

# China / Hong Kong Company Update

## HKT Trust

Bloomberg: 6823 HK Equity | Reuters: 6823.HK

Refer to important disclosures at the end of this report

DBS Group Research . Equity

12 Aug 2022

### BUY

Last Traded Price (11 Aug 2022): HK\$10.92 (HSI : 20,082)

Price Target 12-mth: HK\$13.30 (22% upside)

#### Analyst

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#### What's New

- 1H22 results in line; AFF increased by 2.2% y-o-y
- Local business maintained stable growth; local TSS and local mobile core revenue grew 3% and 2%, respectively
- Expect 30% 5G penetration for post-paid customer base by FY22
- Maintain BUY with a TP of HK\$13.3 for its attractive dividend yield of 7%

#### Price Relative



#### Forecasts and Valuation

FY Dec (HK\$m)	2021A	2022F	2023F	2024F
Turnover	33,961	34,767	35,512	36,212
EBITDA	12,619	13,149	13,486	13,861
Pre-tax Profit	5,819	5,946	6,042	6,298
Net Profit	4,808	4,951	5,031	5,245
Net Profit Gth (Pre-ex) (%)	(9.3)	3.0	1.6	4.2
EPS (HK\$)	0.63	0.65	0.66	0.69
EPS Gth (%)	(9.3)	2.9	1.6	4.2
Diluted EPS (HK\$)	0.63	0.65	0.66	0.69
DPS (HK\$)	0.73	0.75	0.77	0.79
BV Per Share (HK\$)	4.90	4.76	4.67	4.58
PE (X)	17.2	16.7	16.4	15.8
P/Cash Flow (X)	7.8	7.4	7.3	7.1
P/Free CF (X)	15.3	12.7	12.2	12.7
EV/EBITDA (X)	9.8	9.6	9.5	9.4
Net Div Yield (%)	6.7	6.9	7.0	7.2
P/Book Value (X)	2.2	2.3	2.3	2.4
Net Debt/Equity (X)	1.1	1.2	1.3	1.4
ROAE (%)	12.8	13.5	14.1	15.0
AFF	5,513	5,670	5,818	5,950
AFF Gth (%)	2.4	2.8	2.6	2.3
AFF Rev (%)		(0.4)	(0.5)	New
Consensus EPS (HK\$)		0.65	0.68	0.69
Other Broker Recs:		B:11	S:0	H:1

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

### Still a trusted pick

#### Investment Thesis

Attractive dividend yield of c.7% with steady AFF growth at an expected CAGR of c.3% in FY21-FY24.

Further roaming revenue shrinkage unlikely. As the COVID-19 outbreak has reduced the number of travellers, roaming revenue accounts for only c.5% of the total during the pandemic, vs. c.13% before COVID-19. Thus, any roaming revenue recovery will be positive for AFF growth.

Expect higher 5G penetration to drive ARPU recovery. We forecast post-paid mobile ARPU to improve by 1% and 2% in FY22 and FY23, respectively.

#### Valuation:

Our TP of HK\$13.3 is based on a dividend discount model (DDM), assuming a 7.2% cost of equity.

#### Where we differ:

The market is concerned about the impact of lower IT spending in the enterprise market due to COVID-19. We believe that the impact is manageable, as demand for telecommunication services such as broadband is relatively stable.

#### Key Risks to Our View:

**Price war in mobile market.** Hong Kong's mobile market is crowded with four major players and a price war would put pressure on the company's mobile ARPU.

**Interest rate upcycle.** Any increase in interest rates will reduce the adjusted funds flow (AFF) and thereby dividend distribution.

#### At A Glance

Issued Capital (m shrs)	7,576
Mkt Cap (HKm/US\$m)	82,730 / 10,546
Major Shareholders (%)	
PCCW Ltd	51.9
Free Float (%)	48.1
3m Avg. Daily Val. (US\$m)	8.76
GICS Industry: Communication Services / Telecommunication Services	



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**WHAT'S NEW****1H22 results in line; local operation registered solid growth****1H22 results highlights**

Total revenue grew by 3% y-o-y to HK\$16.2bn, with revenue excluding mobile product sales increasing by 5% y-o-y to HK\$14.9bn. Segment wise, TSS revenue increased by 5% y-o-y to HK\$11.6bn, with local TSS services and international communications services revenue increasing by 3% and 9%, respectively. Mobile service revenue grew by 2% y-o-y to HK\$3.6bn, supported by 2% y-o-y growth in the local core business due to rising 5G adoption and higher revenue contribution from mobile enterprise solutions. Revenue contribution from roaming and IDD remained under pressure.

The company's mobile post-paid subs base increased 42k y-o-y to 3,305k, with the churn rate slightly expanding to 0.9%. Its 5G customer base reached 867k as of Jun 2022, representing 26% of the post-paid subs base. Mobile post-paid exit ARPU remained stable at HK\$187 in 1H22, as the 5G service plan uplift was partially offset by competition in the price-conscious segment.

EBITDA increased by 2% y-o-y to HK\$5.8bn, with the EBITDA margin contracting 0.4ppt y-o-y to 36.1%. Adjusted funds flow (AFF) increased by 2% y-o-y to HK\$2.4bn, in line with market expectations. The company proposed an interim dividend of HK\$0.3136 per share staple unit (SSU), representing a full payout of AFF.

**Outlook**

We expect the fixed-line business to grow at a low single-digit rate, driven by continued upgrades to FTTH services, an expanding uptake of home Wi-Fi services, as well as accelerated enterprise digital transformation. The competition in the residential broadband market is still manageable for HKT, as evidenced by its stable customer base.

For the mobile business, mobile roaming revenue has been affected since the outbreak of the pandemic. However, further shrinkage is unlikely, given the gradual easing of quarantine measures in Hong Kong. Compulsory hotel quarantine has been cut to three days for overseas travellers. Local mobile service revenue will continue to benefit from rising 5G adoption and growing mobile enterprise solutions revenue. As of Jul 2022, the 5G penetration rate reached 28% for post-paid subscribers, and management expects it to reach at least 30% by FY22. We forecast that post-paid mobile ARPU would improve by 1% and 2% in FY22 and FY23, respectively.

HKT continues to enhance its operating efficiency, with 8% of opex savings in 1H22 and a lower opex-to-revenue ratio of 13.5%, compared to 15.2% in 1H21. HKT will further improve its operating efficiency by accelerating digitalisation and optimising sales channels.

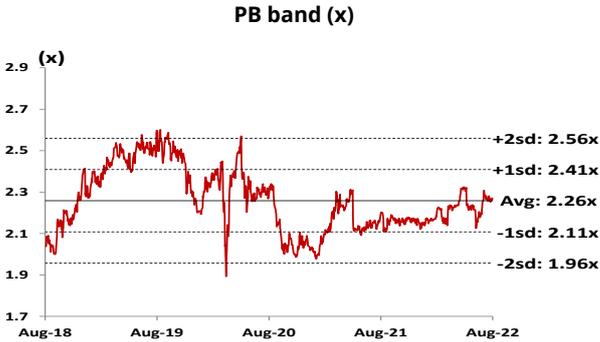
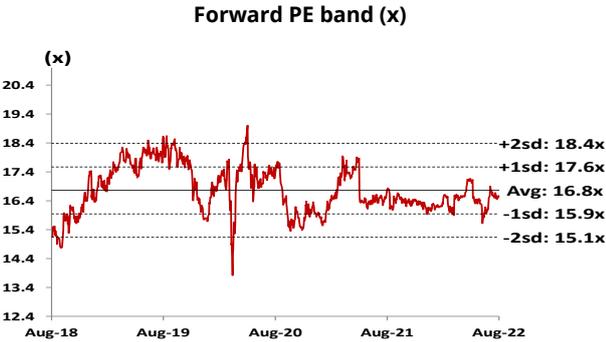
We have kept our AFF forecast largely unchanged. We forecast AFF growth to increase by 2.8%, 2.6%, and 2.3% for FY22, FY23, and FY24, respectively. We maintain our BUY call with the TP unchanged at HK\$13.3, for its attractive dividend yield of 7%. Our TP is based on the DDM, assuming a 7.2% cost of equity.

**Company Background**

HKT is an integrated telecom service provider in Hong Kong, with the largest market share in the fixed-line and mobile markets. The company's broadband services are provided via the brand "Netvigator" and its mobile services are provided via the brands "csl.", "1010", and "SUN Mobile". HKT is 52%-owned by PCCW (8 HK).

**HKT Trust**

**Historical PE and PB band**



Source: Thomson Reuters, DBS HK

## HKT Trust

### Key Assumptions

FY Dec	2020A	2021A	2022F	2023F	2024F
Fixed-line sub growth (%)	(2.9)	(3.1)	(1.5)	(1.5)	(1.5)
Broadband sub growth (%)	0.5	0.3	0.7	0.7	1.4
Mobile sub growth (%)	(1.6)	3.6	1.3	1.3	1.0
Mobile ARPU	139.0	139.0	139.0	141.0	144.0
EBITDA margin (%)	38.7	37.5	37.8	38.0	38.3

Source: Company, DBS HK

### Segmental Breakdown (HK\$ m)

FY Dec	2020A	2021A	2022F	2023F	2024F
<b>Revenues (HK\$ m)</b>					
TSS	22,357	21,812	22,320	22,717	23,072
Mobile	10,366	11,748	11,932	12,168	12,408
PayTV	647	2,456	2,579	2,708	2,843
Other businesses	241	872	959	1,007	1,037
Eliminations	(1,222)	(2,927)	(3,023)	(3,088)	(3,149)
<b>Total</b>	<b>32,389</b>	<b>33,961</b>	<b>34,767</b>	<b>35,512</b>	<b>36,212</b>

Source: Company, DBS HK

### Income Statement (HK\$ m)

FY Dec	2020A	2021A	2022F	2023F	2024F
Revenue	32,389	33,961	34,767	35,512	36,212
Cost of Goods Sold	(15,703)	(16,729)	(16,973)	(17,310)	(17,602)
<b>Gross Profit</b>	<b>16,686</b>	<b>17,232</b>	<b>17,794</b>	<b>18,202</b>	<b>18,610</b>
Other Opng (Exp)/Inc	(9,498)	(10,127)	(10,369)	(10,478)	(10,569)
<b>Operating Profit</b>	<b>7,188</b>	<b>7,105</b>	<b>7,425</b>	<b>7,724</b>	<b>8,042</b>
Other Non Opg (Exp)/Inc	361	(8)	0	0	0
Associates & JV Inc	(79)	(130)	(125)	(120)	(120)
Net Interest (Exp)/Inc	(1,296)	(1,148)	(1,354)	(1,562)	(1,624)
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	0	0	0	0	0
<b>Pre-tax Profit</b>	<b>6,174</b>	<b>5,819</b>	<b>5,946</b>	<b>6,042</b>	<b>6,298</b>
Tax	(855)	(997)	(981)	(997)	(1,039)
Minority Interest	(16)	(14)	(14)	(14)	(14)
Preference Dividend	0	0	0	0	0
<b>Net Profit</b>	<b>5,303</b>	<b>4,808</b>	<b>4,951</b>	<b>5,031</b>	<b>5,245</b>
Net Profit before Except.	5,303	4,808	4,951	5,031	5,245
EBITDA	12,529	12,619	13,149	13,486	13,861
<b>Growth</b>					
Revenue Gth (%)	(2.2)	4.9	2.4	2.1	2.0
EBITDA Gth (%)	(2.2)	0.7	4.2	2.6	2.8
Opg Profit Gth (%)	(6.6)	(1.2)	4.5	4.0	4.1
Net Profit Gth (%)	1.6	(9.3)	3.0	1.6	4.2
<b>Margins &amp; Ratio</b>					
Gross Margins (%)	51.5	50.7	51.2	51.3	51.4
Opg Profit Margin (%)	22.2	20.9	21.4	21.8	22.2
Net Profit Margin (%)	16.4	14.2	14.2	14.2	14.5
ROAE (%)	14.0	12.8	13.5	14.1	15.0
ROA (%)	5.2	4.5	4.5	4.5	4.6
ROCE (%)	7.0	6.4	6.6	6.8	6.9
Div Payout Ratio (%)	101.5	114.7	114.5	115.6	113.4
Net Interest Cover (x)	5.5	6.2	5.5	4.9	5.0

Source: Company, DBS HK

## HKT Trust

### Interim Income Statement (HK\$ m)

FY Dec	1H2020	2H2020	1H2021	2H2021	1H2022
Revenue	14,606	17,783	15,643	18,318	16,157
Cost of Goods Sold	(6,941)	(8,762)	(7,550)	(9,179)	(8,134)
<b>Gross Profit</b>	<b>7,665</b>	<b>9,021</b>	<b>8,093</b>	<b>9,139</b>	<b>8,023</b>
Other Oper. (Exp)/Inc	(4,608)	(4,890)	(5,127)	(5,000)	(5,014)
<b>Operating Profit</b>	<b>3,057</b>	<b>4,131</b>	<b>2,966</b>	<b>4,139</b>	<b>3,009</b>
Other Non Opg (Exp)/Inc	(50)	411	0	(8)	3
Associates & JV Inc	(30)	(49)	(63)	(67)	(38)
Net Interest (Exp)/Inc	(658)	(638)	(561)	(587)	(627)
Exceptional Gain/(Loss)	0	0	0	0	0
<b>Pre-tax Profit</b>	<b>2,319</b>	<b>3,855</b>	<b>2,342</b>	<b>3,477</b>	<b>2,347</b>
Tax	(414)	(441)	(434)	(563)	(435)
Minority Interest	(7)	(9)	(8)	(6)	(2)
<b>Net Profit</b>	<b>1,898</b>	<b>3,405</b>	<b>1,900</b>	<b>2,908</b>	<b>1,910</b>
Net profit bef Except.	1,898	3,405	1,900	2,908	1,910

### Growth

Revenue Gth (%)	(3.3)	(1.2)	7.1	3.0	3.3
Opg Profit Gth (%)	(9.1)	(4.6)	(3.0)	0.2	1.4
Net Profit Gth (%)	(12.2)	11.5	0.1	(14.6)	0.5

### Margins

Gross Margins (%)	52.5	50.7	51.7	49.9	49.7
Opg Profit Margins (%)	20.9	23.2	19.0	22.6	18.6
Net Profit Margins (%)	13.0	19.1	12.1	15.9	11.8

Source: Company, DBS HK

### Balance Sheet (HK\$ m)

FY Dec	2020A	2021A	2022F	2023F	2024F
Net Fixed Assets	24,221	25,387	26,491	27,567	28,619
Invts in Associates & JVs	813	915	890	870	850
Other LT Assets	68,400	72,175	72,809	73,437	74,491
Cash & ST Invts	2,737	3,070	2,686	2,622	2,090
Inventory	820	1,218	1,249	1,278	1,308
Debtors	3,253	3,953	4,047	3,989	4,068
Other Current Assets	2,927	2,894	2,873	2,851	2,830
<b>Total Assets</b>	<b>103,171</b>	<b>109,612</b>	<b>111,044</b>	<b>112,615</b>	<b>114,256</b>
ST Debt	1,552	61	61	61	61
Creditors	3,945	5,250	5,580	5,691	5,787
Other Current Liab	9,872	10,892	10,892	10,892	10,892
LT Debt	40,719	43,628	45,628	47,628	49,628
Other LT Liabilities	9,183	12,584	12,743	12,902	13,072
Shareholder's Equity	37,838	37,141	36,070	35,357	34,718
Minority Interests	62	56	70	84	98
<b>Total Cap. &amp; Liab.</b>	<b>103,171</b>	<b>109,612</b>	<b>111,044</b>	<b>112,615</b>	<b>114,256</b>
Non-Cash Wkg. Capital	(6,817)	(8,077)	(8,304)	(8,464)	(8,473)
Net Cash/(Debt)	(39,534)	(40,619)	(43,003)	(45,067)	(47,599)
Debtors Turn (avg days)	38.6	38.7	42.0	41.3	40.6
Creditors Turn (avg days)	110.7	151.5	177.7	180.0	179.6
Inventory Turn (avg days)	28.6	33.6	40.5	40.4	40.5
Asset Turnover (x)	0.3	0.3	0.3	0.3	0.3
Current Ratio (x)	0.6	0.7	0.7	0.6	0.6
Quick Ratio (x)	0.4	0.4	0.4	0.4	0.4
Net Debt/Equity (X)	1.0	1.1	1.2	1.3	1.4
Net Debt/Equity ex MI (X)	1.0	1.1	1.2	1.3	1.4
Capex to Debt (%)	11.3	12.0	10.1	9.7	10.2
Z-Score (X)	1.7	1.6	1.6	1.6	NA

Source: Company, DBS HK

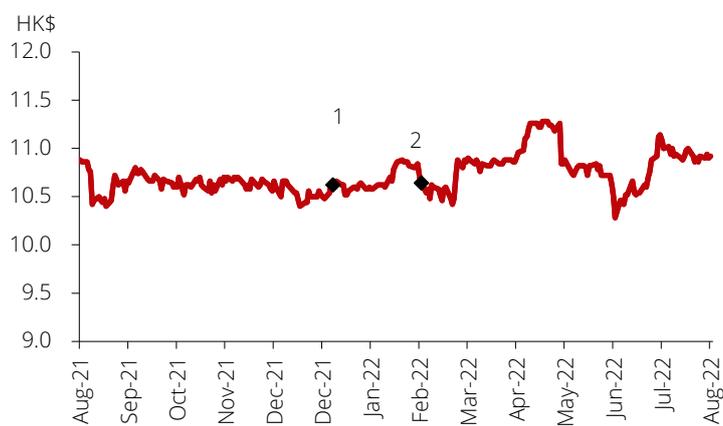
**HKT Trust**
**Cash Flow Statement (HK\$ m)**

<b>FY Dec</b>	<b>2020A</b>	<b>2021A</b>	<b>2022F</b>	<b>2023F</b>	<b>2024F</b>
Pre-Tax Profit	6,174	5,819	5,946	6,042	6,298
Dep. & Amort.	5,341	5,652	5,850	5,882	5,939
Tax Paid	(516)	27	(592)	(602)	(627)
Assoc. & JV Inc/(loss)	79	130	25	20	20
(Pft)/ Loss on disposal of FAs	0	0	0	0	0
Chg in Wkg.Cap.	(1,717)	(2,322)	(1,483)	(1,555)	(1,713)
Other Operating CF	1,179	1,335	1,402	1,609	1,669
<b>Net Operating CF</b>	<b>10,540</b>	<b>10,641</b>	<b>11,147</b>	<b>11,396</b>	<b>11,586</b>
Capital Exp.(net)	(4,765)	(5,223)	(4,630)	(4,630)	(5,088)
Other Invt.(net)	0	(2)	0	0	0
Invt in Assoc. & JV	(1,815)	(292)	0	0	0
Div from Assoc & JV	0	0	0	0	0
Other Investing CF	(39)	108	0	0	0
<b>Net Investing CF</b>	<b>(6,619)</b>	<b>(5,409)</b>	<b>(4,630)</b>	<b>(4,630)</b>	<b>(5,088)</b>
Div Paid	(5,336)	(5,428)	(6,022)	(5,744)	(5,884)
Chg in Gross Debt	1,818	1,444	2,000	2,000	2,000
Capital Issues	48	0	0	0	0
Other Financing CF	(809)	(932)	(2,879)	(3,086)	(3,146)
<b>Net Financing CF</b>	<b>(4,279)</b>	<b>(4,916)</b>	<b>(6,901)</b>	<b>(6,830)</b>	<b>(7,030)</b>
Currency Adjustments	33	3	0	0	0
Chg in Cash	(325)	319	(384)	(64)	(532)
Opg CFPS (HK\$)	1.62	1.71	1.67	1.71	1.76
Free CFPS (HK\$)	0.76	0.72	0.86	0.89	0.86

Source: Company, DBS HK

**HKT Trust**

**Target Price & Ratings History**



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	5-Jan-22	HK\$10.64	HK\$13.30	Buy
2:	25-Feb-22	HK\$10.70	HK\$13.30	Buy

Source: DBS HK

Analyst: Tsz Wang Tam  
Harry Zhuang

**HKT Trust**

DBS HK recommendations are based on an Absolute Total Return\* Rating system, defined as follows:

**STRONG BUY** (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

**BUY** (>15% total return over the next 12 months for small caps, >10% for large caps)

**HOLD** (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

**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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Sources for all charts and tables are DBS HK unless otherwise specified.

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