

*Jan-17*

## **OMAN TELECOM SECTOR**

*Increase in royalty charges to impact 2017 earnings, downgrade to neutral...*



الخليجية بادر للأسواق المالية ش.م.ع.  
GULF BAADER CAPITAL MARKETS S.A.O.C.

### ***Oman Telecom Sector – Increase in royalty charges to impact 2017E Earnings, Neutral on valuations...***

<b>Omantel</b>	<b>Closing Price:</b> RO 1.450	<b>Rating:</b> Neutral	<b>Fair Value:</b> 1.520
<b>Ooredoo Oman</b>	<b>Closing Price:</b> RO 0.612	<b>Rating:</b> Neutral	<b>Fair Value:</b> 0.670

#### **The Event- Increase in the Telecom Sector Royalty Charges to 12% from 7% levels**

- Towards fag end of 2016, the Capital Market Authority (CMA) received an official letter from the Telecommunication Regulatory Authority (TRA) mentioning that the decision of Council of Ministers to revert the Royalty on all telecommunication Operators to its previous rate of 12% as specified in Royal Decrees, effective 1<sup>st</sup> Jan 2017
- **The current royalty rate is 7% of total revenues and this would be increased to 12% of revenues, starting Jan 2017.**
- As per Omantel announcement in the MSM, if the increase had been applied for the first nine months of 2016, the effect on net profit would have been a reduction of RO 16 million (for 9 months). As per our estimates, the annualized impact would be c. RO 21.3 million (forming c. 17% of net profit)
- As per Ooredoo Oman bourse announcement, if the increase had been applied for the first nine months of 2016, the effect on net profit would have been a reduction of RO 8.7 million (for 9 months). As per our estimates, the annualized impact would be c. RO 11.6 million (forming c. 23% of net profit)

The increase in royalty changes had been discussed by the Shura Council and the Government over the last two years with the prevailing tough economic conditions. On this anticipation, both Omantel (down 3.2% in 2016 and further -4.3% declined today) and Ooredoo Oman (down 6.8% in 2016 and further -7.3% today) stocks had underperformed lately as against the benchmark MSM Index (gained 7% in 2016). The prevailing higher dividend yield would protect further downside.

#### **Our Scenario Analysis on 2017 Earnings – Incorporated 12% royalty charges and 15% corporate tax rates**

Post this news announcement, we have revised our earnings models of Omantel and Ooredoo Oman incorporating 12% royalty charges (against 7% earlier) and also the expected increase in corporate tax to 15% levels starting 2017E. The combined impact would be double-whammy and negatively reflect in lower earnings for both the companies under our coverage.

**Impact on Omantel:** As per our estimates, Omantel 2017E royalty charges is estimated to increase c. RO 21 million, higher by 59% as compared to previous estimates and this would lead to c.9% decline in EBITDA and c. 15% decline in net profit against our earlier projections. Revised EPS for 2017 is estimated at RO 0.133 as compared to RO 0.157. We do expect lower dividends of RO 0.100 for 2017E (to be paid during Aug 2017 and Mar 2018). **At the current levels, the stock trades at PE (2017E revised) of 10.9X, PBV (2017E) of 1.8X and provides dividend yield of 6.9%. We revise the rating to Neutral with fair value of RO 1.520**

**Impact on Ooredoo Oman:** As per projections, 2017E royalty charges of Ooredoo is anticipated to increase c. RO 14 million, higher by 71% as compared our earlier estimates and this would in turn lower EBITDA by 9% and Net profit by 21% against our earlier workings. The revised 2017E EPS would be RO 0.054 as compared to RO 0.069. We also estimate lower dividend of RO 0.038 for 2017E (to be paid in Mar 2018). At the current levels, the stock trades at PE (2017E) of 11.4X, PBV (2017E) of 1.6X and dividend yield of 6.2%. **While we don't see any impact to 2016 profits and dividends, this would mean 7.5% yield based on Mar 2017 dividends, this may protect the downside. We downgrade to Neutral rating with 12 month fair value of RO 0.670**

**Caveats to remain with new telecom law, changes in access and Interconnection charges and the new third mobile licence**

Find below the workings on Omantel and Ooredoo Oman along with revised valuations.

## Omantel- Impact Analysis

2017 Estimates- Post Royalty Charges increase to 12% of revenue and Assuming 15% Corporate Tax, no impact estimated on Third Mobile License						
Figures in RO 000s	2016 est.	No change in 2016	2017-old est.	2017-new est.	In Absolute terms (Increase/ Decrease)	% Change
Revenue	539,163		558,776	558,776	-	0.0%
Royalty Charges	35,034		36,360	57,721	21,361	58.7%
EBITDA	233,496		240,484	219,123	(21,361)	-8.9%
Tax	16,128		20,768	17,564	(3,204)	-15.4%
<b>Net Profit after tax- after minority</b>	<b>118,268</b>		<b>117,685</b>	<b>99,528</b>	<b>(18,157)</b>	<b>-15.4%</b>
EPS (In RO)	0.162		0.157	0.133		-15.3%
DPS (In RO)	0.115		0.115	0.100		-13.0%
Div. Payout (%)	71%		73%	75%		
<b>Valuations (Closing- RO 1.450)</b>	<b>2016 est.</b>		<b>2017-old est.</b>	<b>2017-new est.</b>		
PE (x)	9.2		9.3	10.9		
PBV (x)	1.8		1.7	1.8		
Div. Yield (x)	7.9%	Interim-40% paid during Aug 2016	7.9%	6.9%	Total dividends (Interim-Aug 17 and Final- Mar 18)	
		Final- 75% to be paid during Mar 2017				
<b>Fair Value - 12 month (In RO)</b>	<b>1.520</b>	Based on DCF, DDM and PE valuation				
Current closing	1.450					
<b>Upside</b>	<b>4.8%</b>					
<b>Rating</b>	<b>Neutral</b>	Downgraded from Accumulate				

Source: Company Reports; GBCM Research

## Ooredoo Oman- Impact Analysis

2017 Estimates- Post Royalty Charges increase to 12% of revenue and Assuming 15% Corporate Tax, no impact estimated on Third Mobile License						
Figures in RO 000s	2016 est.	No change in 2016	2017-old est.	2017-new est.	In Absolute terms (Increase/ Decrease)	% Change
Revenue	271,417		280,867	280,867	-	0.0%
Royalty Charges	18,999		19,661	33,704	14,043	71.4%
EBITDA	122,993		125,052	113,817	(11,235)	-9.0%
Tax	6,578		7,875	6,190	(1,685)	-21.4%
<b>Net Profit after tax</b>	<b>48,237</b>		<b>44,624</b>	<b>35,074</b>	<b>(9,550)</b>	<b>-21.4%</b>
EPS (In RO)	0.074		0.069	0.054		-21.7%
DPS (In RO)	0.046		0.048	0.038		-20.8%
Div. Payout (%)	62%		70%	70%		
<b>Valuations (Closing- RO 0.612)</b>	<b>2016 est.</b>	<b>Comment</b>	<b>2017-old est.</b>	<b>2017-new est.</b>	<b>Comment</b>	
PE (x)	8.3		8.9	11.4		
PBV (x)	1.7		1.6	1.6		
Div. Yield (x)	7.5%	To be paid during Mar 2017	7.8%	6.2%	To be paid during Mar 2018	
<b>Fair Value - 12 month (In RO)</b>	<b>0.670</b>	<b>Based DCF, EV and PE valuation</b>				
Current closing	0.612					
<b>Upside</b>	<b>9.5%</b>					
<b>Rating</b>	<b>Neutral</b>	Downgraded from Buy				

Source: Company Reports; GBCM Research

### **Stock Rating Methodology:**

**Buy** - Upside more than 20%

**Accumulate** - Upside between 10% and 20%

**Neutral** - Upside or downside less than 10%

**Reduce** - Downside between 10% and 20%

**Sell** - Downside more than 20%

**Not Rated** - Stocks not in regular research coverage

### **Time Horizon**

**LT** – Long Term rating with a 12 to 18 month horizon

**ST** – Short Term rating with a 3 to 6 month horizon

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