Q4, 2019 Earnings Call Transcript

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 Q4 earning call, the conference will start in 5 minutes. Please note that if you get disconnected, you can call gain with the same PIN given to you before. Today, we will have Mr. Ameen Al Shiddi – stc group CFO – along with Mr. Ali Al Harbi Corporate Finance Vice President.

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

Presentation:

Welcome to the year 2019 financial performance conference call of stc group. We will walk you through certain business outlines, and achievements for the year 2019 and in particular, Q4 2019 performance. After the performance highlights, we will start the questions & answers session and try to address all the questions related to quarterly and full year financial results

We continued to achieve our DARE Strategy by maintaining the company's leadership position and delivering best digital solutions to the market. We aspire to become a world-class digital leader in the MENA Region. As we have mentioned in the past as well, we have always been a major and crucial part of the Kingdom's National Transformation Plan 2020 and Vision 2030. We see a clear and distinguished role for stc, as it has strategically positioned itself as the "go to service provider" for the government and enterprise entities by way of offering high quality solutions.

On the business side of the YTD results, all business segments have achieved growth in their top-lines. The group has achieved highest revenue since year 2013. Further, even before the proportional consolidation non-controlling international investment, the revenue achieved in year 2019 remains the highest in terms of overall growth, due to the healthy contribution from all business units and subsidiaries within the group.

The Consumer Business Unit (CBU) witnessed a Y-o-Y increase in mobility, data revenue and working lines. In terms of 5G technology, we have deployed over 2,300 towers, which resulted into increase in capital expenditures for Q4 and depreciation expense. Furthermore, FTTH subscribers base have increased by 23% as compared to Q4 2018, thanks to the vast fiber optics network rollout that has reached 217,000 Km by the end of year 2019.

In terms of CBU pricing, we have seen many promotions in the last quarter but we are not expecting any major change in pricing during the year 2020. However, we are closely monitoring the market dynamic with respect to product pricing, and will respond accordingly as and when required. Overall, I think that the consumer business has delivered decent results in year 2019, supported by a pricing rationalization with the exception of certain cases.

Moving on to Enterprise Business Unit (EBU) performance, we have earned good revenues from Cyber Security, cloud computing and managed services. Additional focus will be placed on IOT, integration and advisory segments during year 2020, as there is a huge growth potential in these business segments, and it is expected to positively contribute towards the group's top-line. Furthermore, we are optimistic that capital investments done by stc in year 2019 and earlier will yield reasonable returns and margins will improve going forward.

Taking about overall financial performance of the group, revenues have increased approximately by 5%, gross profit improved by 6% plus, and operating profit by 2%. The group EBITDA increased by 7.3% to almost SAR 21 billion. Part of that growth, as previously highlighted, is due to IFRS impact. However, excluding IFRS impact, stc realized 3.5% Y-o-Y increase in EBITDA. For the net income, we were able to maintain the profitability for the whole year reaching to SAR 10.755 billion.

In Q4 2019, net income declined Y-o-Y, in which part of that, is due to reversal of government charges amounting to SAR 580 million that were booked in Q4, 2018, which has resulted into roughly 22% decline in in Q4, 2019 net income. Also, stc made investments in IT related services & applications, capability building, customer acquisitions, stc pay marketing, and launching of new brand across the group level, which impacted the Q4 2019 depreciation and expenses. This is the overall financial performance highlights for the Q4 2019 and the full year.

We will now start the Q&A session.

Q&A Session:

Person/ Company	Question	Answer
Mohammed Faisal **Riyad Capital**	**Q1:** Can you provide the breakdown on the cash and convertible notes that stc will receive as part of the Uber/Careem acquisition, and the period in which it will be reflected?	**A1:** When the financial statement in Tadawul website is released, you can see a clear breakdown and disclosure as to the particulars of the deal. Further, please note that we have also an indirect ownership through two venture funds. The indirect ownership has been recognized in Q4 financial statements as per the fair value methodology provided by the funds. The direct ownership, as we also highlighted in Tadawul announcement will be recognized in Q1 2020 financial statements because the deal was closed on 2nd January 2020.
Hassan Abdelgalil **CI Capital**	**Q1:** Revenue performance, can you say more on the decrease on revenue compared to the 9 months or the 3 quarters of 2019. **Q2:** Are there any details on the expansion into MENA? **Q3:** A question on the acquisition in MENA, do you target to have a controlling stake or you are fine with minority stake or non-controlling stake?	**A1:** There were some fluctuations in the revenue side due to seasonality factor related to some of the subsidiaries, and non-recurring revenues that were booked in other quarters but not in the 4th quarter of year 2019. However, I think the focus should be on the overall yearly performance and achievements of the group, rather than looking at the quarterly performance only. **A2:** As previously mentioned, we have been working on selected opportunities within the MENA region as part of our DARE strategy is to acquire companies related to media, fintech, and IT services, or acquisitions that can be part of the overall expansion story for the group. Any progress in this aspect, will be immediately announced through the official channels i.e. Tadawul. **A3:** Overall, what we are looking for is a controlling stake, if it is a traditional telecom service company. However, we might change our approach in case of an ICT company.
Nishit Lakhotia **SICO**	**Q1:** Selling and marketing expenses are higher in Q4 due to rebranding and increased cost for customer acquisition. Are these costs behind now? Can we expect to see some of these costs in Q1 2020 as well? What is exactly the promotions that have been done and how is the competition environment. **Q2:** Depreciation & Amortization has gone up in Q4 due to 5G and other investments. Is this the rate that we can expect in coming quarters? **Q3:** Regarding government receivables, how are you managing working capital with the government, are you perhaps delaying payment of royalty charges?	**A1:** Part of these expenses are related to the branding. However, a big part can also be attributed to promotions and commissions at group and subsidiary levels. However, it also helped the group to grow its active user base. With regards to the booking period, the majority of the branding cost has been booked in Q4 2019, a slight portion might be booked in Q1 2020. The higher cost of customer acquisition is not necessarily going to continue for 2020. **A2:** As for Capex, there was a lot of acceleration that happened from September until year-end, which affected depreciation and amortization expense. Nonetheless, this is not expected to continue on a quarterly basis. Furthermore, when looking at the depreciation & amortization for the whole year, not all of it was related to capex and expansion, part of it is related to the IFRS 16 accounting treatment. **A3:** No, we are paying on time.

JP Davids **JP Morgan**	**Q1:** Regarding the enterprise business unit, you have been the market share taker in this particular segment. Moreover, in your remarks, you highlighted your investments into cloud computing managed services and cyber security, could you provide us with an outlook for the revenue synergy you see in this particular vertical and the prospect for market share in the medium-term? **Q2:** Could you provide an update on with tractions of the stc pay?	**A1:** Looking at the ability of stc to provide solutions for the market and the investment we have made in our subsidiaries i.e. stc solutions, I think the opportunity is huge and I believe that we will continue to capture market share in all segments going forward. This is a double-digit growth area that we believe will continue to grow for the next three years. However, the challenge will be in the margins, some of these services do not have high margins compared to the traditional services. In the long term, its impact will not only going to be in the topline, but also it will be profitable and will continue to have a positive impact on EBITDA. **A2:** The active users for stc pay jumped from 50 thousand user to 500K-600K active users in less than a year. There is Huge growth potential in stc pay. We will continue to invest in order to capture growth in this particular segment. We will update the market soon about stc pay and its strategy.
Evgeny Annenkov **Merrill Lynch**	**Q1:** Can you comment on working capital in Q4?	**A1:** The challenge with working capital is the receivable with the government, and that is something we disclosed in stc's financials. Given the current situation, we have been able to manage our receivables and payables in an efficient manner. Currently we are working closely with the government to collect our receivables. stc has collected all the receivables related to the years 2014, 2015, and 2016. Now we are in discussion with the government to finalize the collection for the year 2017 amounting to SAR 6 billion plus, hopefully in Q1, 2020, and then we will work on the year 2018 collection. Other than that, we are fine. We are trying to optimize our working capital by considering different financing options in 2020, though, nothing has been decided from the board yet.
Ondrej Cabejsek **UBS**	**Q1:** Since most NTP 2020 targets end in 2020, does this mean we can expect higher capex in this year? And what is your progress in relation to these KPIs? **Q2:** Beyond 2020, are there any other targets other than NBB? **Q3:** Are the targets for 5G beyond 2020 stc's initiative or are they driven by the government?	**A1:** 2018 and 2019 targets have been achieved, and we are on track to achieve 2020's target. Capex for 2020 is expected to be quite aggressive due to 5G deployment, and the continuation of the NBB project. So overall, 2020 will be a year of expansions, very similar to 2019 or slightly higher. **A2:** Yes, 5G will continue its expansion beyond 2020. However, this will depend on the market, 5G appetite, and the overall business case. **A3:** This is stc's initiative, as it is stc's decision to expand or not.

Turki AL Ashaikh (IR General Manager):

Thank you all once again for participating in stc's Q4, 2019 conference call. If you need any further information, please don't hesitate to email us at IRU@stc.com.sa, you may disconnect now and thank you.

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