

## China Unicom (762 HK)

### Headwinds ahead in 2020

- China Unicom's revenue is expected to grow 0.9% YoY in 2020E without benefiting much from the 5G launch and co-operation with China Telecom (728 HK)
- China Unicom's mobile ARPU in 2019 dropped the most and was the lowest among telecom operators, showing the higher prevalence of lower-end users than peers
- We expect net profit to grow 9.7% YoY in 2020E
- Maintain **HOLD** with TP of HK\$4.80, which implies 1.4x/1.3x FY20E/ FY21E EV/EBITDA

**We project mobile ARPU to drop at 3.0%/1.5%/0.3% YoY in 2020E-22E.** China Unicom's mobile ARPU dropped the most and was the lowest in FY19 among telecom operators. Due to the influence of Speed Upgrade and Tariff Reduction and market competition, we expect its ARPU to continue to fall.

**We expect blended mobile user to drop at 0.6%/0.3%/0.2% YoY for 2020-22E.** Due to market saturation and stiff competition, the Group's mobile user growth would drop in 2019.

**2020E CAPEX to be RMB70bn, up 24.1% YoY (including RMB35 bn for 5G, up 343% YoY).** China Unicom will co-share and co-build 5G network with China Telecom (728 HK). We expect limited contributions from the 5G network to the Group in 2020 given its lower-end user profile than China Mobile's (941 HK).

**Valuation.** We trim FY20E-21E net profit by 27.1%/ 34.0% YoY to reflect policy impact on mobile ARPU and user saturation. We lower TP from HK\$ 8.00 to HK\$ 4.80, implying 1.4x/ 1.3x FY20E/ FY21E EV/EBITDA. Maintain **HOLD** based on limited share price upside (8.1%).

**Risk factors:** 1) Delayed launch of 5G network; 2) Further reduction in mobile data tariff by regulators; 3) Decline of mobile users and ARPU.

#### Results and Valuation

FY ended Dec 31	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	290,877	290,515	293,112	297,937	303,758
Chg (% YoY)	5.8	(0.1)	0.9	1.6	2.0
Net profit (RMB mn)	10,197	11,330	12,428	14,136	17,166
Chg (% YoY)	457.8	11.1	9.7	13.7	21.4
EPS (RMB)	0.333	0.370	0.406	0.462	0.561
Chg (% YoY)	347.9	11.1	9.7	13.7	21.4
BVPS (RMB)	10.27	10.48	10.73	11.03	11.41
Chg (% YoY)	(17.1)	2.1	2.4	2.8	3.4
P/E (x)	11.7	10.8	9.8	8.6	7.1
P/B (x)	0.38	0.38	0.37	0.36	0.35
ROAE (%)	3.3	3.6	3.9	4.3	5.0
ROAA (%)	1.8	2.1	2.2	2.3	2.6
DPS (RMB)	0.13	0.15	0.16	0.18	0.22
Dividend Yield (%)	3.44	3.70	4.06	4.62	5.61

\*Exchange rate assumption for FY20E-22E: 1 HKD = 0.900 RMB

Source(s): Bloomberg, ABCI Securities estimates

## Company Report

April 2, 2020  
Rating: **HOLD**  
TP: **HK\$4.80**

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Share price (HK\$)	4.44
Est. share price return	8.1%
Est. dividend yield	4.1%
Est. total return	12.2%
Previous Rating & TP	HOLD/HK\$8.0
Previous Report Date	Sept 4, 2019

Source(s): Bloomberg, ABCI Securities estimates

#### Key Data

52Wk H/L(HK\$)	10.50/3.84
Issued shares (mn)	30,598.1
Market cap (HK\$ mn)	135,855
Avg daily turnover (HK\$ mn)	279.4
Major shareholder(s)	
China Unicom Group	53.5%
Capital Group Cos Inc	1.3%
Blackrock	1.0%

Source(s): Company, ABCI Securities

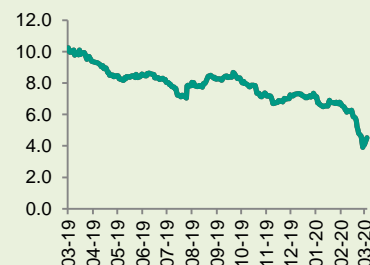
#### Share Performance (%)

	Absolute	Relative*
1-mth	(32.4)	(18.6)
3-mth	(37.1)	(22.7)
6-mth	(45.3)	(36.6)

\*Relative to HSI

Source(s): Bloomberg, ABCI Securities

#### Share performance (HK\$)



Source(s): Bloomberg, ABCI Securities



China Unicom's FY19 net profit came in weaker than expected due to the higher operating costs (mainly from employee benefit expenses) and lower than expected mobile ARPU. Due to the launch of Speed Upgrade and Tariff Reduction policy and fierce market competition, FY19 mobile ARPU fell 11.6% YoY to RMB 40.4. Compared with other telecom operators, China Unicom's mobile ARPU dropped the most (-11.6%YoY) and was the lowest among peers in FY19, showing a lower user tier than other telecom operators. Although its mobile ARPU was the lowest, China Unicom still fell behind others in mobile user growth at only 1.1% in 2019, compared to China Mobile's 2.7% and China Telecom's 10.7%.

Exhibit 1: Telecom operators' 2019 mobile operational data comparison table

	China Mobile	China Unicom	China Telecom
ARPU (RMB)	49.1	40.4	45.8
YoY	-7.5%	-11.6%	-9.3%
Mobile users (mn)	950.3	318.5	335.6
YoY	2.7%	1.1%	10.7%

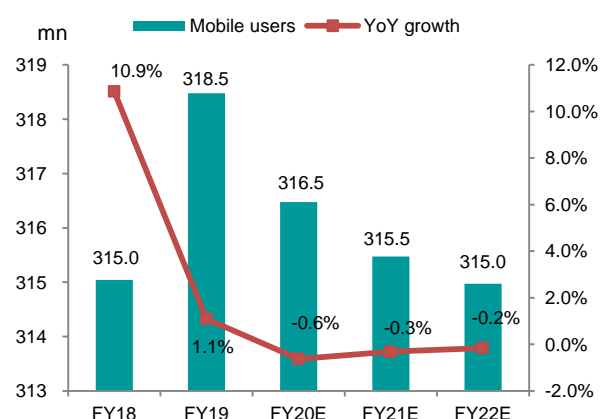
Source(s): Companies

The Group's blended mobile users grew 1.1% to 318.5mn in FY19 (including 254mn 4G users, representing an 80% 4G user penetration rate). China Unicom provides the 2020 guidance with 50mn 5G user additions in 2020 and a CAPEX of RMB70bn (+ 24.1% YoY, including RMB35 bn for 5G, + 343% YoY). China Unicom will continue to co-build and co-share (250,000 of base stations) with China Telecom in 5G network in 2020 to save CAPEX.

We estimate China Unicom's blended mobile users to drop 0.6%/ 0.3%/ 0.2% in 2020-22E. Due to the Speed Upgrade and Tariff Reduction policy and market competition; we project mobile ARPU to decline by 3.0%/ 1.5%/ 0.3% in 2020E-22E.

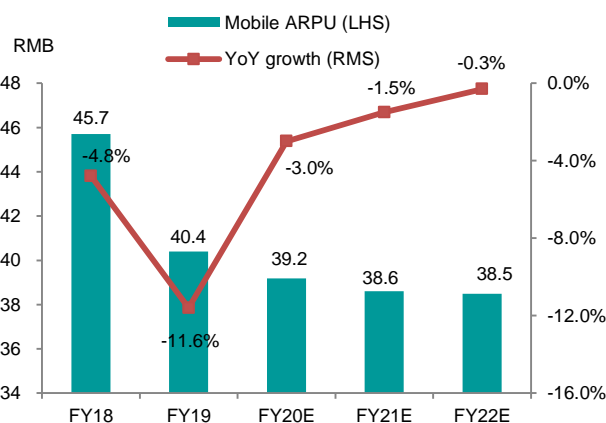
Under the virus outbreak, management expect: (1) fewer customers to visit its retail shops; (2) SME customers' bad debts may increase; (3) cloud computing usage to increase.

Exhibit 2: China Unicom's mobile users and growth



Source(s): Company, ABCI Securities estimates

Exhibit 3: China Unicom's mobile ARPU and growth



Source(s): Company, ABCI Securities estimates



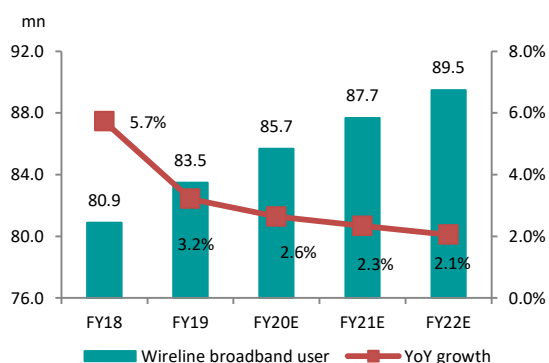
Exhibit 4: Telecom operators' 2019 wireline broadband operational data comparison table

	China Mobile	China Unicom	China Telecom
Wireline broadband users (mn)	187.0	83.5	153.1
yoy	19.4%	3.2%	5.0%
Wireline broadband ARPU (RMB)	32.8	41.6	38.1
yoy	-2.1%	-6.7%	-14.0%

Source(s): Companies

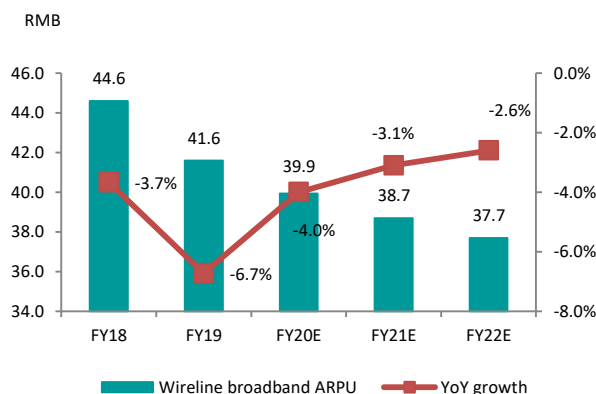
In 2019, China Unicom's wireline broadband business was disappointing with the slowest growth in user amid its smallest user base compared with other telecom operators. We believe the Company is relative weak in broadband services competitiveness among the peers which may be due to its relative high ARPU and poor broadband access quality. The Group's wireline broadband user grew 3.2% to 83.5mn in FY19. We estimate China Unicom's wireline broadband user to grow 2.6%/2.3%/2.1% in 2020E-22E. Wireline broadband ARPU dropped 6.7% in FY19. We project the Group's wireline broadband ARPU to drop 4.0%/3.1%/2.6% in 2020E-22E.

Exhibit 5: China Unicom's wireline broadband user and growth



Source(s): Company, ABCI Securities estimates

Exhibit 6: China Unicom's wireline broadband ARPU and growth



Source(s): Company, ABCI Securities estimates

We cut 2020E-21E revenue by 10%/20% due to the adjustment of ARPU and user estimates. We revise down 2020-21E net profits by 27.1%/ 34.0% to reflect policy impacts on mobile ARPU and fierce market competition.

Exhibit 7: Changes in our financial estimates

	OLD			NEW			CHANGE		
(RMB Bn)	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Revenue	325,680	372,421	N/A	293,112	297,937	303,758	-10.0%	-20.0%	N/A
Operating profit	14,084	17,971	N/A	12,574	13,656	16,573	-10.7%	-24.0%	N/A
Net Profit	17,059	21,405	N/A	12,428	14,136	17,166	-27.1%	-34.0%	N/A

Source(s): Company, ABCI Securities estimates



Exhibit 8: Major assumptions:

	FY20E	FY21E	FY22E
Overall mobile users (mn)	316.5	315.5	315.0
Mobile ARPU (RMB)	39.2	38.6	38.5
5G users (mn)	50.0	120.0	190.0
5G ARPU (RMB)	47.0	51.0	56.0
Non-5G mobile users (mn)	266.5	195.5	125.0
Non-5G ARPU (RMB)	34.5	32.0	30.0

Source(s): ABCI Securities estimates

## HOLD with TP of HK\$4.80

TP falls from HK\$ 8.00 to HK\$ 4.80 based on our DCF model (WACC: 13.2%; perpetuity growth rate: 2%), which represents 1.4x/ 1.3x FY20E/ FY21E EV/EBITDA. Maintain **HOLD** on limited share price upside (8.1%).

Exhibit 9: Peer comparison

			P/E				P/B				ROE	ROA	EV/EBITDA
	Ticker	Price*	18A	19A	20E	21E	18A	19A	20E	21E	20E	20E	20E
<b>China Market</b>													
China Unicom	762 HK	4.44	10.8	10.0	8.4	7.2	0.4	0.4	0.4	0.3	4.7	2.7	1.0
China Mobile	941 HK	57.05	7.8	9.0	9.3	9.1	0.9	0.9	0.9	0.8	9.6	6.5	2.3
China Telecom	728 HK	2.32	7.2	7.7	7.6	7.4	0.5	0.5	0.4	0.4	6.1	3.3	1.9
China Tower	788 HK	1.70	76.3	48.1	33.8	25.7	1.4	0.4	1.4	1.3	4.0	2.3	5.7
Simple Avg.			25.5	18.7	14.8	12.4	0.8	0.5	0.8	0.7	6.1	3.7	2.8
<b>US Market</b>													
AT&T	T US	28.05	9.9	19.5	17.0	13.7	2.9	2.6	2.3	1.9	15.3	6.7	13.3
Verizon	VZ US	52.92	14.3	11.5	10.8	10.5	4.2	3.6	3.1	2.7	30.9	7.0	6.7
T-Mobile	TMUS US	85.13	23.4	19.6	17.6	14.9	2.7	2.4	2.1	1.8	11.5	3.3	6.5
American Tower	AMT US	206.97	74.9	48.9	46.0	40.5	17.3	18.3	21.8	36.5	41.6	4.1	22.8
Simple Avg.			13.0	16.8	15.1	13.0	2.8	2.5	2.2	2.0	14.3	4.3	8.2

\*Based on closing price on April 1, 2020

Source(s): Bloomberg's market consensus



Consolidated income statement (2018A-2022E)

FY Ended Dec 31 (RMB mn)	2018A	2019A	2020E	2021E	2022E
Mobile service revenue	165,064	156,381	149,295	146,360	145,575
Fixed line service revenue	96,295	105,659	113,478	120,286	126,060
Others	29,518	28,475	30,339	31,290	32,123
<b>Total revenue</b>	<b>290,877</b>	<b>290,515</b>	<b>293,112</b>	<b>297,937</b>	<b>303,758</b>
Interconnection charges	(12,579)	(11,513)	(11,421)	(11,330)	(11,239)
D&A	(75,777)	(83,080)	(83,495)	(84,664)	(85,765)
Network operation & support	(55,077)	(43,236)	(43,295)	(43,176)	(42,945)
Employee benefit expenses	(48,143)	(50,516)	(49,243)	(50,649)	(51,639)
Cost of product sold	(27,604)	(26,412)	(27,958)	(28,881)	(29,689)
Other operating expenses	(62,561)	(64,480)	(65,125)	(65,581)	(65,909)
<b>Total operating expenses</b>	<b>(281,741)</b>	<b>(279,237)</b>	<b>(280,537)</b>	<b>(284,281)</b>	<b>(287,185)</b>
<b>Operating Profits</b>	<b>9,136</b>	<b>11,278</b>	<b>12,574</b>	<b>13,656</b>	<b>16,573</b>
Finance cost	(1,625)	(2,123)	(2,488)	(2,833)	(3,335)
Interest income	1,712	1,272	1,358	2,479	3,561
Others (including associates, JV & other)	3,858	3,740	4,097	4,374	4,665
<b>Profit before tax</b>	<b>13,081</b>	<b>14,167</b>	<b>15,540</b>	<b>17,676</b>	<b>21,464</b>
Tax	(2,824)	(2,795)	(3,066)	(3,487)	(4,235)
<b>Profit after tax</b>	<b>10,257</b>	<b>11,372</b>	<b>12,474</b>	<b>14,189</b>	<b>17,230</b>
Minority interests	60	42	46	52	64
<b>Shareholders' net profit</b>	<b>10,197</b>	<b>11,330</b>	<b>12,428</b>	<b>14,136</b>	<b>17,166</b>
<b>EBITDA</b>	<b>84,910</b>	<b>94,358</b>	<b>96,070</b>	<b>98,321</b>	<b>102,338</b>
<b>EPS (RMB)</b>	<b>0.333</b>	<b>0.370</b>	<b>0.406</b>	<b>0.462</b>	<b>0.561</b>
<b>DPS (RMB)</b>	<b>0.134</b>	<b>0.148</b>	<b>0.162</b>	<b>0.185</b>	<b>0.224</b>
<b>Costs ratios:</b>					
<b>% to revenue:</b>					
Interconnection charges	4.3%	4.0%	3.9%	3.8%	3.7%
D&A	26.1%	28.6%	28.5%	28.4%	28.2%
Networks, operations and support expenses	18.9%	14.9%	14.8%	14.5%	14.1%
Employee benefit expenses	16.6%	17.4%	16.8%	17.0%	17.0%
Cost of product sold	9.5%	9.1%	9.5%	9.7%	9.8%
Other operating expenses	21.5%	22.2%	22.2%	22.0%	21.7%
<b>Revenue composition:</b>					
<b>% to revenue</b>					
Mobile service revenue	56.7%	53.8%	50.9%	49.1%	47.9%
Fixed line service revenue	33.1%	36.4%	38.7%	40.4%	41.5%
Others	10.1%	9.8%	10.4%	10.5%	10.6%

Source(s): Company, ABCI Securities estimates



Consolidated balance sheet (2018A-2022E)

As of Dec 31 (RMB mn)	2018A	2019A	2020E	2021E	2022E
PPE	384,475	367,401	376,586	386,001	395,651
Interest in associates	35,758	36,445	37,174	37,917	38,676
Other non-current assets	44,178	75,058	70,978	67,732	65,159
<b>Total non-current assets</b>	<b>464,411</b>	<b>478,904</b>	<b>484,738</b>	<b>491,650</b>	<b>499,485</b>
Cash & cash equivalents	30,060	34,945	66,850	97,622	128,256
Accounts receivables	14,433	17,233	14,455	14,693	15,812
Others	31,416	31,417	29,014	28,209	28,294
<b>Total current assets</b>	<b>75,909</b>	<b>83,595</b>	<b>110,319</b>	<b>140,524</b>	<b>172,362</b>
<b>Total assets</b>	<b>540,320</b>	<b>562,499</b>	<b>595,058</b>	<b>632,174</b>	<b>671,847</b>
Accounts payable and accrued liabilities	122,458	121,564	86,657	96,475	98,535
Loans	15,085	14,559	10,794	8,473	7,021
Others	77,367	69,067	136,072	158,376	186,989
<b>Total current liabilities</b>	<b>214,910</b>	<b>205,190</b>	<b>233,523</b>	<b>263,324</b>	<b>292,545</b>
Promissory notes	999	2,998	1,799	1,079	648
Others	10,125	33,556	31,405	30,261	29,616
<b>Total non-current liabilities</b>	<b>11,124</b>	<b>36,554</b>	<b>33,203</b>	<b>31,340</b>	<b>30,264</b>
<b>Total liabilities</b>	<b>226,034</b>	<b>241,744</b>	<b>266,727</b>	<b>294,664</b>	<b>322,808</b>
<b>Shareholders' profit</b>	<b>313,922</b>	<b>320,047</b>	<b>327,946</b>	<b>337,115</b>	<b>348,630</b>
<b>Non-controlling interests</b>	<b>364</b>	<b>708</b>	<b>385</b>	<b>395</b>	<b>409</b>
<b>Total equity</b>	<b>314,286</b>	<b>320,755</b>	<b>328,331</b>	<b>337,510</b>	<b>349,038</b>

Source(s): Company, ABCI Securities estimates



### Consolidated Cash Flow Statement (2018A-2022E)

As of Dec 31 (RMB mn)	2018A	2019A	2020E	2021E	2022E
Operating profit before change in working capital	13,081	14,167	15,540	17,676	21,464
Change in working capital	375	(6,550)	8,175	4,537	2,184
Others	82,114	88,886	87,436	88,947	90,544
Tax	(3,183)	(2,825)	(5,554)	(6,320)	(7,570)
<b>Operating cash flow</b>	<b>92,387</b>	<b>93,678</b>	<b>105,598</b>	<b>104,840</b>	<b>106,623</b>
CAPEX	(52,176)	(56,187)	(58,996)	(61,946)	(65,043)
Others	(9,003)	(2,866)	(2,478)	(2,312)	(2,112)
<b>Investing cash flow</b>	<b>(61,179)</b>	<b>(59,053)</b>	<b>(61,474)</b>	<b>(64,258)</b>	<b>(67,155)</b>
Dividend paid	(1,591)	(4,100)	(4,529)	(4,968)	(5,651)
Others	(32,467)	(25,665)	(7,712)	(4,862)	(3,202)
<b>Financing cash flow</b>	<b>(34,058)</b>	<b>(29,765)</b>	<b>(12,241)</b>	<b>(9,830)</b>	<b>(8,853)</b>
Net increase in cash & cash equivalents	(2,850)	4,860	31,883	30,752	30,615
Cash & cash equivalents at beginning of year	32,836	30,060	34,945	66,850	97,622
Effect of changes in foreign exchange rate	74	25	23	20	18
<b>Cash &amp; cash equivalents at end of year</b>	<b>30,060</b>	<b>34,945</b>	<b>66,850</b>	<b>97,622</b>	<b>128,256</b>

Source(s): Company, ABCI Securities estimates

### Financial Ratios:

As of Dec 31 (RMB mn)	2018A	2019A	2020E	2021E	2022E
EBITDA margin (%)	29.2%	32.5%	32.8%	33.0%	33.7%
Operating margin (%)	3.1%	3.9%	4.3%	4.6%	5.5%
Net profit margin (%)	3.5%	3.9%	4.2%	4.7%	5.7%
ROAA (%)	1.8%	2.1%	2.2%	2.3%	2.6%
ROAE (%)	3.3%	3.6%	3.9%	4.3%	5.0%
Net debt/ equity (%)	0.9%	8.3%	16.4%	11.9%	9.9%
Liabilities/ assets (%)	41.8%	43.0%	44.8%	46.6%	48.0%
<b>YoY Growth:</b>					
Revenue	5.8%	-0.1%	0.9%	1.6%	2.0%
EBITDA (%)	4.3%	11.1%	1.8%	2.3%	4.1%
Net profit (%)	457.8%	11.1%	9.7%	13.7%	21.4%

Source(s): Company, ABCI Securities estimates

## Disclosures

### Analyst Certification

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Rating	Definition
Buy	Stock return rate $\geq$ Market return rate (10%)
Hold	- Market return rate (-10%) $\leq$ Stock return rate < Market return rate (+10%)
Sell	Stock return < - Market return (-10%)

Notes: Stock return rate: expected percentage change of share price plus gross dividend yield over the next 12 months  
Market return rate: average market return rate since 2008 (HSI total return index 2008-19 CAGR at 10%)

Time horizon of share price target: 12-month

Stock rating, however, may vary from the stated framework due to factors including but not limited to: corporate governance, market capitalization, historical price volatility relative to corresponding benchmark index, average daily turnover of the stock relative to market capitalization of the stock, competitive advantages in corresponding industry, etc.

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