

# China / Hong Kong Company Update

## SmarTone

Bloomberg: 315 HK EQUITY | Reuters: 0315.HK

Refer to important disclosures at the end of this report

DBS Group Research . Equity

16 Jan 2024

**HOLD** (Downgrade from BUY)

Last Traded Price (15 Jan 2024): HK\$4.13 (HSI : 16,216)

Price Target 12-mth: HK\$4.20 (2% upside) (Prev HK\$7.1)

### Analyst

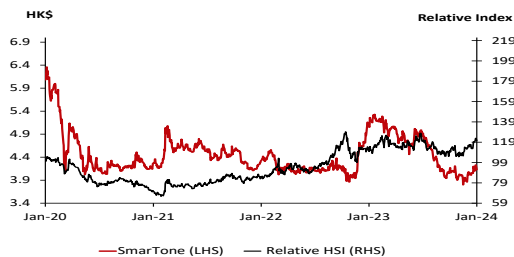
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### What's New

- Mobile roaming recovery on track; expect roaming revenue to hit 85% of pre-COVID level in FY6/24, from 58% in FY6/23
- Lowered earnings forecasts by 9%/11%/12 for FY6/24-FY6/26, to reflect lower ARPU assumptions due to intensifying competition
- Expect earnings to increase by 74%, 9.8%, and 9.6% in FY6/24, FY6/25, and FY6/26, respectively
- Downgrade to HOLD as roaming recovery has largely been priced in; TP of HK\$4.2

### Price Relative



### Forecasts and Valuation

FY Jun (HK\$m)	2023A	2024F	2025F	2026F
Turnover	6,763	6,898	7,012	7,040
EBITDA	2,462	2,546	2,607	2,622
Pre-tax Profit	453	658	722	791
Net Profit	269	467	513	562
Net Profit Gth (Pre-ex) (%)	(36.5)	73.7	9.8	9.5
EPS (HK\$)	0.24	0.42	0.46	0.51
EPS Gth (%)	(36.3)	73.7	9.8	9.5
Diluted EPS (HK\$)	0.24	0.42	0.46	0.51
DPS (HK\$)	0.32	0.33	0.36	0.40
BV Per Share (HK\$)	4.60	4.69	4.81	4.94
PE (X)	17.0	9.8	8.9	8.1
P/Cash Flow (X)	2.0	1.9	1.9	1.8
P/Free CF (X)	2.6	2.5	2.4	2.3
EV/EBITDA (X)	1.4	1.2	1.0	0.8
Net Div Yield (%)	7.7	8.0	8.8	9.6
P/Book Value (X)	0.9	0.9	0.9	0.8
Net Debt/Equity (X)	CASH	CASH	CASH	CASH
ROAE(%)	5.3	9.1	9.7	10.4
Earnings Rev (%)		(9)	(11)	(12)
Consensus EPS (HK\$)		0.43	0.49	0.51
Other Broker Recs:		B:2	S:0	H:2

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

## Roaming recovery on track

### Investment Thesis

**Second largest mobile player in Hong Kong.** SmarTone is a mobile operator in Hong Kong focusing on the high-end customer segment. It has c.19% share in terms of post-paid mobile subscribers, the second in the market after HKT. The company also offers 5G home broadband and enterprise solutions, which are new growth areas.

**Roaming recovery is the key growth driver.** Roaming revenue accounted for only c.5% during the pandemic vs c.16% before COVID-19. Roaming revenue is ramping up with increasing number of in-bound and out-bound travelers. We expect roaming revenue will recover to c.85% of pre-COVID level in FY6/24.

**Mobile ARPU uptrend mainly driven by roaming recovery.** We expect flattish local mobile service revenue growth in FY24 due to the intensifying competitive environment. However, we expect robust roaming recovery will support the growth of ARPU and future earnings for the company.

**Downgrade to HOLD with TP of HK\$4.2 (previously HK\$7.1),** as (1) we believe the positive impact from roaming recovery has been largely priced in, and (2) we expect competition to intensify ahead, and the stock lacks a catalyst for further rerating. We have cut our earnings forecasts by 9%, 11%, and 12% for FY6/24, FY6/25 and FY6/26, respectively, to reflect lower ARPU assumptions due to the intensifying competition environment and higher cost of inventories and services assumptions. We forecast earnings to grow by 73.7%, 9.8%, and 9.6% in FY6/24, FY6/25 and FY6/26, respectively. We revised our TP to HK\$4.2 (lowered from HK\$7.1), based on 10x FY26/24 PE (from 15x), 1SD below its historical average.

### Key Risks

**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 earnings, as mobile roaming business enjoys a higher margin.

### At A Glance

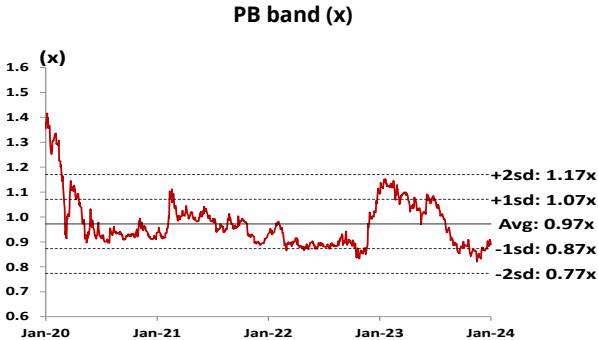
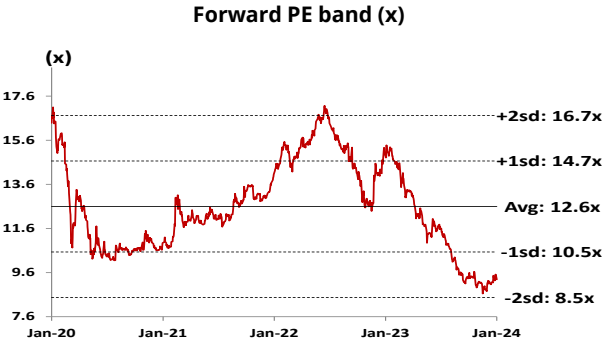
Issued Capital (m shrs)	1,106
Mkt Cap (HKm/US\$m)	4,568 / 584
Major Shareholders (%)	
Cellular 8 Holdings Ltd.	69.2
Free Float (%)	30.8
3m Avg. Daily Val. (US\$m)	0.20
GICS Industry: Communication Services / Telecommunication Services	

### SmarTone

#### Company Background

SmarTone (SMT) is a mobile operator in Hong Kong focusing on the high-end customer segment. It has a c.16% mobile submarket share. Its major shareholder is Sun Hung Kai Properties.

#### Historical PE and PB band



Source: Thomson Reuters, DBS HK

## SmarTone

## Key Assumptions

FY Jun	2022A	2023A	2024F	2025F	2026F
Mobile Sub number (k)	2,748.0	2,737.0	2,729.0	2,729.0	2,734.0
Mobile ARPU (HK\$)	136.0	138.0	143.0	146.0	147.0

Source: Company, DBS HK

## Segmental Breakdown (HK\$ m)

FY Jun	2022A	2023A	2024F	2025F	2026F
<b>Revenues (HK\$ m)</b>					
Mobile service	4,489	4,546	4,682	4,796	4,824
Handset and accessory sales	2,469	2,217	2,217	2,217	2,217
<b>Total</b>	<b>6,957</b>	<b>6,763</b>	<b>6,898</b>	<b>7,012</b>	<b>7,040</b>

Source: Company, DBS HK

## Income Statement (HK\$ m)

FY Jun	2022A	2023A	2024F	2025F	2026F
Revenue	6,957	6,763	6,898	7,012	7,040
Cost of Goods Sold	(2,402)	(2,199)	(2,195)	(2,195)	(2,195)
<b>Gross Profit</b>	<b>4,555</b>	<b>4,564</b>	<b>4,704</b>	<b>4,818</b>	<b>4,846</b>
Other Opng (Exp)/Inc	(3,811)	(3,861)	(3,981)	(4,031)	(3,991)
<b>Operating Profit</b>	<b>744</b>	<b>702</b>	<b>723</b>	<b>787</b>	<b>855</b>
Other Non Opg (Exp)/Inc	0	0	0	0	0
Associates & JV Inc	0	0	0	0	0
Net Interest (Exp)/Inc	(144)	(249)	(65)	(65)	(64)
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	0	0	0	0	0
<b>Pre-tax Profit</b>	<b>600</b>	<b>453</b>	<b>658</b>	<b>722</b>	<b>791</b>
Tax	(177)	(185)	(191)	(209)	(229)
Minority Interest	0	0	0	0	0
Preference Dividend	0	0	0	0	0
<b>Net Profit</b>	<b>423</b>	<b>269</b>	<b>467</b>	<b>513</b>	<b>562</b>
Net Profit before Except.	423	269	467	513	562
EBITDA	2,575	2,462	2,546	2,607	2,622
<b>Growth</b>					
Revenue Gth (%)	3.5	(2.8)	2.0	1.7	0.4
EBITDA Gth (%)	4.7	(4.4)	3.4	2.4	0.6
Opg Profit Gth (%)	10.3	(5.5)	2.9	8.8	8.7
Net Profit Gth (%)	(4.8)	(36.5)	73.7	9.8	9.5
<b>Margins &amp; Ratio</b>					
Gross Margins (%)	65.5	67.5	68.2	68.7	68.8
Opg Profit Margin (%)	10.7	10.4	10.5	11.2	12.1
Net Profit Margin (%)	6.1	4.0	6.8	7.3	8.0
ROAE (%)	8.2	5.3	9.1	9.7	10.4
ROA (%)	3.6	2.3	4.3	4.8	5.2
ROCE (%)	5.8	4.6	6.4	7.1	7.8
Div Payout Ratio (%)	78.5	131.7	78.5	78.5	78.5
Net Interest Cover (x)	5.2	2.8	11.1	12.1	13.3

Source: Company, DBS HK

## SmarTone

## Interim Income Statement (HK\$ m)

FY Jun	2H2021	1H2022	2H2022	1H2023	2H2023
Revenue	3,476	3,792	3,166	3,809	2,954
Cost of Goods Sold	(1,277)	(1,492)	(910)	(1,458)	(741)
<b>Gross Profit</b>	<b>2,199</b>	<b>2,299</b>	<b>2,256</b>	<b>2,351</b>	<b>2,212</b>
Other Oper. (Exp)/Inc	(1,905)	(1,908)	(1,903)	(1,960)	(1,901)
<b>Operating Profit</b>	<b>294</b>	<b>391</b>	<b>353</b>	<b>391</b>	<b>311</b>
Other Non Opg (Exp)/Inc	0	0	0	0	0
Associates & JV Inc	0	0	0	0	0
Net Interest (Exp)/Inc	(41)	(55)	(88)	(35)	(214)
Exceptional Gain/(Loss)	0	0	0	0	0
<b>Pre-tax Profit</b>	<b>254</b>	<b>336</b>	<b>264</b>	<b>356</b>	<b>97</b>
Tax	(76)	(83)	(93)	(100)	(84)
Minority Interest	0	(1)	1	0	0
<b>Net Profit</b>	<b>178</b>	<b>251</b>	<b>172</b>	<b>256</b>	<b>13</b>
Net profit bef Except.	178	251	172	256	13

## Growth

Revenue Gth (%)	27.3	16.9	(8.9)	0.5	(6.7)
Opg Profit Gth (%)	82.7	2.9	19.9	0.1	(11.8)
Net Profit Gth (%)	56.8	(5.7)	(3.5)	1.8	(92.4)

## Margins

Gross Margins (%)	63.3	60.6	71.3	61.7	74.9
Opg Profit Margins (%)	8.5	10.3	11.1	10.3	10.5
Net Profit Margins (%)	5.1	6.6	5.4	6.7	0.4

Source: Company, DBS HK

## Balance Sheet (HK\$ m)

FY Jun	2022A	2023A	2024F	2025F	2026F
Net Fixed Assets	3,654	3,690	3,545	3,543	3,596
Invts in Associates & JVs	0	0	0	0	0
Other LT Assets	5,526	4,806	4,316	3,847	3,378
Cash & ST Invts	2,195	1,177	1,638	2,072	2,508
Inventory	100	106	106	106	106
Debtors	344	351	359	367	375
Other Current Assets	762	768	768	768	768
<b>Total Assets</b>	<b>12,581</b>	<b>10,899</b>	<b>10,732</b>	<b>10,703</b>	<b>10,731</b>
ST Debt	1,445	2	2	2	2
Creditors	239	317	420	557	738
Other Current Liab	2,407	2,385	2,396	2,348	2,304
LT Debt	66	64	64	64	64
Other LT Liabilities	3,270	3,046	2,657	2,410	2,158
Shareholder's Equity	5,154	5,084	5,193	5,323	5,465
Minority Interests	0	0	0	0	0
<b>Total Cap. &amp; Liab.</b>	<b>12,581</b>	<b>10,899</b>	<b>10,732</b>	<b>10,703</b>	<b>10,731</b>
Non-Cash Wkg. Capital	(1,441)	(1,476)	(1,583)	(1,663)	(1,793)
Net Cash/(Debt)	684	1,111	1,572	2,006	2,442
Debtors Turn (avg days)	17.7	18.8	18.8	18.9	19.2
Creditors Turn (avg days)	209.0	231.1	361.9	476.7	553.0
Inventory Turn (avg days)	50.4	85.7	104.3	103.7	90.8
Asset Turnover (x)	0.6	0.6	0.6	0.7	0.7
Current Ratio (x)	0.8	0.9	1.0	1.1	1.2
Quick Ratio (x)	0.6	0.6	0.7	0.8	0.9
Net Debt/Equity (X)	CASH	CASH	CASH	CASH	CASH
Net Debt/Equity ex MI (X)	CASH	CASH	CASH	CASH	CASH
Capex to Debt (%)	47.1	863.6	833.3	833.3	833.3
Z-Score (X)	1.8	1.9	NA	NA	NA

Source: Company, DBS HK

## SmarTone

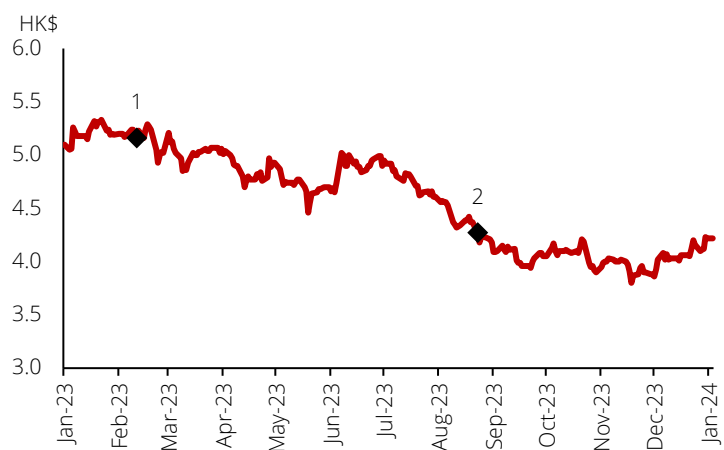
## Cash Flow Statement (HK\$ m)

FY Jun	2022A	2023A	2024F	2025F	2026F
Pre-Tax Profit	600	453	658	722	791
Dep. & Amort.	1,820	1,922	1,823	1,820	1,767
Tax Paid	(109)	(185)	(191)	(209)	(229)
Assoc. & JV Inc/(loss)	0	0	0	0	0
(Pft)/ Loss on disposal of FAs	11	6	0	0	0
Chg in Wkg.Cap.	(265)	74	39	77	126
Other Operating CF	(21)	57	45	44	44
<b>Net Operating CF</b>	<b>2,036</b>	<b>2,329</b>	<b>2,374</b>	<b>2,455</b>	<b>2,499</b>
Capital Exp.(net)	(712)	(570)	(550)	(550)	(550)
Other Invt.(net)	(1,693)	1,986	0	0	0
Invt in Assoc. & JV	0	0	0	0	0
Div from Assoc & JV	0	0	0	0	0
Other Investing CF	(217)	(509)	(302)	(385)	(390)
<b>Net Investing CF</b>	<b>(2,622)</b>	<b>907</b>	<b>(852)</b>	<b>(935)</b>	<b>(940)</b>
Div Paid	(342)	(332)	(359)	(383)	(419)
Chg in Gross Debt	(96)	(1,445)	0	0	0
Capital Issues	0	0	0	N/A	0
Other Financing CF	(686)	(689)	(703)	N/A	(703)
<b>Net Financing CF</b>	<b>(1,124)</b>	<b>(2,466)</b>	<b>(1,061)</b>	<b>(1,085)</b>	<b>(1,122)</b>
Currency Adjustments	0	0	0	0	0
Chg in Cash	(1,709)	770	461	434	436
Opg CFPS (HK\$)	2.08	2.04	2.11	2.15	2.15
Free CFPS (HK\$)	1.19	1.59	1.65	1.72	1.76

Source: Company, DBS HK

**SmarTone**

**Target Price & Ratings 12-mth History**



S.No.	Date	Closing Price	Target Price	Rating
1	23-Feb-23	HK\$5.19	HK\$8.10	BUY
2	4-Sep-23	HK\$4.37	HK\$7.10	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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