

Hutchison Telecom

Bloomberg: 215 HK Equity | Reuters: 0215.HK

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DBS Group Research . Equity

28 Feb 2022

HOLD (Downgrade from BUY)

Last Traded Price (25 Feb 2022): HK\$1.32 (HSI : 22,767)

Price Target 12-mth: HK\$1.10 (17% downside) (Prev HK\$1.40)

Analyst

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What's New

- Further deterioration in 2H21 with a net loss of HK\$27m, compared to a net profit of HK\$31m in 1H21
- Local service revenue growth slowed down from 4% in 1H21 to 0.2% in 2H21, a major disappointment
- Cut earnings by 49% and 44% for FY22 and FY23 respectively on slower service revenue growth and higher network costs
- Downgrade to HOLD, with a lower TP of HK\$1.1 on earnings cut

Pure mobile player with ample cash

Investment Thesis

Huge cash position to be unlocked. We estimate Hutchison Telecom (HT) would have net cash of c.HK\$4bn after distribution of special dividend in 2021, equivalent to c.HK\$0.8 per share. The value could be unlocked with further special dividends in the future.

Expect higher 5G penetration to drive ARPU recovery. We forecast mobile ARPU to improve by c. 3% each in FY22 and FY23.

Mobile roaming revenue remains under pressure. Due to prolonged travel restrictions from various variant outbreaks globally and 5th COVID-19 wave in Hong Kong, mobile roaming revenue will remain sluggish at least in 1H22.

Valuation:

Our TP of HK\$1.1 is based on sum of the parts: (1) HK\$0.3 per share for the mobile business at 15x FY22 PE, in line with its major peer, (2) net cash of HK\$0.8 per share.

Where we differ:

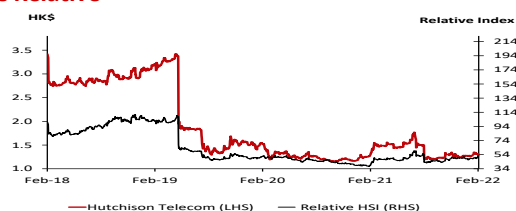
More cautious on earnings recovery. Due to the slowdown of local service revenue growth in 2H21 and weaker service revenue growth compared to peers, we are more cautious on Hutchison Telecom's earnings recovery trajectory compared to peers.

Key Risks to Our View:

Irrational market competition (downside risk). Hong Kong's mobile market is crowded with four major players. Irrational pricing may lead to a price war.

Recovery of mobile roaming revenue (upside risk). Faster than expected mobile roaming revenue will lead to higher EBITDA and earnings, as mobile roaming business enjoys higher margin.

Price Relative



Forecasts and Valuation

FY Dec (HK\$m)	2020A	2021A	2022F	2023F
Turnover	4,545	5,385	5,512	5,663
EBITDA	1,606	1,445	1,481	1,556
Pre-tax Profit	444	86	133	229
Net Profit	361	4	108	186
Net Profit Gth (Pre-ex) (%)	(15.9)	(98.9)	2,591.1	72.5
EPS (HK\$)	0.07	0.00	0.02	0.04
EPS Gth (%)	(15.9)	(98.9)	2,591.1	72.5
Diluted EPS (HK\$)	0.07	0.00	0.02	0.04
DPS (HK\$)	0.07	0.27	0.07	0.07
BV Per Share (HK\$)	2.50	2.24	2.19	2.16
PE (X)	17.6	1590.3	59.1	34.3
P/Cash Flow (X)	4.9	1.9	6.2	5.4
P/Free CF (X)	9.0	2.5	10.2	8.1
EV/EBITDA (X)	0.7	1.7	1.8	1.7
Net Div Yield (%)	5.7	20.7	5.7	5.7
P/Book Value (X)	0.5	0.6	0.6	0.6
Net Debt/Equity (X)	CASH	CASH	CASH	CASH
ROAE (%)	3.0	0.0	1.0	1.8
Earnings Rev (%)			(49)	(44)
Consensus EPS (HK\$)			0.04	0.05
Other Broker Recs:		B:2	S:0	H:4

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

At A Glance

Issued Capital (m shrs)	4,819
Mkt Cap (HK\$m/US\$m)	6,361 / 815
Major Shareholders (%)	
CK Hutchison Holdings Ltd.	66.1
Li Ka Shing Foundation	7.3
Free Float (%)	26.6
3m Avg. Daily Val. (US\$m)	0.26
GICS Industry: Communication Services / Telecommunication Services	



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Hutchison Telecom**WHAT'S NEW****2H21 disappointed with net loss of HK\$27m; sluggish local service revenue growth in 2H21****FY21 and 2H21 results highlights**

Revenue increased by 18% y-o-y to HK\$5,385m in FY21, mainly attributable to 70% y-o-y growth in hardware and other product sales.

Service revenue decreased 1% y-o-y to HK\$3,241m in FY21. Local service revenue grew 2% y-o-y to HK\$2,980m in FY21, driven by 35% y-o-y growth corporate solution revenue. However, local service revenue growth slowed from 4% in 1H21 to 0.2% in 2H21, mainly attributable to lower local postpaid net ARPU of HK\$159 in FY21 compared to HK\$160 in 1H21.

Total customers decreased 1% from 3,233k as of Jun 21 to 3,202k as of Dec 21. Postpaid customers increased by 1% from 1,423k to 1,442k as of Dec 21, while prepaid customers decreased 3% from 1,810k as of Jun 21 to 1,760k as of Dec 21. Local postpaid net ARPU decreased from HK\$160 in 1H21 to HK\$159 in FY21, despite 5G penetration rising from 10-15% as of Jun 21 to 21% as of Dec 21 among postpaid customers.

Service EBITDA decreased by 21% y-o-y in 2H21 to HK\$692m (vs. HK\$723m in 1H21). Service EBITDA margin was down 6ppts y-o-y to 44% in FY21.

Net profit plunged by 99% y-o-y to HK\$4m in FY21. Earnings had deteriorated to net loss of HK\$27m in 2H21 from net profit of HK\$31m in 1H21 due to slower local service revenue growth and increasing network costs in 2H21, vs. net profit of HK\$146m in 1H20 and HK\$251m in 2H20.

A final dividend per share (DPS) of HK\$0.0521 was proposed, same as FY20, totaling full year DPS of HK\$0.2729, including a special dividend of HK\$0.198 per share that was announced in FY21 interim results.

Outlook

The impact of COVID-19 has been longer than our expectations due to the various variant outbreaks globally

and 5th COVID-19 wave in Hong Kong. We expect mobile roaming business to remain under pressure at least in 1H22. However, further roaming revenue shrinkage is unlikely.

Growth of local service revenue will be driven by expanding corporate solutions revenue, increasing 5G broadband users and customers upgrading to 5G. However, we cut our postpaid ARPU assumption by 2% and 3% respectively for FY22 and FY23 due to a sluggish recovery of local postpaid net ARPU in 2H21. We forecast ARPU to grow by c.3% each in FY22 and FY23 respectively.

Despite a 47% hike in capex in FY21 due to investments in 5G infrastructure, management expects capex to reduce to HK\$400m-HK\$500m in FY22. The company targets to maintain similar dividend to that of FY20 before earnings fully recovers and 100% payout going forward. Besides, after settling 5G capex and evaluation of potential investment opportunities, the company may consider declaring another special interim dividend in 1H22.

Downgrade from BUY to HOLD with a lower TP of HK\$1.1

We have cut our earnings by 49% and 44% for FY22 and FY23 respectively after incorporating slower service revenue recovery. We expect earnings to grow from HK\$4m in FY21 to HK\$108m and HK\$186m in FY22 and FY23. We downgrade Hutchison Telecom from BUY to HOLD with a lower TP to HK\$1.1, which is based on sum of the parts: (1) HK\$0.3 per share for the mobile business at 15x FY22 PE, in line with the target multiple for its major peer, (2) net cash of HK\$0.8 per share.

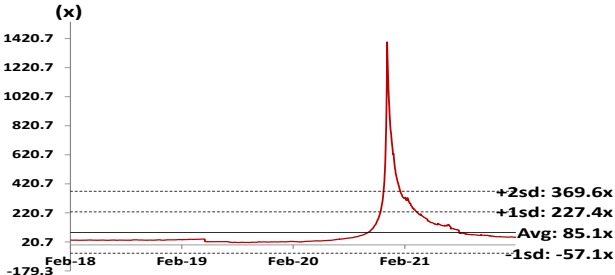
Company Background

Hutchison Telecom (HT) has now become a pure mobile operator following the sale of its fixed-line assets, operating under the brand "3 Hong Kong". It has a c.20% mobile subscriber market share. Its major shareholder is CK Hutchison Holdings Limited.

Hutchison Telecom

Historical PE and PB band

Forward PE band (x)



PB band (x)



Source: Thomson Reuters, DBS HK

Hutchison Telecom

Key Assumptions

FY Dec	2019A	2020A	2021A	2022F	2023F
Mobile sub number (k)	3,655.0	3,279.0	3,202.0	3,234.0	3,284.0
Mobile ARPU (HK\$)	87.0	79.0	83.0	86.0	88.0

Source: Company, DBS HK

Segmental Breakdown (HK\$ m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Revenues (HK\$ m)					
Moible	3,613	3,285	3,241	3,325	3,454
Hardware sales	1,969	1,260	2,144	2,187	2,209
Total	5,582	4,545	5,385	5,512	5,663

Source: Company, DBS HK

Hutchison Telecom

Income Statement (HK\$ m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Revenue	5,582	4,545	5,385	5,512	5,663
Cost of Goods Sold	(1,941)	(1,238)	(2,082)	(2,128)	(2,154)
Gross Profit	3,641	3,307	3,303	3,384	3,509
Other Opng (Exp)/Inc	(3,255)	(2,921)	(3,183)	(3,229)	(3,267)
Operating Profit	386	386	120	155	242
Other Non Opg (Exp)/Inc	0	0	0	0	0
Associates & JV Inc	(4)	(4)	(4)	(4)	(4)
Net Interest (Exp)/Inc	153	62	(30)	(18)	(9)
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	0	0	0	0	0
Pre-tax Profit	535	444	86	133	229
Tax	(98)	(83)	(82)	(25)	(44)
Minority Interest	(8)	0	0	0	0
Preference Dividend	0	0	0	0	0
Net Profit	429	361	4	108	186
Net Profit before Except.	429	361	4	108	186
EBITDA	1,569	1,606	1,445	1,481	1,556
Growth					
Revenue Gth (%)	(29.4)	(18.6)	18.5	2.4	2.7
EBITDA Gth (%)	45.3	2.4	(10.1)	2.5	5.0
Opg Profit Gth (%)	22.2	0.0	(68.9)	29.2	56.3
Net Profit Gth (%)	6.2	(15.9)	(98.9)	2,591.1	72.5
Margins & Ratio					
Gross Margins (%)	65.2	72.8	61.3	61.4	62.0
Opg Profit Margin (%)	6.9	8.5	2.2	2.8	4.3
Net Profit Margin (%)	7.7	7.9	0.1	2.0	3.3
ROAE (%)	3.1	3.0	0.0	1.0	1.8
ROA (%)	2.6	2.5	0.0	0.7	1.2
ROCE (%)	2.2	2.5	0.0	1.0	1.5
Div Payout Ratio (%)	75.1	100.0	32,875.0	335.4	194.5
Net Interest Cover (x)	NM	NM	4.0	8.5	26.3

Source: Company, DBS HK

Interim Income Statement (HK\$ m)

FY Dec	2H2019	1H2020	2H2020	1H2021	2H2021
Revenue	3,067	1,982	2,563	2,565	2,820
Cost of Goods Sold	(1,217)	(315)	(923)	(911)	(1,171)
Gross Profit	1,850	1,667	1,640	1,654	1,649
Other Oper. (Exp)/Inc	(1,613)	(1,530)	(1,391)	(1,568)	(1,615)
Operating Profit	237	137	249	86	34
Other Non Opg (Exp)/Inc	0	0	0	0	0
Associates & JV Inc	(2)	(2)	(2)	(2)	(2)
Net Interest (Exp)/Inc	61	52	10	(10)	(20)
Exceptional Gain/(Loss)	0	0	0	0	0
Pre-tax Profit	296	187	257	74	12
Tax	(55)	(41)	(42)	(43)	(39)
Minority Interest	0	0	0	0	0
Net Profit	241	146	215	31	(27)
Net profit bef Except.	241	146	215	31	(27)
Growth					
Revenue Gth (%)	(21.2)	(21.2)	(16.4)	29.4	10.0
Opg Profit Gth (%)	79.5	(8.1)	5.1	(37.2)	(86.3)
Net Profit Gth (%)	17.0	(22.3)	(10.8)	(78.8)	N/A
Margins					
Gross Margins (%)	60.3	84.1	64.0	64.5	58.5
Opg Profit Margins (%)	7.7	6.9	9.7	3.4	1.2
Net Profit Margins (%)	7.9	7.4	8.4	1.2	(1.0)

Source: Company, DBS HK

Hutchison Telecom

Balance Sheet (HK\$ m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Net Fixed Assets	2,326	2,551	3,001	3,157	3,313
Invt in Associates & JVs	336	282	215	211	207
Other LT Assets	5,539	5,558	7,253	6,978	6,576
Cash & ST Invt	5,416	5,251	3,975	3,731	3,660
Inventory	55	92	96	93	94
Debtors	564	839	729	781	770
Other Current Assets	240	241	177	177	177
Total Assets	14,476	14,814	15,446	15,129	14,798
ST Debt	0	0	0	0	0
Creditors	1,509	1,495	1,693	1,629	1,474
Other Current Liab	466	518	452	452	452
LT Debt	0	0	0	0	0
Other LT Liabilities	538	754	2,486	2,486	2,486
Shareholder's Equity	11,963	12,047	10,815	10,562	10,386
Minority Interests	0	0	0	0	0
Total Cap. & Liab.	14,476	14,814	15,446	15,129	14,798
Non-Cash Wkg. Capital	(1,116)	(841)	(1,143)	(1,030)	(884)
Net Cash/(Debt)	5,416	5,251	3,975	3,731	3,660
Debtors Turn (avg days)	36.3	56.3	53.1	50.0	50.0
Creditors Turn (avg days)	790.0	39,159.3	772.2	759.8	677.1
Inventory Turn (avg days)	39.2	1,916.3	45.5	43.3	41.0
Asset Turnover (x)	0.3	0.3	0.4	0.4	0.4
Current Ratio (x)	3.2	3.2	2.3	2.3	2.4
Quick Ratio (x)	3.0	3.0	2.2	2.2	2.3
Net Debt/Equity (X)	CASH	CASH	CASH	CASH	CASH
Net Debt/Equity ex MI (X)	CASH	CASH	CASH	CASH	CASH
Capex to Debt (%)	N/A	N/A	N/A	N/A	N/A
Z-Score (X)	2.2	1.8	1.3	1.4	1.4

Source: Company, DBS HK

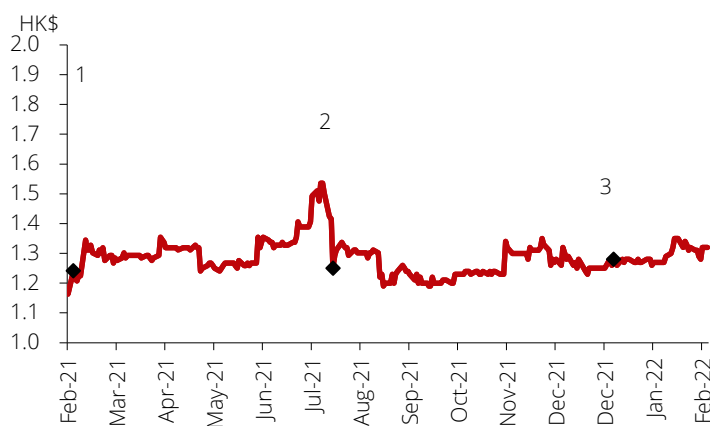
Cash Flow Statement (HK\$ m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Pre-Tax Profit	535	444	86	133	229
Dep. & Amort.	1,207	1,224	1,300	1,330	1,317
Tax Paid	0	(24)	0	(25)	(44)
Assoc. & JV Inc/(loss)	4	4	4	4	4
(Pft)/ Loss on disposal of FAs	0	0	0	0	0
Chg in Wkg.Cap.	76	(102)	348	(113)	(146)
Other Operating CF	(337)	(249)	1,638	(310)	(183)
Net Operating CF	1,485	1,297	3,376	1,018	1,178
Capital Exp.(net)	(503)	(593)	(874)	(397)	(397)
Other Invt.(net)	(203)	(202)	(2,040)	(103)	(103)
Invt in Assoc. & JV	0	0	0	0	0
Div from Assoc & JV	0	0	0	0	0
Other Investing CF	151	46	(2,586)	2,593	45
Net Investing CF	(555)	(749)	(5,500)	2,093	(455)
Div Paid	(4,150)	(291)	(1,315)	(361)	(361)
Chg in Gross Debt	(448)	(422)	(398)	(433)	(433)
Capital Issues	0	0	0	0	0
Other Financing CF	(471)	0	0	0	0
Net Financing CF	(5,069)	(713)	(1,713)	(794)	(794)
Currency Adjustments	0	0	0	0	0
Chg in Cash	(4,139)	(165)	(3,837)	2,317	(71)
Opg CFPS (HK\$)	0.29	0.29	0.63	0.23	0.27
Free CFPS (HK\$)	0.20	0.15	0.52	0.13	0.16

Source: Company, DBS HK

Hutchison Telecom

Target Price & Ratings History



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	1-Mar-21	HK\$1.34	HK\$2.10	Buy
2:	28-Jul-21	HK\$1.63	HK\$1.90	Buy
3:	5-Jan-22	HK\$1.26	HK\$1.40	Buy

Source: DBS HK

Analyst: Tsz Wang Tam
Harry Zhuang

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FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

*Share price appreciation + dividends

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