Telecommunications

It's Confirmed: A Second 5G Network

OVERWEIGHT

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The government on Wednesday confirmed its plan for a second 5G network, marking a departure from the single wholesale network (SWN) model for the rollout of 5G in Malaysia. We are positive on the development as this could lead to lower 5G access charges and hence better earnings and free cash flows for the telcos, allowing them to pay better dividends. Meanwhile, the government's commitment towards bridging the digital divide and driving Industrial Revolution 4.0 will further boost investment and demand for telco services. Wider coverage, better affordability and faster speed are set to boost subscription and ARPU. We reiterate our OVERWEIGHT call on the sector and raise the TPs for our sector top picks, namely, CDB (OP; TP: RM5.15) and MAXIS (OP; TP: RM5.03) by 11% each.

The Ministry of Commmunications and Digital finally announced on Wednesday that Malaysia will be moving into a dual wholesale network (DWN) in 2024 ending the uncertainties of the 5G rollout and the negative implications on the sector since the single wholesale network (SWN) was mooted in 2021.

We are not totally surprised by this confirmation given the new government's policy shake-ups in recent months. The unity government led by Pakatan Harapan (PH) is committed to dismantling monopolies and promoting competition. Recall, the SWN model for the rollout of 5G via Digital National Berhad (DNB) has come under constant criticisms due to its monopolistic nature, which could lead to excessive pricing, and to a certain extent, lack of transparency. In 2022, DNB announced that the SWN model would cost telco operators RM30k per Gbps a month (or RM0.13 per GB) on 5G leasing charges. Assuming a take-up rate of 1,000Gbps, this would ultimately cost the telcos a whopping RM360m/year to provide 5G to consumers, and they also have to pay a fixed upfront fees regardless of how far the 5G population coverage progresses − a concern to the market as dividend payments might be significantly reduced given the additional costs. The introduction of a second 5G network operator would challenge DNB's grip on the market, spurring competition that could result in reduced 5G leasing charges, a boon to the telco operators.

The new administration has maintained consistently its stance on the telco sector and the SWN model namely: (i) rolling out the 5G expeditiously, (ii) efficient telecommunication services to enhance consumer experience, (iii) affordability to bridge the digital divide, and (iv) breaking the monopolistic structure of the SWN model. A second 5G network will: (i) spur competition in 5G leasing costs, and ultimately lead to a reduction in access prices, (ii) allow telcos to purchase 5G access on a need basis, hence eliminating upfront payment fees, and (iii) result in better margins, earnings and free cash flows, leading to a sustainable dividend payment as seen before 2020.

On the heels of the government announcement, **CDB** announced that that it is terminating its share subscription agreements (SSAs) to take up a 25% stake in **DNB,** citing conditions precedent under the SSA had lapsed. The SSA was expected to cost CDB an estimated RM357m in cash.

We believe a second 5G network will be positive for the telco operators (i.e. improved profitability) and consumers (i.e. competition resulting in better services, broader bandwidth, improved speed and affordability). We reiterate our **OVERWEIGHT** stance on the sector and see a second 5G network as a re-rating catalyst to the sector.

In view of the latest development, we raise our TPs for **CDB, MAXIS** and **AXIATA (OP; TP: RM4.27)** by 8−11% each, as we increase our EV/EBITDA multiple by 1x to 12x to reflect the improved fundamentals, which are also closer to the sector's historical average of 13x.

Our sector top picks remain **CDB** and **MAXIS.**

We like **CDB** for the following reasons; (i) it is the new market leader in the mobile space with a combined market share of 43% following the merger of Celcom and DIGI, (ii) Celcom's key point is its network capacity with wider coverage while DIGI has in-depth coverage with an emphasis on urban areas. Celcom's 4G and 4G+ cover 96% and 90% respectively of the population, while DIGI's 4G and 4G+ are at 95% and 80%, respectively, (iii) its competitive pricing and attractive bundling to attract migrants, domestic customers and the B40s, (iv) superior EBITDA margins of both DIGI and Celcom at 5−6 ppt above the industry average of 41%−42%, and (v) rollout of 5G will boost its subscribers given the absence of MAXIS' presence in this space currently.

We are positive on **MAXIS** given: (i) its strong branding and customer loyalty, especially in the premium segment, (ii) the resilient demand for its services as it is ahead of competitors in terms of putting up new 4G towers, fiberisation of premises and upgrading of existing towers, thus boosting its B2B revenue as both corporates and SMEs continue to upgrade their digital infrastructure, and (iii) being non-commital to the SWN model, allowing it to have lower 5G costs in the interim period.

Changes in Valuation Basis, TPs and Recommendations									
Company	FY23 EV/EBITDA (x)			TP (RM)			Recommendation		
	After	Before	Chg	After	Before	Chg (%)	After	Before	Chg
AXIATA	12*	11*	↑	4.27	3.96	+8	OP	OP	↔
CDB	12	11	↑	5.15	4.64	+11	OP	OP	↔
MAXIS	12	11	↑	5.03	4.52	+11	OP	OP	↔
OCK	7	7	↔	0.69	0.69	0	OP	OP	↔
TM	7	7	↔	7.69	7.69	0	OP	OP	↔

**Only for operations in Malaysia*

Source: Kenanga Research

Peer Comparison

Name	Rating	Last Price (RM) @ 23 Mac 2023	Target Price (RM)	Upside (%)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Core EPS (sen)		Core EPS Growth		PER (x) - Core Earnings		PBV (x)	ROE (%)	Net. Div. (sen)	Net Div Yld (%)
								1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.
STOCKS UNDER COVERAGE																	
AXIATA GROUP BHD	OP	3.04	4.27	40.46%	27,904.0	Y	12/2023	13.2	15.6	-23.7%	18.5%	23.0	19.4	1.5	6.6%	12.0	3.9%
CELCOMDIGI BHD	OP	4.44	5.15	15.99%	52,087.9	Y	12/2023	18.4	19.4	79.3%	5.8%	24.1	22.8	3.1	13.1%	15.6	3.5%
MAXIS BHD	OP	4.52	5.03	11.28%	35,392.3	Y	12/2023	16.5	16.7	9.5%	0.8%	27.3	27.1	5.6	19.6%	16.0	3.5%
OCK GROUP BHD	OP	0.400	0.690	72.50%	421.9	Y	12/2023	3.6	5.4	13.6%	49.3%	11.0	7.4	0.6	6.3%	0.5	1.3%
TELEKOM MALAYSIA BHD	OP	4.97	7.69	54.73%	18,995.2	Y	12/2023	30.5	29.4	0.6%	-3.6%	16.3	16.9	2.2	13.7%	17.0	3.4%
SECTOR AGGREGATE					**134,801.3**					**13.7%**	**5.7%**	**23.0**	**21.8**	**2.6**	**11.9%**		**3.1%**

Source: Bloomberg, 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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