

Telekom Malaysia Bhd

Looking Out for 2H19

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TM's 2H19 could see top-line weakness on lower ARPU from new product pricing, in our view. Better cost structures should persist, albeit at a slower scale than 1H19 on back-loaded operations. We believe its shares sell-down triggered by mobile-related news could be overdone, as we believe any near-term implementation and the scale would not be materially impactful. Maintain OP and DCF-driven TP of RM3.95 (WACC: 9.5%, TG: 1.5%).

Tightrope for top-line. In the recent 1H19 results, revenue decline of 4% YoY was mainly caused by lower voice and internet demand (fewer Streamyx subscribers but buffered a growing Unifi base). We believe the guidance for a low to mid-single digit decline in FY19 should still hold, as demand for main products will likely be weaker on stiffer competition. With new pricings being offered since Sep 2019 heading the government's call to make internet more assessable, it will be interesting to see the consumers' response towards the brand. However, this could dent ARPU numbers in 2H19 (vs. 2Q19 Streamyx @ RM86/user and Unifi @ RM177/user). That said, the commissioning of customer projects in 2H could offer some revenue support.

Cost snipping. Yield from the Performance Improvement Plan (PIP) should continue to trickle into 2H19 results, albeit at a lower rate than 1H19 due to the group typically being operationally back-loaded. Recall that 1H19 registered opex improvements of 11%, which translated to EBIT of RM777.9m (+75% YoY) and margin of 14.0% (+6.3ppt). We are banking on margin to persist at this robust level, but caution that 2H projects could undermine direct costs. At the meantime, the abovementioned compressed ARPU could also contribute to weaker margins. Nonetheless, we believe it would be highly unlikely for the group to miss its FY19 EBIT guidance of being better than FY18.

Finding the right way forward. Market has been abuzz on the recent news that the group is looking to venture aggressively into mobile. We believe that a likely hurdle in its implementation could be the upcoming assignment by MCMC of the 700MHz, 2300MHz and 2600MHz spectrums by 2H20. However, do recall that its mobile business has been operational since Jan 2018 and thus not an entirely new venture for the group.

Also, during the recent MCMC Public Inquiry, the group expressed itself as suitable for allocation of the entire spectrum blocks to facilitate 5G in the future owing to their extensive nationwide fibre coverage. However, reiterating views from our 10 Sep 2019 sector report "Spectrum Inquiry; The Word is Out", we believe that condensing spectrum licenses may not make the most commercial sense as it does not give other operators an equal ground to experiment the most efficient use of the spectrums. Additionally, monopolistic issues may arise.

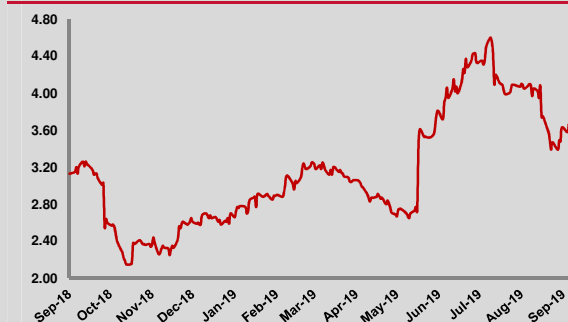
Maintain OUTPERFORM and DCF-driven TP of RM3.95. Our target price (based on WACC: 9.5%, TG: 1.5%) implies an EV/Fwd. EBITDA of 5.5x against our FY20E earnings, with no changes to our FY19E/FY20E assumptions in this note. We had earlier re-rated the stock from MARKET PERFORM in our above mentioned sector update. Reiterating our call premise, we believe the share price weakness following the management's expression to branch aggressively into mobile could be overdone. Any loss of cost savings could be exaggerated as its existing mobile business has been operational since Jan 2018, and granted the scale, it may not incur as significant amount in start-up costs.

Risks to our call include: (i) weaker-than-expected voice and internet demand, (ii) stronger -than-expected OPEX, and (iii) stiffer competition.

OUTPERFORM ↔

Price : RM3.66
Target Price : RM3.95 ↔

Share Price Performance



KLCI	1,599.49
YTD KLCI chg	-5.4%
YTD stock price chg	37.6%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	T MK Equity
Market Cap (RM m)	13,781.0
Shares Outstanding	3,765.3
52-week range (H)	4.60
52-week range (L)	2.15
3-mth avg daily vol	9,044,265
Free Float	29%
Beta	2.1

Major Shareholders

Khazanah Nasional Bhd	26.2%
Employees Provident Fund	16.7%
Skim Amanah Saham Bumiputera	11.8%

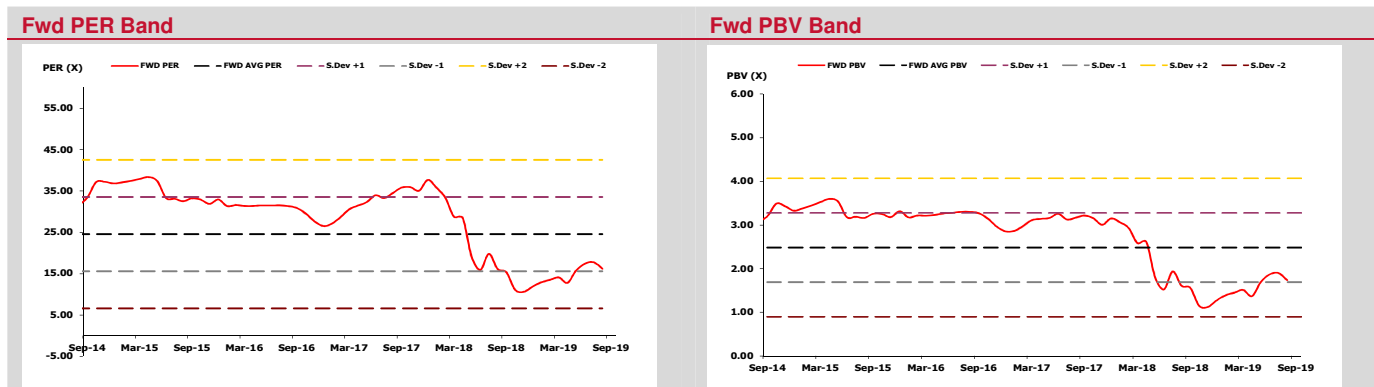
Summary Earnings Table

FY Dec (RM'm)	2018A	2019E	2020E
Turnover	11,819	11,234	11,302
EBITDA	3,933	3,753	3,769
EBIT	344	1,298	1,395
PBT	17	1,034	1,153
PATAMI	153	749	888
Core PATAMI	632	850	888
Consensus (NP)	-	879	883
Earnings Revision	-	0.0%	0.0%
Core EPS (sen)	16.7	22.5	23.5
Core EPS growth (%)	-25.5	34.4	4.5
NDPS (sen)	2.0	10.0	12.0
BVPS (RM)	2.0	2.1	2.2
PER (x)	21.9	16.3	15.6
PBV (x)	1.8	1.8	1.7
Net Gearing (x)	0.8	0.7	0.6
Net Div. Yield (%)	0.5	2.7	3.3

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Income Statement						Financial Data & Ratios					
FY Dec (RM m)	2016A	2017A	2018A	2019E	2020E	FY Dec (RM'm)	2016A	2017A	2018A	2019E	2020E
Revenue	12,061	12,085	11,819	11,234	11,302	Growth (%)					
EBITDA	3,749	3,817	3,933	3,753	3,769	Turnover	2.9%	0.2%	-2.2%	-4.9%	0.6%
Depreciation	(2,549)	(2,484)	(3,405)	(2,332)	(2,373)	EBITDA	7.6%	1.8%	3.0%	-4.6%	0.4%
Operating Profit	1,115	1,276	344	1,298	1,395	Operating Profit	6.5%	14.5%	-73.0%	277.0%	7.5%
Interest Inc/(Exp)	(225)	(255)	(348)	(303)	(292)	PBT	0.7%	14.1%	-98.3%	N.M.	11.5%
Associate Earnings	29	28	21	40	50	Core Net Profit	-4.7%	0.1%	-25.5%	34.4%	4.5%
Profit Before Tax	919	1,048	17	1,034	1,153	Profitability (%)					
Taxation	(305)	(318)	(278)	(321)	(346)	Operating Margin	9.2%	10.6%	2.9%	11.5%	12.3%
Minority Interest	163	199	414	36	81	PBT Margin	7.6%	8.7%	0.1%	9.2%	10.2%
PATAMI	776	930	153	749	888	Core Net Margin	7.0%	7.0%	5.4%	7.6%	7.9%
Core PATAMI	848	849	632	850	888	Effective Tax Rate	33.2%	30.3%	N.M.	31.0%	30.0%
						ROA	3.1%	3.7%	0.6%	3.1%	3.7%
						ROE	10.0%	12.0%	2.0%	9.7%	10.9%
						DuPont Analysis					
						Net Margin (%)	7.0%	7.0%	5.4%	7.6%	7.9%
						Assets Turnover (x)	0.5	0.5	0.5	0.5	0.5
						Leverage Factor (x)	3.3	3.2	3.2	3.0	2.9
						ROE (%)	10.0%	12.0%	2.0%	9.7%	10.9%
						Leverage					
						Debt/Asset (x)	0.3	0.3	0.4	0.4	0.4
						Debt/Equity (x)	1.1	1.0	1.1	1.1	1.0
						Net (Cash)/Debt	5,437	6,430	5,745	5,833	5,245
						Net Debt/Equity (x)	0.7	0.8	0.8	0.7	0.6
						Valuations					
						Core EPS (sen)	22.4	22.5	16.7	22.5	23.5
						NDPS (sen)	21.5	21.5	2.0	10.0	12.0
						BV/sh (RM)	2.0	2.1	2.0	2.1	2.2
						PER (x)	16.3	16.3	21.9	16.3	15.6
						Div. Yield (%)	5.9%	5.9%	0.5%	2.7%	3.3%
						PBV (x)	1.8	1.8	1.8	1.8	1.7
						EV/EBITDA (x)	4.6	4.5	1.0	3.5	4.3

Source: Kenanga Research



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Peer Table Comparison

Name	Last Price (RM)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div Yld (%)	Target Price (RM)	Rating
					1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.		
Stocks Under Coverage																	
AXIATA GROUP BERHAD	4.30	39,253.3	Y	12/2019	5.4%	0.2%	4.7%	22.0%	38.6	36.8	30.2	1.7	1.6	4.5%	2.3%	4.80	MP
DIGI.COM BERHAD	4.78	37,164.5	Y	12/2019	-6.3%	3.1%	-9.2%	0.9%	24.1	26.6	26.3	55.2	54.1	205.7%	3.7%	4.70	MP
MAXIS BERHAD	5.65	44,185.8	Y	12/2019	-1.7%	0.6%	-11.1%	4.4%	25.0	28.1	26.9	6.2	6.0	21.6%	3.0%	4.90	UP
OCC GROUP BERHAD	0.625	544.7	Y	12/2019	8.3%	12.5%	15.0%	7.8%	20.4	17.8	16.5	1.1	1.0	6.0%	0.0%	0.630	MP
TELEKOM MALAYSIA BERHAD	3.66	13,781.0	Y	12/2019	-4.9%	0.6%	34.4%	4.5%	21.9	16.3	15.6	2.0	1.9	11.8%	2.7%	3.95	OP
Simple Average					0.1%	3.4%	6.8%	7.9%	26.0	25.1	23.1	13.2	12.9	49.9%	2.4%		
Stocks Not Under Coverage - Consensus																	
TIME DOTCOM BERHAD	8.96	5,246.4	Y	12/2019	11.3%	11.2%	11.2%	9.3%	18.2	16.4	15.0	2.0	1.9	12.1%	2.2%	10.28	BUY

Source: Kenanga Research

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Stock Ratings are defined as follows:**Stock Recommendations**

OUTPERFORM : A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM : A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM : A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT : A particular sector's Expected Total Return is MORE than 10%
NEUTRAL : A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT : A particular sector's Expected Total Return is LESS than -5%

*****Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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Published and printed by:

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