Zain Group
Q1 2021
Earnings Conference Call

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Chaired by:
Ziad Itani
Arqaam Capital

Zain Group Q1 2021 Earnings Call Transcript

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Zain Group Executive Management:

Ossama Matta - Group Chief Financial Officer
Kamil Hilali – Group Chief Strategy Officer
Mohammad Abdal - Group Chief Communications Officer
Iyadh Borgi - Group Operation & business Performance Director
Aram Dehyan - Group Investor Relations Senior Manager

Moderator:
Ziad Itani, Arqaam Capital

Ziad Itani:
Greetings ladies and gentlemen, this is Ziad from Arqaam Capital and I would like to welcome you all to the Zain Group's Q1 2021 Results Conference Call. It is my pleasure to host Zain Group senior management today on the call. By now you should have received the company's presentation and earnings release for the 1st quarter and detailed financials which have all been uploaded on the Group's website.

Now without further delay, I will hand the call to Mohammad Abdal, Zain Group's Chief Communications Officer. Thank you.

Mohammad Abdal:
Thank you, Ziad. And welcome everyone to Zain's Q1 2021 earnings conference call. With me today Ossama Matta, Group CFO, Kamil Hilali, Group Chief Strategy Officer, Iyadh Borgi, the Operation & business Performance Director and Aram Dehyan, IR Senior Manager. In a moment, we will take you through the IR presentation which has been posted earlier today on our corporate website, and after that we're happy to answer any question you may have.

During this call, we will be making forward-looking statements which are predictions, projections or other statements about future events. These statements are based on current expectations and assumptions that are subject to risks and uncertainties.

Please refer to our detailed cautionary statement found in slide number 2.

With that, I will now turn the call over to Ossama.

Ossama Matta:
Thanks, Mohammad. Good afternoon to everyone and thank you for joining us on today's call.

The world continues to deal with the pandemic, and we are trying our best to keep the operations running smoothly. We continue focusing on our primary aim to lessen the impact of the pandemic on society by granting increased digital access to essential medical, commercial, educational and financial services. We are aware that countries are still dealing with great challenges on account of COVID-19, however we hope all of you and your families are keeping healthy and safe.
I would like to start by briefly touching upon the operational highlights of the quarter:

- Zain KSA's continually improving cash flow has seen the OPCO **completely settle the Group Shareholder Loan** with an upstream of USD 553 million during Q1 2021.
- Our operations in Iraq and South Sudan launched high speed **4G commercial services**, boosting connectivity to their economies.

- **Zain Cash Jordan** gets initial approval for Credit Solutions, subject to fulfilling all regulatory requirements within 6 months.
- **Zain esports** successful rollout continues as one of the fastest growing esports brands across Middle East attracting over 15,000 registered players and 25 million views across various social media channels.
- **The Zain Group Application Program Interface (API)** platform continues to grow with 12 digital partnerships offering 24 attractive services, resulting in substantial revenue with 5 million monthly transactions and totaling over 80 million transactions since its launch.
- Our persistent efforts in **Sustainability** were rewarded as Zain was the highest ranked MEA operator in CDP global index with respect to its efforts to address climate change.
- Moreover, Zain Group published its **10th annual sustainability report**, titled 'The Ten-Year Journey' as well as an insightful report on 'Women in Technology-Bridging the Gender Gap in STEM Fields'.

Our 4Sight strategy is taking shape that support our vision of becoming a leading ICT and digital lifestyle provider. **Pages from 7 to 14** showcases the key elements of our strategy and the major achievements during the period.

Moving into the 1st quarter financial highlights starting from page (16).
Despite the COVID impact and major currency devaluation in two of our key markets namely Iraq and Sudan, we concluded the quarter with consolidated revenue of USD 1.3 billion, down 6% YoY, while consolidated EBITDA for the quarter dropped 7% compared to Q1 '20, to reach USD 523 million, nevertheless still reflecting a healthy EBITDA margin of 41%. Consolidated net income dropped 5% to reach USD 147 million, reflecting Earnings Per Share of 10 Fils (USD 0.03). Excluding the one-time gain of ~USD 15m from the sale and lease back of towers in Kuwait during Q1 '20, the Group's net income reflects a 4% increase YoY.

We ended the quarter serving 48.5 million customers, which is a drop of approximately 3% mainly on account of the conclusion of the management contract with Touch Lebanon back in October 2020.

For Q1 2021, foreign currency translation impact **(page 19)**, mainly due to the currency devaluation in Sudan from 55 to 375 (SDG / USD), and a 19% currency devaluation in Iraq from an average of 1,190 to 1,470 (IQD / USD), cost the Group USD 177 million in revenue and USD 66 million in EBITDA.

Excluding the FX translation impact, Revenue growth would have been +7% and EBITDA growth would have been +5%

It should be noted that the impact of the pandemic on the business was minimal during Q1 ‘2020, given its early stage of spread at the time, however in Q1 2021 the impact was more profound.

CAPEX on page **(20)**… The Group continued to invest at healthy levels across operations. We closed the quarter with a total of USD 415 million, spent on 5G rollouts, coupled with FTTH and 4G expansion, as well as spectrum license fees in key markets (tangible capex represents 5.5% to total group revenue). As you see in the slide, the majority of intangible Capex is coming from the grant of 4G license in Iraq, and the renewal of the 900 MHz license in Jordan.

Our Debt Profile on the next page… The Group continues to maintain healthy cash flows, with total debt reducing by 17% (in KD terms) compared to Q1 ‘20 and net debt / EBITDA currently stands at 2.2x.

Moving to the Opcos... Let’s move to slide (26) - Zain Kuwait.
Operationally, Zain Kuwait remains the most profitable company within the Group and maintains its market lead in terms of both value share and customer base, serving 2.5 million customers. Its market leadership in all key financial indicators is highlighted by its revenue representing 40% of the total market revenue and 73% of the industry’s net income.

For Q1 2021, the operator recorded a stable revenue of USD 263 million, due to growth in 5G segment partially offset by decrease in roaming revenue due to extended air travel restrictions.

Due to several cost optimization initiatives implemented by the operation, the EBITDA increased by 5%. As well healthy acquisitions translated in a better collections and lower bad debts.

Net income for the quarter grew by 8% YoY excluding the $15m Gain on Sale and leaseback of towers in Q1-2020.

During the quarter, the operator witnessed impressive growth in both 5G mobile and broadband customers and resulting revenue capturing the largest 5G market share in the country. The operation invested USD 13 million (5% of its revenue) in CAPEX.

On the regulatory side, Zain implemented the reduction of 55% in international cross connect costs in Feb 2021 approved by CITRA last year. Also, CITRA awarded a MVNO license to Virgin, expected to launch in Q3/Q4, 2021.

Continuous innovation and digital transformation saw the launch of a new and dynamic customer app offering many new features, as well as enhancement of its web and zBot chat service.

From a B2B perspective, Zain Kuwait partnered with the Ministry of Interior to revamp the Kuwait TV app to live stream 9 local video and 11 radio channels. Also, the operator entered deals with Kuwait International Bank and Boubyan Bank for data related services.

Saudi Arabia which is on slide (27).

Revenue for the quarter dropped by 5% as several challenges continue to impact the operation. The decrease in revenue is attributable to the impact of the COVID-19 pandemic, MTR reduction, and VAT increase from 5% to 15% commencing in July 2020, coupled with decrease in customer base due to:

- Departure and drop in the number of expats in the country.
- Lack of Visitors and Pilgrims due to Umrah closure and flights restrictions (lower Inbound roaming revenue).
- CITC disconnections continue to impact the customer base negatively, in addition to the new governmental requirement (Tawakalna application required for customers mobility).

EBITDA for the quarter decreased by 22% YoY with an EBITDA margin of 38% on account of conclusion of CITC settlement agreement in 2020. Net income reached USD 11 million during the quarter.

The operation made the full settlement of the SHL (USD 553 million paid in Q1-21, including both SHL and interest). Zain KSA have also achieved an overall decrease in Finance Cost by USD 37 million compared to Q1-20.

During the quarter, Zain KSA invested USD 19 million (4% of revenue) on CAPEX thereby integrating more than 4,500 5G sites till date.

Zain KSA and Mobily received an approval from the regulator to merge their telecoms towers into a new commercial entity and to sell that entity to a consortium of new owners, of which they themselves will be a part… This merger aims to drive efficiency and enhance coverage across the Kingdom.

Moving to slide (28), which is Zain Iraq.

As we mentioned in our last call, on 19 Dec 2020, Iraqi dinar devalued against the USD by 19% from IQD 1,190 to 1,470 vs USD.

Overall revenue continued to be impacted by COVID, curfews across the country as well as decreased economic impact, resulting in 27% YoY decrease. EBITDA for the quarter decreased by 26% and Net income for the quarter dropped by 44%, mainly due to the revenue drop from currency devaluation.

- Customer base reached highest ever levels with 16.2m customers in such a challenging environment driven by external events, with an increase of 1% YoY derived by market share gains in Arabic North, Kurdistan and Central East regions

The operator invested USD 174 million in Capex out of which USD 148 million relates to 4G license. In February 2021, Zain Iraq launched the first 4G service in Iraq with a hugely successful media campaign (highest views on every social platform, 3-8x competition) and captured 720k customers within 1 month of launch with highest speed network in Iraq and 34% of data traffic on 4G.

Zain Jordan, on slide (29) which is.

Zain Jordan remains the market leader, serving 3.6 million customers. Revenue for the quarter increased by 4% YoY, mainly due to increase in broadband and FTTH revenue on account of increased work from home requirements. Consequently, EBITDA grew by 11%, maintaining a healthy margin of 45%. Notably, net income for the quarter increased by 23%, mainly due to the top line performance.

CAPEX in Jordan amounted to USD 185 million in Q1 2021. CAPEX was mainly spent on the renewal of the 900 MHz technology neutral license amounting to USD 183 million.
Zain Jordan's focus on fintech saw Zain Cash, the country's most prominent e-wallet, increase its customer base by over 4% compared to the Q4-20 and witness a doubling of card payment transactions during the year.

Zain Sudan which is on slide (30):

With a leading customer market share of 49%, Zain Sudan was able to further improve its market position by reporting customer growth of 6% YoY, to a new record of 17.2 million, representing 36% and also the largest contributor of Zain Group's total customer base.

As mentioned earlier, On 21 February 2021, the Central Bank of Sudan revised its exchange rate policy from "fixed rate" to "flexible managed floating rate". Accordingly, the SDG devalued from 55 pounds to 375 pounds per US Dollar.

Despite the pandemic and devaluation impact on revenue, Zain Sudan reported 3% revenue growth, to reach USD 92 million, due to continuous price revamps. EBITDA increased by 13% to USD 42 million, and net income increased to reach USD 18 million compared to USD 4 million last year.

The expansion of 4G combined with data marketing initiatives, saw data revenue grow by 32%, representing 29% of total revenue.

Zain Sudan invested USD 14 million in CAPEX or 15% of its revenue.

VAT on telecom services has now increased from 35% to 40% and tax on telecom services as a percentage of gross revenue has increased from 7% to 10%, effective from 1 Jan 2021.

Finally, Zain South Sudan which is on page (32):

Starting from this call, we will be covering our operation in S.Sudan too, due to its significant growth over the years, contributing 7% of the Group's profitability during the quarter.

The operation's revenue has been growing since Q1 2019, reaching USD 30 million in Q1 2021, compared to USD 18 million in Q1, 2020 driven by prices and bundles revamp, international re-zoning, network performance improvement, and efficiency enhancement.

EBITDA for the Q1 2021 almost doubled compared to last year reaching USD 11 million, with an EBITDA margin of 37%. Net income reached USD 11 million for the quarter, compared to USD 3 million last year.

These impressive KPIs are a result of the improving socio-economic conditions of the country, allowing us to restore many sites that were offline during the conflict, combined with the launch of 4G services in Q1 2021 and ongoing expansion & improvements in the network. This also helped the customer base increase by 9% YoY, reaching to 1.1 million customers.

With that, I'll hand over to Mohammad Abdal for Q&A.

Mohammad Abdal:
Thanks, Ossama. With that, we will now move to the Q&A session. And we ask that you limit yourself to one question and one follow-up.

Ziad Itani:
Hi, while we wait for the questions, I have couple of them… first on Iraq with regards to the license renewal, was this was paid in Q1 and was it entirely paid in USD or IQD? and was it from sourced by the cash available within in Iraq? That's my first question.

Ossama Matta:
Yes, it was USD 233 million, and it was paid in full in Q1-2021 and it was sourced from the cash in Zain Iraq as well as the help from the Group to Zain Iraq. But this has also been up streamed from Iraq to the Group during this quarter Q2.

Ziad Itani:
And with regards to the 4G plans, how much Capex you would estimate for 4G over the next 3 years and how much coverage can we expect?

Ossama Matta:
We already invested on the 4G and this happened in 2020, we were planning for the 4G and that's why it was easy for us to launch the 4G services in Iraq ahead of competition with approximately 4,000 sites already providing 4G services in Iraq and approximately this year we're going to spend around UD 30 million on 4G in 2021.

Ziad Itani:
Ok thank you and in terms of smart phone penetrations can we get an idea on what's the rate in Iraq currently? How many 4G customers you have?

Ossama Matta:
More than a million customers now have 4G services.

Ziad Itani:
Okay perfect, next question basically on the Saudi market Q1 was rather disappointing given the heavy 5G Capex as well as recovery and mobility, why did we see the revenues retract sequentially? What's the main reason why competition is growing and what's the plan for that market basically especially that you know Zain is the leader when it comes to 5G deployment, as well as capturing potential market share in the post-paid segment?

Ossama Matta:
Re Saudi, when we compare it to last year we see a drop in the revenue for sure we have been saying before like our base now becomes Q4 2020 rather than comparing it with Q1 2020 now if you look at Saudi and you analyze the performance you will see that we have been suffering in the prepaid segment and Zain KSA specially in Saudi is more sensitive in this segment than the other operators most of our revenues come from prepaid and we have been losing on the prepaid segment because of the Covid 19 and the restrictions and Hajj.

We are relooking at this we are pushing more on the 5G as 5G helped us a lot during Q1, as did iPhone 12. We have seen increase in pick up on the post-paid from the 5G. What we also introduced in the market is something new like we have bundles based on speed as well you have 100 Mbps package and 200 Mbps package. This is competing very well with the FTTH we are planning to do what we have done in Riyadh across the big cities like Jeddah and Damam.

B2B is doubling when u look at the growth it is actually doing great double-digit growth is happening on a quarterly basis, we still want to crack into the Government projects not easy to do that because of the dominance of STC but we are getting some projects there I believe the focus will be on 5G on B2B consumer of course. We are relooking at our strategy in Zain KSA in terms of prepaid segments and lately also we have as a board in Saudi and as a Group we have approved to go into a digital game as an operator and we have hired McKinsey to look at certain pockets in revenues and efficiency so things will move into the right direction, but it will take some time. The other interesting thing that happened in Saudi is the tower deal I would expect this to materialize faster than what we used to say before because the regulator already approved the consortium we are in, and now it is about the commercial discussions that will happen between us and IHS.

Omar Maher:
Hi everyone, thanks for the presentation. On Sudan, would like to get a sense of what's going on there… strong growth in subscribers base in the previous years, that slowed in 2020 with the COVID onwards… currency translation, was it a blended rate that you used before? Or u already started the price adjustments? How fast should we expect these price adjustments to happen in Sudan and Iraq as well?

Ossama Matta:
Thank you for your questions, regarding the customer base we are growing healthy in Sudan and we are a bit specific in terms of acquisition of customers. It is very important for us not to be considered the dominant player in the market because this will have impact on us in terms of the services that we can provide, but we will be more looked at by the regulator when we have dominancy in the market that's why we are basically picky in terms of the acquisitions of customers and also we have a lot of CVM activities during the last year specially during the last 6 months of last year and this quarter this is in terms of the customer base.

In terms of the devaluation of the currency last year in 2020 we have been doing a lot of price ups and we have linked these price ups to the black market, we translated the revenues or the balance sheet of Zain Sudan when we consolidated at 55 SDG/USD but we linked the packages and our prices with the black market rate in 2020… so we started increasing on a quarterly basis, it was I think maximum 25% increase allowed by the regulator. This helped us when they basically floated the SDG to become at 375. Remember that they did the floating in February towards the last 10 days so if you look at January it was at 55 so the translation of the revenues for January was at 55 while the rest of February it was at an average rate and in March it was at 375 or 380 depending on the market.

The mechanism that we put in place we have already increased the prices of international roaming by 400% the voice and the data has been increased by 300% or there is a plan effective 1 April and 300% voice and 200% on data and this plan will be 100% completed between Q2 and Q3, by doing so we will basically recover most of what we have lost in terms of translation. Also, one more thing in Sudan the license terms that we have any devaluation in currency more than 5%, Zain will go automatically and increase the prices without going back to the regulator for approval this we don't have in Iraq so this has helped us a lot as well.

Omar Maher:
Are you growing in line with the market or market share gains on subscribers?

Ossama Matta:
I think we are growing, and the price increases we have seen some improvement in terms of network elements I mean congestions we are providing better services. I think it is fine we don't have an issue on the customer base or the price uplifts.

Dalal Darwish:
Thanks for the presentation and Eid Mubarak. Couple of questions here… for the Group EBITDA, when we calculate the EBITDA on opco level it doesn't add up to the total reported Group EBITDA, is there any one-off in place during the quarter?
My 2nd question is on plans for future tower deals, are you looking into any other markets?

Kamil Hilali:
As part of the new strategy and all new digital infrastructure is a new growth area, so indeed we are talking with the existing towerco player TASC to create a JV for the rest of the countries we operate in… we are in the process doing so ,I believe in the next 12 months well have some updates to announce… but this is the aim, we still believe in the towerco model, and we want to be part of it, rather than sell and lease them back.

Ossama Matta:
on the EBITDA, when we consolidate EBITDA, there are certain unknown items to the outside world, some of the operations we have such as MADA, NXN, the management fees that we charge the operations which is included in EBITDA, when we consolidate all of these, they get eliminated on Group level… and plus there are some provisions that has been reversed on Group level, that are not needed… that's why you have seen EBITDA more than the number when you add up all the operations.

Dalal Darwish:
One follow question on Zain KSA…how will you use the $553m up streamed during Q1'21?

Ossama Matta:
We have already used it on paying Group debt as well as to pay Group dividends, noting it's the first time we didn't draw down on loans to pay dividends.

Dalal Darwish:
On guidance on future dividends policy of 33 fils?

Ossama Matta:
We gave guidance, we expect to have around 3 to 5% growth on bottom line. Nevertheless, due to Zain Iraq and Sudan, we will have more clarity by end of Q2, 2021. From profitability point of view, we don't expect to earn less than last year, and I don't expect to pay dividend less than last year.

Nishit Lakotia:
Hi everyone, I have some questions:

1. Re Sudan, given the increase in prices and general economic conditions in Sudan, where do you see it going forward given the VAT and USD issues, are you confident you can sustain the growth especially the currency translation especially in USD terms since the impact will be in 2nd quarter?
2. Re South Sudan, what's driving the 300% growth in South Sudan?
3. Re the Kuwait Tax regulator issue of KD 23 million, that there will be a judgement soon, is there a provision for this?

Ossama Matta:
Re the Tax NLST case, its approximately KD 23 million, regarding a dispute since 2010 with the Kuwait tax department, when we sold the African operations, there will no impact on P&L as we made provisions already for it should we lose the case, which we are hopeful of not losing.

Iyad Borgi:
Re Zain Sudan, the plan for the full year saw it planning earlier this year in February, revamping prices just before the official devaluation, and the team started a plan to revamp prices every three months, started from April and will be reviewed in June and October 2021, that will see prices increase by up to 300% in voice and 200% on data. This will limit the impact of the purchasing power of the customer. The April price increase of about 150% resulted in an increase of revenues of 100%, this is a good indication, achieving our 2021 targets.

Regarding, South Sudan management have been very active in rolling our new services to attract customers given the roll out 4G there, noting we restored many parts of the networks that were offline and we expect the trend to continue for the year, due to the continuous price revamp and new offers introduced in the market.

Ossama Matta:
One more matter on Sudan, the black market always existed there, so to basically assist the economy, the Sudan Central Bank and IMF discussions was to float the currency and eliminate the black Market so they can provide aid and funds to Sudan. We increased prices because it's now official devaluation and it will help the organization.

Nishit Lakotia:
Follow up Question on Sudan…re cash upstream, previously you have been hedging against inflation by buying real estate, how will this change given changing black-market conditions?

Ossama Matta:
Before the company used to pay for investments and CAPEX through different means, now it is simpler and easier to do so. We invested before available extra cash in real estate, now we look at these real estate assets and decide what to do with them, especially since we might need to liquidate some of these assets to pay for further CAPEX investments in Sudan.
The upstream of cash will be subject to the new conditions of the Sudan Central bank but we believe it should be easier with the new floating rules. We don't envisage we will need to upstream cash from Sudan due to investment required in 4G and expanding the network.

Abdullah:
Good afternoon everyone and Eid Mubarak… I would like to ask you about the prepaid segment of the Saudi market. The prepaid base contribution increased from 38% in Q3 2020 to 64% in Q1 2021… is it some activity the company took or forced migration of the existing customers?

Iyad Borgi:
This is reallocation of the base; we still have hybrid packages which were under the postpaid and now migrated to the prepaid because the revenue was under the prepaid.

Ossama Matta:
Hybrid is in between, you can't know if its Postpaid or a prepaid.

Abdulla:
Thank you, Do you consider them as a postpaid users with a control cap?

Iyad Borgi: yes, that's correct.

Ziad Itani:
No more questions so I will hand it back to Mohammad Abdal for any closing remarks.

Mohammad Abdal
Thank you Ziad, please refer to the Investor Relations website for additional updates and feel free to contact the IR team at IR@zain.com for further information. We look forward to your future participation in our Q2 2021 update.

Wishing you all a Happy Eid …Thank you for joining the call… Stay Safe.
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