Capital Markets Argentina

Communications

TELECOM 2Q19

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Telecom 2Q19

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August 2019

Telecom (BCBA: TECO2)
15/08/19
AR$ 125,45/ US$10,95

Target Price: AR$ 133,62
Expected Return (AR$): 6,5 %
Market Performer

PricesRange(in AR$)

Lowest in 52 Weeks	**Highest in 52 Weeks**
100	**157,95**

TECO2BA and MERVAL Index: % changes

Source: Yahoo Finance

TECO2BA and S&P500 % changes

Source: YahooFinance

	Revenues (AR$ mill)	EBITDA (AR$ mill)	Net Profit (AR$ mill)	EV/ EBITDA (x)	P/BV (X)	P/E (x)	EPS (AR$)
2018	168.046	56.368	5.294	6,20	1,19	50,28	2,50
2019E	171.407	58.278	12.795	5,83	1.46	20.47	5,90
2020E	185.119	62.941	20.020	5,93	1.60	14,00	9,23

Shares Outstanding	2.154.000
ADRsOutstanding	434.000
MarketCapitalization($mill)	283.251
Net debt ($mill)	75.268
FirmValue ($mill)	358.519

TELECOM: PRIVATE CONSUMPTION STILLS HURTS SALES

- Quarterly sales fell 14.0% in real terms from a year ago, in line with our projections, which contemplate recessionary conditions until the third quarter of the year.
- Even though the Telecommunications industry and the firm were less affected by the recessionary situation that started in June 2018, than other more cyclical industries, like Construction (see Annexe 1), this quarter´s sales drop was higer than industry and general activity figures.
- The reason behind the drop in sales during 2Q19 is that the recession continued to affect disposable income after taxes and tariffs, and that TELECOM is applying an aggressive price strategy, with important promotions that last a year. This combined with high inflation, affects revenues in real terms. On the other hand, operating costs continue to decrease due to the merger synergies, but less than proportionally (8,8% y/y).
- The different dynamic of revenues and costs produce lower profitability (ARPUs or Average Return per User) in the different business segments as follows:

SEGMENT	ARPU	% Change y/y
Mobile Services	$341,2	-0,5
Internet	$867,4	-11,4
Cable TV	$914,8	-16,2
Fixed and Data	$246,5	-10,6

- Consequently, Telecom Argentina has worsened its consolidated operating margin during 2Q19 compared to same quarter of last year. However EBITDA improved q/q and y/y and net margin increased considerably from -24,9% to +11,52% y/y. The reasons were the important foreign exchange losses of 2Q18, against the foreign exchange gains of this quarter. The last two years and a half quarterly profitability ratios were as follow:

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	2T19 (1)	1T19 (1)	4T18	3T18	2T18	1T18 (1)	4T17	3T17	2T17	1T17
EBITDA margin	34,60%	32,70%	29,68%	33,70%	33,80%	37,80%	29,70%	29,90%	33,50%	32,50%
Operating margin	9,60%	10,14%	28,12%	20,10%	15,38%	20,40%	17,20%	18,00%	18,10%	19,60%
Net Margin	11,52%	2,89%	20,99%	-38,70%	-24,90%	23,40%	11,30%	12,30%	10,60%	13,30%

(1) Adjusted for inflation.

Total loans stock remained at US$ 2.282 million.

Net Debt amounts to AR$ 75.268 in June 30 2019.

Net Debt/EBITDA went from 1,23x to 1,21x q/q.

Furthermore, the firm improved its debts maturity schedule. Of total debt, 10% matures in 2019, 16% in 2020, 40% in 2021 and 34% matures after 2022.

QUARTER RELEVANT FACTS:

In July, the firm issued 7-year corporate bonds for US$ 400 million with a 8% rate which replaces a US$250 million issue expiring in 2021.

In May, 2018 dividends were distributed and stockholders received ARS 2.92 per share and AR$14.63 per ADR.

PROSPECTS:

If political risk does not complicate activity and inflation, the firm, which depends mainly on private consumption, should increase its revenues as a consequence of a recomposition of household income, as this variable becomes a policy priority and as long as inflation decreases. On the other hand, the firm should also benefit from higher costs savings due to the merger´s synergies. The firm leads its business segment and has a CAPEX that can be slowed down if adjustments are required.

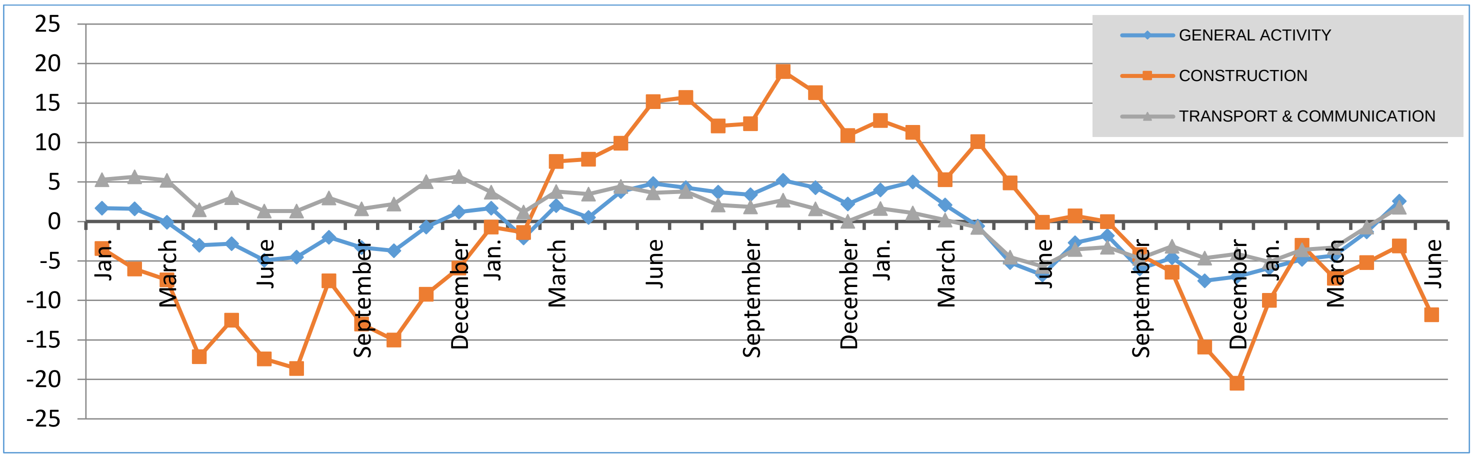
STOCK VALUATION:

Telecom´s stock was less volatile than its peers y-t-d (see Annexe 1 for comparison with the cement firm, Loma Negra, and the Merval S&P Index). Even considering the drop after the Primaries of August 11, the stock quotes 5% higher than the beginning of the year, while the MERVAL S&P lost 5% in the same period.
The target price is calculated with the Discounted Cash Flow Method (DCF). As this method includes country risk, we consider a country risk of 700 points and a long-term growth of 3%, we obtain a target price of AR$ 133,62. In this case, our rating is Market Performer.

ANNEXES:

ANNEXE1-

1-A- GDP, CONGTRUCTION and TRANSPORT and COMMUNICATION GROWTH:



Source: Indec.

1-B- TECO2 STOCK PRICES COMPARED TO LOMA NEGRA BA STOCK PRICES AND MERVAL INDEX Jan19-Aug19 (in % change)

Source: Yahoo Finance

ANNEXE 2:

CASH FLOW PROJECTIONS

	RESULTS ajusted for INFLATION		PROJECTIONS		
	2017 ajus.	2018 ajus.	2019E	2020E	2021E
Total revenues	172.354	168.046	171.407	185.119	199.929
Operating Costs & Expenses		111.678	113.129	122.179	131.953
EBITDA	**54.598**	**56.368**	**58.278**	**62.941**	**67.976**
EBITDA Margin %	31,7%	33,5%	34,0%	34,0%	34,0%
Depreciations	9.804	35.100	-30.000	-31.500	-33.075
Operating Profit	**14.309**	**21.257**	**28.278**	**31.441**	**34.901**
Operating Margin %	8,3%	12,65%	16,50%	16,98%	17,46%
Financial Results	713	-18.795	-10.000	-2.000	2.000
Profit before Taxes	**15.022**	**2.462**	**18.278**	**29.441**	**36.901**
Taxes	-5.516	2.838	-5.484	-9.421	-11.808
Non Controlling Participation	0	0	0	0	
Net Profit	**9.506**	**5.300**	**12.795**	**20.020**	**25.093**
Net Margin %	5,52%	3,15%	7,46%	10,81%	12,55%
Depreciations	9.804	35.100	30.000	31.500	33.075
Interests	828	1.864	2.000	1.859	2.000
CAPEX	-25.000	-45.000	-32.000	-39.000	-39.000
Working Capital	19.958	11.963	5.550	6.150	7.500
FCFF		**9.227**	**18.345**	**20.529**	**28.668**

ASSUMPTIONS (Averages)	
Country Risk	7%
Risk Free Rate	2,95%
Excess return	4%
Beta	0,95
Cost of Equity	12%
Cost of Debt	10%
WACC	11,50%

Source: Based on the firms´Financial Statements

ANNEXE 3:

FINANCIAL DATA and RATIOS:

ANNUAL FINANCIAL DATA AND RATIOS				QUARTERLY					
	2016	2017	2018 (A)	1Q18 (A)	1Q19 (A)	1Q18 (A)	1Q19 (A)	2Q18 (A)	2Q19 (A)
RENTABILITY									
EBITDA %	33,4%	31,7%	33,5%	37,80	32,70	33,80	34,60	33,80	34,60
OPERATING PROFIT	20,4%	10,3%	12,6%	20,40	10,14	19,50	9,60	19,50	9,60
NET PROFIT	17,5%	8,6%	3,3%	23,40	2,89	-24,90	11,52	-24,90	11,52
RENTABILITY OVER ASSETS (ROA)	15,8%	15,9%	5,8%	4,43	3,46	1,82	0,97	1,82	0,97
RENTABILITY OVER EQUITY (ROE)	21,6%	18,0%	2,2%	7,20	5,64	2,95	1,60	2,95	1,60
						-3,89		-3,89	
CURRENT LIQUIDITY		0,60	0,60	0,63	0,73	0,47	0,63	0,47	0,63
INDEBTEDNESS									
Total Indebtedness over Equity(Total Liabilities/Equity)		70,0%	60,0%	62,40	63,31	90,14	63,29	90,14	63,29
Net Debt/EBITDA		18,0%	116,0%	0,7 x	1,23x		1,20X		1,20X
Short Term Loans/Total Loans		25,3%	8,6%	25,27	21,57	55,6%	25,8%	55,6%	25,8%

Source: Based on the firms´Financial Statements

(A) Adjusted for inflation.

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