

4Q 2017 Results Update
January 30, 2017

Recommendation	Neutral
Previous Recommendation	Overweight
Current Price (SAR)	72.6
Target Price (SAR)	75.5
Upside/Downside (%)	4.0%

As of January 30, 2018
Key Data (Source: Bloomberg)

Market Cap (SAR bn)	145.3
52 Wk High (SAR)	78.9
52 Wk Low (SAR)	64.5
Total Outstanding shares (in bn)	2.0
Free Float (%)	16.2%

STC Vs TASI (Rebased)


Price Performance (%)	Absolute	Relative
1m	(5.6)	(0.3)
6m	1.4	8.2
12m	(6.8)	(0.2)

Major Shareholders (%)	%
Public Investment Fund	70.0%
General Org For Social Insurance	7.0%
General Retirement Org	6.8%

Quarterly Sales (SAR mn) and Operating Margin


Source: Bloomberg, Company Financials, FALCOM Research; Data as of 30th January 2018

Cost optimisation initiatives support earnings growth

Saudi Telecom Company (STC) reported a 27.2% YoY increase in 4Q17 earnings, with net income rising to SAR 2.65bn, considerably outperforming street estimates (+17% vs. consensus and +1.1% QoQ). This outperformance was mainly due to cost control measures, which lowered operating costs and elevated gross and operating margins, despite a decline in revenue (-2.7% QoQ and -4.0% YoY). 4Q17 net profit stood at the highest level since 3Q14.

- Consolidated revenue declined to SAR12.5bn in 4Q17, down 4.0% YoY from SAR13.0bn in 4Q16. Weak consumer sentiment amid challenging economic conditions, and regulatory environment such as lifting the ban on VOIP and implementation of expats levy significantly affected international call revenue leading to a drop in service revenue. This was partially offset by strong growth in data revenue and a 20% YoY increase in FTTH customer base. Furthermore, the company's focus on diversifying income sources yielded positive results, as indicated by enterprise and wholesale sector revenue growth.
- Gross profit stood at SAR7.6bn in 4Q17, up 8.0% YoY, supported by improving operational efficiency and cost optimisation, despite the decline in revenue. Gross margins continued to improve in 4Q17, reaching the highest level to 60.7% since 4Q14.
- EBIT surged 60.9% YoY to SAR2.9bn in 4Q17 vs. SAR1.8bn in the corresponding period last year, supported by a SAR690mn decline in selling and marketing expenses. This helped improve EBIT margin to 23.5% in 4Q17 from 14.1% in 4Q16.
- Subdued other income and expenses (SAR25mn) in 4Q17 compared with SAR389mn in 4Q16 restricted net income growth. Consequently, net income grew by 27.2% to SAR2.6bn in 4Q17 vis-à-vis SAR2.1bn in 4Q16.
- In terms of full year numbers, consolidated revenue slipped 4.3% to SAR51.4bn in FY17 from SAR53.7bn in the prior year. This remains mostly in line with our estimate. Successful cost control measures resulted in an increase in gross margins to 57.5% with gross profit amounting to SARA29.6bn. EBITDA rose 7.1% to SAR19.3bn in FY17 vs SAR18.0bn in FY16
- Net profit increased 14.3% YoY in FY17 to SAR10.2bn from SAR8.9bn in FY16, in line with our estimate of SAR10.3bn.
- According to sources, CITC ordered investigation of data price hike by telecom companies in the Kingdom, following VAT implementation and, thereafter, asked telecom companies to correct prices and offers. If the regulator decides to take further action against telecom companies, it would be a negative for the sector, especially for STC, the market leader.
- Overall, we believe the company is available at a cheap valuation due to current negative news flow, although it would benefit from Vision 2030 in the medium to long term, wherein the government identified the telecom sector as one of the pillars of future growth.

Valuation: We had initiated STC with an 'Overweight' rating with a fair value of SAR75.5 per share. Currently, the rating is 'Neutral' due to increase in share price.

	4Q'17	4Q'16	% YoY	FY17	FY16	% YoY
Revenues (SAR bn)	12.5	13.0	(4.0)	51.4	53.7	(4.3)
Gross Profit (SAR bn)	7.6	7.0	8.0	29.6	28.7	3.0
Operating Profit (SAR bn)	2.9	1.8	60.9	11.1	10.0	11.6
Net Profit (SAR bn)	2.6	2.1	27.2	10.2	8.9	14.3
EPS (SAR)	1.32	1.04	27.2	5.09	4.45	14.3
Gross Margin (%)	60.7	54.0	12.5	57.5	53.4	7.7
Operating Margin (%)	23.5	14.1	67.5	21.6	18.5	16.6
Net Profit Margin (%)	21.2	16.0	32.4	19.8	16.6	19.5

Source: Company Financials, FALCOM Research

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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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