CelcomDigi Bhd

Uplifted by Network Cost Synergies

OUTPERFORM ↔

Price :	**RM4.26**
Target Price :	**RM5.34 ↑**

By Kylie Chan Sze Zan / kyliechan@kenanga.com.my

CDB's 1HFY23 results exceeded our forecast but disappointed the market. Its higher service revenues at the prepaid and home segments more than offset weaker postpaid revenue. Its 3QFY23 EBITDA margin soared to 51% on lower O&M and depreciation costs. We raise our FY23F and FY24F earnings by 14% and 12%, respectively, lift our TP by 5% to RM5.34 (from RM5.07) but maintain our OUTPERFORM call.

Its 9MFY23 core net profit of RM1.1b trumped our expectation at 87% of our full-year forecast but disappointed the market at 68% of the full-year consensus estimate. The variance against our forecast came mainly from lower-than-expected operations and maintenance (O&M) costs and regulatory fees. CDB declared DPS of 3.3 sen in 3QFY23, which is in-line with our expectation. This brings cumulative YTD DPS to 9.7 sen (9MFY22: 9.0 sen).

YTD drag from depreciation. Its service revenue improvement (+0.3% YTD) was mainly driven by the prepaid and home segments. This was on the back of: (i) subscriber base expansion, and (ii) steady take-up of new high-speed fiber plans and add-on offerings. This more than offset weaker postpaid revenues emanating from: (i) dip in interconnect rates (effective: Mar 2023), and (ii) slower traction for on-demand offerings.

However, its bottom-line dipped by 29% YTD mainly due to accelerated depreciation (YTD: RM678m) that more than negated the absence of Cukai Makmur.

QoQ surged due to cost boost. Its service revenue was flattish as expansion in the wholesale and prepaid segments more than offset weakness at the postpaid segment. The latter was impacted by: (i) lower usage, and (ii) further regulatory curbs in early July on bulk messaging (messages containing URLs, requests for personal information and phone numbers).

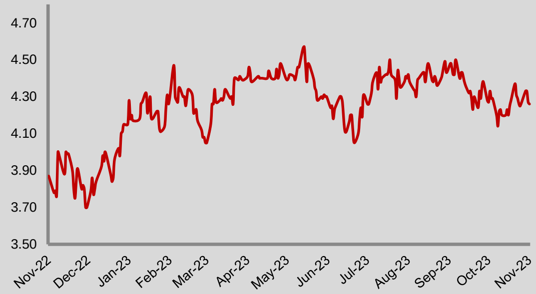
Nevertheless, its EBITDA margin surged to 50.5% (2QFY23: 47.6%) on the back of lower costs for: (i) devices, (ii) sales and marketing, (iii) O&M and (iv) regulatory and network costs. The reduction in O&M costs was attributed to: (i) cost synergies from network integration (modernization and phase-out of tower sites), and (ii) slower network maintenance activities.

The above, coupled with lower accelerated depreciation, enabled bottom-line to spike 36% QoQ. To a lesser extent, earnings also received a boost from a close to 5-fold increase in contribution from an associate and a joint venture. The latter are involved in enterprise solutions including cybersecurity.

Breather in prepaid net adds after a stellar 1HFY23. YoY, its subscriber base expansion (+636k) was due to sustained traction in net adds across the board. However, QoQ net adds for the prepaid segment slowed down to 22k in 3QFY23 after averaging an impressive 140k in 1HFY23.

Its 3QFY23 prepaid and postpaid ARPUs declined YoY to RM28 (3QFY22: RM29) and RM67 (3QFY22: RM71), respectively. To recap, postpaid ARPU was as high as RM71 in 1QFY22 before the start of its sequential rout. As mentioned above, its decline was due to lower interconnect rates and slower traction for on-demand offerings.

Share Price Performance



KLCI	1,460.67
YTD KLCI chg	-2.3%
YTD stock price chg	6.5%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	CDB MK EQUITY
Market Cap (RM m)	49,976.2
Shares Outstanding	11,731.5
52-week range (H)	4.60
52-week range (L)	3.64
3-mth avg daily vol	2,038,025
Free Float	47%
Beta	1.3

Major Shareholders

Axiata Group Bhd	33.1%
Employees Provident Fund	9.6%
Amanah Saham Nasional	5.7%

Summary Earnings Table

FY Dec (RM b)	2022A	2023F	2024F
Revenue	12,511	12,512	12,590
EBITDA	5,728	6,098	6,255
EBIT	3,032	2,453	2,576
PBT	2,742	1,976	2,069
Net Profit	1,880	1,462	1,512
Core Net Profit	**1,691**	**1,407**	**1,507**
Consensus (NP)	-	1,649	1,936
Earnings Revision	-	+14.1	+12.4
EBITDA Margin (%)	45.8	48.7	49.7
Core EPS (sen)	13.6	12.0	12.8
Core EPS growth (%)	-15.1	-11.7	7.1
DPS (sen)	20.0	18.0	21.0
BVPS (RM)	1.4	1.3	1.2
PER (x)	32.1	36.4	33.9
PBV (x)	3.2	3.3	3.5
Net Gearing (x)	0.8	0.8	0.8
Div. Yield (%)	4.6	4.1	4.8

Key takeaways from its results briefing are as follows:

1. CDB maintained its earnings guidance of: (i) flat-to-low single-digit EBITDA growth (YTD: +3%) and (ii) 15%-18% capex-to-revenue ratio (YTD: 8%). In order to reach the latter, CDB expects capex to accelerate in 4QFY23.
2. CDB also maintained its guidance for gross merger synergies of RM200m-RM250m (YTD: RM98m,) and integration cost of RM200m (YTD: RM60m). Based on the company's assertion that both targets remain on track YTD, this implies significant catch-up in 4QFY23.
3. CDB achieved enterprise revenue growth of 1.5% YTD emanating from the SME segment, ICT and connectivity solutions. This is aligned with its strategy to accelerate 5G monetization.
4. Out of the 74% CDB subscribers that have provisioned (activated) their 5G devices, merely 11% are active users. In our view, this suggests sluggish take-up and awareness of 5G services at this juncture.

Forecasts. We raise our FY23F and FY24F net profit forecasts by 14% and 12%, respectively, to reflect lower regulatory fees and O&M costs.

Correspondingly, we raise our TP by 5% to RM5.34 (from RM5.07) based on an unchanged at 12x FY24F EV/EBITDA, which reflects a discount to the sector's historical average of 13x. The discount is to reflect regulatory uncertainty surrounding the implementation of the new Dual Wholesale Network (DWN) model. There is no adjustment to our TP based on ESG given a 3-star rating as appraised by us (see Page 4).

We like CDB for the following reasons: (i) merger synergies are expected to amount to NPV of RM8b over 5 years – emanating from network (RM5.5b), IT (RM1.1b) and others (RM1.4b), (ii) robust FCF yield of more than 7% in FY23-34 which implies capacity to pay steady dividends, and (iii) leading subscriber base share of 39% and 20% in the postpaid and prepaid segments, respectively, translating to pricing power and economies of scale. Maintain **OUTPERFORM**.

Risks to our call include: (i) slower than expected realization of merger synergies, (ii) unfavourable outcome to the implementation of the dual wholesale network by the government, and (iii) competition between telco players turn irrational.

Results Highlights

FYE Dec (RM m)	3Q FY23	2Q FY23	QoQ Chg	3Q FY22	YoY Chg	9M FY23	9M FY22	YoY Chg
Revenue	3,104.4	3,123.0	-0.6%	3,072.0	1.1%	9,407.4	9,205.0	2.2%
EBITDA	**1,566.7**	**1,487.0**	5.4%	**1,436.0**	9.1%	**4,534.0**	**4,413.1**	2.7%
Depreciation	(871.7)	(896.0)	-2.7%	(633.0)	37.7%	(2,684.1)	(1,878.0)	42.9%
Net Finance Costs	(136.4)	(136.1)	0.2%	(119.0)	14.6%	(413.7)	(383.0)	8.0%
JV	13.4	2.9	367.1%	5.0	167.7%	23.3	13.0	78.9%
EI	0.3	10.3	-96.9%	0.0	nm	41.2	(52.1)	-179.1%
Pretax Profit	**572.4**	**468.0**	22.3%	689.0	-16.9%	**1,500.7**	**2,113.0**	-29.0%
Taxation	(113.6)	(120.4)	-5.7%	(212.0)	-46.4%	(373.5)	(656.0)	-43.1%
Minority Interest	(3.1)	(4.4)	-29.7%	0.0	nm	(10.3)	0.0	nm
Reported Net Profit	**455.7**	**343.2**	32.8%	**477.0**	-4.5%	**1,116.9**	**1,457.0**	-23.3%
Core Net Profit	**455.4**	**333.0**	36.8%	**477.0**	-4.5%	**1,075.7**	**1,509.1**	-28.7%
Core EPS (sen)	3.9	2.8	36.4%	3.4	14.0%	9.2	9.6	-4.1%
DPS (sen)	3.3	0.0	nm	3.4	-2.9%	9.7	9.0	7.8%
EBITDA margin	50.5%	47.6%		46.7%		48.2%	47.9%	
PBT Margin	18.4%	15.0%		22.4%		16.0%	23.0%	
Core Net margin	14.7%	10.7%		15.5%		11.4%	16.4%	

Source: Company, Kenanga Research

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Segmental Highlights

FYE Dec (RM m)	3Q FY23	2Q FY23	QoQ Chg (%)	3Q FY22	YoY Chg	9M FY23	9M FY22	YoY Chg (%)
Service Revenue								
Postpaid	1,257.0	1,267.0	-0.8	1,287.0	-2.3	3,807.0	3,829.0	-0.6
Prepaid	1,146.0	1,144.0	0.2	1,125.0	1.9	3,427.0	3,388.0	1.2
Wholesale & Others	265.0	255.0	3.9	261.0	1.5	763.0	785.0	-2.8
Home Fiber	45.0	42.0	7.1	35.0	28.6	127.0	99.0	28.3
Total	**2,713**	**2,708**	**0.2**	**2,708**	0.2	**8,124**	**8,101**	**0.3**
Device	**392**	**416**	**-5.8%**	**364**	**7.7%**	**1,286**	**1,103**	**16.6%**

Source: Company, Kenanga Research

Operating Metrics

	3Q FY23	2Q FY23	QoQ Chg	3Q FY22	YoY Chg
Subscribers ('000)					
Postpaid	6,864	6,772	92	6,652	212
Prepaid	13,614	13,592	22	13,216	398
Wholesale & Others	121	113	8	96	25
ARPU (RM)					
Postpaid	67.0	68.0	(1)	71.0	(4)
Prepaid	28.0	28.0	0	29.0	(1)
Home Fiber	126.0	127	(1)	124	2.0

Source: Company, Kenanga Research

Peer Comparison

Name	Rating	Last Price (RM)	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	2.42	3.45	42.6%	22,213.4	Y	12/2023	(2.5)	7.3	-121.2%	187.1%	N.A.	33.1	1.2	-3.1%	9.5	3.9%
CELCOMDIGI BHD	OP	4.26	5.34	25.4%	49,976.2	Y	12/2023	12.0	12.8	-16.8%	7.2%	35.5	33.2	3.2	9.2%	18.0	4.2%
MAXIS BHD	OP	4.08	5.30	29.9%	31,954.9	Y	12/2023	17.0	16.7	11.0%	-1.6%	24.0	24.4	5.3	21.4%	21.0	5.1%
OCK GROUP BHD	OP	0.395	0.730	84.8%	416.6	Y	12/2023	3.3	5.0	3.3%	50.1%	11.9	7.9	0.7	5.8%	0.0	0.0%
TELEKOM MALAYSIA BHD	OP	5.23	6.57	25.6%	20,065.4	Y	12/2023	43.3	41.3	30.6%	-4.7%	12.1	12.7	2.2	19.7%	24.0	4.6%
SECTOR AGGREGATE					**124,626.5**					**-21.0%**	**22.2%**	**29.9**	**24.4**	**2.5**	**10.6%**		**3.6%**

Source: Bloomberg, Kenanga Research

Stock ESG Ratings:

	Criterion	Rating				
GENERAL	Earnings Sustainability & Quality	★	★	★	★	
	Corporate Social Responsibility	★	★	☆		
	Management/Workforce Diversity	★	★	★		
	Accessibility & Transparency	★	★	★	★	
	Corruption-Free Pledge	★	★	★		
	Carbon-Neutral Initiatives	★	★	★	☆	
SPECIFIC	Occupational Health & Safety	★	★	★		
	Protection of Customer Data	★	★	☆		
	Cyber Security	★	★	★		
	Energy Efficiency	★	★	★		
	Digital Transformation	★	★	★		
	Supply Chain Sustainability	★	★	★	☆	
	OVERALL	★	★	★		

☆ denotes half-star
★ -10% discount to TP
★★ -5% discount to TP
★★★ TP unchanged
★★★★ +5% premium to TP
★★★★★ +10% premium to TP

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.***

Published by:

KENANGA INVESTMENT BANK BERHAD (15678-H)
Level 17, Kenanga Tower, 237, Jalan Tun Razak, 50400 Kuala Lumpur, Malaysia
Telephone: (603) 2172 0880 Website: www.kenanga.com.my E-mail: research@kenanga.com.my