



Net income aided by gain on tower sale; a weak normalized bottom line dragged by higher OPEX; revenue growth remains strong

Zain KSA's net income surged to SAR 563mn in Q1-23 from SAR 81mn in Q1-22. The net income was significantly higher than AJC's and consensus estimates of SAR 113mn and SAR 207mn, respectively. It is noteworthy that the bottom line was boosted by recognition of a one-off gain of SAR 532mn on sale tower assets during the quarter. As per our calculations, normalized net income (excluding one-off gain) is ~SAR 31mn. The lower-than-expected normalized net income was primarily due to higher-than-expected OPEX (excluding D&A), partly offset by slightly higher revenue and better GP margin. Revenue increased by 11.2% Y/Y to SAR 2,422mn, in line with our estimate of SAR 2,375mn. The GP margin stood at 58.4% vs. 56.7% in Q1-22 and our estimate of 57.0%. We maintain our TP at SAR 12.8/share, while keeping the "Neutral" recommendation on Zain KSA.

- Zain KSA's net income jumped SAR 563mn in Q1-23 from SAR 81mn in Q1-22, above our and market estimates of SAR 113mn and SAR 207mn, respectively. The company recorded a net gain of SAR 532mn related to the sale of tower assets. We estimate normalized net income (excluding one-off gain) to be at ~SAR 31mn, which was significantly below our expectation. The deviation from our estimate was mainly due to higher OPEX (excluding D&A), even though revenue and GP margin were above our estimate.
- Revenue increased 11.2% Y/Y to SAR 2,422mn in Q1-23, in line with our estimate of SAR 2,375mn. The healthy growth in the top line was attributed to an increase in revenue for B2B, 5G and Tamam. On a Q/Q basis, revenue inched up by 0.8%.
- Gross profit rose 14.5% Y/Y to SAR 1,415mn, as revenue growth was further bolstered by expansion of GP margin. The GP margin expanded ~170bps Y/Y to 58.4% from 56.7% in Q1-22 and above our estimate of 57.0%.
- Operating profit was flat Y/Y at SAR 201mn in Q1-23, below our estimate of SAR 278mn, as a significant jump in OPEX wiped off the positive impact from gross profit growth. OPEX increased by SAR 195mn Y/Y, while depreciation and amortization decreased SAR 16mn Y/Y. Operating margin stood at 8.3% in Q1-23 compared to 9.2% in Q1-22 and below our estimate of 11.7%.

AJC view: Zain KSA's Q1-23 results were below our expectations if positive effect of gains from sale of tower asset is excluded. However, the company managed to post double-digit revenue for the fifth consecutive quarter. Moreover, the gross margin was also healthy at 58.4%. On the other hand, a spike in OPEX is a concern and it needs to be seen if there were any one time expenses or impairments that led to an increase in OPEX. Nevertheless, we expect OPEX to increase this year, as the sale of towers and leaseback is expected to have a negative impact on operating profit. We forecast operating profit for FY23E to be at SAR 1,151mn, implying a 5.7% Y/Y growth, as higher OPEX is expected to be offset by strong revenue growth and healthy gross margin. Zain KSA currently trades at an EV/EBITDA ratio of 5.5x based on our FY23 estimates. We maintain our TP at SAR 12.8/share, while keeping the "Neutral" recommendation on Zain KSA.

Results Summary

SARmn	Q1-22	Q4-22	Q1-23	Change Y/Y	Change Q/Q	Deviation from AJC Estimates
Revenue	2,179	2,404	2,422	11.2%	0.8%	2.0%
Gross Profit	1,236	1,452	1,415	14.5%	-2.6%	4.5%
Gross Margin	56.7%	60.4%	58.4%	-	-	-
EBIT	201	379	201	-0.1%	-47.0%	-27.7%
Net Profit	81	250	563	599.2%	125.2%	396.3%
EPS	0.09	0.28	0.63	-	-	-

Source: Company Reports, Aljazira Capital *NM: Not meaningful

Recommendation	Neutral
Target Price (SAR)	12.8
Upside / (Downside)*	-20.6%

Source: Tadawul *prices as of 08th of May 2023

Key Financials

SARmn (unless specified)	FY21	FY22	FY23E	FY24E
Revenue	7,901	9,075	9,888	10,357
Growth %	-0.2%	14.9%	9.0%	4.7%
Net Income	214	550	1,027*	829
Growth %	-17.6%	156.5%	86.8%	-19.3%
EPS	0.24	0.61	1.14	0.91

Source: Company reports, Aljazira Capital

*FY23E net income does not include additional gains from tower deal

Key Ratios

	FY21	FY22	FY23E	FY24E
Gross Margin	61.8%	58.6%	58.6%	58.4%
Net Margin	2.7%	6.1%	10.4%	8.0%
ROE	2.4%	5.2%	8.8%	6.6%
P/E (x)	High	16.4	14.1	17.5
P/B (x)	1.2	0.8	1.2	1.2
EV/EBITDA (x)	5.6	4.0	5.5	4.8

Source: Company reports, Aljazira Capital

Key Market Data

Market Cap(bn)	13.0
YTD%	60.2%
52 week (High)/(Low)	16.34/9.86
Share Outstanding (mn)	898.7

Source: Company reports, Aljazira Capital

Price Performance



Source: Tadawul, Aljazira Capital

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TERMINOLOGY

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3. **Neutral:** The rating implies that the stock is trading in the proximate range of its 12 months price target. Stocks rated "Neutral" is expected to stagnate within +/- 10% range from the current price levels over next twelve months.
4. **Suspension of rating or rating on hold (SR/RH):** This basically implies suspension of a rating pending further analysis of a material change in the fundamentals of the company.

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