

02 January 2020

Telecommunications

A Whole Lot of Bricks to Lay

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NEUTRAL



We maintain our NEUTRAL call on the telecommunications sector. MCMC has identified that our national 5G will be built upon the 700MHz, 3.5GHz and 26/28GHz bands, with the initial rollouts for the first two bands to be managed by a consortium formed by multiple licensees. The consortium structure would fulfil MCMC's desire for a more inclusive sharing framework and with minimal duplication of infrastructure. Commercialisation could kick in as early as 3QCY20. However, for the industry, there is still the lack of details on certain 5G aspects. (i.e. capex spends, commercial pricing, demand). Our Top Pick for the sector is TM (OP, TP: RM4.30). Though it would appear TM's bid as a sole national infrastructure provider for 5G could be silenced, as we assess TM from a dual strategic view; (1) it continues to play a significant role in the deployment of 5G infrastructure with its extensive fibre network, or (2) it focuses on its core fixed line and fibre business while riding on its leaner cost structure, with both scenarios resulting in positive outcomes. On the other hand, betting investors may look on a potential re-entry into the FBMKLCI during the June 2020 review.



Some surprises in 3QCY19 results. Within our coverage, **TM** was the only stock which delivered better-than-expected results, as its cost saving efforts yielded better-than-expected results. However, this also came from some delayed spending in capex, which management assures to keep with its guidance for FY19. To recap on the other stocks which performed within; (i) **AXIATA** saw top-line boosted by better numbers in regional operations with profits buoyed by efficiency gains from larger OpCos (Celcom, XL), (ii) **DIGI** continued with its revenue and earnings' decline as expected, with the softening of the prepaid segment but better margin was recorded on operational improvements, (iii) **MAXIS'** flattish revenue came

from poorer service revenue but was buffered by stronger device sales, which translated to poorer earnings on higher staff cost and depreciation, and (iv) towerco **OCK** performed in-line with the anticipation of lumpier 4Q earnings from higher tower deliveries.

The road to 5G. MCMC has revealed that it identified the 700MHz, 3.5GHz and 26/28GHz bands for the roll-out of 5G in the country. Also, in the statement the regulator indicated that the first two bands would be allocated to a consortium formed by multiple licensees as opposed to the current individual licensee structure. This would put an end to any speculation hailing a national infrastructure provider, as the proposed structure could lean towards greater emphasis in network and infrastructure sharing which could minimise costs from any one operator while preventing duplication of resources. We see that this structure would also make sense, with most incumbents having forged partnerships and collaborations for an eventual joint-deployment when the spectrums are made ready. Even towerco OCK has signed a memorandum of understanding with China Unicom to collaborate in mobile infrastructure and network services initiatives. For the 26/28GHz bands, MCMC looks to assign the 24.9-26.5GHz range via a tender process with the 26.5-28.1GHz to be awarded on a first-come first-serve basis. However, no indicative spectrum pricing has been provided at this juncture. With the completion of the assignment process, MCMC expects that we could see the commercial deployment of 5G by 3QCY20.

For the shorter road ahead, the NFCP (National Fiberisation and Connectivity Plan) is slated for the first round of tender awards in January 2020 for the installation of network facilities and services based on 3G and 4G technology in selected regions. This works to meet one of the objectives to achieve average connectivity speeds of 30Mbps in 98% of populated areas by 2023. The move to introduce entry-level fixed broadband package at 1% of GNI (est. RM40/mth) should also be on its way this year. However, the quality of service to be provided could require further feasibility studies, especially in rural areas.

Maintain Neutral on Telecommunications. We anticipate investors to be fairly passive towards the sector until more solid developments and news flows arise, namely on the assignment of the abovementioned spectrums and further tie-ins or collaborations between the incumbent players. Adding to this, hesitation could also arise with implications arising from higher-than-expected capex (mainly on spectrum pricing and 5G needs). This could be a near-term double-edged sword to the assignees as higher operational spending could dent earnings potential. The nature of 5G itself may not paint an overly encouraging picture, as the industry would have to determine: (i) the commercially viable pricing, (ii) demand and early adoption rates given the lack of applications requiring the technology in the immediate future, and (iii) general maintenance costs for the new technology. Nonetheless, the proposed consortium structure should ease the pains of any one network operator. On other fronts, U Mobile's pursuit for a public listing re-emerges, with the tentative timeline at end-2020 to raise up to USD500m.

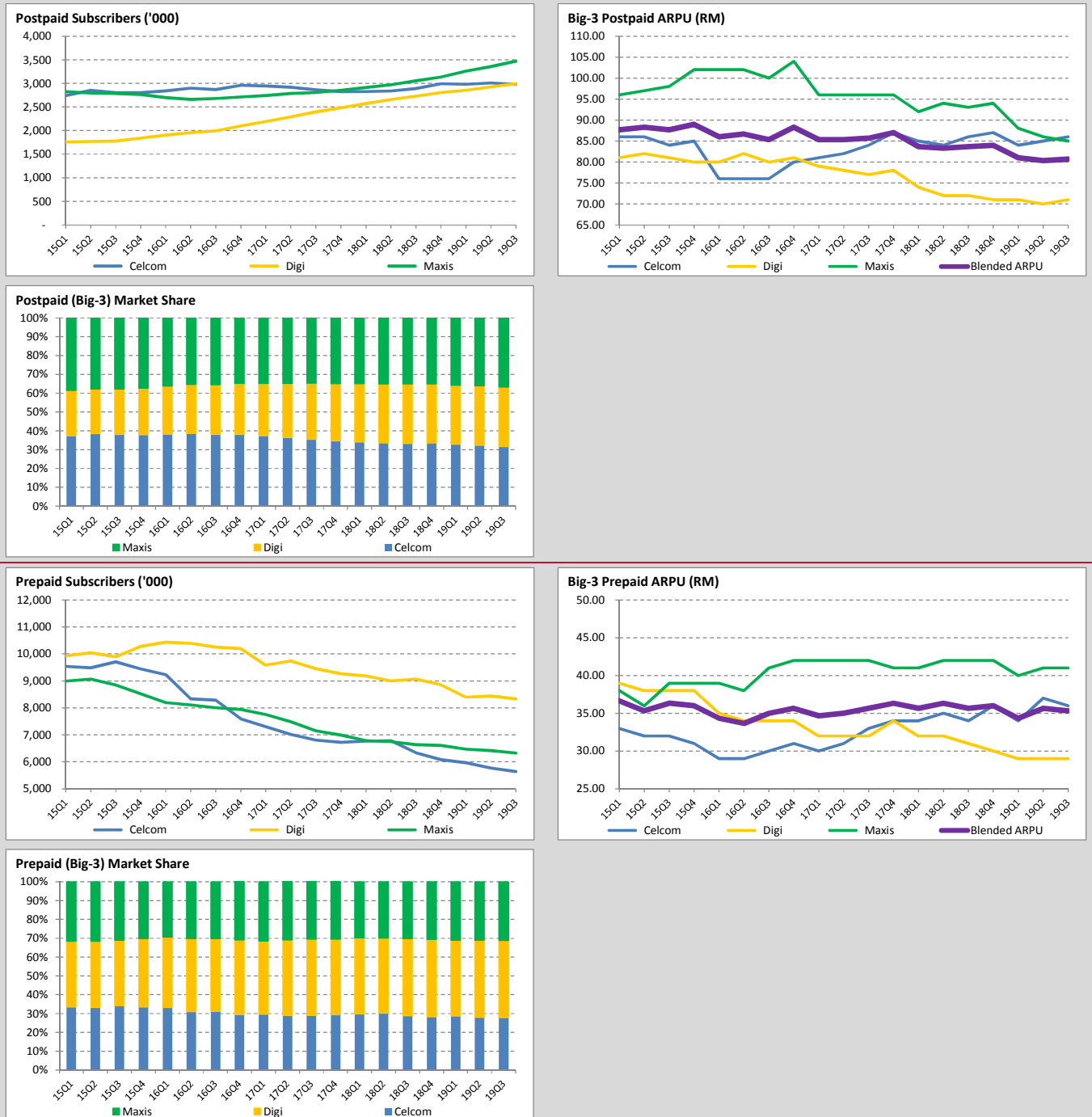
Top pick for the sector is TM (OP, TP: RM4.30). We see an attractive opportunity for TM. Building a case for TM, we present two separate scenarios for consideration; (1) TM partakes in the deployment of 5G network infrastructure provider, having the widest fibre network which it would administer with the incumbent celcos and in turn to boost its own mobile initiatives, or (2) TM fails with its bid and focuses on its core broadband and fixed line business, where it could continue to reap its cost savings efforts and pushing its endeavour to fulfil NFCP agendas. Both scenarios offer favourable risk-to-reward ratios at current price point (trading at below 5.5x EV/Fwd. EBITDA, 0.5SD below its 3-year mean. A little up ahead, risk-tolerant investors could also take a bet for the possible re-entry of the stock into the KLCI during the June 2020 review.



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No surprising shifts in market landscape. 3QFY19 reported numbers continued to highlight steady growth in postpaid subscriptions (+9% YoY) at the expense of prepaid users (-8% YoY). The change in consumer preference comes from more value-for-money offerings within the postpaid space, which could also be bundled with new attractive device launches. Between the Big-3 incumbents, Maxis holds the fort in postpaid market share (c.37%) while Digi remains the leader in the prepaid space (c.41%) thanks to the success of its internet-based plans.

Est. Postpaid and Prepaid Statistics in 3Q19



Source: Companies, Kenanga Research

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Peer Table Comparison

Name	Last Price @ 20-Dec-19 (RM)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net DivYld (%)	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.		
<u>Stocks Under Coverage</u>																	
AXIATA GROUP BHD	4.22	38,670.3	Y	12/2019	5.5%	-0.5%	7.1%	19.6%	37.9	35.3	29.5	1.6	1.6	4.6%	2.4%	4.80	OP
DIGI.COM BHD	4.55	35,376.3	Y	12/2019	-5.9%	1.5%	-8.8%	2.0%	23.0	25.2	24.7	52.6	51.5	206.7%	3.9%	4.70	MP
MAXIS BHD	5.45	42,621.7	Y	12/2019	-1.3%	0.9%	-10.2%	3.5%	24.1	26.8	25.9	6.0	5.9	22.0%	3.5%	4.90	UP
OCK GROUP BHD	0.585	560.8	N	12/2019	8.3%	12.5%	15.1%	7.6%	19.1	16.6	17.0	1.0	1.0	6.0%	0.0%	0.585	MP
TELEKOM MALAYSIA BHD	3.86	14,535.5	Y	12/2019	-4.8%	1.1%	54.9%	6.1%	23.1	14.9	14.0	2.1	2.0	13.6%	3.0%	4.30	OP
Simple Average					0.4%	3.1%	11.6%	7.8%	25.4	23.8	22.2	12.7	12.4	50.6%	2.6%		
<u>Consensus Estimates</u>																	
TIME DOT COM BHD	9.11	5,340.1	Y	12/2019	11.3%	11.1%	12.1%	8.7%	18.5	16.5	15.2	2.0	2.0	12.2%	2.2%	10.23	BUY

Source: Kenanga Research

Stock Valuation Methods

Companies	Target Price (RM)	Rating	Valuation Methodology
AXIATA GROUP BHD	4.80	OP	Sum-of-parts (refer below)
DIGI.COM BHD	4.70	MP	Discounted cash flow (WACC: 7.2%, TG: 1.5%)
MAXIS BHD	4.90	UP	Discounted cash flow (WACC: 8.8%, TG: 1.5%)
OCK GROUP BHD	0.585	MP	Discounted cash flow (WACC: 9.5%, TG: 1.5%)
TELEKOM MALAYSIA BHD	4.30	OP	Discounted cash flow (WACC: 9.1%, TG: 1.5%)

Source: Kenanga Research

AXIATA Sum-of-Parts Valuation

Companies	Methodology	Earnings Multiple	Equity Value (RM'm)	Effective Stake (%)	Effective Value (RM'm)
Celcom (Malaysia)	DCF	WACC: 7.9%, TG: 1.3%	24,294.8	100.0%	24,294.8
XL (Indonesia)	DCF	WACC: 9.9%, TG: 2.5%	15,610.9	66.4%	10,359.4
Robi (Bangladesh)	EV/EBITDA	5.0x	8,096.1	68.7%	5,562.0
Dialog (Sri Lanka)	EV/EBITDA	4.8x	5,129.9	83.3%	4,274.2
Ncell (Nepal)	EV/EBITDA	5.0x	6,424.5	80.0%	5,139.6
Smart (Cambodia)	EV/EBITDA	6.0x	4,581.9	72.5%	3,321.9
edotco	EV/EBITDA	7.0x	4,349.4	63.0%	2,740.1
Vodafone Idea (India)	Market Price		6,724.1	1.6%	108.9
Total Effective Value					55,801.0
(-) Net Debt					12,261.1
Total Equity Value					43,539.8
No. of Axiata Shares ('m)					9,058.6
Value/Share (RM)					4.80

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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