

## COMPANY NOTE

Company Update

China | Telecommunications | Telecom Services

29 May 2015

# Jefferies

## China Unicom Ltd. (762 HK) China TMT Tour: Key Takeaways from Meeting with China Unicom Chairman

### Key Takeaway

**During Jefferies 13th China TMT tour, we hosted a meeting with China Unicom Chairman, Mr. Chang. Key takeaways: (1) Tower negotiation is close to finalization, timetable remains unchanged. (2) Accelerating deployment of 3G/4G network and targets nationwide coverage by YE2015. (3) CU is seeking to cooperate with Internet companies to promote data usage. Hold.**

### Tower negotiation is close to finalization, timetable remains unchanged.

According to Unicom's management, discussion of tower asset injection is at the final stage and transactions will be completed before the end of August. As one of the two operators with fewer tower sites, CU will benefit from tower sharing and quickly expand its 3G/4G network coverage. Management said a superior fixed-line network will complement bandwidth and wireless coverage.

**Accelerating deployment of 3G/4G network.** CU's current Capex budget has factored in the broadband and 4G network construction, in line with SASAC's recently published guidance on operators' network Capex. We maintain our previous estimate of Capex at RMB100bn, +17.8% YoY. CU will accelerate the deployment of 3G network in rural areas and 4G network in key cities. By YE2015, CU targets to complete its nationwide 3G/4G coverage. While FY15/16 are both Capex peak years for CU, Capex in FY16 is expected to be lower than in FY15.

**CU is seeking to cooperate with Internet companies to promote data usage.** As discussed in our takeaways from meetings with CM and CT in the past few days, all three carriers expect mobile data usage to increase as mobile data tariff declines, as subs habits change and increase usage of mobile apps. As a low-cost handset is no longer an advantage for CU as in the 3G era, CU is exploring new ways to differentiate itself. CU is seeking to cooperate with Internet companies to promote their data usage, such as data packages tailored for watching video content on LeTV.

### Valuation/Risks

Maintain Hold and DCF-based price target of HK\$15, implying FY15E/16E 4x/3.8x EV/EBITDA and 20.9x/19.6x P/E, respectively. CU is trading at FY15E 3.7x EV/EBITDA and 18.2x P/E, a 44% discount to emerging Asia peer group avg FY15E EV/EBITDA. Risks include competition in 4G LTE, and the threat from OTT players from Internet industry.

RMB	Prev.	2014A	Prev.	2015E	Prev.	2016E	Prev.	2017E
Rev. (MM)	--	284,681.0	--	288,997.0	--	296,377.0	--	307,394.0
EBITDA (MM)	--	92,771.0	--	100,589.0	--	105,485.0	--	109,162.0
EV/EBITDA		3.9x		3.6x		3.5x		3.4x
Net Profit	--	12,055.0	--	13,692.0	--	14,580.0	--	15,348.0
Chg (% YoY)	--	14.9%	--	13.6%	--	6.5%	--	5.3%
Div. Yield		1.86%		2.08%		2.23%		2.38%
<b>EPS</b>								
FY Dec	--	HK\$0.63	--	HK\$0.72	--	HK\$0.76	--	HK\$0.80
FY P/E		21.4x		18.7x		17.7x		16.8x

**HOLD**

Bloomberg HKSE: 762 HK  
Reuters: 0762 HK  
Price target HK\$15.00  
Price HK\$13.46

**HOLD**

Bloomberg NYSE: CHU  
ADR Price target \$19.40  
ADR Price \$17.38

### Financial Summary

Book Value (MM):	HK\$284,426.0
Book Value/Share:	HK\$11.92
Net Debt (MM):	HK\$139,013.0
Return on Avg. Equity:	5.4%
Long-Term Debt (MM):	HK\$29,850.0
Cash & ST Invest. (MM):	HK\$31,635.0

### Market Data

52 Week Range 762 HK:	HK\$16.00 - HK\$10.04
52 Week Range CHU:	\$19.88 - \$12.93
Total Entprs. Value (MM) 762 HK:	HK\$458,068.8
Total Entprs. Value (MM) CHU:	\$59,382.9
Market Cap. (MM) 762 HK:	HK\$319,055.8
Market Cap. (MM) CHU:	\$41,453.0
Shares Out. (MM) 762 HK:	23,704.0
Shares Out. (MM) CHU:	2,385.1

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## Jefferies China TMT Tour Takeaways

During Jefferies 13th China TMT tour, we hosted a meeting with China Unicom Chairman, Mr. Chang. Key takeaways are as follows:

### **Tower negotiation is close to finalization, timetable remains unchanged.**

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As discussed in our takeaways from meeting with CM and CT in the past few days, all three carriers expect mobile data usage to increase as mobile data tariff declines and as subs habits changes and increase usage of mobile apps.

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## Chart 1: Financial Summary

Profit and Loss statement						Cash flow statement					
Rmb mn	2013A	2014A	2015E	2016E	2017E	Rmb mn	2013A	2014A	2015E	2016E	2017E
Revenues	295,038	284,681	288,997	296,377	307,394	PBT ex. Exceptionals	13,714	15,931	18,094	19,268	20,283
Operating expenses	(211,075)	(191,910)	(188,408)	(190,892)	(198,232)	Depn and amortization	68,196	73,868	79,356	82,837	85,869
EBITDA	83,963	92,771	100,589	105,485	109,162	Change in working cap.	(2,052)	(3,657)	4,539	4,923	8,167
Depreciation/Amortization	(68,196)	(73,868)	(79,356)	(82,837)	(85,869)	Others	(1,376)	1,952	(4,402)	(4,688)	(4,935)
Operating profit	15,767	18,903	21,232	22,648	23,293	CF from operations	78,482	88,094	97,587	102,340	109,384
Other income	887	1,362	1,362	1,362	1,362	Capex	(72,758)	(69,586)	(100,000)	(90,545)	(69,869)
Non-operating income	0	0	0	0	0	Others	(4,352)	(5,733)	0	0	0
EBIT	15,767	18,903	21,232	22,648	23,293	CF from investing	(77,110)	(75,319)	(100,000)	(90,545)	(69,869)
Interest income	173	283	344	453	831	Free cash flow	4,651	(366)	(39)	14,353	41,792
Finance cost	(3,113)	(4,617)	(4,844)	(5,194)	(5,203)	Equity raised/ (repaid)	0	0	0	0	0
Profit before tax	13,714	15,931	18,094	19,268	20,283	Dividends paid	(2,686)	(3,677)	(5,439)	(5,792)	(6,097)
Taxation	(3,306)	(3,876)	(4,402)	(4,688)	(4,935)	Change in bank loan	2,166	(6,167)	11,000	3,000	(2,000)
Minority	0	0	0	0	0	Others	2,446	871	0	0	0
Net income	10,408	12,055	13,692	14,580	15,348	CF from financing	1,926	(8,973)	5,561	(2,792)	(8,097)
Net income (adj.)	10,408	12,055	13,692	14,580	15,348	Total net cash provided / (used)	3,298	3,802	3,147	9,003	31,418
Shares outstanding	23,782	23,947	23,947	23,947	23,947	Beginning net cash / (debt)	18,250	21,506	25,308	28,455	37,459
Weighted average share	23,658	23,852	23,852	23,852	23,852	Ending net cash / (debt)	21,506	25,308	28,455	37,459	68,876
EPS (Rmb)	0.44	0.51	0.57	0.61	0.64						
DPS (HK\$)	0.20	0.25	0.28	0.30	0.32						
Balance sheet						Ratio Analysis (%)					
Rmb mn	2013A	2014A	2015E	2016E	2017E		2013A	2014A	2015E	2016E	2017E
Cash	21,506	25,308	28,455	37,459	68,876	EBITDA margin	28.5%	32.6%	34.8%	35.6%	35.5%
Time deposits	54	56	56	56	56	Operating margin	5.3%	6.6%	7.3%	7.6%	7.6%
Accounts receivable	14,842	14,671	14,893	15,274	15,842	Net profit margin	3.5%	4.2%	4.7%	4.9%	5.0%
Prepayments	9,664	10,029	10,181	10,441	10,829	Revenue growth	18.5%	-3.5%	1.5%	2.6%	3.7%
Other current asset	6,144	6,510	6,576	6,690	6,859	EBITDA growth	15.6%	10.5%	8.4%	4.9%	3.5%
Current asset	52,210	56,574	60,162	69,919	102,462	Net profit growth	46.7%	15.8%	13.6%	6.5%	5.3%
Fixed assets and CIP	431,625	438,321	458,965	466,672	450,672	EPS growth	46.1%	14.9%	13.6%	6.5%	5.3%
Other non-current asset	45,336	50,177	50,177	50,177	50,177	BVPS	9.3	9.5	9.9	10.3	10.6
Non-current asset	476,961	488,498	509,142	516,849	500,849	Interest coverage (x)	3.2	5.1	4.1	4.4	4.4
Total Assets	529,171	545,072	569,304	586,769	603,311	Net debt to total capital	34%	31%	31%	29%	20%
Short-term loan	129,422	112,649	120,649	120,649	118,649	Net debt to equity	55%	49%	50%	46%	31%
Accounts payable	102,212	120,371	124,640	129,101	136,578	Sales/assets	56%	53%	52%	51%	52%
Advances from customers	129,422	112,649	120,649	120,649	118,649	Assets/equity	242%	240%	241%	240%	238%
Current portion of long term debt	48	45	51	56	56	Total liabilities	310,272	317,531	333,511	342,187	349,479
Other current liabilities	(65,865)	(53,794)	(61,083)	(59,867)	(56,053)	Net debt	121,393	111,210	119,063	113,059	79,642
Current liabilities	295,239	291,920	304,905	310,588	317,880	Minority interest	0	0	0	0	0
Long-term bank loan	13,483	23,880	26,874	29,869	29,869	Shareholder's equity	218,899	227,541	235,794	244,581	253,832
Other non-current liabilities	1,550	1,731	1,731	1,731	1,731	Total liability and equity	529,171	545,072	569,304	586,769	603,311
Long-term liabilities	15,033	25,611	28,605	31,600	31,600	ROA	3.0%	3.5%	3.8%	3.9%	3.9%
ROA	3.0%	3.5%	3.8%	3.9%	3.9%	ROE	4.9%	5.4%	5.9%	6.1%	6.2%
ROE	4.9%	5.4%	5.9%	6.1%	6.2%	ROCE	4.6%	5.2%	5.7%	5.8%	5.8%
ROCE	4.6%	5.2%	5.7%	5.8%	5.8%						

Source: Company data, Jefferies

## Company Description

China Unicom is China's 2nd largest mobile and fixed-line carrier, providing GSM and WCDMA mobile services, broadband and fixed-line telephony services.

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The expected total return (price appreciation plus yield) for Buy rated securities with an average security price consistently below \$10 is 20% or more within a 12-month period as these companies are typically more volatile than the overall stock market. For Hold rated securities with an average security price consistently below \$10, the expected total return (price appreciation plus yield) is plus or minus 20% within a 12-month period. For Underperform rated securities with an average security price consistently below \$10, the expected total return (price appreciation plus yield) is minus 20% or less within a 12-month period.

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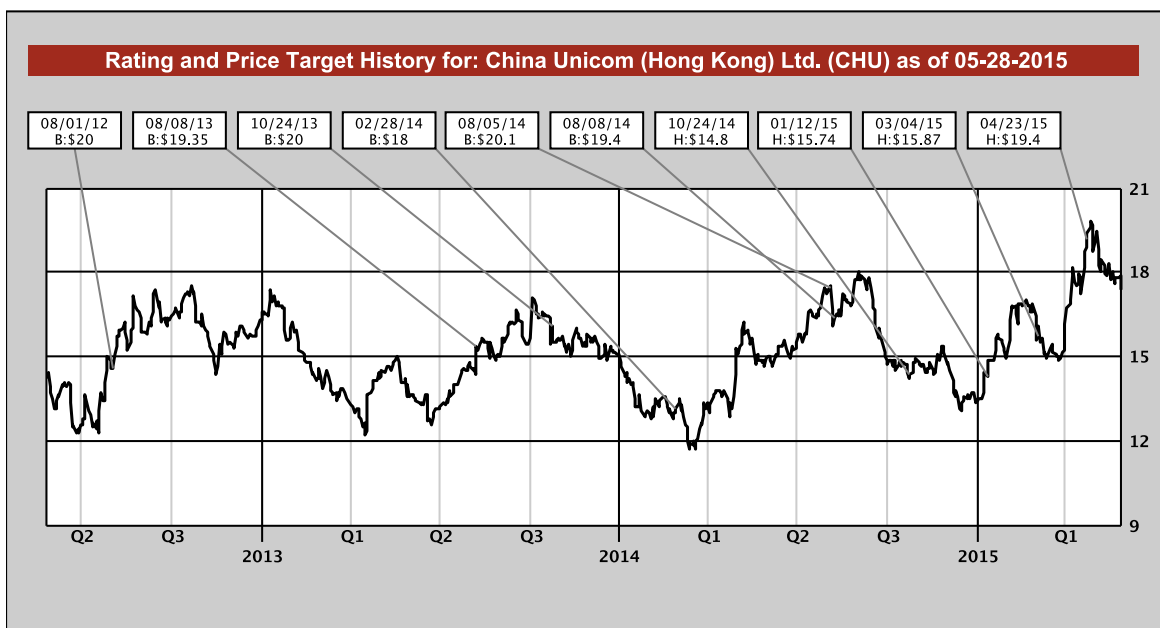
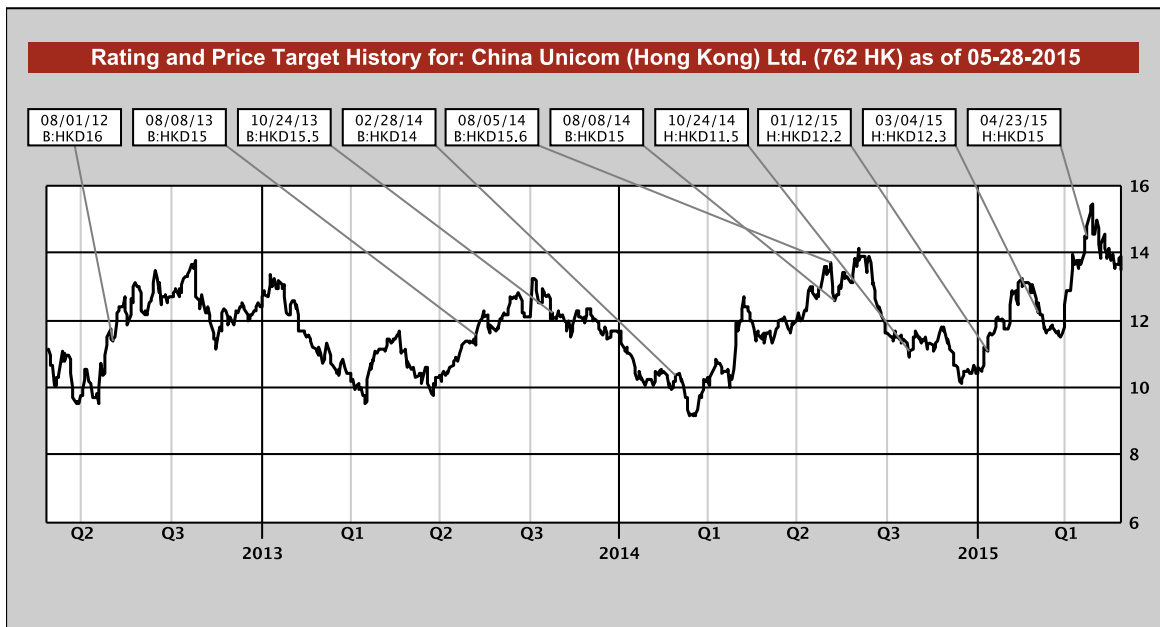
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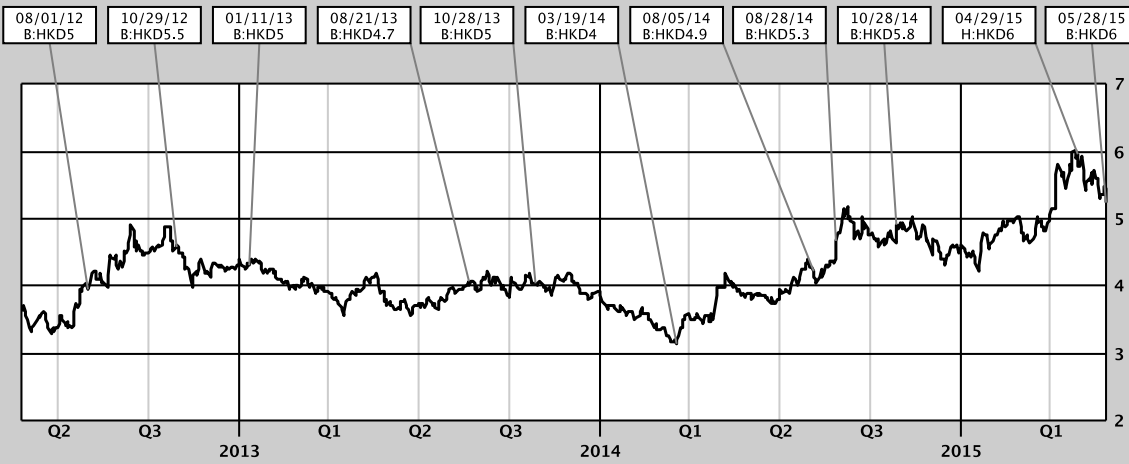
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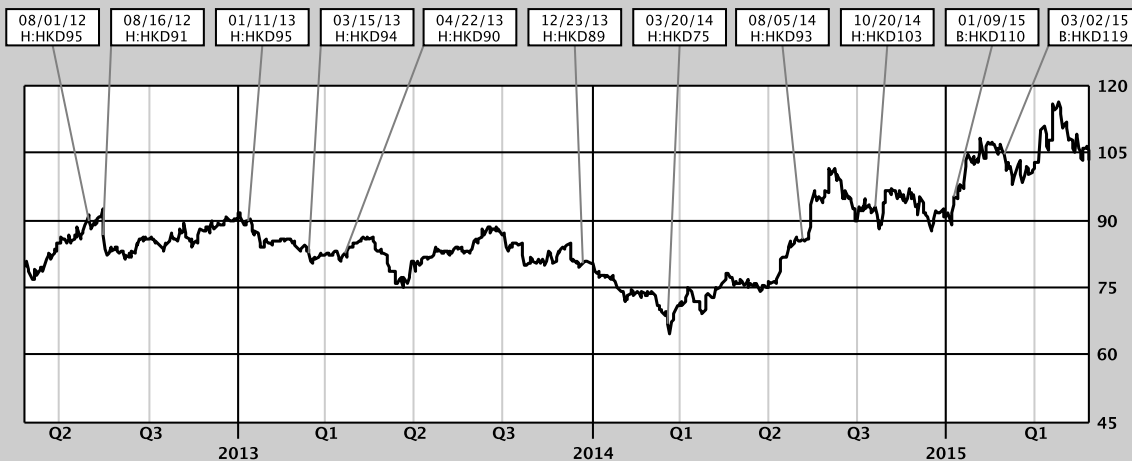
- China Mobile Limited (941 HK: HK\$103.30, BUY)
- China Telecom Corp Ltd. (728 HK: HK\$5.24, BUY)



## Rating and Price Target History for: China Telecom Corp Ltd. (728 HK) as of 05-28-2015



## Rating and Price Target History for: China Mobile Limited (941 HK) as of 05-28-2015



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Rating	Count	Percent	IB Serv./Past 12 Mos.	
			Count	Percent
BUY	1069	51.39%	291	27.22%
HOLD	844	40.58%	162	19.19%
UNDERPERFORM	167	8.03%	13	7.78%



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