

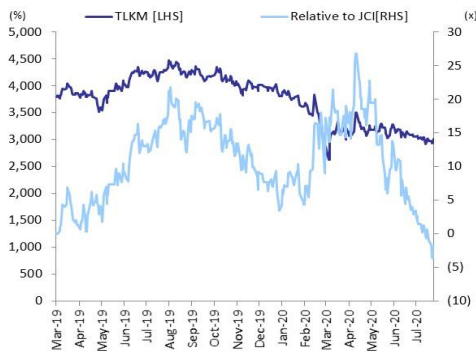
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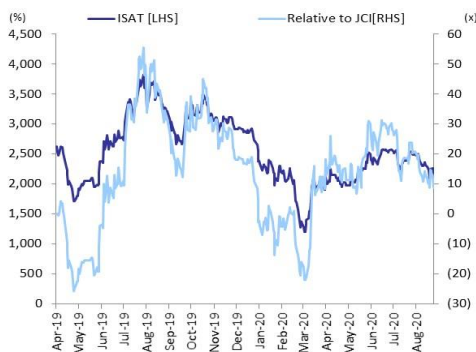
Telco

Takeaways with Hutchison 3 Indonesia: Capacity for more growth in 2H20

TLKM relative to JCI Index



ISAT relative to JCI Index



Source : Bloomberg



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The Vice CEO of Hutch3, Pak Danny, offered another interesting take on the current state of telcos. Hutch3 is said to have capacity to grow market share in several selected areas in ex-Java and east Java and elevate its revenues growth in 2H20. Hutch3 maintains a rather negative view on the school subsidies. Hutch3 reiterates its market commitment to make bid in the upcoming spectrum auction. Erosion of consumer income is a given, may have lasting effects, and is enough to make operators look further at their consolidation options.

Hutch3 sets a high FY20F target. Hutch3 sets the bar high at 18-20%yoy for 2020F topline growth from the 12%yoy growth estimated in 1H20. Hutch3 may adjust due to the aggressiveness of Telkomsel with Unlimited offerings and tap the students' market, but Hutch3 remains committed to its target. Hutch3 says it is imperative to go to market given the availability of capacity in selected areas where they have the coverage.

Ex-Java continues to be a lucrative market. Following the results in 2Q20, Hutch3 picked up pace. The company can do well in Makassar, Manado, Gorontalo, and North Sumatra where they capacity and coverage and be able to take share from the incumbent even of 1%. The ex-Java growth is more upbeat and currently 30% of Hutch3 revenues are coming from ex-Java areas. In the other areas where Hutch's position is at par vs peers, the company will try to improve the yield and ARPU such as Jakarta and Tangerang, taking a constructive view.

Hutch3's negative view on school subsidies. In terms of school subsidies, Hutch 3 said that the first batch may have ended on 15th September, but will be followed by another deadline on the 25th Sept. for those who did not make it in the 1st batch. Hutch also confirms that it rewards students with a one-time 30GB education data bonus by submitting a Hutch 3 number to the Dapodik/Education Ministry. Nonetheless, the CSR and school subsidies are deemed to cause friction rather than being a benefit on 2 fronts. Firstly, the ARPU for Hutch3 students ranges currently from Rp80-100k, (govt. led program bringing it down to around Rp35k), and secondly Hutch3 is forced to sell at below cost. Moreover, Hutch3 asserts that there is a 5GB allocation for school students in the package to access all apps incl. YouTube (15GB for tertiary students). Be that as it may, we still believe there is a grey area given the fact that the Ministry has not yet offered the specifications/allocations of the 35GB pack. 18-20% of Hutch3 subs are students, and it is believed that ~50% of them will register in this govt-led program. As such, there are still several moving variables to determine whether this program is network dilutive and/or ARPU dilutive.

Hutch3 and the 2300MHz spectrum auction. Hutch3 will definitely participate in the upcoming auction to take place by YE20 being the lowest holder of spectrum in Indonesia currently. Hutch3 is still evaluating its options depending on how the govt will set the rules of this auction for 30MHz of spectrum in 2300MHz. The scenario considered on the table now is 3x10MHz, i.e. aiming for 3 winners in this auction. Hutch3 stated that the optimum size for its subs base would be 20MHz, nonetheless would still consider bidding for 10MHz only.

A more Neutral Sectoral View. Our talks with Indosat and Hutch3 make us rethink our sector view and we take a more neutral stance, mainly due to the lasting effects on disposable income for telco services perceived from Covid19.

Company	Ticker	Rec	Target	Market	P/E (x)		P/BV (x)		ROE (%)
			Price (Rp)	Cap. (RpBn)	2020F	2021F	2020F	2021F	2021F
Telkom	TLKM IJ	BUY	3,800	298,177.3	15.3	16.0	3.0	3.0	18.7
Indosat Ooredoo	ISAT IJ	BUY	3,500	11,791.6	n/m	n/m	1.0	1.1	(8.9)
XL Axiata	EXCL IJ	BUY	3,100	27,147.4	64.2	34.0	1.4	1.3	4.0

Hutch3 on fiberization; better wait first. Hutch3 will be more active in fiberizing towers when needed. Fiberization is an important aspect for network performance. Nonetheless we understand that Hutch3 prioritizes first on the return this investment will have in a 7-10yrs scope. Hutch3 thus chooses to delay fiberization where it can, and benefit from lower fiber prices as these come down at a rate of 10-15% annually. As of now, capacity is enough to provide the high throughput as per Hutch3.

Hutch3 and equipment suppliers. On the criticism and potential squeeze of Huawei and other Chinese makers, Hutch 3 does not expect major disruptions, and does not expect Huawei phasing out next year or even in the next 2-3yrs ahead. Chinese makers may not be offering pricing advantages but admittedly the operator enjoys better service/support overall than from European makers, thus in this respect Indo telcos may face some impediments.

Consolidation options considered more than ever. The economic situation is hampered by Covid19, and may take some time to recover from lasting effects on disposable income for telcos. The telco consolidation process may speed up based on this perspective with operators being ***very busy*** evaluating their options with both no.2 and no.3 offering their own unique value in a possible merger with Hutch3.

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