March 12, 2010

Pakistan Market

MORNING BRIEFING

PTCL: Ufone - unlocking potential

KSE100 Index: Closing 9879.70 ↑ (+94.72)

Increasing regional M&A activity in the cellular segment and impressive broadband performance has led us to revisit our valuations and estimates for PTCL. With an increased volume of regional transactions providing price discovery, we have changed our valuation basis for Ufone to EV/Subscriber from DCF previously. As a result, our fair value of Ufone is upgraded to Rs31/share from Rs24/share earlier. Moreover, impressive growth in broadband (164% in 1HFY10) provides optimism on the revenue outlook, strengthening PTCL's ability to counter shrinking fixed line business. Further, with the TSF agreement with Etisalat ending in Oct 2011, gross margins will witness a 150bps jump FY12 onwards. Hence, we reiterate our 'Buy' call on the scrip. PTCL currently trades at an impressive FY10E and FY11F EV/EBITDA of 3.5x and 3.4x respectively, a 43-47% discount to the region. Moreover, the scrip also offers an attractive dividend yield of 8.4%. Nevertheless we do not rule out (1) significant deterioration in the fixed line subscriber base (2) intense competition in the broadband/WLL segments and (3) regulatory changes as key risk to our thesis.

Valuation: Fair value revised to Rs31

We have revised upwards our target price for PTCL to Rs31/share from Rs24/share earlier, mainly attributable to the switch in valuation methodology for the cellular arm-Ufone. After the recent round of transactions providing pricing discovery, we have shifted our valuation basis for Ufone to EV/Subscriber from DCF earlier. We have used an average of two relevant transactions and applied a discount of 50% to account for penetration and ARPU differences with regional peers and a further discount of 20% to adjust for a minority stake – giving Ufone a value of Rs13/share (from Rs6/share earlier). We have also tweaked estimates for the broadband segment, as we now expect the subscribe base to grow at a 3-year CAGR (FY10-FY13) of 51%. The fair value offers an attractive upside of 49%.

Broadband– Aggressive strategy paying dividends

Given abysmally low penetration of ~0.4% currently (global penetration 7.8%), the broadband segment offers tremendous room for expansion to the telecom operators in Pakistan. This potential is reflected in the extraordinary subscriber growth of 150% in 1HFY10. PTCL in particular, has been aggressive in this segment and despite being a late entrant, has attained a market share of ~50%. Its monopolist position in the local loop segment has provided the necessary platform to go all out and promote the DSL broadband, which remains the most used technology for the provision of broadband services, not just in Pakistan but also regionally. In addition to this, PTCL has also actively participated in four USF broadband projects, three of which are projected to bring in ~159k subscribers by Dec 2010. Given this, we expect the share of broadband in total revenues to reach 12% by FY12 from 6% at present.

News flow hinting towards property resolution

Recent news flow suggests that a resolution may be round the corner, for the long deferred property dispute. Any agreement would release the pending US$800mn proceeds towards the GoP & lead to a possible property revaluation in the future.

For more details please refer to our detailed report titled "PTCL: Ufone – unlocking potential".

mustufa.bilwani@js.com
92 (21) 111-574-111 (ext. 3100)

Also in focus

Component changes to Dow Jones SAFE Indexes

In its annual review, nine Pakistani companies have been removed while two have been added in DOW Jones SAFE Pakistan Index and Dow Jones SAFE 100 Index. Two companies that have been added are Nestle Pakistan and Pakistan Tobacco Company while the companies that were removed include Glaxo Smith Klien, Arif Habib Securities, EFU General, Bank Alfalah, National Refinery, Packages Limited, Shell Pakistan, Sui Southern & Sui Northern Gas Pipeline. Dow Jones SAFE 100 Index measure the performance of 100 blue chip companies in five of the eight member states of South Asian Federation of Exchanges (SAFE) which include India, Bangladesh, Pakistan, Mauritius and Sri Lanka.

JS Global Capital Limited
6th Floor, Faysal House, Main Shahrah-e-Faisal, Karachi

Research:	Equity Sales:
Tel: +92 (21) 32799005	Tel: +92 (21) 32799513
Fax: +92 (21) 32800163	Fax: +92 (21) 32800166
js.research@js.com	junaid.iqbal@js.com
Fixed Income Sales:	**Corporate Finance:**
Tel: +92 (21) 32799541-44	Tel: +92 (21) 32799005
Fax: +92 (21) 32800165	Fax: +92 (21) 22800163
tariq.usman@js.com	azhar.iqbal@js.com