Interglobe Aviation Limited

IPO Note

Interglobe Aviation Ltd operates Indigo, which is the largest passenger airline in India with a market share of 37.4% (as of August 31, 2105). It is a low-cost carrier (LCC) with an asset light business model which enables it to have lowest cost and highest profitability amongst Indian airline companies.

Cost competiveness vs its peers: Interglobe Aviation (Interglobe) has been the only passenger aircraft operator in India to post consistent profits over the past seven years. The magnitude of the aircraft orders placed by the company has enabled it to negotiate favorable terms with Airbus, as well as with other suppliers and service providers. This has created a structural cost advantage for the company in terms of operations and maintenance of aircrafts compared to its peers.

Capitalizing on highly underpenetrated Indian air travel industry: The Indian air travel industry is underpenetrated in comparison to other countries with penetration levels of 0.08 annual domestic carrier seats per capita against other other developing markets such as Brazil, Turkey, Indonesia and China, where penetration rates are between 0.35 and 0.65. The Industry is growing at ~12.0% CAGR over the past nine years and is expected to grow at a similar pace. Going forward, we expect that improving penetration level will provide an opportunity to Indigo to capture market share as it is expanding its fleet size from currently 97 to 158 by FY2108E. Indigo is better placed compared to its peers to leverage on the anticipated growth in the industry as the competition would face constraints in adding capacity owing to stressed balance sheet and low or no profitability.

Soft Crude prices to benefit the Aviation Industry: Aviation Turbine Fuel (ATF) forms a major cost component for all airline operators. Soft ATF prices have boosted the operating performance of airline operators, including Indigo. ATF prices are expected to continue to be tepid in the near future, mainly due to higher global inventory levels of crude and owing to the subdued demand scenario. We expect lower crude prices and consequently lower ATF prices to lead to a decline in airfares, which should boost air traffic volume growth in the country. Load factors will resultantly head higher, while the same has already been witnessed in 1QFY2016 for all airline companies.

Outlook and Valuation: At the upper end of the price band, Interglobe is valued at 2.1x EV/Sales and at a P/E of 21.3x (FY2015). The company is not comparable to domestic peers on P/E basis as most of them are loss making while the premium on EV/Sales basis is warranted due to Interglobe's superior operating performance and profitability. We have compared Interglobe to its like to like international peer Ryanair, which trades at 3.2x EV/Sales and at a P/E multiple of 20.6x (FY2015). We believe that the valuation of Interglobe is justified, considering the opportunity present in the vastly underpenetrated Indian air travel market. Interglobe is better placed than its peers to capture higher market share on the back of its proven Management track record, continuous fleet addition and with its sustainable profitable business model. **Hence we recommend a "Subscribe" to the issue at the higher end of the price band.**

Exhibit 1: Key Financial

Y/E March (₹ cr)	FY2012	FY2013	FY2014	FY2015
Net Sales	5,565	9,203	11,117	13,925
% chg	*45.2*	*65.4*	*20.8*	*25.3*
Adj. Net Profit	141	783	474	1,296
% chg	*(75.7)*	*457.2*	*(39.4)*	*173.1*
OPM (%)	*0.9*	*9.7*	*4.6*	*13.4*
EPS (₹)	4.1	22.8	13.8	37.7
P/E (x)	187.0	33.6	55.4	20.3
RoE (%)	57.8	201.4	112.8	304.0

*Source: Company, Angel Research; Note:*EPS is based on Pre IPO outstanding shares at upper price band*

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Issue Open: October 27, 2015
Issue Close: October 29, 2015

Issue Details

Face Value: ₹10

Present Eq. Paid up Capital: ₹344cr

Offer Size: 4.3cr Shares

Post Eq. Paid up Capital: ₹360cr

Issue size (amount)**: ₹3,100cr - ₹3,270cr

Price Band**: ₹700-765

Post-issue implied mcap**: ₹25,332cr-27,566

Promoters holding Pre-Issue: 93.4%

Promoters holding Post-Issue: 84.6%

*Note:**at Lower and Upper price band respectively*

Book Building

QIBs	At least 50%
Non-Institutional	At least 15%
Retail	At least 35%

Post Issue Shareholding Pattern

Promoters Group	84.6
MF/Banks/Indian FIs/FIIs/Public & Others	15.4

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Company Background

Interglobe Aviation Ltd operates Indigo, which is one of the largest passenger airlines in India, with a market share of 37.4% (as of August 31, 2105). As per a report by CAPA, Indigo is the seventh largest LCC in the world by total seats (as of FY2015). Indigo started operations in August 2006 with a single aircraft and has grown its fleet size to 97 Airbus A320s with an average fleet age of 3.7 years. Presently, it operates services to 33 airports in India and to 5 international airports, with a maximum of 623 domestic flights per day.

It operates on a LCC business model with particular focus on the domestic Indian air travel market, while the share of its international routes is relatively low. It has an asset light model with 22 of the current 97 aircrafts on finance lease and the remaining 75 on an operating lease. It has an order book of 430 A320neo aircrafts that are slated to be delivered over the next decade. The A320neo aircrafts are the new engine option aircrafts that have enhanced seating capacity and deliver fuel savings of up to 15%. Its bulk aircraft procurement strategy and focus on being a pure LCC enables it to maintain one of the lowest CASK (Cost per Available Seat Kilometer) ex-fuel compared to other Indian and international airline operators.

Issue details

The issue comprises of fresh issue of equity shares of ₹10 each in the price band of ₹700-₹765 aggregating up to ₹1,272cr; and offer for sale by Promoters and Non-Promoters of 2.61cr shares aggregating to ₹1,998cr (at the upper end of the price band). The issue constitutes 11.9% of the post issue paid-up equity share capital of the company.

Exhibit 1: Share holding pattern

Particulars	Pre-Issue		Post-Issue	
	No. of shares	(%)	No. of shares	(%)
Promoter and Promoter Group	32,10,54,000	93.4	30,49,85,000	84.6
Non-Promoters	1,75,52,000	5.1	75,09,000	2.1
Others	51,10,000	1.5	4,78,52,065	13.3
Total	34,37,16,000	100	36,03,46,065	100

Source: Company, Angel Research

Exhibit 2: Offer size breakup

	No. of Shares (cr.)	Value (₹ cr)
Fresh Issue	1.7	1,272
Offer for Sale	2.6	1,998
Total	4.3	3,270

Source: Company, Angel Research

Objects of the Issue

- Retirement of certain outstanding lease liabilities and consequent acquisition of aircrafts amounting to ₹1,166cr.
- Purchase of ground support equipment for airline operations amounting to ₹34cr.
- The balance, which is contingent upon the issue price, will be utilised for general corporate purpose.

Investment Arguments

Cost competiveness vis-à-vis its peers

Interglobe has been the only passenger airline operator in India to consistently post profits over the past seven years while its Indian peers have posted losses, during the same period. The consistent profitability is largely due to its operating structure, which provides it an edge over competition.

Exhibit 3: Cost structure advantage in comparison to Peers

Expenses as a percentage of Sales	SpiceJet	Indigo	Ryanair
Maintenance	12.9	3.0	2.4
Fleet Related (Lease/Depreciation/Interest)	22.2	17.0	9.9
Operating Expenses (Fuel, Airport Charges, Overheads)	83.1	69.6	70.6

Source: Company, Angel Research

The magnitude of the aircraft orders placed by the company has enabled it to negotiate favorable terms with Airbus as well as other suppliers and service providers. This has created a structural cost advantage for the company in terms of operations and maintenance of aircrafts.

Maintenance costs: Indigo's young fleet (with an average fleet age of 3.2 years as against 4.1 years for SpiceJet), is mostly on a short term operating lease. This enables Indigo in achieving reliability in aircraft performance and lower maintenance costs. The company's maintenance cost, at 3.0% of sales, is significantly lower to its closest industry Peer SpiceJet, which has maintenance cost of 12.9%.

Fleet related expenses: Interglobe has deferred incentives which include profits from the sale and lease back of aircrafts from the lessor which the company is showing as differed incentive on the liabilities side and setting off against lease rentals. As a result, its fleet related expenses are lower compared to its peers.

Other operating expenses: Even on other operating cost basis which include employee, fuel, airport charges, etc, Indigo has fared better than its closest peer.

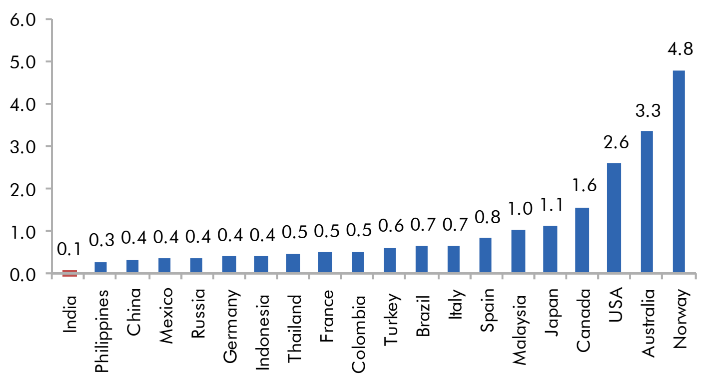
Company expected to deliver strong growth

We expect the company to report strong growth going forward and outperform competition in terms of market share gains. Our view is on the back of the following reasons:-

(a) Low air travel penetration in India to unearth growth opportunities for the company: According to a report by CAPA, India has one of the lowest air travel penetration rates in the world, defined on the basis of annual domestic carrier seats per capita. At 0.08, the annual domestic carrier seat per capita in India is low vis-a-vis other developing markets such as Brazil, Turkey, Indonesia and China, where penetration rates are between 0.35 and 0.65 (annual seats per capita).

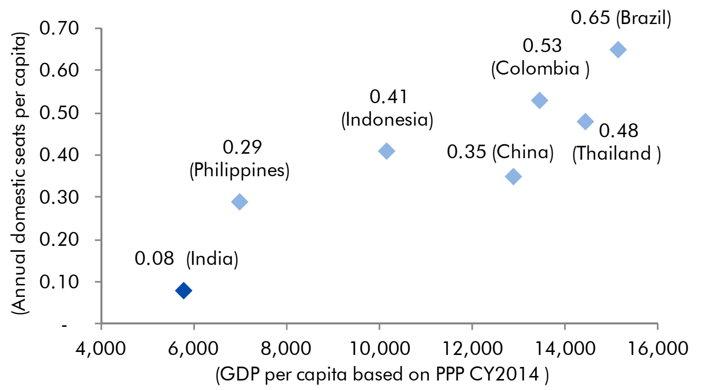
Also, the per capita income of a nation and air travel bear close correlation; air travel demand is greater in developed countries than in developing countries. Going forward, we believe that growth in India's GDP would boost air travel penetration in India. We believe that Interglobe is well positioned to capture a good share of such anticipated growth in the Indian air travel market. Moreover, as India's per capita income doubles over the next five to sever years, the growth in air traffic is expected to be exponential.

Exhibit 4: Annual domestic seats per capita



Source: Company, Angel Research

Exhibit 5: GDP growth & Air travel trends

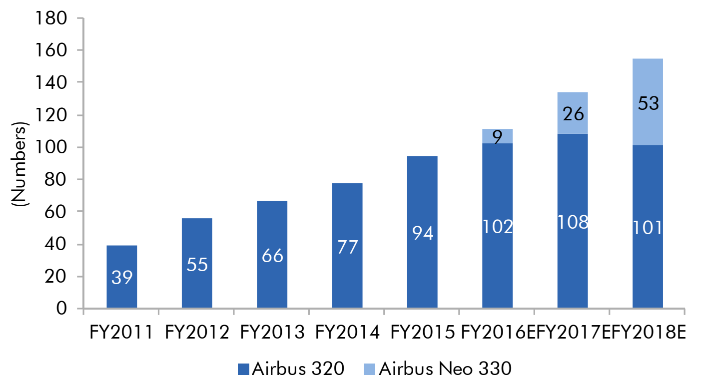


Source: Company, Angel Research

(b) **Healthy capacity expansion:** The company's fleet has expanded from 39 aircrafts in FY2011 to 97 currently. The company plans to further expand the fleet to 154 aircrafts by FY2018, which would include the purchase of 53 new Airbus A 320neo aircrafts (having a better fuel efficiency profile and higher seating capacity).

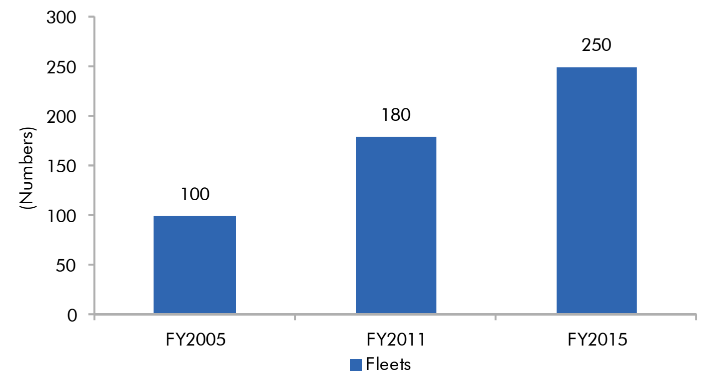
Earlier in 2011, the company had placed an order with Airbus for 180 aircrafts, to be delivered over the period of FY2015-23. In FY2015, the company placed a fresh order with Airbus for 250 aircrafts, the delivery of which would be phased between FY2018-26. Further, we do not foresee the company's competition resorting to any aggressive expansion as most of the companies in the sector are currently incurring losses. As a result, we believe that the company is well placed to capture a higher market share in the growing Indian air travel industry.

Exhibit 6: Robust capacity expansion plan



Source: Company, Angel Research

Exhibit 7: Aircraft orders status

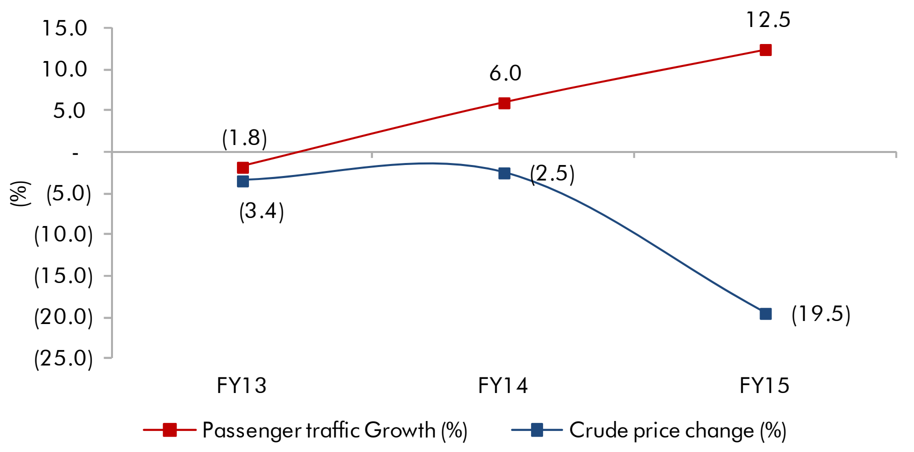


Source: Company, Angel Research

Weakness in Crude translates to favorable environment for Aviation Industry

ATF is a major cost component for all airline operators. As on FY2015, the fuel cost as a percentage of sales stood at 41.3% for Indigo. Prior to September 2014, fuel expense as a percentage of sales was in the range of 49.4%. The decline in prices of ATF has boosted the operating performance of air line operators, including Indigo. ATF prices are likely to continue to be tepid in the near future, mainly due to higher global inventory levels of crude and owing to a subdued demand scenario. Going forward, we expect lower crude prices and consequently lower ATF prices to lead to a decline in airfares, which in turn would possibly boost air traffic volumes. Load factors will resultantly head higher, while the same has already been witnessed in 1QFY2016 for all airline companies.

Exhibit 8: Falling crude prices vs passenger traffic growth



Source: Company

Key risks/concerns

Low Entry Barriers: The Indian airline industry is characterized by low entry barriers given the availability of leasing options and external finance. Increased competition can impact the load factors of airline companies.

Increase in Crude Oil prices: Since crude oil is a major portion of operating expense for all airline carries, any sharp increase in crude oil prices will impact the profitability of the company.

Currency Fluctuation Risk: Most of the company's debt is funded via ECBs. Any adverse impact on the currency could impact the profitability of the company.

Outlook and Valuation

Interglobe has steadily increased its fleet size since its inception and remained profitable over the years, largely due to its bulk aircraft procurement strategy and operational efficiencies. The company has registered a CAGR of 39.8% in revenues over FY2010-15 to ₹13,925cr and its earnings have grown at a CAGR of 22.0% to ₹1,296cr over the same period. For 1QFY2016, the company has reported a net profit of ₹640cr. The company is expected to grow on the back of opportunities arising out of growth in the domestic air travel industry. Also, decline in average ticket prices should result in higher volume growth for the company.

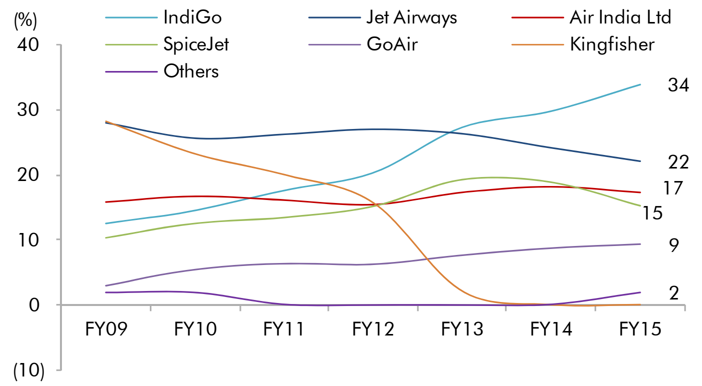
At the upper end of the price band, Interglobe is valued at 2.1x EV/Sales and at a P/E of 21.3x (FY2015). The company is not comparable to domestic peers on P/E basis as most of them are loss making while the premium on EV/Sales basis is warranted due to Interglobe's superior operating performance and profitability. We have compared Interglobe to its like to like international peer Ryanair, which trades at 3.2x EV/Sales and at a P/E multiple of 20.6x (FY2015). We believe that the valuation of Interglobe is justified, considering the opportunity present in the vastly underpenetrated Indian air travel market. Interglobe is better placed than its peers to capture higher market share on the back of its proven Management track record, continuous fleet addition and with its sustainable profitable business model. **Hence we recommend a "Subscribe" to the issue at the higher end of the price band.**

Exhibit 9: Valuations

		Currency	Sales	PAT	PAT Margin (%)	P/E	EV/Sales
Interglobe Aviation	FY2015	₹ cr	13,925	1,296	9.3	21.3	2.0
SpiceJet	FY2015	₹ cr	5,202	(748)	-	-	0.8
Ryanair*	FY2015	€ mn	5,654	867	15.3	20.6	3.2

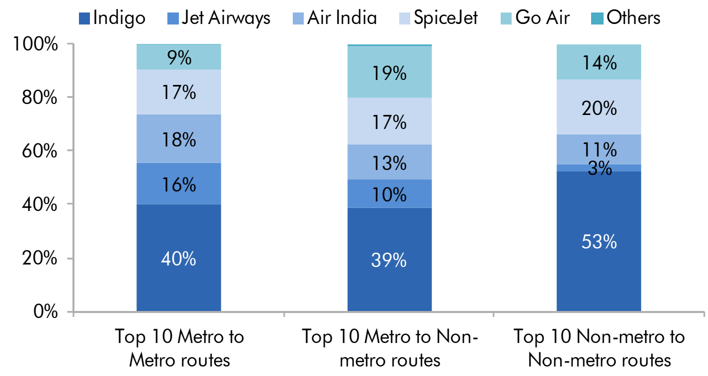
*Source: Company, Angel Research; Note: *Mcap based on post IPO O/s Shares at upper price band*

Exhibit 10: Market Share FY09-15



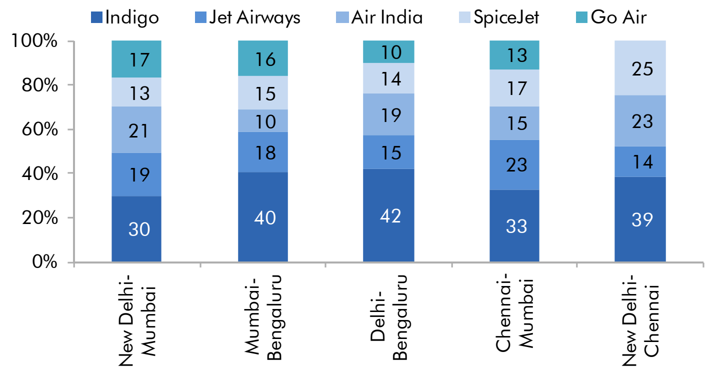
Source: Company

Exhibit 11: Segmental market share (top 10 routes–FY15)



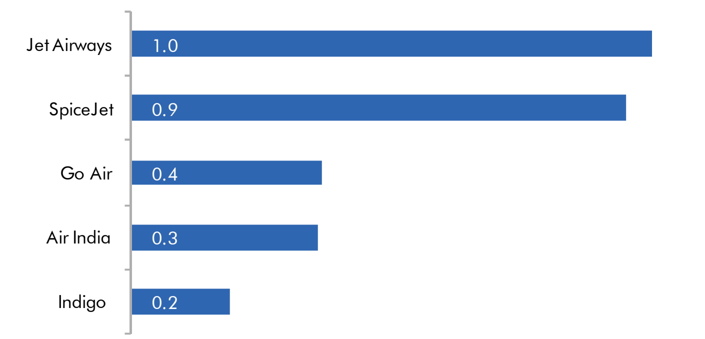
Source: Company

Exhibit 12: Market share (top 5 domestic - by traffic)



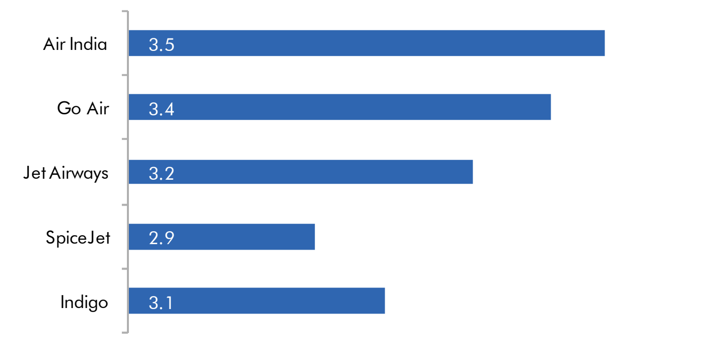
Source: Company

Exhibit 13: Maintenance Cost per ASK (US¢) (FY2014)



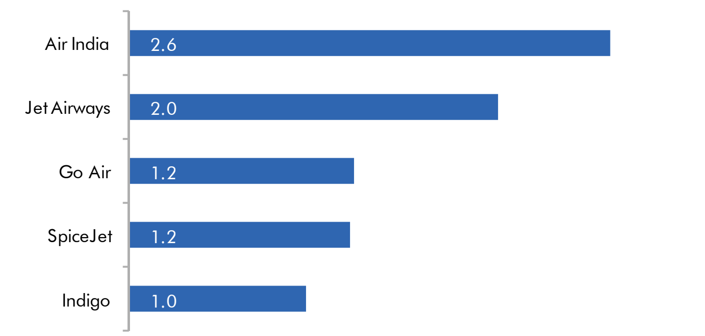
Source: Company; Note: ASK (Available Seat Kilometer)

Exhibit 14: Fuel Cost per ASK (US¢) (FY2014)



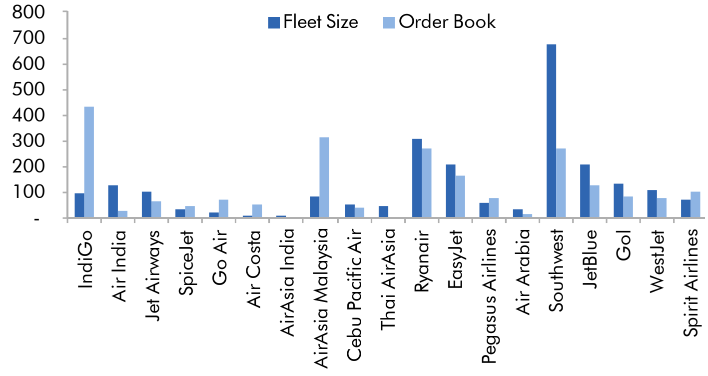
Source: Company; Note: ASK (Available Seat Kilometer)

Exhibit 15: Ownership Cost Per ASK (US¢) (FY2014)



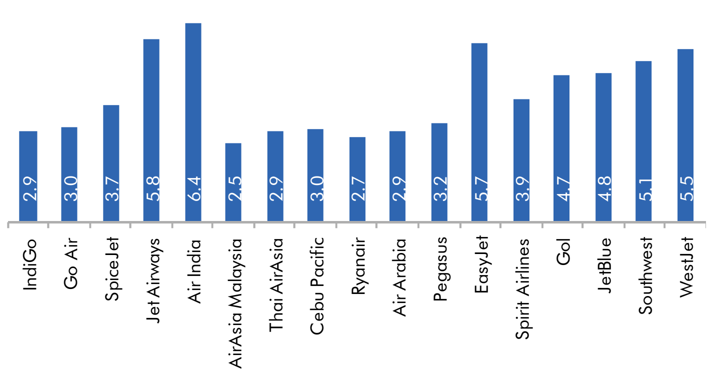
Source: Company; Note: ASK (Available Seat Kilometer)

Exhibit 16: Fleet Size and Order Book



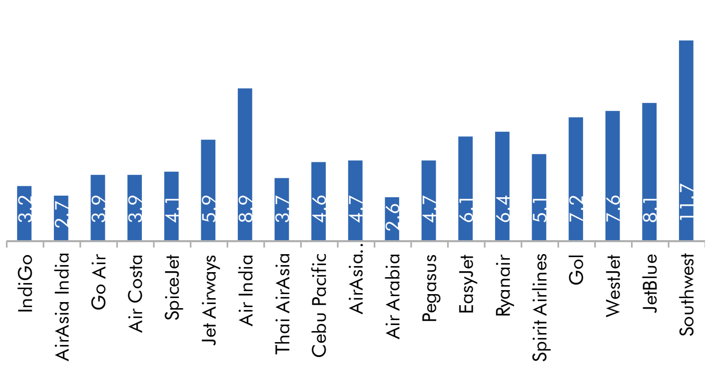
Source: Company

Exhibit 17: CASK (ex-fuel) (US¢)



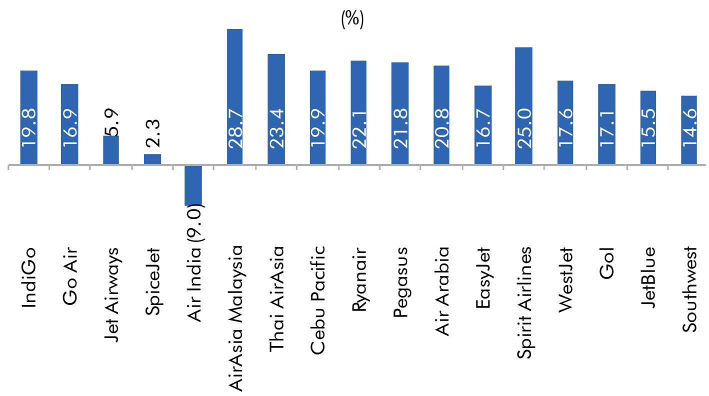
Source: Company; Note: CASK (Cost per Available Seat Kilometer)

Exhibit 18: Average Fleet Age (years)



Source: Company

Exhibit 19: EBITDAR margin



Source: Company

Profit & Loss Statement

Y/E March (₹ cr)	FY2012	FY2013	FY2014	FY2015	1QFY2016
Net Sales	**5,565**	**9,203**	**11,117**	**13,925**	**4,212**
% Chg	*45.2*	*65.4*	*20.8*	*25.3*	
Total expenditure	**5,516**	**8,309**	**10,610**	**12,056**	**3,239**
Aircraft and engine rentals (net)	801	1,356	1,670	1,952	602
Aircraft fuel expenses	2,874	4,313	5,513	5,748	1,348
Purchase of stock in trade	34	56	58	82	23
Employee benefits	512	690	921	1,189	383
Other expenses	1,296	1,896	2,447	3,088	884
EBITDA	**49**	**894**	**507**	**1,870**	**972**
EBIDTA %	***0.9***	***9.7***	***4.6***	***13.4***	***23.1***
Depreciation	67	86	226	302	120
EBIT	**(18)**	**808**	**281**	**1,567**	**852**
Interest and Financial Charges	51	58	123	116	33
Other Income	144	237	316	384	106
PBT	**75**	**987**	**474**	**1,836**	**925**
Tax	(66)	204	(1)	540	285
% of PBT	*(87.7)*	*20.7*	*(0.2)*	*29.4*	*30.8*
PAT before Exceptional item	141	783	474	1,296	640
Exceptional item	-	-	-	-	-
PAT	**141**	**783**	**474**	**1,296**	**640**
% Chg	*(75.7)*	*457.2*	*(39.4)*	*173.1*	
PAT %	*2.5*	*8.5*	*4.3*	*9.3*	*15.2*
***EPS (₹)**	**4.1**	**22.8**	**13.8**	**37.7**	**18.6**

*Note: *EPS calculation is based on Pre IPO outstanding shares*

Balance Sheet

Y/E March (₹ cr)	FY2012	FY2013	FY2014	FY2015	1QFY2016
Sources of Funds					
Equity Capital	31	31	31	34	344
Reserves Total	213	358	390	392	(483)
Networth	**243**	**389**	**421**	**426**	**(139)**
Total Debt	936	1,699	3,081	3,588	3,567
Other long term liabilities	279	723	1,296	2,017	2,198
Deferred Incentives	1,180	1,530	1,753	1,752	1,647
Long term provisions	16	23	37	52	55
Total Liabilities	**2,589**	**4,419**	**6,640**	**8,245**	**7,744**
Application of Funds					
Net Block	886	1,764	3,956	4,876	4,842
Capital WIP	-	7	-	0	1
LT Loans and Advances	297	525	801	1,124	1,154
Other non-current assets	89	486	1,432	1,606	1,510
Investments	523	1,138	1,272	517	0
Current Assets	**1,785**	**1,932**	**1,643**	**2,651**	**3,069**
Inventories	37	52	67	131	168
Sundry Debtors	39	69	89	105	117
Cash and Bank Balance	1,309	1,341	1,102	1,999	2,269
ST Loans and Advances	318	359	223	156	211
Other Current Asset	82	112	162	261	302
Current Liabilities	**992**	**1,434**	**2,464**	**2,529**	**2,831**
Net Current Assets	**793**	**498**	**(821)**	**122**	**238**
Total Assets	**2,589**	**4,419**	**6,640**	**8,245**	**7,744**

Cash flow statement

Y/E March (₹ cr)	FY2012	FY2013	FY2014	FY2015	1QFY2016
Profit before tax	75	987	474	1,836	925
Depreciation	67	86	226	302	120
Change in Working Capital	(265)	327	1,080	(45)	155
Less: Other income	(144)	(237)	(316)	(384)	(106)
Direct taxes paid	66	(204)	1	(540)	(285)
Cash Flow from Operations	**(201)**	**958**	**1,465**	**1,169**	**809**
(Inc)/ Dec in Fixed Assets	(55)	(885)	(2,185)	(921)	33
(Inc)/ Dec in Investments	(1,326)	(1,662)	(2,410)	(1,788)	(517)
Other income	144	237	316	384	106
Cash Flow from Investing	**(1,484)**	**(2,935)**	**(5,501)**	**(2,822)**	**(312)**
Issue/(Buy Back) of Equity	-	-	-	0	309
Inc./(Dec.) in loans	255	1,214	1,968	1,244	162
Dividend Paid (Incl. Tax)	-	(638)	(442)	(1,291)	(1,207)
Others	1,963	1,431	2,271	2,597	509
Cash Flow from Financing	**2,218**	**2,008**	**3,797**	**2,550**	**(227)**
Inc./(Dec.) in Cash	533	32	(239)	898	270
Opening Cash balances	**776**	**1,309**	**1,341**	**1,102**	**1,999**
Closing Cash balances	**1,309**	**1,341**	**1,102**	**1,999**	**2,269**

Key Ratios

Y/E March	FY2012	FY2013	FY2014	FY2015
Valuation Ratio (x)				
P/E (on FDEPS)	187.0	33.6	55.4	20.3
P/CEPS	127.0	30.3	37.5	16.5
Per Share Data (₹)				
EPS (Basic)	4.1	22.8	13.8	37.7
EPS (fully diluted)	4.1	22.8	13.8	37.7
Cash EPS	6.0	25.3	20.4	46.5
Returns (%)				
RoCE (Pre-tax)	-	38.70	8.01	39.04
Angel RoIC (Pre-tax)	-	109.1	11.7	77.8
RoE	57.8	201.4	112.8	304.0
Turnover ratios (x)				
Asset Turnover (Net Block) (x)	6.3	5.2	2.8	2.9
Inventory / Sales (days)	2	2	2	3
Receivables (days)	3	3	3	3
Payables (days)	66	63	85	77

*Note:*EPS calculation is based on Pre IPO outstanding share and valuation is computed at upper price band*

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