

Can **Philippine's** **second-largest Telco** **company** PLDT regain its lost market share?

CASE  STUDY
VALUATION MASTER CLASS
by
A. Stoltz INVESTMENT
RESEARCH



Valuation Master Class



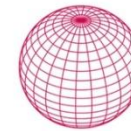
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Ask
Ajarn
Andrew

Can Philippine's second-largest Telco company PLDT regain its lost market share?



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Sector: Comm. Serv.



Philippines' second-largest mobile network operator with a total mobile subscriber base of 71m, equaling around 46% market share

My value estimate:

PHP2,302

(Upside 22%)

BUY



3 things to know about this company

- ★ Broadband expansion unlocks growth, but is competitive
- ★ Superior network quality helps to defend market share
- ★ Ancillary businesses are important in the long-term

Key statistics

Analyst consensus (12)

PHP1,888

(Upside 0%)

HOLD

PE ratio

13x

Dividend yield

4.1%



Sales

Story

FVMR

Value

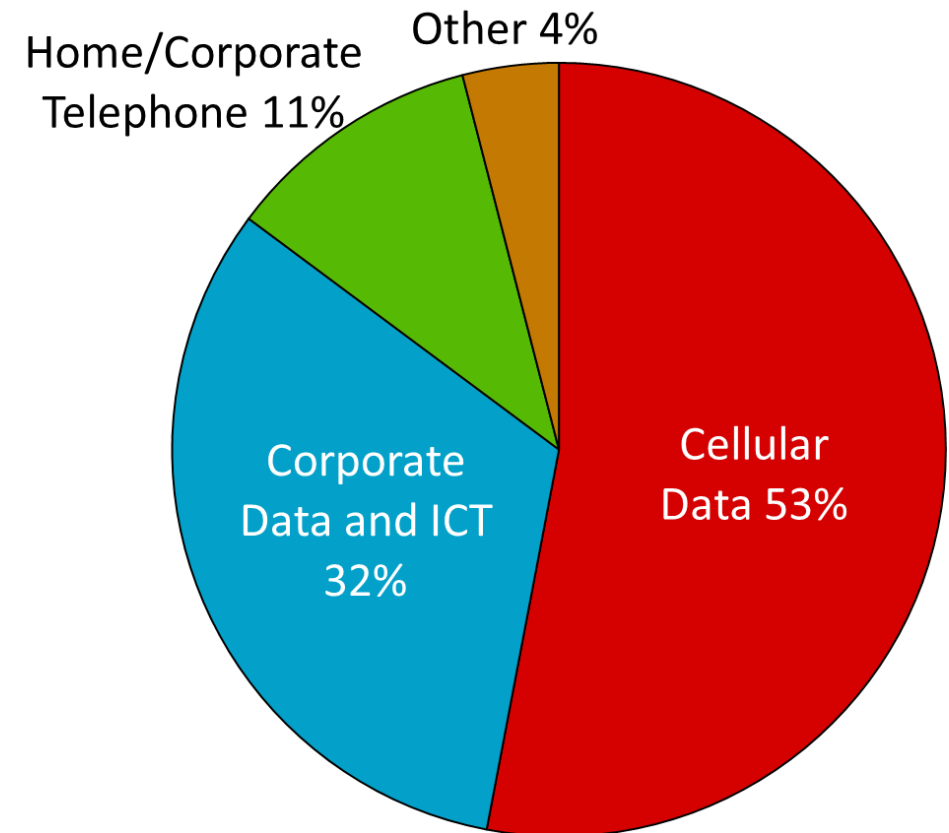
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Risks

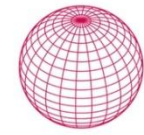
Wireless services 56%



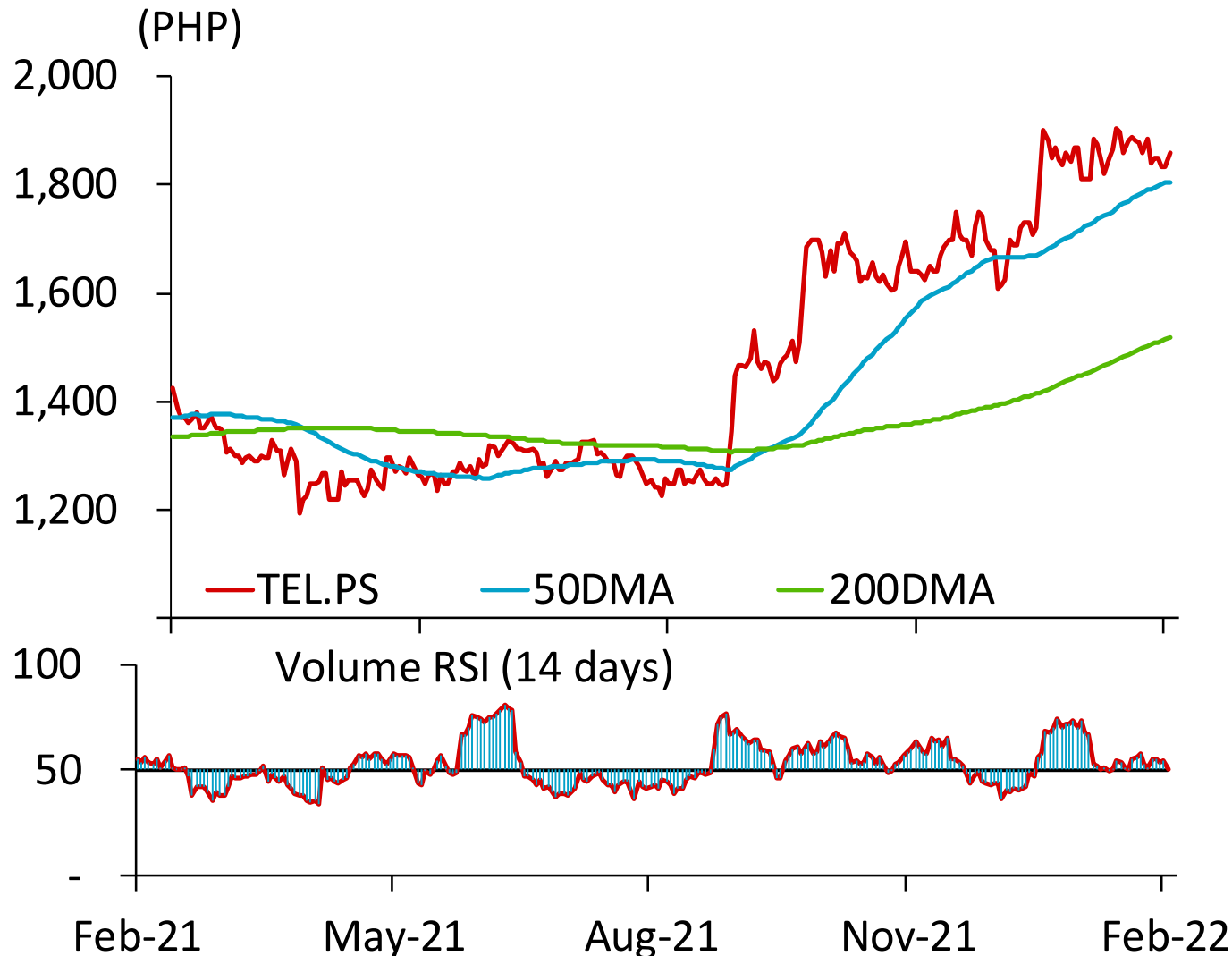
Fixed line services 44%



Price and volume remain bullish

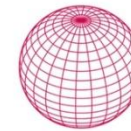


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- ★ In 2H21, PLDT saw a massive 50%+ share price increase
 - The increase is mainly attributable to positive news about its latest fintech investments PayMaya and soon-to-launch digital bank Maya
- ★ Price signal remains strong as 50DMA is well above the 200DMA
- ★ Volume RSI has been strong recently; hence, still providing good support

1 Broadband expansion unlocks growth, but is competitive



Sales

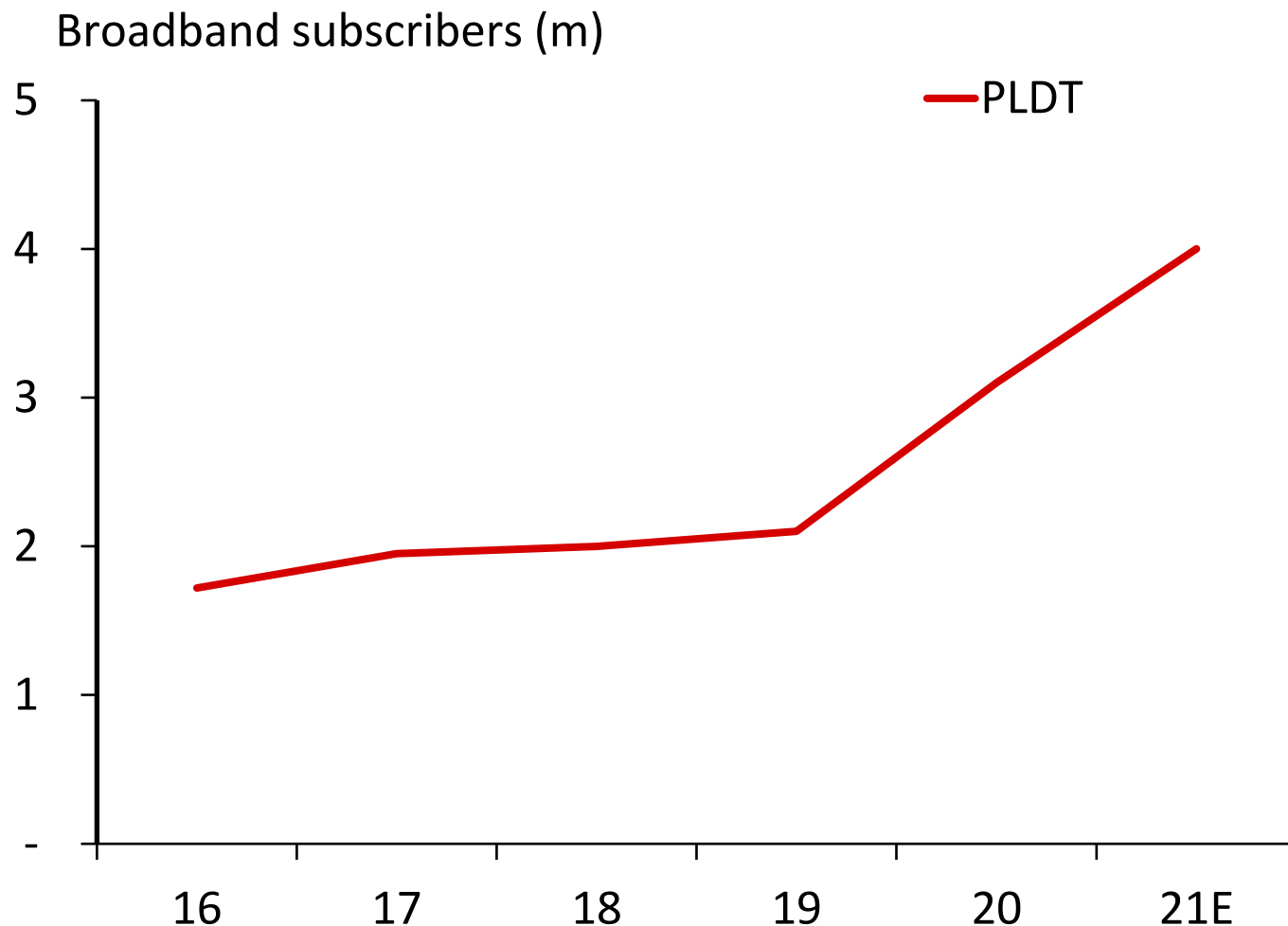
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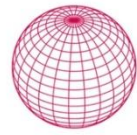
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Risks



- ★ While the mobile market in the Philippines is already quite mature, PLDT sees good growth prospects for home broadband
 - **The pandemic triggered increased demand for fast internet connectivity at home**
- ★ Hence, PLDT engaged in an extensive fiber optics rollout which currently passes 13m homes, providing strong growth opportunities

Its closest competitor accelerated its rollout as well



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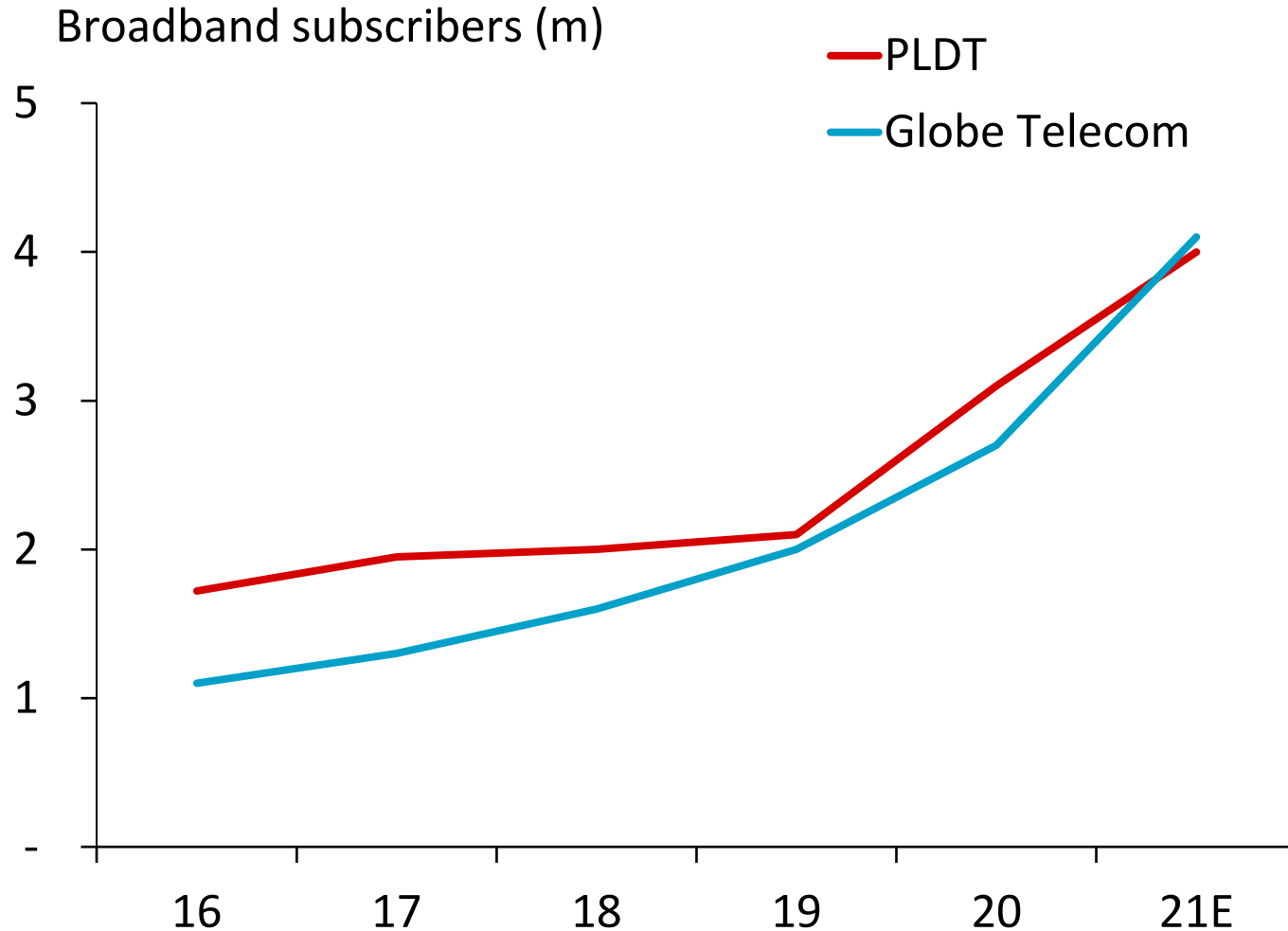
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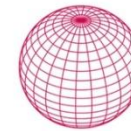
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Risks



- ★ PLDT has started much earlier with its fiber optics rollout than its main competitor Globe
- ★ However, during the past 3 years, Globe saw an exponential growth attributable to its high CAPEX allocated to broadband
 - In 21E, Globe might surpass PLDT for the first time in terms of total broadband subscribers

2 Superior network quality helps to defend market share



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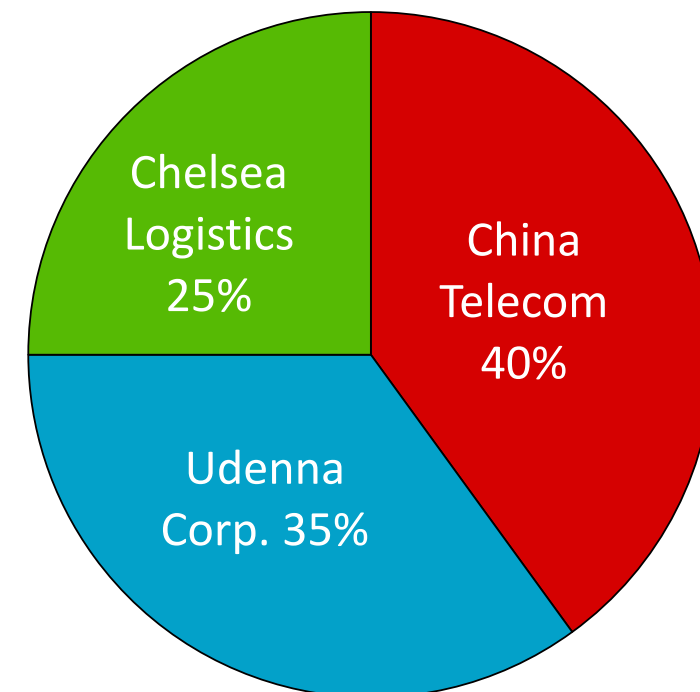
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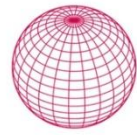
Risks

- ★ In March 2021, the China-backed company Dito started its commercial operations and challenges the duopoly
 - Throughout the past year, it already acquired 5.3m subscribers
 - Annual CAPEX of more than PHP50bn to expand network coverage fast
- ★ For 2022, Dito targets to double its subscriber base to 12m, which means it could steal subscribers from PLDT

Dito consortium



PLDT offers the fastest internet connectivity in the Philippines



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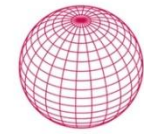
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Risks

Report published by OpenSignal.com about Mobile Network Experience (100-point scale)

	Dito	Globe	PLDT
Video experience (0-100 pts)	51	55.5	61.6
Games experience (0-100 pts)	40.7	37.7	49.2
Voice app experience (0-100 pts)	70.9	69	74.6
Download Speed experience (mbps)	10.4	10.7	20.7
4G availability (% of time)	97.5	84.6	86.5
4G coverage (0-10 pts)	3	7.2	7.5
Mobile subscribers (m)	5.3	76.6	70.5

- ★ PLDT continues to defend its dominant position in terms of network quality
 - The download speed is almost 2 times faster than both of its competitors
- ★ Maintaining a superior quality is necessary to avoid losing customers in a mature market
 - Hence, I believe that PLDT can withstand price pressures from Dito in the near-term future



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Risks

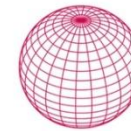
★ Through its investment in Voyager, PLDT offers the mobile payment solution and e-wallet “PayMaya”

- With 41m registrations, it is the second-largest e-wallet in the Philippines (Globe’s GCash has 51m users)

★ The e-wallet business still produces annual losses of PHP2bn+, providing a drag on profits in the short run

- However, the investment could pay off big in the future





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Risks

- ★ PLDT also tries to grow its data segment by investing in value-added content services such as Pay TV
 - The most prominent one is Signal TV, part of PLDT's investment in MediaQuest
 - Signal TV has 3.7m subscribers as of 3Q21
- ★ It allows PLDT to create attractive bundle offers of mobile, fixed-line and TV packages
 - I believe that complimentary services like this are going to be important to realize growth in a mature market





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What Is Liabilities To Assets Ratio?



What Is Growth Year Over Year?

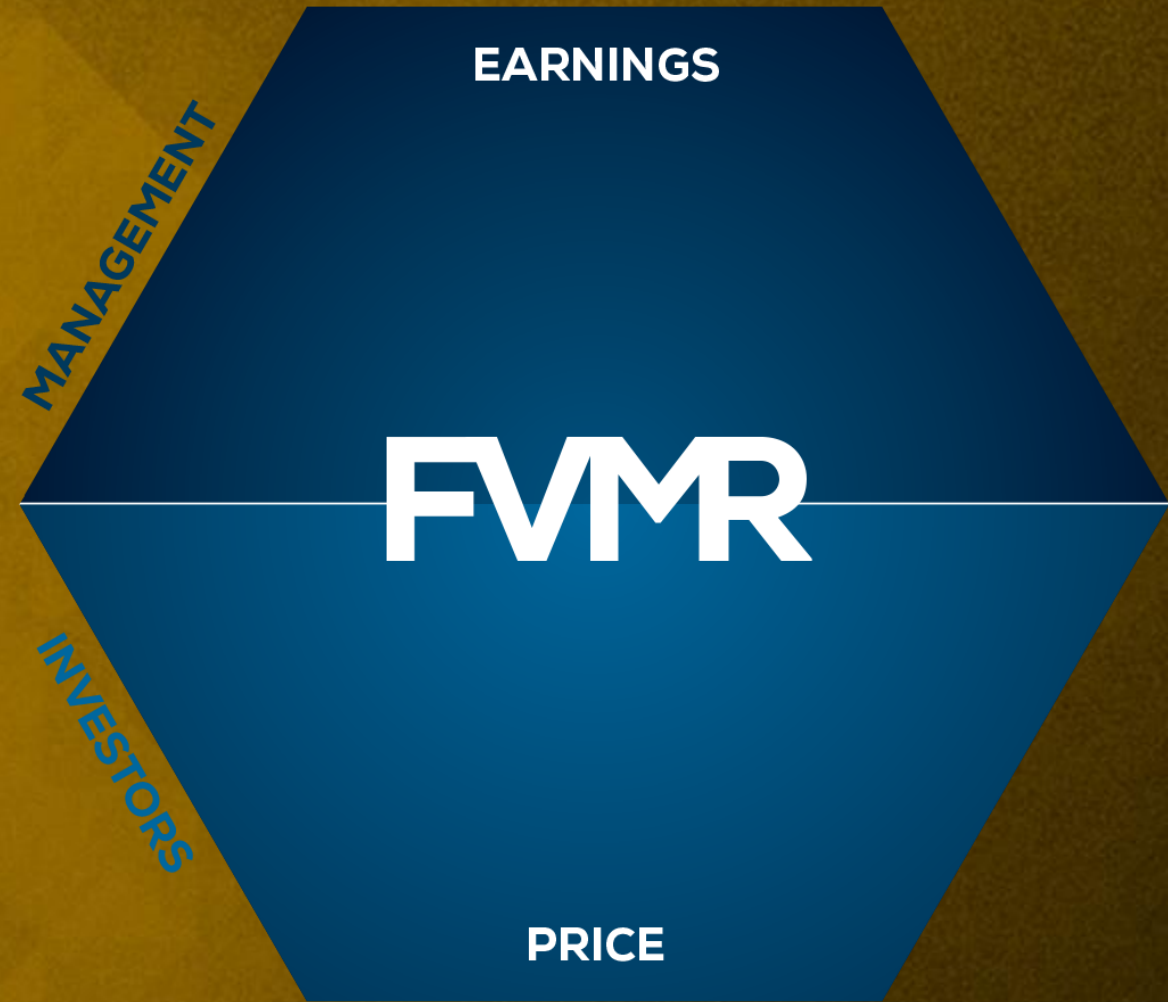
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FVMR Scorecard

- ★ Measures a stock's attractiveness relative to all other companies
- ★ Attractiveness is based on four elements
 - Fundamentals, Valuation, Momentum, and Risk
- ★ Scale from 1 (Best) to 10 (Worst)



Strong fundamentals ride momentum



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Fundamentals



(%)	Dec-17	Dec-18	Dec-19	Dec-20	PTM**
Operating profit margin	8.7	9.1	22.7	21.3	23.8
Recurring net margin	10.8	5.6	13.1	13.7	13.8
Asset turnover	34.2	35.0	33.6	32.9	33.0
Return on assets	3.7	2.0	4.4	4.5	4.5
Recurring return on equity	16.0	8.4	19.8	21.8	23.2

Valuation



(x)	Dec-17	Dec-18	Dec-19	Dec-20	PTM**
Price-to-sales	2.0	1.5	1.4	1.5	1.8
Price-to-earnings	18.4	27.0	11.0	10.6	13.3
Price-to-book	3.0	2.2	2.2	2.3	3.1
PE-to-EPS growth (PEG)	nm	nm	0.1	0.9	2.3
EV/EBIT	27.4	24.8	11.5	12.8	12.9

Momentum



(%)	Dec-17	Dec-18	Dec-19	Dec-20	PTM**
Revenue growth	(3.2)	3.0	2.7	7.0	7.7
Recurring EPS growth	(26.5)	(46.5)	140.4	12.0	5.7
Operating profit margin chg. (bps)	(609)	36	1,362	(137)	(57)
	6mth	3mth	1mth	3wk	1wk
Price change	22.4	10.2	0.1	(4.4)	(4.4)

Risk

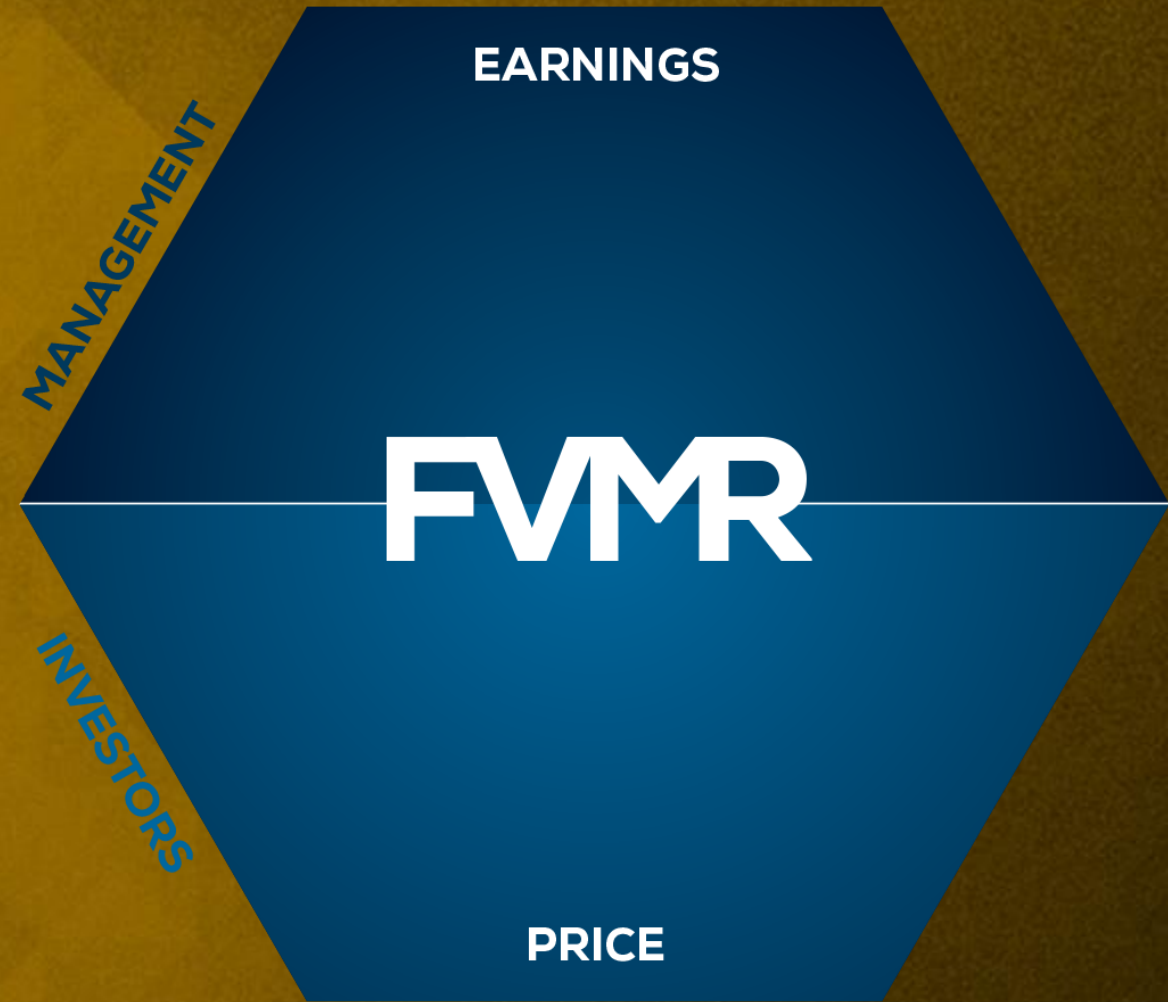


(x)	Dec-17	Dec-18	Dec-19	Dec-20	PTM**
Current ratio	0.5	0.5	0.4	0.4	0.3
Net debt-to-equity (%)	134.2	106.5	159.0	172.4	197.7
Times-interest-earned	1.7	1.8	3.9	3.3	3.9
	5yr	3yr	1yr	6mth	3mth
Beta	0.6	0.5	0.5	0.5	0.7

Note: Benchmarking against 120 non-financial companies in Philippines.

Recently, I created a short
online course explaining my
FVMR investing approach

I usually sell it
for \$97 but for
a limited time
I am offering
it for FREE



Consensus don't see further upside



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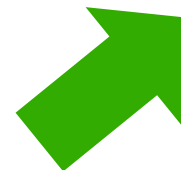
Risks

Analyst consensus valuation

Recommendation	Oct-21	Nov-21	Dec-21	Current
Strong buy	4	4	4	4
Buy	4	5	7	7
Hold	3	3	2	2
Sell	1	1	1	1
Strong sell	-	-	-	-
Average score	2.1	2.1	2.0	2.0

Price target	Oct-21	Nov-21	Dec-21	Current
Median	1,700	1,750	1,875	1,890
Mean	1,634	1,724	1,906	1,946

14
analysts



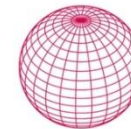
Upside: 0%

Analyst consensus 3-year forecast

(%)	18	19	20	21E	22E	23E
Revenue growth	2.5	2.7	7.0	8.0	6.2	4.8
Gross margin	57.6	66.0	64.4	na	na	na
EBIT margin	10.7	24.0	22.0	21.4	20.9	21.0
Net margin	11.5	13.3	13.4	14.3	13.4	13.2

- ★ The majority analysts has a BUY recommendation, but upside is already captured by recent price rally
- ★ Consensus expects solid single-digit revenue growth for the future
 - Also, margins are expected to stay stable

Profit & loss statement



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(YE Dec, PHP m)	2019A	2020A	2021E	2022E
Revenue	169,187	181,004	194,579	204,308
Cost of goods & services	(57,481)	(64,416)	(69,076)	(74,573)
Gross profit	111,706	116,588	125,504	129,736
SG&A	(70,789)	(75,751)	(80,750)	(85,809)
Other operating (exp)/inc	(378)	(1,090)	(654)	(667)
EBIT	40,539	39,747	44,099	43,259
Interest expense (net)	(6,713)	(8,797)	(9,274)	(10,444)
Other non-operating inc/(exp)	1,440	5,617	2,809	2,865
Earnings before taxes (EBT)	35,266	36,567	37,633	35,680
Income tax	(9,550)	(8,441)	(8,656)	(8,206)
Earnings after taxes (EAT)	25,716	28,126	28,978	27,473
Equity income/Minority interest	(1,800)	(2,624)	(1,466)	236
Earnings from cont. operations	23,916	25,502	27,512	27,709
Forex/Exceptionals before tax	(1,395)	(1,218)	-	-
Net profit	22,521	24,284	27,512	27,709

★ Its investment in the e-wallet PayMaya is still not profitable yet but could start deliver profits in 22E

- Over time, it could evolve to a serious profit contributor



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Risks

(YE Dec, PHP m)	2019A	2020A	2021E	2022E
Cash & short-term investments	35,676	48,566	38,916	30,646
Accounts receivable	24,433	23,852	24,322	25,539
Inventories	3,412	4,085	4,413	4,764
Other current assets	12,056	10,935	15,566	16,345
Total current assets	75,577	87,438	83,218	77,294
Long-term investments	59,380	56,571	57,240	57,812
Net fixed assets	248,802	280,066	327,383	376,306
Intangible assets	6,446	3,950	2,517	1,083
Goodwill	61,379	61,379	61,379	61,379
Other long-term assets	73,443	86,442	99,408	100,402
Total assets	525,027	575,846	631,144	674,277

- ★ Heavy CAPEX required to expand broadband and 5G coverage to defend market share

Balance sheet - liabilities



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(YE Dec, PHP m)	2019A	2020A	2021E	2022E
Overdrafts & short-term loans	22,937	21,613	21,866	25,096
Accounts payable	158,891	169,352	178,445	192,646
Other current liabilities	22,620	22,572	27,241	28,603
Total current liabilities	204,448	213,537	227,553	246,345
Long-term debt	185,934	221,177	251,045	263,597
Other long-term liabilities	18,355	21,467	22,111	22,774
Total liabilities	408,737	456,181	500,708	532,716
Minority interest	4,303	4,257	4,591	4,928
Paid-up capital - Common shares	131,405	131,405	131,405	131,405
Paid-up capital - Preferred shares	510	510	510	510
Retained earnings	18,063	25,652	36,089	46,876
Revaluation/Forex/Others	(37,991)	(42,159)	(42,159)	(42,159)
Total equity	111,987	115,408	125,845	136,632
Total liab & shareholders' equity	525,027	575,846	631,144	674,277

- ★ Issuance of long-term debt necessary to fund expansion
 - Operating cash flows are not sufficient to fund growth internally yet



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(YE Dec)	2019A	2020A	2021E	2022E
General growth (YoY, %)				
Revenue	2.7	7.0	7.5	5.0
Assets	8.8	9.7	9.6	6.8
Gross profit	17.8	4.4	7.6	3.4
Operating profit	130.1	(2.0)	10.9	(1.9)
Attributable profit	19.1	7.8	13.3	0.7
EPS	19.1	7.8	13.3	0.7
Recurring EPS	128.6	7.2	9.1	0.7
Du Pont analysis (%)				
Net profit margin	13.3	13.4	14.1	13.6
Revenue per PHP100 of assets	33.6	32.9	32.2	31.3
Assets/equity (x)	4.5	4.9	5.1	5.0
Return on equity	20.2	21.6	23.1	21.2
Others (%)				
Effective tax rate	28.2	23.9	23.0	23.0
Dividend payout ratio	68.8	67.2	62.0	61.0

★ Dividend payout is high which means it could continue to deliver a solid dividend yield of 4%+



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(YE Dec)	2019A	2020A	2021E	2022E
Internal liquidity (x)				
Current ratio	0.4	0.4	0.4	0.3
Quick, or acid test ratio	0.4	0.4	0.3	0.3
Working cap. mgmt (Days)				
Inventory conversion period	20	21	22	22
Receivables collection period	55	48	45	44
Days from raw mat to coll	74	69	67	66
Payables deferral period	974	917	906	896
Cash conversion cycle	(900)	(848)	(840)	(830)
Profitability ratios (%)				
Gross profit margin	66.0	64.4	64.5	63.5
EBIT margin	24.0	22.0	22.7	21.2
EBIT return on avg assets	8.0	7.2	7.3	6.6
Return on average assets	4.5	4.4	4.6	4.2
Financial risk (x)				
Liabilities-to-assets (%)	77.9	79.2	79.3	79.0
Debt-to-equity	1.9	2.1	2.2	2.1
Net debt-to-equity	1.6	1.7	1.9	1.9
Times-interest-earned	9.6	9.0	9.5	9.1
Effective interest rate (%)	4.4	4.4	4.0	4.0

- ★ Leverage slightly increased over time
 - However, I don't expect it to grow much further

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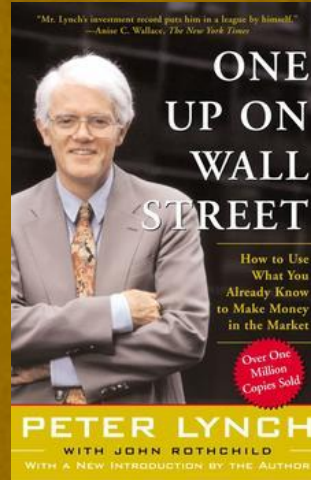


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A. Stotz Investment Research Stock Picking Checklist

Inspired by

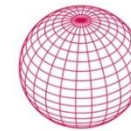
Peter Lynch's book



- ★ Where he talked about "ten baggers", stocks that go up 10x
- ★ We did extensive research on ten baggers and found...
- ★ 9 factors that drive long-term share price performance

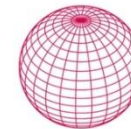


Long-term share price performance potential



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	A. Stotz Investment Research Stock Picking Checklist	Potential	Comment	Good / Moderate / Weak
Sales	1. Management – Management has a proven commitment to growth	Moderate	In 2017, PLDT lost its market-leading position to Globe; 5-year revenue CAGR was only 2%	
Story	2. Growth – Product and industry can support a decade of 10%+ annual growth	Moderate	Mobile penetration is high, but broadband and fintech investment could unlock growth	
FVMR	3. Sustainable – Competitive strategy creates sustainably high gross margin	Moderate	Market is with 3 players concentrated; however, new entrant Dito could start a price war	
WCB	4. Quality – Good earnings quality, non-core items are small or non-existent	Moderate	High fluctuations due to non-core items; but net profit has been consistently positive	
Ratios	5. Efficiency – In the long run sales grow faster than assets	Weak	Heavy fixed investments required to grow; asset turnover is with 30% very low	
Value	6. Tight – Relatively low cash conversion cycle, negative is best	Good	Cash conversion is negative	
	7. Cash flow – Operating cash flow is consistently positive	Moderate	Consistent operating cash flows, but were not always sufficient to cover high investing outflows	
Risks	8. Capacity – Company has access to capital to fund growth	Weak	Leverage significantly increased	
	9. Inexpensive – Valuation is reasonable, avoid very expensive stocks	Moderate	Trades slightly lower on both 21E PE and PB compared to Philippine Telecoms, but higher ROE	



Sales

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Risks

(YE Dec, PHP m)	2019A	2020A	2021E	2022E
EBIT	40,539	39,747	44,099	43,259
Est tax rate (%)	28	24	23	23
NOPAT	29,109	30,256	33,956	33,310
Add: Depre & amort	40,414	49,976	53,282	58,467
Less: CAPEX	(89,611)	(72,270)	(69,166)	(75,957)
Chg in A/R	2,428	581	(470)	(1,216)
Chg in inventory	(534)	(673)	(328)	(351)
Chg in oth curr assets	(3,652)	1,121	(4,631)	(778)
Chg in A/P	6,668	10,461	9,093	14,200
Chg in oth curr liabs	2,676	(48)	4,669	1,362
Less: Chg in working cap	7,586	11,442	8,333	13,217
Less: Chg in invest cap				
Free cash flow to firm	(12,502)	19,404	26,406	29,036

- ★ Negative FCFF in 2019 likely to be an exemption
 - I expect stable and growing FCFF from 21E onward



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Forecast assumptions

3-year average	Consensus	My assumptions
Revenue growth (CAGR)	6.3	6.0
Gross margin	na	63.8
EBIT margin	21.1	21.7
Net margin	13.6	13.8

My valuation method

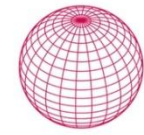
Market: Philippines

Market risk-free rate	5.0
Market equity risk premium	8.0
Market return	13.0
Company beta (x)	0.8
COE	11.0

WACC	7.7
Terminal growth rate	2.0

Valuation Method:
FCFF

- ★ Similar to consensus, I expect stable revenue growth over the next few years
 - I am a bit more optimistic on margins as I expect the third competitor Dito will not be able to scale fast enough and achieve similar network quality
- ★ Over the long run, I assume PLDT to grow in line with population growth, which is around 2%



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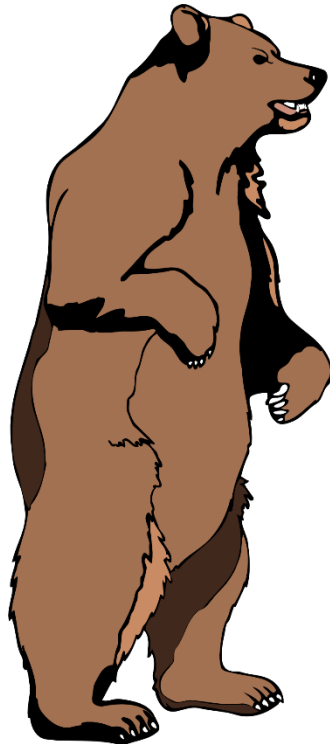
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Ratios

Value

Risks

Bear
PHP2,195
(Upside 16%)



Base
PHP2,302
(Upside 22%)



Bull
PHP2,410
(Upside 28%)



World Class Benchmarking Scorecard

- ★ We identify a company's competitive position relative to global peers
- ★ We use a composite rank of profitability and growth, called "Profitable Growth"
- ★ Scale from 1 (Best) to 10 (Worst)



Average profitability but volatile growth



Sales

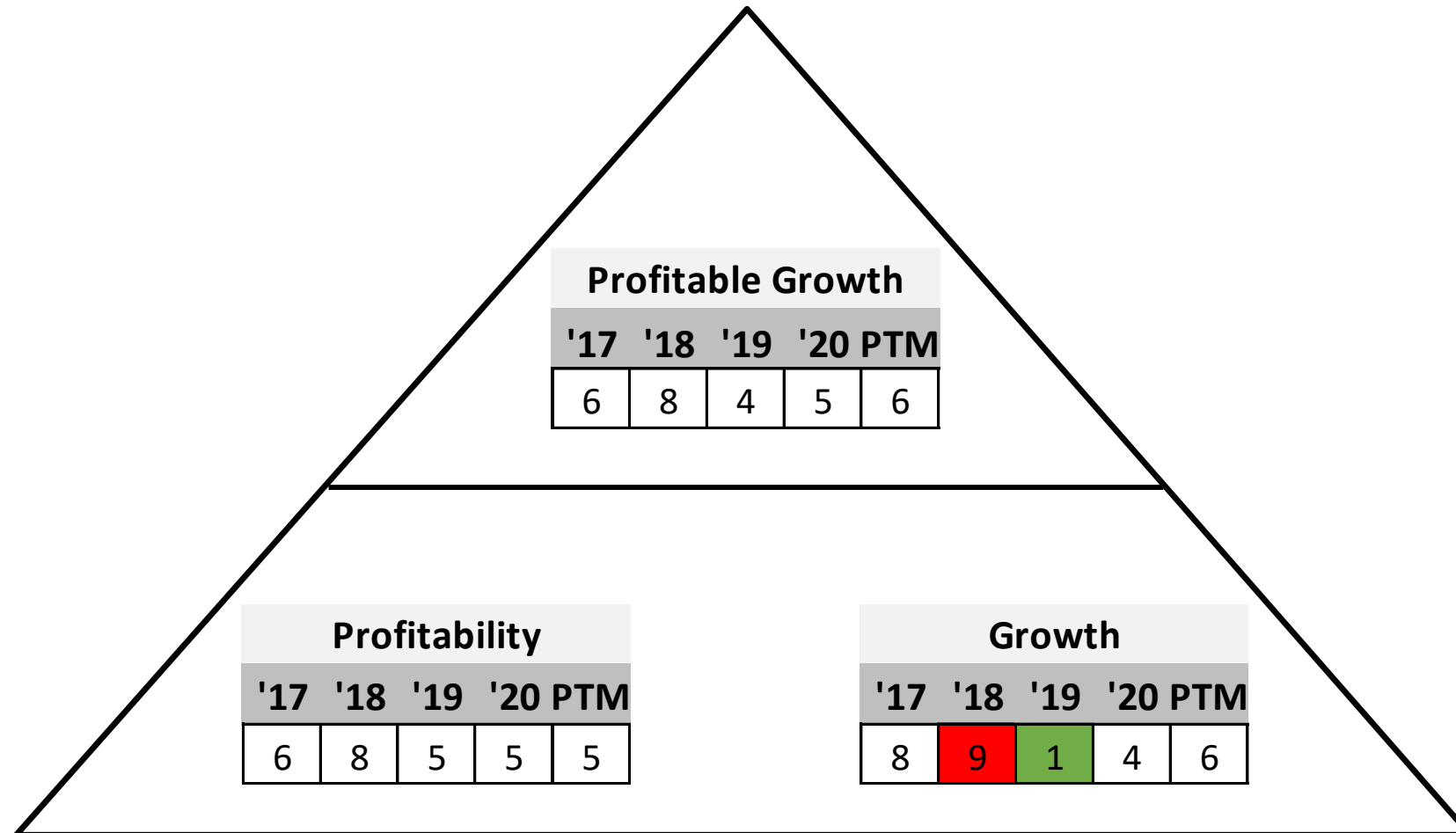
Story

FVMR

Value

WCB

Risks



Benchmarked against 270 large Comm. Serv. companies worldwide.



Sales

Story

FVMR

Value

WCB

Risks

- ★ Less-than-expected return on CAPEX in a capital-intensive industry
- ★ Overestimation of profit contribution from Fintech investments
- ★ Failure to keep up with technological changes

CONCLUSION

- Maintaining a superior network quality is critical success factor
- FinTech investments and value-added services could drive stable growth in a rather mature market
- High ROE and dividend yield make it an attractive play



**Can Philippine's
second-largest
Telco company
PLDT regain its lost
market share?**

