

PLDT acquires DGTL

Summary

PLDT to own 87.5% to 100% of DGTL

JGS to end up with 10.1% of PLDT and P14.5 billion

PLDT to conduct tender offer for DGTL shares at P1.60

DGTL – tender for P1.60

JGS – sell at P25.00 or better

PLDT – hold, expected to breach P2,500

GLO – hold, expected to reach P900

JG Summit Holdings (JGS) and PLDT (TEL) recently entered into a deal that would transfer control of Digitel (DGTL) from the JGS group to PLDT. The transaction greatly affects the telco industry as it reduces the major players from three to two. PLDT will now control almost 70% of the market with over 60 million subscribers while Globe will have slightly more than 30% with over 26 million subscribers.

Affected Parties

JG Summit Holdings (JGS) – listed holding company of the Gokongwei family. Has investments in Universal Robina Corporation (URC), which is in the food business, Robinson's Land Corporation (RLC), which is into property, Cebu Air (CEB), which operates Cebu Pacific, the number one local airline, and Digitel (DGTL), which operates Sun Cellular. JGS also has investments in banks, media, and petrochemicals.

Philippine Long Distance Telecommunication (TEL) – the country's premier corporation is the largest component of the PSEi. PLDT operates Smart, Talk 'N Text, and Red Mobile. Together, its three brands have a total of over 45 million subscribers. PLDT also has the largest number of subscribers for landline and internet. The company also has interests in Meralco (MER) through its subsidiary, PLDT Comm. And Energy Ventures (PCEV).

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Digitel (DGTL) – Digital Telecommunications, or Digitel as it is more popularly known, operates Sun Cellular, the pioneer in offering unlimited services for mobile phones. With 15 million subscribers, it is the third largest telco in terms of subscriber number.

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Globe (GLO) – Globe is an Ayala-affiliated company and is the second largest telco in terms of subscriber number. Globe also operates TM and has over 26 million subscribers. Globe had been a strong number 2 to PLDT in the telco industry before the entry of Sun Cellular. Sun Cellular's low pricing strategy has cut into the profitability of Globe in recent times.

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The Deal

| PLDT receives: | JGS receives: |
|--|--|
| 1) 3.277 billion shares of DGTL (51.55% of DGTL's current shares outstanding) | 1) P69.2 billion worth of PLDT shares (at P2,500 per share) or 27.68 million shares. |
| 2) Convertible Bonds issues by DGTL to JGS. These bonds are convertible to 18.6 billion DGTL shares on June 30, 2011. PLDT has indicated that it will most probably convert the bonds. | |
| 3) P34.1 billion worth of intercompany advances made by the JGS Group to Digitel and its subsidiaries. | |

PLDT is also set to conduct a tender offer for the remaining 48.45% of the current outstanding shares of DGTL. The tender offer will be at P1.60 per share. PLDT is willing to pay in cash or in PLDT shares (at P2,500 per PLDT share) at the option of the DGTL shareholder. Pending the relevant approvals, the transaction is expected to be completed by the end of the 2nd quarter of 2011.

Consequences and Recommendations

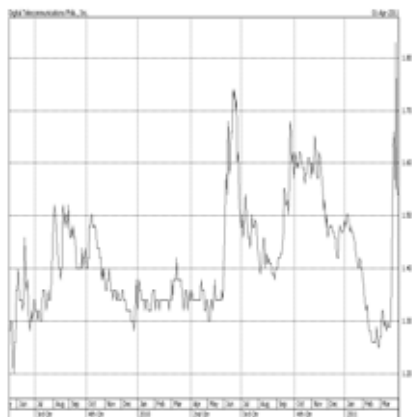


PLDT – TEL will now control a dominant share of the mobile market. It will control four mobile brands: Smart (targeted at a higher end market), Talk 'N Text (targeted at the mass market), Red Mobile (relaunched recently), and Sun (specializes in offering unlimited services). The wide array of brands as well as the sheer number of subscribers will give PLDT a huge advantage moving forward. However, it still remains to be seen what exactly PLDT will do with Sun.

PLDT has hinted that it will keep Sun as a separate entity that will continue to offer its unlimited services. This will be the case for now as PLDT assesses how it can best play its most recent acquisition. Cost savings should be visible soon as there are bound to be redundancies between PLDT's mobile operations and Digitel's. Sun Cellular subscribers can also benefit from the wide range of services that PLDT can offer.

Post-conversion of the convertible bonds, PLDT will have between 21.87 billion to 24.96 billion shares of DGTL which would translate to 87.6% to 100% of the then outstanding shares of DGTL. How much PLDT will own of DGTL depends on how many DGTL minority shareholders accept the tender offer of PLDT. It is expected that a significant portion of minority shareholders will accept the tender offer.

Shareholders of PLDT are advised to hold on to their shares. Cost savings are expected to translate to better margins while the addition of over 15 million subscribers will lead to a jump in its wireless revenues. Also, the transaction will not cost PLDT too much cash, which will allow PLDT to keep up its strong dividend policy (PLDT is expected to give out another P78.00 in cash dividends this August). The acquisition of DGTL will allow PLDT to register growth in the next few years. This is in contrast to the stagnant 2011 and 2012 the company previously foresaw.



Digitel – As a listed company, DGTL will most likely follow in the footsteps of PCEV (PLDT Comm. And Energy Ventures, formerly Piltel). Current shareholders are advised to wait for the tender offer (expected some time in May or June). The tender offer of P1.60 is as good an offer as shareholders are going to get in the foreseeable future. The tender offer is payable in cash or PLDT shares (valued at P2,500). If by the time the tender offer arrives TEL is trading above P2,500 then DGTL shareholders should tender for PLDT shares. If TEL is trading below P2,500 then DGTL shareholders should tender for cash. Either way, eligible shareholders should tender their shares.

Alternatively, those looking to play this development in a different way can accumulate DGTL at P1.55 and below and tender the same shares at P1.60 when PLDT makes its tender offer. Those doing so will make a small gain in a few months time. The risk here is that there is a chance that the tender offer may be delayed since the transaction between JGS and PLDT is still pending regulatory and shareholder approval.

JG Summit – The holding company of the Gokongwei family came out a winner in swapping its DGTL-related assets for a stake in PLDT. Not only was JGS able to get a premium for its shares in DGTL, it was also remunerated by PLDT for much of the cash it had plowed into DGTL over the last several years. As part of the deal, an associate company of First Pacific will acquire 5.81 million PLDT shares from JGS at P2,500 per share. JGS is expected to own 10.1% of PLDT as well as receive approximately P14.5 billion which it can use for other purposes.



For now it seems that the price of JGS has already fully adjusted. We estimate that the deal increases the value of JGS shares by P6.00. Prior to the deal being announced, JGS was trading around P19.00. Therefore, we see JGS stabilizing around P25.00 for the time being. Shareholders are now advised to take profit in JGS as it has reached its peak for now.

Globe – While Globe was not part of the deal, it came away a winner. Globe had been struggling to compete with the prices and promos that were being offered by Sun. In fact, Sun had been slowly trimming the gap between itself and Globe in terms of number of subscribers. We believe that PLDT's acquisition of DGTL will have a positive impact on Globe's performance. We should start seeing improved numbers for Globe towards the end of the year.



Competition in the telco industry had been fierce. With PLDT's acquisition of DGTL, the telco industry once again becomes more like a duopoly. Without having to spend a dime, Globe will see its margins improve as it is seen to regain some of the pricing power it had prior to Sun's entry. Globe is expected to stabilize around P900.00 in the near future as its recent rise is due to the expected improvement in its net income this year. Shareholders are advised to hold on to their GLO share for dividend reasons. Improved bottomline figures for GLO will translate to higher cash dividends for shareholders. Once PLDT's plans for DGTL, and the Sun Cellular brand, becomes clearer then it will be time to reassess GLO's value.