Telecom Services

Belgian Telcos: Downgrade PROX to Underperform; Upgrade OBEL to Buy

13 January 2020

Key Takeaway

Regulatory intervention fuels intensifying competition in Belgium by leveling the playing field in convergence. PROX's premium valuation does not reflect the risks, such as slowing convergence uptake and looming ARPH dilution. We cut FCF estimates and downgrade to Underperform (PT €20.7). OBEL has established execution credibility in convergence, and the new 'Love Duo' product should drive further share gains and EBITDA accretion. We upgrade to Buy (PT €23.9).

Belgian market structure changing. Disruptive competitive forces unleashed by regulatory intervention in cable wholesale, slowing fixed-mobile convergence uptake and increasing infrastructure competition are affecting the Belgian market structure. While this has been unfolding for some time, several factors come together into 2020e. (a) The regulator appears prepared to make cable resale commercially viable (now a loss leader), (b) OBEL has established execution credibility in convergence, and the recently introduced 'Love Duo' product looks particularly well positioned, (c) PROX is already suffering from rising churn in 4P and now faces underlying ARPH dilution from more convergence competition, (d) a cable technology upgrade might well intensify infrastructure competition.

Proximus. We downgrade to Underperform with a PT of €20.7 (prior: Hold, PT €23.1). The stock has rerated last year and now trades on extended multiples (13.9x 2020e EV/OpFCF vs incumbent peers on 12.9x). In our view, this does not sufficiently reflect the risks. In particular, uptake of convergence products - the company's silver bullet in recent years - is slowing. This is partially a base effect, but the issue is exacerbated by OBEL's convergence push which has forced the industry including PROX into changing product mix with the risk of underlying ARPH dilution (2020e will benefit from a technical one-off uplift). Also, the cable upgrade to Docsis 3.1 and industrial policy may well drive capex creep at PROX (expect guidance in this direction at 4Q19). We cut FCF forecasts by -12%/-16% for 2020e/21e. This puts a squeeze on dividend coverage (although we think the dividend is protected by government interests).

Orange Belgium. We upgrade to Buy at a PT of €23.9 (prior: Hold, PT €15.1). The mobile-centric core business is delivering solid trends. At the same time, evidence is mounting that the cable resale project is working. This crucially levels the competitive playing field as PROX and cable can no longer rely on convergence offers as a source of competitive differentiation inaccessible to OBEL. OBEL's 'Love Duo' product introduced in 2019 looks like a particularly savvy move, addressing an underserved market segment. Despite lower pricing (ARPH-dilutive), we believe it is accretive to EBITDA. We concede that OBEL trades on extended near-term multiples due to the cable start-up investments (14.2x 2020e EV/OpFCF vs sector on 12.7x), following a significant rerating of the stock. However, forecast free cash flow growth (+10% CAGR 2019e-22e) should rapidly compress these multiples (13.2x/11.1x EV/OpFCF already by 2021e/22e) as the cable resale business builds scale and benefits from lower regulated wholesale costs.

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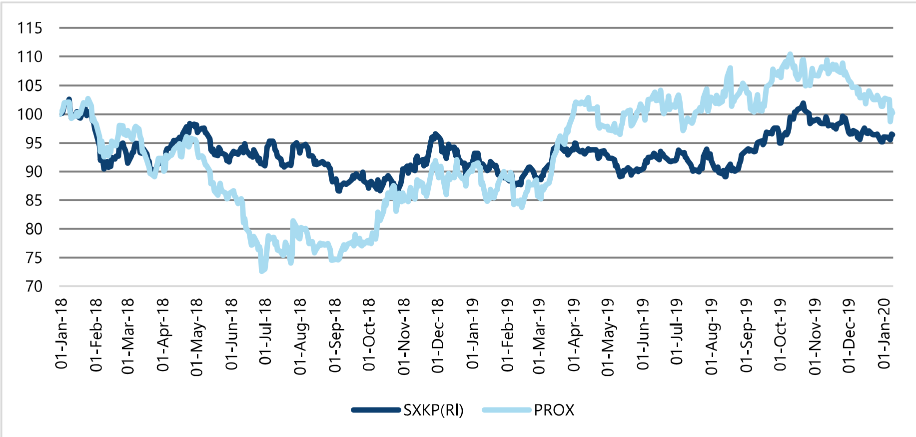
Summary of Changes										
Company	Ticker	Rating	Price	Price Target	EPS Estimates 2018	EPS Estimates 2019	EPS Estimates 2020	P/E 2018	P/E 2019	P/E 2020
Orange Belgium	OBEL BB	BUY	€20.60	€23.90	€0.65	€0.60	€0.90	31.7x	34.3x	22.9x
Previous		*HOLD*		*€15.10*	*€0.65*	*€0.62*	*€0.84*			
Proximus	PROX BB	UNPF	€25.23	€20.70	€1.74	€1.70	€1.74	14.5x	14.8x	14.5x
Previous		*HOLD*		*€23.10*	*€1.74*	*€1.75*	*€1.80*			

EPS: EPS: JEF adjusted

Proximus (PROX BB, Underperform, PT €20.7)

We downgrade Proximus to Underperform (from Hold) at a PT of €20.7 (prior €23.1). We had upgraded to Hold in July 2018 mainly on valuation grounds as concerns over a fourth mobile entrant looked overplayed at the time (see *Benelux telcos: Estimate refresh; Upgrading Proximus to Hold*, 18 Jul 2018). However, following TR of +38% since mid-2018 (sector +6%, see Exhibit 1), PROX's valuation is back in premium territory (13.9x 2020e EV/OpFCF vs incumbent peers on 12.9x).

Exhibit 1 - PROX vs SXKP (total return)



Source: Jefferies, FactSet

At the same time, operating risks are looking more severe, in our view. A sharp recovery of domestic service revenue trends looks vulnerable to competitive developments, in particular OBEL's continued inroads in fixed-mobile convergence bundling and an associated mix shift towards 'skinny' bundles in the market. Also, new leadership might feel compelled to accelerate the full-fibre (FTTH/B) rollout in response to industrial policy demands and cable's speed upgrade (Docsis 3.1). We think these two issues easily have the ability to absorb continued cost cutting where PROX has execution credibility and recent newsflow is supportive. On the other hand, FCF barely covers the dividend as it stands, which severely limits management's room for manoeuvre on fibre, given the high priority PROX's majority owner, the Belgian state, appears to place on the dividend.

To reflect the situation, we cut FCF estimates materially (-12%/-16% for 2020e/21e). This is mainly driven by higher capex expectations, now above the current €1bn envelope (€1.05bn/€1.08bn for 2020e/21e). The amount of the assumed increase is meant to strike a balance between the need for an acceleration of FTTH/B rollout on the one hand, and limited financial flexibility on the other, given the apparently sacrosanct dividend.

Reflecting new estimates, particularly higher capex, our DCF-based SOTP target valuation indicates a new PT of €20.7 (prior €23.1). At our PT, the stock would trade on 12.3x 2020e EV/OpFCF, a slight discount to incumbent peers on 12.9x. (For completeness, this corresponds to a less relevant 5.5x 2020e EV/EBITDA vs incumbent peers on 6.3x). The PT implies a 1-year forecast total return of -11%, which corresponds to an Underperform recommendation in the Jefferies ratings system (prior: Hold).

Consumer Business Unit (CBU)

Competition triggered by regulatory intervention in fixed, slowing fixed-mobile convergence uptake and increasing infrastructure competition all weigh on PROX's top-line outlook. The company needs to defend its high-end customer base against a focused premium operator with a strong fixed network (TNET) and at the same time face off a price-disruptive challenger (OBEL) that has made significant progress to break into PROX/cable near-duopoly in the fixed broadband market.

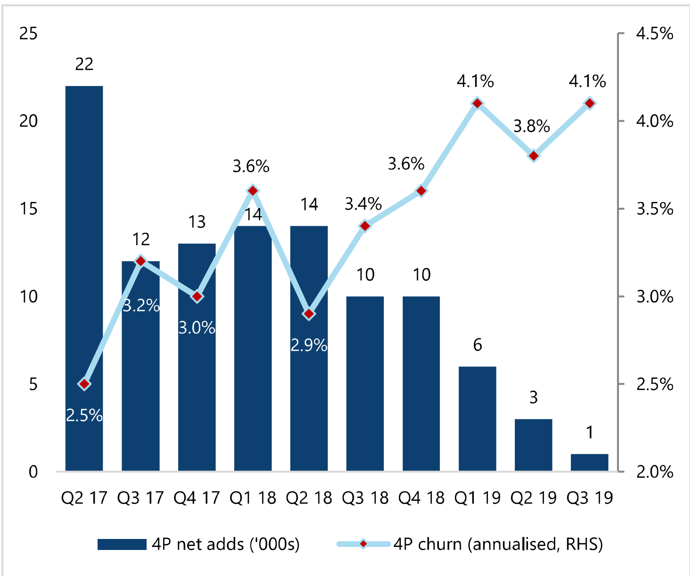
We concede that we have been highlighting these issues for some time (*Belgian Telcos: Pressure Building,* 28 November 2017). In a battle of retreat, PROX has managed to mitigate them by ring-fencing and upselling its customer base to convergence bundles, in particular to its flagship quad-play (4P) Tuttimus plan.

However, the first cracks in this success story have emerged and could well depress retail service revenue trends, in our view. Two factors stand out:

- Net adds for the Tuttimus convergence product have slowed visibly since the beginning of 2019 from a quarterly average of +12k in 2018 to +3k in 9M19 (see Exhibit 2). We note churn has increased and is now trending at an annualised rate above 4.0% (2018: ~3.5%).
- PROX has successfully lifted c.55% of its fixed broadband (FBB) customer base into a fixed-mobile convergence (FMC) plan (see Exhibit 3). Base effects, together with the competitive situation (including OBEL but also TNET's push following the BASE acquisition), have slowed PROX's penetration increase to c.0.3pp per quarter by now.

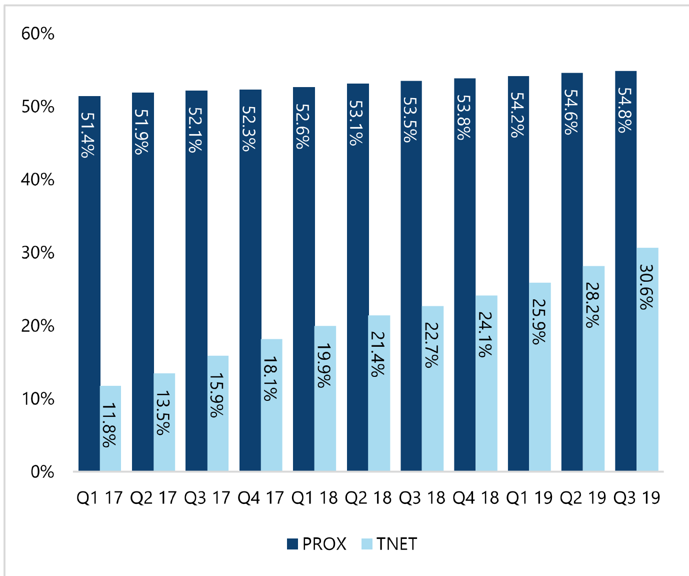
These are two separate points. Tuttimus is PROX's high-end 4P flagship product, but the company does compete with fixed-mobile convergence also in lower-end 2P and 3P offers.

Exhibit 2 - 4P evolution of net adds and churn



Source: Jefferies, company data

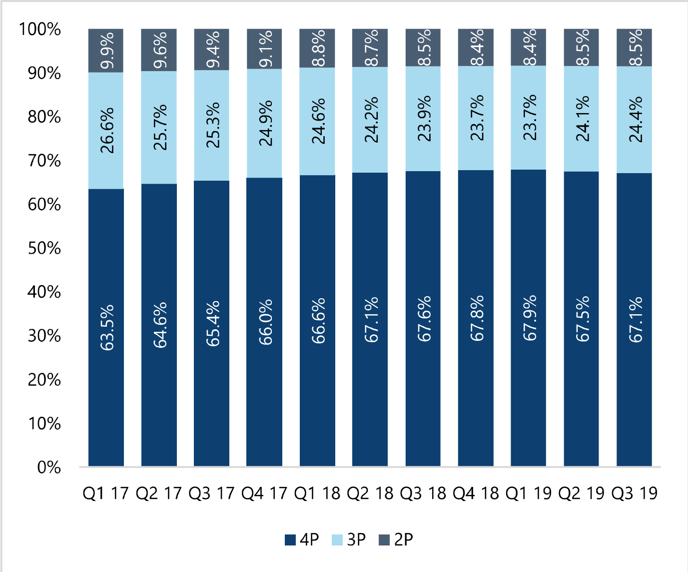
Exhibit 3 - FMC subs as % of fixed broadband customers



Source: Jefferies, company data

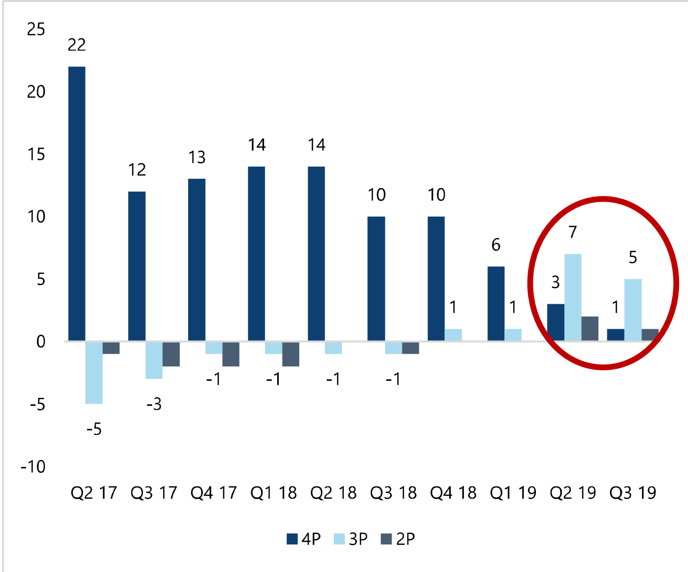
While we expect further FMC expansion (albeit at a slow pace), in fact the value mix within the convergence base has started to shift towards cheaper bundles (see Exhibit 4). Prior to 2019, the take-up rate of the 4P bundle within the convergence base has consistently increased and grew from 63.5% in 1Q17 by +4.4p.p. to 67.9% in 1Q19. However, since then, net take-up of 3P bundles has outpaced 4P adoption by 12k to 4k (see Exhibit 5). In this context, we also refer to the market discussion at the end of this note, in particular Exhibits 47 and 48.

Exhibit 4 - Mix of convergence base by x-play bundle



Source: Jefferies, company data

Exhibit 5 - Convergence net adds by x-play type (in '000s)



Source: Jefferies, company data

We attribute the strong increase in 3P net adds since 2Q to the introduction of Epic combo plans on 2 April 2019. These 3P bundles come with headline prices of €79.99/month for the 'full' and of €64.99/month for the 'light' version. This compares to minimum of €93.98/month for the standard or €84.99/month for the basic Tuttimus (4P) version and to the existing FMC 3P Minimus plans from €83.98/month for the standard or €74.99/month for the basic plan. For the market pricing context to these comments, we also refer to Exhibits 33-36 and the associated discussion.

It should be obvious that the shift in the convergence mix towards cheaper bundles will put pressure on PROX's ARPH. In 2019e, ARPH growth is shaping up towards +1.4% y/y (2018: +0.9%). The growth is mainly a mix effect, and its acceleration is driven mostly by the benefit of a +€2 price increase for most bundles in January and PROX's ongoing upselling efforts. These factors helped to more than compensate the revenue drag from intra-EU call regulation.

However, from January 2020, PROX increases prices by only +€1.5 (i.e., a €0.5 drag on y/y growth) and ARPH dilution from the mix shift within the FMC base also weighs on ARPH growth, in our view. These effects will not be offset by the lapping of the regulatory impact from mid-May 2020, on our estimates, and we model a slowdown in overall ARPH growth to +0.9%/+0.8% y/y in 2020e/21e on an underlying basis.

There is a one-of uplift effect, though. PROX has now followed the French operators in an ARPH-enhancing one-off manoeuvre as of 1 Jan 2020. This involves the insertion of media content into existing product bundles (specifically, most offers involving a Proximus-branded fixed broadband service), without any additional charges to end-customers. As media content attract zero VAT in Belgium, this means the VAT on the nominal value of the media content (between €14 and €15, with regional variation) is 'saved' from PROX's view (the customer pays an unchanged amount). All said, this lifts ARPH by about €3 (21% of €14-€15) for slightly more than 1m bundle customers. At the EBITDA level, this ARPH uplift is reduced by the (unreported) fees PROX pays to the media content providers.

This effect is obviously a one-off, and we add it on the mentioned underlying trend in Exhibit 6 (visible in 4-P and 3P convergent ARPH). On our assumption, ARPH growth would be temporarily lifted by +1.7pp to 2.5% y/y in 2020e, before dropping back to the mentioned underlying growth of +0.8% y/y in 2021e.

Exhibit 6 - Proximus CBU ARPH by X-play type

ARPH (€) x-play	Q4 18	Q1 19	Q2 19	Q3 19	Q4 19e	2018	2019e	2020e	2021e
4-Play	**110.7**	**111.8**	**111.3**	**111.3**	**110.4**	**111.4**	**111.4**	**113.9**	**113.3**
Convergent	104.6	104.9	104.5	103.4	102.8	105.7	103.4	104.9	103.5
Fixed	56.8	57.6	56.7	56.9	56.2	57.5	56.8	56.0	55.4
3-Play	**73.3**	**74.1**	**73.7**	**73.8**	**73.5**	**74.1**	**73.6**	**74.9**	**75.1**
Convergent	71.4	71.9	71.9	71.5	69.3	71.8	71.7	71.7	71.7
Fixed	54.5	55.2	54.8	54.7	55.4	54.8	55.2	55.5	55.6
2-Play	**58.5**	**59.1**	**58.9**	**58.8**	**58.9**	**58.7**	**59.1**	**59.6**	**59.8**
Fixed voice	27.2	27.3	26.8	26.8	27.2	27.2	27.2	27.4	27.5
Internet	31.3	31.6	31.5	31.3	31.3	31.1	31.9	32.4	32.8
Mobile	37.2	37.4	38.7	38.4	38.5	37.8	38.4	38.4	38.3
1-Play	**33.9**	**34.2**	**35.0**	**34.8**	**35.0**	**34.2**	**34.9**	**35.3**	**35.5**
ARPH x-play	**65.8**	**66.7**	**66.8**	**66.8**	**66.7**	**65.9**	**66.9**	**68.5**	**69.1**
ARPH x-play growth y/y									
4-Play	**-1.2%**	**0.3%**	**-0.4%**	**-0.4%**	**-0.2%**	**-1.2%**	**-0.3%**	**2.2%**	**-0.5%**
Convergent	-1.1%	-1.5%	-1.5%	-1.8%	-1.5%	-0.5%	-1.9%	1.4%	-1.3%
Fixed	-2.5%	-1.2%	-1.9%	0.0%	-1.4%	-2.9%	-1.6%	-1.3%	-1.1%
3-Play	**-1.8%**	**-1.0%**	**-1.1%**	**0.3%**	**0.0%**	**-2.1%**	**-0.9%**	**1.7%**	**0.3%**
Convergent	-0.7%	-1.2%	0.1%	0.2%	-0.4%	-0.6%	0.7%	0.0%	0.0%
Fixed	1.5%	-0.2%	0.0%	0.3%	0.7%	1.9%	0.8%	0.5%	0.3%
2-Play	**1.0%**	**-0.2%**	**0.3%**	**0.6%**	**1.0%**	**1.0%**	**1.1%**	**0.8%**	**0.4%**
Fixed voice	3.0%	-1.4%	-0.5%	-0.3%	1.2%	3.4%	0.7%	0.5%	0.4%
Internet	2.8%	2.1%	1.4%	1.0%	-0.5%	3.0%	2.8%	1.5%	1.2%
Mobile	-4.4%	-2.1%	0.3%	3.6%	3.0%	-4.5%	1.5%	0.0%	-0.2%
1-Play	**-1.4%**	**-0.8%**	**1.0%**	**3.2%**	**3.0%**	**-1.4%**	**2.2%**	**1.0%**	**0.7%**
ARPH x-play	**0.6%**	**1.2%**	**1.0%**	**1.7%**	**1.4%**	**0.9%**	**1.4%**	**2.5%**	**0.8%**

Source: Jefferies estimates, company data

A slowdown in upselling momentum and underlying ARPH dilution prevents meaningful underlying X-play revenue growth, on our estimates (see Exhibit 7). We model peak growth in 2019e at +0.7% y/y that drops back to +0.2% for 2020e/21e, lifted to +1.8% by the one-off media content effect in 2020e. Overall revenue growth is further impacted by the structural decline in prepaid (-18.5%/-12.5%/-11.8% y/y in 2019e/20e/21).

We do not view stable underlying X-play revenue as a weak trend for PROX, in particular in such a challenging competitive environment. However, a development along those lines does not warrant a premium valuation either, in our view. Furthermore, we see downside risk to our estimates given uncertainty about the impact on OBEL's new 2P FMC plan, TNET's rollout of Docsis 3.1, and a possible ownership change at Voo that could put PROX's commercial momentum in Wallonia under pressure.

Exhibit 7 - CBU revenue breakdown

Revenues (€m)	Q4 18	Q1 19	Q2 19	Q3 19	Q4 19e	2018	2019e	2020e	2021e
4-Play	241	247	247	247	246	948	987	1,028	1,041
Convergent	80	80	82	83	84	325	329	357	376
Fixed	82	82	80	79	78	334	319	303	290
3-Play	162	162	162	162	162	659	648	661	666
Convergent	19	20	20	20	20	79	80	81	81
Fixed	49	49	48	47	47	201	191	184	179
2-Play	68	68	68	67	67	280	271	265	259
Fixed voice	22	22	20	20	19	94	81	69	58
Internet	14	15	15	15	15	54	60	66	70
Mobile	77	77	80	80	80	312	317	317	317
1-Play	113	113	115	114	114	460	458	452	445
X-Play revenues	**585**	**590**	**591**	**590**	**588**	**2,348**	**2,363**	**2,406**	**2,411**
Prepaid	**17**	**15**	**19**	**15**	**14**	**77**	**63**	**55**	**48**
Terminal Sales	**50**	**37**	**32**	**31**	**47**	**184**	**147**	**132**	**132**
Tango	**31**	**28**	**28**	**29**	**31**	**116**	**116**	**116**	**116**
Other net revenues	**44**	**32**	**28**	**30**	**36**	**155**	**126**	**126**	**126**
Net Revenues (comparable)	**727**	**702**	**698**	**695**	**716**	**2,880**	**2,815**	**2,835**	**2,834**
Other operating income	7	6	7	5	5	23	23	23	23
Revenues (comparable)	**735**	**708**	**706**	**700**	**721**	**2,903**	**2,838**	**2,858**	**2,857**
Revenue growth y/y									
4-Play	6.1%	6.7%	4.5%	3.1%	2.2%	7.5%	4.1%	4.2%	1.2%
Convergent	-2.3%	-2.2%	-0.2%	2.5%	4.7%	-3.3%	1.2%	8.7%	5.3%
Fixed	-4.1%	-4.1%	-4.9%	-4.0%	-5.1%	-3.5%	-4.6%	-4.9%	-4.5%
3-Play	-3.2%	-3.1%	-2.6%	-0.8%	-0.3%	-3.4%	-1.7%	2.0%	0.8%
Convergent	-4.6%	-3.5%	-0.8%	2.3%	2.9%	-6.0%	0.7%	1.6%	0.0%
Fixed	-4.9%	-6.4%	-5.3%	-5.2%	-4.0%	-4.3%	-5.0%	-3.5%	-3.1%
2-Play	-4.8%	-5.6%	-4.1%	-3.1%	-2.1%	-4.8%	-3.4%	-2.0%	-2.2%
Fixed voice	-11.1%	-15.1%	-14.3%	-14.3%	-13.4%	-10.5%	-13.8%	-14.7%	-15.6%
Internet	12.0%	10.9%	10.0%	10.3%	9.3%	12.5%	11.7%	8.9%	6.9%
Mobile	-4.8%	-2.4%	0.7%	2.7%	3.5%	-5.7%	1.5%	0.2%	-0.2%
1-Play	-5.0%	-3.6%	-1.3%	0.2%	0.9%	-5.2%	-0.4%	-1.3%	-1.5%
X-Play revenues	**0.0%**	**0.3%**	**0.3%**	**0.7%**	**0.6%**	**0.2%**	**0.7%**	**1.8%**	**0.2%**
Prepaid	**-22.7%**	**-25.0%**	**-9.5%**	**-21.1%**	**-19.3%**	**-23.8%**	**-18.5%**	**-12.5%**	**-11.8%**
Terminal Sales	**-10.7%**	**-28.8%**	**-28.9%**	**-16.2%**	**-5.6%**	**-8.0%**	**-20.0%**	**-10.0%**	**0.0%**
Tango	**-3.1%**	**0.0%**	**0.0%**	**0.0%**	**0.0%**	**1.8%**	**0.0%**	**0.0%**	**0.0%**
Other net revenues	**-2.2%**	**-13.5%**	**-20.0%**	**-23.1%**	**-19.2%**	**4.0%**	**-19.0%**	**0.0%**	**0.0%**
Net Revenue growth y/y (comparable)	**-1.8%**	**-3.2%**	**-2.8%**	**-2.0%**	**-1.5%**	**-1.0%**	**-2.3%**	**0.7%**	**-0.1%**
Other operating income	40.0%	20.0%	40.0%	0.0%	-28.6%	15.0%	0.0%	0.0%	0.0%
Total revenue growth y/y (comparable)	**-1.2%**	**-3.0%**	**-2.5%**	**-2.0%**	**-1.9%**	**-0.9%**	**-2.2%**	**0.7%**	**-0.1%**

Source: Jefferies estimates, company data

Enterprise Business Unit (EBU)

We take a cautious stance on PROX's revenue outlook in the b2b segment (our 2020e/21e forecasts sit c.-1.5%/-2.6% below consensus). Next to the structural decline of the legacy connectivity business, we see increasing competitive pressures weighing on the top-line.

- TNET revamped its b2b product portfolio for the SOHO market in September and highlighted a 20% increase in broadband intake on its 3Q19 conf call. Going forward, management expects 'more growth in the SOHO business for us'. The outlook for the Large Enterprise and SME market was framed as 'choppy' following the integration of Nextel. However, given PROX's dominant market position in that segment, it is difficult to envisage an opportunity to accelerate growth, in our view.
- With the acquisition of BKM in July, OBEL underlined its ambition to play a growing role in the ICT market. Its current share in b2b fixed is still low and offers opportunities for share gain, compared to OBEL's c.30% share in b2b mobile according to management.

On the 3Q19 conf call, PROX itself described the competitive intensity in the b2b market as 'very high' and singled out the pricing environment in b2b mobile as 'tough'. This indeed shows in soft mobile ARPU trends at -3.8%/-3.2%-/3.0% y/y in 3Q-1Q19 and softening net adds at +6k/+5k/+20k in 3Q-1Q19.

PROX's dominant market position in b2b makes the company vulnerable to share-hungry competitors. We model persistent service revenue decline at c.-2% y/y over our forecast horizon (see Exhibit 8). On the total b2b net revenue level, inorganic tailwinds from small acquisitions in b2b have lapped out in 3Q19 and we model net revenue decline to accelerate from -0.3% y/y in 2019e to -1.2% in 2020e and then stabilising around that level going forward.

Exhibit 8 - EBU revenue breakdown

Revenues (€m)	Q4 18	Q1 19	Q2 19	Q3 19	Q4 19e	2018	2019e	2020e	2021e
Voice	49	49	47	45	44	203	185	170	155
Data (Internet & Data Connectivity)	61	62	61	61	61	246	245	246	246
Fixed Services	110	110	108	106	105	449	430	416	401
Mobile Services	80	78	81	80	80	316	319	317	315
Service revenue	190	189	189	185	185	765	749	733	717
Terminals (fixed & mobile)	14	14	13	12	16	56	55	55	55
Tango	8	7	4	6	6	30	23	23	23
Telecom revenue	212	210	206	203	207	852	827	810	794
ICT	143	132	128	126	143	519	529	529	529
Advanced Business Services	5	10	10	9	10	27	39	39	39
Other Products	3	3	2	2	2	11	9	9	9
Total net revenues	**362**	**355**	**347**	**340**	**362**	**1,408**	**1,404**	**1,388**	**1,371**
Other operating income	2	2	2	1	1	5	6	6	6
Total revenues	**364**	**357**	**348**	**342**	**363**	**1,413**	**1,410**	**1,394**	**1,377**
Revenue growth y/y									
Voice	-5.8%	-7.5%	-7.8%	-8.2%	-9.4%	-6.9%	-8.7%	-8.2%	-8.7%
Data (Internet & Data Connectivity)	-1.6%	1.6%	-1.6%	-1.6%	0.1%	-0.4%	-0.4%	0.4%	0.0%
Fixed Services	-3.5%	-3.5%	-4.4%	-4.5%	-4.2%	-3.4%	-4.1%	-3.3%	-3.5%
Mobile Services	1.3%	1.3%	1.3%	0.0%	-0.2%	0.0%	0.9%	-0.7%	-0.5%
Service revenue	-1.6%	-1.0%	-2.1%	-3.1%	-2.5%	-2.2%	-2.1%	-2.2%	-2.2%
Terminals (fixed & mobile)	-17.6%	-22.2%	-7.1%	9.1%	13.4%	12.0%	-2.0%	0.0%	0.0%
Tango	14.3%	-12.5%	-42.9%	-14.3%	-31.3%	11.1%	-25.0%	0.0%	0.0%
Telecom revenue	-2.3%	-3.2%	-3.7%	-2.9%	-2.5%	-0.8%	-3.0%	-2.0%	-2.0%
ICT	2.9%	7.3%	1.6%	0.0%	0.3%	4.4%	2.0%	0.0%	0.0%
Advanced Business Services	-44.4%	66.7%	42.9%	12.5%	103.0%	-3.6%	45.0%	0.0%	0.0%
Other Products	0.0%	0.0%	0.0%	-33.3%	-40.0%	-8.3%	-20.0%	0.0%	0.0%
Total net revenue	**-1.6%**	**1.4%**	**-0.9%**	**-1.7%**	**0.0%**	**1.0%**	**-0.3%**	**-1.2%**	**-1.2%**
Other operating income	100.0%	100.0%	100.0%	0.0%	-50.0%	-16.7%	20.0%	0.0%	0.0%
Total revenue	**-1.4%**	**1.7%**	**-0.9%**	**-1.4%**	**-0.3%**	**0.9%**	**-0.2%**	**-1.2%**	**-1.2%**

Source: Jefferies estimates, company data

Domestic cost and EBITDA

PROX has demonstrated a solid track-record of executing cost efficiency programs that have helped to offset top-line pressures. This is clearly an upside risk to our cautious views.

To quantify this question, we note that the latest cost savings plan announced in January 2019 envisages domestic gross opex savings of €240m between 2019-2021. The expected net cost savings or the phasing of the €240m have not been disclosed. However, for past savings programs, management have indicated net opex savings at ~38% of the targeted gross figure (see Exhibit 9). Extrapolating a similar ratio onto the new cost savings plan would indicate estimated net opex savings of ~€92m by 2022 from this latest programme.

Exhibit 9 - Proximus - net vs gross opex savings of efficiency programmes

Cost saving plans (in €m)	2015-18 original	2015-18 updated	2015-19	2019-22
Gross opex savings	260	320	400	240
Net opex savings	100	125	150	92
- net as % of gross savings	38%	39%	38%	38%

Source: Jefferies estimates, company data

We would argue that our model forecasts fully discount cost savings at this planned level. As shown in Exhibit 10, our revenue and EBITDA progression imply net cost savings of €102m between 2018-2022, in line with the €92m we derived in Exhibit 9.

Exhibit 10 - Proximus - domestic opex forecasts

(in €m)	2018	2022
Total domestic opex	-1,652	-1,550
Net cost savings		102

Source: Jefferies estimates, company data

In Exhibit 11, we lay out our domestic forecasts for revenue, opex and EBITDA. In summary, we expect top-line pressures to be offset by solid cost execution, but do not forecast meaningful EBITDA growth over the medium term - we model an 2018-21e EBITDA CAGR of +0.7% including the discussed one-off uplift in 2020e.

Exhibit 11 - Domestic revenue, cost and EBITDA trends and forecasts

(in €m)	Q4 18	Q1 19	Q2 19	Q3 19	Q4 19e	2018	2019e	2020e	2021e
Domestic revenue (adj)									
Consumer Business Unit (CBU)	735	708	706	700	721	2,903	2,838	2,858	2,857
Enterprise Business Unit (EBU)	364	357	348	342	363	1,413	1,410	1,394	1,377
Wholesale	51	42	45	49	45	201	181	179	177
Other (incl eliminations)	-15	-11	-15	-20	-12	-57	-58	-58	-58
Domestic revenue (adj)	**1,134**	**1,096**	**1,084**	**1,071**	**1,117**	**4,460**	**4,371**	**4,373**	**4,353**
Domestic direct margin (adj)									
Consumer Business Unit (CBU)	550	558	555	550	553	2,219	2,219	2,224	2,222
Enterprise Business Unit (EBU)	244	247	246	236	244	959	973	962	950
Wholesale	41	35	36	38	38	165	147	145	144
Other (incl eliminations)	5	8	6	2	4	21	20	0	0
Domestic direct margin (adj)	**840**	**848**	**843**	**827**	**839**	**3,364**	**3,359**	**3,331**	**3,316**
Domestic direct margin (adj) % revenue									
Consumer Business Unit (CBU)	74.8%	78.8%	78.6%	78.6%	76.7%	76.4%	78.2%	77.8%	77.8%
Enterprise Business Unit (EBU)	67.0%	69.2%	70.7%	69.0%	67.2%	67.9%	69.0%	69.0%	69.0%
Wholesale	80.4%	83.3%	80.0%	77.6%	83.6%	82.1%	81.0%	81.0%	81.0%
Other (incl eliminations)	-33.3%	-72.7%	-40.0%	-10.0%	-33.3%	-36.8%	-34.5%	0.0%	0.0%
Domestic direct margin (adj) % revenue	**74.1%**	**77.4%**	**77.8%**	**77.2%**	**75.1%**	**75.4%**	**76.8%**	**76.2%**	**76.2%**
Domestic opex (adj)									
Personnel expenses and pensions	-282	-275	-269	-273	-275	-1,108	-1,092	-1,065	-1,045
- % revenue	-24.9%	-25.1%	-24.8%	-25.5%	-24.6%	-24.8%	-25.0%	-24.3%	-24.0%
Other operating expenses	-144	-143	-128	-123	-139	-546	-533	-528	-525
- % revenue	-12.7%	-13.0%	-11.8%	-11.5%	-12.5%	-12.2%	-12.2%	-12.1%	-12.1%
Other (plug)	0	-1	-1	-2	0	2	-4	0	0
- % revenue	0.0%	-0.1%	-0.1%	-0.2%	0.0%	0.0%	-0.1%	0.0%	0.0%
Domestic opex (adj)	**-426**	**-419**	**-398**	**-398**	**-414**	**-1,652**	**-1,629**	**-1,592**	**-1,570**
- change y/y	0	1	1	10	12	1	23	37	22
Domestic EBITDA (adj)	**414**	**428**	**446**	**430**	**424**	**1,711**	**1,729**	**1,739**	**1,746**
- % revenue	36.5%	39.1%	41.1%	40.1%	38.0%	38.4%	39.6%	39.8%	40.1%

Source: Jefferies estimates, company data

FTTH and capex

We amend the domestic forecasts by the less relevant Carrier Services ones in Exhibit 12 for completeness, and now turn to capex. We model an increase in the capex/sales ratio by +2pp to 25% until 2021e (see Exhibit 12), as we expect PROX's new CEO to accelerate FTTH rollout. This corresponds to an increase of our capex estimates for 2020e/21e by +6%/+9%, respectively. This capex intensity would be among the highest in the sector (see Exhibit 13).

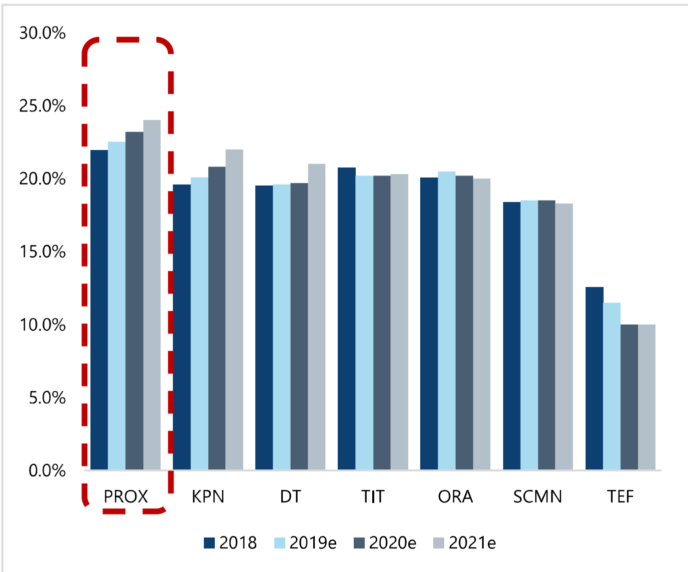
Exhibit 12 - Proximus group revenue, EBITDA and capex forecasts

(in €m)	Q4 18	Q1 19	Q2 19	Q3 19	Q4 19e	2018	2019e	2020e	2021e
Revenue (adj)									
Domestic	1,134	1,096	1,084	1,071	1,117	4,460	4,371	4,373	4,353
Carrier services	341	319	329	335	330	1,347	1,313	1,274	1,241
Revenue (adj)	**1,475**	**1,415**	**1,413**	**1,407**	**1,447**	**5,806**	**5,685**	**5,647**	**5,594**
Direct margin (adj)									
Domestic	840	848	843	827	839	3,364	3,359	3,331	3,316
Carrier services	81	79	80	83	84	317	326	326	325
Direct margin (adj)	**921**	**926**	**923**	**911**	**922**	**3,681**	**3,684**	**3,657**	**3,641**
Direct margin (adj) % revenue									
Domestic	74.1%	77.4%	77.8%	77.2%	75.1%	75.4%	76.8%	76.2%	76.2%
Carrier services	23.8%	24.8%	24.3%	24.8%	25.3%	23.5%	24.8%	25.6%	26.2%
Direct margin (adj) % revenue	**62.4%**	**65.4%**	**65.3%**	**64.7%**	**63.7%**	**63.4%**	**64.8%**	**64.8%**	**65.1%**
Opex (adj)									
Domestic	-426	-419	-398	-398	-414	-1,652	-1,629	-1,592	-1,570
Carrier services	-40	-44	-42	-43	-44	-163	-173	-174	-174
Opex (adj)	**-466**	**-463**	**-440**	**-441**	**-458**	**-1,815**	**-1,802**	**-1,766**	**-1,744**
- % revenue	-31.6%	-32.7%	-31.1%	-31.3%	-31.7%	-31.3%	-31.7%	-31.3%	-31.2%
EBITDA (adj)									
Domestic	414	428	446	430	424	1,711	1,729	1,739	1,746
Carrier services	41	35	38	40	40	154	153	152	151
EBITDA (adj)	**455**	**463**	**484**	**470**	**464**	**1,865**	**1,882**	**1,891**	**1,898**
- % revenue	40.1%	42.2%	44.6%	43.9%	41.5%	41.8%	43.1%	43.2%	43.6%
Capex	**322**	**219**	**247**	**222**	**332**	**1,019**	**1,020**	**1,050**	**1,080**
- % revenue	28.4%	20.0%	22.8%	20.7%	29.7%	22.8%	23.3%	24.0%	24.8%

Source: Jefferies estimates, company data

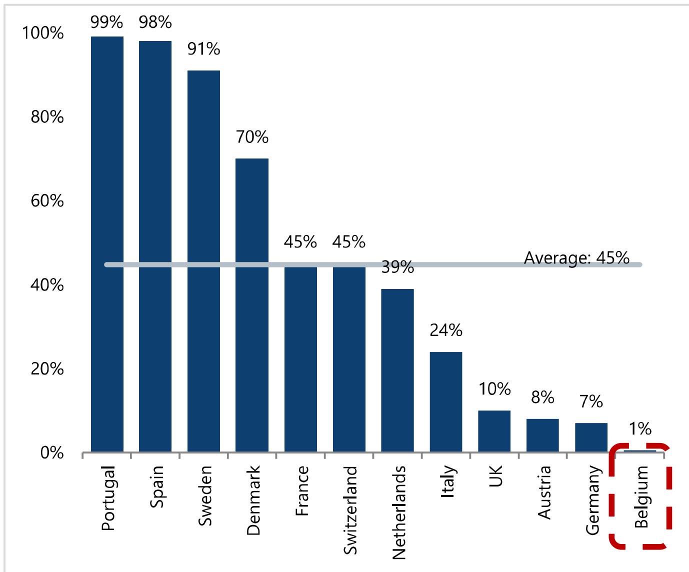
Two forces are at play and drive the increase in our capex estimates. First, Belgium severely lags behind other European countries in FTTH coverage. A study for the FTTH Council published in March 2019 suggested that only 0.5% of Belgian homes were passed with an FTTH connection by September 2018 vs an average of 45% for the largest European markets (see Exhibit 14). From what we observed so far, political pressure for PROX to accelerate fibre rollout has been rather muted and by no means resembles difficult situations that incumbents in Germany or the UK find themselves in. However, we would expect the political language to start changing over time given such a coverage gap risks putting Belgium on the back foot in terms of competitiveness in a European and global context.

Exhibit 13 - We expect PROX's capex/sale ratio to remain one of the highest amongst European incumbent peers...



Source: Jefferies estimates, company data

Exhibit 14 - ... as Belgium has lots of catching up to do in terms of FTTH coverage in Europe



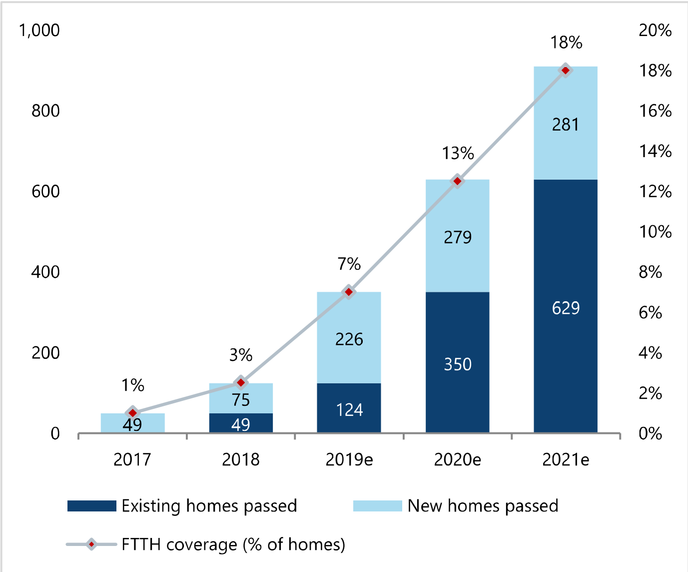
Source: Jefferies, FTTH Council Europe Conference (data as of Sep-18)

Second, this structural lag is now subject to a competitive catalyst. In September 2019, TNET announced the launch of a Docsis 3.1 modem, capable to deliver broadband speeds of 1Gbps and more. These gigabit speeds are available to TNET's entire cable footprint of c.3m homes and businesses in Flanders and Brussels. By contrast, PROX currently offers maximum speeds of only 100Mbps. To stay competitive against TNET with its focus on the premium segment, we believe it necessary for PROX to roll out FTTH beyond its original targets - in particular in Flanders and Brussels, where TNET is present.

Already on the 3Q19 results call, PROX's interim CEO hinted towards an acceleration of FTTH rollout, but deferred any specific detail to 4Q19e results. Notably, this will also be the first time when the new CEO Guillaume Boutin will host the call in that capacity (he previously was Chief Consumer Market Officer at PROX). A leadership change is a natural opportunity to adjust course, in our view.

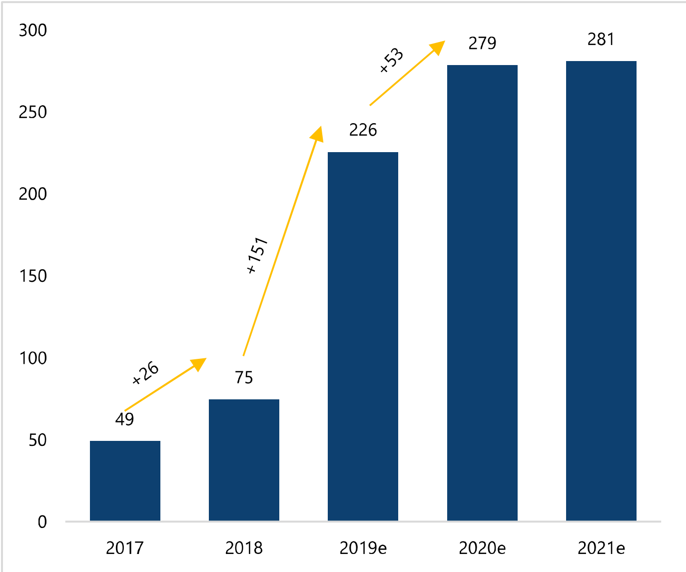
To revisit the base line for such an acceleration, we estimate that under the current plan, PROX has 350k (out of c.5m homes in Belgium) residential homes passed with FTTH, which corresponds to the 7% target laid out in its December 2016 fiber project (see Exhibit 15). Under this project, residential FTTH coverage will reach ~18% or c910k homes passed by 2021, ~40% by 2026 (c2.1m homes) and >50% by 2031 (c2.7m homes). FTTH rollout to enterprises is prioritised and should cover 40% of businesses by 2019, ~65% by 2021 and >85% by 2026.

Exhibit 15 - Residential homes passed with FTTH under current management plans (in '000s)



Source: Jefferies estimates, company data

Exhibit 16 - Residential FTTH rollout costs pa under current management plans (€m)



Source: Jefferies estimates, company data. Note: Average cost per home at €1k as indicated by PROX

On these management plans, the pace of residential FTTH deployment would have to step up to at least >280k per year in 2020e/21e (from the estimated >150k for 2019e). At an assumed average cost of c.€1k per home passed, this already implies an incremental c.€53m in capex to c.€280m in 2020e/21e (see Exhibit 16). This corresponds to an increase of the fibre share in total capex from c.30% in 2019e to c.36% in 2020e/21e, assuming the €1bn capex envelope as indicated.

In our view, this leaves limited room for an acceleration such as hinted at by management already, and arguably necessary to defend PROX's infrastructure position vs cable Docsis 3.1. This is the reason why we increase our capex assumptions to €1.05bn/€1.08bn in 2020e/21e, allowing for c.50k/80k faster fibre build. The scale of the acceleration is of course highly uncertain, as it is largely a discretionary management decision. We have chosen these figures to max out the financial headroom set by the FCF and dividend as discussed next. The company is likely to comment on this when the new CEO presents the 2020e outlook with 4Q19e results, in our view.

FCF and dividend

A potential acceleration of FTTH deployment to better compete with TNET is likely to put FCF under pressure, in our view. We outline our FCF forecasts (in the company definition) in Exhibit 17. A stable DPS at €1.50, which we believe is protected by the government's focus on this source of cash and its control of PROX, would correspond to payout ratios around 100% over the forecast horizon. This is ultimately what we targeted with our capex assumptions - we believe the investment budget at PROX is in all likelihood reversed out of the available resources after the payout of the dividend.

Exhibit 17 - FCF and dividend forecasts

(in €m)	Q4 18	Q1 19	Q2 19	Q3 19	Q4 19e	2018	2019e	2020e	2021e
FCF (adj in company definition)									
EBITDA (adj)	455	463	484	470	464	1,865	1,882	1,891	1,898
Incidentals	-13	-8	-8	-14	-15	-71	-45	-60	-56
Financial income (P&L)	-11	-11	-14	-12	-18	-56	-55	-55	-56
Tax (P&L)	-46	-52	-54	-51	-48	-191	-205	-195	-198
Non-cash corrections	5	24	14	23	34	-17	92	99	99
Change in working capital	-31	49	-34	101	-116	28	0	0	0
Cash flow from operations	**359**	**465**	**387**	**517**	**302**	**1,558**	**1,670**	**1,680**	**1,686**
Capex	-285	-299	-236	-257	-241	-1,099	-1,033	-1,063	-1,093
Other operational investment cash flow (co def)	28	-30	-4	1	0	-8	-32	0	0
Adjustments for non-operational investments (co def)	4	31	0	0	0	51	31	0	0
Lease payments	0	-23	-18	-21	-25	0	-87	-87	-87
FCF (adj in company definition)	**106**	**143**	**129**	**240**	**0**	**501**	**549**	**531**	**507**
Minority dividends	0	0	-29	0	0	-28	-29	-29	-29
FCF (adj in company definition) after minority divi	**106**	**143**	**100**	**240**	**0**	**473**	**520**	**502**	**478**
Dividend (cash paid)	-161	-1	-324	0	-159	-485	-484	-484	-484
- corresponding DPS (€)						1.50	1.50	1.50	1.50
Dividend payout ratio (cash)						103%	93%	96%	101%

Source: Jefferies estimates, company data

Valuation

A flat EBITDA trend and investing into fibre for future growth is not necessarily a particularly weak profile in a sector context, in our view. Also, we already mentioned that we regard the risk of an outright dividend cut rather limited given PROX's strong balance sheet (2019e: 1.3x net debt/EBITDA post IFRS16) and the controlling influence of the 'cash-hungry' Belgian state.

Still, we believe PROX's difficult situation is not fully reflected in the stock's valuation. On 13.9x 2020e EV/OpFCF, PROX currently trades at a premium to incumbent peers on 12.9x 2020e EV/OpFCF. On our target price, PROX would trade on 12.3x - at a slight discount to peers.

Our PT of €20.7 is derived from a DCF-based SOTP valuation (see Exhibit 18), and corresponds to a forecast 1-year total return of -11%. This corresponds to an Underperform rating in the Jefferies ratings system (prior: Hold).

Exhibit 18 - Proximus DCF-based SOTP target valuation

(in €m)	Value	Per share	Valuation comment
Firm excl. ICS	9,071	28.1	12.5x 20e OpFCF, DCF
ICS	732	2.3	10.9x 20e OpFCF, DCF
Core EV	**9,803**	**30.4**	**12.3x 20e OpFCF**
Tax assets	62	0.2	NPV of cash tax savings
Pension	-415	-1.3	FY18 at book, post tax
Restructuring	-412		
Spectrum	-266	-0.8	
Net debt	-2,107	-6.5	End-2020e, pre-IFRS16
Equity	**6,667**		
Number of shares	323		
Equity per share (€)	**20.7**		

Source: Jefferies estimates

New estimates and changes

We summarise new estimates in Exhibits 19 and 20, and changes in Exhibit 21.

Exhibit 19 - Proximus estimate summary

(in €m)	2018	2019e	2020e	2021e
Revenues (adjusted)	**5,806**	**5,685**	**5,647**	**5,594**
Growth yoy	0.5%	-2.1%	-0.7%	-0.9%
Incidentals	23	0	0	0
Revenue (reported)	**5,829**	**5,685**	**5,647**	**5,594**
EBITDA (adjusted)	**1,865**	**1,882**	**1,891**	**1,898**
EBITDA margin (adjusted)	32.1%	33.1%	33.5%	33.9%
Incidentals	-71	-45	-60	-56
EBITDA (reported)	**1,794**	**1,924**	**1,918**	**1,928**
Depreciation and amortisation	-1,016	-1,126	-1,129	-1,124
Operating income	**778**	**798**	**788**	**804**
Operating income (adjusted)	**849**	**843**	**848**	**860**
Net financial income	-56	-55	-55	-56
Associates	-1	0	0	0
Income before taxes	**721**	**743**	**733**	**748**
Tax expense	-191	-205	-195	-198
Minority interest	-22	-22	-22	-22
Net income	**508**	**516**	**516**	**527**
Net income (adjusted)	**561**	**549**	**561**	**569**
Growth yoy	0.4%	-2.1%	2.1%	1.4%
EPS (basic, reported, EUR)	1.57	1.60	1.60	1.63
EPS (basic, adjusted, EUR)	**1.74**	**1.70**	**1.74**	**1.76**
DPS (ordinary, EUR)	**1.50**	**1.50**	**1.50**	**1.50**
Capex	1,019	1,020	1,050	1,080
Net debt (company definition)	**2,148**	**2,134**	**2,107**	**2,103**

Source: Jefferies estimates, company data

Exhibit 20 - Proximus adj. revenue and EBITDA breakdown

(in €m)	2018	2019e	2020e	2021e
Revenue (adjusted)				
- Consumer Business Unit (CBU)	2,903	2,838	2,858	2,857
- Enterprise Business Unit (EBU)	1,413	1,410	1,394	1,377
- Wholesale	201	181	179	177
- Eliminations (domestic)	-57	-58	-58	-58
Domestic	4,460	4,371	4,373	4,353
Carrier Services (ICS)	1,347	1,313	1,274	1,241
Eliminations	-1	1	0	0
Total revenue (adjusted)	**5,806**	**5,685**	**5,647**	**5,594**
EBITDA (adjusted)				
Domestic	1,711	1,729	1,739	1,746
Carrier Services (ICS)	154	153	152	151
Group EBITDA (adjusted)	**1,865**	**1,882**	**1,891**	**1,898**

Source: Jefferies estimates, company data

Exhibit 21 - Proximus changes to estimates

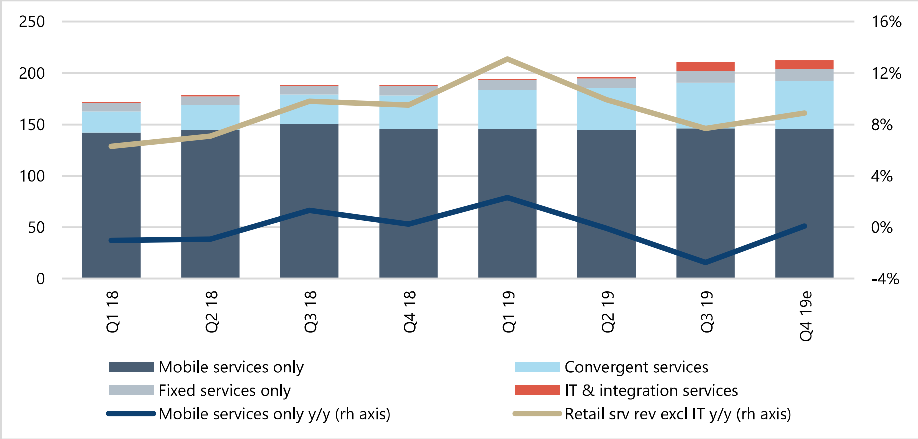
(in EUR m)	2019e	2020e	2021e
Revenues (adj) - New	**5,685**	**5,647**	**5,594**
Revenues (adj) - Old	5,670	5,618	5,573
Change	0.3%	0.5%	0.4%
EBITDA (adj) - New	**1,882**	**1,891**	**1,898**
EBITDA (adj) - Old	1,871	1,867	1,862
Change	0.6%	1.3%	1.9%
Depreciation - New	**-1,126**	**-1,129**	**-1,124**
Depreciation - Old	-1,094	-1,079	-1,073
Change	2.9%	4.7%	4.8%
EBIT (adj) - New	**843**	**848**	**860**
EBIT (adj) - Old	864	876	877
Change	-2.5%	-3.2%	-2.0%
PBT - New	**743**	**733**	**748**
PBT - Old	758	820	820
Change	-2.0%	-10.6%	-8.8%
Taxes - New	**-205**	**-195**	**-198**
Taxes - Old	-209	-217	-217
Change	-1.9%	-10.4%	-8.6%
Net income (adj) - New	**549**	**561**	**569**
Net income (adj) - Old	564	581	581
Change	-2.6%	-3.4%	-2.0%
EPS (adj) - New	**1.70**	**1.74**	**1.76**
EPS (adj) - Old	1.75	1.80	1.80
Change	-2.6%	-3.4%	-2.0%
DPS (ordinary) - New	**1.50**	**1.50**	**1.50**
DPS (ordinary) - Old	1.50	1.50	1.50
Change	0.0%	0.0%	0.0%
Capex - New	**1,020**	**1,050**	**1,080**
Capex - Old	1,004	994	987
Change	1.6%	5.6%	9.4%
FCF - New	**518**	**531**	**507**
FCF - Old	524	603	604
Change	-1.1%	-11.8%	-16.0%
Net debt - New	**2,134**	**2,107**	**2,103**
Net debt - Old	2,136	2,045	1,953
Change	-0.1%	3.0%	7.7%

Source: Jefferies estimates

Orange Belgium (OBEL BB, Buy, PT €23.9)

OBEL's strategy of levelling the competitive playing field through its fixed-mobile project is clearly working, in our view. Mobile-only service revenue remains stable in its own right (see dark bars/line in Exhibit 22), and the additional contribution from the convergence offers lifts overall service revenue into high single-digit percentage growth, well above that of peers at this time (light bars/line in Exhibit 22). We also refer to Exhibits 31 and 32 for the market context to these trends.

Exhibit 22 - OBEL Belgium retail service revenue trends



Source: Jefferies estimates, company data

Ultimately this reflects the fact that PROX and TNET had long used convergence as the key competitive tool as a differentiation tool against mobile-centric OBEL. Following regulatory intervention that opened the cable network to (forced) wholesale, OBEL is now competing on a more level playing field. In this sense, OBEL's success as shown in Exhibit 22 is not overly surprising in principle. The crucial question has been and is the sustainability of OBEL's cable resale. This has two components, OBEL's execution capabilities and regulatory support given TNET and VOO are not willing suppliers for obvious reasons.

We upgrade OBEL to Buy (from Hold) at a PT of €23.9 (prior €15.1) on the emerging track record for savvy execution and evidence for continued regulatory support.

- On execution, OBEL has positioned its convergence product in a future-proof and currently underserved segment of the market. Drastic competitive measures taken by PROX and TNET in response are proof of the effectiveness of OBEL's strategy, in our view. OBEL's cable momentum is already solid (see Exhibits 47 and 48) and likely to accelerate further on the latest product introduction (Love Duo), in our view. While Love Duo will clearly weigh on ARPU, we expect it to be accretive on strong intake. We forecast OBEL to more than triple revenues from convergence services by 2022e (to €351m) vs 2018 (€106m).
- On regulation, all indications are that OBEL will benefit from material further cuts to the regulated wholesale access tariffs. We discussed this in more detail in *New cable wholesale prices* (10 July 2019). The fact that these regulated cuts fall somewhat short of OBEL's public demands just mean that management has chosen an effective lobby position in the regulatory debate.

In addition, the painful drag in FY2019e from the loss of BASE MVNO customers to TNET will annualise from 1Q20e onwards and in fact reverse as high-margin MVNO revenues from Medialaan start to contribute.

We revisit the cable economics in this note and suggest that without overly aggressive assumptions, OBEL's FCF would expand materially from current levels. We forecast 10% OpFCF CAGR 2019e-22e, reflecting an increase of OpFCF forecasts by +10%/+11% in 2020e/21e.

Orange Belgium's share price has appreciated materially in 2019 (+22% TR), but against the background of strong execution and regulatory support, and the associated outlook for strong future FCF growth, we believe the current valuation leaves further upside. OBEL now trades on 14.2x 2020e EV/OpFCF, a premium to the sector on 12.7x. On strong forecast OpFCF growth, this trading multiple would reduce to 13.2x/11.1x already in 2021e/22e. Our PT of €23.9 would have OBEL on 16.2x 2020e EV/OpFCF, or 12.8x by 2022e.

Cable economics revisited

To start with, we outline an indicative scenario for OBEL's cable economics in Exhibit 23. The key point here is the impact of the reduced wholesale cost. We commented in the mentioned note from 10 July 2019 on the next regulatory step that should bring down the cost to about €16/line in from 2020e. While the decision has yet to be finalised, we believe the indications are that the draft will be close to the outcome. That c.€4 cost reduction alone should drive the EBITDA per customer close to break-even. Additionally, management has commented on the continuing measures to reduce other cost items such as repair cost in direct cost, and customer service in indirect cost. We also assume that the 'other' indirect cost remains about flat in absolute terms, which should lead to a dilution on per-line basis as shown in Exhibit 23 (scale effects).

Exhibit 23 - Love Trio indicative economics over time

(in €/month) per subscriber	2018e	2019e	2020e	2021e
Cable revenue per sub	**38.0**	**42.0**	**42.0**	**42.0**
Cable direct cost per sub	**-40.1**	**-35.3**	**-29.7**	**-29.7**
- wholesale	-23.4	-20.3	-16.2	-16.2
- content	-9.0	-9.0	-9.0	-9.0
- other	-7.7	-6.0	-4.5	-4.2
Cable gross profit per sub	**-2.1**	**6.7**	**12.3**	**12.3**
Cable indirect cost per sub	**-11.8**	**-8.4**	**-6.3**	**-5.5**
- customer service etc	-5.0	-4.0	-3.0	-2.8
- other	-6.8	-4.4	-3.3	-2.7
Cable opex per sub	**-51.9**	**-43.6**	**-36.0**	**-35.2**
Cable EBITDA per sub	**-13.9**	**-1.6**	**6.0**	**6.8**
- EBITDA margin	**-38.1%**	**-3.9%**	**14.4%**	**16.2%**

Source: Jefferies estimates, company information

We highlight that OBEL does not report its cable economics in any detail. Instead, management has made only summary comments on particular aspects at various points in time over the years. Therefore, the presentation in Exhibit 23 should not be taken literally - the point is to show the indicative impact of the regulatory decision.

Enabling a positive EBITDA contribution from cable alone is just a milestone, of course. After all, the project is absorbing material capex as well. Before getting into that in more detail, we address the impact of the new Love Duo product in Exhibit 24. Clearly, this is an ARPU-dilutive proposition. However, as management pointed out already on the 3Q19 call, the product comes with a different cost structure. In particular, the content costs drop away (no TV component) and the wholesale cost should be lower (as already contained in the regulator's draft proposal, see our mentioned report from 10 July 2019).

Exhibit 24 - Economics of Love Trio vs Duo (2020e)

(in €/month) per subscriber	Trio	Duo
Cable revenue per sub	**42.0**	**30.0**
Cable direct cost per sub	**-29.7**	**-17.7**
- wholesale	-16.2	-13.2
- content	-9.0	-
- other	-4.5	-4.5
Cable gross profit per sub	**12.3**	**12.3**
Cable indirect cost per sub	**-6.3**	**-6.3**
- customer service etc	-3.0	-3.0
- other	-3.3	-3.3
Cable opex per sub	**-36.0**	**-24.0**
Cable EBITDA per sub	**6.0**	**6.0**
- EBITDA margin	**14.4%**	**20.1%**

Source: Jefferies estimates

Again stressing the indicative nature of these analyses due to lack of definite information as discussed earlier, we note that the calculation in Exhibit 24 suggests EBITDA per line for Love Duo is in fact similar to Love Trio. This is a crucial point, of course. Love Duo addresses a segment of the Belgian market that is arguably underserved following the dominant players' tactics of loading more and more product into the offered bundles in order to justify price rises ('more for more'). Inasmuch as a 'skinny' bundle such as Love Duo should lead to further customer intake (OBEL's management suggested no less than 30% of the market might be addressable in this way), it should drive EBITDA accretion due to the similar EBITDA/line contribution.

What this means in practice is spelled out in Exhibit 25. We assume Love Duo intake runs at 30% of OBEL's total cable intake, which slows from 2021e onwards. The net add envelope is designed to get to a 27% (vs now 15%) convergence penetration in OBEL's postpaid mobile subscriber base, excluding m2m, by 2025e, assuming 1.4 mobile customers (SIMs) per line. We have also made some assumptions about churn in the two products, linked to PROX's disclosure of churn in its different product lines. This will be used to derive connection capex below.

Exhibit 25 - Orange Belgium cable subscriber scenario

(in '000s)	2018	2019e	2020e	2021e	2022e	2023e	2024e	2025e
Cable subscribers	**180**	**265**	**354**	**437**	**504**	**555**	**590**	**609**
- Love Trio	180	262	324	382	429	465	490	503
- Love Duo	0	3	30	55	75	90	101	106
Cable net adds	**77**	**85**	**89**	**83**	**67**	**51**	**35**	**19**
- Love Trio	77	82	62	58	47	36	25	13
- Love Duo	0	3	27	25	20	15	11	6
-- Duo % total net adds	0%	4%	30%	30%	30%	30%	30%	30%
Annual churn								
- Love Trio	6.5%	5.5%	5.5%	5.5%	5.5%	5.5%	5.5%	5.5%
- Love Duo	0.0%	0.0%	7.0%	7.0%	7.0%	7.0%	7.0%	7.0%
Gross adds	**86**	**97**	**106**	**105**	**94**	**81**	**68**	**54**
- Love Trio	86	94	78	78	69	60	51	41
- Love Duo	0	3	28	28	25	21	17	13

Source: Jefferies estimates, company data

We translate the indicative per-customer models in Exhibits 23 and 24 into an indicative cable revenue and EBITDA scenario in Exhibit 26. This is a merely technical result of prior assumptions. Exhibit 27 then models out a cable capex scenario. This assumes unit connection capex of €330 of which around €130 set-top box cost (management had talked about €350 with €130 STB for 2019, and the expectation that this could be reduced). We then assume about 1.3 STBs per line in Trio, and about €10m p.a. other capex that starts to expand with increasing scale over time. Overall this would take capex towards €40m by 2022e, i.e., cash break-even by then. Management had indicated cash break-even by late 2021e on a run-rate basis on the 3Q19 results call.

Exhibit 26 - Orange Belgium cable revenue/EBITDA scenario

(in €m)	2019e	2020e	2021e	2022e	2023e	2024e	2025e
Average revenue per subs (€)	**41.7**	**41.4**	**40.7**	**40.4**	**40.1**	**40.0**	**39.9**
- Love Trio	42.0	42.0	42.0	42.0	42.0	42.0	42.0
- Love Duo	0.0	30.0	30.0	30.0	30.0	30.0	30.0
Revenue	**111.4**	**153.6**	**193.3**	**227.8**	**255.0**	**274.8**	**287.3**
EBITDA	**-4.4**	**22.4**	**32.3**	**41.5**	**49.4**	**55.7**	**60.3**

Source: Jefferies estimates, company data

Exhibit 27 - Orange Belgium cable capex scenario

(in €m)	2019e	2020e	2021e	2022e	2023e	2024e	2025e
Connection capex/line excl STB (€)	200	200	200	200	200	200	200
STB cost (€)	130	130	130	130	130	130	130
Number of STB/line	1.3	1.3	1.3	1.3	1.3	1.3	1.3
Connection capex	35	35	34	30	26	22	18
Other capex (IT, network, etc)	10	10	10	10	10	10	10
Total cable capex	**45**	**45**	**44**	**40**	**36**	**32**	**28**

Source: Jefferies estimates, company data

The conclusion we can draw from this analysis is that under assumptions that we would consider not unduly optimistic, the OBEL's cable project would provide about €30m y/y tailwind to OpFCF in 2020e, and then around €10m p.a. until cash break-even in 2022e. In our view, this is a rather benign impact for a key project catching up with competitors in the area of convergence and thus preventing OBEL's core mobile business from relegation to a niche product in the Belgian market.

New estimates and changes

We summarise our new estimates in Exhibit 28 and changes in Exhibit 29.

Exhibit 28 - Orange Belgium P&L forecasts

(in €m)	2018	2019e	2020e	2021e
Total revenue	**1,280**	**1,327**	**1,423**	**1,489**
- growth y/y	2.7%	3.7%	7.3%	4.6%
EBTIDAaL (2018: Restated EBITDA)	**286**	**297**	**320**	**338**
- % total turnover	22.4%	22.4%	22.5%	22.7%
- % service+wholesale revenue	26.1%	34.6%	33.7%	33.3%
Add back: Lease costs	0	45	45	45
Restructuring and redundancy charges	-8	0	0	0
Consolidated EBITDA	**279**	**342**	**365**	**384**
D&A and impairment (incl RoU depreciation)	-236	-291	-291	-291
Result of operating activities (EBIT)	**43**	**51**	**75**	**93**
Net financial income	-5	-3	-3	-3
Result of operating activities after net finance costs	**38**	**48**	**71**	**90**
Tax Expense	-6	-12	-18	-22
Net profit	**32**	**36**	**54**	**67**
Adjustments for one-offs	6	0	0	0
Net profit (adjusted)	**39**	**36**	**54**	**67**
Weighted average number of ordinary shares	60	60	60	60
Basic EPS (€)	**0.54**	**0.60**	**0.90**	**1.13**
Basic EPS (€, adjusted)	**0.65**	**0.60**	**0.90**	**1.13**
Total DPS (€)	**0.50**	**0.50**	**0.55**	**0.60**
Capex (incl spectrum)	179	185	194	208
Net debt	**264**	**228**	**149**	**75**

Source: Jefferies estimates, company data

Exhibit 29 - Orange Belgium changes to estimates

(in EUR m)	2019e	2020e	2021e
Revenue - New	**1,327**	**1,423**	**1,489**
Revenue - Old	1,318	1,388	1,442
Change	0.6%	2.5%	3.2%
EBITDAaL - New	**297**	**320**	**338**
Restated EBITDA - Old	292	305	317
Change	1.7%	4.9%	6.7%
EBITDA - New	**342**	**365**	**384**
EBITDA - Old	336	349	361
Change	2.0%	4.8%	6.3%
D&A, impairment (incl RoU depreciation) - New	**-291**	**-291**	**-291**
D&A, impairment - Old	-279	-278	-278
Change	4.2%	4.6%	4.6%
EBIT - New	**51**	**75**	**93**
EBIT - Old	56	71	83
Change	-8.9%	5.7%	12.2%
PBT - New	**48**	**71**	**90**
PBT - Old	53	67	80
Change	-9.5%	6.0%	12.7%
Net income - New	**36**	**54**	**67**
Net income - Old	37	51	60
Change	-3.5%	6.0%	12.7%
EPS (adj, €) - New	**0.60**	**0.90**	**1.13**
EPS (adj, €) - Old	0.62	0.84	1.00
Change	-3.5%	6.0%	12.7%
DPS (€) - New	**0.50**	**0.55**	**0.60**
DPS (€) - Old	0.50	0.55	0.60
Change	0.0%	0.0%	0.0%
Capex (excl spectrum) - New	**185**	**194**	**208**
Capex (excl spectrum) - Old	183	191	200
Change	1.3%	1.8%	4.1%
OpFCF - New	**111**	**126**	**130**
OpFCF - Old	109	114	118
Change	2.3%	10.2%	11.0%
Net debt - New	**228**	**149**	**75**
Net debt - Old	195	128	65
Change	16.5%	16.3%	16.0%

Source: Jefferies estimates

Valuation

Our PT of €23.9 (prior €15.1) is derived from a DCF-based target valuation (see Exhibit 30), and corresponds to 16.2x 2020e EV/OpFCF as mentioned earlier (sector on 12.7x). The drivers of the increase to our prior PT are higher revenue estimates, on only fine-turned margin assumptions and now slightly lower capital intensity assumptions reflecting the room for cable capex reductions as highlighted in the earlier section on cable economics. Our PT implies a forecast 1-year total return of +23%, which corresponds to a Buy recommendation in the Jefferies system (prior: Hold).

Exhibit 30 - Orange Belgium DCF-based target valuation

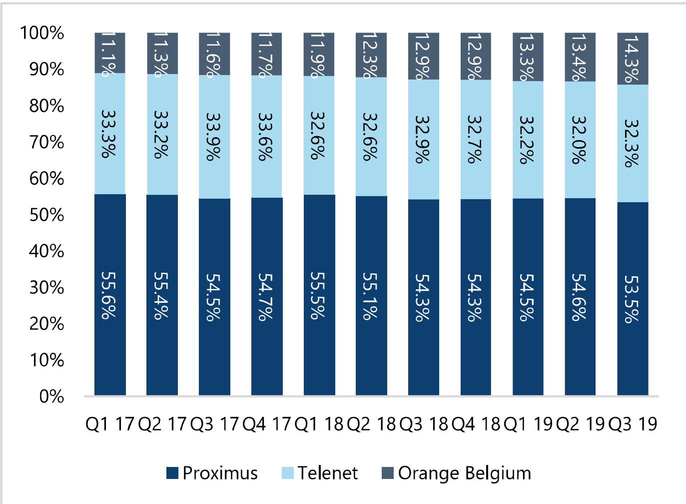
(in €m)	2019e	2020e	2021e	2022e	2023e	2024e	2025e	Term
Revenues	**1,327**	**1,423**	**1,489**	**1,545**	**1,588**	**1,618**	**1,635**	**1,635**
- Growth y/y	3.7%	7.3%	4.6%	3.8%	2.8%	1.9%	1.1%	0.0%
EBITDAaL	**297**	**320**	**338**	**355**	**368**	**379**	**387**	**392**
- EBITDA margin	22.4%	22.5%	22.7%	23.0%	23.2%	23.4%	23.7%	24.0%
D&A	-246	-246	-246	-246	-246	-246	-246	-213
- % sales	-18.5%	-17.3%	-16.5%	-15.9%	-15.5%	-15.2%	-15.0%	-13.0%
EBIT	**51**	**74**	**93**	**109**	**123**	**133**	**141**	**180**
Tax charge	-13	-19	-23	-27	-31	-33	-35	-45
- Tax rate	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%
NOPAT	**284**	**301**	**315**	**327**	**338**	**346**	**352**	**347**
Chg in working capital/other	1	3	2	2	1	1	1	0
Capex	-221	-194	-208	-208	-206	-204	-200	-213
- % sales	16.6%	13.6%	14.0%	13.4%	13.0%	12.6%	12.2%	13.0%
FCF	**64**	**111**	**110**	**122**	**133**	**143**	**153**	**135**
Discount period (years)	0.0	0.0	1.0	2.0	3.0	4.0	5.0	5.0
Discount factor	1.000	1.000	0.938	0.881	0.826	0.775	0.728	0.728
PV of FCF	**0**	**0**	**103**	**107**	**110**	**111**	**111**	**98**
Sum of PV of FCF	542							
PV of terminal value	1,496							
Total EV	**2,038**							
Other liabilities (incl spectrum)	-454							
Net debt, end-2020e	-149							
Equity Value	**1,435**							
No. shares (m)	60							
Value per share (€)	**€ 23.9**							

Source: Jefferies estimates

Belgian market backdrop

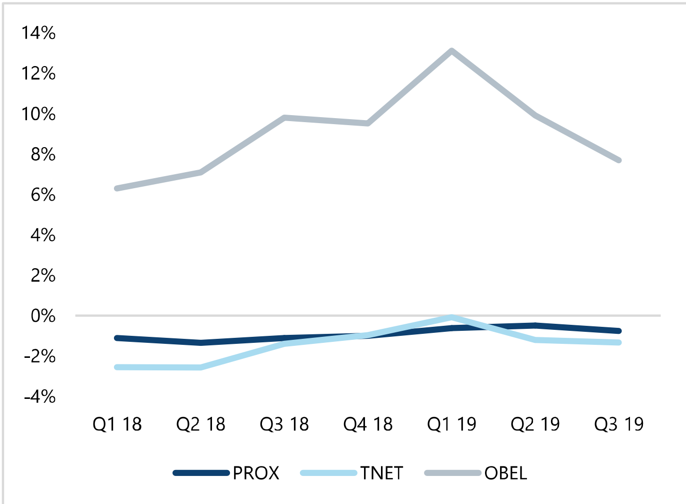
As discussed in more detail in the company sections above, disruptive competitive forces unleashed by regulatory intervention are changing the structure of the Belgian market. The aggregate picture is shown in Exhibits 31 and 32. OBEL's share recovery is enabled by regulated wholesale access to cable, allowing the company to compete in fixed-mobile convergence. We argued that the initial required heavy investments are past their peak and on a path towards break-even in the medium term.

Exhibit 31 - Belgium retail service revenue share



Source: Jefferies estimates, company data. Note: PROX shows CBU X-Play & prepaid revs plus EBU telecom service revs; TNET shows subscription revs; OBEL shows retail service revs

Exhibit 32 - Retail service revenue growth by operator y/y (adj)



Source: Jefferies, company data. Note: PROX CBU X-Play & prepaid plus EBU telco srv revs; TNET subscription revs rebased in co def, OBEL retail srv revs excl 'IT & Integration Services'

Convergence Pricing

In the company discussions above, we have repeatedly referred to the convergence product situation following OBEL's introduction of Love Duo in 2019. In the following, we provide more detailed context for reference.

Premium segment

In the premium segment, customers take 4P bundles with a comprehensive TV proposition. This has been the focus area for the initial convergence push by PROX and TNET. OBEL is less credible in this segment given that its 4P *Love Trio* bundle comes with a rather basic TV proposition, without even optional access to the sports content available from PROX & TNET.

As a result, competitive activity in the premium segment is relatively benign, in our view, as PROX and TNET have an incentive to up- and cross-sell their high-loyalty customers. Seasonal promotions typically last for only 3 months with discounts of ~30% at PROX and ~20% at TNET, which we would regard as 'normal'.

Comparing prices for 4P products between PROX and TNET is not a straightforward exercise, though. For example, TNET allows its customers to allocate the monthly mobile data allowance over up to 5 mobile SIMs at no extra cost and offers 3x the broadband speeds than PROX. However, PROX allows the subscriber of a 4P bundle to zero-rate one app of choice, and includes press content worth ~€30/month and one pay-TV add-on at no extra charge.

This lack of comparability is likely intentional, of course. In any case, taking the promotional discounts into consideration, we believe PROX's ~10% discount vs TNET won't be enough to lure customers away from TNET, given its slightly superior connectivity package (Exhibit 33).

We have included Wallonian cable operator Voo for completeness, but its lower-quality overall proposition poses a limited competitive threat to PROX, in our view, despite pricing its offers (i.e. Quatro Max) at a ~20% discount.

Exhibit 33 - Belgium - Pricing of 4P bundles in the premium segment

Convergence Pack	List price (€/mth)	Promo price (€/mth)	Promo time (mths)	One-off fees (€)	12-mth total price (€)	Mobile lines	Extra line option	Mobile voice (mins/line)	Fixed voice (mins)	TV channels	TV add-ons
PROX - Tuttimus (5GB)*	95.48	60.48	3	0	1,041	1x	Yes	120	Ultd	80+, 1x movie	1x free
TNET - WIGO S (6GB)	94.73			0	1,137	Up to 2x	Incl	Ultd	Ultd	80+ (60 HD)	optional
PROX - Tuttimus (15GB)*	106.48	71.48	3	0	1,173	1x	Yes	Ultd	Ultd	80+, 1x movie	1x free
TNET - WIGO (15GB)**	115.11	90.00	3	0	1,306	Up to 5x	Incl	Ultd	Ultd	80+ (60 HD)	optional
VOO - Quatro max	95.00	75.00	9	0	936	1x	Yes	Ultd	Ultd to fixed	70	1x free
PROX - Tuttimus (Ultd)	120.48	85.48	3	0	1,341	1x	Yes	Ultd	Ultd	80+, 1x movie	1x free
TNET - WIGO (Ultd)	203.74	160.00	3	0	2,314	Up to 5x	Incl	Ultd	Ultd	80+ (60 HD)	optional

Source: Jefferies, company website. Note: *PROX zero-rates one social media app of choice. **TNET zero-rates apps Yelo Play, Play Sports, WhatsApp and Facebook messenger.

Mid-tier segment

The mid-tier segment is the fiercely competitive part of the market where OBEL's disruptive impact is most clearly visible. OBEL appears to target predominantly its existing mobile customers who have fixed products from other providers. The size of this pool of customers at OBEL is still ~2.2m customers by 3Q19 representing ~85% of the mobile contract base ex m2m.

A second pool of targets are more price-sensitive fixed subscribers at PROX and TNET, who have been priced up by the historical 'more for more' strategies of the two incumbents. To retain such customers, PROX uses the *Minimus* product (3P ex fixed voice) and its value brand *Scarlet*. By contrast, TNET seems to have surrendered this segment to OBEL, relying instead on the associated wholesale fees collected from OBEL, in our view. For example, TNET does not offer a 3P (mobile, BB, TV) bundle. Instead, customers must select the Internet+TV plan and then separately add the mobile option.

Pricing in this segment is shown in Exhibit 34. At the headline level, TNET prices its plan at an average 56% premium to OBEL's Love Trio bundles. Even when adjusting *Love Trio* for the 300Mbps speed boost (+€10/month), the premium drops to a still significant average of 36%. By contrast, PROX's price premium for its *Minimus* plans to OBEL is much narrower, but still visible at an average of 24%.

Exhibit 34 - Belgium - Pricing of 3P bundles in the mid-tier segment & average price premia to OBEL

Convergence Pack	List price (€/mth)	List premium to OBEL	Promo price (€/mth)	Promo time (mths)	One-off fees (€)	12-mth total price (€)	Mobile lines	Mobile data (GB/line)	BB speed (Mbps)	Fixed voice (mins)	TV channels	TV add-ons
TNET - All-Internet, TV, Mobile (6GB)	108.07	69%	96.48	3	0	1,262	1x	6	300/20	-	80+ (60 HD)	optional
PROX - Minimus (5GB)*	75.99	19%	55.99	3	0	852	1x	5	100/6	-	80+	optional
OBEL - Love Trio (Dolphin)	64.00		56.50	3	49	795	1x	3	100/5	-	70+ (46 HD)	-
TNET - All-Internet, TV, Mobile (6GB)	108.07	57%	96.48	3	0	1,262	1x	6	300/20	-	80+ (60 HD)	optional
VOO - Trio max (mobile)	87.45	27%	72.45	9	0	890	1x	12	400/20	-	70	1x free
PROX - Minimus (15GB)*	86.99	26%	66.99	3	0	984	1x	15	100/6	-	80+	optional
VOO - Trio relax (fixed)	68.45	-1%	58.45	6	0	761	-	-	125/6.5	Ultd to fixed	70	optional
OBEL - Love Trio (Koala)	69.00		59.00	3	49	847	1x	8	100/5	-	70+ (46 HD)	-
PROX - Minimus (30GB)*	96.99	23%	76.99	3	0	1,104	1x	30	100/6	-	80+	optional
OBEL - Love Trio (Cheetah)	79.00		64.00	3	49	952	1x	30	100/5	-	70+ (46 HD)	-
TNET - All-Internet, TV, Mobile (Ultd)	111.59	41%	100.00	3	0	1,304	1x	Ultd	300/20	-	80+ (60 HD)	optional
PROX - Minimus (Ultd)*	100.99	28%	80.99	3	0	1,152	1x	Ultd	100/6	-	80+	optional
OBEL - Love Trio (Eagle)	79.00		59.00	3	49	937	1x	Ultd	100/5	-	70+ (46 HD)	-

TNET premium to OBEL	**56%**
TNET premium to OBEL (adj for BB speed boost)	**36%**
PROX premium to OBEL	**24%**

Source: Jefferies, company data. Note: *PROX zero-rates one social media app of choice.

Mid-tier segment 'light'

At the beginning of 3Q19, OBEL launched its pure FMC 2P bundles, *Love Duo,* which are ~€15/month cheaper than the *Love Trio* plans, but do not include TV.

To preempt any adverse churn impacts on their respective customer base from these new bundles, PROX and TNET introduced new products, *Epic combo* and *Yugo*. These offers are specifically positioned to attract the millennial group within the customer base.

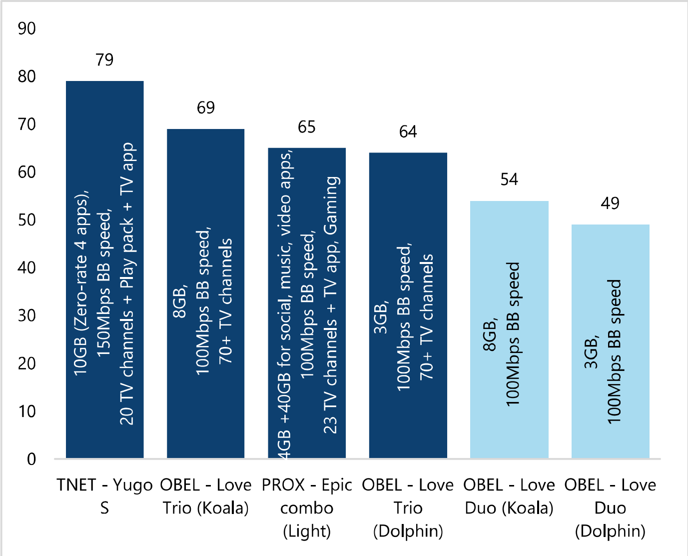
A common denominator of *Love Duo*, *Epic combo* and *Yugo* is the absence of a fixed line. However, *Love Duo* neither includes TV content nor does it offer extra data or zero-rates specific apps (Epic combo and Yugo do).

In Exhibits 35 and 36, we compare all three and OBEL's *Love Trio* plans.

- PROX's *Epic combo* plans look attractive. The price premium to *Love Duo* plans of up to €16/month is justified by the availability of 40GB extra data for a wide selection of popular apps and the inclusion of TV content, in our view. Of course, a consumer only interested in a basic fixed-mobile plan would prefer OBEL or PROX's value brand *Scarlet*, for which comparable tariffs start at €42/month (5GB/50Mbps BB speed).
- TNET's *Yugo* plans look visibly mispriced and are up to €25/month more expensive in the FMC 'light' and up to €38/month in the FMC 'light+' segment vs *Love Duo* plans.

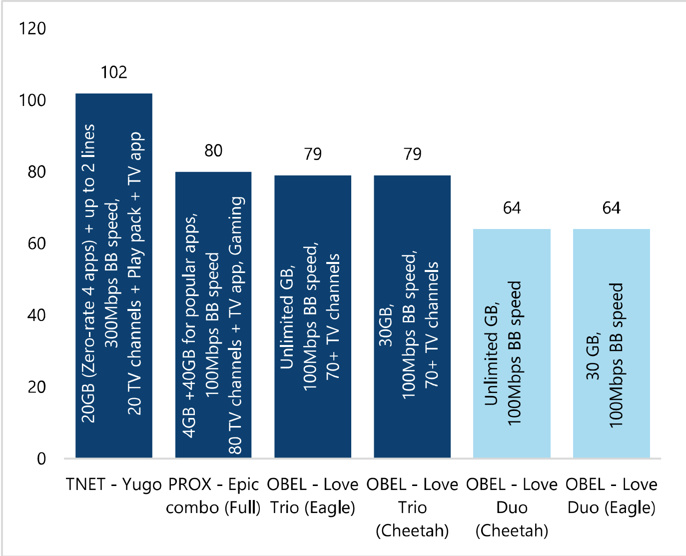
Such a divergence in pricing strategies supports our conclusion that PROX is fighting more aggressively to retain its price-sensitive customers - even at the cost of risking ARPU dilution. By contrast, TNET seems willing to let price-sensitive customers churn to OBEL, given that it can re-capture a portion of the associated lost revenue via cable wholesale revenues.

Exhibit 35 - Belgium 3P "light" FMC bundles



Source: Jefferies, company website

Exhibit 36 - Belgium 3P "light+" bundles



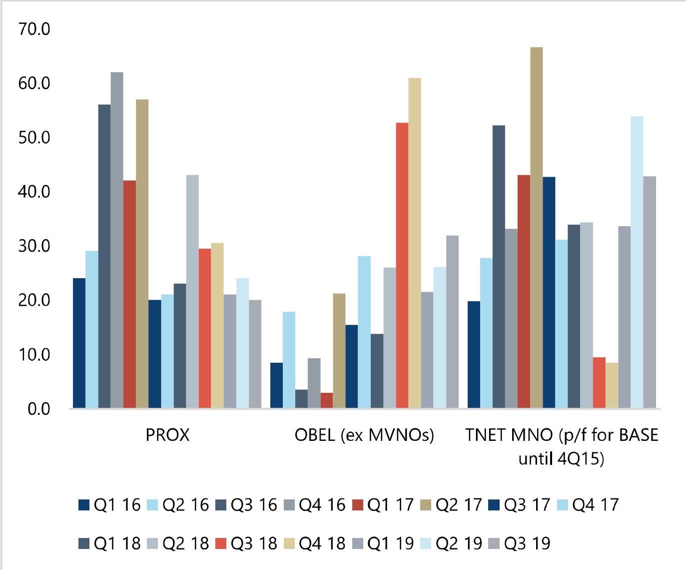
Source: Jefferies, company website

Belgium mobile

Commercial trends in the mobile market are increasingly driven by FMC. Between the two incumbents, TNET likely has the better prospects in this regard due to its lag (31% of its fixed broadband customers currently also take a mobile plan compared to 55% at PROX). In fact, PROX's mobile penetration into its fixed broadband base seems to be slowing already on base effects as discussed in the PROX company section. In 2018/19, penetration has merely expanded by +0.3/+0.4p.p. at PROX vs TNET at +1.5/+2.2p.p.

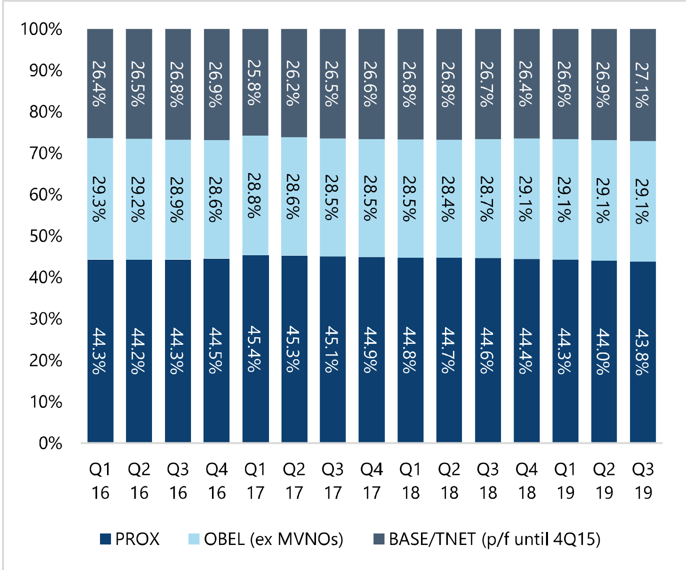
In terms of subscriber numbers, this 'catch-up' has been especially visible since the beginning of 2019, with net postpaid intake at TNET outpacing PROX/OBEL in each quarter (see Exhibit 37), reflecting aggressive cross-selling efforts (TNET is the only operator that allows sharing mobile data over multiple lines) and a revamp of its mobile tariff portfolio in 1Q19. This has translated into share gain of +0.7p.p. since 4Q18 - primarily at the expense of PROX (-0.6p.p.) with virtually no change at OBEL (see Exhibit 48). Given TNET's headroom in cross-selling mobile into fixed relative to PROX, we expect current share trends to continue.

Exhibit 37 - Belgium postpaid net adds (excl m2m, excl Proximus' free data cards)



Source: Jefferies, company data

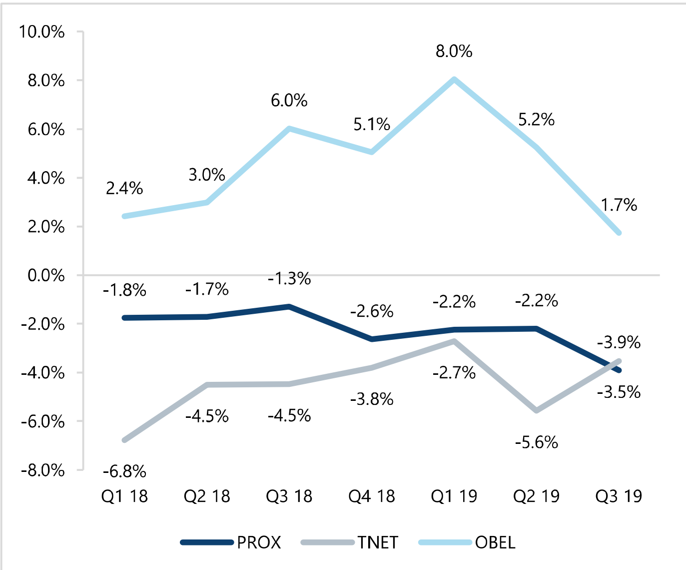
Exhibit 38 - Belgium postpaid subscriber share (excl m2m, excl Proximus' free data cards)



Source: Jefferies, company data

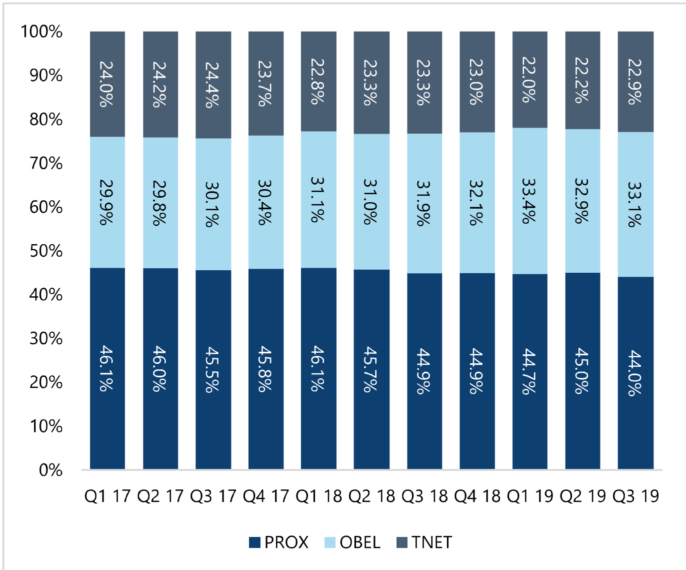
OBEL's mobile service revenue growth remains well ahead of peers in 3Q at +1.7% y/y on our estimates vs TNET/PROX at -3.5%/-3.9% y/y (Exhibit 39), continuing a trend of consistent gaining share expansion (Exhibit 40). Recent slow-downs in MSR growth at OBEL and the accelerated decline at PROX primarily reflects headwinds from the introduction of intra-EU call regulation and lower out-of-bundle revenues due to the proliferation of higher data plans in the market.

Exhibit 39 - Mobile service revenue growth by operator y/y



Source: Jefferies, company data

Exhibit 40 - Mobile service revenue share by operator

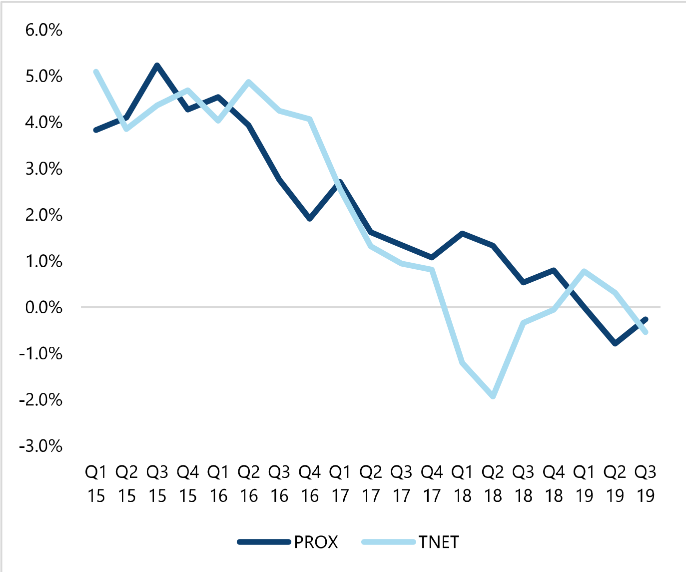


Source: Jefferies, company data

Belgium fixed

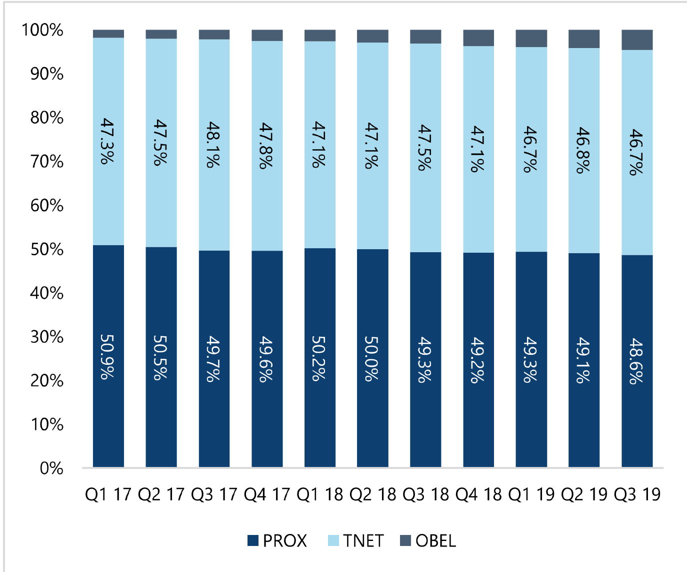
Revenue trends in the fixed market are driven by mainly two factors. (1) Structural decline in legacy fixed voice that is only partially offset by bundling these services into FMC plans and (2) competitive pressures unleashed by the regulatory decision to give operators wholesale access to cable networks. These factors have led to a consistent drop in fixed service revenues at PROX and TNET from as high as 5% in 2015 to a slight decrease in 3Q19 (see Exhibit 41). We believe that structural and competitive revenue pressure on PROX/TNET's fixed business will persist but revenue share loss to OBEL (see Exhibit 42) to come through only gradually given OBEL's cable project is still relatively small in scale and management will likely focus on profitability over accelerated customer share gain, in our view.

Exhibit 41 - Fixed service revenue growth by operator y/y



Source: Jefferies, company data

Exhibit 42 - Fixed service revenue share by operator



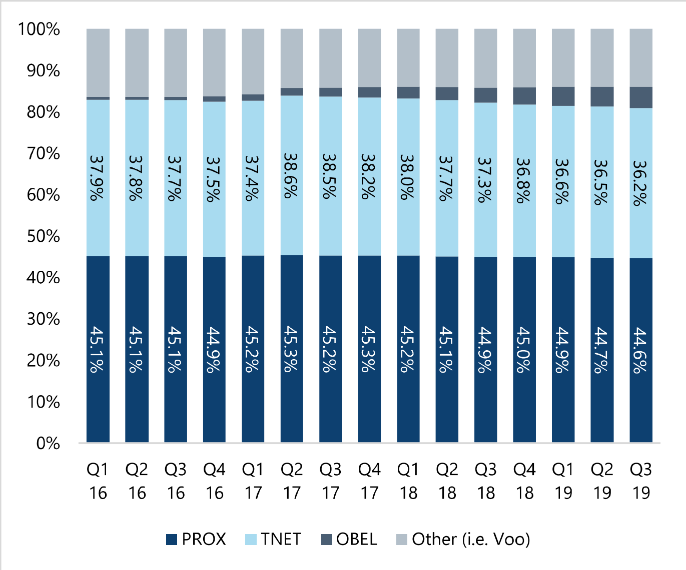
Source: Jefferies, company data

OBEL's impact on the commercial performance of its peers is evident - in particular on TNET that seems to have left the value segment to OBEL in return for high-margin wholesale revenues. By contrast, PROX defends its share decisively and attempts to prevent churn by capturing the price-sensitive customers within its base via its value brand Scarlet. The introduction of Epic (an offer designed for millennials) is positioned to compete with OBEL's recently launched dualplay FMC plan (see a more detailed pricing analysis further below).

This strategic approach has had success. PROX has defended a fixed broadband market share at around 45% since the market entry of ORA late-2016 (Exhibit 43). By contrast, TNET has served as the main share donor to OBEL that has accumulated ~4p.p. over the same time period. As OBEL's convergence activities seem to have mainly focused on the Flemish region so far, we do not observe material market share movements in the 'Other' (i.e. Wallonian cable operator Voo).

TNET's severe customer losses in 3Q/4Q were the result of churn during the integration of acquired SFR customers - from which OBEL has clearly benefited (Exhibit 44).

Exhibit 43 - Belgium fixed broadband subscriber shares



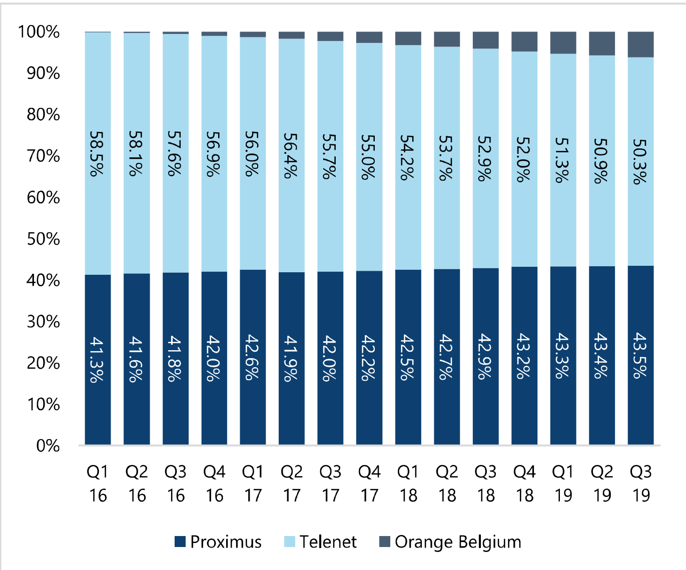
Source: Jefferies, company data, BIPT. Note: Telenet's 2Q17 organic and adjusted for SFR BeLux acquisition

Exhibit 44 - Belgium fixed broadband net intake (in '000s)

Source: Jefferies, company data. Note: Telenet's 2Q17 adjusted for SFR BeLux acquisition

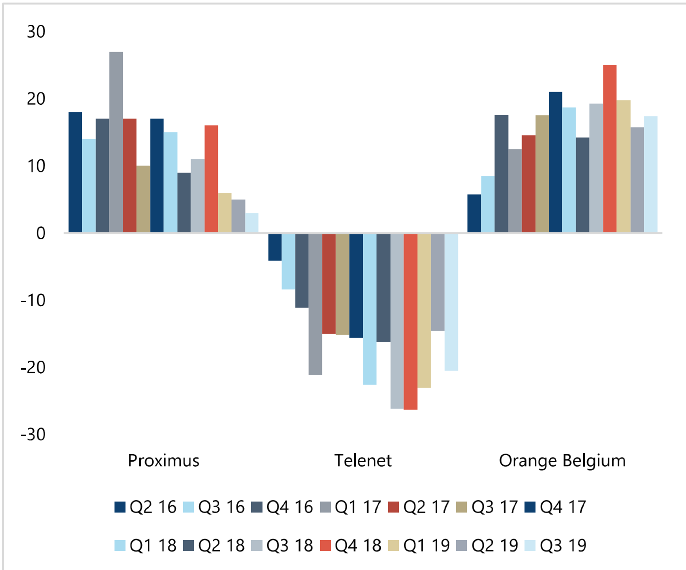
Share and subscriber trends in fixed broadband are mirrored in the pay-TV segment (see Exhibits 45 and 46). TNET serves as the main share donor to OBEL, and more recently a pronounced slowdown in net intake at PROX suggests that upselling momentum is fading there as well, in our view.

Exhibit 45 - Belgium pay-TV subscriber shares



Source: Jefferies, company data

Exhibit 46 - Belgium pay-TV net intake (in '000s)

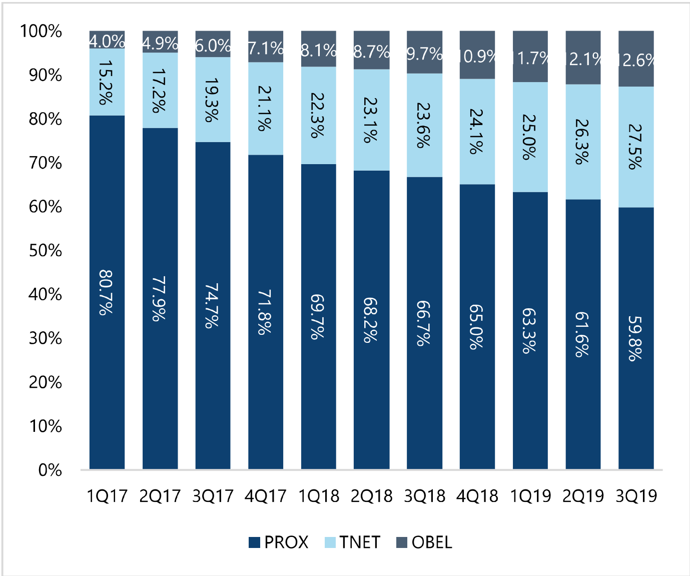


Source: Jefferies, company data. Note: Telenet's 2Q17 adjusted for SFR BeLux acquisition

Belgium convergence

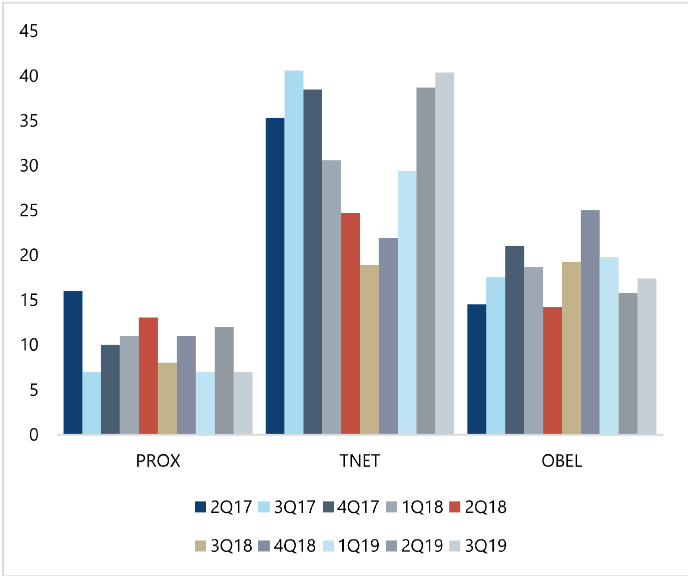
In the FMC segment (see Exhibit 47 and 48), customer trends are primarily driven by (a) the extent to which PROX and TNET have already pushed FMC into their respective fixed broadband customer bases, with TNET lagging PROX as mentioned earlier, and (b) OBEL's share gain reflecting its disruptive pricing strategy as discussed earlier.

Exhibit 47 - Belgium fixed-mobile convergence share



Source: Jefferies, company data

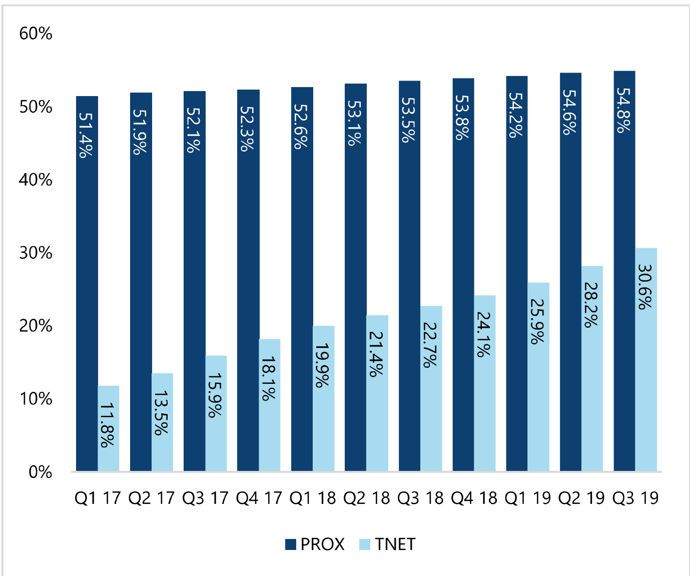
Exhibit 48 - Belgium fixed-mobile convergence net adds ('000s)



Source: Jefferies, company data

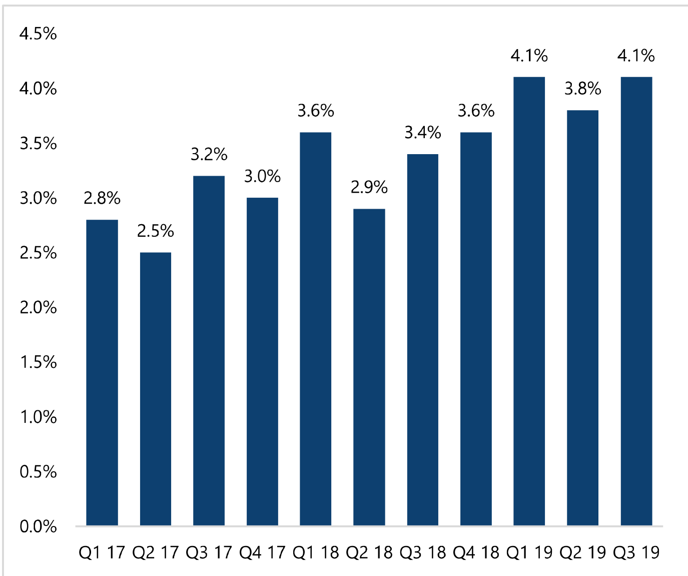
Exhibit 49 provides the data on the penetration differential. Specifically for PROX, which reports detailed churn metrics, we note an uptick in 4P churn in the flagship Tuttimus plan (Exhibit 50). 4P churn rates have slowly crept up from an annualised 2.8% in 1Q17 to 4.1% by 3Q19, suggesting a mix of competitive pressure and/or customers trading down (possibly to the lower-priced Epic bundles). We see further downside risk from the introduction of skinnier and cheaper FMC bundles such as PROX's own Epic, TNET's Yugo but also OBEL's Love Duo, as discussed in the company section.

Exhibit 49 - FMC subs as % of fixed broadband customers



Source: Jefferies, company data

Exhibit 50 - Proximus - Annulised 4P full churn rate



Source: Jefferies, company data

Detailed estimate tables

Proximus

Exhibit 51 - Proximus P&L forecasts

(in EUR m)	2018	2019e	2020e	2021e
Revenues (adjusted)	**5,806**	**5,685**	**5,647**	**5,594**
- Growth yoy	0.5%	-2.1%	-0.7%	-0.9%
Incidentals	23	0	0	0
Revenues (reported)	**5,829**	**5,685**	**5,647**	**5,594**
EBITDA (adjusted)	**1,865**	**1,882**	**1,891**	**1,898**
- Growth yoy	2.3%	0.9%	0.5%	0.4%
EBITDA margin (adjusted)	**32.1%**	**33.1%**	**33.5%**	**33.9%**
Incidentals	-71	-45	-60	-56
EBITDA (reported)	**1,794**	**1,924**	**1,918**	**1,928**
Depreciation and amortisation	-1,016	-1,126	-1,129	-1,124
Operating income	**778**	**798**	**788**	**804**
Operating income (adjusted)	**849**	**843**	**848**	**860**
Net financial income	-56	-55	-55	-56
Associates	-1	0	0	0
Income before taxes	**721**	**743**	**733**	**748**
Tax expense	-191	-205	-195	-198
Minority interest	-22	-22	-22	-22
Net income	**508**	**516**	**516**	**527**
Net income (adjusted)	**561**	**549**	**561**	**569**
Number of shares (basic, period-end)	338	338	338	338
Number of treasury shares (basic, period-end)	15	15	15	15
Number of shares (basic, period-avg)	323	323	323	323
EPS (basic, reported, EUR)	**1.57**	**1.60**	**1.60**	**1.63**
EPS (basic, adjusted, EUR)	**1.74**	**1.70**	**1.74**	**1.76**
DPS (interim, EUR)	0.50	0.50	0.50	0.50
DPS (final, EUR)	1.00	1.00	1.00	1.00
DPS (ordinary, EUR)	**1.50**	**1.50**	**1.50**	**1.50**
DPS (special, EUR)	0.00	0.00	0.00	0.00

Source: Jefferies estimates, company data

Exhibit 52 - Proximus cash flow statement forecasts

(in EUR m)	2018	2019e	2020e	2021e
Cash-flow from operating activities				
Net income (group share)	**508**	**516**	**516**	**527**
Adjustments for:				
- Minority interests	22	22	22	22
- Depreciation and amortisation	1,016	1,126	1,129	1,124
- Fixed asset impairment	23	0	0	0
- Provisions	-4	0	0	0
- Deferred tax expense	-16	10	10	10
- Impairment on participating interests	0	0	0	0
- Associate income	1	0	0	0
- Fair value adjustments on financial instruments	0	0	0	0
- Loans amortisation	2	0	0	0
- Gain on disposal of consolidated companies	0	-6	0	0
- Gain on disposal of other participating interests and associate	0	0	0	0
- Gain on disposal of PP&E	-22	-1	0	0
- Other non-cash movements	-1	3	3	3
Operating cash flow before working capital	**1,530**	**1,670**	**1,680**	**1,686**
Decrease/(increase) in working capital	**28**	**0**	**0**	**0**
Net cash flow provided by operating activties	**1,558**	**1,670**	**1,680**	**1,686**
Cash flow from investing activities				
Purchase of intangible assets and property, plant and equipmer	-1,099	-1,033	-1,063	-1,093
Cash paid for acquisitions of other participating interests	-3	-1	0	0
Cash paid for consolidated companies	-51	-40	0	0
Dividends received from non-consolidated companies	1	0	0	0
Cash received from sales of consolidated companies, net of casl	0	9	0	0
Cash received from sales of intangible assets and PP&E	37	0	0	0
Cash received from sales of other non-current assets	8	0	0	0
Net cash used in investing activities	**-1,107**	**-1,065**	**-1,063**	**-1,093**
Cash flow from financing activities				
Dividends paid to shareholders	-485	-484	-484	-484
Dividends paid to minority interests	-28	-29	-29	-29
Net acquisition/disposal of treasury shares	4	9	9	9
Purchase of investments	1	0	0	0
Increase of shareholders' equity	-4	0	0	0
Issuance/(repayment) of long term debt	-1	-31	46	52
Lease payments	0	-87	-87	-87
Issuance/(repayment) of short term debt	68	0	0	0
Net cash provided by/(used in) financing activities	**-444**	**-622**	**-545**	**-538**
Net increase/(decrease) of cash and cash equivalents	**7**	**-17**	**73**	**56**
Cash and cash equivalents at the beginning of the period	**333**	**340**	**323**	**396**
Cash and cash equivalents at the end of the period	**340**	**323**	**396**	**452**

Source: Jefferies estimates, company data

Exhibit 53 - Proximus balance sheet forecasts

(in EUR m)	2018	2019e	2020e	2021e
Assets				
Current assets				
Inventories	129	129	129	129
Trade receivables	1,042	1,042	1,042	1,042
Contract assets	83	83	83	83
Current income tax assets	68	68	68	68
Other current assets	155	155	155	155
Investments	4	4	4	4
Cash and cash equivalents	340	323	396	452
Asset classified as held for sale	0	0	0	0
Current assets	**1,822**	**1,804**	**1,877**	**1,933**
Non-current assets				
Goodwill	2,470	2,470	2,470	2,470
Intangible assets with finite useful life	1,154	1,154	1,154	1,154
Property, plant and equipment	3,054	3,070	3,075	3,115
RoU asset	0	327	327	327
Contract costs	116	116	116	116
Enterprises accounted for under the equity method	0	0	0	0
Other participating interests	0	1	1	1
Deferred income tax assets	12	12	12	12
Pension assets	0	0	0	0
Other non-current assets	43	43	43	43
Non-current assets	**6,850**	**7,193**	**7,198**	**7,238**
Total assets	**8,671**	**8,998**	**9,075**	**9,171**
Liabilities and equity				
Current liabilities				
Interest-bearing liabilities	234	234	234	234
Provisions for pensions and similar obligations	0	74	74	74
Lease liabilities	0	74	74	74
Trade payables	1,361	1,361	1,361	1,361
Contract liabilities	109	109	109	109
Income tax payables	56	56	56	56
Other current payables	578	578	578	578
Liabilities associated with assets classified as held for sale	0	0	0	0
Current liabilities	**2,338**	**2,486**	**2,486**	**2,486**
Non-current liabilities				
Interest-bearing liabilities	2,263	2,232	2,278	2,330
Lease liabilities	0	260	260	260
Provisions for pensions and similar obligations	553	553	553	553
Provisions	142	142	142	142
Deferred income tax liabilities	91	101	111	121
Other non-current payables	132	120	107	95
Non-current liabilities	**3,181**	**3,408**	**3,451**	**3,501**
Shareholders' equity	**3,005**	**2,972**	**3,013**	**3,066**
Minority interests	**148**	**141**	**134**	**127**
Total liabilities and equity	**8,671**	**9,007**	**9,084**	**9,180**
Net debt				
Net debt (company definition)	2,148	2,134	2,107	2,103

Source: Jefferies estimates, company data

Orange Belgium

Exhibit 54 - Orange Belgium P&L forecasts

(in €m)	2018	2019e	2020e	2021e
Total revenue	**1,280**	**1,327**	**1,423**	**1,489**
- growth y/y	2.7%	3.7%	7.3%	4.6%
EBTIDAaL (2018: Restated EBITDA)	**286**	**297**	**320**	**338**
- % total turnover	22.4%	22.4%	22.5%	22.7%
- % service+wholesale revenue	26.1%	34.6%	33.7%	33.3%
Add back: Lease costs	0	45	45	45
Restructuring and redundancy charges	-8	0	0	0
Consolidated EBITDA	**279**	**342**	**365**	**384**
D&A and impairment (incl RoU depreciation)	-236	-291	-291	-291
Result of operating activities (EBIT)	**43**	**51**	**75**	**93**
Net financial income	-5	-3	-3	-3
Result of operating activities after net finance costs	**38**	**48**	**71**	**90**
Tax Expense	-6	-12	-18	-22
Net profit	**32**	**36**	**54**	**67**
Adjustments for one-offs	6	0	0	0
Net profit (adjusted)	**39**	**36**	**54**	**67**
Weighted average number of ordinary shares	60	60	60	60
Basic EPS (€)	**0.54**	**0.60**	**0.90**	**1.13**
Basic EPS (€, adjusted)	**0.65**	**0.60**	**0.90**	**1.13**
Total DPS (€)	**0.50**	**0.50**	**0.55**	**0.60**

Source: Jefferies estimates, company data

Exhibit 55 - Orange Belgium cash flow statement forecasts

(in €m)	2018	2019e	2020e	2021e
Cash flow from operating activities				
Consolidated net income	**32**	**36**	**54**	**67**
Non-cash adjustments for:				
- Tax Expense	6	12	18	22
- Net finance costs	5	3	3	3
- Depreciation, amortisation and impairment (before lease cost	236	246	246	246
- Other	3	16	13	13
Adjusted result of operating activities before net finance co	**281**	**359**	**378**	**397**
Net changes in working capital	38	1	3	2
Operating taxes and levies paid	-26	-13	-13	-13
Interest paid	-4	-2	-2	-2
Tax paid	-29	-10	-18	-22
Net cash from operating activities	**261**	**334**	**349**	**362**
Cash from investing activities				
Purchase of intangible and tangible assets	-179	-185	-194	-208
Debt associated to purchase of assets	-1	-20	0	0
Acquisition of investments and businesses	-4	-35	0	0
Net cash used in investing activities	**-185**	**-241**	**-194**	**-208**
Cash flows from financing activities				
Long-term borrowings - repayments	-50	0	0	0
Short-term borrowings - net	15	0	0	0
Own shares issued/acquired	2	0	0	0
Dividends paid	-30	-30	-30	-33
Net cash used in financing activities	**-63**	**-77**	**-77**	**-80**
Net increase/decrease in cash and cash equivalents	**13**	**16**	**78**	**74**
Cash and cash equivalents at the beginning of the period	**13**	**27**	**43**	**121**
Cash and cash equivalents at the end of the period	**26**	**43**	**121**	**196**

Source: Jefferies estimates, company data

Exhibit 56 - Orange Belgium balance sheet forecasts

(in €m)	2018	2019e	2020e	2021e
Assets				
Non-current assets				
Goodwill	67	67	67	67
Intangible assets	285	285	285	285
Tangible assets	772	712	660	622
RoU asset	0	285	285	285
Interest in associates	4	5	5	5
Non-current financial assets	3	3	3	3
Other non-current assets	1	1	1	1
Deferred taxes	3	3	3	3
Total non-current assets	**1,136**	**1,361**	**1,310**	**1,272**
Current assets				
Inventories	28	29	31	33
Trade receivables	194	200	214	224
Other current assets	78	110	110	110
Cash and cash equivalents	27	43	121	196
Total current assets	**327**	**382**	**477**	**563**
Total assets	**1,463**	**1,744**	**1,787**	**1,835**
Equity and liabilities				
Total equity	**587**	**596**	**619**	**654**
Non-current liabilities				
Long-term interest-bearing borrowings	270	250	250	250
Non-current lease liabilities	0	237	237	237
Other non-current liabilities	68	68	68	68
Deferred taxes	8	8	8	8
Total non-current liabilities	**346**	**563**	**563**	**563**
Current liabilities				
Short-term interest bearing borrowings	21	21	21	21
Current lease liabilities	0	46	46	46
Trade payables	267	274	294	308
Employee benefits related liabilities	31	31	31	31
Current taxes payables	3	5	5	5
Liabilities related to contracts with customers	59	59	59	59
Other payables	149	149	149	149
Total current liabilities	**530**	**585**	**605**	**619**
Total liabilities	**876**	**1,148**	**1,168**	**1,182**
Total equity and liabilities	**1,463**	**1,744**	**1,787**	**1,835**
Net debt				
Net debt	**264**	**228**	**149**	**75**

Source: Jefferies estimates, company data

PROXIMUS (PROX BB)

RATING	PRICE	MARKET CAP
UNDERPERFORM	€25.23^	€8.5B / $9.5B
PRICE TARGET (PT)	**UPSIDE SCENARIO PT**	**DOWNSIDE SCENARIO PT**
€20.70 (FROM €23.10)	€28.00	€15.80

^Prior trading day's closing price unless otherwise noted.

Estimates				
€	2018A	2019E	2020E	2021E
Consensus EPS	-	1.68	-	-
Previous				
EPS	1.74	1.70	1.74	1.76
Previous		1.75	1.80	1.80

Valuation				
	2018A	2019E	2020E	2021E
P/Rev	1.5x	1.5x	1.5x	1.5x
Div. Yield	5.95%	5.95%	5.95%	5.95%
FCF Yield	5.31%	6.42%	6.18%	5.87%
FY P/E	14.5x	14.8x	14.5x	14.3x

EPS: JEF adjusted

The Long View

Scenarios

Base Case

- Competitive friction intensifying, catalysed in particular by disruptive cable resale project by Orange Belgium.
- PROX faces universal cable coverage and a cable network that is in the process of being upgraded to Docsis 3.1.
- Cash flow risks from potential competitive pressure, fibre capex and changes to tax code.
- Limited flexibility on cost trends due to strong labour protection and wage inflation.
- Target multiple: 12.3x 2020e EV/OpFCF; target price: €20.7.

Upside Scenario

- Orange Belgium fails with cable resale project (e.g., on execution or lack of regulatory support).
- Better mobile data monetisation on usage growth combined with relative unit price stability.
- Cost cutting beyond indicated plans despite structural impediments.
- Broadband market consolidation (i.e. Voo).
- Target multiple: 15.3x 2020e EV/EBITDA; target price: €28.0.

Downside Scenario

- Orange Belgium's cable resale launch gains more traction than anticipated.
- Competitive imbalances cause mobile price disruption, limiting upside from underlying mobile data volume growth.
- Cable operators push more aggressively for market share in fixed (or mobile).
- Macro pressure on fiscal tightening driven by high government debt.
- Potential new entrant in mobile market.
- Target multiple: 10.3x 2020e EV/EBITDA; target price: €15.8.

Investment Thesis / Where We Differ

- Orange Belgium's catch-up in fixed-mobile convergence is a strategic necessity and aligned with regulatory interests – threatening to dilute the benefits from Proximus' successful fixed-mobile strategies pursued since 2007.
- Proximus is defending position through ARPU-dilutive alternatives ('Scarlet' value brand, Epic offer aimed at millenials) which risk revenue pressure even on share defence.
- Even after rebasing the DPS level from 2014 onwards, the dividend is not well covered by forecast free cash flow, presumably on the wishes of the controlling owner (Belgian government, holds 53.5% of PROX).

Catalysts

- Newsflow on progress with renewal of fixed market regulation.
- Newsflow on potential new market entry in mobile.
- Spectrum auction (postponed to likely late 2020e).
- 4Q19 results: 21 February 2020.
- 1Q20 results: 30 April 2020.
- 2Q20 results: 31 July 2020.
- 3Q20 results: 30 October 2020.

ORANGE BELGIUM (OBEL BB)

RATING	PRICE	MARKET CAP
BUY	€20.60^	€1.2B / $1.4B
PRICE TARGET (PT)	**UPSIDE SCENARIO PT**	**DOWNSIDE SCENARIO PT**
€23.90 (FROM €15.10)	€28.10	€17.60

^Prior trading day's closing price unless otherwise noted.

Estimates				
€	2018A	2019E	2020E	2021E
EPS	0.65	0.60	0.90	1.13
Previous		0.62	0.84	1.00
Consensus EPS	-	0.66	-	-
Previous				

Valuation				
	2018A	2019E	2020E	2021E
Div. Yield	2.43%	2.43%	2.67%	2.91%
FCF Yield	6.50%	6.60%	8.74%	8.69%
FY P/E	31.7x	34.3x	22.9x	18.2x

The Long View

Scenarios

Base Case

- Solid progression in mobile core business (share and ARPU).
- Successful cable resale project based on continued regulatory support (wholesale access terms), enabling further convergence upsell at improving margins.
- Continued solid cost control.
- Material OpFCF expansion on EBITDA growth and capex control.
- Target multiple: 16.2x 2020e EV/OpFCF; target price: €23.9.

Upside Scenario

- Stronger-than-expected mobile data growth.
- Good market pricing discipline in mobile.
- Strong progress with cable resale.
- Successful participation in potential market consolidation.
- Better-than-expected net cost savings.
- Potential minority buy-out interest by majority shareholder Orange.
- Target multiple: 18.2x 2020e EV/OpFCF; target price: €28.1.

Downside Scenario

- Execution issues in cable resale, and/or fading regulatory support on cable wholesale conditions – limiting Orange Belgium's progress on convergence.
- Increased competitive intensity in Belgian mobile (pricing, device subsidies).
- Unexpected need for high capex even beyond currently guided scale.
- Potential new entrant in mobile market as a result of the (postponed) Belgian spectrum auction.
- Target multiple: 13.2x 2020e EV/OpFCF; target price: €17.6.

Investment Thesis / Where We Differ

- Orange Belgium delivers rather solid progression in its core mobile business.
- The cable resale project is critical to a catch-up in fixed-mobile convergence. Evidence for successful execution is mounting, e.g., the introduction of the well-positioned 'Love Duo' product in 2019.
- Incumbent competitors (PROX/TNET) have limited ability to fend off the OBEL convergence challenger tacts due to their already material convergence base.
- Start-up investments in cable/convergence to turn into EBITDA accretion and eventual cash break-even on regulatory support (wholesale access terms).

Catalysts

- Newsflow on progress with renewal of fixed market regulation.
- Newsflow on potential new market entry in mobile.
- Spectrum auction (postponed to likely late 2020e).
- 4Q19 results: 5 February 2020.

Company Description

Orange Belgium

Orange Belgium is the #2 mobile network operator in Belgium, offering services in both the consumer and corporate segments. The company started to resell cable infrastructure to end-customers in 2016. Orange Belgium also operates in Luxembourg, where it provides mobile and fixed services. Orange Belgium is 53% owned by Atlas Services Belgium (ASB), which is 100% controlled by Orange.

Proximus

Proximus is the Belgian telecommunication incumbent, offering a full-service portfolio in its home market. The company is also a major provider of international carrier services, in particular to mobile operators. Proximus operates in the Luxembourg mobile market through its subsidiary Tango. The Belgian state holds 53.5% of outstanding shares.

Company Valuation/Risks

Orange Belgium

Our PT of €23.9 is based on a DCF valuation and corresponds to 16.2x 2020e EV/OpFCF. Risks to the upside include a potentially better trading environment, in particular on data monetisation, cost-cutting ahead of expectations, and better-than-expected cable resale traction. To the downside, we mention execution risks at the cable resale project, regulation (in particular of cable resale), potential new market entry in mobile, and high capex intensity.

Proximus

Our PT of €20.7 is derived from a DCF-based SOTP valuation and corresponds to 12.3x 2020e EV/OpFCF. Risks to the upside include potential execution failures at OBEL's cable project, better mobile data monetisation, better upsell momentum, a more benign pricing and promotional development in the market, and even better cost control. To the downside, we mention OBEL's cable resale project, regulation, potential new market entry in mobile, and fixed broadband competition from cable.

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(Article 3(1)e and Article 7 of MAR)

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Rating and Price Target History for: Proximus (PROX BB) as of 01-10-2020

Rating and Price Target History for: Orange Belgium (OBEL BB) as of 01-10-2020

Notes: Each box in the Rating and Price Target History chart above represents actions over the past three years in which an analyst initiated on a company, made a change to a rating or price target of a company or discontinued coverage of a company.

Legend:

I: Initiating Coverage

D: Dropped Coverage

B: Buy

H: Hold

UP: Underperform

Distribution of Ratings

Distribution of Ratings						
			IB Serv./Past12 Mos.		JIL Mkt Serv./Past12 Mos.	
	Count	Percent	Count	Percent	Count	Percent
BUY	1210	52.65%	105	8.68%	15	1.24%
HOLD	933	40.60%	31	3.32%	4	0.43%
UNDERPERFORM	155	6.74%	1	0.65%	0	0.00%

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