

Equity
Market Analysis / Spain
07 October 2016 (09:50 CET)

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Spanish Telecoms

Telefónica (Outperform) Target price: EUR13.00. Closing price as of 06/10/2016: EUR8.89
Euskaltel (Outperform) Target price: EUR12.50. Closing price as of 06/10/2016: EUR8.71

Spanish Telcos: a new bad boy is in town

Yesterday, the regulatory authorities cleared the acquisition of Yoigo by MasMovil, paving the way for the fourth Spanish Mobile operator with 4.2mn subscribers (10.5% share), EUR1.1bn of revenues and EUR108mn of EBITDA. The company emerges as the main threat to the current disciplined pricing environment in Spain and is undoubtedly a player to closely track going forward. However, in our view, the room for aggressive price discounts has now narrowed and price sensitivity has diminished significantly among consumers. This, together with the company's limited financial capacity lead us to believe that nothing is really going to change in Spain's more rational competitive environment.

- **The fourth Spanish player is now a reality.** Spanish regulatory authorities have finally given green light to the acquisition of Yoigo by MásMovil, leading to the creation of Spain's fourth national telecom operator. In the last year Más Movil has announced the acquisition of; i) Yoigo for a total consideration of EUR612mn (7.4x EV/EBITDA, 5.3x adjusted for synergies), and ii) Pepehone (MVNO operator) for a total of EUR158mn. The total investment of EUR770mn has been partially financed through debt and a EUR160mn capital increase (subscribed by Providence) and a EUR165mn issue of convertible bonds.
- **But what exactly is MasMóvil?** The incorporation of Yoigo and Pepehone has created a company with EUR1.1bn of revenue and EUR108mn of EBITDA, with 4.2mn residential mobile customers, 10.5% market share. The company will now run Yoigo's mobile network, which does not have full coverage in Spain but is completed through a roaming agreement with Telefónica (which will be transferred to Orange in 2017). Additionally, as result of the conditions imposed in the Orange – Jazztel transaction, MasMovil also accounts for 730k homes passed with FTTH (5% coverage) and full access to Orange's ADSL network at a pure variable cost.

After the EUR160mn capital increase (subscribed by Providence) we estimate the company would have a net debt position of c.EUR645mn (6.0x ND/EBITDA), which would be reduced to EUR480mn (4.4x ND/EBITDA) if adjusted for the EUR165mn of convertible bonds.

- **Opportunities and threats.** As a challenger, MasMovil benefits from a very low cost base and a very favourable access to Orange's ADSL coverage, which should enable it to exploit the hard discount business model (cheapest with on par quality). Additionally the company has a clear opportunity to expand its presence in the Fixed-line segment leveraging on its 730k homes passed (5% coverage), which we believe should be progressively expanded to 2.3mn homes (15% coverage in the next 2-3 years). However, we also believe challenges it must overcome to achieve this are significant, and the path to success will not be free of risks;
 - On the one hand, after the sharp deflation in the Spanish Telecom sector over the last decade, the margin to offer attractive discounts has narrowed significantly, which in our view, will be further aggravated by the palpable reduction in price sensitivity among Spanish consumers.
 - FTTH coverage is limited (5% at present), and even if the economics of accessing Orange's ADSL network are very attractive, we believe migration to FTTH is accelerating and there is no going back. ADSL is now residual and will become non-existent some years down the road.
 - Finally, financial constraints will force MasMovil to carefully allocate cash-flow between capex and SAC, and will limit its commercial firepower.
- **All in all, we do not rule out the possibility that MasMovil could be a new threat for Spain's rational pricing environment and believe it should be closely tracked. However, in our view the company lacks a minimum coverage on the Fixed-line side and will have to overcome falling price sensitivity amongst consumers which will make growth more challenging for a price-discount player. We thus believe the new company will not have a material impact on the improved competitive landscape in Spain.**