

Sector: Telecom
Results Update

	Change
Reco: Buy	↔
CMP: Rs. 553	
Price Target: Rs. 710	↑
↑ Upgrade ↔ No change ↓ Downgrade	

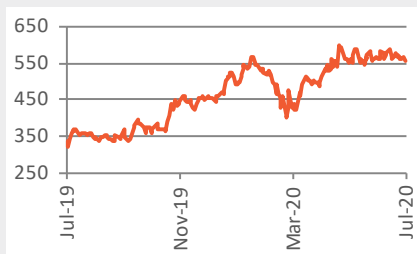
Company details

Market cap:	Rs. 301,611 cr
52-week high/low:	Rs. 611/321
NSE volume: (No of shares)	20.3 lakh
BSE code:	532454
NSE code:	BHARTIARTL
Sharekhan code:	BHARTIARTL
Free float: (No of shares)	191.4 cr

Shareholding (%)

Promoters	56.2
FII	22.3
DII	18.7
Others	2.8

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-1.2	7.5	12.8	63.7
Relative to Sensex	-11.0	-6.2	19.8	61.4

Sharekhan Research, Bloomberg

Bharti Airtel delivered in-line revenue and margin performance despite strict nationwide lockdown mandates, while net loss widened owing to incremental provision for the AGR dues. Further, the company positively surprised by reporting improvement in ARPU despite slower 4G subscriber additions, nil revenue from international segment, SIM consolidation at the bottom of the pyramid and increase in worker migration. Consolidated revenues increased by 0.9% q-o-q (up 15.4% y-o-y) to Rs. 23,939 crore, in-line with our estimates. India wireless/Africa businesses revenue declined 0.6% each on q-o-q basis, but they grew 18.5%/16.4% y-o-y respectively. EBITDA margin improved ~63BPS q-o-q to 43.5%, in-line with our estimates, led by 134 bps q-o-q improvement in India wireless business margin. Reported net loss was widened to Rs. 15,933 crore, owing to Rs. 11,746 crore of exceptional loss due to one-time incremental provisioning for AGR dues. Though the overall data was up by 12%/73% q-o-q/y-o-y, the pace of 4G subscriber addition was impacted owing to lower shipment of smartphones. We believe ARPU would continue to improve on the back of continued up-gradation from 2G to 4G, increasing post-paid subscribers and segmentation price hike for the premium users. Further, the focus on differentiation strategy on (1) better customer experience, (2) unique businesses and solutions (payment bank services bundled into telecom and Airtel platinum) and (3) digital platform (help to retain quality customers and strip out waste from the business) would help to improve wallet share from subscribers.

Key positives

- ARPU improved to Rs. 157 despite nil international revenues & SIM consolidation.
- Data traction remained strong with data traffic up 12%/73% q-o-q/y-o-y
- Capex moderated (down 65% q-o-q) on expected lines

Key negatives

- Lost 3.8 million mobile subscribers during the quarter
- Africa business remained weak on q-o-q basis

Our Call

Valuation – Maintain Buy with a revised PT of Rs. 710: We have raised our earnings estimates for FY2021E/FY2022E as ARPU continued to improve and strong commentary around monetization of digital assets and recovery in broadband segment. Further, the company has provisioned incremental Rs. 107 billion towards AGR with total provision of Rs. 470 billion+ which should cover the total demand of AGR dues by DOT (including interest charges). Further, the recent series of fund-raising in the last one year and potential asset sale alleviates concerns on liquidity. Though the next hearing by Supreme Court on the AGR case is scheduled on August 10, we believe that staggered payments would be allowed for the telcos. We remain positive on Bharti, considering its steady EBITDA performance in a tough environment, scope for growth in the number of 4G subscribers and improving free cash flows. Further, the valuation of Reliance Jio (~15x of 1 year forward EV/EBITDA) from recent deals indicate significant premium to Bharti Airtel FY2022 EV/EBITDA of 7.5x. Hence, we maintain our Buy rating on the stock with a revised price target (PT) of Rs. 710.

Key Risks

Increasing competition could keep up the pressure on realisations. Any slowdown in data volume growth could affect revenue growth. AGR dues, if levied fully, could be a huge stress on the balance sheet.

Valuation	Rs cr				
Particulars	FY18	FY19	FY20	FY21E	FY22E
Revenue	82,638.8	80,780.2	87,539.0	100,876.9	112,864.2
OPM (%)	36.4	32.0	41.7	46.7	49.8
Adjusted PAT	1,099.0	-3,977.8	-3,630.4	3,032.6	7,581.6
% YoY growth	-77.9	NM	NM	NM	150.0
Adjusted EPS (Rs.)	2.7	-10.0	-7.0	5.9	14.8
P/E (x)	201.2	NM	NM	93.6	37.4
P/B (x)	4.3	4.2	3.9	4.7	4.2
EV/EBITDA (x)	13.3	16.0	10.7	9.0	7.5
RoNW (%)	1.4	-4.9	-4.7	-16.3	10.5
RoCE (%)	6.1	2.4	4.5	8.8	12.0

Source: Company; Sharekhan estimates

Another strong quarter: Bharti Airtel delivered in-line revenue and margin performance despite strict nationwide lockdown mandates, while net loss widened owing to incremental provision for the AGR dues. However, the company surprised us with reporting an improvement in ARPU despite nationwide lockdown mandates, weak international revenue and a slowdown in economy. Consolidated revenues increased by 0.9% q-o-q (up 15.4% y-o-y) to Rs. 23,939 crore, in-line with our estimates, led by 0.9% q-o-q (up 14.6% y-o-y) growth in India business. India wireless/Africa businesses revenue declined 0.6% each on q-o-q basis, but they grew 18.5%/16.4% y-o-y respectively. ARPU grew 1.8% q-o-q (up 21.3% y-o-y) to Rs. 157 from the elevated base of last quarter, whereas number of subscribers in India wireless business declined by 3.8 million (down 1.3% q-o-q) during the quarter. EBITDA margin improved ~63BPS q-o-q to 43.5%, in-line with our estimates, resulting in 2.4%/26.4% q-o-q/y-o-y growth in EBITDA. Reported net loss was widened to Rs. 15,933 crore during the quarter, owing to Rs. 11,746 crore of exceptional loss due to incremental provision and interest on license fee and spectrum usage charges of Rs. 10,744 crore and tax exceptional also for the prior years. Excluding exceptional items from Q1FY2021, adjusted net loss during the quarter stood at Rs. 544 crore.

ARPU likely to improve further, focus on digitization: The management reiterated its earlier stance that ARPU should improve to Rs. 200 in the short term from the current level of Rs. 157 and thereafter it should improve to Rs. 300 in the long term for profitable growth as well as RoCE of over 15% for its business. The improvement in ARPU would be supported by continued up-gradation from 2G to 4G, increasing post-paid subscribers and segmentation price hike for the premium users. We believe the bundling of home broadband, DTH and wireless services under one-bill initiative would help the company to improve its ARPU going forward. Further, management highlighted that its differentiation in service offerings to customers is critical for its growth. It has been focusing differentiation strategy in three areas such as (1) customer experience, (2) unique businesses and solutions – launched two services during this quarter (i) payment bank services bundled into telecom (cash back, interest to bank account, insurance, etc) and (ii) Airtel platinum (reward services to customers who are in higher band) and (3) digital platform (retain quality customers and strip out waste from the business) – strength remains in (i) data, (ii) distribution, (iii) payment and (iv) network. Higher digitisation would enable the company to increase monetisation from its digital assets and value-added services, reduce churn rate across verticals and improve wallet share from subscribers.

Key result highlights from Concall

- ◆ **COVID impact in Q1FY2021:** Due to the COVID-19 led lockdown, supply chain was disrupted during the quarter, leading to a sharp drop in smartphone shipments. This in-turn impacted 2G to 4G upgrade. Further, offline channel partners were closed including its own retail stores which restricted people ability to recharge conveniently. The pace of network deployment was also slowed down. The company has been managing its network remotely, activating new channels accelerating digital channels. These steps help the company to offset some challenges during the lockdown. Management expects business to recover in Q2FY2021 as smartphone shipments are back to pre-COVID level and most of its stores are open now.
- ◆ **India wireless business reported better-than-expected performance:** India wireless business revenue remained flat (down 0.6% q-o-q) sequentially despite a challenging environment (weak international revenue, SIM consolidation at the bottom end of pyramid and increase in worker migration), while it increased 18.5% y-o-y to Rs. 12,877 crore. However, ARPU surprised positively with an increase of 1.8% q-o-q and 21.3% y-o-y to Rs. 157 during the quarter. Note that number of subscribers declined by 3.8 million during the quarter. EBITDA margin of India wireless business improved by 134 bps q-o-q to 40.6%, while the EBIT increased 6x q-o-q.
- ◆ **Healthy India wireless operating metrics:** Net addition of subscribers during the quarter was impacted due to the nationwide lockdown and unavailability of retail stores for recharge. However, data subscribers increased by 0.5 million at 149 million, an increase of 0.3% q-o-q and 24% y-o-y. The number of 4G subscribers increased by around 1.9 million to 138.3 million, a growth of 1.5% q-o-q and 45% y-o-y. The management highlighted that 4G customer additions were impacted owing to lower shipment of smartphones. Overall data was up by 12%/73% q-o-q/y-o-y, while usage per customer increased by 115/40% q-o-q/y-o-y to 16.7 GB per subscriber due to work-from-home modes. A strong growth (up 11% y-o-y) in voice traffic to 820 billion minutes.

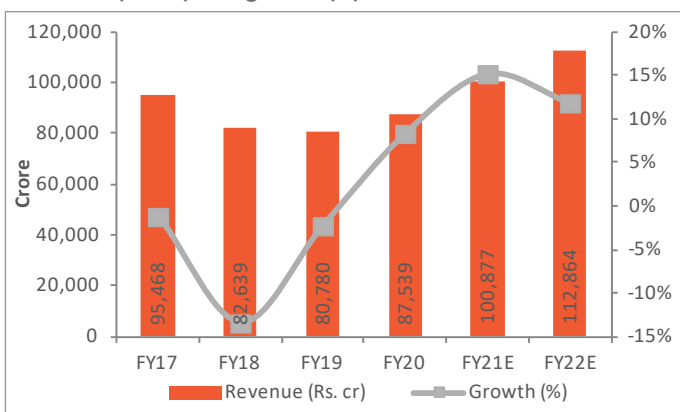
- ◆ **Growth momentum to continue in home broadband:** Home broadband revenue grew 1.1% q-o-q, led by an increase in demand during the lockdown restrictions across the country. The growth was driven by 1.4% q-o-q growth in subscriber additions, while ARPU growth remained flat on a q-o-q basis during the quarter. The home broadband business continues to remain resilient and shows significant long term promise in the wake of the new normal of work from home and social distancing established post COVID-19. Management sees high traction for its broadband offering. Hence, the company has accelerated installations and rollouts to capitalize demand. However, the growth was impacted to some extent due to temporary closure of small offices and shops which chose to turn off service during the lockdown. The management believes these would be restored in the coming months. The company has tied up with local operators to provide last mile connectivity in 11 cities.
- ◆ **Enterprise segment growth accelerated:** The enterprise business delivered 3.7% q-o-q revenue growth, while EBITDA margin contracted 359 bps q-o-q to 36.3%. EBITDA declined 5.6% q-o-q. The company helped the customers to reduce disruption during the challenging times through its products and platforms. The company launched video conferencing solution in partnership during the quarter.
- ◆ **Digital revenue is considered to be the heart of the business:** In recent times, digital revenue is considered the heart of the business as it complements the core business and helps in enhancing the overall business and profitability by i) significant new customer additions, ii) retaining customers for a longer duration and iii) improving the efficiency resulting in lower opex. The company has set-up a large digital team of 1500 employees. It has also been focusing on scaling its digital assets that would help in (1) advertisement revenue, (2) commissions from partnership and (3) monetizing its own products that the company is working on.
- ◆ **Airtel Platform provides synergies to maximise revenue and profitability:** The company's Airtel Platform helps it in gaining traction for the following i) increases data consumption, ii) provides access to 277 million individual users, 80 million homes and 2,000 corporates to cross-sell products and services, iii) enhances digital payments in a significant manner and iv) Network and location based services.
- ◆ **Further improvement in ARPU likely:** The management expects ARPU to increase at a healthy pace to Rs 200 and thereafter to Rs 300 in the long-term. This is likely as growth in postpaid users is expected to be healthy owing to differential between the prepaid and postpaid tariff being narrowed down considerably.
- ◆ **Capex moderated along the expected lines:** Total capex during the quarter moderated to Rs 3,975 crore from Rs. 11,339 crore from Q4FY2020, owing to strict lockdown measures which restricted the network deployment works. Capex is expected to go up as ARPU improves to provide better customer experience to the subscribers.
- ◆ **Fund raising helps the company to maintain liquidity position:** Improved operational performance coupled with multiple fund raising i) \$2 billion through QIP, ii) \$1 billion through FCCB and iii) \$250 million through perpetual bonds (tap on existing bonds), (iv) \$750 million from Africa unit and (v) \$235 million from Carlyle from 25% stake sale in its data centre, helped the net debt/ EBITDA ratio improve to 2.74x as on June 30, 2020 as compared to 2.88x in Q4FY2020. Net debt decreased to \$15.4 billion from \$16.3 billion in Q4FY2020. Management indicated that the company has raised around Rs. 60,000 crore from equity infusion.
- ◆ **Provided final provision of RS. 10,744 crore for AGR:** On July 20, 2020, Supreme Court had made it clear that there can be no scope of re-assessment or recalculation of AGR dues. Hence, the company provided an incremental provision of Rs. 107 billion (including net interest on total provision created considering interest rate as per the affidavit filed by DoT) towards AGR during the quarter, with total provision of around Rs. 475 billion. However, the hearing in Supreme Court on the AGR matter is scheduled to happen on August 10 2020.

Results

Particulars	Q1FY21	Q1FY20	y-o-y (%)	Q4FY20	q-o-q (%)
Net sales	23,938.7	20,737.9	15.4	23,722.7	0.9
License fees and spectrum charges	2,076.8	1,839.1	12.9	2,057.0	1.0
Employee expenses	1,156.6	864.1	33.9	1,031.6	12.1
Access and interconnection charges	2,801.1	2,562.7	9.3	2,827.0	-0.9
Network operating expenses	5,103.6	4,663.6	9.4	5,201.5	-1.9
Other expenses	1,662.6	1,735.7	-4.2	1,504.9	10.5
Operating profit	10,407.9	8,234.1	26.4	10,165.2	2.4
Interest expenses	3,456.2	3,392.8	1.9	4,130.2	-16.3
Depreciation	7,226.8	6,758.7	6.9	7,055.0	2.4
Tax	3,817.5	-607.0	-	-2,033.5	-
Reported net income	-15,933.1	-2,866.0	-	-5,237.0	-
Adjusted net income	-544.3	-1,396.6	-	-471.0	-
EPS (Rs.)	-1.1	-2.7	-	-0.9	-
Margins (%)			bps		bps
OPM	43.5	39.7	377	42.8	63
NPM (adjusted)	-2.3	-6.7	446	-2.0	-29

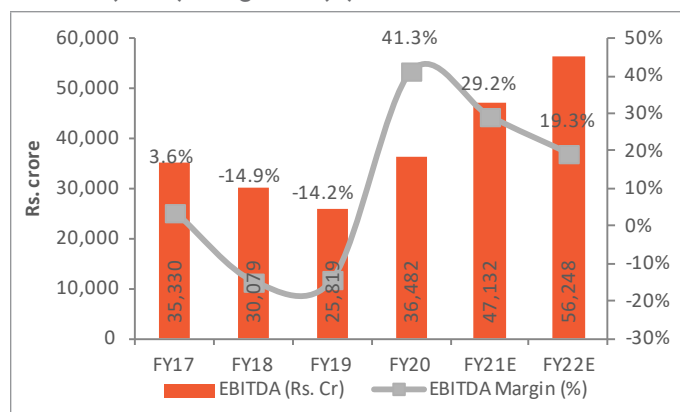
Source: Company; Sharekhan Research

Revenue (Rs. cr) and growth (%)



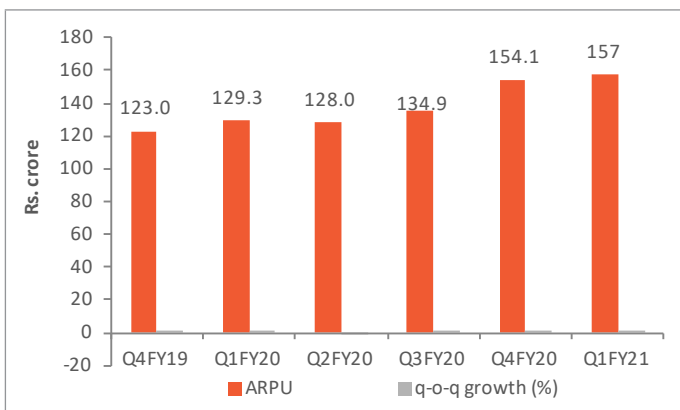
Source: Company, Sharekhan Research

EBITDA (Rs. cr) and growth (%)



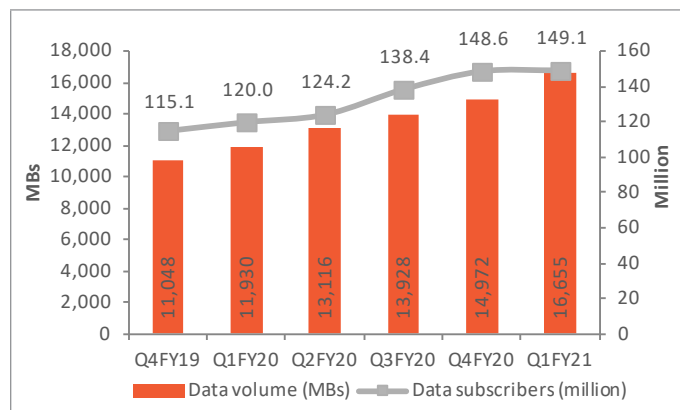
Source: Company, Sharekhan Research

ARPU continued to grow



Source: Company, Sharekhan Research

Strong traction for data



Source: Company, Sharekhan Research

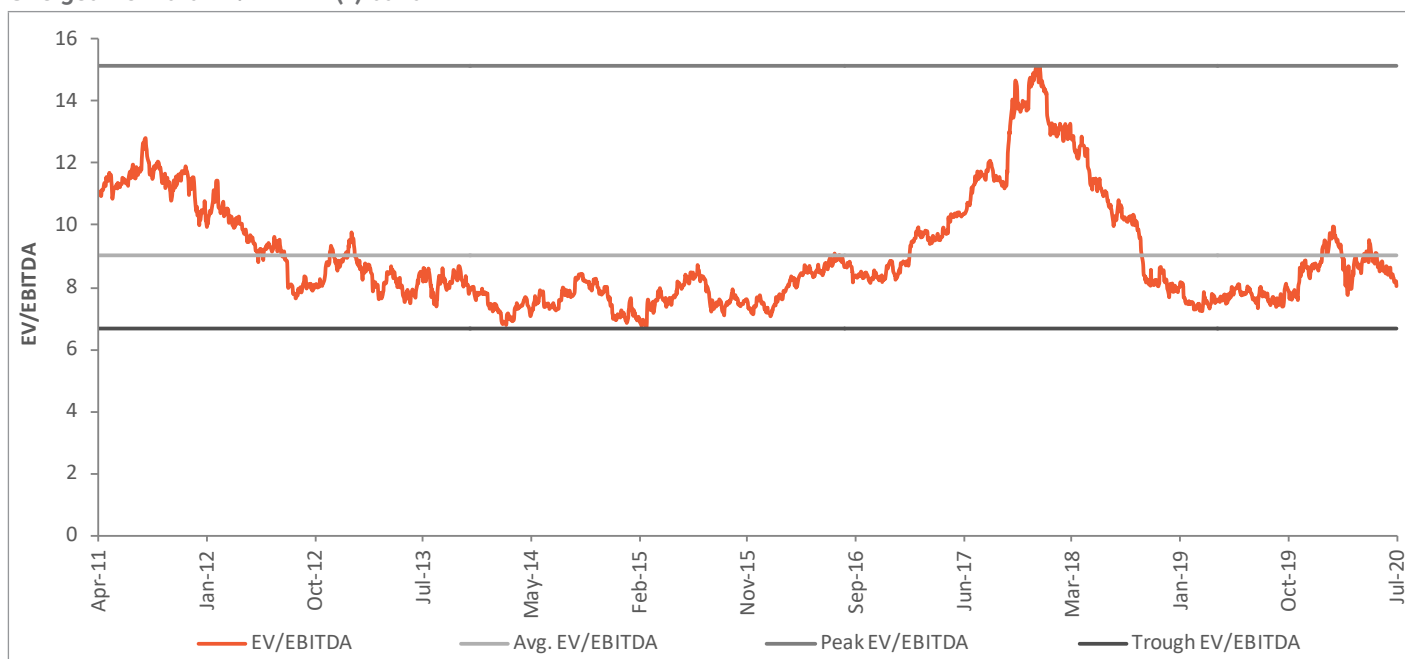
Outlook

Though Bharti Airtel will be able to withstand competition now, we believe that the company's capex intensity will improve in its wireless business and investments in contents to create differentiation in the market. We believe Bharti's free cash flow is set to improve going ahead with the increase of ARPU and better cost management. Higher digitisation would enable the company increase monetisation of digital assets and value-added services, a reduced churn rate across verticals and improved wallet share from subscribers. With a comparatively a strong balance sheet and adequate network investments, Bharti is well-placed to capitalise on opportunities of a recovery in the industry.

Valuation

Maintain Buy with a revised PT of Rs. 710: We have raised our earnings estimates for FY2021E/FY2022E as ARPU continued to improve and strong commentary around monetization of digital assets and recovery in broadband segment. Further, the company has provisioned incremental Rs. 107 billion towards AGR with total provision of Rs. 470 billion+ which should cover the total demand of AGR dues by DOT (including interest charges). Further, the recent series of fund-raising in the last one year and potential asset sale alleviates the concerns on liquidity. Though the next hearing by Supreme Court on the AGR case is scheduled on August 10, we believe that staggered payments would be allowed for the telcos. We remain positive on Bharti, considering its steady EBITDA performance in a tough environment, scope for growth in the number of 4G subscribers and improving free cash flows. Further, the valuation of Reliance Jio (~15x of 1 year forward EV/EBITDA) from recent deals indicate significant premium to Bharti Airtel FY2022 EV/EBITDA of 7.5x. Hence, we maintain our Buy rating on the stock with a revised price target (PT) of Rs. 710.

One-year forward EV/EBITDA (x) band



Source: Sharekhan Research

About company

Established in 1995, Bharti Airtel is one of the leaders in the Indian mobile telephony space with operations in 18 countries across Asia and Africa. The company ranks among the top three mobile service providers globally in terms of subscribers. Airtel is a diversified telecom service provider offering wireless, mobile commerce, fixed line, home broadband, enterprise and DTH services. It expanded into Africa by acquiring Zain's Africa operations in 2010 and is present in 14 African markets. Bharti Airtel had over 420 million customers across its operations at the end of March 2020. It owns a 53.51% stake in Bharti Infratel, which in turn owns a 42% stake in Indus Towers.

Investment theme

Revenue accretion from the 4G upgrade, minimum-ARPU plans (rolled out across India) and recent tariff hike helped the company to report improvement in ARPU. Further, the government's data localisation policies with an increasing penetration of smartphones are likely to boost strong demand for data over medium-to-long term. Despite a predatory pricing strategy from new entrants since its commercial launch in September 2016, Bharti Airtel has been resilient in sustaining its revenue market share (RMS) as it has been drastically standardising its plans to retain customers and acquiring subscribers through M&A activities. In DTH, Bharti expects to maintain steady growth by adding new subscribers in rural areas by launching USB-enabled STBs, increasing reach in cities taking advantage of flat-screen TV upgrades and driving up ARPUs by selling OTT boxes and hybrid HD STBs. We believe the company is well-poised to deliver strong multi-year EBITDA growth phase given recent developments in the Indian wireless industry.

Key Risks

1) Increasing competition could pressurise realisations; and 2) Slower growth in data volumes could affect data revenue growth.

Additional Data

Key management personnel

Sunil Mittal	Chairman
Gopal Vittal	MD & CEO (India and South Asia)
Raghunath Mandava	CEO (Africa)
Badal Bagri	Chief Financial Officer
Pankaj Tewari	Company Secretary

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	GIC Pte Limited	3.55
2	ICICI Prudential Asset Management	2.80
3	SBI Funds Management Pvt Ltd	2.32
4	BlackRock Inc	1.60
5	Vanguard Group Inc/The	1.45
6	Capital Group Companies	1.39
7	Franklin India Equity	1.05
8	Aditya Birla Sun Life Asset Management	1.03
9	Franklin Resources Inc	0.99
10	ICICI Prudential Life Insurance Co	0.97

Source: Bloomberg

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