Saudi Telecom
Telecom – Industrial
STC AB: Saudi Arabia
10 August 2022

الراجحي المالية
Al Rajhi Capital

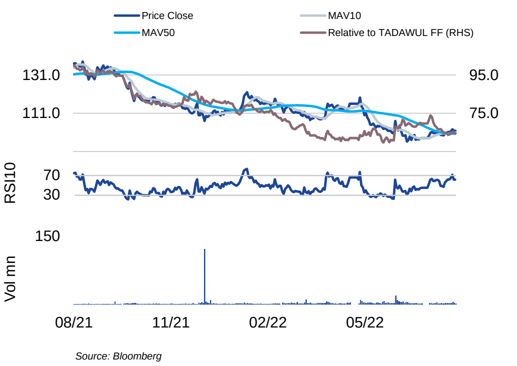
US$54.2bn	30%	US$95.92mn
Market cap	Free float	Avg. daily volume

Target price	114.00	+12% over current
Current price	102.20	as at 9/8/2022

Existing rating

Underweight | Neutral | **Overweight**

Performance



Earnings

(SAR mn)	2021	2022E	2023E
Revenue	63,417	69,035	73,597
Y-o-Y	7.6%	8.9%	6.6%
Gross Profit	33,794	37,357	39,826
Gross margin	53.3%	54.1%	54.1%
EBITDA	22,841	24,931	26,799
EBITDA margin	36.0%	36.1%	36.4%
Net profit	11,311	13,084	14,442
EPS (SAR)	5.66	6.54	7.22
DPS (SAR)	4.00	4.00	4.00
EV/EBITDA	8.9	8.1	7.6
P/E	18.0	15.6	14.1

Source: Company data, Al Rajhi Capital

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STC

Favourable valuation; Upgrade to an overweight rating with a TP of SAR114/share.

In the first half of 2022, revenue grew by 7.4% y-o-y and growth was seen across all segments with the enterprise segment growing in double-digit. Gross margin improved slightly to 54% (53.5% in 1H2021). Operating profit stood at SAR7.5bn a 22.2% margin compared to 21.3% (12% y-o-y growth), EBITDA rose by 9% to reach SAR12.5bn and EBITDA Margin at 36.9% compared to 36.3% for the 1H2021. Net profit reached SAR5.9bn in 1H22 with 17.3% margin despite recording SAR512mn impairment of its investment (Adjusted NI SAR6.4bn and 18.8% margin) vs SAR5.8bn in 1H21 and an 18.3% margin. Moreover, given the company's capex plans, a special dividend is unlikely this year further worsening the already weak sentiment. The stock has seen considerable correction and we think that most of the negatives are already factored into the price such as "high interest-rate-environment" which is affecting the cost of equity and low expectations for special dividend. As such we do not see any major downside from current levels. We revised our TP to SAR114/sh from SAR120/sh. This translates to a 12% upside from the CMP of SAR102.2/sh and an overweight rating.

2Q results.

The 2Q22 revenue came closely in line with our estimate, while cost of revenue was lower than expected which positively reflected in the quarter's profitability, boosting EBITDA to SAR6.2bn, a growth of (10.3% y-o-y). However, the strong growth in EBITDA is slightly distorted by the lower base comparison of 2Q21 which at that time the recovery from the pandemic was weak. Gross margin improved both y-o-y and q-o-q and could be attributed to 1) the change in the segment contribution to total revenue as enterprise segment is growing 2) better pricing in the enterprise segment as its leading the growth in the company (16% y-o-y), which got positively affected from the economic recovery after the pandemic.

Figure 1 STC Q2 2022 results

(SAR mn)	2Q 2022	2Q 2021	Y-o-Y	1Q 2022	Q-o-Q	ARC est	vs ARC
Revenue	16,939	15,899	6.5%	16,991	-0.3%	17,020	-0.5%
Gross profit	9,174	8,352	9.8%	9,150	0.3%	9,021	1.7%
Gross margin	54.2%	52.5%		53.9%		53.0%	
Operating profit	3,720	3250.3	14.5%	3,824	-2.7%	3,587	3.7%
Operating margin	22.0%	20.4%		22.5%		21.1%	
Net profit	2,837	2,872	-1.2%	3,122	-9.1%	3,069	-7.5%
Net margin	16.7%	18.1%		18.4%		18.0%	

Source: Company data, Al Rajhi Capital

Valuation and risks: We arrived at our 12m forward-looking target price for the company using an equal mix of DCF and EV/EBITDA. The DCF target price is based on a 2.0% terminal growth and a WACC of 8.73% reaching to SAR115/sh. The EV/EBITDA is based on 9x (which is close to its 5-year average) gives a SAR113/sh. Overall, we reduced our target price to SAR114/sh. Based on our TP, we have an overweight rating. Upside risks to our valuation are, increase in data prices, lower than expected capex spends, payment from Government for receivables, lower cost of goods sold, further material traction in fintech boosting cash flows. Downside risks are impairment of receivables, higher than expected capex, increase in competition in consumer and business segments and rise in SAIBOR which could put the stock price under pressure as investors ask for higher yield.

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"Overweight": Our target price is more than 10% above the current share price, and we expect the share price to reach the target on a 12 month time horizon.

"Neutral": We expect the share price to settle at a level between 10% below the current share price and 10% above the current share price on a 12 month time horizon.

"Underweight": Our target price is more than 10% below the current share price, and we expect the share price to reach the target on a 12 month time horizon.

"Target price": We estimate target value per share for every stock we cover. This is normally based on widely accepted methods appropriate to the stock or sector under consideration, e.g. DCF (discounted cash flow) or SoTP (sum of the parts) analysis.

Please note that the achievement of any price target may be impeded by general market and economic trends and other external factors, or if a company’s profits or operating performance exceed or fall short of our expectations.

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