Bargain-hunting in Europe – it's Ireland today

Quick Note

June 24, 2013

Rating Remains	Buy
Target price Remains	HKD 100.00
Closing price June 21, 2013	HKD 78.05

Event – Hutch acquiring O2 Ireland for €780mn

- Bloomberg today quoted Hutch's 3-Ireland statement that Hutch (4th-largest player in the Irish mobile market) is buying Telefonica's (TEF SM) O2 unit in Ireland (2nd largest) for €780mn. There will be an additional deferred payment of €70mn if certain performance targets are reached.
- The deal itself should not be a surprise to the market, as Bloomberg reported the possible sale of O2 Ireland on 10th June already. Telefonica has been attempting to sell assets since last year to reduce its debt levels.
- With the two operators combined, Hutch will command a 37.5% share of the Irish mobile market, just behind Vodafone's (VOD LN) leading over-40% share. This merger will give Hutch a much stronger footing in Ireland, and also likely give rise to revenue/cost benefits from a much more consolidated market.
- Acquisition valuation – €780mn is equivalent to 6x EV/EBITDA in 2012, lower than the 6.9x that Hutch paid for Orange Austria (not listed) last year. Admittedly, 6x is higher than the average of 5x for Europe telco operators, but we believe there will be a number of cost synergy benefits that Hutch can potentially realise in the future, so that the acquisition valuation might come down to less than 5x.
- Please see table below for the financial details of 3-Ireland and O2 Ireland.

Fig. 1: Financial details of 3-Ireland and O2 Ireland

	Hutch 3-Ireland	O2 in Ireland
Revenue, 2012 (Eur mn)	174 (+16% y-y)	629 (-13% y-y)
EBITDA, 2012 (Eur mn)	19 (loss)	130 (-37% y-y)
EBITDA margin, 2012	-10.9%	20.7%
Subscribers	819k (end of 2012)	1,561 mn (Mar 2013)
Market share	A combined 37.5%	

Source: Company data, Comreg

Our view: more bargain-hunting in Europe should pay off in the future

- Ireland is the only European market that has as yet failed to generate positive EBITDA for Hutch's 3 Group. From the table above, we can comfortably conclude that 3-Ireland will turn EBITDA-positive after this acquisition and, more importantly, put Hutch in a very competitive position in the Irish market.

Research analysts

Hong Kong Conglomerates

Benjamin Lo - NIHK
benjamin.lo@nomura.com
+852 2252 6220

Sylvia Chan - NIHK
sylvia.chan@nomura.com
+852 2252 1414

See Appendix A-1 for analyst certification, important disclosures and the status of non-US analysts.

- *The bigger implication for investors is that we should expect the Hutch group to continue bargain-hunting in Europe*. Its infrastructure subsidiary Cheung Kong Infrastructure (1038 HK, NR) has made a few acquisitions in the UK and Europe in the past two years, while Hutch's telecom division has now secured a firmer market position in both Ireland and Austria. *As we argued in our recent Hutch report (Positive thesis continues into 2013; TP raised), Europe is incrementally less of a concern for investors, and our positive thesis for Hutch is premised on the continued "unwinding of the Europe fear factor". We believe that, one day, these bargain-hunting exercises will bear fruit for Hutch.*
- Share price reaction – While we are positive on Hutch, this acquisition alone is unlikely to have a major share price impact, in our view, owing to its relatively small scale (less than 2% of Hutch's total NAV).
- As a final note, this deal is subject to regulatory approval, which is fairly uncertain, in our view. The merger of Hutch's 3-Austria (4th-largest player) and Orange Austria (3rd largest) faced very stringent anti-trust scrutiny last year, and it took almost a year for Hutch to gain the necessary approvals after agreeing to some remedies.

Share outperformance to continue; maintain Buy rating with TP at HKD100

- *Hutch has outperformed the MSCI-HK by 3% in the past one month.* We expect its share outperformance to continue on the back of: (1) the "unwinding of the Europe fear factor", and (2) Hutch's relatively small exposure to Hong Kong properties (11% of NAV) and China overall (19% of EBIT), both of which have become more of a concern for investors than its Europe exposure.
- Hutch's share is trading at a 35% discount to 2013F NAV and 10x 2013F P/E while yielding over 3%. Our TP of HKD100 is based on a 19% discount (ie. half-SD below mean) to our 2013F NAV.

Appendix A-1

Analyst Certification

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Materially mentioned issuers

Issuer	Ticker	Price	Price date	Stock rating	Sector rating	Disclosures
Hutchison Whampoa	13 HK	HKD 78.05	21-Jun-2013	Buy	Not rated	A10,A13

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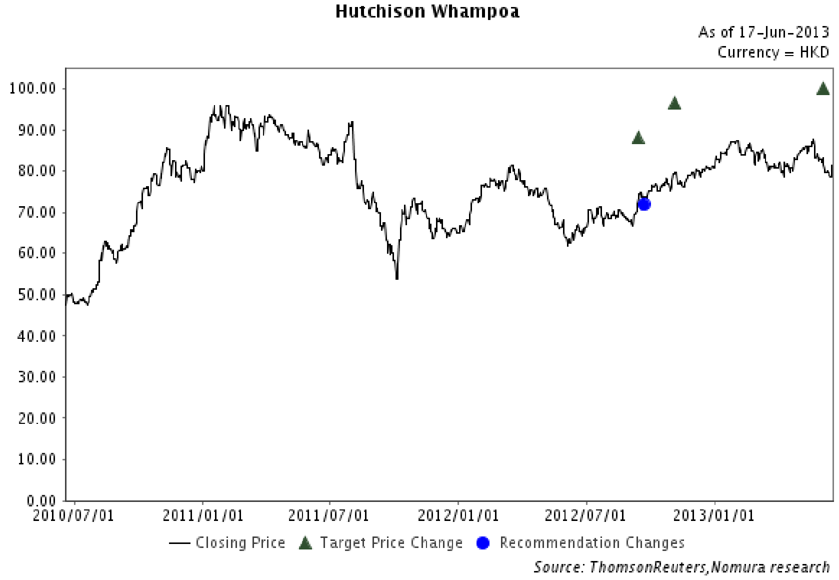
Hutchison Whampoa (13 HK) **HKD 78.05 (21-Jun-2013)** Buy (Sector rating: Not rated)

Rating and target price chart (three year history)



Date	Rating	Target price	Closing price
05-Jun-13		100.00	81.45
05-Nov-12		96.40	79.65
13-Sep-12	Buy		73.25
13-Sep-12		88.00	73.25

For explanation of ratings refer to the stock rating keys located after chart(s)

Valuation Methodology Our TP of HKD100 is based on a 19% discount (ie. half-SD below mean) to 2013F NAV of HKD123. Our NAV is in turn based on sum-of-the-part valuation - retail is valued on 12x EV/EBITDA; development properties are valued on DCF; investment properties are valued on cap rates that are in line with Nomura Property Research team's assumptions; both unlisted ports and 3 Group are valued on DCF; and all separately listed assets are valued at their respective market values.

Risks that may impede the achievement of the target price Downside risks include: (1) 3 Group turning FCF-negative; (2) further deterioration of Europe macro conditions; (3) further tightening in the Chinese property market; (4) significant reduction in value of its holdings in US Treasury notes and listed/traded debt securities which totalled HKD14bn at the end of 2012 (equivalent to 11% of its total liquid assets, and less than 3% of our FY13F NAV); (5) forex fluctuations.

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Explanation of Nomura's equity research rating system in Japan and Asia ex-Japan

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