

## Saudi Telecom Company

Strong growth in topline offset by one-offs

### 2Q22 Net Profit lower than our estimate

Saudi Telecom Company's (STC/the Group) net profit rose marginally 0.6% YOY to SAR 2,837 Mn in 2Q22, lower than our estimate of SAR 2,983 Mn. It was mainly driven by rise in revenue largely offset by rise in direct cost, operating expenses, losses from associates & JVs and impairment of investment in BGSM investment.

### P&L Highlights

STC's revenue rose 6.5% YOY to SAR 16,939 Mn in 2Q22 due to various investments made by the company with strong growing demand for its services supported by healthy growth in the digital economic sector in KSA and GCC region. STC's KSA performed excellently delivering a 9.1% top-line growth resulting into a topline growth of 7.4% YOY in 1H22. Revenue from STC KSA Enterprise Business Unit rose 15.9% YOY whereas, Wholesale Business Unit revenue rose 6.1% YOY in 1H22. Similarly, Consumer Business Unit revenue rose 6.1% YOY driven by increase in mobility revenue growth of 6.7% YOY and increase in working lines by 5.9% YOY in 1H22. Residential segment registered a topline growth of 3.0% YOY led by strong growth in FTTH and Fixed wire access subscriber base by 3.4% YOY and 13.5% YOY, respectively in 1H22. Direct cost grew 2.9% YOY to SAR 7,765 Mn in 2Q22. Thus, gross profit rose 9.8% YOY to SAR 9,174 Mn in 2Q22 with a gross margin of 54.2% in 2Q22 compared to 52.5% in 2Q21. Operating expenses rose SAR 353 Mn YOY in absolute values due to continued investments in new entities as per the Group's policy. EBITDA rose 10.3% YOY to SAR 6,204 Mn in 2Q22. Depreciation and amortization expenses amounted to SAR 2,484 Mn in 2Q22 as compared to SAR 2,376 Mn in 2Q21. Resultantly, operating profit rose significantly by 14.5% YOY to SAR 3,720 Mn in 2Q22 with a margin of 22.0% in 2Q22 compared to 20.4% in 2Q21. On the other hand, other expenses rose SAR 365 Mn YOY in 2Q22 attributable to a loss in net share of associates and JVs of SAR 283 Mn and an impairment provision of SAR 298 Mn associated with BGSM investment owing to an interest rate hike in Malaysia resulting in the re-evaluation of the investment.

### Balance Sheet Highlights

The group's total equity rose 12.3% YOY to SAR 71.8 Bn in 2Q22. The board of directors recommended increasing the group's capital by 150% by issuing bonus shares worth SAR 30 Bn by capitalizing the amount from retained earnings. A bonus of 1.5 shares will be issued for every one share. The board of directors also recommended amending the dividend policy by paying a minimum dividend of SAR 0.4 per share on quarterly basis effective from 4Q21 with a validity of three years. The directors also approved issuing ESOP of 15 Mn shares with the amount not exceeding SAR 453 Mn which will be presented for voting at the upcoming EGM.

### Target price and rating

We maintain our BUY rating on Saudi Telecom Company with a target price of SAR 135.0. STC is the leading telecom company in Saudi Arabia with 73.9% market share by revenue as of 31<sup>st</sup> March 2022. The Group benefits from strong government support with 64% ownership. To expand STC's scale and scope, the Group is forming a number of partnerships and announcing investments in

**Rating : BUY**

### First Look Note – 2Q22

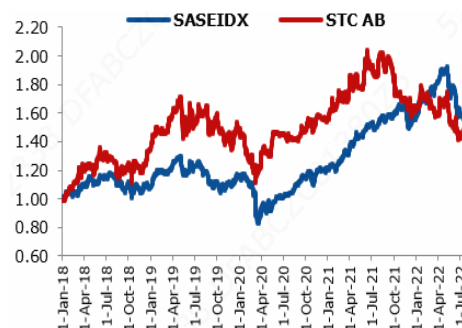
**Sector: Telecom**

#### Recommendation

Current Price (03-Aug-22)	101.60
Target Price (SAR)	135.00
Upside/Downside (%)	+33%

#### Stock Information

Market Cap (mm)	205,200.00
Paid Up Capital (mm)	20,000.00
52 Week High	138.60
52 Week Low	95.20
3M Avg. daily value (SAR)	360,483,000



#### Financial Ratios

Dividend Yield (12m)	3.90
Dividend Pay-out (%)	70.62
Price-Earnings Ratio (x)	17.97
Price-to-Book Ratio (x)	2.91
Book Value (SAR)	35.23
Return-on Equity (%)	16.83
Earning Per Share (SAR)	5.71
Beta	0.74

#### Stock Performance

5 Days	2.19%
1 Months	5.56%
3 Months	-11.55%
6 Months	-12.01%
1 Year	-24.89%
Month to Date (MTD)	1.79%
Quarter to Date (QTD)	5.66%
Year to Date (YTD)	-8.72%

new sectors and domains. For instance, STC launched Saudi Cloud Computing Company (SCCC) in a joint venture with Alibaba Cloud. The newly established company will provide integrated cloud services to both public and private and expected to benefit from strong growth in this business domain. STC holds 55% stake in SCCC with an investment of SAR 492 Mn. STC's subsidiary, solutions by stc acquired 89.5% stake in Giza Systems Company with an additional 34% stake in its subsidiary Giza Arabian Systems. The group also announced their success in developing multi-layer 4G and 5G NSA network in collaboration with a leading digital enabler Manvenir on the ORAN platform. STC's strategic acquisitions are in line with its targets to expand domestically as well as internationally. The group is on right track to establish "MENA Hub" (a digital hub) by investing USD 1 Bn connecting three continents with high-efficiency fiber optic cables expanding its services globally. Furthermore, STC held a strong balance sheet with low leverage with a sound credit rating profile to fund its internal and external expansion plans. The expansion plan envisaged by the Group will positively impact topline. STC continued to pay stable dividends for the last four years. Thus, based on our analysis, we maintain a BUY rating on the stock.

#### STC- Relative Valuation

(At CMP)	2018	2019	2020	2021	2022F
P/E (x)	18.85	19.05	18.48	17.96	17.27
P/B (x)	3.10	3.29	3.18	2.93	2.77
EV/EBITDA	9.61	9.57	8.78	8.69	7.99
Dividend Yield	5.91%	3.94%	4.92%	3.94%	3.94%

FABS Estimates & Co Data

#### STC - P&L

SAR mm	2Q21	1Q22	2Q22A	2Q22F	Var.	YOY Ch	QOQ Ch	2021	2022F	Change
Sales	15,899	16,991	16,939	16,748	1.1%	6.5%	-0.3%	63,417	68,363	7.8%
Direct costs	-7,547	-7,841	-7,765	-7,704	0.8%	2.9%	-1.0%	-29,623	-31,732	7.1%
<b>Gross profit</b>	<b>8,352</b>	<b>9,150</b>	<b>9,174</b>	<b>9,044</b>	1.4%	9.8%	0.3%	<b>33,794</b>	<b>36,630</b>	8.4%
<b>EBITDA</b>	<b>5,627</b>	<b>6,300</b>	<b>6,204</b>	<b>6,247</b>	-0.7%	10.3%	-1.5%	<b>22,841</b>	<b>25,027</b>	9.6%
Depreciation & amortization	-2,376	-2,476	-2,484	-2,487	-0.1%	4.5%	0.3%	-9,713	-10,199	5.0%
<b>Operating profit (EBIT)</b>	<b>3,250</b>	<b>3,824</b>	<b>3,720</b>	<b>3,760</b>	-1.1%	14.5%	-2.7%	<b>13,128</b>	<b>14,828</b>	13.0%
Zakat	-220	-296	-282	-290	-2.9%	28.2%	-5.0%	-1,040	-1,129	8.6%
<b>Profit attributable</b>	<b>2,821</b>	<b>3,035</b>	<b>2,837</b>	<b>2,983</b>	<b>-4.9%</b>	<b>0.6%</b>	<b>-6.5%</b>	<b>11,311</b>	<b>11,764</b>	<b>4.0%</b>

FABS estimate & Co Data

#### STC- Margins

	2Q21	1Q21	2Q22A	2Q22F	YOY Ch	QOQ Ch	2021	2022F	YOY Ch
Gross margin	52.5%	53.9%	54.2%	54.0%	163	31	53.3%	53.6%	29
EBITDA Margin	35.4%	37.1%	36.6%	37.3%	124	-45	36.0%	36.6%	59
Operating margin	20.4%	22.5%	22.0%	22.5%	152	-54	20.7%	21.7%	99
Net profit margin	17.7%	17.9%	16.7%	17.8%	-100	-111	17.8%	17.2%	-63

FABS estimate & Co Data

**Research Rating Methodology:**

Rating	Upside/Downside potential
BUY	Higher than +15%
ACCUMULATE	Between +10% to +15%
HOLD	Lower than +10% to -5%
REDUCE	Between -5% to -15%
SELL	Lower than -15%

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