

# Philippines Telecoms

# NEUTRAL

 [Unchanged]

## Year Ahead 2023: Heightened competition

### Pressure on prices and margins; TEL our Top Pick

Even at only c.25% penetration, growth in fixed-line customers significantly decelerated in Jan-Sep 2022 (see *Hitting the brakes* report). This has led to intensified competition among the telcos, which are fighting for market share through 'shifting promos' and offering higher speeds at unchanged price points. In its base plan of PHP1,500/mo., CNVRG now offers up to 200Mbps, outdoing GLO/TEL's 150/100Mbps offerings. All three telcos have introduced lower-priced plans at PHP1,250-1,299/mo. (at 25-50Mbps). CNVRG also entered the prepaid market, with an initial offer of PHP700/mo. while GLO is launching a prepaid fibre service, on top of its new prepaid wifi plan. While these initiatives are good for consumers and deepen the country's digital penetration, telcos may see declining ARPUs and margins; hence, we keep our NEUTRAL call on the sector.

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### Acronyms:

*Mbps* - Megabits per second  
*ARPU* - Average revenue per user

### Other stocks mentioned:

*DITO Telecommunity Corp.* (DITO PM, CP: PHP2.99, Not rated)

### Wireless still growing; albeit at slower pace

Telcos are already feeling the pinch from inflation, with TEL and GLO both reporting declines in mobile top-ups and reloading frequency. For FY23E, we expect muted +2.9%/3.0% YoY recovery in mobile data demand for TEL/GLO. The presence of DITO should present little competition given its issues with signal reliability and negative equity. Further, the new law requiring prepaid SIM registration, with the deadline for compliance expected to be in Apr 2023 (180 days after the SIM card registration act was passed), could lead to a drop in mobile subscribers. But this should not be a cause for concern because these SIMs are not significant revenue drivers, and can even add significantly to telco costs as they need to implement security measures to block scam messages.

### Focusing on new business

The slowdown in core telco segments (i.e. mobile data and fixed broadband) has compelled telcos to focus on new businesses, such as data centers, fintech, media, and even online healthcare. While new ventures take time to scale and achieve profitability, data centers are already driving enterprise revenues and GLO's fintech unit GCash achieved profitability in 3Q21. TEL's Maya is only expected to turn profitable in 2024. We believe telco capex peaked in 2021 on aggressive fibre expansion, and should start to decline from 2023. This should help the telcos keep gearing ratios low and sustain their high dividend payout ratios.

### TEL our Top Pick; GLO new TP at PHP2,695

TEL remains our Top Pick in the sector for its fixed-line and enterprise leadership, and continued efforts to provide fast reliable internet connection. We are also positive on GLO given its leadership in mobile. With the competitive threat from DITO now subdued, GLO can continue growing steadily in mobile. We also like that its fintech venture GCash is now profitable, and new business ventures appear promising. Our new rolled-forward TP for GLO is PHP2,695 (+1.7%) taking into account +3.2/3.0% core income adjustments and a lower 2023 capex forecast.

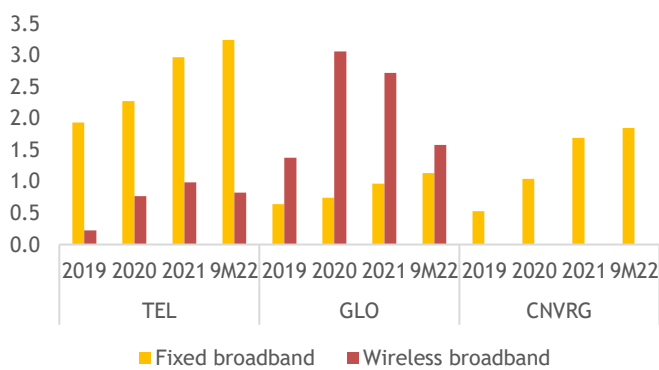
Stock	Bloomberg code	Mkt cap (USD'm)	Rating	Price (LC)	TP (LC)	Upside (%)	P/E (x)		P/B (x)		Div yld (%)	
							22E	23E	22E	23E	22E	23E
PLDT Inc.	TEL PM	6,476	Buy	1,668.00	2,075.00	30	9.4	12.3	2.8	2.6	8.6	6.6
Globe Telecom	GLO PM	5,551	Buy	2,150.00	2,695.00	30	9.2	10.3	4.1	3.7	5.0	5.0
Converge ICT	CNVRG PM	1,985	Hold	15.20	12.90	(15)	13.3	9.8	2.6	2.0	0.0	0.0

# 1. Stiff fixed-line competition; prepaid broadband still in soft launch

Even at only c.25% penetration, the rise in fixed-line customers has sharply slowed since the beginning of the year with the trend persisting in 9M22. This spurred telcos to be more competitive, with growth strategies now including winning market share from rivals through ‘shifting promos’ and high speed offerings for the same price points.

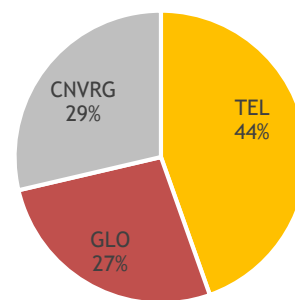
In 9M22, net adds for the three telcos reached only 594k, down 50.6% YoY. TEL still has largest share of net adds at 44%, allowing it to retain the highest percentage of subscriber share at 52.1%.

**Fig 1: Fixed and wireless broadband subscribers (in millions)**



Source: Company

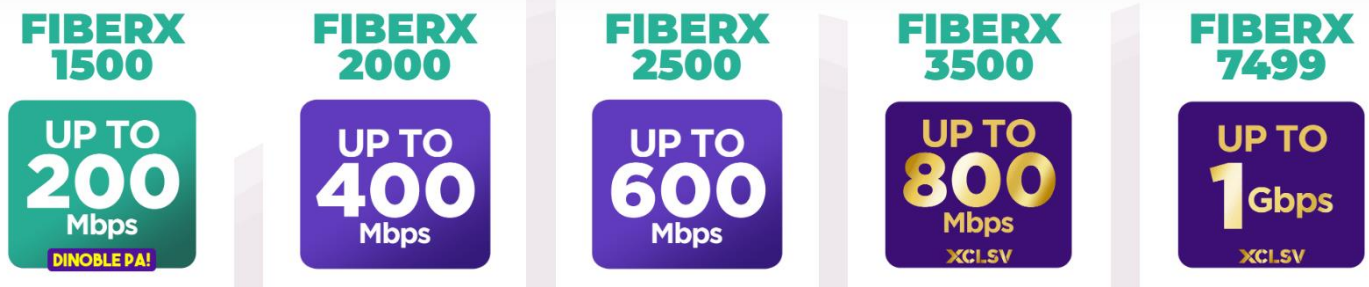
**Fig 2: Share of net adds for fixed broadband for 9M22**



Source: Company, Maybank IBG Research

CNVRG’s base plan of PHP1,500/mo. now offers up to 200Mbps of speed, topping that of GLO/TEL at 150/100Mbps.

**Fig 3: CNVRG’s new data plans**



Source: Company website

The three telcos introduced lower-priced broadband plans at PHP1,250-1,299/mo., with speeds of between 25-50Mbps. CNVRG’s initial prepaid offer costs PHP700/mo., with an installation cost of PHP1,000. GLO, meanwhile, is launching a prepaid fibre service (similar to CNVRG) on top of its newly launched prepaid Wifi. While these initiatives are good for consumers and deepen the country’s digital penetration, telcos may see a drop in ARPU and margins due to cannibalisation (i.e. higher-plan clients could downgrade to lower plans).

Fig 4: Comparison of fibre broadband plans

Plan (PHP/mo.)	GLO	TEL	CNVRG
1,250			50Mbps
1,299	50Mbps	25Mbps	
1,500			200Mbps
1,699	150Mbps	100Mbps	
1,749		150Mbps	
2,000			400Mbps
2,099	300Mbps	200Mbps	
2,499	500Mbps		600Mbps
2,699		400Mbps	
3,499	800Mbps		800Mbps

Source: Company websites

Fig 5: TEL switching promotion



Source: Company

## 2. Softer mobile data growth due to inflation impact

Telcos are already feeling the pinch from inflation, with TEL and GLO both seeing declines in mobile top-ups and reloading frequency. For 2023E, we expect 2.9%/3.0% recovery in mobile data demand for TEL/GLO, mainly driven by increased mobility.

We don't expect too much competition from DITO, due to concerns on signal reliability, and going concern issue as evidenced by its negative equity of PHP28.7b as at end-9M22.

Republic Act No. 11934, or the SIM Card Registration Act, was signed into law on 10 Oct 2022, with the Implementing rules and regulations (IRR) released on 12 Dec. The deadline for prepaid sim registration is expected to be in Apr 2023; a move seen to purge text/call scams, potentially leading to a drop in mobile subscribers. We, however, are not concerned since these sims are not significant revenue drivers, and can even be expensive to operate as telcos need to implement security measures to block scam messages.

Based on the IRR, the following information are needed for registration.

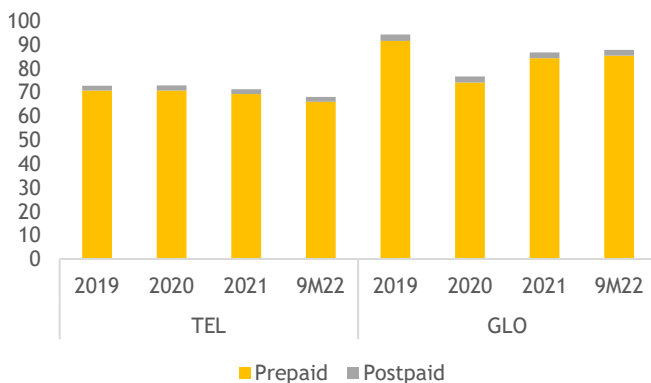
**For individuals:**

- Full Name
- Date of birth
- Sex
- Present/official address
- Type of ID presented
- ID number presented

**For juridical entity:**

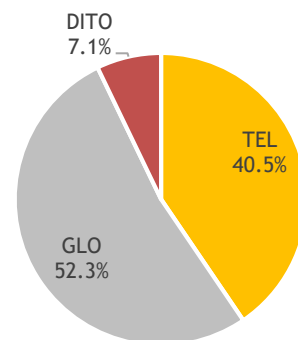
- Business name
- Business address
- Full name of authorized signatory

**Fig 6: Mobile subscribers (in millions)**



Source: Company

**Fig 7: Share of subscribers**



Source: Company, Maybank IBG Research

### 3. Forecast changes for GLO

We tweak our net income forecasts as we adjust for the timing of the recognition of tower sales. Our core income forecast is adjusted by +3.2%/3.0% on account of the following:

**Fig 8: Summary of forecast changes**

	FY22 (old)	FY22 (new)	% Change	FY23 (old)	FY23 (new)	% Change	Remarks
Service revenues	161,568	161,860	0.2%	164,811	163,977	-0.5%	Slight reduction in service revenue forecast for FY23E due to slower broadband net adds.
Nonservice revenues	16,335	16,335	0.0%	16,509	16,509	0.0%	
<b>TOTAL REVENUES</b>	<b>177,904</b>	<b>178,195</b>	<b>0.2%</b>	<b>181,320</b>	<b>180,486</b>	<b>-0.5%</b>	
<b>INCOME</b>							
Interest income	211	189	-10.6%	161	189	17.7%	We adjusted the timing of gain on sale recognition given the longer-than-expected period of closing the sale.
Gain on disposal of property and equipment - net	16,212	7,774	-52.0%	1,556	11,451	635.9%	
Equity in net income of joint ventures	1,795	1,218	-32.1%	2,388	2,357	-1.3%	We cut our equity income forecast on account of lower income booked by Mynt in 3Q22, as well as the expectation of higher costs in 4Q given new product offerings.
Other income - net	11,390	11,569	1.6%	1,088	1,083	-0.5%	
	29,607	20,750	-29.9%	5,192	15,081	190.4%	
<b>COSTS AND EXPENSES</b>							
General, selling and administrative expenses	74,368	74,489	0.2%	76,492	76,150	-0.4%	We cut our depreciation forecast given GLO's lower capex guidance of USD1.3b for 2023.
Depreciation and amortization	49,744	48,335	-2.8%	54,673	47,541	-13.0%	
Cost of sales	17,790	17,820	0.2%	18,132	18,049	-0.5%	
Interconnect costs	1,112	1,114	0.2%	1,134	1,128	-0.5%	
Financing costs	8,652	8,652	0.0%	8,906	8,906	0.0%	
Impairment losses and others	3,558	3,564	0.2%	3,626	3,610	-0.5%	
	153,795	153,973	0.1%	157,314	155,384	-1.2%	
<b>INCOME BEFORE TAX</b>	<b>53,716</b>	<b>44,972</b>	<b>-16.3%</b>	<b>29,198</b>	<b>40,183</b>	<b>37.6%</b>	
<b>PROVISIONS FOR TAX</b>							
Current	12,835	10,315	-19.6%	6,976	9,217	32.1%	
Deferred	594	478	-19.6%	323	427	32.1%	
	13,429	10,793	-19.6%	7,300	9,644	32.1%	
<b>NET INCOME</b>	<b>40,287</b>	<b>34,179</b>	<b>-15.2%</b>	<b>21,899</b>	<b>30,539</b>	<b>39.5%</b>	
<b>Net income to:</b>							
Parent	40,190	34,097	-15.2%	21,846	30,465	39.5%	
NCI	97	82	-15.2%	53	73	39.5%	
<b>EBITDA</b>	<b>81,076</b>	<b>81,209</b>	<b>0.2%</b>	<b>81,935</b>	<b>81,549</b>	<b>-0.5%</b>	
<b>Core income</b>	<b>19,572</b>	<b>20,193</b>	<b>3.2%</b>	<b>21,846</b>	<b>22,491</b>	<b>3.0%</b>	

Source: Maybank IBG Research

**GLO's 9M22 earnings snippets:**

- **GLO posted 3Q22 net income of PHP6.8b**, up 38.5% YoY (+18.3% QoQ) as a result of recognition of partial gain from the tower sale amounting to PHP1.4b net. 9M22 net income is at PHP26.5b, up 47.8% YoY. Core income at PHP16.0b is ahead our FY22 estimate at 81.8% as a result of a lower effective tax rate of 21% vs our 25% forecast.
- **EBITDA** is up 6% YoY to PHP60.3b, inline at 74.4% of our FY estimate. EBITDA margin stood at 51.1%.
- **Service revenues** rose 3.9% YoY, driven by mobile data which saw 8% YoY growth. Mobile data now accounts for 78% of mobile revenues versus 74% last year. Voice and SMS are down by 14% and 7% YoY, respectively.
- **Home broadband** dipped 8.5% YoY, driven by a drop in fixed wireless clients, bringing total broadband subscribers down 27% YoY. Net adds for fixed broadband amounted to 70.9k. Decline in wireless broadband was higher at 44.0% YoY vs the 24.6% YoY increase in fixed line.
- **Corporate data revenues** grew by 21% YoY, driven by an uptick in (Information and Communication Technology) ICT, particularly from business application services, cloud and data center.
- **Capex** totaled PHP74.4b in 9M22 (84% of PHP89b target), 84% of which was allocation for data requirements.
- **Gross debt-to-equity** is at 1.94x (max 3.1x) while gross-debt-to-EBITDA stood at 2.62x (max 3.5x); net debt-to-equity is at 1.86x while net debt-to-EBITDA is at 2.5x. Debt service cover ratio (DSCR) was at 3.79x (min 1.3x).

## 4. TEL our Top Pick; GLO new TP at PHP2,695

TEL remains our Top Pick in the sector given its leadership in fixed line and enterprise, and continued efforts to provide fast reliable internet connections to Filipinos. We are also positive on GLO for its leadership in mobile. With the competitive threat posed by DITO now subdued, GLO can continue growing steadily in the space. We also like that its fintech venture GCash is now profitable, and new business ventures appear promising.

Our income adjustments and lower capex forecast for 2023 for GLO lead to a slightly higher rolled-forward TP at PHP2,695 (+1.7%).

**Fig 9: TEL target price computation**

	Target price
NPV of FCFF (PHPm)	104,314.3
Voyager	59,628.8
Terminal value	447,569.3
Net debt	(163,251.1)
Equity value	448,261.4
# of shares (million)	216.1
<b>Equity value per share (PHP)</b>	<b>2,075.0</b>

Source: Maybank IBG Research

**Fig 10: GLO target price computation**

	Target price
NPV of FCFF (PHPm)	84,510.7
Terminal value	422,478.3
Mynt	53,250.0
Net debt	(173,061.3)
Equity value	387,177.7
# of shares (million)	143.7
<b>Equity value per share (PHP)</b>	<b>2,695.0</b>

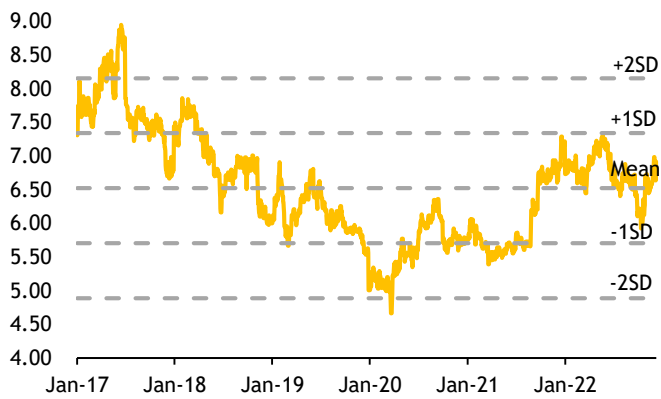
Source: Maybank IBG Research

**Fig 11: CNVRG target price computation**

	Target price
Enterprise value (PHPm)	144,481
Net debt	19,811
Equity value (PHPm)	124,669
Weighted ave. shares outstanding (m)	7,266
Target price before discount (PHP/sh)	17.2
CG discount (25%)	4.3
<b>Target price (PHP/sh)</b>	<b>12.9</b>

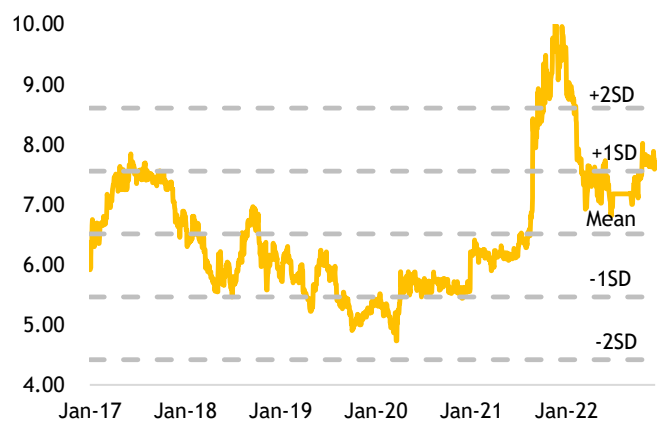
Source: Maybank IBG Research

**Fig 12: TEL 5-yr EV/EBITDA**



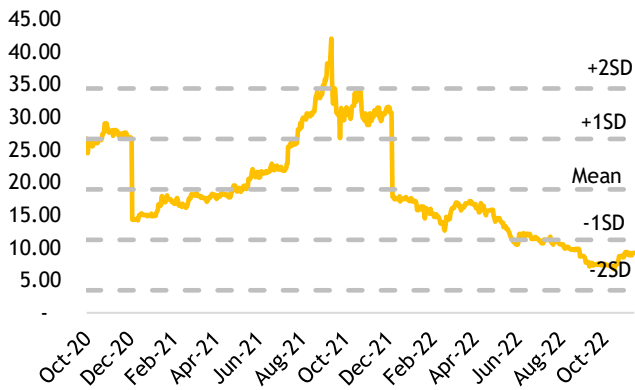
Source: Bloomberg

**Fig 13: GLO 5-yr EV/EBITDA**



Source: Bloomberg

**Fig 14: CNVRG 1-yr EV/EBITDA**



Source: Bloomberg

**Fig 15: Income growth forecasts**

	Net income (PHPm)			Core income (PHPm)			EBITDA (PHPm)		
	FY21A	FY22E	FY23E	FY21A	FY22E	FY23E	FY21A	FY22E	FY23E
TEL	26,367	38,597	29,652	30,233	32,433	33,066	96,169	97,711	102,883
GLO	23,653	34,097	30,465	23,653	20,193	22,491	74,922	81,209	81,549
CNVRG	7,156	8,319	11,281	7,156	8,319	11,281	14,801	18,037	22,757
<i>Growth</i>									
TEL	8.6%	46.4%	-23.2%	11.4%	7.3%	2.0%	2.5%	1.6%	5.3%
GLO	27.3%	44.2%	-10.6%	27.3%	-14.6%	11.4%	10.2%	8.4%	0.4%
CNVRG	111.2%	16.3%	35.6%	111.2%	16.3%	35.6%	80.1%	21.9%	26.2%

Source: Maybank IBG Research



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