

# TIM Brasil

## 1Q23 Preview: Tug of war

LatAm Telecom

### Main takeaways:

**(i)** We expect accesses to drop (-1.2% q/q Genial Est.), with the reclassification of part of Oi's clients; **(ii)** TIM Ultrafibra growing in FTTH (+6.4% q/q Genial Est.); at the expense of FTTC (-12.1% q/q Genial Est.); **(iii)** We project ARPUs to be slightly up (+1.0% q/q Genial Est.); Revenue should come in accelerated y/y (+17.7% Genial Est.), but shrinking q/q (-5.3% Genial Est.); **(iv)** Pressure on costs is the new normal; **(v)** We should see slightly weaker EBITDA (-10.3% q/q Genial Est.); **(vi)** Net profit should follow top line decline (-43.7% q/q Genial Est.).

TIM Brasil will release its 1Q23 result on May 08<sup>th</sup>, after market close. We expect the quarter to be solid but with a **deceleration's sings**, with a **slight q/q drop but a y/y increase** as the clients' base continues to reflect the part acquired from Oi Móvel. Besides that, **1Q23 will be the first quarter with a fair year-on-year comparison basis regarding fiber**, counting on the change in the business model after the I-System sale, which **led to the Company changing CAPEX for OPEX**.

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### Company

#### TIMS3 BZ Equity

Buy

Price: R\$ 13.80 (05-May-2023)

Target Price 12M: R\$ 16.00

## 1Q23 Preview

**We expect accesses to drop, with the reclassification of part of Oi's clients.** With the data reported by Anatel about the number of mobile accesses in 1Q23, we see that TIM closed the quarter with 61.7mn, a drop of -1.2% q/q, despite the increase of +18.0% y/y. We expect to report postpaid accesses falling, with prepaid ones rising due to a reclassification of clients acquired from Oi Móvel, in which they were classified by Oi as postpaid clients, but in TIM's view belong to hybrid prepaid plans (Plano Controle).

Therefore, we have in the subdivision a net addition in the prepaid segment of 413k users in 1Q23, while the postpaid segment we project a decrease of -1,117k. Thus, consolidating a customer base of 35.6mn Genial Est. in the prepaid plan (+1.2% q/q; +22.6% y/y), and a base of 26.0mn Genial Est. in the post (-4.3% q/q; +12.3% y/y).

**TIM Ultrafibra growing in FTTH at the expense of FTTC.** Keeping the momentum seen in the broadband market, the most updated and fastest technology should continue to increase accesses, reaching 584mn Genial Est. in 1Q23 (+6.4% q/q; +33.5% y/y). At the other end, FTTC, should continue to fall, expected to lose -12.1% q/q and coming in at our estimates at 147mn. Still, TIM Ultrafibra's total accesses should grow, since the data reported by Anatel show that the rise in FTTH more than compensates the loss of FTTC, with 732mn at the end of 1Q23 (+2.2% q/q; +6.2% y/y).

**We project ARPUs to be slightly up.** We expect a slight increase for all the Company's ARPUs, with the mobile portion reaching ARPU of R\$27.1 Genial Est. (+1.0% q/q), driven by increases in Prepaid ARPU of +2.1% q/q to R\$14.0 and +2.1% q/q in Postpaid ARPU.

Despite not having an effect on consolidated mobile ARPU, we expect that the reclassification of part of the customer base coming from Oi Móvel, with the downgrade from Postpaid to Prepaid, should bring a cleaner ARPU for the Postpaid plan, with the exclusion of a representative part of customers that were driving down the segment's ARPU. Therefore, we also expect the same effect to be responsible for a slight increase in Prepaid ARPU, as it includes a part with a relatively higher average ticket, precisely because they are customers from a hybrid plan.

Furthermore, we did not see any relevant price adjustments during the quarter, so that they should be made in 2Q23 and add to the results going forward. Thus, we can also expect readjustments in Oi's client base, who arrived in 2Q22 and have a non-adjustment contract for 1 year, with this term coming to an end in 2Q23. With the trend of switching from FTTC to FTTH, TIM Ultrafibra's ARPU should continue to show small upward trends, since congruent with the improvement in speed and stability of the internet connection, we observe a premium and more expensive service, which in our projection should reach R\$95.4 Genial Est., a very slight increase of +0.4% q/q and +4.3% y/y.

**Table 1. Operationals TIM (1Q23 Genial Est.)**

(R\$ millions)	1Q23E	4Q22	% q/q	1Q22	% y/y
	Genial Est.	Consolidated		Consolidated	
<b>Total Base</b>	<b>62.455</b>	<b>63.201</b>	<b>-1,2%</b>	<b>52.994</b>	<b>17,9%</b>
<b>TIM Ultrafibra Costumer Bas</b>	<b>734</b>	<b>716</b>	<b>2,6%</b>	<b>689</b>	<b>6,5%</b>
FTTH	587	549	7,0%	438	34,2%
FTTC	147	167	-12,0%	252	-41,5%
<b>Mobile Costumer Base</b>	<b>61.721</b>	<b>62.485</b>	<b>-1,2%</b>	<b>52.305</b>	<b>18,0%</b>
Pre-pago	35.372	35.240	0,4%	29.089	21,6%
Pós-pago	26.349	27.245	-3,3%	23.215	13,5%
<b>Mobile Monthly Churn (%)</b>	<b>4,2%</b>	<b>7,1%</b>	<b>-2,83p.p</b>	<b>3,1%</b>	<b>1,12p.p</b>
<b>Tim Ultrafibra ARPU (R\$)</b>	<b>95,4</b>	<b>95,0</b>	<b>0,4%</b>	<b>91,4</b>	<b>4,3%</b>
<b>Mobile ARPU (R\$)</b>	<b>27,5</b>	<b>26,9</b>	<b>2,2%</b>	<b>27,4</b>	<b>0,1%</b>
Prepaid	14,0	13,7	2,1%	13,2	5,8%
Postpaid	39,0	38,2	2,1%	39,1	-0,1%

Source: TIM, Genial Investimentos

**Revenue should come in accelerated y/y, but shrinking q/q.** In a mild slowdown typical of 1Qs, we expect reported net revenues to fall slightly to R\$5.5bn Genial Est. (-5.3% q/q; +17.7% y/y), influenced by a small retraction in mobile service revenues, its most representative business, which should hit R\$5.0bn Genial Est.

On the fixed services side, we expect flat revenues, with FTTH increments being offset by FTTC losses, to reach a revenue within TIM Ultrafibra similar to 4Q22, hitting R\$207mn Genial Est. (-0.1% q/q; +8.2% y/y). Therefore, we project a revenue of R\$321mn Genial Est. for the fixed service, with a +8.1% y/y growth, but moving sideways on a quarterly basis.

In handset and devices sales, despite expecting a -24.0% q/q deceleration due to strong seasonality common to 4Qs as a result of year-end events that stimulate retail, we still estimate a +30.1% y/y growth. We believe that the operation was driven by a higher share of premium products, mainly related to Apple devices, in addition to inflation, which continues to have an effect and helps to pass on product prices; therefore, we expect a net revenue of R\$187mn Genial Est. in 1Q23 for the unit.

**Table 2. Revenue TIM (1Q23 Genial Est.)**

(R\$ millions)	1Q23E	4Q22	% q/q	1Q22	% y/y
	Genial Est.	Consolidated		Consolidated	
<b>Net Revenue</b>	<b>5.633</b>	<b>5.874</b>	<b>-4,1%</b>	<b>4.727</b>	<b>19,2%</b>
<b>Mobile Service</b>	<b>5.115</b>	<b>5.305</b>	<b>-3,6%</b>	<b>4.286</b>	<b>19,3%</b>
Client Generated	4.665	4.869	-4,2%	3.900	19,6%
Interconnection	120	113	5,8%	112	7,0%
Costumer Platform	53	51	4,0%	35	49,4%
Others	277	271	2,0%	239	15,9%
<b>Fixed Service</b>	<b>322</b>	<b>323</b>	<b>-0,5%</b>	<b>297</b>	<b>8,2%</b>
TIM Ultrafibra	208	207	0,1%	192	8,4%
Others	114	116	-1,7%	106	7,9%
<b>Products</b>	<b>196</b>	<b>246</b>	<b>-20,1%</b>	<b>143</b>	<b>36,8%</b>

Source: TIM, Genial Investimentos

**Pressure on costs is the new normal.** Since the control stake sale of I-Systems, its fiber internet company, to IHS, TIM has added a fixed cost in its operation, focused on the lease of the neutral network. The counterpart is the reduction in the level of CAPEX for the expansion in the reach of TIM Ultrafibra, which it would have had to spend it on if it had not sold the control. In theory, the effect would tend to be cash flow neutral, in the worst-case scenario, but our evaluation is that there is already a significant increase in costs, bringing only the negative side in the short term, without the counterpart that we would like to see in CAPEX.

Still following the OPEX expansion, some costs seem to us to be tied to Oi Móvel's assets along with its customer base. So, we see that some should still be maintained, but with a view of smoothing over time. An example we highlight is PDA, in which TIM maintains a good credit management, causing us to have a view of line improvement, but that in the year-on-year comparison should still come in high, with a similar level since 2Q22, after the consolidation of the acquired operator, which came with clients more likely not to pay than when compared to clients originated by TIM itself.

Therefore, we expect TIM's costs to come in at -R\$2.9bn Genial Est., showing a stability q/q, but an acceleration of +12.7% y/y, without much prospect of improvement in the short term, given the change in the business model.

**We should see slightly weaker EBITDA.** Based on a net revenue expected to fall, coupled with the maintenance of costs, we expect a shrinking EBITDA q/q, but it should still show a significant increase y/y, mainly due to the acquisition of Oi Móvel, which even bringing costs and expenses, managed to create a revenue increase that offset the M&A in absolute terms.

Our projection points to an EBITDA of R\$2.6bn Genial Est. (-10.3% q/q), with an EBITDA margin of 47.3%, falling -2.63p.p. Year-on-year, we project a +23.8% rise in EBITDA with a margin up +2.35p.p, which may make 1Q23 one of the few quarters in which we will see a margin increase y/y, precisely because, until then, we had not found signs of post-M&A improvement in relative terms.

**Net profit should follow top line decline.** With a projection for a financial result of -R\$344mn, we still see a higher leverage than the historical average penalizing the operational result with high financial expenses, reaching a net profit of R\$332mn Genial Est., contracting -43.7% q/q and -20.7% y/y.

The short-term drop is justified by an expectation of a slight retraction in revenue, while costs should remain at a similar level. Looking at a longer timeframe, we see that since the acquisition of Oi, even with a nominally rising EBITDA, the **(i)** depreciation increasing due to a larger amount of weak assets acquired, and a **(ii)** financial result with higher interest on its debt, hindered the formation of net income, causing our expectation to be a drop y/y, with a net margin at 6.0%, down by -4.08p.p y/y and -2.89p.p y/y.

**Table 3. Income Statement TIM (1Q23 vs. Genial Est.)**

(R\$ millions)	1Q23E	4Q22	% q/q	1Q22	% y/y
	Genial Est.	Consolidated		Consolidated	
<b>Net Revenue</b>	<b>5.633</b>	<b>5.874</b>	<b>-4,1%</b>	<b>4.727</b>	<b>19,2%</b>
COGS	(3.016)	(2.944)	2,5%	(2.604)	15,8%
<b>EBITDA</b>	<b>2.616</b>	<b>2.930</b>	<b>-10,7%</b>	<b>2.123</b>	<b>23,2%</b>
EBITDA Margin (%)	46,5%	49,9%	-3,44p.p	44,9%	1,54p.p
D&A	(1.839)	(1.858)	-1,0%	(1.399)	31,5%
<b>EBIT</b>	<b>777</b>	<b>1.072</b>	<b>-27,5%</b>	<b>724</b>	<b>7,3%</b>
EBIT Margin (%)	13,8%	18,3%	-4,46p.p	15,3%	-1,52p.p
Financial Result	(344)	(350)	-1,8%	(248)	38,6%
<b>Net Income</b>	<b>322</b>	<b>590</b>	<b>-45,4%</b>	<b>419</b>	<b>-23,1%</b>
Net Margin (%)	5,7%	10,0%	-4,33p.p	8,9%	-3,14p.p

Source: TIM, Genial Investimentos

### Our Take on TIM

We expect 1Q23 to be a continuation of what has been seen in the last few quarters, pursuing synergies after the acquisition of Oi Móvel, based on an active management of the customer base and its classification, with its respective implicit costs. In the short term, we see that TIM should present solid results, but still impacted by its leverage of 1.4x Net Debt/EBITDA at the end of 4Q22, which should remain at similar levels for 1Q23, with a more significant cooling off only coming towards the end of the year and the return to the historic average only for 2024.

**Tug of war.** Looking ahead, we put great weight in our bias for the Company in relation to its ability to upsell its mobile customer base, especially considering the adjustments Oi's base may add. However, **we still see TIM one step behind Telefônica Brasil (Vivo)** in its ability to transition clients from prepaid to postpaid plans. Considering that the contracts coming from Oi mobile may be subject to readjustments as of 2Q23, we see that there is a cost catalyst to unlock value, while a frustration if it does not occur may worsen the expectation of ARPU increase in its base going forward.

In addition, we have the readjustment of its organic base, which began in April, with an increase of R\$3 to R\$6 for control plans, with Postpaid between R\$15 to R\$30 depending on the package. Thus, we see as positive the readjustment, which if it does not result in a large increase in cancellations, results in a slight increase of upside in our accounts, even with the maintenance of still strong costs. Therefore, we believe that the higher investments combined with an also higher leverage, continue to pull the cash generation down. However, we see that the readjustments, both of the own base and the long-awaited readjustment on the customer base coming from Oi Móvel can promote greater margin gain and create a cash flow increase. So, we see an effect in the short term as two vectors making forces in opposite directions, similar to a tug-of-war.

We believe that within the next few quarters the **readjustments may speak louder to investors in terms of triggers for the stock prices**, as higher leverage and a higher level of CAPEX already seem to have priced in. Thus, **we still see TIM relatively discounted**, trading at an **EV/EBITDA of 4x in 23E**, we maintain our **BUY recommendation, raising the Target Price to R\$16.00** vs. R\$15.50 previously, which implies a current **upside of +15.94%**.

## Appendix: TIM

**Figure 1. TIM – Income Statement in R\$ Millions (Genial Est. 2023-2028)**

<b>Income Statement</b>	<b>2023E</b>	<b>2024E</b>	<b>2025E</b>	<b>2026E</b>	<b>2027E</b>	<b>2028E</b>
<b>Net Revenue</b>	<b>22.575</b>	<b>23.036</b>	<b>23.674</b>	<b>24.397</b>	<b>25.199</b>	<b>25.984</b>
(-) COGS	(11.778)	(12.611)	(13.383)	(13.909)	(14.373)	(14.820)
<b>EBITDA</b>	<b>10.796</b>	<b>10.425</b>	<b>10.291</b>	<b>10.488</b>	<b>10.826</b>	<b>11.164</b>
(-) D&A	(7.145)	(6.356)	(5.993)	(5.723)	(5.532)	(5.405)
<b>EBIT</b>	<b>3.651</b>	<b>4.070</b>	<b>4.298</b>	<b>4.765</b>	<b>5.294</b>	<b>5.759</b>
(+/-) Financial Result	(1.232)	(559)	(316)	(98)	103	292
<b>EBT</b>	<b>2.236</b>	<b>2.837</b>	<b>3.455</b>	<b>4.206</b>	<b>4.978</b>	<b>5.661</b>
(-) Taxes	(548)	(776)	(927)	(1.110)	(1.298)	(1.464)
<b>Net Income</b>	<b>1.688</b>	<b>2.061</b>	<b>2.528</b>	<b>3.096</b>	<b>3.680</b>	<b>4.197</b>
<b>Profitability</b>						
Net Margin (%)	7,48%	8,95%	10,68%	12,69%	14,61%	16,15%

**Figure 2. TIM– Cash Flow in R\$ Million (Genial Est. 2023-2028)**

<b>Cash Flow</b>	<b>2023E</b>	<b>2024E</b>	<b>2025E</b>	<b>2026E</b>	<b>2027E</b>	<b>2028E</b>
<b>Net Revenue</b>	<b>22.575</b>	<b>22.706</b>	<b>23.011</b>	<b>23.357</b>	<b>23.741</b>	<b>24.165</b>
(-) COGS	(11.778)	(11.640)	(11.805)	(11.990)	(12.195)	(12.420)
<b>EBITDA</b>	<b>10.796</b>	<b>11.066</b>	<b>11.206</b>	<b>11.366</b>	<b>11.546</b>	<b>11.745</b>
<b>EBIT</b>	<b>3.651</b>	<b>4.070</b>	<b>4.298</b>	<b>4.765</b>	<b>5.294</b>	<b>5.759</b>
(-) Taxas	(548)	(776)	(927)	(1.110)	(1.298)	(1.464)
(+) D&A	7.145	6.356	5.993	5.723	5.532	5.405
(+/-) Δ WK	12	(199)	151	55	22	19
(-) Capex	(4.063)	(4.147)	(4.261)	(4.391)	(4.536)	(4.677)
<b>FCFF</b>	<b>6.198</b>	<b>5.304</b>	<b>5.254</b>	<b>5.042</b>	<b>5.014</b>	<b>5.042</b>

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