

China / Hong Kong Company Guide

China Mobile

Version 11 | Bloomberg: 941 HK EQUITY | Reuters: 0941.HK

Refer to important disclosures at the end of this report

DBS Group Research . Equity

19 Mar 2020

HOLD

Last Traded Price (19 Mar 2020):HK\$48.25 (HSI : 21,709)
Price Target 12-mth:HK\$51.00 (5.7% upside) (Prev HK\$67.00)

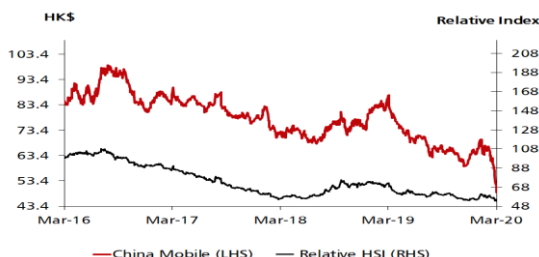
Analyst

Tsz-Wang TAM, CFA+852 36684195, tszwangtam@db.com
Chris KO CFA, +852 36684172, chriskof@db.com

What's New

- FY19 net profit declined by 10% y-o-y, in line with market expectations
- Expect initial loss for the launch of 5G services in FY20
- Total budgeted capex increased by 8% to Rmb180bn with 5G capex of Rmb100bn
- Maintain HOLD due to stronger market competition in 5G era, with lower TP of HK\$51.0

Price Relative



Forecasts and Valuation

FY Dec (RMBm)	2019A	2020F	2021F	2022F
Turnover	745,917	773,274	807,687	839,533
EBITDA	313,533	315,864	324,925	335,387
Pre-tax Profit	142,133	137,257	142,220	151,388
Net Profit	106,641	103,347	107,083	113,986
Net Profit Gth (Pre-ex) (%)	(9.5)	(3.1)	3.6	6.4
EPS (RMB)	5.21	5.05	5.23	5.57
EPS (HK\$)	5.74	5.56	5.76	6.13
EPS Gth (%)	(9.5)	(3.1)	3.6	6.4
Diluted EPS (HK\$)	5.74	5.56	5.76	6.13
DPS (HK\$)	3.22	3.22	3.22	3.22
BV Per Share (HK\$)	59.39	61.73	64.28	67.19
PE (X)	8.4	8.7	8.4	7.9
P/Cash Flow (X)	4.2	3.5	3.3	3.2
P/Free CF (X)	19.5	11.4	11.1	10.4
EV/EBITDA (X)	1.5	1.4	1.3	1.1
Net Div Yield (%)	6.7	6.7	6.7	6.7
P/Book Value (X)	0.8	0.8	0.8	0.7
Net Debt/Equity (X)	CASH	CASH	CASH	CASH
ROAE (%)	9.9	9.2	9.1	9.3
Earnings Rev (%)		0	0	New
Consensus EPS (RMB)		5.13	5.22	5.50
Other Broker Recs:		B:18	S:1	H:7

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

Facing challenges in 5G era

Facing challenges in 5G era. We have a HOLD rating on China Mobile (CM) in view of its potential market share loss in the 5G era despite its attractive valuation. China Telecom and China Unicom will co-build and co-share one 5G network to match the coverage and quality of CM's 5G network. This will reduce the network advantage that CM enjoyed in the past.

Where we differ: MNP to accelerate market share reshuffle. The market expects CM to keep its dominant market share of 60% in the 5G era. We reckon that with the nation-wide implementation of mobile number portability policy, the mobile sub churn rate will be higher during the upgrade to 5G services. This may lead to market share loss for CM.

Potential catalysts (downside): Higher-than-expected capex budget. For CM to maintain its market share, it may accelerate its 5G network build-out to increase network coverage and quality. This will lead to lower return on investment, limitation on potential dividend hike and share price pressure.

Valuation:

Our TP of HK\$51.0 is based on SOP method: (i) telecom operations at HK\$48.0 per share based on 9x FY20 PE (vs. 12x previously) excluding Towerco's earnings, and (ii) Towerco's value of HK\$3.0 per share. We lower our target multiple in light of the weaker market sentiment.

Key Risks to Our View:

Faster-than-expected 5G penetration ramp-up (upside risk). 5G service ARPU is higher than 4G. Higher-than-expected 5G penetration will generate higher return on investment.

Policy risk (downside risk). China's telecom sector has been subjected to policy risks, such as management reshuffle and tariff cuts. This could bode ill for its business performance.

At A Glance

Issued Capital (m shrs)	20,475
Mkt Cap (HK\$m/US\$m)	987,919 / 127,245
Major Shareholders (%)	
China Mobile Communications Group	72.7
Free Float (%)	27.3
3m Avg. Daily Val. (US\$m)	186.53
GICS Industry: Communication Services / Telecommunication Services	



Live more, Bank less

China Mobile**WHAT'S NEW****In-line FY19 results****FY19 results highlights**

Total revenue increased by 1% y-o-y to 746bn with service revenue growing 0.5% to Rmb674bn. EBITDA increased by 7.4% y-o-y to Rmb296bn due to change of accounting standards. On a comparable basis, EBITDA dropped by 1.6% y-o-y. Net profit decreased by 9.5% y-o-y to Rmb107bn, in line with market expectations. A final DPS of HK\$1.723 was proposed. Together with an interim DPS of HK\$1.527, its full-year DPS of HK\$3.250 represents 55% payout ratio (vs. 49% in FY18). This is in line with company guidance of maintaining absolute dividend per share.

Outlook

The company is targeting a 5G subs base of 70m by the end of 2020, which implies a penetration rate of 7%. As 5G services command higher pricing than 4G services, this will be positive for mobile ARPU. We forecast mobile ARPU to stabilise in FY20 and improve by 3% in FY21, respectively, from a declining trend. Due to the nationwide implementation of mobile number portability which will lead to more intense market competition and lower demand for second SIM cards, we expect a slower mobile sub growth of 1% for both FY20-21.

The major incremental operating expenses for 5G network involve tower leasing fees and electricity costs. The company has budgeted a total capex of Rmb180bn, representing an 8% y-o-y increase, with Rmb100bn for 5G-related capex. This is in line with market expectations. It also plans to build 250k 5G base stations in 2020. It has budgeted Rmb45bn, representing 8% y-o-y increase for tower leasing fee. We estimate that there will be an initial operating loss of 5G services.

Currently, CM has a dominate mobile market share of 60%. China Telecom and China Unicom are co-building and co-sharing one 5G network to match CM's 5G network coverage and quality. This will reduce the competitive advantages of China Mobile as it had in 4G era and increase the risks of losing mobile sub market share.

We have maintained our earnings estimates. We forecast the net profit to change by -3% and +4% in FY20-21 respectively. We maintain our HOLD rating in view of its potential market share loss in the 5G era despite its attractive valuation, with a lower TP of HK\$51.0. Our TP is based on SOP method: (i) telecom operations at HK\$48.0 per share based on 9x FY20 PE (vs. 12x previously) excluding Towerco's earnings, and (ii) Towerco's value of HK\$3.0 per share. We lower our target multiple in light of the weaker market sentiment.

China Mobile

CRITICAL FACTORS TO WATCH

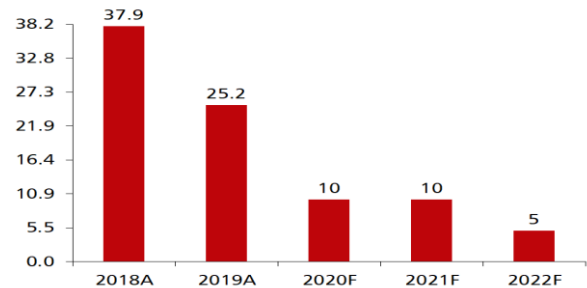
Critical Factors

Mobile subscriber growth. Mobile penetration in China has become more saturated, and we only expect aggregate sub base to expand by a single-digit rate per annum in the next few years. The company targets 70m 5G subs, which will be mainly from 4G sub upgrades, by the end of FY20. We expect mobile sub base to expand by 10m (or 1%) in both FY20-21.

Mobile ARPU (average revenue per user) increase. We believe that CM's respective 2G/3G/4G and 5G ARPUs are on a declining trend due to market competition. However, 2G/3G/4G subs upgrading to 5G will be positive to overall ARPU as 5G services generate much higher ARPUs than 2G/3G/4G services. We expect mobile ARPU to stabilise in FY20 and improve by 3% in FY21 driven by higher 5G penetration.

Capex is manageable. We expect capex in FY20 to increase by 8% to Rmb180bn with increase in mobile capex partly offset by decrease in fixed-line capex. We expect 5G related capex to be Rmb100bn in FY20. This will be supported by Rmb200bn+ operating cash flow.

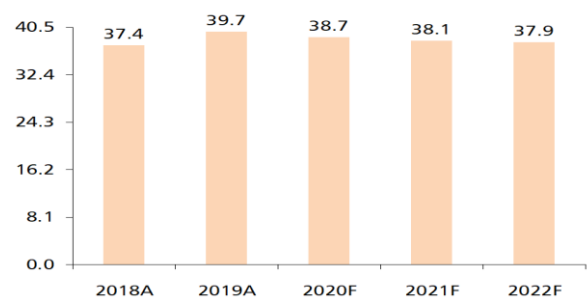
Mobile sub net add (m)



Mobile ARPU (Rmb)



EBITDA margin (%)



Source: Company, DBS HK

China Mobile

Balance Sheet:

Strong cash position. CM's balance sheet is strong with c.Rmb300bn+ net cash as at end-FY19. CM generates very strong operating cash flows of Rmb200bn+ to support its capex and remains free cash flow positive. We expect capex in FY20 to increase by 8% to Rmb180bn. The company targets to maintain absolute dividend per share.

Share Price Drivers:

5G mobile subscriber growth. The company targeted 70m 5G subs by the end of FY20, which implies a monthly net-add of 5-6m 5G subs. The company reports sub numbers every month; lower 5G sub net-adds will be negative for the share price and vice versa.

Higher-than-expected capex budget. For CM to maintain its market share, it may accelerate its 5G network build-out to increase network coverage and quality. This may lead to lower return on investment, limitation on potential dividend hike and share price pressure.

Key Risks:

Faster-than-expected 5G penetration ramp-up (upside risk). 5G service ARPU is higher than 4G. Higher-than-expected 5G penetration will generate higher return on investment.

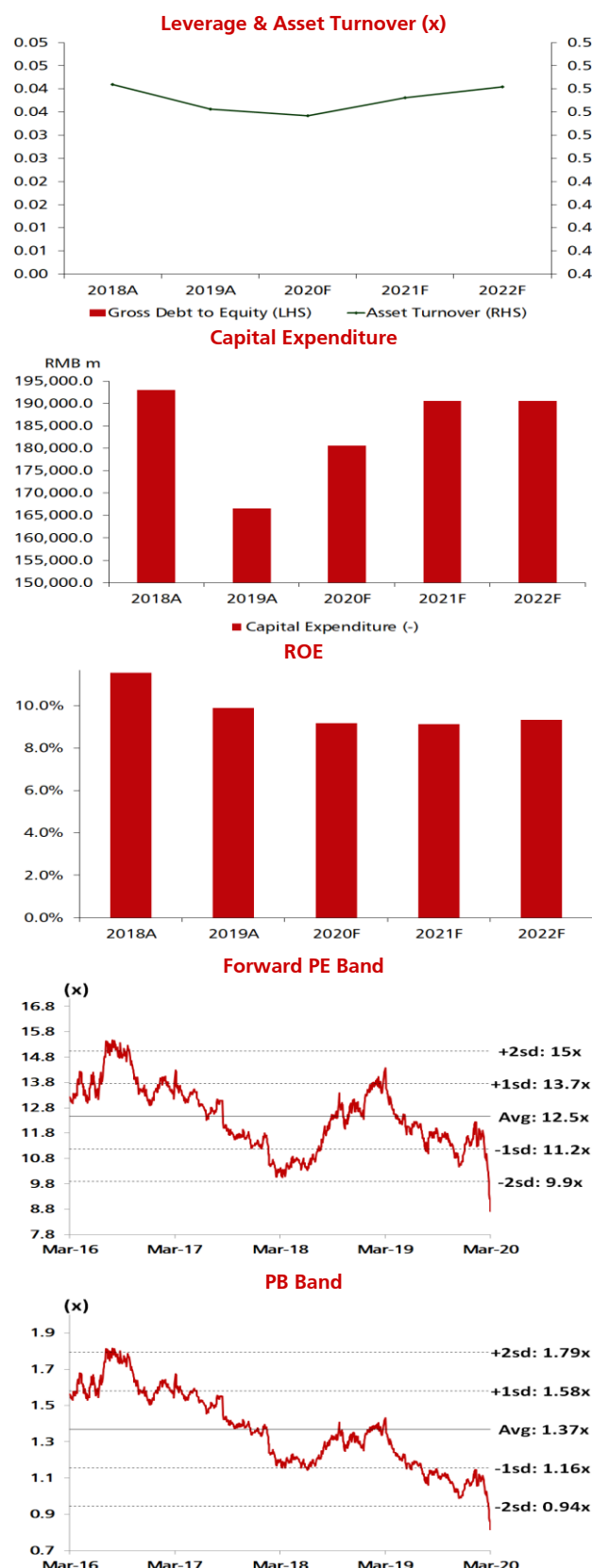
Policy risk (downside risk). China's telecom sector has been subjected to policy risks, such as management reshuffle and tariff cuts. This could be unfavourable for its business performance.

Environmental, Social, Governance:

Some investors are concerned about its state-owned-enterprise background. Policy risks such as speed upgrade with reduction in tariff and industry restructuring could lead to discounts on valuation. The company may also be pressured by the government to invest in 5G networks at a faster pace and larger scale. This will lower the company's network investment return.

Company Background

China Mobile (CM) is the largest mobile operator in Mainland China. It provides 2G services based on GSM technology and provides 3G/4G services based on Chinese-developed TD-SCDMA/TD-LTE technologies. It also operates fixed-line services, after acquiring Tietong.



Source: Company, DBS HK

China Mobile

Key Assumptions

FY Dec	2018A	2019A	2020F	2021F	2022F
Mobile sub net add (m)	37.9	25.2	10.0	10.0	5.0
Mobile ARPU (Rmb)	53.1	49.0	49.1	50.6	52.5
EBITDA margin (%)	37.4	39.7	38.7	38.1	37.9

Source: Company, DBS HK

Income Statement (RMB m)

FY Dec	2018A	2019A	2020F	2021F	2022F
Revenue	736,819	745,917	773,274	807,687	839,533
Cost of Goods Sold	(615,432)	(632,768)	(662,791)	(694,166)	(718,128)
Gross Profit	121,387	113,149	110,483	113,521	121,406
Other Opng (Exp)/Inc	0	0	0	0	0
Operating Profit	121,387	113,149	110,483	113,521	121,406
Other Non Opg (Exp)/Inc	2,906	4,029	4,029	4,029	4,029
Associates & JV Inc	13,861	12,641	12,276	13,027	13,027
Net Interest (Exp)/Inc	15,741	12,314	10,469	11,644	12,927
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	0	0	0	0	0
Pre-tax Profit	153,895	142,133	137,257	142,220	151,388
Tax	(35,944)	(35,342)	(33,765)	(34,986)	(37,242)
Minority Interest	(170)	(150)	(145)	(151)	(160)
Preference Dividend	0	0	0	0	0
Net Profit	117,781	106,641	103,347	107,083	113,986
Net Profit before Except.	117,781	106,641	103,347	107,083	113,986
EBITDA	292,839	313,533	315,864	324,925	335,387

Growth

Revenue Gth (%)	(0.5)	1.2	3.7	4.5	3.9
EBITDA Gth (%)	3.3	7.1	0.7	2.9	3.2
Opg Profit Gth (%)	1.0	(6.8)	(2.4)	2.7	6.9
Net Profit Gth (%)	3.1	(9.5)	(3.1)	3.6	6.4

Margins & Ratio

Gross Margins (%)	16.5	15.2	14.3	14.1	14.5
Opg Profit Margin (%)	16.5	15.2	14.3	14.1	14.5
Net Profit Margin (%)	16.0	14.3	13.4	13.3	13.6
ROAE (%)	11.6	9.9	9.2	9.1	9.3
ROA (%)	7.7	6.7	6.3	6.3	6.5
ROCE (%)	9.1	7.6	7.1	7.1	7.4
Div Payout Ratio (%)	49.1	56.1	57.9	55.9	52.5
Net Interest Cover (x)	NM	NM	NM	NM	NM

Source: Company, DBS HK

China Mobile

Interim Income Statement (RMB m)

FY Dec	2H2017	1H2018	2H2018	1H2019	2H2019
Revenue	351,643	391,832	344,987	389,427	356,490
Cost of Goods Sold	(299,491)	(322,147)	(293,285)	(329,672)	(303,096)
Gross Profit	52,152	69,685	51,702	59,755	53,394
Other Oper. (Exp)/Inc	0	0	0	0	0
Operating Profit	52,152	69,685	51,702	59,755	53,394
Other Non Opg (Exp)/Inc	1,939	751	2,155	1,213	2,816
Associates & JV Inc	4,542	5,747	8,114	6,579	6,062
Net Interest (Exp)/Inc	8,109	8,036	7,705	5,723	6,591
Exceptional Gain/(Loss)	0	0	0	0	0
Pre-tax Profit	66,742	84,219	69,676	73,270	68,863
Tax	(15,055)	(18,477)	(17,467)	(17,151)	(18,191)
Minority Interest	(83)	(101)	(69)	(56)	(94)
Net Profit	51,604	65,641	52,140	56,063	50,578
Net profit bef Except.	51,604	65,641	52,140	56,063	50,578

Growth

Revenue Gth (%)	4.0	0.8	(1.9)	(0.6)	3.3
Opg Profit Gth (%)	0.4	2.5	(0.9)	(14.2)	3.3
Net Profit Gth (%)	7.1	4.7	1.0	(14.6)	(3.0)

Margins

Gross Margins (%)	14.8	17.8	15.0	15.3	15.0
Opg Profit Margins (%)	14.8	17.8	15.0	15.3	15.0
Net Profit Margins (%)	14.7	16.8	15.1	14.4	14.2

Source: Company, DBS HK

Balance Sheet (RMB m)

FY Dec	2018A	2019A	2020F	2021F	2022F
Net Fixed Assets	766,454	770,265	784,085	804,628	824,594
Invts in Associates & JVs	145,325	155,228	163,228	171,228	179,228
Other LT Assets	89,015	173,881	161,647	144,615	124,548
Cash & ST Invts	425,623	421,362	450,726	482,806	522,354
Inventory	8,857	7,338	7,607	7,946	8,259
Debtors	66,083	66,827	69,278	72,361	75,214
Other Current Assets	34,553	34,339	35,319	36,551	37,691
Total Assets	1,535,910	1,629,240	1,671,889	1,720,134	1,771,888
ST Debt	0	0	0	0	0
Creditors	194,068	167,714	173,865	181,603	188,763
Other Current Liab	280,330	294,353	308,494	321,576	322,138
LT Debt	0	0	0	0	0
Other LT Liabilities	5,703	59,884	38,557	18,557	8,249
Shareholder's Equity	1,052,405	1,103,773	1,147,312	1,194,587	1,248,766
Minority Interests	3,404	3,516	3,661	3,812	3,972
Total Cap. & Liab.	1,535,910	1,629,240	1,671,889	1,720,134	1,771,888
Non-Cash Wkg. Capital	(364,905)	(353,563)	(370,156)	(386,321)	(389,737)
Net Cash/(Debt)	425,623	421,362	450,726	482,806	522,354
Debtors Turn (avg days)	30.1	32.5	32.1	32.0	32.1
Creditors Turn (avg days)	170.5	147.0	131.6	129.8	129.7
Inventory Turn (avg days)	7.6	6.6	5.8	5.7	5.7
Asset Turnover (x)	0.5	0.5	0.5	0.5	0.5
Current Ratio (x)	1.1	1.1	1.2	1.2	1.3
Quick Ratio (x)	1.0	1.1	1.1	1.1	1.2
Net Debt/Equity (X)	CASH	CASH	CASH	CASH	CASH
Net Debt/Equity ex MI (X)	CASH	CASH	CASH	CASH	CASH
Capex to Debt (%)	N/A	N/A	N/A	N/A	N/A
Z-Score (X)	2.9	2.6	2.7	2.7	2.8

Source: Company, DBS HK

China Mobile

Cash Flow Statement (RMB m)

FY Dec	2018A	2019A	2020F	2021F	2022F
Pre-Tax Profit	153,895	142,133	137,257	142,220	151,388
Dep. & Amort.	154,621	159,714	163,076	166,348	166,926
Tax Paid	(33,236)	(35,944)	(35,342)	(33,765)	(34,986)
Assoc. & JV Inc/(loss)	(13,861)	(12,641)	(10,000)	(10,000)	(10,000)
(Pft)/ Loss on disposal of FAs	0	0	0	0	0
Chg in Wkg.Cap.	(45,529)	7,459	7,733	8,077	8,395
Other Operating CF	(9,739)	(48,058)	(3,253)	(1,867)	(4,525)
Net Operating CF	206,151	212,664	259,472	271,013	277,198
Capital Exp.(net)	(192,975)	(166,580)	(180,580)	(190,580)	(190,580)
Other Invts.(net)	(27,788)	163,394	0	0	0
Invts in Assoc. & JV	(375)	0	0	0	0
Div from Assoc & JV	691	2,528	2,000	2,000	2,000
Other Investing CF	8,216	(35,270)	10,080	11,255	12,538
Net Investing CF	(212,231)	(35,928)	(168,500)	(177,325)	(176,042)
Div Paid	(59,930)	(54,859)	(59,808)	(59,808)	(59,808)
Chg in Gross Debt	2,262	0	0	0	0
Capital Issues	0	0	0	0	0
Other Financing CF	(152)	(3,246)	(1,800)	(1,800)	(1,800)
Net Financing CF	(57,820)	(58,105)	(61,608)	(61,608)	(61,608)
Currency Adjustments	566	0	0	0	0
Chg in Cash	(63,334)	118,631	29,364	32,080	39,548
Opg CFPS (RMB)	12.29	10.02	12.29	12.84	13.13
Free CFPS (RMB)	0.64	2.25	3.85	3.93	4.23

Source: Company, DBS HK

China Mobile

Target Price & Ratings History



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	10-May-19	HK\$72.75	HK\$94.70	Buy
2:	9-Aug-19	HK\$63.05	HK\$75.00	Buy
3:	3-Jan-20	HK\$65.50	HK\$67.00	Hold

Source: DBS HK

Analyst: Tsz-Wang TAM, CFA

Chris KO CFA,

DBS HK recommendations are based on an Absolute Total Return* Rating system, defined as follows:

STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

**Share price appreciation + dividends*

Completed Date: 19 Mar 2020 18:23:27 (HKT)

Dissemination Date: 19 Mar 2020 18:26:04 (HKT)

Sources for all charts and tables are DBS HK unless otherwise specified.

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DBS Bank (Hong Kong) Limited13th Floor One Island East, 18 Westlands Road, Quarry Bay, Hong Kong

Tel: (852) 3668-4181, Fax: (852) 2521-1812

DBS Regional Research Offices

HONG KONG

DBS Bank (Hong Kong) Ltd

Contact: Carol Wu

13th Floor One Island East,

18 Westlands Road,

Quarry Bay, Hong Kong

Tel: 852 3668 4181

Fax: 852 2521 1812

e-mail: dbsvhk@dbs.com

MALAYSIA

AllianceDBS Research Sdn Bhd

Contact: Wong Ming Tek (128540 U)

19th Floor, Menara Multi-Purpose,

Capital Square,

8 Jalan Munshi Abdullah 50100

Kuala Lumpur, Malaysia.

Tel.: 603 2604 3333

Fax: 603 2604 3921

e-mail: general@alliancedbs.com

SINGAPORE

DBS Bank Ltd

Contact: Janice Chua

12 Marina Boulevard,

Marina Bay Financial Centre Tower 3

Singapore 018982

Tel: 65 6878 8888

Fax: 65 65353 418

e-mail: equityresearch@dbs.com

Company Regn. No. 196800306E

INDONESIA

PT DBS Vickers Sekuritas (Indonesia)

Contact: Maynard Priajaya Arif

DBS Bank Tower

Ciputra World 1, 32/F

Jl. Prof. Dr. Satrio Kav. 3-5

Jakarta 12940, Indonesia

Tel: 62 21 3003 4900

Fax: 6221 3003 4943

e-mail: indonesiaresearch@dbs.com

THAILAND

DBS Vickers Securities (Thailand) Co Ltd

Contact: Chanpen Sirithanarattanakul

989 Siam Piwat Tower Building,

9th, 14th-15th Floor

Rama 1 Road, Pathumwan,

Bangkok Thailand 10330

Tel. 66 2 857 7831

Fax: 66 2 658 1269

e-mail: research@th.dbs.com

Company Regn. No 0105539127012

Securities and Exchange Commission, Thailand