SK Telecom- Q1 24 Quick Take: Decent topline, but some margin pressure as AI investments start to impact

By Chris Hoare | May 8, 2024

What's new: Topline came in better than expected, supported by a better mobile performance from higher roaming users well as sustained performance from SK Broadband. EBITDA was relatively in line while net profit beat on expectations this quarter (12% ahead), helped by other income from its investment assets. Our thoughts below.

Consolidated group performance:

- **Consolidated revenue trend remained modest, up by 2.3% YoY (FY23: 1.8%) led by mobile, enterprise solutions and SK Broadband.** This was 0.5% ahead of consensus and in line with us.
  - **Mobile service revenue (ex-IC) came in 0.5% above expectations.** It improved to 1.4% YoY from 0.8% (FY23: 0.9%), driven by an uptick in roaming users (+55% YoY to 1.39m) led by family roaming plans and promotions. Given South Korea's 5G maturity, we believe 1-2% growth is sustainable and is likely a function of the maturity than regulatory pressure which has since eased following the Value Up programme and with the overhang of the fourth operator now lifted. At this stage, we think the impact from Stage X's entry is likely minimal given the maturity of 5G handset penetration (c.60%+) and the relatively poor coverage ability of mmWave spectrums (28GHz won by Stage X).
  - SK Broadband also improved to +2.8% from 2.5% YoY (FY23: 2.9%) led by its Fixed Line and B2B Biz. While management had previously expressed interest for SK Broadband to do an IPO, the timeline remains unclear.
  - Separately, Enterprise (comprised of Data Center, Cloud and leased lines) sustained decent growth again, up 8.7% YoY. Contribution from Enterprise remains smaller relative to KT and LG at 9.3% this

  - quarter. We remain bullish on Enterprise being a key theme in Korea as corporate spending as % of GDP remains under-indexed when benchmarked against DM peers.
  - Given the developments around the telco-specific large language models and A.dot (personal AI assistant launched in September 2023; 4m subscribers as of March 2024), monetisation may begin coming through from this year which would be positive. Overall we are somewhat sceptical about SKT's ability to drive returns from its AI investments.
- **Consolidated EBITDA slightly missed expectations by 0.1%**. It stayed flat YoY at KRW 1.4tn as slower rise in commissions cost were offset by higher labour costs, likely as a function of its focus on AI. As a result, EBITDA margin was down by 0.7pp to 31.9%. In spite of this, EBIT recorded 0.8% YoY growth as depreciation was slightly lower.
- **Bottom line beat estimates by 12% and grew 21.5% YoY** to KRW 353bn owing to a rise in "non-operating profit related to investment assets".
- Shareholder remuneration was somewhat underwhelming as the company focuses on AI capex. For instance while capex spend can be lumpy across quarters, Q1's capex intensity rose to 7% vs 4.8% last year. There was no change in DPS this quarter and remained at KRW 830/share which is also disappointing.
- **Weakness in mobile ARPU overshadowed by strong net additions** . Although mobile ARPU was down 2.9% YoY to KRW 29.2k, SKT added 354k subscribers as the rise in MNO outweighed the decline in MVNO subscribers. 5G subscribers grew by 432k to reach 15.9m which implies 69% 5G penetration.
- **Better broadband KPIs**: SKB added 64k broadband customers, up 55k last quarter to reach 6.9m; PayTV added sustained another 34k net additions to reach 6.7m. On our estimates, broadband ARPU improved by 1.1% YoY while decline in PayTV ARPU was down by 1.3% YoY vs. -0.1% last quarter.

Conclusion:

We expect to see sustained topline growth from B2B and this is coming through. 4m subscribers to A. is a positive figure and may suggest that monetisation of AI is closer than we had anticipated. However, the focus on AI is likely behind the recently announced shareholder remuneration which was slightly underwhelming.

While margins were weaker this quarter, we think SK Telecom has been executing decently around its cost control outside of AI, with lower marketing and labour costs being under control. Overall we still expect rising return capital and cash flow, despite the AI investments. Within the South Korean space, we continue to prefer KT as its corporate governance has seemingly improved and for its exposure to higher growth non-telcos segments like Fintech, content and Enterprise, and less focus on AI. We remain Buyers of SKT with a price target of KRW 116,000.

Full 12-month historical recommendation changes are available on request

Reports produced by New Street Research LLP, 18th Floor, 100 Bishopsgate, London, EC2N 4AG. Tel:+44 20 7375 9111.

New Street Research LLP is authorised and regulated in the UK by the Financial Conduct Authority and is registered in the United States with the Securities and Exchange Commission as a foreign investment adviser.

Regulatory Disclosures: This research is directed only at persons classified as Professional Clients under the rules of the Financial Conduct Authority ('FCA'), and must not be re-distributed to Retail Clients as defined in the rules of the FCA.

This research is for our clients only. It is based on current public information which we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied on as such. We seek to update our research as appropriate, but various regulations may prevent us from doing so. Most of our reports are published at irregular intervals as appropriate in the analyst's judgment. This research is not an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. It does not constitute a personal recommendation or take into account the particular investment objectives, financial situations, or needs of individual clients.

All our research reports are disseminated and available to all clients simultaneously through electronic publication to our website.

New Street Research LLC is neither a registered investment advisor nor a broker/dealer. Subscribers and/or readers are advised that the information contained in this report is not to be construed or relied upon as investment, tax planning, accounting and/or legal advice, nor is it to be construed in any way as a recommendation to buy or sell any security or any other form of investment. All opinions, analyses and information contained herein is based upon sources believed to be reliable and is written in good faith, but no representation or warranty of any kind, express or implied, is made herein concerning any investment, tax, accounting and/or legal matter or the accuracy, completeness, correctness, timeliness and/or appropriateness of any of the information contained herein. Subscribers and/or readers are further advised that the Company does not necessarily update the information and/or opinions set forth in this and/or any subsequent version of this report. Readers are urged to consult with their own independent professional advisors with respect to any matter herein. All information contained herein and/or this website should be independently verified.

All research is issued under the regulatory oversight of New Street Research LLP.