GO internet

Full year results

Back on track

Telecoms

With funding in place, GO is stepping up the implementation of its network and we reduce FY17 EPS forecasts to capture this profile as well as the new €1.75m loan, but leave FY18 estimates largely unchanged. A pick-up in the pace of subscriber additions could trigger upside to our base case DCF of €2.8/share. In addition, with 3.5GHz now earmarked for 5G services, GO's spectrum could be used for a wider service offering in the longer term and may put it in focus for operators looking to secure 5G capacity.

Year end	Revenue (€m)	EBITDA* (€m)	EPS* (c)	EV/sales (x)	EV/EBITDA (x)	P/E (x)
12/15	5.3	2.0	3.8	4.3	11.0	47.2
12/16	6.4	2.5	3.7	3.5	8.8	49.7
12/17e	7.7	3.2	3.2	2.9	6.9	56.1
12/18e	9.6	4.5	8.2	2.3	4.9	22.1

Note: *PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

FY16 results reflect slower roll-out of network

Despite the slower pace of network roll-out in 2016, GO continued to show steady financial progress. FY16 revenues of €6.4m increased in line with the subscriber base (+21%). EBITDA of €2.5m, while up 25%, was 11% lower than our forecast, reflecting the launch costs of the new fibre service in Perugia. Following last October's €4m funding round, management took advantage of favourable terms before the year-end to acquire additional base stations. Consequently, despite the slowdown in installation of base station last year, capital expenditure increased 28% to €5.7m and net debt was €3.0m (vs €2.3m forecast).

Funding in place – network roll-out accelerated

GO has also secured an additional €1.75m loan and is now able to reaccelerate the rate at which it implements its 4G LTE wireless network. The additional funding will also enable it to widen the scope of its fibre service partnership with Enel, currently in Perugia, to other cities later in the year. We update forecasts to reflect the current capital expenditure profile, and incorporate the additional financing costs in our estimates, which leads to a reduction in our FY17 EBITDA and EPS forecasts of 7% and 26% respectively. We consider this an acceleration of plans, rather than an uplift, and consequently the impact on our FY18 forecasts is less pronounced (5% reduction to FY18 EPS).

Valuation: 5G adds options for GO's 3.5GHz

The shares trade at a 35% discount to our base case DCF (€2.8/share versus €3.1/share before), which currently does not take into account potential valuation implications attached to GO's exclusive ownership of 42MHxz of spectrum in the 3.5GHz band. With this band recently earmarked by the European regulators for 5G, the possibility for GO to monetise this spectrum more widely has become a question of when and how, rather than if. Hutchinson's recent acquisition of UK peer (UK Broadband) also demonstrates that companies with access to this spectrum have become attractive to MNOs looking to secure 5G capacity.

4 April 2017

Price	**€1.82**
Market cap	**€19m**

Net debt (€m) at 31 December 2016	3.0
Shares in issue	10.6m
Free float	31%
Code	GO
Primary exchange	AIM Italia
Secondary exchange	NA

Share price performance

%	1m	3m	12m
Abs	6.0	21.9	36.1
Rel (local)	2.1	16.4	18.6
52-week high/low		€1.8	€1.1

Business description

GO internet provides fixed broadband internet and telephone services using fourth-generation (4G) wireless technology. The service is currently offered in the Emilia-Romagna and Marche regions of Italy, where GO has an exclusive right of use for 42MHz in the 3.5GHz frequency band. In partnership with Enel Open Fibre since Q117, it also offers a high-speed fibre to the home service (up to 1Gbps) in the city of Perugia (Umbria).

Next events

AGM	27 April 2017

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Edison profile page

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FY16 results review

The lack of clarity over funding during the first nine months of 2016 (refer to our report Rights issue for accelerated network roll-out for more detail) meant that GO had to slow the pace at which it rolled out its network to conserve liquidity. Subscriber growth tends to track base station installations and, consequently, while subscriber numbers have continued to increase (as GO back-filled its existing capacity), net additions during 2016 of 6.4k were not as strong as in FY15 (8.4k). Nevertheless, the full year results show continued solid financial progress.

Revenues increased by 21% to €6.4m, in line with our forecast, tracking the 20% year-on-year increase in subscribers to 37,749 at the year end. EBITDA of €2.5m (40% margin – flat on the interim) was 11% below our estimates, which we attribute to a higher level of marketing spend in relation to the launch of the new fibre service in Perugia in partnership with Enel Open Fibre. At the operating level, this was offset by a lower than forecast depreciation charge (due to a slower roll-out of the network in H216) leaving operating profits of €0.7k (+25% y-o-y), broadly in line with our expectations. However, a slightly higher tax charge meant that net profit of €0.3m was slightly short of our forecast.

Following the €4.0m October 2016 capital raise, management is accelerating the roll-out of the network and has taken advantage of favourable terms offered by Huawei to purchase approximately €2m of base stations just before the year end. Consequently, capital expenditure of €5.7m was considerably above our estimate of €3.2m, as was the year-end net debt of €3.0m.

Exhibit 1: Summary FY16 results and forecasts, €000s

	2015	2016e	2016 reported	Y-o-y change	diff to forecasts	2017e (new)	2018e (new)
Total net subscribers	31,356	37,783	37,749	20%	0%	45,048	55,310
Net subscriber additions	8,356	6,427	6,393	-23%	-1%	7,265	10,261
Total revenues	5,144	6,369	6,380	21%	0%	7,689	9,640
Operating profit	587	710	732	25%	3%	836	1,611
Interest	(275)	(250)	(252)	-8%	1%	(340)	(340)
PBT	312	460	480			496	1,272
Tax	(8)	(100)	(164)		64%	(156)	(399)
Net income	304	360	316	4%	-12%	340	873
EBITDA	2,010	2,830	2,516	25%	-11%	3,193	4,483
EBITDA margin	39%	44%	40%			42%	47%
Working capital	35	(7)	2,130			1,131	618
Other	0	0	(26)			0	0
Capex	(4,476)	(3,232)	(5,716)	28%	77%	(4,500)	(4,118)
FCF	(2,714)	(759)	(1,512)	-44%	99%	(671)	244
Financing/other	8	(3,968)	(3,968)		0%	753	0
Net debt - closing	5,463	2,254	3,007	-45%	33%	3,678	3,434
of which cash	339	3,548	2,406	610%	-32%	1,815	339

Source: GO internet (historics), Edison Investment Research (forecasts)

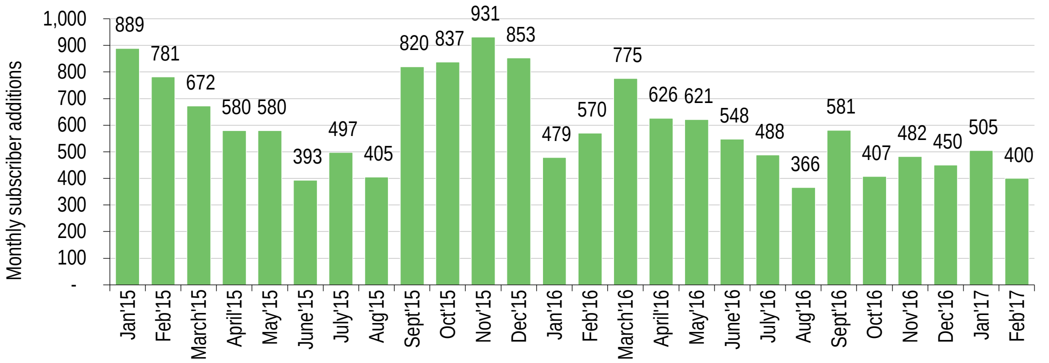
Financing in place – network roll-out back on track

In October 2016, GO announced the successful completion of its 77-for-100 rights issue at 0.86 per share (raising €4.0m via issuing 4.6m shares in total). In addition, in January 2017 it secured an additional €1.75m loan from Banca Intesa.

With this funding in place, GO has the resources to reaccelerate the roll-out of its 4G LTE high-speed wireless broadband network, targeting approximately 100-120 new base station installations in FY17 (compared to c 30 installed in FY16).

Additionally, in July 2016 GO announced that it had partnered with Enel Open Fibre in Perugia to market its ultra-wideband, fibre-to-the-home network. The additional funds will also enable it to widen the scope of its marketing for the promotion of this high-speed wireline network. Take-up in the first few months has been encouraging and the offer will be extended to another city in Q217, potentially adding other cities in Italy as the year progresses.

Exhibit 2: Monthly net subscriber additions



Source: GO internet data

Forecasts revision: Accelerated investment & financing

We assume GO maintains a higher level of marketing spend in FY17 to support the new wireline services and a faster pace of deployment for its wireless network which leads to a reduction in our FY17 EBITDA forecast by 7%. The additional cost of financing the €1.75m loan leads to a reduction in our EPS forecast by 26% in FY17. We view the increase in capital expenditure as an acceleration of plans rather than an uplift and consequently we leave our FY18 forecasts largely unchanged at the operating level.

GO reported FY16 year-end net debt of €3.0m, with cash of €2.4m. Debt comprises two bank loans of approximately €2.3m (c 3.5% interest) repayable in annual instalments by 2019 and 2023 respectively, and sale and leaseback arrangements mainly with Huawei for €2.1m, the outstanding payments due on the licence acquisition for the Emilia-Romagna region of €0.3m (repayable in annual instalments to 2024) and other credit lines (€0.6m).

We are increasing our FY17 capital expenditure forecast from €4.0m to €4.5m, and again in FY18 from €3.4m to €4.1m. Despite this increase and the higher than forecast FY16 year-end debt level, we raise our FY17 forecast net debt by only 9% to €3.7m. GO's strong relationship with Huawei has enabled it to secure favourable payment terms on the procurement of its base stations, which we expect to result in a significant working capital inflow in the current year. Provided this is the case, GO is adequately funded to execute a more aggressive roll-out plan in the forecast period, although it may seek to add to its facilities to provide additional flexibility in the event these payment terms are not repeated in for future equipment purchases.

Exhibit 3: Summary forecast changes, €000s

	2016			2017e			2018e		
	Forecast	Reported	Difference	Old	New	Change	Old	New	Change
Subscribers	37,783	37,749		44,179	45,048		55,337	55,310	
Revenues	6,369	6,380	(0%)	7,699	7,689	0%	9,675	9,640	0%
EBITDA	2,830	2,516	(11%)	3,423	3,193	(7%)	4,369	4,483	3%
Operating profit									
PBT	460	480	4%	673	496	(26%)	1,333	1,272	(5%)
Net income (headline)	360	136	(62%)	462	340	(26%)	914	873	(5%)
EPS (normalised, diluted)	4.2	3.7	(12%)	4.4	3.2	(26%)	8.6	8.2	(5%)
Capex	(3,232)	(5,716)	77%	(3,999)	(4,500)	13%	(3,422)	(4,118)	20%
Net debt	2,340	3,007	28%	3,388	3,678	9%	4,522	3,434	(24%)

Source: Edison Investment Research

3.5GHz spectrum increasingly valuable in 5G

The commercialisation of its wireless network in the in the Marche and Emilia-Romagna regions of Italy is the primary driver of forecasts and underpins our base case DCF valuation of €2.8 per share (down from €3.1 following the reduction in our EBITDA forecast). Along with the pace of expansion of this wireless network, there are a number of other initiatives that could have a significant impact on GO's valuation. In summary:

- The success of its new partnership with Enel Open Fibre, which could be extended beyond Perugia to other cities in Italy.
- The possibility of greatly enhancing the footprint of its wireless network by participating in spectrum tenders.
- Option value associated with Spectrum ownership.

Since our last update it is the value of GO's spectrum in a wider context that requires greater attention given wider developments in the industry. When GO first acquired its spectrum, there was little interest by the industry in the 3.5GHz frequencies and GO secured 42MHz of spectrum in this frequency band for a relatively low price. However, with the explosion of mobile data, the lower frequencies currently used by mobile service providers are rapidly becoming saturated and mobile operators are looking to higher frequencies to satisfy capacity demands as the industry moves towards the gigabit technologies offered in a 5G environment.

Intel, Qualcomm and Huawei have all started producing chipsets that support 3.5GHz frequency for tablet and smartphone reception, which are now being incorporated across a spectrum of equipment, including smartphones (Sony, Samsung and ZTE phones using Qualcomm Snapdragon 835 chipset are expected to be on the market in the coming months). Furthermore, regulators across Europe (Ofcom, ITU) have now identified three key bands that will enable 5G in Europe – 700MHz, 24.5-27.5Ghz and, critically for GO, 3.4-3.8GHz.

This opens up a number of new possibilities for GO longer term, from wholesaling its spectrum to telecoms operators, to potentially even adding its own mobile offering to its fixed wireless broadband services. It also makes GO a more attractive target for one of the larger operators looking to secure 5G spectrum.

Assessing the actual value of GO's spectrum is at this stage highly speculative. However, there is an interesting reference case in the UK. Hutchinson 3's UK arm recently acquired UK Broadband for €350m (£250m plus £50m deferred investment). At an implied value per subscriber of €23k (UK Broadband has only 15k subscribers, mainly in London), the acquisition is largely ascribed to its ownership of 208MHz of nationwide spectrum holdings between 3.5 and 3.7HGz range, giving a significant boost to 3UK's capacity in this band. Hutchinson's acquisition is a lower-risk and cheaper route to securing spectrum than relying on the spectrum auctions – scheduled for later in 2017 in the UK. Via UK Broadband, Hutchinson secures the spectrum for only 3c per MHz per population compared to the 43c it paid for its 800MHz of 4G spectrum in 2013. As a benchmark, this indicates a potential spectrum value of €8m (assuming the UK Broadband takeover value per MHz per population), up to €122m (using the price Hutchinson paid for its spectrum in 2013). This is in addition to the value of GO's wireless subscriber network and installed base of 37.7k subscribers.

For GO, the question has now become how and when, rather than if it can leverage its frequencies beyond wireless broadband services with a mobile offer. Irrespective of its eventual commercial strategy, owning exclusive access to these frequencies in the valuable Marche and Emilia-Romagna regions in Italy has put GO on the map of mobile operators looking to secure capacity for 5G mobile services.

On the other hand, it complicates GO's own plans to bid for additional 3.5GHz spectrum to widen its wireless footprint to other regions, as these auctions are likely to be hotly contended now. In early 2015, AGCOM announced its intention to release an additional 200MHz of spectrum in the 3.6GHz frequency band. The government was keen to add services in areas of the country that currently have poor or no reception (digital divide areas). The auctions, which have already been subject to delays (they were originally expected last year), are likely to be delayed further as the regulator reassesses its strategy in light of the 5G standards that are being recommended.

Valuation and investment case

With funding in place, GO is in a strong position to reaccelerate the deployment of its network, both within and beyond its existing regions. Our base case DCF valuation, which factors in our forecasts to FY18 followed by stable subscriber additions for a further five years (and assumes an 11.5% WACC and a 2% terminal growth rate), returns a valuation of €2.8 per share, 35% above the current share price. Investors should also consider the following:

- GO is targeting the 1m homes in the Marche and Emilia-Romagna regions that have chosen to relinquish their fixed line and, with 38.6k subscribers as of February 2017, there is considerable headroom for growth. Management plans to double its network coverage in the next few years to 30% of homes and the introduction of the 100Mbps and soon 300Mbps service should further improve its competitive offering.
- Enel's entry to the fibre market in Italy is potentially very disruptive. We view GO's recently announced agreement with Enel as a relatively low-risk route to extending its brand outside its current regions, potentially nationally in Italy. Even a fairly small degree of success nationwide could have a significant impact on GO's overall financial position longer term.
- 5G spectrum option. As outlined above, the 3.5GHz frequency band has been identified within 5G standards, which adds commercial opportunities for GO internet in the longer term and puts it on the radar of larger operators that are likely to look to secure frequency for a 5G environment.
- The pending spectrum auctions offer a further opportunity for GO to expand its footprint beyond its current regions. Given recent developments in 5G, GO is likely to face a more intense level of competition than we previously thought, which reduces its chance of securing frequency. However, the auctions will help to set a price for the value of the spectrum that GO currently holds.

Risks and sensitivities

GO competes with a number of much larger, well-funded operators. Our forecasts assume, a stable pricing environment and steady progression in subscribers. However, the market is highly competitive and GO needs to react to market trends.

While we do not consider our subscriber forecasts for the new Enel service to be aggressive (peaking at 200 new subscribers a month), they are fairly speculative. The financial impact could be significantly higher or lower than we assume.

Exhibit 4: Financial summary

€000s	2013	2014	2015	2016	2017e	2018e
31-December	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS						
Revenue	2,645	3,899	5,285	6,380	7,689	9,640
Cost of Sales	(1,170)	(2,053)	(2,735)	(2,977)	(3,558)	(4,109)
Gross Profit	1,504	1,896	2,550	3,403	4,131	5,530
EBITDA	887	1,425	2,010	2,516	3,193	4,483
Operating Profit (before amort. and except.)	166	373	587	732	836	1,611
Intangible Amortisation	0	(50)	(86)	(120)	0	0
Exceptionals	(54)	(7)	(67)	(60)	0	0
Other	0	0	0	0	0	0
Operating Profit	111	316	434	552	836	1,611
Net Interest	(202)	(292)	(275)	(252)	(340)	(340)
Profit Before Tax (norm)	(36)	81	312	480	496	1,272
Profit Before Tax (FRS 3)	(90)	24	159	300	496	1,272
Tax	(10)	(48)	(8)	(164)	(156)	(399)
Profit After Tax (norm)	(46)	33	304	316	340	873
Profit After Tax (FRS 3)	(100)	(24)	151	136	340	873
Average Number of Shares Outstanding (m)	5.54	6.56	7.97	8.63	10.61	10.61
EPS - normalised (c)	(0.84)	0.50	3.82	3.66	3.21	8.23
EPS - normalised fully diluted (c)	(0.84)	0.50	3.82	3.66	3.21	8.23
EPS - (IFRS) (c)	(1.81)	(0.37)	1.90	1.58	3.21	8.23
Dividend per share (€)	0.00	0.00	0.00	0.00	0.00	0.00
Gross Margin (%)	56.2	48.0	48.2	53.3	53.7	57.4
EBITDA Margin (%)	33.2	36.1	38.0	39.4	41.5	46.5
Operating Margin (before GW and except.) (%)	6.2	9.4	11.1	11.5	10.9	16.7
BALANCE SHEET						
Fixed Assets	6,536	8,117	11,158	14,729	16,872	18,118
Intangible Assets	2,404	2,465	2,767	2,979	2,938	2,578
Tangible Assets	4,132	5,652	8,391	11,750	13,934	15,540
Investments	0	0	0	0	0	0
Current Assets	2,023	6,527	4,330	4,526	3,822	2,228
Stocks	166	814	967	814	830	830
Debtors	1,729	3,429	2,729	1,307	1,176	1,059
Cash	128	2,284	338	2,405	1,815	339
Other	0	0	296	0	0	0
Current Liabilities	(3,065)	(5,093)	(7,835)	(7,758)	(8,775)	(6,636)
Creditors	(1,384)	(3,839)	(5,034)	(5,998)	(7,015)	(4,876)
Short term borrowings	(1,681)	(1,254)	(2,801)	(1,760)	(1,760)	(1,760)
Long Term Liabilities	(4,515)	(3,911)	(3,000)	(3,000)	(3,080)	(1,360)
Long term borrowings	(4,368)	(3,771)	(3,000)	(3,000)	(3,080)	(1,360)
Other long term liabilities	(147)	(140)	0	0	0	0
Net Assets	979	5,640	4,653	8,497	8,838	12,350
CASH FLOW						
Operating Cash Flow	1,297	1,842	2,045	4,646	4,324	5,101
Net Interest	(202)	(292)	(275)	(252)	(340)	(340)
Tax	(10)	(48)	(8)	(164)	(156)	(399)
Capex	(1,844)	(2,670)	(4,476)	(5,716)	(4,500)	(4,118)
Acquisitions/disposals	0	0	0	0	0	0
Financing	0	4,324	0	3,968	0	0
Dividends	0	0	0	0	0	0
Other	(29)	6	(8)	(26)	0	0
Net Cash Flow	(788)	3,162	(2,722)	2,456	(671)	244
Opening net debt/(cash)	5,152	5,921	2,741	5,463	3,007	3,678
HP finance leases initiated	0	0	0	0	0	0
Other	19	18	0	0	0	0
Closing net debt/(cash)	5,921	2,741	5,463	3,007	3,678	3,434

Source: GO internet (historics), Edison Investment Research (forecasts)

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