

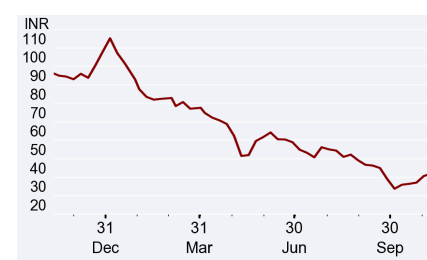
# Vodafone Idea (VODA.BO)

## Results: Equity Raise Should Allay Concerns; Operationally Weak

- Citi's Take** — Vodafone Idea announced a potential plan to raise up to Rs250bn in equity capital by 4QFY19, with both Vodafone Group (Rs110bn) and Aditya Birla Group (Rs72.5bn) intending to participate – sending a strong signal of commitment to the business and its investment requirements. The investment amounts to significant dilution (70%) at current depressed valuations but should be positive, as it should help address going-concern risks emanating from high leverage and losses. Business continuity should be positive for Bharti Infratel as well, in our view.
- Pro-forma metrics – some reclassifications, task cut out now** — 2QFY19 pro-forma revenue declined 7% QoQ; EBITDA margin at 8.1% declined 250bps QoQ, as the combined entity lost c13mn subscribers, and ARPU fell 5% QoQ. Vodafone Idea's subs total 422mn (and c36% rev. market share) – including c100mn broadband subs (vs. 66mn for Bharti and 250mn+ for Jio). However, data usage/sub appears lower – at <8GB/mth for broadband subs vs. >11GB/mth for Jio and >9GB/ mth for Bharti. ARPU was Rs88 (Bharti at Rs100 and Jio at Rs131). The reported sub-base includes some reclassifications – we await clarity at the November 21st analyst meeting.
- Net debt and capex** — Net debt was Rs1.1tn; Vodafone Idea could reduce this by cRs330bn via the capital raise announced as well as the sale of its 11.15% shareholding in Indus Tower and the fibre asset monetization plan announced. Pro-forma capex for 1H FY19 was Rs58bn – well below the Rs330bn spend for Jio and Rs128bn for Bharti (India mobile only).
- Implications** — The capital raise is a positive, in our view. Realization of opex/capex synergy benefits from the merger is critical (the company expects NAV of total synergies extractable at US\$10bn). Management commentary indicates that the merger synergy realization plan is on track – translation into substantial margin gains in the coming quarters is important. Going forward, execution on synergy extraction, 4G network rollout (77% broadband tower penetration vs. 90% for Bharti), and broadband subs trend are critical to watch.

<b>Buy/High Risk</b>	<b>1H</b>
Price (14 Nov 18 15:30)	Rs41.15
Target price	Rs83.00
Expected share price return	101.7%
Expected dividend yield	0.0%
<b>Expected total return</b>	<b>101.7%</b>
Market Cap	Rs359,461M
	US\$4,950M

### Price Performance (RIC: VODA.BO, BB: VODA IN)



### Statistical Abstract

Year to	Net Profit	Diluted EPS	EPS growth	P/E	P/B	ROE	Yield
31 Mar	(RsM)	(Rs)	(%)	(x)	(x)	(%)	(%)
2017A	-9,622	-2.67	-131.2	-15.4	0.6	-3.8	0.0
2018A	-41,682	-9.56	na	-4.3	0.7	-16.0	0.0
2019E	-56,000	-12.85	-34.3	-3.2	0.8	-22.9	0.0
2020E	-55,385	-12.71	1.1	-3.2	1.1	-29.3	0.0
2021E	-52,067	-11.94	6.0	-3.4	1.6	-38.5	0.0

Source: Powered by dataCentral

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### See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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Figure 1. Pro-forma results summary

(In Rs m)	1QFY19	2QFY19	QoQ %
Revenue	129,441	120,238	-7%
EBITDA	13,722	9,778	-29%
EBITDA Margin %	10.60%	8.10%	
Capex	25,213	32,956	31%
ARPU (Rs/mth)	92	88	-4%
Minutes on network (m)	732,837	731,195	0%
Data volume (petabytes)	1,889	2,260	20%

Source: Company reports and Citi Research

Figure 2. Reported results summary

	2QFY19*	1QFY19	QoQ %	2QFY18	YoY %
<b>Gross revenues</b>	<b>76,635</b>	<b>58,892</b>	<b>30.1%</b>	<b>74,655</b>	<b>2.7%</b>
Employee cost	(4,958)	(3,924)	26.4%	(4,418)	12.2%
Network opex	(35,976)	(26,427)	36.1%	(25,361)	41.9%
License fees and spectrum charges	(7,990)	(5,961)	34.0%	(7,689)	3.9%
Access and Interconnect charges	(9,478)	(7,744)	22.4%	(11,198)	-15.4%
Advertising and SAC costs	(9,105)	(6,236)	46.0%	(8,854)	2.8%
Other expenditure	(4,514)	(2,006)	125.0%	(2,119)	113.0%
Total Opex	(72,021)	(52,298)	37.7%	(59,639)	20.8%
<b>EBITDA</b>	<b>4,614</b>	<b>6,594</b>	<b>-30.0%</b>	<b>15,016</b>	<b>-69.3%</b>
<b>EBITDA margins (%)</b>	<b>6.0%</b>	<b>11.2%</b>		<b>20.1%</b>	
Depreciation and Amortisation	(30,059)	(20,924)	43.7%	(21,143)	42.2%
EBIT	(25,445)	(14,330)	77.6%	(6,127)	315.3%
Interest Charge	(21,662)	(15,258)	42.0%	(12,283)	76.4%
Dividend from Indus	423	598		843	
<b>PBT</b>	<b>(44,533)</b>	<b>(27,576)</b>	<b>61.5%</b>	<b>(17,113)</b>	<b>160.2%</b>
Tax	453	(3,504)	-112.9%	6,047	-92.5%
Exceptional Items	(5,658)	33,645		0	
<b>PAT</b>	<b>(49,738)</b>	<b>2,565</b>	<b>-2039.1%</b>	<b>(11,066)</b>	<b>349.5%</b>

Source: Company reports and Citi Research \*2Q19 includes post-merger results for period from 31Aug-30Sep'18

Figure 3. Pro-forma KPIs

	1QFY19	2QFY19
Subscriber base (m)	435.4	422.3
ARPU blended	92	88
Average MoU (mins)	555	568
Blended Churn %	4.1%	4.3%
Total unique towers	201,854	202,650
Total unique broadband towers	151,544	155,511
Total broadband sites	340,709	365,575
Total MoU (m mins)	732,837	731,195
Total data volume (Petabytes)	1,889	2,260
Total data subscribers (m)	141.7	140.1
Data usage by data subscriber (MB)	5,114	5,740
Broadband subscribers (m)	95.3	99.7

Source: Company reports and Citi Research

## Vodafone Idea

### Valuation

Our target price for Idea is Rs83/share. We value the company on FY24E, which we believe is the appropriate steady state year to value the combined entity as 1) migration to 4G would be complete, 2) competitive intensity would have normalized as market shares stabilize and network utilization reaches optimum level, and 3)

Idea + Vodafone would have achieved their steady stage synergy run rate. We apply EV/EBITDA valuation methodology to Idea + Vodafone's FY24E EBITDA and discount back to Sep-19E to arrive at our target price. We value Idea at a 20% premium to its historical trading average (since listing; 2007) i.e. at 10x EV/EBITDA. This is at a 35% premium to Airtel's long-term trading average. The premium (against history and Airtel) is justified, in our view, due to the above-average EBITDA growth that we expect the business to generate.

## Risks

We assign a High Risk rating given the inherent volatility due to high leverage. Key downside risks that could push the stock below our target price include 1) protracted competitive intensity as Airtel/Jio compete for market share even beyond normalization of shares and increased network utilization; 2) lower synergy benefits; and 3) leverage continues to sharply rise despite efforts to reduce gross debt thereby pressuring cash flows.

## Bharti Infratel

(BHRI.BO; Rs261.00; 1; 14 Nov 18; 15:30)

## Valuation

Our target price for Bharti Infratel of Rs354 is arrived at using a SOTP approach. We value the standalone business and Indus Towers, where it holds a 42% stake separately using DCF. Infratel's is valued at Rs202/share and its stake in Indus at Rs152/share. This includes our explicit assumptions of the small cell opportunity.

Our DCF based on Mar-19E is based on explicit forecasts for FY19-26E, with terminal growth rate of 3%. WACC for the stand-alone business at 10.4% (7% risk free rate, 7% market risk premium, unlevered beta at 0.68 and 8% cost of debt) is slightly higher than that for Indus at 9.7% (7% risk free rate, 7% market risk premium, unlevered beta at 0.6 and 8% cost of debt) given the stand-alone business' sub-optimal capital structure.

The target price implies a Mar-20E EV/EBITDA multiple of 10.7x, 7% premium to its historical trading average. We believe that the multiple is fair given medium-term growth prospects - 2/4% colocations/EBITDA CAGR (FY20E-27E).

## Risks

Lower-than-expected rationalization of towers of the merging Idea and Vodafone and Jio colocation additions are the key upside risks. Key downside risks that could impede the stock from reaching our target price include a) higher-than-expected tenancy loss from consolidation, b) lower-than-expected revenue accretion from small cells as operators deploy in-house, c) use of massive MIMO leads to lower than-expected need for incremental sites, and d) value dilutive acquisitions to deploy cash generated by the business or cash available due to leveraging up the balance sheet to move toward a more efficient capital structure.

# Appendix A-1

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Analyst: Vijit Jain  
Covered since September 25 2018



	Date	Rating	Target Price	Closing Price
1	29-Nov-15 00:00:23	1	*500.00	399.05
2	02-Feb-16 07:26:38	1	*470.00	366.50
3	09-May-16 01:48:26	1	*480.00	378.00
4	26-Jul-16 05:30:53	1	*460.00	362.00

	Date	Rating	Target Price	Closing Price
5	27-Jul-16 19:42:04	1	*475.00	380.90
6	05-Feb-17 23:47:16	*2	*315.00	299.00
7	19-Apr-17 02:29:48	2	*335.00	347.50
8	10-May-17 03:05:04	2	*365.00	366.90

	Date	Rating	Target Price	Closing Price
9	06-Jul-17 03:33:08	*1	*470.00	412.60
10	30-Jan-18 17:00:00	1	*425.00	343.00
11	01-Oct-18 07:04:54	1	*396.00	265.05
12	25-Oct-18 14:15:12	1	*354.00	265.80

\*Indicates Change

Rating/target price changes above reflect Eastern Time

### Vodafone Idea (VODA.BO)

#### Ratings and Target Price History Fundamental Research

Analyst: Vijit Jain  
Covered since September 25 2018



	Date	Rating	Target Price	Closing Price
1	21-Jan-16 17:51:49	3	*110.00	113.90
2	09-May-16 02:18:50	3	*100.00	114.50
3	18-Aug-16 04:12:32	3	*91.00	93.80

	Date	Rating	Target Price	Closing Price
4	01-Sep-16 20:49:15	3	*70.00	83.35
5	15-Feb-17 02:12:34	3	*100.00	107.15
6	10-Apr-17 19:37:01	3	*80.00	87.80

	Date	Rating	Target Price	Closing Price
7	15-May-17 18:01:34	3	*78.00	86.05
8	31-Jul-17 00:03:16	3	*75.00	92.30
9	30-May-18 06:00:00	*1H	*83.00	61.55

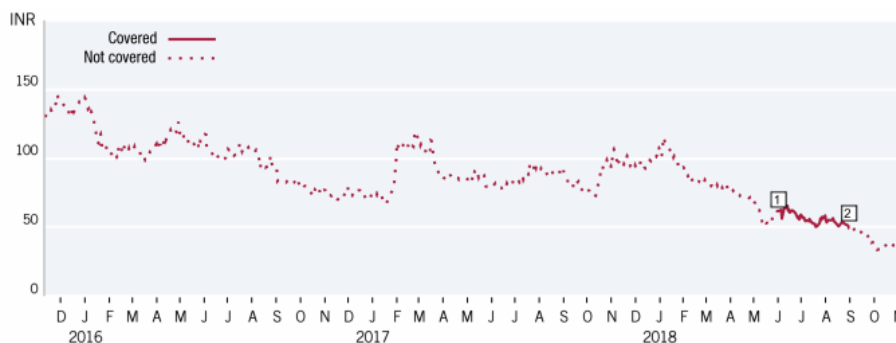
\*Indicates Change

Rating/target price changes above reflect Eastern Time

## Vodafone Idea (VODA.BO)

### Catalyst Watch Research

Analyst: Vijit Jain  
Covered since September 25 2018



	Date	Expected Direction	Duration	Action	Closing Price
1	30-May-18 06:00:00	Upside	90 Days	Open	61.55

	Date	Expected Direction	Duration	Action	Closing Price
2	28-Aug-18 09:41:50	Upside	90 Days	Close	51.20

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12 Month Rating			Catalyst Watch		
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54%	35%	11%	9%	88%	3%
64%	63%	56%	70%	64%	63%

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