

26 October 2015 | Corporate Update

Digi.Com Berhad

High-Definition voice calls in 2016

INVESTMENT HIGHLIGHTS

- **Digi mulling Voice-over-LTE (VoLTE) services in 2016**
- **Continuous leverage on LTE network to improve voice and internet services**
- **New offering expected to combat declining ARPU - a concern among industry peers**
- **We expect potential problems associated to VoLTE to be transitory**
- **Reiterate BUY with unchanged target price of RM7.04 per share based on DDM valuation methodology**

Digi is testing VoLTE. Subsequent to Digi.com Bhd's (Digi) claims of having the widest 4G Long-term Evolution (LTE) coverage to-date, it is seeking to add more value to their services by adding Voice-over-LTE (VoLTE) on its 4G LTE (Long Term Evolution) network. Digi is also currently experimenting the viability of providing Voice over WiFi (VoWiFi) and LTE Advance (LTE-A).

Enhancing network experience. There are several advantages of implementing VoLTE. These include: (i) Better network experience which are six times more efficient than 2G and three times more efficient than 3G; (ii) Crystal clear audio quality with noise cancellation and High-Definition (HD) voice calls; (iii) Faster call connection; and (iv) Faster connection speed enabling simultaneous browsing, downloads and streaming.

Positive on the development. We view Digi's bold statement of having the widest 4G LTE network positively as it is a testament to Digi's commitment to further improve its services to the subscribers. Should the rollout take place next year, Digi would be the *first* mobile network operator (MNO) to rollout VoLTE in Malaysia. There could potentially be a boost in new subscribers from the rollout of VoLTE. However, note that regionally, Singapore's MNOs already has VoLTE services since 2Q2014.

Higher voice calling could provide support to dwindling ARPU. There is a possibility that users might need to pay more with VoLTE. This could help battle the decrease in average revenue per user (ARPU). Digi's ARPU has been under pressure since 2013, decreasing to RM46 from RM48 in 2013. This is in-line with the general industry trend.


Reiterate BUY

Unchanged Target Price (TP): RM7.04

RETURN STATS	
Price (23 rd October 2015)	5.63
Target Price	7.04
Expected Share Price Return	+25.0%
Expected Dividend Yield	+5.0%
Expected Total Return	+30.0%

STOCK INFO	
KLCI	1,710.93
Bursa / Bloomberg	6957 / DIGI MK
Board / Sector	Main/ Services
Syariah Compliant	Yes
Issued shares (mil)	7,775
Par Value (RM)	0.01
Market cap. (RM'm)	43.8
Price over NA	77.4x
52-wk price Range	RM4.86 – RM6.65
Beta (against KLCI)	1.03
3-mth Avg Daily Vol	11.4m
3-mth Avg Daily Value	RM61.1m
Major Shareholders (%)	
Telenor ASA	49.00
EPF	14.10

Potential problems associated to VoLTE to be transitory. VoLTE potentially requires both participants to have 4G smartphone and 4G coverage. However, at present, the coverage of 4G is not as widespread as 2G and 3G. This means that VoLTE calls will not always be available. Also, if the user moves out of the 4G coverage during the call, there is a high chances that the call will drop. Pricing may also be an issue as MNO may charge a higher fee. However, we view that all these problems could transitory as: (i) 4G coverage continue to increase; (ii) Users progressively upgrade to 4G smartphones, (iii) Prices stabilise; and (iv) Networks aligned their technology.

Reiterate BUY. Digi is our top pick in the mobile sub-segment. Digi possesses a strong management team. Based on the historical track record, the group has managed to compete with its peers despite its subservient position in the spectrum allocation domain. This is shown in its ability to move in-tandem with the demand of the market, especially the prepaid segment. Furthermore, latest earnings result has shown that there is encouraging growth in the post-paid segment which is usually dominated by its peers. On another note, the stock offers higher dividend yield of more than 5% as compared to its peers. We advice investors to take this opportunity to further increase their shareholdings in Digi as we believe there could be further upside to their future earnings should the company manage rollout VoLTE service according to its plan. All in, we reiterate our **BUY** recommendation on Digi with an unchanged target price of **RM7.04** per share based on DDM valuation methodology. 

DIVIDEND DISCOUNT MODEL ASSUMPTIONS

Expected market return	10%
Risk free rate	4%
Beta	1.00x
Terminal growth	5%

INVESTMENT STATISTICS

FYE Dec	FY13	FY14	FY15F	FY16F
Revenue (RM'm)	6,733	7,019	7,499	7,976
EBIT (RM'm)	2,155	2,671	2,807	2,943
Pretax Profit (RM'm)	2,140	2,645	2,772	2,909
Net Profit (RM'm)	1,696	2,031	2,079	2,182
EPS (sen)	22	26	27	28
EPS (%)	41.4	19.8	2.3	5.0
PER (x)	26	22	21	20
Net Dividend (sen)	21	26	27	28
Net Dividend (%)	3.7	4.6	4.8	5.0

Source: Company, MIDFR

DAILY PRICE CHART



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Table 1: List of country with VoLTE

Mobile operator	Country	Deployment date
Telstra	Australia	September 2015
Batelco	Bahrain	September 2015
SEATEL	Cambodia	July 2015
Rogers	Canada	March 2015
China Mobile	China	August 2015
T- Mobile	Czech Republic	May 2015
O2	Germany	April 2015
Vodafone	Germany	March 2015
3	Hong Kong	May 2014
CMHK	Hong Kong	September 2015
Csl. / 1010	Hong Kong	August 2014
PCCW	Hong Kong	May 2014
SmarTone	Hong Kong	August 2014
Vodafone	Italy	July 2015
Au	Japan	December 2014
NTT Docomo	Japan	June 2014
SoftBank	Japan	December 2014
VIVA	Kuwait	June 2015
Swisscom	Liechtenstein	June 2015
Orange	Romania	September 2015
Vimpelcom	Russia	August 2015
M1	Singapore	April 2015
Singtel	Singapore	May 2014
StarHub	Singapore	June 2014
Vodafone	Spain	July 2015
Vodacom	South Africa	April 2015
KT	South Korea	October 2012
LG U+	South Korea	August 2012
SK Telecom	South Korea	August 2012
Swisscom	Switzerland	June 2015
Ambit Microsystems	Taiwan	May 2015
DTAC	Thailand	October 2015
3	United Kingdom	September 2015
AT & T	United States	May 2014
Evolve Broadband	United States	2013
MetroPCS	United States	August 2012
T-Mobile	United States	May 2014
Verizon	United States	September 2014

Source: Various, Wikipedia, Companies, MIDFR

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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 <i>rise</i> 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	Total return is expected to be <-15% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> 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.