

China Tower (788 HK)

2Q23 results in-line with expectations; cash flow under temporary pressure

China Tower released its 1H23 results, posting revenue and NP growth of 2.2% and 14.6% YoY. The sales from the legacy business (81% of total revenue) declined by 2.9% YoY, mainly due to additional pricing discount under the new Commercial Pricing Agreement (the number should grow 3.4% YoY under previous agreement). Their DAS and Two Wings business grew double-digit (30.4% in 1H23); however, the impact is minimal given their revenue contribution is less than 20%. Looking forward, we expect China Tower's overall growth will be in low single digits, affected by continuous cost optimization in major China telecoms. **Maintain HOLD with TP at HK\$0.89.**

- **Cost optimization from China telcos will continue to weigh on legacy tower business growth.** This segment's sales grew 3.4%/1.8% YoY in 2021/22. We tracked a key indicator to estimate China telco's tower leasing burden (figure 2), which clearly showed a declining trend. Therefore, we expect the tower sales will decline low single-digit (2.4%/3.6% YoY) in 2023/24E, factoring in the new pricing discount. DAS and Two Wings business (smart tower business and energy operations) may grow at double-digit. However, we think these segments do not have a meaningful impact on total revenue. Overall sales of the Company is likely to be flat (2.1%/1.9% YoY for 2023/24E).
- **Company's free cash flow under temporary pressure due to new pricing agreements with China telcos and heavier capex.** Free cash flow plunged by more than 105% in 1H23 to RMB-1.27bn as the Company's accounts receivable surged by more than 50% in 1H23 compared to FY22. Meanwhile, Company's capex grew by 41.1% YoY in 1H23 as it accelerated investments in the Two Wings business segments and ongoing constructions. However, mgmt. suggests the temporary cash flow pressure is unlikely to impact its full year dividend pay-out. We expect the Company's cash flow condition to return to normal level in 2H23-2024 as we are currently in the beginning phase of the new pricing agreements.
- **Maintain HOLD with TP adjusted to HK\$0.89,** based on 2.7x FY24 EV/EBITDA, which is ~1SD below 1-year forward EV/EBITDA multiple, as we think the overall growth for China Tower is limited.

Earnings Summary

(YE 31 Dec)	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue (RMB mn)	86,585	92,170	94,098	95,879	97,371
YoY growth (%)	6.8	6.5	2.1	1.9	1.6
Operating profit (RMB mn)	13,035	13,312	14,279	14,208	14,175
YoY growth (%)	8.5	2.1	7.3	(0.5)	(0.2)
EBITDA (RMB mn)	63,017	62,844	64,228	66,017	67,625
Net profit (RMB mn)	7,329.0	8,787.0	9,406.1	9,838.7	10,292.3
YoY growth (%)	14.0	19.9	7.0	4.6	4.6
EPS (RMB)	0.04	0.05	0.05	0.06	0.06
ROE (%)	3.9	4.6	4.8	4.9	5.1
EV/EBITDA (x)	3.16	2.84	2.76	2.38	2.00
Dividend yield (%)	3.6	4.5	5.0	5.4	5.8

Source: Company data, Bloomberg, CMBIGM estimates

HOLD (Maintain)

Target Price HK\$0.89
(Previous TP) HK\$1.01
Up/Downside 14.1%
Current Price HK\$0.78

China Technology

Lily YANG, Ph.D
(852) 3916 3716
lilyyang@cmbi.com.hk

Kevin ZHANG
(852) 3761 8727
kevinzhang@cmbi.com.hk

Stock Data

Mkt Cap (HK\$ mn)	137,286.6
Avg 3 mths t/o (HK\$ mn)	82.9
52w High/Low (HK\$)	1.00/0.71
Total Issued Shares (mn)	46,663.9

Source: FactSet

Shareholding Structure

Citigroup	9.0%
GIC	7.0%

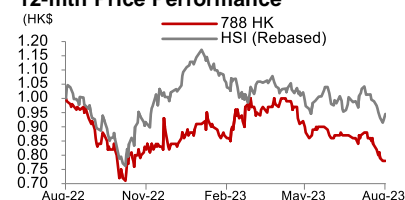
Source: Bloomberg

Share Performance

	Absolute	Relative
1-mth	-7.1%	-4.8%
3-mth	-13.3%	-9.0%
6-mth	-9.3%	-0.3%

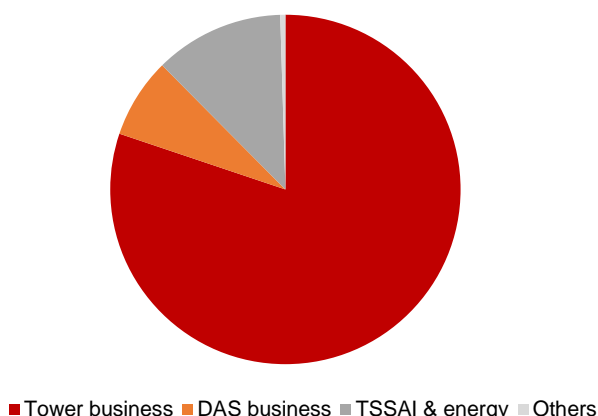
Source: FactSet

12-mth Price Performance



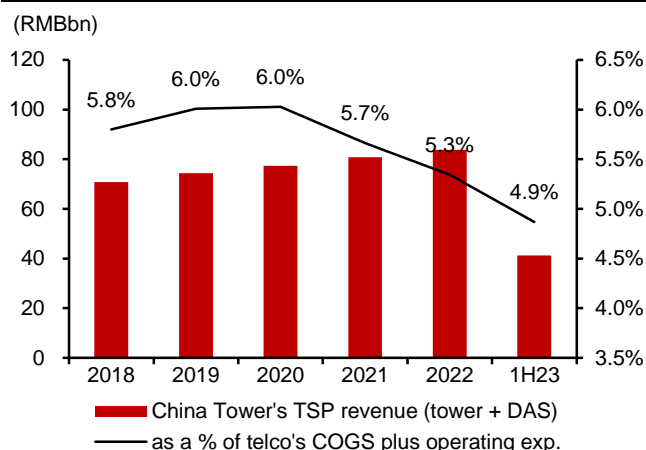
Source: FactSet

Figure 1: Revenue breakdown: Tower business contributed 80% of 6M23 revenue



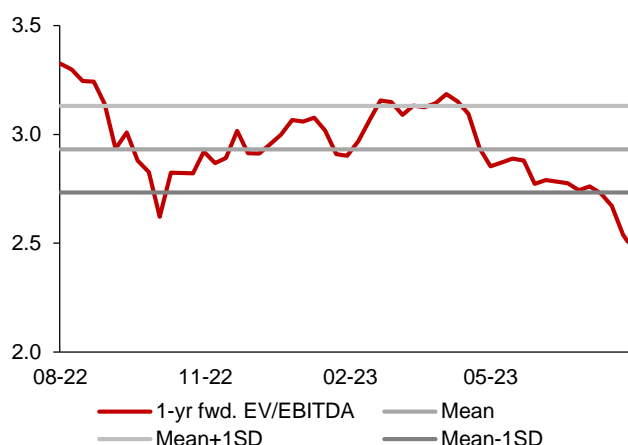
Source: Company data, CMBIGM estimates

Figure 2: China Tower's revenue accounted for a smaller % of telco's COGS & operating exp.



Source: Company data, CMBIGM estimates

Figure 3: 12M forward EV/EBITDA band



Source: Company data, CMBIGM estimates

Figure 4: 12M forward EV/EBITDA chart



Source: Company data, CMBIGM estimates

Figure 5: CMBIGM estimates vs. consensus

RMB mn	CMBI estimates			Consensus			Diff (%)		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Revenue	94,098	95,879	97,371	94,687	99,371	103,820	-1%	-4%	-6%
Operating Profit	14,279	14,208	14,175	14,941	16,985	20,601	-4%	-16%	-31%
Net profit	9,406	9,839	10,292	9,541	10,964	14,180	-1%	-10%	-27%
EPS (RMB)	0.05	0.06	0.06	0.05	0.06	0.08	-1%	-8%	-25%
Operating Margin	15.2%	14.8%	14.6%	15.8%	17.1%	19.8%	-0.6 ppt	-2.3 ppt	-5.3 ppt
Net Margin	10.0%	10.3%	10.6%	10.1%	11.0%	13.7%	-0.1 ppt	-0.8 ppt	-3.1 ppt

Source: Company data, CMBIGM estimates

Figure 6: Earnings revision

RMB mn	New		Old		Diff (%)	
	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
Revenue	94,098	95,879	96,537	100,566	-3%	-5%
Operating Profit	14,279	14,208	15,456	16,542	-8%	-14%
Net profit	9,406	9,839	9,649	10,698	-3%	-8%
EPS (RMB)	0.05	0.06	0.06	0.06	-10%	-6%
Operating Margin	10.0%	10.3%	10.0%	10.6%	0 ppt	-0.4 ppt
Net Margin	94,098	95,879	96,537	100,566	-3%	-5%

Source: Company data, CMBIGM estimates

Financial Summary

INCOME STATEMENT	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Revenue	81,099	86,585	92,170	94,098	95,879	97,371
Operating expenses	(69,087)	(73,550)	(78,858)	(79,819)	(81,671)	(83,196)
D&A	(47,515)	(49,982)	(49,532)	(49,949)	(51,809)	(53,450)
Admin expense	(6,115)	(6,875)	(7,940)	(8,103)	(8,065)	(7,996)
Repairs and maintenance	(5,805)	(5,796)	(7,593)	(7,292)	(7,238)	(7,156)
Site operating lease expenses	(4,627)	(5,161)	(5,857)	(5,352)	(5,262)	(5,149)
Others	(5,025)	(5,736)	(7,936)	(9,122)	(9,298)	(9,445)
Operating profit	12,012	13,035	13,312	14,279	14,208	14,175
Other income	318	303	1,095	573	584	593
Interest income	36	22	124	0	0	0
Interest expense	(3,959)	(3,745)	(3,003)	(2,512)	(1,884)	(1,266)
Other income/expense	0	0	0	0	0	0
Pre-tax profit	8,407	9,615	11,528	12,340	12,908	13,503
Income tax	(1,980)	(2,287)	(2,741)	(2,934)	(3,069)	(3,211)
After tax profit	6,427	7,328	8,787	9,406	9,839	10,292
Minority interest	(1)	(1)	0	0	0	0
Net profit	6,428	7,329	8,787	9,406	9,839	10,292

BALANCE SHEET	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Current assets	43,204	48,344	49,706	61,419	59,037	57,783
Cash & equivalents	5,042	6,471	5,117	4,112	9,537	15,010
Account receivables	30,658	34,194	42,260	54,954	47,104	40,338
Inventories	0	0	0	0	0	0
Prepayment	7,504	7,679	2,329	2,352	2,397	2,434
Other current assets	0	0	0	0	0	0
Contract assets	0	0	0	0	0	0
Non-current assets	294,176	274,915	255,854	242,302	228,068	212,310
PP&E	231,684	221,419	209,377	199,548	187,682	174,697
Right-of-use assets	34,553	32,877	31,578	29,362	26,323	22,525
Intangibles	0	0	0	0	0	0
Goodwill	0	0	0	0	0	0
Other non-current assets	27,939	20,619	14,899	13,392	14,063	15,089
Total assets	337,380	323,259	305,560	303,721	287,106	270,093
Current liabilities	106,635	76,182	65,158	46,842	33,416	20,023
Short-term borrowings	61,999	37,142	25,597	9,634	0	(10,144)
Account payables	31,460	25,264	26,646	24,914	22,369	20,315
Other current liabilities	5,752	6,342	5,510	5,596	5,290	4,976
Lease liabilities	7,006	6,913	7,127	6,477	5,548	4,679
Contract liabilities	0	0	0	0	0	0
Accrued expenses	418	521	278	222	209	197
Non-current liabilities	44,499	57,723	46,811	59,594	52,870	45,746
Long-term borrowings	27,121	41,572	31,448	44,960	39,610	33,813
Other non-current liabilities	17,378	16,151	15,363	14,634	13,260	11,934
Total liabilities	151,134	133,905	111,969	106,437	86,285	65,770
Share capital	176,008	176,008	176,008	176,008	176,008	176,008
Retained earnings	10,237	13,346	17,583	21,277	24,812	28,315
Other reserves	0	0	0	0	0	0
Total shareholders equity	186,245	189,354	193,591	197,285	200,820	204,323
Minority interest	1	0	0	0	0	0
Total equity and liabilities	337,380	323,259	305,560	303,721	287,106	270,093

CASH FLOW	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Operating						
Profit before taxation	8,407	9,615	11,528	9,406	9,839	10,292
Depreciation & amortization	47,515	49,982	49,532	49,949	51,809	53,450
Change in working capital	(4,901)	(2,360)	(7,454)	(14,714)	5,393	5,311
Others	6,527	3,266	11,528	2,404	249	(703)
Net cash from operations	57,548	60,503	65,134	47,045	67,289	68,350
Investing						
Capital expenditure	(37,800)	(32,513)	(28,639)	(33,623)	(33,300)	(32,845)
Acquisition of subsidiaries/ investments	0	0	0	0	0	0
Others	(97)	998	982	(2,404)	(3,111)	(3,862)
Net cash from investing	(37,897)	(31,515)	(27,657)	(36,027)	(36,412)	(36,707)
Financing						
Dividend paid	(2,561)	(3,934)	(4,618)	(5,712)	(6,303)	(6,790)
Net borrowings	(6,594)	(10,521)	(21,870)	(2,451)	(14,984)	(15,941)
Proceeds from share issues	0	0	0	0	0	0
Others	(11,682)	(13,105)	(12,337)	(3,860)	(4,166)	(3,439)
Net cash from financing	(20,837)	(27,560)	(38,825)	(12,023)	(25,453)	(26,170)
Net change in cash						
Cash at the beginning of the year	6,223	5,042	6,471	5,117	4,112	9,537
Exchange difference	5	1	(6)	0	0	0
Cash at the end of the year	5,042	6,471	5,117	4,112	9,537	15,010

Disclosures & Disclaimers

Analyst Certification

The research analyst who is primary responsible for the content of this research report, in whole or in part, certifies that with respect to the securities or issuer that the analyst covered in this report: (1) all of the views expressed accurately reflect his or her personal views about the subject securities or issuer; and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific views expressed by that analyst in this report.

Besides, the analyst confirms that neither the analyst nor his/her associates (as defined in the code of conduct issued by The Hong Kong Securities and Futures Commission) (1) have dealt in or traded in the stock(s) covered in this research report within 30 calendar days prior to the date of issue of this report; (2) will deal in or trade in the stock(s) covered in this research report 3 business days after the date of issue of this report; (3) serve as an officer of any of the Hong Kong listed companies covered in this report; and (4) have any financial interests in the Hong Kong listed companies covered in this report.

CMBIGM Ratings

BUY	: Stock with potential return of over 15% over next 12 months
HOLD	: Stock with potential return of +15% to -10% over next 12 months
SELL	: Stock with potential loss of over 10% over next 12 months
NOT RATED	: Stock is not rated by CMBIGM
OUTPERFORM	: Industry expected to outperform the relevant broad market benchmark over next 12 months
MARKET-PERFORM	: Industry expected to perform in-line with the relevant broad market benchmark over next 12 months
UNDERPERFORM	: Industry expected to underperform the relevant broad market benchmark over next 12 months

CMB International Global Markets Limited

Address: 45/F, Champion Tower, 3 Garden Road, Hong Kong. Tel: (852) 3900 0888 Fax: (852) 3900 0800

CMB International Global Markets Limited ("CMBIGM") is a wholly owned subsidiary of CMB International Capital Corporation Limited (a wholly owned subsidiary of China Merchants Bank)

Important Disclosures

There are risks involved in transacting in any securities. The information contained in this report may not be suitable for the purposes of all investors. CMBIGM does not provide individually tailored investment advice. This report has been prepared without regard to the individual investment objectives, financial position or special requirements. Past performance has no indication of future performance, and actual events may differ materially from that which is contained in the report. The value of, and returns from, any investments are uncertain and are not guaranteed and may fluctuate as a result of their dependence on the performance of underlying assets or other variable market factors. CMBIGM recommends that investors should independently evaluate particular investments and strategies, and encourages investors to consult with a professional financial advisor in order to make their own investment decisions.

This report or any information contained herein, have been prepared by the CMBIGM, solely for the purpose of supplying information to the clients of CMBIGM or its affiliate(s) to whom it is distributed. This report is not and should not be construed as an offer or solicitation to buy or sell any security or any interest in securities or enter into any transaction. Neither CMBIGM nor any of its affiliates, shareholders, agents, consultants, directors, officers or employees shall be liable for any loss, damage or expense whatsoever, whether direct or consequential, incurred in relying on the information contained in this report. Anyone making use of the information contained in this report does so entirely at their own risk.

The information and contents contained in this report are based on the analyses and interpretations of information believed to be publicly available and reliable. CMBIGM has exerted every effort in its capacity to ensure, but not to guarantee, their accuracy, completeness, timeliness or correctness. CMBIGM provides the information, advices and forecasts on an "AS IS" basis. The information and contents are subject to change without notice. CMBIGM may issue other publications having information and/ or conclusions different from this report. These publications reflect different assumption, point-of-view and analytical methods when compiling. CMBIGM may make investment decisions or take proprietary positions that are inconsistent with the recommendations or views in this report.

CMBIGM may have a position, make markets or act as principal or engage in transactions in securities of companies referred to in this report for itself and/or on behalf of its clients from time to time. Investors should assume that CMBIGM does or seeks to have investment banking or other business relationships with the companies in this report. As a result, recipients should be aware that CMBIGM may have a conflict of interest that could affect the objectivity of this report and CMBIS will not assume any responsibility in respect thereof. This report is for the use of intended recipients only and this publication, may not be reproduced, reprinted, sold, redistributed or published in whole or in part for any purpose without prior written consent of CMBIGM.

Additional information on recommended securities is available upon request.

For recipients of this document in the United Kingdom

This report has been provided only to persons (I) falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (as amended from time to time) ("The Order") or (II) are persons falling within Article 49(2) (a) to (d) ("High Net Worth Companies, Unincorporated Associations, etc.") of the Order, and may not be provided to any other person without the prior written consent of CMBIGM.

For recipients of this document in the United States

CMBIGM is not a registered broker-dealer in the United States. As a result, CMBIGM is not subject to U.S. rules regarding the preparation of research reports and the independence of research analysts. The research analyst who is primary responsible for the content of this research report is not registered or qualified as a research analyst with the Financial Industry Regulatory Authority ("FINRA"). The analyst is not subject to applicable restrictions under FINRA Rules intended to ensure that the analyst is not affected by potential conflicts of interest that could bear upon the reliability of the research report. This report is intended for distribution in the United States solely to "major US institutional investors", as defined in Rule 15a-6 under the US, Securities Exchange Act of 1934, as amended, and may not be furnished to any other person in the United States. Each major US institutional investor that receives a copy of this report by its acceptance hereof represents and agrees that it shall not distribute or provide this report to any other person. Any U.S. recipient of this report wishing to effect any transaction to buy or sell securities based on the information provided in this report should do so only through a U.S.-registered broker-dealer.

For recipients of this document in Singapore

This report is distributed in Singapore by CMBI (Singapore) Pte. Limited (CMBISG) (Company Regn. No. 201731928D), an Exempt Financial Adviser as defined in the Financial Advisers Act (Cap. 110) of Singapore and regulated by the Monetary Authority of Singapore. CMBISG may distribute reports produced by its respective foreign entities, affiliates or other foreign research houses pursuant to an arrangement under Regulation 32C of the Financial Advisers Regulations. Where the report is distributed in Singapore to a person who is not an Accredited Investor, Expert Investor or an Institutional Investor, as defined in the Securities and Futures Act (Cap. 289) of Singapore, CMBISG accepts legal responsibility for the contents of the report to such persons only to the extent required by law. Singapore recipients should contact CMBISG at +65 6350 4400 for matters arising from, or in connection with the report.