

Tugas Laporan Tertulis

Judul:

“PT Indosat Tbk. (ISAT) Qualitative Analysis”

oleh:

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*Isi laporan dibuat sepenuhnya dalam Bahasa
Inggris. Laporan tidak terpisah daripada
lampiran-lampiran yang disertakan.*



S1 Finance

Universitas Prasetiya Mulya

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PT INDOSAT TBK. ★★☆☆☆

Exchange	Ticker	Last Close	Market Cap.	Sector
JCI	ISAT	6,500 (8 Feb 2017)	34.64tn IDR	Telecommunication

I. SUMMARY

Mediocre economic growth does not dampen the demand for telecommunication services. Cellular growth, along with MIDI and fixed telecommunications, remained robust throughout the year. Although competition is fierce, ISAT is well positioned to capture the growing piece of the market. However, **issues in profitability prevent the company from being a stellar performer**. ISAT's recent developments have been focused to raise competitiveness in the cellular market. Partnership with the Swedish music streaming service Spotify (2016 H1) aimed to increase value by delivering affordable music streaming services to customers. The company has also introduced a new Data Rollover program, which lets customers 'roll over' their remaining data to next month's quota, a feature not commonly seen in retail packages.

II. BUSINESS DESCRIPTION

PT Indosat Tbk. (ISAT) is an Indonesian company providing telecommunication networks and services and information technology (IT) services. ISAT operates through three segments: **cellular**, **fixed telecommunications**, and **MIDI** (Multimedia, Data Communication, Internet). ISAT provides basic telecommunication services as well as multimedia and Internet services, and is also engaged in mobile and fixed telecommunication networks. Furthermore, ISAT also provides payment transaction and money transfer services through its telecommunication networks. The company also provides corporate services to large, medium, and small enterprises.

Indosat was founded in 1967, over 49 years ago, and was designated PMA (investment from foreign entities) as per Indonesian regulations. In November 2015, Indosat was renamed Indosat Ooredoo after its controlling company Qtel, a Qatari telecommunications company, rebranded itself as Ooredoo.

III. MACROECONOMIC SUMMARY

Indonesia has been posting a rather lackluster economic growth, hovering around 5% GDP growth, though **demands for telecommunication services remained robust**. Increasing GDP per capita, as well as stable population growth, backs up the increasing adoption of smart-devices. This,

combined with future infrastructure-focused development plans by the government allow for a steady organic growth of the industry.

IV. SECTOR OVERVIEW AND OUTLOOK

The Indonesian market for cellular services is the world's fourth largest, after China, India and the United States. Competition among cellular service providers in Indonesia is based on various factors, including pricing, network quality and coverage, the range of services, features offered, and customer service.

In general, telecommunication is an expensive business, with heavy reliance on capital and complex technologies which needs upgrading every few years. Companies need to be large enough to withstand the costs of managing and expanding their networks and services. Size matters in this industry; big companies are more apt to use their own extensive networks, while smaller competitors with lesser coverage must rely more on other networks' interconnection.

Indonesia has a moderate number of telecommunication companies, but three of them holds around 80% of the market. They are **Telekomunikasi Indonesia, Indosat, and XL Axiata** (TLKM, ISAT, EXCL, respectively). Combined, they are considered the 'Big Three' of Indonesia's telecommunication.

Ticker	Mkt Cap. (IDR)
TLKM	398.16 tn
ISAT	34.64 tn
EXCL	31.00 tn
FREN	6.33 tn
BTEL	1.90 tn

Figure 1. Market capitalization of major players

Key Industry Trends

Trends that help shape the industry's current landscape are as follows:

- *Increasing smartphone adoption* – Smartphone adoption is expected to reach 92 million users in 2019, up from 55 million in 2015. Furthermore, it is not uncommon for the more well-offs to have and use two or three mobile devices at the same time. Recent number shows the average subscriber holds around 1.5 simcards concurrently. Coupled with stable, albeit slower, economic growth, this trend does not look to be abating soon.
- *Increasing reliance to online contents* – more consumer and business functions are starting to be available on the Internet, boosting the demand for devices, data packages, streaming services, and faster broadband connections.

- *Traditional voice & SMS activities in decline* – along the lines of increasing reliance to chat and video calls, traditional talktime and messaging are in decline.
- *Data is the new source of growth* – there has been increasing attention to data growth, which in 2014-15 has grown around five to nine times revenue growth. It is perceived that data will drive the majority of telecommunication's business in the near future.

Further discussion on the nature of the industry will make use of Porter's Five Forces framework. They are, in order of perceived importance, as follows.

<i>HIGH</i>	<p><i>Industry Competition</i></p> <p>Internal competition is fierce, and leads to a somewhat depressed pricing particularly in the retail cellular market. The “Big Three” dominates the market, but lesser competitors have tried to compete with innovative marketing and data packages.</p>
<i>LOW</i>	<p><i>Threats of New Entrants (Barriers to Entry)</i></p> <p>High capital and advanced financing needed in this industry poses a very significant challenge to potential newcomers. Expensive fixed assets and limited licensing opportunities have proved effective in restricting the number of players in Indonesia's telecommunication market. If anything, foreign telecommunication companies may deserve more attention, since it is not uncommon for acquisitions to take place.</p>
<i>LOW</i>	<p><i>Threats of Substitute Products</i></p> <p>In Indonesia, mobile data service is the primary method of Internet access, caused by the underdevelopment of public data access infrastructure such as Wifi hotspots. This makes many Internet-related products and services very hard to be substituted, a fact which contributes to carriers' strong hold on pricing. There are, however, some concerns on cannibalization of the revenue from telephone minutes, since some customers have begun to opt for VoIP (Voice over IP) as primary means of verbal communication.</p>
<i>LOW</i>	<p><i>Power of Buyers</i></p> <p>Sale of cellular services, which comprises the majority of this sector's revenue, is mainly obtained through continual subscriptions from a large and varied number of individual customers. The customer base is very fragmented, and it is not uncommon for one individual to have subscriptions to two or more carriers. This allows carriers to easily dictate the terms and pricing of their product services. Sales to corporate and business customers is, in general, dependent on the nature of the services required, but no buyer has any significant bargaining power over the carriers.</p>

NEUTRAL *Power of Suppliers*

BTS (Base Transceiver Stations), the main equipment required to deliver services, are transacted on a rent-basis, and one device can serve multiple frequencies. To obtain antennae locations, carriers extend offers to land owners deemed to have strategic locations, most of which are individual entities.¹ This ensures high availability, predictable expense streams, and manageable transactions.

V. COMPANY ANALYSIS

ISAT earned the bulk of its revenue through its cellular division (81.8%), followed by MIDI (14%) and fixed telecommunication (4.2%). Cellular contribution has remained stable in recent years, while MIDI is generally rising and fixed telecommunication falling. Robust smartphone usage patterns ensures that there is ample space for further growth.

	2011	2012	2013	2014	2015
Cellular	81.4%	82.5%	81.2%	80.9%	81.8%
MIDI	12.5	13.0	13.7	14.6	14.0
Fixed	6.1	4.6	5.1	4.6	4.2

Figure 2. ISAT's revenue breakdown

Company's Profitability

From profitability's point of view, things are not looking so well. **ISAT posted negative earnings from year 2013 to 2015, although there are some signs of reversal.** Falling margins further exacerbate this problem. There are signs of weakening in gross margin and EBITDA, but none as bad as operating margin: latest annual report numbers reveal that it has fallen about one-fourth from its 2011 level.

	2011	2012	2013	2014	2015
ROE	4.61%	2.02%	(15.88%)	(13.48%)	(10.04%)
ROA	1.59	0.70	(5.07)	(3.72)	(2.41)
<i>Margins</i>					
Gross Margin	63.13	60.28	58.26	56.78	58.11
EBITDA	45.74	47.01	43.50	41.40	42.73
Operating Margin	13.75	10.11	5.94	7.24	9.97

Figure 3. ISAT's profitability ratios

In 2016 however, ISAT managed to post IDR 7.6 tn of revenue in Q3, continuing a streak of positive earning from Q1. This is mainly the result of

¹ It is not uncommon for landowner him/herself to advertise a space as 'BTS-optimal' or 'BTS-ready' in an effort to attract the carriers' development teams.

good organic growth combined with lesser volatility from its foreign currency exposure. The company has decreased its USD-denominated bonds to USD 186.4mi (-63% yoy) while increasing IDR-denominated bonds to IDR 14.5tn (+34% yoy). This change in liability structure helps to guard against mounting uncertainty in the American currency.

As a major player, ISAT is one of the leader in pricing. The recent partnership with the Swedish music streaming service Spotify is aimed to bolster the company's value proposition to its customers, particularly to those sufficiently comfortable in accessing the Internet for various services (the number of which is growing). There are, however, gaps in the quality of ISAT's service, most notable one being that it is not known for good overall signal coverage (overall coverage champion is TLKM, which, in turn, is notorious for its relatively high data service prices).²

Risks to profitability with regards to industry conditions is as follows.

Threats to profitability	Degree	Summary
Industry Rivalry	High	Generally, somewhat depressed pricing as result of competition. Robust value propositions are needed to compete effectively.
Threats of New Entrants	Low	High barriers to entry preserve industry's 'pie size' as a whole.
Threat of Substitutes	Low	Current products and services are hard to substitute.
Bargaining Power of Suppliers	Neutral	Little bargaining power from suppliers. Significant challenges revolve mostly around keeping tabs on expenses.
Bargaining Power of Buyers	Low	Little to no bargaining power from customers, but the 'churn rate' ³ must be vigilantly monitored.

Figure 4. Porter's Five Forces impact to profitability

Based on the analysis, it suffices to say that **industry competition remains the most significant challenge faced by ISAT**. As telecommunication industry grows, it will become more complex, requiring greater technical expertise from the companies. ISAT's future outlook is, although not bleak, remains mediocre if it cannot soon catch up in market share, operations, and profitability.

² See Appendix for coverage map.

³ The rate at which customers leave for a competitor. The telecommunication industry has one of the highest churn rates of any industry; this is mainly due to the fierce competition.

APPENDIX

Attached are extra information for review.

I. Company's Info Sheet as per its annual report.

Name of the organization	PT Indosat Tbk, known as "Indosat Ooredoo"
Primary brands, products and/or services	<ul style="list-style-type: none">• Postpaid and Prepaid Cellular Services under the Mentari, Matrix and IM3 brands• Fixed data services, which include multimedia, data communications and Internet (MIDI) services marketed primarily to business customers. We also offer satellite-based services such as transponder leasing and VSAT services and IT services, such as Disaster Recovery Center, Data Center services, and Indosat Ooredoo Cloud Services with infrastructure-as-a-service. We provide these services directly and through our subsidiaries, Lintasarta and IM2.• Fixed telecommunications (voice) services.• Digital services.
Location of the organization's headquarters	Jakarta, Indonesia
Operational area and markets served	Indosat Ooredoo serves both retail, Small Medium Enterprise (SME) and large enterprise customers across the Republic of Indonesia.
Nature of ownership and legal form	Publically listed Indonesian legal entity
<i>Scale of the company</i>	
Number of cellular subscribers	69.7 million
Number of permanent employees	3,178 (not including subsidiaries)
Number of BTS	50,687
Revenues in 2015	Rp26,768.5 billion
Total assets as of December 31, 2015	Rp55,388.5 billion

Identity and percentage of largest shareholders	Ooredoo Asia Pte Ltd. is the largest shareholder with 65% ownership.
Significant changes in size or ownership, or supply chain	No significant changes took place during the reporting period with regard to ownership or share capital structure. Certain assets/facilities were strategically closed while new ones were upgraded, but the scale of the overall organization did not change materially during the year, nor did its supply chain.

II. Smartphone growth in Asia Pacific

Indonesia is one of the fastest growing market for Internet-enabled smartphones in the region.

No. of smartphone users (mil.)	2015	2016E	2017F	2018F	2019F
China	525	563	599	640	687
India	167	204	243	279	317
Indonesia	55	65	74	83	92
South Korea	33	34	35	36	37
Phillipines	26	29	33	36	39

Source: http://www.indonesia-investments.com/zh_cn/news/todays-headlines/internet-smartphone-penetration-in-indonesia-estimated-to-grow-strongly/item7010, taken 2017-02-06.

III. Coverage Map for the “Big Three” Major Carriers

Note: The thicker the green, the better.

Telkomsel (TLKM)



Indosat (ISAT)



Excelindo (EXCL)

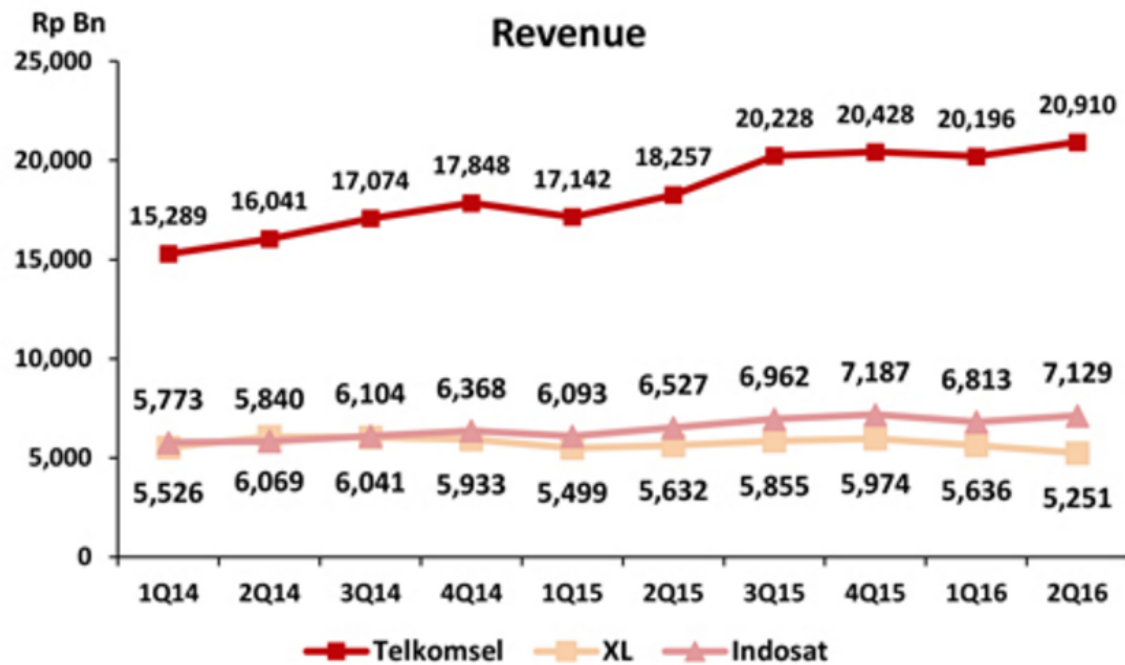


Source: <https://opensignal.com/networks/indonesia>, taken 2017-02-05.

V. Big Three operators' revenue

TLKM outpaces both ISAT and EXCL. EXCL shows signs of faltering in recent quarters.

Big 3 operators' revenue



Source: DBS, taken 2017-02-06.

DISCLAIMER

This research report is made for Prasetiya Mulya University as part of grading consideration for *Security Analysis* class. It is in no way intended to be used as financial advice, and does not represent the views of Prasetiya Mulya University.

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