

Company update

Telecom

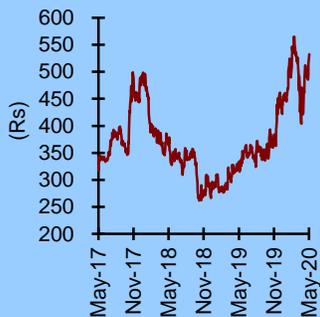
Target price: Rs610

Shareholding pattern

	Jun '19	Sep '19	Dec '19
Promoters	62.7	62.7	62.7
Institutional investors	35.2	35.5	30.5
MFs and others	8.3	8.8	9.3
Insurance Cos.	4.7	4.3	4.7
FII's	22.1	22.4	16.5
Others	2.1	1.8	6.8

Source: NSE

Price chart



INDIA

Bharti Airtel

BUY

Maintained

Rs528

Market share gain an upside risk

Bharti Airtel's (Bharti) incremental AGR (including NLD) and incremental EBITDA have shown healthy improvement with market shares starting to increase. Company's incremental AGR and incremental EBITDA (YoY) gaps vs RJio's were Rs14bn and Rs7bn in Q3FY20, respectively adjusted for net-IUC. The gaps have significantly narrowed in past seven quarters, and we expect them to further shrink going forward. We see upside risk to Bharti's market share on acceleration of its network investment, particularly in challenger circles. Our analysis shows that for every 100bps higher market share for Bharti, its equity value rises by Rs182bn, or Rs33/sh (5% of our SoTP-based value). Maintain BUY with an unchanged target price of Rs610.

► **Bharti's incremental AGR (including NLD) and incremental EBITDA have shown remarkable improvement.** Bharti incremental AGR (including NLD) YoY has shown significant improvement from a negative Rs24bn in Q4FY18 to a positive Rs15bn in Q3FY20, an improvement of Rs39bn. Adjusted for net-IUC, AGR gap has narrowed to Rs14bn for Bharti against RJio and we expect it to further shrink in coming quarters. Despite decline in AGR, Bharti has broadly maintained its market share while VIL continue to show negative incremental revenues. Bharti's AGR (including NLD) market share was 31.6% in Q3FY20 (vs 31.8% in Q4FY18).

Incremental EBITDA has improved from a negative Rs18bn in Q4FY18 to a positive Rs7bn in Q3FY20. We expect Bharti's EBITDA expanding much faster in the next few quarters due to the benefit of tariff hikes taken in Dec'19. Adjusted for net-IUC, the company's incremental EBITDA gap against RJio has narrowed to Rs7bn. We see this gap fast reducing on rising incremental revenues for Bharti. Company's EBITDA market share is still 26.3% among the top three operators, and we see huge scope for improvement in this parameter.

► **Market share has upside risk.** Bharti's market share has upside risk vs consensus estimate due to: 1) the huge 4G network expansion planned by it over next 24 months, particularly in nine circles where it traditionally was a challenger, or has recently lost huge market share. Network expansion should help Bharti increase its 4G coverage, which should result in higher incremental market share; and 2) we believe Bharti will be a net gainer from SIM consolidation.

► **100bps rise in market share implies Rs182bn (Rs33/sh) rise in equity value for Bharti.** Our analysis shows that every 100bps gain in market share by Bharti can potentially add Rs182bn to its equity value, or Rs33/sh (5% of our SoTP based value). However, we believe rising market share can lead to rerating in valuation multiples, and the upside could be higher than Rs33/sh.

Market Cap	Rs2880bn/US\$38.1bn
Reuters/Bloomberg	BRTI.BO / BHARTI IN
Shares Outstanding (mn)	5,455.6
52-week Range (Rs)	568/312
Free Float (%)	37.3
FII (%)	16.5
Daily Volume (US\$/'000)	110,803
Absolute Return 3m (%)	2.6
Absolute Return 12m (%)	60.7
Sensex Return 3m (%)	(23.3)
Sensex Return 12m (%)	(18.3)

Year to Mar	FY19	FY20E	FY21E	FY22E
Revenue (Rs bn)	808	892	1,025	1,135
Net Income (Rs bn)	(17)	(3)	79	129
EPS (Rs)	(4.1)	(0.5)	15.5	25.1
% Chg YoY	NA	NA	NA	62.6
P/E (x)	NA	NA	33.3	20.5
CEPS (Rs)	49.3	43.1	59.6	69.7
EV/E (x)	13.1	10.1	7.5	6.2
Dividend Yield (%)	0.5	0.5	0.5	0.6
RoCE (%)	2.2	2.1	6.6	8.6
RoE (%)	(2.3)	(0.3)	7.8	11.7

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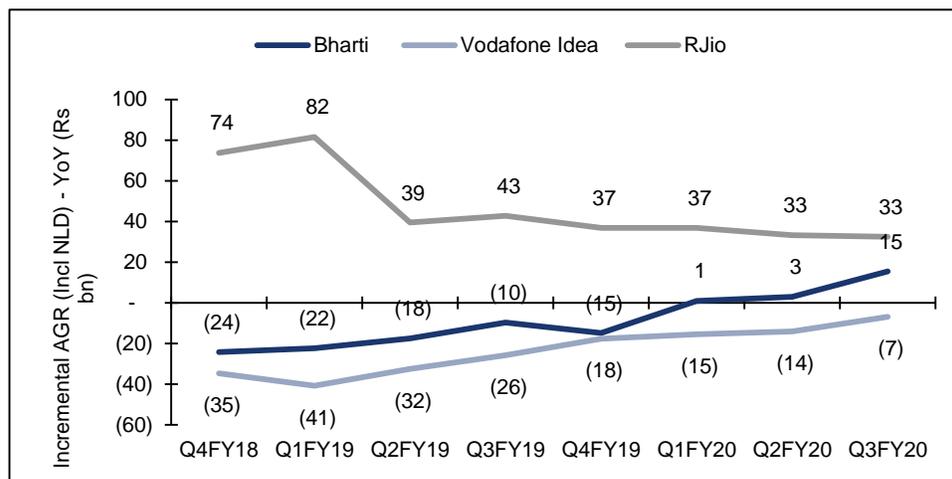
Bharti's incremental AGR (including NLD) YoY has shown significant improvement

Bharti Airtel's (Bharti) incremental revenues (based on AGR, including NLD) were Rs15bn in Q3FY20 from a negative Rs24 in Q4FY18, an improvement of Rs39bn in seven quarters. This compares to Vodafone Idea's (VIL) incremental revenues of a negative Rs7bn in Q3FY20 from a negative Rs35bn in Q4FY18, an improvement of Rs28bn. On the contrary, Reliance Jio's (RJio) incremental revenues dipped to Rs33bn from Rs74bn in Q4FY18, which implies a deterioration of Rs41bn. Earlier (in its initial period), RJio was benefiting from rapid expansion of its 4G subs on a favourable base.

We reckon that in Q3FY20 Bharti lost some revenues as RJio started charging for off-net outgoing calls, which had a negative impact on Bharti. Our working shows, adjusted for net-IUC, the difference between incremental revenues of Bharti and RJio was Rs14bn (vs reported Rs18bn) in Q3FY20. We see high probability of Bharti significantly narrowing the incremental revenue gap against the market leader in coming quarters.

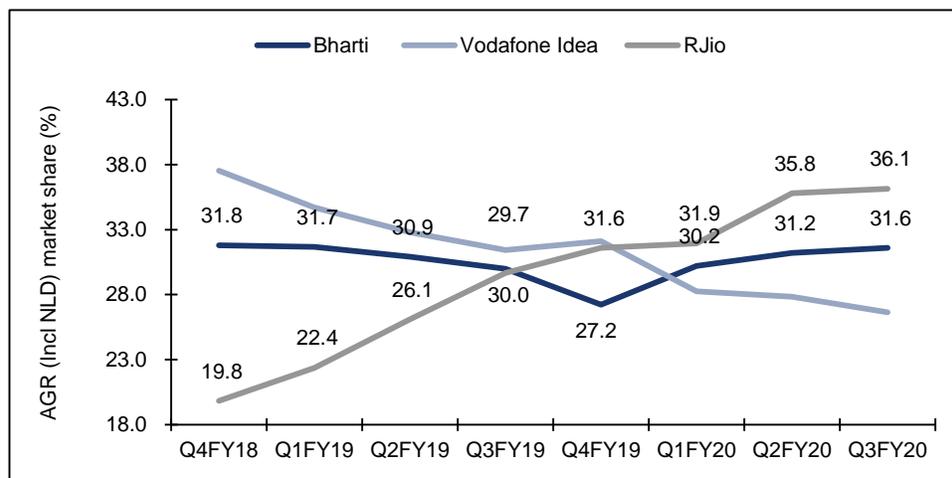
Despite revenue decline, Bharti has mostly held on to its AGR (including NLD) market share in 31-32% range. Its market share of 31.6% in Q3FY20 is shy away from its Q4FY18 market share of 31.8%. Consensus and our estimates mostly reckon Bharti will maintain its market share at existing levels in coming years. **However, we see upside risk to Bharti AGR market share on fast expanding incremental revenues.**

Chart 1: Bharti's incremental AGR (including NLD) YoY has improved significantly, and it is narrowing the gap against market leader



For VIL, we have done simple addition of numbers of Idea Cellular and Vodafone India during pre-merger
 Source: Company data, I-Sec research

Chart 2: Bharti has mostly maintained its AGR (including NLD) market share, but can it expand the same in the near term?



Source: Company data, I-Sec research

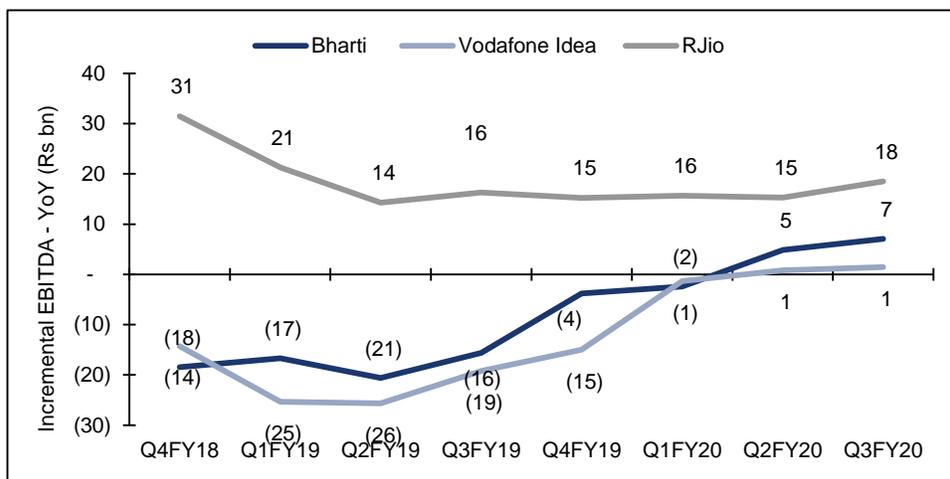
Bharti’s mobile EBITDA market share has huge scope for expansion

Incremental EBITDA and EBITDA market share is critical for value creation as it is closest to FCF, and requires deeper analysis in our view. Bharti was losing incremental EBITDA at (negative) Rs18bn in Q4FY18, which has now improved to a positive Rs7bn. We see this expanding much faster in coming quarters due to benefit of tariff hikes taken in Dec’19. This compares to VIL’s slightly positive incremental EBITDA of Rs1bn (mostly attributable to synergy benefit) from a negative of Rs14bn in Q3FY18.

RJio’s incremental EBITDA has been in a tight range for past six quarters at Rs14bn-18bn. Adjusted for net-IUC, Bharti’s incremental EBITDA gap against RJio has narrowed to Rs7bn. We see this gap shrinking further in coming quarters on higher incremental revenues for Bharti.

Unlike revenue market share, Bharti has lost its EBITDA market share due to accelerated investment in 4G network. Bharti’s EBITDA market share (based on top-3 operators’ numbers) was only 26.3% in Q3FY20 while RJio captured 61% mobile EBITDA market share. Considering that Bharti is reducing the incremental EBITDA gap against RJio, we expect it to expand its EBITDA market share faster than AGR (including NLD) as it can steadily deliver incremental EBITDA margin of 60-70%, while RJio’s incremental EBITDA margin has been volatile and lower.

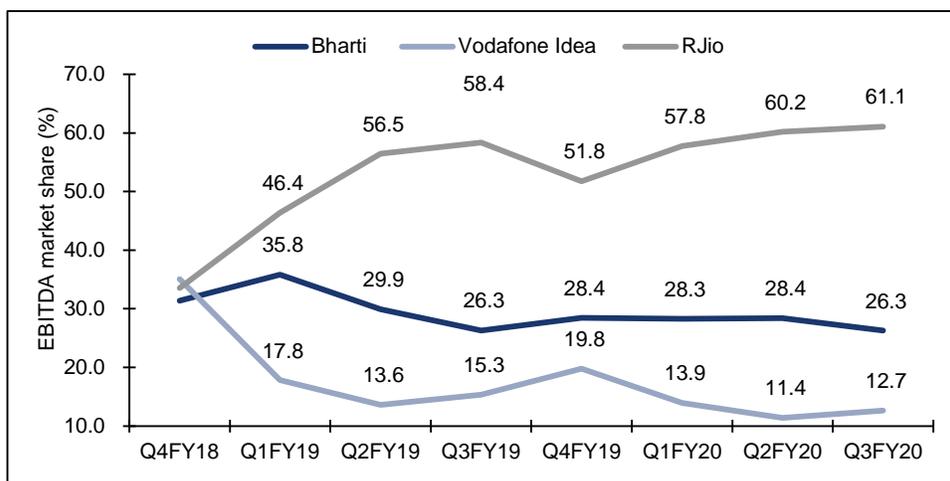
Chart 3: Bharti's incremental EBITDA (YoY) has seen significant turnaround



Note: Bharti EBITDA represents EBITDA for its mobile segment, and EBITDA for all the three operators are adjusted for Ind-AS 116 impact. For Bharti and RJio, we have adjusted EBITDA based on their Ind-AS 116 disclosure of Q1FY20.

Source: Company data, I-Sec research

Chart 4: Huge scope exists for Bharti to expand its EBITDA market share



Source: Company data, I-Sec research

Why Bharti should gain market share

It is highly likely that Bharti may start expand its AGR (including NLD) market share in coming quarters due to:

- Its aggressive investment in network expansion, which should increase its 4G coverage. This compares to limited investment by peers. Per media report ([refer](#)), Bharti has awarded US\$1bn contract to Nokia to expand and modernise its 4G network in nine circles, including rural areas. Under the deal, 300,000 radio units will roll out across spectrum bands 900MHz, 1800MHz, 2100MHz and 2300MHz. This work is expected to be complete by 2022. It would also include rolling out of 22-26k fresh towers.

Of the nine circles, five are Bharti's traditional challenger circles (non-900MHz circles) – Mumbai, Maharashtra, Gujarat, Kerala and Madhya Pradesh –and three circles are where Bharti has lost significant market share – Bihar, Odisha and Uttar

Pradesh (East). The network expansion in our view will benefit Bharti and probably poses a risk to VIL's market share as many of these are the latter's leadership circles.

- In our view, SIM consolidation, triggered by tariff hike, should positively benefit Bharti.

We see upside risk to our estimates if Bharti gains higher than expected market share.

Table 1: Market share (based on Q3FY20 circle-wise AGR)

Circles (%)	Bharti	VIL	RJIO
Mumbai	26.4	36.8	35.3
Maharashtra	19.5	38.5	39.8
Gujarat	12.8	38.1	45.7
Kerala	14.6	51.4	23.5
U.P east	29.6	17.0	52.3
M.P	17.9	18.0	60.9
W.B	22.4	22.3	53.0
Bihar	28.9	5.2	64.1
Odisha	29.1	6.3	58.0
Pan-India	28.6	22.7	44.4

Source: Company data, I-Sec research

100bps rise in market share implies Rs182bn (Rs33/sh) rise to equity value for Bharti

Our analysis shows every 100bps higher market share for Bharti can potentially add Rs182bn to its equity value, or Rs33/sh (5% of our SoTP based value). However, we believe rising market share will lead to rerating in valuation multiples, and the upside could be higher than Rs33/sh.

Table 2: Our analysis shows 100bps rise in market share adds Rs182bn to Bharti's equity value

Rs bn	FY21E	FY22E	FY23E	FY24E	FY25E
Industry revenue	1,771	2,050	2,342	2,655	3,013
1% market share	17.7	20.5	23.4	26.6	30.1
EBITDA (80% margin)	14.2	16.4	18.7	21.2	24.1
NOPAT	10.6	12.2	14.0	15.8	18.0
FCFF	10.6	11.0	11.3	11.6	11.8
WACC	11%				
Terminal EBITDA multiple (x)	8.0				
PV of FCFF	56				
PV of terminal value	126				
Total	182				

Source: Company data, I-Sec research

Table 3: Bharti Airtel – SoTP based valuation

Business units (Rs/sh)	Methodology	FY22E
India (excluding tower business)	11.0x EV/EBITDA	720
Africa business	6.0x EV/EBITDA (proportionate)	61
Tower business (including Indus)	DCF (proportionate, 20% holdco discount)	47
Enterprise value		828
Less: Net debt	Proportionate	146
Total		682
AGR case liability		72
Fair value (Rs/sh)		610

Source: Company data, I-Sec research

Financial summary

Table 4: Profit & loss statement

(Rs mn, year ending March 31)

	FY19	FY20E	FY21E	FY22E
Operating Income (Sales)	807,802	891,681	1,025,027	1,135,034
Operating Expenses	549,613	576,139	591,079	626,609
EBITDA	258,189	315,542	433,948	508,425
% margins	32.0	35.4	42.3	44.8
Depreciation & Amortisation	213,475	223,635	226,451	228,618
Net Interest	110,134	84,665	87,512	90,575
Other Income	18,814	10,902	10,106	10,581
Recurring PBT	(46,606)	18,145	130,092	199,813
Add: Extraordinaries	29,288	-	-	-
Less: Taxes	(34,193)	8,344	37,055	54,987
- Current tax	(34,193)	8,344	37,055	54,987
- Deferred tax				
Less: Minority Interest	4,095	12,502	13,745	15,869
Net Income (Reported)	12,780	(2,702)	79,292	128,957
Recurring Net Income	(16,508)	(2,702)	79,292	128,957

Source: Company data, I-Sec research

Table 5: Balance sheet

(Rs mn, year ending March 31)

	FY19	FY20E	FY21E	FY22E
Assets				
Total Current Assets	368,692	352,553	467,985	566,097
of which cash & cash eqv.	149,228	136,292	242,133	336,103
Total Current Liabilities & Provisions	566,706	586,233	604,258	614,242
Net Current Assets	(198,014)	(233,680)	(136,274)	(48,145)
Investments	88,937	135,121	141,869	149,092
of which				
Strategic/Group	88,937	135,121	141,869	149,092
Other Marketable				
Net Fixed Assets	1,772,095	1,804,147	1,826,863	1,826,897
Goodwill	362,663	371,987	374,119	375,262
Total Assets	2,025,681	2,077,574	2,206,578	2,303,106
Liabilities				
Borrowings	1,254,283	1,043,278	1,114,278	1,103,278
Deferred tax liability	(78,082)	(78,082)	(78,082)	(78,082)
Minority Interest	135,258	130,296	126,098	122,781
Equity Share Capital	19,987	25,655	25,655	25,655
Face Value per share(Rs)	5.0	5.0	5.0	5.0
Reserves & Surplus	694,235	956,427	1,018,629	1,129,474
Net Worth	714,222	982,082	1,044,283	1,155,129
Total Liabilities	2,025,681	2,077,574	2,206,578	2,303,106

Source: Company data, I-Sec research

Table 6: Quarterly trend

(Rs mn, year ending March 31)

	Mar-19	Jun-19	Sep-19	Dec-19
Net sales	206,568	208,125	211,990	220,216
% growth (YoY)	4.8	3.1	3.5	7.0
EBITDA	66,803	83,173	89,049	93,203
Margin (%)	32.3	40.0	42.0	42.3
Other income	1,685	2,101	2,066	2,629
Add: Extraordinaries	20,221	(14,694)	(307,110)	(10,500)
Net profit	1,072	(28,660)	(230,449)	(10,353)

Source: Company data

Table 7: Cashflow statement

(Rs mn, year ending March 31)

	FY19	FY20E	FY21E	FY22E
Operating Cashflow	184,451	220,933	305,742	357,575
Working Capital Changes	(58,196)	14,699	8,815	10,834
Capital Commitments	(307,362)	(252,480)	(247,965)	(231,256)
Free Cashflow	(181,107)	(16,848)	66,592	137,153
Cashflow from Investing Activities	(77,418)	(14,630)	48,983	119,819
Issue of Share Capital	(238)	249,390	-	-
Buyback of shares Inc (Dec) in				
Borrowings	102,494	(214,000)	71,000	(11,000)
Dividend paid	(46,617)	(13,469)	(14,142)	(14,849)
Extraordinary Items	29,288	-	-	-
Chg. in Cash & Bank balance	7,509	7,291	105,841	93,970

Source: Company data, I-Sec research

Table 8: Key ratios

(Year ending March 31)

	FY19	FY20E	FY21E	FY22E
Per Share Data (in Rs.)				
Recurring EPS	(4.1)	(0.5)	15.5	25.1
Reported EPS	3.2	(0.5)	15.5	25.1
Recurring Cash EPS	49.3	43.1	59.6	69.7
Dividend per share (DPS)	2.5	2.6	2.8	2.9
Book Value per share (BV)	178.7	191.4	203.5	225.1
Growth Ratios (%)				
Operating Income	(3.5)	10.4	15.0	10.7
EBITDA	(14.2)	22.2	37.5	17.2
Recurring Net Income	(187.2)	(83.6)	NM	62.6
Diluted Recurring EPS	(187.2)	(87.2)	NM	62.6
Diluted Recurring CEPS	(6.8)	(12.6)	38.4	17.0
Valuation Ratios (% YoY)				
P/E	(128.1)	NM	34.2	21.0
P/CEPS	10.7	12.3	8.9	7.6
P/BV	3.0	2.8	2.6	2.3
EV / EBITDA (incl Indus)	13.4	10.3	7.6	6.4
EV / Operating Income	4.7	4.1	3.5	3.1
EV / Operating FCF	(21.1)	(214.9)	53.9	25.4
Operating Ratios				
Other Income / PBT (%)	(40.4)	60.1	7.8	5.3
Effective Tax Rate (%)	73.4	46.0	28.5	27.5
NWC / Total Assets (%)	(9.8)	(11.2)	(6.2)	(2.1)
Inventory Turnover (days)	0.6	0.6	0.6	0.6
Receivables (days)	19.4	84.9	77.1	70.7
Payables (days)	181.0	173.2	151.7	136.9
Net Debt/EBITDA Ratio (x)	4.3	2.9	2.0	1.5
Capex % of sales	38.0	28.3	24.2	20.4
Profitability Ratios (%)				
Rec. Net Income Margins	(2.0)	(0.3)	7.7	11.4
RoCE	2.2	2.1	6.6	8.6
RoIC	0.9	2.9	8.0	10.7
RoNW	(2.3)	(0.3)	7.8	11.7
Dividend Yield	0.5	0.5	0.5	0.5
EBITDA Margins	32.0	35.4	42.3	44.8

Source: Company data, I-Sec research

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