# PTCL: Ufone dividend drives 3Q earnings/‘Buy’

KSE100 Index: Closing 10271.71 ↓ (-7.81)

Pakistan Telecom recently reported its 3QFY10 results, recording an unconsolidated earnings growth of 31% in 3QFY10 and 9% in 9MFY10. The growth in 3Q profits was primarily attributable to the Rs673mn dividend income from Ufone, its wholly owned cellular subsidiary. Revenues however, remained under pressure and were down 4%YoY in 9MFY10 due to the shrinking fixed line business; leading operating margins to contract to 35%, from 37% earlier. Going forward, we expect earnings to remain resilient, and with positives in the offing such as the growing focus on the broadband segment, we continue to see strong potential in the stock, and reiterate our ‘Buy’ call. The company also announced a 17.5% cash dividend with the results.

## Revenue drops 4%YoY, Op. profits down 7%YoY

Revenues continued to register a declining trend, albeit slowly in 3QFY10, as it fell 1% to Rs13.7bn, taking cumulative revenues to Rs43bn. This was primarily owing to a fall in the domestic revenue, which went down by 7%YoY in 9MFY10. The international revenue stream however, continued to show positive momentum and increased by 23%YoY.

Revenue stream from the broadband segment continued to grow on the back of strong subscriber growth. Broadband subscribers are currently estimated to be ~450k, and with EVO sales gathering pace, along with the already popular DSL broadband; customers are expected to grow impressively. Apart from offering ample growth opportunities in an otherwise mature business model, broadband segment also offers the highest margins amongst its other business segment. The management is targeting to double its subscriber base by the end of FY11.

## Ufone dividend- key growth driver in 3Q

Dividend income from its 100% owned cellular subsidiary at Rs673mn was the primary earnings driver in the period. This is Ufone’s first dividend payout in FY10 which is encouraging, as it did not pay any dividends in FY09. Moreover, interest received on loans to its subsidiary, along side returns earned on short term investments helped ‘Other operating income’ to reach Rs1.7bn in 3QFY10 (up 56%) and Rs3.9bn (up 32%) in 9MFY10.

**Financial highlights**

| (Rs mn) | 9MFY10 | 9MFY09 | Δ% |
|---|---|---|---|
| Revenue | 43,119 | 45,021 | -4% |
| Operating Cost | (27,883) | (28,188) | -1% |
| Gross Profit | 15,236 | 16,833 | -9% |
| *Gross Margin* | *35.3%* | *37.4%* | |
| Admin. & General Expenses | (5,334) | (6,431) | -17% |
| Selling & Marketing expenses | (1,439) | (1,327) | 8% |
| Operating profit | 8,463 | 9,075 | -7% |
| Other operating income | 3,923 | 2,964 | 32% |
| Financial Cost | (344) | (912) | -62% |
| Profit/(Loss) Before Taxation | 12,042 | 11,126 | 8% |
| Taxation | (4,182) | (3,902) | 7% |
| Profit/(Loss) After Taxation | 7,860 | 7,224 | 9% |
| Basic Earning per share | 1.54 | 1.42 | 9% |

*Source: Company announcement*

## ‘Quadplay’ to aid revenues going forward

PTCL has recently announced another bundled package, this time tying up four services, under the name ‘Quadplay Unlimited’. This package brings together fixed line, broadband, television and I-Sentry (surveillance system) services under a single offer. We believe bundling of multiple services at attractive offers to aid revenues of the company going forward.

## Outlook: +ve news flow could trigger rally

We continue to remain upbeat on the scrip, and expect more positive news flow be a central feature going forward. Etisalat reiterating its interest in the company has hinted at a possible increase in its holding, highlights the long term potential in PTCL, in our view. The management is continuing to work on measures to counter depleting fixed line revenues, with bundled packages being one such measure. In addition to this, the revenue stream is expected to improve further from the recent upward revision in tariffs on FLL.

We reiterate our ‘Buy’ call with a fair value of Rs31. The scrip currently trades at an attractive FY11F EV/EBITDA and PE of 3.1x and 9.9x, respectively. It also offers an attractive dividend yield of 9%.

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## Also in focus

### IMF releases 5th tranche

IMF has completed its fourth review and approved the release of the 5th tranche of US$1.13bn. This brings the total amount received by Pakistan to US$7.27bn of the US$10.6bn loan agreement. Pakistan has been granted waivers with respect to; (1) delays in implementation of VAT and the last phase of the power tariff pass-through (2) most importantly the missed quantitative performance criteria of fiscal deficit and government borrowing from SBP for the quarter. Furthermore, the IMF board has decided to club the remaining 3 disbursements of the loan into 2 payments. The SBA programme will be completed by December 2010.

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