Conference Call Transcript

13 November 2023

INTERIM RESULTS ANALYST CALL

Operator

Welcome to the Vodacom Group Limited results conference call for the six months ended 30 September 2023. Vodacom Group CEO, Shameel Joosub, will host the conference call. Before I hand the call over to Shameel, we would like to ask that you refer to and familiarise yourself with Vodacom's forward looking disclaimer. This is set out on slide 39 of the interim results presentation and can be located on www.vodacom.com. Alternatively, if you would like a copy of the results announcement or presentation sent to you, please email investorrelations@vodacomir.co.za. Participants on this conference call are in listen-only mode and there will be an opportunity to ask questions later in the conference. Also note that this event has been recorded. I would now like to hand the conference over to Shameel. Please go ahead, sir.

Shameel Joosub

Thank you. Good afternoon and good morning to those joining the call in the US. I'm joined by our group CFO, Raisibe Morathi, as well as our Head of Investor Relations, JP Davids. Our group operates across eight markets in Africa with a combined population of more than 500 million people. Based on the performance in the first six months, our consolidated operations are on track to deliver around R150 billion of revenue this financial year.

Further, our 35% stake in Safaricom provides exposure to another major source of revenue and growth on the continent. Our diversified footprint and product suite is supporting excellent revenue growth, and we are tracking at the top end of our medium-term target. Higher interest rates, elevated levels of inflation and currency volatility did however weigh on the group's earnings in the period.

To mitigate these headwinds, we are accelerating cost savings into the second half to accelerate EBITDA growth. Vodacom is a purpose-led company and we connect for a better future. To deliver lasting societal value, we have developed tech for good platforms across energy, healthcare, education, and agriculture. This reporting period, we showcased our healthcare platform in Egypt, where we are leading the universal health insurance and the Egyptian university programmes. We are digitizing medical records and hospital and insurance information to drive seamless delivery of medical care and improve outcomes for beneficiaries. This platform is live across 270 hospitals and serves over 6 million people. It also provides a case study for healthcare across the continent.

Over and above our three purpose pillars, we step up when it matters. In the period, we donated healthcare packages following a cholera outbreak in South Africa. In the DRC, following a devastating flood, we provided free connectivity and free M-PESA transfers in the regions to affected customers. Our steadfast agenda on financial inclusion for all has seen us reach 74 million financial service customers, up an impressive 16.4%.

I'm particularly excited about the structural growth opportunity of the recent launch of M-PESA in Ethiopia. And alongside our growth in our agent and merchant networks, we are scaling our super apps, VodaCash, VodaPay, and M-PESA.

In my presentation this morning, I also provided an update to our strategy called the System of Advantage. I revisited the investment cases and progress we are making in Vodafone Egypt and Ethiopia and discussed some of the key variables for these assets. Despite the big move in the Egyptian Pound since we announced the transaction in 2021, I'm pleased to report that Vodafone Egypt was earnings accretive in the first half. This was testament to the resilient margin of the business, helped by owning its towers and localising of costs.

I also discussed how we have transformed Vodacom into a data-led organisation. Big data is the engine of our digital ecosystem and supports our customer value management, loyalty and financial services. One of the most exciting aspects of our big data and AI capabilities is our 360 degree view of the customer. This is where the power of data pulls together insights from telco, financial services, and loyalty to drive our global recommender engine, which is using predictive AI. This is where the power of data can translate into a distinct competitive advantage and material revenue outcomes.

Shifting to fibre, we were surprised and disappointed by the Competition Commission's position to not recommend Vodacom's proposed purchase of a 30% stake in Maziv. The next step is for the proposed transaction to be presented to the Competition Tribunal, which will more than likely take place in May next year. We remain confident that the Tribunal will recognise the pro-competitive advantages that the proposed transaction would have on the fibre market, and the country as a whole.

In addition to our progress with purpose and strategy, I'm pleased to report financial results that showcase the resilience of our business and growth potential. At a group level, our financial highlights included the revenue of R72.8 billion, which was a strong result and up 35.5%. On a pro forma basis, including Vodafone Egypt in both years, the revenue growth was up 9%. Group service revenue growth was up 42.9% or 9% on a pro forma and target comparable basis. This was at the higher end of our mid to high single digit medium term range.

Our key growth drivers were data revenue and new services, including financial services. Data customers reached 77.8 million with the inclusion of Vodafone Egypt, while data traffic growth was more than 40%. Group EBITDA increased 35.1% to R27.3 billion. On a pro forma basis, EBITDA growth was 5.5%. This is slightly below our mid-term expectation and we anticipate an improved group performance in the second half.

Group operating profit was up 4.3% on a pro forma basis, below the EBITDA growth trend as a result of higher depreciation and amortisation. Our headline earnings per share decreased 4.2% to 438 cents per share. This result was impacted by start-up losses in Ethiopia, higher interest rates and a prior year deferred tax recognised in Tanzania.

Pleasingly, Vodafone Egypt contributed 16 cents per share to headline earnings per share, despite having issued 242 million new group shares and debt to finance the acquisition. The board declared an interim dividend of 305 cents per share, which reflects our updated and simplified dividend policy of at least 75% of headline earnings. As a reminder, last year's interim dividend of 340 cents per share was set at 80% of headline earnings and announced before we closed the Vodafone Egypt transaction.

If we now look at the business from a product level, new services which compromise fixed, IoT, digital, and financial services reach 19.8% of group service revenue, moving closer to our target of 25% to 30% in the medium term. Financial services delivered growth of 39.9% or 20% on a pro forma basis including Egypt, as we continue to scale user adoption, new products and services.

Alongside the super rollout, our active merchant base continued to scale meaningfully in South Africa and across our international markets. Our merchant base was up threefold to almost 292,000. This growth helps expand our addressable revenue pool beyond peer-to-peer payments and withdrawals into both online and offline commerce.

Now shifting focus to South Africa, service revenue grew 4% to R30.7 billion, supported by new services and mobile data. New services were up 18.8% and contributed 16.6% or R5.1 billion of South African service revenue. Financial service revenue increased 10.8%, underpinned by insurance growth of 17.2%. Our super app, VodaPay, reached 4.1 million customers or registered users through 7.6 million downloads.

Mobile contract revenue was up 4.1% supported by a more for more price increase and 105,000 new customers in the half. Vodacom business excluding wholesale revenue was up 3.8%. The modest growth reflects that corporate customers were recalibrating spend as employees returned to their offices.

Our prepaid segment delivered a good performance given the challenging macro backdrop and grew 3.1%. Pleasingly, prepaid data growth increased by 15.3%, supported by network investment. This supported prepaid revenue growth of 3.5% in the quarter. Data metrics remained strong with data traffic up 45.2%. EBITDA grew by 1.6% as we faced higher electricity prices and reinvested cost savings into network resilience and maintenance. We expect cost savings to accelerate in the second half, supporting stronger EBITDA growth.

Our international operations reported service revenue growth of R14.7 billion, up 16.6%. The reported growth was supported by currency tailwinds, while normalised service revenue growth was 4%. This underlying performance was supported by strong growth in data and M-PESA.

From a market perspective, we delivered strong double-digit growth in Tanzania, while the DRC was subdued by the macroeconomic environment. Mozambique's performance was impacted by price transformation and will begin to lap this transformation in the second half of the financial year. Our customer base increased 22.3% to 53.7 million with net additions of 3.5 million customers in the half reflecting strong commercial traction across the portfolio.

Data revenue increased 34.9% supported by data traffic growth of 40.4% and 19.6% smartphone user growth. M-PESA revenue is up 26.8% to R3.8 billion contributing 25.9% of international service revenue. M-PESA growth was supported by strong performance in Tanzania. International EBITDA grew 14.1% to R5.4 billion. On a normalised basis, EBITDA was up 4.3%, supported by cost containment.

Vodafone Egypt delivered another strong performance. Local currency service revenue was up 28% in the period supported by increased data demand, as well as growth in Vodafone Cash and fixed line services. In the second quarter, service revenue accelerated to 28.4%, supported by strong adoption of our revamped flex offer with enhanced value and embedded entertainment offerings. Customers reached 47 million, up 5.5%, and was another driver of growth.

Data metrics were strong in Egypt. Data traffic was up 42.9% and supported by double-digit growth in data customers. Vodafone Cash revenue more than doubled its contribution to service revenue to 5.6%. The growth of Vodafone Cash was supported by an almost 60% increase in customers to 6.7 million customers. Vodaphone Egypt contributed R6.2 billion to group EBITDA or 22.9%. The group EBITDA margin of 42% was delivered despite accelerated inflationary pressures and enhanced promotion activity.

Looking in the second half, we are working on a price up in Egypt, and this has the support of key stakeholders. A price up along with a laser focus on costs will help us address the inflation pressures in the market.

Shifting then to Safaricom from a numbers' perspective, Safaricom contributed R1.5 billion to the group's operating profit down 1.1%. Given this marginal decline includes what we expect to be peak losses in Ethiopia, Safaricom could be contributing positively to our bottom line from next year. Service revenue was up 9.8% supported by strong growth in M-PESA and data revenues. M-PESA revenue was up 16.5% with second quarter growth accelerating to 21.4%, supported by new services, including a successful partnership with government called the 'hustler fund'.

EBITDA in Kenya was up 13%, with margins improving 3.7ppts to 55.9%. Safaricom's overall EBITDA, including Ethiopia, increased 8.6%, reflecting the start-up losses associated with the Ethiopian rollout. By the end of September, Safaricom Ethiopia had already reached 4.1 million customers and more than 2,000 integrated sites. Safaricom Ethiopia also launched M-PESA in August 2023. We see M-PESA accelerating our vision to transform lives in the country, supported by the group's proven record in financial services in Africa.

Given Safaricom's excellent performance in this period, it upgraded its guidance for Kenya and the Safaricom group. Safaricom now targets double-digit EBIT growth in Kenya, which is ahead of inflation and is an encouraging outlook. This concludes my review. Raisibe and I are now ready to answer any questions you may have.

Operator
Thank you very much. Ladies and gentlemen, if you would like to ask a question, please press * and then 1 on your touch-tone phone or on the keypad on your screen. You will hear a confirmation tone that you have joined the queue. If you decide to withdraw the question, please press * and then 2 to remove yourself from the list. Our first question is from Maurice Patrick of Barclays. Please go ahead.

Maurice Patrick
Yes, hi guys. Thanks for taking the questions. If I can ask a couple of high level questions. In the past, Shameel, you asked about Etisalat and the extent to which you would work with them or their interest in Vodacom. And you talked about cooperation with them as Vodafone's largest shareholder. I'm just curious of thoughts in terms of how that discussion and dialogue has evolved over the last six months.

And then the second question, please, is really around the potential monetisation of mobile money or M-PESA. You saw MTN… I wouldn't say rush to a sale but talk about selling a stake in their business. And you've talked about it in the past. I wonder what your updated thoughts were on that. Thank you very much.

Shameel Joosub
I'll start with the Etisalat part. So, I think the cooperation is already happening, but a lot of it, to be honest, is happening at the Vodafone level. So, we're involved in some of the work streams, but not all the work streams. But definitely the cooperation between the two entities is happening. I can't give you the exact details around that. I think you'd have to ask Vodaphone that.

In terms of the M-PESA sale process, I think what we have done successfully is separated the different companies into different entities except for Kenya. And essentially we've got standalone entities across all the markets. So, should we decide to monetise, we're ready for that. And we will of course build up some good inventory. I think we felt previously that the timing was too early and that there was more opportunity to try and grow the business, which is where we're still focusing on.

We are trying to give more colour on the business. And I think you'll agree that the business has been accelerating. And so, I think very good growth this year will be circa $1.6 billion or $1.7 billion in terms of absolute revenue coming from financial services in both Kenya and the Vodacom footprint. So, I think very, very strong. We're seeing the number of use cases and acceleration happening.

So, we're still doubling down to make sure that we can grow the use cases, the one app strategy, the mini app strategy, M-PESA for kids, the investments, the international money transfer and so on. So, we haven't decided yet or made any decisions to pursue a potential sale. And I mean, we're not really encouraged by what's actually happened with some of these things, yeah? We've also managed to partner with Visa and get some contributions towards our projects, some contributions without equity.

Maurice Patrick
Great. Thank you.

Operator
Thank you very much. The next question is from Rohit Modi of Citi. Please go ahead.

Rohit Modi
Thank you for taking my questions, just a couple. Firstly, on the service revenue in the second half in South Africa, I believe there will be a tougher comp because you gained some market share in the second half. Also, as you highlighted, due to normalisation of return of work, you had a drag this quarter. You might have a similar drag in the next few quarters as well. How do you see the momentum of service revenue growth in the next two quarters? Secondly, on the Telkom side, what kind of impact have you seen from Telkom and RT15 this quarter? Thank you.

Shameel Joosub
I think from a market share perspective, starting off, I think it's been a very strong execution in the first half in a multitude of different ways. Firstly, I think starting off with the network, the power resiliency and so on, has definitely created a competitive advantage last year. And that has continued into this year. So, I think that's played out quite positively for us. I think the contract revenue growth that you are seeing in South Africa… Remember that some of the increases have come through the quarter, so you will see all of that in the next half.

I think prepaid has seen a distinct improvement in performance, so that is good. We are hoping to continue that trend into the next half, at least from an ARPU perspective, being able to maintain or grow ARPU. But also, we go into the second half with a strong customer base in prepaid, or an increased customer base. I think that bodes well. From an enterprise perspective, RT15 is largely behind us now, but we have had some reduction in revenue. That is coming from enterprise numbers that have been subdued because of wholesale revenues more than our business customers. So, RT15 is in the base, some of the pressure, otherwise we would have seen stronger growth in enterprises coming from people returning to work. And as they're returning to work, businesses such as the banks and so on, are cutting allowances that were given to individuals.

JP Davids
I think you've covered Telkom. Is there anything more you wanted to talk about Telkom specifically?

Shameel Joosub
No, I think on the Telkom side, we know that they did give 20% of their traffic to MTN.

Rohit Modi
Thanks.

Operator
Thank you. The next question is from Madhvendra Singh of HSBC. Please go ahead.

Madhvendra Singh
Yes, hi. Thanks for taking my questions again. So, a couple of questions from my side. A small follow-up on mobile money performance basically in Mozambique. It seems there was a decline in the quarter again. So, if you could talk about the reasons behind that and whether that was expected. You did tell us about the price transformation on the telco side, but is that happening on the mobile money side as well? So, if you could give some colour there.

And secondly, sorry to ask this again, on the dividend side, what would it take for you to increase the pay-out ratio? Is there a level of leverage in mind or do you need to see some other factors before you could think about increasing the pay-out ratio itself? If you could talk about those, that will be helpful. Thank you.

Shameel Joosub
Okay, so on the mobile money performance, I think there was some pressure in the half in terms of transformation coming from two fronts actually. One is some tightening of some loan criteria that the bad debt is sitting with the third party or with the bank. But essentially, a tightening some of the criteria around that where we did see some drop off. Not huge, about 200,000 customers. But essentially, that created some pressure points. That was the one.

And then the second one is certain being able to, we've had a more competitive space in terms of the competitor offering free P2P services in some instances. So, we've had to change some of our pricing around mobile money. Also, some disruption due to approval timelines in Mozambique. So yeah, it did put a bit of extra pressure that we didn't need. But the fundamentals of the mobile money business in Mozambique is still very good.

Raisibe Morathi

On the dividend, the question of scenarios for increasing the pay-out, we define our dividend policy as a minimum of 75%, which means that flexibility is always there. But having just revised the dividend policy a year ago, the idea was to fund the growth in terms of the acquisition of Egypt. And for that reason, it is not an appropriate time at this stage to pay above the 75% when we obviously can do that at an appropriate time. And I think a reference point is that in H1 last year, we did pay above the 75%, so we paid at 80%. But for now, it is not the right time. And obviously, as we continue to pay down the debt, maybe that opportunity will come up.

Madhvendra Singh

So, I'm just trying to understand the thought process here. So, would it be more of a factor of free cash flow going up or the leverage coming down sufficiently below where we are right now?

Raisibe Morathi

So, the cash flow is not the key factor for the dividend being paid out at 75%. So, the 75% was the best way to simplify our dividend policy and also to get a bit more leverage. So, the cash flow… And if you look at the cash flow at minus R250 million, it is a factor of in the base we had Safaricom's dividend that was previously received in this period having been received on the 31st of March as opposed to the 1st of April type thing.

So, that dividend of R1.3 billion is creating a base effect, obviously, for this period. And then the second thing is that we had to pay the provisional tax for Egypt. So, a combination of those. So, if you were to adjust for those, you would have a positive R2 billion on the free cash flow.

In terms of the seasonality of our business, our cash flow comes through much stronger in the second half of the year. So therefore, the cash flow will correct and we don't see any abnormality in the cash flow other than just explaining those one offs. So, for that reason, a completely different aspect from looking at the dividend at 75%. 75% is of headline earnings. So, for as long as the business produces headline earnings you will be able to see the 75% being paid out as dividend.

Madhvendra Singh
Great, thank you. May I ask one more question? Do I have time?

JP Davids
Sure, go for it, Madi.

Shameel Joosub
Thank you. So, one question on Egypt. I understand that the price floor is already there in the market. Have you been able to get any price hikes as well? And given the inflation remains quite high, I'm just wondering your thought process, as well as what the government or regulators thoughts are around that. Can we expect a price hike there? Thank you.

Shameel Joosub
So, we've agreed in principle a price hike for the industry. The timing is not certain and we are hoping that it will happen post the elections, early January. Everybody's ready. We're just waiting now for the final go ahead.

JP Davids
Just to add a little bit more colour, the one thing you will also see coming through from the asset in Egypt is a very focused cost programme. So, a clear objective to run their opex below the rate of inflation. So, you're tackling inflation in two aspects, trying to get a better revenue outcome, and then also trying to de-risk the business from a cost perspective. And I guess clearly one of the benefits we pulled out from the presentation earlier is a lot of Vodafone Egypt's costs are localised in Egyptian Pounds, and that is obviously one of the benefits of owning your own infrastructure in the market.

Madhvendra Singh
No, great. I mean, the margin performance in Egypt is definitely quite commendable. So, thanks. Yeah.

Operator
The next question we have is from Curtis Schacht of Sustainable Capital. Please go ahead.

Curtis Schacht
Hi there. Thank you so much for making the time. I'm just curious. A bunch of your competitors have been talking about the balance of power shifting from tower companies to the TowerCos. So, I just

wonder if you can just comment on if you see any cost savings down the line as leases come for renewal.

Shameel Joosub
Yeah, so remember we don't have a huge amount. I mean, we use TowerCos in the countries, but remember most of our towers are owned except for Tanzania where we've used the TowerCos more extensively. And so basically, what we are doing is of course, wherever we can, we're trying to renegotiate some of the leases as they come up. Particularly in Tanzania and the DRC, we're trying to reduce costs by having discussions with the TowerCo operators to try and bring down our cost-base level. So, yes, we are trying to leverage that. Does that mean that the power sits with the TowerCos? I wouldn't go that far. But I would say that of course we do have the leverage of, if you want to renew, to try and renegotiate the better terms.

Curtis Schacht
Sure, understood.

Shameel Joosub
But I think the structural advantage that we have is that most of our towers are actually owned.

Curtis Schacht
Yeah, understood. And in terms of those renegotiations, would that be purely around price or would you also be looking to shift the energy price exposure to the tower companies as well?

Shameel Joosub
So, it's a multitude of different things. One is the inflationary parts that you want to contain, so you want to make sure that that's contained. And of course, there's multiple ways in which you can do it. You can have an all-in agreement which includes power, or you can have an agreement that excludes power. And those can become a see-through or pass-through cost. So, there's different ways in which to look at it, and it really depends on the negotiation, yeah?

Curtis Schacht
Cool, understood. Thanks so much.

Operator
The next question we have is from Myuran Rajaratnam of MIBFA. Please go ahead.

Myuran Rajaratnam

Good afternoon and thanks for the opportunity. My question is on Safaricom. That extra bit that Vodafone owns, is this not a good time to buy that? I mean, the previous slug we bought I think around the 20s, right? Does it not make sense to buy now? Or do we only buy when it's suitable for them, not when it's suitable for us?

Shameel Joosub
Look, I think, to be frank with you, I don't think they're going to sell at the low of the market. I don't think we need to wait until the price is very high either. But I think at this stage, they're not willing to sell at the low prices. Of course, as you know, the share price is at a couple of years low, right? So, I don't think they're necessarily going to sell at this point. But I think we certainly do want to still buy the 5% at the right price. And that right price would be somewhere, maybe not as low as it is today, but of course not as high as it was. Every couple of months we go back and have that conversation. I think at this point, what we're really focusing on is trying to de-lever our debt.

Myuran Rajaratnam
In Egypt, do you think the group balance sheet can handle buying, if it comes available, the remainder of Vodafone Egypt?

Raisibe Morathi
Yeah, look, it can. I mean, everything is based on looking at business merit at that point in time, but it's a good business. Owning more of it wouldn't hurt. And at this point in time, we are looking at the data that we have. But yeah, if something like that comes up, we'll look at it on merit at that point in time.

Shameel Joosub
We do have a first right of refusal, just to be clear.

Myuran Rajaratnam
Yeah. I understand. Great. Thank you very much, guys.

Operator
Ladies and gentlemen, just a final reminder, if you would like to ask a question, you're welcome to press * and then 1. We will pause for a moment to see if we have any questions. It seems we have no further questions. I would like to hand back to Shameel for any closing comments.

Shameel Joosub

Thank you and thank you for joining us on today's call. If there are any other questions that you might have, please reach out to the Vodacom investor relations team. Enjoy the rest of your day. Thank you.

END OF TRANSCRIPT