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Vodafone Group

Dividend outlook; a potential turning point

Reiterate Rating: BUY | PO: 132.00 GBp | Price: 67.64 GBp

23 January 2024

Equity

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Rebase ahead to sustainable, growing yield

Vodafone's restructuring is well underway with portfolio change and new partnerships agreed to improve customer service and drive Enterprise growth. The former is a catalyst to new capital allocation - flagged by management - at upcoming FY results. We model a scenario assuming Spanish and UK deals that dilute mid-term average cash flows c20%, with VOD cutting divi 40% to provide a sustainable base and supplementing with E1bn annual buyback within leverage constraints. That equates numerically to 7% yield, growing up to 5% pa at current price, within stable 2.5x leverage. This is not unattractive and is perhaps the best way to see the 'wood for the trees' amidst the complexity of VOD over the coming 18-24m. Reiterate Buy.

Restructuring implications: cash flows, divi and leverage

We model a scenario with Vodafone ex-Spain from FY March 25 and assume the merger of UK operations with Hutch from FY26 (both broadly in-line with expected timeline). The Spain sale dilutes initial cash flows c10% and the UK merger a further 20% with restructuring (FY26 aggregate peak -31%) although this unwinds by year 4 (FY29), then full runrate UK merger synergies support 5% group FCF accretion by FY30.

We assume VOD's priority is to derive a dividend floor with room to grow. Thus, based on 2/3 payout of diluted average mid-term cash flows we model a 40% dividend cut (to E5.4c/share). With excess cash flow and sale proceeds, VOD can supplement with E1bn pa buyback to support DPS growth (up to 5% pa, per share price re-rating) within secure investment grade leverage. New yield 7% compares to current 12% (priced at risk).

But FX weighs on near-term numbers

Meanwhile VOD numbers could move lower on currency weakness in emerging markets, notably Egypt with a potential devaluation (1yr currency forward 66% lower than spot). We adjust FY24/25/26 EBITDAal -0.7%/-2.1%/-4.2%, distributable FCF -7.4%/-4.4%/-5.5%. Consensus looks behind on currencies in outer years, BofA FY26 FCF 5% below. We lower PO to 122p from 132p, leaving dividend forecast unchanged pending formal Spain and UK completion, but noting current yield 12% is pricing in material downside.

Estimates (Mar) (EUR)	2022A	2023A	2024E	2025E	2026E
EPS (Adjusted Diluted)	0.10	0.43	0.03	0.05	0.06
EPS Change (YoY)	427.7%	346.7%	-92.7%	45.2%	30.7%
Dividend / Share	0.09	0.09	0.09	0.09	0.09
ADR EPS (Adjusted Diluted - US$)	1.11	4.44	0.34	0.49	0.64
ADR Dividend / Share (US$)	1.05	0.94	0.98	0.98	0.98
Valuation (Mar)					
P/E	8.37x	1.80x	25.4x	17.5x	13.4x
Dividend Yield	11.4%	11.4%	11.4%	11.4%	11.4%
EV / EBITDA*	5.97x	6.19x	6.93x	6.78x	6.57x
Free Cash Flow Yield*	22.6%	20.6%	15.1%	16.0%	16.3%

* For full definitions of *iQmethod*SM measures, see page 12.

Stock Data

Price (Common / ADR)	67.64 GBp / 8.78 USD
Price Objective	132.00 GBp / 14.40 USD
Date Established	4-Dec-2023 / 4-Dec-2023
Investment Opinion	B-1-8 / B-1-8
52-Week Range	64.65 GBp-103.24 GBp
Market Value (mn)	18,315 GBP
Shares Outstanding (mn)	27,077.3 / 2,707.7
Average Daily Value (mn)	45.07 USD
Free Float	95.0%
BofA Ticker / Exchange	VODPF / LSE
BofA Ticker / Exchange	VOD / NAS
Bloomberg / Reuters	VOD LN / VOD.L
ROE (2024E)	1.4%
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".

Refer to important disclosures on page 13 to 16. Analyst Certification on page 11. Price Objective Basis/Risk on page 11.

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Timestamp: 23 January 2024 12:30AM EST

iQprofile[SM] Vodafone Group

Key Income Statement Data (Mar)	2022A	2023A	2024E	2025E	2026E
(EUR Millions)					
Sales	45,580	45,706	43,948	44,792	45,652
EBITDA Adjusted	15,208	14,665	13,104	13,396	13,810
Depreciation & Amortization	(9,858)	(9,649)	(9,331)	(9,126)	(8,922)
EBIT Adjusted	5,350	5,016	3,774	4,270	4,888
Net Interest & Other Income	(1,710)	(1,480)	(1,650)	(1,645)	(1,653)
Tax Expense / Benefit	(1,330)	(481)	(556)	(688)	(848)
Net Income (Adjusted)	2,773	11,818	860	1,249	1,632
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	860	1,249	1,632
Depreciation & Amortization	9,858	9,649	9,331	9,126	8,922
Change in Working Capital	(31.0)	256	(225)	(75.0)	0
Deferred Taxation Charge	0	0	0	0	0
Other CFO	(224)	(9,464)	252	333	874
Cash Flow from Operations	**12,912**	**12,259**	**10,218**	**10,633**	**11,428**
Capital Expenditure	(8,306)	(8,378)	(7,549)	(7,509)	(8,023)
(Acquisition) / Disposal of Investments	NA	NA	NA	NA	NA
Other CFI	101	11,909	687	37.4	87.4
Cash Flow from Investing	**(8,205)**	**3,531**	**(6,862)**	**(7,472)**	**(7,936)**
Share Issue / (Repurchase)	(2,029)	(1,893)	0	0	0
Cost of Dividends Paid	(539)	(400)	(501)	(506)	(535)
Increase (decrease) debt	2,332	(3,702)	(364)	(164)	(466)
Other CFF	(4,785)	3,629	(2,127)	(2,327)	(2,025)
Cash Flow from Financing	**(5,021)**	**(2,366)**	**(2,992)**	**(2,998)**	**(3,026)**
Total Cash Flow (CFO + CFI + CFF)	**(314)**	**13,424**	**364**	**164**	**466**
FX and other changes to cash	1,989	(9,215)	(364)	(164)	(466)
Change in Cash	1,675	4,209	0	0	0
Change in Net Debt	657	(7,911)	(364)	(164)	(466)
Net Debt (Reported)	62,596	54,685	54,321	54,157	53,691
Net Debt (Adjusted)	41,578	33,375	33,011	32,847	32,381
Key Balance Sheet Data					
Property, Plant & Equipment	40,804	37,992	37,577	37,785	38,671
Goodwill	31,884	27,615	27,615	27,615	27,615
Other Intangibles	21,360	19,592	18,026	16,501	15,016
Other Non-Current Assets	31,368	39,660	39,540	39,495	39,087
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	153,420	152,058	151,051
Long-Term Debt	58,131	51,669	51,305	51,141	50,675
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	90,824	90,810	90,494
Total Equity	56,977	64,483	62,596	61,248	60,557
Total Equity & Liabilities	153,953	155,521	153,420	152,058	151,051
Business Performance*					
Return On Capital Employed	2.71%	3.37%	2.13%	2.45%	2.82%
Return On Equity	5.02%	20.0%	1.38%	2.07%	2.78%
Operating Margin	11.9%	30.3%	8.59%	9.53%	10.7%
Free Cash Flow (MM)	5,193	4,508	3,305	3,505	3,557
Quality of Earnings*					
Cash Realization Ratio	4.66x	1.04x	11.9x	8.52x	7.00x
Asset Replacement Ratio	0.84x	0.87x	0.81x	0.82x	0.90x
Tax Rate	32.4%	3.75%	24.1%	23.8%	24.3%
Net Debt/Equity	110%	84.8%	86.8%	88.4%	88.7%
Interest Cover	2.72x	2.90x	2.29x	2.60x	2.96x

* For full definitions of *iQmethod*[SM] measures, see page 12.

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

Investment conclusions

In our Vodafone upgrade last year we looked forward to portfolio restructuring under new management as a means to review, reshape and recapitalise Vodafone into a reduced portfolio of higher quality assets.

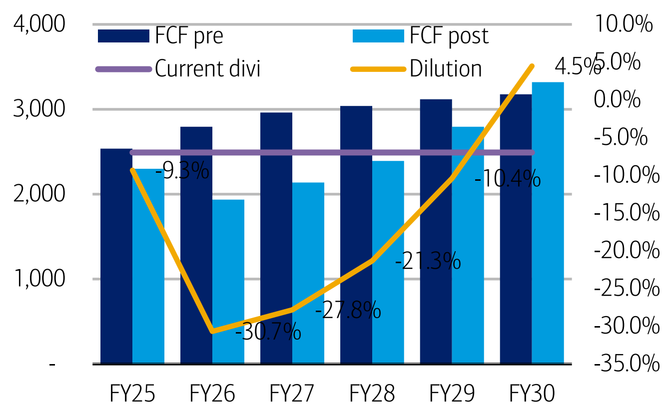
Following this Vodafone chose to promote CFO Margherita Della Valle from CFO to CEO to replace Nick Read at FY results in a move that we regarded as a surprise given multiple reports of external candidates. Nevertheless, there has been significant progress made to restructure Vodafone since then with portfolio restructuring alongside strategic initiatives to support regional autonomy and new partnerships such as the one struck with Microsoft to incorporate generative AI into customer services and develop Enterprise IoT services alongside other actions.

In this research we focus more on portfolio restructuring and the immediate impact on free cash flows that should shape - per Vodafone's commentary - its capital allocation policy. We base our analysis on the closure of the Spanish sale (due imminently) and proposed merger of UK operations with Hutch (estimated completion end calendar 2024). Vodafone has received an offer for Italian operations from Iliad and confirmed wider market discussions but given the uncertainty around any deal that might manifest (and require lengthy regulatory approval) we do not factor this into Vodafone's immediate dividend decision.

Our conclusion is that distributable free cash flow is diluted around 10% by the sale of Spain in FY25, although this unwinds over time with improved coupons on preference equity. And that the UK merger should be an incremental 20% dilution as restructuring costs weigh heavily (together 31% in FY March 26) before unwinding as synergies accrue. We forecast group FCF accretion only by FY March 2030.

Exhibit 1: Distributable FCF – pre/post Spain/UK M&A

Post M&A FCF below current divi payout FY25-28, Group accretion by FY30



Source: BofA Global Research estimates, company report

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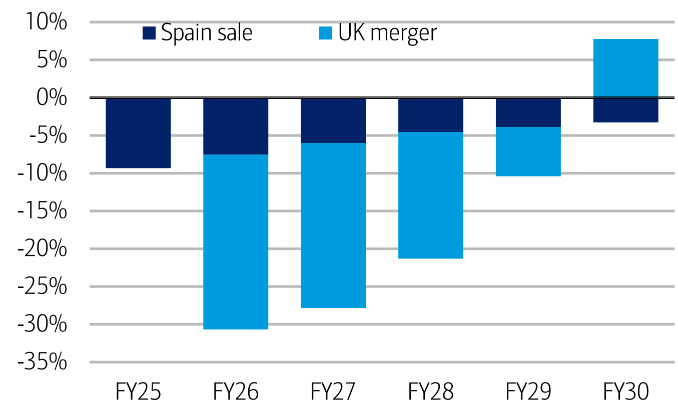
Exhibit 2: Distributable FCF dilution– Spain/UK composition

Spain initially 10% dilutive but unwinds with preference equity coupons, UK dilution material with £500m integration costs before Y5 £700m synergy.



Source: BofA Global Research estimates, company report

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A key observation is that current dividend (E9c DPS outflow cE2.5bn) is uncovered from FY25-28 under our scenario, too long to be a sustainable policy. Thus, in our scenario, we consider a revised policy during this interim period (as has been openly communicated by VOD management), with 2/3 average cash flow payout deriving a 40% dividend cut (initially to E5.4c DPS, outflow E1.5bn).

This frees cash flow while additional balance sheet headroom is freed up by Spanish sale proceeds (less incremental UK debt), enabling VOD to supplement dividend with buyback of E1bn per annum during the period, fuelling DPS growth (up to 5% PA) based on a static payout and reduced share count.

Beyond FY28 with a potential call option to acquire the Merged UK minority stake (cost cE7.5bn), leverage could nudge up but with full runrate synergies emerging to manage back down in just one year. VOD could choose to maintain dividend here, or even continue growth as payout ratio continues to fall.

Exhibit 3: Group Net Debt & leverage impact, dividend cut scenario, EURm

Deducting Spanish proceeds FY25, adding initial incremental UK debt FY26, adjusting for new cash flows and buyback/dividend cut

Net Debt	FY 24	FY25	FY26	FY27	FY28	FY29	FY30
b/f		**33,686**	**29,780**	**32,317**	**32,674**	**32,778**	**38,986**
- M&A Spain proceeds		- 4,100					
- M&A UK new debt			1,978			7,433	-
- Post M&A cash flow		- 2,300	- 1,937	- 2,138	- 2,391	- 2,795	- 3,320
- Divi +1yr		1,495	1,495	1,495	1,495	1,569	1,648
(divi / FCF payout)		65%	77%	70%	63%	56%	50%
- Buyback		1,000	1,000	1,000	1,000		
c/f	**33,686**	**29,780**	**32,317**	**32,674**	**32,778**	**38,986**	**37,315**
- Leverage	2.6	2.4	2.5	2.5	2.4	2.8	2.6
- proportionate		2.4	2.4	2.4	2.3	2.8	2.6
Shares		27,680	26,390	25,101	23,811	22,521	22,521
Buyback		- 1,290	- 1,290	- 1,290	- 1,290	-	-
Share price (EUR)		78	78	78	78	78	78
New DPS p/sh		5.4	5.7	6.0	6.3	6.6	6.9
- YoY			5%	5%	5%	5%	5%
- yield		7%	7%	8%	8%	9%	9%

Source: BofA Global Research estimates, company report

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Our conclusion is that VOD could rebase payout during the initially dilutive period, but supplement with buyback until full UK integration and synergy realization on a 4-5 year outlook. This would provide a more visible, sustainable base to grow dividend, and from an attractive initial yield of 7%.

Meanwhile we adjust numbers to reflect EM currency volatility

One of the potential restructuring opportunities we flagged in our upgrade was the sale of Vodacom in Africa. At the time we argued that there was little obvious structural synergy in Vodafone's equity holding and that selling the stake would free significant capital but also reduce EM risk from VOD's cost of capital. However, Vodafone's new CEO has stated her ambition to own the asset, and with this comes fresh currency risk as inflation remains high in Türkiye and Egypt considers a devaluation.

We summarise changes to current forecasts as follows, primarily driven by currency devaluation prospects. Net Debt is E500m higher due to the inclusion of KDG minority payments. Sum of parts PO moves to 122p on these factors.

Note that we have maintained our preferred approach of not adjusting public forecasts until deal closure, so right now we maintain our outlook including Spain and the UK and with dividend unchanged; analysis in the report is on a proforma basis. Summarising other changes:

Exhibit 4: VOD Group forecast changes, EURm

Notable currency adjustments (bottom of table) driving FY 26/27 impact.

	New				Old				Chg			
Group	**Mar 24E**	**Mar 25E**	**Mar 26E**	**Mar 27E**	**Mar 24E**	**Mar 25E**	**Mar 26E**	**Mar 27E**	**Mar 24E**	**Mar 25E**	**Mar 26E**	**Mar 27E**
Revenues	44,113	44,167	44,260	45,359	43,948	44,792	45,652	46,529	0.4%	-1.4%	-3.1%	-2.5%
EBITDAaL	13,016	13,115	13,235	13,643	13,104	13,396	13,810	14,191	-0.7%	-2.1%	-4.2%	-3.9%
PBT	2,350	2,791	3,120	3,730	2,311	2,888	3,483	4,064	1.7%	-3.3%	-10.4%	-8.2%
EPS	6.4	7.6	8.5	10.2	6.3	7.9	9.5	11.1	0.9%	-4.2%	-10.3%	-7.9%

Exhibit 4: VOD Group forecast changes, EURm
Notable currency adjustments (bottom of table) driving FY 26/27 impact.

	New				Old				Chg			
DPS	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	0.0%	0.0%	0.0%	0.0%
Capex	-7,627	-7,408	-7,480	-7,688	-7,549	-7,509	-8,023	-8,143	1.0%	-1.4%	-6.8%	-5.6%
FCF pre divi	2,181	2,537	2,794	2,963	2,355	2,655	2,957	3,249	-7.4%	-4.4%	-5.5%	-8.8%
FCF VOD guide	3,131	3,387	3,494	3,563	3,305	3,505	3,557	3,799	-5.3%	-3.4%	-1.8%	-6.2%
Net Debt	33,686	33,640	33,337	32,865	33,011	32,847	32,381	31,624	2.0%	2.4%	2.9%	3.9%
Service revenues	**Mar 24E**	**Mar 25E**			**Mar 24E**	**Mar 25E**			**Mar 24E**	**Mar 25E**		
Germany	11,477	11,273			11,491	11,287			-0.1%	-0.1%		
Italy	4,201	4,241			4,211	4,251			-0.2%	-0.2%		
UK	5,624	5,843			5,635	5,823			-0.2%	0.3%		
Spain	3,435	3,435			3,435	3,435			0.0%	0.0%		
Other Europe	4,439	4,591			4,439	4,591			0.0%	0.0%		
Europe	**28,991**	**29,195**			**29,026**	**29,200**			**-0.1%**	**0.0%**		
Vodacom	5,960	5,758			5,979	6,034			-0.3%	-4.6%		
Other Asia	1,818	1,876			1,782	2,036			2.0%	-7.9%		
Other and eliminations	446	446			446	460			0.0%	-3.1%		
Group	**37,215**	**37,275**			**37,233**	**37,731**			**0.0%**	**-1.2%**		
Adjusted EBITDAaL												
Germany	5,118	5,020			5,124	5,013			-0.1%	0.1%		
Italy	1,351	1,388			1,366	1,427			-1.1%	-2.7%		
UK	1,305	1,389			1,308	1,404			-0.2%	-1.1%		
Spain	859	881			859	878			0.0%	0.3%		
Other Europe	1,483	1,534			1,483	1,534			0.0%	0.0%		
Europe	10,118	10,212			10,141	10,256			-0.2%	-0.4%		
- ex Spain	9,259	9,331			9,281	9,378			-0.2%	-0.5%		
Vodacom	2,514	2,491			2,581	2,679			-2.6%	-7.0%		
Other Asia (Turk)	534	563			533	611			0.2%	-7.9%		
Common functions	-150	-150			-150	-150			0.0%	0.0%		
Group	**13,016**	**13,115**	**13,235**	**13,643**	**13,104**	**13,396**	**13,810**	**14,191**	**-0.7%**	**-2.1%**	**-4.2%**	**-3.9%**
FX												
GBP/EUR	0.86	0.86	0.86	0.86	0.86	0.86	0.86	0.86	0.2%	-0.3%	-0.3%	-0.3%
EGP/EUR	33.60	44.36	54.82	57.56	33.63	34.47	35.33	36.21	-0.1%	28.7%	55.2%	59.0%
TRY/EUR	28.93	40.31	59.50	68.43	27.58	28.96	30.41	31.93	4.9%	39.2%	95.7%	114.3%
ZAR/EUR	20.29	20.95	22.80	23.94	20.28	20.79	21.31	21.84	0.0%	0.8%	7.0%	9.6%

Source: BofA Global Research estimates, company report

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With currency impact more in FY25 we remain broadly in-line with FY24 estimates on constant currency basis:

Exhibit 5: VOD guidance vs. BofA, constant currency, EURm
BofA remains in-line with FY24 guidance

FY 24E	Guidance	BofA
Adjusted EBITDAaL	cE13.3bn	13,314
Adj. FCF	c E3.3bn	3,254

Source: BofA Global Research estimates, company report

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Proforma Vodafone

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

And this presents a further 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 has publicly discussed the potential (and need) for Italian consolidation for some time, alongside other market participants. In Feb 2022 Iliad offered to acquire Vodafone Italy for E11.25bn but Vodafone rejected the approach. Iliad has since made another offer in December 2023 valuing VOD Italy at E10.45bn via E6.5bn cash and E2bn shareholder loan for an initial 50% stake that would be sold in 10% annual tranches over the subsequent 5 years. VOD has acknowledged the offer but made no further comment. Such a deal would need to be approved by the EU competition Commission, with a stage 2 investigation requiring at least 12m to close (if approved), based on previous precedent.

  There are multiple moving parts in Italy with Fastweb also reported to be interested in Vodafone, while Tel Italia management has indicated a willingness to participate in market consolidation and reports suggest Wind Tre could participate too. So while there is an Iliad offer, we are less sure of an outcome and regulation would be a significant hurdle with any proposed consolidation of Iliad who was the effective remedy to the merger on Wind and Tre in 2018.

In conclusion, our approach to a 24-36m outlook that could shape policy is to consider the Spanish and UK deals but to side-line Italy for now, with the caveat that any deal could further adjust expectations.

Proforma model

Our analysis begins with YE 2024 group unadjusted forecasts then we deduct Spain (impact March YE 25), 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.

- 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 (both EURm), UK standalone / UK merged (both £m)

Building to data to model: proforma = Group untouched – Spain – UK standalone + UK merged.

Group untouched, EUR	**FY24**	**FY25**	**FY26**	**FY27**	**FY28**	**FY29**	**FY30**
EBITDAaL	13,016	13,115	13,235	13,643	13,962	14,294	14,607
FCF VOD	3,131	3,387	3,494	3,563	3,639	3,719	3,777
FCF clean	2,181	2,537	2,794	2,963	3,039	3,119	3,177
Net Debt	33,686	33,640	33,337	32,865	32,317	31,689	31,003
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		881	895	909	924	938	954
Capex		- 496	- 536	- 584	- 593	- 602	- 612
OpFCF		384	359	326	331	336	342
Taxed	0%	384	359	326	331	336	342
UK standalone, £	**Assumptions**	**FY25**	**FY26**	**FY27**	**FY28**	**FY29**	**FY30**
EBITDAaL		1,194	1,237	1,265	1,294	1,324	1,354
Capex		- 665	- 680	- 696	- 712	- 728	- 745
OpFCF		529	557	569	582	596	609
Interest, £4.3bn	2.5%	- 108	- 108	- 108	- 108	- 108	- 108
Taxed FCF	0%	422	449	462	475	488	502
- EUR		491	523	537	553	568	584
UK Merged, £	**Assumptions**		**FY 26**	**FY 27**	**FY 28**	**FY 29**	**FY 30**
EBITDAaL			1,456	1,459	1,586	1,861	2,173
- VOD			1,237	1,265	1,294	1,324	1,354
- 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			- 1,412	- 1,400	- 1,390	- 1,359	- 1,234
- VOD			- 680	- 680	- 696	- 712	- 728
- Hutch			- 743	- 743	- 741	- 740	- 739
- Synergy (capex 2/3)	233		12	23	47	93	233
OpFCF			**44**	**59**	**196**	**502**	**939**
Interest			- 150	- 153	- 155	- 154	- 146
Tax	10%		-	-	- 4	- 35	- 79
FCF			**- 106**	**- 94**	**37**	**314**	**714**
- Distribution							- 400
Net Debt	**6,000**		**6,106**	**6,200**	**6,163**	**5,849**	**5,536**
- 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			1,693	1,697	1,846	2,165	2,528
FCF			- 123	- 109	43	365	830

Source: BofA Global Research estimates, company report

Exhibit 6: Underlying assumptions, Group untouched / Spain (both EURm), UK standalone / UK merged (both £m)
Building to data to model: proforma = Group untouched – Spain – UK standalone + UK merged.

Group untouched, EUR	**FY24**	**FY25**	**FY26**	**FY27**	**FY28**	**FY29**	**FY30**
EBITDAaL	13,016	13,115	13,235	13,643	13,962	14,294	14,607
FCF VOD	3,131	3,387	3,494	3,563	3,639	3,719	3,777
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Net Debt	33,686	33,640	33,337	32,865	32,317	31,689	31,003
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		881	895	909	924	938	954
Capex		- 496	- 536	- 584	- 593	- 602	- 612
OpFCF		384	359	326	331	336	342
Taxed	0%	384	359	326	331	336	342
UK standalone, £	**Assumptions**	**FY25**	**FY26**	**FY27**	**FY28**	**FY29**	**FY30**
EBITDAaL		1,194	1,237	1,265	1,294	1,324	1,354
Capex		- 665	- 680	- 696	- 712	- 728	- 745
OpFCF		529	557	569	582	596	609
Interest, £4.3bn	2.5%	- 108	- 108	- 108	- 108	- 108	- 108
Taxed FCF	0%	422	449	462	475	488	502
- EUR		491	523	537	553	568	584
UK Merged, £	**Assumptions**		**FY 26**	**FY 27**	**FY 28**	**FY 29**	**FY 30**

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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.
- 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 + new UK /synergy FY26

	FY24	**FY25**	**FY26**	**FY27**	**FY28**	**FY29**	**FY30**
EBITDAaL pre	**13,016**	**13,115**	**13,235**	**13,643**	**13,962**	**14,294**	**14,607**
- Spain, less EBITDAaL		- 881	- 895	- 909	- 924	- 938	- 954
- UK, add Hutch consol			402	404	406	408	410
- UK, add synergy			27	54	109	217	543
EBITDAaL post	**13,016**	**12,235**	**12,769**	**13,191**	**13,552**	**13,981**	**14,606**
- proportional		12,235	11,854	12,246	12,563	12,920	13,367

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 free cash flow from FY25.
- Add back the interest benefit (at VOD's 2.5% cost of debt) on E4.1bn cash consideration, and coupons on the E900m deferral (5% years 1-3, then 10%, 12.5/15% thereafter).
- 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 c10% and the UK initially a further 20% before normalising by year 4 cash flow positive and by year 5 at the group level.

Exhibit 8: Group free cash flow impact, EURm

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

FCF pre	**FY24**	**FY25**	**FY26**	**FY27**	**FY28**	**FY29**	**FY30**
FCF pre - VOD	3,131	3,387	3,494	3,563	3,639	3,719	3,777
FCF pre - clean (ex restructure/spec)	2,181	2,537	2,794	2,963	3,039	3,119	3,177
- Spain, less standalone taxed OpFCF	-	-384	-359	-326	-331	-336	-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
- UK, less standalone FCF			-523	-537	-553	-568	-584
- UK add merger FCF			-123	-109	43	365	830
FCF post		**2,300**	**1,937**	**2,138**	**2,391**	**2,795**	**3,320**
- dilution		-9.3%	-30.7%	-27.8%	-21.3%	-10.4%	4.5%

Source: BofA Global Research estimates, company report

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Net Debt impact – assuming dividend sustained.

For Net Debt / leverage we illustrate VOD's untouched Net Debt carried forward from FY24 forecasts, then:

- Deduct Spanish proceeds in FY25, add incremental £1.7bn UK merger debt in FY26, add a payment to acquire Hutch minorities per the call option in FY29 (year 4, as the asset moves into positive cash flow, at implied 8.5x EBITDAaL)
- Deduct adjusted free cash flows defined above.
- Add back dividend outflow assuming no change to current E9c DPS.

We illustrate implied Net Debt/EBITDAaL and also include a proportionate multiple given the 51% ownership of the UK EBITDAaL and Net Debt.

Exhibit 9: Group Net Debt impact, EURm

Deducting Spanish proceeds, adding UK debt, adjusting for new cash flows.

Net Debt	**FY 24**	**FY25**	**FY26**	**FY27**	**FY28**	**FY29**	**FY30**
B/f	33,375	33,686	29,776	32,308	32,661	32,761	39,891
- M&A Spain		-4,100					
- M&A UK			1,978			7,433	
- Cash flow		-2,300	-1,937	-2,138	-2,391	-2,795	-3,320
- Divi +1yr		2,491	2,491	2,491	2,491	2,491	2,491
c/f	**33,686**	**29,776**	**32,308**	**32,661**	**32,761**	**39,891**	**39,062**
- Leverage	2.6	2.4	2.5	2.5	2.4	2.9	2.7
- prop		2.4	2.4	2.4	2.3	2.9	2.7

Source: BofA Global Research estimates, company report

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Initial conclusions

Given deal proceeds, VOD's leverage should remain broadly stable and secure at c2.5x until the payment to acquire Hutch minorities in year 4 moves this upwards. However interim FY25-28 cash flows are diluted c23% from pre-deal levels at an average E2.2bn level and thus below the cE2.5bn current dividend outflow.

Our view is that while a brief period with dividend uncovered could be considered, a 3–4-year gap is too long and that VOD will choose to rebase the dividend lower to levels that could be guaranteed and used as a base to grow. Per our point around leverage being stable, and as a fuel to potential DPS growth, we expect VOD to 'fill the gap' with buyback (as has been alluded to by the CEO and CFO).

Adjusting shareholder remuneration assumptions

With the above in mind, we consider the potential to reduce dividend outflow and balance with buyback, both assuming that leverage around 2.5x is maintained.

The following working considers a potential reduction in payout of FY 25-28 average free cash flow, and the implications for dividend. Our assumption is that a cut of 40%

should broadly assume a more secure 2/3 payout (broadly in-line with sector average) to provide a buffer to delever and as a base to grow.

Exhibit 10: Dividend cut scenario based on sustainable payout
A 40% cut to divi reduces payout during the dilutive M&A period.

FY25-FY28 average FCF	**2,192**
Payout	68%
New payout	1,495
Old payout	2,491
Change	-40%

Source: BofA Global Research estimates, company report

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We then model a modified Net Debt working, assuming new payout initially but a 4-year FY25-28 E1bn per annum buyback to broadly bridge the gap to 2.5x leverage before easing in FY 29 ahead of the UK minority acquisition, nudging leverage upwards.

Note that we model the impact of buyback on dividend assuming a static share price at the time of writing that would support compound DPS growth of 5%. Clearly this could translate into an increase in share price and reduced dividend growth. From FY 28 onwards as UK cash flow accretion kicks in we assume hard coded 5% dividend increase.

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 proceeds (FY25), 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		33,686	29,780	32,317	32,674	32,778	38,986
- M&A Spain		- 4,100					
- M&A UK			1,978			7,433	-
- Cash flow		- 2,300	- 1,937	- 2,138	- 2,391	- 2,795	- 3,320
- Divi +1yr		1,495	1,495	1,495	1,495	1,569	1,648
(divi / FCF payout)		65%	77%	70%	63%	56%	50%
- Buyback		1,000	1,000	1,000	1,000		
c/f	**33,686**	**29,780**	**32,317**	**32,674**	**32,778**	**38,986**	**37,315**
- Leverage	2.6	2.4	2.5	2.5	2.4	2.8	2.6
- proportionate		2.4	2.4	2.4	2.3	2.8	2.6
Shares		27,680	26,390	25,101	23,811	22,521	22,521
Buyback		- 1,290	- 1,290	- 1,290	- 1,290	-	-
Share price (EUR)		78	78	78	78	78	78
New p/sh		5.4	5.7	6.0	6.3	6.6	6.9
- YoY			5%	5%	5%	5%	5%
- yield		7%	7%	8%	8%	9%	9%

Source: BofA Global Research estimates, company report

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Price objective basis & risk

Vodafone Group (VODPF / VOD)

Our 122p PO (US$13.28 ADR) 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.

EMEA - Telecoms Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	BT	BTGOF	BT/A LN	David Wright
	Cellnex	CLNXF	CLNX SQ	David Wright
	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
	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				
	1&1 AG	DRHKF	1U1 GY	Titus Krahn
	KPN	KKPNF	KPN NA	Titus Krahn
	Liberty Global	LBTYA	LBTYA US	David Wright
	Telecom Italia -RSP	TIAJF	TITR IM	David Wright
	Telecom Italia SPA	TIIAY	TIIAY US	David Wright
	Telecom Italia SPA	TIAOF	TIT IM	David Wright
	Telenor	TELNF	TEL NO	Titus Krahn
	Telenor	TELNY	TELNY US	Titus Krahn
UNDERPERFORM				
	Bouygues	BOUYF	EN FP	Titus Krahn
	Elisa	ELMUF	ELISA FH	Titus Krahn

EMEA - Telecoms Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	Proximus	BGAOF	PROX BB	Titus Krahn
	Swisscom	SWZCF	SCMN SW	Titus Krahn
	Swisscom	SCMWY	SCMWY US	Titus Krahn
	Telia Company	TLSNF	TELIA SS	Titus Krahn
	Telia Company	TLSNY	TLSNY US	Titus Krahn
RSTR				
	Telefonica Deutschland	TELDF	O2D GY	David Wright

*iQ*method℠ Measures Definitions

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

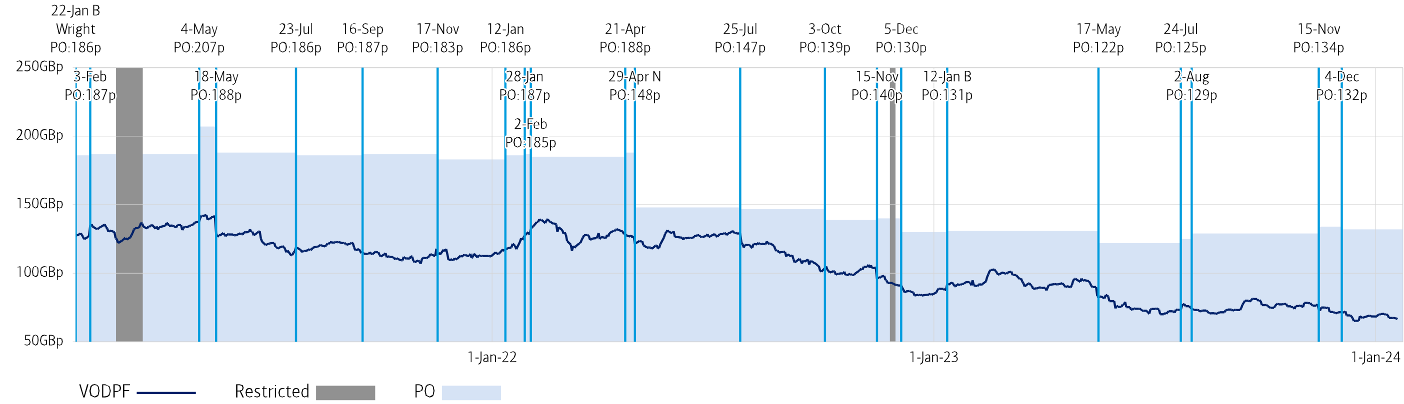
iQmethod℠ is the set of BofA Global Research standard measures that serve to maintain global consistency under three broad headings: Business Performance, Quality of Earnings, and validations. The key features of iQmethod are: A consistently structured, detailed, and transparent methodology. Guidelines to maximize the effectiveness of the comparative valuation process, and to identify some common pitfalls.

iQdatabase® is our real-time global research database that is sourced directly from our equity analysts' earnings models and includes forecasted as well as historical data for income statements, balance sheets, and cash flow statements for companies covered by BofA Global Research.

Disclosures

Important Disclosures

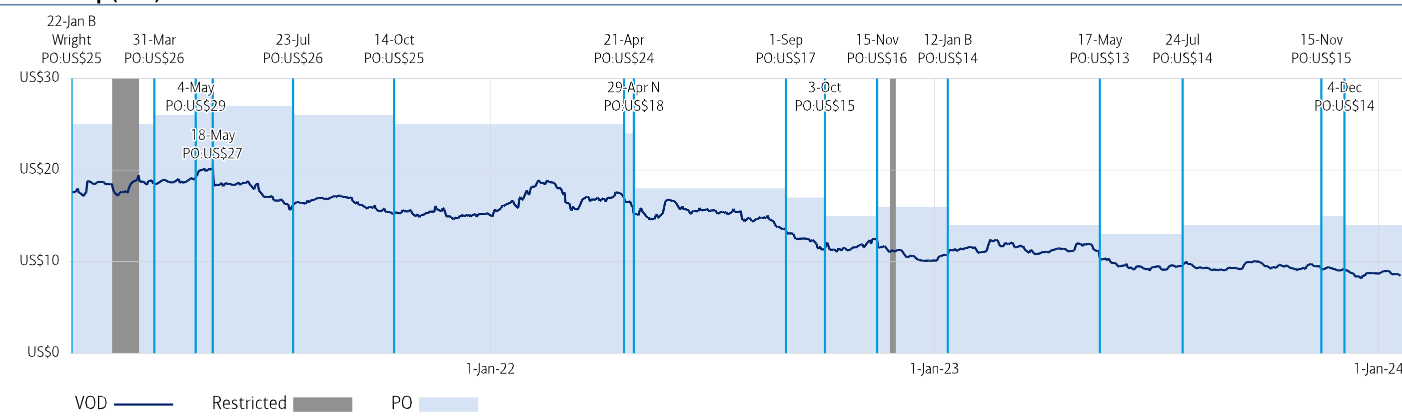
Vodafone Group (VODPF) Price Chart



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

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Vodafone Group (VOD) Price Chart



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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%

[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.

FUNDAMENTAL EQUITY OPINION KEY: Opinions include a Volatility Risk Rating, an Investment Rating and an Income Rating. VOLATILITY RISK RATINGS, indicators of potential price fluctuation, are: A - Low, B - Medium and C - High. INVESTMENT RATINGS reflect the analyst's assessment of both a stock's absolute total return potential as well as its attractiveness for investment relative to other stocks within its Coverage Cluster (defined below). Our investment ratings are: 1 - Buy stocks are expected to have a total return of at least 10% and are the most attractive stocks in the coverage cluster; 2 - Neutral stocks are expected to remain flat or increase in value and are less attractive than Buy rated stocks and 3 - Underperform stocks are the least attractive stocks in a coverage cluster. An investment rating of 6 (No Rating) indicates that a stock is no longer trading on the basis of fundamentals. Analysts assign investment ratings considering, among other things, the 0-12 month total return expectation for a stock and the firm's guidelines for ratings dispersions (shown in the table below). The current price objective for a stock should be referenced to better understand the total return expectation at any given time. The price objective reflects the analyst's view of the potential price appreciation (depreciation).

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.

INCOME RATINGS, indicators of potential cash dividends, are: 7 - same/higher (dividend considered to be secure), 8 - same/lower (dividend not considered to be secure) and 9 - pays no cash dividend. *Coverage Cluster* is comprised of stocks covered by a single analyst or two or more analysts sharing a common industry, sector, region or other classification(s). A stock's coverage cluster is included in the most recent BofA Global Research report referencing the stock.

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BofAS or an affiliate has received compensation from the issuer for non-investment banking services or products within the past 12 months: Vodafone Group.
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