

Rating **Buy**
12- Month Target Price **SAR 11.50**

ZAIN COMPANY
1Q2019 First Look

Expected Total Return

| | |
|----------------------------|-----------|
| Price as on April 18, 2019 | SAR 10.62 |
| Upside to Target Price | 8.3% |
| Expected Dividend Yield | 0.0% |
| Expected Total Return | 8.3% |

Market Data

| | |
|-----------------------|-------------------|
| 52 Week H/L | SAR 11.30/5.77 |
| Market Capitalization | SAR 6,188 million |
| Shares Outstanding | 584 |
| Free Float | 51.8% |
| 12-Month ADTV | 4,324,662 |
| Blomberg Code | ZAINKSA |

1-Year Price Performance



Source: Bloomberg



| Fig in SAR mln | RC Est. | Actuals |
|----------------|---------|---------|
| Sales | 1,703 | 2,093 |
| Gross Profit | 1,379 | 1,480 |
| Net Income | 213 | 129 |
| EPS (SAR) | 0.36 | 0.22 |

Target Price Nears

Zain has now posted profits for the third consecutive quarter although 1Q2019 net profit of SAR 129 million missed both our expectations and market consensus. It appears both operational performance as well as reversal of provisions were below expectations. We are happy to note revenue growth both on a quarterly and yearly basis to SAR 2.1 billion, much higher than expectations. Gross margins remain elevated at 71% but are down from 89% last year as 4Q2018 incorporated higher reversals. Operating profit declined by -39% Q/Q but increased +167% Y/Y while EBITDA margin improved to 46% from 34% last year. Zain's stock price neared our target price of SAR 11.50 at the Tadawul recently before correcting. We are in the process of re-evaluating our assumptions and will get back to investors soon with updated forecasts and target price. For now, we maintain our Buy recommendation and target price of SAR 11.50, despite the stock offering less than 15% upside.

Revenues grow +24% Y/Y

The company's topline grew by +2% Q/Q and +24% Y/Y to SAR 2.1 billion on the back of rising demand for the company's products and services while we believe the impact of higher data prices is also flowing through. This is despite the decrease in industry subscriber numbers by -2.3% Q/Q to 41.3 million. Zain has reported 8.2 million subscribers at the end of 1Q, adding 200K subscribers compared to 2018. At the same time, we believe Mobily is now giving tougher competition specially in the business segment while decreasing number of expats as well as blue collar workers preferring Virgin and Lebara would be challenges going forward.

Gross margin at 71%

Gross profit reached SAR 1.5 billion, down -19% Q/Q but up +32% Y/Y. The Y/Y rise is a consequence of a decrease in royalty fees from 15% to 10%. Gross margin reached 71% this quarter compared to 89% last quarter and 66% last year. The decline in margins Y/Y is likely due to lower reversals as compared to the previous quarter.

EBIT down by -39% Q/Q

Operating profit came down -39% Q/Q to SAR 382 million but has increased by +167% Y/Y. On a yearly basis, operating and administrative expenses have decreased by SAR 21 million due to reclassification of lease from operating expenses to depreciation on adoption of IFRS 16.

Third consecutive quarterly net profit

Zain achieved a net profit of SAR 129 million, which missed both our forecasts and market consensus. According to the Company, the quarterly decline in net income is due to the variance in reversal to the tune of SAR 278 million from the settlement signed with MOF, MCIT and CITC. We are encouraged by the significant improvement in EBITDA to SAR 955 million compared to SAR 570 million last year. EBITDA margin has improved from 34% last year to 46% this quarter. We are in the process of updating our assumptions and would issue updated forecasts and target price soon.

Key Financial Figures

| FY Dec31 (SAR mln) | 2018A | 2019E | 2020E |
|--------------------|-------|-------|-------|
| Sales | 7,531 | 7,965 | 8,153 |
| Gross Profit | 5,425 | 5,728 | 5,870 |
| EBITDA | 3,009 | 2,896 | 2,989 |
| Net Profit | 332 | 807 | 819 |
| EPS (SAR) | 0.57 | 1.38 | 1.40 |

Key Financial Ratios

| FY Dec31 | 2018A | 2019E | 2020E |
|--------------|-------|-------|-------|
| Gross Margin | 72% | 72% | 72% |
| EBIT Margin | 16% | 20% | 19% |
| Net Margin | 4.4% | 10.1% | 10.0% |
| EV/EBITDA | 7.24x | 7.13x | 6.67x |
| P/FCF | 0.8x | 2.4x | 2.6x |

Stock Rating

| Buy | Neutral | Sell | Not Rated |
|--|---|--------------------------------------|--------------------------|
| Expected Total Return Greater than 15% | Expected Total Return between -15% and +15% | Expected Total Return less than -15% | Under Review/ Restricted |

** The expected percentage returns are indicative, stock recommendations also incorporate relevant qualitative factors*

For any feedback on our reports, please contact research@riyadcapital.com

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