

3Q20 Results Update

December 02, 2020

Recommendation	Neutral
Previous Recommendation	Neutral
Current Price (SAR)	101.8
Target Price (SAR)	101.0
Upside/Downside (%)	(0.8%)

As of November 04, 2020

Key Data (Source: Bloomberg)

Market Cap (SAR bn)	203.6
52-Wk High (SAR)	106.6
52-Wk Low (SAR)	72.3
Total Outstanding Shares (in bn)	2.0
Free Float (%)	30.0%

STC vs. TASI (Rebased)

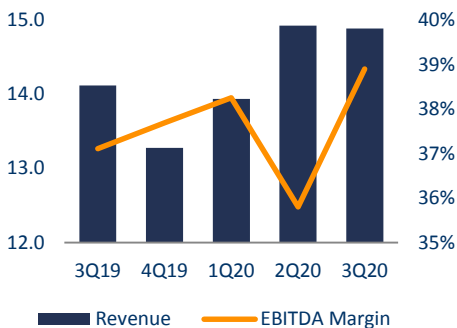


Price Performance (%)	Absolute	Relative
1m	1.4%	2.5%
6m	15.2%	(7.5%)
12m	7.2%	1.5%

Major Shareholders (%)

Public Investment Fund	70.0%
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Quarterly Revenue (SAR bn) and EBITDA Margin



Source: Bloomberg, Company Financials, FALCOM Research; Data as of November 04, 2020

Higher operating, finance expense weigh on margins

Saudi Telecom Co. (STC) reported a 5.4% YoY increase in 3Q20 revenue to SAR 14.9bn and a 6.4% YoY rise in 9M20 revenue to SAR 43.7bn. The growth in 3Q20 revenue was aided by a strong performance in consumer business segment. Gross profit grew 13.3% YoY to SAR 9.0bn on account of a 4.6% YoY drop in cost of sales to SAR 5.9bn. This offset the increase in SG&A expense and resulted in a 4.0% YoY increase in operating profit to SAR 3.5bn. A higher top line and lower cost of sales counterbalanced the surge in net finance charges and zakat expense, and led to a 0.7% YoY rise in net profit (attributable to equity holders) to SAR 2.8bn. Net profit margin for the quarter stood at 18.6% compared with 19.5% in 3Q19.

The Consumer segment witnessed strong growth in 9M20 on a 25.2% YoY and 8.5% YoY increase in the FTTH and broadband subscriber base, respectively. The segment was also boosted by a 10.1% YoY surge in data revenue. STC is expected to report higher revenue in 2020 compared with 2019 levels, amid growing demand for data services. STC is seeking to spin off its STC Solutions segment through an IPO, which is reportedly in the early stages of discussion. The company has also inked an agreement with NEOM Co. to establish 5G network infrastructure within the NEOM megacity and is likely to benefit from the partnership in the long term. The company showcases a strong balance sheet with low debt-to-equity and net debt-to-EBITDA ratios, which would be favorable for further expansion in the 5G space in KSA. However, headwinds in the form of heightened competition and stringent regulations may hamper the company's performance. Declining margins and rising receivables also remain a concern for the company in the near term. Thus, in view of the countervailing factors, we maintain our "Neutral" rating on the company's stock.

- STC's revenues rose 5.4% YoY to SAR 14.9bn in 3Q20. The company recorded a 6.4% YoY rise in 9M20 revenue to SAR 43.7bn due to growth in its Consumer segment, primarily due to an increase in FTTH and broadband subscribers, in addition to higher data revenues. Apart from the Consumer segment, revenue contribution from Enterprise and Wholesale segments also increased in 9M20.
- Gross profit grew 13.3% YoY to SAR 9.0bn as cost of sales dropped 4.6% YoY to SAR 5.9bn in 3Q20. As a result, gross profit margin expanded to 60.3% against 56.1% in 3Q19.
- The higher gross profit offset the impact of the increase in total SG&A expense, resulting in the company reporting a 4.0% YoY increase in operating income to SAR 3.5bn. However, EBIT margin contracted to 23.2% in 3Q20 from 23.6% in 3Q19.
- Higher net finance charges and zakat expense were offset by an improved top line and led to 0.7% YoY growth in net income (attributable to equity holders) to SAR 2.8bn for 3Q20. Nevertheless, net profit margin narrowed to 18.6% from 19.5% in 3Q19.
- On September 13, STC stated that it failed to reach an agreement with Vodafone Egypt to acquire a 55.0% stake in the company.
- On October 21, STC announced a cash dividend of SAR 1.0 per share to its shareholders for 3Q20 performance. The dividend amounts to SAR 2.0bn and is equivalent to 10.0% of the company's share capital.
- On October 28, rating agency Tassnief assigned a "AAA" long-term rating to STC on account of its strong operational capabilities and robust financial position.

Valuation: We retain our target price at SAR 101.0 per share and maintain "Neutral" rating on the stock.

	3Q20	3Q19	% YoY	FY20E	FY19	% YoY
Revenues (SAR mn)	14,881	14,114	5.4%	56,881	54,376	4.6%
Gross Profit (SAR mn)	8,971	7,921	13.3%	33,275	32,407	2.7%
EBITDA (SAR mn)	5,788	5,238	10.5%	21,330	21,281	0.2%
Net Profit (SAR mn)	2,766	2,746	0.7%	11,276	10,755	4.9%
EPS basic (SAR)	1.38	1.37	0.7%	5.64	5.38	4.9%
Gross Margin (%)	60.3%	56.1%	4.2%	58.5%	59.6%	(1.1%)
EBITDA Margin (%)	38.9%	37.1%	1.8%	37.5%	39.1%	(1.6%)
Net Profit Margin (%)	18.6%	19.5%	(0.9%)	19.8%	19.8%	0.0%

Source: Company Financials, FALCOM Research

FALCOM Rating Methodology

FALCOM Financial Services uses its own evaluation structure, and its recommendations are based on quantitative and qualitative data collected by the analysts. Moreover, the evaluation system places covered shares under one of the next recommendation areas based on the closing price of the market, the fair value that we set and the possibility of ascent/descent.

Overweight: The Target share price exceeds the current share price by $\geq 10\%$.

Neutral: The Target share price is either more or less than the current share price by 10%.

Underweight: The Target share price is less than the current share price by $\geq 10\%$.

To be Revised: No target price had been set for one or more of the following reasons: (1) waiting for more analysis, (2) waiting for detailed financials, (3) waiting for more data to be updated, (4) major change in company's performance, (5) change in market conditions or (6) any other reason from FALCOM Financial Services.

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