27 February 2015 | 4QFY14 Results Review

Telekom Malaysia Berhad

Maintain **NEUTRAL**

FY14 earnings surpassed expectation

Increased **Target Price (TP): RM7.43**
(*Previously* RM6.42)

INVESTMENT HIGHLIGHTS

- **Higher 4Q14 normalised earnings after excluding expenses related to the MESRA programme and unrealized forex losses**
- **FY14 normalised earnings exceeded expectations**
- **Declared dividend of 22.9sen per share, which translates into a dividend yield of 3.2%**
- **Maintain NEUTRAL with a revised target price of RM7.43**

Lower normalised earnings. Telekom Malaysia's (TM) 4Q14 reported lower earnings at -36.6%yoy to RM218.3m. However, after adjusting for exceptional items amounting to RM131.9m, the company's normalised earnings were higher at RM350.2m, or +20.9%yoy. The large portion of the exceptional items pertains to unrealised forex losses on long term loans (RM43.2m) as well as MESRA programme (RM83.4m).

Full year FY14 earnings better than expected. Full year FY14 normalised earnings declined by -9.4%yoy to RM941.2m. The reduction in earnings was mainly caused by higher operating costs which shrank the profit margin by -1.4ppts to 8.4%. Despite the on-year decline, TM's earnings still exceeded ours and consensus full year earnings estimates by variance of more than 10%.

Higher topline growth. TM's full year FY14 revenue grew by +5.7%yoy to RM11,235.1m. This was mainly supported by the expansion in non-voice revenue segment. Revenue from the internet, data and others segments increased by +11.9%yoy, +3.7%yoy and +18.8%yoy respectively. On the contrary, the voice revenue declined by -4.1%yoy.

Expansion in broadband customer. The broadband customer base grew by +0.7%yoy to 2.2m customers. This was mainly attributable to the increase in UniFi subscribers to 729k from 635k a year ago, particularly from the residential segment. However, expansion is partially offset by the lower Streamyx customers which declined by 78k subscribers.

Mixed average revenue per user (ARPU). Both the Streamyx and UniFi ARPU increased by RM5 and RM7 to RM90 and RM192 respectively. This was a result of TM's marketing campaign to entice its customers to upgrade to the higher surfing speed package. On the other hand, the fixed line ARPU decreased by RM2 to RM33.

RETURN STATS	
Price (26 Feburary 2015)	RM7.10
Target Price	RM7.43
Expected Share Price Return	+4.6%
Expected Dividend Yield	+ 3.5%
Expected Total Return	+8.1%

STOCK INFO	
KLCI	1,820.97
Bursa / Bloomberg	4863 / T MK
Board / Sector	Main/ Services
Syariah Compliant	Yes
Issued shares (mil)	3,719.4
Par Value (RM)	0.70
Market cap. (RM'm)	26,407.5
Price over NA	3.8x
52-wk price Range	RM5.58 – RM7.60
Beta (against KLCI)	0.72
3-mth Avg Daily Vol	6.3m
3-mth Avg Daily Value	RM43.2m
Major Shareholders (%)	
Khazanah	28.95
EPF	14.64
ASB	13.31

Higher cost incurred as a percentage of revenue. For full year FY14, total sales costs accounted for 88.6% of revenue as compared to 87.2% in FY13. This has led to higher operating costs of +7.6% to RM10.1b. The increase in costs was mainly attributable to: i) higher bad debt due to tighter credit treatment policy; ii) higher maintenance due to higher customer projects in line with higher revenue; iii) higher supplies and materials due to higher cost of sales, higher cable cost and higher subscriber equipment and; iv) higher depreciation and amortization due to impact of accelerated depreciation for USP assets as well as higher asset base.

Lower capital expenditure (capex) spent in FY14. TM's capex was RM1,836m in FY14 as compared to RM1,863m in FY13.The lower capex was a result of lower spending in the area of access from the high speed broadband (HSBB) segment. All-in, capex-to-revenue ratio stands lower at 16.3% as opposed to 17.5% in FY13.

Dividend payout. The group declared a dividend per share of 13.4sen in 4Q14. Cumulative full year FY14 dividend declared was 22.9sen per share. This is 3.2sen per share lower than what was declared in FY13. Based on the last closing price of RM7.10, this translates into a dividend yield of 3.2%. Nonetheless, this has exceeded our dividend expectation of 19.6sen per share.

Impact on earnings. In line with the group's FY14 earnings results, we are revising upward FY15 earnings by +14.7%. We are taking into account: i) higher-than-expected internet and data revenue; ii) better operating profit margin; and iii) lower effective tax rate. We are also increasing our FY15 dividend assumption in-tandem with the upward revision in earnings base on an unchanged payout ratio of 90%.

Maintain NEUTRAL recommendation. Despite lower revenue contribution from the voice segment, revenue growth from the non-voice segment remains encouraging. This is supported by the expanding broadband customer base and higher ARPU. In addition, the award of the HSBB Phase 2 and sub urban broadband (SUBB) projects worth RM3.4b is expected to further boost TM's broadband coverage area while offering higher internet surfing speed. However, we view that future dividend payments might be capped in view of the upcoming mega projects. Despite the upward revision in dividend estimates, we are expecting dividend yield to hover around three to four percent in the foreseeable term. We reiterate our **NEUTRAL** recommendation on TM with a revised target price of RM7.43 (previously RM6.42) based on DDM valuation methodology.

DIVIDEND DISCOUNT MODEL ASSUMPTIONS

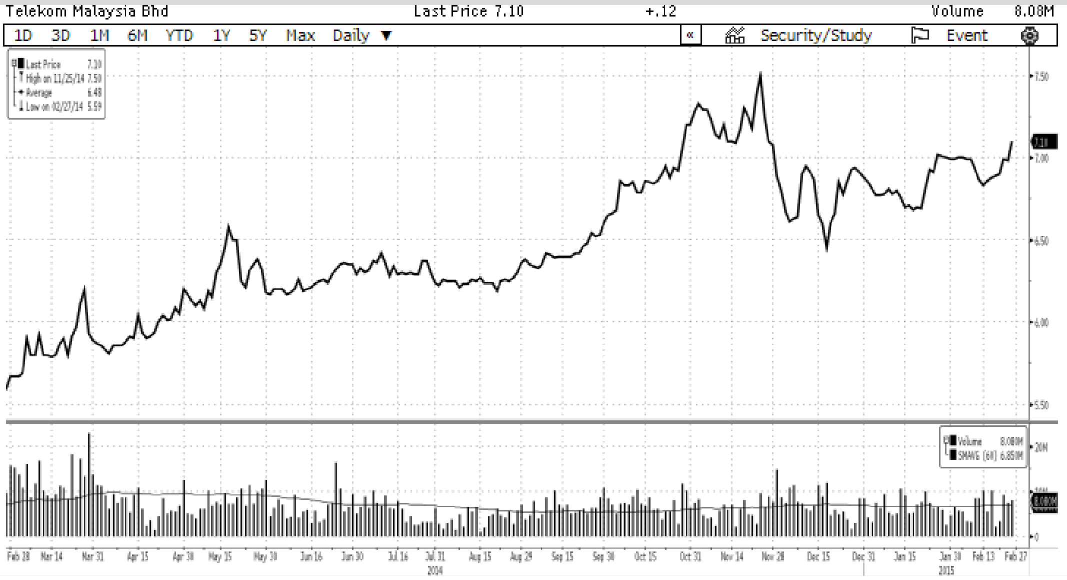
Expected market return	10.00%
Risk free rate	4.16%
Beta	0.72
Terminal growth	5.00%
Cost of equity	8.36%

INVESTMENT STATISTICS

FYE 31 Dec	2013	2014	2015F	2016F
Revenue (RM'm)	10,628.7	11,177.9	11,897.6	12,606.9
EBIT (RM'm)	1,373.6	1,279.6	1,513.4	1,601.1
PBT (RM'm)	1,046.0	1,080.4	1,294.7	1,352.0
Normalised PATAMI (RM'm)	1,038.5	941.2	996.9	1,041.0
Normalised EPS (sen)	29.0	25.9	27.4	28.6
EPS growth (%)	17.9	-10.7	5.9	4.4
PER(x)	24.5	27.4	25.9	24.8
Net Dividend (sen)	26.1	22.9	24.7	25.8
Net Dividend Yield (%)	3.7	3.2	3.5	3.6

Source: announcement, MIDFR estimates

DAILY PRICE CHART



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4QFY14 RESULTS SUMMARY

(All in RM'm unless stated otherwise)	Quarterly Results			Cumulative		
FYE June	**4Q14**	**YoY (%)**	**QoQ (%)**	**2014**	**2013**	**YoY (%)**
Revenue	3,157.3	6.0	19.8	11,235.1	10,628.7	5.7
EBITDA	960.4	0.3	9.2	3,635.6	3,531.6	2.9
Depreciation and amortisation	-631.0	9.0	10.7	-2,341.3	-2,159.7	8.4
EBIT	329.4	-13.1	6.5	1,294.3	1,371.9	-5.7
Other gains/losses	-1.7	142.9	-120.7	4.8	1.7	182.4
Net finance cost	-79.1	13.8	41.5	-202.9	-331.5	-38.8
Associate income	5.1	628.6	292.3	9.3	3.9	138.5
PBT	253.7	-18.1	-3.5	1,105.5	1,046.0	5.7
Taxation	-46.0	-201.5	-35.5	-263.0	1.8	-14,711.1
MI	10.6	-198.1	-492.6	-10.7	-35.6	-69.9
PATAMI	218.3	-36.6	15.6	831.8	1,012.2	-17.8
Normalised PATAMI	350.2	20.9	82.8	941.2	1,038.5	-9.4
EPS (sen)	9.46	16.8	81.9	25.9	29.0	-10.8
		+/- ppts	+/- ppts			+/- ppts
Normalised EBITDA margin (%)	30.4	-1.7	-2.9	32.4	33.2	-0.9
Normalised EBIT margin (%)	10.4	-2.3	-1.3	11.5	12.9	-1.4
Normalised PATAMI margin (%)	11.1	1.4	3.8	8.4	9.8	-1.4
Effective tax rate (%)	18.1	32.8	-9.0	23.8	-0.2	24.0

Source: Company, MIDFR

DISCLOSURES AND DISCLAIMER

MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS	
STOCK RECOMMENDATIONS	
BUY	Total return is expected to be >15% over the next 12 months.
TRADING BUY	Stock price is expected to *rise* by >15% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -15% and +15% over the next 12 months.
SELL	*Negative* total return is expected, by -15% or more, over the next 12 months.
TRADING SELL	Stock price is expected to *fall* by >15% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.
SECTOR RECOMMENDATIONS	
POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.