

Company update

Telecom

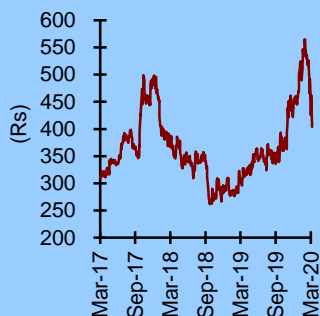
Target price: Rs610

Shareholding pattern

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

Source: NSE

Price chart



INDIA

Bharti Airtel

BUY
Maintained
Rs404

Four major concerns about Bharti Airtel...

Businesses globally are being impacted by extreme externalities including: COVID-19, crude price decline and currency volatility. Also, Indian telcos are facing significant payment demands arising from adverse ruling by the Supreme Court on AGR dues. In this note, we analyse four major concerns about Bharti Airtel and their impact on its fair value: 1) impact of crude price decline on Airtel Africa's fair value; 2) Bharti Infratel's fair value if Vodafone Idea (VIL) shuts shop; 3) INR depreciation; and 4) rise in AGR dues, and cashflow situation. Our analysis shows none of these concerns have any major impact on Bharti Airtel's SoTP-based valuation. Our estimates therefore remain unchanged and so does our target price at Rs610. Reiterate BUY. (Note: we are yet to incorporate the recent equity dilution in our estimates).

- **Extreme externalities warrant risk analysis.** We see significant rise in risk from externalities such as COVID-19, crude price decline and currency volatility impacting many businesses worldwide. This extraordinary situation warrants deeper risk analysis to assess the impact on Bharti Airtel. We see COVID-19 having little impact on the Bharti's mobile and other businesses; rather, with many subscribers at home and working / communicating virtually, the boost to mobile volumes is obvious. However, the significantly generous allowances in voice and data mean limited benefit. But, crude price and currency volatility do pose risk to Bharti Airtel, which we analyse in this report.
- **No empirical evidence of correlation between crude prices and *naira* to Airtel Nigeria's performance.** Airtel Africa's stock price has corrected by 62% in CY20-TD on 64% dip in crude prices, but surprisingly the *naira* has depreciated only 1.2%. We see concerns about the impact of crude price fall and currency depreciation on mobile services demand. In CY15 and CY16, crude prices saw steep decline and the *naira* too depreciated sharply. However, Bharti Africa's mobile services revenue grew 4.2% and 12.7% respectively during the two years. Our analysis covering CY11-CY18 finds no significant correlation of crude prices and *naira* to mobile service demand. However, if our valuation factors-in the risk by cutting our multiple to 4x FY22E EBITDA (from 6x in base case), the hit on our fair value for Bharti Airtel is only 3.4%, or Rs21/sh.
- **INR depreciation has negligible impact on Bharti Airtel's SoTP valuation.** Unlike five years back, when INR depreciation posed certain risk due to pain in Airtel Africa, the operations in the region have come a long way. Airtel Africa now positively contributes to earnings and valuation, hence cross-currency INR depreciation (INR depreciation against African currencies) positively impacts Bharti Airtel's earnings and fair value, albeit marginally. We see dip in Bharti Airtel's valuation due to its foreign currency debt in India, but the risk is covered by the benefit from Airtel Africa's value accretion. Therefore, on consolidated basis, INR depreciation does not impact Bharti Airtel's fair value.
- **Other risks:** Though AGR dues pose a risk to Bharti Infratel's fair value if VIL shuts shop, Bharti Airtel's mobile business may see windfall gain. Further, we see the company's cash balance completely protecting it from worst case risk of AGR dues.

Market Cap	Rs2204bn/US\$22.0bn
Reuters/Bloomberg	BRTI.BO / BHARTI IN
Shares Outstanding (mn)	5,455.6
52-week Range (Rs)	533/276
Free Float (%)	37.3
FII (%)	16.5
Daily Volume (US\$/'000)	111,285
Absolute Return 3m (%)	(11.0)
Absolute Return 12m (%)	32.7
Sensex Return 3m (%)	(35.9)
Sensex Return 12m (%)	(30.1)

Year to Mar	FY19	FY20E	FY21E	FY22E
Revenue (Rs bn)	808	892	1,025	1,135
Net Income (Rs bn)	(17)	(3)	79	129
EPS (Rs)	(4.1)	(0.5)	15.5	25.1
% Chg YoY	(187.2)	(87.2)	NM	62.6
P/E (x)	(99.7)	NM	26.6	16.4
CEPS (Rs)	49.3	43.1	59.6	69.7
EV/E (x)	11.3	8.6	6.4	5.3
Dividend Yield (%)	0.6	0.6	0.7	0.7
RoCE (%)	2.2	2.1	6.6	8.6
RoE (%)	(2.3)	(0.3)	7.8	11.7

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We have tried to outline four investor concerns for Bharti Airtel, and their impact on its fair value. The four key concerns are: 1) impact of crude price decline on Airtel Africa's fair value (Nigeria economy is susceptible to crude price decline, which can cause currency volatility impacting reported numbers); 2) risk from Bharti Infratel's fair value in case of Vodafone Idea (VIL) shuts shop; 3) INR depreciation; and 4) rise in AGR dues, and cashflow situation. We have tried to analyse the impact of each of these concerns on our fair value for Bharti Airtel.

Concern-1: Risk to Airtel Africa fair value from dip in crude price

Airtel Africa's financial performance in the recent past has been very strong led by strong performance in the Nigeria market. Nigeria contributed 40% to Airtel Africa's revenues (in USD terms) and 49% to its EBITDA. Airtel Nigeria revenues and EBITDA grew at CQGRs of 5.6% and 8.9% respectively in past six quarters, which is very impressive. In Nigeria, Airtel benefited from reduction in competitive intensity from exit of the most aggressive operator (Etisalat). Another major operator in Nigeria, MTN, (market leader with over 37% subscriber market share and likely much higher revenue share) was impacted by a litigation with Nigeria government.

Oil & gas sector plays significant role in the Nigerian economy, accounting for 65% of total government revenues. Nigeria is Africa's largest oil-producing country, and 13th largest globally (source: *eiti.org*). Therefore, any volatility in crude prices exerts significant impact on the economy, and we note that crude prices have dropped by a whopping 64% in CY20-TD. We see this impacting Airtel Africa in two ways: 1) significant slowdown in the economy and consequent impact on Airtel Africa revenues; and 2) risk of currency depreciation amplifying adverse impact on Airtel Africa's USD revenues.

The concern is also visible from the 62% correction in Airtel Africa's stock price in CY20-TD. Also, the market (FTSE) has corrected by ~32% due to COVID-19 situation.

However, what is surprising is that the Nigerian currency (*naira*) has been outperforming and has dipped only 1.2% in CY20-TD despite significant fall in crude prices. We are not experts in African currencies, hence don't want to predict their exchange rates. However, we do believe the market is efficient enough and any significant risk should also be reflected in currency.

Table 1: Airtel Africa's performance has been very strong in recent past...

US\$ mn	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20	Q2FY20	Q3FY20
Revenue	745	769	783	781	796	844	883
Growth (% YoY)					6.9	9.8	12.8
EBITDA	301	326	318	344	339	366	394
Growth (% YoY)					12.8	12.3	23.9
EBITDA (%)	40.4	42.4	40.6	44.0	42.6	43.4	44.6
Depreciation and Amortisation	141	137	145	145	157	162	163
EBIT	160	189	173	199	182	204	231
EBIT (%)	21.4	24.6	22.1	25.5	22.9	24.2	26.2
PBT	96	52	106	199	95	153	159
PAT (reported)	142	59	123	89	125	107	90
PAT margin (%)	19.0	7.7	15.7	11.4	15.7	12.7	10.2

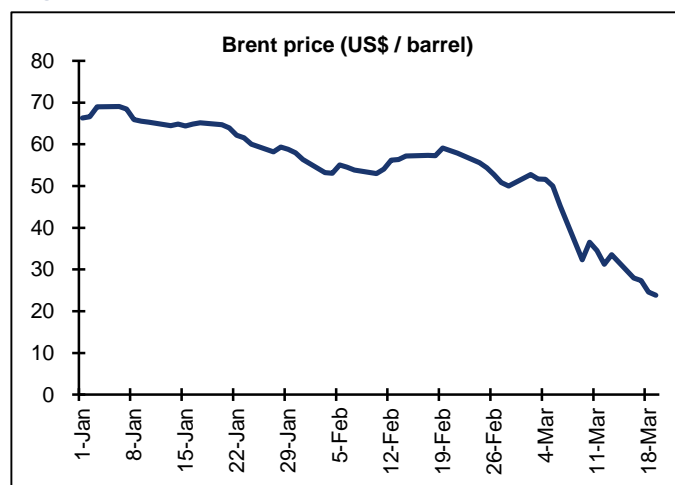
Source: Company data, I-Sec research

Table 2: ...led by strong performance in Airtel Nigeria. Nigeria revenue / EBITDA grew at CQGRs of 5.6% and 8.9% in past six quarters

US\$ mn	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20	Q2FY20	Q3FY20
Subs (mn)	32.6	34.2	36.6	37.1	37.5	39.5	39.9
Net add (mn)		1.6	2.4	0.5	0.3	2.0	0.3
ARPU	2.7	2.7	2.7	2.7	2.8	2.8	3.0
Growth (% YoY)					3.7	3.7	11.1
Revenue	255	262	284	299	311	326	354
Growth (% YoY)					22.0	24.4	24.6
% of Airtel Africa	34.3	34.1	36.3	38.3	39.1	38.6	40.1
EBITDA	116	128	141	159	165	172	194
Growth (% YoY)					42.2	34.4	37.6
EBITDA (%)	45.5	48.9	49.6	53.2	53.1	52.8	54.8
% of Airtel Africa	38.6	39.3	44.3	46.2	48.7	47.0	49.2
Depreciation and Amortisation	41	38	36	41	44	45	48
EBIT	75	90	105	118	121	127	146
EBIT (%)	29.4	34.4	37.0	39.5	38.9	39.0	41.2

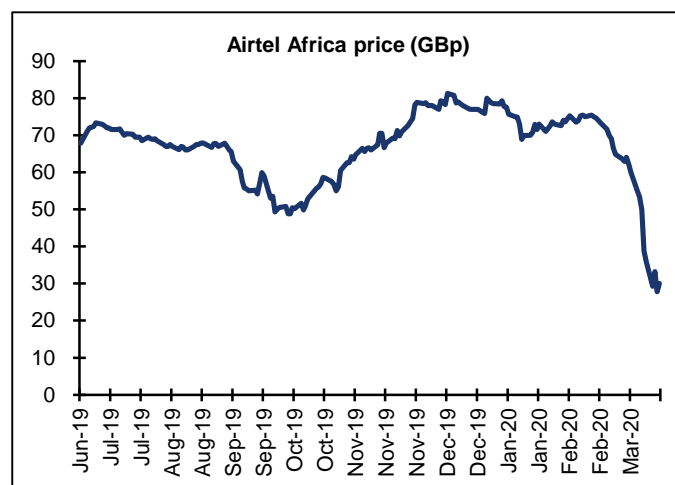
Source: Company data, I-Sec research

Chart 1: Can falling crude prices pose risk to Airtel Nigeria...



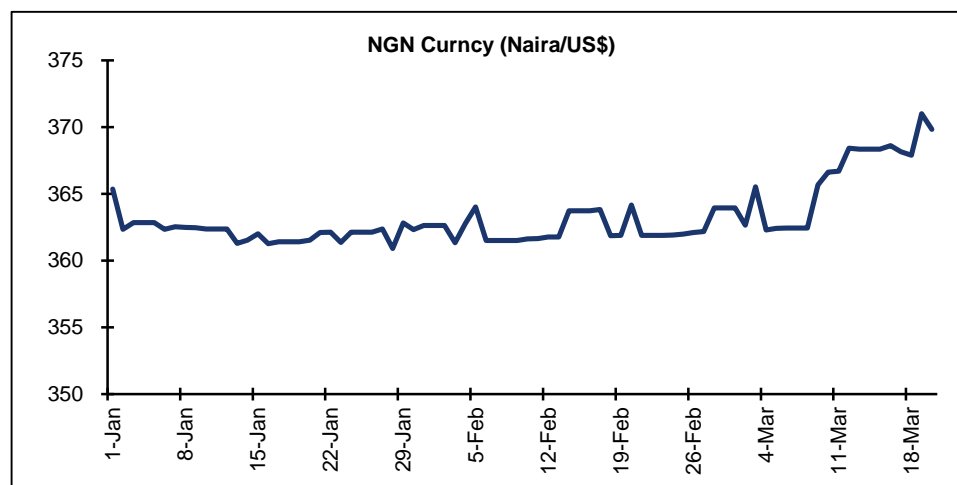
Source: Bloomberg, I-Sec research (last price as on 20-Mar-20)

Chart 2: ...as indicated by Airtel Africa stock price dip? Or is it a function of sell-off in the market?



Source: Bloomberg, I-Sec research (last price as on 20-Mar-20)

Chart 3: On the contrary, the Nigerian currency (naira) has outperformed (it has depreciated only 1.2% vs 64% fall in crude prices)



Source: Bloomberg, I-Sec research (last price as on 20-Mar-20)

Does crude price fall and *naira* depreciation pose risk to demand for Airtel Nigeria's mobile services?

We have tried to analyse the risk to mobile services demand in Nigeria on crude price decline and *naira* depreciation against the USD. The popular perception is that these two events are obvious risks to mobile services demand because: 1) decline in crude prices means lower revenue to government (hence lower government spend), and lower economic activities including job creation. Any curtailment of government spend could hurt demand for mobile services; and 2) depreciation of the *naira* would mean rise in inflation (as Nigeria is significantly dependent on imports for many products) and lower spend on mobile services.

We have charted out Airtel Nigeria's subscribers, ARPU, revenue and operating profit (EBIT) since CY11 to see how these two events impacted its performance in the past. We have also tried to correlate Airtel Nigeria performance with average crude price each year and average *naira*/USD exchange rate. Notably, the *naira* was pegged to USD till 19th Jun'16 and started free float from 20-June-16 when currency depreciated 30%.

We note CY15 and CY16 were the years when Nigeria was impacted by steep decline in crude prices as well as currency depreciation. In fact, as mentioned above, the *naira* going free float led to its sharp depreciation. However, we note Airtel Nigeria's mobile services revenue (in *naira* terms) grew at 4.2% and 12.7% YoY in CY15 and CY16 respectively. Of course, the revenue growth coincided with Etisalat's exit from Nigeria, which reduced competition. However, the competitive situation has not changed much since then in our view.

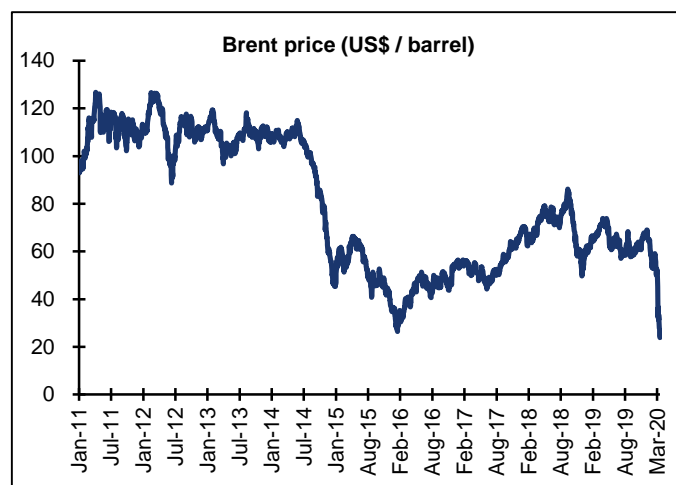
In our analysis covering CY11-CY18, we see significant volatility in both crude and *naira*, but Airtel Nigeria's mobile services revenue has not shown much of correlation. This gives us enough reason not to panic in the present precarious situation. Yes, we do remain cautious, but believe the situation is fundamentally not too bad as reflected in Airtel Africa's stock price.

Table 3: We see no major correlation in Airtel Nigeria's revenues to crude / *naira* during CY11-CY18

	CY11	CY12	CY13	CY14	CY15	CY16	CY17	CY18
Subs (mn)	18.0	23.1	24.8	27.6	32.3	34.1	37.2	44.2
Net add (mn)		5.1	1.8	2.7	4.7	1.8	3.1	6.9
ARPU (Naira)		931	772	761	694	705	737	782
Growth (% YoY)			(17.0)	(1.5)	(8.7)	1.6	4.5	6.1
Revenue (Nigerian Naira, bn)	203.8	229.7	222.2	239.1	249.1	280.8	315.5	382.1
Growth (% YoY)		12.7	(3.3)	7.6	4.2	12.7	12.3	21.1
EBIT	4.2	23.0	6.9	2.4	33.6	30.7	51.3	116.3
EBIT (%)		10.0	3.1	1.0	13.5	10.9	16.2	30.4
Average Crude price (US\$/barrel)	111	112	109	99	52	44	54	71
Change (% YoY)		0.8	(2.8)	(9.1)	(47.1)	(15.7)	23.2	30.9
Naira/US\$ (US\$)	156	159	159	165	198	258	334	362
Change (% YoY)		(1.9)	(0.3)	(3.7)	(19.8)	(30.5)	(29.4)	(8.3)

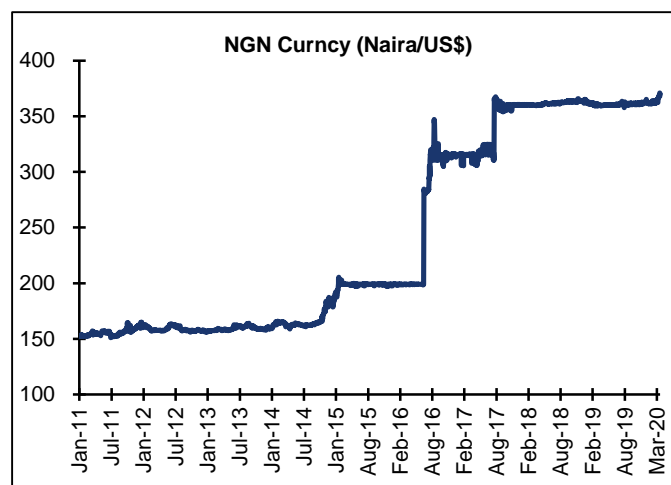
Source: Company data, I-Sec research

Chart 4: Since CY11, crude has been volatile and seen steep falls even in the past...



Source: Bloomberg, I-Sec research (last price as on 20-Mar-20)

Chart 5: ...so has been the *naira*/USD exchange rate



Source: Bloomberg, I-Sec research (last price as on 20-Mar-20)

Airtel Africa: Healthy balance sheet, and self-sustainable

Airtel Africa's balance sheet is healthy enough to sail through the currently tough situation. We believe it can manage to hold up even if revenues dip for another couple of quarters in worst scenario. Airtel Africa's bank borrowing net of cash balance was US\$2bn compared to EBITDA (adjusted for lease obligation) of US\$346mn in Q3FY20. This works out to an ND/EBITDA ratio of 1.5x, which is very strong. Including lease liability, net debt was US\$3.2bn and ND/EBITDA was 2.1x, which too is healthy.

Further, Airtel Africa generated US\$40bn of FCF post finance cost and lease obligation in 9MFY20. We expect the African subsidiary to break even on FCF basis in FY20 itself, which means it is self-sustainable.

Table 4: Airtel Africa's balance sheet is healthy to sail through the currently tough situation

US\$ mn	Q3FY20
LT borrowings	2,503
ST borrowings	949
Total	3,452
Cash & equivalent	1,385
Net debt	2,067
Lease liabilities	1,166
Net debt incl lease liabilities	3,233
ND/EBITDA (Q3 annualised)	2.1

Source: Company data, I-Sec research

Table 5: Airtel Africa is self-sustainable, and we expect it to break even on FCF basis in FY20 itself

US\$ mn	9MFY20
CFO	1,009
Less	
Finance cost	247
Lease obligation	137
CFO after finance cost	625
Chg in working capital	(21)
CFO after working capital	604
Less	
Tangible assets	548
Intangible assets	16
FCF	40

Source: Company data, I-Sec research

Airtel Africa: We don't see much risk to estimates; impact on Bharti Airtel's fair value could be 3% in worst case

Considering past volatility and low visibility on the future, we have always been conservative in our estimates for Airtel Africa. We are factoring-in revenue and EBITDA CAGRs of just 4% and 5.3% respectively over FY20E-FY22E. Our EBITDA growth till FY22E is almost negligible at Q3FY20 reported numbers. Therefore, we remain fairly confident of Airtel Africa achieving these numbers; in fact, we can even see an upside if things stabilise.

Table 6: We conservatively estimate revenue and EBITDA CAGRs of just 4% and 5.3% for Airtel Africa over FY20E-FY22E

US\$ mn	FY19	FY20E	FY21E	FY22E
Revenue	3,077	3,323	3,489	3,594
<i>Growth (% YoY)</i>		8.0	5.0	3.0
EBITDA	1,196	1,296	1,378	1,438
<i>Growth (% YoY)</i>		8.3	6.3	4.3
<i>EBITDA (%)</i>	38.9	39.0	39.5	40.0
Depreciation and Amortisation	451	459	462	475
EBIT	745	837	916	962
<i>EBIT (%)</i>	24.2	25.2	26.3	26.8
PBT	434	620	711	772
PAT	230	337	394	431
<i>PAT margin (%)</i>	7.5	10.1	11.3	12.0

Source: Company data, I-Sec research

We have always assigned a higher multiple (6.0x FY22E) to Airtel Africa (vs market expectations) and we believe the subsidiary will eventually get higher valuation due to Airtel Money business. Airtel Money already contributes 9.3% of revenues and 10.2% to Airtel Africa's EBITDA. Airtel Money is a sticky business that helps in significantly reducing churn in the core mobile business. Airtel Money is also growing much faster and now contributes directly to profit. Airtel Money is also a higher RoCE business, hence deserves much higher multiples compared to the mainstream mobile business.

Airtel Africa contributes Rs42 to our SoTP valuation of Rs610 for Bharti Airtel, which means it contributes only 6.9% to Bharti Airtel's fair value. Even in worst case, if we assign 4.0x EV/EBITDA multiple to Airtel Africa, its contribution dips to Rs21, which means a cut of Rs21 to our present valuation. This works out to a 3.4% hit to our fair value for Bharti Airtel.

Table 7: In worst case, where we assign 4.0x EV/EBITDA multiple to Airtel Africa, the downside to Bharti Airtel's fair value is just 3.4%

US\$ mn	Base case FY22E	Scenario 1 FY22E	Scenario 2 FY22E
EBITDA	1,438	1,438	1,438
<i>Multiple (x)</i>	<i>6.0</i>	<i>5.0</i>	<i>4.0</i>
Enterprise value	8,626	7,188	5,751
Less: Africa local debt	234	234	234
Enterprise value	8,392	6,955	5,517
Less: Opco minority interest	420	348	276
Airtel Africa EV	7,973	6,607	5,241
Less: Net debt	2,471	2,471	2,471
Airtel Africa Equity value	5,501	4,136	2,770
<i>INR/USD</i>	<i>70.0</i>	<i>70.0</i>	<i>70.0</i>
Airtel Africa Equity value (Rs mn)	3,85,093	2,89,491	1,93,889
<i>Bharti Airtel stake (%)</i>	<i>56.0</i>	<i>56.0</i>	<i>56.0</i>
Attributable Airtel Africa Equity value (Rs mn)	2,15,652	1,62,115	1,08,578
Outstanding share (mn)	5,131	5,131	5,131
Attributable Airtel Africa Equity value (Rs/sh)	42	32	21
Bharti Airtel fair value (Rs/sh)	610	599	589
<i>Africa % of total fair value</i>	<i>6.9</i>	<i>5.3</i>	<i>3.6</i>

Source: Company data, I-Sec research

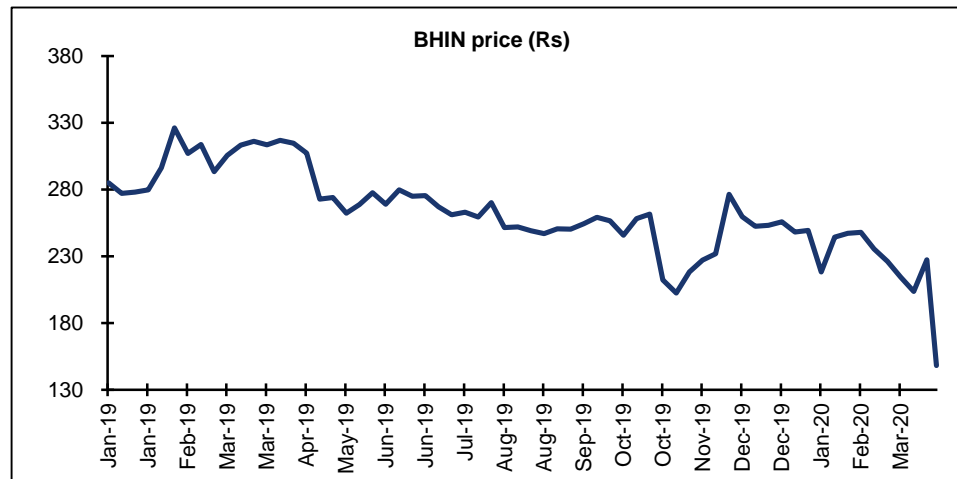
Concern-2: Risk to Bharti Infratel's fair value if Vodafone-Idea shuts shop

Vodafone-Idea (VIL) is an anchor tenant on Bharti Infratel and Indus Towers, and contributes significant EBITDA. VIL is facing its worst crisis post it lost its AGR dues case vs the government of India. Its AGR liability stands at Rs583bn. Promoters of VIL (Vodafone Plc and Aditya Birla Group) have earlier said if they are asked to pay the entire amount, they will have no option but to shut shop. We too don't see how VIL will cough up such a large sum entirely upfront.

VIL has contested the amount dues and submitted a self-assessment, which showed its dues at Rs215bn. However, on 18th Mar'20, the Supreme Court said it will not allow re-assessment of dues and ordered operators to pay dues based on DoT demand. This is a big blow to both Bharti Airtel and VIL, which expected their respective AGR dues to fall significantly if the self-assessment was accepted. The Supreme Court has agreed to DoT's request for a rescue plan, which is the only silver lining. However, the probability of VIL surviving has been fading. We believe the government would intervene and would not allow the industry to further consolidate in our base case.

Nonetheless, investors remain fearful (rightly so), and Bharti Infratel stock price has already dipped 42% in CY20-TD vs Nifty decline of 28%.

Chart 6: Bharti Infratel stock has dipped 42% in CY20-TD on fear of VIL shutdown



Source: Bloomberg, I-Sec research (last price as on 20-Mar-20)

Bharti Infratel contributes Rs53 to our SoTP valuation, or 8.6% of our fair value, for Bharti Airtel. In VIL exits, we see Bharti Infratel fair value decline by ~40%, which means Bharti Infratel contribution to Bharti Airtel would fall by Rs22 to Rs31. This works out to a hit of 3.5% to Bharti Airtel's fair value if VIL shuts down.

However, Bharti Airtel's mobile business will see windfall gain in the event of VIL winding up as the industry would become a duopoly. We believe the 3.5% downside can be easily offset by value gain in mobile business.

Table 8: Bharti Infratel contributes 8.6% to Bharti Airtel's fair value; VIL shutdown can erode Bharti Airtel's valuation by 3.5%

Rs mn	FY22E
Indus Towers	
Equity value based on DCF	6,30,343
<i>BHIN stake (%)</i>	42.0
Attributable Equity value	2,64,744
Bharti Infratel	
Equity value based on DCF	3,66,289
Bharti Infratel consolidated	6,31,033
<i>Bharti Airtel stake (%)</i>	53.5
Attributable Equity value	3,37,603
<i>Less: Holding company discount (%)</i>	20.0
Equity value	2,70,082
<i>Outstanding share (mn)</i>	5,131
Attributable Airtel Africa Equity value (Rs/sh)	53
Bharti Airtel fair value (Rs/sh)	610
<i>Africa % of total fair value</i>	8.6

Source: Company data, I-Sec research

Concern-3: INR depreciation

We have divided the impact of INR depreciation into two buckets: 1) impact on Airtel Africa, and 2) impact on India business – and the combined impact on Bharti Airtel's SoTP-based fair value.

Impact on Airtel Africa

Earlier, Airtel Africa incurred losses and had negative FCF, hence was a drag on Bharti Airtel, and INR depreciation only amplified the pain. Bharti India was funding the cash gap, which increased in INR terms on cross currency depreciation. The Africa entity had huge foreign currency debt and contributed negative equity value, which increased on INR depreciation (thereby lowering Bharti Airtel's fair value).

Airtel Africa is now a profitable and self-sustaining entity as explained in Concern-1. Therefore, cross-currency depreciation would now make a positive contribution to Bharti Airtel's consolidated EBITDA / net profit. Airtel Africa has also reduced considerable debt through the Africa opco tower sale and IPO proceeds, thus creating positive equity value, which would benefit from INR depreciation.

In our scenario analysis, if we decrease the INR/USD rate from Rs70 to Rs75, the translation impact of Airtel Africa on our estimate of Bharti Airtel's consolidated revenues and EBITDA would increase the numbers by 1.5%-2% each over FY20E-FY22E. In our scenario analysis, we have assumed stable Africa local currencies against the USD – which means the benefit will reduce if Africa currencies too depreciate.

Table 9: Bharti Airtel's consolidated revenues and EBITDA benefit from INR depreciation (assuming Africa local currencies are stable)

	FY20E	FY21E	FY22E
US\$ mn			
Revenue	3,323	3,489	3,594
EBITDA	1,296	1,378	1,438
EBITDA (%)	39.0	39.5	40.0
PBT	620	711	772
PAT	337	394	431
Rs mn (INR/USD = Rs70)			
Revenue	2,32,626	2,44,257	2,51,585
EBITDA	90,724	96,481	1,00,634
EBITDA (%)	39.0	39.5	40.0
PBT	43,394	49,764	54,048
PAT	23,584	27,577	30,159
Rs mn (INR/USD = Rs75)			
Revenue	2,49,242	2,61,704	2,69,555
EBITDA	97,204	1,03,373	1,07,822
EBITDA (%)	39.0	39.5	40.0
PBT	46,494	53,318	57,909
PAT	25,268	29,547	32,313
% change in consolidated due rupee depreciation			
Revenue	1.9	1.7	1.6
EBITDA	2.1	1.6	1.4

Source: Company data, I-Sec research

We also see Bharti Airtel's consolidated SoTP valuation benefiting from INR depreciation. If we change our INR/USD assumption from Rs70 to Rs75, Africa's contribution to Bharti Airtel's fair value increases to Rs45 from Rs42, and Bharti Airtel's SoTP valuation increase by 0.5%. This again assumes stable Africa local currencies; if they depreciate, the benefit reduces. Bharti Airtel's SoTP valuation would be negatively impacted if Africa currencies depreciate more than the INR. However, we note the impact on either case is negligible.

Table 10: INR depreciation positively impacts Bharti Airtel's SoTP valuation, though negligibly

	Base case FY22E	Scenario 1 FY22E
US\$ mn		
EBITDA	1,438	1,438
Multiple (x)	6.0	6.0
Enterprise value	8,626	8,626
Less: Africa local debt	234	234
Enterprise value	8,392	8,392
Less: Opco minority interest	420	420
Airtel Africa EV	7,973	7,973
Less: Net debt	2,471	2,471
Airtel Africa Equity value	5,501	5,501
INR/USD	70.0	75.0
Airtel Africa Equity value (Rs mn)	3,85,093	4,12,600
Bharti Airtel stake (%)	56.0	56.0
Attributable Airtel Africa Equity value (Rs mn)	2,15,652	2,31,056
Outstanding share (mn)	5,131	5,131
Attributable Airtel Africa Equity value (Rs/sh)	42	45
Bharti Airtel fair value (Rs/sh)	610	613
Africa % of total fair value	6.9	7.3

Source: Company data, I-Sec research

Impact from India business

Bharti India has currency exposure in three items: 1) foreign currency debt (for India business) and subsequent interest cost; 2) payables to capex creditors; and 3) capex spend.

Bharti follows a policy to hedge entire foreign currency payable for rolling 12 months. Therefore, we see significant exposure to foreign currency variations.

Notably, we understand Bharti India has foreign currency debt of US\$2bn; hence INR depreciation negatively impacts our SoTP valuation for Bharti Airtel. If INR/USD depreciates from Rs70 to Rs75, the impact on Bharti's equity value is Rs10bn, or Rs2/sh (0.3% dip in fair value).

Non-current payables to equipment suppliers stood at Rs16bn as of FY19-end. Current payables to capex creditors was Rs104bn. However, as we said, rolling 12-month foreign currency payables are hedged, so it does not have any impact from currency movements. We see negligible impact of INR depreciation on payables to suppliers.

Bharti Airtel has incurred capex of Rs81bn in India mobile business, and bulk of it would be imports. Therefore, INR depreciation certainly increases capex spend, but we also see deflation in pricing for capex equipment. Therefore, it is difficult to estimate the impact, but we are certain the impact on overall SoTP valuation would be negligible.

Concern-4: Rise in AGR dues

Bharti Airtel's cash balance situation is prepared for worst case in AGR; VIL will struggle

DoT AGR dues demand on Bharti group (including Telenor India) stands at Rs440bn compared to the company's provision of Rs353bn (however, based on self-assessment, it was just Rs130bn).

Considering the earlier strong observations by Supreme Court, we have the cash balance situation for Bharti Airtel and VIL in case of worst outcome in the next hearing (after two weeks), i.e. the Court rejects DoT's rescue plan, and operators are required to make the entire payment immediately. However, we see reasonable probability for the rescue plan getting approved on larger economic interest. We see Bharti Airtel having Rs190bn cash balance available against balance AGR dues of Rs260bn. Company is also generating free cashflow from its operations, and it has indemnity with Telenor for AGR dues (which means cash balance gap would be much lower for Bharti Airtel). We see no worst case risk for Bharti on the AGR dues front. However, we see VIL having cash balance of only Rs30bn, and it also needs to fund its quarterly cash losses from operations. We see VIL struggling to meet its AGR dues in a worst case scenario.

Table 11: AGR due for the operators

Rs mn	DoT demand	Self-assessment	Payments made	Balance
Bharti + Telenor	4,39,800	1,30,040	1,80,040	2,59,760
Vodafone Idea Ltd	5,82,540	2,15,330	68,540	5,14,000
Tata Group	1,67,980	21,970	41,970	1,26,010
BSNL	58,359			58,359
MTNL	43,521			43,521

Source: Company data, I-Sec research

Table 12: In case of full payment of AGR dues (worst case), Bharti Airtel can manage to pay up...

	Rs mn
Bharti Airtel consolidated cash & equivalent as on Q3FY20	3,07,224
Less: cash at	
Airtel Africa	98,834
Bharti Infratel	52,964
Bharti India cash	1,55,426
Add: Fund raising	
QIP	1,44,002
FCCB	72,001
Bharti India cash	3,71,429
Less: AGR payment made	1,80,040
Bharti India cash	1,91,389

Source: Company data, I-Sec research

Table 13: ...while VIL will struggle

	Rs mn
VIL cash & equivalent as on Q3FY20	1,28,152
Less: cash utilised	
AGR payment made	68,540
Spectrum EMI	30,000
VIL cash	29,612

Source: Company data, I-Sec research

Higher DoT demand poses 1.6% risk to our SoTP valuation for Bharti Airtel

We are already deducting Rs370bn towards AGR dues for Bharti Airtel to arrive at its fair value. However, DoT's demand is higher at Rs440bn and we don't see this amount reducing; hence it poses risk to our SoTP-based valuation for Bharti Airtel.

We estimate Telenor India's AGR dues at Rs20bn out of the Rs440bn where Bharti Airtel has indemnity on these liabilities in its merger agreement. Therefore, we see an additional risk of Rs50bn to Bharti Airtel's equity value, or an additional hit of Rs10/sh. This works out to 1.6% of our fair value for Bharti Airtel.

Table 14: DoT demand when charged to Bharti Airtel's fair value, leads to a downside of 1.6%

Rs mn	FY22E
DoT demand	4,39,800
Less	
Telenor India share (Indemnity)	20,000
Charged to Bharti's SoTP value	3,70,000
Additional charge	49,800
<i>Outstanding share (mn)</i>	<i>5,131</i>
Attributable Airtel Africa Equity value (Rs/sh)	10
Bharti Airtel fair value (Rs/sh)	610
<i>Africa % of total fair value</i>	<i>1.6</i>

Source: Company data, I-Sec research

Table 15: Bharti Airtel – SoTP-based valuation

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

Source: Company data, I-Sec research

Financial summary

Table 16: Profit & loss statement

(Rs mn, year ending March 31)

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

Source: Company data, I-Sec research

Table 17: Balance sheet

(Rs mn, year ending March 31)

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

Source: Company data, I-Sec research

Table 18: Quarterly trend

(Rs mn, year ending March 31)

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

Source: Company data

Table 19: Cashflow statement

(Rs mn, year ending March 31)

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

Source: Company data, I-Sec research

Table 20: Key ratios

(Year ending March 31)

	FY19	FY20E	FY21E	FY22E
Per Share Data (in Rs.)				
Recurring EPS	(4.1)	(0.5)	15.5	25.1
Reported EPS	3.2	(0.5)	15.5	25.1
Recurring Cash EPS	49.3	43.1	59.6	69.7
Dividend per share (DPS)	2.5	2.6	2.8	2.9
Book Value per share (BV)	178.7	191.4	203.5	225.1
Growth Ratios (%)				
Operating Income	(3.5)	10.4	15.0	10.7
EBITDA	(14.2)	22.2	37.5	17.2
Recurring Net Income	(187.2)	(83.6)	NM	62.6
Diluted Recurring EPS	(187.2)	(87.2)	NM	62.6
Diluted Recurring CEPS	(6.8)	(12.6)	38.4	17.0
Valuation Ratios (% YoY)				
P/E	(99.7)	(781.5)	26.6	16.4
P/CEPS	8.4	9.6	6.9	5.9
P/BV	2.3	2.2	2.0	1.8
EV / EBITDA (incl Indus)	11.3	8.6	6.4	5.3
EV / Operating Income	4.0	3.4	2.9	2.5
EV / Operating FCF	(17.8)	(179.2)	44.8	21.0
Operating Ratios				
Other Income / PBT (%)	(40.4)	60.1	7.8	5.3
Effective Tax Rate (%)	73.4	46.0	28.5	27.5
NWC / Total Assets (%)	(9.8)	(11.2)	(6.2)	(2.1)
Inventory Turnover (days)	0.6	0.6	0.6	0.6
Receivables (days)	19.4	84.9	77.1	70.7
Payables (days)	181.0	173.2	151.7	136.9
Net Debt/EBITDA Ratio (x)	4.3	2.9	2.0	1.5
Capex % of sales	38.0	28.3	24.2	20.4
Profitability Ratios (%)				
Rec. Net Income Margins	(2.0)	(0.3)	7.7	11.4
RoCE	2.2	2.1	6.6	8.6
RoIC	0.9	2.9	8.0	10.7
RoNW	(2.3)	(0.3)	7.8	11.7
Dividend Yield	0.5	0.6	0.6	0.6
EBITDA Margins	32.0	35.4	42.3	44.8

Source: Company data, I-Sec research

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