

19 April 2024

Axiata Group

Dialog Axiata Acquires Airtel Lanka

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AXIATA's 83%-owned Sri Lankan unit, Dialog Axiata PLC, is acquiring smaller competitor Airtel Lanka via a share swap. The estimated consideration of SLR9.8b (RM156m) translates to FY23 price/sales multiple of 0.75x, which we deem as reasonable. The impact on AXIATA's earnings and valuations is insignificant. We maintain our forecasts, TP of RM3.05 and OUTPERFORM call.

10% share swap with Bharti Airtel Group. The vendor, India-based Bharti Airtel Limited (Bharti), is a global telco operator with over 500m customers in 17 countries across South Asia and Africa. Meanwhile, Bharti Airtel Lanka (Private) Ltd (Airtel Lanka) is its 100%-owned subsidiary that first commenced operations in 2009. This deal is subject to approval from Dialog's shareholders and completion of conditions precedent, including clearance from the Colombo Stock Exchange. Meanwhile, the Telecommunications Regulatory Commission of Sri Lanka has granted its approval.

Buying at 0.75x price/sales. Dialog will issue 952.7m new shares equivalent to 10.355% of its existing share base to Bharti which translates to an estimated purchase consideration of SLR9.8b (RM156m based on Dialog's last 90-day VWAP). This implies estimated FY23 price/sales multiple of 0.75x - which appears reasonable in comparison to its listed Sri Lankan peers' average of 1.0x. Whilst the price may seem expensive vis-à-vis Dialog (0.45x), it is significantly lower than SLT-Mobitel (1.56x). Therefore, we deem this acquisition as fairly priced.

Merger of smallest and biggest. Dialog is the market leader in Sri Lanka with a 17m subscriber base while Airtel Lanka has around 5m customers on its 5G-ready 4G network. We understand that it is the 4th largest player in Sri Lanka in a market dominated by four major telcos. The 2nd largest player is SLT-Mobitel, which is majority-owned by the government. Meanwhile, the 3rd largest operator is Hutchison Telecommunications Lanka, which was formed following the merger of Hong Kong-based CK Hutchison Holdings Ltd and UAE-based Etisalat in 2018.

Airtel needs a lot of fixing. Based on our estimates, Airtel Lanka delivered core LBITDA of SLR2.1b (RM32m) in FY23 (FY22: RM273m LBITDA). In FY23, its estimated core loss of SLR12.3b (RM196m) primarily consists of depreciation (45%) and finance costs (37%). The latter was attributed to its significant debt holdings totalling c. SLR68.1b (RM1.05b), which mainly consists of long-term debt (97%) that matures in March 2027. Meanwhile, its cash holdings as at end-FY23 amounted to SLK1.06b (RM17m). On the back of this, we estimate that AXIATA's FY24F net debt/EBITDA will increase slightly to 2.36x (from 2.23x).

Neutral given smallish impact. The announcement is well within expectations, given that back in May 2023, AXIATA had entered into a binding term sheet for this merger. We are neutral at this juncture, as details remain sketchy, and Dialog merely accounts for 4% of our valuation. Post share swap, we estimate that AXIATA's stake in Dialog's enlarged share cap will be reduced to 74% (from 83%).

OUTPERFORM ↔

Price : **RM2.55**
Target Price : **RM3.05** ↔

Share Price Performance



| | |
|---------------------|----------|
| KLCI | 1,544.76 |
| YTD KLCI chg | 6.2% |
| YTD stock price chg | 7.1% |

Stock Information

| | |
|-----------------------|------------------|
| Shariah Compliant | Yes |
| Bloomberg Ticker | AXIATA MK Equity |
| Market Cap (RM m) | 23,413.9 |
| Shares Outstanding | 9,181.9 |
| 52-week range (H) | 3.10 |
| 52-week range (L) | 2.16 |
| 3-mth avg. daily vol. | 7,021,471 |
| Free Float | 24% |
| Beta | 1.4 |

Major Shareholders

| | |
|------------------------------|-------|
| Khazanah Nasional Bhd | 36.7% |
| Employees Provident Fund | 17.9% |
| Skim Amanah Saham Bumiputera | 15.1% |

Summary Earnings Table

| FYE Dec (RMm) | 2023A | 2024F | 2025F |
|---------------------|-------------|------------|------------|
| Revenue | 22,002 | 24,083 | 25,273 |
| EBITDA | 9,797 | 8,929 | 9,239 |
| EBIT | 2,597 | 1,907 | 1,863 |
| PBT | 793 | 1,546 | 1,555 |
| PATAMI | -125 | 657 | 661 |
| Core PATAMI | 542 | 657 | 661 |
| Consensus (NP) | - | 664.6 | 935.7 |
| Earnings Revision | - | - | - |
| Core EPS (sen) | 5.6 | 7.2 | 7.2 |
| Core EPS Growth (%) | -53.3 | 27.1 | 0.6 |
| DPS (sen) | 10.0 | 10.0 | 10.5 |
| BVPS (RM) | 2.4 | 2.4 | 2.3 |
| PER (x) | 45.3 | 35.6 | 35.4 |
| PBV (x) | 1.1 | 1.1 | 1.1 |
| Net Gearing (x) | 0.9 | 0.9 | 0.9 |
| Div. Yield (%) | 3.9 | 3.9 | 4.1 |

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On the bright side, according to Fitch, Dialog expects to narrow Airtel Lanka's LBITDA and gradually reach break-even within 12 months of this merger. This may be achieved via cost savings from integrated network, sales and marketing channels and other administrative expenses. Given this scenario, earnings drag from Airtel Lanka may not persist for long. To recap, DIALOG contributed 20% to AXIATA's FY23 normalized PATAMI.

Spectrum holdings the prized asset. In our view, the key benefit for Dialog in this acquisition would be the takeover of Airtel Lanka's spectrum holdings. Based on Fitch, this merger will enable Dialog to secure a portion of Airtel Lanka's 75MHz spectrum across the 850MHz to 2.6GHz bands. Enlarged spectrum holdings may translate to capex savings for Dialog when rolling out both 5G and its home broadband services that rely solely on wireless technology. Additionally, this merger will enable Dialog to further consolidate its leading market share of c. 57% and ease competitive pricing pressures.

Merger synergies may turnaround losses Moreover, to some extent, the merged entity may achieve greater economies of scale, reduce infrastructure duplication, and derive technology and capex synergies. In turn, this would lead to enhanced service levels, cost savings and operational efficiencies. Moreover, we do not discount the possibility that Airtel Lanka may extract interest savings from debt refinancing. This is because Dialog may be able to secure more competitive interest rates via its relatively superior credit ratings. To recap, post unveiling of this merger proposal, Fitch reaffirmed Dialog's National Long-Term Rating at 'AAA (Ika)' with a Stable Outlook.

Forecasts. Maintained pending more details from an upcoming briefing on this transaction.

Valuations. We also maintain our Sum-of-Parts TP of RM3.05 (refer below). There is no adjustment to our TP based on ESG given a 3-star rating as appraised by us (see Page 4).

Investment case. We continue to like AXIATA for: (i) its plans to deleverage and strengthen its balance sheet, (ii) growth prospects for digital telcos and tower assets at emerging markets, and (iii) strong asset monetization prospects for Edotco and its digital businesses. Maintain **OUTPERFORM**.

Risks to our call include: (i) a strong USD may weigh on the performance of its digital telcos at frontier markets (e.g. Robi Bangladesh, Dialog Sri Lanka, Smart Cambodia), (ii) gestational earnings and cash flows drag from Link Net's aggressive expansion, and (iii) capex up-cycle from looming implementation of 5G in Indonesia.

AXIATA's Sum-of-Parts Valuation

| Unit | Valuation Methodology | Enterprise Value (RM m) | Effective Stake | Hold Co. Discount | Effective Value (RM m) |
|---|-----------------------|-------------------------|-----------------|-------------------|------------------------|
| Celcom (Malaysia) | CDB TP | 68,395 | 33.0% | 10% | 20,313 |
| XL (Indonesia) | 4.0x EV/EBITDA | 20,003 | 66.5% | 10% | 11,972 |
| Robi (Bangladesh) | 5.0x EV/EBITDA | 11,235 | 61.9% | 10% | 6,260 |
| Dialog (Sri Lanka) | 2.0x EV/EBITDA | 1,652 | 83.0% | 10% | 1,234 |
| Smart (Cambodia) | 3.0x EV/EBITDA | 3,069 | 72.5% | | 2,225 |
| Link Net (Indonesia) | 5.0x EV/EBITDA | 2,984.2 | 79.5% | | 2,372 |
| EDOTCO | 8.0x EV/EBITDA | 13,803.4 | 63.0% | | 8,696 |
| Digital Services | EV/Sales | 1,534.05 | 100.0% | | 1,534 |
| Total Effective Enterprise Value | | | | | 54,607 |
| (-) Hold Co Net Debt and MI | | | | | -26,802 |
| Total Equity Value | | | | | 27,805 |
| No. of Shares (m) | | | | | 9,179 |
| Target Price (RM) | | | | | 3.05 |

Source: Kenanga Research

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Income Statement

| FYE Dec (RM m) | 2021A | 2022A | 2023A | 2024F | 2025F |
|------------------------|---------------|---------------|--------------|--------------|--------------|
| Revenue | 25,901 | 27,496 | 22,002 | 24,083 | 25,273 |
| EBITDA | 12,088 | 16,436 | 9,797 | 8,929 | 9,239 |
| Depreciation | -8,095 | -12,204 | -7,200 | -7,022 | -7,375 |
| EBIT | 3,993 | 4,232 | 2,597 | 1,907 | 1,863 |
| Net Interest | -1,414 | -1,713 | -2,040 | -1,910 | -1,914 |
| Associates | 4 | -51 | 903 | 1,549 | 1,606 |
| Exceptionals | -409 | 8,646 | -667 | 0 | 0 |
| PBT | 2,174 | 11,114 | 793 | 1,546 | 1,555 |
| Taxation | -897 | -1,094 | -651 | -232 | -233 |
| Minority Interest | -458 | -268 | -267 | -657 | -661 |
| Net Profit | 819 | 9,751 | -125 | 657 | 661 |
| Core Net Profit | 1,228 | 1,106 | 542 | 657 | 661 |

Balance Sheet

| FYE Dec (RM m) | 2021A | 2022A | 2023A | 2024F | 2025F |
|---------------------|---------------|---------------|---------------|---------------|---------------|
| Fixed Assets | 26,975 | 27,201 | 27,440 | 26,439 | 25,381 |
| Intangible Assets | 21,723 | 13,442 | 12,238 | 12,238 | 12,238 |
| Oth Fixed Assets | 11,442 | 26,304 | 28,157 | 29,705 | 31,311 |
| Inventories | 223 | 216 | 219 | 212 | 223 |
| Receivables | 5,061 | 6,944 | 4,809 | 5,263 | 5,592 |
| Other Curr Assets | 418 | 82 | 968 | 968 | 968 |
| Cash | 6,969 | 7,452 | 4,612 | 4,300 | 3,681 |
| Total Assets | 72,811 | 81,641 | 78,442 | 79,126 | 79,394 |
| Payables | 13,555 | 10,580 | 9,317 | 10,199 | 10,702 |
| ST Borrowings | 4,231 | 7,088 | 2,666 | 2,602 | 2,539 |
| Other ST Liability | 2,566 | 3,406 | 3,210 | 3,210 | 3,210 |
| LT Borrowings | 14,819 | 18,348 | 22,176 | 21,646 | 21,117 |
| Other LT Liability | 12,313 | 11,540 | 11,540 | 11,540 | 11,540 |
| Net Assets | 25,326 | 30,680 | 29,533 | 29,929 | 30,287 |
| S/holders' Equity | 18,005 | 23,935 | 22,064 | 21,803 | 21,500 |
| Minority Interests | 7,061 | 6,745 | 6,171 | 6,828 | 7,489 |
| Total Equity | 25,066 | 30,680 | 28,235 | 28,631 | 28,989 |

Cashflow Statement

| FYE Dec (RM m) | 2021A | 2022A | 2023A | 2024F | 2025F |
|-----------------------|-------------|------------|---------------|-------------|-------------|
| Operating CF | 8,837 | 8,935 | 7,678 | 9,130 | 9,171 |
| Investing CF | -8,117 | -11,585 | -4,700 | -6,021 | -6,318 |
| Financing CF | -1,217 | 3,412 | -5,267 | -3,421 | -3,472 |
| Change In Cash | -496 | 762 | -2,289 | -312 | -619 |
| Free CF | 2,589 | -795 | 709 | 3,110 | 2,852 |

Financial Data & Ratios

| FYE Dec | 2021A | 2022A | 2023A | 2024F | 2025F |
|------------------------|--------|--------|--------|--------|--------|
| Growth | | | | | |
| Revenue | 7% | 6% | -20% | 9% | 5% |
| EBITDA | 6% | 36% | -40% | -9% | 3% |
| EBIT | 37% | 6% | -39% | -27% | -2% |
| PBT | 86% | 411% | -93% | 95% | 1% |
| Core Net Profit | 103% | -10% | -51% | 21% | 1% |
| Profitability | | | | | |
| EBITDA Margin | 47% | 60% | 45% | 37% | 37% |
| EBIT Margin | 15% | 15% | 12% | 8% | 7% |
| PBT Margin | 8% | 40% | 4% | 6% | 6% |
| Core Net Margin | 5% | 4% | 2% | 3% | 3% |
| Eff. Tax Rate | -41% | -10% | -82% | -15% | -15% |
| ROA | 2% | 1% | 1% | 1% | 1% |
| ROE | 7% | 5% | 2% | 3% | 3% |
| DuPont Analysis | | | | | |
| Net Margin | 4.7% | 4.0% | 2.5% | 2.7% | 2.6% |
| Asset T/over (x) | 0.4 | 0.3 | 0.3 | 0.3 | 0.3 |
| Lever. Factor (x) | 4.0 | 3.4 | 3.6 | 3.6 | 3.7 |
| ROE | 6.9% | 5.3% | 2.4% | 3.0% | 3.1% |
| Leverage | | | | | |
| Debt/Asset (x) | 0.3 | 0.3 | 0.3 | 0.3 | 0.3 |
| Debt/Equity (x) | 1.1 | 1.1 | 1.1 | 1.1 | 1.1 |
| Net (Cash)/Debt | 12,081 | 17,984 | 20,230 | 19,948 | 19,974 |
| Net Gearing (x) | 0.7 | 0.8 | 0.9 | 0.9 | 0.9 |
| Valuations | | | | | |
| Core EPS (sen) | 13.4 | 12.1 | 5.6 | 7.2 | 7.2 |
| DPS (sen) | 8.0 | 14.0 | 10.0 | 10.0 | 10.5 |
| BV/share (RM) | 2.0 | 2.6 | 2.4 | 2.4 | 2.3 |
| Core PER (x) | 19.1 | 21.2 | 45.3 | 35.6 | 35.4 |
| Div. Yield (%) | 3.1 | 5.5 | 3.9 | 3.9 | 4.1 |
| PBV (x) | 1.3 | 1.0 | 1.1 | 1.1 | 1.1 |
| EV/EBITDA (x) | 4.7 | 3.2 | 5.6 | 3.0 | 3.0 |

Source: Kenanga Research

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Peer Comparison – Telecommunication

| 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. |
| Telecommunication | | | | | | | | | | | | | | | | | |
| AXIATA GROUP BHD | OP | 2.55 | 3.05 | 19.6% | 23,413.9 | Y | 12/2024 | 7.2 | 7.2 | 21.2% | 0.6% | 35.6 | 35.4 | 1.3 | 3.0% | 10.0 | 3.9% |
| CELCOMDIGI BHD | OP | 4.09 | 5.83 | 42.5% | 47,981.9 | Y | 12/2024 | 17.2 | 18.9 | 6.1% | 10.1% | 23.8 | 21.6 | 2.9 | 12.3% | 13.8 | 3.4% |
| MAXIS BHD | OP | 3.50 | 5.30 | 51.4% | 27,412.3 | Y | 12/2024 | 16.7 | 17.9 | 6.2% | 7.2% | 21.0 | 19.6 | 4.8 | 22.7% | 20.0 | 5.7% |
| OCC GROUP BHD | OP | 0.600 | 0.795 | 32.5% | 634.1 | Y | 12/2024 | 5.1 | 5.2 | 26.8% | 3.1% | 11.9 | 11.5 | 0.9 | 8.0% | 1.5 | 2.5% |
| TELEKOM MALAYSIA BHD | OP | 6.09 | 7.22 | 18.6% | 23,371.2 | Y | 12/2024 | 45.5 | 46.1 | -13.4% | 1.4% | 13.4 | 13.2 | 2.3 | 17.9% | 23.0 | 3.8% |
| SECTOR AGGREGATE | | | | | 122,813.3 | | | | | 0.9% | 5.7% | 21.3 | 20.2 | 2.4 | 12.8% | | 3.9% |

Source: Bloomberg, Kenanga Research

Stock ESG Ratings:

| | Criterion | Rating | | | | |
|-----------------------|-----------------------------------|--------|---|---|---|--|
| GENERAL | Earnings Sustainability & Quality | ★ | ★ | ★ | ★ | |
| | Community Investment | ★ | ★ | ★ | | |
| | Workers Safety & Wellbeing | ★ | ★ | ★ | | |
| | Corporate Governance | ★ | ★ | ★ | | |
| | Anti-Corruption Policy | ★ | ★ | ★ | | |
| | Emissions Management | ★ | ★ | | | |
| SPECIFIC | Cybersecurity & Data Privacy | ★ | ★ | ★ | | |
| | Network Quality & Coverage | ★ | ★ | ★ | | |
| | Digitalisation & Innovation | ★ | ★ | ★ | | |
| | Supply Chain Management | ★ | ★ | ★ | | |
| | Talent Management | ★ | ★ | ★ | | |
| Customer Satisfaction | ★ | ★ | ★ | | | |
| OVERALL | | ★ | ★ | ★ | | |

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

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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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