



## Telekom Malaysia Berhad

Risks are Manageable

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BUY

TM's share price has been on a downward trend, following announcements made in Budget 2017. While there are concerns about a 50% reduction in connectivity prices within two years, we view the impact as manageable. The rollout of HSBB2 and SUBB is on track to meet targets, which should help sustain Unifi net adds momentum. Although webe contributions remains insignificant, we are upbeat on its prospects. It continues to rollout new sites and has received the approval to deploy LTE on its 2300MHz spectrum. Take up of its postpaid plans has been within expectations, with its prepaid offering expected to be launched in 2H2017. Expectations of narrowing losses with a PAT breakeven timeline of three to five years will aid bottom line growth. Maintain BUY on TM with a TP of RM7.95/share.

### Budget 2017 Initiatives Manageable

TM's share price has been on a down trend following announcements made during Budget 2017. Recall, this include requirements for: 1) fixed line broadband service providers to offer higher speeds at the same price effective January 2017, and 2) within the next two years, speeds are expected to be doubled with a 50% reduction in prices. Overall, we believe the fall in share price may be slightly overdone, as the impact from the above initiatives are manageable.

In line with the announcement, the group will be offering complimentary speed upgrades to its subscribers in phases over 2017. However, alleviating concerns over down trading activities, this will be applicable only to existing and new subscribers who sign up before 2017. In addition, the recently reduced prices of RM179 and RM229 for its Unifi Advance packages are part of its typical year end promotional campaign. We expect prices to revert to normal upon the end of its promotional period. Expansion plans are already in the pipeline to support increased data usage. Capex is expected to remain elevated in the high 20s (as % of revenue) in FY17, before moderating to the low to mid 20s in FY18.

Our concern lies more on the additional doubling of speeds and 50% reduction in prices within two years. However, this is still an unknown variable with discussions still ongoing. As we understand, the 50% reduction refers to connectivity prices. In this scenario, future ARPU can be managed by bundling additional value additional services to existing packages. Existing services available as add-ons include security & surveillance, home gadget protection, parental control and voice IDD. Another way to tackle this is through the implementation of data caps. By applying this, higher speeds can be offered at lower prices, while also encouraging heavy data users to subscribe for higher priced plans.

### Share Information

Bloomberg Code	T MK
Stock Code	4863
Listing	Main Board
Share Cap (mn)	3,757.9
Market Cap (RMmn)	22,359.7
Par Value (RM)	1.00
52-wk Hi/Lo (RM)	6.90/5.81
12-mth Avg Daily Vol ('000 shrs)	5,242.9
Estimated Free Float (%)	30.9
Beta	0.68
Major Shareholders (%)	

Khazanah Nasional - 26.2

EPF - 17.0

Skim Amanah Saham - 12.6

Kumpulan Wang Persaraan - 5.0

### Forecast Revision (%)

	FY16	FY17
Forecast Revision (%)	-	-
Core Net Profit (RMm)	767.2	945.4
Consensus	816.4	882.3
TA/Consensus (%)	94.0	107.1
Previous Rating	Buy (Maintained)	

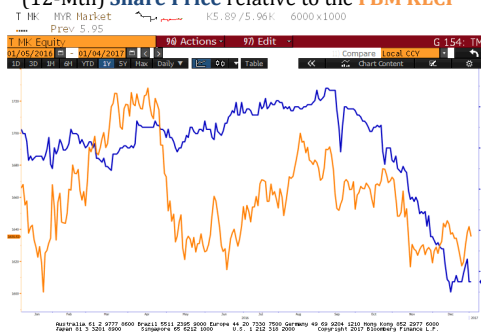
### Financial Indicators

	FY16	FY17
Net Gearing (%)	59.9	64.0
CFPS (sen)	92.4	99.2
P/CFPS (x)	6.4	6.0
ROE (%)	9.6	11.7
ROA (%)	3.2	4.0
NTA/Share (RM)	1.9	2.0
P/NTA (x)	3.1	3.0

### Share Performance

Price Change (%)	T	FBMKLCI
1 mth	(2.9)	0.4
3 mth	(12.0)	(1.5)
6 mth	(12.4)	(1.2)
12 mth	(10.4)	(1.1)

### (12-Mth) Share Price relative to the FBMKLCI

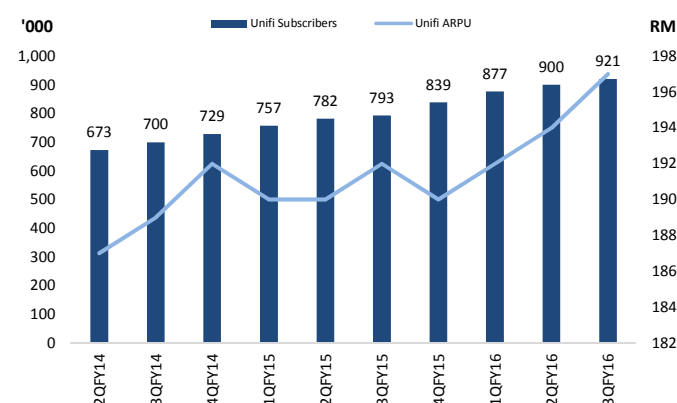


Source: Bloomberg

## HSBB 2 and SUBB On Track

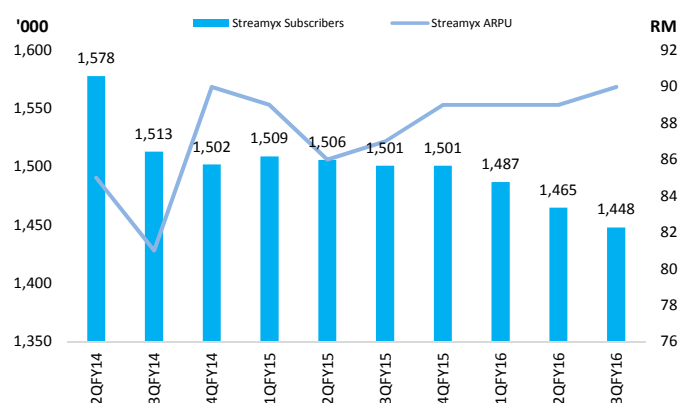
The rollout of the High Speed Broadband Project Phase 2 (HSBB 2) and the Sub-Urban Broadband Project (SUBB) are progressing well. To date, it has rolled out more than 200k and 140k premises for HSBB 2 and SUBB. Timelines are to achieve 390k and 420k premises for HSBB 2 and SUBB by 2017 and 2019. Taking into consideration that areas covered by HSBB 2 and SUBB are of lower density, take up for services have been encouraging. We expect subscriber net adds momentum to sustain, as latent demand is unlocked through the progressive rollout of both projects.

Figure 1 : Unifi Subscribers and ARPU



Source: Companies, TA Securities

Figure 2 : Streamyx Subscribers and ARPU



Source: Companies, TA Securities

## webe Updates

While it is still too early to disclose contributions from webe, take up rates have been in line with expectations. Postpaid plans were made nationwide available in end September 2016. Previously only for existing TM/webe customers with certified smartphones, it has made its postpaid plan available to everyone for a competitive price of RM79/month with unlimited data, voice and SMS. There are also plans to launch its prepaid offerings in the 2H2017.

In terms of network, it currently operates 1,600 sites. LTE is being deployed on its 850MHz spectrum, but it had recently received approval to utilise its 2300MHz spectrum as well. Better propagation abilities of the 850MHz spectrum will help it expand its coverage and provide in-building penetration, while utilisation of its 2300MHz spectrum allows it to build capacity to support more users.

Premised on its competitive pricing and continual network improvements, we expect webe subscriber trends to progressively pick up in the coming quarters. We view webe as a medium term driver for the group. Expectations of narrowing losses at webe will provide a boost to the group's bottom line, with a PAT breakeven timeline of 3 to 5 years.

## Valuation

We value TM at an unchanged TP of RM7.95/share. This is based on a DCF valuation with WACC at 6.9% and long term growth rate of 1.0%. Key buying points include: 1) Dominant position in less competitive fixed broadband space; 2) Narrowing losses at webe, and 3) Affordable valuations at an EV/EBITDA of 6.4x, implying a 40% discount against its mobile peers. **BUY.**

**P&L**

YE Dec 31 (RMmn)	FY14	FY15	FY16F	FY17F	FY18F
Revenue	11,235	11,722	12,324	12,935	13,400
EBITDA	3,728	3,677	3,914	4,256	4,571
Depreciation & amortisation	(2,341)	(2,437)	(2,695)	(2,704)	(2,851)
Net finance cost	(155)	(159)	(229)	(255)	(274)
Forex	(48)	(184)	0	0	0
Associates	9	25	26	27	29
Others	(88)	(9)	0	0	0
PBT	1,106	912	1,016	1,325	1,475
Taxation	(263)	(320)	(305)	(397)	(442)
MI	(11)	109	56	18	3
Net profit	832	700	767	945	1,035
Core net profit	941	895	767	945	1,035
EPS (sen)	25.0	23.8	20.4	25.2	27.6
DPS (sen)	22.9	21.4	18.4	22.6	24.8

**Ratios**

YE Dec 31 (RMmn)	FY14	FY15	FY16F	FY17F	FY18F
<b>Valuations</b>					
PER (x)	23.8	25.0	29.1	23.7	21.6
EV/EBITDA (x)	7.3	7.4	7.0	6.4	6.0
Dividend yield (%)	3.8	3.6	3.1	3.8	4.2
PBV (x)	3.0	2.9	2.9	2.8	2.8

**Profitability ratios (%)**

ROAE	12.3	11.2	9.6	11.7	12.6
ROAA	4.3	3.8	3.2	4.0	4.3
EBITDA margin	33.2	31.4	31.8	32.9	34.1
PBT margin	9.8	7.8	8.2	10.2	11.0

**Liquidity ratios (x)**

Current ratio	1.3	1.3	1.2	1.1	1.0
Quick ratio	1.3	1.2	1.2	1.1	0.9

**Leverage ratios (x)**

Total liabilities/equity	1.8	2.0	2.0	1.9	1.9
Net debt/equity	0.4	0.5	0.6	0.6	0.7
Int. coverage ratio	8.9	7.8	5.3	6.1	6.3

**Growth ratios (%)**

Sales	5.7	4.3	5.1	5.0	3.6
Pretax	5.7	(17.5)	11.5	30.3	11.3
Earnings	(9.4)	(4.9)	(14.3)	23.2	9.5
Total assets	(2.8)	1.1	1.0	1.5	1.4

**Balance Sheet**

YE Dec 31 (RMmn)	FY14	FY15	FY16F	FY17F	FY18F
Fixed assets	14,785	15,187	15,825	16,597	17,323
Associates + Subsidiaries	7	26	52	79	108
Goodwill	582	608	578	550	523
Others	769	1,295	1,036	1,063	1,083
LT assets	16,142	17,116	17,492	18,289	19,037
Inventories	116	237	154	162	167
Trade receivables	2,825	2,947	2,993	3,141	3,254
Cash	2,986	3,512	2,477	1,794	1,165
Others	554	602	602	602	602
Current assets	6,481	7,298	6,226	5,699	5,189
<b>Total assets</b>	<b>22,623</b>	<b>24,413</b>	<b>23,717</b>	<b>23,988</b>	<b>24,225</b>
Trade payables	3,605	4,367	3,659	3,840	3,978
ST borrowings	197	408	363	351	341
Others	1,055	1,047	1,047	1,047	1,047
Current liabilities	4,857	5,823	5,069	5,238	5,366
LT borrowings	6,251	7,175	6,904	6,663	6,470
Others	3,555	3,376	3,742	3,927	4,089
LT liabilities	9,806	10,552	10,645	10,590	10,559
Share capital	2,604	2,631	2,631	2,631	2,631
Reserves	4,968	5,150	5,170	5,345	5,489
Shareholders' funds	7,571	7,781	7,800	7,975	8,119
MI	389	258	202	184	181
<b>Total liabilities and equity</b>	<b>22,623</b>	<b>24,413</b>	<b>23,717</b>	<b>23,988</b>	<b>24,225</b>

**Cash Flow**

YE Dec 31 (RMmn)	FY14	FY15	FY16F	FY17F	FY18F
PBT	1,106	912	1,016	1,325	1,475
Depreciation and amortisation	2,341	2,437	2,673	2,660	2,785
Net interest	181	170	229	255	274
Other non-cash	(73)	(63)	(26)	(27)	(29)
Changes in WC	(126)	123	(246)	9	7
Tax paid & others	(414)	(637)	(668)	(748)	(783)
<b>Operational cash flow</b>	<b>3,014</b>	<b>2,942</b>	<b>2,978</b>	<b>3,472</b>	<b>3,729</b>
Capex	(2,101)	(2,547)	(3,304)	(3,447)	(3,551)
Interest received	120	134	135	96	67
Others	(181)	(137)	0	0	0
<b>Investing cash flow</b>	<b>(2,162)</b>	<b>(2,550)</b>	<b>(3,169)</b>	<b>(3,351)</b>	<b>(3,484)</b>
Net share issue	779	269	0	0	0
Dividend paid	(957)	(879)	(747)	(771)	(891)
Net change in debts	(213)	743	(317)	(253)	(203)
Others	10	0	220	220	220
<b>Financial cash flow</b>	<b>(381)</b>	<b>134</b>	<b>(844)</b>	<b>(804)</b>	<b>(874)</b>
<b>Net cash flow</b>	<b>471</b>	<b>526</b>	<b>(1,035)</b>	<b>(683)</b>	<b>(629)</b>
Opening cash flow	2,515	2,986	3,512	2,477	1,794
Forex	(0)	0	0	0	0
<b>Closing cash flow</b>	<b>2,986</b>	<b>3,512</b>	<b>2,477</b>	<b>1,794</b>	<b>1,165</b>

**Stock Recommendation Guideline**

- BUY** : Total return within the next 12 months exceeds required rate of return by 5%-point.
- HOLD** : Total return within the next 12 months exceeds required rate of return by between 0-5%-point.
- SELL** : Total return is lower than the required rate of return.
- Not Rated:** The company is not under coverage. The report is for information only.

**Total Return** is defined as expected share price appreciation plus gross dividend over the next 12 months.

**Required Rate of Return** of 7% is defined as the yield for one-year Malaysian government treasury plus assumed equity risk premium.

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