LatAm TMT

Global deep dive in Telcos: BZ Telcos showing above average trends

Estimate Change

11 March 2024

Equity
Latin America
Telecommunications, Media and Technology

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FTTH = Fiber to the Home

MSR = Mobile service revenue

AMX = America Movil

Brazilian telcos should continue to perform in 2024

After Brazilian (BZ) Telcos delivered total return of 50% in 2023 (+6% TIM, -2% Vivo YTD) vs IBOV at +22% (-6% YTD), investors are questioning if the better operational momentum is priced in. Moreover, we analyzed the Telcos vs global peers, considering: i) markets they operate; ii) Real top line and EBITDA growth; iii) opportunity to raise prices; iv) Distribution yield; and iv) operating cash flow (EBITDA-Capex). We concluded that BZ Telcos are in a better position vs. peers already adjusting for Ke; given: i) higher real growth potential and dividend yield. We maintain our preference for Vivo vs TIM given its better operational results and higher distribution yield. We also update our numbers for TIM with its new dividends guidance and reiterate our Buy rating and R$22 PO.

In line w/ historical valuation despite better momentum

For 2024 we expect LatAm Telcos to post an MSR growth in BZ of +6%, vs inflation of ~4%, while maintaining/reducing nominal capex. For most of the last 10 years the segment posted below inflation growth and capex increased on a sequential basis, which changed after sector consolidation (Oi's acquisition). Despite the better momentum, they are trading mostly in line with their historical EV/EBITDA average, with Vivo at 4.5x, in line with average and TIM at 4.3x, 5% premium (exhibit 16). We believe there is room for further rerating considering the better dynamics for top line growth and Capex.

Global picture: Higher growth and lower leverage

To minimize market differences (competition/Ke), we adjusted our EV/EBITDA with average US/EU Ke of 8%. Moreover, Vivo and TIM would have some of the highest multiples vs peers, but also the highest real total returns, which we believe justify higher multiples (exhibit 6). We highlight Vivo and TIM also had some of the best numbers for (i) leverage, (ii) capex/revenues reduction and (iii) real revenue and EBITDA growth.

Bullish overall on Telcos - Relative preference for Vivo

We are bullish on BZ Telcos but maintain a relative preference for Vivo given: (i) better operational momentum on mobile, (ii) strong net adds that should support 1Q results, (iii) higher dividends for 2024 at 9.5% vs TIM at 8.5% and (iv) high growth in B2B digital + B2C new businesses (7% of revenues and 30% YoY growth in 2023). We reiterate our Buy rating for Vivo (PO of R$64) and TIM (PO of R$22). (see: [Year Ahead: Bullish on Brazilian large Telcos... selective on Tech]).

AMX should also post solid FCF generation

Although AMX has less exposure to the BZ market (~20% of EBITDA) we remain bullish (Buy, MXN21 PO) as we see a solid outlook for FCF generation (9% yield 24). In addition, differently from TIM and Vivo, it is trading at a discount to historical avg.

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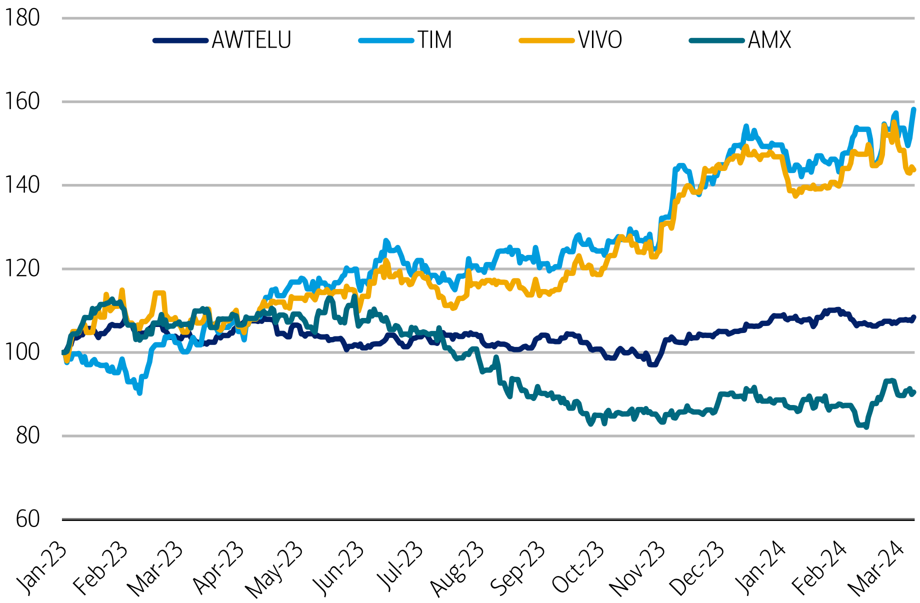
Brazilian Telcos outperforming peers

Analyzing the stock performance of the Brazilian Telcos for the past year (sector consolidation) we can see that they outperformed its peers considerably. While TIM and Vivo's stock was up ~50% since the start of 2023, the Global Telcos index was only up 7% and AMX was down ~10%. Overall, we believe the strong performance of the BZ Telcos in the last year was justified given the positive changes in the mobile market post consolidation, along with strong results on Fixed (FTTH).

Exhibit 1: The Brazilian Telcos have outperformed international peers since the start of 2023
Stock performance since Jan 2023



Source: Bloomberg

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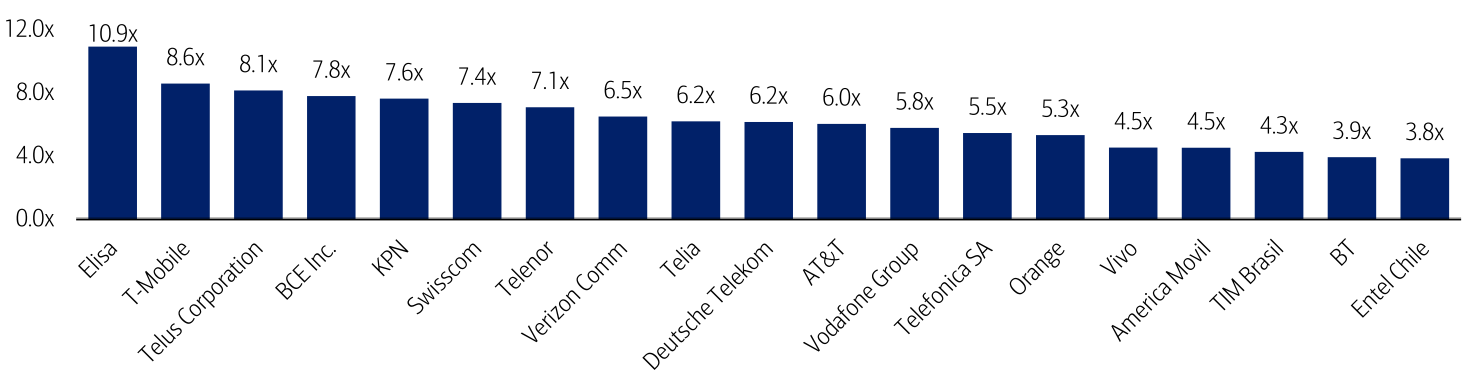
Brazil Telcos more expensive than average (Ke adjusted)….

To better understand the LatAm Telcos' valuation against international peers we adjusted their EV/EBITDA multiples using US/EU average Ke (Vivo at 12.4%, TIM at 12.9% and US/EU at ~8%). After the adjustment, Vivo's 4.5x EV/EBITDA 24 raises to 7.9x, TIM raises from 4.3x to 7.4x and AMX from 4.5x to 7.4x. With that, Vivo would rank as the fourth most expensive, while TIM at 5th and AMX 6th. We believe this is justifiable given the stronger momentum and dynamics for top line growth, margin expansion and increasing operating cash flow.

Exhibit 2: Not adjusting for Ke, the Brazilian Telcos have some of the lowest multiples among peers
Telcos EV/EBITDA 24 ratio



Source: Bloomberg, BofA Global Research

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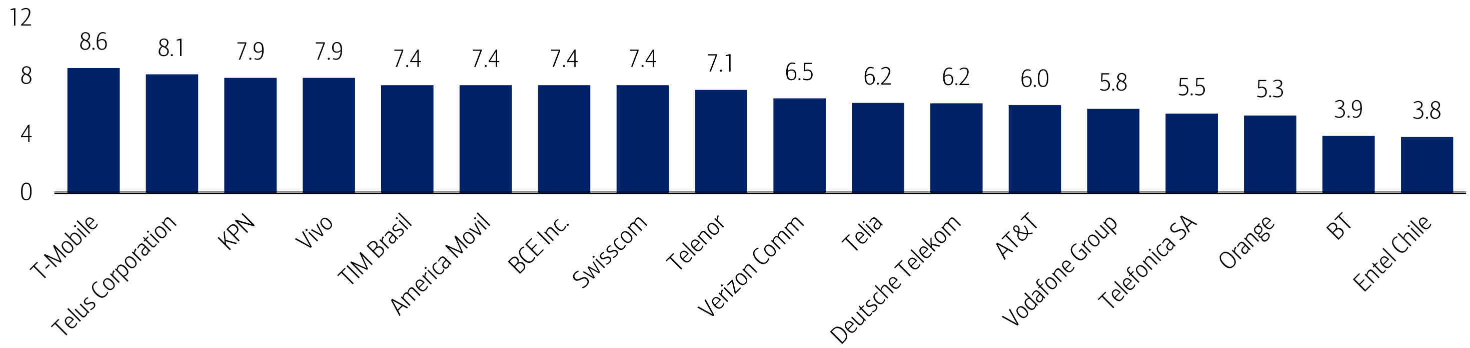
Exhibit 3: Adjusting for Ke, Brazilian Telcos multiples are closer to the top of the range
Telcos EV/EBITDA 24 ratio (With Vivo, TIM and AMX adjusted for Europe and US average Ke)



Source: Bloomberg, BofA Global Research

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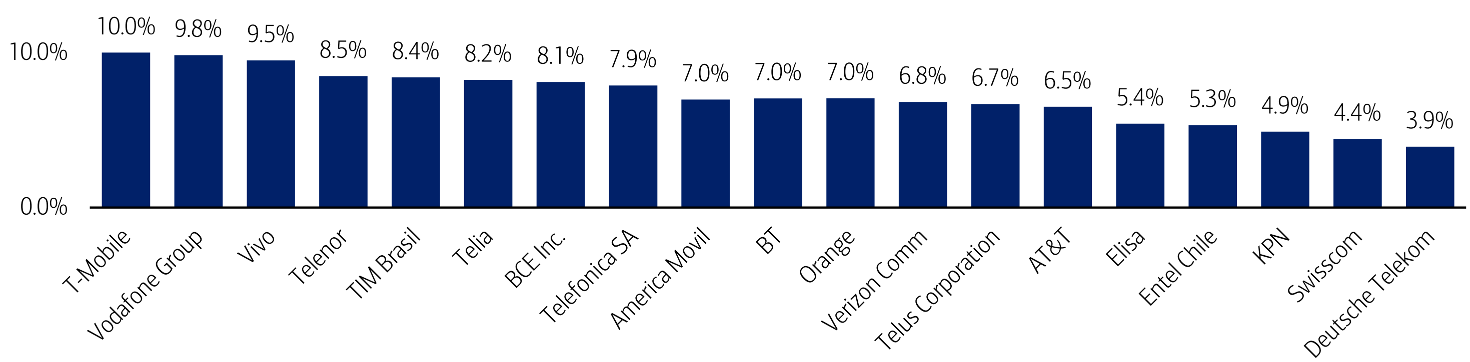
… but they are leading in terms of total return…

We expect the BZ Telcos to have a significant dividend distribution in 2024, due to its strong cash generation. Looking versus US/EU peers, Vivo and TIM should have the first and third highest total real return ratios in 2024 (real EBITDA growth + dividend Yield). AMX should also have an above average return, but below TIM and Vivo.

Exhibit 4: Vivo has one of the largest dividend yields expected for 2024
Dividend yield 2024 for the Telcos



Source: Bloomberg, BofA Global Research

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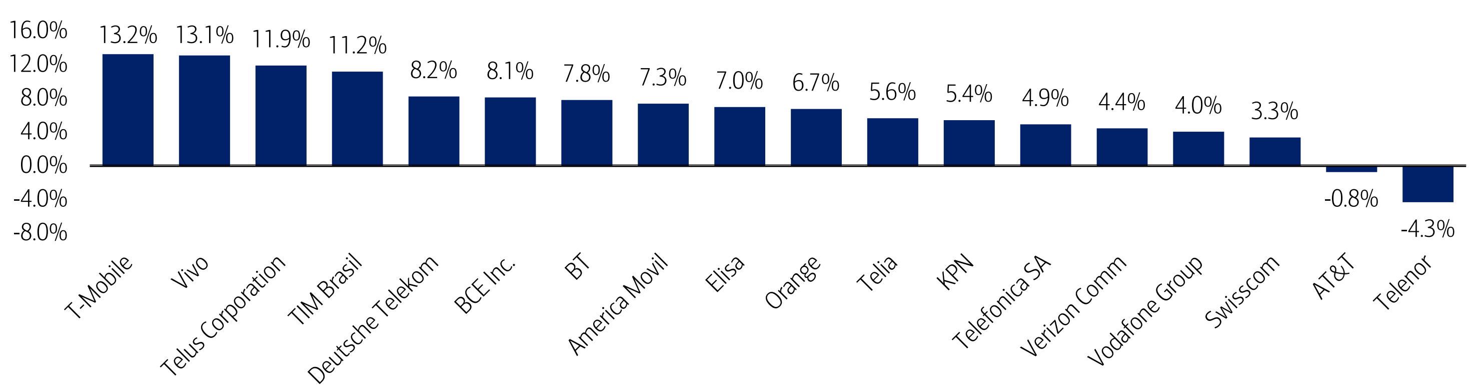
Exhibit 5: The BZ telcos are among the ones with the highest real total returns for 2024
Real total return for the Telcos for 2024 (Dividends + repurchase + Real EBITDA growth)



Source: Bloomberg, BofA Global Research

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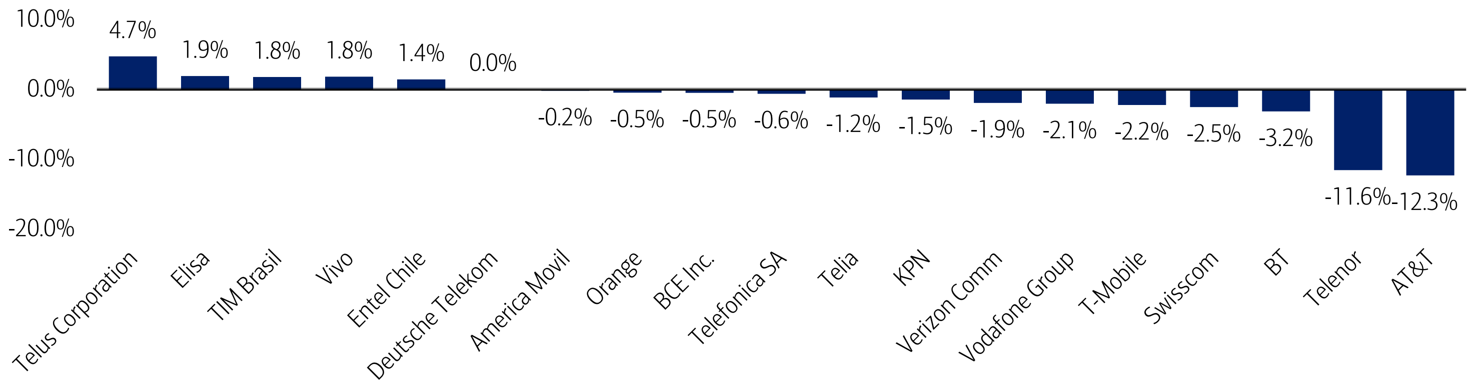
… among the ones with higher real growth rates…

Looking at the real growth ratios for top line and EBITDA, although Vivo and TIM are not at the very top, they are in top 6 for both categories, being among the few ones with real growth (Considering the inflation of each country). Although these levels of growth are above historical average, we believe there is a high likelihood they will continue in the Mid-term given a more rational market post consolidation. AMX is closer to the average.

Exhibit 6: BZ Telcos also should have some of the highest real growth rates for 2024
Real revenue growth CAGR 24-26



Source: Bloomberg, BofA Global Research

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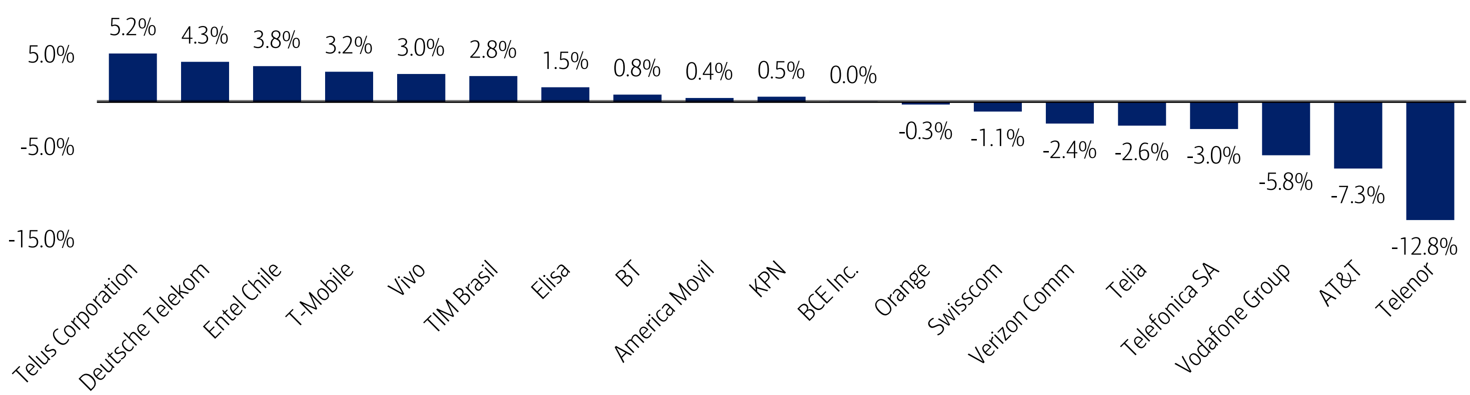
Exhibit 7: Vivo and TIM should have a high EBITDA real growth rate for the coming years
Real EBITDA growth CAGR 24-26



Source: Bloomberg, BofA Global Research

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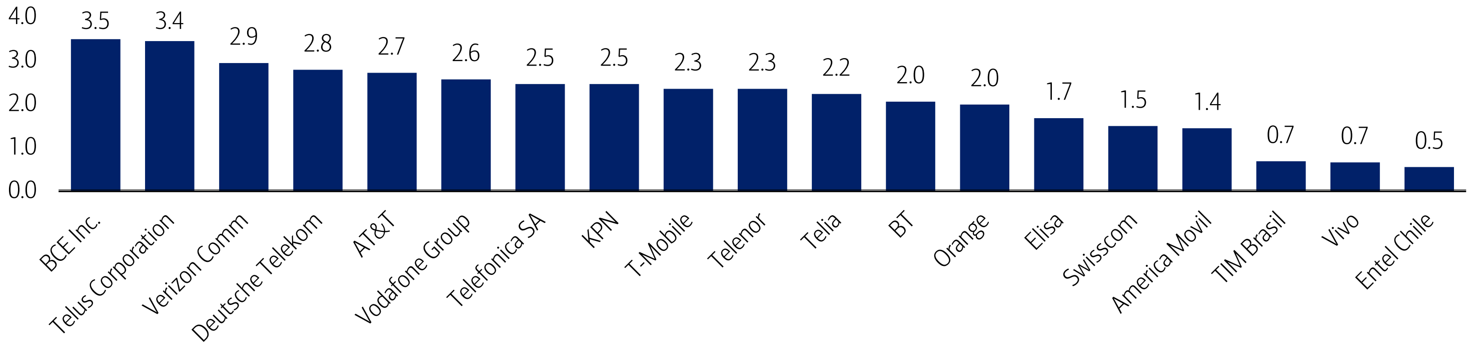
… lower leverage….

Looking at leverage, the LatAm telcos have the lowest ND/EBITDA ratios among global peers, which in our view should help support higher dividends in the MT to LT and reduces risk. In addition, if we look at Vivo and TIM ex-lease, both companies are already net cash, and should continue to generate cash at a solid rate (~9% FCFE yield for Vivo and TIM in 2024).

Exhibit 8: On top of having the lowest leverage ratios among peers, BZ Telcos are actually net cash ex-lease
Net debt/EBITDA ratio 24YE for the Telcos



Source: oomberg, BofA Global Research

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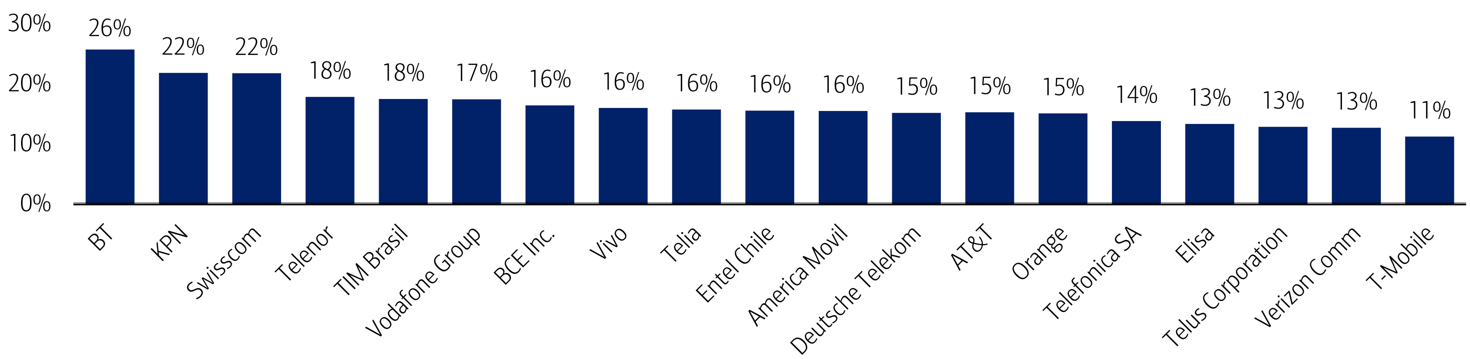
... and their capex is declining fast

Another segment in which LatAm telcos are among the best is in terms of capex reduction as a percentage of revenue. Despite Vivo and TIM's capex already declining 6% and 5% respectively in 2023, we expect both to continue decreasing their capex/revenues. We expect Vivo and TIM's capex to decline by 210 bps and 280bps of revenues for 2026 vs 2023. For AMX this difference should be even more significant, as capex is expected to have a sharp YoY decline, to a total of ~USd7bn for 2024.

Exhibit 9: The BZ telcos still have slightly higher capex/revenues than its peers average
Capex as a percentage of net revenues for the telcos for 2024



Source: Bloomberg, BofA Global Research

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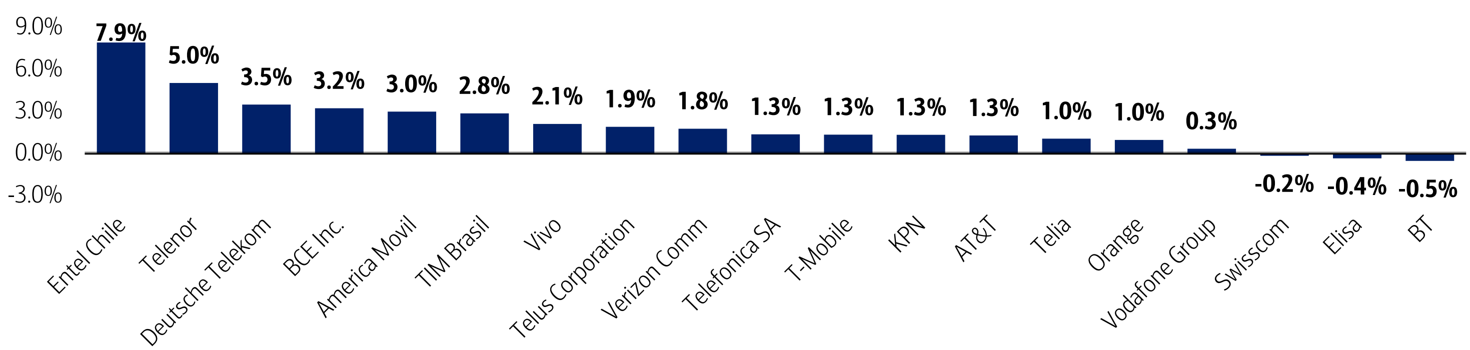
Exhibit 10: The LatAm Telcos should have a significant reduction in capex/revenues in the coming years
Decline in capex as a percentage of net revenues from 2023 to 2026



Source: Bloomberg, BofA Global Research

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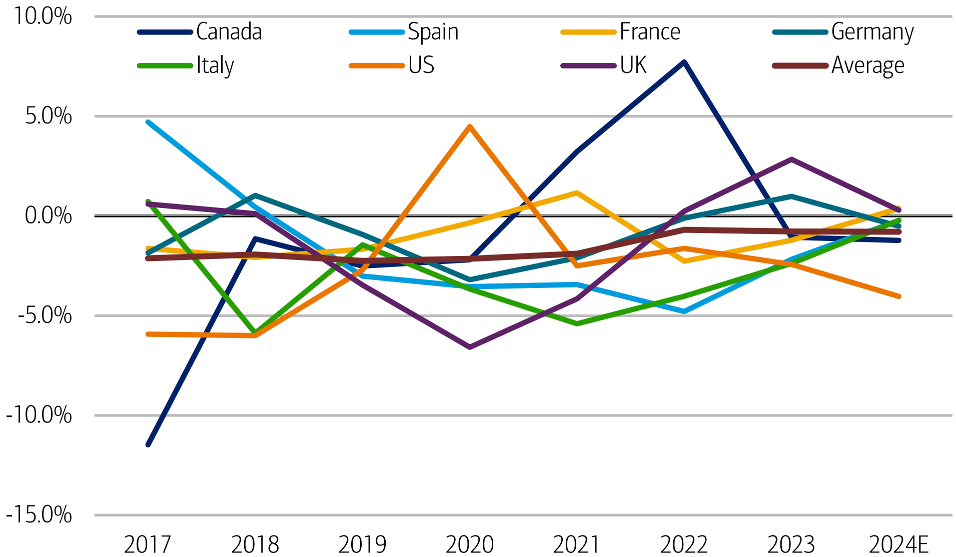
ARPU mostly lower in consolidated markets

When looking at the ARPU evolution in most consolidated markets, even the ones with 3 players, like in Brazil, ARPU had a slight decline for the past years. This is a negative sign for the sustainability of the LT ARPU expansion in Brazil, but at least looking at the ST/MT, we believe ARPU should continue to see real growth, given favorable market conditions. (see: Global Wireless Matrix: Stable global service revenue growth expected in '23E (+5.5%) after an extraordinary)

Exhibit 11: In more consolidated markets, ARPU has mostly trended down in the past few years
YoY ARPU expansion per country



Source: BofA Global Research

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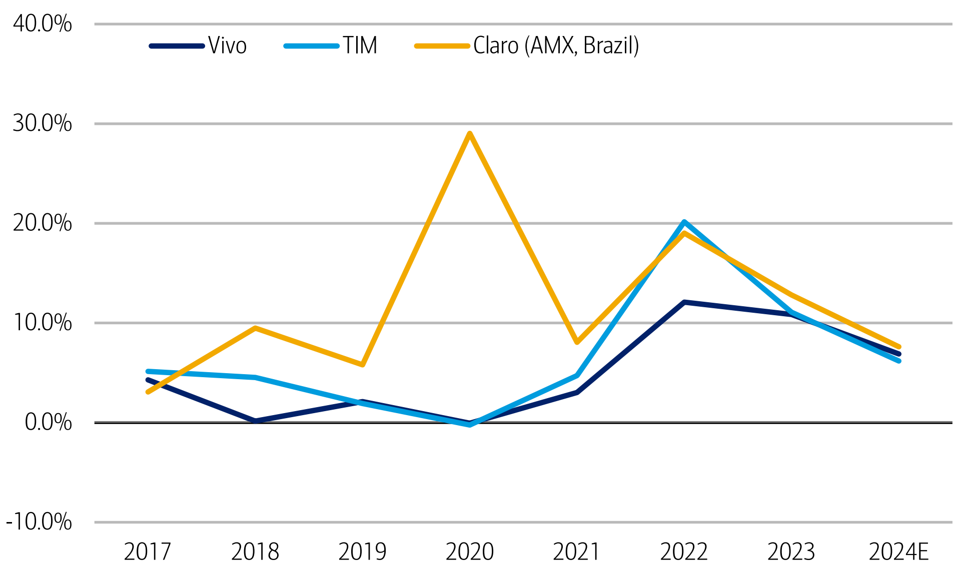
Exhibit 12: We expect the BZ telcos to continue posting real MSR growth in the ST
BZ telcos Mobile service revenue growth



Source: Company data; BofA Global Research

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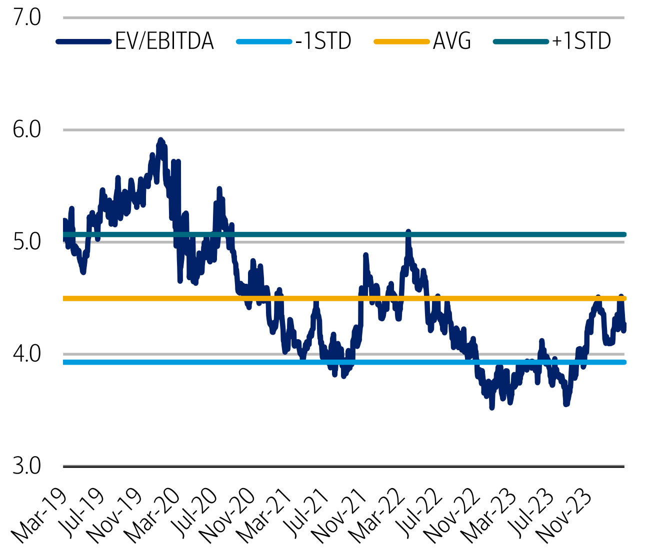
Mostly in line with historical average

Despite currently being their best operational momentum in years, the large Telcos are still trading in line to its L5Y EV/EBITDA average. Vivo trades in line and TIM at a 5% premium. At the same time, this is one of the largest premiums to historical levels among global peers, as most Telcos are trading at a discount. For AMX, although the operational momentum is not as strong as for the BZ telcos, the company is even trading at a ~10% discount to historical average.

Exhibit 13: Vivo is trading slightly above its L5Y EV/EBITDA average
Vivo's L5Y EV/EBITDA history



Source: Bloomberg, BofA Global Research

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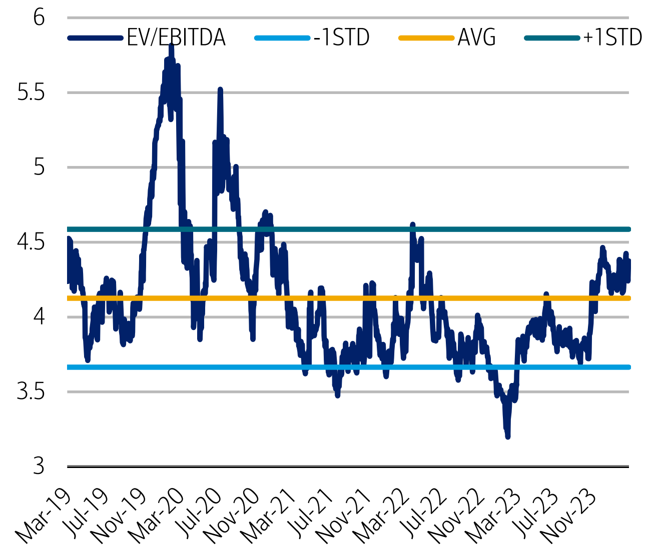
Exhibit 14: TIM is trading slightly above its L5Y EV/EBITDA average
TIM's L5Y EV/EBITDA history



Source: Bloomberg, BofA Global Research

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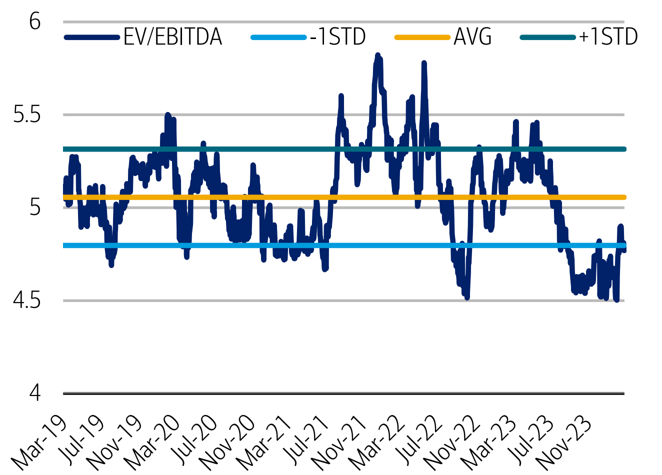
Exhibit 15: AMX is trading at a discount to its L5Y average
AMX's L5Y EV/EBITDA history



Source: Bloomberg, BofA Global Research

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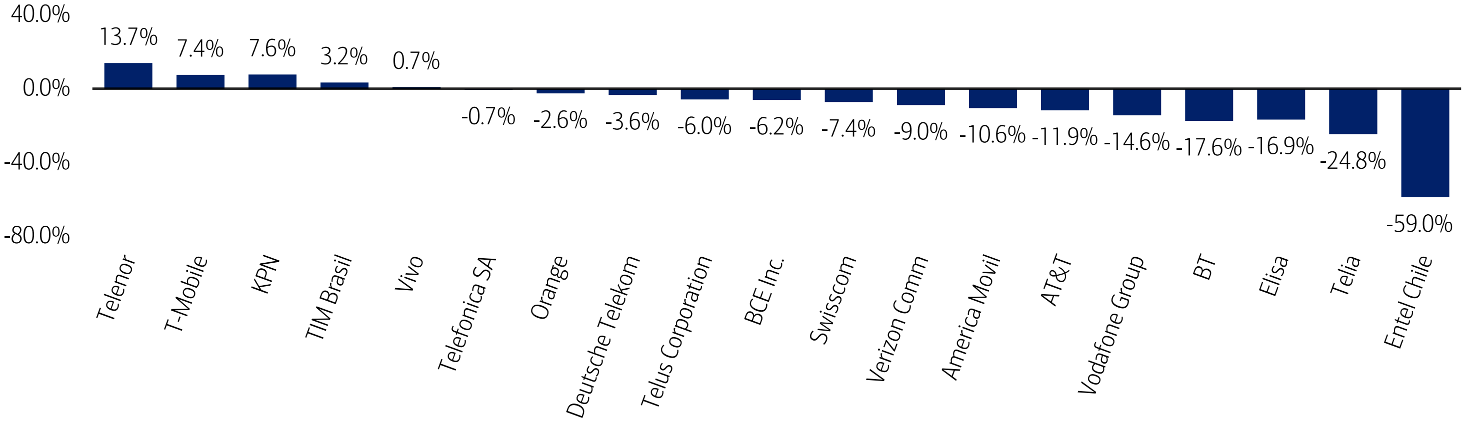
Exhibit 16: Vivo and TIM are among the only Telcos trading at a premium to historical average
EV/EBITDA 24 premium to L5Y average



Source: Bloomberg, BofA Global Research

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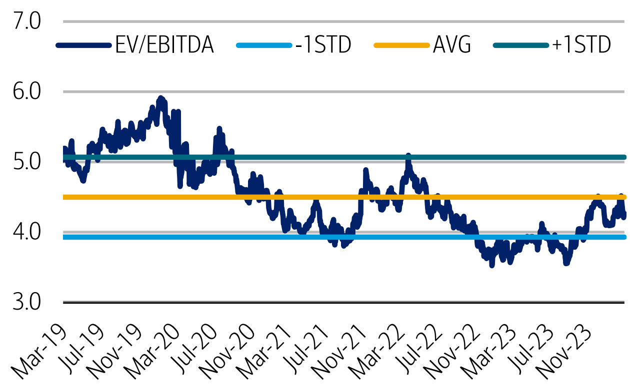
Exhibit 17: For L3Y, Vivo is trading at a larger premium to average
Vivo's L3Y EV/EBITDA history



Source: Bloomberg, BofA Global Research

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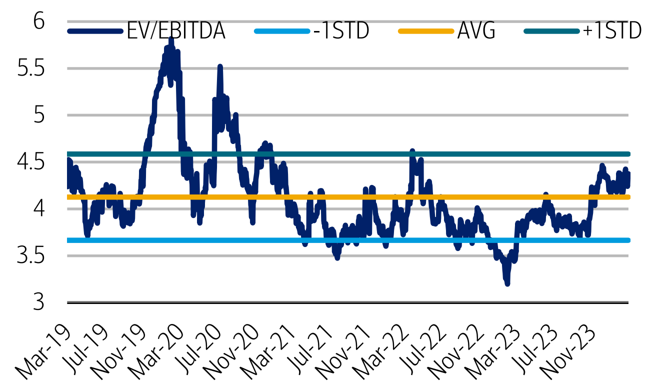
Exhibit 18: For L3Y, TIM is trading at a larger premium to average
TIM's L3Y EV/EBITDA history



Source: Bloomberg, BofA Global Research

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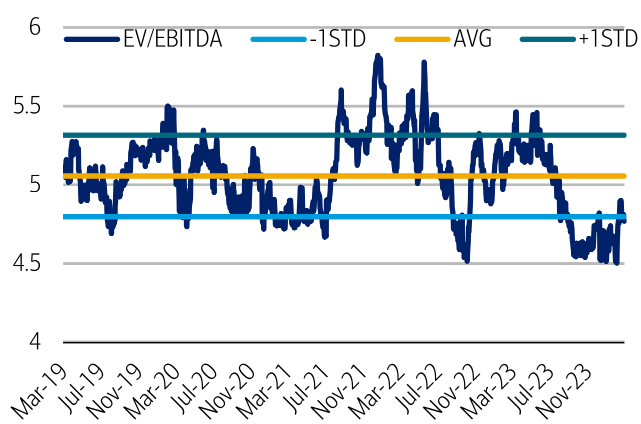
Exhibit 19: AMX is also trading at a discount to its L3Y average
AMX's L3Y EV/EBITDA history



Source: Bloomberg, BofA Global Research

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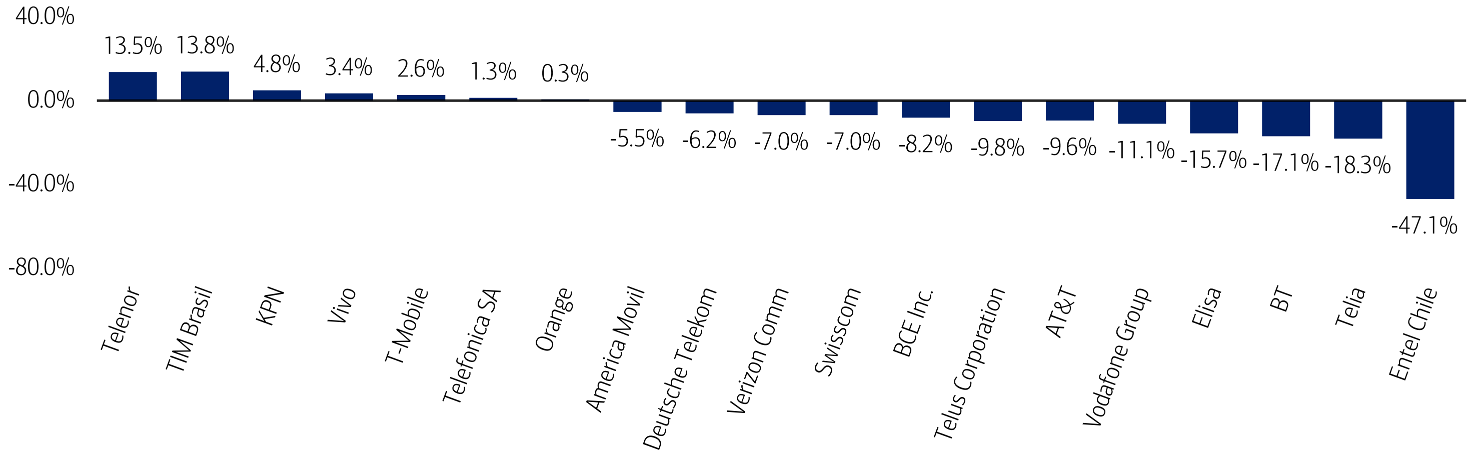
Exhibit 20: R Vivo and TIM are among the only Telcos trading at a premium to historical average
EV/EBITDA 24 premium to L3Y average



Source: Bloomberg; BofA Global Research

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Updating our estimates for TIM – Buy and R$22 PO

We update our numbers for TIM Brazil with its new dividends guidance for the next three years, leading to a higher dividend yield and slightly lower net income. We reiterate our Buy rating and PO of R$22.

Exhibit 22: We reduce our net income for TIM as we incorporate higher dividends
TIM's old Vs New estimates

	New			Old			% chg.			Consensus			New vs. Consensus		
	2024E	2025E	2026E	2024E	2025E	2026E	2024E	2025E	2026E	2024E	2025E	2026E	2024E	2025E	2024E
Revenue	25,415	26,723	27,969	25,415	26,723	27,969	0.0%	0.0%	0.0%	25,295	26,516	27,771	0.5%	0.8%	0.7%
EBITDA (adjusted)	12,600	13,375	14,082	12,600	13,375	14,082	0.0%	0.0%	0.0%	12,585	13,330	14,023	0.1%	0.3%	0.4%
EBITDA margin	*49.6%*	*50.1%*	*50.3%*	*49.6%*	*50.1%*	*50.3%*	*0bps*	*0bps*	*0bps*	*49.8%*	*50.3%*	*50.5%*	*-17bps*	*-22bps*	*-15bps*
Net profit (reported)	3,538	4,422	4,925	3,538	4,437	4,983	0.0%	-0.3%	-1.2%	3,409	4,192	4,887	3.8%	5.5%	0.7%
EPS (stated)	1.46	1.83	2.03	1.46	1.83	2.06	0.0%	-0.3%	-1.2%	1.41	1.73	2.02	3.8%	5.5%	0.7%

Source: Bloomberg; BofA Global Research

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Exhibit 23: Stocks mentioned
Prices and ratings for stocks mentioned in the report

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
AMX	AMX US	America Movil	US$ 19.11	B-1-7
AMXVF	AMXB MM	America Movil	MXN 16.07	C-1-7
VIV	VIV US	Telefonica Brasil	US$ 10.54	B-1-7
XCPTF	VIVT3 BZ	Telefonica Brasil	BRL 52.31	B-1-7
TIMB	TIMB US	TIM Brasil	US$ 18.97	B-1-7
XZUAF	TIMS3 BZ	TIM Brasil	BRL 18.95	B-1-7

Source: BofA Global Research

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Price objective basis & risk

America Movil (AMXVF / AMX)

Our price objective of MXN21/US$24 per share is based on a 10-year DCF-to-Firm, discounted at a weighted average cost of capital (WACC) of 9.5%, assuming a capital structure of 75% equity / 25% debt in the long term. Our cost of equity (Ke) is composed of a Beta of 0.95, a risk-free rate of 3%, a market risk premium of 6% and a country risk in Mexico of 150bps. We use cost of debt of 4.2% and terminal growth rate of 3%.

Downside risks: (i) macro scenario in its key markets, (ii) regulation in MX, (iii) stronger-than-expected competition for Telcel.

Upside risks: (i) faster-than-expected growth for Telcel due to low competition, (ii) higher synergies from the acquisition of Oi's assets in Brazil and (iii) higher demand in Brazil for both fixed and mobile due to the ICMS reduction

Telefonica Brasil (XCPTF / VIV)

Our price objective of R$64/US$13 per share is based on a 10-year DCF-to-Firm, discounted at a weighted average cost of capital (WACC) of 12.5%, assuming a capital structure of 95% equity / 5% debt in the long term. Our cost of equity (Ke) is composed of a Beta of 0.80, a risk-free rate of 3%, a market risk premium of 5.7% and a country risk in Brazil of 280bps. We use cost of debt of 5% and terminal growth rate of 3%.

Risks: (i) limited benefit from the macroeconomic recovery given its premium customer base, (ii) legacy business continues to pressure top-line growth, (iii) price pressure in the mobile segment given the highest ARPU in the space, (iv) creation of dividend tax would strongly impact Vivo.

TIM Brasil (XZUAF / TIMB)

Our price objective of R$22/US$22 per share is based on a ten-year DCF-to-Firm, discounted at a weighted average cost of capital (WACC) of 12.3%, assuming a capital structure of 90% equity / 10% debt in the long term. Our cost of equity (Ke) is composed of a Beta of 0,90, a risk-free rate of 3%, a market risk premium of 5.7% and country risk in Brazil of 280bps. We use cost of debt of 5% and terminal growth rate of 3%.

Upside risks: (i) leaner than its peers in terms of systems since Pay TV and fixed telephony are irrelevant, (ii) major beneficiary from potential synergies with Oi, (iii) establishment of new fronts of revenue growth, such as the partnership with C6 Bank or advertising, (iv) potential to benefit the most in a scenario of macro recovery, (v) run sharing agreement with Vivo, which should lead to opex and capex savings.

Downside risks: (i) limited growth for the sector puts pressure on prices, (ii) net adds, which have been weak over the last two years, leading to market share losses, (iii) inefficient capital structure, as its controlling shareholder is highly leveraged, (iv) reduced focus on FTTH, which is a high-growth business but still too small for the company.

Analyst Certification

We, Fred Mendes, CFA, Gustavo Tiseo, Lucca R Brendim and Mirela Oliveira, hereby certify that the views each of us has expressed in this research report accurately reflect each of our respective personal views about the subject securities and issuers. We also certify that no part of our respective compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

Special Disclosures

BofA Securities is currently acting as advisor to Cassa Depositi e Prestiti SpA in connection with its proposed non-binding offer jointly with Macquarie Asset Management, for the acquisition of Telecom Italia's NetCo, which was announced on March 5, 2023.Any proposed transaction is expected to be subject to approval by shareholders of Telecom Italia.This research report is not intended to provide voting advice, serve as an endorsement of the proposed transaction, or result in the procurement, withholding or revocation of a proxy.

BofA Securities is currently acting as Financial Advisor to Telefonica SA in connection with its voluntary public cash offer for outstanding shares of Telefonica Deutschland Holding AG, which was announced on November 7, 2023.

Latin America - Telecom Services and Information Technology Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	America Movil	AMX	AMX US	Fred Mendes, CFA
	America Movil	AMXVF	AMXB MM	Fred Mendes, CFA
	Desktop S.A	XNUKF	DESK3 BZ	Fred Mendes, CFA
	Eletromidia	XSUHF	ELMD3 BZ	Fred Mendes, CFA
	Locaweb	XZVMF	LWSA3 BZ	Fred Mendes, CFA
	Telefonica Brasil	XCPTF	VIVT3 BZ	Fred Mendes, CFA
	Telefonica Brasil	VIV	VIV US	Fred Mendes, CFA
	Televisa	TV	TV US	Fred Mendes, CFA
	Televisa	GRPFF	TLEVICPO MM	Fred Mendes, CFA
	TIM Brasil	TIMB	TIMB US	Fred Mendes, CFA
	TIM Brasil	XZUAF	TIMS3 BZ	Fred Mendes, CFA
	TOTVS	XBEGF	TOTS3 BZ	Fred Mendes, CFA
	VTEX	VTEX	VTEX US	Fred Mendes, CFA
NEUTRAL				
	Intelbras S.A.	XLTXF	INTB3 BZ	Fred Mendes, CFA
UNDERPERFORM				
	Brisanet	XNHKF	BRIT3 BZ	Fred Mendes, CFA
	Megacable Holdings SAB	MHSDF	MEGACPO MM	Fred Mendes, CFA
	Unifique S.A	XFYDF	FIQE3 BZ	Fred Mendes, CFA

Disclosures

Important Disclosures

Equity Investment Rating Distribution: Media & Entertainment Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships R1	Count	Percent
Buy	35	53.85%	Buy	15	42.86%
Hold	15	23.08%	Hold	8	53.33%
Sell	15	23.08%	Sell	7	46.67%

Equity Investment Rating Distribution: Technology Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships R1	Count	Percent
Buy	215	53.09%	Buy	111	51.63%
Hold	97	23.95%	Hold	45	46.39%
Sell	93	22.96%	Sell	24	25.81%

Equity Investment Rating Distribution: Telecommunications Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships R1	Count	Percent
Buy	57	51.82%	Buy	43	75.44%
Hold	27	24.55%	Hold	17	62.96%
Sell	26	23.64%	Sell	12	46.15%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships R1	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

R1 Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster[R2]
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

[R2]Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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