AVENDUS

February 09, 2012

BUY

Bharti Airtel

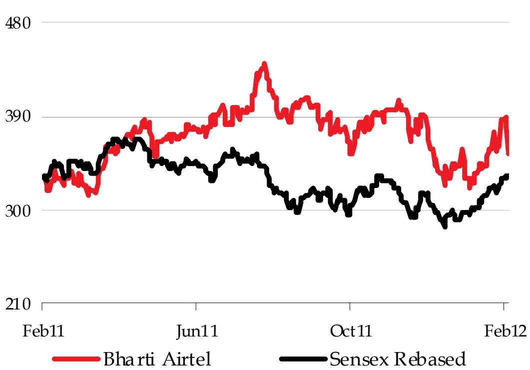
Target Price (INR) 463

Muted quarter, but outlook remains strong; maintain Buy

Rating	↔
Last Price (INR)	**354.0**
Bloomberg code	BHARTI IN
Reuters code	BRTI.BO
Avg. Vol. (3m)(mn)	7.05
Avg. Val.(3m)(INRbn)	2.58
52-wk H/L (INR)	448 / 309
Sensex	17,707
MCAP (INRbn/USDbn)	1,344 / 27.35

Shareholding (%)	09/11	12/11
Promoters	68.3	68.5
MFs, FIs, Banks	8.7	8.2
FIIs	17.1	17.5
Public	1.4	1.4
Others	4.4	4.5

Stock Chart (Relative to Sensex)



Stock Perfm. (%)	1m	3m	1yr
Absolute	7.0	-10.9	6.2
Rel. to Sensex	-4.6	-11.6	6.6

Financials (INRmn)	03/11	03/12f	03/13f
Sales	594,672	716,005	792,605
YoY (%)	42	20	11
EBITDA (%)	33.6	33.2	36.1
A.PAT	60,469	46,086	84,561
Sh o/s (diluted)	3,798	3,798	3,798
A.EPS (INR)	15.9	12.1	22.3
YoY (%)	-33	-24	83
D/E (x)	1.2	1.3	1.0
P/E (x)	22.2	29.2	15.9
EV/E (x)	9.7	8.4	6.7
RoCE (%)	10	6	9
RoE (%)	13	9	15

Quarterly Trends	03/11	06/11	09/11	12/11
Sales (INRmn)	162,654	169,749	172,698	184,767
PAT (INRmn)	14,009	12,152	10,250	10,113

Consolidated revenue growth of 7% q-o-q was aided by ARPM increase of 3% in the India and South Asia business, stable ARPMs in the African business and 11% INR depreciation. However, minutes growth slowed in the Indian and African wireless businesses. Consolidated EBITDA margins dipped 142-bp q-o-q due to provisions in the Bangladesh business and sponsorship of events such as the Indian Grand Prix. We estimate better ARPMs and EBITDA margins over FY13f-FY14f due to a reduction in competition. Our forecasts include minutes growth of c6% over FY13f-FY14f. However, we reduce our PAT forecasts for FY12-FY14 by up to 19% due to higher depreciation and taxes. We roll over our TP to Dec12 and cut it by 4% to INR463. Maintain Buy. Risk factors include currency fluctuation and impact of the tariff hike on minutes.

ARPM growth and currency aids revenue, but minutes growth falters

Revenue in the India and South Asia wireless business increased by 4% q-o-q due to a 3% q-o-q increase in ARPM. However, minutes growth was muted, at 1% q-o-q. Similarly, on constant currency, revenue in the African business slowed to 4% q-o-q, despite stable ARPMs. This was due to minutes growth of 3% q-o-q compared to 10% during 1QFY12-2QFY12. Consolidated revenues grew 7% q-o-q, aided by 11% INR depreciation. Our forecasts include y-o-y minutes growth of 6.0% in FY13f and 5.6% in FY14f. However, we estimate the reducing competition to enable further tariff hikes in FY13f and FY14f, aiding revenue growth.

Higher SG&A costs led to 142-bp q-o-q dip in EBITDA margins

Provisions in the Bangladesh business and sponsorship of events such as the Indian Grand Prix led to a 131-bp q-o-q increase in SG&A costs as a percentage of sales. This mainly led to a 142-bp q-o-q drop in consolidated EBITDA margins. Absence of provisions in the Bangladesh business, further tariff hikes in India and better EBITDA margins in the African business are likely to improve consolidated EBITDA margins by 296-bp in FY13f and 171-bp in FY14f.

Increase in depreciation impacted PAT margins

PAT margins declined by 46-bp q-o-q due to a 100-bp increase in depreciation as a percentage of sales. Depreciation grew by 13% q-o-q, despite a 6% q-o-q increase in investments in fixed assets. This was due to 40% q-o-q increase in depreciation in African biz. led by revised assessment of life of fixed assets.

Outlook remains strong; maintain Buy

We estimate lower competition and an upward bias for pricing over FY13f-FY14f. Hence, we change our revenue and EBITDA forecasts for FY12-FY14 by between -0.5% and 2.0%. An increase in depreciation and taxes leads us to cut our FY12-FY14 PAT forecasts by up to 19%. We continue to value the African business at a one-year forward EV/EBITDA of 5.2x and the Indian non-tower business at a one-year forward EV/EBITDA of 7.3x. Our valuations for the tower business imply an EV/tower of INR6.9mn. We roll over our TP to Dec12 and cut it by 4% to INR463. We maintain Buy. Risk factors include currency fluctuation and a higher-than-expected impact of the likely tariff hike on minutes.

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Exhibit 1: Result snapshot for 3QFY12

(INRmn)	Dec10 (3m)	Sep11 (3m)	q-o-q (%)	Dec11 (3m)	y-o-y (%)
Total operating income	157,560	172,698	7	184,767	17
Total operating expenses	107,777	114,547	9	125,183	16
EBITDA	49,783	58,151	2	59,584	20
Other Income	243	-20	-60	-8	-103
Depreciation	27,101	31,639	13	35,734	32
EBIT	22,926	26,492	-10	23,842	4
Interest	7,433	11,013	-28	7,963	
Recurring PBT	15,493	15,479	3	15,878	2
Net extra ordinary items	0	0		0	
PBT (reported)	15,493	15,479	3	15,878	2
Total taxes	3,390	4,886	13	5,521	63
PAT (reported)	12,103	10,593	-2	10,357	-14
(+) Share in assoc. earnings	0	0		0	
Less: Minority interest	-928	343		244	
Prior period items	0	0		0	
Net income (reported)	13,031	10,250	-1	10,113	-22
Shares outstanding (mn)	3,794	3,794		3,794	
EPS (INR)	3.4	2.7	-1	2.7	-22
Operating ratios (%)					
EBITDA margin	31.6	33.7	-142-bp	32.2	65-bp
EBIT margin	14.6	15.3	-244-bp	12.9	-165-bp
Net profit margin	8.3	5.9	-46-bp	5.5	-280-bp

Source: Company, Avendus Research

PAT forecasts for FY12f-FY14f cut by up to 19%

Revenue forecasts over FY12f-FY14f are marginally changed, however we have lowered our forecasts for EBITDA margins by up to 104-bp over FY12f-FY14f due to likelihood of higher SG&A costs. Our PAT forecasts are cut by up to 19% over FY12f-FY14f due to increase in depreciation of up to 4%, compared to earlier forecasts. Also higher tax rate in 3QFY12 has led us to increase our tax expense by up to 8% over FY12f-FY14f.

Exhibit 2: Earnings revision summary

(INRmn)	FY12f			FY13f			FY14f		
	Old	New	Var (%)	Old	New	Var (%)	Old	New	Var (%)
Revenue	708,362	716,005	1.1	788,266	792,605	0.6	878,187	873,984	-0.5
EBITDA	241,375	237,495	-1.6	291,963	286,329	-1.9	337,544	330,653	-2.0
PAT	56,852	46,086	-18.9	97,500	84,561	-13.3	124,126	113,587	-8.5
EPS (INR)	15.0	12.1	-18.9	25.7	22.3	-13.3	32.7	29.9	-8.5

Source: Company, Avendus Research

Exhibit 3: Key financials for BHARTI – Africa region

(USDmn)	Dec10 (3m)	Sep11 (3m)	q-o-q (%)	Dec11 (3m)	y-o-y (%)
Revenue	911	1,030	2.6	1,057	16.1
EBITDA	190	270	4.3	282	48.5
EBITDA Margin	20.8	26.2	44-bp	26.7	584-bp

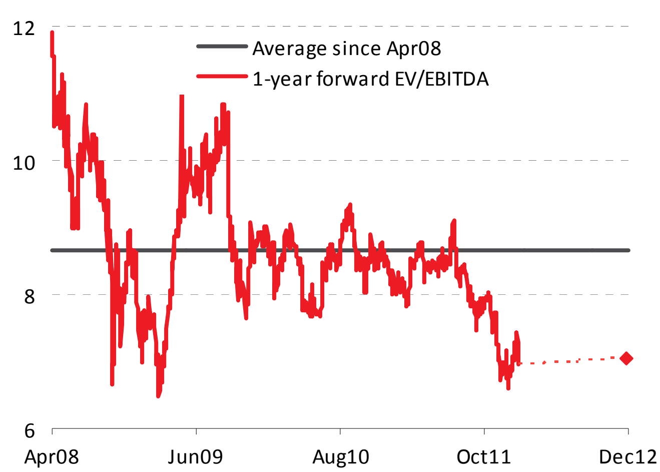
Source: Company, Avendus Research

Exhibit 4: Key segmental financials for BHARTI – India and South Asia region

	Dec10 (3m)	Sep11 (3m)	q-o-q (%)	Dec11 (3m)	y-o-y (%)
Revenue (INRmn)					
Mobile	91,459	97,827	4.0	101,764	11.3
Enterprise	10,503	11,042	7.6	11,881	13.1
Telemedia	9,068	9,528	-4.2	9,128	0.7
Digital TV Services	2,133	3,135		3,327	
Others	660	859	-22.5	666	0.9
Passive Infra	21,972	23,766	2.6	24,393	11.0
Total before eliminations	135,795	146,157	3.4	151,158	11.3
Eliminations	-18,582	-19,367		-19,530	
Total after eliminations	117,213	126,790	3.8	131,628	12.3
EBITDA* (INRmn)					
Mobile	31,689	32,926	4.6	34,431	8.7
Enterprise	2,260	2,371	-15.3	2,008	-11.2
Telemedia	4,045	4,213	-15.9	3,542	-12.4
Digital TV Services	-150	116		90	
Others	-3,583	-1,969		-3,139	
Passive Infra	8,486	8,902	2.3	9,110	7.4
EBITDA before eliminations	42,747	46,559	-1.1	46,043	7.7
Eliminations and acquisition costs	-658	-831		-818	
EBITDA after eliminations	42,089	45,728	-1.1	45,225	7.5
EBITDA Margin* (%)					
Mobile	34.6	33.7	18-bp	33.8	-81-bp
Enterprise	21.5	21.5	-457-bp	16.9	-462-bp
Telemedia	44.6	44.2	-541-bp	38.8	-580-bp
Digital TV Services	-7.0	3.7		2.7	
Passive Infra	38.6	37.5	-11-bp	37.3	-128-bp
Consolidated - India and SA	35.9	36.1	-171-bp	34.4	-155-bp

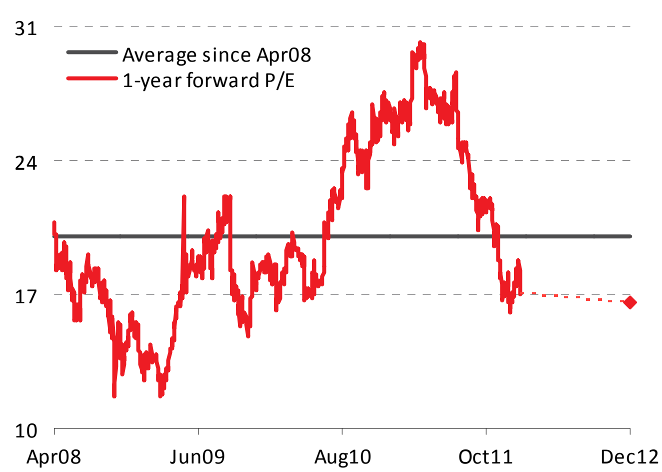
Source: Company, Avendus Research

Exhibit 5: 1-year forward EV/EBITDA



Source: Company, Bloomberg, Avendus Research

Exhibit 6: 1-year forward P/E



Source: Company, Bloomberg, Avendus Research

Risk factors

- **Currency fluctuations**: Significant currency fluctuation may lead to an increase in forex loss and higher net debt.
- **Impact of tariff hikes:** A higher-than-expected impact of the likely tariff hikes on minutes of use per subscriber may lead to slower minutes growth and revenue growth.

Financials and Valuations

Income statement (INRmn)

Fiscal year ending	03/11	03/12f	03/13f	03/14f
Total operating income	**594,672**	**716,005**	**792,605**	**873,984**
Total operating expenses	**395,103**	**478,510**	**506,276**	**543,331**
EBITDA	**199,569**	**237,495**	**286,329**	**330,653**
Other income	5,089	-2,437	4,569	5,445
Depreciation	101,988	134,522	143,914	154,201
EBIT	**102,670**	**100,535**	**146,984**	**181,897**
Interest	25,816	32,681	28,580	24,874
Recurring PBT	76,854	67,854	118,404	157,024
Net extra ordinary items	0	0	0	0
PBT (reported)	76,854	67,854	118,404	157,024
Total taxes	17,804	21,364	32,038	38,916
PAT (reported)	59,051	46,490	86,366	118,108
(+) Share in assoc. earnings	-74	0	0	0
Less: Minority interest	-1,492	404	1,805	4,520
Prior period items	0	0	0	0
Net income (reported)	60,469	46,086	84,561	113,587
Avendus net income	**60,469**	**46,086**	**84,561**	**113,587**
Shares outstanding (mn)	3,798	3,798	3,798	3,798
Avendus dil. shares (mn)	3,798	3,798	3,798	3,798
Avendus EPS (INR)	**16**	**12**	**22**	**30**

Growth ratios (%)

Total operating income	42.1	20.4	10.7	10.3
EBITDA	19.1	19.0	20.6	15.5
EBIT	-16.3	-2.1	46.2	23.8
Recurring PBT	-26.9	-11.7	74.5	32.6
Avendus net income	-32.6	-23.8	83.5	34.3
Avendus EPS	-32.6	-23.8	83.5	34.3

Operating ratios (%)

EBITDA margin	33.6	33.2	36.1	37.8
EBIT margin	17.3	14.0	18.5	20.8
Net profit margin	10.1	6.5	10.6	12.9
Other income/PBT	6.6	-3.6	3.9	3.5
Effective Tax rate	23.2	31.5	27.1	24.8

Balance sheet (INRmn)

Fiscal year ending	03/11	03/12f	03/13f	03/14f
Equity capital	18,988	18,988	18,988	18,988
Preference capital	0	0	0	0
Reserves and surplus	468,680	486,322	570,883	684,470
Net worth	**487,668**	**505,310**	**589,871**	**703,458**
Minority interest	28,563	29,242	30,368	32,425
Total debt	616,708	722,349	665,116	551,328
Deferred tax liability	-34,212	-48,834	-50,299	-51,808
Total liabilities	**1,098,727**	**1,208,067**	**1,235,056**	**1,235,403**
Net block	1,288,743	1,380,253	1,374,976	1,361,095
CWIP	0	0	0	0
Goodwill	0	0	0	0
Investments	9,650	34,329	42,640	53,021
Cash	9,575	13,916	17,724	16,038
Inventories	2,139	2,775	2,590	3,350
Debtors	54,929	60,062	65,887	72,993
Loans and advances	49,687	64,861	61,090	59,949
less: Current liabilities	308,731	339,667	321,171	322,138
less: Provisions	7,265	8,461	8,680	8,905
Net working capital	-199,666	-206,515	-182,560	-178,713
Total assets	**1,098,727**	**1,208,067**	**1,235,056**	**1,235,403**

Cash flow statement (INRmn)

Fiscal year ending	03/11	03/12f	03/13f	03/14f
Net profit	60,469	46,086	84,561	113,587
Depreciation	101,988	134,522	143,914	154,201
Deferred tax	0	0	0	0
Working capital changes	126,381	11,190	-20,147	-5,533
Less: Other income	5,089	-2,437	4,569	5,445
Cash flow from operations	**283,749**	**194,236**	**203,759**	**256,810**
Capital expenditure	-746,224	-91,510	5,277	13,881
Strategic investments	57	-42	0	0
Marketable investments	42,856	-24,637	-8,311	-10,381
Change in other loans & adv.	0	0	0	0
Goodwill paid	0	0	0	0
Other income	5,089	-2,437	4,569	5,445
Cash flow from investing	**-698,222**	**-118,626**	**1,535**	**8,945**
Equity raised	0	0	0	0
Change in borrowings	514,810	105,641	-57,232	-113,788
Dividends paid (incl. tax)	-4,443	0	0	0
Others	-111,641	-176,910	-144,253	-153,653
Cash flow from financing	**398,725**	**-71,269**	**-201,485**	**-267,441**
Net change in cash	**-15,748**	**4,341**	**3,808**	**-1,685**

Key Ratios

Fiscal year ending	03/11	03/12f	03/13f	03/14f
Valuation ratios (x)				
P/E (on Avendus EPS)	22.2	29.2	15.9	11.8
P/E (on basic, reported EPS)	22.2	29.2	15.9	11.8
P/CEPS	8.3	7.4	5.9	5.0
P/BV	2.8	2.7	2.3	1.9
Dividend yield (%)	0.3	0.0	0.0	0.0
Market cap. / Sales	2.3	1.9	1.7	1.5
EV/Sales	3.3	2.8	2.4	2.1
EV/EBITDA	9.7	8.4	6.7	5.5
Net Cash / Market cap.	1.4	3.6	4.5	5.1
Per share ratios (INR)				
Avendus EPS	15.9	12.1	22.3	29.9
EPS (Basic, reported)	15.9	12.1	22.3	29.9
Cash EPS	42.8	47.6	60.2	70.5
Book Value	128.4	133.1	155.3	185.2
Dividend per share	1.0	0.0	0.0	0.0
Total assets / equity (x)	1.8	2.3	2.2	1.9
Return ratios (%)				
ROCE	9.8	5.9	8.6	10.7
ROIC	10.4	6.1	9.0	11.3
ROE	13.3	9.3	15.4	17.6
ROA	7.4	4.0	6.9	9.2
OCF/Sales	47.7	27.1	25.7	29.4
FCF/Sales	-77.8	14.3	26.4	31.0
Turnover ratios (x)				
Asset turnover (x)	0.7	0.6	0.6	0.7
Gross asset turnover	0.5	0.5	0.6	0.6
Inventory / Sales (days)	0.8	1.3	1.2	1.2
Receivables (days)	27.8	29.3	29.0	29.0
Payables (days)	326.7	368.1	343.0	301.5
Working capital cycle (days)	-89.6	-109.5	-96.9	-82.5
Solvency ratios (x)				
Gross debt to equity	1.3	1.4	1.1	0.8
Net debt to equity	1.2	1.3	1.0	0.7
Net debt to EBITDA	2.8	2.6	1.9	1.3
Interest Coverage (on EBIT)	4.0	3.1	5.1	7.3

Note: Above financials are based on the IFRS method as reported by BHARTI.

Analyst Certification

I, Abhay Moghe, PGDBM, research analyst and author of this report, hereby certify that all of the views expressed in this document accurately reflect our personal views about the subject company/companies and its or their securities. We further certify that no part of our compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this document.

Disclaimer

Disclosure of Interest Statement (as of February 8, 2012)

	Analyst ownership of the stock	**Avendus or its associate company’s ownership of the stock**	**Investment Banking mandate with associate companies of Avendus**
Bharti Airtel	No	No	No

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