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Mumbai

## CRISIL Research assigns IPO grade '4/5' to Bharti Infratel Ltd

CRISIL has assigned a CRISIL IPO Grade "4/5" (pronounced "four on five") to the proposed initial public offer (IPO) of Bharti Infratel Ltd (Bharti Infratel). This grade indicates that the fundamentals of the IPO are 'above average' relative to the other listed equity securities in India. However, this grade is not an opinion on whether the issue price is appropriate in relation to the issue fundamentals. The grade is not a recommendation to buy, sell or hold the graded instrument, or a comment on the graded instrument's future market price or its suitability for a particular investor.

Bharti Infratel (including its 42% equity interest in Indus Towers Ltd) is a leading passive infrastructure service provider for telecom services in India. Its network of towers covers all the 22 telecom circles in the country. The company stands to gain from the increase in penetration of voice and data services, which is expected to drive the telecom companies' (telcos') demand for base transceiver stations (BTS) and additional towers. The tenancy ratio is expected to increase as telcos roll out 3G/4G on 2100 Mhz and 2300 Mhz bands. Bharti Infratel and Indus Towers will benefit from any expansion of the network by India's leading telcos - Bharti Airtel, Vodafone and Idea Cellular Ltd - as they are the preferred players for passive infrastructure requirements of the three telcos. Large-scale operations, first-mover advantage and pool sharing arrangement among the top three telcos have resulted in better-than-industry tenancy ratio for Bharti Infratel. It is expected to improve further leading to high operating leverage and improvement in profitability. The assigned grade also reflects the strong and stable operating cash flows resulting from long-term contracts. The company's robust back-end processes, which ensure higher reliability of network uptime for its clients, support the grade.

However, low return on capital employed (RoCE) is a concern. Since tower infrastructure is a business with high operating leverage, RoCE is expected to improve in line with an increase in the tenancy ratio albeit from a lower base. Low asset turnover and minimal use of leverage in a capital intensive industry have resulted in low return on equity (RoE) for Bharti Infratel over the past three years, which can increase if the leverage is corrected. Also, the overcapacity in the industry is expected to limit the demand for rollout of new towers. Further, regulatory changes and the resultant uncertainty pose a risk to telecom players as their network rollout plans could be hampered.

Bharti Infratel's consolidated operating income has increased at a four-year CAGR of 91% to Rs 92.6 bn in FY12 driven by addition of new towers and an increase in the tenancy ratio. EBITDA margins have remained steady at 35-37% over FY10-FY12. Strong growth in EBITDA and an increase in non-operating income (primarily interest income on loans given to group companies) resulted in adjusted net profit growing at 108% CAGR over FY08-12 to Rs 7.5 bn. RoCE and RoE have increased over the past five years largely due to increase in asset turnover but they continue to remain low (RoE was 5.3% in FY12). The company's consolidated net worth is Rs 139 bn as of FY12 and it has a low debt-equity ratio of 0.2x.

### About the company and the issue

Bharti Infratel was incorporated in 2006 as a subsidiary of Bharti Airtel, a global telecommunications company which currently has operations in 20 countries across Asia and Africa. Bharti Airtel is India's leading telecom service provider with revenues of Rs 714 bn (as of FY12) and revenue market share of 30% (as on quarter ended June 30, 2012). Bharti Infratel is a provider of tower and related passive infrastructure. The company was formed as per the demerger scheme wherein Bharti Airtel transferred its towers to Bharti Infratel through a scheme of arrangement effective as on January 31, 2008. Bharti Infratel operates in 11 of the 22 telecom circles. Bharti Infratel entered into a joint venture with Vodafone India and Idea Cellular to set up Indus Towers Ltd to benefit from the tower sharing arrangement. Bharti Infratel, Vodafone India and Aditya Birla Telecom (subsidiary of Idea Cellular) hold 42%, 42% and 16%, respectively, of the equity interest in Indus Towers. Indus Towers operates in 15 telecommunications circles in India, of which four circles overlap with those of Bharti Infratel. The company will use the IPO proceeds for installation of new towers, upgradations and replacements on existing towers, and green initiatives at its tower sites.

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