

Conference Call Transcript

31 January 2023

Q3 RESULTS ANALYST CALL

Operator

Good day, ladies and gentlemen, and welcome to the Vodacom Group Limited trading update call for the three months ended 31 December 2022. Vodacom Group CEO, Shameel Joosub, will host the conference call. Before I hand over to Shameel, I would ask that you refer to and familiarise yourself with Vodacom's forward looking disclaimer. This is set out on page 16 of the trading update and can be located on www.vodacom.com. Alternatively, if you'd like a copy of the results announcement sent to you, please email investor relations website at vodacomir@vodacom.co.za. All participants will be in listen only mode. There will be an opportunity to ask questions later during the conference. If you should need assistance during the call, please signal an operator by pressing * then 0. Please note that this call is being recorded. Shameel, over to you.

Shameel Joosub

Thank you, Irene. Good afternoon, everyone. 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, who have dialled in from Cairo where we've been spending the last couple of days. The third quarter of the financial year marked the completion of the highly anticipated consolidation of Vodafone Egypt into the group. In December last year, we announced the finalisation of the R43.6 billion deal, the largest in Vodacom Group's history. Vodafone Egypt's growth outlook is supported by leadership across both consumer and enterprise segments, a clear network and spectrum advantage versus peers, and a brand synonymous with technology leadership.

We see a massive addressable market for financial services in Egypt and intend to leverage our financial services products roadmaps, including our Super App approach to unlock this opportunity. We look forward to unpacking these opportunities with you at our upcoming investor day in Cairo on the 7th of March. Vodafone Egypt was consolidated from the 8th of December 2022 and contributed R1.9 billion to group revenue for the 23 days. This was a key factor alongside currency gains and operating model resilience in the 14.8% growth in our revenue this quarter.

Our operating model and strategy called the System of Advantage are purpose led. To support digital inclusion, we're expanding our connectivity reach, financing affordable smartphones, providing free access platforms, and transforming pricing. Leveraging our big data and CVM capabilities we've accelerated personalised offers to customers. By combining the CVM capabilities with our innovative loyalty programmes, we were able to drive strong customer engagement across our markets despite the macro challenges.

In South Africa, we successfully integrated our summer campaign and behavioural loyalty programme, VodaBucks, into the VodaPay platform, driving accelerated adoption of the Super App. Another of our many purpose-led initiatives which we are proud of is Code like a Girl programme. This programme aims to tackle low representation of girls in science, technology, engineering and mathematics, or STEM for short. Through this initiative, we aim to get more girls into careers that require coding skills, or to help them get a start as STEM entrepreneurs. First implemented in 2017, we have ramped up efforts in the quarter, particularly in South Africa, Mozambique and Lesotho, by connecting more girls through Code like a Girl. Investments of this nature are helping to build a more digital, inclusive, sustainable future on the continent.

With Egypt in the portfolio our population reach now exceeds 500 million people across Africa, representing a clear growth path for our connectivity services, including mobile and fixed. Our System of Advantage also sets out a plan to establish a meaningful play in digital and financial services. Our ecosystem spans across big data, IoT, financial and digital services. In financial services we remain Africa's leading fintech operator, with \$366.7 billion of M-PESA transaction value processed over the last 12 months, up 17% year on year. This represents a major milestone for M-PESA with us processing over \$1 billion a day. Financial service customers in South Africa and international are up 2.6 million in the quarter and with the inclusion of Egypt and Safaricom's last recorded KPIs, our financial service customers now exceed 70 million as a group.

On that exciting note, other group highlights for the quarter included a revenue of R30.7 billion, up 14.8%. This included contribution for Egypt for 23 days on the quarter. Growth is also supported by exchange rate tailwinds across our international markets. Excluding the impacts on currency in Egypt, the revenue was up 4.7%. This normalised growth was driven by data revenue and financial services. Data customers were up 2.4 million in the third quarter with data traffic growth of more than 30%. Financial service revenue was R2.6 billion, up 30.6%, making up 10.9% of consolidated service revenue.

Our financial service strategy is supported by a dual sided ecosystem across consumers and merchants, bringing these segments together to exceptional and personalised experiences relating to entertainment, e-commerce, payments, savings, investments, lending and insurance services. As key drivers of the strategy, our two Super Apps, VodaPay and M-PESA, integrate our own products and services with the best offerings from our partners. In aggregate, our new service categories which include financial and digital services, fixed and IoT contributed 19.7% to group service revenue, up 2% from last year. Capital expenditure increased by 28.3% or 18.9% excluding the impact of Egypt. Our year to date capex to sales intensity is 13.9%, within our target range of 13% to 14.5%, positioning as to capture the strong growth in data traffic.

Let's shift focus a bit to South Africa. Service revenue grew 3% to R15.4 billion in the quarter, supported by mobile contract, a good performance in prepaid and growth in our new services. New services were up 9.9% and contributed 15% or R2.3 billion to South Africa service revenue. Financial services revenue increased 12.6% supported by our insurance portfolio and an acceleration in Airtime Advance in the third quarter. Our insurance policies went up 11.1% to 2.6 million as we continue to expand our portfolio of products. Our Super App, VodaPay, continued to gain traction with 2.7 million registered users through 4.5 million downloads and over 100 mini apps.

Our contract revenue grew 3.1% and we added 132,000 customers in the quarter, both in the consumer segment benefitting from the contract price increases earlier in the financial year and strong demand in the quarter. Our mobile business segment faced a demanding comparative prior year quarter, which included a boost from the Omnicom variant and related spike in work from home usage in December 2021. Overall, Vodacom Business service revenue declined 3.5% to R4.3 billion. Growth was also impacted by pressure associated with the government's RT15 contract and a decline in wholesale revenue as we lapped a tough competitor.

Pleasingly, our prepaid mobile segment delivered a good performance given the challenging macro backdrop. Prepaid revenue growth accelerated to 3.7% from 2.7% in the second quarter as we leverage our CVM capabilities to deepen our engagement through a successful summer campaign. Data metrics remain strong. Data traffic accelerated to 39.3% in the quarter supported by investment into network resilience and extended hours of load shedding. We added 1.7 million data customers in the quarter and increased the number of smart devices in our network by 13% to 29.5 million. Average usage per smart device increased 27.4% to 3.2 GB per customer.

Our international operations reported service revenue growth of R7 billion, up 18%. On a normalised basis, service revenue growth was 4.5% underpinned by data and M-PESA. Compared to the second quarter, growth in the third quarter slowed somewhat, reflecting network availability challenges in the DRC associated with the floods in Kinshasa and fuel supply disruptions. We added 4.3 million customers in the quarter, reaching a customer base of 48.1 million, reflecting some commercial traction across the portfolio.

Data services remained a key driver of growth and our commitment to connect for a better future. Data revenue increased 32.3% supported by data traffic growth of 30.8%. M-PESA revenue was up 33.6% to R1.8 billion for the quarter, contributing 25.3% to international service revenue. New growth areas in M-PESA such as lending and savings products continue to gain traction, contributing half of the growth in the quarter. In Tanzania and Mozambique, we granted an impressive R3.2 billion of loans in the quarter.

As I highlighted earlier, we consolidated Vodafone Egypt on the 8th of December. In our release, we also provide an update on the trading performance for the full quarter, which is strong. In local currency service revenue was up 23.4% in the third quarter, supported by an increase in data demand as well as growth in VodaCash and fixed line services. ARPU growth of 17.5% in the quarter was supported by the accelerated investment into the network and spectrum over the last few years. An additional R1.1 billion was invested into the network in the quarter.

Data metrics remain strong with data traffic up 44.8% and data customer growth of 11% to 25.6 million customers now using data. Financial services, a key focus area for us, was R351 million for the quarter, up 59.2%. This traction was supported by strong growth in financial services customers, which reached 4.8 million. Results from associate, Safaricom, are disclosed on a bi-annual basis and therefore are not included in the quarterly update. However, I would like to highlight the following updates from Ethiopia.

Safaricom Ethiopia surpassed 1 million active customers in mid-November. And the network rollout also continued apace in the quarter. By 31st of December, Safaricom Ethiopia had expanded its coverage to 21 cities across Ethiopia, on track to reach its goal of 25 cities by April 2023. Raisibe and I are now ready to answer any questions you might have.

Operator

Thank you. Ladies and gentlemen, if you would like to ask a question, you're welcome to * and then 1 on your touchtone phone or on the keypad on your screen. If you wish to withdraw the question, you may press * and then 2 to remove yourself from the question queue. Once again, if you would like to ask a question, you're welcome to press * and then 1. We will pause a moment while we wait for the question queue to build. Our first question is from Jonathan Kennedy-Good of JP Morgan. Please go ahead.

Jonathan Kennedy-Good

Good afternoon. Thanks for the opportunity to ask questions. Just a couple from me on the VodaPay business in South Africa. Would you be able to share with us what kind of revenue run rate in Rands the business is generating at the moment and how we should think about what the cash in and cash out services could add to that business? Should we expect a strong acceleration there? And then secondly, given this calendar year has been more of the same in terms of power outages, how are you thinking about improving network resilience? And what kind of issues are you coming across? Is it feasible and necessary to invest in diesel generation at the site level? And then finally, obviously on prepaid the numbers look pretty solid. Are you taking any market share in South Africa from your competitors? I think you indicated last quarter you might have been doing that already.

Shameel Joosub

Yeah, let me start off with the VodaPay one. We now have 2.7 million registered users on the app. So that's a positive. We're not providing GMV values yet. What we are seeing is a deepening of the number of transactions per customer. And that's growing quite nicely. But also, the primary use case has been airtime, transport, vouchers, and then of course lending. So, those use cases have been growing strongly and we're now seeing more and more growth coming through in terms of that. So, I mean, it's still very early days. We're only providing guidance on the number of registered users as we continue to grow the utilisation.

The second question on prepaid, on the prepaid revenue growth, yes, I think we have had a strong quarter. I think a very well executed summer campaign played a big role. And also, a very big focus on active day management, breaking the base down into segments and then looking at how we can drive more utilisation through our CVM platform. I also think the summer campaign being able to basically take advantage of the campaign but also convert the VodaBucks into cash on VodaPay also played a role. So, you had all these functions basically help to increase active days. And then of course, Airtime Advance also performed very well in the quarter where we also took certain

measures to increase the addressable base. And I think that has helped us as well to increase active day usage. JP, what was the second question?

Raisibe Morathi

I'll take the question about power outages. Yes, indeed, the power outages continue to persist. December was one of the worst months. But in terms of our plan where we were rolling out generators, we are continuing with a blend of generators which are stationary as well as the mobile ones. And we are also combining batteries with the generators in different sites. And the long term play given that Eskom seems to be struggling, is to really relook at our strategy in terms of where we need to have alternative power in some of the sites for the longer term. But fortunately, in this tough season in December, we've been able to support the network through those difficult environments. And that is part of the reason the prepaid revenue has continued to do well.

Shameel Joosub

Maybe just to add, as an industry what we have been doing under the minister's guidance is gotten together to see how we can cooperate more and getting some leeway from the Competition Commission and so on, so that the telcos can work together to make sure that South Africa stays connected and that we can share more in terms of generators and power and so on. And government will be working with us to ease some of the rules so that we can try and make sure that from a telco perspective that we keep the networks up. I think one of the strategic advantages that we have at the moment is that we definitely have more power availability than some of our competitors.

Jonathan Kennedy-Good

Great, thank you.

Operator

The next question is from Preshendran Odayar of Nedbank CIB. Please go ahead.

Preshendran Odayar

Hi, everyone. Thanks for the questions, and congratulations on the quarterly results. I've got three questions. I'll start on two for South Africa first. Can you please tell us what the IoT revenue was for the quarter? I clearly remember the normalised number for IoT is around R350 million per quarter. So, I just wanted to know what that was for this quarter. Secondly, on South Africa, what was causing the decline in your Vodacom Business revenue? And how impactful has Telkom's roaming agreement moving to MTN – I know it's not the whole roaming agreement, but a portion of that –

how impactful has that been to your numbers? Then the third question is on international markets and DRC in particular. You mentioned in the release that this was a drag on your normalised service revenue growth. Yet in the quarter, you had 3 million net adds, which is probably the highest net adds you've had in a single quarter for the DRC. Just want to know how this didn't translate into any service revenue growth. Thanks.

Shameel Joosub

JP, do you want to start, or Raisibe?

JP Davids

Yeah, so I'll just take the number question IoT. So, the number was pretty much bang on R300 million again in the quarter. The year on year growth rate was under a bit of pressure this quarter, simply because of some project based work in the comparative. And that we called out in the announcement.

Shameel Joosub

On the enterprise side, I think the issues really come from a strong comparative last year, more than anything else. That was the biggest impact in the decline. Smaller contributions came from roaming, where effectively there has been a bit of a decline on the Telkom roaming. But it's also been offset by increased traffic because we have more availability. So, they are giving us more traffic at this stage. And then, thirdly, of course, the whole year will be impacted by some pressures on RT15 where, of course, you've had the repricing and of course there will have been some movement in customers. But as you can see from the net adds situation, we are managing the situation relatively well, considering that we moved from exclusivity to being an open opt in or opt out by each department.

Raisibe Morathi

So, on the impact of Telkom roaming migrating to the competitor, a part of that contract has indeed moved. And that has had an impact on the growth in VB service revenue. But that is only part of the reason explaining the growth in VB. Obviously, the other part is to do with the base effect, as indicated by JP earlier on. But yeah, there has been some change in that.

JP Davids

Okay, and then Preshendran, your last question was on DRC. Just a little bit of colour there. So, the way to think about it, I guess, is a game of two halves in the DRC in terms of the quarter. So, we did have a decent November and October reflected in the net adds. You will see those are largely non

data net adds, so on the traditional GSM side. It was really pretty much the whole of December that was wiped out by the floods. I guess the net adds doesn't capture the shape of the quarter. And it was really one of the three months that unfortunately had the wobble because of the floods. And also, there were fuel shortages that were persistent through the quarter, but particularly into December. Hopefully that helps.

Preshendran Odayar

Yes, thanks. Thanks very much, everyone.

Operator

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

Madhvendra Singh

Yes, hi. So, my question is on the prepaid strength in South Africa. So, if you could talk a bit more about your power backup strategy there, because if I understand correctly, the power shortages were quite serious, but despite that you have been able to manage the network very well. Maintaining 3.7% growth I think is very impressive. So, I'm just wondering what really worked well for you? Was it the battery backups that helped or did you have to deploy more mobile generators and so on, to ensure that those batteries get charged? Or the situation was not as bad that you did have enough Eskom power to actually be able to charge the batteries.

And I also want to understand how long these battery backups generally run for. How many hours coverage do they offer? And the second part of this same question is that if you did have to deploy these diesel generators to these sites, would we have to see some kind of negative impact on margins, if at all, and whether the net absolute impact on EBITDA would be something to worry about at all? Thank you.

Shameel Joosub

I think maybe I don't want to create the impression that the growth in prepaid has got to do only with power. I think the commercial execution has been strong. So, let me just start off with the commercial execution. I think, again, a very well executed summer campaign. I think what happened was the summer through VodaPay part proved to be very successful. The ability for customers to earn bucks, convert it into cash, spend it over the platform, we saw a nice acceleration of utilisation on the platform beyond airtime, which is very good. So, people coming in to do more, which in turn creates active day utilisation. Then we use our CVM tools to get them special offers, made sure that the offers were there as part of the summer campaign, and so on. And then, of

course, a very well executed part in retail in the stores and so on. And in some of the big channels we gained market share.

So, it's a multitude of different factors that normally play out for you to get the growth. It's not just one thing. Then we had the Airtime Advance part, which also helped. And then we had a well-executed programme that took advantage of us having more power than some of the competition, where effectively what does happen is when the power goes down, customers go to their phones. So, effectively, that does give you a boost during those hours that the network is down. So, you saw that coming through in increased data traffic utilisation. But it does last for as long as the battery lasts.

Your question on the batteries, generally we would have four hours standby across most of the sites. At some sites we have six hours and other hub sites we have eight hours. The important hub sites we would also have generators available. At all the hub sites we have standby generators as well. And then we have a mobile generator part that effectively moves between the sites depending on the criticality of a particular area and how the power situation is holding up. So, there's a multitude of different things. Of course, higher stages of load shedding cause more havoc on the network.

On the positive side, it gives you more growth. On the negative side, you have to be able to cope with it. In the last half, we explained we had about R150 million of additional costs from power. And so, you can expect a little bit more than that, but essentially circa in that kind of ballpark of extra costs that we carry. That said, we did explain that we do see an acceleration of EBITDA in the second quarter in South Africa based on our different cost programmes, but also based on the competitive profile of the first half versus the second half.

Madhvendra Singh

Thank you very much, Shameel. Thank you.

Operator

Ladies, gentlemen, just another reminder, if you would like to ask a question, you're welcome to press * and then 1. Our next question is from David Lerche of Sanlam Private Wealth. Please go ahead.

David Lerche

A question for JP and Raisibe since you're in country there in Egypt. Any views on your ability to continue to push through inflation through to your pricing there, given the disappointing and unfortunate collapse of that currency? And just any additional comments around that currency. And I suppose in due course, your ability of course to repatriate cash out of Egypt there back to the group. Thank you.

Raisibe Morathi

Good afternoon. So yes, indeed, we are in Egypt. So, the macroeconomic environment whilst it is challenging, there is a lot of work that is being done by the government obviously, in response to the support from IMF and the Gulf States. There is finance economic reforms and a great effort towards a free float currency. So, while it's not there yet, but we do believe that the efforts that are being put in place, and also, if I could say, the pressure that comes from the IMF should be helpful catalysts towards at least containing the currency crisis. So, at this point in time, whilst inflation is high, interest rates have been picking up, hopefully, the further pressure will be less than that that we have already seen.

So, currently, the good thing is that the business is growing very well, gaining market share and also growing above the inflation levels. So, from that perspective, we do see some growth of inflation. The pricing, as you indicated, requires approval from the regulator. We're not there yet. But there's an effort and discussions by the industry with the regulators to try and obviously bring that on board. In terms of the ability to repatriate the dividend, indeed, in the liquidity challenge that we are sitting with that might be a short term challenge. But we are hoping that the reforms that are being put in place should be able to cure that going forward. We've just been in for a month. So, we do hope that in the medium term things should be better than what they are today.

David Lerche

Thank you.

Operator

Our next question is from Rohit Modi of Citi. Please go ahead.

Rohit Modi

Hi, thank you for taking my question. Just two questions from my side. First the power cost, please can you give more colour in terms of what you're expecting for the second half in terms of additional impact on the power cost? And how do you see power costs evolving next year? Do you see there'll be additional pressure from the power cost side, or you see this get moderated next year?

Secondly, on the government contract, RT15, can you give some colour in terms of how much more impact do you see coming from the RT15 contract in the next quarter and following year? Thank you.

Raisibe Morathi

On the power cost, as we indicated in with the interim results, around R150 million. So, we are not seeing that number blowing up. And that is because there is a blend of a number of initiatives that come with the mix of diesel generators as well as the batteries and also just better utilisation of our assets. So, we also have closed deals with the oil majors in terms of getting a discount on the wholesale price for the diesel. And some price moderation has begun to come through for diesel. So, that also helps. So, a combination of those factors. We believe that we will still be able to meet our guidance in terms of where we thought our overall cost of additional energy. Obviously, that is on the basis that the power outages do not get much worse than where we are right now.

Shameel Joosub

I think on the RT15 the way to think about it is threefold. I think this year was probably the year where you took a lot of the pressures on RT15, specifically from a repricing perspective. I think we've been able to contain losses, but also, we've been able to gain some more business as well in the process. But you have had some repricing and there will be contracts that still come out of contract next year. So, there will be some pressure still into next year. But I'd say most of it has been taken this year in terms of the impact of RT15.

Rohit Modi

Thank you.

Operator

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

Shameel Joosub

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

END OF TRANSCRIPT