

2 December 2009

M2 Telecommunications

Hold

Important: The above recommendation has been made on a 12 month view and may not suit your investment needs or timeframe. The basis it is prepared on is summarised on the last page of this report. **PLEASE CONTACT YOUR ADVISER TO DISCUSS THIS GENERAL RECOMMENDATION BEFORE ACTING ON IT.**

Target price
A\$1.69

Price
A\$1.65

Market Cap
A\$188.9m

Turnover- monthly rolling value
A\$3.3m

MTU91202

Service with a smile

Over the last five years as a listed telco reseller, MTU has delivered strong organic and acquisitive growth. Following the recent acquisitions of PeopleTel and the business telecoms assets of Commander, MTU has gained significant scale and expertise and is well positioned for the NBN evolution. We initiate coverage with a Hold recommendation and A\$1.69 price target.

Key Forecasts

	FY08A	FY09A	FY10F	FY11F	FY12F
EBITDA (A\$m)	9.1	13.3	30.5	33.1	33.9
Reported Net Profit (A\$m)	5.2	7.5	15.6	18.1	20.1
Normalised Net Profit (A\$m) ¹	5.7	8.3	15.6	18.1	20.1
Normalised EPS (¢) ¹	7.2	9.9	14.2	16.5	18.2
Normalised EPS Growth (%)	137.5	45.6	87.7	16.4	10.6
Dividend Per Share (¢)	5.0	5.5	7.0	8.0	9.0
Dividend Yield (%)	3.0	3.3	4.3	4.9	5.5
Normalised PE (x)	22.8	16.6	11.6	10.0	9.1
EV/EBITDA (x)	15.6	14.3	6.5	5.4	4.6
Price/Net Oper. CF (x)	5.8	7.2	7.9	5.0	4.7
ROIC (%)	29.6	39.2	33.0	33.1	32.0

Source: Company data, RBS Morgans forecasts

Company description – an independent telecommunications reseller

M2 Telecommunications (MTU) is a network independent telecommunications reseller and wholesaler of fixed line voice, mobile and internet services. Since listing on the ASX in 2004 at 25cps (A\$14.4m market cap) MTU has grown rapidly through organic and acquisition growth. More recently MTU has evolved into a much larger telco via the acquisition of People Telecom in April 2009 and the business telecoms assets of Commander in June 2009. These acquisitions should contribute around A\$190m in recurring revenue or 50% of FY10 revenue.

Consistent high double digit growth with margins now improving

MTU has consistently delivered above average Compound Annual Growth Rates (CAGR) since it listed in 2004. Its 6 year revenue CAGR is 74.6%, EBITDA 59.0%, EPS 23.7% and DPS 28.52%. EBITDA margins have typically declined around 80bps pa however following the substantial increase in scale look likely to improve to around 7.8% in FY10.

NBN looks likely to be a positive for MTU

NBN details are still unclear. Given the last few miles of fibre are likely to be operated by an independent company that will not resell direct to the public, in our opinion, the NBN is likely to benefit smaller, more nimble and customer centric operators such as MTU. The caveat being an assumption that MTU's scale provides reasonable access to volume discounts.

Investment view: Hold recommendation A\$1.69 price target

We value MTU at A\$1.69 per share based on an equally weighted DCF based valuation and PE compco. Our DCF based valuation is A\$1.76 and our PE based valuation of A\$1.62. In setting our PE valuation we have applied a 20% discount to peers given MTU is a reseller and therefore does not own its own infrastructure. Key risks relate to margin pressure from suppliers and the implications of the NBN.

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MTU initiation of coverage

Company overview

MTU was founded in 1999 as a telecommunications hardware manufacturer. By 2001 the business had evolved into a telecommunications reseller of fixed line and mobile communications to SMEs. MTU listed on the ASX in late 2004 and posted an FY04 profit of A\$1.3m from A\$15.3m in revenue. Shortly thereafter MTU expanded into telecommunications wholesaling. In August 2005 MTU signed an Alliance with Optus Mobile as a Mobile Virtual Network Enabler (MVNE). Following several significant acquisitions including Commander and People Telecom (detailed below) MTU has emerged in 2009 as the 7th largest telco industry player.

Given MTU does not own much infrastructure they compete on the basis of customer services and by offering clients a customised value proposition. For example a manufacturing SME may be looking for cheap call rates to China where its key products are produced. Telstra and Optus typically offer packages but don't provide customised offerings. The scale and lack of flexibility of these large carriers has meant MTU is able to profitably offer customised services.

Table 1 : MTU divisional composition

Revenue	2003	2004	2005	2006	2007	2008	2009
Retail	7.5	15.3	23.7	33.5	33.3	51.9	112.4
Retail yoy gth		104%	55%	41%	-1%	56%	117%
Wholesale	0	0	0	0	10.5	57.4	90.3
Wholesale yoy gth						446%	57%
Total	7.5	15.3	23.7	33.5	43.8	109.2	202.7
Total yoy gth		104%	55%	41%	31%	149%	86%

Source: Company data; RBS Morgans estimates

Telecommunications competitive landscape in order of size

MTU has approximately 1% of the A\$36bn telecommunications market which places them as the 7th largest Australian telco.

- Telstra (TLS) FY09 revenue of A\$25,371m, EBITDA of A\$10,945m, EBIT of A\$6,555m
- Optus / Singtel (SGT) FY09 revenue of S\$9,387m, EBITDA S\$6,481m, EBIT of S\$1,064m
- Hutchison/ Vodafone (HTA) FY09 revenue of A\$1,883m, EBITDA of A\$318.7m, EBIT of A\$67m

Resellers or partial network owners

- AAPT/ Powertel/ Telecom NZ (TEL:NZ) FY09 revenue of NZ\$1,177, EBITDA of NZ\$88m
- Soul / TPG (SOT) FY09 revenue of A\$481.2m, EBITDA of A\$95.8m
- iinet (IIN) FY09 revenue of A\$417.8m, EBITDA of A\$67.3m
- **M2 Telecommunications (MTU)** FY09 normalised revenue of A\$360m (assuming full year contributions from recent acquisitions). Reported revenue in FY09 of A\$202.7m, EBITDA of A\$13.3m

Most comparable to MTU

- Macquarie Telecom (MAQ) – FY09 revenue of A\$253.8m, EBITDA of A\$25.0m (up 81.9% yoy). FY10 Outlook not provided
- ComTel (CMO): (Vodafone / Hutchison – mobile reseller). FY09 mobile revenue of A\$24.3m; EBITDA of A\$5.7m. FY10 Outlook – expect EBITDA to be down 5% in FY10 due to a decline in post paid mobile customer base and before restructuring costs
- Primus Telecom (subsidiary of PRTL:NASDAQ) – Australian 3Q09 revenue of US\$63.7m
- Amcom (AMM) – FY09 Revenue of A\$53.0m, EBITDA of A\$17.4m and EBIT of A\$15.0m
- Clever Communications (CVA) – FY09 Revenue of A\$14.3m; Gross profit of A\$6.5m; and EBITDA of A\$1.7m
- My Net Phone (MNF) – FY09 revenue of A\$9.8m; Gross profit of A\$4.0m and EBITDA of A\$0.2m.

Competitive position

MTU is a telecommunications reseller which differentiates itself from the larger telcos on the grounds of customer service and its ability to customise offerings to suit customers.

Suppliers

MTU currently purchases wholesale services from the major telcos. Major suppliers are Telstra (fixed line and broadband) and Optus (Mobile and wireless Broadband), however MTU does sell services from other carriers such as Vodafone. MTU does not own DSLAM infrastructure, instead preferring to resell Telstra and Optus ADSL and ADSL 2+ offerings.

MTU's scale continues to offer them upside as higher volumes relate to better purchasing arrangements and improved margin. While there is some reliance on pricing from suppliers, MTU is able to renegotiate prices generally on an annualised basis and therefore has the ability to move across to other carriers should they experience margin pressure from a single supplier. The National Broadband Network (NBN) is likely to change the competitive landscape significantly.

NBN implications

Details of the National Broadband Network (NBN) currently remain unclear, however it appears that Australia's telecommunications infrastructure will be operated by an independent network. Theoretically this levels the playing field and removes Telstra's significant competitive advantage. This levelling of the playing field should allow for smaller, more nimble players with better customer service (such as MTU) to compete with the incumbents. In our opinion, the only real disadvantage relates to buyer power as companies like Telstra who control more than 50% of the market should be able to buy access at lower prices. Given MTU has been able to operate profitably under the current regime we expect their business position will be much improved under the NBN.

Sensitivities

MTU is most sensitive to movements in its gross margin. We estimate a 1% movement in MTUs Cost of Goods Sold margin has a 10% impact on EBITDA.

Table 2 : ARPU sensitivities

Movement	1%	5%	-1%	-5%
REV	0.7%	3.6%	-0.7%	-3.6%
EBITDA	1.8%	9.2%	-1.8%	-9.2%
GM	0.1%	0.6%	-0.1%	-0.7%

Source: RBS Morgans estimates

Table 3 : COGS margin sensitivities

COGS margin	1%	5%	-1%	-5%
REV	0.0%	0.0%	0.0%	0.0%
EBITDA	-10.7%	-53.3%	10.7%	53.3%
GM	-5.0%	-24.9%	5.0%	24.9%

Source: RBS Morgans estimates

Our A\$1.76 DCF based valuation is based on a WACC of 13.50%. Increasing our WACC by 10% to 14.85% decreases our DCF based valuation to A\$1.57, while decreasing our WACC by 10% to 12.15% increases our valuation to A\$2.01.

Table 4 : PE compco

	FY10F
Peer multiple to apply (x)	14.3
(Disc)/prem to peers	-20%
PE to apply to M2 Comms (x)	11.4
M2 Comms EPS (c)	14.2
M2 Comms PE valuation (A\$ps)	1.62

Source: RBS Morgans

Valuation, risks and catalyst

We value MTU at A\$1.69 per share based on an equally weighted DCF and PE compco valuation. Our DCF based valuation of A\$1.76 applies a Wacc of 13.50% and is based on forecasts out to FY19. Our PE compco based valuation of A\$1.62 applied a multiple of 11.4x FY10F PE which is based on a 20% discount to the telecommunications sector (detailed in Table 7). We have applied this discount to peers given MTU is a reseller so typically does not own its own infrastructure whereas peers detailed below typically own some significant portions of infrastructure and therefore are less likely to suffer supplier margin pressure.

MTU's key risks relate to supplier margin pressure. Historically resellers have experienced significant problems when suppliers have increased prices; resulting in significant disruptions to the business model and in some case the destruction of profitability. Given MTU's diversity of earnings and suppliers we expect this risk is limited. We also note MTU typically has the ability to pass on pricing pressure to customers within six months.

Table 6 : MTU metrics at A\$1.71 price target

	FY10F
PE	11.9
EV/EBITDA	6.7
PE relative to ASX200	-22%
Yield	4.1%
PEG	0.18

Source: RBS Morgans

Table 5 : MTU metrics at current share price

	2009A	2010F
PE	19.7	11.9
EV/EBITDA	11.1	6.5
PE relative to ASX200	18%	-24%
Yield	3.6%	4.3%
PEG	0.71	0.18

Source: RBS Morgans estimates

Table 7 : Peer comparison

	FY09A PE	FY10F PE	FY09A EPS growth	FY10F EPS growth	FY09A ev/EBITDA	FY10F ev/EBITDA
PWK	31.7	13.1	31.0%	142.0%	20.1	6.8
SOT	63.8	26.2	0.0%	143.4%	11.7	8.9
IIN	11.3	9.5	18.6%	19.5%	4.5	3.8
AMM	13.6	10.2	21.3%	34.1%	10.8	7.3
DTL	13.8	12.6	8.4%	9.2%	7.4	7.4
Average	26.8	14.3	27.0%	69.6%	10.9	6.9
MTU	19.2	11.3	27.0%	69.9%	5.8	3.8
XJO	16.2	15.3			9.7	8.9

Source: RBS Morgans estimates; Pricedat COB 1 Dec 2009

Chart 1 : Comparable companies

	Rec	Mcap US\$m	1mth % chg	YTD % chg	P/E				EV/EBITDA				3 yr CAGR (%)				
					Actual	FY + 1	FY + 2	FY + 3	Actual	FY + 1	FY + 2	FY + 3	Rev	EBITDA	OpCF	EPS	DPS
Australasia Full Service																	
Singapore Telecom	Hold	43,069.1			13.02	11.95	10.68	10.05	8.30	7.15	6.42	5.84	9.0%	8.1%	--	9.0%	--
Telecom Corporation	Hold	3,371.0			9.50	11.05	10.45	8.75	4.01	3.95	3.73	3.61	-0.6%	1.9%	12.9%	2.8%	-5.9%
Telstra Corporation	Buy	79,101.4			10.42	9.53	8.57	7.89	5.20	4.77	4.44	4.17	3.6%	5.3%	9.2%	9.7%	4.6%
Median					10.42	11.05	10.45	8.75	5.20	4.77	4.44	4.17	3.6%	5.3%	11.1%	9.0%	-0.7%
Australia Small Cap																	
Amcom Telecommunications	Buy	122.7			13.62	10.16	8.67	7.91	10.84	7.33	6.36	5.69	11.8%	15.6%	50.7%	19.9%	11.2%
Hutchison Telecom (Aust)	Buy	1,690.8			n.m.	n.m.	10.29	5.88	9.58	3.82	2.74	2.02	17.3%	30.8%	-189.6%	-313.7%	--
iiNet	Buy	265.6			11.44	9.58	7.85	6.76	4.58	3.82	3.17	2.60	6.0%	11.7%	24.2%	19.2%	22.9%
Pipe Networks	Hold	323.2			31.80	13.14	12.97	10.32	20.12	6.79	6.69	5.58	32.1%	50.4%	-179.1%	45.5%	20.5%
SP Telemedia	Buy	1,097.2			64.77	26.61	23.38	21.30	11.90	9.06	8.24	7.60	0.0%	11.3%	-9.8%	44.9%	26.0%
Median					22.71	11.65	10.29	7.91	10.84	6.79	6.36	5.58	11.8%	15.6%	-9.8%	19.9%	21.7%
Asian Full Service																	
Bharti Airtel Ltd	Buy	24,392.6	2.58	-16.18	7.24	12.72	12.81	11.69	9.33	7.15	6.77	6.01	27%	23%	109%	25%	--
China Unicom (Hk) Ltd	Hold	31,679.0	2.56	12.04	15.23	21.17	25.87	20.86	3.73	4.77	4.78	4.35	22%	23%	-16%	77%	8%
Telekomunikasi Indonesia Tbk Pt	Buy	19,271.4	7.14	30.43	16.74	14.96	13.17	11.89	4.63	5.74	5.14	4.65	6%	1%	-8%	-1%	-1%
Philippine Long Distance Tel	Buy	10,187.4	0.39	21.75	13.10	11.84	11.13	10.27	5.06	5.89	5.53	5.29	3%	0%	6%	-1%	12%
Kt Corp (P)	Buy	8,552.7	-1.03	2.67	17.37	7.38	8.19	8.21	3.50	3.24	2.69	2.53	3%	-7%	-158%	-29%	-18%
Median					15.23	12.72	12.81	11.69	4.63	5.74	5.14	4.65	5.8%	0.8%	-7.8%	-0.6%	3.5%
Rest of world Full Service																	
Deutsche Telekom Ag	Hold	64,211.2	3.75	-8.39	12.51	15.06	13.90	13.24	5.22	4.63	4.49	4.40	0%	2%	6%	-23%	3%
Telefonica S.A. (Adr)	Strong Buy	99,205.8	3.52	28.59	12.04	11.10	10.28	--	4.90	--	--	--	8%	12%	4%	25%	28%
France Telecom	Buy	68,746.8	-1.92	-13.18	8.74	9.50	9.38	9.04	5.14	4.86	4.77	4.57	1%	8%	5%	63%	-6%
Bt Group Plc	Hold	18,471.6	8.24	6.72	7.12	10.65	9.52	8.95	5.09	4.56	4.46	4.33	2%	-16%	-18%	-132%	-24%
Telecom Italia Spa	Hold	21,323.7	-6.01	-7.48	6.45	10.22	9.94	9.19	5.10	4.85	4.57	4.33	-1%	-6%	-4%	-10%	-29%
At&T Inc	Buy	159,268.0	5.43	-5.30	9.60	12.73	12.00	11.04	5.66	5.64	5.35	4.79	25%	27%	24%	5%	6%
Verizon Communication	Buy	89,849.7	8.32	-6.70	12.45	12.88	12.67	11.87	5.52	4.17	4.29	4.69	3%	4%	10%	6%	4%
Hutchison Whampoa Ltd (Adr)	Strong Buy	26,955.1	-6.05	34.35	12.73	14.00	17.73	--	--	--	--	--	--	--	--	--	--
Median					10.82	11.92	11.14	10.12	5.14	4.74	4.53	4.48	1.9%	3.9%	4.8%	4.6%	2.7%
American Small Cap																	
3Com Corporation	Hold	2,929.3	38.43	225.44	16.49	24.33	20.24	--	4.24	--	--	--	1%	132%	24%	--	--
Cbeyond Inc	Buy	373.6	-11.40	-19.27	107.50	--	1376.00	54.00	8.60	--	--	--	18%	11%	-330%	-24%	--
Ciena Corp	Hold	1,112.1	2.45	81.34	10.38	--	145.07	28.93	6.74	-40.04	14.28	--	17%	16%	-197%	246%	--
Consolidated Communication Holdi	Hold	445.2	2.46	26.43	21.15	17.67	17.33	20.58	7.14	--	--	--	9%	11%	-5%	-27%	0%
Exfo Electro Optical Engineering	Hold	85.1	0.81	24.67	37.40	30.66	15.75	--	--	--	--	--	6%	-172%	--	-177%	--
Global Crossing Ltd	Buy	694.8	-14.76	45.47	--	--	--	--	5.26	--	--	--	12%	181%	-141%	-22%	--
Globecomm Systems Inc.	Buy	163.9	15.27	42.99	49.06	23.79	18.36	--	10.14	--	--	--	4%	-5%	-211%	--	--
Internap Network Svcs. Corp.	Hold	186.3	16.51	46.80	30.58	--	--	--	-1.27	--	--	--	12%	-253%	-193%	-377%	--
Jds Uniphase Corp	Hold	1,620.7	21.60	103.56	41.28	26.62	17.90	14.02	-1.27	--	--	--	-3%	-286%	-254%	--	--
Juniper Networks Inc	Hold	13,488.0	-0.66	46.60	21.75	30.15	23.20	19.17	7.84	17.13	13.67	--	16%	-208%	3%	-181%	--
Level 3 Communications Inc	Underper	1,967.7	-11.77	71.43	--	--	--	--	5.88	8.85	7.46	8.17	8%	26%	-41%	-38%	--
Limelight Networks Inc	Buy	283.7	-6.94	36.73	--	--	--	95.71	-0.83	--	--	--	26%	-249%	-11%	149%	--
Surewest Communications	Buy	123.8	-13.55	-23.47	145.67	249.71	145.67	--	5.61	--	--	--	1%	-2%	-254%	-46%	-21%
Switch & Data Facilities Co Inc	Hold	643.2	5.50	151.69	--	184.58	66.91	28.29	9.31	--	--	--	15%	18%	192%	-5%	--
Median					33.99	28.39	21.72	28.29	5.88	8.85	13.67	8.17	10.4%	4.2%	-140.8%	-27.4%	-10.3%
American data center services																	
Equinix Inc	Buy	3,795.1	7.35	82.89	30.98	58.60	48.19	32.28	12.14	13.74	12.82	9.58	35%	45%	28%	-335%	--
Internap Network Svcs. Corp.	Hold	186.3	16.51	46.80	30.58	--	--	--	-1.27	--	--	--	12%	-253%	-193%	-377%	--
Rackspace Hosting Inc	Buy	2,233.3	4.41	238.85	95.95	78.77	49.90	32.68	5.28	13.10	10.32	8.30	33%	27%	-273%	--	--
Savvis Inc	Buy	694.4	-27.07	85.34	--	--	--	--	5.19	5.39	5.09	4.15	4%	17%	-247%	-74%	--
Switch & Data Facilities Co Inc	Hold	643.2	5.50	151.69	--	184.58	66.91	28.29	9.31	--	--	--	15%	18%	192%	-5%	--
Terremark Worldwide Inc	Buy	400.8	-6.50	59.13	--	--	--	33.01	9.71	10.83	8.44	7.89	35%	25%	25%	--	--
Median					30.98	78.77	49.90	32.48	7.30	11.96	9.38	8.10	24%	22%	-84%	-205%	n.m.

Source: Australian companies are RBS Morgans estimates. All others are Thomson Reuters consensus estimates; Priced at 30 Nov 09

Table 8 : MTU history timeline

Event	Date	Notes
Acquisition of Commander business telecoms assets	Jun-09	Paid A\$19m in cash.
Acquires People Telecom (PEO:ASX)	Dec-08	Paid approx 3x PBT. Expected to be 15-20% EPS accretive. 0.0916 MTU shares for 1 PEO, 0.6886 cps in cash for 1 PEO shares and 0.344 cps.
Acquires Unitel (exc Commander business)	Feb-08	Approx 3x PBT (A\$10m + A\$2.5m earn out). Contributed A\$3.2m NPAT and A\$40m in revenue on a full year basis.
Acquires Orion (OTL:ASX) / Southern Cross Telco	Oct-07	Paid A\$22.0m (cash and scrip). Contributed A\$26.9m in revenue and A\$1.8m in NPAT on a full year basis). 22.9cps for OTL. Expected to be 40% EPS accretive. 0.238 M2 shares for 1 Orion share, 6.55cps in cash; and excess cash.
Wholesale deal with People Telecom mob	FY08	
ADSL2 product launched through subsidiary WCG (Wholesale Communications Group)	Aug-07	
Acquisition of Tenex Telecommunications	Jul-07	Acquired for approx 1.75 x NPAT (10% EPS accretion). Paid A\$0.51m in cash.
Extensions of Optus wholesale (MVNE) post-paid mob services to Sept 2010	Jun-07	
Acquires WCG	May-07	Paid for 3x NPAT (>30% EPS accretion). A\$1.5m (cash and scrip). Contributed around A\$0.7m NPAT and A\$10.0m revenue on a full year basis.
Signs wholesale agreement with Vodafone NZ	Aug-06	
Mr Farrow replaces MR Max Bowen as Chairman	May-06	
Licensing agreement with e-Direct (mobile connectivity)	Mar-06	
Acquires Protel	Feb-05	Paid 3.7x F NPAT. A\$1.5m + A\$1.5m earnout (cash and scrip)
Alliance with Optus Mobile (reselling Optus Mobile services)	Aug-05	
IPO	Oct-04	At 25 cps, PE of 7.1x, EV/EBIT of 3.6x
M2 established	Dec-1999	

Source: Company data; Iress; RBS Morgans estimates

More about MTU and the management team

Table 9 : Board of Directors

Name	Position	Background
Craig Farrow	Chairman	Mr Farrow holds a Bachelor of Economics degree from the University of Adelaide; a Diploma of Financial Services; is a Fellow of the Institute of Chartered Accountants and the Australian Institute of Company Directors. He is a founding partner of Brentnalls SA, Chartered Accountants and former National Chairman. Mr Farrow holds advisor or directorship roles with several consulting and trading enterprises and is National Chairman of the Institute of Chartered Accountant's Public Practice Advisory Committee. Mr Farrows has been a non Executive Director of MTU since its inception.
Vaughan Bowen	Managing Director	Mr Bowen holds a Bachelor of Commerce degree (UNSW) and is a member of the Australian Institute of Company Directors. He co-founded M2 in late 1999 and has managed MTU for over 10 years.
Max Bowen	Non Executive Director	Mr Bowen is a highly experienced Project Manager and property developer. He has acted in a senior advisory capacity to corporations and public utilities, including PricewaterhouseCoopers, Optus, Sydney Olympic Village, Sydney Harbour Foreshore Authority and Federal Airports Corporation. Mr Bowen is a Non Executive Director of MTU and has also served as Chairman.
Dennis Basheer	Non Executive Director	Mr Basheer is a company director experienced in property development, project management and franchise developments. He has been an executive director to MTU since 2003 and is primarily focussed on corporate and channel sales.
John Hynd	Non Executive Director	Mr Hynd holds a Bachelor of Laws degree from the University of Adelaide, is a Fellow of the Taxation Institute of Australia, a member of the Intellectual Property Society of Australia and New Zealand, a member of the Advisors Group with Family Business Australia and a former member of the Law Council of the Law Society of South Australia. Mr Hynd's expertise lies in intellectual property legal affairs within the technology industry. He has served as a non-executive director of MTU since its incorporation.
Mr Michael Simmons	Non-Executive Director	Mr Simmons was appointed to the Board to MTU on 26 th November 2009. He is experienced in the telecommunications sector having previously held the role of Managing Director of Terria (FTTN consortium bidder). Prior to this Mr Simmonds was the CEO of ASX listed SP Telemedia. (SOT) and the CFO of NBN Television which was acquired by SOT.

Source: Company data; RBS Morgans estimates

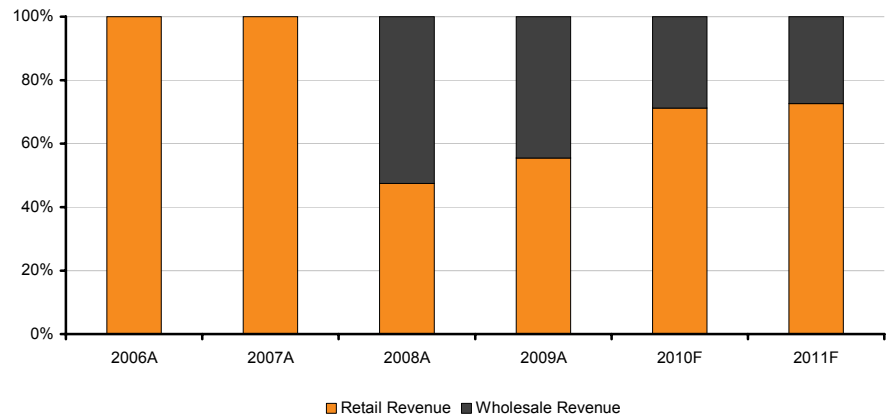
Table 10 : Business lines and customer propositions

M2 retail brand	Target Market	Core Proposition	Path to Market
Commander	Small and Medium Business (SMB) and small corporates	Telco services and equipment	National exclusive dealer network
People Telecom	SMB	Customised telco services	National I dealer network
M2 Telecom	SMB	Loyalty Programs and association alliances	Specialist dealer network
Southern Cross Telco	SME and residential	Regional focus	Direct and dealer networks

Source: Company data; RBS Morgans

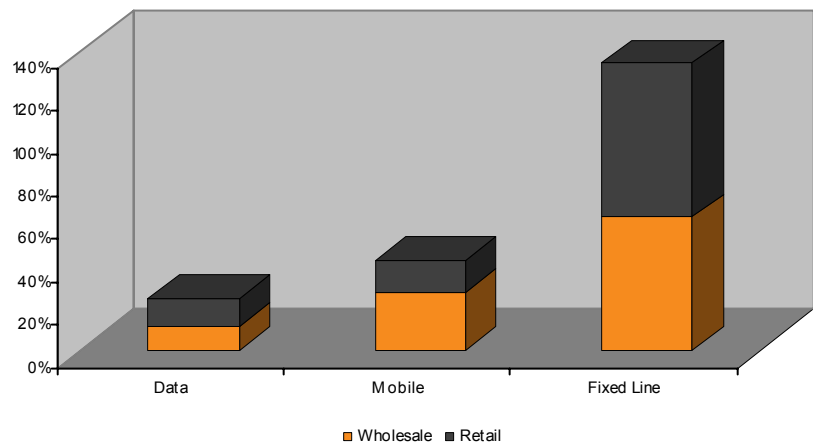
Divisional summary

Chart 2 : Revenue split



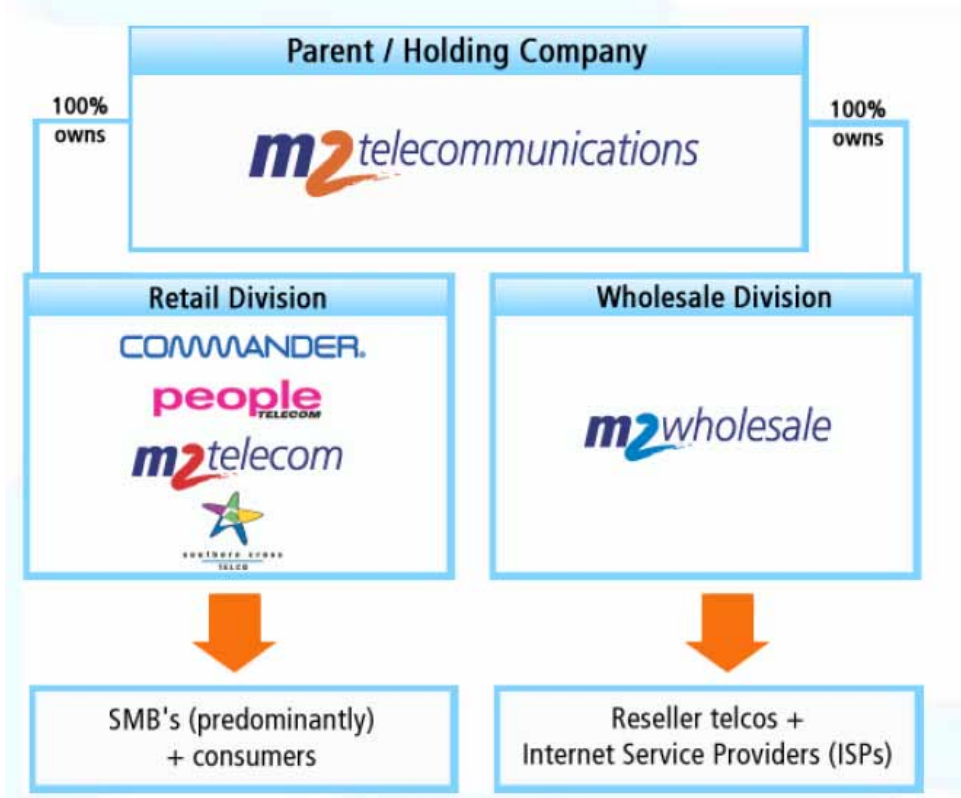
Source: Company data; RBS Morgans estimates

Chart 3 : FY09A divisional revenue splits



Source: Company data; RBS Morgans estimates

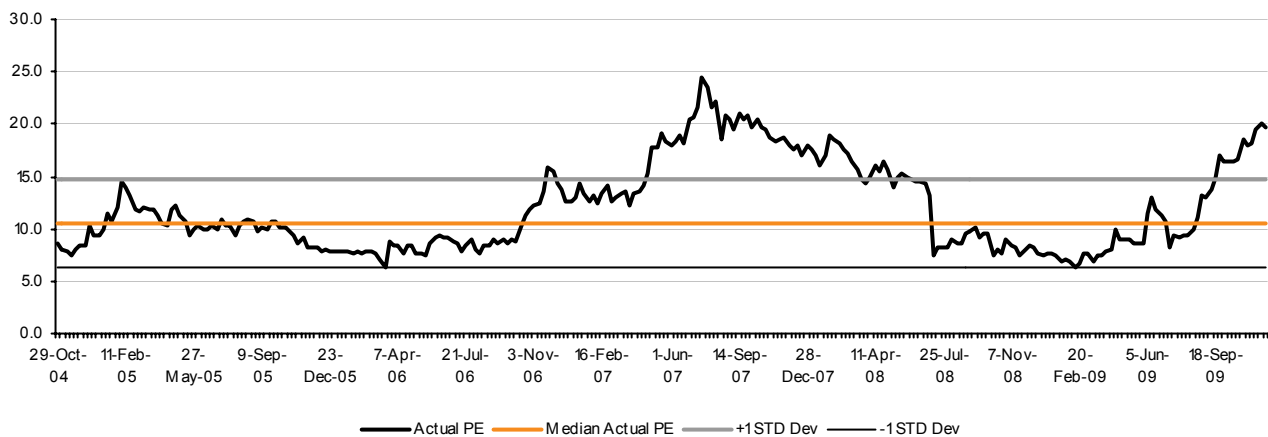
Chart 4 : MTU corporate structure



Source: Company data

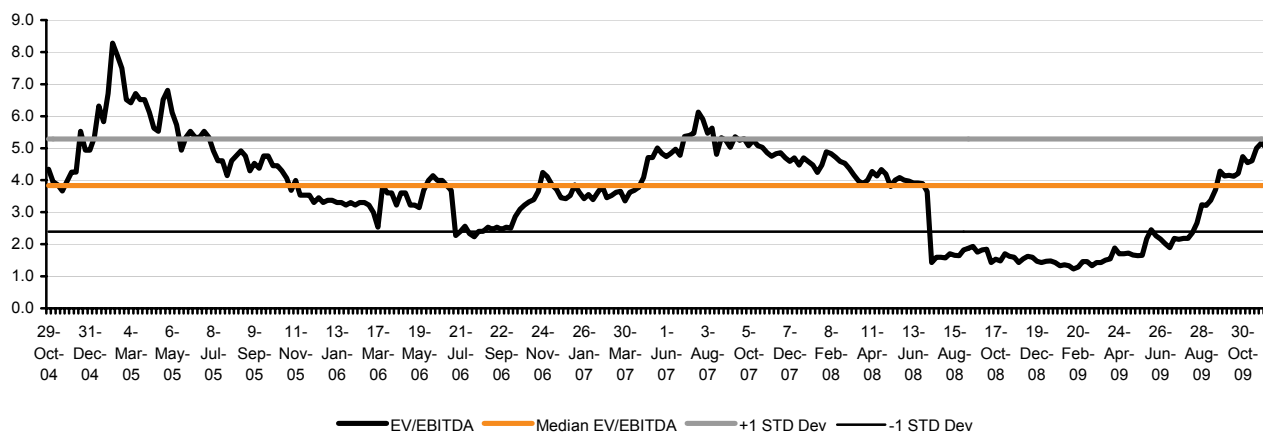
Trading history

Chart 5 : Historic PE band (long term PE of 9.0x implies fair value of A\$1.30)



Source: Company data; RBS Morgans estimates

Chart 6 : Historic EV/EBITDA (long term ev/EBITDA of 3.8x implies fair value of A\$1.34)



Source: Company data; RBS Morgans estimates

Chart 7 : Historic PE relative to ASX200 (long term 33% discount to ASX200 implies fair value PE of 10.2x or A\$0.87)

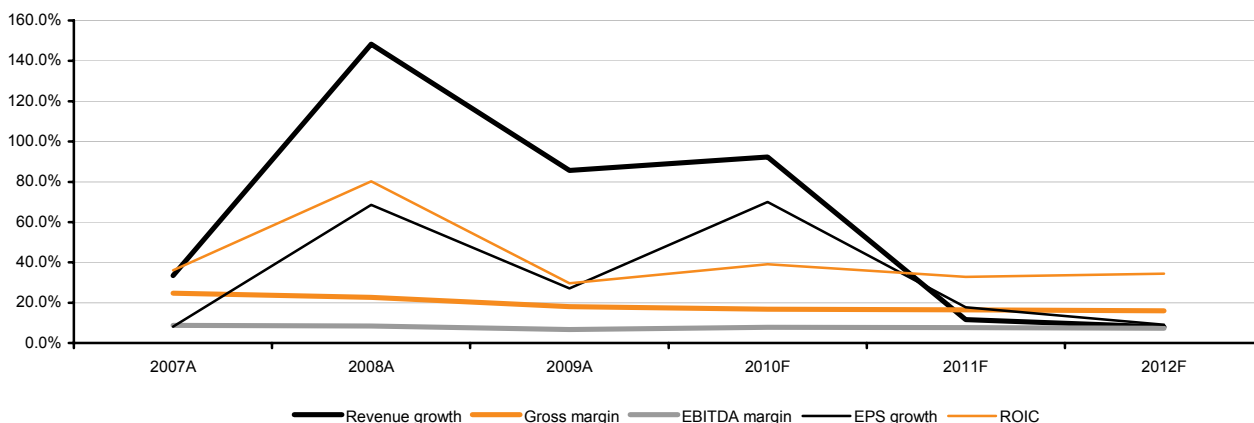


Source: Company data; RBS Morgans estimates

Financial commentary

- MTU has provided FY10 guidance for revenue of A\$370-400m; EBITDA of A\$29-31m; NPAT of A\$14.5-15.5m and EPS of 13.3-14.3cps. FY09 normalised revenue was A\$360m (assuming full year contributions from recent acquisitions) so guidance assumes underlying revenue growth of 2.8-11.1%;
- MTU has consistently delivered above average growth rates. Since 2002 its CAGR are : revenue +74.6%; EBITDA +59.0%; PBT +63.2%; NPAT +50.8%; EPS +23.7%; and DPS +28.5%;
- Our DCF is based forecasts out to 2020 which we believe are conservative. We are forecasting a 10 year revenue CAGR of 7.1%; EBITDA CAGR of 2.5%; NPAT CAGR of 4.7%; and EPS CAGR of 5.2%;
- Operating cashflow has consistently been strong, averaging 80% of EBITDA. This is consistent with what we'd expect from a healthy growing company and indicates a sound relationship between reported earnings and underlying cashflow;
- As a reseller MTU does not have an intensive capex requirement. We forecast FY10 capex of A\$2.0m which is around 0.5% of revenue. We expect capex to remain at a similar level going forward (assuming no further acquisitions);
- As at 30 June 2009 net debt was A\$9.6m (net debt/ equity of 19.7%) with 24.3x EBIT cover. We expect debt to peak in the 1H10 as MTU takes on an additional A\$10m in debt to fund payments for a deferred payment associated with the acquisition of Commander. We expect operating cashflow generated by MTU during FY10 to lower net debt to around A\$1.5m by the end of FY10. At the peak of debt levels we expect MTU's EBIT cover to remain comfortably above 10x.
- MTU's Return On Invested Capital (ROIC) was 17.4% in FY09, we expect this to increase strongly in FY10 to around 30% as the company consolidates recent acquisitions. MTU's ROIC and ROE remain comfortably ahead of our 13.5% WACC.

Chart 8 : Key trends



Source: Company data; RBS Morgans estimates

RESEARCH TEAM

ROGER LEANING	-	Executive Director - Research	SCOTT MURDOCH	-	Analyst
CHRIS BROWN	-	Senior Analyst	SCOTT POWER	-	Director - Research
NIK BURNS	-	Senior Analyst	TOM SARTOR	-	Associate Director - Research
ALEX CLARKE	-	Analyst	TAMARA STRETCH	-	Associate Director - Research
FIONA BUCHANAN	-	Director - Research	TANYA SOLOMON	-	Associate Director - Research
NICK HARRIS	-	Senior Analyst	PAUL STEVENSON	-	Analyst
MICHAEL KNOX	-	Executive Director - Economic Strategy	REBECCA SULLIVAN	-	Research/Special Projects
JAMES LAWRENCE	-	Fixed Interest Analyst	SAM TURNER	-	Analyst
JOSEPHINE LITTLE	-	Associate Director - Research	MARCEL VON PFYFFER	-	Director - Strategy
BELINDA MOORE	-	Director - Research			

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