Malaysia Sector Update

10 January 2025

Communications | Telecommunications

Telecommunications

Clearing The Air On 5G

Neutral (Maintained)

Stocks Covered	6
Rating (Buy/Neutral/Sell):	4 / 2 / 0
Last 12m Earnings Revision Trend:	Negative

Top Picks	Target Price
Telekom Malaysia (TM MK) – BUY	MYR8.45
Axiata Group (AXIATA MK) – BUY	MYR3.40
CelcomDigi (CDB MK) – BUY	MYR4.35

Analyst

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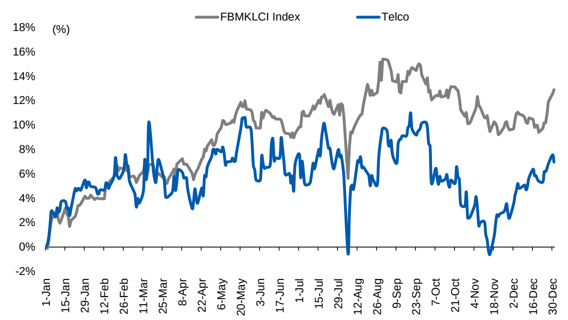
- **Preferred picks: Telekom Malaysia (TM), Axiata Group (Axiata) and CelcomDigi (CDB).** Malaysian telcos saw 5% share price returns in 2024 (2023: +0.3%), with TM outflanking (+25%) the MNOs (-5 to -9%). Excluding TM, telcos delivered a -2% return. We see another year of stock picking, noting that regulatory risks (drawn-out 5G policy saga and possible review of access prices by year-end) may continue to cast a pall on overall sector outlook (reflected in valuations). Maintain sector NEUTRAL.
- **Nominal growth seen; competition should stay elevated**. For 2025, we see nominal mobile service revenue (MSR) growth as usage/spending propensity may be crimped by the secondary effects of further subsidy rationalisation. Coupled with 5G monetisation challenges, mobile ARPUs may continue to reel under pressure. We see the sustained competition in the FBB segment as MNOs continue to peddle FBB-mobile packages to drive customer retention. In our view, enterprise-solutions will continue to drive 5G demand as retail use cases remain scarce. We see good progress made by the MNOs on commercialising 5G solutions across a number of verticals.
- **5G uncertainty lingers on; network collaborations a foregone conclusion.** The selection of U Mobile (UM) as the second 5G network access provider has caught the market by surprise. Clarity is sought on: i) MNOs commitment to Digital Nasional Berhad (DNB) now that it no longer holds exclusive 5G access, ii) the continuity of long-term lease agreements with telcos, and iii) 5G-related capex. Our base case view is for UM to enter into network collaborations to defray 5G capex, which could range from MYR3-4bn, by our estimates. The sharing of network infrastructure would expedite site deployments, allowing population coverage targets to be met more swiftly.
- **Data centres (DCs) – the story continues**. The burgeoning demand for DCs should continue to benefit fixed integrated telcos. We note the completion of TM's new cable landing station in Morib would allow it to better serve the connectivity needs of new DCs sprouting up in the south of the Klang Valley. TM's JV with Singtel (ST SP, BUY, TP: SGD3.60) (51:49) to develop a 64MW artificial intelligence (AI)-DC is on track for completion by 4Q26. We previously estimated the AI-DC could potentially contribute MYR80-85m to TM's earnings (based on its stake).
- **Sector valuation (-1.8SD of historical EV/EBITDA mean) is reflective of the regulatory quagmire and competitive risks.** TM's ownership of core digital infrastructure assets makes it an indispensable connectivity play. We project a respectable FY24F-26F earnings CAGR of 11.7%, driving ROIC expansion. We also like Axiata for its earnings recovery and balance sheet deleveraging thesis, helped by macroeconomic tailwinds and continued operational improvements. Meanwhile, we see CDB as a value play, being a key sector laggard. Stronger merger synergies in FY25-26 should drive a re-rating of the stock. Key risks for the sector/stocks: Competition, weaker-than-expected earnings, and regulatory setbacks.

Malaysian telcos' share price performance in 2024



Source: Company data, RHB

Company Name	Rating	Target (MYR)	% Upside (Downside)	P/E (x) Dec-25F	P/B (x) Dec-25F	ROAE (%) Dec-25F	Yield (%) Dec-25F
Axiata Group	Buy	3.40	48.5	15.0	0.9	3.6	4.4
CelcomDigi	Buy	4.35	18.9	21.5	2.5	11.8	3.6
Maxis	Neutral	3.92	8.6	19.5	4.1	21.1	4.4
OCK Group	Buy	0.70	50.5	10.8	0.9	8.9	2.0
Telekom Malaysia	Buy	8.45	29.0	13.3	2.4	18.6	4.1
Time dotCom	Neutral	5.10	11.4	17.0	1.1	6.4	4.7

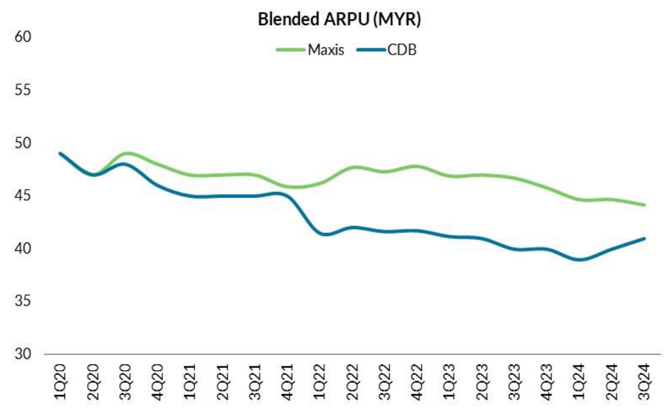
Source: Company data, RHB

Key Highlights

Industry MSR flat in 9M24; 5G base growing but monetisation remains a challenge

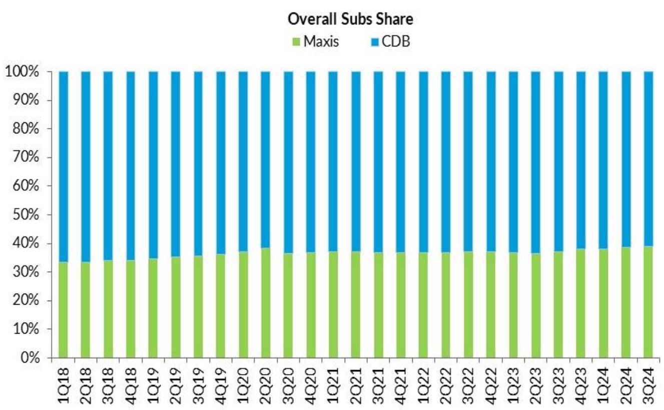
Industry MSR (Big-2 MNOs) ticked up a marginal 0.6% YoY in 9M24, with postpaid growth (+2.8%) offsetting extended prepaid weakness (-2.3%). Pre-to-post migration, higher take-up of fibre broadband (FBB)-mobile bundles and family plans drove postpaid growth while SIM consolidation and price competition clipped the prepaid segment. For 2025, we see nominal MSR growth as weaker usage/spending propensity (secondary effects of further subsidy rationalisation) would likely weigh on ARPUs alongside 5G monetisation challenges (outsized data quotas). As at end-Sep 2024, 5G mobile penetration stood at 31% (c. 46% of the population).

Figure 1: Blended mobile ARPUs (Big-2)



Note: Blended ARPU nos for CDB from 1Q20-4Q21 are based on standalone Digi nos
Source: Company, data, RHB

Figure 2: Mobile subscriber market share (Big-2)



Note: CDB numbers based on post-merger data and adjusted historical data
Source: Company, data, RHB

5G use cases still confined to enterprises; base growing nicely

Thus far, enterprise solutions have mainly spearheaded underlying 5G demand as retail use cases remain scarce. We see telcos making good progress on commercialising 5G solutions across verticals ie manufacturing, logistics, oil & gas, healthcare, automotive, consumer retail and financial services with the use of AI and machine learning. Enterprise contributions for the MNOs remained modest relative to mobile connectivity revenues, at c.11% and 18% of Maxis and CDB's overall service revenues. ICT solution sales for both MNOs (where the bulk of enterprise 5G revenues are booked) grew 13-14% in 9M24. Maxis' enterprise revenue (excluding mobile connectivity) is about three times bigger than CDB as it had an earlier head start with the acquisitions of several enterprise-related assets strengthening its portfolio of enterprise offerings.

Figure 3: Maxis MoU with UTAR to explore 5G solutions in healthcare and education

Source: Company data

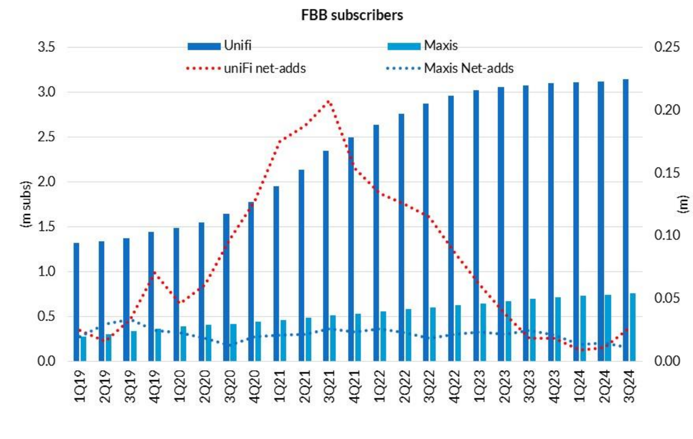
Figure 4: Malaysia's first 5G AI-powered warehouse inventory management system for DHL was commissioned by CDB in 2023

Source: Company data

FBB growth up double-digit; more room for upside given the still modest household FBB penetration

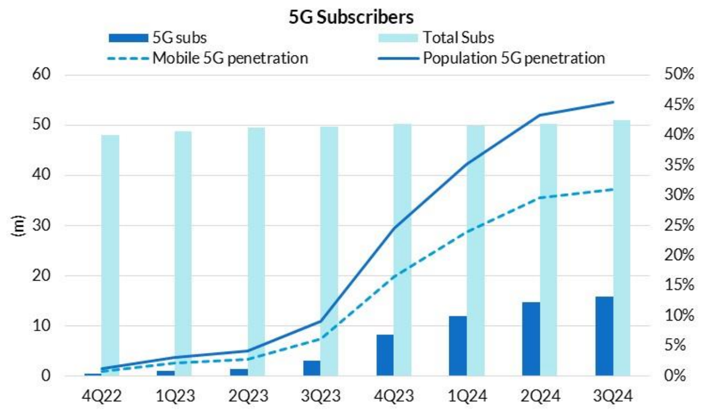
We see sustained competition in the FBB segment as MNOs should continue to peddle FBB-mobile packages to drive customer retention. Customers on bundled packages exhibit lower flight risks and are less likely to churn compared to a standalone mobile subscription with good ARPU accretion. Those on multiple service bundles are also more likely to opt for other digital solutions/services (including lifestyle devices) offered by the telcos which prolongs the customer value lifecycle. Both CDB and Maxis recorded robust double-digit growth in home fibre revenue YTD. Despite the elevated competition, FBB stalwarts, TM's and Time dotCom's (TDC) retail FBB revenue and subs base continued to grow, with improved product value propositions and the expansion into Tier-2 markets.

Figure 5: Home FBB subscribers (TM Unifi & Maxis)



Source: Company, data, RHB

Figure 6: 5G subscribers and penetration



Source: Company data, RHB, Malaysian Communications and Multimedia Commission (MCMC)

5G uncertainty lingers on; joint network collaborations a foregone conclusion

The selection of UM as the second 5G network access provider has caught the market by surprise (see our earlier report: *Telecommunications : The "U" Connection*). Here, investors' hopes of a final resolution to the protracted 5G policy debacle were arguably short-lived as the appointment has raised more questions. Clarity is sought on: i) the MNOs commitment to DNB now that it no longer has exclusivity to 5G access/spectrum, ii) the continuity of long-term lease agreements with the telcos where lease payments have been nominal, and iii) 5G capex. A second 5G access provider has altered the supply-driven model of DNB, and in theory, would contribute to higher cost to serve with traffic split two ways.

Following the announcement, UM's founding investor and major shareholder, Singapore Technologies Telemedia (ST Telemedia) (linked to Temasek) has sold down its stake to a local entity controlled by Tan Sri Vincent Tan, UM's other key shareholder. We see UM entering into network collaborations with other MNOs as it is only logical to do so to defray network capex, which could range from MYR3-4bn, by our estimates. The sharing of network infrastructure would expedite site deployments, allowing population coverage targets to be met more swiftly.

While UM has yet to unveil its rollout plans, we gather from industry sources that it could potentially deploy 5,000-7,000 5G sites nationwide via the upgrades of existing/brownfield 4G sites and new builds. UM had in Jul 2024 inked MoUs with four network infrastructure providers – Bullish Aim, OCK Group (OCK MK, BUY, TP: MYR0.70), Edgepoint Towers and Naza Communications to facilitate site deployments. We believe a combination of vendor financing, deferred payment option, and debt funding are being explored to fund the network expansion.

Figure 7: UM's major shareholder announced the sale of a majority stake on 4 Dec 2024 to a local entity controlled by TSVT

STTelemedia

(UEN/Company Registration No. 199500279W)
(Incorporated with limited liability in Singapore)

ANNOUNCEMENT

ENTRY BY WHOLLY-OWNED SUBSIDIARY INTO SHARE PURCHASE AGREEMENT

Singapore Technologies Telemedia Pte Ltd (the "**Issuer**") wishes to announce that on 4 December 2024, its wholly-owned subsidiary, Straits Mobile Investments Pte. Ltd. (the "**Vendor**"), has entered into a conditional share purchase agreement pursuant to which, Mawar Setia Sdn. Bhd. (the "**Purchaser**"), a private limited company incorporated in Malaysia, will acquire from the Vendor a majority stake in the Issuer's subsidiary, U Mobile Sdn. Bhd. ("**U Mobile**"), a mobile and broadband service provider in Malaysia (the "**Proposed Transaction**").

Following completion of the Proposed Transaction, the Vendor will hold a minority stake of approximately 20% in U Mobile, and U Mobile will cease to be a subsidiary of the Issuer. In addition, a supplemental letter agreement to the existing shareholders' agreement in respect of U Mobile (the "**Shareholders' Agreement**") will be entered into between, amongst others, the Purchaser, the Vendor and STT Communications Ltd, a direct wholly-owned subsidiary of the Issuer and sole shareholder of the Vendor, in respect of the amendment to certain rights and obligations of the parties under the Shareholders' Agreement.

Completion of the Proposed Transaction is subject to the satisfaction of certain conditions precedent including the receipt of regulatory approvals in respect of the Proposed Transaction and is expected to take place no later than the third quarter of 2025.

4 December 2024

Source: ST Telemedia

DCs – still a good infrastructure and connectivity play for integrated telcos

The burgeoning demand for DCs should continue to benefit fixed integrated telcos. We see TM as an indispensable connectivity play with earnings upside from the wholesaling of fibre bandwidth/connectivity to hyper-scalers and co-location DC providers alongside the improved utilisation of its twin-core DCs in Iskandar Puteri and Cyberjaya (TM One) where capacity upgrades should be completed by end-2025. We also note the completion of TM's new cable landing station in Morib would allow it to better serve the connectivity needs of new DCs sprouting up in the South of the Klang Valley.

TM's JV with Singtel (51:49) to develop a 64MW AI-DC in Iskandar Puteri is on track for completion by 4Q26. We previously estimated the AI-DC could potentially contribute MYR80-85m to TM's earnings pa (based on its stake). Similar to Maxis, TM is also offering GPU as-a-service (GPUaas) as part of its enterprise grade DC offerings.

JENDELA Phase 2 (JP2) likely to be announced by 2H25; tender rules to be tightened after setbacks encountered in JP1

We expect the regulator to announce the second phase of the programme to expand the nation's digital connectivity over the next six months. Under the Phase 1 (JP1) implementation which took place from Sep 2020 to end-2022, 4G population coverage expanded to 96.9% (mid-2021: 91.8%) while the number of fibre premises passed widened to 7.5m. Mobile broadband speeds also improved to 35Mbps (average), surpassing the initial target of 25-30Mbps.

Construction of 1,661 4G towers in rural areas was a key feature of JP1 with 1,018 of the towers in Sabah and Sarawak. However, only 58% of the towers were completed (on air) as at end-Oct 2024, with the bulk of the non-operational towers (577) located in East Malaysia. Given the multiple delays and execution challenges encountered under JP1, the process for site selection for JP2 will be overhauled and the tender process tightened.

JP2 aims to raise internet coverage to 100% of the population with average mobile speeds of 100Mbps. Alternative technologies will be considered, including that of low-orbit satellites as workarounds to terrestrial technologies which were found to be less accessible in the more remote areas. On top of increasing the number of fibre premises passed to 9m under JP2, the scope of the Point of Presence (POP) fibre hub project administered by the Ministry of Communications will also be expanded via a MYR800m allocation in Budget 2025.

Maintain sector NEUTRAL; valuation at -1.8SD of historical EV/EBITDA is reflective of the regulatory quagmire

Overall, we see the tight competition among the MNOs extending into 2025 with macroeconomic and policy headwinds (the government's reform agenda and subsidy rationalisation plans) casting a pall on the overall sector outlook. The regulator's choice of the second 5G network provider has also raised more questions, with renewed concerns over execution risks. On a relative basis, we continue to prefer fixed/integrated and infrastructure players due to their more discernible and structural growth catalysts.

Our preferred picks are TM, Axiata, and CDB

Telekom Malaysia (T MK, BUY, TP: MYR8.45)

TM remains our preferred sector pick as its ownership of core digital infrastructure assets makes it an indispensable connectivity play. We see the group delivering respectable FY24F-26F earnings CAGR of 11.7% on further cost efficiencies, which would further catalyse ROIC expansion. The stock continues to trade at a discount to historical EV/EBITDA mean with upside risk to DPS from strong FCF generation and the under-leveraged balance sheet (FY24F net debt/EBITDA at 0.9x). Our MYR8.45 TP implies a prospective EV/EBITDA of 7x (4% ESG premium incorporated).

Axiata Group (AXIATA MK, BUY, TP: MYR3.40)

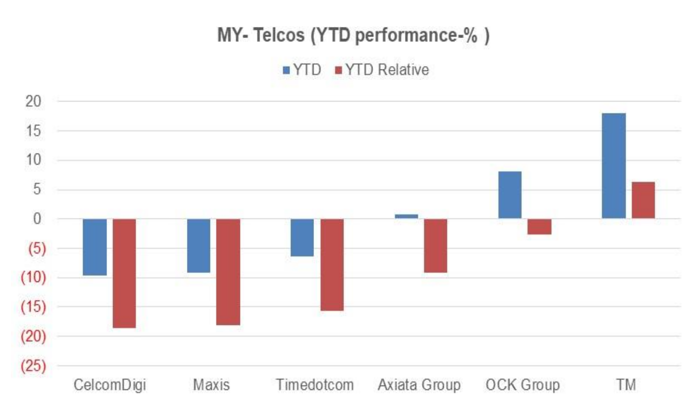
We believe the earnings recovery and balance sheet deleveraging thesis for Axiata are playing out nicely, helped by macroeconomic tailwinds and continued operational improvements. The group's net debt/EBITDA is at the lowest point in two years. Axiata trades at -1.5SD from its historical EV/EBITDA mean. Its improving risk-reward profile is a key re-rating catalyst. A 2% ESG premium is baked into our TP.

CELCOMDIGI (CDB MK, BUY, TP: MYR4.35)

We see CDB as a value play, with valuation at -1.5SD of historical EV/EBITDA mean. It was one of the worst performing telcos in the region in 2024 with expectations at the low ebb. We believe the soft patch in the mobile business is likely behind the group with a stabilisation of subs while prepaid ARPU grew on a YoY basis for the second quarter in a row in 3Q24. Stronger merger synergies in FY25-26 should drive a re-rating of the stock. Our TP has factored in a 6% ESG premium.

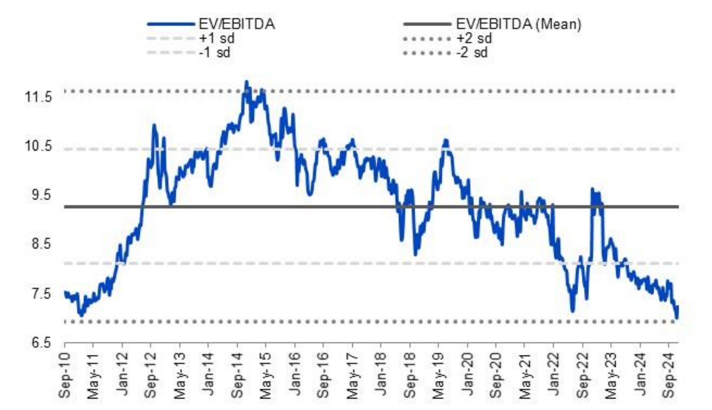
Key downside risks for the sector/stocks are competition, weaker-than-expected earnings, and regulatory setbacks.

Figure 8: Sector performance vs FBM KLCI in 2024



Source: Company, data, RHB

Figure 9: 1-year forward sector EV/EBITDA



Source: Company, data, RHB

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Neutral:	Share price may fall within the range of +/- 10% over the next 12 months
Take Profit:	Target price has been attained. Look to accumulate at lower levels
Sell:	Share price may fall by more than 10% over the next 12 months
Not Rated:	Stock is not within regular research coverage

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Analyst	Company
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