

20 October 2011

Buy

Target price
SR47.70

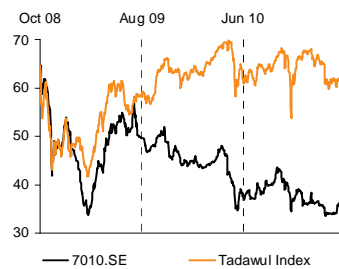
Price
SR36.10

Short term (0-60 days)
n/a

Market view
No Weighting

Price performance

	(1M)	(3M)	(12M)
Price (SR)	34.10	35.80	39.10
Absolute (%)	5.9	0.8	-7.7
Rel market (%)	6.1	6.4	-5.3
Rel sector (%)	5.7	3.4	1.3



Market capitalisation
SR72.20bn (€14.00bn)

Average (12M) daily turnover
SR34.27m (US\$9.10m)

Sector: Tadawul Telecoms Index
RIC: 7010.SE, STC AB
Priced SR36.10 at close 19 Oct 2011.
Source: Bloomberg

Analyst

Shrouk Diab
United Arab Emirates
+971 552 248 033
shrouk.diab@rasmala.com

Dubai International Financial Centre,
The Gate Village, Building 10, Level 1,
P.O. Box 31145, Dubai, United Arab
Emirates

www.rasmala.com

STC

STC releases 3Q11 results

Initial reaction to Saudi Telecom Company's (STC's) 3Q11 results: revenues and EBITDA in-line with our estimates, but net profit misses expectations.

Key forecasts

	FY09A	FY10A	FY11F	FY12F	FY13F
Revenue (SRm)	50,780	51,787	54,878	56,800	58,789
EBITDA (SRm)	20,612	19,625	20,305	20,732	21,164
Reported net profit (SRm)	10,863	9,440	8,341	8,787	9,448
Normalised net profit (SRm)	10,863	9,440	8,341	8,787	9,448
Normalised EPS (SR)	5.43	4.72	4.17	4.39	4.72
Dividend per share (SR)	3.00	3.00	3.00	3.50	3.50
Dividend yield (%)	8.31	8.31	8.31	9.70	9.70
Normalised PE (x)	6.65	7.65	8.66	8.22	7.64
EV/EBITDA (x)	4.66	4.92	4.48	3.57	2.57
EV/invested capital (x)	1.29	1.24	1.21	1.00	0.76
ROIC - WACC (%)	0.00	0.00	0.00	0.00	0.00

Accounting standard: local GAAP
Source: Company data, Rasmala forecasts

year to Dec, fully diluted

Revenue grew yoy by 6% to SR14.02bn end of 3Q11, in line with expectations

STC's revenue increased to SR14.02bn for 3Q11 compared to SR13.23bn end of 3Q10, a yoy increase of 6%. According to STC, local growth was driven by handset/media devices and overall broadband revenue (a 151% yoy increase in mobile broadband revenue and a 66% yoy increase in mobile broadband subscribers). In the international operations, STC saw significant growth in broadband revenue as a result of the increased use of social networking services via handsets and smartphones by the younger generation in Indonesia, India and Turkey. In STC's Viva operations, STC managed to increase market share in Bahrain and Kuwait. Overall, our revenue estimate was below results by 3.6% for 3Q11 and was below by 1.3% in terms of 9M11 revenue results.

EBITDA generally in-line with expectations, while net profit misses

EBITDA for 3Q11 amounted to SR5.2bn, a yoy decrease of 4%. Our EBITDA estimate was below results by 4.9% for 3Q11 and was below by 1.8% in terms of 9M11 EBITDA reported results. Meanwhile, net income for 3Q11 amounted to SR1.6bn, a yoy decline of 53% and a qoq decrease of 31%. Our net profit estimate was widely below results by 29% for 3Q11 and below by 10.7% in terms of 9M11, due to: a) SR780m in FX losses booked this quarter; and b) provision of SR134m due to the recent Council of Ministers decree. The decree states that STC should pay additional financial costs that might arise from merging the two systems of Public Pension Fund and General Organisation for Social Insurance as a result of liberalising the telecom sector. Similarly, there was SR728m recorded in 3Q10, representing gains from the sale of fixed assets (towers) to Aircel in India.

Disappointing results may affect share price negatively

In the light of STC's 3Q11 results, which missed both our estimates and consensus estimates from Bloomberg, particularly on the net profit line, we believe that this could pose some selling pressure on the stock. We will be revising our estimates, once the full financial set of results for 3Q11 is available. Our target price for STC remains unchanged at SR47.70, and we maintain our Buy recommendation.

Important disclosures can be found in the Disclosures Appendix.

Distributed outside MENA by The Royal Bank of Scotland N.V. and its affiliates under a strategic alliance with Rasmala Investment Bank Ltd.

Table 1 : STC 3Q11 and 9M11 results

SRm unless stated otherwise	3Q11	3Q10	growth	9M11	9M10	growth
Revenue	14,015	13,232	6%	40,971	38,343	7%
EBITDA	5,198	5,417	-4%	15,098	14,381	5%
EBITDA margin (%)	37.1%	40.9%		36.9%	37.5%	
Net profit	1,562	3,317	-53%	5,391	7,151	-25%

Source: STC

Table 2 : Our estimates versus actual results

SRm unless stated otherwise	Ours		Actual		Variance	
	3Q11F	9M11	3Q11	9M11	3Q11	9M11
Revenue	14,543	41,499	14,015	40,971	-3.6%	-1.3%
EBITDA	5,468	15,368	5,198	15,098	-4.9%	-1.8%
EBITDA margin (%)	37.6%	37.0%	37.1%	36.9%		
Net profit	2,210	6,040	1,562	5,391	-29.3%	-10.7%

Source: Rasmala estimates, STC

Table 3 : Bloomberg consensus estimates versus actual results

SRm unless stated otherwise	Consensus		Actual		Variance	
	3Q11F	9M11	3Q11	9M11	3Q11	9M11
Revenue	14,168	41,124	14,015	40,971	-1.1%	-0.4%
EBITDA	5,706	15,606	5,198	15,098	-8.9%	-3.3%
EBITDA margin (%)	40.3%	37.9%	37.1%	36.9%		
Net profit	2,468	6,297	1,562	5,391	-36.7%	-14.4%

Source: Bloomberg, STC

Income statement

SRm	FY09A	FY10A	FY11F	FY12F	FY13F
Revenue	50780	51787	54878	56800	58789
Cost of sales	-19779	-21449	-22775	-23572	-24398
Operating costs	-10388	-10712	-11799	-12496	-13228
EBITDA	20612	19625	20305	20732	21164
DDA & Impairment (ex gw)	-7799	-8645	-9502	-9575	-9672
EBITA	12814	10981	10803	11158	11492
Goodwill (amort/impaird)	0.00	0.00	0.00	0.00	0.00
EBIT	12814	10981	10803	11158	11492
Net interest	-1023	-1497	-1421	-1063	-406.1
Associates (pre-tax)	0.00	0.00	0.00	0.00	0.00
Other pre-tax items	340.1	2053	474.2	287.4	78.1
Reported PTP	12130	11537	9856	10382	11164
Taxation	-976.6	-1493	-887.0	-934.4	-1005
Minority interests	-290.5	-603.8	-627.8	-661.4	-711.2
Other post-tax items	0.00	0.00	0.00	-0.00	0.00
Reported net profit	10863	9440	8341	8787	9448
Tot normalised items	0.00	0.00	0.00	0.00	0.00
Normalised EBITDA	20612	19625	20305	20732	21164
Normalised PTP	12130	11537	9856	10382	11164
Normalised net profit	10863	9440	8341	8787	9448

Source: Company data, Rasmala forecasts

year to Dec

Balance sheet

SRm	FY09A	FY10A	FY11F	FY12F	FY13F
Cash & market secs (1)	7422	5904	14000	23975	37143
Other current assets	14918	12762	16087	17437	18121
Tangible fixed assets	53026	55135	54916	54272	53138
Intang assets (incl gw)	28916	31806	31806	31806	31806
Oth non-curr assets	4990	5101	5101	5101	5101
Total assets	109272	110709	121910	132592	145309
Short term debt (2)	0.00	0.00	0.00	0.00	0.00
Trade & oth current liab	29519	26642	30662	32295	34052
Long term debt (3)	22254	21736	25849	19349	13049
Oth non-current liab	6703	8863	8963	9063	9163
Total liabilities	58475	57241	65474	60707	56265
Total equity (incl min)	50797	53468	56437	71884	89044
Total liab & sh equity	109272	110709	121910	132592	145309
Net debt	23893	24284	18783	1874	-17794

Source: Company data, Rasmala forecasts

year ended Dec

Cash flow statement

SRm	FY09A	FY10A	FY11F	FY12F	FY13F
EBITDA	20612	19625	20305	20732	21164
Change in working capital	-2570	-110.8	2213	717.0	1274
Net interest (pd) / rec	-695.9	-1102	-1421	-1063	-406.1
Taxes paid	-832.3	-976.6	-938.8	-887.0	-934.4
Other oper cash items	-1110	203.9	-887.0	-934.4	-1005
Cash flow from ops (1)	15404	17640	19271	18565	20093
Capex (2)	-13542	-13046	-9283	-8931	-8537
Disposals/(acquisitions)	0.00	0.00	0.00	0.00	0.00
Other investing cash flow	-432.7	326.2	208.7	0.00	0.00
Cash flow from invest (3)	-13975	-12720	-9074	-8931	-8537
Incr / (decr) in equity	0.00	0.00	0.00	0.00	0.00
Incr / (decr) in debt	0.00	0.00	2404	2465	2371
Ordinary dividend paid	-5943	-6109	-6000	-6000	-7000
Preferred dividends (4)	0.00	0.00	0.00	0.00	0.00
Other financing cash flow	3874	-328.8	1495	3923	6312
Cash flow from fin (5)	-2069	-6438	-2101	387.8	1683
Forex & disc ops (6)	0.00	0.00	0.00	-47.4	-70.4
Inc/(decr) cash (1+3+5+6)	-639.5	-1518	8096	9975	13168
Equity FCF (1+2+4)	1862	4594	9988	9634	11555

Source: Company data, Rasmala forecasts

year to Dec

Recommendation structure

Absolute performance, long term (fundamental) recommendation: The recommendation is based on implied upside/downside for the stock from the target price and only reflects capital appreciation. A Buy/Sell implies upside/downside of 10% or more and a Hold less than 10%.

Performance parameters and horizon: Given the volatility of share prices and our pre-disposition not to change recommendations frequently, these performance parameters should be interpreted flexibly. Performance in this context only reflects capital appreciation and the horizon is 12 months.

Market or sector view: This view is the responsibility of the strategy team and a relative call on the performance of the market/sector relative to the region. Overweight/Underweight implies upside/downside of 10% or more and Neutral implies less than 10% upside/downside.

Target price: The target price is the level the stock should currently trade at if the market were to accept the analyst's view of the stock and if the necessary catalysts were in place to effect this change in perception within the performance horizon. In this way, therefore, the target price abstracts from the need to take a view on the market or sector. If it is felt that the catalysts are not fully in place to effect a re-rating of the stock to its warranted value, the target price will differ from 'fair' value.

Valuation and risks to target price

STC (RIC: 7010.SE, Rec: Buy, CP: SR36.10, TP: SR47.70): We initiate coverage on STC with a target price of SAR47.7 per share, which is calculated based on a sum-of-the-parts, DCF valuation. Risks to our valuation include increased domestic competition in both the mobile and data front, as well as foreign currency fluctuations given the growing revenue contribution from STC's international expansions.

Disclaimer

This report is prepared by Rasmala Investment Bank Limited ("RIB"). RIB is regulated by the Dubai Financial Services Authority ("DFSA"). RIB products or services are only made available to customers who RIB is satisfied meet the regulatory criteria to be a "Professional Client", as defined under the Rules and Regulations of the Dubai International Financial Centre ("DIFC").

Our investment recommendations take into account both risk and expected return. We base our long-term fair value estimates on a fundamental analysis of a company's future prospects, after having taken perceived risks into consideration. We have conducted reasonable research to arrive at our investment recommendations and fair value estimates for the company or companies mentioned in this report. Although the information in this report has been obtained from sources that RIB believes to be reliable, we have not independently verified such information thus it may not be accurate or complete. RIB does not represent or warrant, either expressly or impliedly, the accuracy or completeness of the information or opinions contained within this report and no liability whatsoever is accepted by RIB or any other person for any loss howsoever arising, directly or indirectly, from any use of such information or opinions or otherwise arising in connection therewith.

Readers should understand that financial projections, fair value estimates and statements regarding future prospects may not be realized. All opinions and estimates included in this report constitute our judgment as of this date and are subject to change without notice. This research report is prepared for general circulation and is intended for general information purposes only. It is not intended as an offer or solicitation or advice with respect to the purchase or sale of any securities referred to in the report. It is not tailored to the specific investment objectives, financial situation or needs of any specific person that may receive this report. We strongly advise potential investors to seek financial guidance when determining whether an investment is appropriate to their needs.

RIB is not registered with the U.S. Securities and Exchange Commission, or any U.S. state authority, as a broker-dealer or investment advisor. This report has not been approved, disapproved or recommended by the U.S. Securities and Exchange Commission, any state securities commission in the United States, the securities commission of any non-U.S. jurisdiction or any other U.S. or non-U.S. regulatory authority. None of these authorities has passed on or endorsed the merits or the accuracy or adequacy of this report.

RIB and its group entities (together and separately, "Rasmala") does and may seek to do business with companies covered in its reports. As a result, users should be aware that the firm may have a conflict of interest that could affect the objectivity of this report. Investors should consider this report as only a single factor in making their investment decision. Rasmala and its respective employees, directors and officers shall not be responsible or liable for any liabilities, damages, losses, claims, causes of action, or proceedings (including without limitation indirect, consequential, special, incidental, or punitive damages) arising out of or in connection with the use of this report or any errors or omissions in its content.

The research analyst or analysts responsible for the content of this research report certify that: (1) the views expressed and attributed to the research analyst or analysts in the research report accurately reflect their personal opinion(s) about the subject securities and issuers and/or other subject matter as appropriate; and, (2) no part of his or her compensation was, is or will be directly or indirectly related to the specific recommendations or views contained in this research report. On a general basis, the efficacy of recommendations is a factor in the performance appraisals of analysts.