April 2, 2018

Maybank Kim Eng

Singapore Telcos

Everything On HOLD

NEUTRAL *[Upgrade]*

Telecommunications

Singapore

Base case priced in - Upgrade to NEUTRAL view

With the Singapore telcos de-rating close to levels we envisage in our base case scenario of gradual erosion in incumbents' revenues, we upgrade StarHub and M1 in this note to HOLDs and our sector view to NEUTRAL. However, it is still too early to be positive on the sector with new MVNOs and TPG set to launch in 2H18, and neither can we write off the worst case scenario risk we painted in our *13 March 2018 Sector Note*. Singtel's geographically diversified structure offers relative resilience to Singapore risks but it also faces potential competitive challenges in its other major markets. In the sector, we prefer Singtel.

A taste of things to come

Following TPG's teaser announcement on 19 March 2018 offering free SIMs, unlimited voice and 3GB/month data for senior citizens for 24 months, the Singapore focused StarHub and M1 share prices have de-rated by 5% and 2%, respectively. Regardless of the fact that TPG's segment is niche and that the full mechanics have not yet been revealed, we believe the market took it as a sign that TPG intends to put up a fight for share. By playing the good corporate citizen card, not only did TPG create public goodwill but we believe it also helps it to negotiate building and housing access for its nationwide coverage rollout by end-2018.

The de-rating is not excessive

Per our base case scenario for the industry that TPG (TPM AU, Not Rated) and the various MVNOs attain a less than 10% industry wireless revenue share by 2019E, we think the stocks are not at particularly compelling value levels yet. We do note that cash dividend yields even in the 2019E pressure point may pique interest at 5%-7% levels for the three telcos.

Watching closely

Although TPG's stated purpose at the onset was for only 5-6% market share, we cannot discount our worst case scenario that tariff wars ensue and a more aggressive market share grab takes place. Incumbents attempting to stay out and let MVNOs compete with TPG for a lower income segment is ideal but contamination is always possible. Our sensitivity analysis (see Fig 4) shows that every 1% change in wireless revenue would impact core profits and TPs by 1% to 3%.

Analyst

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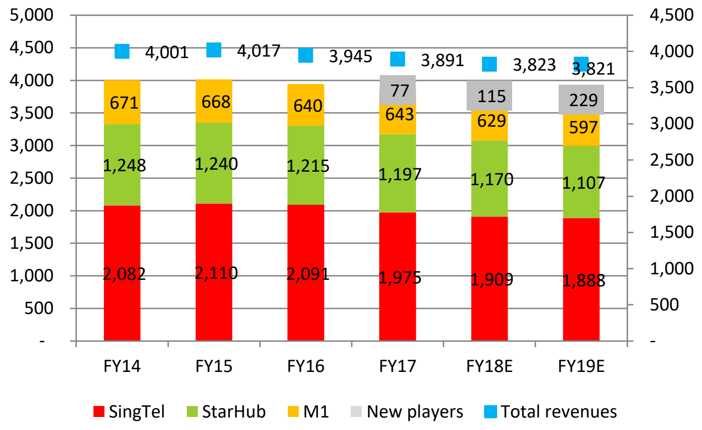
Price performance (as at 30 Mar 2018)

	1-mo	3-mo	12-mo	YTD
STI	**-2.6%**	**0.7%**	**8.0%**	**0.7%**
SingTel	-0.3%	-5.6%	-14.2%	-5.6%
StarHub	-8.0%	-19.3%	-20.4%	-19.3%
M1	-0.6%	-2.2%	-18.7%	-2.2%

Source: Factset

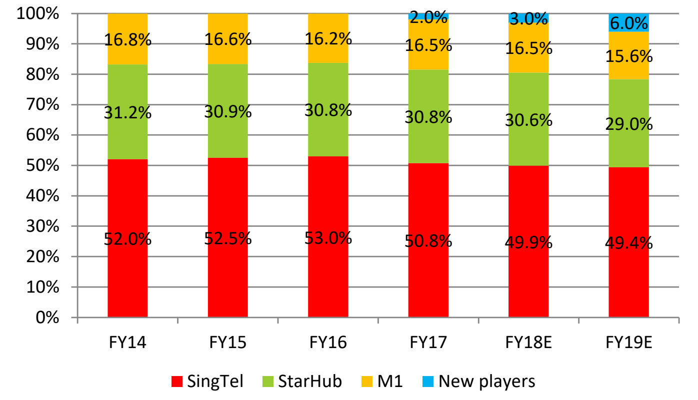
Stock	Bloomberg code	Mkt cap (USD'm)	Rating	Price (LC)	TP (LC)	Upside (%)	P/E (x) 18E	P/E (x) 19E	P/B (x) 18E	P/B (x) 19E	Div yld (%) 18E	Div yld (%) 19E
Singtel	ST SP	41,218	Hold	3.39	3.69	9	15.3	15.6	1.8	1.8	5.7	4.7
StarHub	STH SP	3,061	Hold	2.33	2.27	(3)	17.3	18.5	13.5	16.9	6.9	6.9
M1	M1 SP	1,233	Hold	1.75	1.63	(7)	12.8	17.5	3.4	3.3	6.2	4.6

Fig 1: Industry wireless revenue* (SGD m)



Source: Company data, Maybank Kim Eng
**Calendarised to end-Dec*

Fig 2: Industry wireless revenue market shares*



Source: Company data, Maybank Kim Eng
**Calendarised to end-Dec*

Fig 3: TP methodologies

Company	Methodology
SingTel	SOTP based on DCF of various parts*
StarHub	DCF based, WACC 5.3%, LTG -1%
M1	DCF based, WACC 4.1%, LTG -1%

Source: Maybank Kim Eng
**Pls refer to Singtel tear sheet for full details*

Fig 4: Sensitivity analysis to 1% wireless revenue change

Company/Variable	FY18E	FY19E	FY20E
SingTel (Singapore and Australia, end-Mar, SGD m)			
EBITDA change	na	0.7%	0.7%
EBITDA margin change	na	0.1%	0.1%
Core profit change	na	0.6%	0.6%
Target price change	0.5%		
StarHub (end-Dec, SGD m)			
EBITDA change	1.1%	1.0%	1.0%
EBITDA margin change	0.1%	0.1%	0.1%
Core profit change	2.3%	2.2%	2.5%
Target price change	1.6%		
M1 (end-Dec, SGD m)			
EBITDA change	1.3%	1.3%	1.3%
EBITDA margin change	0.2%	0.2%	0.2%
Core profit change	2.4%	2.9%	3.4%
Target price change	2.7%		

Source: Maybank Kim Eng

Value Proposition

- Telco conglomerate whose companies have significant, if not leading, shares in their markets.
- High growth phase for wireless segment has passed. Competition is generally on the rise in this segment in most markets.
- Enterprise and digital services to provide next legs of growth while cash is harvested from wireless leadership to support investments and capex.
- Healthy balance sheet backs 60-75% dividend payout commitment on recurring profit. Non-core asset-sale proceeds are partly committed to exceptional payouts.
- Despite its acquisitions in recent years, SingTel continues to generate 14-16% ROIC.

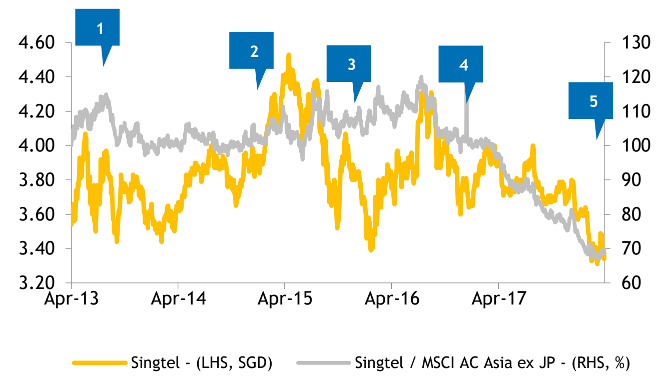
SingTel's SOTP breakdown

Valuation	Stake (%)	Valuation method	Valuation (SGD m)	Per share (SGD)
Consolidated Businesses				
SingTel	100.0	DCF (5.5% WACC, 0% TG, 0.60 beta)	6,899	0.42
Optus	100.0	DCF (5.7% WACC, 0% TG, 0.65 beta)	15,511	0.95
Sub Total			**22,410**	**1.37**
	Stake (%)	**Valuation method**	**Valuation (SGD m)**	**Per share (SGD)**
Associates & Investments				
Telkomsel (Indonesia)	35.0	DCF (10.8% WACC, 3% TG, 1.0 beta)	13,736	0.84
Bharti Airtel (India)	38.6	SOTP (10.5% WACC, 3% TG, 0.9 beta)	10,479	0.64
AIS (Thailand)	23.3	DCF (7.0% WACC, 2% TG, 1.0 beta)	6,234	0.38
Globe (Philippines)	47.2	DCF (6.7% WACC, 1% TG, 1.05 beta)	3,811	0.23
Intouch (Thailand)	21.0	SOTP (AIS TP and mkt cap of THCOM TB)	1,868	0.11
NetLink NBN Trust (Singapore)	25.0	Consensus target price	912	0.06
SingPost (Singapore)	25.8	DCF (7.6% WACC, 1% TG, 0.95 beta)	757	0.05
Sub Total			**37,040**	**2.32**
Total Equity Value			**59,450**	**3.69**

Source: Maybank Kim Eng

Price Drivers

Historical share price trend



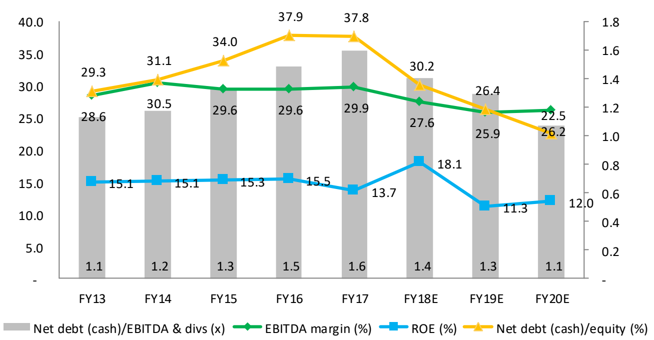
Source: Company, Maybank Kim Eng, Factset

1. Launch of 4G services that ended unlimited data plan competition.
2. All regional associates powered earnings in FY15.
3. Proposal for fourth mobile licence. Bharti's profits started to taper off.
4. TPG won licence in a general spectrum auction.
5. Proposal to increase effective stake in Bharti to 39.5%

Financial Metrics

- Singapore and Australia operational EBITDA forecast to decline by 11% 2-year CAGR on the back of higher equipment subsidies.
- Pretax associate income could soften the blow by growing 15% over the same period.
- We forecast net debt to EBITDA, including associate dividends, forecast to remain healthy at 1.5x in FY18-19E; leaving room for sustainable dividend payout at the upper range of the payout policy and / or acquisitions.

Financial ratios have not succumbed to competitive pressure



Source: Company, Maybank Kim Eng

Swing Factors

Upside

- Strong growth in enterprise and Digital Life to economies of scale.
- Ebbing competitive heat in India.
- Subsidies per smartphone drop.

Downside

- Wireless margin compression triggered either by TPG in Singapore and / or Australia or pre-emptive strikes by incumbents. These are not likely in consensus forecasts.
- Long-term capex for 5G rollout not likely priced in.
- Worse-than-expected cannibalisation of wireless voice, SMS and roaming by data.

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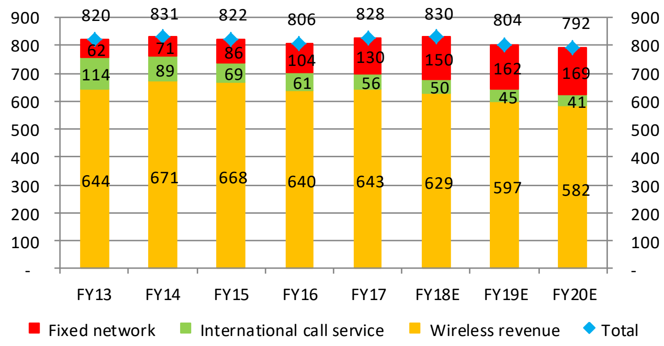
Value Proposition

- Historically, the purest play in the Singapore wireless sector but has been expanding more meaningfully into fixed broadband and enterprise segments.
- The high growth phase of wireless has passed and wireless data cannibalization of voice and SMS is stifling growth.
- Seeking to tap into Smart Nation projects to enhance its enterprise service revenues and track record.

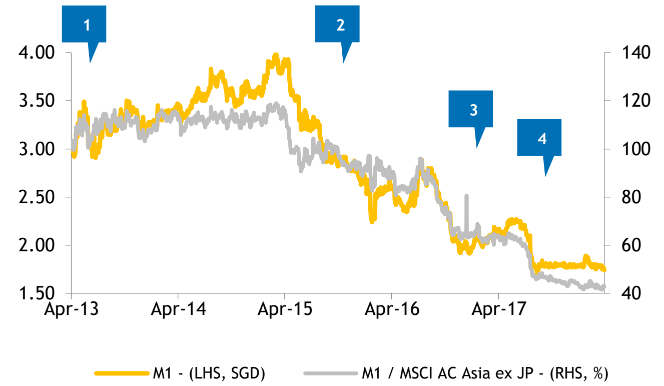
M1's service revenue breakdown (SGD m)



Source: Company, Maybank Kim Eng estimates

Price Drivers

Historical share price trend



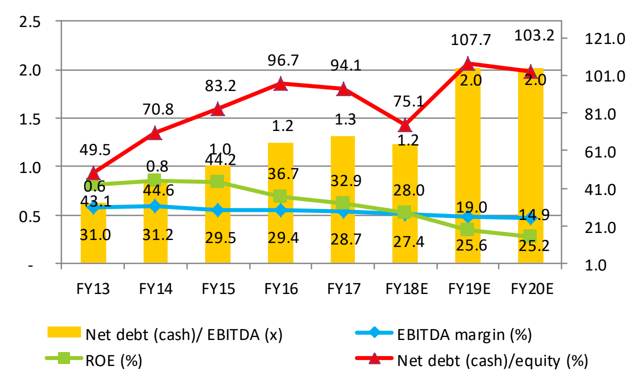
Source: Company, Maybank Kim Eng, Factset

1. Industry re-rating on the back of the launch of 4G services that led to the end of unlimited data plan competition and a move to tiered data plans.
2. Proposals for fourth mobile license issuance began to drive an industry de-rating.
3. New spectrum auction entry of TPG followed by additional frequency won during general spectrum auction (GSA) continues domino effect.
4. Soft 2Q17 results and cancellation of shareholder review weaken share price further.

Financial Metrics

- We assume competition from new players will manifest in tariff plan pressure similar to the 3G price war period in 2009-2012. We assume M1's wireless service revenues decrease by a 3% CAGR over 2017-2020E.
- We forecast a positive 9% CAGR over 2017-2020E for fixed network revenue that will help offset wireless and international call revenue pressure.
- Despite our overall service revenue decline assumptions from 2018E to 2020E, the balance sheet is still able to sustain cash dividends at the committed 80% payout level for 2018E-19E and even increase this to 90% in 2020E.

Balance sheet still able to support payout



Source: Company, Maybank Kim Eng estimates

Swing Factors

Upside

- A benign competitive environment or a hasty retreat by new entrants would be an unexpected surprise.
- Growth in fixed network via fixed broadband and/or enterprise could provide earnings surprises in the medium to long term.
- Any takeover interest by a new entrant or TPG could trigger a sector re-rating.

Downside

- Should TPG resort to handset subsidies to poach subscribers an escalation in incumbents' own efforts could take place.
- Higher-than-expected capex pressure as a result of competition and/or 5G rollout.
- Risks of a more rapid decline in wireless voice, SMS and roaming as data adoption gains momentum.

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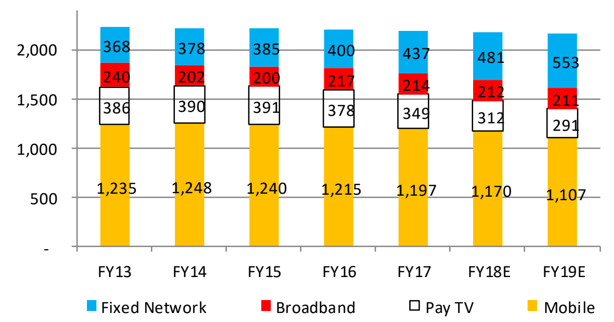
Value Proposition

- Second-largest operator in a mature, high income ASEAN economy. Entrant of fourth operator threatens market share, returns and cost of capital.
- Cyclical EBITDA margin within the calendar year due to smartphone launches and a largely postpaid revenue driven market that values equipment subsidies.
- Network management experience and breadth drives increased initiatives to tap private and public enterprise contracts.
- Dividend yield has been a key investment thesis. Despite reducing payout commitment (from SGD0.20 to SGD0.16), potential for DPS to exceed EPS remains, as in prior years.

StarHub's fixed network services its main bright spot (SGD m)



Source: Company data, Maybank Kim Eng

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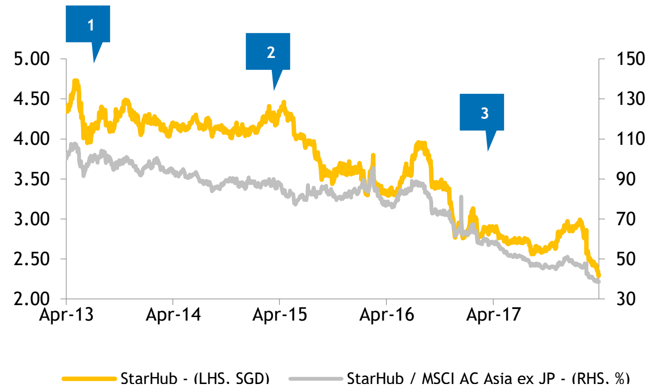


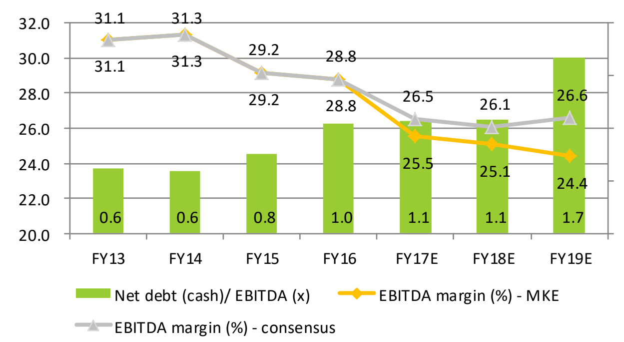
Source: Company, FactSet, Maybank Kim Eng

1. Industry re-rating on the launch of 4G services to help replace unlimited-data 3G plans to pay-as-you-use plans.
2. Consistent dividend payout kept share price generally stable.
3. Expectations of a new entrant initially with a Dec 2016 spectrum auction that led to TPG's entry. Also, dividend payout commitment cut by 20% to SGD0.16 per share.

Financial Metrics

- Despite margin pressure the committed SGD0.16 DPS remains within debt covenants.
- Gearing could come under pressure with spectrum payments and competition related capex in the coming months and years.
- Key financial/operating metrics we would be watching for in subsequent quarters are subsidy levels, mobile subscriber recontracting rates, and pay TV churn.

Leverage rising with margins weakening



Source: Company data, FactSet, Maybank Kim Eng

Swing Factors

Upside

- Enterprise segment targeting, including government contracts revolving around the Smart Nation initiatives provides source of new revenues, despite competition with SingTel.
- Network alliance with M1 to reduce network redundancies and operating expenses, and future joint capex planning is under negotiation.

Downside

- Re-contracting/retention costs likely to rise on the back of new smartphone launches and defensive preparation against TPG's entry.
- Further wireless tariff package pressure on rates and/or data allocations possible with new competition.
- Further investments in enterprise or content space that may have a gestation period before realizing returns.

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