S&D expenses	3,186	3,394	3,279	2.9%	-3.4%
Other operating expenses	7,848	9,485	8,944	14.0%	-5.7%
Total operating expenses	**24,185**	**32,129**	**31,206**	**29.0%**	**-2.9%**
EBITDAR	**5,514**	**1,920**	**669**	**-87.9%**	**-65.2%**
EBITDAR margin (%)	*18.6%*	*5.6%*	*2.1%*		
Lease rentals	2,158	2,073	2,082	-3.5%	0.4%
EBITDA	**3,356**	**(153)**	**(1,413)**	**-142.1%**	**824.3%**
EBITDA margin (%)	*11.3%*	*-0.4%*	*-4.4%*		
Sale and Lease back income	1351	1,367	1,060	-21.5%	-22.4%
Others	356	408	385	8.2%	-5.6%
Total Non operating income	**1,707**	**1,775**	**1,446**	**-15.3%**	**-18.5%**
Cost Ratios					
Fuel cost / Operating revenues	33.5%	45.9%	46.8%		
S&D Expenses / Operating revenues	10.7%	10.0%	10.3%		
Employee Cost / Operating revenues	10.8%	10.6%	12.8%		

Source: Citi Investment Research and Analysis

Continued losses at the PAT level have resulted in erosion of book value.

Debt levels appear to be fairly steady, for now.

Figure 2. Jet Airways: Balance Sheet (Rs m)

	As at Sep-10	As at Mar-11	As at Sep-11
Sources of Funds			
Share Capital	863	863	863
Reserves and Surplus	25,479	25,180	16,576
Total Shareholders' Funds	**26,342**	**26,043**	**17,439**
Total Debt	**137,371**	**134,804**	**141,231**
Deferred Tax Liability		336	
Deferred Payments for Jetlite investments	1,375		
Total Sources of Funds	**165,088**	**161,184**	**158,670**
Applications of Funds			
Total Net Fixed Assets	**143,559**	**139,647**	**144,176**
Investments	16,450	17,251	16,451
Current Assets			
Inventories	6,439	7,112	7,787
Sundry Debtors	8,634	9,658	11,661
Cash and bank balances	7,576	5,877	5,666
Loans and advances	23,574	27,329	27,718
Total Current Assets	**46,223**	**49,976**	**52,832**
Current Liabilities and Provisions			
Current Liabilities	39,702	43,821	52,771
Provisions	1,442	1,869	2,017
Total Current Liabilities and Provisions	**41,144**	**45,690**	**54,788**
Net Current Assets	**5,079**	**4,285**	**(1,956)**
Total Application of Funds	**165,088**	**161,184**	**158,670**

Source: Company, Citi Investment Research and Analysis

Total op revenue / RPK (including surcharge, baggage etc) dropped ~10% YoY, resulting in EBITDAR loss of ~Rs 1.1bn (Rs 2bn/Rs 1bn profit in 2QFY11 and 1QFY12 respectively). Fuel costs rose ~47% YoY despite a modest 16% YoY growth in block hours- a reflection of heightened oil prices. While the company was able to cut S&D expenses by 9% YoY, higher employee expenses (+41% YoY) and higher other expenses (+13% YoY), resulted in the high EBITDAR loss for Jet's domestic operations.

Figure 3. Jet Airways: Domestic Operations (Rs m except for operational data)

	2QFY11	1QFY12	2QFY12	% Chg YoY	% Chg QoQ
Operational Data					
Block hours	46158	54,874	53,309	15.5%	-2.9%
ASKs (mn)	2849	3,216	3,047	6.9%	-5.3%
RPKs (mn)	2035	2,399	2,198	8.0%	-8.4%
PLF (%)	71.4%	74.6%	72.1%		
Passengers flown (mn)	2.32	2.78	2.60	12.1%	-6.6%
Departures	27,182	32,746	32,316	18.9%	-1.3%
Total operating revenues	**12,378**	**15,083**	**12,093**	**-2.3%**	**-19.8%**
Salaries and Wages	1,763	2,059	2,485	41.0%	20.7%
Fuel Costs	3,939	6,320	5,774	46.6%	-8.6%
S&D expenses	1,497	1,409	1,362	-9.0%	-3.3%
Other operating expenses	3179	4,283	3,585	12.8%	-16.3%
Total operating expenses	**10,378**	**14,071**	**13,206**	**27.2%**	**-6.1%**
EBITDAR	**2,000**	**1,012**	**(1,113)**	**nm**	**nm**
EBITDAR margin (%)	16.2%	6.7%	-9.2%		
Lease rentals	995	1,077	1,085	9.0%	0.7%
EBITDA	**1,005**	**(65)**	**(2,198)**	**nm**	**nm**
EBITDA margin (%)	8.1%	-0.4%	-18.2%		
Non operating income	340	379	363	6.8%	-4.3%

Source: Company, Citi Investment Research and Analysis

While substantially lower than 2QFY11 margins of ~20%, Jet's international operations in 2QFY12 are healthy given the overall challenging macro environment (deprecating INR and sustained high crude oil prices.

Figure 4. Jet Airways: International Operations (Rs m except for operational data)

	2QFY11	1QFY12	2QFY12	% Chg YoY	% Chg QoQ
Operational Data					
Block hours	39618	43,255	43,230	9.1%	-0.1%
ASKs (mn)	5631	6,103	6,167	9.5%	1.0%
RPKs (mn)	4527	4,912	4,967	9.7%	1.1%
PLF (%)	80.4%	80.5%	80.5%	0.2%	0.1%
Passengers flown (mn)	1.13	1.28	1.29	14.2%	0.4%
Departures	8,446	9,404	9,442	11.8%	0.4%
Total operating revenues	**17,321**	**18,966**	**19,782**	**14.2%**	**4.3%**
Salaries and Wages	1,446	1,555	1,586	9.7%	2.0%
Fuel	6,003	9,316	9,138	52.2%	-1.9%
S&D expenses	1,689	1,985	1,917	13.5%	-3.4%
Other operating expenses	4669	5,202	5,359	14.8%	3.0%
Total operating expenses	**13,807**	**18,058**	**18,000**	**30.4%**	**-0.3%**
EBITDAR	**3,514**	**908**	**1,782**	**-49.3%**	**96.2%**
EBITDAR margin (%)	20.3%	4.8%	9.0%		
Lease rentals	1,163	996	996	-14.4%	0.0%
EBITDA	**2,351**	**(88)**	**786**	**nm**	**nm**
EBITDA margin (%)	13.6%	-0.5%	4.0%		
Sale and Lease back income	1351	1367	1060	-21.5%	-22.4%
Others	16	29	23	43.8%	-20.2%
Total Non operating income	**1,367**	**1,396**	**1,083**	**-20.8%**	**-22.4%**

Source: Citi Investment Research and Analysis

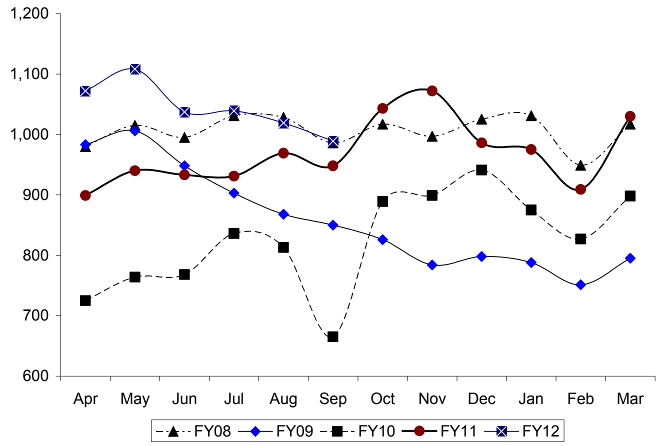
JetLite operations mirror the domestic (9W) operations- an EBITDAR loss driven by mounting fuel cost pressures. A higher proportion of JetLite in overall domestic services offered by Jet suggests that overall yield could be impacted, going forward

Figure 5. JetLite: 2QFY12 Results (Rs m except for operational data)

	2QFY11	1QFY12	2QFY12	% Chg YoY	% Chg QoQ
Operational Data					
ASKs (mn)	1,263	1,447	1,472	16.5%	1.7%
RPKs (mn)	937	1,159	1,100	17.4%	-5.1%
PLF (%)	74.2	80.1	74.7		
Departures	9,536	10,063	10,518	10.3%	4.5%
Block Hours	16,354	17,265	17,702	8.2%	2.5%
Pax flown (m)	0.95	1.20	1.19	25.3%	-0.8%
Operating Revenues	**3,815**	**4,288**	**3,910**	**2.5%**	**-8.8%**
	-	-			
Employee Costs	452	426	416	-8.0%	-2.3%
Fuel Expenses	1,711	2,770	2,692	57.3%	-2.8%
S&D Expense	302	299	284	-6.0%	-5.0%
Other Operating Expenses	912	959	937	2.7%	-2.3%
Total Operating Expenses	**3,377**	**4,454**	**4,329**	**28.2%**	**-2.8%**
EBITDAR	**438**	**(166.2)**	**(419.0)**		
EBITDAR Margin (%)	11.5	(3.9)	(10.7)		

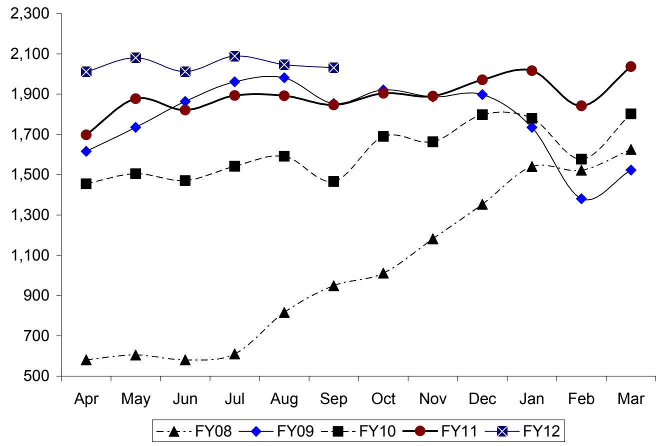
Source: Company, Citi Investment Research and Analysis

Figure 6. Jet Airways: Domestic ASK Trend (m)



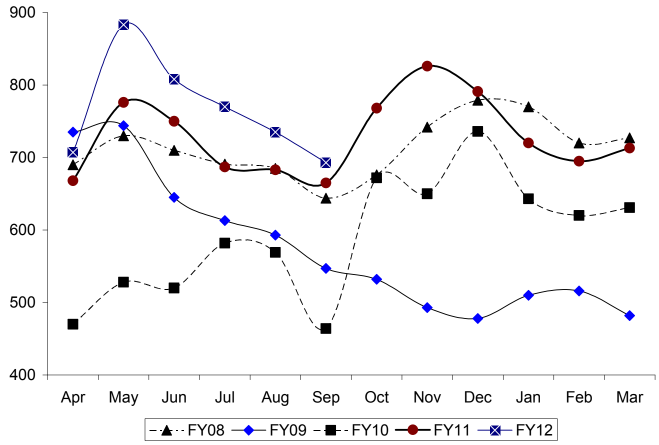
Source: Company, Citi Investment Research and Analysis

Figure 7. Jet Airways: International ASK Trend (m)



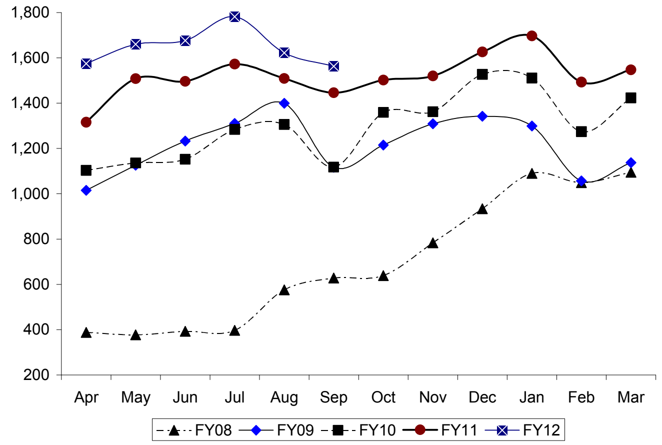
Source: Company, Citi Investment Research and Analysis

Figure 8. Jet Airways: Domestic RPK Trend (m)



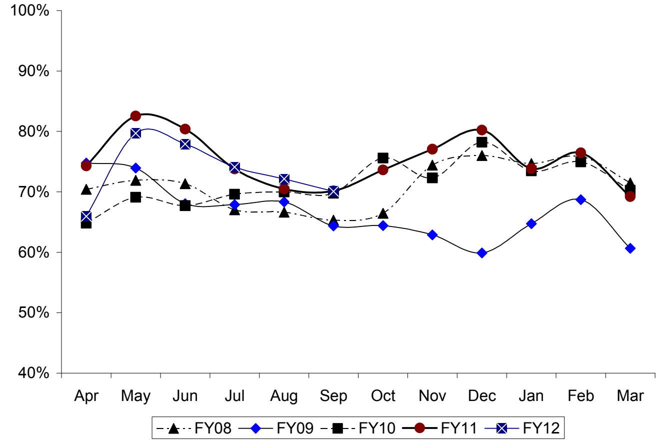
Source: Company, Citi Investment Research and Analysis

Figure 9. Jet Airways: International RPK Trend (m)



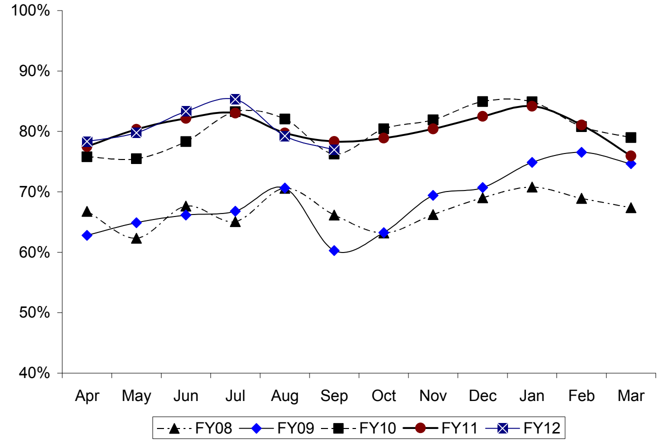
Source: Company, Citi Investment Research and Analysis

Figure 10. Jet Airways: Domestic PLF Trend (%)



Source: Company, Citi Investment Research and Analysis

Figure 11. Jet Airways: International PLF Trend (%)



Source: Company, Citi Investment Research and Analysis

Jet Airways

Company description

Jet Airways is one of India's leading domestic airlines with ~20% market share (~26% including Jet Lite). Long the leader in the domestic market, it has scaled up its international operations and now flies to several international destinations in the Asia Pacific region, US, Europe and Middle East. Jet 's fleet has consolidated over the past 2 years - we forecast 131 planes at end FY13 vis-a-vis 115 planes at end FY09.

Investment strategy

We rate Jet Airways shares Sell / High Risk (3H) with a target price of Rs215. Jet is one of India's leading airlines with a market share of around 26% and a very solid positioning in the business traveler segment. Over the past few years, industry growth has been well over 20%, but growth was unsustainable, characterized by aggressive reduction in fares. In the current cycle, we expect demand growth of around 14% CAGR over FY11-13E for the industry. Competitive intensity has abated, but with six main players we think the business environment will remain fairly challenging. We maintain our Sell rating as we see the current stock price as adequately discounting the positives.

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 prolonged 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

Analyst Certification

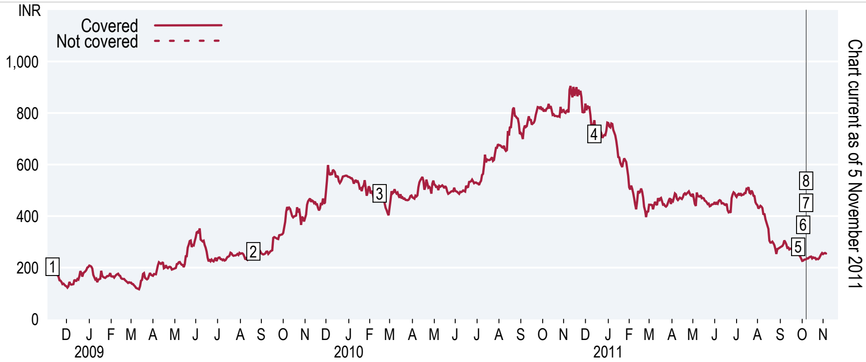
The research analyst(s) primarily responsible for the preparation and content of this research report are named in bold text in the author block at the front of the product except for those sections where an analyst's name appears in bold alongside content which is attributable to that analyst. Each of these analyst(s) certify, with respect to the section(s) of the report for which they are responsible, that the views expressed therein accurately reflect their personal views about each issuer and security referenced and were prepared in an independent manner, including with respect to Citigroup Global Markets Inc and its affiliates. No part of the research analyst's compensation was, is, or will be, directly or indirectly, related to the specific recommendation(s) or view(s) expressed by that research analyst in this report.

IMPORTANT DISCLOSURES

Jet Airways (JET.BO)

Ratings and Target Price History
Fundamental Research

Analyst: Jamshed Dadabhoy



	Date	Rating	Target Price	Closing Price
1	10-Nov-08	*3H	*167.00	202.20
2	20-Aug-09	3H	*174.00	243.50
3	15-Feb-10	3H	*428.00	476.90
4	14-Dec-10	*3M	*696.00	771.90
5	27-Sep-11	3M	*230.00	264.60
6	4-Oct-11	3M	*215.00	227.20
7	7-Oct-11	Stock rating system changed		
8	7-Oct-11	*3H	215.00	232.50

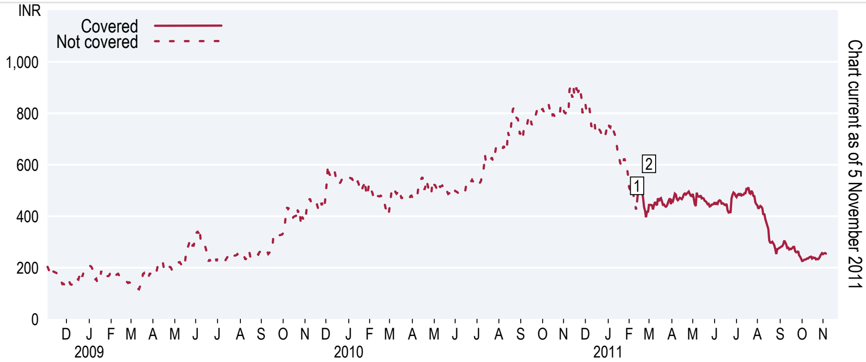
* Indicates change

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
2	1-Mar-11	*REM LP	-	444.10

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Citigroup Global Markets Inc. or its affiliates beneficially owns 1% or more of any class of common equity securities of Jet Airways. This position reflects information available as of the prior business day.

Citigroup Global Markets Inc. or an affiliate received compensation for products and services other than investment banking services from Jet Airways in the past 12 months.

Citigroup Global Markets Inc. currently has, or had within the past 12 months, the following as clients, and the services provided were non-investment-banking, securities-related: Jet Airways.

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