

Jefferies

Europe / Telecom Services: Belgian Telcos: Pressure Building

Key Takeaway

We believe the Belgian telecom market is emerging from a lull since the last serious disruption in 2012. The established broadband players have started to visibly feel and react to OBEL's efforts to establish a credible position in fixed-mobile convergence. At the same time, TNET is preparing its previously sub-par mobile network for duty, with a material effect on OBEL financials. We reiterate our Underperform on PROX (PT €21.9), and Hold on OBEL (PT €20.2).

Market on the move. The Belgian fixed market is showing clear signs of increasing commercial activity. OBEL is now in the market with price-aggressive convergence bundles and has expressed intentions to further accelerate its cable efforts. Its room for manoeuvre may well increase if wholesale price regulation is switched from retail-minus to cost-plus as we believe is likely. OBEL's price-based strategy not only threatens share for PROX and cable (TNET & Voo), but on the margin also undermines their ability to raise prices and/or upsell in our view. We do note deteriorating broadband trends at TNET and to an extent also at PROX, an issue they have started to address with unusually steep promotional discounts. In mobile, TNET is offering large and flexible data buckets and hosts an increasing number of MVNOs, primarily at the expense of OBEL. This is the logical escalation of its mobile activities after turning into an MNO with the acquisition of BASE in 2016. The historical network quality gap of BASE appears to be closing fast, in particular in Flanders, and since TNET is attacking from the rear (at least partially, reflecting BASE's weak starting position), this is an incremental source of competitive friction. We have been highlighting these issues for some time, but they have taken longer to crystallise than we would have thought.

Proximus (PROX BB, Underperform, PT €21.9). Against this tough trading backdrop, we see little reason to become more constructive on Proximus, in particular considering the stock's premium valuation (14.6x 2018e EV/OpFCF vs incumbents on 12.5x). We note consensus for 2017e/18e FCF has declined by -12%/-3% since 3Q16. Particular issues for PROX into 2018e will be the financial impact from an increasing reliance on the Scarlet value brand in order to fend off OBEL. PROX, as a DSL/fibre player, may be less directly exposed to OBEL's attempts to attract cable customers than TNET/VOO, but the cable fightback in the form of commercial aggression indirectly affects PROX too, of course.

Orange Belgium (OBEL BB, Hold, PT €20.2). We find it harder to take a decisive view on OBEL. The core mobile operation is delivering rather solid momentum, cost management has been impressive, and we believe the company now has a fighting chance to mitigate the competitive pressure from convergence. On the other hand, OBEL is facing a material headwind in the form of high-margin MVNO revenue loss in 2018e/19e, the rapidly growing cable revenue is coming with significant EBITDA losses, and the cable project is still subject to execution risk and quite significant regulatory uncertainty. Our revised near-term (2018e) EBITDA forecasts for OBEL end up c.10% below consensus. In this unusually polarised balance, the stock's valuation at 14.1x 2018e EV/OpFCF offers no particular handle either, in our view. At this time, we feel the downside issues (MVNO revenue loss, EBITDA pressure from cable, regulatory uncertainty) are more likely to prevail in the near term, and so merely reiterate our Hold recommendation (PT €20.2, prior €19.5).