

Q2, 2021 Earnings Call Transcript

Call Date	4 th August, 2021
stc's Attendees	Mr. Ameen Al Shiddi – stc group CFO Mr. Ali Alharbi – Corporate Finance, VP Mr. Turki Alashaikh – Investor Relations, GM

Turki AL Ashaikh (IR General Manager):

Thank you everyone for joining stc's Q2 earning call. Today, we will have Mr. Ameen Al Shiddi – stc group CFO – along with Mr. Ali Al Harbi the Corporate Finance Vice President.

We will start with a 5-10 minutes presentation followed by Q&A session, thank you.

Presentation (Mr. Ameen Al Shiddi – stc group CFO):

Welcome to stc's Q2 2021 financial performance conference call. I hope that everyone is safe and in a good health!

With the continues support from the Kingdom to successfully increase Covid-19 vaccinations across the country, lifting travel restrictions, and returning to normal life, stc achieved strong financial results during the second quarter as it continues to carry out its digitization journey which is compatible with its "dare" strategy **2.0**.

According to the global magazine "Forbes", stc was ranked first as the strongest telecommunications company in the MENA region. In addition, stc Group announced the approval from the Capital Market Authority for solutions by stc to float **24 million shares** for IPO, representing **20%** of the company's shares. In addition, stc succeeded in providing the largest advanced 5G network in the Middle Eastern region covering most regions of the Kingdom, and those achievements are the result of a continuous effort in developing the network's infrastructure and systems.

6 Month Overview:

- During the first half of 2021, stc launched the Advanced Technology and Cybersecurity Company; a new company dedicated to providing advanced cybersecurity services and solutions in the business sector. The launch comes to keep abreast of the growing demand for digital services in parallel with stc's DARE strategy.
- In addition, stc was ranked as the most valuable brand amongst telecommunications companies in the region reaching **USD 9.2 Billion** according to Brand Finance.
- stc has inaugurated the digital operations control center, which is considered the largest integrated operating center in the region with an area of more than **42,000** square meters that can accommodate about **2,300** employees. The center will enhance Saudi Arabia's position as a leading regional business center, and it will lay the foundation for the company to become a regional center offering a system of digital services in the Middle East and North Africa. This would help to achieve the objectives of the second phase of stc's strategy "DARE", in order to enable digital transformation in various fields, benefit from the Kingdom's strategic location at the crossroads of three continents.
- As an extension of the swift successes accomplished by stc in transforming stc pay into a digital bank after the approval from the Council of Ministers, becoming one of the first digital banks in the Kingdom of Saudi Arabia. This reflects the company's commitment to its "Dare 2.0" strategy to grow in new, unconventional paths and play a pivotal role in digital transformation and digital empowerment of the public and private sectors in line with the ambitious goals of the Kingdom's Vision 2030 towards a prosperous and diversified economy.

Business overview: Despite the challenges faced throughout the year, all stc's business units achieved an increase in revenue for the period.

- Enterprise Business Unit achieved an increase in revenues for the period by **29.3%** thanks to the company's ability to provide innovative products and services that meet the needs of the public and private sector.

- On the other side, Consumer Business Unit contributed positively to the results for the period as a result of an increase in operating lines by **3.4%**, an increase in fixed wireless access subscribers by **6.1%**, and an increase in demand for fiber-optic services, which led to an increase in the subscriber base by **20.8%**.
- lastly, Wholesale business unit revenues for the period increased by **5.5%**, as a result of stc's investments in infrastructure, which is starting to positively reflect on the unit's results.

Infrastructure:

- stc has deployed more than **4,000** towers in over **47** cities around the Kingdom. The next phase of 5G deployment will witness an expansion by increasing the network by **2,000** to **2,500** towers to reach over **71** new cities across the Kingdom. This is part of stc's effort to develop and improve the country's infrastructure.

stc pay:

- Registered Users: **Over 6 million** subs.
- Number of Visa cards issued: **Over 1 million**
- Numbers of POS Machines: More than **50k POS** out of 400k (in the total market).
- stc pay's full digital banking license enables the provision of all banking services such as accepting deposits, providing loans, and creating saving products.

Financial performance:

stc was able to improve all its financial metrics for the 6 month period as well as the 2nd quarter compared to the corresponding quarter last year, as it has achieved the highest quarterly and semi-annual revenues in its history.

- **Revenues** for the 2nd quarter reached **SR 15,899m** with an increase of **6.56%** compared to the corresponding quarter last year. For the first half of 2021, the **revenues** reached **SR 31,594m** an increase of **9.49%**.
- **Gross Profit** for the 2nd quarter reached to **SR 8,352m** with an increase of **0.13%** compared to the corresponding quarter last year. For the first half of 2021, the **Gross Profit** reached **SR 16,909m** with an increase of **2.25%**.
- **Operating Profit** for the 2nd quarter reached to **SR 3,250m** with an increase of **6.14%** compared to the corresponding quarter last year. For the first half of 2021, the **Operating Profit** reached **SR 6,732m** with an increase of **10.98%**.
- **Earnings before Interest, Taxes, Zakat, Depreciation and Amortization (EBITDA)** for the 2nd quarter reached to **SR 5,627m** with an increase of **5.34%** compared to the corresponding quarter last year. For the first half of 2021, the **Earnings before Interest, Taxes, Zakat, Depreciation and Amortization (EBITDA)** reached **SR 11,468m** with an increase of **7.47%**.
- **Net Profit** for the 2nd quarter reached to **SR 2,821m** with an increase of **3.56%** compared to the corresponding quarter last year. For the first half of 2021, the **Net Profit** reached **SR 5,773m** with an increase of **2.41%**. It is worth noting that this increase was achieved even with the exceptional capital gains of approximately **SR 650m** resulting from the Careem deal that were booked for the same period of 2020.

Lastly, as a continuation of our great performance in the past years, and our ambition to deliver strong results to our shareholders, it is important to note that we must carry on with our balanced approach where we can deliver increased profitability to our shareholders while taking into consideration the investment that we need to make to expand stc's business.

We will now start the Q&A session.

Q&A Session:

Person/ Company	Question	Answer
<p>Abdulaziz Alhubaishi</p> <p>Jadwa Investment</p>	<p>Q1: On the tower business in Saudi Arabia, What is your strategy in terms of your tower portfolio? And can stc monetize these towers?</p> <p>Q2: Could you please give us updates and your expectations about Aqalat?</p>	<p>A1: Tower related business is one of stc’s strategy pillars and this is why we carved out the towers to our subsidiary TAWAL, which we own 100%. The first phase was achieved very successfully, which are the cost reductions and efficiency created from to the towers that were carved out! As for now, we are getting in the second phase, which is expanding the business either locally or regionally. We are in discussions with our subsidiaries in Bahrain and Kuwait and some other countries to see the potential of expansion. Locally, we cannot disclose the discussion we have at the moment! However, we believe that tower consolidations will create value for all the local operators.</p> <p>A2: Aqalat’s strategy has been approved and there have been discussions about certain projects to monetize the lands that we have. The strategy is to sell, develop or rent these lands. However, these projects take time especially the ones that were tagged to be developed as it requires certain approvals. Definitely, in the long term it will contribute to stc’s overall performance.</p>
<p>Ashar Saleem</p> <p>FALCOM</p>	<p>Q1: Regarding Aqalat, what is the size of stc’s land bank?</p> <p>Q2: On Careem sale, can you please explain if the proceeds from the deal is done? Or is there still an additional proceeds to be received?</p> <p>Q3: Regarding the new cyber security company, is it part of existing business or a new created business? What kind of products and services it offers?</p>	<p>A1: We have a sizable land portfolio and some of these lands are in prime locations that can be developed. We will not get into developing ourselves, but we are planning to partner with some of real estate’s developers and see how we can monetize these lands with them. As I mentioned, these kind of discussions takes time. However, there is an overall approved strategy for Aqalat and the subsidiary is working based on it</p> <p>A2: Most of the proceeds of Careem’s deal are already received and reorganized. However, a minor amount remaining depends on some regulatory requirements in certain areas to be obtained.</p> <p>A3: It is a new company dedicated to providing advanced cybersecurity services and solutions to the private and public sectors. The launch comes to keep abreast of the growing demand for digital services in parallel with stc’s DARE strategy. The company will provide hardware, software and professional services. Its vision to become one of the largest cybersecurity solution provider in the region.</p>

	<p>Q1: Can you shed some light on the Cybersecurity company, is it going to be in a way competing with the services that are already provided by Solutions or it would act as a complement?</p>	<p>A1: They are different; the Cybersecurity company is not part of Solutions. All the services related to the cybersecurity from hardware and software will be under the Cybersecurity company's mandate. Further, the cybersecurity company will be able to offer its services/product independently to its customers. We believe that stc's market reach and its network will help our subsidiaries to provide the best services to their customers.</p>
<p>Ziad Itani Arqaam Capital</p>	<p>Q1: When it comes to the gross profit margins there seem to be some pressure where it declined by more than 300 bps Y-o-Y. What is the reason behind this pressure, does it come from the change in the revenue mix mainly from B2B segment, which has lower margins, or are you seeing some pressure in other segments mainly the retail segment because of the 5G network costs or the increase in VAT?</p> <p>Q2: When we look at the EBITDA margins there has been some substantial cost control done on General and Administration expenses. What is the reason behind that and is it sustainable going forward?</p>	<p>A1: When it comes to cost of sales, it is about both margin and the mix of revenue. Some of our services and products provided by the subsidiaries are low margin in nature compared to the connectivity margins, which considered high in margins. Some of our subsidiaries are in investing mode more than focusing on the profitability side, which ultimately increased the costs of sales. Additionally, the 5G investments are also contributing to the costs! However, we are adopting a balanced approach when it comes to investment and profitability in a way that it won't impact stc's EPS, return on equity, return of assets, and to maintain a continuance growth in ROIC.</p> <p>A2: There are huge efforts done to reduce the cost under stc's cost optimization program! It is a sophisticated program supervised by the Board of Directors. It has detailed initiatives with clear targets and KPIs on every corporate head unit either functional or business. It is supervised by the highest level to ensure costs are under control and we will continue with it in the future. Overall, the EBITDA margin is almost at the same level as last year. From group perspective, we are one of the highest companies in the region when it comes to EBITDA margin.</p>

<p>Jai Lawrence Al Mal Capital</p>	<p>Q1: Can you share any financial details in terms of stcPay or Solutions for H1 of this year?</p> <p>Q2: In terms of depreciation and amortization costs increased slightly, will that remain in the same level going forward?</p>	<p>A1: As for Solutions by stc Financials, it will be listed very soon in the next two months. At that time, you will be able to see their financials separately. As for stcpay, since we are working on fulfilling SAMA final requirements we can't disclose much details on stcpay till the time we complete these requirements.</p> <p>A2: As for depreciation and amortization, it is expected to increase to some extent due to the investment we are planning to put in place for both the core and non-core business. Those investments are not only related to stc KSA, but also stc's subsidiaries are investing to grow their business too!</p>
<p>Amir Badran Quencia Capital</p>	<p>Q1: Government ICT projects going forward will be awarded through request for proposal and not thru direct awarding which some of your competitors are optimistic that it will enable them to increase the possibility for them to be awarded some of these projects. Can you please comment on that?</p>	<p>A1: Our current market share is not a result of direct awarding, rather, a result of our technological capabilities. Having said that, we always welcome competition, as it is healthy for the market. Moreover, we have always invested in delivering high quality services and end-to-end solutions. In addition, the increased demand we are seeing right now will compensate for any competition that might arise.</p>
<p>Ashar Saleem Falcom</p>	<p>Q1: How stc is positioned in regards to data centers?</p>	<p>A1: Data centers are one of the growth areas that we have been investing in and will continue to do so, as we have noticed high demand in this area, and we are expecting this market to continue it growth.</p>

<p>Abdulaziz Alhebaishi</p> <p>Jadwa</p>	<p>Q1: As we see more ICT contributing to the topline of the company; Shifting the business would require more skills, as well as revamping the employee base. How would that mix help in generating the highest margins?</p>	<p>A1: When we started the ICT business, we were able to maintain healthy margins while improving the bottom line and topline. We want to compete aggressively when it comes to ICT sector!</p> <p>Further, as we continue to invest and since some of stc's subsidiaries are in growth mode, therefore, margins need to be carefully monitored.</p> <p>Moreover, when it comes to the manpower, we have elevated stc's employees capabilities by offering training along with hiring fresh minds. stc was one of the few companies who kept on hiring even in the heart of COVID-19 pandemic crisis.</p> <p>At the end, all these factors will clearly contribute into the right mix and capabilities for our company.</p>
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Turki AL Ashaikh (IR General Manager):

Thank you all again for participating in stc's Q2, 2021 conference call. If you need anything, please do not hesitate to email us at IRU@stc.com.sa,

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