

Highlights of Major Telecom Companies' Financial Results for Fiscal Year Ended March 2020

The following is Japan Credit Rating Agency, Ltd. (JCR)'s perception of the current status and highlights for rating concerning the financial results for the fiscal year ended March 2020 (FY2019) and earnings forecasts for FY2020 of Japan's four major telecom companies: NIPPON TELEGRAPH AND TELEPHONE CORPORATION ("NTT"), KDDI CORPORATION ("KDDI"), NTT DOCOMO, INC. ("NTT DOCOMO") and SoftBank Corp. ("SoftBank"); collectively, the "Companies."

1. Industry Trend and Impact of COVID-19 Pandemic

In the domestic mobile communications market, the total number of subscribers for KDDI, NTT DOCOMO and SoftBank as of March 31, 2020 came to 184.75 million, up 3.7% from the previous year. Even though the penetration rate has already exceeded 100%, subscribers are still increasing. That said, other than the main lines for private telephone services, these subscriptions include the lines exclusively for data communications and those for mobile virtual network operators (MVNOs), of which earnings contribution is small with low monthly average revenue per user (ARPU). Hence the number of subscribers for the main lines is critical in terms of earnings, but given the already high penetration rate, a future leap in the number is unlikely.

The COVID-19 has both negative impacts, such as a decline in visitors to cell-phone shops and usage of global roaming services, and positive impacts including increased demand for telecommunications due to telework. Overall impacts on the industry are expected to be marginal.

In October 2019, the Telecommunications Business Act was amended. On mobile phones, the revised act includes descriptions such as "complete separation between communication fees and handset prices," "correction of excessive customer retention," and "optimization of soliciting by operators and sales representatives," among others. Telecom companies have so far, promoted sales through a method of substantial discount of handset prices. That said, as a result of various restrictions on sales, the number of handsets sold started to decline. Even so, as the Companies have hardly gained profits from sales of handsets, the act does not have a large impact on profits.

KDDI, NTT DOCOMO and SoftBank commenced the commercial 5G service in March 2020. The operating areas are limited at the moment, but each of the Companies is actively working to expand the areas. KDDI and Softbank set up a JV in an attempt to share base-station assets in local areas, aiming to accelerate geographical spread of 5G services. Accordingly, 5G-compatible handsets are expected to be the mainstream in sales. Competitiveness might vary depending on each Company's 5G geographical expansion and services.

2. Financial Results

The Companies remain highly profitable. The combined operating income of NTT, KDDI and SoftBank (the "combined operating income") grew 2.1% year on year to 3,499 billion yen in FY2019. However, NTT's operating income declined 7.8% to 1,562.1 billion yen. Although the regional communication business and the long distance and international communications business achieved an income increase, the mobile communications business reported an income decrease because of the impact of the "return benefits to customers" program for new rate plan Gigaho and Gigalight at NTT DOCOMO and a cost increase stemming from restructuring in its global business. Meanwhile, KDDI's operating income reached 1,025.2 billion yen, up 1.1% year on year, hitting a record high. The number of its group IDs (the number of au subscribers plus MVNO subscribers) has been inching up and mobile communication revenues kept high, while the life design domain offering optional services continues expanding. Softbank reported an operating income of 911.7 billion yen, up 11.4% year on year (after catch-up adjustment for the impact of making Z Holdings Corporation ("Z Holdings") a subsidiary), marking a record high. It continues to be highly competitive by developing three brands (SoftBank, Y!mobile and LINE MOBILE) responding to user needs, all of which have been gaining subscribers steadily. Having made Z Holdings into a subsidiary in June 2019, Softbank is expanding profits.

On the financial front, both NTT and KDDI maintain a good financial position. SoftBank, on the other hand, has much room compared to its peers for improving the net interest-bearing debt/EBITDA ratio, equity ratio and other financial indicators. In FY2019, it bore financial burden on a consolidated basis due to making Z Holdings into a consolidated subsidiary and acquisition of ZOZO by Z Holdings. That said, given the stable cash flow generating ability, JCR assumes that SoftBank's financial indicators will improve as net interest-bearing debt declines steadily going forward.

3. Highlights for Rating

NTT and NTT DOCOMO have not disclosed their FY2020 earnings forecasts since it is difficult to calculate forecasts due to the impact of the COVID-19. They will likely be affected in sales from services because of limited face-to-face communications. However, given that most of their profits are from monthly fees based on contracts, their earnings capacity will unlikely significantly deteriorate as long as existing contracts are maintained. Hence they seem to be able to continue ensuring high-level profits. For NTT DOCOMO, as subscribers who use a monthly discount program (tsukizuki support) are going to decline in tandem with expansion of subscribers to new rate plans, cost reduction is assumed to progress more than a decrease in communications income. KDDI and SoftBank are projecting net sales and operating income at the almost same level as the previous period.

In April 2020, Rakuten, Inc. fully commenced its mobile phone carrier service. By launching rate plans characterized with provision of large volume data at low prices, developing aggressive sales promotion of offering service for free for a year up to 3 million subscribers. With its own area currently limited to large metropolitan areas, the scale of Rakuten's operating area is insufficient. Therefore, it does not have a substantial impact on the Companies' existing contracts. That said, as its own area expands with time, Rakuten may gradually gain more competitiveness. It could bring about fiercer competition within the industry, having a negative impact on each of the Companies' profits. JCR will hence keep an eye on Rakuten's moves.

As main subscribers are hardly likely to increase, the Companies are focusing on improving optional services and developing non-telecom domains. For telecom services, there is not much difference now among the Companies in terms of rate plans, handsets and communications quality, whereas optional services have much room for introducing new ideas, which could be a key to differentiation. NTT DOCOMO, for instance, defines content services (video streaming, etc.), financial and payment services, support services for customers' peace of mind, etc. as the "smart life domains," and is striving to expand these domains. SoftBank is aggressively developing non-telecom domains, such as smartphone settlement service PayPay, AI-based taxi transportation platform DiDi, community-centric workspace provider WeWork, etc., while enhancing cooperation with subsidiary Z Holdings. In particular, PayPay is showing a significant growth, exceeding 28 million registered users in April 2020. At a time when the telecommunications business is expected to hit a growth plateau, the Companies intend to further enhance their earnings bases by beefing up the non-telecom domains. JCR will closely watch progress in such efforts.

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(Chart 1) Consolidated Results of Major Telecom Companies

(JPY 100 mn, %, times)

		Net Sales (Operating Revenue)	Operating Income	EBITDA	EBITDA Margin	Net Income	Net Interest- bearing Debt	Equity Capital	Total Assets	Net Interest- bearing Debt/ EBITDA	Equity Ratio	Net DER
NTT (9432)	FY2018	118,798	16,938	32,414	27.3	8,545	33,165	92,649	222,951	1.0	41.6	0.4
	FY2019	118,994	15,621	29,795	25.0	8,553	36,663	90,611	230,141	1.2	39.4	0.4
	FY2020F	-	-	-	-	-	-	-	-	-	-	-
KDDI (9433)	FY2018	50,803	10,137	15,986	31.5	6,176	10,711	41,834	73,304	0.7	57.1	0.2
	FY2019	52,372	10,252	17,508	33.4	6,397	13,111	43,844	95,801	0.7	45.8	0.3
	FY2020F	52,500	10,300	17,600	33.5	6,400	-	-	-	-	-	-
NTT DOCOMO (9437)	FY2018	48,408	10,136	15,590	32.2	6,636	-1,699	53,718	73,405	-	73.2	-
	FY2019	46,512	8,546	14,440	31.0	5,915	-1,038	52,499	75,359	-	69.7	-
	FY2020F	-	-	-	-	-	-	-	-	-	-	-
SoftBank (9434)	FY2018	46,568	8,181	13,670	29.4	4,624	25,533	14,981	80,363	1.9	18.6	0.5
	FY2019	48,612	9,117	16,065	33.0	4,731	39,384	10,005	97,922	2.5	10.2	0.5
	FY2020F	49,000	9,200	-	-	4,850	-	-	-	-	-	-
Three Companies Total	FY2018	207,064	34,269	60,497	29.2	19,028	73,190	146,953	354,005	1.2	41.5	0.5
	FY2019	219,978	34,990	63,368	28.8	19,681	89,158	144,460	423,864	1.4	34.1	0.6
	FY2020F	-	-	-	-	-	-	-	-	-	-	-

Source: Prepared by JCR based on financial materials of the above companies

Notes:

1. Three Companies Total covers: NTT, KDDI and SoftBank.
2. Figures for FY2020F are those announced by the above companies.

<Reference>

Issuer: NIPPON TELEGRAPH AND TELEPHONE CORPORATION

Long-term Issuer Rating: AAA Outlook: Stable

Issuer: NTT DOCOMO, INC.

Long-term Issuer Rating: AAA Outlook: Stable

Issuer: SoftBank Corp.

Long-term Issuer Rating: AA- Outlook: Stable

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