

China / Hong Kong Company Update

HKBN Ltd.

Bloomberg: 1310 HK Equity | Reuters: 1310.HK

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DBS Group Research . Equity

16 Jan 2024

BUY

Last Traded Price (15 Jan 2024): HK\$3.41 (HSI : 16,216)
Price Target 12-mth: HK\$5.70 (67% upside) (Prev HK\$5.50)

Analyst

Andy Yu +852 3668 4194 andyyuakh@db.com
Tsz Wang Tam +852 36684195 tszwangtam@db.com

What's New

- Residential and enterprise business to grow by 1.4% and 14% y-o-y in FY8/24, accelerating from -1.7% and 9% growth in FY8/23, respectively
- Raised AFF forecasts by 6-7% for FY8/24-FY8/26, on higher residential and enterprise business revenue assumptions
- Forecast AFF to grow by 3.1%, 9.6%, and 6.4% for FY8/24-FY8/26, respectively
- Maintain BUY on attractive dividend yield of 12%; TP of HK\$5.7

Price Relative



Forecasts and Valuation

FY Aug (HK\$m)	2023A	2024F	2025F	2026F
Turnover	11,692	12,190	12,724	13,357
EBITDA	2,281	2,475	2,560	2,606
Pre-tax Profit	(1,231)	64	179	238
Net Profit	(1,267)	116	238	301
Net Profit Gth (Pre-ex) (%)	N/A	N/A	105.7	26.4
EPS (HK\$)	(0.97)	0.09	0.18	0.23
EPS (HK\$)	(0.97)	0.09	0.18	0.23
EPS Gth (%)	N/A	N/A	105.7	26.4
Diluted EPS (HK\$)	(0.86)	0.08	0.16	0.20
DPS (HK\$)	0.40	0.41	0.45	0.48
BV Per Share (HK\$)	2.33	2.01	1.76	1.52
PE (X)	nm	38.6	18.7	14.8
P/Cash Flow (X)	2.5	2.2	2.1	2.0
P/Free CF (X)	3.8	3.0	2.8	2.8
EV/EBITDA (X)	6.3	5.8	5.5	5.2
Net Div Yield (%)	11.7	12.1	13.3	14.1
P/Book Value (X)	1.5	1.7	1.9	2.2
Net Debt/Equity (X)	3.3	3.7	4.1	4.6
ROAE (%)	(31.8)	4.1	9.7	14.0
AFF Rev (%)		7	7	6
Consensus EPS (HK\$)		0.15	0.31	0.45
Other Broker Recs:		B:3	S:0	H:2

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

Surfing on the digitalisation wave

Investment Thesis

A leading pure fixed-lined operator in Hong Kong, HKBN has market share of 34% in terms of residential broadband subscribers, behind HKT's 55% market share. In addition, the company also serves enterprise customers by offering broadband and one-stop ICT solutions.

Shifting to ARPU maximisation in residential broadband market. The company is now shifting its focus towards ARPU maximisation after reaching 920k subscribers in FY8/23 (up from 897k in FY8/22). Apart from lifting prices, the strategy involves: (1) offering bundling solutions by partnering with OTT content providers like TVB, Disney+, Netflix and IQIYI; and (2) upselling higher bandwidth solutions. Since the start of 2HFY8/23, new contract ARPU has maintained its uptrend and reached HK\$201 in Aug (26% higher than its base ARPU of HK\$179).

Enterprise business the key growth driver. The company's growth potential in the enterprise segment is substantial. The Total Addressable Market (TAM), including system integration services, is >10x larger compared to the traditional telecom industry, as indicated by management. The company's enterprise segment exhibited positive momentum, with orders growing by 18% in 2H FY8/23. The strong FY23 backlog is expected to contribute to future revenue, thereby supporting future AFF growth.

BUY, TP lifted to HK\$5.7 (from HK\$5.5). We maintain BUY for the stock's attractive dividend yield of 12% with an AFF CAGR of 6.3% in FY8/23-FY8/26. Our TP is based on dividend discount model (DDM) and assumes 9.9% cost of equity and 1% terminal growth rate.

Key Risks

Price war. Competitors irrationally undercutting HKBN's prices for a prolonged period.

Protracted COVID-19 impact will increase uncertainties in the economic environment and limit information technology (IT) spending by enterprises.

At A Glance

Issued Capital (m shrs)	1,312
Mkt Cap (HKm/US\$m)	4,408 / 564
Major Shareholders (%)	
CPP Investment Board	13.9
MBK Partners K.K.	11.1
TPG Capital, L.P.	11.1
GIC Private Limited	8.0
Free Float (%)	56.0
3m Avg. Daily Val. (US\$m)	1.75
GICS Industry: Communication Services / Telecommunication Services	

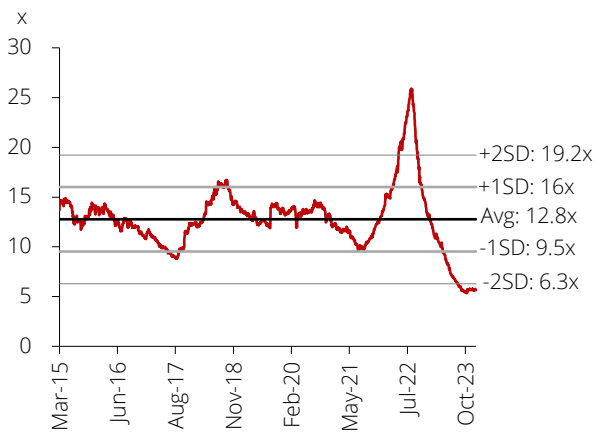
HKBN Ltd.

Company Background

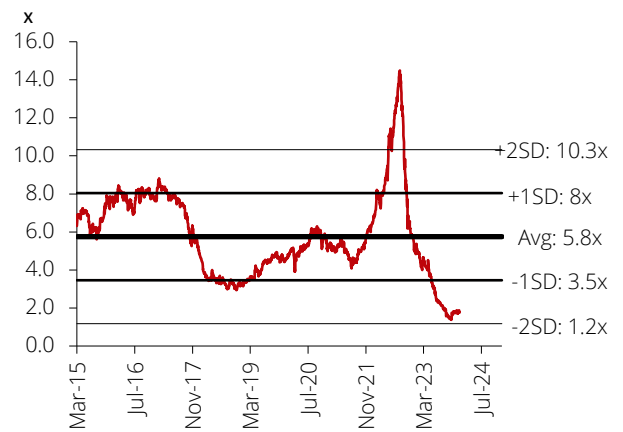
HKBN is a broadband service provider in Hong Kong which was previously under City Telecom (now renamed HKT [1137 HK]) founded by Ricky Wong in 1992. In 2012, HKBN was sold to CVC Capital Partner in a management buyout and was listed in 2014. It has become the second largest player in the residential as well as enterprise broadband markets, with market shares of c.34% and c.37%, respectively. The company has a dividend policy of paying at least 75% of adjusted free cash flow (AFF).

Historical EV/EBITDA and PB band

Forward EBITDA band (x)



PB band (x)



Source: Thomson Reuters, DBS HK

HKBN Ltd.
Key Assumptions

FY Aug	2022A	2023A	2024F	2025F	2026F
Residential broadband sub (k)	897.0	920.0	930.0	940.0	945.0
Residential broadband ARPU (HK\$)	184.0	179.0	181.0	182.0	183.0
Mobile sub base (k)	241.0	239.0	235.0	235.0	235.0
Mobile ARPU (HK\$)	110.0	110.0	110.0	111.0	111.0

Source: Company, DBS HK

Segmental Breakdown (HK\$ m)

FY Aug	2022A	2023A	2024F	2025F	2026F
Revenues (HK\$ m)					
Residential revenue	2,433	2,393	2,425	2,442	2,455
Enterprise revenue	4,427	4,825	5,483	6,176	6,952
Product revenue	4,766	4,474	4,281	4,107	3,950
Total	11,626	11,692	12,190	12,724	13,357

Source: Company, DBS HK

HKBN Ltd.
Income Statement (HK\$ m)

FY Aug	2022A	2023A	2024F	2025F	2026F
Revenue	11,626	11,692	12,190	12,724	13,357
Cost of Goods Sold	(7,156)	(7,525)	(7,738)	(8,010)	(8,399)
Gross Profit	4,470	4,167	4,452	4,715	4,957
Other Opng (Exp)/Inc	(3,532)	(3,445)	(3,619)	(3,769)	(3,953)
Operating Profit	938	723	833	946	1,004
Other Non Opg (Exp)/Inc	60	10	6	10	10
Associates & JV Inc	(49)	(70)	(71)	(71)	(71)
Net Interest (Exp)/Inc	(236)	(693)	(704)	(706)	(705)
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	0	(1,200)	0	0	0
Pre-tax Profit	712	(1,231)	64	179	238
Tax	(159)	(36)	52	59	63
Minority Interest	0	0	0	0	0
Preference Dividend	0	0	0	0	0
Net Profit	553	(1,267)	116	238	301
Net Profit before Except.	553	(67)	116	238	301
EBITDA	2,571	2,281	2,475	2,560	2,606
Growth					
Revenue Gth (%)	1.4	0.6	4.3	4.4	5.0
EBITDA Gth (%)	1.7	(11.3)	8.5	3.5	1.8
Opg Profit Gth (%)	15.1	(23.0)	15.3	13.6	6.1
Net Profit Gth (%)	167.5	N/A	N/A	105.7	26.4
Margins & Ratio					
Gross Margins (%)	38.5	35.6	36.5	37.1	37.1
Opg Profit Margin (%)	8.1	6.2	6.8	7.4	7.5
Net Profit Margin (%)	4.8	(10.8)	1.0	1.9	2.3
ROAE (%)	10.6	(31.8)	4.1	9.7	14.0
ROA (%)	2.6	(6.6)	0.6	1.4	1.7
ROCE (%)	4.1	4.4	5.5	6.5	7.0
Div Payout Ratio (%)	142.2	N/A	468.3	249.5	209.9
Net Interest Cover (x)	4.0	1.0	1.2	1.3	1.4

Source: Company, DBS HK

Interim Income Statement (HK\$ m)

FY Aug	2H2021	1H2022	2H2022	1H2023	2H2023
Revenue	5,234	6,803	4,823	6,707	4,985
Cost of Goods Sold	(3,025)	(4,500)	(2,656)	(4,573)	(2,952)
Gross Profit	2,210	2,303	2,167	2,134	2,033
Other Oper. (Exp)/Inc	(1,789)	(1,804)	(1,668)	(1,741)	(1,693)
Operating Profit	421	499	499	393	340
Other Non Opg (Exp)/Inc	0	0	0	0	0
Associates & JV Inc	(31)	(10)	(40)	(62)	(8)
Net Interest (Exp)/Inc	(155)	(105)	(131)	(320)	(374)
Exceptional Gain/(Loss)	0	0	0	0	(1,200)
Pre-tax Profit	235	385	328	11	(1,242)
Tax	(76)	(80)	(79)	12	(48)
Minority Interest	0	0	0	0	0
Net Profit	158	304	249	23	(1,291)
Net profit bef Except.	158	304	249	23	(91)
Growth					
Revenue Gth (%)	4.8	9.2	(7.9)	(1.4)	3.4
Opg Profit Gth (%)	68.4	20.3	18.6	(21.3)	(31.9)
Net Profit Gth (%)	N/A	526.7	57.3	(92.4)	N/A
Margins					
Gross Margins (%)	42.2	33.9	44.9	31.8	40.8
Opg Profit Margins (%)	8.0	7.3	10.3	5.9	6.8
Net Profit Margins (%)	3.0	4.5	5.2	0.3	(25.9)

Source: Company, DBS HK

HKBN Ltd.**Balance Sheet (HK\$ m)**

FY Aug	2022A	2023A	2024F	2025F	2026F
Net Fixed Assets	3,731	3,419	3,390	3,187	2,989
Invt in Associates & JVs	74	11	11	11	11
Other LT Assets	13,578	11,885	11,390	10,973	10,563
Cash & ST Invt	1,129	1,017	1,160	1,453	1,757
Inventory	111	106	108	110	112
Debtors	967	909	928	946	965
Other Current Assets	835	801	803	819	835
Total Assets	20,427	18,148	17,789	17,498	17,231
ST Debt	298	285	285	285	285
Creditors	779	928	974	1,023	1,074
Other Current Liab	2,054	1,900	1,972	2,017	2,065
LT Debt	10,913	10,672	10,672	10,672	10,672
Other LT Liabilities	1,459	1,313	1,253	1,198	1,145
Shareholder's Equity	4,924	3,051	2,633	2,303	1,990
Minority Interests	0	0	0	0	0
Total Cap. & Liab.	20,427	18,148	17,789	17,498	17,231
Non-Cash Wkg. Capital	(919)	(1,011)	(1,108)	(1,166)	(1,227)
Net Cash/(Debt)	(10,082)	(9,940)	(9,797)	(9,503)	(9,200)
Debtors Turn (avg days)	32.0	29.3	27.5	26.9	26.1
Creditors Turn (avg days)	56.7	52.2	56.9	57.0	56.3
Inventory Turn (avg days)	7.3	6.6	6.4	6.2	6.0
Asset Turnover (x)	0.6	0.6	0.7	0.7	0.8
Current Ratio (x)	1.0	0.9	0.9	1.0	1.1
Quick Ratio (x)	0.7	0.6	0.6	0.7	0.8
Net Debt/Equity (X)	2.0	3.3	3.7	4.1	4.6
Net Debt/Equity ex MI (X)	2.0	3.3	3.7	4.1	4.6
Capex to Debt (%)	4.6	5.2	5.2	5.2	5.2
Z-Score (X)	NA	NA	NA	NA	NA

Source: Company, DBS HK

Cash Flow Statement (HK\$ m)

FY Aug	2022A	2023A	2024F	2025F	2026F
Pre-Tax Profit	712	(1,231)	64	179	238
Dep. & Amort.	1,696	1,461	1,444	1,417	1,404
Tax Paid	(166)	(239)	(8)	5	9
Assoc. & JV Inc/(loss)	(4)	0	0	0	0
(Pft)/ Loss on disposal of FAs	(47)	0	0	0	0
Chg in Wkg.Cap.	(628)	(125)	(144)	(169)	(165)
Other Operating CF	299	1,895	704	706	705
Net Operating CF	1,862	1,761	2,061	2,139	2,192
Capital Exp.(net)	(516)	(570)	(570)	(570)	(570)
Other Invt.(net)	0	0	0	0	0
Invt in Assoc. & JV	(60)	0	0	0	0
Div from Assoc & JV	0	0	0	0	0
Other Investing CF	267	36	8	6	7
Net Investing CF	(309)	(534)	(562)	(564)	(563)
Div Paid	(1,146)	(525)	(534)	(569)	(614)
Chg in Gross Debt	(455)	(254)	0	0	0
Capital Issues	0	0	0	0	0
Other Financing CF	(343)	(561)	(822)	(712)	(712)
Net Financing CF	(1,944)	(1,340)	(1,355)	(1,281)	(1,326)
Currency Adjustments	(6)	0	0	0	0
Chg in Cash	(397)	(112)	143	293	303
Opg CFPS (HK\$)	1.90	1.44	1.68	1.76	1.80
Free CFPS (HK\$)	1.03	0.91	1.14	1.20	1.24

Source: Company, DBS HK

HKBN Ltd.

Target Price & Ratings 12-mth History



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	27-Apr-23	HK\$5.99	HK\$9.50	Buy
2:	3-Nov-23	HK\$2.92	HK\$5.50	Buy

Source: DBS HK

Analyst: Tsz Wang Tam

Andy Yu

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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DBS Bank (Hong Kong) Limited

13th Floor One Island East, 18 Westlands Road, Quarry Bay, Hong Kong

Tel: (852) 3668-4181, Fax: (852) 2521-1812

HKBN Ltd.

DBS Regional Research Offices

HONG KONG

DBS Bank (Hong Kong) Ltd

Contact: Dennis Lam

13th Floor One Island East,
18 Westlands Road, Quarry Bay, Hong Kong

Tel: 852 3668 4181

Fax: 852 2521 1812

e-mail: dbsvhk@dbs.com

SINGAPORE

DBS Bank Ltd

Contact: Andy Sim

12 Marina Boulevard,
Marina Bay Financial Centre Tower 3
Singapore 018982

Tel: 65 6878 8888

e-mail: groupresearch@dbs.com

Company Regn. No. 196800306E

INDONESIA

PT DBS Vickers Sekuritas (Indonesia)

Contact: Maynard Priajaya Arif

DBS Bank Tower
Ciputra World 1, 32/F
Jl. Prof. Dr. Satrio Kav. 3-5
Jakarta 12940, Indonesia

Tel: 62 21 3003 4900

Fax: 6221 3003 4943

e-mail: indonesiaresearch@dbs.com

THAILAND

DBS Vickers Securities (Thailand) Co Ltd

Contact: Chanpen Sirithanarattanakul

989 Siam Pivat Tower Building,
9th, 14th-15th Floor

Rama 1 Road, Pathumwan,

Bangkok Thailand 10330

Tel. 66 2 857 7831

Fax: 66 2 658 1269

e-mail: research@th.dbs.com

Company Regn. No 0105539127012

Securities and Exchange Commission, Thailand