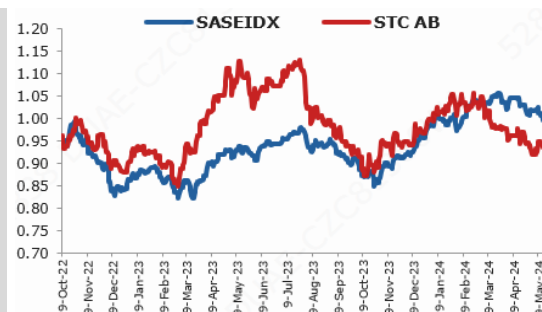


Saudi Telecom Company (STC)

Increase in mobile subscribers coupled with higher voice and data volumes drove profitability

Current Price	Target Price	Upside/Downside (%)	Rating
SAR 38.00	SAR 46.00	+21%	BUY

- STC's KSA Mobile subscribers rose 10.4% YOY to 26.9 Mn in 1Q24, while fixed subscribers marginally increased 2.2% YOY to 5.6 Mn in 1Q24.
- Public Investment Fund (PIF) and STC signed a final agreement to sell a 51% stake in TAWAL to PIF.
- STC Group established a strategic partnership between Saudi Railway Company and sirar to improve cybersecurity and technology
- STC Solutions signed a memorandum of understanding with Devoteam Global Group to explore global investment and collaboration opportunities in technology and related fields.
- STC formed a strategic alliance with China Mobile International Limited to enhance IoT connectivity in several industries in the MENA region.



1Q24 Net Profit in line with our estimate

STC Group ("STC, "the Company") recorded a 5.7% YOY growth in net profit to SAR 3,286 Mn in 1Q24, in line with our estimate of SAR 3,220 Mn. The growth in profit is mainly attributable to the increase in revenues coupled with a decline in selling and distribution expenses and zakat charges partially offset by the increase in cost of revenue, G&A expenses, and net finance cost.

P&L Highlights

STC's revenue grew 5.1% YOY to SAR 19.1 Bn in 1Q24 owing to a rise in subscriber base and increase in overall revenue. STC KSA's mobile subscribers rose 10.4% YOY to 26.9 Mn in 1Q24, while the fixed subscriber base increased 2.2% YOY to 5.6 Mn. Channel segment revenue rose 10.3% YOY to SAR 4.1 Bn in 1Q24 while Solutions segment revenue grew 4.9% YOY to SAR 2.8 Bn. Healthy growth in revenue from commercial segments drove STC KSA's revenue. STC's direct cost grew 8.6% YOY to SAR 9.7 Bn in 1Q24. Thus, gross profit increased 1.6% YOY to SAR 9.4 Bn in 1Q24. Gross profit margin declined 165 bps YOY and 191 bps QOQ to 49.1% in 1Q24. Selling and overhead expenses declined 5.1% YOY to SAR 1.2 Bn YOY in 1Q24. Moreover, G&A Expenses grew 5.5% YOY to 1.7 Bn in 1Q24. As a result, the Company's EBITDA rose 2.1% YOY to SAR 6.5 Bn in 1Q24. EBITDA margin declined 100 bps YOY and increased 249 bps QOQ to 33.9% in 1Q24. Depreciation and amortization expenses marginally grew 0.2% YOY to SAR 2.6 Bn in 1Q24. Thus, operating profit rose 3.4% YOY to SAR 3.9 Bn in 1Q24 with a decline in operating margin by 33 bps YOY to 20.2% in 1Q24. The Company's other expenses fell 10.0% YOY to SAR 306 Mn in 1Q24. STC's finance income 22.9% YOY to SAR 442 Mn in 1Q24. On the other hand, finance charges increased significantly from SAR 238 Mn in 1Q23 to SAR 415 Mn in 1Q24 due to a significant increase in debt.

Stock Information

Market Cap (SAR, mn)	190,000.00
Paid Up Capital (mn)	50,000.00
52 Week High	44.75
52 Week Low	34.09
3M Avg. daily value (SAR)	144,701,900

1Q24 Result Review (SAR, mm)

Total Assets	159,683
Total Liabilities	77,107
Total Equity	82,767
EBITDA	6,474
Net Profit	3,286

Financial Ratios

Dividend Yield (12m)	6.84
Dividend Pay-out (%)	59.98
Price-Earnings Ratio(x)	14.06
Price-to-Book Ratio (x)	2.35
Book Value (SAR)	16.14
Return-on Equity (%)	17.38

Stock Performance

5 Days	-0.13%
1 Months	-0.72%
3 Months	-6.99%
6 Months	1.87%
1 Year	-11.83%
Month to Date (MTD%)	0.93%
Quarter to Date (QTD%)	-1.47%
Year to Date (YTD%)	-3.42%

In addition, zakat expense declined 34.7% YOY to SAR 246 Mn in 1Q24. The share of profit attributable to non-controlling interest holders increased from SAR 26 Mn in 1Q23 to SAR 45 Mn in 1Q24.

Balance Sheet Highlights

STC's debt grew from SAR 10.7 Bn in 1Q23 to SAR 22.0 Bn in 1Q24. Cash and cash equivalent increased from SAR 26.1 Bn in 1Q23 to SAR 26.8 Bn in 1Q24. The Company's capex stood at SAR 1.7 Bn in 1Q24 compared to SAR 1.2 Bn in 1Q23. The Company's free cash flow stood at negative SAR 0.3 Bn in 1Q24 compared to positive SAR 2.1 Bn in 1Q23.

Target Price and Rating

We maintain our BUY rating on Saudi Telecom Company with an unchanged target price of SAR 46.00. STC's KSA Mobile subscribers rose 10.4% YOY to 26.9 Mn in 1Q24 and fixed subscribers increased 2.2% YOY to 5.6 Mn. Strong growth in subscriber base and solid growth in data volumes drove profitability. Voice call volumes in the Mosque of Makkah rose 35% YOY in Ramadan, while data volumes witnessed a 37% YOY increase due to solid developments in technology and enhanced efficiency of services. Public Investment Fund (PIF) and STC signed final agreement to sell 51% stake in TAWAL to PIF, forming the largest regional telecom company. The merged company will own c. 30,000 mobile towers. Additionally, STC Group established a strategic partnership between Saudi Railway Company and sirar to improve cybersecurity and technology in critical infrastructure sectors to enhance Saudi Railway Company's railway network and travel & cargo transport security. Furthermore, Solutions signed a memorandum of understanding with Devoteam Global Group to explore global investment and collaboration opportunities in technology and related fields. The agreement builds upon solutions acquisition of a 40% stake in Devoteam Middle East. STC and Devoteam leverage common markets and evaluate collaboration and investment prospects in the ICT landscape. Moreover, STC formed a strategic alliance with China Mobile International Limited to enhance IoT connectivity in several industries in the MENA region. The partnership aims to leverage both companies digital transformation strengths and offer innovative solutions, strengthening STC's position in the IoT market. Furthermore, solutions signed a term sheet agreement with Nile, a US based Network as a Service (NaaS) leader to establish a joint venture during "LEAP 2024" to strengthen their market presence as well as service offerings. The joint venture will offer secure, comprehensive enterprise network solutions (NaaS) in Saudi Arabia and the MENA region. The Company's strong expansion plans to improve digital infrastructure in the MENA region will lead to solid cash flows in the upcoming period. Thus, based on our analysis, we assign a BUY rating on the stock.

STC - Relative valuation

(at CMP)	2019	2020	2021	2022	2023	2024F
PE	17.8	17.3	16.8	15.6	14.3	15.8
PB	3.1	3.0	2.7	2.6	2.4	2.3
EV/EBITDA	9.0	8.2	8.1	7.1	7.5	7.3
Dividend yield	4.2%	5.3%	4.2%	4.2%	4.2%	4.2%

FABS Estimates & Co Data

STC – P&L

SAR mn	1Q23	4Q23	1Q24	1Q24F	Var.	YOY Ch	QOQ Ch	2023	2024F	YOY Ch
Sales	18,179	17,724	19,100	19,021	0.4%	5.1%	7.8%	72,337	75,876	4.9%
Cost of Sales	-8,945	-8,675	-9,714	-8,940	8.7%	8.6%	12.0%	-34,533	-35,662	3.3%
Gross profit	9,234	9,049	9,386	10,081	-6.9%	1.6%	3.7%	37,804	40,214	6.4%
Selling & overhead exp.	-1,298	-1,396	-1,232	-1,617	-23.8%	-5.1%	-11.7%	-5,914	-6,829	15.5%
G&A expenses	-1,593	-2,086	-1,680	-1,807	-7.0%	5.5%	-19.5%	-7,206	-7,588	5.3%
EBITDA	6,343	5,567	6,474	6,657	-2.7%	2.1%	16.3%	24,683	25,798	4.5%
Dep & Amort	-2,613	-2,716	-2,618	-2,669	-1.9%	0.2%	-3.6%	-10,483	-10,676	1.8%
Operating profit	3,731	2,851	3,856	3,988	-3.3%	3.4%	35.2%	14,200	15,121	6.5%
Other income/(exp)	-340	-226	-306	-254	20.7%	-10.0%	35.3%	353	-1,015	NM
Finance Income	360	431	442	253	75.0%	22.9%	2.7%	1,513	1,011	-33.2%
Financial charges	-238	-480	-415	-429	-3.3%	74.1%	-13.6%	-1,271	-1,716	35.0%
Profit before zakat	3,512	2,575	3,577	3,558	0.5%	1.9%	38.9%	14,795	13,402	-9.4%
Zakat	-377	-313	-246	-268	-8.1%	-34.7%	-21.4%	-1,375	-1,072	-22.1%
Profit before NCI	3,135	2,262	3,331	3,290	1.2%	6.3%	47.3%	13,419	12,329	-8.1%
NCI	26	-12	45	70	-35.7%	NM	NM	124	280	NM
Net Profit	3,109	2,274	3,286	3,220	2.0%	5.7%	44.5%	13,295	12,049	-9.4%

FABS estimate & Co Data

STC – Margins

	1Q23	4Q23	1Q24	YOY Ch	QOQ Ch	2023	2024F	YOY Ch
Gross Profit	50.8%	51.1%	49.1%	-165	-191	52.3%	53.0%	74
EBITDA	34.9%	31.4%	33.9%	-100	249	34.1%	34.0%	-12
Operating Profit	20.5%	16.1%	20.2%	-33	410	19.6%	19.9%	30
Net Profit	17.1%	12.8%	17.2%	10	437	18.4%	15.9%	-250

FABS estimate & Co Data

Valuation:

We use Discounted Free Cash flow (DCF) and Relative Valuation (RV) to value Saudi Telecom Company. We have assigned 70% weight to DCF and 30% to RV.

Valuation Method	Target	Weight	Weighted Value
DCF Method	49.93	70.0%	34.95
Relative Valuation (RV)	36.84	30.0%	11.05
Weighted Average Valuation (SAR)			46.00
Current market price (SAR)			38.00
Upside/Downside (%)			+21%

1) DCF Method:

STC is valued using free cash flow to firm. We have discounted the cash flow using the weighted average cost of capital of 8.4%. It is arrived after using cost of equity of 8.6% and after-tax cost of debt of 6.6% with debt-to-equity ratio of 11.6%. Cost of equity is calculated by using 10-year government bond yield of 5.3%, beta of 0.95 and equity risk premium of 3.5%. Government bond yield is calculated after adding KSA 10-year CDS spread over 10-year US risk free rate. The cost of debt is calculated using the cost of 6.8% after adjusting a tax rate arriving at after-tax cost of debt of 6.6%. Also, assumed a terminal growth rate of 2.0%.

Sum of PV (SAR, Mn)	58,903
Terminal value (SAR, Mn)	192,530
FV to Common shareholders (SAR, Mn)	249,649
No. of share (Mn)	5,000
Current Market Price (SAR)	38.00
Fair Value per share (SAR)	49.93

DCF Method

(All Figures in SAR Mn)	FY 2024E	FY 2025E	FY 2026E	FY 2027E	FY 2028E
NOPAT	15,468	16,604	17,290	18,238	18,694
Depreciation and Amortization	10,567	11,264	11,695	12,211	12,940
(-) CAPEX	-13,450	-13,666	-13,738	-13,637	-13,688
(-) Change in Net Working Capital	-8,739	5,272	778	2,631	569
Free Cash Flow to Equity (FCFF)	2,383	19,474	16,026	19,443	18,515
Discounting Factor	0.95	0.88	0.81	0.74	0.68
Discounted FCFF	2,261	16,978	12,837	14,309	12,519

Source: FAB Securities

2) Relative Valuation:

We have used local as well as international peers to value STC and it is valued using the EV/EBITDA multiple. It is valued at EV/EBITDA multiple of 6.8x in line with peers.

Company	Market (USD Mn)	EV/EBITDA (x)		P/E (x)	
		2024F	2025F	2024F	2025F
Etihad Etisalat Company (Mobily)	10,540	6.8x	6.2x	15.6x	14.0x
Thaicom	390	13.9x	17.2x	43.7x	73.7x
Emirates Telecommunications Group Company	38,300	6.4x	5.8x	14.8x	13.2x
Telstra Group Ltd	28,300	6.8x	6.5x	20.6x	19.1x
Bharti Airtel	96,040	9.3x	10.4x	96.0x	37.5x
Average		8.6x	9.2x	38.1x	31.5x
Median		6.8x	6.5x	20.6x	19.1x
Max		9.3x	10.4x	43.7x	37.5x
Min		6.8x	6.2x	15.6x	14.0x

Source: FAB Securities

Research Rating Methodology:

Rating	Upside/Downside potential
BUY	Higher than +15%
ACCUMULATE	Between +10% to +15%
HOLD	Lower than +10% to -5%
REDUCE	Between -5% to -15%
SELL	Lower than -15%

FAB Securities Contacts:

Research Analyst

Ahmad Banihani +971-2-6161629 ahmad.banihani@Bankfab.com

Sales & Execution

Abu Dhabi Head Office

Trading Desk +971-2-6161700/1 Online Trading Link
 +971-2-6161777

Institutional Desk +971-4-4245765

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