Saudi Telecom Sector – Bracing regulatory headwinds

- **Regulatory changes will impact sector earnings**
- **Market competition to further intensify with lower interconnection rates**
- **Reinitiate coverage of Mobily with ‘Sell’ rating, maintain ‘Neutral’ on STC**

Regulatory headwinds impacting sector’s profitability

Saudi telecom sector is witnessing headwinds from several regulatory changes such as fingerprint verification, reduction in interconnect charges, GCC’s roaming rate cut and probable fee on internet services. In addition, the current economic condition remains challenging because of low oil price regime. The initiatives related to biometric user verification and Saudisation is expected to hamper growth of telcos in the kingdom. The decline in Mobile termination rates is expected to negatively on STC, being the largest operator, but should be positive on smaller players like Zain and Mobily. In addition, Saudi telcos, particularly Zain and Mobily, are actively working on selling off their tower infrastructure to improve their operational efficiency and strengthening their balance sheet. Further, Mobily, after more than 2 years of tumultuous past, is now done with accounting restatement and litigation and is focussing on improving financial performance. We believe this is likely to reinvigorate competition in the market with due support from lower interconnect charges.

Reinitiate on Mobily with a Sell Rating; STC – Neutral with cushion on downside

With this report, we restart our coverage on **Mobily**, with a TP of SAR 24/sh and a **“Sell”** rating. We believe that the recovery in profitability of the telco will be slow and that the stock has overshot its fundamentals in the recent rally. We maintain our **“Neutral”** on **STC** with a TP of SAR 68/sh, as we believe that the full impact from regulatory headwinds, like further cut in interconnect costs, will be felt in the coming quarters and that the telco’s earnings will be broadly flat (2016-19E). However, as STC has committed to pay minimum SAR 1/sh in quarterly dividends until FY18, the company has a cushion on the downside and will be the favoured telco operator by the QFIs and domestic institutions/asset managers and also retail.

Finger print verification to limit near term revenue growth

As part of a security initiative, Saudi’s telecom regulator Communication and Information Technology Commission (CITC) has directed kingdom’s telecom operators to register the finger prints of their subscribers. The new regulation requires the customers to provide fingerprints on special device which will be linked to National Information Centre to ensure the identities of SIM owners. The first phase of implementation started in January 2016 and the telcos were given three months' time to verify c. 53mn customers. As per Zain KSA's 1Q16 conference call, CITC extended the deadline for prepaid and postpaid subscribers to June 07, and July 17, 2016 respectively. We believe that it may lead to suspension of unverified customers after the deadline and will also impact the telcos' revenue from 2H16 onwards. In addition, the finger print verification comes with an additional cost for the telcos which includes capex on biometric machines and operating expenses on additional staff for awareness about the initiative, which will further impact the profitability.

Tower sale to reduce leverage

Saudi telcos, particularly Zain KSA and Mobily, are planning to sell and then lease back the towers for operational use. Mobily and Zain KSA are already in talks with potential buyers. The main reasons behind the move is to improve their operational efficiency by focussing on their core business and to strengthen their balance sheet by reducing their debt and utilise the case for capex.

As per our analysis of recent tower deals, one tower may fetch c. USD 180,000, which translates to total deal size of USD 1.8bn and USD 1.1bn for Mobily and Zain KSA's existing tower infrastructure.

The tower sale will lead to lower depreciation charge which will be compensated by incremental lease expense. In addition, the proceeds from the sale may be utilised for repayment of existing debt resulting in lower finance cost. We believe that the successful tower sale will be a positive trigger for both Mobily and Zain KSA as both telcos have high net Debt to EBITDA ratios of 4.7x and 5.9x in FY15. Mobily and Zain hold portfolio of 10,000 and 7,000 towers respectively and successful tower sale at a comparable price will be a positive catalysts for the telcos and will potentially lead drive a rerating.

Exhibit 1: Major Telecom Tower Deals

Location	Seller	Buyer	Year	No. Of towers	Deal size (USD mn)	Value per tower (USD)
India	Airtel	GTL	2010	17,500	1,800	102,857
Germany	KPN	American Tower Corp	2012	2,000	501	250,500
US	Global Tower Partners	American Tower Corp	2013	15,700	4,800	305,732
Brazil	TIM	American Tower Corp	2014	6,480	1,200	185,185
Nigeria	Airtel	American Tower Corp	2014	4,800	1,050	218,750
Indonesia	PT Telkom	Tower Bersama	2014	4,000	904	226,000
Africa	Airtel	Multiple	2015	8,300	1,700	204,819
India	Rcom	NA	2016	45,000	3,500	77,778
India	Idea cellular	NA	2016	11,000	1,200	109,091
Tanzania	Airtel	Na	2016	1,350	179	132,593
		Average				181,331

Source: Media Publications, COMPANY X Research

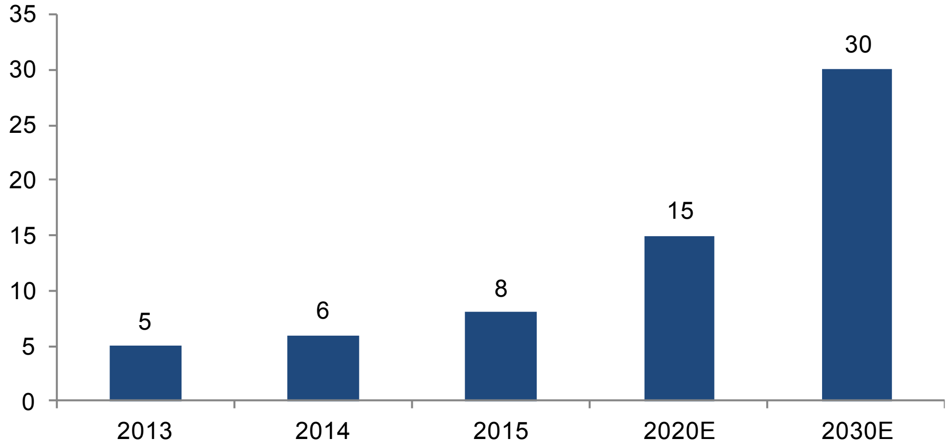
GCC roaming rate cut to have marginal impact on the top line

There has been a 40% cut in roaming rates for GCC based mobile users travelling within the region, with effect from 1st April 2016. The rate cut will affect roaming charges for calls, data tariffs, and text messages within the six-nation bloc. As per GCC's Assistant General Secretary, the consumers would save USD 1.14bn in FY16, led by lower roaming rates. We believe that the impact on the telco's bottom-line will not be significant because of increased elasticity of roaming usage and lower interconnection charges.

Increase in Umrah visa to favourably impact the sector

The Kingdom of Saudi Arabia plans to increase religious tourism in the country. The number of Umrah visas issued in FY14 and FY15 were 6mn and 8mn respectively which is expected to go up to 15mn by FY20. The kingdom aims to increase the pilgrimage visas to 30mn by FY30 end as a part of its Saudi Vision 2030, which was launched on April 25, 2016. The growth in country's mobile segment has been stagnant with flat subscriber numbers over the past five years. The increase in number of incoming tourists would potentially increase the demand for telecommunication services, driving the growth for the telcos in the country.

Exhibit 2: Umrah Visa numbers (mn)



Source: Saudi Vision 2030, COMPANY X Research

Lower interconnection charges bode well for Mobily and Zain KSA

The CITC reduced the wholesale prices of mobile and fixed line interconnections in March 2016. The mobile interconnection charges were reduced by 33% to SAR 0.10/min from SAR 0.25/min and fixed line charges were reduced by 36% to SAR 0.045 from SAR 0.07. This is the second rate cut during the past thirteen months with the last rate cut implemented from April 26, 2015. The reduction in termination rates is expected to lower the price paid by the users and further intensify the competition in the already saturated market. The lower interconnect charges will dilute the competitive advantage for STC customers for on-net calls and may lead to higher churn rate. At the same time, we expect Mobily and Zain KSA to benefit due to relatively smaller customer base. This was also evident from YoY increase in gross margin in 1Q16 for Mobily and Zain KSA, because of termination rate cut in February 2015. However, STC's 1Q16 gross margin declined to 56.6% from 60.5% YoY. With the recent cut in interconnect charges in March 2015, we believe the trend will continue and further help the smaller players.

MVNO having only a minimal impact on competition currently

Saudi's telecom market is highly competitive with three full service mobile operators and two Mobile virtual Network Operators (MVNOs) currently. Like other GCC states, mobile penetration is high at 168%[1] (FY15) in the kingdom. The two existing MVNOs, Virgin Saudi and Lebara, which were launched in FY14, have been able to capture only c. 2% subscriber market share so far (Zain Group presentation). The CITC accepted interests for third MVNO license in the kingdom on the network of Zain KSA. Although

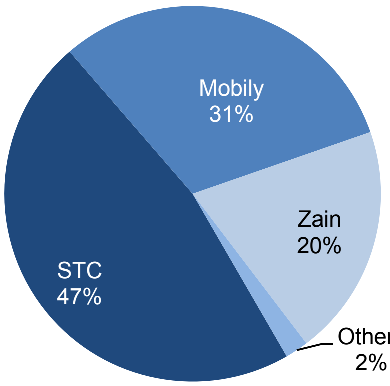
[1] Business Monitor

launch of the third MVNO will add to the competition in the already saturated Saudi mobile market, we believe that impact will not be significant.

STC continues to lead the market

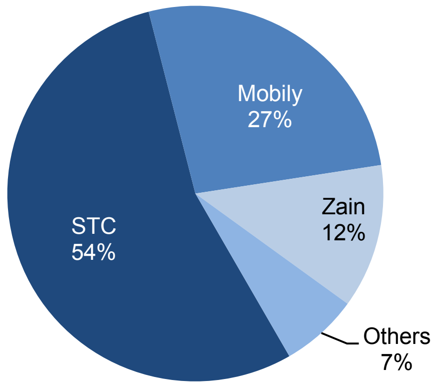
Saudi Telecom Company remains the largest telco in the kingdom with a strong revenue share of 58% and a subscriber market share of 47%. However, being the largest means that the telco is at the most risk to lose market share from increasing competition from other players. Mobily lost ground to competition in FY15 after reporting a market share of 31% compared to 38% in FY14. Despite the loss in market share, Mobily remained the second largest operator in Saudi while Zain KSA gained market share from Mobily in FY15, increasing to 20% in FY15 from 17% YoY.

Exhibit 3: KSA – Mobile subscriber market share



Source: Zain Presentation FY15, COMPANY X Research

Exhibit 4: KSA – revenue market share



Source: CITC, Company Data, COMPANY X Research

Intense competition in KSA telecom; Zain aggressive in prepaid segment

Price comparison and analysis of Saudi telco's mobile plans reveals that in the post-paid segment, Mobily offers the most competitive pricing in the country with maximum benefits in terms of free minutes, SMS, data etc. In SAR 250, Mobily offers 15 GB data along with 5,000 on-net minutes and 5,000 sms' compared to 600 min and 2 GB data by Zain and unlimited minutes and 2 GB data offered by STC in SAR 200. Also, Mobily offers SAR 800 cash back on smart devices irrespective of the duration of contract. In the prepaid segment, Zain offers most competitive prices with more number of voice minutes and data at similar or lower prices. STC and Mobily offers less talktime and no SMS at similar price levels in their pre-paid packages compared to Zain KSA.

Exhibit 5: Prepaid pricing comparison for Saudi telcos

Operator	Charges (SAR)	Talktime (on-net min)	Data (GB)	SMS	Validity
STC	55	600	2		1 Month
	110	500	5		1 Month
Mobily	65	500	2		1 Month
	120	1000	6		1 Month
Zain	45	3000	2	1000	7 days
	140	3000	5	1000	1 Month

Source: Company Data, COMPANY X Research, data as at 04th May 2016

Risk of additional burden expected on telco's in the form of Internet fees

In another regulatory move, CITC is considering imposing a new fee on telcos to be applied on their revenues contributed from internet services. The new internet fees would be charged on the telecom operators and the charges are not expected to be passed on to the consumers. We await further clarity on the type of services covered and the detail of fees to assess the impact; remains a potential negative trigger for the sector.

Telecom

Saudi Telecom Company

Price Data (SAR)	
Current Price	64.70
Target Price	68.00
52 wk High/Low	73.25/52.75

Ratings	
Short-term	Neutral
Long-term	Neutral
Risk Profile	Normal

Market Data	
Sector	Telecom
Market Cap	USD 34.5bn
Primary Market	Saudi Arabia
Other Exchg	
Reuters	7010.SE
Bloomberg	STCAB
Free Float	16%

Valuation Ratio	2015A	2016E
P/E x	14.7	13.1
P/BV x	2.3	2.1
EV/EBITDA x	7.2	5.6
Div Yld %	5.8	6.2

Trading Data	
Daily Vol (6M Avg)	0.7
Daily T/o (6M Avg USD)	12.4
Issued Shares	2,000.0

All in millions

Performance (%)	1m	3m	12m
Absolute	5.1	3.9	-7.4
Relative	-3.3	-8.1	24.6

Preferred telco with dividend cushion

- **Considerable negative impact from regulatory headwinds**
- **No near term trigger for the stock; assured dividend yield of 6.2% at current levels**
- **Preferred stock within Saudi telecom sector; Reiterate 'Neutral' rating**

Regulatory changes and increasing competition to impact performance

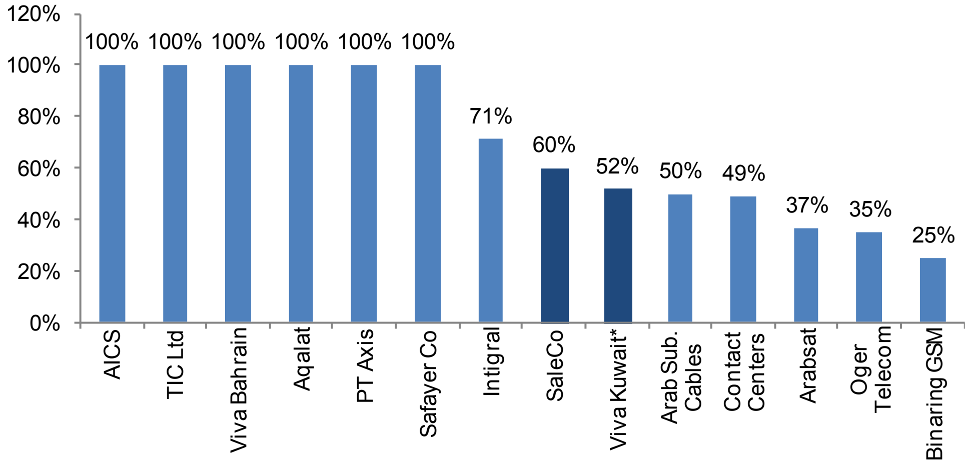
As discussed earlier, Saudi telecom market is witnessing several regulatory changes, which will lead to higher competitive intensity and margin pressure in the industry. Moreover, STC, being the largest telecom player in the KSA and leader in both mobile and fixed line services in Saudi Arabia, will have the most impact from these changes. The impact from recent cut in the mobile interconnection charges, which were reduced by 33% to SAR 0.10/min from SAR 0.25/min and fixed line charges being reduced by 36% to SAR 0.045 from SAR 0.07 will be felt in the subsequent quarters, impacting the telco's margin. In addition, Mobily which lost c. 7% market share in FY15 to Zain and MVNOs, is now making a comeback and can be a formidable challenger to STC in both retail and enterprise segment. STC's mobile pricing and data plans currently are costlier compared to Zain and Mobily and increase in competition will likely impact the telco's market share and ARPUs.

Expect growth led by increase in stakes in subsidiaries

STC acquired additional 25.8% share in its subsidiary Viva Kuwait in February 2016, resulting in its stake of 51.8% from 26% earlier. The stake was acquired through a voluntary tender offer which closed on 31st January 2016 for SAR 1.59bn. Higher stake would mean lower minority interest (MI) for Viva earnings in STC's consolidated financials. We expect MI to decline going forward, our estimates suggest an incremental earnings of SAR 120.5mn from higher stake in Viva.

STC owns 60% stake in Sale Advanced Co. Ltd. (SaleCo) and offered to acquire remaining 40% stake in its Riyadh based subsidiary for SAR 400mn (USD 106.7mn) in December 2015. The acquisition will be financed by company's own resources. We believe STC is using its strong cash position to increase stake in its performing subsidies in order to grow its bottom line as the domestic market remains saturated.

Exhibit 6: STC Ownership



*Note: STC increased stake in Viva Kuwait in February 2016

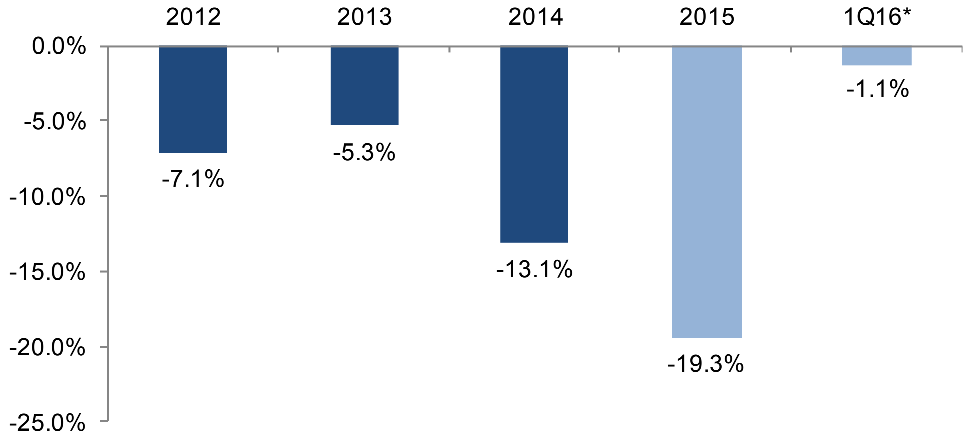
Source: Company Data, COMPANY X Research

Forex impact continue to dictate equity accounted investments' contribution

In FY15, STC reported 45.2% YoY increase in losses accounted under equity method to SAR 379mn, which majorly consists of 25% stake in Binariang GSM Holding and 35% stake in Oger telecom. Binariang's 100% subsidy Maxis communications reported FY15 earnings of RM 1.7bn, up 1.3% YoY. Oger's subsidiary Turk Telekom reported FY15 earnings at TL 907.4mn, down 54.8% from TL 2bn earnings YoY. We believe STCs increased losses under equity method were contributed by forex losses on USD denominated debt led by depreciation of Turkish Lira against USD.

The telco's equity accounted units reported SAR 28mn of profit in 1Q16 compared to SAR 145mn of loss YoY. The positive contribution from equity accounted units was primarily due to lower forex losses from STC's associate Oger Telecom. It was largely in line with our expectation as we estimated a profit of SAR 50mn from STC's equity accounted units.

Exhibit 7: Turkish Lira vs. USD



Note: 1Q16 currency depreciation compared to 4Q16 end
Source: Company Data, Bloomberg, COMPANY X Research

1Q16 earnings declined YoY

STC's 1Q16 net earnings declined 5% to SAR 2.4bn, compared to 1Q15 earnings of SAR 2.5bn. The company's gross margin declined to 56.6% in 1Q16, compared to 60.5% YoY. We estimate that the decline in gross margin was driven by lower mobile and fixed interconnection rates implemented in April 2015. STC, being market leader in both mobile and fixed, its interconnection revenues would have declined more compared to drop in interconnection costs, which led to lower gross margins. STC's EBITDA also decreased 3.8% YoY to SAR 5.0bn in 1Q16. The company's revenues registered a moderate growth of 2.3% YoY to SAR 12.8bn in 1Q16 driven by YoY growth of 2.9% and 3.7% in domestic and international operations respectively. STC's EBITDA and net margins declined to 39% and 18.6% in 1Q16 compared to 41.4% and 20.1% YoY.

Exhibit 8: 1Q16 Snapshot (SAR bn)

	1Q16	4Q15	1Q15	YoY	QoQ
Revenue	12.8	13.2	12.5	2.3%	-3.7%
Gross Profit	7.2	8.0	7.5	-4.3%	-9.9%
Gross Margin	*56.6%*	*60.5%*	*60.5%*		
Operating profit	3.0	2.6	3.4	-11.1%	17.6%
Operating Margin	*23.5%*	*19.3%*	*27.1%*		
Net Profit	2.4	2.0	2.5	-5.1%	21.8%
Net Margin	*19%*	*15%*	*20%*		

Source: Company Data, COMPANY X Research

Reiterate Neutral rating with a TP of SAR 68.0/sh, offering an upside of 5%

We reiterate our **'Neutral'** recommendation with one-year blended target price of SAR 68.0/sh, offering an upside of 5.1% from current levels. The current share price implies a P/E ratio of 13.1x on our FY16 EPS estimate of SAR 4.92/sh. Going forward, we expect STC's earnings to grow at a CAGR of 3.8% between FY15-18 period. The telco announced a dividend of SAR 1/sh for 1Q16 amounting to a total dividend payment of SAR 2bn, in line with the telco's three year dividend policy announced on 11th November 2015. We expect the telco to maintain the quarterly dividend levels with FY16 dividend estimate of SAR 4/sh, translating to a dividend yield of 6.2% at current levels. However, the strong cash and short term deposits of SAR 23.4bn at end of 1Q16, signifies the upside risk on dividend.

However, between the three telecom operators in Saudi Arabia, STC remains a safer bet, considering the assurance on dividends. Although earnings of the telco will be muted, STC will be preferred by both QFIs and retail for its track record of paying quarterly dividends. In addition, STC, being one of the large caps in Tadawul, should benefit from inflows on MSCI upgrade of Saudi Arabia to emerging index, likely in 2017 or 2018.

Exhibit 9: STC – Blended Valuation

(price in SAR)	Price	Weightage
DCF	69.1	50.0%
Price/ Earnings	67.7	50.0%
STC – Target price, SAR	**68.0**	
Current Price	64.7	
% Upside	5.1%	

Source: Company Data, COMPANY X Research

Telecom

Price Data (SAR)	
Current Price	29.20
Target Price	24.00
52 wk High/Low	37.80/18.85

Ratings	
Short-term	Neutral
Long-term	Sell
Risk Profile	High

Market Data	
Sector	Telecom
Market Cap	USD 6.0bn
Primary Market	Saudi Arabia
Other Exchg	
Reuters	7020.SE
Bloomberg	EECAB
Free Float	61%

Valuation Ratio	2015A	2016E
P/E x	-20.7	52.4
P/BV x	1.5	1.4
EV/EBITDA x	11.8	7.6
Div Yld %	0.0	0.0

Trading Data	
Daily Vol (6M Avg)	1.7
Daily T/o (6M Avg USD)	12.5
Issued Shares	770.0

All in millions

Performance (%)	1m	3m	12m
Absolute	1.4	23.7	-20.6
Relative	-6.9	11.7	11.4

Etihad Etisalat

Earnings to recover at a slower pace than market expectations

- Current valuations ahead of fundamentals
- Earnings recovery to be slow and gradual
- Reinitiate with a 'Sell' rating; TP at SAR 24/sh

Re-initiate with 'Sell' rating; TP at SAR 24/sh

We reinitiate our coverage on Mobily with a 'Sell' recommendation and a one-year DFC target price of SAR 24/sh, implying a downside of 19.1% from current levels. We have not valued the telco on PE basis as the company's near term earnings estimates are not the true reflective of its earnings potential. However, the market remains competitive with limited growth opportunity and the recent regulatory changes/requirements related to finger print verification and GCC roaming rate cut will impact the telco, while lower interconnect costs should impact the revenues but Mobily should benefit at the net level, being a smaller operator compared to STC.

We expect a modest revenue growth of 2.6% CAGR during FY15-18 period for Mobily, given the competitive and regulatory challenges in the Kingdom. The stock is trading at a P/E multiple of 32.8x on our FY17 EPS of SAR 0.9. We do not expect any dividend payment over the next few years considering the low profitability, difficulty in complying with its debt covenant and capex requirements. However, sale of telecom towers may lead to one time significant cash inflows and can be a potential upside risk to our valuation estimate.

Exhibit 10: Mobily – DCF Valuation

DCF Valuation	
Cost of Capital	9.2%
Exit Multiple- EBITDA	4.5
Enterprise Value (SAR mn)	**30,187**
Shares Outstanding (mn)	770
Value per share (SAR)	**24**
Current Price	29.2
Upside/ (Downside) %	-19.1%

Source: Company Data, COMPANY X Research

Current valuations not backed by expected earnings growth

Mobily's stock has rallied ahead of fundamentals and we believe that the current valuations is not supported by the telco's earning potential and future growth expectations. Prior to the restatement and provisioning, Mobily traded at P/E levels of 10-11x and it should be trading at a discount to the GCC peer group, which is at 12.5x, due to challenging competitive and regulatory environment. Even at a GCC average of 12.5x, the current share price implied net income of SAR 1.8bn. However, the telco's below EBITDA cost items of depreciation, amortisation and finance charge are more stickier in nature and amount to SAR 4.3bn based on the past three quarter average. As a result, the implied EBITDA will be SAR 6.1bn which translates to an EBITDA margin of 40.7% at revenue base of SAR 14.9bn. To improve EBITDA margin from 32.4% in 1Q16 to 40.7%, above EBITDA costs of c. SAR 9.3bn need to cut by another 13% or SAR 1.24bn. According to our analysis, the implied earnings growth looks very optimistic and we believe that the cost reduction exercise will be more gradual. We have not accounted for tower sale in our analysis, which will reduce depreciation and finance cost but should result in a recurring lease rental expense.

Exhibit 11: Implied Cost Savings

GCC average P/E multiple	x	12.5
Current share price	SAR/sh	29.7
Implied EPS	SAR/sh	2.376
Implied Net Income	SAR mn	1,830
Annualised below EBITDA Items – based on the past three quarter average*	SAR mn	4,246
Implied EBITDA	SAR mn	6,076
Annualised revenue – based on past three quarter average and 5% growth	SAR mn	14,914
Implied EBITDA Margin	%	40.7%
1Q16 EBITDA margin	%	32.4%
Further annual Cost saving required	SAR mn	1,239
Annualised cost base till EBITDA – based on 1Q16	SAR mn	9,298
% cost to be reduced to justify current valuation	**%**	**13.3%**

Note: We have assumed that 'other income' and tax expense will offset each other
Source: Company Data, COMPANY X Research

Expect growth from FY16 led by improved operating efficiency

We expect Mobily's FY16 earnings of SAR 432.6mn compared to net loss of SAR 1.1bn in FY15 led by higher provisioning and impact from restructuring. Our estimates suggest the telco's revenues and gross profit to remain flat in FY16 to SAR 14.5bn and SAR 8bn respectively, with a gross margin of 55%, in line with FY15 margins. The telco mainly targets fixing inefficiencies and improvement of processes to increase its margins.

Exhibit 12: Mobily – Key Financial Forecasts

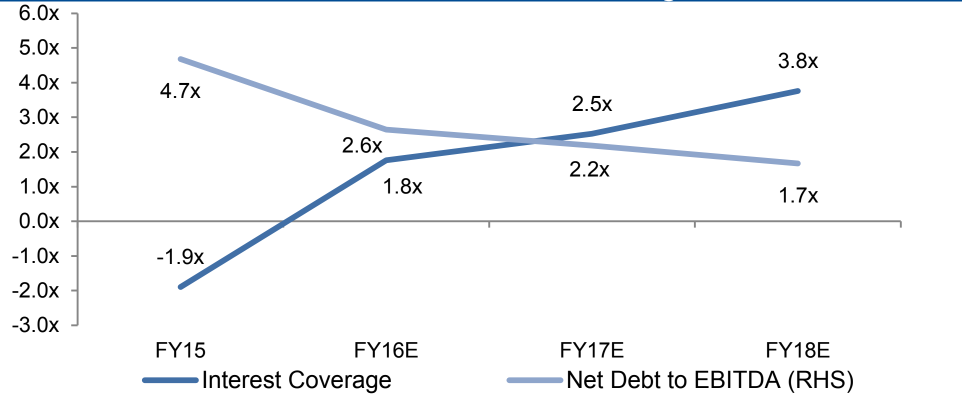
	FY15	FY16E	FY17E	FY18E	CAGR
Revenue	14.4	14.5	14.9	15.6	2.6%
Gross Profit	8.0	8.0	8.3	8.7	3.1%
Gross Margin	*55%*	*55%*	*56%*	*56%*	
EBITDA	2.9	4.5	4.8	5.2	21.1%
EBITDA margin	*20%*	*31%*	*32%*	*33%*	
Net Profit	(1.09)	0.43	0.68	1.01	NM
Net margin	*-7.6%*	*3.0%*	*4.6%*	*6.5%*	

Source: Company Data, COMPANY X Research

Balance sheet to improve gradually with stable operating performance

Mobily's net debt to EBITDA was 4.7x in FY15 due to provisioning and restatements and we expect it to improve to 2.6x and 2.2x in FY16 and FY17 respectively. According to our estimates, Mobily will generate free cash flow of SAR 521mn and SAR 1.4bn in FY16 and FY17 respectively. As a result, Mobily's gearing (net debt to equity) is expected to decrease to 0.63x by FY17 from 0.89x at the end of FY15. We have not accounted for cash flow from tower sale in our estimates. If the tower sale is executed, it may lead to significant decline in leverage and will further improve the balance sheet strength. In addition, we expect the telco's interest coverage ratio to improve to 1.8x and 2.5x in FY16 and FY17.

Exhibit 13: Net debt to EBITDA and Interest Coverage Ratio



Source: Company Data, COMPANY X Research

Cost optimisation initiatives led to improved 1Q16 earnings

Mobily reported 1Q16 earnings of SAR 16.6mn compared to a net loss of SAR 44.5mn in 1Q15 and SAR 10.5mn profit in 4Q15. The company attributed the improved performance to its cost optimisation initiative leading to a decline in costs. However, the telco's revenues declined 6% YoY to SAR 3.4bn primarily due to lower interconnection revenues, handset sales and additional pressure on sales from implementation of finger print verification. Mobily's gross profit improved by 1.6% YoY to SAR 1.9mn despite decline in revenue as lower termination rates from April 2015 benefitted the company. Also lower handset sales (which are generally low margin) may have also pushed gross margin higher in 1Q16. The telco reported EBITDA of SAR 1.1bn, up 20% YoY but largely flat from 4Q15. 1Q16 Snapshot (SAR mn)

	1Q16	4Q15	1Q15	YoY	QoQ
Revenue	3,440	3,527	3,643	-5.60%	-2.50%
Gross Profit	1,925	1,952	1,901	1.30%	-1.40%
Gross Margin	*56.00%*	*55.30%*	*52.20%*		
Operating profit	139	133	50	178.10%	4.40%
Operating Margin	*4.00%*	*3.80%*	*1.40%*		
Net Profit	17	11	-45	137.30%	57.50%
Net Margin	*0.50%*	*0.30%*	*-1.20%*		

Source: Company Data, COMPANY X Research

Tower sale will be a positive trigger for the stock

Mobily is considering to sell its 10,000 towers in Saudi to improve its operational efficiency and strengthen its balance sheet by repaying the existing debt from the cash flow generated from tower sale. Based on previous tower transactions, we believe the price per tower to be c. USD 180,000, which will yield USD 1.8bn (SAR 6.8bn) in cash flow for the company. Mobily can use the funds to repay its debt and fund future capex, which will be positive. However, there is will cash outflow from lease rentals on a regular basis while earnings may also benefit from lower depreciation.

Zain KSA arbitration for SAR 2.2bn in receivables

Mobily filed an arbitration case against Zain KSA in November 2014 in relation to receivables of SAR 2.2bn from Zain KSA arising from the service agreement signed on 6th May 2008 between the two telcos. The agreement covered provision of services including national roaming, site sharing, transmission links and international traffic. By FY15 end, Mobily has provisioned SAR 2.0bn of the SAR 2.2bn receivables as doubtful debt (provision of SAR 1.2bn in FY14 and SAR 800mn in FY15). Accordingly, there is very limited risk (maximum SAR 200mn) of further downside on earnings but upside potential exists if they manage to win even a part of their claim. The case is expected to be resolved before end of FY16.

Saudi Telecom Company Financials

Income Statement (Consolidated)

Year ending 31 Dec (SAR mn)	2015A	2016E	2017E
Revenue	50,837	53,315	54,458
Cost of Goods Sold	(20,493)	(22,925)	(23,390)
Gross Profit	**30,343**	**30,389**	**31,069**
Selling, General and Admin.	(10,973)	(10,995)	(11,200)
EBITDA	**19,370**	**19,395**	**19,868**
Operating Profit	11,936	11,541	11,677
Other Income	(756)	(411)	(360)
Net Interest Income	(238)	(200)	(165)
Tax	(697)	(748)	(792)
Minority Interest	(531)	(410)	(368)
Net Profit	9,335	9,846	10,152

Cash Flow Statement (Consolidated)

Year ending 31 Dec (SAR mn)	2015A	2016E	2017E
Net profit before minority	10,562	11,005	11,312
Depreciation	7,434	7,853	8,191
Other Adjustments	2,933	661	596
Working Capital Changes	(112)	1,548	(1,144)
Cashflow from Operations	**20,818**	**21,067**	**18,956**
Capital Expenditure	(10,348)	(6,704)	(6,463)
Other Investing Activities	(1,491)	(1,204)	(217)
Cashflow from Investing	**(11,840)**	**(7,908)**	**(6,679)**
Debt Raised/Repaid	(1,762)	(2,017)	(282)
Dividend	(8,019)	(8,000)	(8,000)
Other Financing Activities	(160)	(2,192)	(165)
Cashflow from Financing	**(9,941)**	**(12,209)**	**(8,448)**
Net Chg in Cash	(963)	950	3,829

Note: The above statements may not match the published cash flow statements due to adjustments made by us.

Balance Sheet (Consolidated)

Year ending 31 Dec (SAR mn)	2015A	2016E	2017E
Cash & Short Term Deposits	21.30	23.93	28.50
Other Current Assets	16.72	17.94	17.66
Investments	13.39	13.14	13.30
Net Fixed Assets	40.48	40.25	39.47
Net Intangible Assets	4,783	3,866	2,917
Other Non-Current Assets	1,013	1,033	1,043
Total Assets	**97.71**	**100.1**	**102.9**
Current Liabilities	23.86	26.96	27.08
Total Debt	5,665	3,648	3,365
Other Liabilities	8,061	8,006	8,391
Total Liabilities	35.66	37.87	38.08
Minority Interest	1,421	(161)	207
Share Capital	20.00	20.00	20.00
Reserves & Surplus	40.62	42.47	44.62
Shareholders Funds	60.62	62.47	64.62
Total Equity & Liabilities	97.71	100.1	102.9

Key Ratios (Consolidated)

Year ending 31 Dec (SAR mn)	2015A	2016E	2017E
EPS	4.67	4.92	5.08
EPS Growth (%)	(14.8)	5.5	3.1
Gross Margin (%)	61.4	59.7	57.0
EBITDA Margin (%)	38.1	36.4	36.5
EBITDA Growth (%)	1.6	0.1	2.4
Net Margin (%)	19.4	19.2	19.3
ROAE (%)	15.4	16.0	16.0
ROAA (%)	10.5	10.4	10.4
Debt/Equity (%)	9.1	5.8	5.2
Valuation Ratios			
PER (x)	14.7	13.1	12.7
PBV (x)	2.3	2.1	2.0
Dividend Yield (%)	5.8	6.2	6.6
EV/EBITDA (x)	7.2	5.6	5.3

Source: Company, XXX Research, Bloomberg

Etihad Etisalat Financials

Income Statement (Consolidated)

Year ending 31 Dec (SAR mn)	2015A	2016E	2017E
Revenue	14,424	14,458	14,907
Cost of Goods Sold	(6,466)	(6,506)	(6,633)
Gross Profit	**7,958**	**7,952**	**8,273**
Selling, General and Admin.	(5,017)	(3,411)	(3,430)
EBITDA	**2,941**	**4,541**	**4,843**
Operating Profit	(684)	872	1,092
Other Income	121	122	122
Net Interest Income	(361)	(496)	(432)
Tax	(169)	(65)	(100)
Minority Interest	0	0	0
Net Profit	**(1,093)**	**433**	**682**

Cash Flow Statement (Consolidated)

Year ending 31 Dec (SAR mn)	2015A	2016E	2017E
Net profit before tax	(1,093)	433	682
Depreciation	3,625	3,669	3,751
Other Adjustments	1,140	50	22
Working Capital Changes	916	(992)	(449)
Cashflow from Operations	**4,958**	**3,225**	**4,106**
Capital Expenditure	(3,515)	(2,703)	(2,681)
Other Investing Activities	(180)	1,250	0
Cashflow from Investing	**(3,695)**	**(1,453)**	**(2,681)**
Debt Raised/Repaid	(2,730)	(748)	(468)
Dividend	0	0	0
Other Financing Activities	0	0	0
Cashflow from Financing	**(2,730)**	**(748)**	**(468)**
Net Chg in Cash	(1,467)	1,023	957

Note: The above statements may not match the published cash flow statements due to adjustments made by us.

Balance Sheet (Consolidated)

Year ending 31 Dec (SAR mn)	2015A	2016E	2017E
Cash & Short Term Deposits	498	1,520	2,477
Other Current Assets	7,901	6,650	6,954
Investments	19	19	19
Net Fixed Assets	24,46	24,09	23,62
Net Intangible Assets	9,512	8,914	8,317
Other Non-Current Assets	0	0	0
Total Assets	**42,37**	**41,18**	**41,37**
Current Liabilities	18,15	16,10	15,61
Total Debt	8,426	8,847	8,847
Other Liabilities	(8,426	(8,847	(8,847
Total Liabilities	26,81	25,19	24,69
Minority Interest	0	0	0
Share Capital	7,700	7,700	7,700
Reserves & Surplus	7,859	8,292	8,974
Shareholders Funds	15,56	15,99	16,67
Total Equity & Liabilities	**42,37**	**41,18**	**41,37**

Key Ratios (Consolidated)

Year ending 31 Dec (SAR mn)	2015A	2016E	2017E
EPS	(1.42)	0.56	0.89
EPS Growth (%)	(27.7)	(139.6	57.6
Gross Margin (%)	55.2	55.0	55.5
EBITDA Margin (%)	20.4	31.4	32.5
EBITDA Growth (%)	30.9	54.4	6.7
Net Margin (%)	(7.6)	3.0	4.6
ROAE (%)	(6.8)	2.7	4.2
ROAA (%)	(2.5)	1.0	1.7
Debt/Equity (%)	91.7	84.6	78.3
Valuation Ratios			
PER (x)	(20.7)	52.4	33.2
PBV (x)	1.5	1.4	1.4
Dividend Yield (%)	0.0	0.0	0.0
EV/EBITDA (x)	11.8	7.6	7.2

Source: Company, XXX Research, Bloomberg