

Telecommunications

PROX and OBEL To Share Mobile Networks

12 July 2019

Key Takeaway

PROX and OBEL announced plans to share their mobile radio networks while maintaining operational independence. Cost savings are material and credible - we estimate net upside of €0.4/€1.1 per share for PROX/OBEL from the first 10 years, i.e., material upside particularly for OBEL. The regulatory stance might be supportive because the co-operation does not impinge on differentiation and competition, and supports industrial policy goals (coverage, road to 5G).

PROX and OBEL to share radio networks. PROX and OBEL have signed a term sheet aimed at reaching an agreement to consolidate the radio access (RAN) elements of their mobile networks into a 50-50 JV. The two companies would maintain operational independence (no sharing of customer data) and continue to serve their end-customers using only their respective spectrum holdings (retains a degree of ability to differentiate). The partners aim to finalise an agreement by year-end and to start preliminary work in 1Q20e. The sharing agreement includes all mobile technologies (i.e. 2G/3G/4G/5G) and would increase the coverage for both operators by about 20% vs the stand-alone case.

Regulatory stance. The company releases do not mention any regulatory views that they might have solicited in preparation. However, we believe the regulatory stance may not be much of an issue. There is precedence elsewhere in Europe (similar arrangements are in place in Sweden, for example, and have been agreed in Italy), the companies stress that they retain their ability to compete and differentiate their offerings in the end-market, and the agreement is presented as well aligned with industrial policy goals (better coverage as mentioned, faster time-to-market for 5G). If there is an issue, it may relate to where this leaves TNET – we view this as a potential regulatory consideration.

Material financial upside implied. PROX targets an annual cash flow benefit of €35-€40m by 2024 from initial gross investments of €140m in 2021-23 (net of ramping savings €75m). OBEL expects cumulative opex/capex savings of €300m over 10 years with initial costs of €130m over 3 years. These cost savings seem credible to us. What is less clear is what base case these savings are calculated against. This is relevant when assessing implied upside. If management had planned a more material mid-term capex step-up than expected by consensus, the savings vs the *mgmt case* would not necessarily translate to upside to *market expectations*. That said, we provide an indicative valuation in Tables 1 and 2 on page 2. For the first 10 years of the co-operation, we calculate an NPV of around €119m for Proximus, or €0.4/share, corresponding to 1% upside to the current share price. If we add a terminal value assuming zero perpetual growth, this rises to 5% upside. For OBEL, we obtain €63m for the first 10 years, or €1.1/share (6% upside to current share price), rising to 25% if we add a TV. The OBEL implications look material, and we highlight that our model implies an IRR for the first 10 years of 21.0%, corresponding to 3.2x WACC – quite consistent with OBEL's specific indication that the project would have a return of 3x WACC for the first 10 years.

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^Prior trading day closing price unless otherwise noted.

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Exhibit 1 - Proximus - Value-accretion per share from network-sharing deal

(in €m)	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Term.
Savings		7	20	35	50	50	50	50	50	50	50	50
Set-up cost	-10	-43	-43	-43								
Tax impact	3	9	6	2	-13	-13	-13	-13	-13	-13	-13	-13
Total FCF	-8	-27	-18	-6	38	38	38	38	38	38	38	38
Discount factor	1.000	0.941	0.886	0.834	0.785	0.738	0.695	0.654	0.615	0.579	0.545	0.545
Discounted FCF	-7.5	-25.6	-15.5	-5.2	29.4	27.7	26.1	24.5	23.1	21.7	20.4	20.4
PV (Yr 0-10)	119											
- per share (€)	0.4											
- % share price	1%											
Add: Terminal value (g=0%)	327											
NPV	446											
- per share (€)	1.4											
- % share price	5%											

Source: Jefferies estimates, company data. Note: Tax treatment simplified, assuming tax impact of capex at time of spending (rather than actually at time of depreciation).

Exhibit 2 - Orange Belgium - Value-accretion per share from network sharing deal

(in €m)	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Term.
Savings		5	15	25	36	36	36	36	36	36	36	36
Set-up cost	-10	-60	-60									
Tax impact	3	14	11	-6	-9	-9	-9	-9	-9	-9	-9	-9
Total FCF	-8	-41	-34	19	27	27	27	27	27	27	27	27
Discount factor	1.000	0.938	0.881	0.826	0.775	0.728	0.683	0.641	0.601	0.564	0.530	0.530
Discounted FCF	-7.5	-38.7	-29.7	15.5	21.2	19.9	18.7	17.5	16.4	15.4	14.5	14.5
PV (Yr 0-10)	63											
- per share (€)	1.1											
- % share price	6%											
Add: Terminal value (g=0%)	220											
NPV	284											
- per share (€)	4.7											
- % share price	25%											

Source: Jefferies estimates, company data. Note: Tax treatment simplified, assuming tax impact of capex at time of spending (rather than actually at time of depreciation).

Company Valuation/Risks

Liberty Global plc

Our PT of \$33 is derived from a DCF-based SOTP valuation and corresponds to 6.2x 2019e EV/OCF (continuing operations). Downside risks include high financial leverage, which would amplify operational issues from competitive, macroeconomic or regulatory pressure. The footprint expansion adds particular execution risk. Also, concentrated control and heavy use of financial derivatives. Two transformative deals (with Vodafone and Sunrise) are agreed but have not yet received the required approvals by regulators and/or shareholders.

Orange Belgium

Our PT of €15.1 is based on DCF valuation and corresponds to 12.7x 2019e 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, the company's ability to mitigate the loss of MVNO revenues, regulation (in particular of cable resale), still high mobile market price levels, potential new market entry in mobile, and high capex intensity.

Proximus

Our PT of €23.1 is derived from a DCF-based SOTP valuation and corresponds to 5.7x 2019e EV/EBITDA. 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, still high mobile market price levels, potential new market entry in mobile, and fixed broadband competition from cable.

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- Liberty Global plc (LBTYA: \$27.18, BUY)
- Orange Belgium (OBEL BB: €18.76, HOLD)
- Proximus (PROX BB: €25.16, HOLD)

Rating and Price Target History for: Liberty Global plc (LBTYA) as of 07-10-2019



Rating and Price Target History for: Orange Belgium (OBEL BB) as of 07-10-2019



Rating and Price Target History for: Proximus (PROX BB) as of 07-10-2019



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.

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Distribution of Ratings						
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