

Equity Research | China | Telecommunications

1 March 2018

Attractive yield, growth on acquisitions

- CITIC Tel reported a solid set of FY17 results, though slightly behind our estimates in bottom-line, which indicates healthy momentum in its global reach and business transformation.
- The company raised final DPS to HKD0.13, making a full-year payout ratio of 64%. With net gearing (51.2% by FY20E) on the decline, the company will be able to execute more potential acquisitions, in our view.
- We have trimmed our FY18/19E earnings estimates by 5.4%/6.0% and lowered our DCF-based price target to HKD3.0 (from HKD3.2). Trading at FY18E 9.0x PER, 0.9x PBR and 7.4% yield, the company's current valuation looks very attractive. Maintain Buy.

Positive readings from a solid set of FY17 results. Though a bit behind our estimates in bottom-line, CITIC Tel's FY17 key headlines indicate a healthy momentum in the company's strategy, expanding its global reach in data network coverage through acquisition and seeking new revenue streams through innovation. Service revenue grew 5.6% YoY, driven by mobile data (4G subs penetration at 89%), continued solid growth of VPN in China and the inclusion of Acclivis' full-year results and CPC Europe since acquisition, which more than offset decline in Macau fixed-line and leased line (tariff reduction). Encouragingly, revenue from 'DataMall' surged 326.4% YoY to HKD69.5mn, reversing four consecutive years of decline in hubbing (primarily voice hubbing) revenue.

Sustainable dividend payout, still financial leeway for acquisitions. As of end-2017, the company's net gearing had retreated to 73.7 and will continue to decrease to 51.2% in FY20E in our estimates. On the back of declining debts and finance costs, CITIC Tel was able to maintain a steady increase in dividend payout (64% dividend payout ratio for FY17). Fulfilling its commitment in dividend, the company still has financial leeway for potential acquisitions in our view, in particularly over the coming two years during which we should see a gradual decline in its capex before commercial deployment of 5G in 2020.

Attractive dividend yield, valuation at historical trough. We have kept our FY18/19E service revenue estimates largely unchanged, but have trimmed the respective earnings forecasts by 5.4%/6.0%, reflecting higher network operation costs from its global acquisition. Meanwhile, we have lowered our DCF-based price target to HKD3.0 (from HKD3.20), still implying 30.4% potential upside. The company trades at FY18E 9.0x PER, 0.9x PBR and 7.4% dividend yield, which is appealing given its potential long-term growth through acquisitions. Maintain Buy.

CITIC Telecom (1883 HK)

Buy

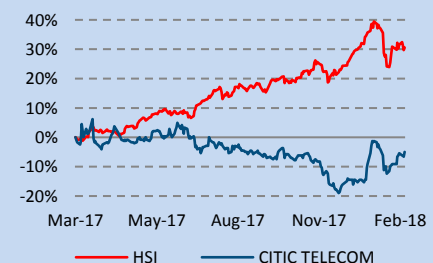
(unchanged)

Price Target	HK\$3.0
(Revision)	(-1.9%)
(upside)	(30.4%)

EPS	2018E	2019E
revision	(-5.4%)	(-6.0%)
Close price	HKD2.30	
Market cap.	USD1,041bn	
Free float	39.5%	
52-week range	HKD1.96 – HKD2.63	
3-mth ave. T/O	HKD10.7mn	

Price as of 1 March 2018

Stock rel HSI performance (%)



LIU Taisheng, Steven, CFA, PhD
(CE No.: AMO971)

stevenliu@csci.hk +852 3465 5652

Figure 1: CITIC Telecom FY17 results summary

FY ended: Dec (HKD mn)	2016	2017	YoY
Macau: mobile service	1,164.8	1,221.1	4.8%
Macau: fixed-line	321.7	280.6	-12.8%
Macau: internet	922.2	933.8	1.3%
Voice hubbing	1,113.2	990.8	-11.0%
SMS hubbing	211.8	280.5	32.4%
VPN	2,176.4	2,185.0	0.4%
Total service revenue	6,005.8	6,340.6	5.6%
Sales of equipment and handsets	1,693.4	1,110.2	-34.4%
Turnover	7,699.1	7,450.8	-3.2%
Other revenue	12.7	46.3	265.7%
Valuation gain on investment property	-	50.6	
Other net gain / (loss)	(22.8)	7.8	-134.1%
Total net revenue	7,689.0	7,555.5	
Network and operations expenses	(4,229.1)	(3,852.8)	-8.9%
Depreciation	(656.4)	(695.6)	6.0%
Staff costs	(851.0)	(961.3)	13.0%
Other operating expenses	(598.5)	(658.9)	10.1%
Total operating expenses	(6,334.9)	(6,168.6)	-2.6%
Operating profit	1,354.1	1,386.9	2.4%
Finance costs	(327.7)	(323.7)	-1.2%
Share of profit of JCE	1.7	(2.0)	
Pre-tax profit	1,028.1	1,061.2	3.2%
Income tax	(165.4)	(165.5)	0.1%
Profit for the year	862.7	895.8	3.8%
Minority	12.6	14.4	14.1%
Net profit	850.1	881.3	3.7%
EBITDA	2,010.5	2,082.6	3.6%
Interim/final dividend per share (HKD cents)	13.20	16.00	21.2%
EPS, basic (HKD)	0.25	0.25	0.1%
EPS, diluted (HKD)	0.25	0.25	0.5%

Source: Company

Income statement (HKDm)

Year end: Dec	2016	2017	2018E	2019E	2020E
Revenue	7,699	7,451	7,654	7,836	8,031
SG&A	(4,229)	(3,853)	(3,892)	(3,964)	(4,037)
Personnel	(851)	(961)	(990)	(1,020)	(1,050)
Other operating expenses	(598)	(659)	(672)	(686)	(699)
Other operating income					
EBITDA	2,021	1,978	2,100	2,167	2,244
Depreciation & Amortization	(656)	(696)	(738)	(745)	(752)
Other income	(10)	105	63	50	42
EBIT	1,354	1,387	1,425	1,472	1,533
Net interest	(328)	(324)	(313)	(300)	(288)
Associates	2	(2)	(1)	(1)	(0)
Exceptional items					
Pretax profit	1,028	1,061	1,111	1,171	1,245
Taxation	(165)	(165)	(189)	(208)	(219)
Minority interests	(3)	(4)	(5)	(5)	(6)
Net profit	850	881	898	948	1,011
Net profit (adjusted)	850	881	898	948	1,011
Basic EPS (HKD)	0.25	0.25	0.26	0.27	0.29
EPS (adjusted) (HKD)	0.25	0.25	0.25	0.26	0.28
DPS (HKD)	0.13	0.16	0.17	0.18	0.19

Balance sheet (HKDm)

Year end: Dec	2016	2017	2018E	2019E	2020E
Cash	1,459	1,636	1,559	1,517	1,518
Short term investments					
Accounts receivables	1,691	1,783	1,890	2,004	2,124
Inventory	70	104	114	126	138
Other current assets	6	4	4	4	4
Total current assets	3,226	3,526	3,567	3,649	3,784
PP&E	2,554	2,626	2,599	2,546	2,488
Intangible Assets	11,475	11,451	11,308	11,164	11,020
Associates and JVs	7	6	6	6	6
Other long term assets	920	975	989	1,004	1,020
Total long term assets	14,957	15,058	14,902	14,720	14,533
TOTAL ASSETS	18,183	18,584	18,469	18,370	18,317
Short term debt	44	284	284	284	284
Accounts payables	1,706	1,739	1,774	1,810	1,846
Other current liabilities	233	213	230	248	268
Total current liabilities	1,983	2,237	2,288	2,342	2,398
Long term debt	7,858	7,541	7,041	6,541	6,041
Deferred tax	249	245	250	255	260
Convertible bonds					
Other long term liabilities	134	132	138	145	152
Total long term liabilities	8,300	7,917	7,429	6,940	6,453
TOTAL LIABILITIES	10,283	10,154	9,717	9,283	8,851
Shareholders' funds	7,871	8,396	8,703	9,023	9,387
Minority interests	29	34	49	64	80
TOTAL LIAB AND EQUITY	18,183	18,584	18,469	18,370	18,317
Net cash / (debt)	(6,442)	(6,190)	(5,766)	(5,308)	(4,807)

Source: Company, Bloomberg, CSCI Research estimates

Cash flow statement (HKDm)

Year end: Dec	2016	2017E	2018E	2019E	2020E
EBIT	1,354	1,387	1,425	1,472	1,533
Depreciation & amortisation	656	696	738	745	752
Net interest	328	324	313	300	288
Taxes paid	(196)	(165)	(199)	(208)	(219)
Changes in working capital	36	(80)	(68)	(74)	(80)
Others	(295)	(615)	(627)	(601)	(576)
Cash flow from operations	1,883	1,446	1,582	1,634	1,699
Capex	(609)	(596)	(567)	(549)	(550)
Acquisitions	(703)	(133)	-	-	-
Disposals	0	-	-	-	-
Others	(25)	-	-	-	-
Cash flow from investing	(1,337)	(728)	(567)	(549)	(550)
Dividends	(425)	(566)	(604)	(642)	(662)
Issue of shares	218	116	12.8	14.1	15.5
Change in debt	3,231	(317)	(500)	(500)	(500)
Others	(3,160)	-	-	-	-
Cash flow from financing	(332)	(872)	(1,091)	(1,128)	(1,147)
Change in cash	214	(154)	(77)	(42)	2
Free cash flow	533	189	1397	1460	1517

Key ratios

Year end: Dec	2016	2017	2018E	2019E	2020E
Operating ratios					
EBIT margin (%)	17.6	18.6	18.6	18.8	19.1
EBITDA margin (%)	26.2	26.5	27.4	27.7	27.9
Effective tax rate (%)	16.1	15.6	17.9	17.8	17.6
Revenue growth (%)	(7.8)	(3.2)	2.7	2.4	2.5
Net income growth (%)	6.0	3.7	1.8	5.6	6.6
EPS growth adj (%)	5.0	0.5	0.7	5.2	6.1
DPS growth (%)	5.6	212	6.3	5.9	2.8
Efficiency ratios					
ROE (%)	10.8	10.5	10.3	10.5	10.8
ROCE (%)	9.1	9.2	9.6	10.0	10.6
Asset turnover (x)	0.4	0.4	0.4	0.4	0.4
Op cash / EBIT (x)	14	10	11	11	11
Depreciation / CAPEX (x)	11	12	13	14	14
Accounts receivable days	80.1	85.1	87.6	90.7	93.8
Accounts payable days	111.6	114.9	115.4	115.4	115.3
Leverage ratios					
Net gearing (%)	819	73.7	66.3	58.8	51.2
Net debt / EBITDA (x)	3.2	3.1	2.7	2.4	2.1
Interest cover (x)	4.1	4.3	4.6	4.9	5.3
Current ratio (x)	16	16	16	16	16
Valuation					
PER (x)	9.1	9.1	9.0	8.5	8.0
EV/EBITDA (x)	7.1	6.9	6.5	6.1	5.7
PBR (x)	10	10	0.9	0.9	0.9
Dividend yield (x)	5.7	7.0	7.4	7.8	8.0



Research

LIU Taisheng, Steven
TMT
(852) 3465 5652
stevenliu@csci.hk

CHAN Ka Yeung, Duncan
Commodity
(852) 3465 5654
duncanchan@csci.hk

TIAN Yang
Automotive
(852) 3465 5775
tianyong@csci.hk

SUN Lingxiao, Roger
Industrials
(852) 3465 5785
rogersun@csci.hk

YAO Xue, Snowy
Power & coal
snowyyao@csci.hk
+852 3465 5675

SHEN Xiangfei, Thomas
(852) 3465 8689
thomasshen@csci.hk

XU Qiwen
(852) 3465 8690
xuqiwen@csci.hk

Institutional Sales & Trading

XIANG Xinrong, Ron
(852) 3465 5633
ronxiang@csci.hk

HO Wen Hao, Jack
(852) 3465 5685
jackho@csci.hk

WANG Zhuo, Gary
(852) 3465 8655
wangzhuo@csci.hk

LEE Ying Ju, Rose
(852) 3465 5707
roselee@csci.hk

LI Jiageng, Mike
(852) 3465 5636
mikeli@csci.hk

XIA Tian
(852) 3465 5670
xiatian@csci.hk

XU Xiaowei, Vincent
(852) 3465 5795
vincentxu@csci.hk

Company Rating Definition

The Benchmark: Hong Kong Hang Seng Index; Time Horizon: 12 months

Buy	12-month absolute total return: $\geq 10\%$
Hold	12-month absolute total return: $> -10\%$ but $< 10\%$
Sell	12-month absolute total return: $\leq -10\%$

Disclosure of Interests

As of the date of this report,

- The research analysts primarily responsible for the preparation of all or part of this report hereby certify that:
 - the views expressed in this research report accurately reflect the personal views of each such analyst about the subject securities and issuers; and
 - no part of the analyst's compensation was, is, or will be directly or indirectly, related to the specific recommendations or views expressed in this research report.
- The research analysts primarily responsible for the preparation of all or part of this report, or his/her associate(s), do not have any interest (including any direct or indirect ownership of securities, arrangement for financial accommodation or serving as an officer) in any company mentioned in this report,
- This report has been produced in its entirety by China Securities (International) Brokerage Company Limited ("China Securities (International)") (CE Number: BAU373, regulated by the Securities and Futures Commission in Hong Kong)
- China Securities (International) and each of its group companies that carry on a business in Hong Kong in investment banking, proprietary trading or agency broking in relation to securities have no financial interest, in aggregate, equal to or more than 1% of the market capitalization in the stocks reviewed in this report.
- China Securities (International) and each of its group companies that carry on a business in Hong Kong in investment banking, proprietary trading or agency broking in relation to securities may receive compensation from or mandates for investment banking services in the past 12 months from listed corporations whose stocks are being reviewed by China Securities (International) in this report.
- China Securities (International) and each of its group companies that carry on a business in Hong Kong in investment banking, proprietary trading or agency broking in relation to securities do not have any individual employed by or associated with them serving as an officer of a listed corporation whose stocks are being reviewed by China Securities (International) in this report.
- China Securities (International) and each of its group companies that carry on a business in Hong Kong in investment banking, proprietary trading or agency broking in relation to securities may act as the market makers in the stocks reviewed by China Securities (International) in this report.

Disclaimer

This report is for information purposes only and should not be construed as an offer to sell or to solicitation of an offer to buy or sell any securities in any jurisdiction. The securities referred to in this research report may not be eligible for sale in some jurisdictions. This information contained in this report has been compiled by China Securities (International) from sources that it believes to be reliable and the opinions, analysis, forecasts, projections and expectations contained in this report are based on such information and are expressions of belief only and no representation, warranty or guarantee is made or given by China Securities (International) or any person for its accuracy or completeness. All opinions and estimates expressed in this report are (unless otherwise indicated) entirely those of China Securities (International) as of the date of this report only and are subject to change without notice. Such opinions and estimates may be different from or contrary to the opinions presented by the other business departments, units or affiliates of China Securities (International), as different assumptions and standards, different views and analytical methods may be adopted in the preparation of such other materials, and China Securities (International) is under no obligation to bring such other materials to the attention of any recipient of this report. Neither China Securities (International) nor its holding companies and affiliates accept any liability whatsoever for any direct or consequential loss arising from any use of material contained in this report or otherwise arising in connection therewith.

Any investment referred to herein may involve significant risk, may be illiquid and may not be suitable for all investors. The value of or income from any investment referred to herein may fluctuate and be affected by changes in exchange rates. Past performance is not indicative of future results. This report does not take into account the investment objectives, financial situation or particular needs of any particular person. Investors are expected to make their own investment decision without relying on this publication. Before entering into any transactions in any securities referred to in this research report investor should consider their own individual investment objectives and financial situation and seek professional financial, tax and legal advice, as necessary.

This report is strictly confidential to the recipient. It is being supplied to you solely for your information and may not be reproduced, redistributed or passed on, directly or indirectly, to any other person or published, in whole or in part, for any purpose. The distribution of this report in other jurisdictions may be restricted by law, and persons into whose possession this report comes should inform themselves about, and observe, any such restrictions. By accepting this report you agree to be bound by the foregoing instructions.

China Securities (International) Research

18/F, Two Exchange Square, Central, Hong Kong

Tel: (852) 34655600 Fax: (852) 21809495

Bloomberg: CSCR <Go>