Conference Transcription

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CONFERENCE DETAILS

Conference Date:	23 January 2013
Conference Time:	08:00 UK
Conference Duration:	Approximately 34 minutes
Chairperson:	Matija Gergolet
Speakers:	Shaikh Mohamed bin Isa Al Khalifa (CEO) Peter Kaliaropoulos (CEO Strategic Assignments) Sameer Altaf, standing in for Marco Regnier, Group CFO

ACT Operator

Ladies and gentleman, thank you for holding. Welcome to Batelco Group Fourth Quarter and Full Year 2012 Financial Results call. Throughout today's presentation all participants will be in a listen-only mode. After the presentation there will be an opportunity to ask questions. If anyone has difficulty hearing the presentation please press *0 on your telephone for operator assistance. I will now hand the conference over to your host Matija Gergolet from Goldman Sachs. Please go ahead sir.

Matija Gergolet

Good morning, ladies and gentleman, and welcome to Batelco Group Fourth Quarter and Full Year 2012 Financial Results. Goldman Sachs is delighted once again to be hosting this call on behalf of Batelco. Today I have the pleasure of introducing Shaikh Mohamed bin Isa Al Khalifa, the Group CEO, who would be joined by the Group senior management team as well.

Following their comments the call will be opened for questions from the participants and also before starting the call the Group would like to make the standard forward-looking safe harbour statement.

Laila Danesh

Thank you, Matija, Batelco Group notes that some of the forthcoming statements are expectations based on reasonable assumptions. These forward-looking statements are subject to numerous risks and uncertainties. These statements may not be regarded as a representation of anticipated results which will occur on the Group's expected objectives. The forward-looking statements are only valid until this date and Batelco Group does not undertake to update these in any form.

With that I would now like to turn the floor over to Shaikh Mohamed Bin Isa Al Khalifa, Group CEO of Batelco.

Shaikh Mohamed bin Isa Al Khalifa

Thank you, Matija for the introduction and to Goldman Sachs for hosting this morning's call to discuss Batelco Group's Fourth Quarter and Year End 2012 Financial Results. I would also like to thank each one of you for joining our call and for your continued interest in the Group and our activities.

Here with me today is Mr Sameer Altaf, standing in for Mr Marco Regnier, Group CFO. Sameer will walk you through the presentation of our results and performance. Also Mr Peter Kaliaropoulos will then join Sameer and myself in answering any questions you may have later in the call.

Looking at the fourth quarter and the full year, we closed 2012 in a strong position. We not only delivered sound financial results but we continue to make important strides in executing our strategy. In terms of growth we are pleased to report a fifth consecutive quarter of growth in our subscriber base. We ended the year with more than 7.8 million customers across our six markets of operation. This represents 6% increase since last quarter and an impressive 18% gain in the Group's subscriber base, when normalised for the STel, since the start of 2012.

Despite ongoing and aggressive competition in Bahrain and elsewhere in the MENA markets, this included 17% growth in the mobile segment year-over-year and 5% since last quarter. We are confident that this underscores our ongoing market leadership in Bahrain in addition to the very strong results delivered by Umniah in Jordan, where we successfully launched the latest 3.75G services in June 2012, as well as from Sabafon in Yemen where market conditions have normalised and where we expect to see continued expansion. Similarly we saw growth in broadband where subscriber numbers increased by a solid 18% quarter-over-quarter and an impressive 52% year-on-year.

To supplement our continued organic growth we are also pleased to announce in the fourth quarter a major acquisition which will see the size, scale and reach of the Group expand significantly. We have stated for some time that this is our aim and we are extremely happy to be moving forward with the acquisition of CWC's Islands & Monaco businesses, which we aim to conclude at the end of first quarter 2013.

This is a truly transformative transaction for the Group and one that will help to diversify our footprint and revenue streams and see us emerge as an international telecommunications company of reference. Furthermore, in addition to an expanded customer base and more diversified revenue streams, this transaction will also see us benefit from the synergies we hope to achieve by the pooling of resources, technologies and expertise. We are confident that we will emerge an even stronger and more competitive organisation, which has been our focus throughout 2012.

As announced last quarter, we have already put in place a major restructuring programme, which will see us become more efficient and streamlined across our businesses and ensure that we are able to both maintain and build our market leadership as we go forward. We continue to make strong progress on our restructuring activities during the fourth quarter in particular in Bahrain where our efforts to rationalise our cost structure is essential to our ability to maintain both the top and bottom line.

Now looking quickly at the financials, performance for the period and the full year were again impacted by ongoing and aggressive competition particularly in Bahrain. Sharper declines year-over-year were also the result of the restructuring costs we noted as well as a result of a number of other one-off adjustments which notwithstanding would have seen EBITDA and margins come in line with prior year periods.

Looking at the Group's overall financial position, it is still robust as is our ability to deliver value to shareholders. For 2012 we are pleased to announce the Board's recommendation to the General Assembly for another substantial shareholder dividend. Our strategy and ongoing efforts to achieve operational excellence and growth continue to see the Group provide shareholders with some of the highest dividend yields in our industry region wide. We also close out the year with a strong balance sheet, significant cash balances and an investment grade credit rating. This will support us as we complete our transaction of the acquisition of CWC's Islands & Monaco division and as we continue to pursue other opportunities for growth.

We have entered 2013 in a strong position to deliver our promises to customers and shareholders alike and look forward to keep you apprised of our progress and growth in the coming months. With that I will now turn the call over to Sameer who will take you through the presentation and the details of the Group's financial results and performance for the period. Sameer.

Sameer Altaf

Thank you, Shaikh Mohamed. I will now discuss the financial and operational section and highlight. If you go to slide number three, it already lists the key highlights for the quarter and the year. However, the key ones are that we achieved the revenues of BD 305 million, EBITDA of BD 102 million with 33% margins, net profit stood at BD 60 million. As at the year-end Group has substantial cash and bank reserves of BD 95 million with significantly low debt. Subscriber base stood at 7.8 million which represents a growth quarter-on-quarter and year-over-year. Inclusive of the bonus shares our dividend payout comes at 84% and on cash basis about 60%.

Coming to slide number five, this shows the quarterly and the year-to-date financial performance. We can say that Q4 '12 was resilient in terms of the results that we delivered. Despite competitive pressures net profit of BD 17.8 million was achieved. At the year-to-date level we would like to reiterate that the performance was in line with the guidance we provided back in October 2012.

On slide number six, if we go to the diversification of the revenues and profits by segment and geography, we see that Bahrain is still the major contributor. However, its share in terms of revenue is decreasing and it has been caught up by the overseas operations which now account for 41% of the revenues versus 38% last year.

This is in line with the diversification strategy of the Group which we have indicated in the past communications as well. More specifically on the segmental profits, Bahrain profitability was impacted by intense competition in the home market, higher restructuring expenses and one-off costs.

Umniah profitability was adversely affected by the higher electricity costs and initial 3G launch costs. Other countries performance was buoyed by the strong gains we saw in QNet in the current year and also noting that last year we took the STel share of losses for Q1.

In terms of product profile on slide number seven, we see that mobile revenues whilst remaining the single largest revenue generator for us as a product, their share has gone down. This is because of the steep decline in revenues we see in Bahrain because of the competitive conditions we are seeing. Other revenues have increased year-on-year mainly on the back of higher devices revenues in Bahrain and Jordan and this obviously has an impact on the margins for the Group.

On slide number eight which is the CapEx and liquidity profile, as we have noted earlier, liquidity profile remains strong. As at year-end we had BD 95 million of cash and bank reserves with the FCF, free cash flow, of BD 41 million. This was well in excess of the guidance we provided back again in October 2012. In terms of the CapEx ratio, we were on dot at 23%, in line with the guidance that we provided.

Coming to the operational review, we had the Group's subscriber summary. We do see strong performance in the subscriber growth in Sabafon quarter-on-quarter and year-on-year. As Shaikh Mohamed noted, this is in line with the improving situation in Yemen and company coming back to normal operations. Bahrain mobile subscribers have marginally increased quarter-on-quarter and that is supported by the aggressive or good customer acquisition and retention campaigns we launched during the quarter, quarter four. Broadband subs continue to show growth trend due to increase in the wireless subs in Bahrain and Jordan and more specifically 3G subscribers.

I will now – for key initiatives, I will hand it over to Mr Peter Kaliaropoulos.

Peter Kaliaropoulos

Great, thank you very much. Good morning to everyone. No surprise that one of the key initiatives is the integration – first of all, the completion of the acquisition of the Monaco & Islands division and then the integration. Adding to that as Shaikh Mohamed said earlier to ensure that we derive the synergies which again in a shareholder's circular we identified $36 million of savings over five years in terms of synergies and obviously we are aiming for more. So that's a priority for us. Of course to complete transaction we also need to ensure the funding is in place and a bond is planned to be issued later this quarter and this year of course of a value $650 million.

The second priority again remains one of ensuring the home market and the most profitable in terms of margins market here in Bahrain. We retain our high value customers. We drive the right strategy which is retention of high value customers but also improvement in costs and overheads. We did announce at the last call that there is a programme of cost optimisation, cost reduction, process re-engineering and overall transformation. We are aiming that that project will deliver starting 2014 an operational saving of BD 20 million, about $52 million in value. That remains a key priority for the Group.

Third fundamental priority is business in Umniah in Jordan. We have invested in a 3G licence, we have invested in a 3G network. We are very pleased with the current take-up of 3G customers versus our competitors. Again the priority for us is to make sure we get the fair share of broadband 3G, broadband customers both wireless and fixed in Jordan and would leverage that investment we've made. Of course we have some operational challenges which we really can't control in Jordan in terms of electricity costs and various other charges that the government is considering. But again the priority remains one of winning more broadband customers and postpaid customers in Jordan.

In Saudi Arabia, our subsidiary Atheeb continues its transformation to become more a B2B organisation. We still have over 100,000, 102,000 residential broadband customers but the focus is on broadband business, broadband and you may have picked up in the press we have signed an MoU with Mobily subject to the regulator approving that. We are still working together with Mobily to convince the regulator and/or change some aspect of that relationship but that will have good news for us because we will be able to resell quite a lot of capacity that exists within the Mobily network and we will be able to leverage their products and vice-versa. They will be able to leverage the fixed voice product that we have. It's the right combination but again it's pending regulatory approvals, which we expect to be forthcoming in a matter of few weeks.

Yemen, certainly we had an Executive Committee business review session with Yemen only a couple of weeks ago. The business has gone back to normal capacity, 4.1 million customers, significant cash flow and profitability in the last 12 months and despite the company that for over a year-and-a-half to two years all it could offer customers is domestic on-net, so mobile Sabafon to mobile Sabafon. You couldn't terminate a call to the fixed network and you couldn't make IDD calls and you didn't have Internet access. Despite that the company had retained just over 3 million customers and as the environment is improving in Yemen, it has now gone back to 4.1 million and we are planning to expand the network, repair some parts of the network that got damaged from various activities. But we are planning now to expand the capacity of the network to about 5.5 million to 6 million customers by the end of 2013 because we do anticipate further growth.

The M&A activity, again Shaikh Mohamed mentioned at the beginning that a key strategic priority is not just to complete the transaction with Cable & Wireless and integrate that company to the operation and achieve the synergies, but it's also important that we are still seeking further profitable growth, not greenfield operations, to acquire companies in geographies that are complimentary to ours to allow for diversification but also to allow for cash flows and dividends which are part of this growth strategy that – we both want to grow but not on the expense of dividends and the expense of profitability.

So in a nutshell, these are the six priorities we have at the Group level right now. I am then happy to answer any more questions if there are and I will hand over to Shaikh Mohamed.

Shaikh Mohamed bin Isa Al Khalifa

Why don't we open up the floor now for any question and answers. We will be happy to answer any question that you have. Go ahead, please.

ACT Operator

Thank you, sir. If any participants would like to ask a question, please press *1 on your telephone. If you wish to cancel your request, please press *2.

The first question is from Christian Kern from JP Morgan. Please go ahead.

Christian Kern – JP Morgan

Hello, gentlemen. Can I just ask in more sort of a strategic question if I may? How would you see the MENA telco landscape in five to ten years? You've made a very decisive move with the acquisitions of the acquisition you've done from CWC. Can you just help us to understand your vision for your company in an evolving MENA telco landscape? Second question would be on the MVNO with Mobily. What would be the target group of some customers here you are addressing, typically, to tackle a niche customers group? I was wondering which group you would be tackling there. Thank you so much.

Shaikh Mohamed bin Isa Al Khalifa

OK, well, I will attempt to answer what we expect the future to look like in the MENA region. Of course, as we have seen in many markets internationally, definitely there should be consolidation happening. However we will see the number of players - the large players really, ones with strong balance sheet, strong customer base being at the forefront. The way that we are positioning our company is really to cater for requirements of niche markets and that's why we entered into these islands away from the MENA region, diversifying to new areas, new geographies. In terms of collaboration, we will see more collaboration happening, more partnerships happening between telecommunications companies. That's as far as my comments are. Peter, you would like to add anymore?

Peter Kaliaropoulos

Just supporting your view, Shaikh Mohamed, certainly if you look strategically on the landscape, consolidation will continue. It may be harder to achieve in terms of timetable in MENA because of some local regulatory issues but you are going to see the industry consolidating further the bigger telecom groups – you know, there are three or four very substantial telecom operators in this region - we believe they will get stronger. A lot of the second-tier operators will try a single product niche to get in the way of the big guys to either be taken over or they will run out of cash. So you are going to have a landscape – in terms of companies you are going to have maybe three-and-a-half, four major brand that are beyond MENA. They are sort of regional and global. You are going to have one company or maybe two but more like one which is that sort of niche, that boutique telco and that has regional capability as well as local capability. And then you are going to see customers migrating from many of the voice products to very high speed broadband applications, IPTV and so on and the voice will be the so-called killer application on a data network.

So you are going to see a transformation on networks to very, very high speed. You are going to see a consolidation of operators down to three or four. You are going to see customers keep demanding very, very high speed, very high value services but that will put pressure on the telcos in terms of CapEx I think. The ongoing CapEx and the upgrade of our infrastructures even in this region will continue for a number of years to come. We still haven't seen video really impacting all our networks and we need to gear up our networks for that capability and the so-called ODT. We talk about ODT, ODT hadn't hit us yet. On the video side we have quite a few voice or message-related applications but the video hasn't hit our networks. So you are going to see more video-driven demand which drives then high speed broadband connections which then drives more of these niche operators out of the business and then you've got the big brands that will dominate the landscape.

You will see more alliances I think in the next five to ten years. You are going to see the lives of Apple, not necessarily Apple, but you are going to see some of the device manufacturers wanting to get a share of recurring revenues. That's the Apple model. I think that's not going to go away. I think some of the other manufacturers will try and find a way or device manufacturers to take a share of the recurring revenues through the application side but also through the airtime as well. And you are going to see some of the network operators like ourselves entertaining alliances to be able to bundle a lot more of the application, the content for a fixed fee per month to various customers.

The enterprise side in the MENA region will grow. I mean there are quite a few customers where B2B is not very sophisticated. The supplier sell boxes but then other companies try to connect these boxes and other companies try to integrate these boxes. So you are going to see on the B2B a significant I think rationalisation and the solutions driven that has been sort of talked about in – has happened in various other countries. You are going to see that solutions mentality for B2B becoming prevalent. The cloud services will take some time but if we are talking five, seven, ten-year horizon, small businesses as they are beginning to grow, they will be happy to use cloud-based computing to run their applications instead of the local PABX, the local switch and so on. Those trends I think will become more and more evident as time goes by and the challenge for the operators is how do we deliver more value to a customer for the same sort of ARPU and try to find an increase in ARPU but at the same time manage the cash flow so we don't keep using the latest technology in the network but the monetisation of that doesn't keep pace with the cash that we spent. That's always a challenge for us.

Christian, your second question, allow me to just maybe clarify what I said before. It was an MOU, memorandum of understanding with Mobily, not an MVNO. In Saudi Arabia, there was an announcement made last week – three MVNO licenses will be issued. There is a process to go through over the next 10 weeks. We have not signed an MVNO with Mobily. We will explore whether it is a strong business case for us to enter into a virtual operator or whether we have a marketing alliance to sell mobility. And I will share with you that's not a decision of the company. But if you look at what's being offered in terms of potential fees that we have to pay for the MVNO, license, revenue share with the government or the regulator in Saudi, the sort of margins that are being offered from the wholesale companies to an MVNO, at this point in time without a lot of detailed analysis, the margins appear to be fairly thin. And when you are not going to win established postpaid customers, you are going to be winning new customers that are coming to the market and they will be looking for a discount, it will be a very challenging business is our current view of making decent cash flow out of it. So again I think for us the jury is out. The Board and the company has to make a decision will we stay in the MVNO and even when we make a decision, obviously we have to make an announcement as a listed company.

Christian Kern – JP Morgan

Thanks for sharing these thoughts and giving me the clarification. It's much appreciated.

Peter Kaliaropoulos

Thank you.

ACT Operator

Sorry, thank you. The next question is from Nishit Lakhotia from SICO. Please go ahead.

Nishit Lakhotia – SICO

Hi, good morning. Thanks for the call. I have a couple of questions regarding the fourth quarter results. One is regarding STel sale. Have you recognised gain of BD 19.2 million from STel sale in this quarter and any update on the legal issue that you have with the local partner there where you have filed the case in England? That's my first question.

Second is on the BD 4.5 million provisional reversal which are expected this quarter. Has that been taken and under what head is it coming? I see basically other operating expenses has been reported in the financial statement. You have a run rate of negative BD 9 million to BD 10 million in the last two, three quarters and that has come slightly positive. So I know there are some one-offs and all inside that. So if you can more clearly describe the one-off in this quarter so that we know exactly how these major adjustments had happened. That's my question.

Secondly, my question is on dividends. Your dividends have fallen almost 50% from 2009 level from 50 Fils to 25 Fils and your payout has come down to 60% if I am looking at the cash dividend component. Can we assume this 60% payout would be like the bottom now in terms of your strategy and how is it going to move forward going forward? Thank you.

Shaikh Mohamed bin Isa Al Khalifa

Thank you, Nishit. I will attempt to answer your last question first and then hand over to Sameer maybe to give you more details. Now, on the dividend, of course we have seen a decline in the net profits of the Group because of the competitive environment and the nature of the market and it's only natural to curtail the dividend payout during the three years if we go back all these years. However, the Board have adopted of course, a policy not to distribute more than 70% of the annual net profit as cash dividend.

This year they chose to also include the share distribution as well. So the combined share and cash, they were satisfied with the 60% of the cash payout because of the impact of the shares. Now we understand of course that the net effect for the shareholder is going to be the same in terms of ownership and in terms of value. However these extra shares are beneficial when we see the changes in the results after the first quarter consolidation of Monaco & Islands and the ongoing growth that we have seen, the turnaround of the situation quarter-on-quarter on our result. So I think the share will be attractive for the investors. We are still in line with our policy in terms of cash dividend not exceeding 70% of the net profit for the year. That's my comment on that last question that you made. The first two questions STel as well as the reversal of certain provisioning, I will invite Sameer to give us some insight on this.

Sameer Altaf

Thanks, Shaikh Mohamed. Nishit, just on the provision reversal, the OpEx reduction that you see this quarter. Yes, we have had certain one-off reversals. As you know, in line with the accounting standards, every quarter, every reporting date, we take a view of the relevant estimates and provisions and depending on any positive settlements that happened. So yes they are affected in Q4.

On the STel one, I will hand over to Peter again.

Peter Kaliaropoulos

OK, STel is very simple. As we announced in October, I think it was end of October, the agreement we had, we have not received the cash and we are now following legal process to ensure we receive the funds. As a result of that we could not book any gain because basically the money has not been received. We filed the court case in the UK courts in December and we are now going through due process. We are not clear at this stage how long it will take but we are pursuing our claims under the settlement agreement, the Deed of Settlement which we believe we have a strong case. So the jury is out on that one. Certainly as soon as – we hoped we can settle without going through full litigation. But at this point in time we are pursuing full litigation and we can't book anything till that happens. I think the 4.5 provision *(inaudible – technical difficulties)*.

Nishit Lakhotia -SICO

OK just –

Sameer Altaf

Nishit, do you have any further questions?

Nishit Lakhotia -SICO

Yes, on this – in terms of one-off reversals, you said yes there have been some one-off reversals. If the STel gain is not there, then you are talking of BD 4.5 million one-off reversal there. Can you highlight a bit more colour on what other one-off charges were there in terms of – because until last quarter you were clearly mentioning how many incremental redundancy expenses were there for the quarter, how it impacted the staff cost. So what has been for the full year? How much of one-off charges have been there? Secondly, is there any other one-off reversals which I think there is because operating expenses have come positive instead of negative BD 9 million to BD 10 million which I was expecting for the quarter? So if you can highlight more colour on that, it will help us in terms of our modelling purpose.

Secondly, on your normalised EBITDA, your normalised EBITDA for third quarter presentation you mentioned it to be around BD 83 million and this quarter you are mentioning it around BD 123 million, so you are talking of almost close of BD 40 million in normalised EBITDA which is more than 50% margins. What is leading to such a high normalised EBITDA during fourth quarter? Thank you.

Sameer Altaf

I will take the normalised EBITDA clarification first. In quarter four, we booked material amount of restructuring expenses in Bahrain and I think this is also in our communication press release. So you will definitely find a big gap between the Q3 EBITDA normalised and the Q4. If you factor in those heavy costs and again we have mentioned roughly about BD 8 million plus, so you will get to that number.

Coming to the one-off reversals, we have during the quarter – again it was in the press release – we got some favourable settlements or orders from our regulator in Bahrain. Obviously based on that, as I said, we take revised estimate of our provisions and take those reversals accordingly. Also in Kuwait and some other jurisdictions, they had again one-off reversals because of the change in the estimate and change in the facts. That's what I would like to say.

Peter Kaliaropoulos

The one-offs have come from regulatory decisions in the two major jurisdictions, right, Bahrain and Kuwait. In Kuwait, for example, when the government tried to – not tried, imposed new pricing, lower pricing on all the ISPs, then the ISPs buy capacity from the Ministry of Communications. They were going to pay for the capacity based on – over time the new prices that the government imposed will be paid over time. They finally negotiate with the government that new lower prices for them to apply immediately. So all of a sudden they were accruing extra costs they were going to pay in that – I mean it was about KD 1.2 million.

Here in Bahrain, again we were – the issues and draft order to fine Batelco Bahrain for some IDD-related activity that was almost two years old, 18 months old. Finally the regulator last quarter came out with a very favourable decision though that that doesn't apply to Batelco. So we had to reverse that provision as well when the flag that BD 4.5 million one-off benefit. These were really regulatory decision because of them it's over sort of BD 10 million, BD 11 million, so it's a big number.

Nishit Lakhotia -SICO

OK, thank you so much.

Shaikh Mohamed bin Isa Al Khalifa

OK, thank you.

ACT Operator

Thank you. Once again if you would like to ask a question, please press *1 on your telephone.

Gentlemen, there appear to be no further questions.

Shaikh Mohamed bin Isa Al Khalifa

OK, very good this means that we have been very transparent and open with all the numbers that we have provided. We thank everybody who have joined us this morning. Again our thanks to Goldman Sachs for setting up this call. Everybody, thank you very much. See you next time.

ACT Operator

Thank you, sir. Thank you, ladies and gentlemen. This does conclude today's presentation. Thank you for participating. You may now disconnect.

END OF CONFERENCE