



# M2 Telecommunications Group

## Initiation of coverage

A market leading reseller of telecommunications services to the small and medium business (SMB) market, M2 Telecommunications (MTU) will deliver record earnings for FY10 and continue a 8-year history of positive earnings growth. Looking ahead we see significant opportunity for continued double-digit organic earnings growth to be complimented by EPS accretive acquisitions.

Price: A\$1.76

Code: MTU

### Key Financial Information

Y/E June		2008A	2009A	2010F	2011F	2012F
Revenue	\$m	109.0	202.5	388.8	425.9	453.6
EBITDA	\$m	8.8	13.1	32.5	40.7	44.9
Reported NPAT	\$m	5.2	7.5	17.6	24.2	27.5
Normalised NPAT	\$m	5.3	8.3	20.3	26.9	30.2
EPS (adj)	CPS	7.2	9.4	18.0	21.9	24.6
EPS Growth	%	82.4	30.5	90.5	21.9	12.1
PER	x	24.3	18.6	9.8	8.0	7.2
EV/EBITDA	x	16.1	15.3	6.7	5.1	4.4
DPS	c	5.0	5.5	11.0	14.0	16.0
Yield	%	2.8	3.1	6.3	8.0	9.1

### Stock Data

Market Capitalisation	\$213m
Issued Capital	121.5
Volume (monthly average)	2.8m
12-month low	\$0.70
12-month high	\$1.97

### Market Data

Small Ordinaries	2339
S&P ASX 200	4449
All Ordinaries	4472

### Valuation & Pricing Data

DCF Valuation	\$2.40
EBITDA Multiple	\$2.08
PE Multiple	\$2.43
<b>12 Month price Target</b>	<b>\$2.40</b>

### Share Price Drivers

Results	↑
Acquisitions	↑
Dividends	↑
NBN	↑↓

### Market leading independent telco reseller

MTU is the largest domestic reseller of 'network independent' telecommunications services to small and medium businesses (SMB) and small / junior telco customers, supplying fixed line, mobile and data services. MTU's operations are supported by a well established distribution capability and, with scale benefits provided from recent acquisitions, the company is well positioned to expand on its current 4% share of the \$6bn SMB telecommunications market.

### \$20m placement builds acquisition war chest

The recent decision to raise \$20m suggests that MTU is looking to make further acquisitions. In the absence of any major acquisition we feel MTU will continue to make EPS accretive 'bolt-on' purchases as represented by the recent acquisition of Clever Communications (ASX: CVA) small business assets for \$5m, which represents an effective acquisition multiple of 2.2x EBITDA.

### Strong earnings history and outlook

Having delivered earnings growth at a CAGR of 29% from 2004 - 2009, 1H10 adjusted EPS grew by 118% on the pcp to 8.7cps, underpinned by recent acquisitions in People Telecom and the telecoms business assets of Commander Communications. We expect the strong earnings momentum to continue, with FY10 EPS (adj.) of 18.0cps and FY11 EPS (adj.) of 21.9cps representing earnings growth of 90.5% and 21.9% respectively.

### Recommendation:

We rate MTU as an attractive investment trading on a FY10 PER of 9.8x and FY11 PER of 8.0x which represents a 36.4% discount to our DCF valuation of \$2.40 per share. In addition to the 5.0c interim dividend, we are expecting a 6.0c final dividend taking the full year dividend to 11.0cps. This implies a yield of 6.3% and should provide support to the stock at current levels.

**Note:** MTU is currently in the final stages of due diligence in respect of an acquisition of certain business assets of a reseller of telecommunications services. Consideration for the acquisition is expected to be \$4m in cash. The pending acquisition is NOT included in our current estimates.

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## EXECUTIVE SUMMARY

Established in 1999 and listing on the ASX in April 2004, MTU has established itself as the largest domestic reseller of telecommunications, which includes fixed line, mobile and data services, to the small and medium business (SMB) market and small / junior telco customers in Australia and retail customers in New Zealand.

In Australia, the telecommunications market is estimated at \$39bn for 2010, a figure which has remained largely static for the past 5-years. Of this, the SMB segment represents approximately 15% or \$6bn per annum. The market consists of 5 major network owners, approximately 90 partial network owners and + 500 resellers. The reseller market is highly fragmented with MTU wholesaling telecommunication services to 200+ small / junior resellers.

**Table 1: Domestic Telecommunications Industry – Service providers**

Net work owners	Partial Network owners	Network Re-sellers
Full network infrastructure	Partial network infrastructure	Minimal network infrastructure
Eg Telstra, Optus, Vodaphone	Eg AAPT, iiNet, Amcom, TPG	Eg. M2 Telecom

MTU's competitive advantage centres on providing a value-add and tailored telecommunications solution to SMB's with a service offering unmatched by major network providers who typically focus on the mass market consumer, government and corporate markets where significant economies of scale exist.

While being the largest domestic reseller, MTU holds a relatively modest 1% of the total telecommunications market and 4% of the SMB segment. We believe MTU has considerable opportunity to grow market share at the expense of Telstra, which holds 80%+ market share of the SMB segment.

### National Broadband (NBN) Company

If as intended NBN Co operates as a monopolistic supplier of wholesale telecommunications services, then MTU will look to source supply of telecommunications services on an arms length basis from NBN Co resulting in little change to their existing business model that currently sources wholesale telecommunications services from full network owners.

Looking ahead, and while completion of the NBN build is expected to be up to 8-years, we do envisage positives emerging from a smooth and cost effective NBN roll-out, which is expected to drive demand for telecommunications services in Australia. We also anticipate that while technological advances can be expected to put pressure on the profitability for traditional telecommunications services, increased demand and supply of telecommunications is likely to drive absolute profits.

### Strong earnings outlook

MTU delivered a strong 1H10 result with revenue growth of 115% driving EBITDA and adjusted EPS growth 150% and of 118% respectively. 1H10 reported EBITDA of \$15.3m included one-off costs of approximately \$1.0m which are expected to provide annualised operational cost benefits of \$0.5m p.a.

*People Telecom & Commander acquisitions have driven a significant step change in MTU earnings*

Based on continued margin expansion and the EPS accretive acquisition of Clever Communications small business assets, we forecast FY10 EPS (adj) of 18.0cps and FY11 EPS (adj) of 21.9cps representing earnings growth of 90.5% and 21.9% respectively.



# COMPANY OVERVIEW

## BACKGROUND

Operating as a ‘network independent’ reseller means that MTU is able to deliver fixed line, mobile and data services under its own brands using the infrastructure of multiple network owners for reselling to retail end users or wholesaling to smaller resellers.

Major network owners, Telstra (fixed line and broadband) and Optus (mobile and wireless broadband), are MTU’s major wholesale suppliers of telecommunications services, while for their fledging New Zealand operations, MTU sources supply from Vodafone (NZ) and Telecom NZ.

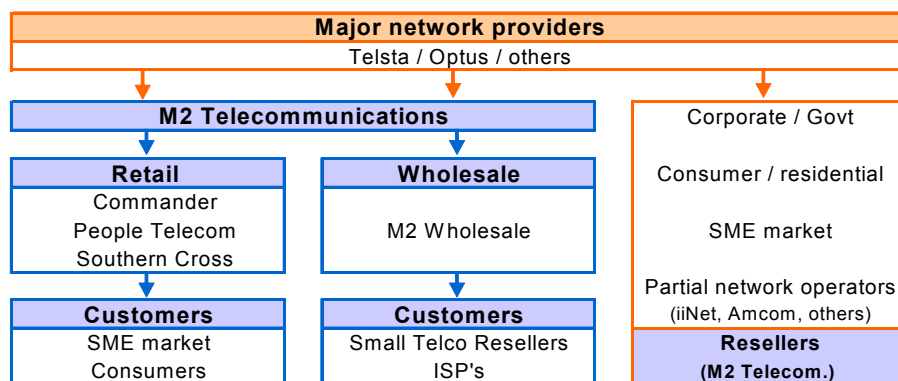
As a reseller of wholesale telecommunications services MTU does not own any significant infrastructure assets, instead differentiating themselves in the market with a ‘value-add’ telecommunications proposition tailored specifically to clients needs and supported with a high level of ongoing customer support and service.

Targeting the small and medium business (SMB) market, MTU distributes directly through its retail operations (Commander, People Telecom & Southern Cross Telco) and indirectly through its M2 Wholesale operations to 200+ small / junior telco resellers.

*M2 Wholesale provides wholesale carriage access to +200 small / junior telco resellers*

MTU’s offering is underpinned by a distribution network of 500+ exclusive individuals operating predominantly under the People Telecom and Commander brands. Distribution is supported by customer service centres in Hobart and Adelaide.

Figure 1: MTU business model and industry position



Source: Company reports

### Small & Medium Business (SMB) market focus

The SMB market for telecommunication services is estimated at \$6bn with Telstra holding an estimated 80%+ market share. Telstra’s dominant position is a legacy of being the ‘default’ telecommunications provider.

The SMB market dynamics provide a logical and attractive opportunity for MTU given:

- large network owners are focused on the mass market residential, corporate and government sectors where economies of scale exist;
- the interest of major network owners are aligned with MTU who effectively take on an agency / customer relationship in expanding network owners wholesale distribution;
- MTU currently has a modest 4% of the SMB market providing significant scope for market share gains, while being able to remain selective in targeting new clients; and
- MTU is the largest independent reseller of telecommunication services domestically providing scale and distribution advantages over smaller / junior telco resellers.



## M2 RETAIL

MTU's foundation business operated under the 'M2 Telecom' brand before recent acquisitions of People Telecom (April '09) and Commander (June '09). These acquisitions resulted in a multi-brand strategy being implemented that now includes Commander, People Telecom and Southern Cross Telco (acquired as part of Orion acquisition in October 2007), with 'M2 Telecom' remaining largely a legacy brand.

*People Telecom and Commander represent two high profile and well recognised consumer brands*

MTU also operates two online consumer brands in Simply Mobiles ([www.simplymobiles.com.au](http://www.simplymobiles.com.au)) and Green Mobiles ([www.greenmobiles.com.au](http://www.greenmobiles.com.au)).

**Table 2: M2 Retail Brands profile**

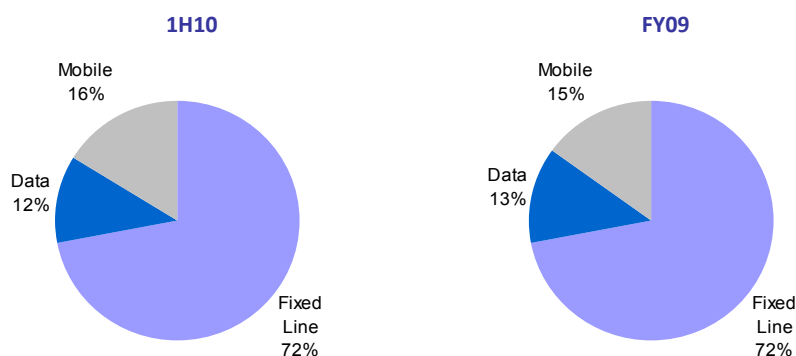
Brand	Target market	Business offering & market
<b>Commander</b>	SMB's and small corporates typically in change mode.	<ul style="list-style-type: none"> <li>Established and reputable brand that bundles telecommunications services and equipment to provide an 'end to end' telco solution.</li> <li>Distribution via 36 independent &amp; territory allocated dealerships selling MTU approved products.</li> </ul>
<b>People Telecom</b>	SMB's with tailored telecommunications solutions.	<ul style="list-style-type: none"> <li>'Challenger' brand to major telco's, offering a customised and tailored telecom solution.</li> <li>National sales channel and independent dealership network.</li> </ul>
<b>Southern Cross</b>	Small office / home office (SOHO) and residential – regional focus.	<ul style="list-style-type: none"> <li>Offering includes a full suite of telecommunication services to consumers and SOHO operations.</li> </ul>

Source: Company reports

### Product mix

Key products include fixed line voice, 3G mobile voice & broadband, ADSL (1 & 2) broadband and corporate VIP services. Fixed line telecommunications services represent the largest and most important telecommunications requirement for SMB's with few cost effective and functional alternatives to fixed line.

**Chart 1: Retail revenue splits**



Source: Company reports



## M2 Retail acquisition history

The People Telecom and Commander acquisitions represented a significant step change for MTU that resulted in revenues doubling to an annualised run rate of \$250m p.a.

More recently, MTU acquired Clever Communications small business assets (Clever Communications) for up to \$5m which represents an acquisition multiple of 2.3x maintainable EBITDA on revenues of \$8m. The attractive acquisition metrics reflecting MTU's significant scale advantage over smaller competitors.

*Clever Communications was acquired for an upfront payment of \$3.75m and a deferred payment of \$1.25m (less adjustments)*

It is expected the Clever Communications brand and distribution capability will be absorbed into the People Telecom operations going forward.

**Table 3: Recent acquisition history – M2 Retail**

Business	Consideration	Metrics	Comments
<b>People Telecom</b>	\$19.4m (inc 28.6m shares @ \$0.60/share & \$2m in cash).	3.2x identifiable EBITDA.	<ul style="list-style-type: none"> <li>A direct competitor that was acquired via a Scheme of Arrangement. People Telecom has expanded the MTU dealership network and established a stronger presence in NSW.</li> <li>The increased revenue base has provided operational synergies, while cost benefits are being realised in the wholesale sourcing of 'telco' services from network owners.</li> <li>Guidance was for the transaction to be 15 - 20% EPS accretive.</li> </ul>
<b>Commander</b>	\$24.4m including inventory and stock.	Approximately 3x maintainable NPAT.	<ul style="list-style-type: none"> <li>Under administration, MTU acquired the telecoms business assets and IP from Commander Communications which provided MTU with another established SMB brand and distribution capability</li> <li>MTU converted Commander's national franchise model into a national dealership model of 36 locations with dealers responsible for hardware sales and inventory on MTU approved products.</li> <li>Dealers cross-sell telco services to customers.</li> <li>Generates hardware inertia rental streams from hardware rentals.</li> <li>Guidance was for the transaction to be +50% EPS accretive.</li> </ul>
<b>Clever Communications</b>	Up to \$5m in cash with \$1.25m deferred (less adjustments).	2.2x maintainable EBITDA.	<ul style="list-style-type: none"> <li>Extended MTU customer base and distribution capability. The attractive acquisition multiple reflective of MTU's existing scale and significant competitive advantage in accessing wholesale telecommunications.</li> <li>We estimate the transaction to be +5% EPS accretive to FY11 earnings.</li> </ul>

Source: Company reports

### Key benefits of expanded retail offering:

- **Cross selling** - Currently 70% of Commander SMB customers do not source their telco services from MTU, providing a significant cross selling opportunity.
- **Rental revenues** - MTU gains the rental revenues stream from financed purchases for Commander hardware and equipment on expiration or completion of the initial contract term. This is as a result of equipment automatically reverting to a rental scheme on the retention of the equipment by the customer, which is commonly the case for a period of 1 -2 years beyond the life of the contract.
- **Scale** - A key competitive advantage in the reseller market and MTU is well positioned to leverage its existing operations with highly accretive bolt-on acquisitions, which should enable MTU to continue to purchase telecommunication services at cheaper rates from suppliers and better rates than competitors.



## Segmented results

Segmented NPAT (pre-unalloc.) lifted by 474% to \$9.4m as the impact of the People Telecom and Commander acquisitions took effect.

We estimate that the \$1.0m in one-off costs (pre-tax) were attributable to the retail operations, which are reflected in the segmented result.

**Table 4: 1H10 Retail interim results**

(\$m) - unless stated	1H09	1H10	Comment
Revenues			
External customers	27.3	114.9	
Intercompany sales		21.3	
<b>Total revenues</b>	<b>27.3</b>	<b>136.4</b>	<i>Impact of acquisitions</i>
<b>NPAT – reported<sup>1</sup></b>	<b>1.6</b>	<b>9.4</b>	<i>Acquisitions, synergies &amp; pre one-off charges</i>
<b>Margins – reported<sup>1</sup></b>	5.9%	6.7%	

Source: Company reports / 1. Pre unallocated corporate overheads

## M2 WHOLESALE

M2 Wholesale supplies wholesale telecommunications services to 200+ small and medium sized telecommunications and Internet Service Providers (ISP's).

Smaller telco providers typically focus on servicing niche markets which include regional, industry or ethnic markets which are too small to negotiate favourable wholesale arrangements directly with major network owners.

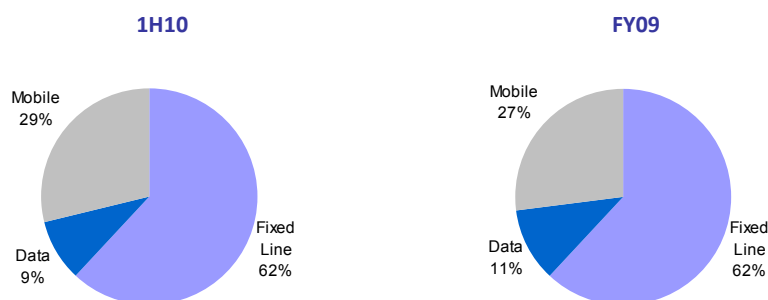
M2 Wholesale was established in mid 2006 following the company's appointment by Optus as its exclusively endorsed Mobile Virtual Network Enabler (MVNE) of Optus mobile 3G services, meaning that MTU can enable mobile resellers to offer services to end-user customers. This arrangement with Optus was recently extended to 2013.

### Product mix

Sell through of wholesale telecommunications services is largely reflective of the retail revenues splits, with a larger mobile representation a result of MTU's exclusive enabling arrangement with Optus (as above).

At an operational level, MTU wholesale is run independently of the retail operations; however scale benefits do emerge across the group in the sourcing of wholesale supply of telecommunications services from network owners.

**Chart 2: Wholesale revenue splits**



Source: Company reports



## M2 Wholesale acquisition history

The Optus arrangement was supported by the acquisitions of Wholesale Communications Group in May 2007 and Unitel Australia in February 2008.

From a standing start in 2006 M2 Wholesale will generate revenues of \$130m for FY10 of which approximately 50% are applicable to acquisitions and 50% organic.

**Table 5: Recent acquisition history – M2 Wholesale**

Business	Consideration	Metrics	Comments
<b>Wholesale Communications Group (WCG)</b>	\$3.3m being a combination of cash, equity and assumption of debt.	3.7x maintainable NPAT.	<ul style="list-style-type: none"> <li>Acquired 100% of WCG which was the largest independent wholesaler of telecommunications services providing a range of wholesale data and voice services to over 200 domestic ISP's.</li> <li>Guidance was for the transaction to be +30% EPS accretive.</li> </ul>
<b>Unitel Australia</b>	\$10.6m in cash and up to \$2.5m deferred over 36 months.	Approximately 3x maintainable NPAT.	<ul style="list-style-type: none"> <li>Acquired from Commander Communications (ASX: CDR), Unitel provided MTU Wholesale with fixed line / local access wholesale services. Unitel provided recurring revenues of \$36m.</li> <li>Guidance was for the transaction to be +50% EPS accretive.</li> </ul>

Source: Company reports

## Segmented results 1H10

Segmented NPAT (pre-unalloc.) fell by 41% to \$1.3m largely as a result of an adverse reallocation of overhead costs in favour of retail operations.

Additionally, a change in the accounting treatment of commissions has resulted in \$0.8m of commissions being deferred in 1H10 that would have been recognised in the pcp.

Although generating skinny margins, M2 Wholesale assists in providing group wide pricing benefits in the sourcing supply of telecommunications services, in addition to low risk incremental sales from new client generation.

**Table 6: 1H10 Wholesale interim results**

(\$m) - unless stated	1H09	1H10	Comment
Revenues			
External customers	59.8	72.8	
Intercompany sales	0.3	1.4	
<b>Total revenues</b>	<b>60.1</b>	<b>74.1</b>	
<b>NPAT – reported<sup>1</sup></b>	<b>2.2</b>	<b>1.3</b>	<i>Adjustments and accounting changes impacting</i>
<b>Margins – reported<sup>1</sup></b>	<b>3.7%</b>	<b>1.8%</b>	

Source: Company reports / 1. Pre unallocated corporate overheads



## INTERIM RESULTS – MTU

MTU delivered a strong 1H10 result with revenue growth of 115% being driven by new revenues from People Telecom and Commander. We estimate comparable revenues remained flat on the pcp.

Reported EBITDA growth of 150% which, based on our assumptions, was driven by a \$10m contribution from People Telecom and Commander which included applicable scale benefits.

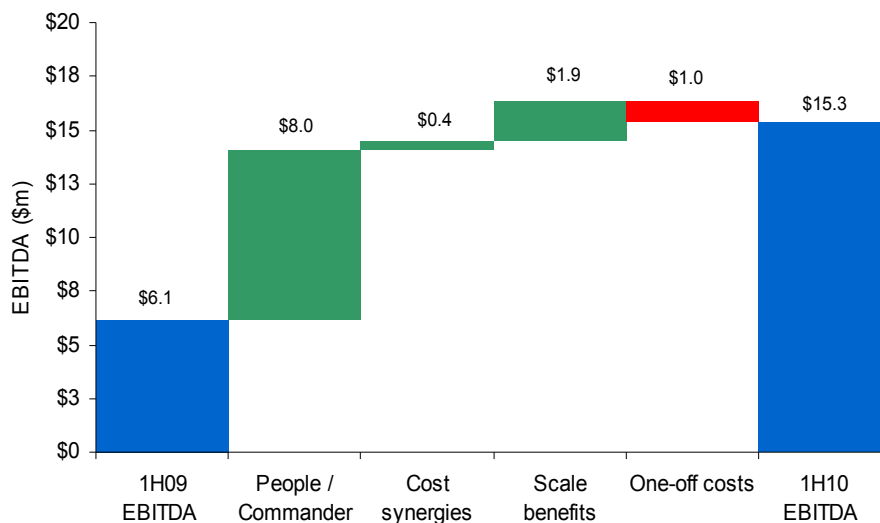
We note that reported EBITDA of \$15.3m includes one-off costs of up to \$1m which will provide an estimated \$0.5m in ongoing cost benefits, with around \$0.4m realised in 1H10.

**Table 7: MTU interim results summary**

(\$m) – unless stated	1H09	1H10	Comment
Revenues			
- M2 comparable	87.1	87.0	<i>Marginally down on a comparable basis</i>
- People / Commander		100.7	<i>Key focus for new revenue growth</i>
<b>Total revenues</b>	<b>87.3</b>	<b>187.7</b>	<b><i>Providing scale benefits</i></b>
EBITDA	6.1	15.3	<i>Excludes one-off costs</i>
EBITDA (%)	6.9	8.1	<i>Scale &amp; cost efficiencies</i>
NPAT	3.2	8.2	
NPAT adjusted	3.2	9.6	<i>Record result</i>
EPS (c) adjusted	4.0	8.7	
EPS Δ (%) adjusted	33.0	118.0	<i>EPS growth momentum continues</i>
Dividend (c)	2.5	5.0	<i>Payout ratio 67% of basic EPS of 7.5cps</i>

Source: Company reports and Balnave Securities estimates

**Chart 3: EBITDA bridge 1H09 – 1H10**



Source: Company reports and Balnave Securities estimates



## SWOT ANALYSIS

### Strengths

- **Niche market player** – targeting the SMB sector, an area that does not get the focus from the larger telcos. MTU is holding only a modest 4% market and therefore there is significant scope for organic growth.
- **Scale** – as the largest reseller of telco services, MTU's scale and distribution capability represents a clear competitive advantage in new business generation and retention.
- **Balance sheet** – the recent \$20m capital raising has left MTU in a positive net cash position, with significant opportunities for acquisitive growth.
- **Minimal infrastructure** – MTU operates with minimal infrastructure allowing funds to be retained for future growth opportunities and/ or returned to shareholders.

### Opportunities

- **Aggregation** – operating in a highly fragmented industry, MTU is well positioned to further leverage its established cost base and distribution capability through acquisitions.
- **NBN Co.** – assuming a competitive wholesaling market remains, then MTU is likely to benefit from the availability of increased services and the convergence of data and telecommunications delivery.
- **Cross selling** – the ability to broaden the distribution capability (Commander & People Telecom) is allowing MTU the capacity to generate new, low risk incremental sales.

### Weaknesses

- **Concentrated market** – MTU's client based is heavily skewed to the small & medium business market which can be highly sensitive to economic conditions. We understand MTU mitigates any customer business risk with appropriate security measures.
- **Acquisition risk** – as with any consolidation play each new vendor potentially provides a unique set of challenges that may or may not be overcome.
- **Key man risk** – current CEO, Vaughan Bowen, has been in the role since MTU was founded and we see his role as significant to MTU's future success.

### Threats

- **Margins** – increased emphasis on the SMB market by competitors, including network owners, may force pricing pressure to retain customers.
- **Diminishing fixed line usage** – while apparent in consumer and corporate markets, fixed line telecommunication remains as a core requirement of SMB's with mobile representing the only alternative currently. Longer-term capacity constraints on mobile networks will necessitate that wired and mobile will co-exist.
- **Convergence of communications** – a move towards digital technology is likely to see the convergence of telecommunications and data supply, meaning MTU needs to ensure its communications offering remains relevant to its customer's requirements, particularly as new entrants look to enter the market.



## FINANCIAL ANALYSIS AND FORECASTS

We forecast FY10 EPS (adj) of 18.0cps and FY11 EPS (adj) of 21.9cps representing earnings growth of 90.5% and 21.9% respectively.

### FY10 assumptions and forecasts:

FY10 revenues to lift by 92% to \$388.8m representing the mid-point of company guidance for FY10 revenues of \$380 - \$400m. The strong revenue growth driven by the People Telecom and Commander acquisitions.

We forecast FY10 EBITDA margins to lift to 8.4%, from 6.5% in the pcp. The margin increase is expected to be driven by a 92% increase in revenues, which is providing MTU with scale benefits in cheaper buying of wholesale telco services, in addition to operational cost synergies being realised.

Our forecasts for FY10 EBITDA of \$32.5m, representing a 148.5% increase on the pcp. This includes one-off costs of up to \$2m which will provide an estimated \$1m in ongoing cost benefits, with an estimated \$0.8m being realised in FY10.

### FY11 assumptions and forecasts:

Revenue growth of 9.6% which includes underlying growth of 7.5%, before the impact of the Clever Communications acquisition.

EBITDA margins are forecast to lift to 9.6%, from 8.4% in the pcp. Our assumptions on margin expansion driven by the full impact of scale and cost benefits achieved in FY10, in addition to the Clever Communications acquisition which will deliver expected FY11 EBITDA of \$2.3m on revenues of \$8m, representing incremental EBITDA margins of 28%, which is reflective of margins achievable on incremental, organic sales growth.

Our forecast for FY11 EBITDA of \$40.7m represents 25.3% growth, including underlying EBITDA growth (excluding Clever Communications) of 18.5%.

*Note: Our FY11 forecasts exclude the impact of a pending 'bolt-on' acquisition announced on the 18th of May 2010 which is expected to cost \$4m in cash.*

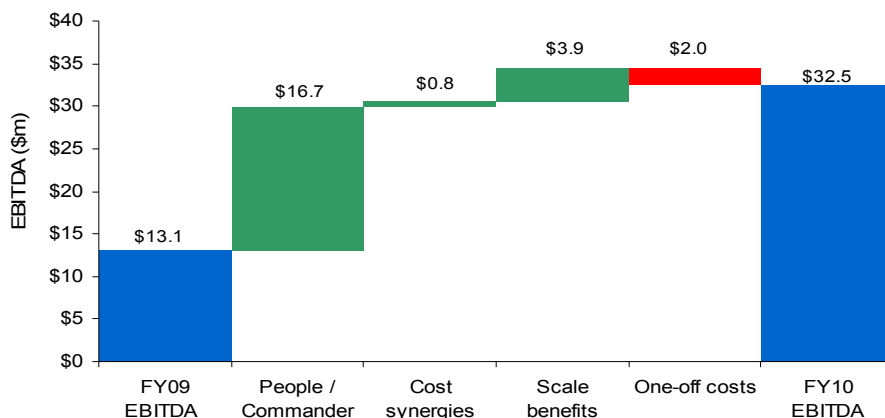
**Table 8: Interim results summary**

(\$m) – unless stated	FY09	1H10	2H10	FY10	Comment	FY11
<b>Revenues</b>						
- M2	202.5	187.7	201.1	388.8	Mid point of guidance – 2H stronger	417.9
- Clever Communications						8.0
Total revenues	202.5	187.7	201.1	388.8		425.9
<b>EBITDA</b>						
- M2	13.1	15.3	17.2	32.5		38.4
- Clever Communications	-	-	-	-		2.3
Total EBITDA	13.1	15.3	17.2	32.5	Excludes one-off redundancy costs	40.7
EBITDA margins	6.5%	8.1%	8.6%	8.4%	2H10 margin expansion – upside exists	9.6%
EBIT	11.0	12.6	14.6	27.2		35.1
NPAT	7.5	8.2	9.4	17.6		24.2
NPAT adjusted	8.3	9.6	10.7	20.3	Adjusted amort of customer contracts	26.9
EPS (c) adjusted	9.4	8.7	9.3	18.0		21.9
EPS Δ adjusted	30.5%	118.0%	73.5%	90.5%		21.9%
Dividend (c)	5.5	5.0	6.0	11.0	In-line with guidance for a 70% pay-out ratio	14.0

Source: Company reports and Balnave Securities estimates



Chart 4: EBITDA bridge FY09 – FY10



Source: Company reports and Balnave Securities estimates

**\$20m Placement.** The impact of the \$20 placement is dilutionary to EPS, but provides significant firepower for EPS accretive acquisitions going forward.

Table 9: EPS impact of \$20m placement

	FY11F			FY12F		
	Pre \$20m	Post \$20	% Δ	Pre \$20m	Post \$20	% Δ
NPAT adj.	25.9	26.9	3.9	28.9	30.2	4.1
EFPOWA	109.8	122.8	11.7	109.8	122.8	11.7
EPS adj.	23.6	21.9	(6.9)	26.3	24.6	(6.5)

Source: Company reports and Balnave Securities estimates

**Other key financial considerations:**

**Capex** - Maintainable capex of \$1.0m p.a. with the likelihood of up to an additional \$2-3m p.a. over the next 2-years for the implementation of a new uniform billing and service system.

**Deferred consideration** - Deferred consideration of \$11m was paid in 1H10. In the 2H10 \$3.75m represents the initial consideration for Clever Communications, with an additional \$1.25m (less adjustments) deferred. For FY11 deferred consideration payments are currently estimated at \$3.4m.

**Intangibles** - The balance sheet has approximately \$70m of intangibles of which a component relating to the cost of acquiring customer contracts is required to be amortised over 3 years at a rate of approximately \$2.7m p.a.

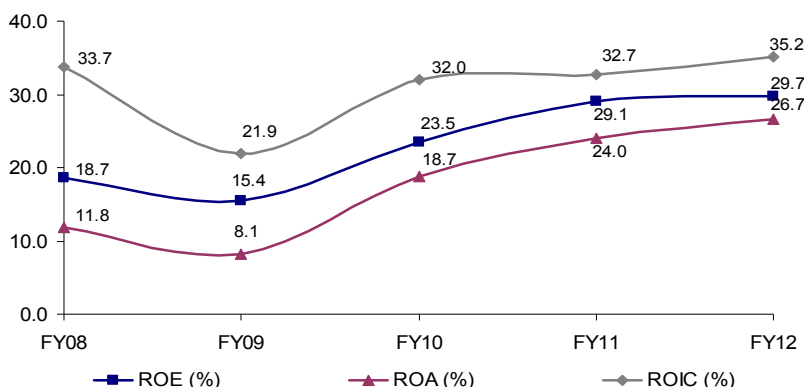
**Net Gearing** - Estimated at a negligible 10% post the \$20m placement.

**Profitability metrics improving**

We forecast a strong rebound in key profitability metrics in FY10 as the company benefits from the acquisitions of People Telecom and Commander made late in FY09.

Both ROIC and ROE metrics are significantly ahead of our estimated WACC of 14.3%.

Chart 5: Forecast profitability metrics



Source: Company reports and Balnave Securities estimates



# INDUSTRY – TELECOMMUNICATIONS MARKET

## INDUSTRY STRUCTURE

The telecommunications industry can be broken into three broad categories, which include:

**Table 10: Domestic Telecommunications Industry – Service providers**

Net work owners	Partial Network owners	Network re-sellers
Full network infrastructure	Partial network infrastructure	Minimal network infrastructure
Eg Telstra, Optus, Vodaphone	Eg AAPT, iiNet, Amcom, TPG	Eg. M2 Telecom, Comtel

Source: Company reports and Balnave Securities

**Network owners** – companies with a full end-to-end network infrastructure (such as wire, cable, fibre or mobile network infrastructure). Network owners include Telstra, Optus, Vodaphone (NZ) and Telecom (NZ). Full network owners operate both retail and wholesale operations, and wholesale to partial network owners and resellers.

**Partial network owners** – companies with partial network infrastructure required to deliver services to their customers (such as DSLAM’s for broadband data or fixed line voice switches). Partial network owners include AAPT, Primus, iiNet, Amcom and TPG Telecom amongst others.

*Partial network owners typically focussed on providing data communications*

**Resellers.** Typically ‘network independent’ and with minimal or no infrastructure, however some network owners will on occasion also use competitor’s services to deliver their product. E.g. Optus selling Telstra products.

### SMALL & MEDIUM BUSINESS (SMB) MARKET - \$6bn p.a.

The telecommunication market in Australia is estimated at \$39bn for 2010, a figure which has remained largely static for the past 5-years. The market is highly concentrated between Telstra (47.6% market share), Optus (21.8% market share) and the combined Vodaphone Hutchinson (12.5% market share).

*Total telecommunications market valued @ \$39bn*

The SMB market for fixed line, mobile and data telecommunications is estimated at \$6bn p.a. and is dominated by Telstra with a market share estimated at +80%. Telstra’s dominance reflecting a legacy of being users ‘default’ telecommunications provider, while many users typically have an apathetic view towards changing their telecommunications services provider.

*The SMB telecommunications market valued @ \$6bn*

The main competitors to MTU in the SMB market include:

- **Telstra.** Dominant market position with a large independent network of PABX resellers and the largest network supplier to resellers;
- **Optus.** Services predominantly consumer through Optus World store networks. Wholesale network supplier to resellers of mobile services with MTU currently their exclusively endorsed aggregator of services and products on the Optus 3G network to smaller telco providers;
- **Primus.** Limited field presence and dealership channels negligible into SMB market;
- **AAPT.** Undertakes significant promotional activity to SMB market, however has limited field presence into SMB market; and
- **Vodafone/ Hutchinson.** No fixed line proposition which limits their relevance to SMB’s.



## THE NATIONAL BROADBAND NETWORK (NBN)

The government has legislated to build a \$43bn, 100 megabits per second (Mbps) fibre-to-the-home (FTTH) NBN to cover 90% of the Australian population, with the remaining 10% to receive 12 Mbps connectivity using the latest wireless and satellite technologies.

The intention is for NBN Co. to be 51% government owned for the build period and act as a monopolistic wholesale entity. NBN Co will offer wholesale network access and capacity to carriers and service providers and will not provide any content of its own, unless the minister deems it viable to provide direct retail services where appropriate. This exception is designed to provide the NBN Co. some flexibility in providing services directly to end users such as government agencies. The intention is however for retail service providers being those providers with direct customer and end user relationships to provider services at the retail level.

The cost of the NBN build could be less than the flagged \$43bn if the existing fibre owning organisations, including telco's, hand over their fibre assets to NBN Co. Further to that, legislation allows for NBN Co. to acquire existing telco's that may be of strategic benefit to the early roll-out of the NBN, even those owning retail businesses. The potential for NBN Co' to acquire established telco's will be significant in driving ongoing consolidation in the second tier telecommunications market with partial network owners, which includes ASX listed iiNet, Amcom and TPG Telecom, being obvious targets given their established value add infrastructure capabilities.

*TPG has recently acquired a 5% stake in Amcom*

A cost effective build of the NBN should ensure competitive pricing of FTTH services and ensure infrastructure based competition is maximised to the benefit of consumers and business. However an optimal outcome is significantly dependant on a cooperative Telstra to ensure a smooth transition of users from its soon to be superseded PSTN to the new NBN FTTH.

A smooth NBN build and roll-out, combined with the 4G network, will provide the opportunity to access and deliver 100+ Mbps of both fixed and mobile connectivity will present significant opportunities for telecommunications companies to benefit from higher internet usage.



# VALUATION

## Discounted Cashflow

We derive a \$2.40 per share valuation for MTU based on a DCF valuation methodology.

Our DCF valuation for MTU represents a 36.4% premium to the current market price.

A \$2.40 per share valuation also implies a forecast FY11 PER of 10.5x and an EV/EBITDA multiple of 6.8x.

Our forecasts reflect the earnings assumptions discussed in the previous section and are detailed below along with our key valuation assumptions.

Table 12: DCF valuation assumptions

DCF Valuation		2009A	2010F	2011F	2012F	→	2020F
EBIT	\$m	11.0	27.2	35.1	39.1	→	54.0
Depreciation & Amortisation	\$m	2.1	5.3	5.6	5.8	→	7.0
Change in working capital	\$m	(1.0)	3.3	4.9	0.7	→	1.3
Capital / investment expenditure	\$m	(10.7)	(18.3)	(6.4)	(2.5)	→	(1.5)
less Tax	\$m	(3.0)	(7.5)	(10.3)	(11.8)	→	(19.7)
Total Free Cash Flow	\$m	(1.6)	10.0	28.8	31.4	→	41.8
Net Present Value	\$m	297.2					
Less: net Debt	\$m	(5.0)					
Equity present value		292.2					
<b>Per Share</b>	<b>\$</b>	<b>2.40</b>					
<b>WACC Assumptions</b>							
Cost of Equity	%	14.9					
Risk Free Rate	%	6.0					
Beta		1.5					
Market Risk Premium	%	6.0					
Cost of Debt	%	7.5					
Source: Balnave Securities							



## Peer Comparison

In establishing a relevant peer group to MTU, we have included a number of ASX listed companies operating as resellers or partial network owners which includes:

**TPG Telecom (ASX: TPM; Mkt Cap \$1.7bn).** A leading provider of internet, voice and data services to residential users, SMB's and corporate/ govt customers in Australia. TPG provides these services under the well established brands in TPG, Soul and Chariot.

**IINet (ASX: IIN; Mkt Cap \$427m).** iiNet is Australia's 3rd largest ISP servicing retail and SMB customers. As a partial network owner IIN owns their own backhaul infrastructure, while reliant on Telstra's copper network to provide the "last mile" to the end user.

**Amcom (ASX: AMM; Mkt Cap \$251m).** Amcom is a partial network owner providing fibre-based telecommunications high speed data connectivity to large corporates, government departments and ISP's through the establishment and ownership of their own fibre networks.

**Data3 (ASX: DTL). Mkt Cap \$125m.** Data3 is a national information and communication technology solution company providing IT solutions through Software Licensing Solutions, Infrastructure Solutions and Recruitment Solutions to align clients' technology and business strategies.

Table 13: MTU peer comparison table

Comparison	EV/EBITDA (x)		PER (x)		EPS Growth (%)	
	FY10F	FY011F	FY10F	FY011F	FY10F	FY011F
MTU – M2 Telecommunications	6.7	5.1	9.8	8.0	90.5	21.9
AMM – Amcom Telecommunications	9.8	7.4	13.9	10.0	(17.3)	39.1
TPM – TPG Telecom	8.8	6.1	19.7	13.5	73.9	45.9
IIN – iiNet	5.1	4.2	12.2	9.5	18.4	27.7
DTL – Data 3	7.8	7.1	11.5	10.5	0.5	9.5
<b>Average</b>	<b>7.9</b>	<b>6.2</b>	<b>14.3</b>	<b>10.9</b>	<b>18.9</b>	<b>30.6</b>
MTU - (Discount)/Premium	(18.0)	(21.2)	(45.9)	(36.3)	378.8	(39.7)

Source: Balnave Securities and Consensus Estimates



# FINANCIALS SUMMARY

M2 Telecommunications Group	Price	\$ 1.76			
	Market Cap	\$ 213.8			Year end 30 June
<b>Profit &amp; Loss (\$m)</b>	<b>2009A</b>	<b>2010F</b>	<b>2011F</b>	<b>2012F</b>	
Sales Revenue	202.5	388.8	425.9	453.6	
EBITDA	13.1	32.5	40.7	44.9	
Depn & Amort	1.3	2.6	2.8	3.1	
Amort - Identifiable Intangibles	0.8	2.7	2.7	2.7	
EBIT	11.0	27.2	35.1	39.1	
Net Interest Expense	-0.5	-2.1	-0.6	0.1	
NPBT	10.5	25.1	34.6	39.2	
Tax expense	-3.0	-7.5	-10.3	-11.7	
NPAT - reported	7.5	17.6	24.2	27.5	
NPAT - Pre Amort Intangibles	8.3	20.3	26.9	30.2	
+/- Significant Items	0.0	0.0	0.0	0.0	
Underlying NPAT - Pre-Amort	8.3	20.3	26.9	30.2	
<b>Cash Flow (\$m)</b>	<b>2009A</b>	<b>2010F</b>	<b>2011F</b>	<b>2012F</b>	
Operating EBITDA	13.1	32.5	40.7	44.9	
- Interest & Tax Paid	3.5	9.6	10.9	11.6	
+/- change in Work. Cap.	-1.0	3.3	4.9	0.7	
- other	-0.5	12.0	0.6	3.4	
Operating Cashflow	9.1	14.1	34.0	30.6	
- Capex	-0.9	-3.0	-3.0	-2.5	
- other	0.0	-15.3	-3.4	0.0	
- equity	-9.7	0.0	0.0	0.0	
Free Cashflow	-1.6	-4.1	27.6	28.1	
- Ord Dividends	-4.3	-12.7	-15.8	-18.2	
- Equity /other	0.5	21.3	0.0	0.0	
Net Cashflow	-5.4	4.5	11.8	9.9	
Cash at beginning of period	6.9	6.7	5.2	6.8	
+/- borrowings / other	6.0	-6.0	-10.3	0.0	
Cash at end of period	7.5	5.2	6.8	16.6	
<b>Balance Sheet</b>	<b>2009A</b>	<b>2010F</b>	<b>2011F</b>	<b>2012F</b>	
Cash	6.7	5.2	6.8	16.6	
Inventories	2.6	1.6	1.7	1.8	
PP&E	5.1	6.7	7.8	8.0	
Debtors	50.1	48.6	49.0	52.2	
Intangibles	70.3	81.9	81.7	78.2	
Other assets	6.7	6.5	6.5	6.5	
Total Assets	141.4	150.5	153.4	163.3	
Borrowings	16.3	10.3	0.0	0.0	
Trade Creditors	55.8	56.4	61.8	65.8	
Other Liabilities	20.8	8.8	8.2	4.8	
Total Liabilities	92.9	75.4	69.9	70.6	
NET ASSETS	48.5	75.1	83.5	92.7	
<b>Board of Directors / Substantial Shareholders</b>					
Name	Shareholding	%			
Craig Farrow - Chairman	1.0	0.8%			
Vaughan Bowen - CEO/MD	10.9	8.9%			
Max Bowen - Non-Executive Director	0.0	0.0%			
Dennis Basheer - Non Executive Director	5.0	4.1%			
John Hynd - Non Executive Director	2.8	2.3%			
Michael Simmons - Non-Executive Director	0.0	0.0%			
<b>Substantial Shareholders</b>	<b>Shareholding</b>	<b>%</b>			
Hunter Hall	13.2	11.7%			
Vaughan Bowen	10.9	9.7%			
National Australia Bank	8.6	7.6%			
<b>Top 20 Shareholders (pre-\$20m placement)</b>	<b>60.0</b>	<b>48.8%</b>			
<b>Valuation ratios</b>	<b>2009A</b>	<b>2010F</b>	<b>2011F</b>	<b>2012F</b>	
EPS (cps)	8.6	15.6	19.7	22.4	
EPS (cps) - pre-amort	9.4	18.0	21.9	24.6	
PER (x)	18.6	9.8	8.0	7.2	
PER Rel - All Ind.	31%	-33%	-32%	-35%	
PER Rel - Small Ind.	24%	-28%	-27%	-31%	
Enterprise Value (\$m)	200.5	218.9	207.0	197.2	
EV / EBITDA (x)	15.3	6.7	5.1	4.4	
EV / EBIT (x)	18.3	8.1	5.9	5.0	
DPS (cps)	5.5	11.0	14.0	16.0	
Dividend Yield (%)	3.1%	6.3%	8.0%	9.1%	
Franking (%)	100%	100%	100%	100%	
CFPS (cps)	10.4	12.5	27.7	24.9	
P / CFPS (x)	16.9	14.1	6.4	7.1	
<b>Profitability ratios</b>	<b>2009A</b>	<b>2010F</b>	<b>2011F</b>	<b>2012F</b>	
EBITDA Margin (%)	6.5	8.4	9.6	9.9	
EBIT Margin (%)	5.4	7.0	8.3	8.6	
ROE (%)	15.4	23.5	29.1	29.7	
ROA (%)	8.1	18.7	24.0	26.7	
ROIC (%)	21.9	32.0	32.7	35.2	
<b>Balance Sheet ratios</b>	<b>2009A</b>	<b>2010F</b>	<b>2011F</b>	<b>2012F</b>	
Net Debt (cash)	9.6	5.0	cash	cash	
Net Gearing (%)	19.7	6.7	cash	cash	
Interest Cover (x)	28.4	15.6	69.7	cash	
NTA per share (\$)	0.0	0.0	0.0	0.0	
Price / NTA (x)	-21.8	-6.8	1.8	14.5	
EFPOWA (m)	87.4	112.8	122.8	122.8	
<b>Growth ratios</b>	<b>2009A</b>	<b>2010F</b>	<b>2011F</b>	<b>2012F</b>	
Sales revenue (\$m)	85.8%	92.0%	9.6%	6.5%	
EBITDA (\$m)	47.8%	148.5%	25.3%	10.3%	
EBIT (\$m)	44.9%	147.6%	29.3%	11.3%	
NPAT (\$m)	45.0%	134.9%	37.8%	13.5%	
EPS adj. (cps)	30.5%	90.5%	21.9%	12.1%	
DPS (cps)	10.0%	100.0%	27.3%	14.3%	
<b>Interim Analysis</b>	<b>2H09A</b>	<b>1H10F</b>	<b>2H10F</b>	<b>1H11F</b>	
Revenues	115.4	187.7	201.1	202.7	
EBITDA	7.1	15.3	17.2	19.0	
EBITDA margin (%)	6.1%	8.1%	8.6%	9.4%	
EBIT	6.0	12.6	14.6	17.6	
EPS (adj)	5.7	8.7	9.7	12.2	
DPS	5.0	5.0	6.0	6.5	
<b>Valuation</b>	<b>2009A</b>	<b>2010F</b>	<b>2011F</b>	<b>2012F</b>	
<b>Normalised EBITDA multiple (x)</b>					
EBITDA (\$m)	13.1	32.5	40.7	44.9	
Target EBITDA multiple (x)	8.1	8.0	7.0	6.3	
Net Debt (cash) (\$m)	9.6	5.0	-6.8	-16.7	
Implied Valuation	96.3	254.9	291.8	299.5	
<b>Per Share</b>	<b>0.85</b>	<b>2.08</b>	<b>2.38</b>	<b>2.44</b>	
<b>Target PE Multiple</b>					
EPS (c)	9.4	18.0	21.9	24.6	
PER Target (x)	15.0	13.5	11.0	10.3	
<b>Per Share</b>	<b>1.42</b>	<b>2.43</b>	<b>2.41</b>	<b>2.53</b>	
<b>Discounted Cash Flow</b>					
Cost of equity	14.9% WACC			14.3%	
Cost of debt	7.5% Terminal Growth Rate			3.0%	
Net Debt/ Net debt + equity	6.3% Per Share			2.40	



## APPENDIX 1: COMPANY HISTORY

Date	Event
04 May 2010	MTU completes share placement at \$1.80 per share to raise \$20m.
15 April 2010	MTU announces the acquisition of selected SMB assets from Clever Communications for \$5m with Clever to contribute annualised EBITDA of \$2.3m
14 April 2010	Optus extends MTU arrangement to wholesale mobile services to small and medium size telecommunications companies to 2013.
26 November 2009	Michael Simmons is appointed as Non- Executive Director
02 June 2009	MTU announces a proposed Asset Sale Deed to acquire all small and medium business assets and associated intellectual property of Commander Communications, which will add +\$100m p.a. of customer revenues.
05 December 2008	MTU announce agreement for MTU to acquire 100% of People Telecom by way of Scheme of Arrangement.
09 September 2008	Medibank Private appoints MTU as their preferred provider of telecommunications services to Medibank Private members.
23 June 2008	MTU announces two year wholesale agreement to supply People Telecom Limited (PEO) with Optus 3G mobile services, valued at \$9m.
25 February 2008	Acquisition of Unitel from Commander is finalized. MTU acquired Unitel for \$10m less adjustments.
04 February 2008	Commander Communications (ASX:CDR) announces binding Share Sale Agreement with MTU for the sale of its wholesale network services subsidiary, Unitel Australia Pty Limited.
06 September 2007	MTU launches Green Mobiles, Australia's first environmental mobile telecommunications service, specifically targeting climate change caused by global warming.
27 July 2007	Vodafone and MTU announce agreement that M2NZ will be able to resell M2 branded mobile services on the existing Vodafone network throughout New Zealand.
02 July 2007	Announces the acquisition of Tenex Pty Ltd, including all their customers and business assets for \$0.5m.
29 June 2007	MTU is to acquire Orion Telecommunications for \$22m.
09 May 2007	MTU announces acquisition of Wholesale Communications Group, Australia's largest Independent wholesaler of telecommunications services.
09 February 2007	MTU announces launch of Third Generation (3G) mobile network service.
29 November 2006	MTU finalises agreements with Red Media Solutions, National Telecoms Group and Mobile Communications Brokers, securing Optus mobile wholesale customers.



<b>16 August 2006</b>	MTU and Vodafone New Zealand enter an agreement for M2NZ to resell Vodafone Wholesale Mobile Services in New Zealand.
<b>31 May 2006</b>	MTU enters agreement with Optus to wholesale Optus mobile services to existing and emerging telecommunications service providers. M2 Wholesale is established on the back of the alliance.
<b>16 May 2006</b>	Craig Farrow is appointed as the new Chairman as Max Bowen steps down from this position.
<b>14 March 2006</b>	M2 enters agreement with E-Direct an established mobile telecommunications sales and marketing organization.
<b>24 January 2006</b>	MTU announces expansion with the launch of its New Zealand operation (M2NZ) Limited.
<b>02 August 2005</b>	M2 announces alliance with Singtel Optus, enabling access to wholesale mobile telecommunications services on the Optus Mobile Network.
<b>02 February 2005</b>	Announces acquisition of 100% share capital of Protel Communications International Pty Ltd and Protel IP Pty Ltd for A\$1.5m and an additional consideration of up to A\$1.5m, payable on 15th July 2006.
<b>07 December 2004</b>	Non-executive director Dean Gingell resigns.
<b>09 November 2004</b>	MTU announces that it will acquire the intellectual property of a range of digital telecommunications products from Datis Technology Pty Ltd.
<b>28 October 2004</b>	MTU lists on ASX.



## APPENDIX 2: DIRECTORS & MANAGEMENT

<b>Craig Farrow</b>	Chairman	<p>Mr Farrow was a founding director of MTU and was appointed Company Chairman in April 2006. Mr Farrow is also a founding partner of Brentnalls SA, Chartered Accountants and former National Chairman of the Brentalls National Affiliation of Accounting firms.</p> <p>Mr Farrow is the Chairman of Tonkin Consulting Engineers, and a national director of the Institute of Chartered Accountants in Australia, Chair of their Governance Committee, and a director or board advisor to several consulting and trading enterprises.</p> <p>Mr Farrow is a Fellow of the Institute of Chartered Accountants and the Australian Institute of Company Directors.</p>
<b>Mr Vaughan Bowen</b>	Managing Director	<p>Mr Bowen co-founded M2 in 1999 and was appointed Managing Director following incorporation.</p> <p>Mr. Bowen spent several years managing and profitably growing the South East Asian operations of Secure Parking, one of the region's largest facilities management companies. He was named as a finalist in the Entrepreneur of the Year Southern Region award in 2004 and 2009.</p> <p>Mr Bowen holds a Bachelor of Commerce degree (UNSW).</p>
<b>Mr Dennis Basheer</b>	Non-Executive Director	<p>Mr Basheer is an experienced company director with a prior focus on property development, project management and franchise developments.</p> <p>Until late 2003, Mr Basheer served as an executive director of M2 and was involved in corporate and channel sales. He is currently involved with the products and service of M2's as a South Australian Dealer.</p>
<b>Mr Max Bowen</b>	Non-Executive Director	<p>Mr Bowen provides the Board with experience gained in a management and business career having more than 40 years industry experience.</p> <p>Over the last 10 years, Max has acted in a senior advisory capacity to corporations and public utilities including, Pricewaterhouse Coopers, Optus, Sydney Olympic Village, Sydney Harbour Foreshore Authority and Federal Airports Corporation.</p> <p>He previously served the company as Chairman, however now holds the role of Non- Executive Director.</p>
<b>Mr John Hynd</b>	Non-Executive Director	<p>Mr Hynd brings over 30 years experience in commercial transactions, corporate advice, corporate governance, insolvency and property development to M2 attributable to being a founding partner of Hynd &amp; Co, a commercial law firm.</p> <p>He holds a Bachelor of Law degree from the University of Adelaide, is a Fellow of the Taxation Institute of Australia, 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.</p> <p>John has served as a non-executive director since MTU's incorporation</p>
<b>Mr Michael Simmons</b>	Non-Executive Director	<p>Mr Simmons has had 10 years of experience in the telecommunications industry, as Chief Executive Officer of SP Telemedia Limited (Soul) and most recently as Managing Director of national broadband network (NBN) bid syndicate, Terria Pty Ltd.</p> <p>Mr Simmons was previously the Chief Financial Officer of NBN Television before becoming CEO of Soul. He is the latest member to join the Board.</p>



## APPENDIX 3: RISK ANALYSIS

<b>Risk</b>	<b>Comment</b>
<b>Economic Sensitivity</b>	While the performance of the small and medium business market is highly correlated to broader economic conditions, telecommunications remains a non-negotiable necessity for any going concern.
<b>Industry Life Cycle</b>	Leveraged to technological change and the industry is currently moving into decline after 5-years of static 'real' growth as higher margin fixed-line services are substituted with lower cost mobile and wireless services. However we expect in the medium-term will see the industry move back to growth with the arrival of latest 4G network technologies and the NBN's fibre-to-the-home (FTTH) new generation network.
<b>Potential Entrants</b>	The attraction for new entrants is diminishing in the short-term with technology reducing the cost of telecommunications and incumbents, particularly those with scale, are well positioned to ward off new players. The NBN can be expected to herald a renewed interest for potential entrants.
<b>Political/Regulatory</b>	The Trade Practices Act 1974 addresses competition issues associated with telecommunications services, while the Telecommunications Act establishes the framework for minimum service standards and carrier licensing. The current government will spend up to \$43bn to establish a National Broadband Network (NBN) which alters the dynamics of the communications sector in Australia.
<b>Power of Buyers</b>	Resellers require scale to be able to negotiate favourable pricing from major network carriers, which is becoming more important as new products and services reduce the ARPU.
<b>Power of Suppliers</b>	Significant power given the high level of market concentration of network ownership, however regulatory changes in 1997 and new entrants have ensured pricing competition.
<b>Competitive Environment</b>	Increased price based competition across the entire telecommunications market has necessitated the need for scale to ensure profitability and competitive advantage.
<b>Technological Change</b>	The evolution of the telecommunications sector is driven by technological change. Once the building of the NBN and the introduction of 4G technology becomes integrated and entrenched in the economy, then Australia will be expected to transition to a digital economy
<b>Social Change</b>	Technological change and convergence of services is broadening the number of users and applications.
<b>Substitutes</b>	A function of technological change which is increasingly allows users a number of avenues for which to undertake their telecommunication needs.



## APPENDIX 4: TOP 20 SHAREHOLDERS (pre recent \$20m placement)

Shareholding	Number	Percentage
Cogent Nominees Pty Limited	16,680,141	15.54%
Mr Vaughan Bowen	13,382,666	12.34%
Telino Pty Limited	5,317,549	4.90%
Dennis Basheer Superannuation Pty Limited	4,101,177	3.78%
Nashar Pty Limited	2,661,497	2.45%
Wicks Group Limited	2,425,000	2.24%
Thirty Fourth Zulu Pty Limited	1,920,133	1.77%
Marcello Barbaro	1,914,500	1.77%
Wyatt Pty Ltd	1,600,000	1.48%
Reven Pty Limited	1,398,481	1.29%
Hyland Securities Pty Limited	1,232,524	1.14%
Dennis n Basheer Nominees Pty Limited	1,143,729	1.05%
Contemplator Pty Ltd	1,000,000	0.92%
J P Morgan Nominees Australia Limited	944,893	0.87%
Mr Edmond Wing Kin Cheung and Mrs Eliza Siu Ling Cheung	894,200	0.82%
Crofar Pty Ltd	800,000	0.74%
Citicorp Nominees Pty Limited	671,745	0.62%
Teloar Pty Ltd	666,666	0.61%
Mr David Marshall Nesbitt	570,000	0.53%
ANZ Nominees Limited	559,185	0.52%
<b>TOTAL</b>		<b>55.32%</b>



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**Stock Recommendations:**

STRONG BUY – Minimum expected upside is 40% over 12-months.

BUY - Minimum expected upside is 20% over 12 months.

HOLD – Minimum expected upside is 5% over 12 months.

REDUCE - Expected upside is below 5% over 12 months.

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