

Singapore Telecommunications (ST SP)

Singtel's NEXT growth engine

NCS set to contribute a bigger slice of ST's pie

Recent NCS acquisitions have bolstered Singtel's plan to seek out new regional businesses. Integrating digital, cloud and platform services (NCS NEXT) with existing capabilities should support higher margins. We continue to like Singtel's ability to: 1) capitalise on regional leadership via exclusive tie-ups with private, public and associates' businesses; 2) drive new growth engines; 3) unlock infrastructure asset value to drive growth. Reiterate BUY with SOTP-based TP of SGD2.98.

Digitalisation of enterprises not in full swing

We think digital transformation for enterprises is still in its early stage. According to IDC, 28% of organisations in APAC are in the most progressive stages of digital transformation maturity. The three sectors that currently drive NCS' business are: a) healthcare & transport; b) financial, industrial and commercials; and c) communications, media and technology. This has led to an unprecedented demand surge for digital and technology services, accelerated by Covid-19. While projects can be deployed within 3-5 years, adapting to change can be slow, extending the runway. With Asia-Pacific countries only realising the need to digitalise, it becomes clear that NCS is riding a multi-year trend.

Sustainable margins needed for re-rating

Technology proliferation started before the pandemic and digital economies were already experiencing a global growth spurt. With NCS building new capabilities and expanding its business as a pan-Asian B2B digital service provider, we forecast NCS' EBITDA margin to widen on higher-margin cloud services. EBITDA has been on the rise and is currently at 10% of ST's Group EBITDA. This is a positive, but we see upside if NCS can demonstrate: a) comparable growth in bookings as peers; b) faster-than-expected revenue growth; and c) sustained margin expansion as NEXT's services form a bigger proportion of NCS' revenue.

FYE Mar (SGD m)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue	16,541	15,567	16,422	17,424	17,369
EBITDA	4,047	3,756	4,081	4,054	4,620
Core net profit	1,074	1,657	2,335	2,641	3,079
Core FDEPS (cts)	6.6	10.1	14.3	16.2	18.8
Core FDEPS growth(%)	(65.3)	54.2	41.0	13.1	16.6
Net DPS (cts)	6.8	5.1	5.1	5.1	5.1
Core FD P/E (x)	38.6	24.1	18.6	16.5	14.1
P/BV (x)	1.5	1.5	1.6	1.6	1.6
Net dividend yield (%)	2.7	2.1	1.9	1.9	1.9
ROAE (%)	3.8	6.2	8.5	9.1	10.2
ROAA (%)	2.2	3.4	4.8	5.3	5.9
EV/EBITDA (x)	13.5	13.8	13.4	13.2	11.3
Net gearing (%) (incl perps)	49.1	45.7	39.5	33.7	28.1
Consensus net profit	-	-	2,218	2,667	3,042
MKE vs. Consensus (%)	-	-	5.3	(1.0)	1.2

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BUY

Share Price	SGD 2.66
12m Price Target	SGD 2.98 (+12%)
Previous Price Target	SGD 2.98

Company Description

Singtel is the largest integrated telecommunications service provider in Singapore and has significant share in Australia, India and ASEAN

Statistics

52w high/low (SGD)	2.66/2.23
3m avg turnover (USDm)	59.7
Free float (%)	41.8
Issued shares (m)	16,515
Market capitalisation	SGD43.9B USD32.3B

Major shareholders:

Temasek Holdings	52.2%
Central Provident Fund	4.9%
Capital Research	1.2%

Price Performance



	-1M	-3M	-12M
Absolute (%)	6	14	7
Relative to index (%)	(1)	5	(0)

Source: FactSet

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Tear Sheet Insert

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 5G to provide next legs of growth, while cash is harvested from wireless leadership to support investments and capex.
- Healthy balance sheet backs DPS payout ratio of 60-80%. Proceeds from sale of non-core assets are partly committed to exceptional payouts.

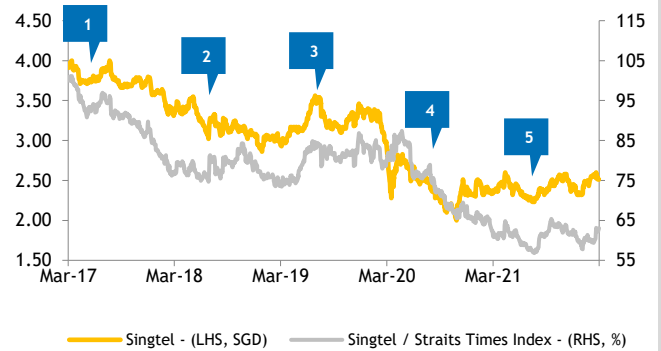
Singtel SOTP valuation

Valuation	Stake (%)	Valuation method	Valuation (LC)	Exch rate (SGD/LC)	Valuation (SGD m)	Per share (SGD)	% of total
SingTel Core Business	100.0	Singtel DCF (6.9% WACC, 0% TG, 0.90 beta) Optus DCF (6.0% WACC, 0% TG, 0.71 beta)	20,382	1.00	20,382	1.25	
(Less) Consol Net Debt					-11,312	-0.69	
Sub Total					9,070	0.56	19%
Associates	Stake (%)	Valuation method	Valuation (LC)	Exch rate (S\$/LC)	Valuation (SGD m)	Per share (SGD)	% of total
Teikomsel (Indonesia)	35.0	70% of Market Cap listed Telkom	#####	10,603	10,094	0.62	16%
Bharti Airtel (India)	31.7	DCF (9.4% WACC, 3% TG, 1.0 beta), mcap of africa and	1,538,551	54.00	28,492	1.75	44%
AIS (Thailand)	23.3	DCF (7.0% WACC, 2% LTG, 1.0 beta)	151,703	24.05	6,308	0.39	10%
Globe (Philippines)	46.9	DCF (5.7% WACC, 1% LTG, 0.7 beta)	132,239	38.13	3,468	0.21	5%
Intouch (Thailand)	21.1	SOTP (AIS TP and mkt cap of THCOM TB)	42,414	24.05	1,764	0.11	3%
NetLink NBN Trust (Singapore)	24.8	DDM (COE 6%, 0% LTG, 0.5 beta)	1,073	1.00	1,073	0.07	2%
SingPost (Singapore)	21.7	Market Cap	361	1.00	361	0.02	1%
Sub Total					51,198	3.16	
		25% discount				(0.79)	
Associates' value						2.37	80%
Total Equity Value						2.98	100%

Source: Factset, Maybank IBG Research

Price Drivers

Historical share price trend



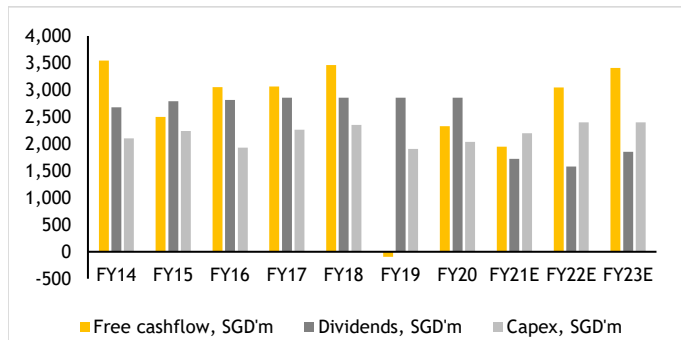
Source: Company, Maybank IBG Research

1. Proposal for fourth mobile licence. Bharti's profits started to taper off.
2. Proposal to increase effective stake in Bharti to 39.5%. Share price continued to be pressured by competitive environment.
3. Australia wireless pricing went through industry-wide reflation.
4. Earnings marred by weakness in ARPU on the back of lower usage of roaming and data given travel restriction and work-from-home arrangements.
5. Ongoing global economic disruption brought about by
6. COVID-19 and structural challenges brought about by intense market competition.

Financial Metrics

- We forecast EBITDA to register a 5.9% CAGR over FY21-23E due to earnings recovery following Covid-19.
- Pretax associate income could contribute to bottom line by growing 27% over the same period, led by Bharti's swing to net profit from net loss.
- We expect net debt to EBITDA, including associate dividends, to remain healthy at 1.6x-2.2x in FY21-23E; providing support to its fixed DPS commitment.

Free cash flow, dividends and capex



Source: Company, Maybank IBG Research

Swing Factors

Upside

- Strong growth in enterprise and Digital Life to positive operating leverage.
- Stronger-than-expected ARPU due to easing in price competition in countries it operates in.
- Faster-than-expected monetisation of 5G development.

Downside

- Further wireless margin compression triggered by competition in Singapore and / or Australia.
- Worse-than-expected cannibalisation of wireless voice, SMS and roaming by data.
- Failure to monetise 5G development.

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Risk Rating & Score ¹	18.2
Score Momentum ²	-1.6
Last Updated	16 Dec 2021
Controversy Score ³ (Updated: 11 Aug 2021)	2 - Customer Incidents

Business Model & Industry Issues

- Singtel is most exposed to cybersecurity and personal data leakage risks given its nature of business. There have been minor lapses due to IT, process and human errors over the years, and Singtel was penalised for an immaterial sum.
- Singtel will continue to educate its staff and improve practices and processes to minimise data breaches.
- As Singtel is in the business of connectivity, it is supporting digital inclusion through connecting communities and supporting the disadvantaged.
- Notably in FY20, the telco supported migrant workers with free remittance service and their WiFi and mobile data needs. It also provided refurbished laptops and data SIMs to disadvantaged students for their home-based learning. In Australia, Optus scaled up “Donate Your Data” to support disadvantaged students by offering them free mobile data access for online learning.
- Singtel displays no exceptional risks for a telco operator for ESG and is in line with peers in tackling ESG issues.

Material E issues

- Achieved carbon emissions intensity reduction of 70% in 2020, well exceeding our 2030 target of 50%.
- Over 84% of waste generated disposed via reuse, recycling or incineration with energy recovered.
- Only Southeast Asian company among a pioneer group of 28 global companies in July 2019 that committed to keeping global temperature increase within 1.5°C and net zero emissions by 2050.

Material S issues

- 28% of female employees in middle and top management.
- Singtel was included in the 2020 Bloomberg Gender-Equality Index and the Refinitiv Global Diversity & Inclusion Index 2019 and named as one of the top 10 employers for Gender Diversity at The Leonie Awards 2019.
- Total training investment of SGD21.9m and pledged SGD45m to boost the digital skills of its workforce through company-wide initiatives over three years.
- Zero fatality rate across Singtel and Optus in FY20.
- To promote digital inclusion, Optus has launched “Donate Your Data” in Australia to help disadvantaged young people bridge the digital divide.
- Singtel also supported 1,000 vulnerable seniors under CareLine 24-hour telephone befriending service with free mobile phone services to promote digital inclusion and well-being.

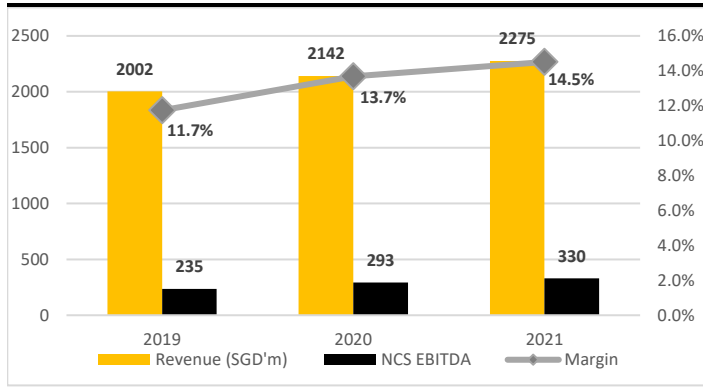
Key G metrics and issues

- Board consists of 10 directors, of which one is executive officer (MD/CEO), the remaining are non-executive & independent directors (including Chairman). 30% are female directors.
- The nomination, audit, investment and remuneration committees are chaired by independent directors.
- Key management/directors’ compensation accounted for 9.4%/1.3% of total employee compensation in 2019.
- There has been no corruption cases reported for the past three years.
- Cyber security and data leakage risks. Conducts its businesses in strict adherence to data protection laws - the Personal Data Protection Act in Singapore and the Privacy Act and Telecommunications Act in Australia.
- There have been minor lapses due to IT, process and human errors. Singtel will continue to educate its staff and improve practices and processes to minimise data breaches.

¹**Risk Rating & Score** - derived by Sustainalytics and assesses the company’s exposure to unmanaged ESG risks. Scores range between 0 - 50 in order of increasing severity with low/high scores & ratings representing negligible/significant risk to the company’s enterprise value, respectively, from ESG-driven financial impacts. ²**Score Momentum** - indicates changes to the company’s score since the last update - a **negative** integer indicates a company’s improving risk score; a **positive** integer indicates a deterioration. ³**Controversy Score** - reported periodically by Sustainalytics in the event of material ESG-related incident(s), with the impact severity scores of these events ranging from Category 0-5 (0 - no reports; 1 - negligible risks; ...; 5 - poses serious risks & indicative of potential structural deficiencies at the company).

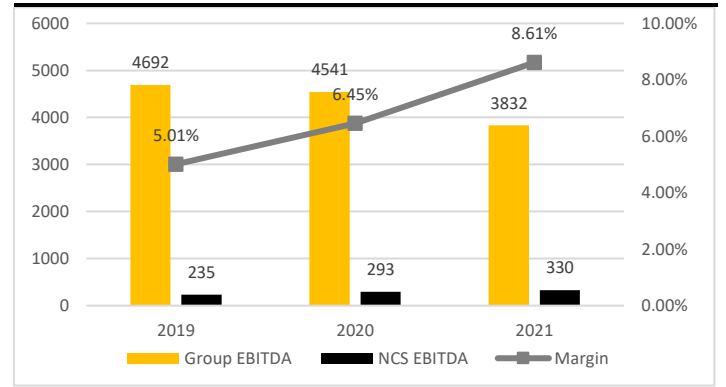
1. Focus Charts

Fig 1: NCS' sales and EBITDA margin over the past 3 years



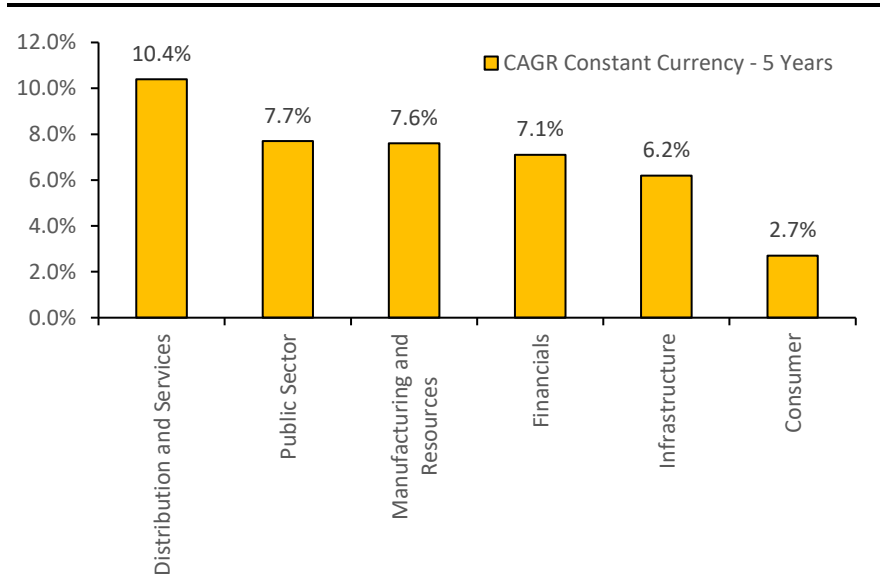
Source: Company

Fig 2: NCS's EBITDA as a % of group EBITDA



Source: Company

Fig 3: Asia Pacific digitalization spending (CAGR by sector)



Source: International Data Corporation (IDC)

2. The basics: Key markets, Growth Model and more

We attended a teach-in session by NCS about its Enterprise Solution business. Combining the experience and expertise of its 10,000-strong team across 55 specialisations, NCS provides differentiated and end-to-end technology services to clients in the public and private sector. NEXT's capabilities span digital, cloud and platforms, with NCS' core offerings in applications, infrastructure, engineering and cybersecurity. Key markets are APAC, Australia and China with the fastest growth on a smaller revenue base. NCS reported FY21 revenue of SGD2.3b (~14% of group revenue), EBIT SGD249m and EBIT margin 10.9%. Overall FY22 revenue growth is projected to be mid-teens, driven by enterprise digitalisation

3. Recent developments at NCS

3.1 NCS' buyout of Dialog, Australia largest private IT services company. Accelerating the plan to be a pan-Asian B2B digital service provider, NCS' acquisition of Dialog should bolster its proposition in Australia by: (1) increasing its number of highly skilled IT specialists; (2) providing greater market access through a wide range of tier-1 clients from a multitude of sectors; and (3) leverage complementary capabilities and expertise to create a stronger end-to-end suite of technology and digital services for NCS' clients in Australia and across the region. Due to the pandemic, Dialog's FY21 earnings was only AUD12m, or just -2% of Singtel's FY21 net income. Nevertheless, we expect earnings to grow as NCS will supplement Dialog by providing a stronger suite of enterprise clients in Australia given NCS' capabilities in AI, cloud computing and cyber security. We can already see good traction for Dialog post-Covid-19 recovery, based on 1H22 results.

3.2 **Acquired Australian digital services company ARQ Group**
Singtel's technology services arm NCS acquired Australian digital services company ARQ Group for SGD297m as part of its regionalisation plans. ARQ is a Melbourne-based digital consultancy group specialising in mobile applications, cloud and data analytics. The acquisition will be NCS's fourth in Australia in the past 15 months.

This acquisition will ramp up NCS presence in the Australian market, bringing in digital competencies that help create a highly compelling end-to-end digital transformation value proposition. For ARQ, joining the NCS family will allow the group to grow internationally serve regional clients besides capturing more domestic market share by leveraging synergies within NCS.

ARQ is one of the largest fast-growing digital services providers in Australia, and it has a strong client coverage and serves half of the Australian Securities Exchange's top 20 companies across the financial services, utilities, retail, healthcare, travel and government sectors. It expects ARQ's revenue to increase 38% YoY to AUD118m by the end of 2022, while EBITDA is projected to rise to AUD18.4m. Post-acquisition, ARQ's 560-strong team will increase NCS's headcount in Australia to 1,900.

FYE 31 Mar	FY20A	FY21A	FY22E	FY23E	FY24E
Key Metrics					
P/E (reported) (x)	48.8	23.7	18.6	16.4	14.1
Core P/E (x)	38.6	24.0	18.6	16.4	14.1
Core FD P/E (x)	38.6	24.1	18.6	16.5	14.1
P/BV (x)	1.5	1.5	1.6	1.6	1.6
P/NTA (x)	3.2	3.0	3.2	3.1	3.0
Net dividend yield (%)	2.7	2.1	1.9	1.9	1.9
FCF yield (%)	0.8	11.1	5.6	7.4	9.1
EV/EBITDA (x)	13.5	13.8	13.4	13.2	11.3
EV/EBIT (x)	27.9	48.5	39.2	40.4	27.5

INCOME STATEMENT (SGD m)

Revenue	16,541.0	15,566.7	16,422.0	17,424.4	17,369.2
EBITDA	4,047.3	3,755.7	4,081.2	4,053.9	4,620.2
Depreciation	(2,580.0)	(2,685.0)	(2,685.0)	(2,731.0)	(2,730.0)
Amortisation	0.0	0.0	0.0	0.0	0.0
EBIT	1,960.3	1,070.7	1,396.2	1,322.9	1,890.2
Net interest income / (exp)	(282.0)	(395.0)	(375.8)	(375.7)	(375.6)
Associates & JV	1,742.7	1,798.0	2,463.0	2,991.3	3,075.8
Exceptionals	(1,381.4)	0.0	0.0	0.0	0.0
Other pretax income	0.0	0.0	0.0	0.0	0.0
Pretax profit	2,039.6	2,473.7	3,483.3	3,938.5	4,590.5
Income tax	(988.0)	(811.0)	(1,142.0)	(1,291.2)	(1,505.0)
Minorities	22.4	(6.2)	(6.2)	(6.2)	(6.2)
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Reported net profit	1,074.0	1,656.5	2,335.1	2,641.1	3,079.3
Core net profit	1,074.0	1,656.5	2,335.1	2,641.1	3,079.3

BALANCE SHEET (SGD m)

Cash & Short Term Investments	999.6	754.7	1,547.3	2,873.4	4,237.8
Accounts receivable	5,559.4	5,443.7	5,742.8	6,093.3	6,074.0
Inventory	279.6	271.6	328.4	348.5	347.4
Reinsurance assets	0.0	0.0	0.0	0.0	0.0
Property, Plant & Equip (net)	10,363.8	11,534.1	11,269.1	11,200.1	11,398.1
Intangible assets	13,735.9	13,129.1	13,129.1	13,129.1	13,129.1
Investment in Associates & JVs	16,287.3	15,790.3	15,790.3	15,790.3	15,790.3
Other assets	1,729.3	1,074.9	1,603.9	1,603.9	1,603.9
Total assets	48,954.9	47,998.4	49,410.9	51,038.6	52,580.6
ST interest bearing debt	3,970.5	2,033.9	2,033.9	2,033.9	2,033.9
Accounts payable	6,373.8	6,784.8	7,462.0	7,917.5	7,892.4
Insurance contract liabilities	0.0	0.0	0.0	0.0	0.0
LT interest bearing debt	10,202.1	10,825.6	10,825.6	10,817.0	10,817.2
Other liabilities	2,382.0	1,843.0	445.0	445.0	445.0
Total Liabilities	22,928.7	21,487.0	20,766.2	21,213.0	21,188.1
Shareholders Equity	26,789.2	26,485.8	28,645.8	29,549.8	30,595.0
Minority Interest	24.8	25.6	25.6	25.6	25.6
Total shareholder equity	26,814.0	26,511.4	28,671.4	29,575.4	30,620.6
Total liabilities and equity	48,954.9	47,998.4	49,437.5	50,788.4	51,808.7

CASH FLOW (SGD m)

Pretax profit	2,039.6	2,473.7	3,483.3	3,938.5	4,590.5
Depreciation & amortisation	2,580.0	2,685.0	2,685.0	2,731.0	2,730.0
Adj net interest (income)/exp	(2,031.9)	(1,695.0)	(1,412.4)	(1,255.9)	(1,401.2)
Change in working capital	78.8	878.1	(207.7)	84.9	(4.7)
Cash taxes paid	0.0	0.0	0.0	0.0	0.0
Other operating cash flow	0.4	0.0	0.4	0.4	0.5
Cash flow from operations	2,666.5	4,031.2	4,548.2	5,498.5	5,914.6
Capex	(2,036.6)	(2,200.0)	(2,420.0)	(2,662.0)	(2,928.0)
Free cash flow	3,395.0	2,328.2	2,128.2	2,836.5	2,986.6
Dividends paid	(2,856.7)	(1,722.2)	(1,634.6)	(1,848.8)	(2,155.5)
Equity raised / (purchased)	0.0	0.0	0.0	0.0	0.0
Change in Debt	0.0	0.0	0.0	0.0	0.0
Other invest/financing cash flow	13,763.4	(353.9)	(1,265.7)	667.6	1,034.9
Effect of exch rate changes	0.0	0.0	0.0	0.0	0.0
Net cash flow	11,536.6	(244.9)	792.6	1,326.1	1,364.4

FYE 31 Mar	FY20A	FY21A	FY22E	FY23E	FY24E
Key Ratios					
Growth ratios (%)					
Revenue growth	(4.8)	(5.9)	5.5	6.1	(0.3)
EBITDA growth	(17.8)	(7.2)	8.7	(0.7)	14.0
EBIT growth	(20.6)	(45.4)	30.4	(5.3)	42.9
Pretax growth	(48.0)	21.3	40.8	13.1	16.6
Reported net profit growth	(65.3)	54.2	41.0	13.1	16.6
Core net profit growth	(65.3)	54.2	41.0	13.1	16.6
Profitability ratios (%)					
EBITDA margin	24.5	24.1	24.9	23.3	26.6
EBIT margin	11.9	6.9	8.5	7.6	10.9
Pretax profit margin	12.3	15.9	21.2	22.6	26.4
Payout ratio	103.3	50.2	35.6	31.5	27.0
DuPont analysis					
Net profit margin (%)	6.5	10.6	14.2	15.2	17.7
Revenue/Assets (x)	0.3	0.3	0.3	0.3	0.3
Assets/Equity (x)	1.8	1.8	1.7	1.7	1.7
ROAE (%)	3.8	6.2	8.5	9.1	10.2
ROAA (%)	2.2	3.4	4.8	5.3	5.9
Liquidity & Efficiency					
Cash conversion cycle	na	na	na	na	na
Days receivable outstanding	125.7	127.2	122.6	122.3	126.1
Days inventory outstanding	na	na	na	na	na
Days payables outstanding	na	na	na	na	na
Dividend cover (x)	1.0	2.0	2.8	3.2	3.7
Current ratio (x)	0.7	0.7	0.8	1.0	1.1
Leverage & Expense Analysis					
Asset/Liability (x)	2.1	2.2	2.4	2.4	2.5
Net gearing (%) (incl perps)	49.1	45.7	39.5	33.7	28.1
Net gearing (%) (excl. perps)	49.1	45.7	39.5	33.7	28.1
Net interest cover (x)	7.0	2.7	3.7	3.5	5.0
Debt/EBITDA (x)	3.5	3.4	3.2	3.2	2.8
Capex/revenue (%)	12.3	14.1	14.7	15.3	16.9
Net debt/ (net cash)	13,173.0	12,104.8	11,312.2	9,977.5	8,613.3

Source: Company; Maybank IBG Research

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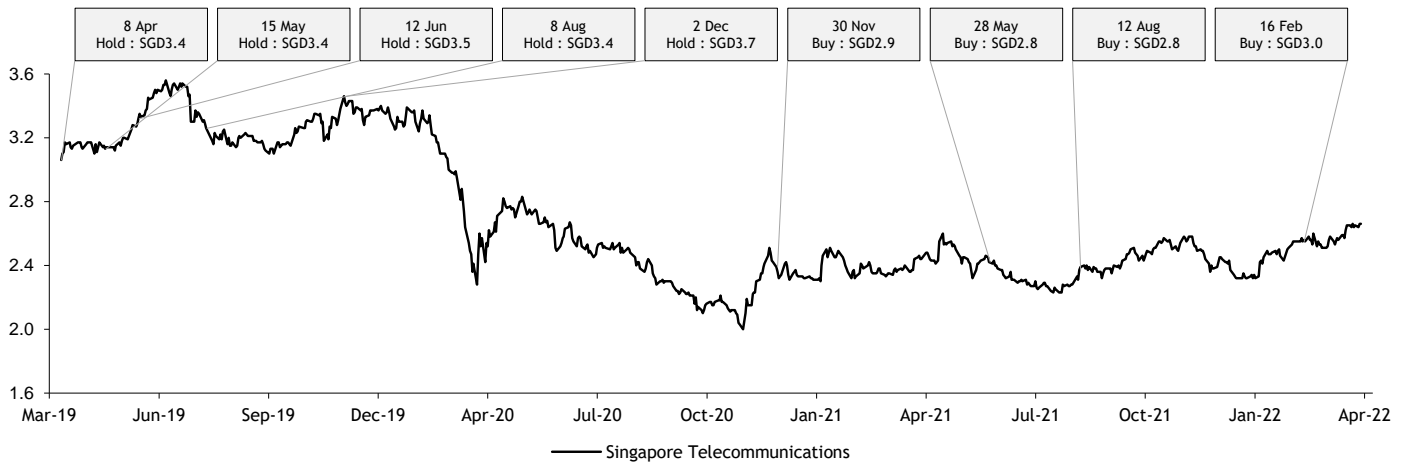
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