# Vodafone Group

# New Vodafone – proforma cash/divi/leverage analysis

**Reiterate Rating: BUY | PO: 120.00 GBp | Price: 70.49 GBp**

15 March 2024

Equity

## Investors look to be paid (handsomely) to wait for cash inflection

Vodafone has announced the sale of Italy as the final major step of its portfolio restructuring following the sale of Spain and proposed UK merger. Cash flow dilution is material with asset sales, and thus VOD has rebased its dividend, but added E4bn buyback from proceeds. This means investors should be paid handsomely, c15% implied returns in FY25 and FY26 as cash flows rebase and inflect to grow once more into FY27. Equity free cash flow yield bottoms 8.4% at current share price, moves back to double digit from FY 28. Vodafone looks increasingly right-sized and incrementally progressive on B2B opportunities and the commercialisation of its central services. A change in management in Germany remains the one concern with a volatile year ahead. We modify our PO slightly to 120p on Italian valuation. Meanwhile our ADR PO goes from $13.22 to $15.3 as we reset currency (using an FX of GBP/USD 1.275). Current forecasts are pre deal closure/pre divi cut, proforma 'new Vodafone' modelled within. Buy.

## Cash flow / dividend / leverage implications

We model group cash flow implications with: 1) 3-year average dilution c32%, 2) peak FY26 dilution of 44% as Italy is sold / UK absorbs integration costs, 3) Longer-term FY30 dilution 10% as UK synergies accrue. Thus VOD has reshaped dividend -50% to ensure sustainable cover at peak, and added E4bn buyback from proceeds beyond its current comfortable 2.5x leverage. We model an increasingly well covered dividend and deleverage mid-term to ensure a 2.5x level with the Hutch minority acquisition FY2029. Additional returns are thus possible under the new 2.25-2.75 range, also with further restructuring, Vantage Towers etc. Note: we maintain current dividend forecast ahead of imminent deal closure, proforma analysis within.

## Investor call feedback

Management feedback from the post deal investor call: 1) Ambition to cover dividend well and with room to grow, 2) Sell vs. joint venture in Italy based on superior combination of value creation vs. proceeds vs. transaction certainty, 3) German building blocks in place to grow, expect growth acceleration, 4) Could extend service contract with Swisscom on shared operations beyond Italy e.g. IoT Swiss.

| **Estimates (Mar) (EUR)** | **2022A** | **2023A** | **2024E** | **2025E** | **2026E** |
|---|---|---|---|---|---|
| EPS (Adjusted Diluted) | 0.10 | 0.43 | 0.06 | 0.08 | 0.09 |
| EPS Change (YoY) | 427.7% | 346.7% | -85.2% | 23.7% | 11.0% |
| Dividend / Share | 0.09 | 0.09 | 0.09 | 0.09 | 0.09 |
| ADR EPS (Adjusted Diluted - US$) | 1.11 | 4.44 | 0.69 | 0.85 | 0.95 |
| ADR Dividend / Share (US$) | 1.05 | 0.94 | 0.98 | 0.98 | 0.98 |
| **Valuation (Mar)** | | | | | |
| P/E | 8.73x | 1.88x | 13.0x | 10.5x | 9.49x |
| Dividend Yield | 10.9% | 10.9% | 10.9% | 10.9% | 10.9% |
| EV / EBITDA* | 6.03x | 6.25x | 7.07x | 6.97x | 6.92x |
| Free Cash Flow Yield* | 21.7% | 19.7% | 13.7% | 14.8% | 15.3% |

* For full definitions of *iQmethod*℠ measures, see page 11.

### Key Changes

| (EUR) | Previous | Current |
|---|---|---|
| Price Obj. | 122.00p | 120.00p |

**David Wright** >>
Research Analyst
MLI (UK)
+44 20 7995 6355
dawright@bofa.com

**Titus Krahn** >>
Research Analyst
MLI (UK)
titus.krahn@bofa.com

### Stock Data

| | |
|---|---|
| Price (Common / ADR) | 70.49 GBp / 9.02 USD |
| Price Objective | 120.00 GBp / 15.30 USD |
| Date Established | 15-Mar-2024 / 15-Mar-2024 |
| Investment Opinion | B-1-8 / B-1-8 |
| 52-Week Range | 62.71 GBp-97.23 GBp |
| Market Value (mn) | 19,089 GBP |
| Shares Outstanding (mn) | 27,080.0 / 2,708.0 |
| Average Daily Value (mn) | 73.36 USD |
| Free Float | 95.0% |
| BofA Ticker / Exchange | VODPF / LSE |
| BofA Ticker / Exchange | VOD / NAS |
| Bloomberg / Reuters | VOD LN / VOD.L |
| ROE (2024E) | 2.8% |
| Net Dbt to Eqty (Mar-2023A) | 84.8% |
| ESGMeter™ | High |

**ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BofA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company.** For full details, refer to "BofA ESGMeter Methodology".

# *iQprofile*℠ Vodafone Group

| Key Income Statement Data (Mar) | 2022A | 2023A | 2024E | 2025E | 2026E |
|---|---|---|---|---|---|
| **(EUR Millions)** | | | | | |
| Sales | 45,580 | 45,706 | 44,168 | 44,502 | 44,538 |
| EBITDA Adjusted | 15,208 | 14,665 | 12,978 | 13,157 | 13,251 |
| Depreciation & Amortization | (9,858) | (9,649) | (9,114) | (8,787) | (8,655) |
| EBIT Adjusted | 5,350 | 5,016 | 3,865 | 4,369 | 4,596 |
| Net Interest & Other Income | (1,710) | (1,480) | (1,700) | (1,709) | (1,716) |
| Tax Expense / Benefit | (1,330) | (481) | (574) | (705) | (771) |
| Net Income (Adjusted) | 2,773 | 11,818 | 1,753 | 2,168 | 2,406 |
| Average Fully Diluted Shares Outstanding | 29,012 | 27,680 | 27,680 | 27,680 | 27,680 |
| **Key Cash Flow Statement Data** | | | | | |
| Net Income (Reported) | 3,309 | 11,818 | 1,753 | 2,168 | 2,406 |
| Depreciation & Amortization | 9,858 | 9,649 | 9,114 | 8,787 | 8,655 |
| Change in Working Capital | (31.0) | 256 | (175) | (75.0) | 0 |
| Deferred Taxation Charge | 0 | 0 | 0 | 0 | 0 |
| Other CFO | (224) | (9,464) | (584) | (449) | (341) |
| **Cash Flow from Operations** | **12,912** | **12,259** | **10,108** | **10,432** | **10,721** |
| Capital Expenditure | (8,306) | (8,378) | (7,609) | (7,430) | (7,490) |
| (Acquisition) / Disposal of Investments | NA | NA | NA | NA | NA |
| Other CFI | 101 | 11,909 | 187 | 37.4 | 87.4 |
| **Cash Flow from Investing** | **(8,205)** | **3,531** | **(7,421)** | **(7,393)** | **(7,402)** |
| Share Issue / (Repurchase) | (2,029) | (1,893) | 0 | 0 | 0 |
| Cost of Dividends Paid | (539) | (400) | (500) | (504) | (533) |
| Increase (decrease) debt | 2,332 | (3,702) | 305 | (43.0) | (295) |
| Other CFF | (4,785) | 3,629 | (2,796) | (2,448) | (2,196) |
| **Cash Flow from Financing** | **(5,021)** | **(2,366)** | **(2,992)** | **(2,995)** | **(3,024)** |
| **Total Cash Flow (CFO + CFI + CFF)** | **(314)** | **13,424** | **(305)** | **43.0** | **295** |
| FX and other changes to cash | 1,989 | (9,215) | 305 | (43.0) | (295) |
| Change in Cash | 1,675 | 4,209 | 0 | 0 | 0 |
| Change in Net Debt | 657 | (7,911) | 305 | (43.0) | (295) |
| Net Debt (Reported) | 62,596 | 54,685 | 54,990 | 54,947 | 54,652 |
| Net Debt (Adjusted) | 41,578 | 33,375 | 33,680 | 33,637 | 33,342 |
| **Key Balance Sheet Data** | | | | | |
| Property, Plant & Equipment | 40,804 | 37,992 | 38,310 | 38,711 | 39,276 |
| Goodwill | 31,884 | 27,615 | 27,615 | 27,615 | 27,615 |
| Other Intangibles | 21,360 | 19,592 | 18,069 | 16,612 | 15,181 |
| Other Non-Current Assets | 31,368 | 39,660 | 39,431 | 39,218 | 38,921 |
| Trade Receivables | 11,019 | 10,705 | 10,705 | 10,705 | 10,705 |
| Cash & Equivalents | 7,496 | 11,705 | 11,705 | 11,705 | 11,705 |
| Other Current Assets | 10,022 | 8,252 | 8,252 | 8,252 | 8,252 |
| Total Assets | 153,953 | 155,521 | 154,087 | 152,817 | 151,655 |
| Long-Term Debt | 58,131 | 51,669 | 51,974 | 51,931 | 51,636 |
| Other Non-Current Liabilities | 5,198 | 4,785 | 4,785 | 4,785 | 4,785 |
| Short-Term Debt | 11,961 | 14,721 | 14,721 | 14,721 | 14,721 |
| Other Current Liabilities | 21,686 | 19,863 | 20,013 | 20,163 | 20,313 |
| Total Liabilities | 96,976 | 91,038 | 91,493 | 91,600 | 91,455 |
| Total Equity | 56,977 | 64,483 | 62,595 | 61,217 | 60,200 |
| Total Equity & Liabilities | 153,953 | 155,521 | 154,087 | 152,817 | 151,655 |
| **Business Performance*** | | | | | |
| Return On Capital Employed | 2.71% | 3.37% | 2.16% | 2.47% | 2.64% |
| Return On Equity | 5.02% | 20.0% | 2.80% | 3.52% | 3.95% |
| Operating Margin | 11.9% | 30.3% | 8.75% | 9.82% | 10.3% |
| Free Cash Flow (MM) | 5,193 | 4,508 | 3,137 | 3,384 | 3,486 |
| **Quality of Earnings*** | | | | | |
| Cash Realization Ratio | 4.66x | 1.04x | 5.77x | 4.81x | 4.46x |
| Asset Replacement Ratio | 0.84x | 0.87x | 0.83x | 0.85x | 0.87x |
| Tax Rate | 32.4% | 3.75% | 24.7% | 24.5% | 24.3% |
| Net Debt/Equity | 110% | 84.8% | 87.9% | 89.8% | 90.8% |
| Interest Cover | 2.72x | 2.90x | 2.27x | 2.56x | 2.68x |

* For full definitions of *iQmethod*℠ measures, see page 11.

## Company Sector

Telecom Services-Wireless/Cellular

## Company Description

Vodafone provides telecoms services, including mobile voice, data and fixed communications. The Group has c450m fixed and mobile customers, with operations across more than 30 countries worldwide. Its main European businesses are in Germany, Italy, Spain, the UK. The UK-listed company also has an extensive EM portfolio, with exposure to wireless businesses in India, and S Africa.

## Investment Rationale

We rate Vodafone Buy. Restructuring is complex and Germany faces operational headwinds. However, looking through the complexity we envisage a new, more constructive shareholder remuneration policy and portfolio restructuring to provide scale and support better returns., or to exit where there is no route to do so.

## Stock Data

| | |
|---|---|
| Shares / ADR | 10.00 |
| Price to Book Value | 0.4x |

## Key Changes

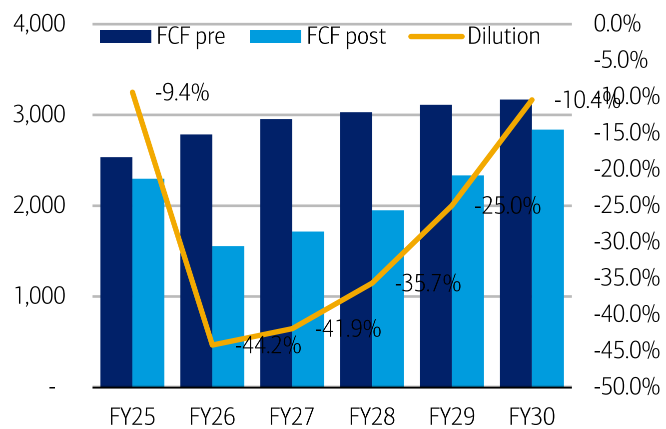
| (US$) | Previous | Current |
|---|---|---|
| Price Obj. | 13.22 | 15.30 |

# Investment conclusions

Following the announcement of a sale of Vodafone Italy to Swisscom and new capital allocation policy we revisit our analysis of Vodafone proforma free cash flows, leverage and implied valuation.

Our conclusion is that distributable free cash flow is diluted around 10% by the sale of Spain in FY25 (assuming imminent closure) although this does unwind over time with improved coupons on preference equity. Closure of Italy due calendar Q1 2025 dilutes cash flows a further 13-14% from FY26. Analysis indicates the UK merger (assuming regulatory approval) should be an incremental 23% dilution in FY26 as initial restructuring costs weigh heavily (aggregate group peak cash flow dilution c44% FY26) although this too unwinds as synergies accrue into UK cash flow accretion by FY29. We forecast longer-term group FCF dilution of 8% versus pre-deal levels.

**Exhibit 1: Distributable FCF – pre/post Spain/Italy/UK M&A**
Post M&A FCF below current divi payout, compelling rebase




**Source:** BofA Global Research estimates, company report

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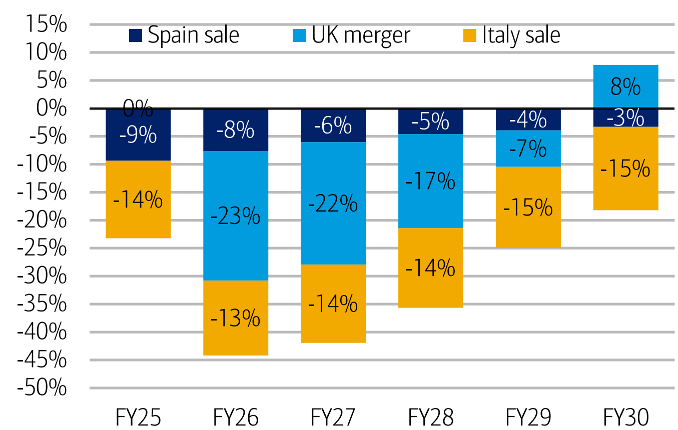
**Exhibit 2: Distributable FCF dilution– Spain/Italy/UK composition**
Spain initially 10% dilutive, unwinds with preference equity coupons, Italy stable dilution, UK dilution initially higher with £500m integration costs before Y5 £700m synergy accrual.




**Source:** BofA Global Research estimates, company report

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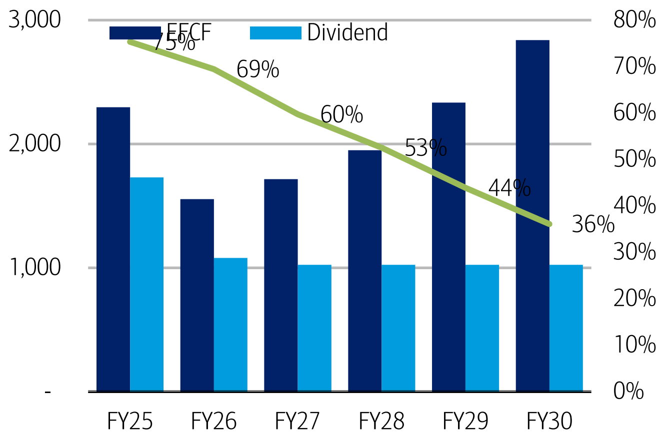
Adding Vodafone's new capital allocation policy with a 50% cut to E4.5c dividend per share and incremental E4bn buyback (E2bn post Spain est FY 25, E2bn post Italy est FY26), we model payout and net debt evolution as follows:

**Exhibit 3: Group divi outflows/payout versus proforma cash flows assuming buyback at 70p/sh**

Dividend outflow post buyback well covered even at peak cash flow dilution in FY26 as Italy is deconsolidated and the UK is initially dilutive. Note FY25 outflow higher as comprises previous final dividend policy.




**Source:** BofA Global Research estimates

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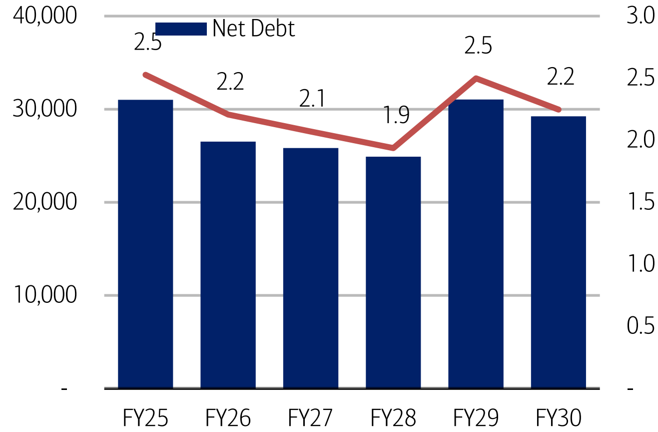
**Exhibit 4: Group Net Debt/leverage evolution, EURm**

Leverage trends lower, sub 2x but back to mid-range with the Hutch minority buyout (puts/calls +3years from expected FY26 completion).




**Source:** BofA Global Research estimates

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## Valuation implications

We present proforma valuation analysis, with forward market cap and net debt (est VOD at 70p/share). Conclusions:

- EV/EBITDA, initially cheap, gaps upwards in FY29 with the higher multiple acquisition of Hutch minorities.
- Cash yields move lower into peak dilution FY26 before recovering over time.

**Exhibit 5: Proforma valuation, EURm**

Cash multiples gap lower into peak dilution before recovering over time.

| | FY 24 | FY25 | FY26 | FY27 | FY28 | FY29 | FY30 |
|---|---|---|---|---|---|---|---|
| Price | | 0.70 | 0.70 | 0.70 | 0.70 | 0.70 | 0.70 |
| Shares | | 25,224 | 22,768 | 22,768 | 22,768 | 22,768 | 22,768 |
| Market cap | | 17,657 | 15,938 | 15,938 | 15,938 | 15,938 | 15,938 |
| EUR | | 20,542 | 18,542 | 18,542 | 18,542 | 18,542 | 18,542 |
| Net Debt | | 31,014 | 26,518 | 25,827 | 24,902 | 31,040 | 29,226 |
| Leverage | | 2.5 | 2.2 | 2.1 | 1.9 | 2.5 | 2.2 |
| EV | | 51,556 | 45,060 | 44,369 | 43,444 | 49,582 | 47,768 |
| Less UK minority debt | | 51,556 | 41,580 | 40,837 | 39,934 | 49,582 | 47,768 |
| EBITDA | | 12,274 | 10,441 | 10,770 | 11,047 | 12,426 | 13,008 |
| EV/EBITDA | | 4.2 | 4.0 | 3.8 | 3.6 | 4.0 | 3.7 |
| FFCF | | 3,072 | 2,218 | 2,361 | 2,573 | 3,110 | 3,569 |
| EV/FFCF | | 6.0% | 4.9% | 5.3% | 5.9% | 6.3% | 7.5% |
| EFCF | | 2,297 | 1,555 | 1,716 | 1,950 | 2,334 | 2,839 |
| EFCF Yield | | 11.2% | 8.4% | 9.3% | 10.5% | 12.6% | 15.3% |
| DPS, EUR | | 4.5 | 4.5 | 4.5 | 4.5 | 4.5 | 4.5 |
| Divi Yield | | 5.5% | 5.5% | 5.5% | 5.5% | 5.5% | 5.5% |

**Source:** BofA Global Research estimates

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## Reiterate Buy; SOTP-based PO to 120p; adjusting ADR PO on FX

Vodafone's capital allocation rebase is not materially different from previous analysis and derives a more sustainable dividend profile while returning excess cash to shareholders. We also take a favourable view of a cleaner portfolio structure with scale assets, deriving positive return on capital vs. hurdle over time. Moves into B2B are also progressive, as is the commercialisation of central functions.

An existing concern is the organic growth prospects of Germany with management changed, and a tough year ahead with TV and housing association impact. We also flag the need for fibre investment over time.

*Note: current published forecasts are unadjusted ahead of deal closure in Spain. Thus we present proforma adjusted numbers in this research. Sum of part PO moves to 120p (from 1229) on Italian valuation, ADR moves to $15.3 as we reset currency adjustment GBPUSD 1.275.*

# Proforma analysis

Forecasting the financial outlook for Vodafone is complex and uncertain given that there are deals agreed and close to completion (Spain), deals proposed but not yet approved from a regulatory standpoint (UK) and deals that are in latter stages of negotiation (Italy).

This presents a challenge for Vodafone that has committed to reviewing its capital allocation policy following portfolio restructuring. Our view is that Vodafone would prefer to reset expectations and provide stability rather than constantly adjusting its policy after each deal. Thus, we put ourselves in Vodafone's shoes (so to speak), modelling what we think are the more likely transactions to complete, and what the implications could be.

To recap recent (material) M&A deals and discussions:

- **Spain**: Vodafone announced the sale of Spanish operations to Zegona in October 2023 for E5bn (implied 5.3x EV/EBITDAaL) comprising E4.1bn cash proceeds and E900m redeemable preference shares with a yield of 5% in years 1-3, then 10%/12.5%/15% thereafter. VOD will retain annual service fees of E110m. With no regulation due the deal is expected to close in calendar Q1 2024.

  *We expect this deal to complete at any time, with buyer funds raised and no regulatory complications.*

- **UK**: VOD announced a proposed merger with Hutch's Three in the UK in June 2023. Both companies will inject Debt (VOD £4.3bn, Hutch £1.7bn) to balance a 51:49 shareholding in favour of VOD who will consolidate the operation. The merger is expected to deliver £700m OpFCF synergy from Year 5 with £500m interrogation costs in the near-term. FCF should positive by year 4. Then both VOD and Hutch have call/put options on the Hutch stake 3 years post completion. Deal completion is expected by end of calendar 2024 as it requires regulatory approval form the UK CMA (competition market authority).

  *UK regulatory commentary is that absolute number of mobile operators (this would represent a 4-3 network consolidation) is not a primary driver of competitive analysis. And while VOD/Three would derive an outsized operator with c44% mobile subscriber share, it would be mobile only versus converged competitors BT and VMO2, thus more balanced on a service revenue basis. There could be remedies around spectrum caps but we believe this deal has a good likelihood of completion.*

- **Italy**: VOD and Swisscom have announced they are in final discussions for a sale of Vodafone operations to Swisscom for E8bn. There are no indications of any resolution regarding potential service fees in a manner similar to Spain, although Vodafone does disclose around E100m non-cash itesm in EBITDAaL (to deduct when considering fre cash flow dilution).

  *Headline 7.6x EBITDA valuation is reasonable but aggregate proceeds of E8bn are significantly below the E10-11bn valuation8 offered by Iliad, albeit in more complex form with the recently proposed JV. Vodafone's approach to value vs. time to deliver value vs. regulatory outlook seems to have tipped in favour of an exit, with an Iliad deal sure to have faced significant regulatory hurdles.*

In conclusion, our approach to a 24-36m outlook that could shape policy is to consider the Spanish, Italian and UK deals, with the caveat that any one could break-down and/or change shape.

## Proforma model

Our analysis begins with YE 2024 group unadjusted forecasts then we deduct Spain (impact March YE 25), Italy (impact March YE 26), deduct standalone UK (impact March YE 26), add-back merged UK (impact March YE 26) and model the impact on cash flows and leverage. Based on these we consider the potential for adjustments to cash returns.

### Underlying assumptions

The following table comprises our forecasts for VOD Group (untouched and published), VOD Spain, VOD UK and merged UK operations. Some core assumptions:

- Spain standalone: We use current forecasts for Spain EBITDAaL and Capex, but assume no cash tax per company commentary (and supported by multiple losses at ONO). We do not consider debt, as we include the net benefits of sale proceeds as a separate line in the cash flow analysis.

- Italy standalone: We use current forecasts for Spain EBITDAaL and Capex, deducting the E97m disclosed non-cash element, while we assume around E50m cash tax paid historically (and thus reducing net cash outflows). Simialr to Spain, we do not consider debt, as we include the net benefits of sale proceeds as a separate line in the cash flow analysis.

- UK standalone: We use current forecasts for UK EBITDAaL and Capex, and assume an interest charge based on the £4.3bn debt associated with VOD UK that will be injected into the merged entity (at VOD Group 2.5% cost of debt). Again we assume limited cash tax.

- Merged UK: We incorporate current VOD UK EBITDAaL and Capex forecasts and those for Hutch UK (we consider reported data but normalise EBITDAaL for consistent SAC accounting, c40% lower). Then, per deal reports, we assume: 1) guidance for £700m OpFCF synergy phased into full runrate by year 5 (we assume 2/3 opex, 1/3 capex per previous precedent) and more up-front phased £500m integration costs, 2) £6bn debt (4.3 VOD 1.7 Hutch) associated with the merged entity at 2.5% cost of debt, 3) no cash taxes until material free cash flow positive in year 5, 4) no cash distribution until <2.5x leverage by year 5. We include a simple working to convert UK Merged EBITDA and FCF to EUR per forecast FX.

**Exhibit 6: Underlying assumptions, Group untouched / Spain / Italy (both EURm), UK standalone / UK merged (both £m)**
Building inputs to a proforma model

| **Group untouched, EUR** | **FY24** | **FY25** | **FY26** | **FY27** | **FY28** | **FY29** | **FY30** |
|---|---|---|---|---|---|---|---|
| EBITDAaL | 12,978 | 13,157 | 13,251 | 13,659 | 13,979 | 14,313 | 14,626 |
| FCF VOD | 3,137 | 3,384 | 3,486 | 3,554 | 3,631 | 3,711 | 3,769 |
| FCF clean | 2,187 | 2,534 | 2,786 | 2,954 | 3,031 | 3,111 | 3,169 |
| Net Debt | 33,680 | 33,637 | 33,342 | 32,879 | 32,339 | 31,720 | 31,042 |
| Leverage | 2.6 | 2.6 | 2.5 | 2.4 | 2.3 | 2.2 | 2.1 |
| **SPAIN standalone, EUR** | **Assumptions** | **FY25** | **FY26** | **FY27** | **FY28** | **FY29** | **FY30** |
| EBITDAaL | | 883 | 897 | 911 | 926 | 941 | 956 |
| Capex | | -498 | -537 | -585 | -594 | -604 | -614 |
| OpFCF | | 385 | 360 | 326 | 332 | 337 | 342 |
| Taxed | 0% | 385 | 360 | 326 | 332 | 337 | 342 |
| **ITALY standalone, EUR** | | FY25 | FY26 | FY27 | FY28 | FY29 | FY30 |
| EBITDAaL | | 1,388 | 1,425 | 1,488 | 1,528 | 1,570 | 1,614 |
| Non-cash | | - 97 | -97 | -97 | -97 | -97 | -97 |
| Capex | | -712 | -724 | -744 | - 764 | -785 | -807 |
| OpFCF | | 579 | 603 | 647 | 667 | 688 | 710 |
| Taxed | 8% | 536 | 558 | 598 | 617 | 637 | 657 |
| **UK standalone, £** | **Assumptions** | **FY25** | **FY26** | **FY27** | **FY28** | **FY29** | **FY30** |
| EBITDAaL | | 1,198 | 1,241 | 1,269 | 1,298 | 1,328 | 1,358 |

**Exhibit 6: Underlying assumptions, Group untouched / Spain / Italy (both EURm), UK standalone / UK merged (both £m)**
Building inputs to a proforma model

| **Group untouched, EUR** | **FY24** | **FY25** | **FY26** | **FY27** | **FY28** | **FY29** | **FY30** |
|---|---|---|---|---|---|---|---|
| Capex | | -667 | -682 | -698 | -714 | -730 | -747 |
| OpFCF | | 531 | 558 | 571 | 584 | 598 | 611 |
| Interest, £4.3bn | 2.5% | -108 | -108 | -108 | -108 | -108 | -108 |
| Taxed FCF | 0% | 423 | 451 | 464 | 477 | 490 | 504 |
| EUR | | 492 | 524 | 539 | 555 | 570 | 586 |
| **UK Merged, £** | **Assumptions** | | **FY 26** | **FY 27** | **FY 28** | **FY 29** | **FY 30** |
| EBITDAaL | | | 1,459 | 1,463 | 1,590 | 1,865 | 2,177 |
| VOD | | | 1,241 | 1,269 | 1,298 | 1,328 | 1,358 |
| Less VOD charges | | | | - | - | - | - |
| Hutch | | | 345 | 347 | 349 | 350 | 352 |
| Synergy (opex 2/3) | 467 | | 23 | 47 | 93 | 187 | 467 |
| runrate | | | 5% | 10% | 20% | 40% | 100% |
| Integration | -500 | | -150 | -200 | -150 | | |
| Capex | | | -1,414 | -1,402 | -1,392 | -1,361 | -1,236 |
| VOD | | | -682 | -682 | - 698 | -714 | -730 |
| Hutch | | | -743 | -743 | -741 | -740 | -739 |
| Synergy (capex 2/3) | 233 | | 12 | 23 | 47 | 93 | 233 |
| **OpFCF** | | | **46** | **61** | **198** | **504** | **941** |
| Interest | | | -150 | -153 | -155 | -154 | -146 |
| Tax | 10% | | - | - | -4 | -35 | -80 |
| **FCF** | | | **-104** | **-92** | **39** | **315** | **716** |
| Distribution | | | | | | | -400 |
| **Net Debt** | **6,000** | | **6,104** | **6,196** | **6,158** | **5,843** | **5,527** |
| Leverage x | 0.0 | | 4.2 | 4.2 | 3.9 | 3.1 | 2.5 |
| EUR | | 0.86 | 0.86 | 0.86 | 0.86 | 0.86 | 0.86 |
| EBITDA | | | 1,698 | 1,702 | 1,850 | 2,170 | 2,533 |
| FCF | | | -122 | -107 | 45 | 367 | 832 |

**Source:** BofA Global Research estimates

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## EBITDAaL impact (used within leverage)

Based on the assumptions above, we illustrate current untouched group EBITDAal forecasts, then:

- Deduct Spain EBIDTAaL from FY25, Italy FY26
- Add back newly consolidated Hutch EBITDAaL from FY26 and synergy (note that integration costs will not be reported at EBITDA but in restructuring cash flows).

We also present proportionate EBITDAaL given the 51% UK ownership from FY26.

**Exhibit 7: Group EBITDAaL impact, EURm**
Proforma = group untouched – Spain FY25 – Italy FY25 + new UK /synergy FY26

| | **FY24** | **FY25** | **FY26** | **FY27** | **FY28** | **FY29** | **FY30** |
|---|---|---|---|---|---|---|---|
| **EBITDAaL pre** | **12,978** | **13,157** | **13,251** | **13,659** | **13,979** | **14,313** | **14,626** |
| Spain, less EBITDAaL | | -883 | -897 | -911 | -926 | -941 | -956 |
| Italy, less EBITDAaL | | | -1,425 | -1,488 | -1,528 | -1,570 | -1,614 |
| UK, add Hutch consol | | | 402 | 404 | 406 | 408 | 410 |
| UK, add synergy | | | 27 | 54 | 109 | 217 | 543 |
| **EBITDAaL post** | **12,978** | **12,274** | **11,358** | **11,718** | **12,039** | **12,426** | **13,008** |
| proportional | | 12,274 | 10,441 | 10,770 | 11,047 | 12,426 | 13,008 |

**Source:** BofA Global Research estimates

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## Free cash flow impact

Based on the assumptions above, we illustrate VOD's untouched 'guidance' free cash flow forecasts for comparability, but start from distributable free cash flow forecasts that include restructuring charges and spectrum, then:

- Deduct Spanish cash flow from FY25, Italy FY26.
- Add back the interest benefit (at VOD's 2.5% cost of debt) on E4.1bn cash consideration from Spain, and coupons on the E900m deferral (5% years 1-3, then 10%, 12.5/15% thereafter).
- Add back the interest benefit (at VOD's 2.5% cost of debt) on E8bn cash consideration from Italy.
- Deduct standalone UK free cash flow from FY26, add back the merged entity free cash flow (initially dilutive, this includes restructuring charges).

We measure dilution, with Spain c9% but unwinding with deferred proceeds, Italy broadly stable at 13-14%, and the UK initially 23% (contributing to peak FY26 dilution close to 50%) before normalising by year 4, more substantially cash flow positive by year 5.

**Exhibit 8: Group free cash flow impact, EURm**

proforma = Group untouched – Spain OpFCF + proceeds – Italy OpFCF + proceeds - UK standalone + UK merged

| **FCF pre** | **FY24** | **FY25** | **FY26** | **FY27** | **FY28** | **FY29** | **FY30** |
|---|---|---|---|---|---|---|---|
| FCF pre - VOD | 3,137 | 3,384 | 3,486 | 3,554 | 3,631 | 3,711 | 3,769 |
| FCF pre - clean (ex restructure/spec) | 2,187 | 2,534 | 2,786 | 2,954 | 3,031 | 3,111 | 3,169 |
| Spain, less standalone taxed OpFCF | - | -385 | -360 | -326 | -332 | -337 | -342 |
| Spain, add interest on cash sale | 2.5% | 103 | 103 | 103 | 103 | 103 | 103 |
| Spain, add interest on def sale | 5.0% | 45 | 45 | 45 | 90 | 113 | 135 |
| Italy, less standalone taxed OpFCF | 7.5% | | -558 | -598 | -617 | -637 | -657 |
| Italy, add interest on cash sale | 2.5% | | 185 | 185 | 185 | 185 | 185 |
| UK, less standalone FCF | | | -524 | -539 | -555 | -570 | -586 |
| UK add merger FCF | | | -122 | -107 | 45 | 367 | 832 |
| **FCF post** | | **2,297** | **1,555** | **1,716** | **1,950** | **2,334** | **2,839** |
| dilution | | -9.4% | -44.2% | -41.9% | -35.7% | -25.0% | -10.4% |

**Source:** BofA Global Research estimates, company report

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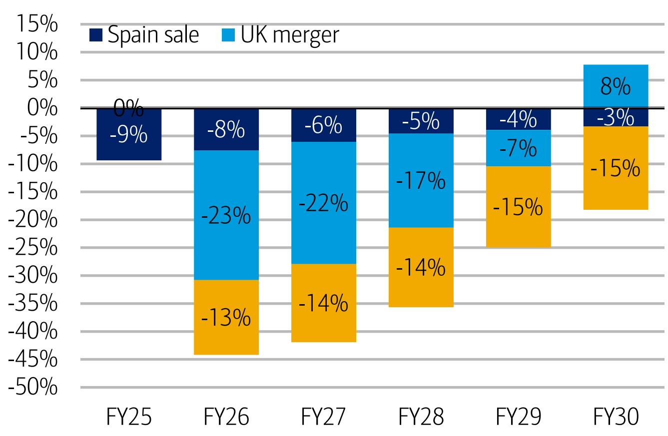
Graphically (and including a reference to current dividend cash outflow):

**Exhibit 9: Distributable FCF – pre/post Spain/Italy/UK M&A**

Post M&A FCF below current divi payout, compelling rebase




**Source:** BofA Global Research estimates

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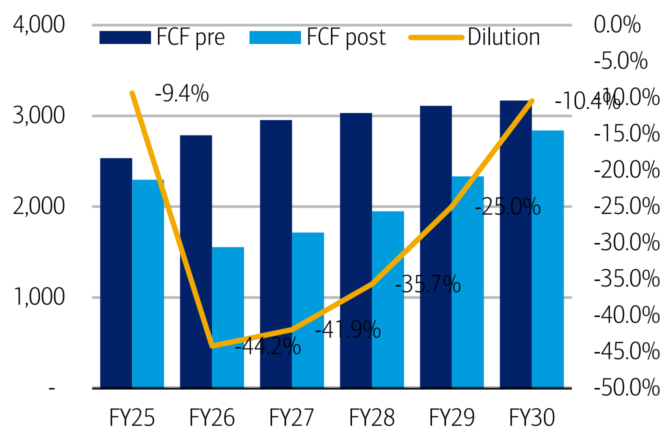
**Exhibit 10: Distributable FCF dilution– Spain/Italy/UK composition**

Spain initially 10% dilutive, unwinds with preference equity coupons, Italy stable dilution, UK dilution initially higher with £500m integration costs before Y5 £700m synergy accrual.




**Source:** BofA Global Research estimates

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### Net Debt impact – new capital allocation profile

Vodafone has announced a new capital return profile with dividend cut 50% to E4.5c guidance and added two buybacks; E2bn post Spain (FY25) and E2bn post Italy (FY 26).

We model net debt on this basis, assuming adjusted free cash flows presented above. Some additional assumptions:

- We base dividend outflow on average shares, assuming 70p/sh (current). Clearly this could moderate.
- FY25 dividend is initially different as it encapsulates the FY24 final of E4.5c (paid June) and we assume new E4.5c annual dividend is paid 50% interim / 50% final per previous policy, so FY25 outflow is a net E7c dividend per share, then new E5c proforma thereafter.

Our conclusion is that a rebased dividend reduces cash flow payout pressure during the initially dilutive M&A period, but that buyback using proceeds should support divi growth during that period ahead of UK cash flow accretion from FY29 onwards that should support more organic growth based on payout.

**Exhibit 11: Group Net Debt impact, dividend cut scenario, EURm**

Deducting Spanish/Italian proceeds (FY25/FY26), adding UK debt (FY26/29), adjusting for new cash flows and buyback/dividend cut

| Net Debt | FY 24 | FY25 | FY26 | FY27 | FY28 | FY29 | FY30 |
|---|---|---|---|---|---|---|---|
| b/f | | 33,680 | 30,474 | 25,977 | 25,287 | 24,362 | 30,500 |
| M&A Spain proceeds | | -4,100 | | | | | |
| M&A Italy proceeds | | | -8,000 | | | | |
| M&A UK new debt | | | 1,978 | | | 7,447 | - |
| Post M&A cash flow | | -2,297 | -1,555 | -1,716 | -1,950 | -2,334 | -2,839 |
| Divi (avg shares) | | 1,190 | 1,080 | 1,025 | 1,025 | 1,025 | 1,025 |
| (divi / FCF payout) | | 52% | 69% | 60% | 53% | 44% | 36% |
| Buyback | | 2,000 | 2,000 | | | | |
| **c/f** | **33,680** | **30,474** | **25,977** | **25,287** | **24,362** | **30,500** | **28,686** |
| Leverage | 2.6 | 2.5 | 2.3 | 2.2 | 2.0 | 2.5 | 2.2 |
| proportionate | | 2.5 | 2.2 | 2.0 | 1.9 | 2.5 | 2.2 |
| Shares | 27,680 | 25,224 | 22,768 | 22,768 | 22,768 | 22,768 | 22,768 |
| Buyback | | -2,456 | -2,456 | | | | |
| Share price (EUR) | | 81 | 81 | | | | |
| Share price (p) | | 70 | 70 | | | | |

**Source:** BofA Global Research estimates

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# Price objective basis & risk

**Vodafone Group (VODPF / VOD)**

Our 120p PO (US$15.3 ADR, using FX rate of GBPUSD 1.275) is based on a sum-of-the-parts analysis.

We value each of the European subsidiaries (where Vodafone discloses revenues, EBITDA and capex) via DCF and/or multiples. We apply multiples of 5.0-6.5x EBITDAaL for operations in Europe and 4.5-6.0x in emerging markets. In line with the remaining coverage, we apply a conglomerate discount of 10% for the group.

We include liabilities for future License spend and potential German capex network investment. We include assets for VOD's deferred tax asset.

Upside risks to our PO are:
1) Market consolidation leading to improved pricing power, 2) unexpected and positive macroeconomic changes, given VOD's diversified footprint.

Downside risks to our PO are:
1) Pressing needs to invest in cable operations in the face of fibre competition, 2) Ongoing dilutive ROCE in non-core regions, 3) unexpected and negative macroeconomic changes, given VOD's diversified footprint.

# Analyst Certification

I, David Wright, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

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| Investment rating | Company | BofA Ticker | Bloomberg symbol | Analyst |
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| | Cellnex | CLLNY | CLLNY US | David Wright |
| | Deutsche Telekom | DTEGY | DTEGY US | David Wright |
| | Deutsche Telekom | DTEGF | DTE GY | David Wright |
| | Freenet AG | FRTAF | FNTN GY | Titus Krahn |
| | Helios Towers plc | HTWSF | HTWS LN | David Wright |
| | Inwit | IFSUF | INW IM | David Wright |
| | Orange | FNCTF | ORA FP | Titus Krahn |
| | Orange | ORAN | ORAN US | Titus Krahn |
| | Tele2 AB | TLTZF | TEL2B SS | Titus Krahn |
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| | Telecom Italia SPA | TIAOF | TIT IM | David Wright |
| | Telefonica SA | TEFOF | TEF SQ | David Wright |
| | Telefonica SA | TEF | TEF US | David Wright |
| | United Internet AG | UDIRF | UTDI GY | Titus Krahn |
| | Vodafone Group | VOD | VOD US | David Wright |
| | Vodafone Group | VODPF | VOD LN | David Wright |
| **NEUTRAL** | | | | |
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| | KPN | KKPNF | KPN NA | Titus Krahn |
| | Telenor | TELNF | TEL NO | Titus Krahn |
| | Telenor | TELNY | TELNY US | Titus Krahn |
| **UNDERPERFORM** | | | | |
| | Bouygues | BOUYF | EN FP | Titus Krahn |

**EMEA - Telecoms Coverage Cluster**

| Investment rating | Company | BofA Ticker | Bloomberg symbol | Analyst |
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| | Swisscom | SWZCF | SCMN SW | Titus Krahn |
| | Swisscom | SCMWY | SCMWY US | Titus Krahn |
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| | Telia Company | TLSNY | TLSNY US | Titus Krahn |
| **RSTR** | | | | |
| | Telefonica Deutschland | TELDF | O2D GY | David Wright |

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| Business Performance | Numerator | Denominator |
|---|---|---|
| Return On Capital Employed | NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization | Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization |
| Return On Equity | Net Income | Shareholders' Equity |
| Operating Margin | Operating Profit | Sales |
| Earnings Growth | Expected 5 Year CAGR From Latest Actual | N/A |
| Free Cash Flow | Cash Flow From Operations – Total Capex | N/A |
| **Quality of Earnings** | **Numerator** | **Denominator** |
| Cash Realization Ratio | Cash Flow From Operations | Net Income |
| Asset Replacement Ratio | Capex | Depreciation |
| Tax Rate | Tax Charge | Pre-Tax Income |
| Net Debt-To-Equity Ratio | Net Debt = Total Debt – Cash & Equivalents | Total Equity |
| Interest Cover | EBIT | Interest Expense |
| **Valuation Toolkit** | **Numerator** | **Denominator** |
| Price / Earnings Ratio | Current Share Price | Diluted Earnings Per Share (Basis As Specified) |
| Price / Book Value | Current Share Price | Shareholders' Equity / Current Basic Shares |
| Dividend Yield | Annualised Declared Cash Dividend | Current Share Price |
| Free Cash Flow Yield | Cash Flow From Operations – Total Capex | Market Cap = Current Share Price × Current Basic Shares |
| Enterprise Value / Sales | EV = Current Share Price × Current Shares + Minority Equity + Net Debt + Other LT Liabilities | Sales |
| EV / EBITDA | Enterprise Value | Basic EBIT + Depreciation + Amortization |

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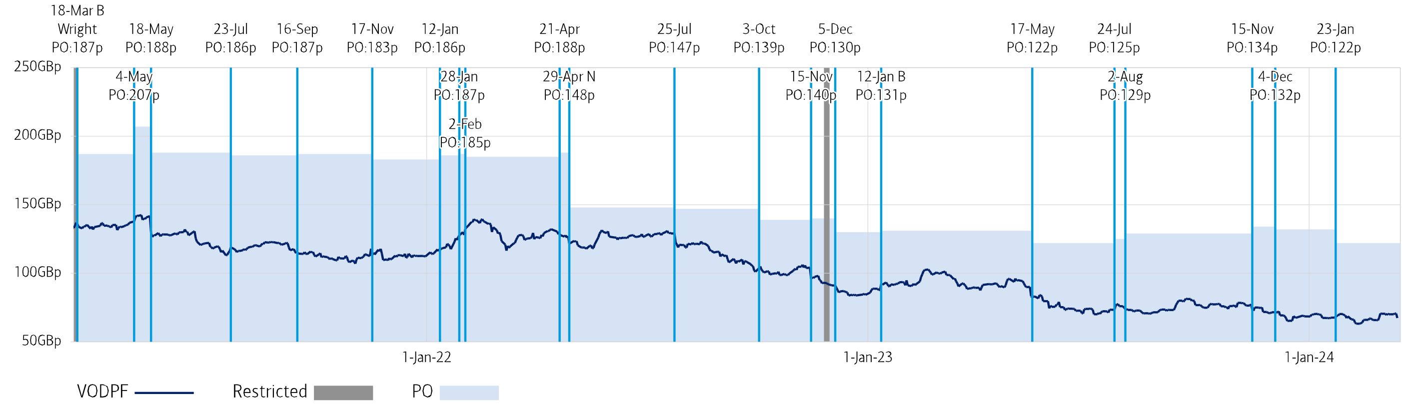


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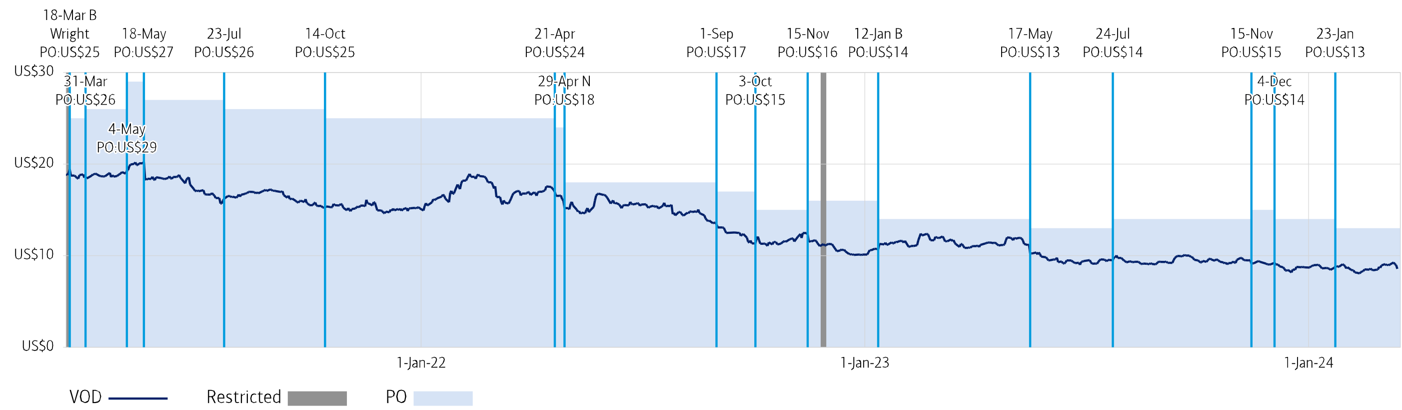
### Vodafone Group (VOD) Price Chart




B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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**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% |

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| Underperform | N/A | ≥ 20% |

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