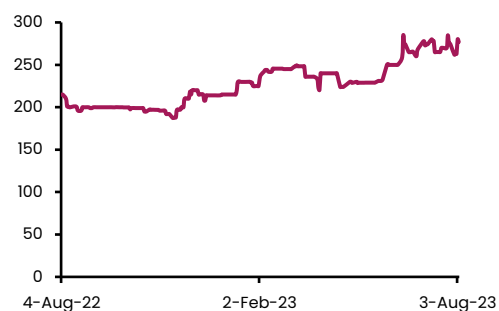




MTNN | ICT | H1:2023

Price	NGN280.00
52-week range	NGN185– NGN285
TP	NGN340.46
Rating	STRONG BUY
Market Cap	NGN5.60trn



Analyst

Moyosore Taiwo

Moyosore.taiwo@arm.com.ng**(MTNN): FX Devaluation limits Bottomline Growth****Earnings Note: H1:2023****Data Revenue Propels Revenue Expansion**

In its recently released H1:2023 financial result, MTN Nigeria Communications Plc (MTNN) posted a higher revenue figure, exceeding its growth level from the previous period. Total revenue grew by 21.96% YoY to NGN1.16trn in H1:2023 (vs. 20.07% YoY in H1:2022), underpinned by strong data revenue growth (+34.79% YoY to NGN469.38bn), improved voice revenue (+13.62% YoY to NGN474.10bn) and other services revenue (+16.62% YoY to NGN215.26bn). However, this impressive growth failed to filter into its bottom line as the company recorded an unrealized foreign exchange (FX) charge of NGN131.45bn in H1:2023. This loss can be linked to the new Nigerian government administration's FX liberalization policy, which resulted in a sharp currency depreciation. Consequently, MTNN recorded a significant 25.40% YoY decline in its profit before tax to NGN200.39bn in H1:2023.

We see a similar trend in MTNN's quarterly performance, as revenue expanded by 23.27% YoY to NGN590.61bn in Q2:2023 (vs. 18.02% YoY in Q2:2022). This growth was largely underscored by solid data revenue performance (+30.30% YoY), a rebounding voice revenue (+19.39% YoY), and other services revenue (+17.68% YoY). The elevated voice revenue can be attributed to a recovery in the aftermath of NIN-related Mobile Sim Card suspensions. Operating costs were also higher in Q2:2023 (24.90% YoY to NGN280.30bn), which limited the pass-through effect of stronger sales, as EBIT closed marginally higher by 24.26% YoY to

NGN214.96bn (vs. +23.03% YoY to NGN172.98bn in Q2:2022). An unrealized FX loss of NGN126.82bn in Q2:2023 reflected higher net finance costs (+255.32% YoY to NGN170.35bn in Q2:2023), and lower profit before tax (-64.32% YoY to NGN44.61bn).

Amidst a challenging macroeconomic business environment, MTNN continues to benefit from its market leader position by driving sales through synergies and aggressive growth, which served to limit the impact of the FX devaluation on its bottom-line. We expect the impact of the FX loss on net finance cost to be one-off, assuming no further significant currency devaluations.

Higher Voice Revenue, Data Continues to Drive Growth

Data revenue continues to propel MTNN's revenue growth, growing 34.79% YoY to NGN469.38bn in H1:2023 (vs. 52.38% YoY in H1:2022). Relative to H1:2022, voice revenue expanded at a faster pace by 13.62% YoY to NGN474.10bn in H1:2023 (vs. 0.91% YoY to NGN417.28bn). We also note higher revenue from other services, largely driven by SMS (40.01% YoY) and Digital (52.54% YoY) services in H1:2023. The overall topline growth can be attributed to an upsurge in subscriber base during the period. As of H1:2023, mobile subscriber count increased by 4.00% to 77.10mn and active data users surged by 11.50% to 41.00mn, fueling topline growth.

Operating Profit: Muted Impact of FX Revaluation on Tower Contracts

EBITDA climbed higher, albeit at a slower pace, by 20.64% YoY to NGN614.45bn in H1:2023 (vs. 22.08% YoY in H1:2022). This was underpinned by the acceleration of total operating expenses (+25.64 YoY in H1:2023 vs. +12.42% YoY in H1:2022). Consequently, EBIT was lower on a YoY basis, recording a 19.66% YoY growth in H1:2023 (vs. 28.72% YoY in H1:2022). It is important to note that the impact of the FX devaluation on operating expenses, which consists of Direct Network Operating Costs (and Built-to-Suit Leases), was muted as lease contracts are renewed quarterly in

advance. Thus, we believe that the full effect would be reflected in MTNN's performance over the next two quarters.

We expect higher operating costs to rein bottom line growth over the next two quarters, as the full extent of the FX devaluation is reflected in the company performance.

Unrealized FX Losses – Profit Margins Negatively Impacted

As of H1:2023, MTNN had a total foreign loan obligation of USD164.90mn which stood at NGN126.56bn (c.14.97% of the total loan portfolio) using an exchange rate of NGN767.5/USD. Shortly before the FX liberalization policy, the Importers and Exporters (I & E) rate stood at NGN471.67 on the official market while the parallel market quoted NGN760.00/USD or a NGN288.30 (61.13%) premium. An exchange rate liberalization (and subsequent convergence) led to a steep devaluation which impacted the finance costs of market operators like MTNN. During H1:2023, the net finance costs for MTNN surged higher by 164.33% YoY to NGN221.18bn (vs. 42.81% YoY in H1:2022). This trickled down to the profit before tax which posited a significant decline of 25.40% YoY to NGN200.39bn in H1:2023 (vs. +24.88% YoY to NGN268.64bn in H1:2022).

After considering the factors outlined, we maintain our bullish stance on MTN Nigeria Communications Plc. and retain a "STRONG BUY" recommendation, with a revised target price of NGN340.46 (21.59% upside potential as of August 7th, 2023). Our positive outlook is predicated on the one-off impact of the steep FX devaluation observed, on net finance costs and sustained topline growth toward the actualization of MTN Ambition 2025. We expect the effect of FX directionality on net finance costs to moderate, albeit with MTNN noting higher operating costs, over the rest of the year. In H1:2023, EBITDA and EBIT margins declined by 58bps and 70bps YoY to 53.03% and 36.38%, respectively. However, excluding the effect of the unrealized FX loss of NGN131.45bn on net finance costs, we observed a stronger coverage ratio as the adjusted

interest coverage ratio in H1:2023 stood at 4.70x (unadjusted: 1.91x), higher than 4.21x recorded in H1:2022. We believe that barring any further significant devaluations, MTNN would continue to post solid performance over the subsequent quarters, with its consistent semi-annual and annual dividend payouts providing additional cashflow benefits.

Overview of Financials H1:2023

Item Lines (Millions of Naira)	H1 2023	H1 2022	% Change
Revenue	1,158,739	950,087	21.96%
Cost of Sales (adj.)	(184,489)	(157,910)	16.83%
Gross Profit	974,250	792,177	22.98%
Operating Expenses (adj.)	(552,675)	(439,875)	25.64%
EBITDA	614,450	509,317	20.64%
Depreciation and Amortization	(192,875)	(157,005)	22.85%
EBIT	421,575	352,312	19.66%
Finance Cost (Net)	(221,184)	(83,677)	164.33%
Profit Before Tax	200,391	268,635	-25.40%
Tax Expense	(71,703)	(87,006)	-17.59%
Profit After Tax	128,688	181,629	-29.15%
Balance Sheet Extract (Millions of Naira)	H1 2023	H1 2022	% Change
Total Asset	3,137,844	2,527,135	24.17%
Shareholders Fund	258,277	267,646	-3.50%
Long-term Liability	1,254,462	1,096,248	14.43%
Short-term Liability	1,623,565	1,161,352	39.80%
Ratios	H1 2023	H1 2022	% Change
Gross Margin	84.08%	83.38%	0.70%
EBITDA Margin	53.03%	53.61%	-0.58%
Operating Margin	36.38%	37.08%	-0.70%
Net Margin	11.11%	19.12%	-8.01%
Return on Asset	4.10%	7.19%	-3.09%
Return on Equity	49.83%	67.86%	-18.04%
Basic EPS (NGN)	1.38	4.19	-67.06%

Overview of Financials Q2:2023

Item Lines (Millions of Naira)	Q2 2023	Q2 2022	% Change
Revenue	590,605	479,103	23.27%
Cost of Sales (adj.)	(95,352)	(81,712)	16.69%
Gross Profit	495,253	397,391	24.63%
Operating Expenses (adj.)	(280,295)	(224,407)	25.64%
EBITDA	311,805	252,169	23.65%
Depreciation and Amortization	(96,847)	(79,185)	22.30%
EBIT	214,958	172,984	24.26%
Finance Cost (Net)	(170,346)	(47,942)	255.32%
Profit Before Tax	44,612	125,042	-64.32%
Tax Expense	(17,223)	(40,237)	-57.20%
Profit After Tax	27,389	84,805	-67.70%
Balance Sheet Extract (Millions of Naira)	Q2 2023	Q2 2022	% Change
Total Asset	3,137,844	2,527,135	24.17%
Shareholders Fund	258,277	267,646	-3.50%
Long-term Liability	1,254,462	1,096,248	14.43%
Short-term Liability	1,623,565	1,161,352	39.80%
Ratios	Q2 2023	Q2 2022	% Change
Gross Margin	83.86%	82.94%	0.91%
EBITDA Margin	52.79%	52.63%	0.16%
Operating Margin	36.40%	36.11%	0.29%
Net Margin	4.64%	17.70%	-13.06%
Return on Asset	0.87%	3.36%	-2.48%
Return on Equity	10.60%	31.69%	-21.08%
Basic EPS (NGN)	1.38	4.19	-67.06%

ARM ratings and recommendations

ARM now employs a two-tier rating system which is based on systemic importance of the security under review and the deviation of our target price for the stock from current market price. We characterize systemic importance as a function of a stock's ranking among the group of top 20 stocks by NSE market capitalization over a trailing 6-month period (minimum) to the review date. We adopt a 5-point rating system for this category of stocks and a 3-point rating system for stocks outside this group. The choice of top 20 stocks arises from the consideration that this group of stocks constitutes >75% of overall market capitalization and stocks outside this group are generally less liquid and individually account for <1% of market capitalization. For stocks in both categories, the basis for ratings subject to target price deviation is outlined below:

TOP 20		NON-TOP 20	
Rating	Deviation	Rating	Deviation
STRONG BUY	>20%	BUY	>20%
OVERWEIGHT	10% – 20 %	NEUTRAL	5% – 20 %
NEUTRAL	0% – 10 %	SELL	<5%
UNDERWEIGHT	-5% – 0%	N/A	
SELL	<-5%		

RECOMMENDATION KEY

Rating	Recommendation
BUY	Accumulate security to a substantial extent constrained only by portfolio diversification considerations
OVERWEIGHT	Accumulate security to an extent moderated by cognizance of its benchmark weight
NEUTRAL	Maintain status quo for security with respect to current holding—i.e. keep if already holding and don't otherwise—subject to reasonable portfolio constraints
UNDERWEIGHT	Minimize exposure to security taking cognizance of its index weighting
SELL	Sell-off security completely from portfolio

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