

China Telecoms Sector

Stocks at bargain prices

- We are raising our tower-business valuation; industry checks suggest government intervention risks have subsided
- Upgrading our ratings for China Telecom and China Unicom to Buy (1) from Outperform (2)
- Reaffirming Positive sector view; China Mobile remains our top pick, followed by China Telecom and then China Unicom

Negative Neutral Positive



Positive
(unchanged)

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What's new: The China Telecoms sector stocks have sold off in the past year by 10-32% on investor concerns over tariff intervention risks and new entrant threats, which appear overplayed to us. After our talks with industry players, we now see the operational outlook for the sector as slightly better than our previous expectation as the competitive environment appears to be benign. We now see deep value in **China Telecom (728 HK, HKD3.44)** and **China Unicom (762 HK, HKD7.87)**, and lift our ratings for both stocks to Buy (1) from Outperform (2). Despite having the least upside potential to our TP, **China Mobile (941 HK, HKD86.75, Buy [1])** remains our top pick for its large index weighting, low earnings volatility and 4G dominance.

What's the impact: We are raising our valuation for the tower company by 26% to CNY170bn (previously CNY135bn; see [What does tower spin-off mean for 2016?](#), 10 March 2016), after revising up our 2016-18E net profit for the tower company by 12-62%. In fact, we believe the tower company could be worth up to CNY282bn, depending on the valuation approach and underlying assumptions. The tower company's IPO is likely to take place in 2017, and we believe sector stocks could run up in the lead-up to such an event. Also, recent developments suggest to us that tariff intervention risks in the near term have diminished. Thus, we are lifting our 2016-18E sector EBITDA by 0.3-2% on the back of a better service revenue growth outlook.

Meanwhile, news of the awarding of a "basic telecom" licence to China Broadcasting Network (CBN) has spooked investors, raising questions over possible entry of a fourth mobile operator. After speaking to industry players, we believe the risks are overplayed in the near term, especially considering the significant challenges — spectrum and capital resources — that need to be surmounted before the threat becomes realistic. As such, we believe the recent depressed share-price performances present attractive entry points for the 3 stocks under our coverage.

What we recommend: Driven by upward adjustments to our valuations of both the tower and core telecom businesses, and incorporating a weaker CNY-HKD rate (1.16 versus 1.19 before), we revise our SOTP-based 12-month TPs as follows: HKD108.70 for China Mobile (from HKD110.80), HKD11.50 for China Unicom (from HKD10.10) and HKD4.58 for China Telecom (HKD4.42 previously). Greater-than-anticipated competitive pressure would be the main risk to our view on all 3 stocks.

How we differ: Even though our sector earnings forecasts are well below the Bloomberg consensus, which we attribute to differing views on the impact of tower leases, we believe sector stocks could still rally as valuations are depressed.

Key stock calls

	New	Prev.
China Mobile (941 HK)		
Rating	Buy	Buy
Target	108.70	110.80
Upside	▲ 25.3%	
China Unicom (762 HK)		
Rating	Buy	Outperform
Target	11.50	10.10
Upside	▲ 46.1%	
China Telecom (728 HK)		
Rating	Buy	Outperform
Target	4.58	4.42
Upside	▲ 33.1%	

Source: Daiwa forecasts

Sector stocks: key indicators

Company Name	Stock code	Share Price	Rating		Target price (local curr.)			EPS (local curr.)					
			New	Prev.	New	Prev.	% chg	FY1			FY2		
								New	Prev.	% chg	New	Prev.	% chg
China Mobile	941 HK	86.75	Buy	Buy	108.70	110.80	(1.9%)	5.043	5.001	0.8%	5.894	5.842	0.9%
China Telecom	728 HK	3.44	Buy	Outperform	4.58	4.42	3.6%	0.196	0.188	3.9%	0.240	0.233	3.2%
China Unicom	762 HK	7.87	Buy	Outperform	11.50	10.10	13.9%	0.085	0.041	107.8%	0.224	0.181	23.8%

Source: Bloomberg, Daiwa forecasts

China Telecoms Sector: key sector assumptions

	2010	2011	2012	2013	2014	2015	2016E	2017E	2018E
China Mobile									
Subscribers (m)									
Mobile	584.0	649.6	710.3	767.2	806.6	826.2	847.2	870.7	894.2
4G only	0.0	0.0	0.0	0.0	90.1	312.3	543.1	684.0	801.5
Fixed broadband						55.0	70.0	82.0	88.0
Adjusted ARPU (CNY)									
Mobile	73.1	71.3	68.7	66.6	61.6	56.4	58.0	59.5	60.4
Broadband						27.7	32.0	33.0	33.9
Others									
Capex (CNY bn)	113.4	123.4	123.4	139.4	170.8	172.5	186.2	160.0	152.0
EBITDA margin (%)	49.3%	47.5%	45.3%	38.2%	36.7%	35.9%	34.3%	35.6%	35.5%
Capex / Service revenue (%)	25.6%	24.3%	22.7%	31.3%	36.7%	33.5%	29.9%	24.3%	22.0%
China Unicom									
Subscribers (m)									
Mobile	167.4	199.7	239.3	281.0	299.1	286.7	264.7	278.7	292.7
4G only	0.0	0.0	0.0	0.0	2.1	44.2	100.2	159.7	219.2
Fixedline	92.9	92.0	87.6	82.1	73.9	67.7	63.7	61.7	62.9
Fixed broadband	55.7	63.9	64.6	68.8	72.3	75.3	78.8	82.3	83.5
Adjusted ARPU (CNY)									
Mobile	43.6	46.9	47.9	48.4	44.6	40.6	44.4	47.5	48.3
Fixedline	28.7	25.2	22.0	20.7	18.3	16.0	15.7	15.4	15.1
Broadband	57.9	57.1	54.9	59.6	62.7	63.7	62.5	61.2	60.0
Others									
Capex (CNY bn)	75.6	77.9	86.8	72.8	69.6	88.5	75.0	73.1	71.8
EBITDA margin (%)	34.8%	30.3%	29.2%	28.5%	32.6%	31.6%	28.8%	29.1%	29.6%
Capex / Service revenue (%)	42.8%	41.2%	47.5%	30.8%	34.7%	56.9%	31.1%	29.0%	27.0%
China Telecom									
Subscribers (m)									
Mobile	90.5	126.5	160.6	185.6	185.6	197.9	212.1	229.5	246.9
4G only	0.0	0.0	0.0	0.0	7.1	58.5	119.0	184.2	245.0
Fixedline	169.6	163.0	155.8	143.6	134.3	127.3	122.3	117.3	118.5
Fixed broadband	76.8	90.1	100.1	107.0	113.1	121.6	127.6	131.6	133.6
Adjusted ARPU (CNY)									
Mobile	54.3	52.4	53.9	54.8	54.0	54.1	54.5	55.1	55.4
Fixedline	28.6	24.1	21.7	20.2	18.7	17.8	17.0	16.6	16.2
Broadband	77.1	72.2	66.6	62.1	59.2	56.3	54.0	53.5	52.9
Others									
Capex (CNY bn)	41.6	48.5	50.0	70.9	80.3	101.9	97.0	85.0	82.3
EBITDA margin (%)	34.5%	30.8%	25.0%	30.0%	29.2%	28.4%	26.6%	27.6%	28.8%
Capex / Service revenue (%)	20.1%	21.5%	20.8%	28.2%	26.8%	37.2%	31.6%	26.1%	24.0%

Source :Companies, Daiwa forecasts; note: December year end for all 3 operators

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Stocks at compelling prices

What's changed?

Following our recent industry discussions, we are revising our SOTP-based target prices for the China Telecom sector-stocks as follows: down 1.9% for China Mobile, up 13.9% for China Unicom and up 3.6% for China Telecom. The revisions are driven by the following factors:

Our SOTP changes are driven by higher tower-company valuations and a better core business outlook, set against a weaker CNY assumption

We are raising our 2017-18E EBITDA forecasts by 0.5-1.6% on the back of slightly higher revenue forecasts, as we believe tariff intervention risks have receded for the short term. As a result, we are revising up our 2017-18E free cash flow forecasts by 1.2-1.9% for China Mobile, 1.6-4.6% for China Unicom, and 1.8-2.5% for China Telecom. Accordingly, and after incorporating a weaker CNY exchange rate (CNY-HKD cross rate of CNY1.16 vs. 1.19 before) we are adjusting our core telecom business valuations by: -2.3% for China Mobile, +7.1% for China Unicom and +0.6% for China Telecom.

We are increasing the forecast profit contribution from the tower company by 6.8-24% over 2017-18E, driven by higher revenue forecasts. In addition, we are raising our valuation for the tower company by 26%, from CNY135bn (which was based on a 2016E price-to-book ratio of 1.0x), to CNY170bn, which is now based on a 2016E price-to-book ratio of 1.3x. For reasons that we elaborate on in later sections of this report (see "How much is the tower company worth?"), we believe the higher price-to-book multiple is justified and could be realized over the coming year as the tower-company is likely to seek an IPO in 2017. Accordingly, and after taking into account weaker CNY-HKD exchange rates (1.16 versus 1.19 before) and changes in the diluted share capital of the companies (China Unicom's diluted share base decreased by 3.4% in 2015 due repayment of its convertible bonds) the valuation attributable to the tower company stake increases by around 24-28% for the 3 stocks in our coverage universe.

China Telecoms Sector: key revisions to valuations

HKD/share	Telecom business	Tower	Investments	Total Fair value	CNY/HKD
China Mobile					
New	102.1	3.7	2.9	108.70	1.16
Previous	104.9	3.0	3.0	110.80	1.19
Change (%)	-2.7	23.7	-2.2	-1.9	-2.5
China Unicom					
New	9.2	2.3		11.50	1.16
Previous	8.3	1.8		10.10	1.19
Change (%)	10.2	27.8		13.9	-2.5
China Telecom					
New	3.9	0.68		4.58	1.16
Previous	3.9	0.55		4.42	1.19
Change (%)	0.6	24.1		3.5	-2.5

Source: Daiwa

China Telecoms Sector: key revisions to forecasts

(in %)	Service Revenue	EBITDA	Profit from tower	Net profit	FCF
China Mobile					
2017E	0.1	0.7	17.8	0.9	1.2
2018E	0.3	0.9	6.8	1.8	1.9
China Unicom					
2017E	0.1	1.2	24.0	23.8	1.6
2018E	0.3	1.6	12.4	15.1	4.6
China Telecom					
2017E	0.3	0.5	24.0	3.2	2.5
2018E	0.5	0.9	12.4	3.8	1.8

Source: Daiwa forecasts

We are upgrading our ratings on China Telecom and China Unicom to Buy (1)

Given the upside potential we see relative to our new target prices, we are upgrading our ratings on China Telecom and China Unicom to Buy (1) from Outperform (2). At the same time, we reaffirm our Buy (1) rating on China Mobile.

Potential share-price catalysts: improvement in ARPU metrics, tower company IPO news

We view the depressed share-price performances in the sector over the past 1 year (-10% to -32%) as presenting attractive entry points. We believe the upcoming results season, where we expect improvement in average revenue per user (ARPU) metrics among sector stocks, as well as news flow pertaining to the tower company's planned IPO in 2017, could be a key share-price catalyst.

Stock selection: China Mobile remains our top pick, followed by China Telecom then China Unicom

Our revised 2016-18E earnings forecasts for all 3 stocks are still below those of the Bloomberg consensus. This could be because we are more bearish on the EBITDA margin prospects for the companies compared with the market; while the operators are likely to face cost pressures over 2016-18 due to tower-lease payments, it is unclear to what extent these pressures are mitigated by savings elsewhere – notably in the areas of network maintenance charges. This could be a key source of variance between Daiwa and the consensus forecasts.

Sector valuations remain compelling, in our view

Despite this, we believe sector valuations are attractive, particularly on the EV/EBITDA measure, and thus expect share prices to rally over the coming year, driven by quarterly results and news flow on the tower company. In the quarterly results, we look for improving trends in ARPU metrics as a validation of our positive investment thesis on the sector.

China Unicom offers the greatest upside potential to our target price, followed by China Telecom and then China Mobile. However, this 'upside potential' measure doesn't take into account the volatility of earnings and returns involved. As such, and after considering potential risk-adjusted returns, we arrive at the following relative preferences in the sector.

Among the 3 stocks, we have a preference for China Mobile. This is because: 1) its EV/EBITDA valuation discount relative to its past-12-year trading history is roughly in the same range as its peers (7% discount vs. 12% discounts for China Telecom and Unicom), 2) it has a large weighting in several emerging markets and China-related benchmarks, thus having the potential to contribute to portfolio performance, 3) the company has less earnings volatility than its peers due to its larger earnings base, and 4) it has a dominant market share in 4G and an improving position in fixed line.

Between China Telecom and Unicom, we prefer the former due to its superior operational momentum – it has been gaining market share in 4G and we expect this trend to continue. We view China Unicom as an undervalued stock, whose value could be crystallised once the tower company's IPO plans gain ground over the next few months.

China Telecoms Sector: Daiwa forecasts relative to Bloomberg consensus forecasts

(in %)	2016E	2017E	2018E
Revenues			
China Mobile	1	3	3
China Unicom	(1)	0	1
China Telecom	(0)	1	3
EBITDA			
China Mobile	(4)	(1)	(2)
China Unicom	(6)	(6)	(5)
China Telecom	(3)	(0)	4
Net profit			
China Mobile	(3)	(4)	(5)
China Unicom	(68)	(47)	(33)
China Telecom	(18)	(11)	(5)

Source: Daiwa forecasts, Bloomberg

China Telecoms Sector: 2016-17E blended valuations

	EV/EBITDA (x)	PER (x)	PBR (x)
China Mobile	4.4	14.2	1.5
China Unicom	3.7	56.5	0.7
China Telecom	3.7	14.1	0.8
Past-12-year average			
China Mobile	4.7	12.4	2.3
China Unicom	4.2	31.8	1.1
China Telecom	4.2	13.7	1.2
Premium/Discount to average			
China Mobile	(7)	14	(33)
China Unicom	(12)	78	(31)
China Telecom	(12)	3	(33)

Source: Bloomberg, Daiwa forecasts

Outlook

The sector's outlook over the next few years is likely to be influenced by developments pertaining to 5 key issues. They are: 1) the prospect of government intervention on tariffs, 2) regulations relating to the real-name registration and asymmetric interconnection policies, 3) new-entrant threats, 4) the nature and extent of cooperation between China Telecom and China Unicom, and 5) the impact of the tower company on profitability and valuations.

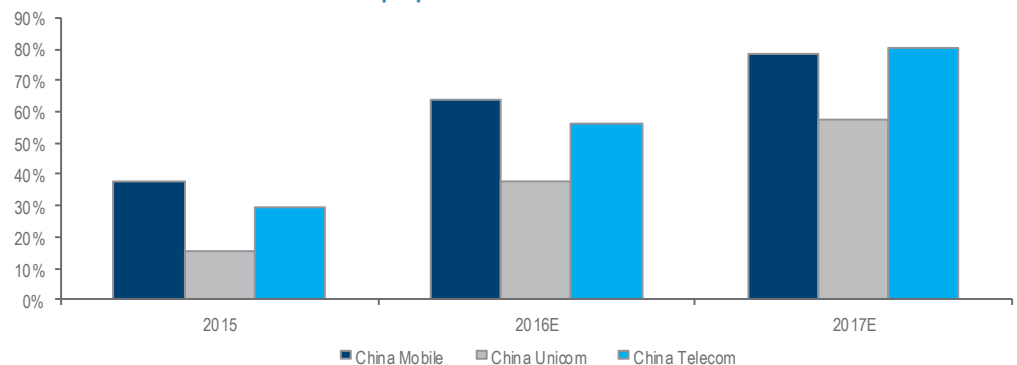
Prospects for further government intervention on tariffs are low

The regulator, the Ministry of Industry and Information Technology (MIIT) directed the mobile operators to abolish domestic roaming tariffs in 3 provinces — Beijing, Tianjin and Hebei — in August 2015 and asked them in 4Q15 to allow their customers to carry over unused data allowances for an additional one-month period. These 2 measures pressured industry revenues in 2015.

4G flat-rate plans are not affected by cuts in domestic roaming tariffs

Given this history, the market has been expecting some degree of tariff intervention again in 2016. However, in May 2016, the MIIT left it to operators to proactively reduce domestic roaming tariffs across the nation instead of mandating an immediate cut across the 27 provinces/municipal areas that were not previously covered. This is a positive outcome for the mobile operators, in our view, because: 1) domestic roaming tariffs are a relevant issue only for 2G and 3G users, as 4G users are charged on a flat-rate basis, and 2) the passage of time makes the issue less relevant, as we expect the proportion of 4G users to increase significantly over the next few years, thus mitigating the overall negative revenue impact.

China Telecoms Sector: 4G users as proportion of total customer base



Source: Companies, Daiwa forecasts

Real-name registration issue likely to have slight negative impact on subscriber growth

Real SIM registration threshold raised to 95% by end-2016

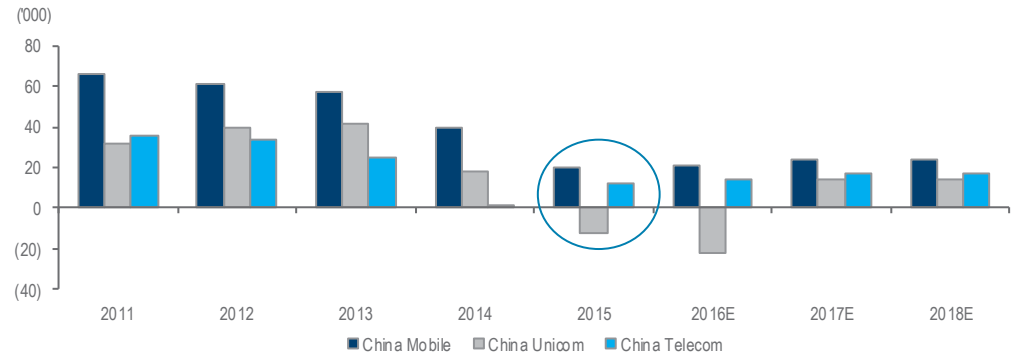
In May 2016, the MIIT imposed tighter subscriber registration norms for operators. Previously the government required that the real SIM registration ratio should be higher than 90% by end-2015; the MIIT has mandated an increase in this threshold to 95% by end-2016 and to 100% by mid-2017.

China Mobile said the proportion of “real-name” users on its network is already over 92% while China Telecom indicated to us that this ratio is around 93%. Further, China Telecom said that nearly all of its new customer additions have real names.

We believe the tighter subscriber registration policy will negatively impact the customer growth outlook for all 3 operators, as some users will invariably have to be cut off from the operators' networks for lack of proper documentation. However, as we believe a large proportion of these users could be inactive or low-income customers, the effect on revenues could be quite modest.

Overall, reflecting trends in May 2016 monthly subscriber data and considering the likely impact of real-name registration policy, we are cutting our mobile subscriber forecasts for China Mobile (by 0.3-0.9% over 2016-18E) and China Unicom (by 0.7-0.8% over 2016-18E). We are, however, raising the numbers slightly for China Telecom (2016-18E: 0.5-1.4%), as YTD trends have been stronger than our expectation.

China Telecoms Sector: mobile net addition trends



Source: Companies, Daiwa forecasts

Asymmetric regulation; little talk of imminent action but remains a longer-term risk

Back in December 2013, the MIIT said it would review the interconnection policy every 2 years, and as such we think another round of asymmetric interconnection rate cuts cannot be ruled out. As a result, China Mobile's 1H14 EBITDA (down 4.3% YoY as service EBITDA margins fell by 4.4pp to 36%) was negatively impacted by these measures, and we believe any new measures could once again try to rebalance industry profits away from China Mobile and towards smaller operators China Telecom and China Unicom.

While this remains a risk to our forecasts on China Mobile, we note there has been little news or market talk around the likelihood or timetable pertaining to such measures.

New entrant risks: an issue worth monitoring

On 5 May 2016, the MIIT awarded a "basic telecom" licence to China Broadcasting Network (CBN). In addition, On 31 May 2016, CBN formed a joint venture with Citic Telecom's (1883 HK, HKD2.91, Buy [1]) parent company with an aim of establishing a fourth mobile operator in China (for details, refer to John Choi's flash note, [Slow and steady progress](#), 14 June 2016).

These are perplexing developments as market talk over the 2014-15 period revolved around industry consolidation (as opposed to new entrants), which was viewed by many in the investing community as reflecting the government's desire to improve efficiencies across a range of industries under its SOE-reform vision.

So what is the regulator's motive and the likely impact of these developments?

CBN has formed a JV to explore a fourth mobile licence

First, based on our understanding of the situation, the licence was awarded to CBN to promote regulatory policy on "three-network convergence", ie, convergence of the cable-TV, telecom and Internet industries. CBN subsidiary, China Cable Television Network, is a cable-TV operator. The 'three-network convergence' policy is a not a new one. It has been in existence since 2010 after nearly 10 years of preparation. It has faced several delays in its implementation according to a research article examining the state of the cable-TV industry (see *Why transforming the cable operators in China is delayed*, Problems and perspectives in Management, Volume 12, Issue 2, 2014).

While it is impossible for us to rationalise the regulator's motive, it appears to be a case of 2 independently pursued policies — SOE reform and 3-network convergence — making progress after one has been on the backburner for a long time.

Second, our discussions with industry players suggest that CBN would be allowed to operate broadband and Internet data services. It is not clear whether the licence would permit mobile services. In any case, most of the industry contacts we spoke to do not think CNB's entry into the mobile market is imminent. We have no way to be certain, though we think there are too many unsettled issues — including spectrum and funding — to think the industry structure will change for the worse any time soon.

Risks appear overplayed; spectrum and capital challenges abound for new entrants

For example, CBN has access to 700MHz spectrum; and we think developing a handset ecosystem on 700MHz would take considerable effort (existing networks and handsets support the 900/1800/2100/2300MHz frequency bands; 4G LTE is developed on 2100MHz/2300MHz spectrum bands), not to mention the capital resources (smaller operator China Unicom is investing CNY63bn over 2015/16E on its 4G radio network alone, excluding transmission, backhaul and IT systems) and regulatory policy support (pertaining to number portability, interconnection rates, domestic roaming arrangements) needed to turn any mobile ambitions into reality.

Thus, despite its importance, based on the evidence available we feel it is premature to believe that new-entrant threats are likely to materialise especially over the next 12 months.

China Telecom–China Unicom: cooperation or merger?

Given there were management changes at China Unicom in 2H15, we continue to believe that the government will give sufficient time for the new management team to turn around the declining operational fortunes of China Unicom before considering an outright merger.

China Telecom–Unicom merger synergies are unclear; but combined entity could become a proxy for the tower industry

M&A between China Telecom and China Unicom in a conventional sense doesn't look like an attractive proposition, as cost synergies, aside from potential 4G capex savings, do not appear obvious to us. For example, we do not think personnel costs would be cut; while we also do not see room for network cost savings as we believe the companies would need to maintain different network platforms (CDMA, FD-LTE, GSM, WCDMA, TD-LTE) for the foreseeable future.

However, one interesting aspect is that a combined China Telecom–China Unicom would effectively be a proxy for the tower industry, as the 2 companies jointly control around 56% of the tower market. As such, a combined entity could benefit from the growth and market dynamics in the tower industry. In addition, the merger could pave way for the combined entity to raise funds for their network expansion through partial divestment of their stakes via the IPO of the tower company, while retaining a sufficient stake to benefit from the growth prospects of the tower industry.

Thus, while a merger appears unlikely to us in the short term it, we believe it remains a possibility around the time of the IPO of the tower company (2017 onwards).

China Telecoms Sector: key financials (2016E)

CNY bn	China Mobile	Telecom + Unicom	China Telecom	China Unicom
Service Revenue	622	548	307	241
EBITDA	245	174	92	82
Net profit	103	18	16	2
Revenue breakdown				
Mobile service	583	281	134	147
Fixed-line service	39	267	173	94
Subscribers (m)				
Wireless	847	477	212	265
4G	543	219	119	100
Fixed line	na	195	127	68
Fixed-broadband	70	197	122	75
Balance sheet (bn)				
Fixed assets	724	934	482	452
Total assets	1470	1233	641	592
Net debt	-376	272	112	160

Source: Daiwa estimates and forecasts

China Telecoms Sector: market shares (2016E)

%	China Mobile	Telecom + Unicom	China Telecom	China Unicom
Service Revenue	53	47	26	21
EBITDA	58	42	22	20
Net profit	85	15	13	2
Revenue breakdown				
Mobile service	67	33	16	17
Fixed-line service	13	87	56	31
Subscribers (m)				
Wireless	64	36	16	20
4G	71	29	16	13
Fixed line	na	na	na	na
Fixed-broadband	26	74	46	28
Balance sheet (bn)				
Fixed assets	44	56	29	27
Total assets	54	46	24	22

Source: Daiwa estimates and forecasts

How should investors position themselves for a possible merger announcement? We think that barring any restrictive regulatory actions, a merger would allow China Mobile to grow its market leadership further as it would be free from distractions and challenges from integrating 2 large and complex organisations. However, given that most M&As in China happen at or above their book values, we also expect both China Unicom and China Telecom shares to rally in the lead-up to any such announcement.

China Telecom-Unicom currently share around 40,000 base stations

Separate from merger talk, China Unicom and China Telecom have been exploring a partnership to share and jointly develop 4G network infrastructure, particularly in rural areas. These initiatives have gained momentum in 2016, and China Unicom said that around 40,000 base stations had been built jointly with China Telecom as of May 2016. While positive, the impact is likely to be quite modest as the co-build base stations account for only a fraction of the 0.9m base stations that China Unicom operates (as of 2015).

How much is the tower company worth?

Based on 1Q16 results and our recent industry visits, we are raising our 2016-18E net profit forecasts for the tower company by 12-62%. The revision is driven by higher revenue forecasts for the tower company. We estimate that the tower company's EBITDA margins could be around 40%; we infer this from China Unicom's 1Q16 results, which suggest that the tower company's 1Q16 net margin was around 5.5%.

Tower company: key metrics

Tower company	2014	2015	2016E	2017E	2018E
CNY bn					
Revenue		10.3	69.2	72.3	73.0
EBITDA			27.7	28.9	29.1
Net income	-0.1	-2.9	5.0	6.0	6.3
Simplified Balance Sheet					
Fixed-assets		187.5	175.3	162.8	149.5
Total Assets	10.1	270.4	258.2	245.6	232.4
Total Debt		68.8	51.7	33.1	13.6
Total Liabilities		144.3	127.1	108.5	89.1
Equity	9.9	126.1	131.1	137.1	143.3
Simplified Cash flow					
Op Cash flow			26.0	26.9	27.1
Capex			-6.9	-7.2	-7.3
FCF			19.1	19.7	19.8
Interest expense			-2.0	-1.1	-0.3
Free Cash Flow to Equity Holders			17.1	18.6	19.5
Assumptions					
EBITDA margin (%)			40%	40%	40%
Capex/Sales			10%	10%	10%
Net interest expense			3.5%	3.5%	3.5%
Tax rate			25%	25%	25%
Net Debt		68.8	51.7	33.1	13.6
Net Debt / EBITDA (x)			1.9	1.1	0.5

Source: Companies, Daiwa forecasts

In addition, others disclosures (2015 20F filings) made over the past couple of months have allowed us to refine some of our underlying assumptions about the tower company and given us a better insight into its valuations.

While we prefer EV/EBITDA, book value is perhaps a more useful metric given available information about the tower company

We use 3 different approaches to value the tower business. An EV/EBITDA target multiple approach gives us a range of CNY115-226bn in equity valuation, while a book value method implies a range of CNY131-210bn. A DCF approach gives us a much higher range (CNY234-282bn), though this appears aggressive for now given its sensitivity to (and lack thereof) the tower company's long-term capex plans.

Tower company valuation under different approaches

	2016E EV/EBITDA			2016E Book Value			DCF		
	6x	8x	10x	1.0x	1.3x	1.6x	8.30%	8.80%	9.30%
Target multiple / WACC CNYbn									
Tower-company	115	170	226	131	170	210	282	256	234
China Mobile	44	65	86	50	65	80	107	97	89
China Unicom	32	48	63	37	48	59	79	72	66
China Telecom	32	47	63	37	48	59	79	71	65
Implied free cash flow yield	11.5%	8.6%	6.9%	10.5%	8.6%	7.3%	5.7%	6.2%	6.7%
Implied PER	23.0	34.2	45.3	26.3	34.2	42.1	56.5	51.5	47.1
Per share (HKD)									
China Mobile	2.5	3.7	4.9	2.8	3.7	4.5	6.1	5.5	5.0
China Unicom	1.6	2.3	3.1	1.8	2.3	2.9	3.8	3.5	3.2
China Telecom	0.46	0.68	0.90	0.52	0.68	0.84	1.13	1.02	0.94
Valuation (USDbn)	17.2	25.5	33.8	19.7	25.6	31.4	42.2	38.4	35.2

Source: Daiwa estimates and forecasts

We prefer to use book value for our valuation purposes, even though we believe an EV/EBITDA metric is the superior measure. This is because currently there is no disclosure over the tower company's EBITDA and debt levels, and we do not expect the situation to change in the near term (until its IPO). In contrast, the book values of the tower company are readily available (easily estimated from quarterly financial reports of the operators).

What is an appropriate valuation multiple?

We value the tower business at 1.3x 2016E book value

We believe 1.0x book value (which we used previously) is a very conservative estimate; as more corporate actions in China telecom industry are transacted at a premium to book values, and taking into account the likely IPO of the tower company in 2017, we think 1.0x book value would underestimate the value of the tower portfolio. China Mobile currently trades at 1.5x 2016E book value, while offering a 10.8% ROE for 2016, on our forecasts. In the case of the tower company, we estimate its 2016 ROE could be lower, at around 3.8%. As such, we believe the tower company should trade at a discount to China Mobile's PBR valuation. While the absolute ROE levels for the tower company appear to be on the low side (and perhaps below its cost of capital), they could improve over the medium term through the use of leverage and improvement in the tower company's profitability. So what level should the tower company trade at? We believe a 2016E PBR of 1.3x is appropriate, which translates into 8x 2016E EV/EBITDA, which also seems reasonable to us.

The tower companies in most parts of Asia trade at a significant EV/EBITDA valuation premium to their domestic mobile counterparts (due to the low-risk nature of revenue contracts for a tower company), and we expect China's situation to be no different. For example, the Indonesian tower companies are currently trading at a 118% EV/EBITDA premium to the Indonesia mobile telecom operators, based on Bloomberg-consensus forecasts. An 8x EV/EBITDA multiple for the China tower industry would put it at an 80-120% premium over the listed mobile operators' valuations, based on our calculations.

Background: The tower company was initially formed in 2014 with CNY10bn in paid-up capital. In 2015, all 3 operators injected assets for which they received payment in the form of both cash and shares.

The tower company purchased the assets by offering a 30-33% premium to their value as recognised in the operators' books. The payment consideration is such that: 1) all 3

operators would recognise deferred gains, and 2) China Mobile and China Unicom would receive cash payments by 2017.

Tower company: current shareholdings

	No of shares (bn)	% shareholding (%)
China Mobile	49.2	38.0%
China Unicom	36.3	28.1%
China Telecom	36.1	27.9%
China Reform	7.8	6.0%
Total	129.3	100.0%

Source: Companies, Daiwa estimates

China Telecoms Sector: tower-spin off multiples

Valuation multiples	Price-to-book (x)	EV/Tower (CNY)	Towers sold
China Mobile	1.30	131,713	780,000
China Unicom	1.32	140,149	390,000
China Telecom	1.33	91,306	330,000

Source: Companies, Daiwa estimates

China Telecoms Sector: payment consideration for 2015 tower spin-off

CNYbn	Shares	Cash	Upfront cash	Deferred cash	Deferred payment date
China Mobile	45.2	57.6	5.0	52.6	Dec-17
China Unicom	33.3	21.3	3.0	18.3	Dec-17
China Telecom	33.1	-3.0	-3.0		

Source: Companies, Daiwa estimates

China Telecoms Sector: one-off accounting gains from 2015 tower spin-off

CNYbn	Appraised Value	Book value	Accounting Gain	Upfront (pre-tax)	Deferred gain (pre-tax)
China Mobile	102.7	78.8	21.7	15.5	6.2
China Unicom	54.7	41.5	12.9	9.2	3.6
China Telecom	30.1	22.7	7.2	5.2	2.0
Total	187.5	143.0	41.8	30.0	11.8

Source: Companies, Daiwa estimates

Operating outlook: China Telecom is gaining share in mobile, while China Mobile is gaining ground in fixed line

After a robust 1Q16, industry subscriber additions for both mobile and fixed-line segments slowed over the April-May period. The average monthly subscriber additions for mobile and fixed line segments slowed from 2.8m (vs. 6.3m in 1Q16) and 1.79m (vs. 3.35m in 1Q16), respectively, quarter-to-date in 2Q16. It appears the slowdown is a normalisation following the blistering start in 1Q16, and may have also been impacted by operators' efforts to meet the tighter real-name subscriber registration standards.

Within the mobile segment, China Telecom has been gaining market share. The company captured 51% of the market net additions over the 2-month April-May period (vs. 25% of market net additions in 1Q16 after adjusting for restatements at China Unicom). As a result, its market share expanded from 15.1% at end-2015 to 15.8% in May 2016. We expect China Telecom's market share to improve further to 17.3% by 2018E.

China Telecoms Sector: mobile market share

	2010	2011	2012	2013	2014	2015	2016E	2017E	2018E
Industry subscribers (m)	859	986	1,112	1,229	1,286	1,306	1,319	1,374	1,429
Industry net additions (m)	112	127	126	117	57	20	13	55	55
Mobile subscriber market share (%)									
China Mobile	68.0	65.9	63.9	62.4	62.7	63.3	64.2	63.4	62.6
China Unicom	19.5	20.2	21.5	22.9	23.3	22.0	20.1	20.3	20.5
China Telecom	10.5	12.8	14.4	15.1	14.4	15.2	16.1	16.7	17.3
4G Mobile subscriber market share (%)									
China Mobile					90.7	75.3	71.2	66.5	63.1
China Unicom					2.1	10.6	13.1	15.5	17.3
China Telecom					7.1	14.1	15.6	17.9	19.6

Source: Companies, Daiwa forecasts

We expect China Telecom to gain mobile market share

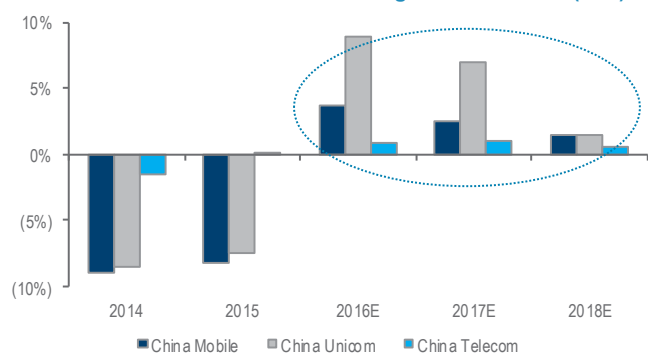
On the other hand, the dominant trend in the fixed-broadband segment remains the market-share gains by China Mobile, which rose by 22.9% at end-2015 to 24.7% by May 2016. We expect it to improve further to 29.2% by end-2018 given the company's recent investment focus in this area post the acquisition of China Tietong business in 4Q15.

China Telecoms Sector: fixed-broadband market share

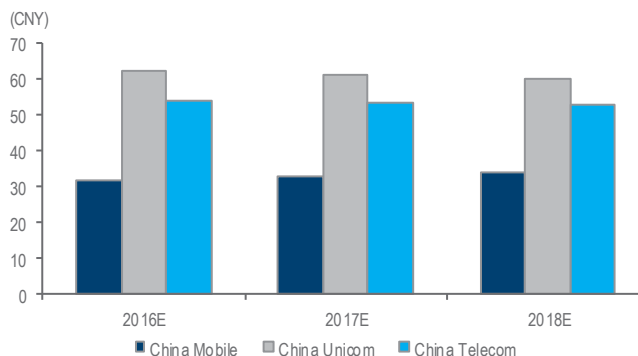
	2010	2011	2012	2013	2014	2015	2016E	2017E	2018E
Industry subscribers (m)	126	150	175	189	200	240	267	288	302
Industry net adds (m)	22	24	25	14	12	40	27	22	14
Market share (%)									
China Mobile						22.9	26.2	28.4	29.2
China Unicom	37.4	37.1	36.5	34.2	34.3	30.1	28.2	27.3	27.3
China Telecom	50.3	51.2	51.4	53.0	53.3	47.0	45.5	44.2	43.6
Others	12.3	11.7	12.1	12.8	12.3				

Source: Daiwa forecasts, Companies

Meanwhile, we expect the ARPU metrics in the mobile segment to improve for all 3 operators in 2016, driven by 4G migration. For 2016, we expect a strong ARPU rebound partly due to base effects (2015 ARPUs were impacted negatively by new mobile data carry-over policies in 4Q15) and because China Unicom has reclassified its subscriber base to eliminate non-generating subs in Jan 2016. In the fixed-line segment, we expect ARPU increases mainly for China Mobile over 2016-18E as its ARPU is currently well below industry peers' and due to its strategic focus on the high-end customer base.

China Telecoms Sector: mobile ARPU growth forecasts (YoY)


Source: Companies, Daiwa forecasts

China Telecoms Sector: fixed-broadband ARPU forecasts


Source: Daiwa forecasts

Accordingly, we forecast a telecoms industry service revenue CAGR of 5.3% over 2015-18. We expect China Mobile to maintain its revenue market share at around 53% as a result of market-share gains in the fixed-line segment.

We forecast a stable revenue market share for China Mobile over 2016-18E

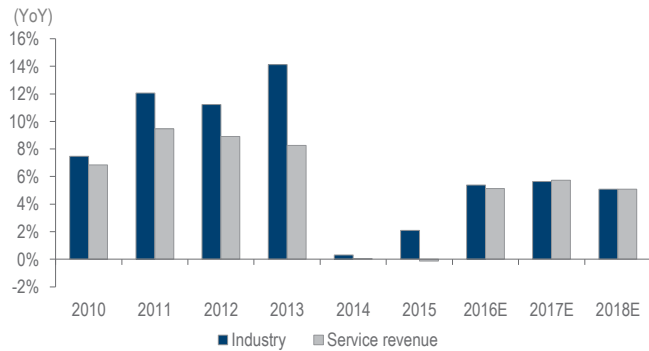
China Telecoms Sector: industry revenue share forecasts

(%)	2011	2012	2013	2014E	2015	2016E	2017E	2018E
Service revenue share								
China Mobile	55.9	54.5	53.1	52.2	52.5	53.2	53.3	53.1
China Unicom	19.7	20.4	21.4	22.0	21.1	20.6	20.4	20.5
China Telecom	24.4	25.1	25.5	25.8	26.4	26.2	26.3	26.4
Mobile service revenue share								
China Mobile	75.5	71.9	69.0	67.9	67.4	67.5	67.1	66.4
China Unicom	14.8	16.2	17.7	18.1	17.4	17.0	17.0	17.2
China Telecom	9.8	11.9	13.3	14.0	15.2	15.5	16.0	16.4
Fixed-line service revenue share								
China Mobile						12.8	14.3	15.2
China Unicom	33.5	33.5	31.1	31.7	31.3	30.8	30.1	29.9
China Telecom	66.5	66.5	61.2	59.9	57.8	56.5	55.5	54.9

Source: Companies, Daiwa forecasts

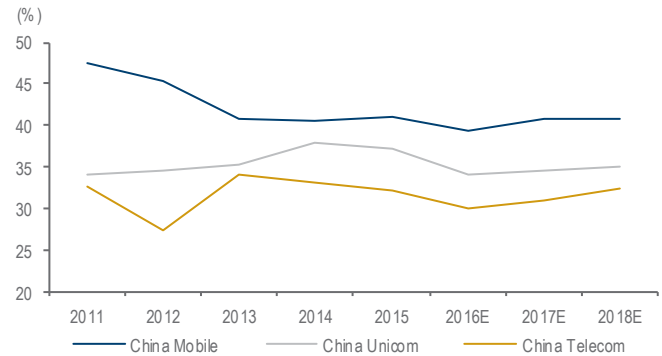
However, given the significant change in operators' business models following the tower divestments in 2015, we expect service EBITDA margins for all 3 companies in our coverage universe to dip initially in 2016, by 1.7-3.2pp, pressured by tower leases. We anticipate that 2016 will be the bottom for the sector service EBITDA margins, and forecast a 1.0-2.4pp improvement over the 2-year period 2016-18E, driven by operational leverage.

China Telecoms Sector: industry-revenue growth (2010-18E)



Source: Companies, Daiwa forecasts

China Telecoms Sector: service EBITDA margin forecasts



Source: Companies, Daiwa forecasts

Overall, we expect China Mobile and China Telecom to see decent net-profit CAGRs for 2015-18E of 5.6% and 5.5%, respectively, while we continue to see China Unicom's net-profits being weighed down by its relatively high cost structure.

China Telecoms Sector: industry growth forecasts (%)

(%, YoY)	2013	2014	2015	2016E	2017E	2018E	2015-18E CAGR
Growth							
Service revenue							
China Mobile	5.4	(1.5)	0.4	6.5	6.1	4.7	5.8
China Unicom	13.5	2.6	(3.9)	2.5	4.6	5.5	4.2
China Telecom	10.1	1.1	2.0	4.6	6.0	5.5	5.3
EBITDA							
China Mobile	(5.2)	(2.1)	2.0	2.2	9.9	4.6	5.5
China Unicom	15.6	10.5	(5.7)	(6.3)	6.1	7.0	2.0
China Telecom	36.3	(1.8)	(0.8)	(2.1)	9.5	10.3	5.7
Net profit							
China Mobile	(5.9)	(10.2)	(0.7)	(4.8)	16.9	5.8	5.6
China Unicom	46.7	15.8	(12.4)	(80.7)	164.2	75.7	(3.7)
China Telecom	17.6	0.8	13.4	(21.1)	22.8	21.2	5.5

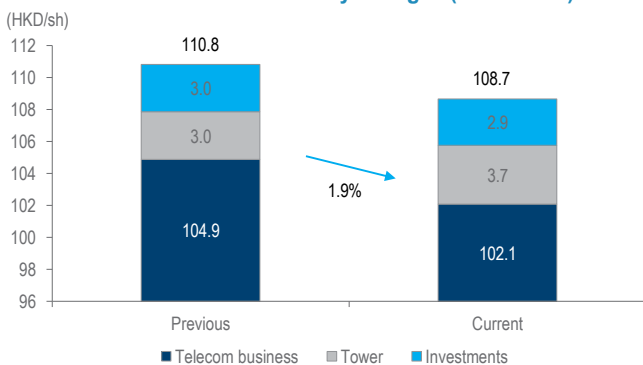
Source: Companies, Daiwa forecasts

Changes to ratings and target prices

China Mobile: reaffirming Buy (1) with new TP of HKD108.70

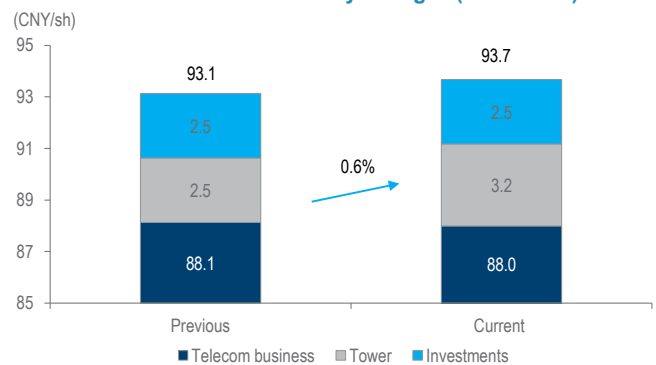
We reaffirm our Buy (1) call on the stock, with a revised SOTP-based 12-month target price of HKD108.70 (previously HKD110.80). Driven by slight upward adjustments to both core earnings (in CNY terms) and our tower-company valuation, we are raising our valuation in CNY terms by 0.6%. But, after factoring in a weaker CNY/HKD exchange rate, our HKD-based target price falls by 1.9% to HKD108.70. An intensification of competition would be the main downside risk to our view.

China Mobile SOTP valuation: key changes (HKD terms)



Source: Daiwa estimates

China Mobile SOTP valuation: key changes (CNY terms)



Source: Daiwa estimates

For 2016-18E, we are fine-tuning up our EPS forecasts (by 0.8-1.8%), driven mainly by 0.9-1.2% upward revisions to our EBITDA forecasts over this period.

China Mobile: changes to key P&L forecasts

CNYbn	New			Old			% Change		
	2016E	2017E	2018E	2016E	2017E	2018E	2016E	2017E	2017E
Service revenue	621.9	659.6	690.9	621.3	658.6	688.7	0.1	0.1	0.3
EBITDA	245.2	269.4	281.7	242.4	267.5	279.1	1.2	0.7	0.9
Profit from tower JV	1.9	2.3	2.4	1.2	1.9	2.2	61.4	17.8	6.8
Net profit	103.3	120.7	127.7	102.4	119.6	125.5	0.8	0.9	1.8
Assumptions (m)									
Mobile subscribers	847.2	870.7	894.2	849.8	876.1	902.5	(0.3)	(0.6)	(0.9)
4G subscribers	543.1	684.0	801.5	571.1	729.2	861.0	(4.9)	(6.2)	(6.9)
Fixed-broadband subscribers	70.0	82.0	88.0	73.0	85.0	91.0	(4.1)	(3.5)	(3.3)
Adj Mobile ARPU (CNY)	58.0	59.5	60.4	57.8	58.9	59.5	0.5	1.0	1.5
Adj Fixed-broadband ARPU (CNY)	32.0	33.0	33.9	33.0	34.0	35.0	(3.0)	(3.0)	(3.0)

Source: Daiwa forecasts

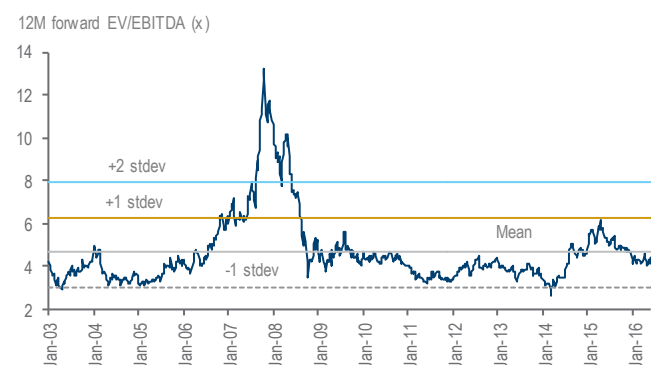
China Mobile remains our top sector pick due to its dominant presence in 4G

We find the shares are trading at blended 2016-17E EV/EBITDA and PERs of 4.4x and 14.2x respectively, versus their past-12-year averages of 4.7x and 12.4x, which represents a 7% discount on a EV/EBITDA basis. We continue to believe that China Mobile is the best positioned in the 4G era given its dominant market share (2016E: 71%), and is likely to improve its market position in the fixed-line segment. Our target price translates to a 1-year forward EV/EBITDA multiple of 5.3x for the core business and 5.8x for the group.

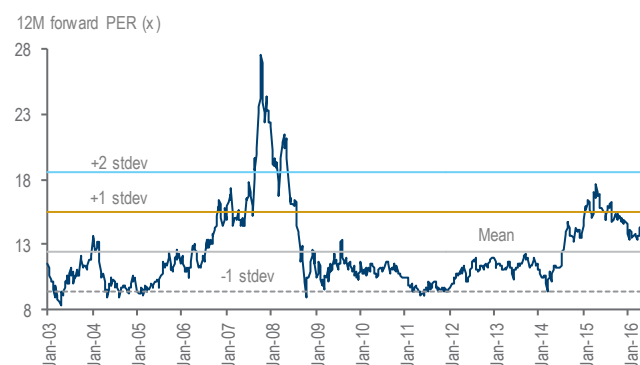
China Mobile: valuation and implied multiples

	Valuation		1-year target multiples	
	HKD/share	CNY/share	EV/EBITDA (x)	PER (x)
Telecom business (core)	102.1	88.0	5.3	17.9
Tower	3.7	3.2	na	31
Investments	2.9	2.5	na	5.6
Total (Group)	108.70	93.7	5.8	17.1

Source: Daiwa estimates

China Mobile: EV/EBITDA valuation bands


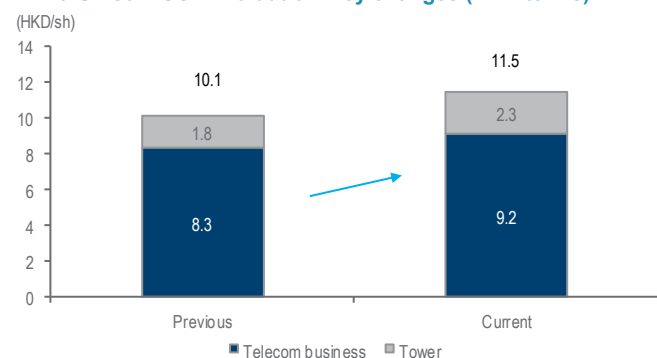
Source: Bloomberg, Company, Daiwa forecasts

China Mobile: PER valuation bands


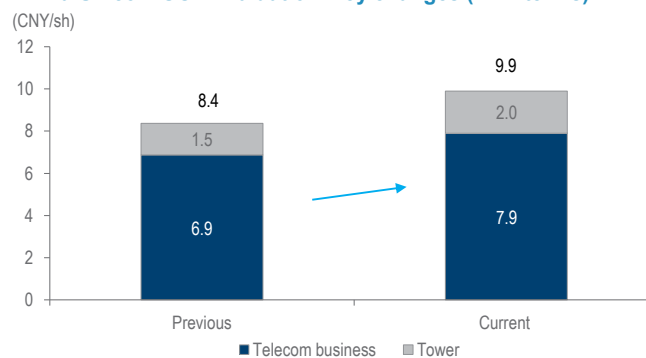
Source: Bloomberg, Company, Daiwa forecasts

China Unicom: upgrading to Buy (1) with new TP of HKD11.5

We upgrade our rating on China Unicom to Buy (1) from Outperform (2), with a revised SOTP-based 12-month target price of HKD11.50 (previously HKD10.10). Driven by upward adjustments to both core EBITDA (in CNY terms) and our tower-company valuation, we are raising our valuation in CNY terms by 18%. But, after factoring in the weaker CNY/HKD exchange rate, our HKD-based target price moderates to an increase of 13.9% to HKD11.5. An intensification of competition would be the main downside risk to our view on China Unicom.

China Unicom SOTP valuation: key changes (HKD terms)


Source: Daiwa estimates

China Unicom SOTP valuation: key changes (CNY terms)


Source: Daiwa estimates

For 2016-18E, we are raising our EPS forecasts by 15-108%, as we revise up our forecast profit contribution from the tower company by 12-61%. The change is especially sharp for 2016E given the low earnings base for that year. In addition, we are raising our core EBITDA forecasts by 1-1.6% over this period to take into account the trends shown in the 1Q16 results.

China Unicom: changes to key P&L forecasts

CNYbn	New			Previous			% Change		
	2016E	2017E	2018E	2016E	2017E	2018E	2016E	2017E	2018E
Service revenue	241.1	252.2	266.1	240.7	252.0	265.2	0.2	0.1	0.3
EBITDA	82.0	86.9	93.0	81.1	85.9	91.5	1.1	1.2	1.6
Profit from tower JV	1.4	1.7	1.8	0.9	1.4	1.6	61.4	24.0	12.4
Net profit	2.0	5.4	9.4	1.0	4.3	8.2	107.8	23.8	15.1
Assumptions (m)									
Mobile subscribers	264.7	278.7	292.7	266.7	280.7	294.7	(0.8)	(0.7)	(0.7)
4G subscribers	100.2	159.7	219.2	104.2	163.7	223.2	(3.8)	(2.4)	(1.8)
Fixed-broadband subscribers	75.3	78.8	82.3	75.8	79.3	82.8	(0.7)	(0.6)	(0.6)
Adj Mobile ARPU (CNY)	44.4	47.5	48.3	44.2	47.3	48.0	0.5	0.5	0.5
Adj Fixed-broadband ARPU (CNY)	62.5	61.2	60.0	62.5	61.2	60.0	0.0	0.0	0.0

Source: Daiwa forecasts

China Unicom is trading below book and we see it as a potential turnaround story

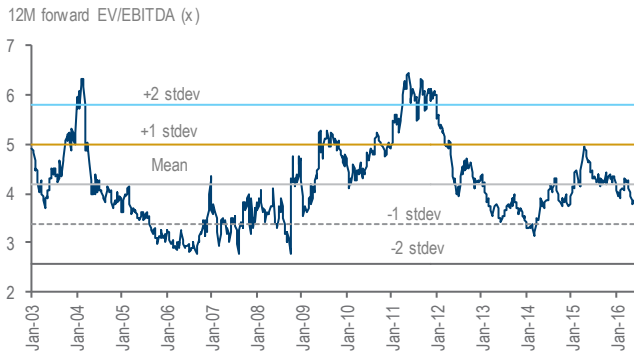
The shares are trading on blended 2016-17E EV/EBITDA and PERs of 3.7x and 56.5x, respectively, versus their past-12-year averages of 4.2x and 31.8x. In addition, we find the stock's PBR (2016E: 0.7x) appealing, and believe the shares could rally as the tower company — which contributes 20% of our SOTP valuation — works towards its planned IPO in 2017. Thus, while 2016 is likely to be a subdued year for earnings, we still believe that China Unicom's share price could rally as tower valuations crystallise over the coming year. Our target price translates into one-year forward EV/EBITDA multiple of 4.0x for the telecom business and 4.5x for the Unicom Group.

China Unicom: valuation and implied multiples

	Valuation		1-year target multiples	
	HKD/share	CNY/share	EV/EBITDA (x)	PER (x)
Telecom business	9.2	7.9	4.0	87.4
Tower	2.3	1.9	na	30
Investments	0.0	0.0	na	na
Total (Group)	11.40	9.8	4.5	63.6

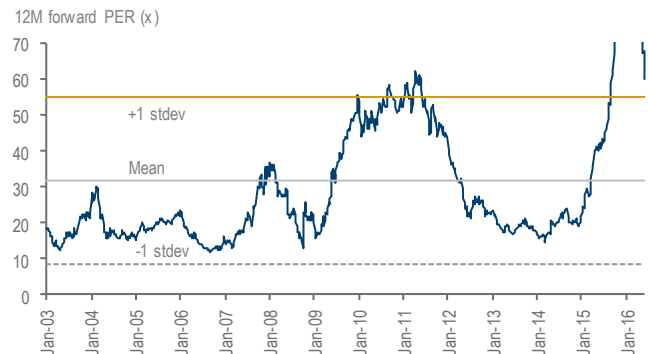
Source: Daiwa estimates

China Unicom: EV/EBITDA valuation bands



Source: Bloomberg, Company, Daiwa forecasts

China Unicom: PER valuation bands

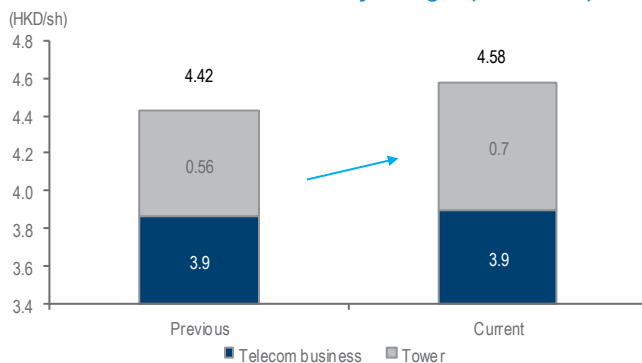


Source: Bloomberg, Company, Daiwa forecasts

China Telecom: upgrading to Buy (1) from Outperform (2) with new TP of HKD4.58

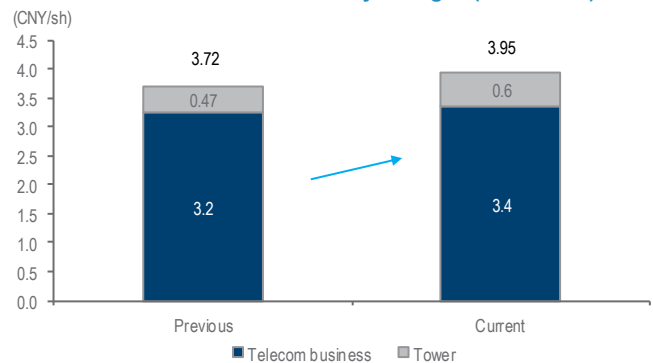
We upgrade our rating on China Telecom to Buy (1) from Outperform (2), with a revised SOTP-based 12-month target price of HKD4.58 (previously HKD4.42). Driven by upward adjustments to both core EBITDA (in CNY terms) and our tower-company valuation, we are raising our valuation in CNY terms by 6%. But, after factoring in the weaker CNY/HKD exchange rate, our HKD-based target price moderates to an increase of 3.5% to HKD4.58. An intensification of competition would be the main downside risk to our view on the stock.

China Telecom SOTP valuation: key changes (HKD terms)



Source: Daiwa estimates

China Telecom SOTP valuation: key changes (CNY terms)



Source: Daiwa estimates

We think China Telecom is executing well in the mobile business

For 2016-18E, we are: 1) raising our service revenue forecasts by 0.2-0.5%, after raising our mobile market subscriber and ARPU forecasts, and 2) lifting our forecast earnings contribution from the tower company by 12-61%. Accordingly, we are raising our EPS forecasts by 3.2-3.9% for the period.

China Telecom: changes to key P&L forecasts

CNYbn	Current			Old			% Change		
	2016E	2017E	2018E	2016E	2017E	2018E	2016E	2017E	2018E
Service revenue	306.7	325.1	342.9	306.3	324.2	341.1	0.2	0.3	0.5
EBITDA	92.1	100.9	111.2	91.9	100.4	110.3	0.3	0.5	0.9
Profit from tower JV	1.4	1.7	1.8	0.9	1.4	1.6	61.4	24.0	12.4
Net profit	15.8	19.4	23.6	15.2	18.8	22.7	3.9	3.2	3.8
Assumptions (m)									
Mobile subscribers	212.1	229.5	246.9	211.2	227.3	243.5	0.5	1.0	1.4
4G subscribers	119.0	184.2	245.0	118.1	178.8	239.5	0.7	3.0	2.3
Fixed-broadband subscribers	121.6	127.6	131.6	122.1	128.1	132.1	(0.4)	(0.4)	(0.4)
Adj Mobile ARPU (CNY)	54.5	55.1	55.4	54.3	54.9	55.1	0.4	0.4	0.4
Adj Fixed-broadband ARPU (CNY)	54.0	53.5	52.9	54.0	53.5	52.9	0.0	0.0	0.0

Source: Daiwa forecasts

The shares are trading on 2017E EV/EBITDA and PERs of 3.7x and 14.1x, respectively, versus their past-12-year averages of 4.2x and 13.7x. While the stock's valuations don't appear compelling on a PER yardstick, we find the PBR (2016E: 0.8x) appealing and

believe the shares could rally as the tower company works towards its planned IPO in 2017. At our target price, the shares would trade on a blended 2016-17E EV/EBITDA multiple of 3.9x for the core telecom business and 4.4x for the group.

China Telecom: valuation and implied multiples

SOTP valuation	Valuation		1-year target multiples	
	HKD/share	CNY/share	EV/EBITDA (x)	PER (x)
Telecom business (core)	3.9	3.4	3.9	16.9
Tower	0.68	0.6	na	31
Total (Group)	4.58	3.95	4.4	18.1

Source: Daiwa estimates

We prefer China Telecom over China Unicom because of its superior operational momentum, especially as both stocks are trading on similar 2016-17E blended EV/EBITDA multiples, based on our forecasts.

China Telecom: EV/EBITDA valuation bands



Source: Bloomberg, Company, Daiwa forecasts

China Telecom: PER valuation bands



Source: Bloomberg, Company, Daiwa forecasts

China Mobile's financial summary

Key assumptions

Year to 31 Dec	2011	2012	2013	2014	2015	2016E	2017E	2018E
Subscribers 'million	649.6	710.3	767.2	806.6	826.2	847.2	870.7	894.2
2G Subscribers	598.4	622.4	575.6	470.8	344.6	210.3	132.8	74.0
3G Subscribers	51.2	87.9	191.6	245.8	169.4	93.8	53.9	18.7
4G Subscribers	0.0	0.0	0.0	90.1	312.3	543.1	684.0	801.5
Blended Average revenue per user per month (CNY)	71.3	68.7	66.6	61.6	56.4	58.0	59.5	60.4
Access lines (m)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Wireline Broadband Subscribers (m)	0.0	0.0	0.0	0.0	55.0	70.0	82.0	88.0

Profit and loss (CNYm)

Year to 31 Dec	2011	2012	2013	2014	2015	2016E	2017E	2018E
Mobile Service	527,999	560,413	590,811	581,817	552,160	582,861	613,311	639,539
Mobile non service	0	0	39,366	59,631	84,246	92,671	97,304	102,169
Other Revenue	0	0	0	0	31,929	39,003	46,263	51,317
Total Revenue	527,999	560,413	630,177	641,448	668,335	714,535	756,878	793,025
Other income	0	0	0	0	0	0	0	0
COGS	0	0	0	0	0	0	0	0
SG&A	(279,587)	(309,043)	(389,829)	(407,889)	(428,581)	(469,324)	(487,481)	(511,291)
Other op.expenses	(94,500)	(98,572)	(104,621)	(114,525)	(136,558)	(137,006)	(140,778)	(146,844)
Operating profit	153,912	152,798	135,727	119,034	103,196	108,205	128,618	134,891
Net-interest inc./exp.)	7,848	12,271	14,958	15,921	15,397	14,571	16,122	19,415
Assoc/forex/extraord./others	4,876	6,299	7,972	9,337	25,415	13,279	14,234	15,002
Pre-tax profit	166,636	171,368	158,657	144,292	144,008	136,055	158,975	169,308
Tax	(40,603)	(41,919)	(36,776)	(33,187)	(35,079)	(32,653)	(38,154)	(41,480)
Min. int./pref. div./others	(109)	(107)	(111)	(126)	(116)	(116)	(116)	(116)
Net profit (reported)	125,924	129,342	121,770	110,979	108,813	103,286	120,705	127,711
Net profit (adjusted)	125,924	129,342	121,770	110,979	108,813	103,286	120,705	127,711
EPS (reported)(CNY)	6.275	6.438	6.058	5.469	5.315	5.045	5.896	6.238
EPS (adjusted)(CNY)	6.275	6.438	6.058	5.469	5.315	5.045	5.896	6.238
EPS (adjusted fully-diluted)(CNY)	6.198	6.359	5.986	5.438	5.313	5.043	5.894	6.236
DPS (CNY)	2.730	2.773	2.621	2.311	2.205	2.098	2.452	2.594
EBIT	153,912	152,798	135,727	119,034	103,196	108,205	128,618	134,891
EBITDA	251,025	253,646	240,426	235,259	240,028	245,211	269,396	281,735

Cash flow (CNYm)

Year to 31 Dec	2011	2012	2013	2014	2015	2016E	2017E	2018E
Profit before tax	166,636	171,368	158,657	144,292	144,008	136,055	158,975	169,308
Depreciation and amortisation	97,113	100,848	104,699	116,225	136,832	137,006	140,778	146,844
Tax paid	(40,078)	(44,583)	(43,222)	(39,040)	(37,794)	(32,653)	(38,154)	(41,480)
Change in working capital	5,426	13,077	19,204	5,347	17,751	(16,845)	68,529	10,067
Other operational CF items	(2,341)	(10,001)	(14,353)	(15,802)	(25,708)	(27,850)	(30,356)	(34,417)
Cash flow from operations	226,756	230,709	224,985	211,022	235,089	195,712	299,771	250,321
Capex	(123,416)	(123,406)	(139,352)	(170,799)	(172,455)	(186,200)	(160,000)	(151,988)
Net (acquisitions)/disposals	123	6	44	(9,508)	(376)	0	0	0
Other investing CF items	(53,656)	(77,235)	(44,559)	19,696	14,433	0	0	0
Cash flow from investing	(176,949)	(200,635)	(183,867)	(160,611)	(158,398)	(186,200)	(160,000)	(151,988)
Change in debt	(5,330)	0	(23,633)	0	(1,000)	0	0	0
Net share issues/(repurchases)	136	531	43	8,215	1,024	0	0	0
Dividends paid	(52,575)	(55,425)	(55,491)	(50,924)	(47,912)	(46,145)	(42,972)	(50,219)
Other financing CF items	6,942	9,456	12,042	14,157	(22,967)	14,571	16,122	19,415
Cash flow from financing	(50,827)	(45,438)	(67,039)	(28,552)	(70,855)	(31,574)	(26,850)	(30,805)
Forex effect/others	41,652	85,289	42,926	(22,905)	(21,526)	0	0	0
Change in cash	40,632	69,925	17,005	(1,046)	(15,690)	(22,062)	112,921	67,529
Free cash flow	103,340	107,303	85,633	40,223	62,634	9,512	139,771	98,333

Source: FactSet, Daiwa forecasts

China Mobile's financial summary continued ...

Balance sheet (CNYm)

As at 31 Dec	2011	2012	2013	2014	2015	2016E	2017E	2018E
Cash & short-term investment	332,978	402,903	419,908	418,862	403,172	381,110	494,032	561,560
Inventory	7,944	7,195	9,152	9,130	9,994	10,685	11,318	11,859
Accounts receivable	28,818	20,429	25,650	30,850	44,176	102,140	46,527	47,486
Other current assets	12,945	16,066	12,479	18,741	31,355	35,542	40,128	44,829
Total current assets	382,685	446,593	467,189	477,583	488,697	529,477	592,004	665,734
Fixed assets	464,400	486,016	564,227	658,136	673,643	723,605	742,828	747,972
Goodwill & intangibles	37,712	37,818	37,957	36,066	36,111	35,343	35,343	35,343
Other non-current assets	67,761	81,682	98,019	124,664	229,444	181,683	191,216	201,400
Total assets	952,558	1,052,109	1,167,392	1,296,449	1,427,895	1,470,108	1,561,390	1,650,450
Short-term debt	68	68	68	68	0	0	0	0
Accounts payable	210,562	228,884	300,350	363,173	414,904	399,976	413,526	425,093
Other current liabilities	62,614	68,844	70,495	68,635	86,134	86,134	86,134	86,134
Total current liabilities	273,244	297,796	370,913	431,876	501,038	486,110	499,660	511,227
Long-term debt	28,617	28,619	4,989	4,992	4,995	4,995	4,995	4,995
Other non-current liabilities	278	385	766	938	1,494	1,494	1,494	1,494
Total liabilities	302,139	326,800	376,668	437,806	507,527	492,599	506,149	517,716
Share capital	2,140	2,142	2,142	400,737	402,130	402,130	402,130	402,130
Reserves/R.E./others	646,924	721,305	786,631	455,839	515,206	572,347	650,080	727,572
Shareholders' equity	649,064	723,447	788,773	856,576	917,336	974,477	1,052,210	1,129,702
Minority interests	1,355	1,862	1,951	2,067	3,032	3,032	3,032	3,032
Total equity & liabilities	952,558	1,052,109	1,167,392	1,296,449	1,427,895	1,470,108	1,561,390	1,650,450
EV	1,195,929	1,126,513	1,085,967	1,087,132	1,103,722	1,125,784	1,012,863	945,334
Net debt/(cash)	(304,293)	(374,216)	(414,851)	(413,802)	(398,177)	(376,115)	(489,037)	(556,565)
BVPS (CNY)	32.337	35.992	39.240	42.613	45.636	48.479	52.346	56.201

Key ratios (%)

Year to 31 Dec	2011	2012	2013	2014	2015	2016E	2017E	2018E
Sales (YoY)	8.8	6.1	12.4	1.8	4.2	6.9	5.9	4.8
EBITDA (YoY)	4.9	1.0	(5.2)	(2.1)	2.0	2.2	9.9	4.6
Operating profit (YoY)	0.5	(0.7)	(11.2)	(12.3)	(13.3)	4.9	18.9	4.9
Net profit (YoY)	5.2	2.7	(5.9)	(8.9)	(2.0)	(5.1)	16.9	5.8
Core EPS (fully-diluted) (YoY)	5.2	2.6	(5.9)	(9.2)	(2.3)	(5.1)	16.9	5.8
Gross-profit margin	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
EBITDA margin	47.5	45.3	38.2	36.7	35.9	34.3	35.6	35.5
Operating-profit margin	29.2	27.3	21.5	18.6	15.4	15.1	17.0	17.0
Net profit margin	23.8	23.1	19.3	17.3	16.3	14.5	15.9	16.1
ROAE	20.6	18.8	16.1	13.5	12.3	10.9	11.9	11.7
ROAA	13.9	12.9	11.0	9.0	8.0	7.1	8.0	8.0
ROCE	23.9	21.3	17.5	14.3	11.5	11.3	12.6	12.3
ROIC	35.0	33.1	28.7	22.3	16.1	14.6	16.7	17.8
Net debt to equity	net cash	net cash	net cash	net cash	net cash	net cash	net cash	net cash
Effective tax rate	24.4	24.5	23.2	23.0	24.4	24.0	24.0	24.5
Accounts receivable (days)	15.1	16.0	13.3	16.1	20.5	37.4	35.8	21.6
Current ratio (x)	1.4	1.5	1.3	1.1	1.0	1.1	1.2	1.3
Net interest cover (x)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Net dividend payout	43.5	43.1	43.3	42.3	41.5	41.6	41.6	41.6
Free cash flow yield	6.9	7.2	5.7	2.7	4.2	0.6	9.3	6.6

Source: FactSet, Daiwa forecasts

Company profile

China Mobile is a leading mobile services provider with operations in Mainland China and Hong Kong. In China, it provides cellular services based on the 2G GSM, 3G TD-SCDMA and 4G TD-LTE technology platforms, and the company has the distinction of possessing the world's largest customer base. At the end of 2013, it had 767m customers. The stock was listed on the New York Stock Exchange and The Stock Exchange of Hong Kong on 22 October 1997 and 23 October 1997, respectively.

China Unicom's financial summary

Key assumptions

Year to 31 Dec	2011	2012	2013	2014	2015	2016E	2017E	2018E
Subscribers 'million	199.7	239.3	281.0	299.1	286.7	264.7	278.7	292.7
4G Subscribers (millions)	0.0	0.0	0.0	2.1	44.2	100.2	159.7	219.2
Blended Average revenue per user per month (CNY)	46.9	47.9	48.4	44.6	40.6	44.4	47.5	48.3
Access lines (millions)	92.9	92.0	87.6	82.1	73.9	67.7	63.7	61.7
Wireline Broadband Subscribers (millions)	55.7	63.9	64.6	68.8	72.3	75.3	78.8	82.3
Access line ARPU	25.2	22.0	20.7	18.3	16.0	15.7	15.4	15.1

Profit and loss (CNYm)

Year to 31 Dec	2011	2012	2013	2014	2015	2016E	2017E	2018E
Mobile	126,526	164,771	207,526	194,898	184,391	190,846	201,046	213,781
Fixed Line	81,705	83,277	86,566	88,481	91,261	94,097	97,218	100,667
Other Revenue	936	878	946	1,302	1,397	0	0	0
Total Revenue	209,167	248,926	295,038	284,681	277,049	284,943	298,264	314,448
Other income	0	0	0	0	0	0	0	0
COGS	0	0	0	0	0	0	0	0
SG&A	(145,755)	(176,267)	(211,075)	(191,910)	(189,547)	(202,990)	(211,322)	(221,456)
Other op.expenses	(58,021)	(61,057)	(68,196)	(73,868)	(76,738)	(77,943)	(78,570)	(79,626)
Operating profit	5,391	11,602	15,767	18,903	10,764	4,010	8,373	13,365
Net-interest inc./(exp.)	(1,244)	(3,424)	(2,940)	(4,334)	(6,496)	(4,385)	(4,605)	(4,282)
Assoc/forex/extraord./others	1,451	1,343	887	1,362	9,767	3,077	3,371	3,457
Pre-tax profit	5,598	9,521	13,714	15,931	14,035	2,702	7,139	12,540
Tax	(1,371)	(2,425)	(3,306)	(3,876)	(3,473)	(667)	(1,763)	(3,097)
Min. int./pref. div./others	0	0	0	0	0	0	0	0
Net profit (reported)	4,227	7,096	10,408	12,055	10,562	2,035	5,376	9,443
Net profit (adjusted)	4,227	7,096	10,408	12,055	10,562	2,035	5,376	9,443
EPS (reported)(CNY)	0.179	0.301	0.440	0.505	0.441	0.085	0.224	0.394
EPS (adjusted)(CNY)	0.179	0.301	0.440	0.505	0.441	0.085	0.224	0.394
EPS (adjusted fully-diluted)(CNY)	0.178	0.288	0.422	0.486	0.441	0.085	0.224	0.394
DPS (CNY)	0.100	0.120	0.160	0.200	0.170	0.033	0.087	0.152
EBIT	5,391	11,602	15,767	18,903	10,764	4,010	8,373	13,365
EBITDA	63,412	72,659	83,963	92,771	87,502	81,953	86,943	92,991

Cash flow (CNYm)

Year to 31 Dec	2011	2012	2013	2014	2015	2016E	2017E	2018E
Profit before tax	5,598	9,521	13,714	15,931	14,035	2,702	7,139	12,540
Depreciation and amortisation	58,021	61,057	68,196	73,868	76,738	77,943	78,570	79,626
Tax paid	(896)	(1,679)	(3,219)	(4,620)	(2,244)	(667)	(1,763)	(3,097)
Change in working capital	4,341	633	(2,263)	(1,329)	(3,340)	(33,225)	23,571	6,376
Other operational CF items	2,402	5,218	6,963	8,592	3,736	1,308	1,234	825
Cash flow from operations	69,466	74,750	83,391	92,442	88,925	48,061	108,750	96,270
Capex	(77,861)	(86,783)	(72,758)	(69,586)	(88,465)	(75,000)	(73,141)	(71,845)
Net (acquisitions)/disposals	(1,936)	1,086	1,544	(2,278)	1,328	0	0	0
Other investing CF items	(3,173)	(13,783)	(5,896)	(3,455)	(4,217)	0	0	0
Cash flow from investing	(82,970)	(99,480)	(77,110)	(75,319)	(91,354)	(75,000)	(73,141)	(71,845)
Change in debt	10,934	36,575	3,645	(27,909)	8,759	20,000	0	0
Net share issues/(repurchases)	35	1	1,102	871	1	0	0	0
Dividends paid	(2,070)	(2,283)	(2,686)	(3,677)	(4,643)	(4,071)	(784)	(2,072)
Other financing CF items	(2,886)	(6,419)	(5,044)	17,394	(5,314)	(4,385)	(4,605)	(4,282)
Cash flow from financing	6,013	27,874	(2,983)	(13,321)	(1,197)	11,544	(5,389)	(6,354)
Forex effect/others	133	(272)	(20)	2	219	219	219	219
Change in cash	(7,358)	2,872	3,278	3,804	(3,407)	(15,176)	30,439	18,290
Free cash flow	(8,395)	(12,033)	10,633	22,856	460	(26,939)	35,609	24,425

Source: FactSet, Daiwa forecasts

China Unicom's financial summary continued ...

Balance sheet (CNYm)

As at 31 Dec	2011	2012	2013	2014	2015	2016E	2017E	2018E
Cash & short-term investment	15,410	18,282	21,560	25,364	21,957	6,562	36,781	54,852
Inventory	4,651	5,803	5,536	4,378	3,946	3,989	4,176	4,402
Accounts receivable	12,615	14,509	15,450	16,803	19,797	34,979	17,350	18,191
Other current assets	6,127	9,580	9,664	10,029	10,970	14,047	17,418	20,875
Total current assets	38,803	48,174	52,210	56,574	56,670	59,577	75,725	98,321
Fixed assets	381,859	430,997	431,625	438,321	454,631	451,688	446,259	438,477
Goodwill & intangibles	2,771	2,771	2,771	2,771	2,771	2,771	2,771	2,771
Other non-current assets	32,800	34,182	42,565	47,406	96,274	77,952	77,952	77,952
Total assets	456,233	516,124	529,171	545,072	610,346	591,987	602,707	617,522
Short-term debt	70,372	139,240	129,470	101,527	106,380	116,380	116,380	116,380
Accounts payable	104,365	117,364	112,804	129,174	178,146	141,824	147,952	155,396
Other current liabilities	39,190	45,716	52,965	50,052	51,548	51,548	51,548	51,548
Total current liabilities	213,927	302,320	295,239	280,753	336,074	309,752	315,880	323,324
Long-term debt	34,502	2,536	13,483	35,047	40,676	50,676	50,676	50,676
Other non-current liabilities	1,906	1,763	1,550	1,731	2,380	2,380	2,380	2,380
Total liabilities	250,335	306,619	310,272	317,531	379,130	362,808	368,936	376,380
Share capital	2,311	2,311	2,328	179,101	179,102	179,102	179,102	179,102
Reserves/R.E./others	203,587	207,194	216,571	48,440	52,114	50,078	54,669	62,040
Shareholders' equity	205,898	209,505	218,899	227,541	231,216	229,180	233,771	241,142
Minority interests	0	0	0	0	0	0	0	0
Total equity & liabilities	456,233	516,124	529,171	545,072	610,346	591,987	602,707	617,522
EV	251,458	285,488	283,387	273,204	287,093	322,488	292,268	274,197
Net debt/(cash)	89,464	123,494	121,393	111,210	125,099	160,494	130,275	112,204
BVPS (CNY)	8.737	8.891	9.204	9.502	9.655	9.570	9.762	10.070

Key ratios (%)

Year to 31 Dec	2011	2012	2013	2014	2015	2016E	2017E	2018E
Sales (YoY)	22.1	19.0	18.5	(3.5)	(2.7)	2.8	4.7	5.4
EBITDA (YoY)	6.4	14.6	15.6	10.5	(5.7)	(6.3)	6.1	7.0
Operating profit (YoY)	4.5	115.2	35.9	19.9	(43.1)	(62.7)	108.8	59.6
Net profit (YoY)	9.8	67.9	46.7	15.8	(12.4)	(80.7)	164.2	75.7
Core EPS (fully-diluted) (YoY)	9.4	61.9	46.7	15.2	(9.3)	(80.7)	164.2	75.7
Gross-profit margin	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
EBITDA margin	30.3	29.2	28.5	32.6	31.6	28.8	29.1	29.6
Operating-profit margin	2.6	4.7	5.3	6.6	3.9	1.4	2.8	4.3
Net profit margin	2.0	2.9	3.5	4.2	3.8	0.7	1.8	3.0
ROAE	2.1	3.4	4.9	5.4	4.6	0.9	2.3	4.0
ROAA	0.9	1.5	2.0	2.2	1.8	0.3	0.9	1.5
ROCE	1.8	3.5	4.4	5.2	2.9	1.0	2.1	3.3
ROIC	1.4	2.8	3.6	4.2	2.3	0.8	1.7	2.8
Net debt to equity	43.5	58.9	55.5	48.9	54.1	70.0	55.7	46.5
Effective tax rate	24.5	25.5	24.1	24.3	24.7	24.7	24.7	24.7
Accounts receivable (days)	20.3	19.9	18.5	20.7	24.1	35.1	32.0	20.6
Current ratio (x)	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.3
Net interest cover (x)	4.3	3.4	5.4	4.4	1.7	0.9	1.8	3.1
Net dividend payout	55.7	39.9	36.4	39.6	38.5	38.5	38.5	38.5
Free cash flow yield	n.a.	n.a.	6.6	14.1	0.3	n.a.	22.0	15.1

Source: FactSet, Daiwa forecasts

Company profile

China Unicom is an integrated information services operator with operations in Mainland China. It provides cellular services, based on 2G GSM, 3G WCDMA technology platforms, in addition to fixed-line and broadband services. As at end 2013, the company had 88 million wire line subscribers and mobile subscribers of about 281 million. The company was listed on the New York Stock Exchange and the Stock Exchange of Hong Kong on 21st June 2000 and 22nd June 2000 respectively.

China Telecom's financial summary

Key assumptions

Year to 31 Dec	2011	2012	2013	2014	2015	2016E	2017E	2018E
Subscribers (m)	126.5	160.6	185.6	185.6	197.9	212.1	229.5	246.9
4G Subscribers (m)	0.0	0.0	0.0	7.1	58.5	119.0	184.2	245.0
Blended Average revenue per user per month (CNY)	52.4	53.9	54.8	54.0	54.1	54.5	55.1	55.4
Access lines (m)	169.6	163.0	155.8	143.6	134.3	127.3	122.3	117.3
Wireline Broadband Subscribers (m)	76.8	90.1	100.1	107.0	113.1	121.6	127.6	131.6
Access line ARPU (CNY)	24.1	21.7	20.2	18.7	17.8	17.0	16.6	16.2

Profit and loss (CNYm)

Year to 31 Dec	2011	2012	2013	2014	2015	2016E	2017E	2018E
Mobile	82,701	117,826	151,186	151,611	156,529	167,165	180,608	194,615
Fixed Line	162,340	165,247	170,398	172,783	174,673	178,601	185,350	191,115
Other Revenue	0	0	0	0	0	0	0	0
Total Revenue	245,041	283,073	321,584	324,394	331,202	345,767	365,959	385,730
Other income	0	0	0	0	0	0	0	0
COGS	0	0	0	0	0	0	0	0
SG&A	(169,688)	(212,232)	(225,033)	(229,541)	(237,096)	(253,634)	(265,075)	(274,499)
Other op.expenses	(51,224)	(49,655)	(69,083)	(66,345)	(67,664)	(68,350)	(72,343)	(77,144)
Operating profit	24,129	21,186	27,468	28,508	26,442	23,783	28,541	34,086
Net-interest inc./(exp.)	(2,254)	(1,564)	(5,153)	(5,291)	(4,273)	(4,542)	(4,870)	(4,732)
Assoc/forex/extraord./others	139	171	773	40	4,524	1,585	1,878	1,963
Pre-tax profit	22,014	19,793	23,088	23,257	26,693	20,826	25,549	31,317
Tax	(5,416)	(4,753)	(5,422)	(5,498)	(6,551)	(4,915)	(6,030)	(7,673)
Min. int./pref. div./others	(96)	(115)	(121)	(79)	(88)	(88)	(88)	(88)
Net profit (reported)	16,502	14,925	17,545	17,680	20,054	15,823	19,431	23,557
Net profit (adjusted)	16,502	14,925	17,545	17,680	20,054	15,823	19,431	23,557
EPS (reported)(CNY)	0.204	0.184	0.217	0.218	0.248	0.196	0.240	0.291
EPS (adjusted)(CNY)	0.204	0.184	0.217	0.218	0.248	0.196	0.240	0.291
EPS (adjusted fully-diluted)(CNY)	0.204	0.184	0.217	0.218	0.248	0.196	0.240	0.291
DPS (CNY)	0.070	0.068	0.075	0.075	0.080	0.063	0.077	0.094
EBIT	24,129	21,186	27,468	28,508	26,442	23,783	28,541	34,086
EBITDA	75,353	70,841	96,551	94,853	94,106	92,132	100,883	111,231

Cash flow (CNYm)

Year to 31 Dec	2011	2012	2013	2014	2015	2016E	2017E	2018E
Profit before tax	22,014	19,793	23,088	23,257	26,693	20,826	25,549	31,317
Depreciation and amortisation	51,224	49,655	69,083	66,345	67,664	68,350	72,343	77,144
Tax paid	(4,064)	(4,011)	(4,539)	(6,407)	(4,099)	(4,915)	(6,030)	(7,673)
Change in working capital	5,336	6,009	450	8,796	18,940	(8,722)	4,786	4,686
Other operational CF items	1,184	834	5,484	9,802	3,778	2,957	2,992	2,769
Cash flow from operations	75,694	72,280	93,566	101,793	112,976	78,495	99,639	108,244
Capex	(48,495)	(50,028)	(70,921)	(80,273)	(101,898)	(97,000)	(85,000)	(82,295)
Net (acquisitions)/disposals	(6)	0	0	710	755	0	0	0
Other investing CF items	4,864	1,776	(37,027)	(2,145)	(1,107)	0	0	0
Cash flow from investing	(43,637)	(48,252)	(107,948)	(81,708)	(102,250)	(97,000)	(85,000)	(82,295)
Change in debt	(21,453)	(14,431)	10,930	(3,797)	11,013	10,000	0	0
Net share issues/(repurchases)	0	0	0	0	0	0	0	0
Dividends paid	(6,174)	(5,625)	(5,433)	(6,198)	(6,160)	(6,461)	(5,098)	(6,260)
Other financing CF items	(2,781)	(1,359)	(5,075)	(5,720)	(4,270)	(4,542)	(4,870)	(4,732)
Cash flow from financing	(30,408)	(21,415)	422	(15,715)	583	(1,003)	(9,967)	(10,992)
Forex effect/others	(265)	923	(395)	(912)	1,264	0	0	0
Change in cash	1,384	3,536	(14,355)	3,458	12,573	(19,508)	4,672	14,957
Free cash flow	27,199	22,252	22,645	21,520	11,078	(18,505)	14,639	25,949

Source: FactSet, Daiwa forecasts

China Telecom's financial summary continued ...

Balance sheet (CNYm)

As at 31 Dec	2011	2012	2013	2014	2015	2016E	2017E	2018E
Cash & short-term investment	29,176	32,712	18,357	21,815	34,388	14,880	19,552	34,509
Inventory	4,840	5,928	6,523	4,225	6,281	6,570	6,953	7,329
Accounts receivable	18,471	18,768	20,022	21,562	21,105	22,129	23,421	24,687
Other current assets	7,089	7,802	7,881	11,941	16,334	16,334	16,442	16,556
Total current assets	59,576	65,210	52,783	59,543	78,108	59,913	66,369	83,080
Fixed assets	287,325	406,227	418,498	426,057	443,084	482,473	495,131	500,281
Goodwill & intangibles	37,633	39,132	37,962	38,901	40,659	29,920	29,920	29,920
Other non-current assets	34,581	34,503	33,996	36,773	67,710	69,094	70,770	72,531
Total assets	419,115	545,072	543,239	561,274	629,561	641,400	662,189	685,812
Short-term debt	20,953	16,735	47,760	44,058	51,758	61,720	61,720	61,720
Accounts payable	104,212	175,072	151,136	161,207	203,143	195,733	202,195	208,521
Other current liabilities	2,093	1,654	1,202	1,060	1,028	1,033	1,028	1,028
Total current liabilities	127,258	193,461	200,098	206,325	255,929	258,487	264,943	271,269
Long-term debt	31,150	83,073	62,617	62,918	64,911	64,830	64,830	64,830
Other non-current liabilities	3,829	2,508	1,860	1,923	3,970	3,970	3,970	3,970
Total liabilities	162,237	279,042	264,575	271,166	324,810	327,287	333,743	340,069
Share capital	80,932	80,932	80,932	80,932	80,932	80,932	80,932	80,932
Reserves/R.E./others	175,158	184,137	196,809	208,251	222,852	232,214	246,548	263,844
Shareholders' equity	256,090	265,069	277,741	289,183	303,784	313,146	327,480	344,776
Minority interests	788	961	923	925	967	967	967	967
Total equity & liabilities	419,115	545,072	543,239	561,274	629,561	641,400	662,189	685,812
EV	263,019	307,361	332,247	325,390	322,552	351,941	347,269	332,313
Net debt/(cash)	22,927	67,096	92,020	85,161	82,281	111,670	106,998	92,041
BVPS (CNY)	3.164	3.275	3.432	3.573	3.754	3.869	4.046	4.260

Key ratios (%)

Year to 31 Dec	2011	2012	2013	2014	2015	2016E	2017E	2018E
Sales (YoY)	11.5	15.5	13.6	0.9	2.1	4.4	5.8	5.4
EBITDA (YoY)	(0.6)	(6.0)	36.3	(1.8)	(0.8)	(2.1)	9.5	10.3
Operating profit (YoY)	(0.1)	(12.2)	29.7	3.8	(7.2)	(10.1)	20.0	19.4
Net profit (YoY)	3.8	(9.6)	17.6	0.8	13.4	(21.1)	22.8	21.2
Core EPS (fully-diluted) (YoY)	3.8	(9.6)	17.6	0.8	13.4	(21.1)	22.8	21.2
Gross-profit margin	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
EBITDA margin	30.8	25.0	30.0	29.2	28.4	26.6	27.6	28.8
Operating-profit margin	9.8	7.5	8.5	8.8	8.0	6.9	7.8	8.8
Net profit margin	6.7	5.3	5.5	5.5	6.1	4.6	5.3	6.1
ROAE	6.8	5.7	6.5	6.2	6.8	5.1	6.1	7.0
ROAA	4.0	3.1	3.2	3.2	3.4	2.5	3.0	3.5
ROCE	7.9	6.3	7.3	7.3	6.5	5.5	6.4	7.4
ROIC	6.5	5.3	6.0	5.8	5.2	4.5	5.1	5.9
Net debt to equity	9.0	25.3	33.1	29.4	27.1	35.7	32.7	26.7
Effective tax rate	24.6	24.0	23.5	23.6	24.5	23.6	23.6	24.5
Accounts receivable (days)	26.7	24.0	22.0	23.4	23.5	22.8	22.7	22.8
Current ratio (x)	0.5	0.3	0.3	0.3	0.3	0.2	0.3	0.3
Net interest cover (x)	10.7	13.5	5.3	5.4	6.2	5.2	5.9	7.2
Net dividend payout	34.1	37.0	34.8	34.4	32.2	32.2	32.2	32.2
Free cash flow yield	11.4	9.3	9.5	9.0	4.6	n.a.	6.1	10.8

Source: FactSet, Daiwa forecasts

Company profile

China Telecom is an integrated information-services operator. The company provides cellular services, based on a CDMA technology platform, in addition to fixed-line and broadband services in China. As at the end of 2013, it had 156 wire-line subscribers and mobile subscribers of about 186m. China Telecom's H shares and American Depositary Shares are listed on Hong Kong stock exchange and the New York Stock Exchange, respectively.

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Disclosure of investment ratings

Rating	Percentage of total
Buy*	65.8%
Hold**	21.8%
Sell***	12.4%

Source: Daiwa

Notes: data is for single-branded Daiwa research in Asia (ex Japan) and correct as of 30 June 2016.

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