13 April 2023
Company Update | Sector: Telecom

Bharti Airtel

BSE SENSEX	S&P CNX
60,393	17,828

Bloomberg	BHARTI IN
Equity Shares (m)	5884
M.Cap.(INRb)/(USDb)	4427 / 54.1
52-Week Range (INR)	877 / 629
1, 6, 12 Rel. Per (%)	-4/-5/1
12M Avg Val (INR M)	5095
Free float (%)	44.9

Financials & Valuations

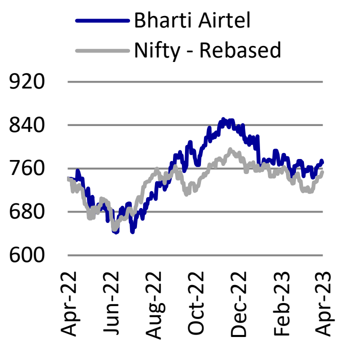
Y/E March	FY23E	FY24E	FY25E
Net Sales	1,399	1,567	1,718
EBITDA	716	817	916
Adj. PAT	76	101	158
EBITDA Margin (%)	51.2	52.1	53.3
Adj. EPS (INR)	13.6	18.1	28.2
EPS Gr. (%)	115	33	56
BV/Sh. (INR)	133	188	216
Ratios			
Net D:E	2.7	1.5	0.8
RoE (%)	10.8	11.3	14.0
RoCE (%)	9.6	9.3	10.8
Div. Payout (%)	0.0	0.0	0.0
Valuations			
EV/EBITDA (x)	9.0	7.3	6.2
P/E (x)	57.0	42.8	27.4
P/BV (x)	5.8	4.1	3.6
Div. Yield (%)	0.0	0.0	0.0

Shareholding pattern (%)

As On	Dec-22	Sep-22	Dec-21
Promoter	55.1	55.1	55.9
DII	19.2	18.9	19.5
FII	21.8	21.9	19.4
Others	4.0	4.1	5.2

FII Includes depository receipts

Stock Performance (1-year)



CMP: INR768 TP: INR950 (+24%) Buy

Soft landing ahead

Earnings pace cools off, capex heats up

Bharti has seen decent earnings growth for the last 12 quarters. However, we expect Bharti to witness 1) a period of soft earnings given low probability of a price hike, and 2) high capex over the next 2-3 years given increased investments in 5G and rural densification. These factors could keep the stock range-bound in the near term, though our long-term BUY view remains intact.

Low probability of near-term price hike may lead to soft earnings

Over the last three years (FY20-23E), Bharti reported a CAGR of 19%/34% in India Mobile revenue/EBITDA, driven by multiple tariff hikes (strong 40% increase in ARPU), a shift from 2G to 4G subscribers, and SUC (spectrum usage charge) savings leading a signification FCF generation. Going forward, we see low probability of a tariff hike in the near term and heightened competition for market share among telcos, which may increase churn and drive SIM consolidation. As a result, we factor in India Mobile revenue/EBITDA growth of 11%/43% over FY23-25E v/s 19%/34% growth over FY20-23E.

Frontloading of 5G and rural capex

Bharti has guided for India Mobile capex of INR750b for the next three years, as it aims to roll out 5G across urban areas by Mar'24 and ramp up rural densification. But, with INR310b capex in FY23 and INR360b in FY24 (based on FY23 exit run rate), we believe Bharti will significantly exceed its INR750b capex target. A new technology upgrade cycle has just started, and historically capex intensity has always stepped up with the launch of new technology upgrade, with continued heavy investments over the next 4-5 years. This was also evident during the 4G rollout when Bharti's annual India Mobile capex increased to INR200b from INR150b. The current low-teens 5G device penetration may accelerate in the next couple of years as the 5G ecosystem develops, requiring deployment of additional spectrum bands (only 3500Mhz now), standalone 5G architecture and VO5G calling which may require heavy investments.

Near-term deleveraging could be limited

Bharti's operational performance has been strong for the past few years, driving healthy FCF generation. However, investments in 5G auction, along with AGR liabilities, have led to limited deleveraging. Going forward, soft earnings growth (low probability of near-term tariff hike) and heavy capex may reduce FCF generation. Bharti's cumulative OCF/FCF of INR1.4t/INR700b for the next two years and inflows from the ~INR210b rights issue could help it reduce debt. Gross/net debt (including lease liability) currently stand at INR2.3t/INR2.1t, which we expect to decline to INR2.0t/INR1.5t in FY25.

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Longer-term growth story intact

While near-term earnings growth may remain soft, we believe Bharti and RJio should be the key beneficiaries of the structural change in the telecom sector. Unlike 3G/4G investment cycles when high capex was accompanied by heightened competition, which led to limited monetization opportunities, the current market situation is far superior. Both RJio and Bharti should benefit from VIL's dwindling market share as the latter seeks a large capital raise to upgrade its network. Further, in the long term, there should be opportunities to monetize heavy investments as the Indian telecom market size of INR2.2t is largely catered by merely two sizeable players – RJio and Bharti, with far lower competitive intensity.

Valuation - High capex should overplay on valuations

The stock is trading at 6x on consolidated FY25E EV/EBITDA, with the India business trading at 9x and Africa at 3x. We have factored in 13% consol. EBITDA growth over FY23-25E (without factoring in tariff hike) with a 3-5% FCF yield. Given the softness in profitability and increased capex, the FCF generation and deleveraging pace should moderate in the near term. As a result, the stock could remain range-bound in the short term. However, the improving monetization opportunity may offset high capital intensity, driving better earnings and FCF generation in the next two years. We derive our SOTP-based TP of INR950 based on FY25E EV/EBITDA of 10x for the India Mobile business and 5x for the Africa business.

Exhibit 1: Bharti's FY25E-based SOTP

	EBITDA (INR b)	Ownership (%)	Proportionate EBITDA (INR b)	EV/EBITDA	Fair Value (INR b)	Value/ Share
India SA business (excl. towers)	650	100.0	650	10	6,653	1131
Tower business (20% discount to fair value)		48.0			155	26
Africa business	266	55.2	147	5	660	112
Less: net debt					1,875	319
Total Value					5,593	950
Shares o/s (b)	5.9					
CMP						768
Upside (%)						24

Source: MOFSL, Company

Earnings likely to soften after strong growth in last 12 quarters

Bharti's India business has reported a 19% CAGR growth for the last three years, driven by a tariff hike (organic and inorganic), subscriber gains from VIL and 4G mix improvement. Going forward, FY24 revenue is expected to be moderate given a low probability of a price hike in the near term. In Jan'23, Bharti increased the price of its 2G base plan to INR155 from of INR99, which VIL and RJio have not followed. This makes it difficult for Bharti to take a subsequent price hike in unlimited data plans in the near term, which may result in soft earnings growth.

We anticipate an 8% CAGR in ARPU over the next two years, led by 1) subscribers upgrading from 2G to 4G, b) upgrade from prepaid to postpaid subscribers, and c) data monetization through higher plans. We expect a modest 3% CAGR in subscriber additions, owing to a slower market share shift from VIL, resulting in an 11% CAGR in overall India revenue.

The decrease in SUC served as a tailwind for EBITDA growth is not fully factored in the base. Incremental EBITDA margin has been ~60-70% over the last few years with healthy revenue growth, but with softening revenue growth over FY23–25, EBITDA too may see a moderate 14% CAGR.

Home broadband, digital and other segments growing but have limited levers

We expect that, excluding Bharti's India division, the revenue and EBITDA CAGR for the next two years will be 10%, aided by the following factors:

- Revenue from the **enterprise business** accounts for ~13% of consolidated revenue. The segment witnessed a 12% CAGR between FY20 and FY23. For the next two years, we expect the enterprise segment to see a CAGR of 9-10%.
- **Home services**: With 5.7m subscribers, Bharti has an 18% market share. For the next two years, the Home segment is expected to see a CAGR of 14-15% (3% contribution of consol revenue). Bharti is expanding its Home service business through two models: 1) Own capex, and 2) LCO model. LCO is an asset-light model with efficient RoCE where Bharti ties up with local cable operators. The decrease in ARPU in Home services from INR840 in FY19 to INR643 in FY23 was due to the blended mix of both the models where the tilt is more toward LCO.
- **Digital TV services:** It contributes only 2% of consolidated revenue. We expect 7-9% revenue growth in the Digital segment for the next two years.

Frontloading of 5G and rural densification to lead to high capex

We expect that the aggressive 5G expansion and rural densification will drive substantial capex in FY24. The company has guided for capex of INR750b over FY23-25 for the India business. This will be frontloaded as the company plans to deploy 5G throughout urban areas by Mar'24 and densify rural areas using fiber and towers by 2QFY24. Accordingly, in FY23, we expect the company to incur INR310b capex. Assuming the current quarterly run rate to continue, Bharti may incur INR360b in capex in FY24. Hence, we expect the company to significantly exceed its INR750b capex target for FY23-25.

4G – project spring saw similar increase

Historically, capex intensity has always increased with the launch of new technology upgrades. During the 4G rollout, the company had launched project spring in FY16 to ramp up 4G coverage over a three-year period with INR600b (i.e. INR200b annually) v/s INR150b annual capex. This capex run rate remained high even after the three-year rollout as 4G deployment continued.

Using 3500Mhz capacity spectrum

Both Bharti and RJio are deploying 3500MHz spectrum for downlink, which requires new radios. Given that 5G is offered as a high-speed network, 3500MHz will be the primary band as it has huge capacity and could offer true 5G speed. RJio is also deploying 700MHz (acquired recently in 5G auction) possibly for uplinking, which could improve its 5G coverage across the network. Currently, only 12-13% of handsets support 5G. Overtime, as 5G gathers steam, Airtel may also deploy lower band/sub- Ghz spectrum in 900MHz, 1800Mhz, etc. as it did in 4G.

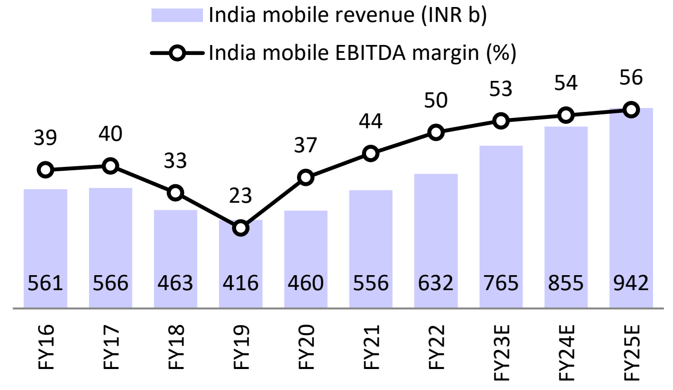
SA v/s NSA - investments

RJio is building a new core to develop 5G separately on a standalone network, whereas Bharti is using the existing 4G core (back-end network) to expand 5G access coverage. This has its positives and negatives. The key positive factor is that it can offer 5G by utilizing the existing 4G core network, offering seamless network without incurring heavy capex to build a fresh 5G core. But the standalone network offers true 5G with a completely advanced network. This may limit its investment in the near term but over time as the 5G ecosystem develops, it may switch to a standalone network with a fresh 5G core.

Rural capex

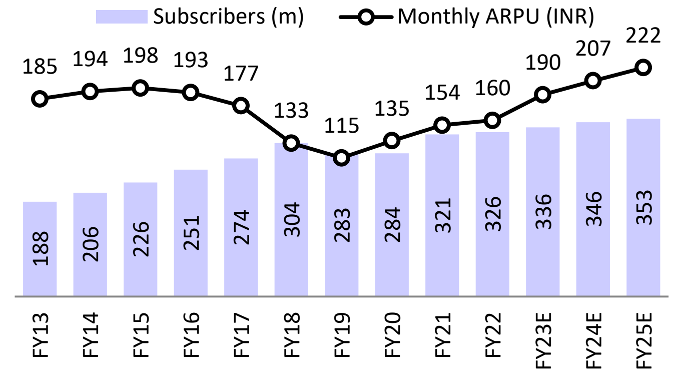
In the past, rural areas mostly used network for incoming calls and with elimination of IUC charges, the ROI of such sites were insignificant. Now with the ramp-up of 4G devices and social media, many rural consumers have been accessing data, thus creating a healthy revenue opportunity. In order to tap these customers, Bharti has been aggressively adding sites in rural areas. The overall number of unique sites, primarily those added in rural areas, is now 263k, up from 190k in FY20. Out of the 60k villages, Bharti has shortlisted 40k villages for rural coverage, which will receive investment due to their favorable ROEs. By 2QFY24, Bharti plans to densify rural areas, which might frontload capex in FY24, post which capex may decline.

Exhibit 2: India Mobile business to see 11%/14% revenue/ EBITDA CAGR over FY23-25



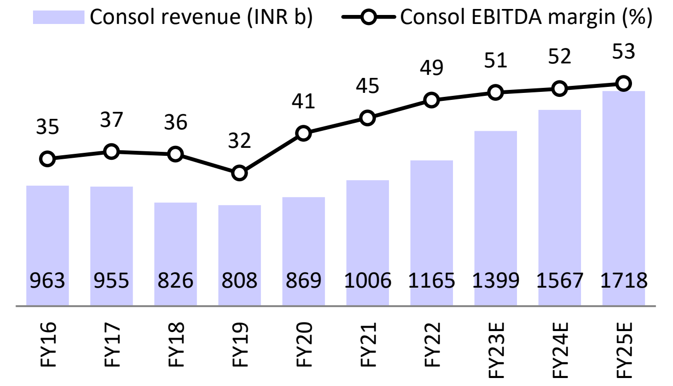
Source: MOFSL, Company

Exhibit 3: ARPU/Subs expected to post 8%/3% CAGR over FY23-25



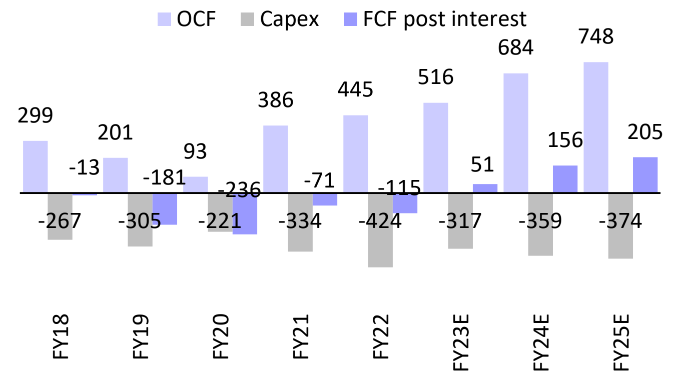
Source: MOFSL, Company

Exhibit 4: Consolidated business to see 11%/13% revenue/ EBITDA CAGR over FY23-25



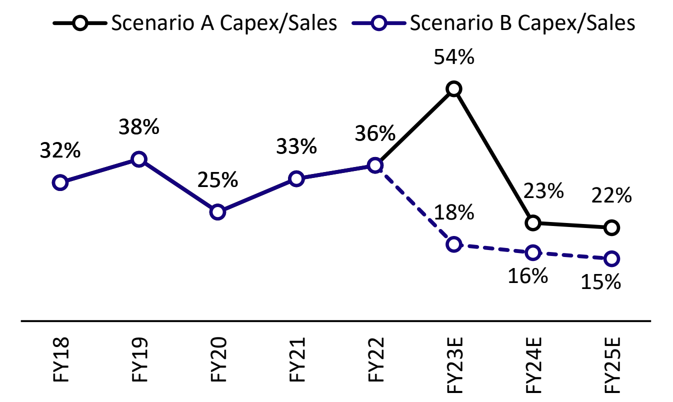
Source: MOFSL, Company

Exhibit 5: Expect limited FCF generation (Pre-Ind AS) (INR b)



Source: MOFSL, Company

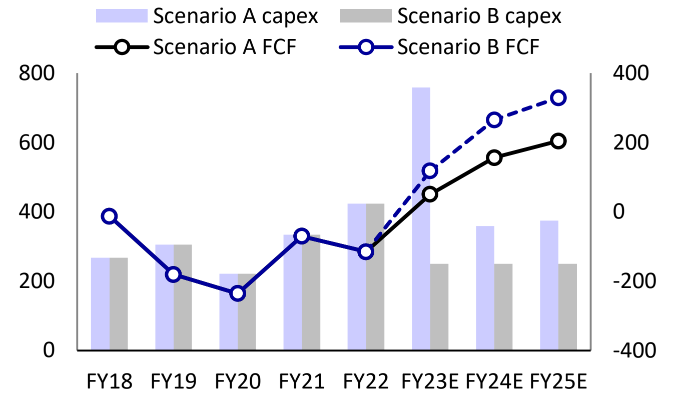
Exhibit 6: Comparatively capex trend remains higher…



Scenario A is the case where the capex is ~INR400b, and
Scenario B is the hypothetical situation with capex runrate of INR250b

Source: MOFSL, Company

Exhibit 7: … due to which FCF generation is low (INR b)



Scenario A is the case where the capex is ~INR400b, and
Scenario B is the hypothetical situation with capex runrate of INR250b

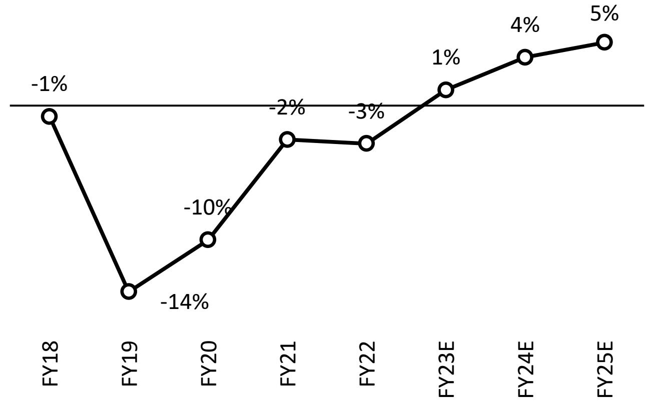
Source: MOFSL, Company

Exhibit 8: Expect INR570b cash inflow in next two years

INR b	FY24E	FY25E	Cumulative
EBITDA	817	916	1,733
less: Tax	-55	-79	-133
less: Pre Ind AS and WC adjustments	-78	-89	-167
less: Capex	-359	-374	-733
FCFF	326	374	699
less: Interest	-169	-169	-338
FCF post interest	**156**	**205**	**361**
add: Right issue	208	0	208
Cash generation	**365**	**205**	**569**

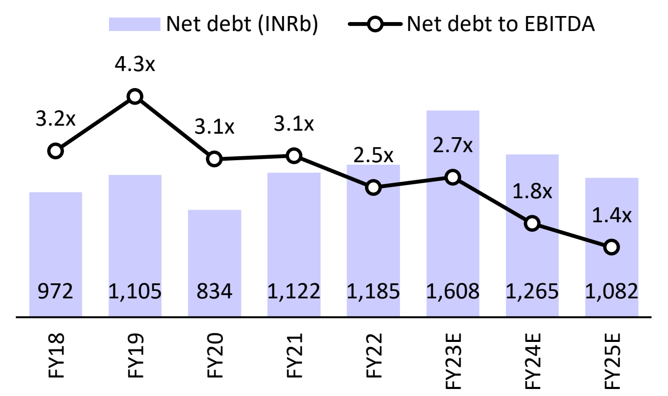
Source: MOFSL, Company

Exhibit 9: FCF yield expected to improve



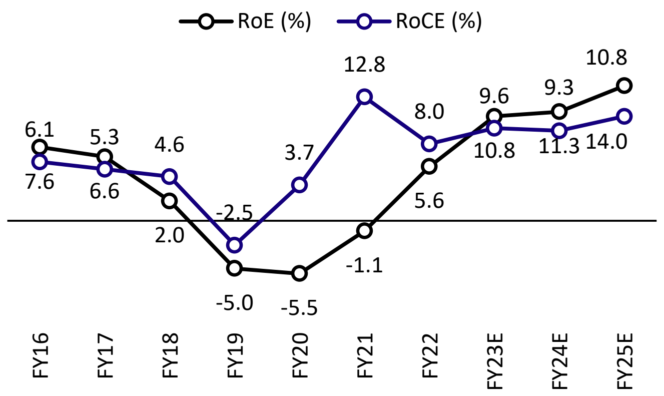
Source: MOFSL, Company

Exhibit 10: Net debt/EBITDA (pre-IndAS) expected to decline



Source: MOFSL, Company

Exhibit 11: Capital ratios expected to improve



Source: MOFSL, Company

Financials and valuation

Consolidated - Income Statement (INR b)

Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
Total Income from Operations	**955**	**826**	**808**	**869**	**1,006**	**1,165**	**1,399**	**1,567**	**1,718**
Change (%)	-1.1	-13.4	-2.2	7.6	15.7	15.8	20.0	12.0	9.6
Total Expenditure	**601**	**526**	**550**	**509**	**552**	**590**	**683**	**750**	**802**
% of Sales	63.0	63.6	68.1	58.6	54.9	50.6	48.8	47.9	46.7
EBITDA	**353**	**301**	**258**	**360**	**454**	**575**	**716**	**817**	**916**
Margin (%)	37.0	36.4	31.9	41.4	45.1	49.4	51.2	52.1	53.3
Depreciation	198	192	213	276	294	331	366	419	454
EBIT	**156**	**108**	**44**	**85**	**160**	**244**	**350**	**398**	**462**
Int. and Finance Charges	77	81	96	135	151	166	188	207	205
Other Income	10	13	5	16	6	30	10	4	25
PBT bef. EO Exp.	**89**	**41**	**-47**	**-34**	**14**	**108**	**171**	**195**	**281**
EO Items	-12	-8	29	-402	-159	17	-7	0	0
PBT after EO Exp.	**77**	**33**	**-17**	**-437**	**-145**	**125**	**165**	**195**	**281**
Total Tax	35	11	-34	-123	89	42	47	55	79
Tax Rate (%)	45.1	33.2	197.4	28.2	-61.7	33.5	28.5	28.0	28.0
Profit from discontinued operations	0.0	0.0	0.0	7.1	110.6	0.0	0.0	0.0	0.0
Minority Interest	4	11	13	15	27	41	44	39	45
Reported PAT	**38**	**11**	**4**	**-322**	**-151**	**43**	**74**	**101**	**158**
Adjusted PAT	**44**	**14**	**-35**	**-41**	**-7**	**35**	**76**	**101**	**158**
Change (%)	-9.5	-68.6	-350.3	16.6	-82.3	-590.2	115.5	33.1	56.0
Margin (%)	4.7	1.7	-4.3	-4.7	-0.7	3.0	5.4	6.5	9.2
Adj EPS	**11.1**	**3.49**	**-8.74**	**-7.47**	**-1.31**	**6.31**	**13.60**	**18.10**	**28.24**

Consolidated - Balance Sheet (INR b)

Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
Equity Share Capital	20	20	20	27	27	28	29	29	29
Total Reserves	655	675	694	744	562	638	711	1,021	1,179
Net Worth	**675**	**695**	**714**	**771**	**590**	**666**	**741**	**1,050**	**1,208**
Minority Interest	69	88	135	250	223	254	298	337	382
Total Loans	1,073	1,113	1,254	1,176	1,628	1,697	2,261	2,161	2,060
Lease liabilities	0	0	0	306	0	0	0	0	0
Deferred Tax Liabilities	-17	-22	-83	-263	-222	-217	-217	-217	-217
Capital Employed	**1,799**	**1,875**	**2,021**	**2,241**	**2,218**	**2,399**	**3,083**	**3,332**	**3,432**
Net Fixed Assets	**1,891**	**1,589**	**1,684**	**1,690**	**2,292**	**2,500**	**3,049**	**2,989**	**2,909**
Goodwill on Consolidation	0	328	333	346	0	0	0	0	0
Capital WIP	0	52	88	40	0	0	0	0	0
Right of use assets	0	0	0	259	0	0	**0**	**0**	**0**
Total Investments	**182**	**180**	**176**	**278**	**329**	**359**	**359**	**359**	**359**
Curr. Assets, Loans&Adv.	**234**	**327**	**382**	**724**	**617**	**561**	**736**	**1,108**	**1,313**
Inventory	0	1	1	2	0	0	0	2	1
Account Receivables	47	59	43	46	36	41	44	51	53
Cash and Bank Balance	13	48	62	136	81	61	173	523	707
Loans and Advances	173	219	276	541	500	459	519	533	552
Curr. Liability & Prov.	**507**	**602**	**641**	**1,097**	**1,020**	**1,020**	**1,061**	**1,124**	**1,148**
Account Payables	497	577	621	621	1,020	1,020	1,061	1,124	1,148
Provisions	10	25	20	476	0	0	0	0	0
Net Current Assets	**-273**	**-275**	**-259**	**-373**	**-403**	**-460**	**-325**	**-16**	**165**
Appl. of Funds	**1,799**	**1,875**	**2,021**	**2,241**	**2,218**	**2,399**	**3,083**	**3,332**	**3,432**

Financials and Valuation

Ratios

Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
Basic (INR)									
EPS	**11.1**	**3.5**	**-8.7**	**-7.5**	**-1.3**	**6.3**	**13.6**	**18.1**	**28.2**
Cash EPS	60.6	51.6	44.7	43.1	52.2	65.5	79.1	93.0	109.5
BV/Share	168.8	173.9	178.7	141.4	107.3	119.1	132.5	187.9	216.1
DPS	1.0	1.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Payout (%)	12.7	43.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Valuation (x)									
P/E	69.7	221.9	-88.7	-103.8	-591.4	122.8	57.0	42.8	27.4
Cash P/E	12.8	15.0	17.4	18.0	14.8	11.8	9.8	8.3	7.1
P/BV	4.6	4.5	4.3	5.5	7.2	6.5	5.8	4.1	3.6
EV/Sales	4.4	5.0	5.3	6.4	5.8	5.1	4.6	3.8	3.3
EV/EBITDA	11.8	13.8	16.7	15.5	12.8	10.4	9.0	7.3	6.2
Dividend Yield (%)	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Return Ratios (%)									
RoE	6.6	2.0	-5.0	-5.5	-1.1	5.6	10.8	11.3	14.0
RoCE	5.3	4.6	-2.5	3.7	12.8	8.0	9.6	9.3	10.8
RoIC	5.4	4.5	-2.6	3.5	14.4	8.6	11.0	11.5	13.8
Working Capital Ratios									
Fixed Asset Turnover (x)	0.5	0.5	0.5	0.5	0.4	0.5	0.5	0.5	0.6
Asset Turnover (x)	0.5	0.4	0.4	0.4	0.5	0.5	0.5	0.5	0.5
Inventory (Days)	0	0	0	1	0	0	0	0	0
Debtor (Days)	18	26	19	19	13	13	11	12	11
Creditor (Days)	190	255	281	261	370	320	277	262	244
Leverage Ratio (x)									
Current Ratio	0.5	0.5	0.6	0.7	0.6	0.5	0.7	1.0	1.1
Interest Cover Ratio	2.0	1.3	0.5	0.6	1.1	1.5	1.9	1.9	2.2
Net Debt/Equity	1.3	1.3	1.4	1.5	2.5	2.3	2.7	1.5	0.8

Consolidated - Cash Flow Statement (INR b)

Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
OP/(Loss) before Tax	77	33	-17	-428	-31	125	165	195	281
Depreciation	198	192	213	277	297	331	366	419	454
Interest & Finance Charges	95	93	110	137	149	165	188	207	205
Direct Taxes Paid	-32	-14	-12	-23	-22	-22	-47	-55	-79
(Inc)/Dec in WC	-27	6	-55	-166	30	-14	-31	40	4
CF from Operations	**311**	**311**	**239**	**-203**	**423**	**585**	**641**	**806**	**866**
Others	-19	-12	-39	384	59	-35	0	0	0
CF from Operating incl EO	**292**	**299**	**201**	**181**	**482**	**550**	**641**	**806**	**866**
(Inc)/Dec in FA	-384	-267	-305	-221	-334	-424	-758	-359	-374
Free Cash Flow	**-92**	**31**	**-105**	**-40**	**148**	**127**	**-118**	**448**	**492**
(Pur)/Sale of Investments	-1	-33	1	-88	38	-5	9	0	0
Others	69	40	19	5	27	10	0	0	0
CF from Investments	**-316**	**-260**	**-285**	**-305**	**-269**	**-419**	**-750**	**-359**	**-374**
Issue of Shares	1	0	99	462	7	10	0	208	0
Inc/(Dec) in Debt	9	40	106	-180	-118	-19	408	-99	-102
Interest Paid	-59	-44	-76	-110	-71	132	-188	-207	-205
Dividend Paid	-9	-33	-47	-18	-27	-14	0	0	0
Others	53	56	13	37	-40	-257	1	0	0
CF from Fin. Activity	**-4**	**19**	**95**	**191**	**-249**	**-148**	**221**	**-98**	**-307**
Inc/Dec of Cash	**-28**	**58**	**10**	**68**	**-36**	**-17**	**112**	**349**	**185**
Opening Balance	18	-10	41	54	131	91	74	186	536
Closing Balance	**-10**	**41**	**54**	**131**	**91**	**74**	**186**	**536**	**720**
Less :- Bank overdraft	**-23**	**-7**	**-8**	**-5**	**10**	**13**	**13**	**13**	**13**
Net Closing Balance	**13**	**48**	**62**	**136**	**81**	**61**	**173**	**523**	**707**

Explanation of Investment Rating	
Investment Rating	**Expected return (over 12-month)**
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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