

22 June 2021

Communications | Telecommunications

Axiata Group (AXIATA MK)

Buy (from Neutral)

Valuation Uplift From CDB. U/G To BUY

- **Upgrade to BUY from Neutral with a higher SOP-derived TP of MYR4.75 from MYR3.80, 19% upside and c.2% yield.** The merger of Celcom and DiGi.Com (DIGI MK, BUY, TP: MYR4.78) is value accretive for Axiata, with the former's valuation unlocked. We see potential FY22F earnings accretion of 13% (including MYR8.0bn in synergies). Key downside risks: Lower-than-expected synergies realised and higher-than-expected competition across its mobile footprint.
- **Merger on.** Axiata has entered into a conditional share purchase agreement with Digi for the proposed merger of its wholly-owned mobile unit, Celcom, with Digi. This follows the earlier announcement of non-binding discussions (9 Apr) to merge their domestic mobile businesses with due diligence completed. The entire exercise is slated for completion by 2Q22 (9-12 months) and subject to relevant regulatory approvals, with EGMs to be convened by DIGI and Axiata and the issuance of a non-objection report from the regulator, the Malaysian Communications and Multimedia Commission (MCMC). We do not anticipate MCMC offering a dissenting opinion, as the overall construct of the merger is positive for the industry and market dynamics.
- **Celcom valued at 9.5x FY20 EBITDA.** The merger will see 3.96bn new Digi shares issued (at MYR4.06), valuing Celcom at MYR17.8bn – an implied 9.5x FY20 EBITDA. The consideration includes MYR1.99bn in cash payable to Axiata (subject to further adjustments at the close of transaction) from Digi and Telenor. Both Axiata and Telenor would have an equal 33.1% stake in the MergeCo - to be renamed Celcom Digi Berhad (CDB). Post-merger, the market capitalisation of CDB of c.MYR56bn (plus synergies) would make it the biggest telco constituent on the FBM KLCI (in the Top 5).
- **Merger synergies higher than expected.** Based on initial estimates, Axiata and Telenor have guided for synergies to the tune of MYR8.0bn, an amount which appears to be ahead of our and market estimates of MYR5-7bn. This would largely come from network, marketing and distribution, and other opex savings. We understand that a high-level integration team (from both Celcom and Digi) of 70 staff has been set-up with a dedicated project management office to oversee the integration. While there will not be forced retrenchments, some realigning of the workforce is to be expected (including potential severance packages), with the combined headcount at c.3,800 (excluding insourced Ericsson staff at Digi and 2,400 staff at Celcom).
- **Potential earnings accretion of 13% (plus synergies).** Based on the guidance of MYR8.0bn in cost synergies (MYR800m pa) and interest savings (MYR2.0bn cash from Telenor and Digi), we estimate FY22 earnings accretion of c.13% for Axiata. Pending further clarity on the scope of cost savings/synergies with detailed work to start in the integration planning phase, we leave our forecasts unchanged for now. Axiata is rated "Good" overall in RHB's proprietary environmental, social and governance (ESG) benchmark.

Forecasts and Valuation	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Total turnover (MYRm)	24,583	24,203	25,619	27,314	28,982
Recurring net profit (MYRm)	960	865	946	1,089	1,184
Recurring net profit growth (%)	19.0	(9.8)	9.4	15.0	8.7
Recurring P/E (x)	37.52	41.61	38.05	33.07	30.42
P/B (x)	2.2	2.0	2.2	2.2	2.2
P/CF (x)	3.15	5.48	3.63	3.32	3.14
Dividend Yield (%)	2.4	1.8	2.2	2.6	2.8
EV/EBITDA (x)	4.12	3.93	3.33	2.86	2.40
Return on average equity (%)	8.7	2.2	5.6	6.7	7.3
Net debt to equity (%)	55.5	44.1	33.4	15.5	net cash

Source: Company data, RHB

Target Price (Return):	MYR4.75 (+19%)
Price:	MYR3.98
Market Cap:	USD8,804m
Avg Daily Turnover (MYR/USD)	16.0m/3.87m

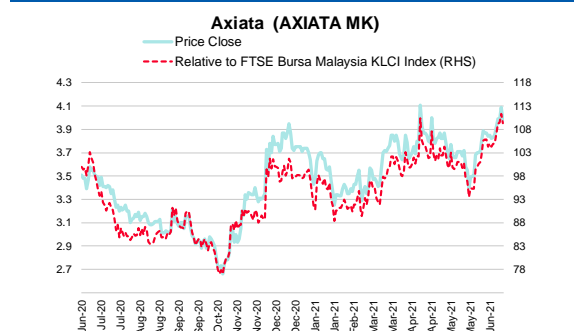
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	6.4	17.1	3.4	6.4	15.0
Relative	9.8	16.5	6.7	11.0	10.7
52-wk Price low/high (MYR)				2.66 – 4.11	



Source: Bloomberg

Overall ESG Score: 3.1 (out of 4)

E: Good

Axiata is committed to the progressive reduction in overall carbon footprint via proactive measures to increase the efficiency of its networks. The company publishes annual emission metrics across its operating companies. edotco Group (Axiata's towerco subsidiary) is one of the pioneers in the development and construction of environmentally-friendly structures, such as carbon fibre and bamboo towers.

S: Good

By virtue of its regional footprint across 11 countries/markets, Axiata boasts the largest headcount of a listed integrated telecommunications entity in Malaysia, with more than 12,900 employees from 38 nationalities. The group offers a world-class working environment, embraces a high-performance culture and aspires to be Asia's top talent factory. Axiata's Young Talent Programme (AYTP), which started in 2011, has benefitted over 2,100 students.

G: Good

The Board is made up of nine Directors, of which five are Independent, with women making up 30%. Axiata is in full compliance of best practises in relation to the tenure of Independent Directors not exceeding a cumulative term of nine years. An investor relations (IR) team facilitates meetings between management and the investment community with an annual Investor Days held.

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Financial Exhibits

Asia	Financial summary (MYR)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Malaysia	Recurring EPS	0.11	0.10	0.10	0.12	0.13
Communications	DPS	0.10	0.07	0.09	0.10	0.11
Axiata	BVPS	1.79	1.95	1.77	1.79	1.81
AXIATA MK	Return on average equity (%)	8.7	2.2	5.6	6.7	7.3
Buy						
Valuation basis	Valuation metrics	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
SOP	Recurring P/E (x)	37.52	41.61	38.05	33.07	30.42
	P/B (x)	2.2	2.0	2.2	2.2	2.2
	FCF Yield (%)	14.5	3.4	9.8	12.4	14.1
	Dividend Yield (%)	2.4	1.8	2.2	2.6	2.8
Key drivers	EV/EBITDA (x)	4.12	3.93	3.33	2.86	2.40
i. Stronger than expected earnings;	EV/EBIT (x)	12.37	19.29	12.55	10.78	9.18
ii. Cost optimisation						
iii. In-country consolidation						
Key risks	Income statement (MYRm)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
i. Competition;	Total turnover	24,583	24,203	25,619	27,314	28,982
ii. Economic shocks from COVID-19;	Gross profit	24,583	24,203	25,619	27,314	28,982
iii. Merger proposal between Celcom and Digi falling through;	EBITDA	10,619	10,657	11,857	12,633	13,343
iv. Regulatory risks	Depreciation and amortisation	(7,084)	(8,485)	(8,710)	(9,287)	(9,854)
	Operating profit	3,535	2,172	3,146	3,346	3,489
	Net interest	(1,508)	(1,516)	(1,170)	(1,169)	(1,168)
	Pre-tax profit	2,872	1,171	2,491	2,792	3,035
	Taxation	(1,057)	(547)	(1,046)	(1,117)	(1,214)
	Reported net profit	1,458	365	946	1,089	1,184
	Recurring net profit	960	865	946	1,089	1,184
Company Profile	Cash flow (MYRm)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Axiata is a leading regional telecommunications group with key mobile assets in Malaysia, Indonesia, Sri Lanka, Cambodia, Bangladesh and Nepal. It also owns edotco Group, one of the largest tower infrastructure services providers in Asia and digital financial services provider, Boost	Change in working capital	3,380	(2,023)	279	515	506
	Cash flow from operations	11,434	6,571	9,920	10,863	11,467
	Capex	(6,202)	(5,330)	(6,400)	(6,400)	(6,400)
	Cash flow from investing activities	(6,202)	(5,330)	(6,400)	(6,400)	(6,400)
	Dividends paid	(865)	(633)	(804)	(925)	(1,006)
	Cash flow from financing activities	(5,054)	2,014	(804)	(925)	(1,006)
	Cash at beginning of period	5,060	4,224	7,194	10,104	14,071
	Net change in cash	178	3,255	2,716	3,537	4,061
	Ending balance cash	5,238	7,479	9,910	13,642	18,132
	Balance sheet (MYRm)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Total cash and equivalents	4,502	7,225	10,135	14,101	18,765
	Tangible fixed assets	25,642	24,496	20,763	18,047	14,691
	Total investments	10,646	10,867	10,881	10,895	10,909
	Total assets	66,635	67,962	67,677	69,274	70,923
	Short-term debt	7,632	2,972	2,972	2,972	2,972
	Total long-term debt	9,194	14,774	14,774	14,774	14,774
	Total liabilities	44,415	44,082	44,886	45,734	46,567
	Total equity	22,220	23,879	22,791	23,541	24,356
	Total liabilities & equity	66,635	67,962	67,677	69,274	70,923
	Key metrics	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Revenue growth (%)	2.9	(1.5)	5.8	6.6	6.1
	Recurrent EPS growth (%)	19.0	(9.8)	9.4	15.0	8.7
	Gross margin (%)	100.0	100.0	100.0	100.0	100.0
	Operating EBITDA margin (%)	43.2	44.0	46.3	46.3	46.0
	Net profit margin (%)	5.9	1.5	3.7	4.0	4.1
	Dividend payout ratio (%)	59.0	173.4	85.0	85.0	85.0
	Capex/sales (%)	25.2	22.0	25.0	23.4	22.1
	Interest cover (x)	2.03	1.28	2.22	2.36	2.46

Source: Company data, RHB

Key Highlights

Figure 1: Potential earnings impact on Axiata

(MYRm)	
Current FY22F core earnings	1,088.8
Less: Celcom's core earnings (100% stake)	(888.8)
Assumed cost synergies (33.1% share of MYR800m)	264.8
33.1% stake in CDB's earnings	691.8
Interest savings on debt (@ 5% interest rate)	75.6
Indicative FY22 core earnings- post merger	1,232.3
Core earnings accretion/dilution	13%

Source: RHB

Figure 2: Axiata's valuation

(MYRm)	
Valuation of 33.1% stake in CDB (assuming MYR8bn synergies)	18,562.4
Cash payment (Digi and Telenor)	1,990.7
Less : Current valuation of Celcom (SOP)	12,899.0
Valuation uplift	7,654.1
Value uplift per Axiata share	0.85
Value per Axiata share (MYR)	4.75
% upside from current price	19%

Source: RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2021-05-26	Neutral	3.80	3.50
2021-02-26	Neutral	3.90	3.55
2020-11-29	Neutral	4.00	3.73
2020-08-28	Buy	3.50	3.01
2020-07-21	Neutral	3.50	3.23
2019-11-29	Neutral	3.90	4.13
2019-09-10	Sell	4.00	4.11
2019-05-29	Neutral	4.30	4.50
2019-04-19	Neutral	4.40	4.04
2019-02-25	Buy	4.80	4.17
2018-11-26	Buy	4.50	3.45
2018-09-19	Neutral	4.90	4.64

Source: RHB, Bloomberg

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