STARHUB LIMITED

LUMIERE CAPITAL

Valuation Date: 4TH February 2018
Stock Exchange: SGX
Ticker: CC3

Recommendation: SELL
Current Price: SGD $2.86
Target Price: SGD $2.37

Downside: 17.1%
Sector: Telecommunications

THE FAULT IN OUR STAR?

(Initiation Report)

SELL

SUMMARY: StarHub Ltd is a Singapore-based info-communications company offering information, communications and entertainment services for consumer and corporate markets.

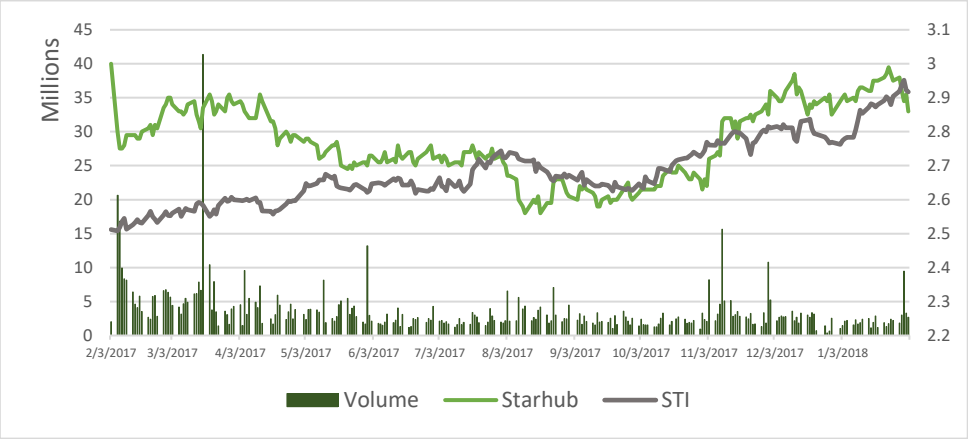


Figure 1

Trading Data	
Closing Price (Feb 4th, 2018)	$ 2.86
Outstanding Shares (mn)	1731.9
Market Capitalisation (bn)	4.84
Enterprise Value (bn)	5.47
Trailing P/E	16.87 x

Sources: Reuters, Team Analysis

Figure 2

Valuation Date: 4th Feb 2018	
Discounted Cash Flow	
1-Year Target Price	S$2.37
Current Share Price	S$2.86
Downside	17.1%

Source: Team Analysis

Figure 3

Key Financials

Year to 31 Dec (S$m)	2017(F)	2018F	2019F	2020F
Revenue	2,330.68	2,267.04	2,214.99	2,173.54
EBITDA	668.83	641.50	617.91	597.66
Operating profit	420.66	382.92	372.92	367.03
Net profit	335.44	301.08	291.31	287.48
EPS (S$ cent)	19.4	17.4	16.8	16.6
PE (x)	14.8	16.4	17.0	17.2
EV/EBITDA (x)	8.2	9.1	9.4	9.7
Dividend yield (%)	7.0	6.3	5.6	4.9
Consensus net profit	276	250	235	226

Source: Team Analysis, Starhub AR & Bloomberg

HIGHLIGHTS: Initiating a coverage with a SELL recommendation through our DCF valuation (Perpetuity Growth Model), we arrived at a target price of S$2.37, indicating a 17.1% downside. We calculated StarHub's implied equity value to be at S$4,105m, using a 3-year projection, a WACC of 6.3% and terminal growth rate of 0.6%. Our target price corresponds to an implied P/E of 12.9x which is derived from an industry median. We strongly believe that there will be no additional headroom for further growth in their main business segments thus, outweighing the probable upside factors.

CORE BUSINESS UNDER FIRE

Promising an eventual takeover of 5-6 % market share, we can expect TPG's entry into the Singaporean market to be no less than aggressive. StarHub will have to adapt to the threat by offering more attractive and affordable plans. We conservatively projected ARPU to fall for Mobile segment at about 4% and kept ARPU for Pay TV segment relatively flat. Thus, affecting overall revenue projection to decline about 2.3% CAGR from prior years. Also, StarHub's strategic shift towards Enterprise fixed Services (EFS) will not be significant enough to cover the loss in revenue.

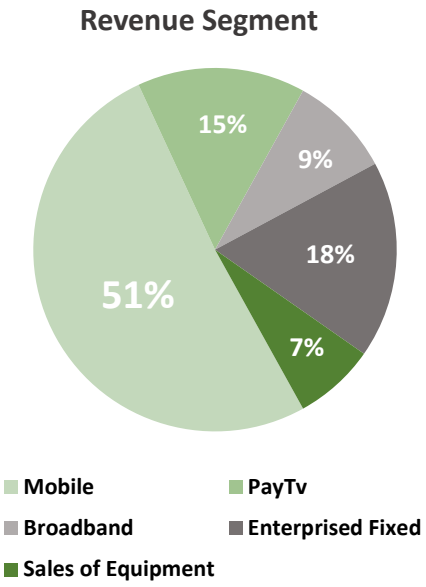
UNSUSTAINABLE DIVIDENDS

StarHub is unlikely to maintain its high dividends given the large capital expenditure commitments for spectrums in 2018, and a slumping NPAT falling at 5% CAGR. We forecast dividend pay-out ratio to fall to 80%, deriving with DPS falling by 14% from 2017 to 2020F. Future dividend cuts will dampen investor's confidence, potentially leading to a sell-off due to lack of growth opportunities

NO ROOM FOR GROWTH

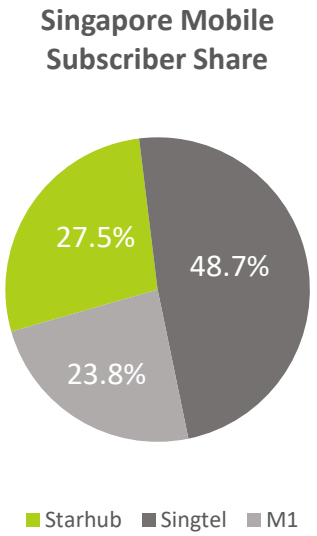
StarHub boasts a steady and diversified domestic business model however its revenue concentration in the Singaporean Market leaves its earning capabilities susceptible to factors pertaining to Singapore's macroeconomic landscape and vulnerable to entrance of new competitors. Given their leveraged balance sheet and lacklustre earnings as of late, StarHub is handicapped in their ability to diversify their revenue generation. Headroom for any further gearing of its balance sheet is also reduced due to high spectrum costs.

Figure 4



Source: Company Data

Figure 5



Source: Company Data

Figure 6

List of Executive Officers	
Tan Tong Hai	CEO
Dennis Chia	CFO
Dr Chong Yoke Sin	CEBG
Howie Lau	CMO
Catherine Chia	VP HR
Jeannie Ong Chief	Strategic Partnership
Veronica Lai	Company Secretary
Tim Goodchild	SVP, Strategic Affairs
Chong Siew Loong	CTO
Kee Yaw Yee	CIO

Source: singstat.gov.sg

BUSINESS DESCRIPTION

StarHub Ltd is a Singapore-based info-communications company. It has 4 main branches of operations: Mobile, PayTV, Broadband and Enterprise Fixed. The Company engaged in operation and provision of telecommunications services and other businesses relating to the info-communications industry. The Company offers a range of information, communications and entertainment services for both consumer and corporate markets. It delivers Mobile, Pay television, Broadband, Fixed network services and equipment sales on an operationally integrated network. It operates a mobile network that provides fourth-generation (4G), third-generation (3G) and second-generation (2G) services and plans to launch their fifth-generation (5G) services by 2020. It also manages an island wide Hybrid Fibre Coaxial (HFC) network that delivers television services and cable broadband services. The Company offers a range of home and business multimedia services and content. As of 3Q2017, StarHub is the second largest of the 4 telecom operators in Singapore.

PRODUCTS AND SERVICES

MOBILE Contract plans tied with mobile phones and tablets where customers typically pay down payments on phones/tablets and pay the remaining sum through monthly contracts that includes different combinations of services/utility such as data plans, call time and short message services.

PAY TV Providing exclusive media content via cable/fibre TV to customers, offering a plethora of television programmes that cater to the tastes of the masses. Also, with StarHub Go being introduced in 2015, StarHub users can now stream their favourite TV programmes from their preferred mobile devices on the go. Payments are in the form of monthly instalments and prices vary with different bundles providing different content.

BROADBAND Providing quality and reliable internet access to homes and offices. Payments are typically by monthly instalments that varies with the different quality of internet access provided.

ENTERPRISE FIXED Providing wide range of business solutions, from fixed data connectivity, mobile and telephony to security and mobility solutions, data centres and data analytics supports both small businesses and large enterprises.

GEOGRAPHIC LOCATION

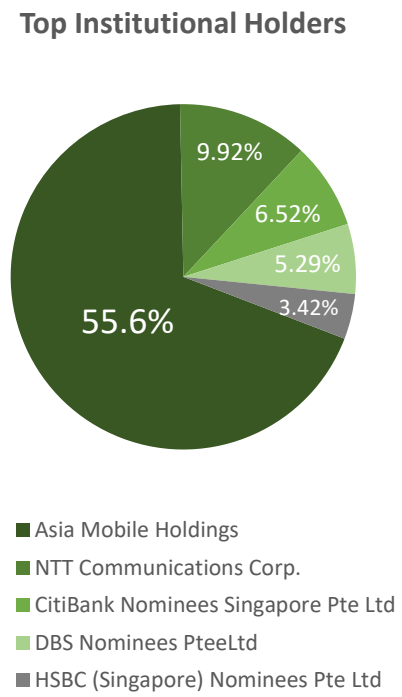
Singapore is a small densely populated island nation is the pioneer and continues to be one of the few countries in the world in which broadband internet access is readily available anywhere in the country. Singapore's smartphone penetration rate is also amongst the highest in the world which in turn naturally leads to an increased demand for mobile plans and services. Given the circumstances of the Singaporean broadband/smartphone landscape, StarHub is in an ideal position to offer innovative and quality solutions to meet the telecommunication needs of consumers.

Figure 7

Board of Directors	
Steven Terrell Clontz	Rachel Eng Yaag Ngee
Tan Tong Hai	Teo Ek Tor
Paul Ma Kah Woh	Stephen Geoffrey Miller
Nihal Vijaya CBE	Liu Chee Ming
Nasser Marafih	Michelle Lee Guthrie
Naoki Wakai	Lim Ming Seong

Source: Company Data

Figure 8



Source: Company Data

COMPANY STRATEGIES

KEEPING UP WITH NEW TECHNOLOGY To stay relevant and competitive in the industry, StarHub must adapt to the ever-changing landscape of telecommunications where possessing the latest technology is paramount. StarHub constantly aims to provide a wider range of services with improved economics and customer engagement, enhancing their competitive edge.

QUALITY SERVICE AND LOYALTY Consistency coupled with reliability in their services allows StarHub to gain the trust and support of its many customers, ensuring their continual usage of services provided. This ensures their competitiveness in network performance and also offers good value for its business, allowing them to be more efficient. A strong, singular focus on the customers' needs is a source of competitive differentiation and gives rise to a higher customer retention rate, longer tenure and higher total value.

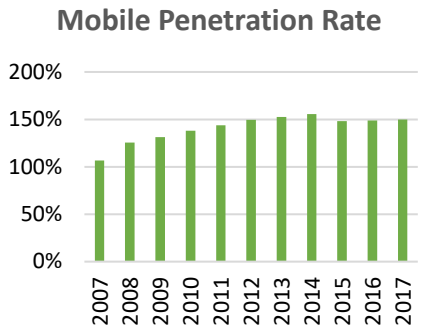
GO-TO ENTERTAINMENT HUB StarHub aims to be a go-to platform for entertainment introducing their Hubbing Strategy where multi-services packs like HomeHubGo and SurfHub are offered to customers at a discounted, value-for-money option. This gives StarHub a competitive edge and increases customer loyalty to the StarHub brand.

CORPORATE GOVERNANCE

SHAREHOLDING STRUCTURE StarHub consists of ordinary shares and treasury shares. Each ordinary share is entitled to one vote. As of 30 September 2017, the share capital of the Company was at S$299.7 million comprising 1,729,063,932 issued ordinary shares. The treasury share balance as of 30 September 2017 totalled S$8.2 million comprising 2,587,511 ordinary shares or 0.1% of issued share capital excluding treasury shares. All shareholders are entitled to attend and vote at general meetings and are afforded the opportunity to participate effectively in the general meetings. Shareholders are allowed to appoint up to two proxies to attend, speak and vote in their place at general meetings.

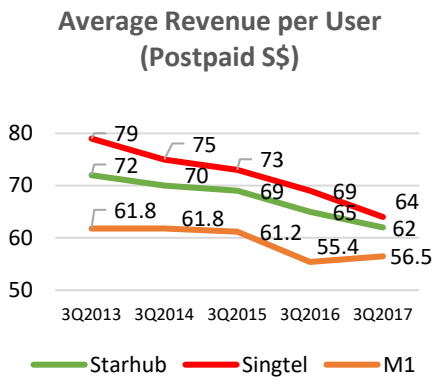
BOARD AND MANAGEMENT The Board consists of 12 Directors who are business leaders and professionals of high calibre and integrity. They possess a broad range of core competencies and experience in banking, accounting and finance, legal, regulatory, technical, business and industry knowledge, management and strategic planning experience, and customer-based experience and knowledge. The Board consists of 5 committees such as the Audit Committee, Strategy Committee, Nominating Committee, Executive Resource and Compensation Committee and the Risk Committee. Each Board Committee is required to operate and make decisions on matters within its terms of reference and applicable limits of authority. All Directors, Management and employees are notified by email prior to the start of each trading blackout period and the restrictions are only lifted after the announcement of the respective financial results. The policy also discourages trading on short-term considerations and reminds Directors, Management and employees of their obligations under insider trading laws.

Figure 9



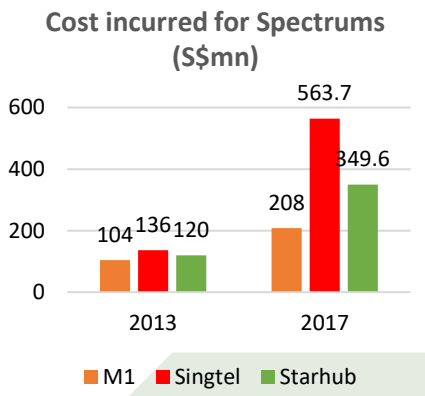
Source: Singstat.gov.sg

Figure 10



Source: StraitsTimes

Figure 11



Source: Team Analysis

INDUSTRY OVERVIEW & COMPETITIVE POSITIONING

LOW POTENTIAL FOR GROWTH IN MOBILE AND BROADBAND

Singapore has seen high smart phone penetration growth rate in the past due to the smart nation initiative. However, this has resulted in a highly saturated market with mobile penetration rate at a staggering 150.80% as at June 2017. The number of mobile subscription is 1.5 times the population of Singapore indicating that each Singaporean has more than one mobile contract signed. Furthermore, Singapore's population growth has been declining with growth rates falling from 2.4% in 2012 to 1.3% in 2017. Therefore, there is lacklustre growth for incumbent in the local scene, unless they engage in aggressive competition and vie for each other's existing market share.

PRICE WAR FRENZY

The pricing for mobile and broadband services in Singapore is highly competitive, where a cut in prices by one firm will be immediately matched by their competitors. This is evident by the similar pricing of services by the current three incumbents (Appendix 3) which only allows for minor price discrepancies due to product differentiation. Therefore, to garner market share, local incumbents compete in price wars. During 2016, in response to new competition from Circles.Life, Singtel slashed more than half the price for their 12GB plan from S$239.90 a month to only S$108.80. Competitors M1 and StarHub immediately responded with similar discounts with M1 offering S$107.90 a month for a 13GB plan.

Price wars are extremely detrimental to the incumbents as it reduces their ARPU. All three incumbents have been facing downward trends (Fig. 10) in their ARPU with StarHub's ARPU falling by 3.68% from 2013 to 2017. Dilution of ARPU is likely to continue, as M1 introduces MySIMe plan during Oct 2017, which offers higher data allowances at more affordable prices. Furthermore, the introduction of MVNOs such as Circle.Life, and the entrant of TPG will further aggravate the price war.

SPECTRUM CONTRAINTS GROWTH OPPORTUNITY

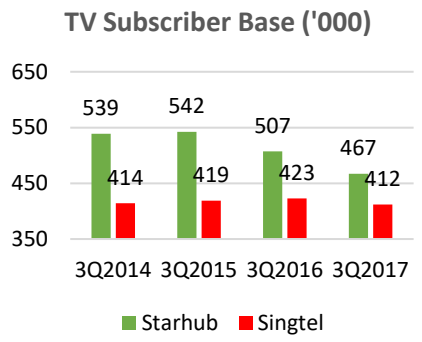
In 2017, IMDA received a total request for 225 MHz of spectrum which was largely oversubscribed by 50. The aggressive bidding was fuelled by the overwhelming demand for high-speed mobile services. Thus, incumbents had to pay exorbitant prices with the 700 MHz spectrum going up to S$90m/lot, and the 2.5GHz spectrum at $11.9m/lot, which are significantly above their reserve prices of S$20m/lot, and S$3m/lot. M1 who lacked the luxury of a strong cashflow failed to claim any 2.5GHz spectrum. We can expect the spectrum prices to remain high as TPG's entry into the industry will likely drive up demand for spectrums.

5G A SILVER LINING

Starhub and Singtel has begun trails on their 5G networks, with plans to begin operations in 2020. 5G is a key component in emerging technologies such as Internet of Things (IoT) and is essential in the new digital economy. Thus, incumbents will be able to tap into a whole new consumer base such as autonomous vehicles and robotics, creating new demand drivers and ultimately fuel growth in a stagnating industry. The increased in demand will allow opportunities for ARPU to grow, as well as an increase in users.

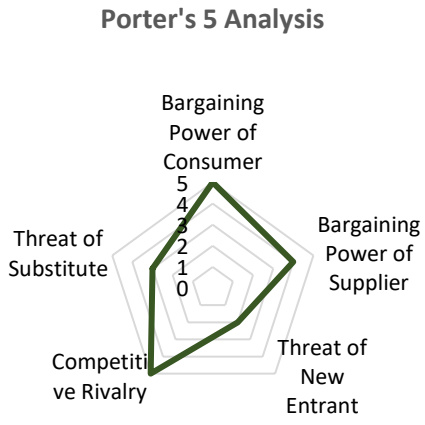
We expect the trend to continue as Netflix has committed S$8.5b in 2017 to produce quality content. However, partnership with other OTT services could potentially dampen the fall.

Figure 12



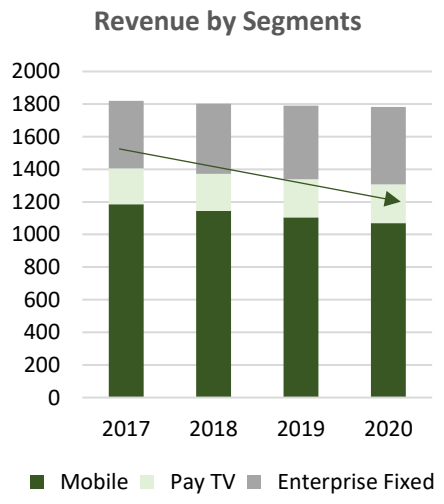
Source: Annual Report

Figure 13



Source: Team Analysis

Figure 14



Source: Team Analysis

PayTV OTT SERVICES PAVING THE WAY

OTT (over-the-top) services such as Netflix and Hulu offer greater convenience, allowing subscribers to view their content on multiple platform including mobile phones, tablets and smart televisions. Furthermore, subscriptions can be as low as S$9.90 a month as compared to cable tv which on average cost $26.75. Though Singtel and Starhub have responded with similar OTT services, Cast and Starhub Go, they are unable to compete with Netflix due to the lack of hit TV shows and quality content. This cord-cutting revolution is eating away at the market share of local incumbents with subscriber base for Starhub falling (Fig. 12) by 13.3% from 2014 to 2017.

COMPETITIVE POSITIONING

Starhub has a market share 26%, with main competitors M1 and Singtel who have 24% and 50% market share. The newer entrants Circles.Life and MyRepublic currently only have a small market share. However, competition remains strong with ongoing price wars caused by low switching cost and lack of product differentiation for consumers. Starhub also faces supply side constraints due to high reliance on handsets for contract sales. The threat of new entries into the industry have become higher due to globalization, allowing for easier entry for larger foreign competitors (Appendix 2)

INVESTMENT THESIS

CORE BUSINESS UNDER FIRE

We can expect TPG's entry to be aggressive, offering more attractive and affordable plans. This is in line with their ambitious promise to mop up 5-6% market share over a brief period. Starhub will have to respond to the threat, hence we forecast ARPU for mobile to fall by 4% CAGR respectively. In our base case, we assume Starhub manages to defend their market share, with user base to plateau. This forecast is comparable to the entry of Circles.Life in 2016 where their defence was successful. However, overall revenues for mobile is still expected to slide at 3.37% CAGR from 2017 to 2021F.

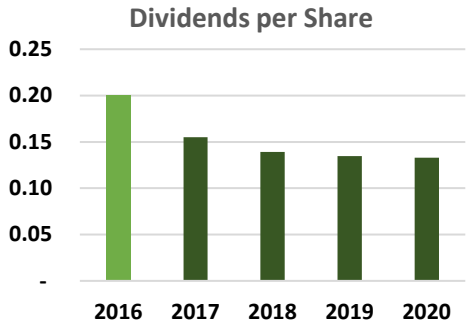
In our bear case, we expect further competitive pressure from newer entrants MyRepublic and Circles.Life, as well as TPG's successful entry into the market, securing 5-6% of market share by 2019. Hence, we forecast user base to fall by 4%, with revenue to fall by 11.5% CAGR.

Outlook for PayTV remains gloomy with subscribers switching over to lower cost OTT services. We forecast user base to fall by 8.5%, ultimately hurting PayTV revenues by 7.88% CAGR.

Starhub's strategic shift towards EFS (enterprise fixed services), with the acquisition of D'Crypt and ASTL. Revenues for corporate data and internet services is expected to increase, hence we forecast revenue for EFS to grow at 4.66% CAGR. However, Starhub's overall revenue will still be in a downward trend at 2.3% CAGR, as revenue segment for EFS remains a small component at 17.8% as at 2017.

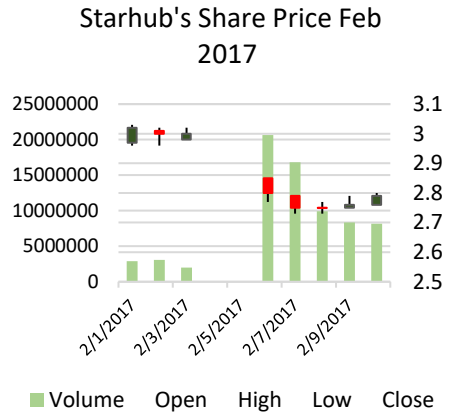
In our bull case, despite increasing revenue for EFS by 15.12%, we only derive at target price of S$2.78, which only justifies a hold call.

Figure 15



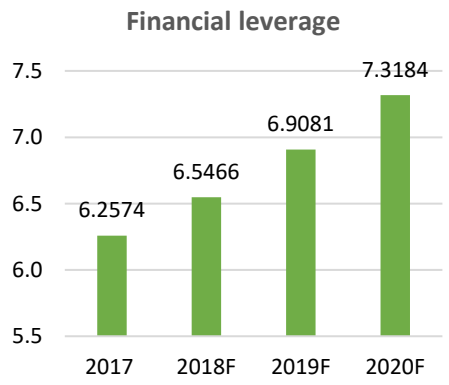
Source: Company Data

Figure 16



Source: Yahoo! Finance

Figure 17



Source: Team Analysis

Figure 18

Assumptions:	
Risk-Free Rate	2.4%
WACC	6.3%
Market Risk Premium	6.7%
DCF Target Price	**S$2.37**

Source: Team Analysis

UNSUSTAINABLE DIVIDENDS

In 2016, StarHub paid dividends at S$0.2 per share, with a dividend pay-out ratio of 102%. The total dividends paid of S$346.2m was more than profit earned of S$341.4m in 2016, indicating that StarHub had to rely on financing to maintain its high dividends. StarHub is unlikely to maintain its high pay-out given the large capital expenditure for spectrums in 2018, and a slumping NPAT falling at 5%CAGR. We forecast dividend pay-out ratio to fall to 80%, deriving with DPS of S$0.155 in 2017, S$0.139 in 2018, S$0.135 in 2019 and S$0.133 in 2020 respectively.

A cut in dividend on one hand, whilst the lack of opportunities for growth on the other hand, will indicate a gloomy prospect on future cash inflow for investors. This could shatter shareholder's confidence, potentially leading to a sell off. On 4th Feb 2017, StarHub announced a dividend cut by 20%, this immediately resulted in Share Price falling by 6.67 the next working day (Fig. 16), indicating a sell-off.

ALL EGGS IN ONE BASKET, NO ROOM FOR GROWTH

As of 17Q3 StarHub's revenue generation is solely from Singapore and management has not disclosed any plans to expand operations overseas and because of this, they are left susceptible to factors affecting Singapore's economy as a whole. Their exposure to risk is further exacerbated by their significantly leveraged balance sheet and downward trending net income which sequentially handicaps their ability to acquire and diversify their revenue generation.

StarHub will have to commit large cashflows for CAPEX in 2018 due to the spectrum upgrades, we forecast an increase of S$317.7m in CAPEX in 2018. The spectrum will be financed by debt, thus we forecast financial leverage to increase by 16.96% from 2017 to 2020F. Starhub is expected to have a decreasing gearing headroom, undermining their ability to expand. Future spectrum bids are expected to be costly as well due to high demand. Furthermore, the inability to pass on the high capex to consumers due to competitive pricing will dampen revenue growths.

VALUATION

We arrive at a one-year target price of S$2.37, driven by our DCF Model. We used a DCF model due to its flexible nature of being able to input various assumptions for Capital Expenditures, as well as the growth rates for different business segments, allowing us to construct a more thorough analysis.

DISCOUNTED CASH FLOW

This model was chosen due to the relatively stable earnings and cash flow that StarHub has been generating over the years. StarHub's revenue consists of various business segments, namely, Mobile, Broadband, PayTV, Fixed Enterprise Services and Sale of Equipment. Each of the business segments are forecasted based on the Company's historical performance, industry, economic outlook, and StarHub's competitive positioning. This method consists of a 3-year forecast up to the year 2020. Based on our DCF analysis, the estimated one-year target price is S$2.37, a -17.1% downside.

COST OF EQUITY

The cost of equity was determined through the Capital Asset Pricing Model (CAPM). The risk-free rate was based off the 10-year Singapore Government average bond rate of 2.40%, estimated by taking the average of several bond yield across recent years. StarHub's raw beta of 0.41 was derived by using ten-year weekly prices against the STI. We constructed a peer analysis to derive the average optimum WACC of 6.3% based on the optimum capital structure of StarHub's peers.

Figure 19: Peer-Comparable (P/E)

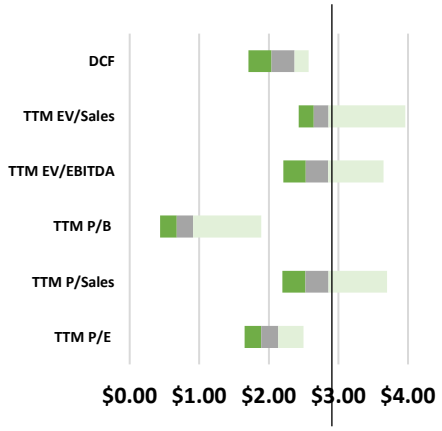
	P/E (x)
Starhub Ltd	17.2x
Singtel Ltd	9.9x
M1 Ltd	12.9x
Median	12.9x

Source: Team Estimates

Figure 20: P/E Band

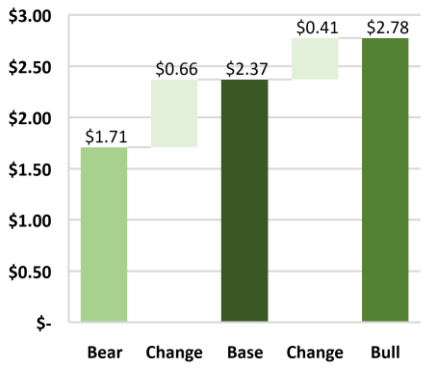
Source: Team Estimates/Bloomberg

Figure 21: Football Field



Source: Team Estimates

Figure 22: Scenario Analysis



Source: Team Estimates

TERMINAL GROWTH RATE

The terminal growth rate was projected to be 0.6% derived from the average inflation rate of Singapore in 2017. Rate of Inflation was chosen as a proxy for the terminal growth rate due to the competitive nature of the telecommunications industry and underwhelming performance of StarHub's business segments.

SECONDARY VALUATION

PE multiple valuation was our secondary valuation approached (Fig. 19), deriving to an implied equity value of S$3,855m. We factored an industry median of 12.9x and a 2018F earnings of S$299.53m, arriving to a fair value of S$2.23 indicating a 22% downside, which is in line with our primary 3 years DCF valuation approached.

OVERVALUED SHARES

From the year 2017, the group's share price has declined by about 4% to S$2.86, mainly due to underwhelming business results (its overall profit fell by 18.1% in the first 9 months of 2017) and fears of heightened competition in the future from incoming new entrant, Australia's TPG Telecom. We strongly believe that the future downside factors would overweigh the negligible upside factors, thus driving the stock price further downwards.

Comparisons using a PE Band Chart (Fig. 20), we observed that Starhub is currently trading at a higher multiple of 17.2x as compared to a -1SD long-term average of PE of 15.4x, indicating that the group's current share price is overvalued and has no room for anymore upwards price adjustments.

PUBLIC COMPARABLE

By amalgamating the various implied share price in a football field chart, we can observe that the current market price of S$2.86 lies above 6 out of 6 of the parameters, reflecting that the current share price is overvalued. As such, we are confident that a downside of -17.1% is well-justified. (Fig. 21)

SENSITIVITY ANALYSIS

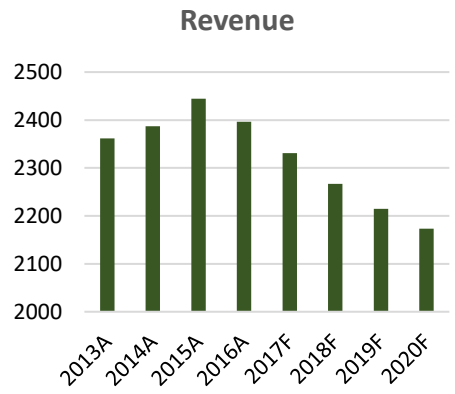
We performed a sensitivity analysis on some of the variables and assumptions of our model, testing the Post-Paid ARPU and subscribers' growth rates, along with WACC and Terminal Growth Rate. ARPU will have to either fall at a slower rate of -1% or subscribers must grow at a rate of 6% for us to conclude at a HOLD situation. Likewise, a reduction of WACC by 0.5% or an increase of Terminal Growth Rate to 1% will change our recommendation.

SCENARIO ANALYSIS

BULL CASE: We consider the bullish potential that StarHub managed to restructure to adapt and focus on its Enterprise Fixed Services business segment, increasing its growth potential in that segment by significant amount. The reforms are then expected to increase the target price of S$2.73. However, even in the bullish case, the target price still represents a downside of 4.6% over its current price.

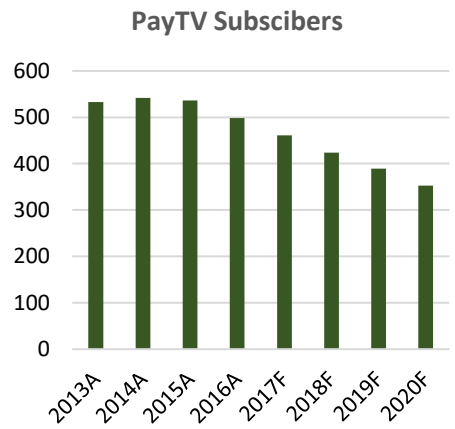
BEAR CASE: The bearish scenario was assumed to be an extremely successful entrance by TPG into Singapore, allowing TPG to gained significant market share, potentially eroding the total number of subscribers and ARPU in StarHub's mobile and broadband services. This development will negatively impact StarHub's largest business stream, causing a drop in target price to S$1.66, a downside of 41.9%.

Figure 23



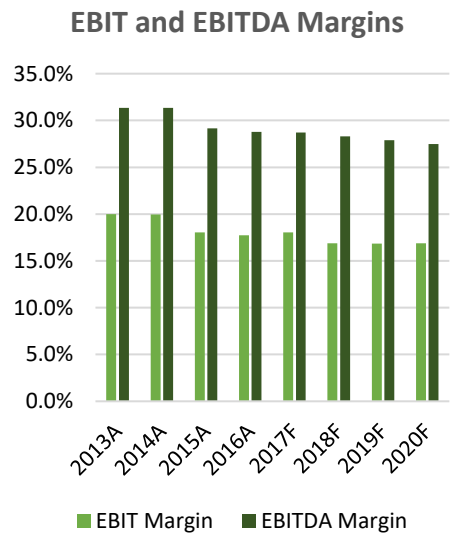
Source: Company Data

Figure 24



Source: Team Estimates

Figure 25



Source: Global-Rates

FINANCIAL ANALYSIS

REVENUE GROWTH

Despite StarHub's 3% CAGR in its Enterprise Fixed business segment, overall revenue has been gradually declining in the historical years, mainly attributed by a -1.1% CAGR in its mobile segment, StarHub's largest revenue stream. Post-Paid and Pre-Paid ARPU has been facing a -3.68% CAGR and -5.43% CAGR decline in historical years respectively, showing signs of distress in its mobile segment. We foresee a further erosion of Post and Pre-Paid ARPU of -4% and -5.43% CAGR in our forecasted years due to continued price wars and the possibility of new entrants affecting its core business segments.

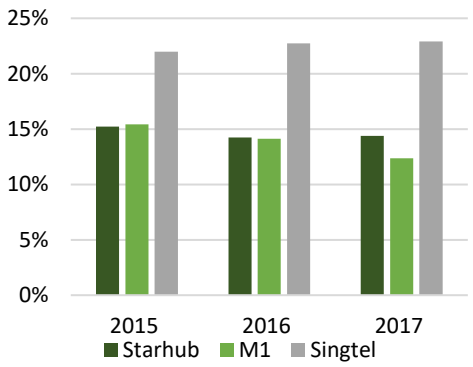
PayTV business segment has shown an unhealthy demand, with number of users falling by 3.58% CAGR in historical years due to the disruptions in the segment (i.e. alternative platforms). We expect a further plunge of 8.5% in number of PayTV users in our forecasted years due to the high competition in this segment. With the above considerations, PayTV revenue are expected to decline by 7.88% CAGR in our forecasted years.

MARGINS StarHub's EBIT and EBITDA margins has been deteriorating in the past five years, falling from 20% and 31.4% in 2013 to 18% and 28.7% in 2017 respectively. This is due to an overall decline in revenue, coupled with increasing operating expenses and depreciation/amortization. This shows a worrying business as additional expenses are not justified by a growth in revenue. A further decay of EBITDA margin is expected for the following years backed by depressed levels of revenue. However, EBIT margins are forecasted to show a slight reversal due to StarHub's decision to cut capital expenditure, resulting in lowered depreciation and amortization in the upcoming years.

CAPITAL EXPENDITURE CAPEX is primarily focused on the purchase network equipment and spectrum licenses due to an advancement in technology. During the last five years, CAPEX % Revenue has been relatively flat, hovering about 11% on average. However, for our forecasted years, we took into consideration StarHub's strategic tie-up with M1, lowering its CAPEX levels due to a reduced need of reinvestment in infrastructure development, with the exception of a substantial surge of CAPEX in 2018 due to StarHub's plan to acquire the licensing for its telecommunication spectrum.

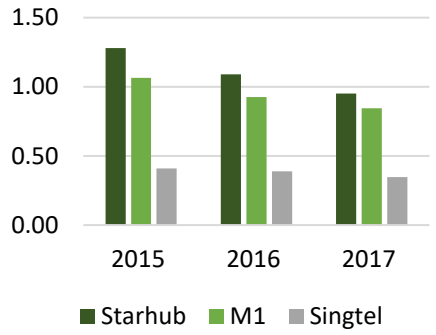
ALTMAN Z-SCORE is performed to determine StarHub's financial health and its likelihood of bankruptcy. With a relatively high score of >2.5, StarHub has a low possibility of liquidation. However, it shows a red flag as StarHub's Z-Score has been weakening, from 3.74 in 2013, to 2.64 in 2017. This might pose a long-term problem due to StarHub's business model as a highly leveraged firm.

Figure 26: Net Profit Margin



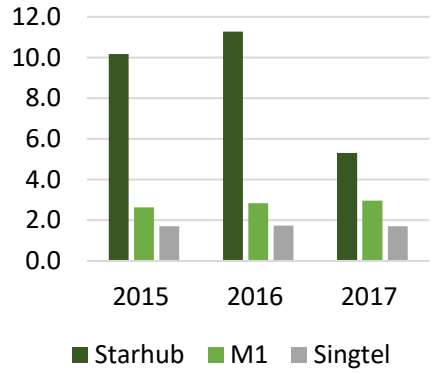
Source: Company Data and Team Analysis

Figure 27: Asset Turnover



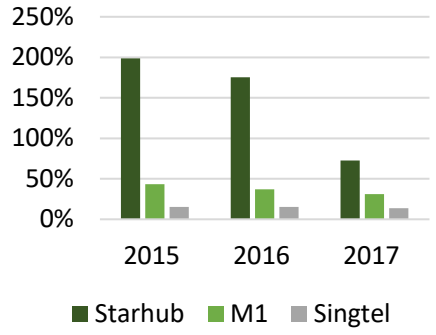
Source: Team Analysis

Figure 28: Financial Leverage



Source: Team Analysis

Figure 29: Return on Equity



Source: Team Analysis

DUPONT ANALYSIS – PEER COMPARABLE

	Starhub			M1			Singtel		
	2015	2016	2017	2015	2016	2017	2015	2016	2017
ROE	198%	175%	73%	43%	37%	31%	15%	15%	14%
Net Profit Margin	15.2%	14.2%	14.4%	15.4%	14.1%	12.4%	22.0%	22.7%	22.9%
Total Asset Turnover	1.28	1.09	0.95	1.07	0.93	0.84	0.41	0.39	0.35
Financial leverage	10.18	11.27	5.30	2.63	2.84	2.96	1.70	1.74	1.71

NET PROFIT MARGIN

A relatively flat Net Profit Margin (NPM) from FY15 to FY17F (Fig. 26) indicated that the group is generating a relatively stable net profit from a dollar of its revenue. However, despite a slight fall in overall revenue from prior years, mainly due to the decreased mobile revenue, net profit is projected to be 1% higher at S$354.6 in FY17F compared to S$341.4m in FY16. This is due to increasing finance expenses. Furthermore, we projected revenue to fall further due to our prudential view point on losing additional Mobile's as well as Pay TV's subscribers, we thus expect future margins to decrease.

AESSET TURNOVER

SingTel has the biggest asset base out of the three, and it might seem to be an arduous barrier for its competitors to overcome. However, fig.27 illustrates that it fairs poorly in terms of utilizing its asset to generate its revenue, thus consequently allows both M1 and Starhub to use that to their advantage with regards to generating higher returns for shareholders.

Starhub's astonishing ROE(Fig.29) is mainly due to having an excessively high Financial Leverage ratio. Its substantial distinction in the ratio as compared to competitors, M1 and Singtel, illustrates that the group's finance a majority of its assets by taking on a hefty amount of debt, in addition to having a vast amount of trade payable debts.

RETURN ON EQUITY

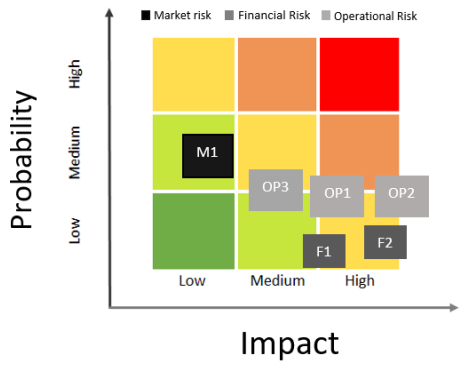
It is noticeable that ROE has been declining mainly due to an issuance of perpetual capital security on 2017 amounting to S$199.6m, thus increasing the group's equity value for about a significant 137% from 2016. It likewise affected the group's excessively high financial leverage on 2017 with a plunged of 6ppts from prior year.

PIOTROSKI F-SCORE of 5 does not show a strong financial position with StarHub's status as a blue-chip stock. This implies lowered margins and higher leveraging YoY, a clear signal of a distress business.

ROA has been diminishing in the historical years, from 20.2% in 2013 to 13.7% in 2017 due to a hit in profits, and a growing asset base. This implies a lack of efficiency in generating revenues and a telltale sign of implausible financial and operational performance.

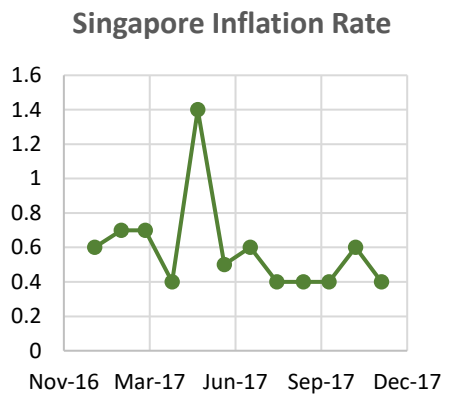
ROCE has also been on the downside, sliding from 38.9% in 2013 to 25.3% in 2016 due to receding levels of profits with increased funding on assets. This decline is in line with ROA as a majority of asset held by StarHub are non-profitable and are acquired by StarHub to stay relevant in this competitive telecommunication industry. Therefore, ROA and ROCE are also expected to continue its downtrend in our forecasted years.

Figure 30: Risk Matrix



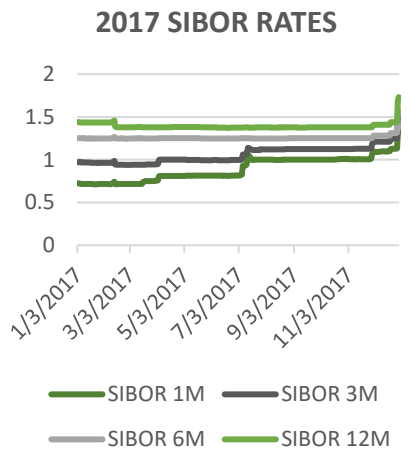
Source: Team Analysis

Figure 31



Source: TradingEconomics.com

Figure 27:



Souce: absCo.com

INVESTMENT RISKS

MARKET RISK

M1: MACROENOMIC FACTORS (LOW IMPACT|MEDIUM PROBABILITY):

These risks include inflation and economic volatility. However, such uncertainties will affect every player in the market. Historically, through strong management and financial position StarHub will be very likely to weather the inflation risks through transferring higher costs to both suppliers and customers.

FINANCIAL RISK

F1: INTEREST RATES (HIGH IMPACT|LOW PROBABILITY):

In tandem with the recent interest rate hikes from the Federal Reserve, SIBOR and LIBOR have been steadily increasing. This could result in an increase in cost of borrowing to finance operations. Since StarHub's liabilities consists a significant amount of interest bearing liabilities, StarHub will have to bear an increase in interest expense. However, likelihood of default of interest expense is unlikely.

F2: LIQUIDITY RISK (HIGH IMPACT|LOW PROBABILITY):

StarHub's current and quick ratio has been varying from 2013 and 2016, with the ratios at 2016 being the healthiest in the recent years. However, there is still a solvency risk. They lack the capability to fully convert their current asset to pay off their current liabilities within a year or short notice should any major shocks or disruptions happen to their flow of business. Conducting business with low liquidity is a possible factor that may lead them to be called upon to meet liabilities in the future. However, the Group has the ability to borrow in short term to meet short-term requirements.

BUSINESS AND OPERATIONAL RISK

OP1: CYBER SECURITY RISK (HIGH IMPACT|LOW PROBABILITY):

StarHub's business as an info-communications service provider is dependent on the security, availability and resilience of the underlying network infrastructure and information systems it operates on. StarHub has a strong track record in this aspect which shows the resilience of their network and hence we deduce that it is unlikely for it to fall prey to such attacks. If such attacks do succeed however, it could adversely affect StarHub's operations bearing significant negative consequences.

OP2: COMPETITORS IN THE MARKET (HIGH IMPACT|LOW PROBABILITY):

Telecommunications is an expensive business in view of the large initial costs to set up telecommunications networks throughout the island. The high initial costs and low subsequent costs of adding additional subscribers allows existing providers to capitalize on economies of scales to keep out new entrants. Apart from the need to set up infrastructure, it also incurs extensive updating costs to ensure security and to avoid obsolescence which most small to medium companies lack the capitalization and expertise to keep up with the industrial requirements. Moreover, licenses to operate a telecommunications business are not easily approved by the IDA of Singapore, hence the threat of new entrants to telco companies in Singapore is low to negligible. Given the recent entrance of TPG, the first major entrant in over 15 years, another major competitor will not be expected anytime soon.

OP3: SUPPLY CHAIN RISK (MEDIUM IMPACT|MEDIUM PROBABILITY):

StarHub works with partners for various aspects of its info-communications business and forms strategic partnerships with key vendors and other complementary service providers to expand its footprint and serve new market segments. Should there being falling out of strategic partnerships, StarHub will lose out in competitiveness hence impacting operations However StarHub's strong senior management team displays a strong track record in this aspect and hence the likelihood of falling out is low.