2nd September 2016

TMT

Iliad

Price EUR186.55

Heading to Italy!

Fair Value EUR212 (+14%) **BUY**

Bloomberg	ILD FP
Reuters	ILD.PA
12-month High / Low (EUR)	236.3 / 168.4
Market Cap (EUR)	10,956
Ev (BG Estimates) (EUR)	12,515
Avg. 6m daily volume (000)	106.7
3y EPS CAGR	20.5%

	1 M	3 M	6 M	31/12/15
Absolute perf.	8.1%	-4.1%	-18.7%	-15.2%
Telecom	-1.2%	-7.9%	-10.4%	-14.4%
DJ Stoxx 600	1.1%	-0.1%	1.5%	-6.1%

YEnd Dec. (EURm)	2015	2016e	2017e	2018e
Sales	4,414	4,671	4,931	5,159
% change		*5.8%*	*5.6%*	*4.6%*
EBITDA	1,490	1,668	1,886	2,094
EBIT	0.0	0.0	0.0	0.0
% change				
Net income	335.0	358.3	456.7	587.2
% change		*6.9%*	*27.4%*	*28.6%*

	2015	2016e	2017e	2018e
Operating margin	15.1	15.3	18.0	20.9
Net margin	7.6	7.7	9.3	11.4
ROE	12.7	12.1	13.4	14.8
ROCE	9.8	9.5	10.9	12.8
Gearing	45.2	52.4	43.2	27.9

(EUR)	2015	2016e	2017e	2018e
EPS	5.58	5.95	7.59	9.76
% change	-	*6.7%*	*27.5%*	*28.6%*
P/E	33.4x	31.3x	24.6x	19.1x
FCF yield (%)	NM	NM	1.0%	3.5%
Dividends (EUR)	0.38	0.38	0.38	0.38
Div yield (%)	0.2%	0.2%	0.2%	0.2%
EV/Sales	2.8x	2.7x	2.5x	2.3x
EV/EBITDA	8.2x	7.5x	6.6x	5.8x
EV/EBIT	NS	NS	NS	NS

Following the European Commission's approval of the merger between Hutchison and Vimpelcom in Italy, Iliad will soon enter the Italian market. Although facing many new challenges in a competitive environment, we believe Iliad has the right assets to seize opportunities in the Italian market and be successful. Moreover, the necessary investments should be spread over time, which would limit the increase in the company's risk profile. We reiterate our Buy recommendation, and stick to our Fair Value of EUR212 pending further comments and guidance from management.

ANALYSIS

- The European Commission yesterday **approved the joint venture between Hutchison and VimpelCom** in Italy, conditional on the structural **remedies** offered by Hutchison and VimpelCom, which **fully address the Commission's competition concerns**. This decision ensures the **market entry of Iliad as a new mobile network operator in Italy.**
- As a reminder, the agreement involves the **transfer of 3G and 4G frequencies** for **EUR450m**, an undertaking of **several thousand sites in dense areas**, an undertaking to bring into force the **RAN-sharing agreement or to acquire several thousand sites in rural areas**, and a **2G/3G/4G roaming agreement** on the merged network, for a period of **five years renewable for a further five-year** period at the initiative of Iliad. In our view, this great set of network and license agrements should clearly **facilitate Iliad's entry and development** in the market from an **operational and technical standpoint**. Iliad said the roaming pricing conditions are "way more favourable" than those in France with Orange, and the contract is "fully variable". Moreover, Iliad is confident there is no further threat from the regulator hanging over the roaming agreement.
- Opportunities also exist from a **marketing standpoint**. The Italian mobile market is **large** (85m lines) and a **mostly prepaid market**, with growth opportunities from the **development of unlimited calls, data usage, 3P offers and fixed/mobile convergence**. We believe Iliad should be able to deal **fixed wholesale agreements** with Fastweb, TI or Enel on DSL and Fiber to develop **Triple Play offers and fixed/mobile convergence**. Nevertheless, challenges exist: firstly, Iliad will **start from scratch**, with **no existing customer base** for **cross selling** lever and **no brand image** in the country, which is likely to lead to **higher acquisition costs**. Secondly, the **mobile penetration rate is already very high** (~140%) and decreasing, and **mobile arpu is already very low** (~EUR12), with **limited economic space for a fall in prices**.
- In all cases, we believe one should not underestimate Iliad's **pricing creativity** and **innovation capacity**, as well as its leadership in terms of **cost efficiency** and know-how in terms of **direct distribution** and **viral marketing**. As a reminder, no French operator was able to anticipate Free Mobile's major breakthrough in 2012. We believe **Iliad's mobile market share target should be around 15%,** with long term revenue expectations between EUR1.5bn and EUR2bn (excluding opportunities in fixed), and **EBITDA breakeven to be reached within three years.**
- Licence payments are to be **phased between between 2017 and 2019**, and Iliad plans to carry out investments over a period of **5-7 years**, entirely financed by the **group's cash and available facilities**. We believe **network CAPEX should be quite progressive**, along with commercial growth. As such, we think the **leverage impact at the group level should be quite limited**: we believe it should not exceed 1.1x or 1.2x EBITDA, and thus we see Iliad's plan in Italy as only **moderately increasing the company's risk profile**.

VALUATION

- We reiterate our **Buy recommendation**, and pending further comments and guidance from management we are sticking to our Fair Value of **EUR212**.

NEXT CATALYSTS

- Q3 results in November 2016.

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BUY ratings 55,3% NEUTRAL ratings 33,3% SELL ratings 11,3%

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