PSG Wealth

MTN

Communication services

Company Update Report

Buy

MTN Nigeria continues to struggle due to the persistent weakness of the naira

Analyst recommendation

Counter	Share price	Intrinsic value	Upside
MTN-ZA	R81	R92	13% upside

As of 23 November 2024

Executive summary

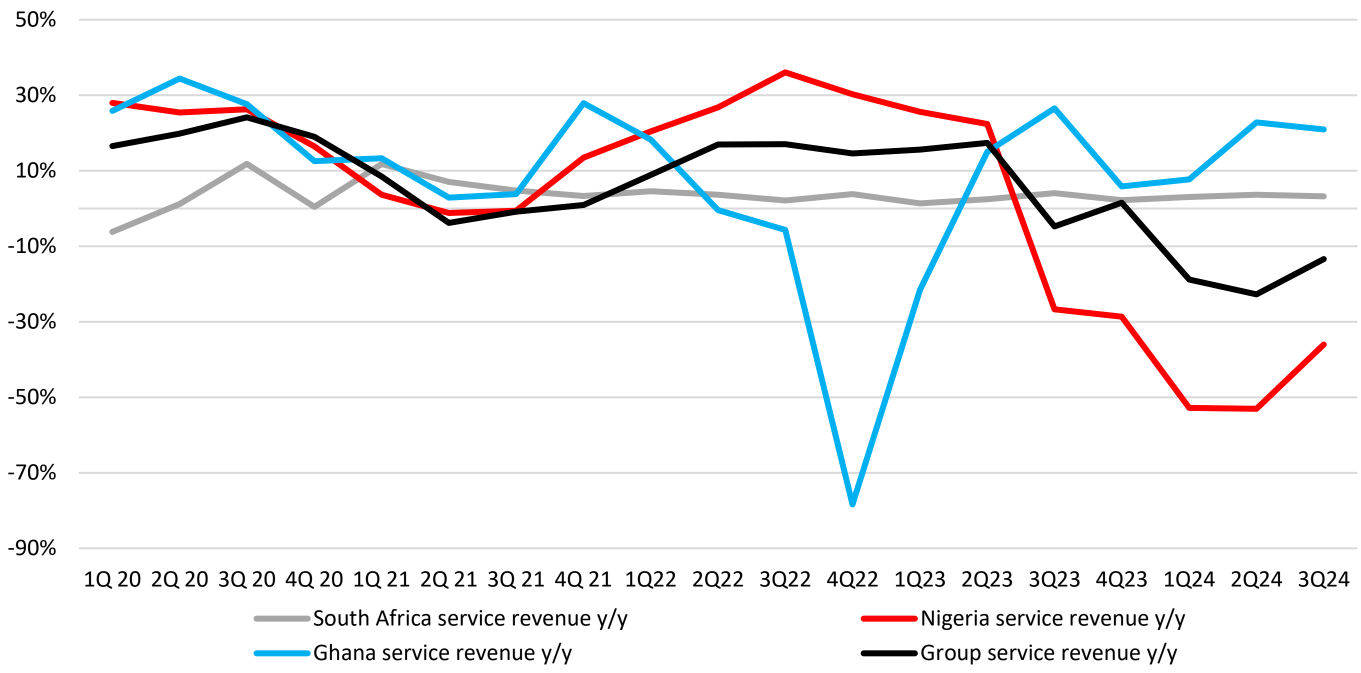
- Top line was in line with management expectations, but cost inflation was elevated in this period from various Opcos weighing in on margins which were impacted by currency volatility and conflict in Sudan.
    - Blended inflation of 13.9% in 3Q24 compared to 17.1% in 3Q23.
    - Group EBITDA increased by 3.4%. The EBITDA margin declined by 9 percentage points (pp) to 33.8%
- The balance sheet remains robust. Group net debt/EBITDA at the holding company (Holdco) level held firm at 0.8x as of 30 September 2024 (31 December 2023: 0.4x).
    - Up streamed cash of R2.2 billion from MTN operating companies over the quarter.
    - The ongoing conflict in Sudan has resulted in disruptions to service delivery and a decline in the customer base, contributing to the revenue shortfall in the MENA region.
    - Despite facing challenges, MTN sustains a robust liquidity position of R32.1 billion as of 30 September 2024.
    - The board anticipates a dividend of 330 cents per share for FY24.
    - MTN has successfully concluded the sale of its South African tower infrastructure, transferring more than 5 700 towers to IHS Towers (NYSE: IHS)
- Intrinsic value of R92.
    a. We update our expectations given the recent devaluation in the naira.
    b. Our bull case is still supported by the inherent valuation in the Fintech business, and we saw a glimpse of that in the recent Mastercard offer.

Analyst thesis

- The current price is discounting no value for MTN Nigeria (R14 of the R92 IV), previously was R18 resulting in our positive view on the asymmetric upside. Indeed, most of the WECA valuation is ignored by the market too.
- Due to the sharp devaluation of the naira, this ultimately results in a higher cost of doing business which affects the entire business model and makes it harder to drive margin recovery.
- Even though Nigeria offers potential advantages, the uncertainty or risk remains high, and there's no known trigger at this moment that would alleviate that risk perception.
- The asset realization process needs to continue which should streamline the portfolio, reduce debt and risk, and enhance returns.
- A significant risk remains MTN's material exposure to forex. The sum of the parts (SOTP) valuation shows that 29% of the exposure comes from South Africa, and the rest is volatile currencies and inflation exposure.

Results

Graph 1: Major opcos service revenue (y/y %): South Africa (in rands)



Source: Company reports

Key trends:

In 3Q24, group service revenue decreased by 13.4% compared to the same period last year.

- The miss was impacted by MTN Nigeria as a result amidst increasing inflation and continued naira volatility.
- MTN SA's EBITDA grew by 2.6% in the quarter.
- MTN SA's EBITDA margin decreased by 0.2pp to 36.4% (down 0.1pp to 36.3% excluding gain on disposal of towers).

Table 1: Service revenue and adj. EBITDA versus expectation

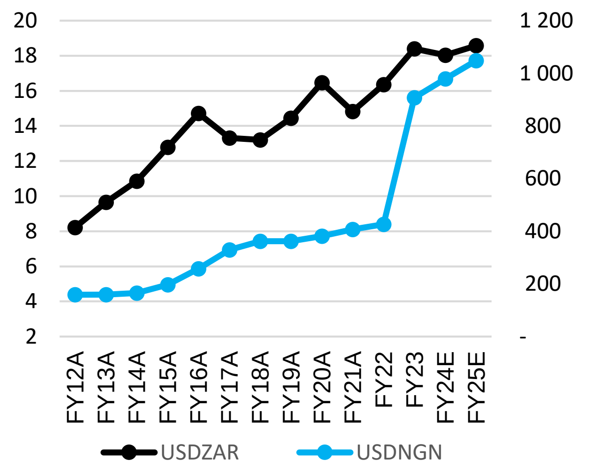
ZAR Mn group	3Q23	2Q24	3Q24	% QoQ	3Q24e	Actual versus estimate
Service revenue	48 307	43 139	42 426	-2%	42 153	1%
Revenue	50 653	45 889	44 774	-2%	44 524	1%
EBITDA adj	20 901	11 751	16 645	42%	16 738	-1%
EBITDA adj. margin	41.1%	26.0%	37.5%	-	37.4%	-
Capex (ex Leases)	8 924	8 221	6 235	-24%	5 788	-
Capex intensity (%)	17.6%	17.9%	13.9%	-	13.0%	-
Subscribers ('000)	283 426	287 086	287 827	0%	287 773	0%
South Africa	**3Q23**	**2Q24**	**3Q24**	**% QoQ**	**3Q24e**	**Actual versus estimate**
Service revenue	10 562	10 697	10 907	2%	10 882	0%
Revenue	12 664	13 232	13 085	-1%	13 049	0%
EBITDA adj	4 693	4 835	4 712	-3%	4 791	-2%
EBITDA adj. margin	37.1%	36.5%	36.0%	-	36.7%	-
Subscribers ('000)	36 798	38 465	39 225	2%	38 407	2%
Postpaid (incl Telemetry)	8 997	9 437	9 709	3%	9 633	1%
Prepaid	27 801	29 028	29 516	-2%	28 774	3%

Source: Standard Bank report

MTN Nigeria

- As of September 2024, the naira closed at N1 542/US$ on the Nigerian Autonomous Foreign Exchange Market (NAFEM), a sharp increase from N907/US$ in December 2023, putting strain on business activities.
- MTN Nigeria's guidance is to drive margin recovery and strengthen its balance sheet.
- Fintech revenue grew by 16.8% spurred by XtraTime.
- Impact of naira devaluation and VAT on tower leases, exacerbated by ongoing inflationary pressures.
- It's worth noting that the company had already repatriated funds out of MTN at naira 600 per USD and the depreciation is less pronounced but it's still detrimental as it's about 40% of the company's operating cost are US dollar tied.
- Over the medium term, a decrease in free cash flow as a lower contribution from MTN Nigeria.
- Inflation is also likely to remain elevated due to the fuel subsidy removal that could further put pressure on margins. This is before any cost savings or additional improvement to top line growth.
- The group announced an additional expense efficiency program of between R7bn to R8bn additional efficiencies over the next three years (from 2024 onwards). This program is group wide, on all opcos but it plays a major role in protecting margins in Nigeria and group level.

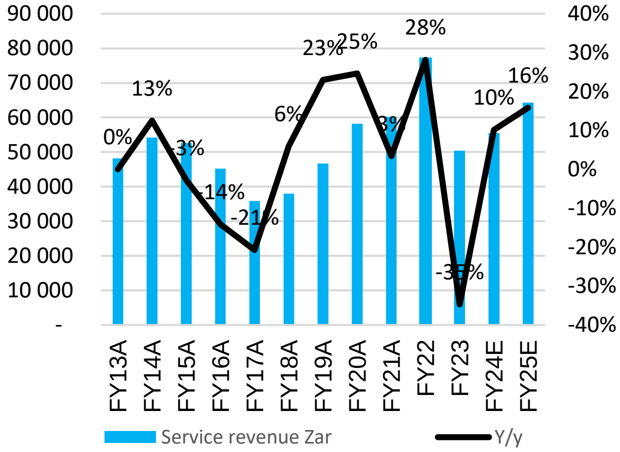
Graph 2: Naira (Rhs) versus USD and rand versus USD (Lhs)



Source: PSG Wealth

A = Actual, E = FactSet consensus expectation

Graph 3: Nigeria service revenue growth



Source: PSG Wealth

Fintech

- MTN has secured agreements with Mastercard for a minority investment of up to $200 million in MTN Group Fintech, valued at $5.2 billion on a cash and debt-free basis.
- The market cap of MTN is about R151.50 billion with an implied fintech value of R98 billion.
- The deal implies a EV/EBITDA of roughly 14.4 times on a historical basis and on a forward basis range of between 10 times to 12 times based on consensus basis. In our valuation, we still have the valuation at EV/EBITDA at 12 times, rationale, reinforced by this deal.
- This deal was less about cash and more about finding a strategic partner to scale up the business. Cited by the company, the partnership will support a number of verticals.
  - Issuance: Mastercard state-of-the-art technology & global network will enable MoMo users to create virtual cards linked to primary MoMo wallets.
  - Acceptance: will enable group fintech merchants to accept Mastercard payments as a trusted and universally recognised payment method.
  - Remittances: Accelerates group fintech's scale and scope as remittances player.

Balance sheet

- The group's net-debt-to-EBITDA of 0.8x as of 30 September 2024 (31 December 2023: 0.4x), remained well within covenant of 2.5x.
- Holdco leverage held firm at 1.8x (30 September 2024), supported by cash up streamed and localisation proceeds.
- Up streamed cash of R2.2 billion from our operating companies for the 3Q24.
- MTN Nigeria repatriated R987 millions of localisations proceeds from MTN Nigeria in Q1. Elected for a scrip dividend option increase the group's effective shareholding from 75.6% to 76.3%. Signs of cash repatriation issue.
- MTN realised approximately R600 million in gross localisation proceeds from MTN Ghana in Q3, bringing the total YTD proceeds from localisations to approximately R2.3 billion.

Valuation

Table 2: Sum of the parts valuation

Region	Stake	Ebitda 2025	EV/EBITDA	Disc equity value	Value per share	Contribution
South Africa*	100%	19 156	3.5	49 939	27	29%
Nigeria*	76%	18 686	2.0	25 291	14	15%
SEA		**37 841**	**2.0**	**75 229**	**4**	
Uganda	83%	3 630	2.0	3 492	2	2%
Rwanda	80%	1 873	1.5	1 994	1	1%
Zambia	90%	1 100	2.0	1 561	1	1%
South Sudan	100%	1 034	1.5	1 101	1	1%
WECA		**14 381**	**1.9**	**26 814**	**15**	
- Cote d'Ivoire	67%	2 229	2.5	4 156	2	2%
- Cameroon	80%	1 825	2.5	3 403	2	2%
- Ghana	81%	10 327	2.5	19 254	10	11%
MENA		**1 034**	**1.5**	**1 551**	**11**	
Sudan	85%	1 034	1.5	1 551	1	1%
Joint ventures		3 838	2.5	9 519	5	
- Iran	49%	3 492	2.5	8 730	5	**5%**
- Botswana	53%	289	2.2	637	0	0%
- Swaziland	30%	56	2.7	152	0	0%
Fintech Buisness***		8 721	10.0	66 240	36	39%
Equity-accounting exclusion		- 4 286	1.5	- 6 429	- 3	-4%
Head offices, GlobalConnect and eliminations		- 1 393	1.5	- 2 090	- 1	-1%
Group		**69 959**	**3.6**	**187 500**	**102**	

Asset sales				16 760	9	10%
Net debt				- 34 900	- 19	-21%
Equity value				169 360	92	100%
# Shares				1 847		
Per share						
Intrinsic value				92		
Share price				81		
Upside (downside)				13%		

Source: PSG Wealth research

*Excludes Fintech |All Fintech operations

Table 3: Bear. base and bull scenarios

Scenarios	Share price	Multiple	Upside/downside	Scenarios prob
Bear case	R79	3.2	-3%	45%
Base case	92	3.6	13%	35%
Bull case	R117	4.5	44%	20%
Value per share				R92.00
Share price				R81.00
upside (downside)				13%

Source: PSG Wealth research

Table 4: Qualitative summary

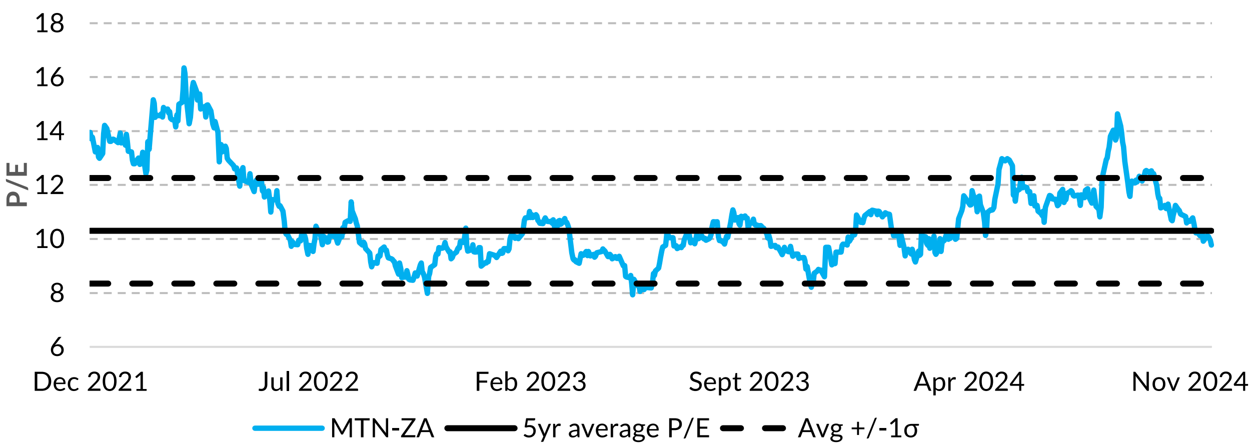
Factor review	Rating	Description
Growth		• Key markets are affected by currency devaluation. • MTN Rwanda affected by zero-termination rates. • Impact of NIN-SIM regulations.
Valuation		We value the company on a forward EV/EBITDA multiple of 3.6x with a 13% upside.
Dividend yield		The dividend yield for MTN Group Limited is 4.2%.
Issuance		No issuance of additional shares over the past year.
Catalyst	• Mastercard offer to leverage on Fintech business. • De-leveraging the balance sheet. • Continued to leverage partnerships to scale platforms.	
Quality of earnings		• Devaluation of the Naira causes a higher cost of doing business. • Margins are affected due to intense market competition and increase in energy costs and rise of inflation. • MTN operates in many African countries, and fluctuations in exchange rates affect profitability.
Moat		Moat: MTN operates mainly as a number one operator in key markets.
Management and governance		Group Executive Committee changes.
Balance sheet		• Robust liquidity position of R32.1 billion. • Group net-debt-to-EBITDA ratio of 0.8x
Risks	• MTN has material exposure to forex. In the SOTP valuation, 29% of the exposure comes from South Africa and the rest is volatile currencies and inflation exposure e.g. the naira. • Recently, we have seen growing levies on mobile money as telcos earned high margins. • Cash repatriation from the various countries. Issues of currency reserves of hard currency. • Increasing forecasting risk, currency volatilities major regions. • Starlink poses a risk to telecommunications sector by offering alternative broadband service.	
Regulation		The sector is heavily regulated—fines and penalties can be massive. Additionally, regulators have been an issue when it comes price increase implementation
ESG		MTN achieved a 13.1% absolute reduction in Scope 1 and 2 emissions (tCO2e), exceeding the 2023 target of 7.5%.
Momentum price		Price momentum is negative.
Momentum earnings		In the last three months, earnings revision has been revised downwards by 81.1%.
Piotroski score		Achieved an average score of 4.0.

Source: PSG Wealth research

Table 5: Company data

52-week high	R118.00
52-week low	R70.43
Market value (bn)	R151.5
Price momentum	Negative
3m earnings revision	-81.1%
Fiscal year end	2024/12/31

Graph 5: Price to earnings



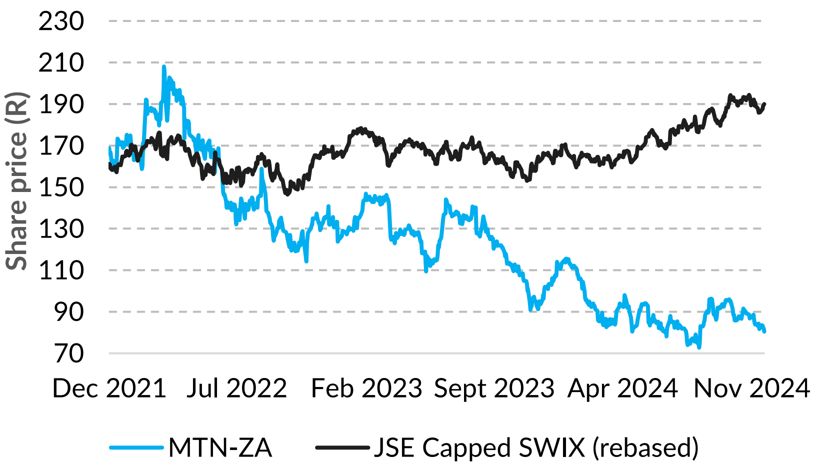
Source: FactSet

Table 6: Valuation multiples

Multiple	Latest: Nov-2024	Last note: Jul-2023
P/E	9.8x	10.0x
P/S	0.7x	1.1x
P/B	1.1x	1.7x
P/CF	2.2x	4.6x
EV/EBITDA	2.8x	3.4x
EV/EBIT	5.5x	5.6x
EV/SALES	1.1x	1.5x
Dividend yield	4.2%	2.7%
FCF yield	3.9%	11.1%

Source: FactSet

Graph 6: Share price history versus benchmark



Source: FactSet

Table 7: Performance versus benchmark

Period	YTD	MTD	3M	6M	1Y	2Y	3Y	5Y	10Y
MTN Group Limited	-30.4%	-8.1%	-16.2%	-6.1%	-20.0%	-40.6%	-50.6%	-14.8%	-64.4%
JSE Capped SWIX	11.4%	0.3%	1.4%	8.5%	15.7%	14.2%	19.2%	37.7%	36.9%

Source: FactSet

Table 8: Key competitors

Company	Code	Price (local)	Market cap (Rbn)	Sales FY0 (Rbn)	EBIT FY0 (Rbn)	Net income FY0 (Rbn)	EV/EBIT	P/E	Price % (3mo)	Price % (1YR)
MTN Group Limited	MTN-ZA	80.4	151	210	47	4	5.5x	9.8x	-16.2%	-20.0%
Telkom SA SOC Ltd.	TKG-ZA	32.1	16	42	4	2	6.9x	7.4x	19.0%	12.1%
Vodacom Group Limited	VOD-ZA	102.5	213	151	35	16	7.2x	10.4x	-9.8%	-2.9%

Table 9: Key financials and ratios

Source: FactSet

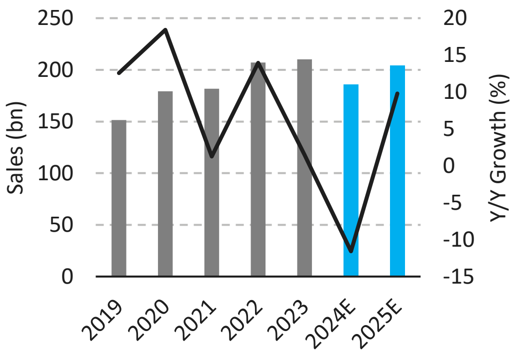
Income statement (ZAR bn)	2017	2018	2019	2020	2021	2022	2023	5Yr CAGR	2024E	2025E
Sales	132.8	134.6	151.5	179.4	181.6	207	210.1	9.32%	196.8	220.9
Y/y growth (%)	-	1.3	12.6	18.4	1.3	14	1.5	-	-6.4	12.3
EBITDA	44.9	48.2	64.1	81.3	79.4	89.9	88.8	-	75.6	87.7
Y/y growth (%)	-	7.4	32.8	26.9	-2.4	13.2	-1.2	-	-14.8	16
EBIT	20.6	23.6	31.6	45.7	43.8	54.9	46.5	12.97%	38.7	47.6
Y/y growth (%)	-	14.7	34.2	44.3	-4.1	25.4	-15.2	-	-16.8	22.9
Net income	4.4	8.7	9	17	17.6	19.3	10.7	14.56%	11.7	17.3
Y/y growth (%)	-	97.5	2.8	89.9	3.4	9.8	-44.6	-	8.9	48.5
EPS	1.8	3.4	4.7	7.5	10.1	10.4	3.1	4.19%	7.2	9.6
Y/y growth (%)	-	85.2	38.9	60	34.2	3.9	-69.8	-	130	33

Balance sheet and cash flow (ZAR bn)	2017	2018	2019	2020	2021	2022	2023	5Yr CAGR	2024E	2025E
Capex	31.4	26.1	27	33	32.6	52.6	46.7	12.38%	41	43.9
Cash from operations	36.3	31.7	36.3	58.5	59.5	68.1	55.7	11.95%	41.7	57.7
Free cash flow	9.6	10.4	18.1	22.7	21.4	32.3	22.0	16.10%	12.9	24.8
Y/y growth (%)	-	8.7	73.3	25.7	-6	51.1	-31.9	-	-41.4	92.6
Cash and ST Investments	16	15.2	21.7	31.6	35.2	44.4	23.2	8.76%	11.1	9.5
Total assets	242.4	244.6	302.3	348.9	359.3	391.9	405.7	10.65%	411.9	423.1
ST debt	9.2	12.4	19.9	23.5	21.9	22.1	38.1	25.12%	28.1	28.1
LT debt	71.2	73.2	120.7	122.2	106.9	118.3	110.3	8.55%	55.9	55.9

Ratios (ZAR bn)	2017	2018	2019	2020	2021	2022	2023	5Yr CAGR	2024E	2025E
EBIT margin (%)	15.5	17.5	20.9	25.5	24.1	26.5	22.1	23.8	19.7	21.5

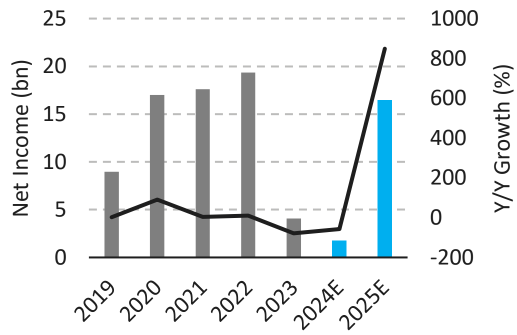
Net income margin (%)	3.3	6.5	5.9	9.5	9.7	9.3	5.1	7.9	5.9	7.8
Current ratio	0.9	0.8	0.9	1	1	1	0.9	0.9	-	-
Total debt to equity	85.3	101	167.6	141.7	116	120.4	106.6	130.5	-	-
Total debt to assets	32.9	33.3	46.5	41.8	35.2	35.8	34.1	38.7	-	-
ROA (%)	1.7	3.5	3.3	5.2	3.8	5.1	1.0	3.7	-	-
ROE (%)	4.5	9.7	10.8	18.2	12.9	17	3.2	12.4	-	-

Graph 7: Annual sales



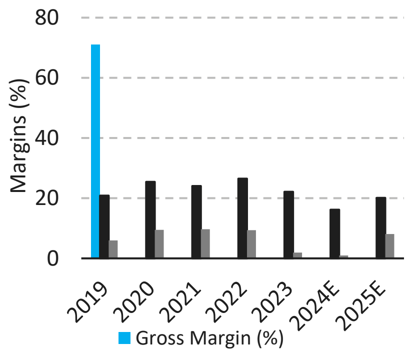
Source: FactSet

Graph 8: Annual net income



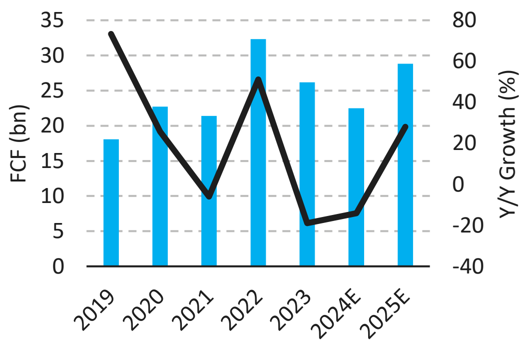
Source: FactSet

Graph 9: Gross. EBIT. net margins



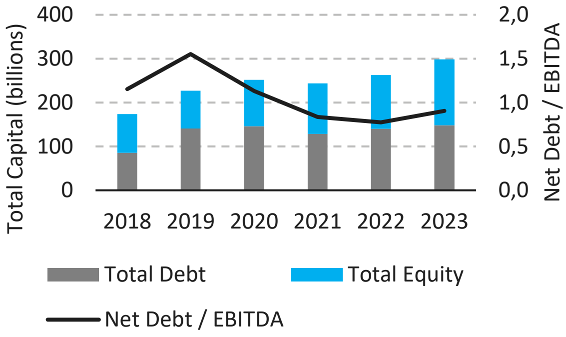
Source: FactSet

Graph 10: Free cash flow



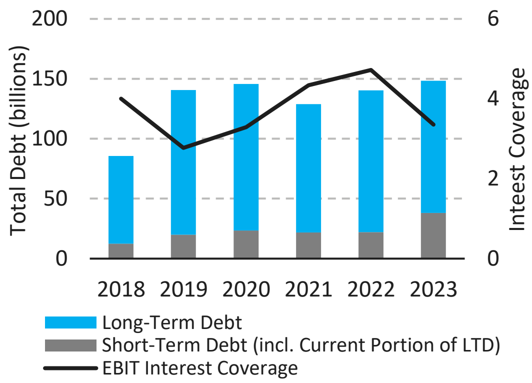
Source: FactSet

Graph 11: Capital structure and net debt/EBITDA



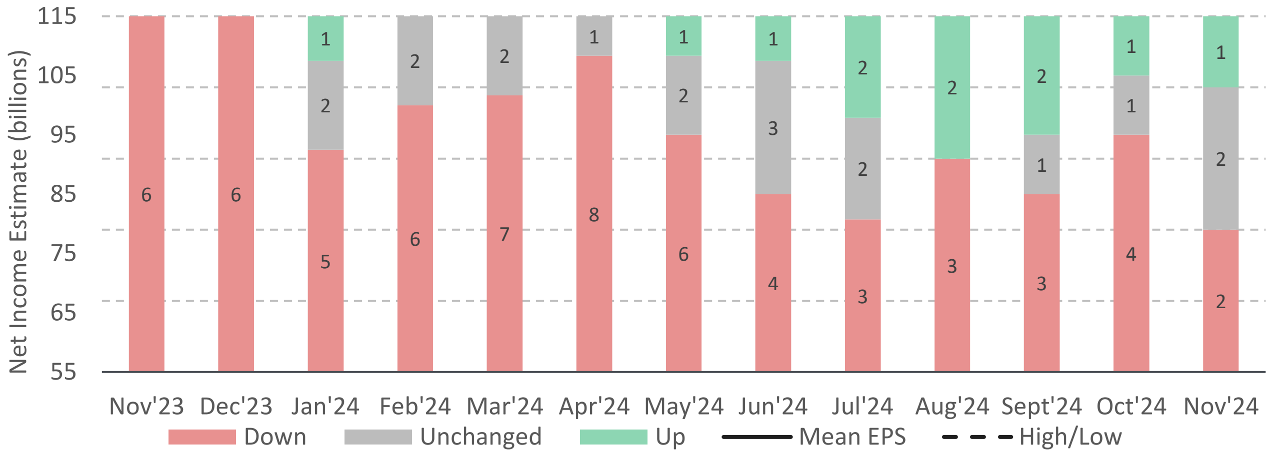
Source: FactSet

Graph 12: Total debt and interest coverage



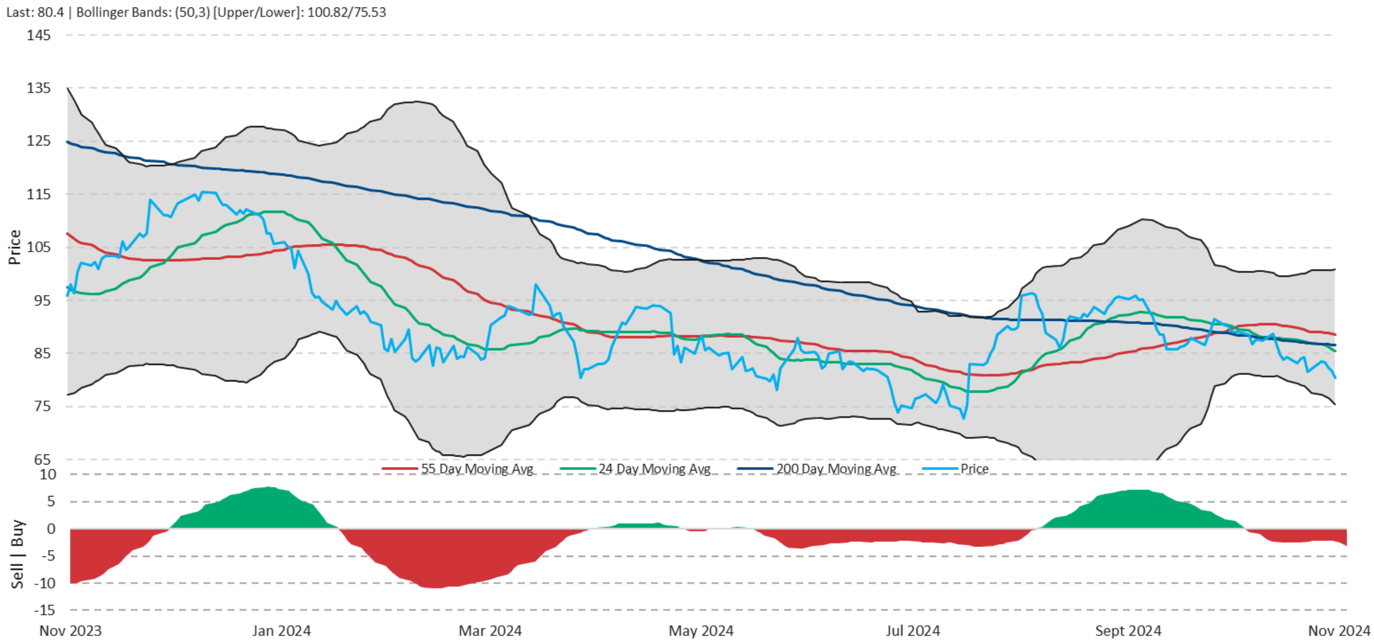
Source: FactSet

Graph 13: Earnings revision



Source: FactSet

Graph 14: Price momentum



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House view guidance: House view guidance is indicative only. Each client's circumstances are different. and it remains critical that indicative guidance is discussed with your portfolio manager or financial adviser.
Date and share price: The date the report was reviewed and approved by the portfolio committee is likely to precede the release date and price on the report.

*Share price as at closing.

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