

Is TM paying too much for P1?

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Telekom Malaysia (TM)'s purchase of a 57% stake in struggling company Packet One Networks Malaysia Sdn Bhd (P1) does not make sense to Tiger, whose tail is in a tangle just mulling over the news.

Tiger loves lurking in the shadows, wistfully watching humans in the corporate jungle shopping for good buys. For you see, humans don't allow tigers to wheel and deal in their patch of the jungle. And so Tiger has to resort to watching the action from afar. Call it voyeurism if you must, there's nothing quite like keeping a close eye on the meaty deals in the market.

This is precisely why when news broke that TM was buying a 57% stake in Green Packet Bhd subsidiary P1, Tiger's ears pricked up with interest. So, the "behemoth" was finally easing into the converged space, Tiger thought. And at what cost? (Convergence refers to overlapping of services such as between fixed and mobile. TM is currently involved mainly in fixed line provision, especially fibred and wired broadband.)

Here's the basics of the deal: TM has agreed to buy 57% of P1 for RM350 million and to subscribe to RM210 million of Green Packet's newly issued redeemable exchangeable bonds. The deal is expected to be completed by the third quarter of this year. This brings TM's total investment in the P1 stake to RM560 million.

With P1, TM is gaining two types of spectrum, namely 2.3 gigahertz (Ghz) for WiMAX and 2.6 Ghz for LTE (long term evolution), which complements TM's existing 10 megahertz (MHz) of the 850 MHz band and 8.5 MHz of the 450 MHz band.

However, TM's purchase of the P1 stake has been deemed by some analysts as being too pricey. According to TA Securities, the acquisition translates to FY13 EV/EBITDA multiple of 20x based on P1's enterprise value of RM750mn, far exceeding TM's FY13 EV/EBITDA of 8x. (EBITDA equals to earnings before interest, taxes, depreciation and amortisation while EV is enterprise value which is the market price of debt plus equity).

CIMB Research called the deal expensive because it implies an enterprise value (EV) per subscriber of US\$1,858. This figure is double the EV/subscriber valuation of

Thailand's fixed wireless broadband provider Jasmine of US\$1,010 in 2014 and US\$868 for 2015. "The acquisition price has an 84% premium over Jasmine's valuation and can only be justified if P1's subscriber base grows four-fold," the research house said. (As at end 2013, P1 had 543,000 subscribers, according to TA Securities).

Tiger tends to agree on the priciness of the deal. Although TM has said it wants to be a converged player and can turn around the loss-making P1 in the long-term, Tiger thinks RM560 million is a lot to pay just for spectrum. (In fact, whispers in the jungle are that TM paid a higher price to edge out competitors Digi and YTL who were also said to be eyeing the P1 stake, but Tiger is not one to gossip).

Being the savvy shopper that she is, Tiger wouldn't fork out a cent for a loss-making company, particularly one that is struggling to make money from its WiMAX services. To be sure, Green Packet CEO CC Puan has said that P1 is prioritising rolling out LTE (long term evolution) over its WiMAX services, but the fact remains that P1 is still loss making and it would take TM a considerable amount of time to turn P1 around. (According to the TA Securities report, TM is targeting a time frame of 12 to 36 months to successfully 'stabilise' operations at P1).

LTE is sometimes referred to as 4G and is therefore a higher specifications cellular frequency than 3G. It differs from WiMAX which is basically a long range wireless broadband frequency which is a cheaper alternative to roll-out than fibre in some places where traffic is not so heavy.

So P1's WiMAX service can complement TM in its provision of broadband services especially for mobile devices on the go such as laptops – and not much else. That is its limitation. LTE can be used for things like tablets and smartphones.

Complicating? Yes, it takes quite a bit to understand the whole thing.

The question is not whether TM can afford to bail out P1. It can – having a healthy balance sheet certainly helps. Rather, the matter at hand is the fact that it has taken on the rather expensive task of turning the company around and then rolling out LTE services to become a converged player. This is what TM told analysts.

In the LTE space, TM will be competing with Maxis, Celcom and Digi, who already have LTE offerings and far more mileage in the mobile space than TM. A possible chink in the armour for TM may be the type of LTE spectrum it has via P1, namely TD-LTE, TD standing for time-division. The drawback here is that TD-LTE has been commercially deployed in far fewer markets than FD-LTE (frequency-division). Hence device availability is a problem for TD-LTE, according to Tony Brown, an analyst at Informa Telecoms and Media.

While the specifics of TM's LTE strategy remain unknown, offering TD-LTE services to mobile users in Malaysia simply will not fly in the short term. Seeing that LTE devices are already in short supply, it could take some time before TM is able to scale in the LTE space. In the meantime, the existing mobile operators would have snagged more LTE customers.

For now, TM is holding its cards close to its chest, so it's tough for Tiger to speculate on how successful the former will be with its P1 stake purchase. One thing's for sure, the road ahead will not be easy for TM, what with competition from existing mobile operators.

Tiger will continue to keep an eye on the scene, but in the meantime...

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