GCC Telecom Sector

July 18, 2022

Company	Rating
Saudi Telecom Co. (STC)	Hold
Etihad Etisalat Co. (Mobily)	Hold
Ooredoo QSC (Ooredoo)	Buy
Emirates Telecommunication Group (Etisalat)	Sell
Mobile Telecommunication Co. Saudi Arabia (Zain KSA)	Buy

- **GCC Telecom sector is well penetrated market and a stable industry**
- **5G development and data to support growth in Average revenue per units (ARPUs)**
- **Valuation upside is limited for most stocks due to industry in a stable state**
- **Likely risk from lower usage of telecom services due to impact of inflation on consumer sentiment**

We initiate coverage on the GCC Telecom Sector with five names in focus – Saudi Telecom Co. **(STC), Etihad Etisalat Co. (Mobily), Mobile Telecommunication Co. Saudi Arabia (Zain KSA), Emirates Telecommunication Group (Etisalat)** and **Ooredoo QSC (Ooredoo)**. Our valuations are based on a mix of DCF, EV/EBITDA, and P/E multiple. The telecom sector in the region is in a mature stage of industry cycle. Over 100% penetration in terms of mobile subscription indicates that organic growth is not feasible and growth in average revenue per user (ARPU) through data and value-added services will be the key growth driver. At the same time, stability in terms of subscribers (low churn), low threat of new entrants (restricted entry due to regulated nature of industry) and hence limited competition results in steady cashflow generation.

- **Well penetrated market, stable industry, defensive sector.** GCC countries have witnessed significant shifts in usage of telecom services in the past two decades. In terms of mobile penetration rate (mobile phone usage), GCC countries have crossed over 100% levels (indicating more than one mobile per person). These high levels also mean the market is well penetrated and the industry is past its subscriber growth phase. Further, low churn (change in telecom service provider) of subscribers also indicates that the industry is in a stable phase. The growth is expected to come from increase in revenue per user from higher usage and/or higher rates, offered for more value-added services. Even in challenging economic cycles, demand for telecom services is not expected to fall substantially as they have become a daily necessity.
- **5G and similar technology trends to drive growth in a competitive market.** The GCC region has seen launch of industry-leading technologies like 5G and Internet of Things (IoT). The technology adoption is being supported from the top, with the governments of GCC countries taking the lead in pushing adoption of latest technologies. The GCC consumers, with a predominantly young population in terms of demographics, are technology savvy in terms of adoption/migration to latest technologies. These favorable dynamics have encouraged GCC telecom providers to take the lead in launching such services. For instance, while the rest of the world is still adopting 5G, telecom operator Etisalat has already started working towards the transition to 6G, which is expected to be 100 times faster than 5G.
- **Strong financials, but valuations imply limited upside for most companies**. GCC telecom companies have reported steady financial performance over the years due to stable mature nature of the industry. The companies generate strong cashflows which also results in regular dividend payouts. At the same time, the scope for positive surprise in performance is also low. Thus, most companies are fairly valued, with select notable exceptions like Zain and Ooredoo.

The risk faced by telecom companies is from lowering of usage by consumers in a high inflationary environment, in order to balance out their overall spend.

Name	Last Px (LCY)	Target Price (LCY)	Upside / (Downside) (%)	Current P/E (x)	P/E'22e, (x)	EV/EBITDA'22e, (x)	ROE'22e, %	Cash Div Yield'22e, (%)
STC	98.0	88.6	-9.6%	17.2	16.2	8.4	16.9%	4.1%
Mobily	34.8	32.4	-6.8%	23.0	21.0	6.5	8.2%	2.9%
Ooredoo	7.8	11.6	49.5%	47.9	26.9	4.4	4.2%	1.5%
Etisalat	25.8	19.2	-25.3%	23.9	23.6	10.8	19.7%	3.8%
Zain KSA	11.3	13.8	22.5%	39.9	44.6	5.3	2.5%	0.0%
Average				30.4	26.5	7.1	10.3%	2.4%

Source: Refinitiv, U Capital Research

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Valuation

We have used a mix of DCF, EV/EBITDA, and P/E to arrive at our target price for each company. We find present value for each year over the forecast period (2022-2026e). This present value is then added to the present value of the terminal year valuation. For terminal value calculation, we use the Weighted Average Cost of Capital (WACC) and terminal growth rate for each entity.

	STC	Mobily	Ooredoo	Etisalat	Zain KSA
EV/EBITDA '22e Median Multiple	5.4	5.4	5.6	5.6	5.6
EBITDA '22e, LCY mn	23,902	5,929	9,075	21,434	3,043
Target Price, LCY	**62.7**	**25.3**	**12.4**	**14.2**	**12.6**
Weight	35%	35%	35%	35%	35%
P/E '22 Median Multiple	19.8	16.2	16.2	19.8	16.2
Earnings per share '22e, LCY	2.4	1.7	0.3	1.1	0.4
Target Price, LCY	**119.6**	**26.8**	**4.7**	**21.6**	**7.3**
Weight	35%	35%	35%	35%	35%
DCF Methodology					
PV of Future Cashflows to the Firm (LCY mn)					
2022e	12,361	2,149	4,031	11,910	1,715
2023e	9,371	2,284	3,935	11,515	1,489
2024e	9,206	2,200	3,709	11,062	1,480
2025e	8,823	2,151	3,433	10,665	1,393
2026e	8,490	2,105	3,433	10,295	1,335
Terminal Value	121,193	38,336	53,144	136,629	18,997
Total PV of Future Cashflows (Enterprise Value, LCY mn)	169,444	49,224	68,253	192,076	26,410
Weight	30%	30%	30%	30%	30%
Assumptions					
Risk Free Rate	3.9%	3.9%	4.1%	3.5%	3.9%
Risk Premium, (Equity Risk Premium)	6.3%	6.3%	6.2%	6.3%	6.3%
Beta (2 year weekly), x	0.80	0.80	0.55	1.23	0.98
Cost of Equity (COE)	8.9%	9.0%	7.5%	11.2%	10.1%
Growth Rate	1.0%	1.0%	1.0%	1.0%	1.0%
Cost of Debt (COD)	3.7%	4.1%	8.3%	3.4%	6.3%
WACC	8.1%	6.5%	7.1%	8.6%	8.1%
Debt/Equity Ratio, %	18.0%	86.6%	86.1%	45.8%	86.3%
Net Debt, LCY mn	4,138	12,777	11,433	(2,434)	5,862
Fair Value of Equity, LCY mn	165,307	36,447	60,026	194,509	20,547
Outstanding Shares, mn	1,997	770	3,203	8,697	899
Target Price, LCY	**82.8**	**47.3**	**18.7**	**22.4**	**22.9**
Weighted Average Target Price, LCY	**88.6**	**32.4**	**11.6**	**19.2**	**13.8**
Current Market Price, LCY	98.0	34.8	7.8	25.8	11.3
Upside/(Downside), %	-9.6%	-6.8%	49.5%	-25.3%	22.5%
Recommendation	**Hold**	**Hold**	**Buy**	**Sell**	**Buy**

Source: Company Financials, Refinitiv, U Capital Research

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Risks to Valuation

Key downside risks to our valuations include
• A scenario of global recession leading to fall in telecom services usage
• Increased competition among existing peers to gain market share leading to discounted sales

Key upside risks to our valuation include
• Stronger than expected demand for telecom services due to better than expected usage from international travelers to the region

Sensitivity Analysis

Our TP for Saudi Telecommunication Company SJSC (STC) is sensitive to average revenue per user (ARPU) and subscriber base. However, between them, the higher sensitivity is towards ARPU. Our TP is also sensitive (though relatively lower) to valuation inputs such as Cost of Equity (CoE) (+/- 1%) and terminal growth rate (+/- 0.25%). Between them, the higher sensitivity is towards the cost of equity.

STC AB

Terminal Growth rate	Cost of Equity: 7%	8%	9%	10%	11%
0.50%	94.1	90.3	87.3	85.0	83.1
0.75%	95.2	91.1	88.0	85.5	83.5
1.00%	96.4	92.0	**88.6**	86.0	83.9
1.25%	97.7	92.9	89.3	86.5	84.3
1.50%	99.2	94.0	90.1	87.1	84.8

Subscriber base mn	ARPU (SAR mn): 192	197	202	207	212
26.59	76.7	80.8	84.9	89.0	93.1
27.09	78.5	82.6	86.8	90.9	95.0
27.59	80.2	84.4	**88.6**	92.8	97.0
28.09	82.0	86.2	90.5	94.8	99.0
28.59	83.7	88.1	92.4	96.7	101.0

Our TP for Etihad Etisalat Company SJSC (Mobily) is sensitive to average revenue per user (ARPU) and subscriber base. However, between them, the higher sensitivity is towards ARPU. Our TP is also sensitive (though relatively lower) to valuation inputs such as Cost of Equity (CoE) (+/- 1%) and terminal growth rate (+/- 0.25%). Between them, the higher sensitivity is towards the terminal rate.

EEC AB

Terminal Growth rate	Cost of Equity: 7%	8%	9%	10%	11%
0.50%	34.9	32.8	31.1	29.7	28.5
0.75%	35.9	33.6	31.7	30.2	28.9
1.00%	37.0	34.5	**32.4**	30.7	29.3
1.25%	38.2	35.4	33.2	31.4	29.8
1.50%	39.5	36.4	34.0	32.0	30.4

Subscriber base mn	ARPU (SAR mn): 99	104	109	114	119
10.64	17.8	22.4	27.0	31.7	36.3
11.14	20.2	24.9	29.7	34.5	39.3
11.64	22.6	27.5	**32.4**	37.4	42.3
12.14	24.9	30.0	35.1	40.2	45.3
12.64	27.3	32.6	37.8	43.0	48.3

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Our TP for Ooredoo QPSC is sensitive to Qatar average revenue per user (ARPU) and subscriber base. However, between them, the higher sensitivity is towards subscriber base. Our TP is also sensitive (though relatively lower) to valuation inputs such as Cost of Equity (CoE) (+/- 1%) and terminal growth rate (+/- 0.25%). Between them, the higher sensitivity is towards the terminal rate.

QTEL UH

Terminal Growth rate	Cost of Equity: 5%	6%	7%	8%	9%
0.50%	12.4	11.7	11.2	10.7	10.3
0.75%	12.7	12.0	11.4	10.9	10.5
1.00%	13.0	12.2	**11.6**	11.1	10.6
1.25%	13.3	12.5	11.8	11.3	10.8
1.50%	13.7	12.8	12.1	11.5	11.0

Subscriber base mn	Qatar ARPU (QAR): 101	106	111	116	121
1.9	10.1	10.3	10.4	10.6	10.7
2.4	10.7	10.8	11.0	11.2	11.4
2.9	11.2	11.4	**11.6**	11.8	12.0
3.4	11.7	12.0	12.2	12.4	12.6
3.9	12.3	12.5	12.8	13.0	13.3

Our TP for Emirates Telecommunications Group Company PJSC (ETISALAT) is sensitive to UAE average revenue per user (ARPU) and subscriber base. However, between them, the higher sensitivity is towards subscriber base. Our TP is also sensitive (though relatively lower) to valuation inputs such as Cost of Equity (CoE) (+/- 1%) and terminal growth rate (+/- 0.25%). Between them, the higher sensitivity is towards the terminal rate.

ETISALAT UH

Terminal Growth rate	Cost of Equity: 9%	10%	11%	12%	13%
0.50%	20.2	19.5	18.9	18.5	18.0
0.75%	20.4	19.7	19.1	18.6	18.1
1.00%	20.7	19.9	**19.2**	18.7	18.3
1.25%	21.0	20.1	19.4	18.9	18.4
1.50%	21.2	20.3	19.6	19.0	18.5

Subscriber base mn	UAE ARPU (AED): 886	936	986	1,036	1,086
9.2	17.7	18.0	18.3	18.6	18.9
10.2	18.2	18.5	18.8	19.1	19.4
11.2	18.6	18.9	**19.2**	19.6	19.9
12.2	19.0	19.4	19.7	20.1	20.4
13.2	19.4	19.8	20.2	20.6	21.0

Our TP for Mobile Telecommunication Co. (ZAIN KSA) is sensitive to average revenue per user (ARPU) and subscriber base. However, between them, the higher sensitivity is towards ARPU. Our TP is also sensitive (though relatively lower) to valuation inputs such as Cost of Equity (CoE) (+/- 1%) and terminal growth rate (+/- 0.25%). Between them, the higher sensitivity is towards the terminal rate

ZAINKSA AB

Terminal Growth rate	Cost of Equity: 8%	9%	10%	11%	12%
0.50%	14.7	14.0	13.4	12.8	12.4
0.75%	15.0	14.2	13.6	13.0	12.5
1.00%	15.3	14.5	**13.8**	13.2	12.7
1.25%	15.7	14.8	14.1	13.4	12.9
1.50%	16.1	15.1	14.3	13.6	13.1

Subscriber base mn	ARPU (SAR mn): 75	80	85	90	95
7.00	11.0	12.4	13.8	15.2	16.6
7.50	11.0	12.4	13.8	15.2	16.6
8.00	11.0	12.4	**13.8**	15.2	16.6
8.50	11.0	12.4	13.8	15.2	16.6
9.00	11.0	12.4	13.8	15.2	16.6

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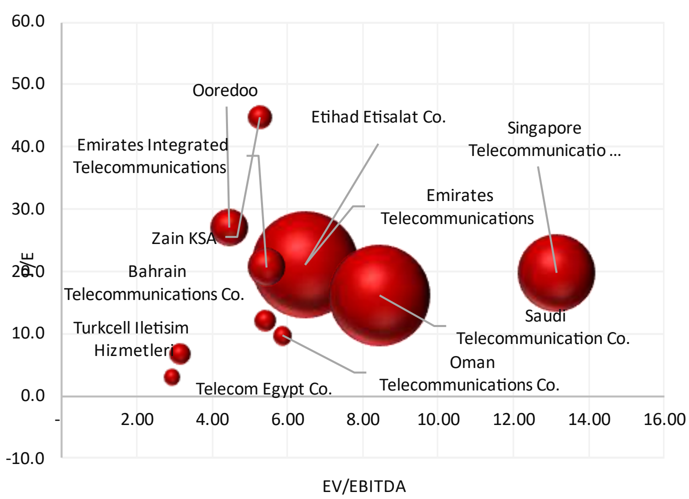
Peer Group Valuation

Peer Group

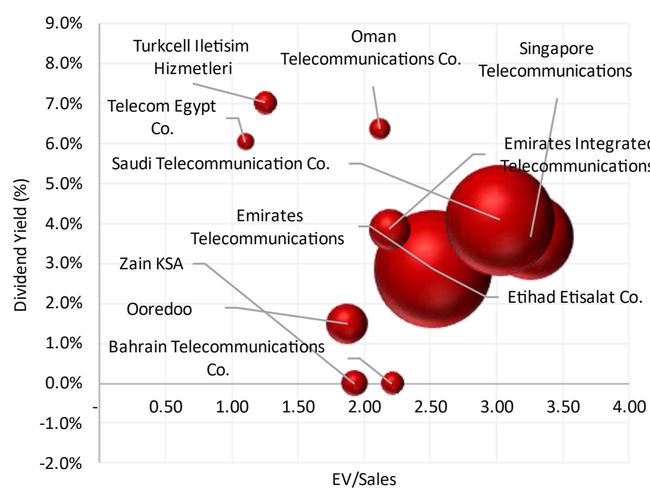
Name	Mkt Cap (USD bn)	Last Px (Local Currency)	Px Change 1M, %	Px Change 3M, %	Px Change YTD, %	Current EV/EBITDA (x)	EV/EBITDA '22e (x)	P/E '22e (x)	EV/Sales '22e (x)	Div Yield '22e
Mobily	7.2	34.8	-8.4%	-14.4%	11.7%	6.8	6.5	21.03	2.52	2.9%
Zain KSA	2.7	11.3	-14.4%	-15.7%	-6.3%	5.0	5.3	44.65	1.92	0.0%
Etisalat	59.9	25.8	-12.4%	-33.2%	-18.7%	8.5	6.5	21.03	2.52	2.9%
STC	52.8	98.0	-3.7%	-13.4%	-12.8%	8.5	8.4	16.20	3.02	4.1%
Ooredoo	6.9	7.8	4.7%	9.7%	10.5%	3.1	4.4	26.93	1.87	1.5%
Du	7.2	5.8	-2.3%	-11.4%	-11.8%	5.7	5.4	20.71	2.19	3.9%
Batelco	2.1	0.5	-4.0%	-12.3%	-16.8%	5.6	5.4	12.10	2.21	NA
Singtel	30.9	2.6	0.8%	-2.3%	12.1%	12.6	13.1	19.77	3.26	3.7%
Telecom Egypt	1.2	13.2	-12.3%	-22.8%	-21.2%	3.1	2.9	2.96	1.10	6.1%
Turkcell Iletisim Hizmetleri	2.2	17.6	-9.4%	-21.0%	-6.4%	3.2	3.1	6.66	1.25	7.0%
Omantel	1.7	0.9	0.0%	0.5%	14.9%	5.9	5.9	9.64	2.12	6.4%
Average						**6.2**	**6.1**	**18.34**	**2.18**	**3.8%**
Median						**5.7**	**5.4**	**19.77**	**2.19**	**3.8%**

Peer Group Valuation (2022E)

EV/EBITDA vs P/E



EV/Sales vs Dividend Yield (%)



Source: Refinitiv; valuation as of 6th July 2022; Size of the bubble indicates market capitalization in USD bn

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Local Peer Group Analysis

The Saudi Arabia Telecom market is currently dominated by three players holding unified licenses namely, Etihad Etisalat Company (Mobily), Saudi Telecom Company (STC), and Mobile Telecommunication Company Saudi Arabia (Zain KSA) apart from Etihad Atheeb Telecommunication which are included in the telecom index. Among the three key telecom players, STC is the biggest with regard to market capitalization at USD 195.8 bn followed by Mobily at USD 26.8 bn which is followed by Zain KSA at USD 10.1 bn. Apart from providing traditional telecom services, telecom companies are now shifting their focus and growing their presence through providing technology-based services while trying to digitize to the extent possible. This is expected to drive the next phase of growth.

Saudi Arabia was among the first countries in the MENA region to launch 5G networks in 2019. In October 2019, Zain KSA launched the third largest 5G network worldwide and the largest 5G network in the Middle East, Europe, and Africa. According to one of the leading magazines, the total number of governorates covered by 5G is~ 60. Internet users grew at a CAGR of ~7% between 2017 and 2021 and internet penetration expected to reach around 97.6 % by 2026. The kingdom is currently witnessing increasing inclination towards cloud-based solutions which is evident from the introduction of the Cloud First Policy in 2019. During 2021, Ministry of Communications and Information Technology (MCIT) launched an USD 18 bn plan to build a network of large-scale data centers across the kingdom.

Currently Saudi Arabia's Information and Communications Technology (ICT) market is valued at over USD 32.1 bn and is considered to be the largest in the Middle East and North Africa (MENA) region. The ICT market is all poised to become a technology service and cloud centre where accessibility to international markets European, Asian, and Africa is achieved through the Red Sea and the Gulf. The key sub sectors of ICT include Internet of Things (IoT), Cloud Computing and 5G amongst others. According to the International Data Corporation, Saudi Arabia's IoT market is estimated to reach USD 2.9 bn by 2025 with an annual growth rate of 12.8%. Several smart cities are being built in the kingdom with the goal to become the highly connected and accessible nation by 2030.

In the UAE telecom space, the main players are Etisalat and Du, occupying the majority of the market share. Additionally, Virgin Mobile UAE is another service provider as a mobile virtual network operator or MVNO. In the Qatar telecom space, Ooredoo and Vodafone Qatar are the main two telecom service providers.

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KSA Telecom Sector

Overview:

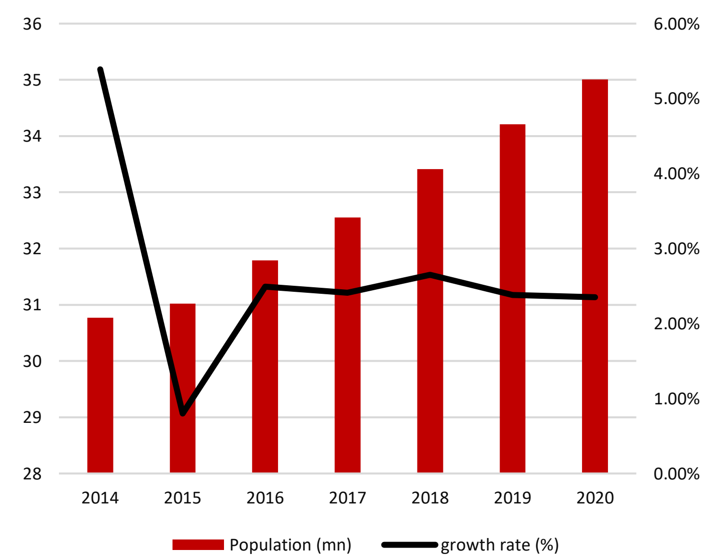
Telephone services were introduced in KSA as early as 1934. Since then, it has had many landmark moments such as the launch of the first fiber optic network in 1984, commencement of mobile phone services in 1995, and liberalization of the telecom market in 2003, which allowed private players to enter the sector. The ICT was the first sector to be privatized in Saudi Arabia. Liberalization started in 2003 with the issue of VSAT service provisioning (2003) and Data services provision (2005). The Communication and Information Technology Commission (CITC) first granted licenses for Mobile virtual network operators (MVNO) in 2014 and so far, four licenses have been issued. As per CITC figures, the Saudi telecom sector contributed 5.3% to the national GDP for the year 2020, growing 4% from 2019. The evolution of the sector is ongoing and with the arrival of 5G, new growth avenue has opened for the operators.

Saudi Arabia's telecom sector is the largest sector in the MENA region in terms of revenue. The telecom industry in Saudi Arabia is saturated in terms of mobile penetration, which reached 115% for the year 2021 with total 41.2 mn number of mobile users. The telecom industry is dominated by 4 players namely Etihad Etisalat Company (Mobily), Saudi Telecom Company (STC), Mobile Telecommunication Company Saudi Arabia (Zain) and Etihad Atheeb Telecommunication Company.

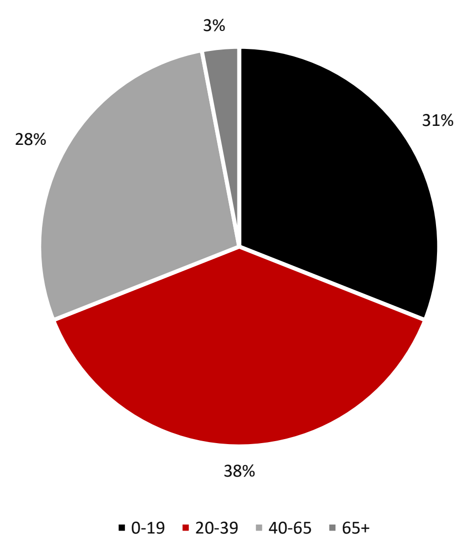
Young population-Driving force for the telecommunication industry

As per CITC, 93% of the Saudi Arabia's population has access to the internet as compared to the global average of 53%. Moreover, Saudi Arabia demographics is skewed towards younger population with 69% of the population below the age of 40. This younger and tech-savvy population is expected to drive demand for ICT services. Additionally, the rising percentage of population using smartphones, along with the improvement of services coupled with technological and infrastructural upgrades, the number of internet users are expected to increase. Mobile usage in Saudi Arabia has also increased due to recent rebound in expat population.

Population (mn) and growth (%)



Population distribution by age (2020)



Source: STC Q4 2021 investors presentation

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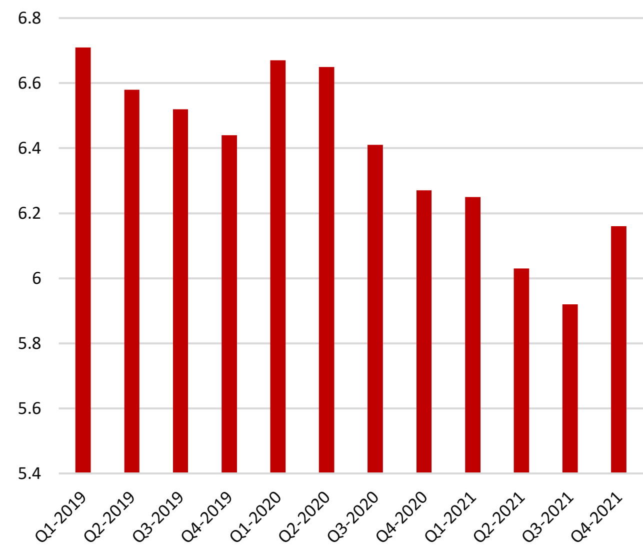
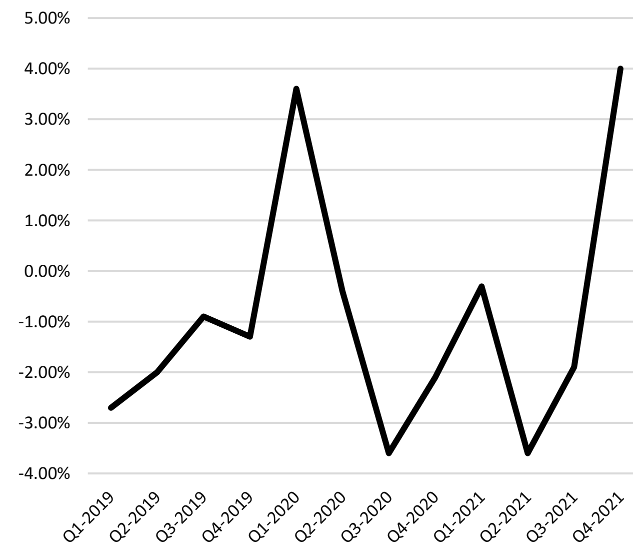
Expat population (mn)



Expat population growth (%)

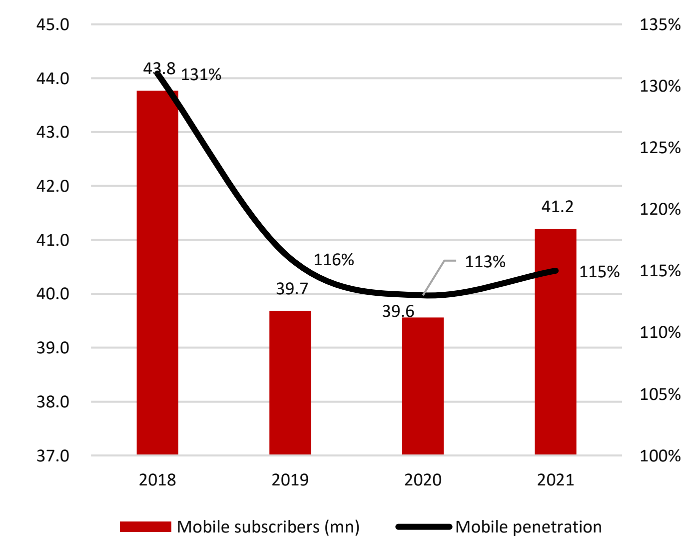


Source: Q4 2021 STC investors presentation

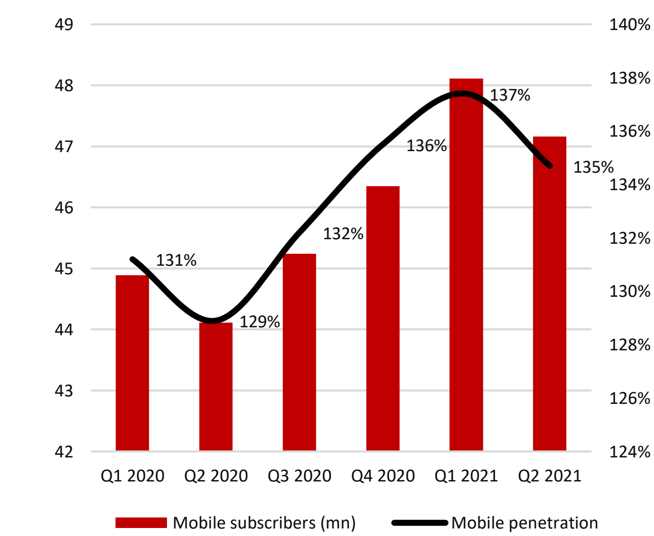
5G development and data to support growth in Average revenue per units (ARPUs)

Globally, telecommunication companies have witnessed a shift in revenue streams from traditional revenue sources such as voice and messaging revenue to more data driven, web-based revenue streams. Saudi Arabia's telecom market is a saturated with more than 100% mobile penetration, which implies lack of opportunities for telecom companies within the kingdom to grow voice services business. However, scope persists for the telecom companies to broaden their range of revenue streams towards data driven, internet revenue streams.

Mobile subscribers (mn) and penetration (%)-annual



Mobile subscribers (mn) and penetration (%)-quarterly



Source: Etisalat annual reports and CITC Q1 2021 presentation

Saudi Arabia was amongst the first countries in the GCC region to launch 5G network in 2019. STC was the first company to launch 5G services in the kingdom through its broadband network. Saudi Arabia has increased the number of areas covered by 5G network at a robust pace in 2021. The top companies in the kingdom have focused largely on investing and growing its 5G business. Accordingly, they have incurred capex on network upgradation for past three years till 2021. These capital expenditures were aligned with the plan

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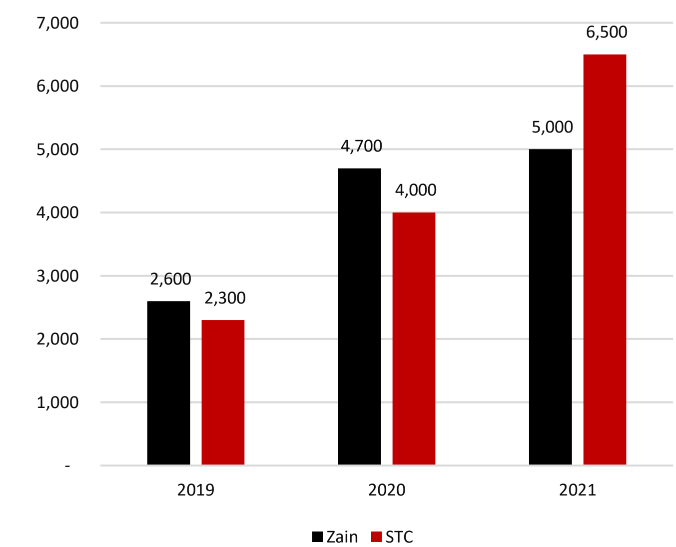
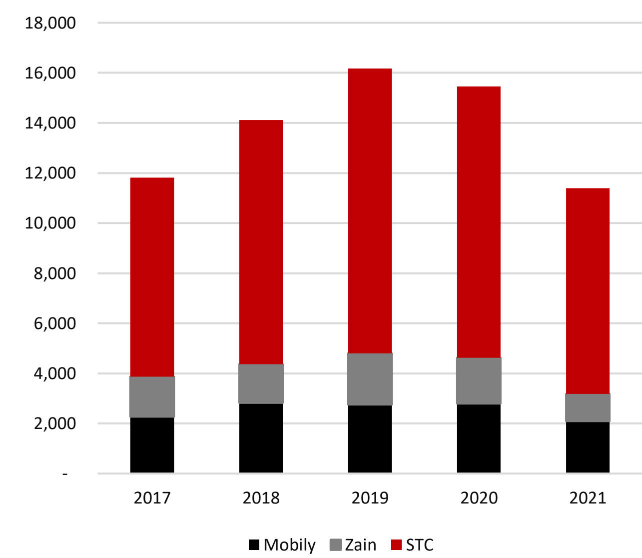
to increase 5G services within the kingdom and spectrum acquisition. By Q3 2021, the total number of governorates covered by 5G increased to 76, as compared to 53 in Q1 2021. Saudi Telecom Company (STC) has the highest coverage with 60 deployments, followed by Zain at 46 and Mobily at 20 governorates. Quick 5G development has also led to an increase in average usage speed for users.

5G network and ICT infrastructure are a crucial part of the kingdom's plan to develop smart cities. The Kingdom has invested around USD 4 billion annually in digital infrastructure, fiber infrastructure, internet networks and 5G services. ICT is a crucial aspect as it connects the different components of the infrastructure. Saudi Arabia aims to plan 10 smart cities in total, with NEOM, a USD 500bn project and Al Qiddiya the kingdoms entertainment, sports, and cultural hub.

Number of 5G Towers

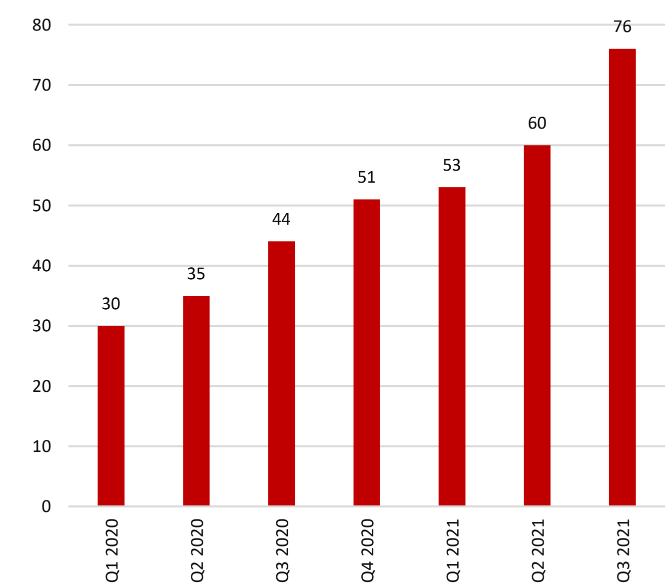


Annual capex (SAR mn)

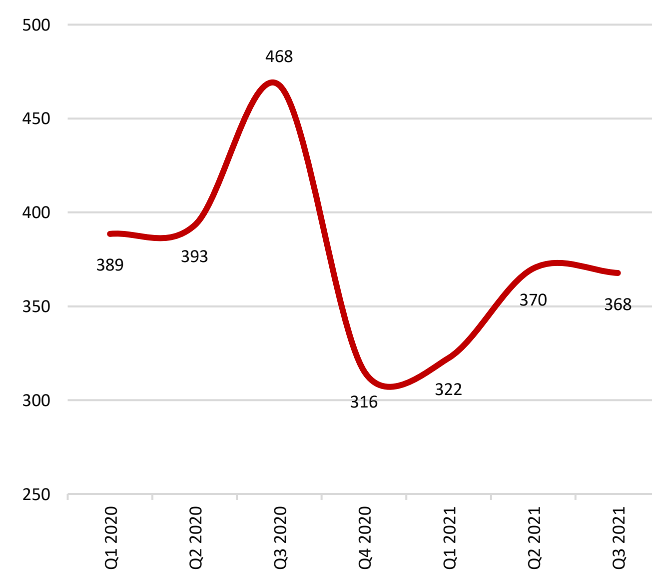


Source: Company Financials. Note: Capex includes Addition to property, plant & equipment, and addition to intangible assets

Governates covered by 5G services



Average 5G download speed (Mbps)



Source: CITC Meqyas Q3 2021 presentation

In 2020, the CITC announced an open access initiative to allow all retail operators to offer their Fibre-to-the-home (FTTH) broadband services to every house in Saudi Arabia. The initiative was undertaken to improve competition and provide competitive prices to

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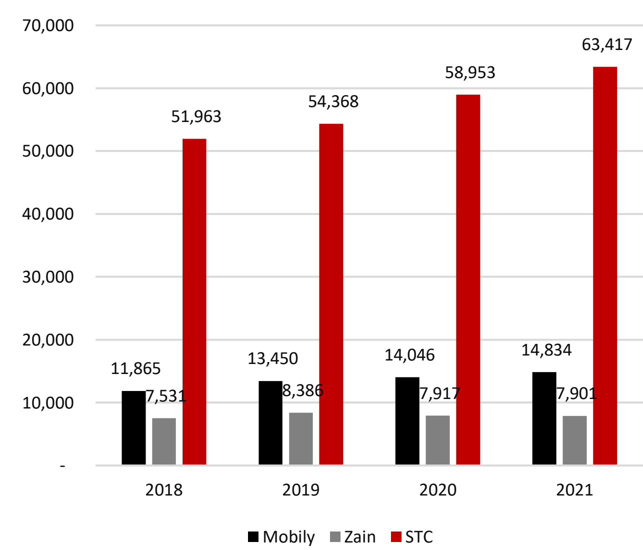
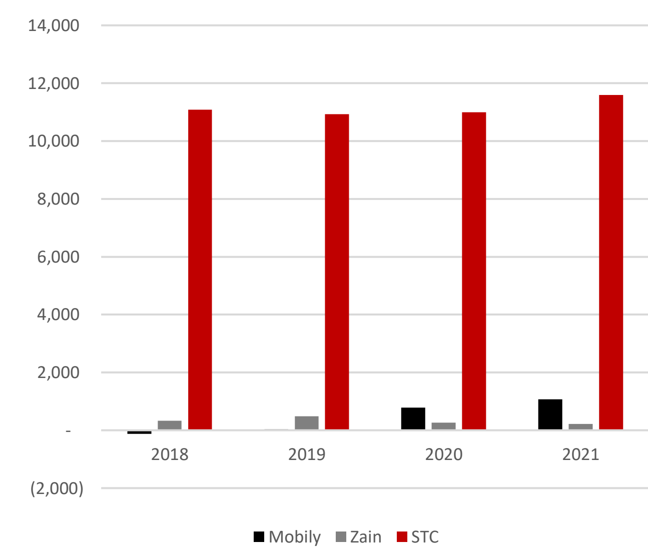
customers. With this announcement, the kingdom aimed at adding 3mn houses to the fiber network. The growth in 5G investments, FTTH and shift in income streams have had a drastic impact on the top 3 companies financials. The top line for Mobily and STC grew at a CAGR of 5.74% and 5.11% since 2018 primarily due to shift in revenue streams, while Zain only grew at a CAGR of 1.21%. However, the share of data revenue for Zain increased to 48% in 2021, whereas, for Mobily the growth in revenue was driven by an increase in mobile subscribers and FTTH revenue.

STC, which has 73.6% of the market share by revenue in KSA and which has 34% of the 5G coverage in Saudi Arabia was at the helm of growth in the kingdom. It benefited by the Internet of Things (IoT) enabled by 5G technology, and achieved its highest revenue in 9 years, to reach SAR 63.42bn. This was largely driven by 10.3% increase in FTTH subscribers and 21.7% wireless subscribers in their consumer business segment.

Revenue trend (SAR mn) of Saudi Telecom companies



Net income trend (SAR mn) of Saudi Telecom companies



Source: Company Financials

Encouraging government reforms

In 2016, to reduce mobile users from taking part in activities that threaten national security, the Saudi Ministry of interior started fingerprint anyone willing to buy a SIM card as a security measure. This led to a decrease in revenue due to drop in mobile revenue subscribers. In October 2016 the CITC announced the extension of telecom licenses by 15 years which was aligned with the kingdoms plan to support vision 2030.

On a company level, for Zain, the extension was fruitful. The extension saved SAR 433mn per year for the company in the form of amortization charge of the license. Zain was offered a unified license which allowed it to provide all telecom services including fixed voice and data services to its customers. Mobily, which is part owned by Etisalat, boost its finances by SAR 260m per year due to the license extension. However, STC had no meaningful gain.

To encourage competition and create more options for customers, CITC announced the opening of Mobile virtual network operators (MVNO) licenses in 2013. Virgin mobile and Jawraa Lebara which were the first companies to receive MVNO licenses. In 2020, CITC provided two more licenses to Integrated telecommunications Mobile company and Future networks for communications company. Overall, currently there are 7 companies that provide telecom services in Saudi Arabia.

In 2020, CITC announced the reduction of termination rates for local mobile and fixed calls. This was announced to encourage, fair competition in the kingdom and provide affordable rates to consumers. Local mobile termination rates (MTR) were set at SAR 0.022 and Fixed termination rates (FTR) were set at 0.011, a drop of 60% and 48% respectively.

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Foreign Investments being attracted to boost ICT sector

The ICT sector in Saudi Arabia is dominated by local players. Between January 2010 and 2019, the ICT sector only received 3% of cumulative FDI inflows. However, in the recent past this trend is expected to change due to the implementation of the vision 2030 program.

The Vision 2030 program has an optimistic view to increase the Saudi Arabia's ICT sector contribution to GDP from 3.6% in 2017 to 4.6% in 2023. It is expected that most of the growth will be driven by IoT and IT. The inward foreign investments are expected to only bring in necessary capital for expansion but also improve management, technical know- how and allow international entry to companies in KSA.

However, there are challenges such as relatively low population, competition among existing firms and dominance of local players. To overcome such challenges, government organizations such as MCIT, SAGIA (Saudi Arabian General Investment Authority) and CMA (Capital Market Authority) have made changes to improve foreign inflows. These include:

- CMA removed the 49% cap on foreign ownership for foreign investors.
- Removal of several industries from the negative list created earlier which limited the activities of wholly owned Saudi companies.
- MCIT developed a national ICT strategy for 2023 which outlines that Saudi Arabia is expected to increase its spending from SAR 14.48 trillion in 2021 to SAR 20.03 trillion by 2025 and spend more than USD 32.9bn for the ICT sector in 2022. The strategy is also aimed at improving employment in the ICT sector, creating more than 25,000 jobs, and increasing the size of the sector by 50%.

Overall, the government is in favour of increasing foreign participation. The Saudi Arabia's Ministry of Investment issued 2,056 new investment licenses to foreign companies in Q4 2021, a huge rise of 358% from 449 a year earlier. The licenses increased from 478 in Q1 2021 to 575 in Q2 2021 to 1,330 in Q3 2021.

Outlook

With the focus on improving the 5G segment by each company accompanied with government support and reforms the IT sector looks promising after a strong recovery in performance by the sector. With rising demand for 5G and early adoption of 5G technology, has placed Saudi Arabia at the top in terms of 5G market. In 2021 the government reforms include:

- CITC launched a 3rd phase of local roaming service in the rural areas
- MCIT announced a partnership between NEOM and OneWeb worth USD 200mn to provide a satellite network that will change broadband networks in Middle East and Africa.

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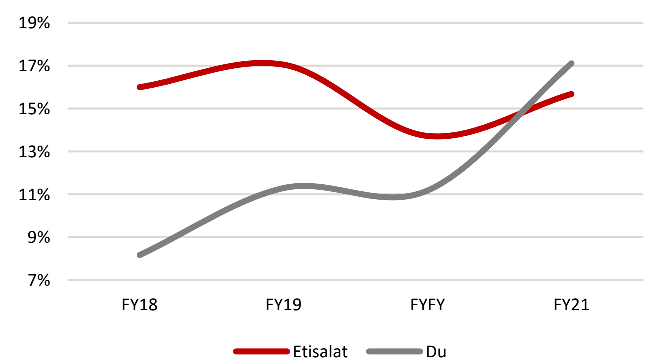
UAE Telecom Sector

Overview

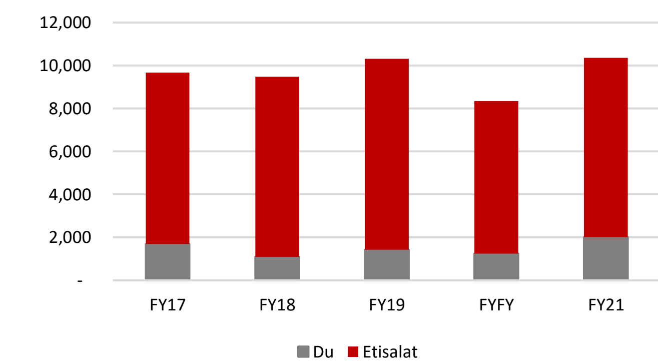
The telecom sector in the UAE is at an advanced stage with the adoption of 5G, plans to launch 6G and introduction of new products. The Telecommunications and Digital Government Regulatory Authority (TDRA) is the sectoral regulator, responsible for formulating policies and managing infrastructure. Until 2006, the sector was a monopoly of Etisalat. This changed with the formation of Du, another telecom company. Du commenced providing ICT services in free zone areas, in turn, making the sector a duopoly. However, since the areas in which the companies operated were different, the companies did not compete and were, in effect, monopolies in their areas.

The country is among the fastest in 5G and fixed broadband download speeds. 5G penetration is increasing in the country. Additionally, the high speed is due to increasing investment in fiber instead of legacy copper networks. The increase in the number of people working from home as well as higher time spent online for entertainment and other purposes during lockdowns, has increased the demand for faster internet speeds. In response to this, companies are investing more in capex and infrastructure. Etisalat announced transitioning plans to 6G in July 2021. The company expects 6G to be 100 times faster than 5G and can be a growth driver for the sector. A key feature of this growth is focus on capital investments by the companies, with over capex exceeding 15% of revenues.

Capex as % of Revenues



Capex (AED mn)



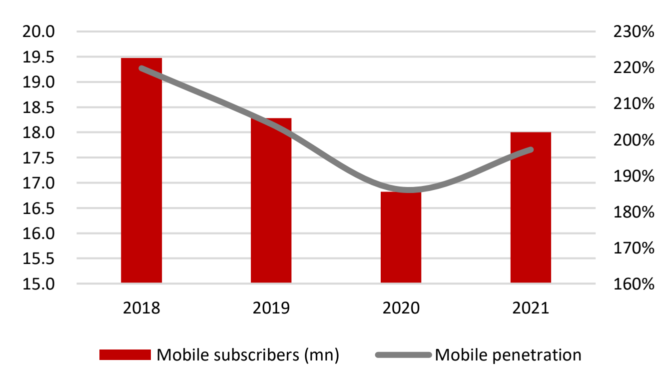
Source: Company Filings

Mordor Intelligence expects the market to grow by 3.5% between FY22-FY27. Given below are the major growth drivers of this market.

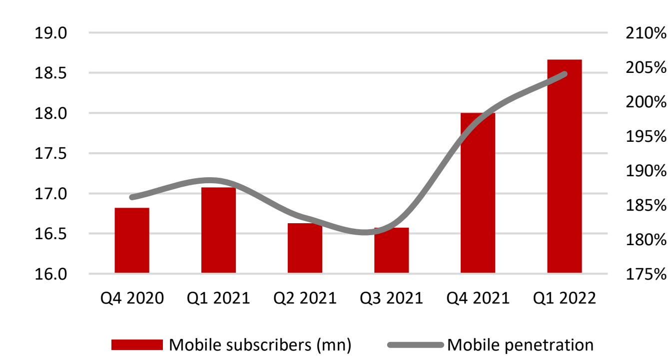
Market moving toward saturation

The UAE market seems to be moving towards saturation. The mobile penetration rate increased to 204% in 1Q22, the highest since 2020. This indicates that subscriber growth may be limited in the future, driven mainly through population increase, rather than increase in penetration. Consequently, ARPU growth will be the major growth driver for the sector. Launch of new products and introduction of 6G may provide opportunities to increase ARPU. However, the rising interest rates and the expected US recession may put pressure on consumers' spending abilities and constrain ARPU in the near to medium term.

Mobile subscribers (mn) and penetration (%)-Annual



Mobile subscribers (mn) and penetration (%)-quarterly



Source: TRDA

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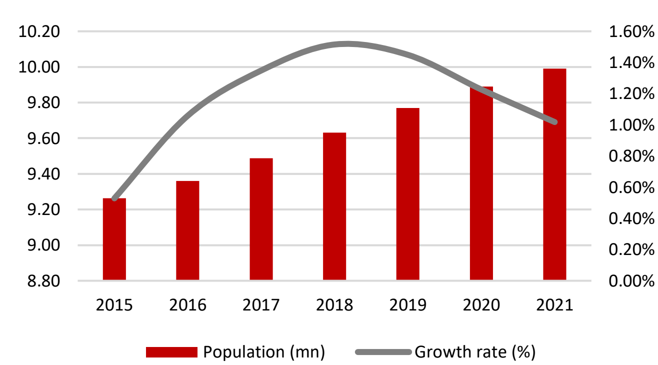
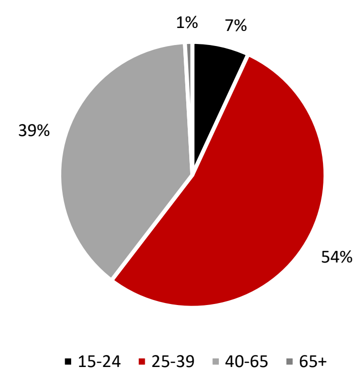
Favourable demographics

The population of the UAE has grown at a CAGR of 1.3% between FY15 and FY21. Population growth ultimately leads to growth in number of subscribers and contribute to sector revenue growth. Furthermore, younger population is more likely to contribute to growth of the sector by spending on newer technologies and products. The median age of UAE's population was 32.8 years in 2020. Additionally, more than half of UAE's workforce is between 25-39 years old.

Population Census



Labor Force distribution by age



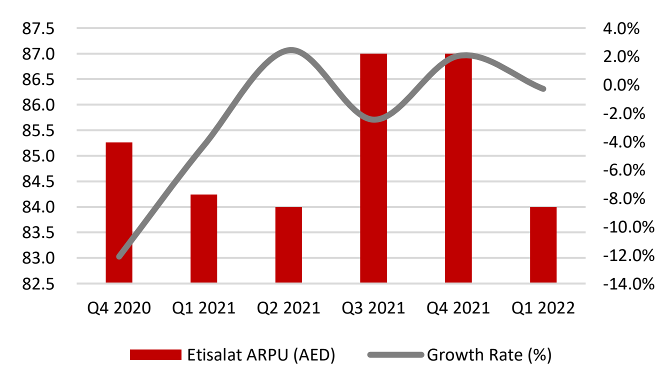
Source: The World Bank, Federal Competitiveness and Statistics Centre

Increasing 5G penetration and partnerships with foreign players to drive ARPU growth

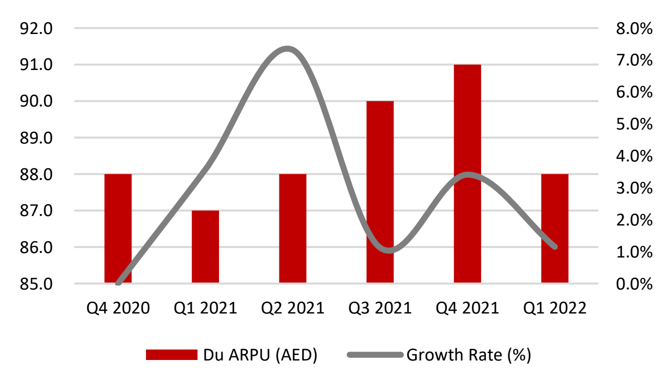
Similar to other countries, UAE telecom companies are earning an increasing portion of their revenues from mobile and internet-based subscriptions. During the lockdowns, as more people stayed home, the demand for mobile and TV services surged. As consumers replace their traditional phones with 5G-enabled smartphones, 5G penetration should rise leading to growth in ARPU. This trend will be complimented by consumers using more than one device and high device replacement rates.

Telecom companies are also launching new products with the intention of increasing ARPU. Companies are also partnering with foreign players to launch products. In 2021, Etisalat partnered with Nokia to provide improved mobile broadband services and increase 5G coverage. Yahsat, a telecom firm, has entered into a solution system integrator partnership agreement with Delta Bridge, through its mobile satellite subsidiary, Thuraya. The partnership will then provide secure satellite communication services and other applications to government and defense clients. 5G also has several applications in the growth of Internet of Things (IoT), which may further provide opportunities in ARPU growth.

Etisalat ARPU Growth



Du ARPU Growth



Source: Company Data

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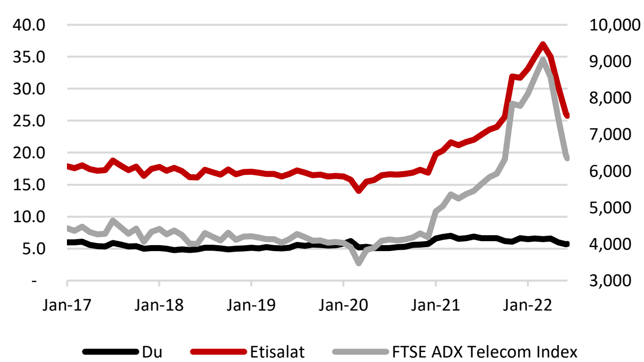
Dubai Plan 2021

The Dubai Plan 2021, announced by the Dubai Government aims to turn Dubai into smart and sustainable city. The plan focuses on six sectors, including communications, through the transformation of 1,000 government services. Other government initiatives such as Smart Dubai 2021, Dubai 10X, Dubai Data Strategy, Dubai Pulse Platform and Dubai Blockchain Strategy aim to transform the city into a model smart city. These initiatives may provide several growth initiatives to telecom companies and contribute to the growth of the sector.

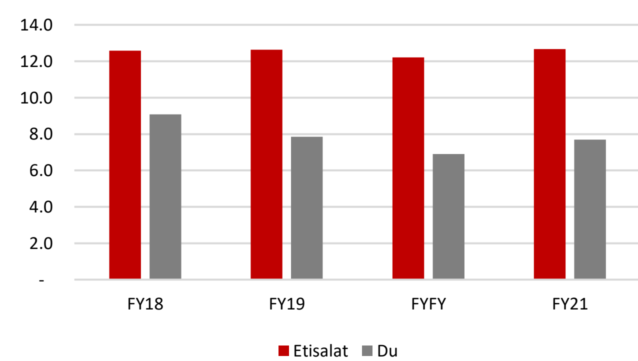
Outlook

While the market seems to be moving towards saturation, opportunities for growth still exist. Favorable government policies and adoption of new technologies such as IoT may boost growth. Furthermore, the increasing adoption of 5G coupled with high rate of device replacement, as well as consumer demand for speed indicates growth support to ARPU. Launching new products, especially by partnering with foreign players may spur innovation and increase growth. The UAE telecom market is now a defensive play rather than a growth play due to market saturation and stable companies.

UAE Telecom Sector Price Performance

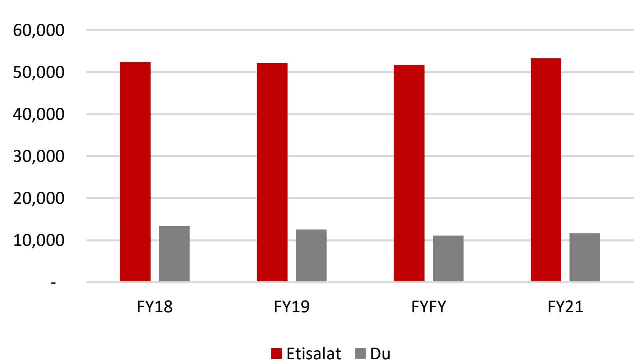


Total Subscribers (in mn)

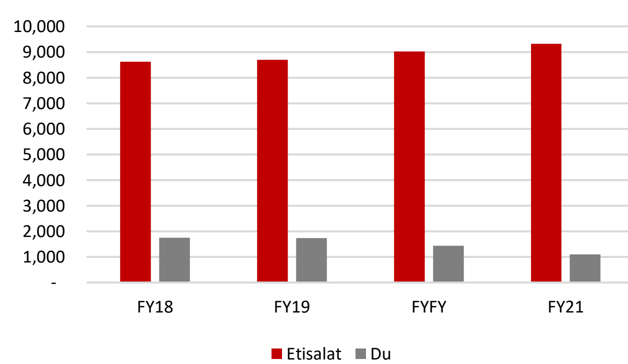


Source: Bloomberg, Company Data

UAE Telecom Companies Revenue (AED mn)



UAE Telecom Companies Net Income (AED mn)



Source: Company Data

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Saudi Telecommunication Company SJSC (STC)

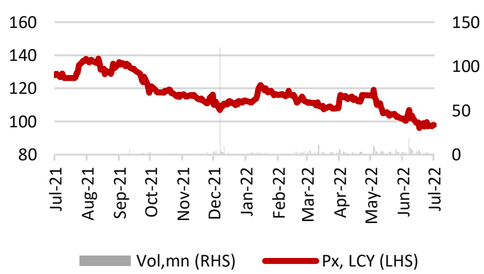
Target Price: SAR 88.6

Downside: 9.6%

Recommendation	**Hold**
Bloomberg Ticker	STC AB
Current Market Price (SAR)	98.00
52wk High / Low (SAR)	138 / 96.1
12m Average Vol. (mn)	2.4
Mkt. Cap. (SAR bn)	195.7
Shares Outstanding (mn)	1,997
Free Float	36.0%
3m Avg Daily Turnover (SAR mn)	374.8
6m Average Daily Turnover (SAR mn)	299.2
PE 2022e	16.2x
EV/EBITDA 2022e	8.4x
Dividend Yield '22e	4.1%
Price Performance:	
1 month (%)	-3.5%
3 months (%)	-15.5%
12 months (%)	-23.9%

Source: Refinitiv, as of 6th July 2022

Price -Volume Performance



Source: Refinitiv

- **Diversified business model helps provide stability to revenues and earnings**
- **One of the largest telecom companies in Saudi Arabia**
- **Healthy dividends to support returns**
- **Technology and Banking businesses may provide significant upside potential**

We initiate coverage on Saudi Telecommunication Company SJSC (STC) with a Hold rating and a target price of SAR 88.6 per share, implying a downside of 9.6% to the last closing price (6 July 2022). Our target price implies a P/E'22e of 36.6x. The stock has fallen in the recent past, owing to the uncertainty caused by the Russia-Ukraine war, rising inflation and interest rates and recession fears.

Investment Thesis

Valuation & Risks: Our valuation is based on a mix of discounted cash flows (30% weight), EV/EBITDA multiple (35% weight) and P/E multiple (35% weight). Key downside risks include an adverse change in regulations, poor M&A execution. Key upside risks include faster growth in the non-core businesses such as technology and stc Bank, expansion in newer markets, sale of the tower business and cash generation from monetization of the company's subsidiaries.

Diversified business model adds stability to revenues and earnings

STC operates in several business segments such as the telecommunications, media services, information technology and banking. Telecommunications is the main segment and helps provide stability to the business as well as finance growth opportunities. Regarding the banking segment, STC is engaged in the banking business through stc Bank (formerly stc Pay) which has the license to operate as a digital bank. Segments such as banking and information technology are expected to be the major growth drivers. Additionally, these businesses have different economic drivers, which make the combined entity more resilient in the face of a macroeconomic crisis.

Largest Telecom company in Saudi Arabia

STC is the largest telecom company in the country with exposure to different businesses. Investment in the company can be seen as a proxy to investment in the Saudi telecom sector as well as the entire economy, especially the non-oil sector. The country also stands to benefit from the Kingdom's focus on diversification and focus on growth of the non-oil sector.

Key Indicators

Year (In SAR mn)	FY19	FY20	FY21	FY22e	FY23e	FY24e
Sales	54,368	58,953	63,417	66,784	69,992	73,015
Gross profit	32,391	33,954	33,794	35,953	37,621	39,257
EBITDA	21,265	22,090	22,841	23,902	25,258	26,417
Operating profit	12,480	12,731	13,128	14,035	14,644	15,025
Net income	10,925	11,185	11,595	12,352	13,576	13,993
EPS	5.33	5.50	5.66	2.42	2.66	2.74
P/E (x)	18.8	19.4	19.9	16.2	14.7	14.3
EV/EBITDA (x)	9.8	9.8	10.1	8.4	8.0	7.6
Dividend yield, %	6.0%	5.6%	3.6%	4.1%	5.1%	6.1%

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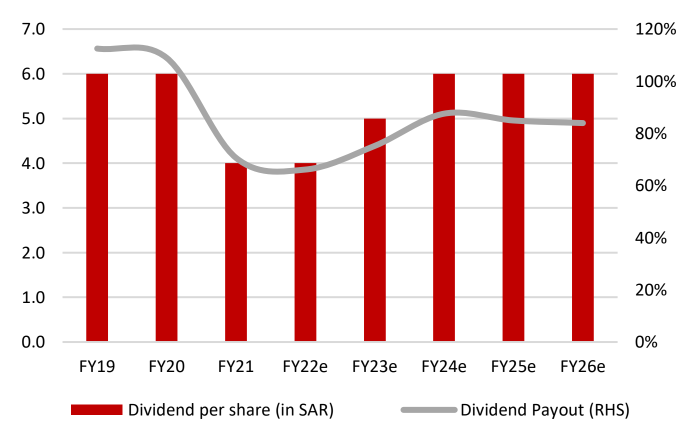
Significant Upside Potential from Asset Monetization

STC has a significant upside potential due to monetization of its ownership in various non-core businesses. The company's management claims to have undertaken the process of making subsidiaries IPO-ready. In 2021, the company monetized its stake in stc Solutions through the IPO route. The company can similarly benefit from monetization in subsidiaries such as Tawal, which operates the tower business; STC Pay, which operates the digital banking business; Aqalat, which operates the real estate business; and its data center business. The company is in the process of transferring the datacenter business to a new subsidiary, which will enhance opportunities for monetization. Monetization can help in significant cash generation, which can lead to higher dividends or free cash to pursue growth opportunities. Additionally, the company may retain control over the monetized assets by owning a majority stake in those companies.

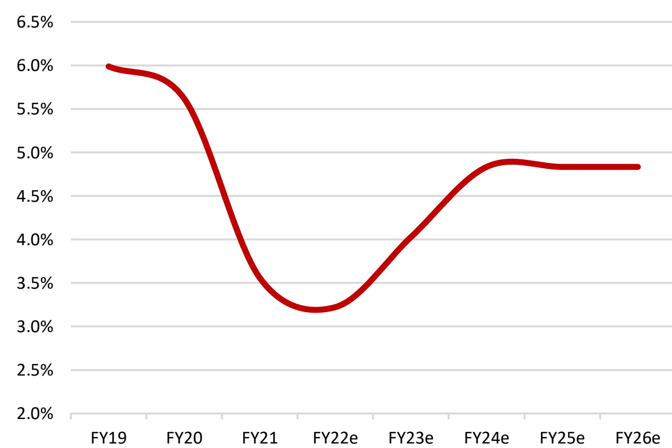
Strong dividend payout visibility on back of improved business performance

STC is seen to maintain a high dividend payout ratio and is seen to maintain a healthy dividend yield around 5%. The company has a new dividend policy whereby it strives to maintain a minimum dividend of SAR 1.6 annually (post-bonus) or SAR 4 per share (pre-bonus). This translates to an annual dividend payment of nearly SAR 8 billion. The company is expected to pay the minimum dividend amounts as the management plans to conserve cash for M&A activities to increase growth. Dividend payments may be higher as the company's financial position improves or it fails to find suitable targets.

Dividend per share (pre-bonus) and Dividend Pay-out Ratio



Movement in Dividend Yield



Source: Company Filings

Bonus issue can enhance returns

STC has announced a 1.5:1 bonus issue, which means that every shareholder who holds shares on the eligibility date will be entitled to 1.5 bonus shares for every 1 existing share held. Due to this, the share capital of the company will be increased from SAR 20bn to SAR 50bn. The bonus issue will be financed from retained earnings, which will be reduced by SAR 30bn. The bonus issue is beneficial to the shareholders as it will lead to higher liquidity in the market and increase stock price in the shorter term as investors buy stock to become eligible for the bonus issue.

Margins to face pressure

We expect gross margins to remain stable. However, operating margins are expected to face pressure due to increase in operating expenses such as SG&A and higher depreciation and amortization expenses due to high capex levels. Depsite the margin presssure, we expect gross and operating profits to increase due to revenue growth.

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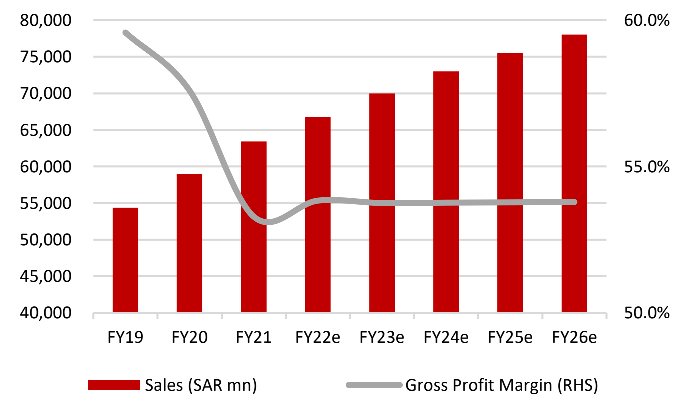
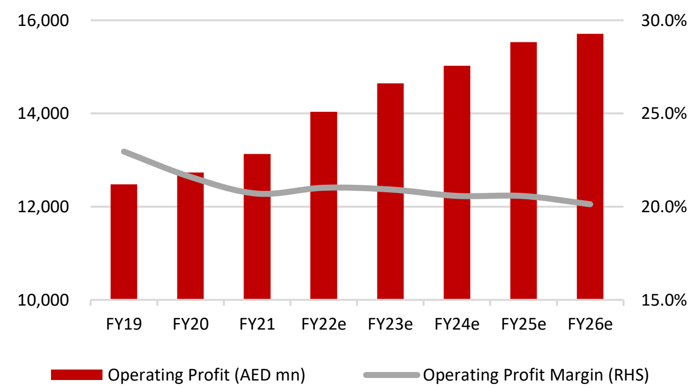
Sales and Gross Profit Margin



Operating Profit and Operating Profit Margin



Source: Company Filings

Downside Risk from Poor M&A Execution

The company is conserving cash for M&A activity. In 1Q22, Tawal entered Pakistan's market by acquiring Awal Telecom. Such acquisitions can pose a risk in the medium to long term as the company may overestimate synergy benefits and thus overpay for certain transactions. Additionally, the company's expansions in overseas markets may prove costly and unsuccessful, if it fails to gain a foothold in such markets. Thus, while acquisitions may increase the revenue of the company, it may lead to lower margins as losses and expenses from acquired firms reduce the profits of the combined entity.

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Relative valuation

We have given equal weightage of 35% each to the P/E and EV/EBITDA multiples. The peer set includes the companies globally. At a median peer P/E multiple of 19.8x and EV/EBITDA multiple of 5.4x, we arrive at target price of SAR 119.6 and SAR 62.7 per share respectively.

Discounted Cash Flow

		FY22	FY23	FY24	FY25	FY26	Terminal Value
Pegged on	July 6, 2022						
Time period index		0.49	1.49	2.49	3.49	4.49	4.49
Free cash flow							
PAT		12,080	13,277	13,685	14,107	14,273	
Interest (1-tax rate)		629	715	680	677	660	
Depreciation		9,867	10,615	11,391	11,841	12,646	
Changes in Working Capital		3,350	(377)	(283)	(267)	(258)	
Less: Capex		(13,087)	(13,711)	(14,303)	(14,788)	(15,289)	
Free cash flow to firm (FCFF)		12,838	10,518	11,170	11,570	12,033	171,762
Discounted FCFF		12,361	9,371	9,206	8,823	8,490	121,193

All figures in SAR mn unless otherwise stated

Enterprise Value	169,444
Less: Net debt (Includes lease liabilities)	4,138
Equity Value	165,307
Shares O/S	1,997
Equity Value per share (in SAR)	82.77
Current share price (SAR)	98.0
% upside/downside	-15.5%

Assumptions	
WACC	8.1%
Tax Rate	8.7%
Cost of debt / Lease Liabilities	3.7%
Cost of Equity	8.9%
Terminal growth rate	1.0%
Cost of equity calculation	
Risk Free Rate	3.9%
Beta	0.8
Equity Risk Premium	6.3%
Weights	
Debt	15.3%
Equity	84.7%

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About STC

Saudi Telecom Company (the Company) is a Saudi Arabia-based company, was established as a Saudi Joint Stock Company, engaged in the telecommunications sector. The Company's main activities comprise the provision of telecommunications, information, media services and digital payments. The Company's subsidiaries include Viva Bahrain Closed BSC, Arabian Internet and Communications Services Co Ltd and STC Gulf Investment Holding SPC, among others. The Company is the most valuable telecoms brand in the Middle East with a total value increasing by 16% to SAR 39.77 billion as of January 2022.

Operation/Segments

Enterprise Business Unit – EBU benefits from the company's ability to accommodate the strong demand from the public and private sectors for Enterprise Business Unit's services and products. The business segment focused on expanding its partnerships.

Consumer Business Unit – B2C has maintained its performance throughout the year achieved a growth due to an increase in sales push on Baity home broadband plans in FTTH-covered areas as well as the growing 5G covered areas. On residential, the market is experiencing growth mainly due to work from home and eLearning measures.

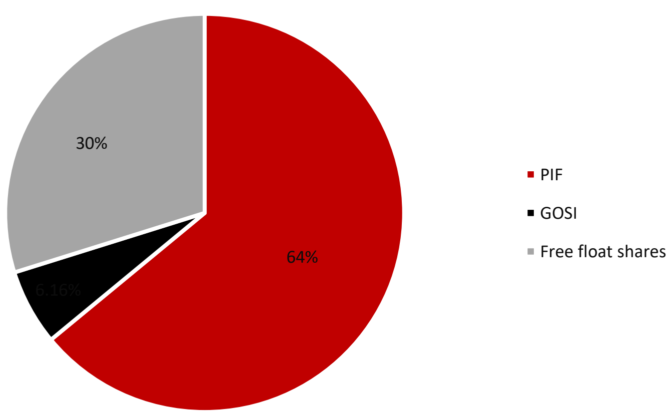
Wholesale Business Unit – STC has made qualitative achievements in the field of wholesale services by providing all the international needs and services of the business units within the company from telephone and internet services. STC maintained its excellence and asserted its international presence with the most advanced and modern network in the MENA region.

Geography

Saudi Telecom Company has operations in Kuwait, Bahrain, Turkey and Malaysia.

Ownership

The shareholding pattern of the company is given below



Source: Company Filings

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Key financials

(SAR mn)	FY19	FY20	FY21	FY22e	FY23e	FY24e
Income Statement						
Sales	54,368	58,953	63,417	66,784	69,992	73,015
COGS	(21,976)	(24,999)	(29,623)	(30,831)	(32,371)	(33,759)
Gross profit	**32,391**	**33,954**	**33,794**	**35,953**	**37,621**	**39,257**
SG&A expenses	(11,126)	(11,864)	(10,953)	(12,051)	(12,363)	(12,840)
Operating profit	**12,480**	**12,731**	**13,128**	**14,035**	**14,644**	**15,025**
Share of results of investments in associates and joint ventures	50	53	(778)	(229)	0	0
Other income – net	(76)	(43)	50	33	35	37
Finance charges	(765)	(624)	(619)	(689)	(783)	(744)
Income before tax	**11,687**	**12,356**	**12,635**	**13,544**	**14,886**	**15,343**
Income tax	(762)	(1,170)	(1,040)	(1,192)	(1,310)	(1,350)
Net income for the period	**10,925**	**11,185**	**11,595**	**12,352**	**13,576**	**13,993**
Balance Sheet						
Cash and bank balances	8,031	9,004	8,281	13,234	13,689	12,628
Financial assets and others	4,474	3,628	3,128	3,128	3,128	3,128
Trade and other receivables	21,372	15,725	25,464	23,786	24,929	25,934
Inventories	1,722	1,009	918	929	976	1,015
Property, plant and equipment	45,085	47,848	47,205	49,664	52,073	54,382
Investments in joint ventures	6,619	6,705	5,925	5,696	5,696	5,696
Right of use assets	2,888	2,893	2,952	3,171	3,381	3,580
Total assets	**118,326**	**121,972**	**127,779**	**134,057**	**138,797**	**141,692**
Trade and other payables	18,242	19,711	17,114	18,798	19,609	20,371
Long-term borrowings	8,923	8,638	7,847	7,483	7,167	6,660
Lease liabilities	2,164	2,238	2,354	2,519	2,748	2,951
Share capital	20,000	20,000	20,000	50,000	50,000	50,000
Statutory reserve	10,000	10,000	10,000	10,000	10,000	10,000
Retained earnings	34,508	37,508	37,985	12,076	15,368	17,070
Total stockholders' equity	**61,763**	**63,946**	**69,271**	**73,362**	**76,653**	**78,355**
Total liabilities & stockholders' equity	**118,326**	**121,972**	**127,779**	**134,057**	**138,797**	**141,692**
Cash Flow Statement						
Cash from operating activities	11,115	29,753	12,682	28,037	25,762	27,125
Cash from investing activities	(1,977)	(17,429)	(1,715)	(12,381)	(12,408)	(12,964)
Cash from financing activities	(8,068)	(9,919)	(10,235)	(8,965)	(10,992)	(13,218)
Net changes in cash	(124)	976	(730)	4,953	455	(1,061)
Cash at the end of the period	8,031	9,004	8,281	13,234	13,689	12,628
Key Ratios						
Current ratio	2.0	1.9	2.3	2.4	2.4	2.4
Inventory turnover ratio	12.8	18.3	30.8	33.4	34.0	33.9
Debtors' turnover ratio	2.5	3.2	3.1	2.7	2.9	2.9
Creditors turnover ratio	1.2	1.3	1.6	1.7	1.7	1.7
Gross profit margin	59.6%	57.6%	53.3%	53.8%	53.8%	53.8%
Operating margin	23.0%	21.6%	20.7%	21.0%	20.9%	20.6%
Net profit margin	20.1%	19.0%	18.3%	18.5%	19.4%	19.2%
EBITDA margin	39.1%	37.5%	36.0%	35.8%	36.1%	36.2%
Average return on equity	17.3%	17.5%	17.0%	16.9%	17.7%	17.7%
Average return on assets	10.5%	10.6%	10.5%	10.7%	10.7%	10.7%
Debt/Equity (x)	0.2x	0.2x	0.2x	0.2x	0.2x	0.1x
Interest coverage ratio (x)	16.3x	20.4x	21.2x	20.4x	18.7x	20.2x
P/E	18.8x	19.4x	19.9x	16.2x	14.7x	14.3x
EV/EBITDA	9.8x	9.8x	10.1x	8.4x	8.0x	7.6x
EV/Sales	3.8x	3.7x	3.6x	3.0x	2.9x	2.8x
EPS (SAR)	5.3	5.5	5.7	2.4	2.7	2.7
Dividend payout ratio	112.5%	109.0%	70.6%	66.1%	75.2%	87.6%
Dividend yield (%)	6.0%	5.6%	3.6%	4.1%	5.1%	6.1%
Net debt	4,163	2,932	4,245	(832)	(1,331)	(576)
Net debt/ EBITDA	0.20	0.13	0.19	-0.03	-0.05	-0.02
ROCE	17.0%	16.7%	17.2%	17.7%	17.8%	17.6%

Source: Company Financials, U Capital Research

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Etihad Etisalat Company SJSC (Mobily)

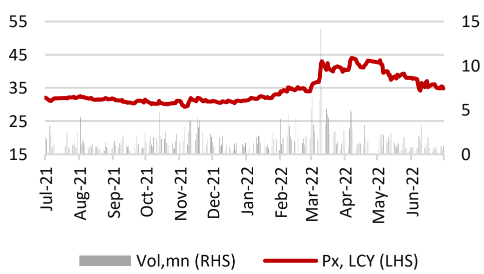
Target Price: SAR 32.4

Downside: 6.8%

Recommendation	Hold
Bloomberg Ticker	EEC AB
Current Market Price (SAR)	34.80
52wk High / Low (SAR)	44 / 29.3
12m Average Vol. (mn)	1.7
Mkt. Cap. (SAR bn)	26.8
Shares Outstanding (mn)	770
Free Float (%)	72.0%
3m Avg Daily Turnover (SAR mn)	56.5
6m Average Daily Turnover (SAR mn)	73.5
PE 2022e (x)	21.0x
EV/EBITDA 2022e (x)	6.5x
Dividend Yield '22e (%)	2.9%
Price Performance:	
1 month (%)	-8.4%
3 months (%)	-13.6%
12 months (%)	8.6%

Source: Refinitiv, as of July 06, 2022

Price -Volume Performance



Source: Refinitiv

- **One of the top three telecom companies in KSA**
- **Deleveraging to benefit the company by reducing risk**
- **Increase in dividends to support returns**
- **Higher capex levels may be necessary to remain competitive**

We initiate coverage on Etihad Etisalat Company SJSC (Mobily) with a Hold rating and a target price of SAR 32.4 per share, implying a downside of 6.8% to the last closing price (06 July 2022). Our target price implies a P/E'22e of 19.6x, and we believe that it is justified as the stock has performed well in the past 12 months, due to a strong growth in revenue and net profit, rising margins, resumption of dividend payments, and reduction in capex.

Investment Thesis

Valuation & Risks: Our valuation is based on a mix of discounted cash flows (30% weight), EV/EBITDA multiple (35% weight) and P/E multiple (35% weight). Key downside risks include an adverse change in regulations, rising interest rates and higher capex requirement than expected. Key upside risks include faster deleveraging, monetization of tower business and higher-than-expected growth in dividends.

One of the top three telecom companies in KSA

Mobily is one of the top three telecom players. The telecom industry in KSA is a highly oligopolistic industry. The industry is expected to benefit from the Kingdom's Vision 2030 initiative to increase contribution of ICT to the GDP and the overall focus on the non-oil sector. Rising adoption of optic fiber and 5G is also positive to the company as it can lead to higher revenue growth.

Decreasing Depreciation to increase profit growth

Mobily's depreciation is decreasing. In FY19, depreciation was 5.7% of average gross PPE. This figure declined to 4.7% in FY21. This may be due to the existence of older assets on the company's books which may be slowly retired or sold. Additionally, depreciation is higher than capex over the past years which has contributed to asset values decreasing faster than their being replaced. We expect this trend to continue though depreciation may be higher as newer assets in PPE increase as a proportion of total PPE.

Key Indicators

Year (in SAR mn)	FY19	FY20	FY21	FY22e	FY23e	FY24e
Sales	13,450	14,046	14,834	15,174	15,600	16,118
Gross profit	7,800	8,152	8,672	8,870	9,134	9,456
EBITDA	4,884	5,336	5,594	5,929	6,029	6,247
Operating profit	967	1,367	1,668	1,936	1,944	1,955
Net income	31	783	1,072	1,274	1,284	1,333
EPS	0.04	1.02	1.39	1.65	1.67	1.73
P/E (x)	619.5	28.6	22.4	21.0	20.9	20.1
EV/EBITDA (x)	6.7	6.6	6.6	6.5	6.4	6.1
Dividend yield	0.0%	1.7%	2.7%	2.9%	2.9%	3.0%

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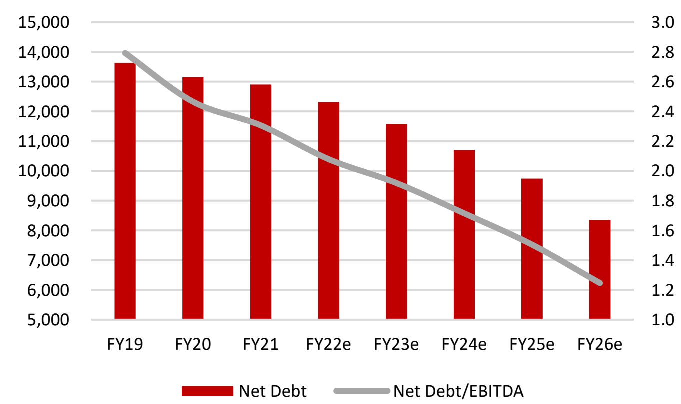
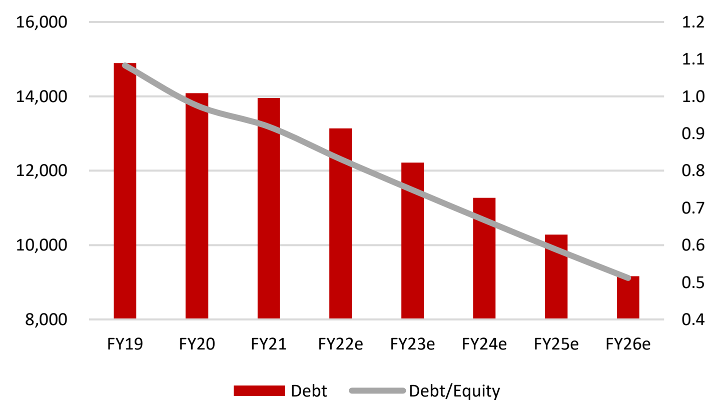
Focus on deleveraging to benefit the company

Mobily is focusing on developing the company. Due to this, deleveraging will be prioritized over other expenditures such as capex and dividend payments. On March 31, 2022, the company has a debt-to-equity ratio of 0.9x, down from 1.1x in FY19. In 1Q22, the company's net-debt to EBITDA ratio was 2.0x, down from 2.6x in FY19. We expect the company to continue its focus on deleveraging as shown in the charts below. However, we also expect the focus to decrease and the company to increase capex and dividends in the future.

Net Debt and Net Debt to EBITDA



Total Debt and Debt to Equity

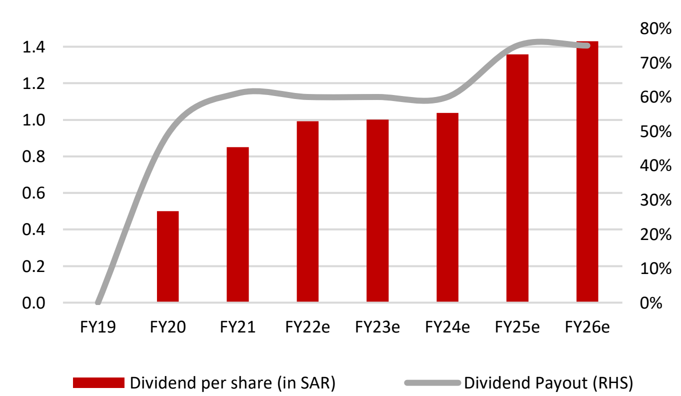


Source: Company Data, U Capital Research

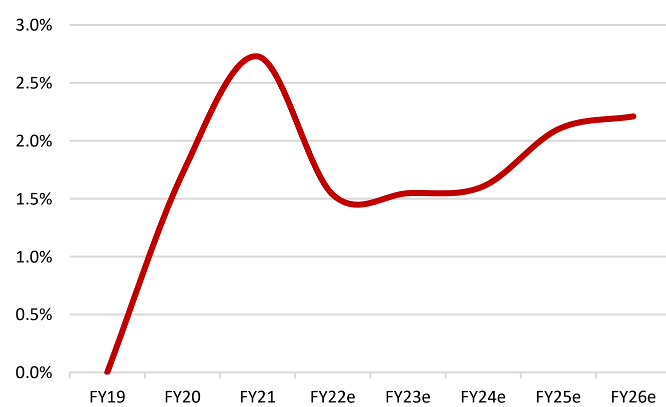
Rising Dividends to support returns

The company has a history of inconsistent dividend payments as dividends were discontinued after FY14 due to financial difficulties. Dividends resumed in FY20 as the company's profits started rising. The company paid a dividend of SAR 0.5 per share in FY20 and SAR 0.85 in FY21. As mentioned earlier, the management plans to focus on deleveraging and then on dividend payments. Due to this reason, we do not expect significant dividend growth at least in the near term. However, when the debt is reduced to levels desired by the management, dividend payments ay increase significantly.

Dividend per share and Dividend Pay-out Ratio



Movement in Dividend Yield



Source: Company Data, U Capital Research

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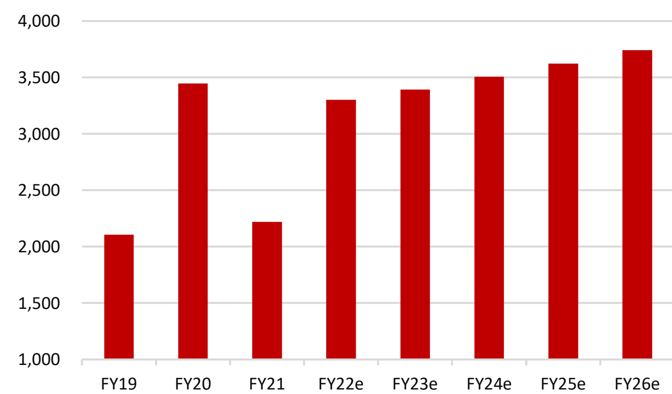
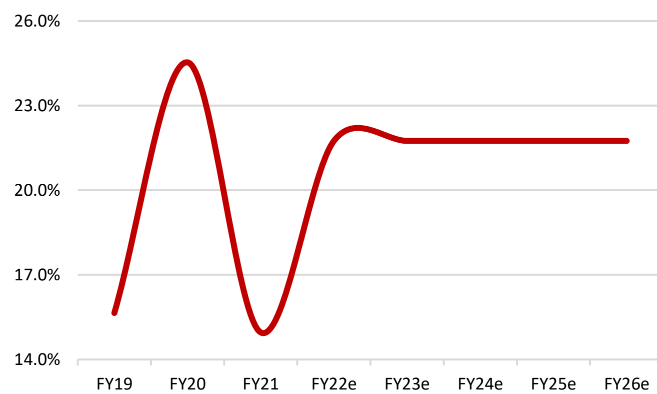
Capex to increase to maintain competitiveness

In FY21, capex fell on absolute and relative basis. As a percentage of revenue, capex was 15% in FY21, from 24.5% in FY20. We believe this fall to be unsustainable and that the company needs to invest more in capex to retain its competitive edge. The company's assets are aging as mentioned earlier. Furthermore, the company is lagging its peers in terms of download fixed and mobile internet download speeds. So, it may have to invest in its infrastructure assets to boost downloading speeds to match its competitors. Due to these factors, we expect the company to ramp up its capex spends from FY22. However, we also expect the company to finance this capex increase through internal accruals, without the need for raising additional debt.

Movement in Capex



Capex as percentage of revenues



Source: Company Data, U Capital Research

Monetization of tower assets to provide upside potential

Monetization of non-core assets, especially the tower assets of the company may provide an upside potential. Monetization will generate additional cash and allow faster deleveraging. It will also allow the company to focus on other factors such as increasing dividend payments and investing in additional capex. UBS estimates that the tower assets of Mobily could be valued at approximately SAR 3.8bn (USD 1bn), which may lead to a reduction in the net debt to EBITDA ratio. Additionally, it would allow the management to concentrate on managing the core business of the company.

Diversification to pose risks

As part of the company's GAIN Strategy, the company plans to enter new businesses such as fintech to benefit from diversification. These businesses may increase revenue growth and provide additional stability to the business. However, this strategy can prove risky due to poor execution or lack of response from the market. These factors may lead to reduction in margins. Additionally, this strategy is likely to result in higher capex, which will go in financing riskier activities instead of improving the core business.

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Relative valuation

We have given equal weightage of 35% each to the P/E and EV/EBITDA multiples. The peer set includes the companies globally. At average median peer P/E multiple of 16.2x and EV/EBITDA multiple of 5.4x, we arrive at target price of SAR 26.8 and SAR 25.3 per share respectively.

Discounted Cash Flow

	FY22e	FY23e	FY24e	FY25e	FY26e	Terminal Value
Pegged on: July 6, 2022						
Time period index	0.49	1.49	2.49	3.49	4.49	4.49
Free cash flow						
PAT	1,274	1,284	1,333	1,394	1,468	
Interest (1-tax rate)	509	510	474	437	399	
D&A	3,993	4,086	4,293	4,495	4,694	
Changes in Working Capital	(260)	23	(18)	(21)	(21)	
Capex	(3,300)	(3,393)	(3,506)	(3,622)	(3,742)	
Free cash flow to firm (FCFF)	2,216	2,510	2,576	2,683	2,798	50,961
Discounted FCFF	2,149	2,284	2,200	2,151	2,105	38,336

All figures in SAR mn unless otherwise stated

Enterprise Value	49,224
Less: Net debt	12,777
Equity Value	36,447
Shares O/S	770
Equity Value per share	47.33
Current share price (AED)	34.8
% upside/downside	36.0%

Assumptions	
WACC	6.5%
Tax rate	8.7%
Cost of debt / Lease Liabilities	4.1%
Cost of Equity	9.0%
Terminal growth rate	1.0%
Cost of equity calculation	
Risk-Free Rate	3.9%
Beta	0.8
Equity Risk Premium	6.3%
Weights	
Debt	46.4%
Equity	53.6%

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About Mobily

Mobily is a Saudi Arabian company established in 2004. It provides integrated services for three main types of customers, namely individuals, business, and carriers. It has one of the largest wireless networks by coverage in Saudi Arabia, as well as the region, and one of the widest FTTH networks, in addition to one of the largest data center systems worldwide. The Company's network comprises its own infrastructure and those of Bayanat al-Oula and SNFN. This is the Kingdom's newest fiber-optic network, with access to all major cities and more than 58,060 km of roads.

Operation/Segments

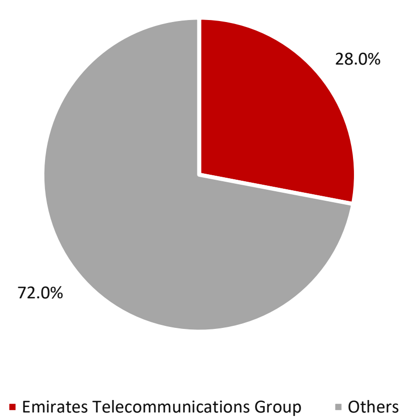
- The Group is engaged in a single line of business, being the supply of telecommunications services and related products. Most of the Group's revenues, profits and assets relate to its operations in the Saudi Arabia. The operating segments that are regularly reported to the chief operating decision maker are Consumer, Business, Wholesale and Outsourcing.
- Consumer Segment - The Consumer segment, Mobily continued to innovate and drive digitization in the Business segment, in line with the objectives outlined in its GAIN strategy. The Company made several strategic investments in digital solutions and expects to succeed in capturing the growth potential in the market.
- Business Segment - Business Unit achieved excellent results in servicing a growing range of company accounts. By focusing on new customer acquisitions and improving the value proposition for existing clients, the Company was able to mitigate threats to its business that were caused by the slow economic recovery in 2021.

Geography

The network has been expanded to connect to neighboring countries including Yemen, the United Arab Emirates and Bahrain, Qatar, Kuwait and Jordan.

Ownership

The shareholding pattern of the company is given below



Source: Company Filings

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Key financials

(SAR mn)

Income Statement	FY19	FY20	FY21	FY22e	FY23e	FY24e
Sales	13,450	14,046	14,834	15,174	15,600	16,118
COGS	(5,650)	(5,894)	(6,163)	(6,304)	(6,466)	(6,662)
Gross profit	**7,800**	**8,152**	**8,672**	**8,870**	**9,134**	**9,456**
SG&A expenses	(2,786)	(2,798)	(2,950)	(2,880)	(3,042)	(3,144)
Operating profit	**967**	**1,367**	**1,668**	**1,936**	**1,944**	**1,955**
Share of results from JVs & associates	(1)	0	(19)	2	0	0
Other income – net	43	11	15	15	16	16
Finance charges	(929)	(561)	(505)	(558)	(559)	(519)
Income before tax	**81**	**826**	**1,149**	**1,392**	**1,403**	**1,457**
Income tax	(49)	(43)	(78)	(118)	(119)	(124)
Net income for the period	**31**	**783**	**1,072**	**1,274**	**1,284**	**1,333**
Balance Sheet						
Cash and bank balances	1,252	929	1,051	812	649	560
Financial assets and others	405	243	325	325	325	325
Trade and other receivables	3,034	3,895	4,582	4,781	4,915	5,064
Inventories	105	73	108	121	124	127
Property, plant and equipment	21,651	21,321	20,380	19,675	18,911	18,099
Intangible assets	8,567	8,240	7,911	7,582	7,253	6,925
Right of use assets	2,379	2,321	2,730	3,072	3,471	3,825
Total assets	**39,216**	**38,408**	**39,364**	**39,147**	**38,929**	**38,705**
Trade and other payables	5,093	4,669	4,606	4,559	4,720	4,854
Long-term borrowings	11,228	10,134	9,624	8,879	8,093	7,256
Lease liabilities	1,857	1,836	2,193	2,137	2,116	2,120
Share capital	7,700	7,700	7,700	7,700	7,700	7,700
Statutory reserve	2,649	2,649	2,649	2,649	2,649	2,649
Retained earnings	3,469	4,206	4,884	5,504	6,024	6,586
Total stockholders' equity	**13,751**	**14,445**	**15,196**	**15,816**	**16,336**	**16,898**
Total liabilities & stockholders' equity	**39,216**	**38,408**	**39,364**	**39,147**	**38,929**	**38,705**
Cash Flow Statement						
Cash from operating activities	4,278	4,622	5,196	5,744	6,130	6,310
Cash from investing activities	(1,892)	(2,866)	(2,916)	(3,788)	(3,874)	(3,984)
Cash from financing activities	(1,398)	(1,626)	(1,775)	(1,467)	(1,687)	(1,717)
Net changes in cash	219	(322)	121	(239)	(162)	(90)
Cash at the end of the period	1,252	929	1,051	812	649	560
Key Ratios						
Current ratio	0.6	0.6	0.7	0.8	0.8	0.9
Inventory turnover ratio	53.9	66.2	68.1	55.1	52.8	53.0
Debtors' turnover ratio	4.4	4.1	3.5	3.2	3.2	3.2
Creditors turnover ratio	1.1	1.2	1.3	1.4	1.4	1.4
Gross profit margin	58.0%	58.0%	58.5%	58.5%	58.6%	58.7%
Operating margin	7.2%	9.7%	11.2%	12.8%	12.5%	12.1%
Net profit margin	0.2%	5.6%	7.2%	8.4%	8.2%	8.3%
EBITDA margin	36.3%	38.0%	37.7%	39.1%	38.6%	38.8%
Average return on equity	0.2%	5.6%	7.2%	8.2%	8.0%	8.0%
Average return on assets	2.5%	3.5%	4.3%	4.9%	5.0%	5.0%
Debt/Equity (x)	1.1x	1.0x	0.9x	0.8x	0.7x	0.7x
Interest coverage ratio (x)	1.0x	2.4x	3.3x	3.5x	3.5x	3.8x
P/E	619.5x	28.6x	22.4x	21.0x	20.9x	20.1x
EV/EBITDA	6.7x	6.6x	6.6x	6.5x	6.4x	6.1x
EV/Sales	2.4x	2.5x	2.5x	2.5x	2.5x	2.4x
EPS (SAR)	0.0	1.0	1.4	1.7	1.7	1.7
Dividend payout ratio	0.0%	49.2%	61.1%	60.0%	60.0%	60.0%
Dividend yield (%)	0.0%	1.7%	2.7%	2.9%	2.9%	3.0%
Net debt	13,642	13,159	12,904	12,330	11,570	10,714
Net debt/ EBITDA	2.79	2.47	2.31	2.08	1.92	1.71
ROCE	3.0%	4.3%	5.4%	6.4%	6.5%	6.8%

Source: Company Financials, U Capital Research

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Ooredoo QPSC

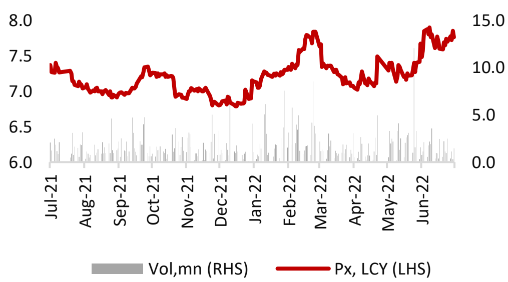
Target Price: QR 11.6

Upside: 49.5%

Recommendation	**Buy**
Bloomberg Ticker	QTEL UH
Current Market Price (QR)	7.8
52wk High / Low (QR)	7.9 / 6.8
12m Average Vol. (mn)	1.7
Mkt.Cap. (QR bn)	24.9
Shares Outstanding (mn)	3203.2
Free Float (%)	30.8%
3m Avg Daily Turnover (QR mn)	13.0
6m Average Daily Turnover (QR mn)	13.8
PE 2022e (x)	26.9x
EV/EBITDA 2022e (x)	4.4x
Dividend Yield '22e (%)	1.5%
Price Performance:	
1 month (%)	3.7%
3 months (%)	10.1%
12 months (%)	5.3%

Source: Refinitiv, as of 06th July 2022

Price -Volume Performance



Source: Refinitiv

- **One of the largest telecommunication services with a presence in MENA, North Africa, and South-East Asia**
- **Major markets include Qatar (36%), Iraq (16%), Kuwait (13%), and Oman (11%)**
- **Merger of Indostat with H3I to bring significant operational synergies**
- **5G rollout and strategic partnership with digital service providers remain key**
- **Bundling OTT services along with new postpaid plans for enhanced customer experience**

We initiate coverage on Ooredoo with a Buy rating and a target price of QR 11.6 per share, implying an upside of 49.5% to the last closing price (6th July 2022). Our target price implies a P/E'22e of 40.3x reflecting significant upside from transformation initiative focusing on topline growth, operating cost, and Capex rationalization. The free cash flow generated from cost optimization and merger deal is expected to lower the debt burden.

Investment Thesis

Valuation & Risks: Our valuation is based on a mix of discounted cash flows (30% weight) and multiples approach (35% weight each to both PE & EV/EBITDA based multiples). Ooredoo is currently trading at a 47.9x its trailing earnings of QR 0.2 per share.

Indostat Ooredoo Hutchison merger to drive network expansion and scale

The merger combines two complementary businesses to become Indonesia's second-largest mobile telecom company with an estimated annual revenue of approximately USD 3 billion. The merger has resulted in Ooredoo's market share increasing from 18% to 26%. Management expects the pre-tax synergy to be about USD 300-400 million over 3-5 years.

Rollout of 5G and digital services to be the growth avenues

5G services are currently available in Qatar, Kuwait, Oman, Maldives, and Indonesia. Ooredoo has signed a partnership with fintech players, premium entertainment services, gaming leaders, and music providers resulting in a 20% revenue growth from digital services.

Risks: Due to its global footprint, exchange rate fluctuation could negatively impact Ooredoo's earnings. Intense competition affects pricing, with more consolidations likely to happen across geographies.

Key Indicators

	FY19	FY20	FY21	FY22e*	FY23e	FY24e
Sales	29,916	28,867	29,900	21,522	21,835	22,105
EBITDA	12,847	12,088	13,050	9,075	9,208	9,316
Operating profit	4,260	3,843	5,076	2,930	2,648	2,337
Finance costs	-2,405	-2,150	-1,994	-1,663	-1,552	-1,426
Net income	2,224	1,422	1,053	1,154	1,030	882
EPS (QR)	0.54	0.35	0.01	0.29	0.26	0.22
P/E	12.5x	24.1x	498.4x	26.9x	30.2x	35.2x
EV/EBITDA	4.2x	4.2x	3.7x	4.4x	4.4x	4.3x
Dividend yield (%)	3.2%	3.2%	3.2%	1.5%	1.3%	1.1%

Note: *Indonesian operations are deconsolidated in FY22 post-merger with Hutchison group

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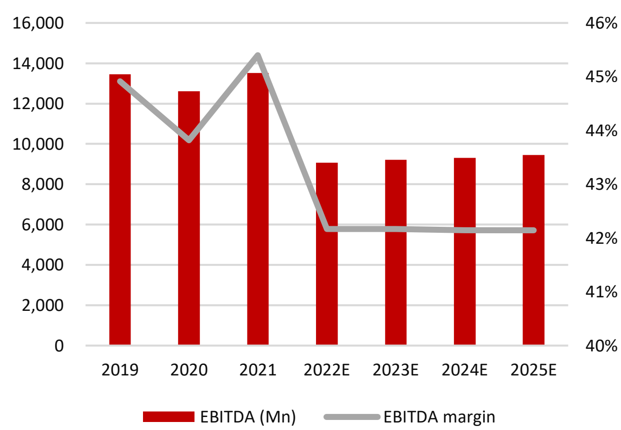
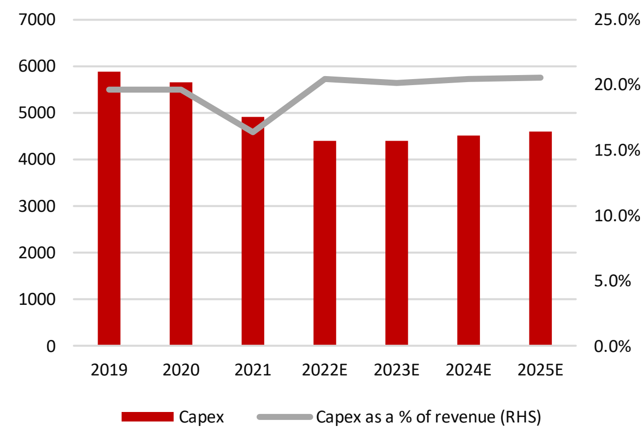
EBITDA margins to decline marginally along with rationalized Capex spending

Historically, the revenues declined at a CAGR of 1.9% during FY16-21, mainly due to an industry-wide shift from voice to data consumption plans, reduction in handset sales, and weak macro-economic conditions in markets served. In FY21, the revenues grew by 4% compared to the previous year, driven by growth in Qatar, Indonesia, and Tunisia. Ooredoo currently has 5G services available in five markets, including Qatar, Kuwait, Oman, Maldives, and Indonesia. EBITDA is expected to decline marginally to 42%, which is 100bps lower than the five-year average EBITDA margin.

EBITDA (QAR mn) and margins (%)



CAPEX (QAR mn) as percentage of revenues

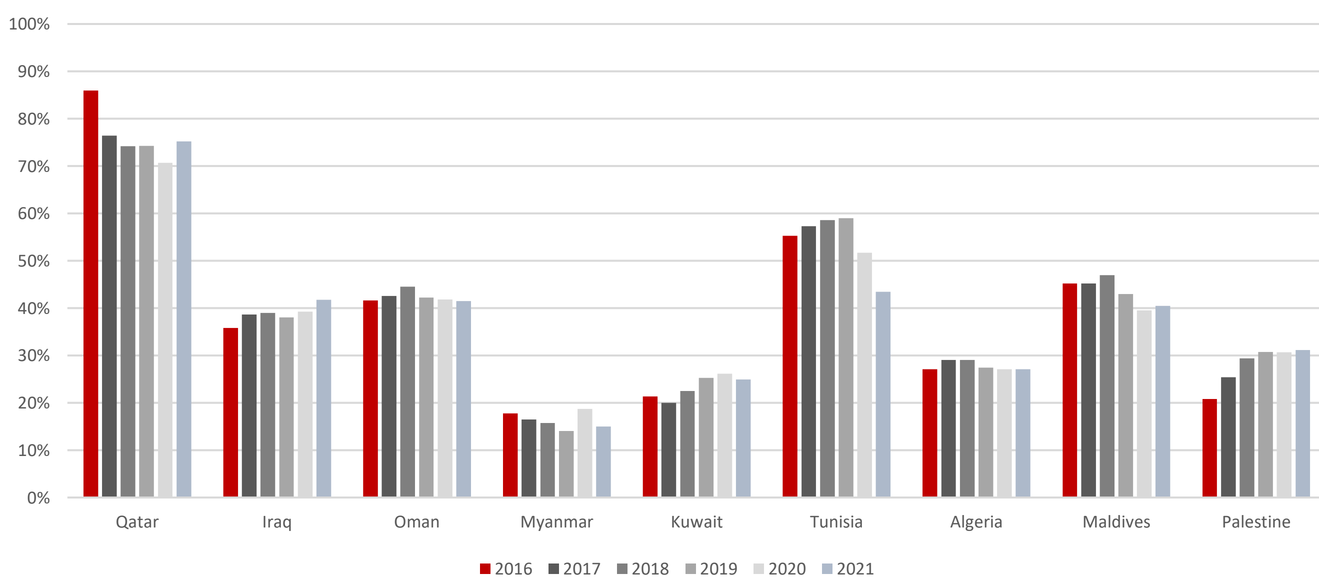


Source: Company Filings, U Capital Research

Stable Market share across Geographies

Ooredoo has a high market share of 75% in Qatar, followed by Tunisia, which has a 58% market share. Across other geographies, it has secured a market share of around 30%. Over the last five years, Ooredoo has retained its market across geographies. In Qatar, Ooredoo competes with Vodafone, which has 25% of Qatar's mobile users.

Market share (%) based on the number of users



Source: Company Filings

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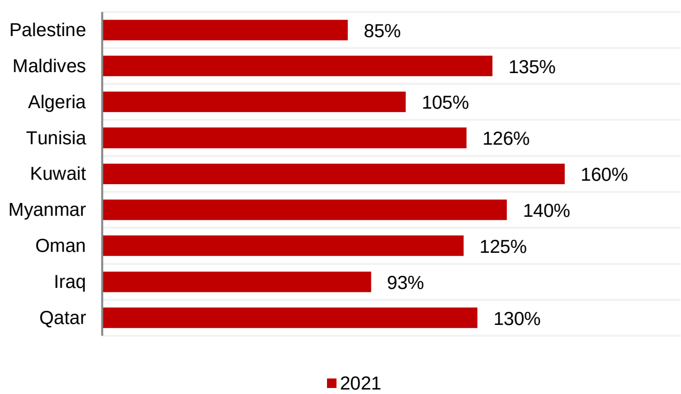
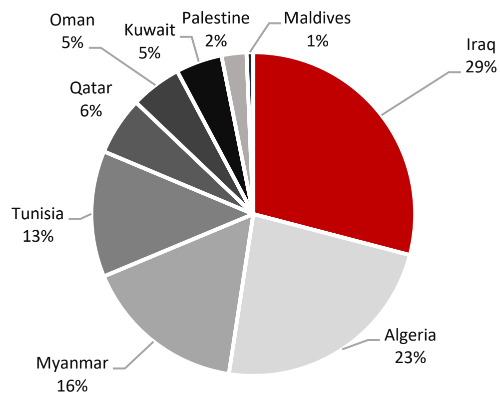
Mobile Users penetration across Geographies

Mobile user penetration is defined as the number of mobile users in a particular geography divided by the population in the region. Across geographies, Kuwait has the highest penetration of 160% in 2021, while Palestine has the lowest penetration of 85%. Assuming that the mobile penetration is expected to remain relatively constant, the 2021-2025 population CAGR of approximately 2% will drive the customer base in the medium term.

Penetration levels



Customer Base across Geography



Source: Company Filings

Indostat Ooredoo Hutchison merger to drive network expansion and scale

Ooredoo Group's Indonesian entity Indostat Ooredoo completed its merger with Hong Kong-based CK Hutchison to become Indostat Ooredoo Hutchison. The merger combines two complementary businesses to become Indonesia's second-largest mobile telecom company with an estimated annual revenue of approximately USD 3 billion. Ooredoo group previously held 65% in Indostat Ooredoo through Ooredoo Asia holding company. CK Hutchison gets half of Ooredoo Asia by swapping its stake in the merged entity for 33% of shares and USD 387 million into the Asia business for the remaining 16.7% stake. The merger has resulted in Ooredoo's market share increasing from 18% to 26%. Management expects the pre-tax synergy to be about USD 300-400 million over 3-5 years.

Management Guidance

Financials	2022 FY Guidance over FY21
Revenue	-2% to +2%
EBITDA	-3% to +1%
Capex	2.75Bn to 3.25Bn

Source: Company Research

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Relative valuation

We have given a weightage of 35% each to the P/E and EV/EBITDA valuation based on multiples. At average median peer P/E multiple of 16.2x and EV/EBITDA multiple of 5.6x, we arrive at target price of QAR 4.7 and QAR 12.4 per share respectively.

Discounted Cash Flow

		FY22	FY23	FY24	FY25	Terminal Value
Pegged on	July 6, 2022					
Time period index		0.49	1.49	2.49	3.49	0.49
Free cash flow						
PAT		923	824	706	612	923
Interest (1-tax rate)		1,330	1,242	1,141	1,024	1,330
Depreciation		6,146	6,560	6,980	7,408	6,146
Changes in Working Capital		171	126	88	(76)	171
Less: Capex		(4,402)	(4,394)	(4,514)	(4,607)	(4,402)
Free cash flow to firm (FCFF)		4,168	4,357	4,400	4,361	4,168
Discounted FCFF		4,031	3,935	3,709	3,433	4,031

Enterprise Value	71,459
Less: Net debt (Includes lease liabilities)	11,433
Equity Value	60,026
Shares O/S	3,203
Equity Value per share	18.7
Current share price (QR)	7.76
% upside/downside	141.5%

ASSUMPTIONS	
WACC	7.1%
Tax Rate	20.0%
Cost of debt / Lease Liabilities	8.3%
Cost of Equity	7.5%
Terminal growth rate	1.0%
Cost of Equity Calculation	
Risk Free Rate	4.06%
Beta	0.55
Equity Risk Premium	6.20%
Weights	
Debt	46.3%
Equity	53.7%

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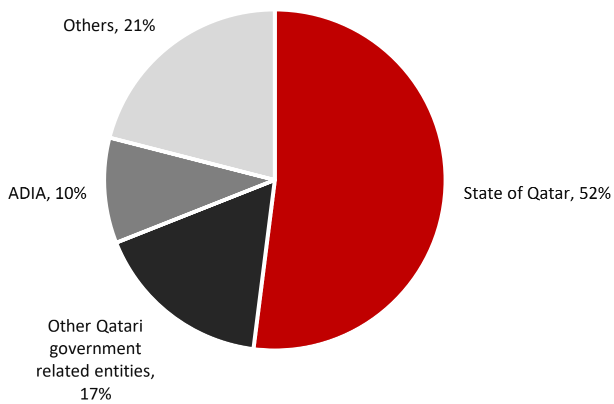
About Ooredoo

National Mobile Telecommunications Company K.S.C.P. provides telecommunications services in Kuwait, Algeria, Tunisia, Maldives, and Palestine. It is involved in the purchase, supply, installation, management, and maintenance of wireless sets and equipment, mobile telephone services, pager systems, and other telecommunication services, as well as in the import and export of sets, equipment, and instruments. The company was incorporated in 1997 and is based in Kuwait City, Kuwait. National Mobile Telecommunications Company K.S.C.P. is a subsidiary of Ooredoo International Investments L.L.C.

Ooredoo's Shareholding Structure



Source: Company filings

Ownership Interest in Operating Entities

	Ownership
Qatar	100%
Indonesia	32%
Iraq	64%
Oman	55%
Myanmar	100%
Kuwait	92%
Tunisia	84%
Algeria	74%
Maldives	83%
Palestine	45%

Source: Company filings

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Key financials

(QR 'Mn)	FY19	FY20	FY21	FY22e	FY23e	FY24e
Income Statement						
Sales	29,916	28,867	29,900	21,522	21,835	22,105
Operating expenses	(11,031)	(13,194)	(13,486)	(9,793)	(9,935)	(10,058)
SG&A expenses	(6,094)	(3,258)	(3,213)	(2,367)	(2,402)	(2,432)
EBITDA	**12,847**	**12,088**	**13,050**	**9,075**	**9,208**	**9,316**
Depreciation and Amortization	(8,588)	(8,245)	(7,974)	(6,146)	(6,560)	(6,980)
Operating profit	**4,260**	**3,843**	**5,076**	**2,930**	**2,648**	**2,337**
Share of results from JVs and associates	57	35	80	38	38	38
Finance costs	(2,405)	(2,150)	(1,994)	(1,663)	(1,552)	(1,426)
Finance income	317	254	190	175	192	192
Income before tax	**2,646**	**1,625**	**1,679**	**1,442**	**1,288**	**1,103**
Income tax	(422)	(203)	(627)	(288)	(258)	(221)
Net income for the period	**2,224**	**1,422**	**1,053**	**1,154**	**1,030**	**882**
Balance Sheet						
Cash and bank balances	14,716	15,678	11,670	12,816	12,785	12,663
Trade and other receivables	8,361	7,783	5,301	5,307	5,384	5,451
Inventories	346	197	181	181	181	181
Property, plant and equipment	27,045	26,120	14,869	13,890	12,644	11,256
Intangible assets, goodwill and long-term prepayments	26,320	26,455	18,088	17,450	16,789	16,103
Investments in joint ventures	1,972	1,696	1,646	7,567	7,567	7,567
Right of use assets	6,034	6,710	2,861	3,595	4,210	4,702
Total assets	**87,982**	**87,737**	**77,358**	**62,493**	**61,251**	**59,617**
Trade and other payables	13,775	15,334	8,943	9,038	9,245	9,403
Long-term borrowings	25,337	24,326	18,943	15,092	12,392	9,692
Lease liabilities	5,693	6,264	3,558	4,427	5,207	5,750
Share capital	3,203	3,203	3,203	3,203	3,203	3,203
Statutory reserve	1,299	1,304	1,327	1,327	1,327	1,327
Retained earnings	12,948	13,278	12,504	13,058	13,552	13,976
Total stockholders' equity	**29,001**	**29,585**	**28,178**	**29,105**	**28,201**	**26,409**
Total liabilities & stockholders' equity	**87,982**	**87,737**	**77,358**	**62,493**	**61,251**	**59,617**
Cash Flow Statement						
Cash from operating activities	11,760	11,111	7,975	7,470	7,716	7,950
Cash from investing activities	(5,887)	(5,338)	(2,950)	(11,105)	(5,268)	(5,398)
Cash from financing activities	(8,815)	(3,891)	(9,099)	4,781	(2,480)	(2,674)
Net changes in cash	(2,941)	1,882	(4,074)	1,146	(31)	(122)
Cash at the end of the period	13,354	14,609	11,644	12,816	12,785	12,663
Key Ratios						
Current ratio	1.0	1.0	1.4	1.4	1.4	1.4
Inventory turnover ratio	49.8	60.4	78.4	66.4	76.6	76.5
Debtors' turnover ratio	3.6	3.6	4.6	4.1	4.1	4.1
Creditors turnover ratio	2.2	2.0	2.5	2.4	2.4	2.4
Operating margin	14.2%	13.3%	17.0%	13.6%	12.1%	10.6%
Net profit margin	7.4%	4.9%	3.5%	5.4%	4.7%	4.0%
EBITDA margin	42.9%	41.9%	43.6%	42.2%	42.2%	42.1%
Average return on equity	7.8%	5.0%	3.9%	4.2%	3.6%	3.0%
Average return on assets	2.6%	1.6%	1.3%	1.6%	1.7%	1.5%
Debt/Equity (x)	1.3x	1.3x	0.9x	0.8x	0.7x	0.6x
Interest coverage ratio (x)	1.8x	1.8x	2.5x	1.8x	1.7x	1.6x
P/E	12.5x	24.1x	498.4x	26.9x	30.2x	35.2x
EV/EBITDA	4.2x	4.2x	3.7x	4.4x	4.4x	4.3x
EV/Sales	1.8x	1.7x	1.6x	1.8x	1.8x	1.8x
EPS (QR)	0.68	0.59	0.49	0.54	0.35	0.01
Dividend payout ratio	46.4%	71.1%	1706.8%	40.0%	40.0%	40.0%
Dividend yield (%)	3.2%	3.2%	3.2%	1.5%	1.3%	1.1%
Net debt (cash)	22,680	21,477	12,285	9,002	6,965	4,767
Net debt/ EBITDA	1.8	1.8	0.9	1.0	0.8	0.5
ROCE	3.6%	2.3%	1.9%	2.3%	2.1%	1.9%

Source: Company Financials, U Capital Research, note: *Indonesian operating entity is deconsolidated post-merger with Hutchison group

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Etisalat PJSC

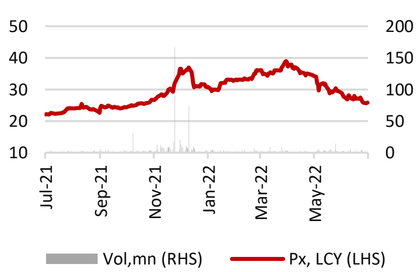
Target Price: AED 19.2

Downside: 25.3%

Recommendation	**Sell**
Bloomberg Ticker	ETISALAT UH
Current Market Price (AED)	25.78
52wk High / Low (AED)	39 / 22
12m Average Vol. (mn)	4.2
Mkt.Cap. (AED bn)	224.2
Shares Outstanding (mn)	8,697
Free Float (%)	75.9%
3m Avg Daily Turnover (AED mn)	78.4
6m Average Daily Turnover (AED mn)	82.2
PE 2022e (x)	23.6x
EV/EBITDA 2022e (x)	10.8x
Dividend Yield '22e (%)	3.8%
Price Performance:	
1 month (%)	-10.6%
3 months (%)	-30.7%
12 months (%)	16.8%

Source: Refinitiv, as of July 6 2022

Price -Volume Performance



Source: Refinitiv

- **One of the largest telecom services providers, with a presence in the Middle East, Africa, and South Asia**
- **Major markets include UAE (58%), Morocco (14%), Egypt (9%), and Pakistan (6%)**
- **Management focus on transformation into technology company would boost growth of non-legacy offerings of fintech, cloud, cybersecurity etc.**
- **Telecom services revenue is expected to be on a steady growth trajectory supported by favorable trends witnessed in demand of e-commerce, e-learning, online content, and remote working etc.**
- **Increased deployment of 5G networks (in UAE and Saudi Arabia) and adoption of bundled services would enhance the overall customer experience**

We initiate coverage on Etisalat with a Sell rating and a target price of AED 19.2 per share, implying a downside of 25.3% to the last closing price (6th July 2022). Our target price implies a P/E'22e of 17.6x reflecting significant upside from transformation initiative focusing on topline growth, operating cost, and Capex rationalization. The free cash flow generated from cost optimization and merger deal is expected to lower the debt burden.

Investment Thesis

Valuation & Risks: Our valuation is based on a mix of discounted cash flows (30% weight) and multiples approach (35% weight each to both PE & EV/EBITDA based multiples). Etisalat is currently trading at 23.9x its trailing earnings of AED 1.08 per share

Transformation into technology company to boost non-legacy offerings

The company aspires to transform into a global technology firm. To achieve the stated objective, it has undergone restructuring and introduced dedicated business verticals that focus on offerings that complement the legacy telecom business. The new verticals of life and enterprise, which cover technology solutions in areas of fintech, entertainment, cloud, cybersecurity, IoT, and AI. The capital vertical would focus on acquisition of attractive technologies, hence exploring inorganic growth opportunities.

Legacy telecom business poised to grow on back of tailwinds

The telecom revenue in all major markets such as UAE, Saudi Arabia, Egypt, Morocco, and Pakistan, is expected to gain steadily, driven by tailwinds. The tailwinds include robust growth of e-commerce and e-learning, and higher demand for online content and gaming. Moreover, remote work and digital banking are increasingly preferred by younger generations.

Risks: The global nature of company's operations faces risks of adverse regulatory actions, exchange rate volatilities and unfavorable geopolitical developments. Moreover, high competition and pricing pressure could squeeze margins.

Key indicators

Year (AED mn)	FY19	FY20	FY21	FY22e	FY23e	FY24e
Sales	52,186	51,708	53,342	54,666	56,311	58,250
Gross profit	19,961	19,868	19,261	20,160	20,540	21,066
EBITDA	19,263	20,915	20,995	21,434	22,064	22,829
Operating profit	11,798	13,015	12,799	13,163	13,318	13,601
Net income	9,495	10,316	11,059	10,817	11,049	11,292
EPS, AED	1.00	1.04	1.07	1.09	1.12	1.14
P/E	16.4	16.4	29.6	23.6	23.1	22.6
EV/EBITDA	7.0	6.8	9.5	10.8	10.5	10.1
Dividend yield, %	4.9%	4.7%	3.8%	3.8%	3.8%	3.9%

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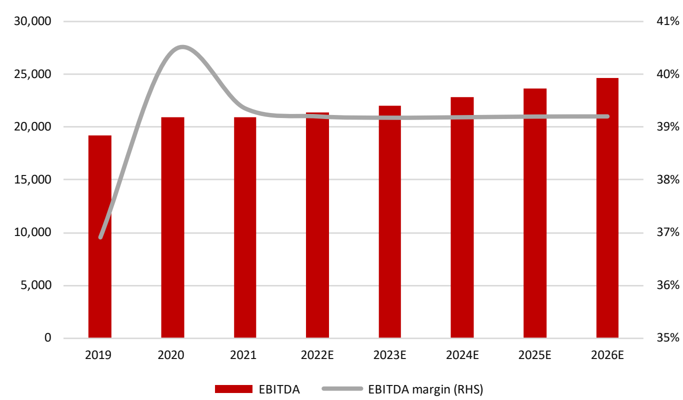
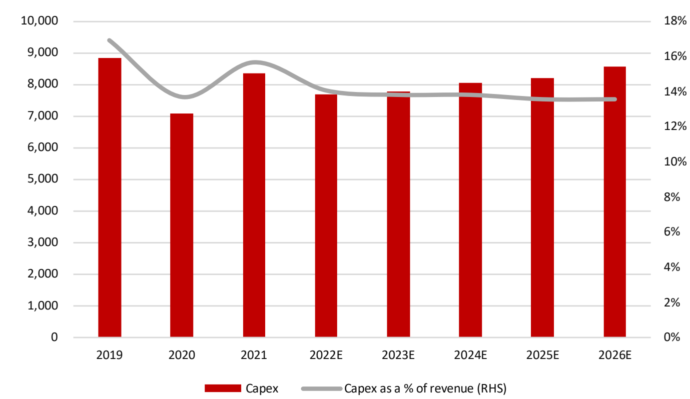
EBITDA margin to decline marginally along with rationalized Capex spending

Revenue had declined about 0.9% YoY in FY20 due to the constrained economic activities in the UAE and other key markets. The regulatory restriction placed to contain the raging effect of COVID-19 pandemic was the primary reason behind this phenomenon. However, with the rapid expansion of vaccination and the subsequent easing of restrictions, the economic activities in the region are coming back on track. This resulted in a 3.2% YoY increase in FY21 revenue, which is expected to improve further in the medium to long term. We forecast the revenue to witness a 2.9% CAGR growth in the period of FY22-26, driven by the positive trends being observed across the key markets. EBITDA margin is expected to reduce marginally by 60 bps in FY22 as compared to FY21.

EBITDA (AED mn) and margin (%)



CAPEX (AED mn) as percentage of revenue (%)

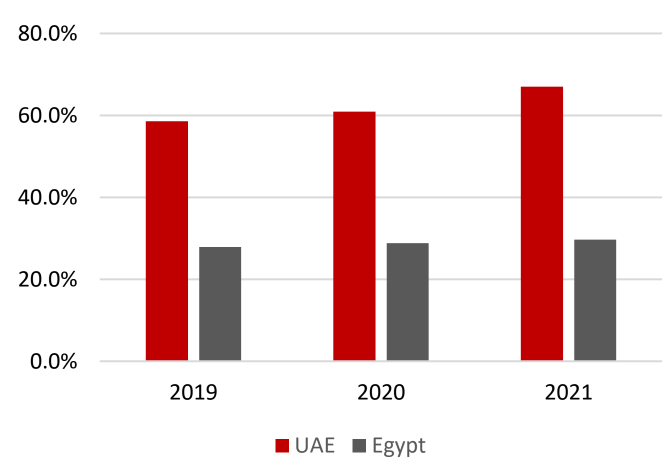


Source: Company Filings, U Capital Research

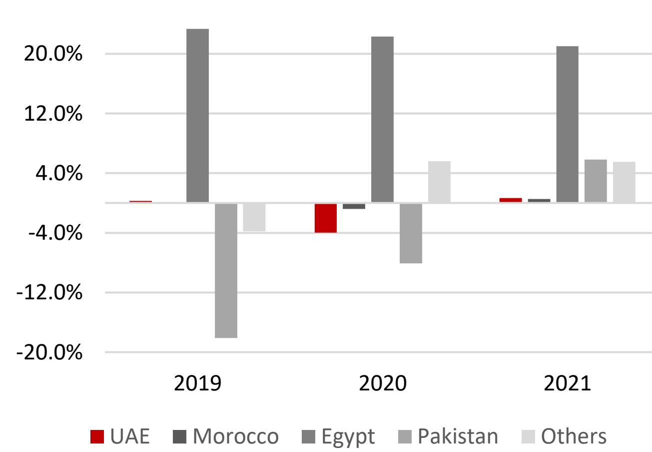
Leading market share in home market, along with good performance in other key markets

Etisalat commands market leadership position in the home market of UAE with a mobile revenue market share of 67.0% (2021). The company has been recognized as one of the fastest mobile networks of the region and is well-placed to leverage on the improving economic conditions. Etisalat Misr has the second largest mobile revenue market share of 29.7% (2021) as against the market leader in Egypt, Vodafone, which controls 43.9% mobile revenue market share. The UAE business (Etisalat UAE) registered revenue growth of about 1.0% in 2021 and reported EBITDA margin of 51.3%. In Saudi Arabia (Mobily), the company reported revenue growth of 5.6% in 2021 and EBITDA margin of 38.0%. Etisalat Misr witnessed revenue growth of 20.0% and EBITDA margin of 41.0% in 2021. PTCL Group (Pakistan) reported revenue growth of 6.0% and EBITDA margin of 30.0%.

Mobile revenue market share (%)



Revenue growth (%yoy)

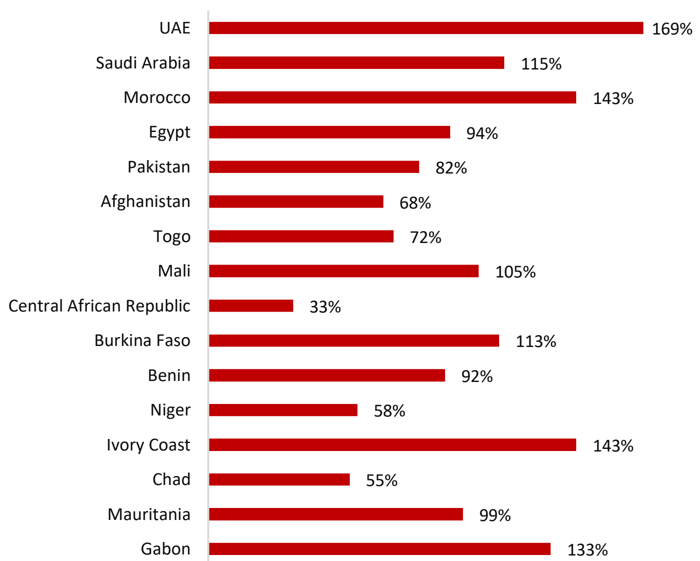


Source: Company Filings

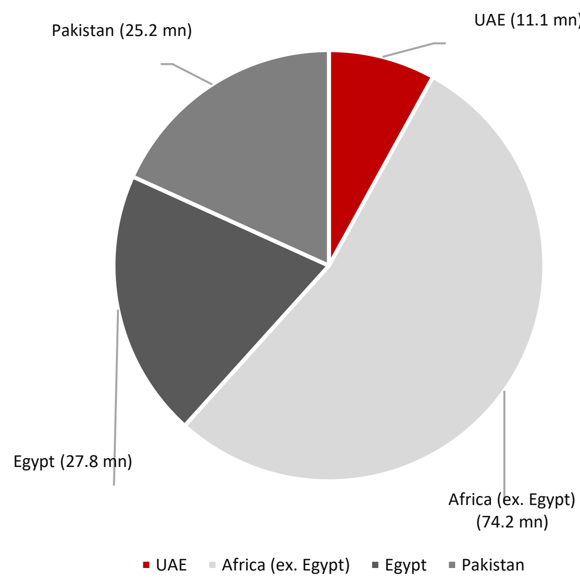
Mobile users and penetration across geographies

Mobile user penetration is defined as the number of mobile users in a particular geography divided by the population in the region. As of 2021, UAE has the highest penetration of 169%, while Central African Republic has the lowest penetration of 33%. The company's top-line would benefit from stable subscriber base across geographies, economic recovery in the post-COVID period and the strong regional ICT market (expected growth rate of over 15% during 2020-25 in UAE, Saudi Arabia, and Egypt).

Penetration levels (2021)



Subscribers by Geography (2021)



Source: Company Filings

Etisalat customers' experience to improve, driven by bundled service packages and 5G implementation

The company and its subsidiaries are engaged in improving customer experience across the markets they serve. The regular offering of voice and data services are being complemented by services such as music, sports, TV, video conferencing, and digital streaming. The bundled services and related equipment being provided by the company through various partnerships, would enhance the overall customer experience in all geographies. Moreover, the company is actively pursuing the implementation of 5G networks in UAE and Saudi Arabia. The enhanced data speed that 5G would offer, would improve the performance of all digital offerings. The company recently acquired elGrocer, an online grocery delivery platform, which would broaden the service offering portfolio.

Management Guidance

Financials	FY22 Guidance over FY21
Revenue growth	Low single digit growth vs. +2.0% to +3.0%
EBITDA margin	~49% vs. ~50%
EPS (AED)	~1.08 vs. ~1.05
Capex/Revenue	16.5% to 17.5% vs. 15.5% to 16.5%

Source: Company Research

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Relative valuation

We have given a weightage of 35% each to the P/E and EV/EBITDA valuation based on multiples. At average median peer P/E multiple of 19.8x and EV/EBITDA multiple of 5.6x, we arrive at target price of AED 21.6 and AED 14.2 per share respectively.

Discounted Cash Flow

		FY22	FY23	FY24	FY25	FY26	Terminal Value
Pegged on	July 6, 2022						
Time period index		0.49	1.49	2.49	3.49	4.49	4.49
Free cash flow							
PAT		9,519	9,723	9,937	10,237	10,613	
Interest (1-tax rate)		1,667	1,717	1,768	1,821	1,876	
Depreciation		8,270	8,746	9,228	9,718	10,221	
Changes in Working Capital		642	624	714	666	758	
Less: Capex		(7,700)	(7,790)	(8,059)	(8,214)	(8,551)	
Free cash flow to firm (FCFF)		12,399	13,020	13,589	14,229	14,918	197,978
Discounted FCFF		11,910	11,515	11,062	10,665	10,295	136,629

Enterprise Value	192,076
Less: Net debt as on Mar,2022	(2,434)
Equity Value	194,509
Shares O/S	8,697
Equity Value per share (in AED)	22.37
Current share price (AED)	25.8
% upside/downside	(13.2%)

ASSUMPTIONS	
WACC	8.6%
Tax Rate	13.6%
Cost of debt / Lease Liabilities	3.4%
Cost of Equity	11.2%
Terminal growth rate	1.0%
Cost of Equity Calculation	
Risk Free Rate	3.5%
Beta	1.2
Equity Risk Premium	6.3%
Weights	
Debt	31.4%
Equity	68.6%

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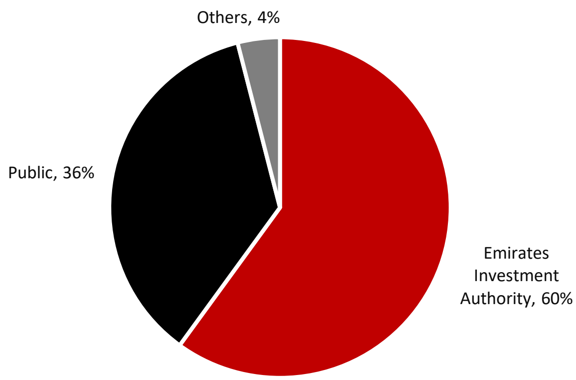
About Etisalat

Emirates Telecommunications Group Company PJSC ("Etisalat" or "e&") was founded in 1976 and primarily provides telecommunication services, apart from media services and related equipment. The company offers mobile (prepaid and postpaid), fixed broadband, cloud, data, voice, satellite, cable television, infrastructure, digital, consultancy, submarine cable services, and other technology solutions. It is also involved in trade of mobile phones and accessories, and installation and management of network systems. As of FY21, the company has presence in 16 countries in the Middle East, Asia, and Africa, and serves over 159 million subscribers.

Etisalat's Shareholding Structure



Source: Company filings

Ownership Interest in Operating Entities

	Ownership
UAE	100%
Saudi Arabia	28%
Afghanistan	100%
Pakistan	23%
Egypt	66%
Morocco	53%
Benin	53%
Burkina Faso	32%
Central African Republic	53%
Mali	27%
Togo	50%
Gabon	27%
Mauritania	27%
Chad	53%
Ivory Coast	45%
Niger	53%

Source: Company filings

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Key financials

(AED mn)	FY19	FY20	FY21	FY22e	FY23e	FY24e
Income Statement						
Sales	52,186	51,708	53,342	54,666	56,311	58,250
COGS	(32,225)	(31,840)	(34,081)	(34,506)	(35,772)	(37,184)
Gross profit	**19,961**	**19,868**	**19,261**	**20,160**	**20,540**	**21,066**
SG&A expenses	(8,356)	(7,583)	(8,040)	(8,360)	(8,612)	(8,908)
Operating profit	**11,798**	**13,015**	**12,799**	**13,163**	**13,318**	**13,601**
Share of results of investments in associates and joint ventures	(36)	197	297	153	151	148
Other income – net	1,363	1,112	1,289	1,200	1,370	1,425
Finance charges	(2,052)	(2,361)	(1,284)	(1,930)	(1,988)	(2,047)
Income before tax	**11,109**	**11,766**	**12,804**	**12,434**	**12,700**	**12,979**
Income tax	(1,614)	(1,451)	(1,745)	(1,616)	(1,651)	(1,687)
Net income for the period	**9,495**	**10,316**	**11,059**	**10,817**	**11,049**	**11,292**
Balance Sheet						
Cash and bank balances	29,657	31,345	28,575	32,610	33,927	35,562
Other current assets	2,278	3,076	3,367	2,784	2,946	3,114
Trade and other receivables	14,641	14,573	14,288	15,145	15,600	16,093
Inventories	783	705	749	788	816	846
Property, plant and equipment	45,070	45,803	43,715	44,369	44,840	45,151
Investments in associates and joint ventures	4,077	4,250	4,452	4,357	4,231	4,072
Right of use assets	2,744	2,700	2,437	2,736	3,005	3,252
Total assets	**128,266**	**133,018**	**128,197**	**132,686**	**137,134**	**141,809**
Trade and other payables	28,098	29,041	28,702	30,239	31,348	32,586
Long-term borrowings	17,350	13,820	19,176	17,493	18,018	18,558
Lease liabilities	2,709	2,785	2,654	2,691	2,740	2,802
Share capital	8,697	8,697	8,697	8,697	8,697	8,697
Statutory reserve	27,813	28,401	28,598	29,455	30,330	31,224
Retained earnings	10,102	11,937	10,291	10,516	10,746	10,981
Total stockholders' equity	**46,611**	**49,034**	**47,586**	**48,668**	**49,773**	**50,902**
Total liabilities & stockholders' equity	**128,266**	**133,018**	**128,197**	**132,686**	**137,134**	**141,809**
Cash Flow Statement						
Cash from operating activities	19,426	18,968	18,111	21,761	19,531	20,319
Cash from investing activities	(17,914)	1,538	642	(7,828)	(7,768)	(8,007)
Cash from financing activities	(9,678)	(9,443)	(13,086)	(9,898)	(10,446)	(10,677)
Net changes in cash	(8,166)	11,063	5,667	4,035	1,317	1,635
Cash at the end of the period	2,827	13,206	28,575	32,610	33,927	35,562
Key Ratios						
Current ratio	1.1	1.0	1.1	1.1	1.1	1.1
Inventory turnover ratio	41.2	42.8	46.9	43.3	44.6	44.7
Debtors' turnover ratio	3.6	3.5	3.7	3.6	3.7	3.7
Creditors turnover ratio	10.3	10.3	11.2	11.4	11.9	12.3
Gross profit margin	38.2%	38.4%	36.1%	36.9%	36.5%	36.2%
Operating margin	22.6%	25.2%	24.0%	24.1%	23.7%	23.4%
Net profit margin	18.2%	19.9%	20.7%	19.8%	19.6%	19.4%
EBITDA margin	36.9%	40.4%	39.4%	39.2%	39.2%	39.2%
Average return on equity	18.6%	18.9%	19.3%	19.7%	19.8%	19.7%
Average return on assets	9.2%	9.8%	10.0%	9.9%	9.7%	9.6%
Debt/Equity (x)	0.4x	0.4x	0.4x	0.4x	0.4x	0.4x
Interest coverage ratio (x)	5.8x	5.5x	10.0x	6.8x	6.7x	6.6x
P/E	16.4x	16.4x	29.6x	23.6x	23.1x	22.6x
EV/EBITDA	7.0x	6.8x	9.5x	10.8x	10.5x	10.1x
EV/Sales	2.6x	2.7x	3.7x	4.2x	4.1x	4.0x
EPS (AED)	1.0	1.0	1.1	1.1	1.1	1.1
Dividend payout ratio	73.2%	67.4%	94.3%	78.0%	78.0%	78.0%
Dividend yield (%)	4.9%	4.7%	3.8%	3.8%	3.8%	3.9%
Net debt	(5,768)	(4,644)	(2,843)	(6,106)	(6,628)	(7,444)
Net debt/ EBITDA	(0.30)	(0.22)	(0.14)	(0.28)	(0.30)	(0.33)
ROCE	14.6%	15.6%	15.8%	16.2%	15.9%	15.8%

Source: Company Financials, U Capital Research

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Mobile Telecommunications company Saudi Arabia (Zain KSA)

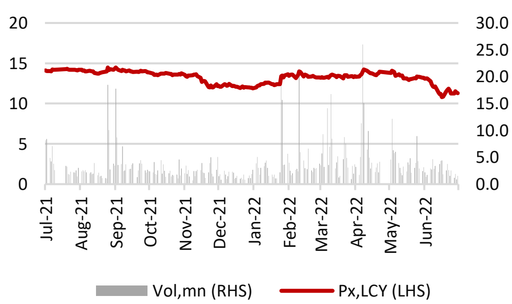
Target Price: SAR 13.8

Upside: 22.5%

Recommendation	**Buy**
Bloomberg Ticker	ZAINKSA:AB
Current Market Price (SR)	11.3
52wk High / Low (SR)	14.5 / 10.8
12m Average Vol. (mn)	3.7
Mkt.Cap. (SR bn)	10.1
Shares Outstanding (mn)	899
Free Float (%)	62.9%
3m Avg Daily Turnover (SR mn)	55.4
6m Average Daily Turnover (SR mn)	57.7
PE 2022e	44.6x
EV/EBITDA 2022e	5.3x
Dividend Yield '22e	0.0%
Price Performance:	
1 month (%)	-6.3%
3 months (%)	-17.2%
12 months (%)	-19.5%

Source: Refinitiv, as of 6th July 2022

Price -Volume Performance



Source: Refinitiv

- **One of the leading telecommunication services providers in the Kingdom of Saudi Arabia**
- **Diversified service offering catering to B2B and B2C sub-segment**
- **Refinancing and availing loans at better commercial terms to support the bottom line**
- **Monetizing from the sale of tower infrastructure to boast cash position and expand on its digital transformation journey**

We initiate coverage on Mobile Telecommunications Company Saudi Arabia with a Buy rating and a target price of SR 13.8 per share, implying an upside of 22.5% to the last closing price (6th July 2022). Our target price implies a P/E'22e of 54.7, reflecting an upside from the transformation initiative focusing on digitization and growth in B2B business. The free cash flow generated from the sale of tower assets will help the company generate shareholder value and provide financial aid to invest in upcoming technologies.

Investment Thesis

Valuation & Risks: Our valuation is based on a mix of discounted cash flows (30% weight), EV/EBITDA multiple (35% weight), and P/E multiple (35% weight). Key downside risks include reduced market share, decreased subscriber base, and delay in selling tower assets. Key upside risks include expansion of B2B portfolio, expansion of 5G network coverage, increased contribution from Tamam Finance company, advancement in digital offerings, and increase in subscriber base.

Expanding 5G coverage and furthering the journey towards digitization.

So far, the Zain KSA has expanded its 5G network coverage to cover 51 cities through 5000+ towers which have also helped the company earn several accolades in terms of speed, coverage, and performance. The company has established itself as one of the leading telecom operators and a digital service operator to individuals and businesses. The company is constantly improving its digital capabilities and digital service offerings.

Sale of towers and better refinancing to support balance sheet

The proceeds from the sale of towers will help the company in unlocking capital and support the company in accelerating its investments to improve customer experience. The company's ability to refinance its loans and avail at better commercial terms helps strengthen its cash position and reflects positively on its income statement.

Key Indicators

Year (In SAR mn)	FY19	FY20	FY21	FY22e	FY23e	FY24e
Sales	8,386	7,917	7,901	8,312	8,346	8,322
Gross profit	5,969	5,445	4,885	4,797	4,843	4,866
EBITDA	3,823	3,441	3,128	3,043	3,083	3,098
Operating profit	1,511	1,002	699	672	821	739
Net income	485	260	214	227	404	348
EPS	0.72	0.38	0.24	0.25	0.45	0.39
P/E (x)	16.7x	35.9x	50.5x	44.6x	25.1x	29.1x
EV/EBITDA (x)	3.7x	4.9x	5.8x	5.3x	5.2x	5.2x
Dividend yield, %	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%

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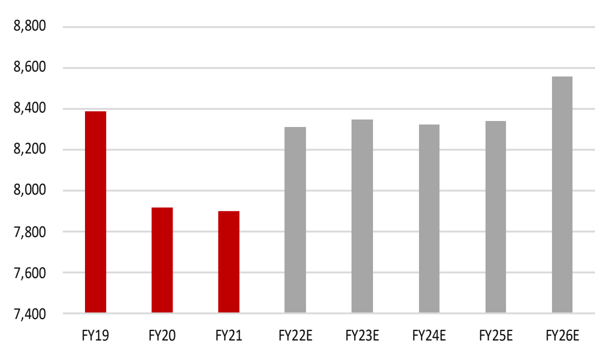
Revenue and gross margins

Gross margins for the company have been declining since FY19. The gross margin in FY20 remained impacted due to higher access charges and the pandemic outbreak, which negatively affected the revenue. FY21 witnessed a dip in gross margin from 68.8% in FY20 to 61.8% in FY21, majorly due to an increase in other elements in the direct cost structure, which increased from SAR 353.1 mn in FY20 to SAR 847.5 mn in FY21, an increase of 140.0% YoY. Baring 2Q21, gross margin in the quarters of FY21 remained on a downward trajectory declining the most in 4Q21, led by an increase in direct cost by 23.9% QoQ. The gross margin during 1Q22 remained marginally higher at 56.7% compared to 56.0% in 4Q21. We expect gross margins to increase over the quarters of FY22, buoyed by an increase in revenue and efficient cost management.

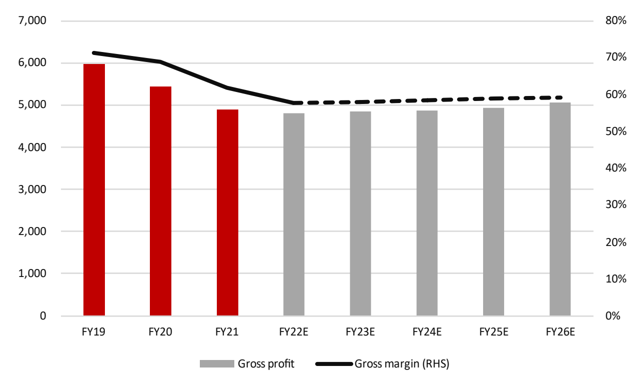
Topline in FY21 remained stable compared to FY20, which fell by 5.6% YoY. The drop in revenue in FY20 is attributed to low income from prepaid, postpaid, and visitor packages stemming from a limited number of visitors for Umrah. Revenue in FY21 remained stable despite a drop in revenue garnered through Zain Sales company which is involved in distributing and selling the company's devices. Zain's subscriber base during FY20 remained low at 7 million, mainly due to expats leaving the Kingdom. FY21 witnessed an increase in customer base from 7 million in FY20 to 8 million, characterized by a major transition from physical stores to online channels. We forecast the subscriber base to remain stable at 8 million for FY22 and to increase to 8.2 million in FY23.

During FY21, ~13% of revenue was utilized to increase the 5G coverage from 54% in FY20 to 63% in FY21. The company has around 4,805 sites and 51 cities under the 5G network. The investments made in the 5G space in the recent past and in the years to come will enable the company to grow its revenue at a CAGR of 4.7% between FY22 and FY26.

Revenue (in SAR mn)



Gross profit and margin (in SAR mn)



Source: Company Filings, U Capital Research

Monetizing the tower assets bodes well for the company

Overview: In February 2022, Zain KSA announced its board of directors' approval of the final offers received from the Public Investment Fund (PIF), HRH Prince Saud Bin Fahad, and Sultan Holding Company to acquire 60%, 10%, and 10% respectively, in the tower infrastructure. PIF's final offer also includes a call option granting PIF the right to buy the remaining 20% stake from Zain KSA for a certain amount. The approved final offers were to acquire stakes in Zain KSA's towers infrastructure comprising 8,069 towers, valuing these assets at SAR 3,026 million (USD 807 million)

The transaction: Zain KSA will sell its passive, physical towers infrastructure to PIF, HRH Prince Saud Bin Fahad, and Sultan Holding company and retain all other wireless communication antennas, software, technology, and intellectual property.

The sale process: Following the board of directors' approval in Feb. 2022 to sell stakes in Zain KSA's tower infrastructure, 80% of overall telecom tower assets amounting to SAR 1,365 million were transferred to assets held for sale, following which the depreciation on those assets ceased to be charged. The tower infrastructure of Zain KSA will be held by Zain Business company once it obtains the license. Zain Business company, a wholly owned subsidiary, is engaged in establishing, constructing, repairing, and maintaining telecom stations and towers. The three investors will then acquire their respective stakes in tower infrastructure held by Zain Business

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company, following which Zain Business will cease to remain Zain KSA's subsidiary and continue to operate as an associate company as Zain KSA continues to own a 20% stake in tower infrastructure held by Zain Business.

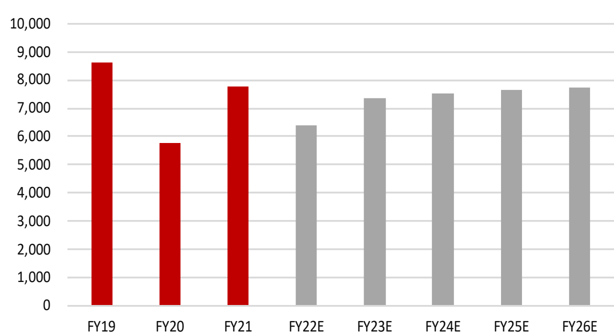
Financial impact: The company has long planned to monetize its tower assets. The sale of tower assets will help Zain KSA reduce its depreciation costs from the sold tower assets. Furthermore, the proceeds from the sale will benefit the company, relying less on debt financing.

The Telecom industry, being capital intensive, requires huge amounts to be spent on capital expenditures. In October 2019, Zain KSA launched the third largest 5G network worldwide and the largest 5G network in the Middle East, Europe, and Africa. The company during FY19 remained under pressure, with debt to equity at 2.1x. The company, in a bid to improve its financial position, which continued to have accumulated losses for quite some time, underwent capital restructuring and rights issue in 4Q20 to strengthen its financial condition, following which its accumulated losses reduced to SAR 54.0 mn from SAR 1,384.1 mn.

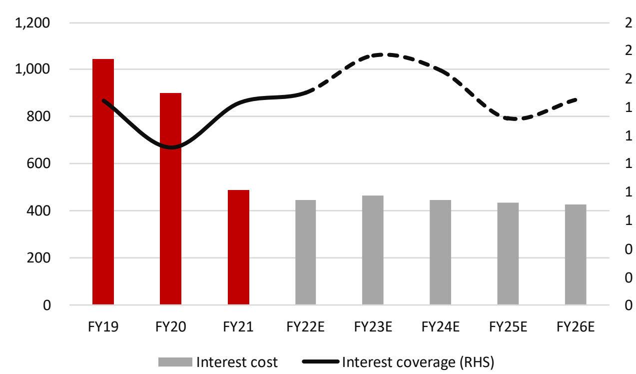
Refinancing and extension of the facility at better terms help reduce the cost structure and tap future opportunities

Zain KSA, in September 2020, refinanced and extended the maturity date of its existing five years syndicated Murabaha facility until 2025 with two years grace period at better commercial terms. Consequently, finance costs during FY21 were reduced by 45.5% YoY despite the increase in overall debt by 34.9% YoY. The company, on April 2022, drew down 2.8 bn from the available syndicated murahaba facility of SAR 6 bn availed at better terms to pay off two debts payments in FY22 (Junior murahaba, which is maturing in FY22, and installment payable to the ministry of finance) bringing the outstanding murahaba financing at SAR 5.7 bn. Overall, the company can reduce its interest cost in the forecast period underpinned by better commercial terms and reducing debt.

Total Debt (SAR mn)



Interest cost (SAR mn) and interest coverage ratio



Source: Company Filings, U Capital Research

Zain's ongoing investment in 5G space coupled with synergies from the sale of tower assets augurs well in the long run

PAT for the company has been falling with a decline of 46.4% YoY in FY20, followed by a decrease of 17.6% YoY in FY21. The fall in FY20 is attributed to travel restrictions limiting the number of business, Umrah, and leisure visitors, coupled with a drop in customer base led by expat exodus. 2021 net profit remained impacted due to no growth in topline coupled with an increase in the cost of sales by 22.0% YoY due to the reversal of provision in FY20. As we advance, we expect the company's ongoing investment in the 5G space and IoT, lower depreciation resulting from the sale of tower assets, and the financing facilities availed at better commercial terms to boost Zain's bottom line and expand its net margin from 2.7% in FY21 to 7.6% in FY26.

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Relative valuation

We have given an equal weightage of 35% each to the P/E and EV/EBITDA multiples. The peer set includes the companies globally. At average median peer P/E multiple of 16.2x and EV/EBITDA multiple of 5.6x, we arrive at target price of SAR 7.3 and SAR 12.6 per share respectively.

Discounted Cash Flow

	FY22	FY23	FY24	FY25	FY26	Terminal Value
Pegged on: July 6, 2022						
Time period index	0.49	1.49	2.49	3.49	4.49	4.49
Free cash flow						
PAT	227	404	348	207	255	
Interest (1-tax rate)	414	431	413	404	395	
Depreciation	2,372	2,262	2,359	2,575	2,671	
Changes in Working Capital	(17)	(161)	(26)	(59)	(92)	
Less: Capex	(1,215)	(1,264)	(1,296)	(1,299)	(1,334)	
Free cash flow to firm (FCFF)	1,781	1,672	1,797	1,828	1,895	26,951
Discounted FCFF	1,715	1,489	1,480	1,393	1,335	18,997

All figures in SAR mn unless otherwise stated

Enterprise Value	26,410
Less: Net debt (Includes lease liabilities)	5,862
Equity Value	20,547
Shares O/S	899
Equity Value per share (in SAR)	22.9
Current share price (SAR)	11.28
% upside/downside	102.7%

Assumptions	
WACC	8.1%
Tax Rate	7.3%
Cost of debt / Lease Liabilities	6.3%
Cost of Equity	10.1%
Terminal growth rate	1.0%
Cost of equity calculation	
Risk Free Rate	3.9%
Beta	1.0
Equity Risk Premium	6.3%
Weights	
Debt	46.3%
Equity	53.7%

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Mobile Telecommunications Company Saudi Arabia (Zain KSA)

About

Mobile Telecommunications Company Saudi Arabia (Zain KSA) (The Company), a member of Zain Group, is a Saudi Arabia-based company engaged in providing mobile telecommunications services across Saudi Arabia. The company operates, purchases, sells, distributes, delivers, installs, manages, and maintains mobile telephone services and equipment. The Group also provides consulting services, constructs and repairs telecom towers, provides fintech services and offers technical drone services along with selling and repairing.

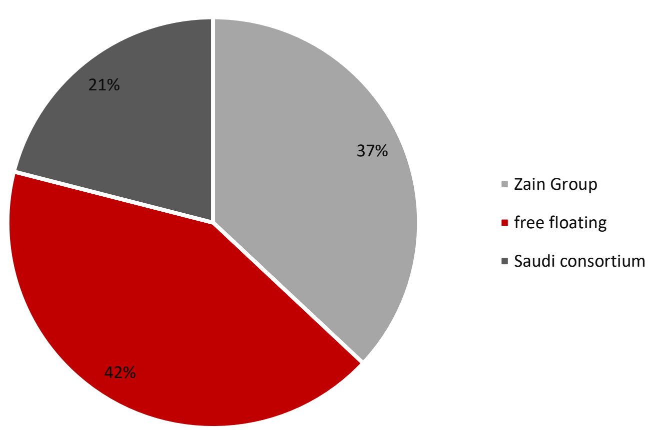
The company commenced its operation in August 2008 following its Initial Public Offering in February 2008. In September 2011, Zain KSA became the first operator in the Middle East to launch a 4G/LTE network commercially. In October 2019, the company launched the world's third largest 5G network and the largest 5G network in the Middle East, Europe, and Africa. The company has over 8 million customers and covers more than 51 cities across the Kingdom with its 5G network.

Subsidiaries:

- **Zain Sales Company:** Established with a share capital of SAR 10,000, the company is engaged in distributing, selling telecom equipment and handsets; and providing consulting services. The company started its operation in 1Q19.
- **Zain Business Company:** Established with a share capital of SAR 10,000, the company is engaged in the establishment, construction, repair, and maintenance of telecom stations and towers. The company is not operational yet.
- **Zain Payments Company:** Zain group's FinTech subsidiary Tamam has been officially licensed by the Saudi Central Bank to offer consumer micro-loans through a fully digital customer experience via a mobile app. The company started its operation during 4Q19.
- **Zain Drones Company:** Established with a share capital of SAR 10,000, the company is engaged in providing professional, scientific, and technical drone services along with selling and repairing drones. The company started its operation during 4Q19.

Ownership

The shareholding pattern of the company is given below



Source: Company filings

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Key financials

(SAR mn)	FY19	FY20	FY21	FY22e	FY23e	FY24e
Income Statement						
Sales	8,386	7,917	7,901	8,312	8,346	8,322
COGS	(2,418)	(2,472)	(3,016)	(3,515)	(3,503)	(3,456)
Gross profit	**5,969**	**5,445**	**4,885**	**4,797**	**4,843**	**4,866**
Operating and administrative expenses	(1,899)	(1,763)	(1,749)	(1,753)	(1,760)	(1,768)
Operating profit	**1,511**	**1,002**	**699**	**672**	**821**	**739**
Share of results of investments in associates and joint ventures	0	0	0	0	59	59
Other income – net	11	28	20	20	20	20
Finance charges	(1,045)	(898)	(489)	(447)	(465)	(445)
Income before tax	**504**	**280**	**231**	**245**	**436**	**375**
Income tax	(19)	(20)	(17)	(18)	(32)	(28)
Net income for the period	**485**	**260**	**214**	**227**	**404**	**348**
Balance Sheet						
Cash and equivalents	1,157	1,103	512	1,786	2,242	2,830
Trade and other receivables	1,730	1,996	2,988	3,302	3,430	3,354
Inventories	242	187	214	249	257	264
Property and Equipment	6,080	6,857	6,640	5,051	4,513	4,298
Right-of-use assets	1,448	1,285	1,331	460	1,714	1,838
Intangible assets	16,216	16,280	15,561	15,026	14,497	13,954
Investment in associates	0	0	0	0	86.5	86.5
Total assets	**27,738**	**28,158**	**27,877**	**26,529**	**27,417**	**27,324**
Trade and other payables	3,100	3,488	3,692	4,042	4,037	3,968
Borrowings and notes payable	7,139	4,396	6,326	5,727	5,818	5,871
Lease liabilities	1,476	1,384	1,473	655	1,558	1,640
Share capital	5,837	8,987	8,987	8,987	8,987	8,987
Statutory reserve	0	0	21	44	85	119
Retained earnings	(1,608)	(54)	139	343	707	1,020
Total stockholders' equity	**4,103**	**8,729**	**9,040**	**9,267**	**9,671**	**10,019**
Total liabilities & stockholders' equity	**27,738**	**28,158**	**27,877**	**26,529**	**27,417**	**27,324**
Cash Flow Statement						
Cash from operating activities	3,326	4,029	1,574	1,650	2,611	2,782
Cash from investing activities	(2,035)	(1,825)	(1,085)	1,165	(1,264)	(1,296)
Cash from financing activities	(1,551)	(2,215)	(861)	(1,542)	(891)	(898)
Net changes in cash	(260)	(11)	(372)	1,274	456	588
Cash at the end of the period	1,157	1,103	512	1,786	2,242	2,830
Key Ratios						
Current ratio	0.8	0.4	0.4	0.5	0.6	0.7
Inventory turnover ratio	10.4	11.5	15.0	15.2	13.8	13.3
Debtors' turnover ratio	5.1	4.2	3.2	2.6	2.5	2.5
Creditors turnover ratio	0.7	0.8	0.8	0.9	0.9	0.9
Gross profit margin	71.2%	68.8%	61.8%	57.7%	58.0%	58.5%
Operating margin	18.0%	12.7%	8.8%	8.1%	9.8%	8.9%
Net profit margin	5.8%	3.3%	2.7%	2.7%	4.8%	4.2%
EBITDA margin	45.6%	43.5%	39.6%	36.6%	36.9%	37.2%
Average return on equity	12.0%	4.1%	2.4%	2.5%	4.3%	3.5%
Average return on assets	1.8%	0.9%	0.8%	0.8%	1.5%	1.3%
Debt/Equity	2.1x	0.7x	0.9x	0.7x	0.8x	0.7x
Interest coverage ratio	1.4x	1.1x	1.4x	1.5x	1.8x	1.7x
P/E	16.7x	35.9x	50.5x	44.6x	25.1x	29.1x
EV/EBITDA	3.7x	4.9x	5.8x	5.3x	5.2x	5.2x
EV/Sales	1.7x	2.1x	2.3x	1.9x	1.9x	1.9x
EPS (SAR)	0.7	0.4	0.2	0.3	0.4	0.4
Dividend payout ratio	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Dividend yield	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Net debt	7,458	4,677	7,286	4,595	5,134	4,681
Net debt/ EBITDA	2.0	1.4	2.3	1.5	1.7	1.5
ROCE	6.5%	5.3%	4.0%	4.0%	4.7%	4.2%

Source: Company Financials, U Capital Research

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Disclaimer

Recommendation

BUY	Greater than 20%
ACCUMULATE	Between +10% and +20%
HOLD	Between +10% and -10%
REDUCE	Between -10% and -20%
SELL	Lower than -20%

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