



Nigerian Telecommunications Sector Report

A Beacon of Hope

March 2023

Executive Summary

2022FY¹ in the global economy was pervaded by uncertainties as the Russian-Ukraine conflict persisted, causing supply-chain disruption and rising energy costs globally. We witnessed the pass-through effect on energy costs in Nigeria, and the telecommunications sector was not spared from the unfortunate incident. However, the industry still recorded decent growth, as evidenced by their most recent financial results and contribution to the nation's GDP numbers.

Coming to the peculiar development in the sector, in 2021, the telco players took some heat in their voice revenue as the Government introduced the critical linkage of NIN² to customers' SIM³. As a result, the companies had to stop SIM sales in the period, impacting subscribers' growth. In 2021, total subscriptions declined by 4.47%. Furthermore, in April 2022, the Federal Government directed the telcos to ban SIMs without NIN linkage.

Given the sector's resilience and the country's favourable demography, we witnessed a surge in Data Revenue in 2022. This boosted the industry's total revenue in the period. Furthermore, it was an eventful year for the sector, as the media was laced with news of 5G deployment, final PSB license awards, Elon Musk's Starlink entrance into the market and Google's Submarine cables. Considering these developments, we are optimistic of the growth in the sector and its overall impact on the economy in 2023FY.

Across the companies under our coverage, we issue a 'STRONG BUY' rating on MTNN and a 'SELL' rating on Airtel Africa. We opine that Airtel Africa is overvalued at the current market price of NGN1,548.7 as of 16th March 2023.

¹ Full-Year

² National Identification Number

³ Subscriber Identity Module



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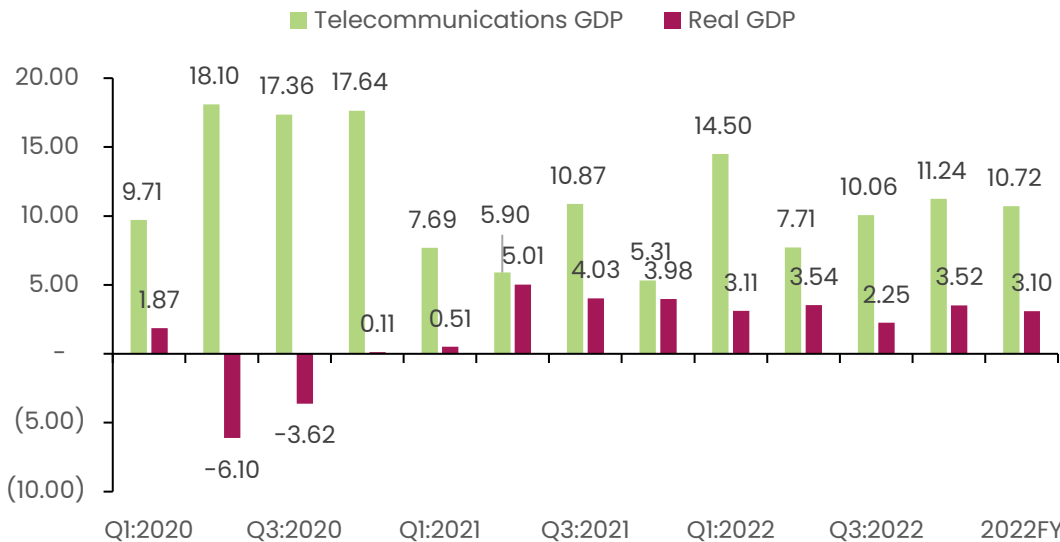
Demographic Evolution

Nigeria remains one of the most densely populated countries in the world. In the most recently released demographic statistics by the National Bureau of statistics, we observed that working people represents the bulk of the population. Meaning, the population with the wherewithal to pay for telecommunications service is enormous and with an outlook for a growing population, that can only mean well for patronage of telecommunication services.

Resilience and Value: An Industry with Enormous Potential

Despite the most recent exacerbations that have engulfed the Nigerian economy, as the oil sector is continually encumbered by first, the concern of plummeting global demand for energy, and the most recent issues around Vandalism and restart concerns, the Nigerian non-oil sector has shown great resilience to provide the required macroeconomic tailwind. Chiefly among the sectors that have continued to ensure this sustained tailwind is the Nigerian telecommunication sector.

Figure 1: Telecommunications GDP and Total Real GDP

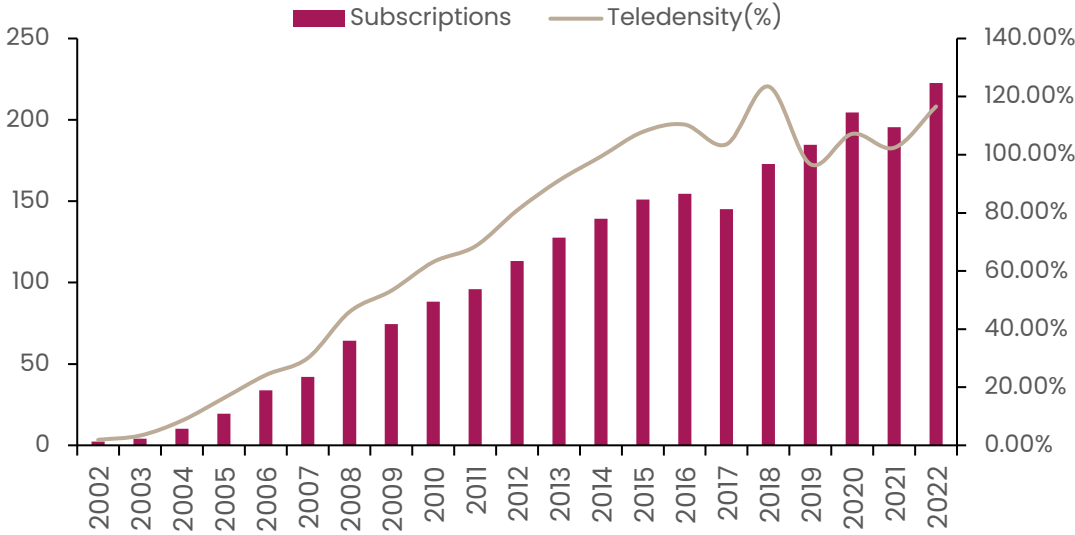


Source: NCC, ARM Research



Over two decades, the telco operators have continued to improve telephone penetration in the country, with telephone subscribers increasing from 2.27million in 2002 to 222.57million in 2022.

Figure 2: Total Active Telephony Subscribers (Millions) and Teledensity



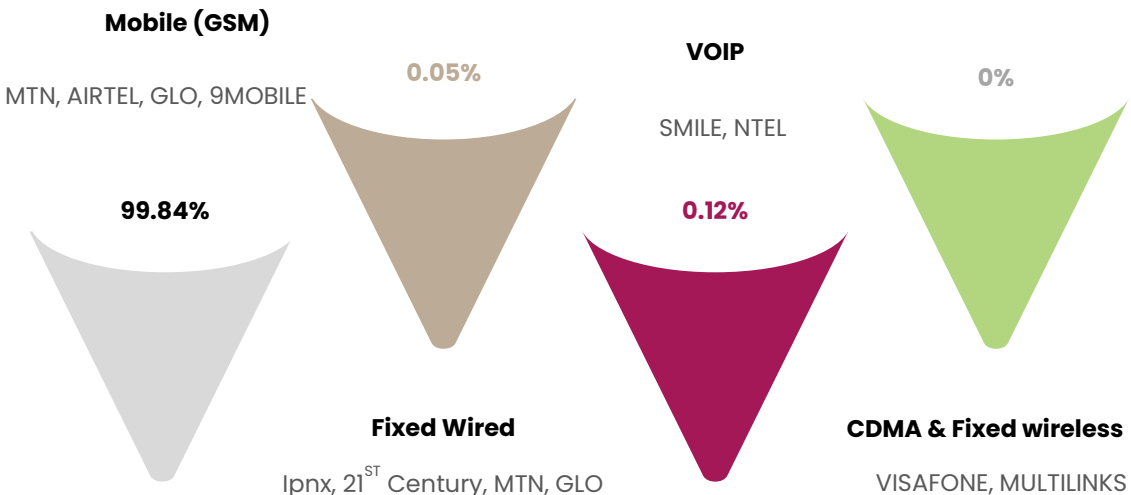
Source: NCC, ARM Research

Industry Competitive Landscape - MTN Nigeria (MTNN) Remains Market Leader

The market structure in the telecommunications industry remains oligopolistic, as MTNN remains the leader of the pack. In the mobile telecoms segment, specifically, the Global System for Mobile Communications (GSM), MTNN leads in the telecommunication space with a 40.71% market share (91.95 million subscribers) as of January 2023. The GSM segment of the telecommunication sector represents a 99.84% market share by technology as shown in Figure 3 below.



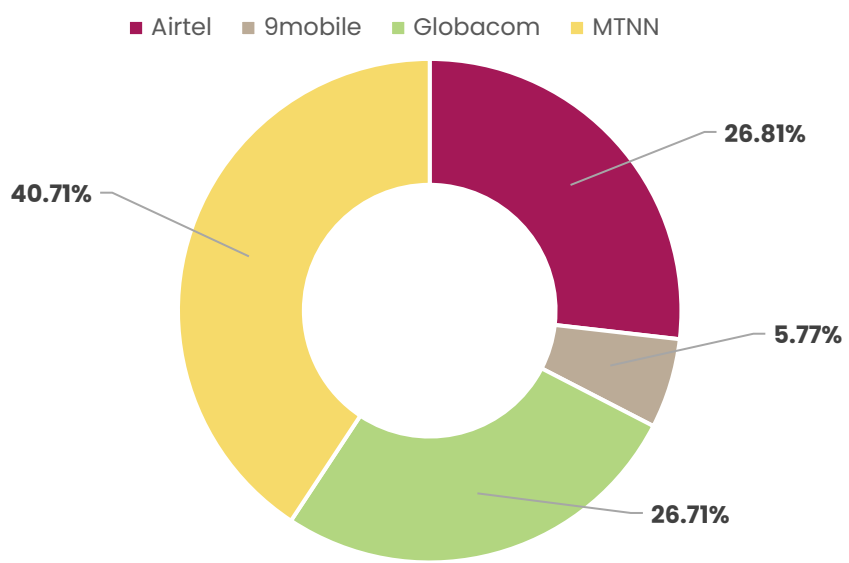
Figure 3: Market Share by Technology as of January 2023



Source: NCC, ARM Research

In August 2001, the first GSM technology was launched by MTN Nigeria. After, Econet (now Airtel Africa), also launched its own Nigerian subsidiary. Furthermore, Globacom entered the market in 2003 and then Etisalat (now 9mobile) in 2009. These four operators have remained the major participants in the market, with MTNN persisting as the sector's market leader.

Figure 4: Market Share of Mobile Operators as of January 2023



Source: NCC, ARM Research



Regulatory Encumbrances: Shrugging off the NIN-SIM Impact

The Nigerian Communications Commission (NCC), through the NCC Act provides a regulatory framework for the Nigerian telecommunications industry. The commission is responsible for issuing necessary licenses for the supply of telecommunications services. Like Banks, the sector faces strict regulations.

In 2021, the commission directed the telecoms consumers to link their National Identity Number (NIN) with their Subscriber Identity Modules (SIMs) as required by the Federal Government, banning new SIM card sales in the period. Consequently, subscriptions declined by 4.47% to 195.46million in 2021. Furthermore, by April 2022, the Federal Government directed the telco companies to bar outgoing calls on all unlinked lines. This affected subscribers' growth in the period. However, the telco players seem to have shrug off the negative impact of the directives as evidenced by the 13.87% growth subscribers base (222.57million) in 2022.

Shifting to a 'survivor mode', the telco players switched their focus to Data revenue, surmounting growth expectations in 2022. For context, MTNN and Airtel Africa grew its Data revenue by 48.02% (2022FY) and 16.95% (9M⁴:2023) respectively.

Broadband Penetration

On broadband penetration, according to the NCC, broadband penetration as of January 2023 had reached 48.20%. To understand what broadband penetration is, there is the need to technically define broadband. According to the Nigerian National Broadband plan (2020 – 2025), broadband was defined as connectivity delivering a minimum of 10 Mbps⁵ in rural areas and a minimum of 25 Mbps in urban areas to every Nigerian at an affordable price and quality by 2025. The level of broadband penetration would depend on the number of people that can access this service.

The Federal Government, through the NCC plans to reach a 70% penetration by 2025. We believe an aggressive roll out of telecommunication infrastructure, especially in

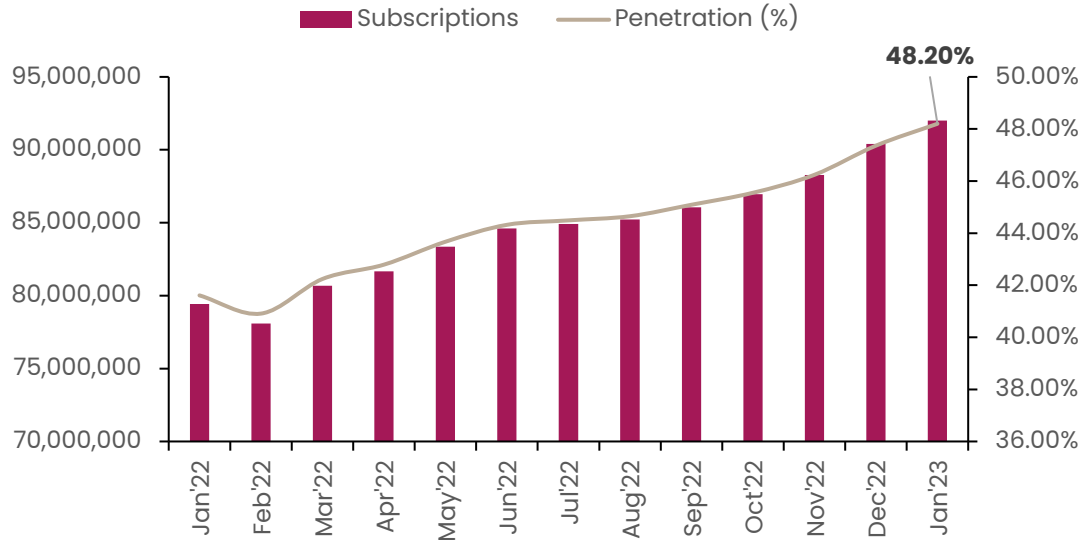
⁴ 9-Month

⁵ Megabits per seconds



the rural areas, would help actualize the commission's goal. Recently, the Minister of the Federal Capital Territory (FCT) slashed Right of Way (RoW) charges by 90% for telcos who want to invest in green areas (places lacking telecommunication infrastructure). We believe this form of incentives should be adopted nationally to encourage telcos willing to set up their infrastructure in rural communities.

Figure 5: Broadband Penetration in Nigeria



Source: NCC, ARM Research



Sector Update – More Inclusion in the Offing

Payment Service Banks (PSBs)- Driving Financial Inclusion

On a quest to drive financial inclusion, in 2018, the CBN introduced new regulatory guidelines for the creation of PSBs with the goal of driving customer deposits, savings, and remittances, particularly in the rural and un-banked regions. This guideline allowed the telcos apply for PSB license through their subsidiaries. With the PSB license, the telcos can provide the outlined services below:

- ❖ Accept deposits from individuals and small businesses which would be covered by the deposit insurance scheme.
- ❖ Invest in FGN and CBN securities.
- ❖ Operate electronic wallet
- ❖ Provide inbound remittance services.
- ❖ Issue prepaid and debit cards on its name.
- ❖ Provide POS and ATM services.
- ❖ Provide financial advisory services

In April 2022, MTNN was granted final approval to operate mobile money (MoMo) payment service bank (PSB) license in Nigeria. Airtel Africa also launched its SMARTCASH PSB in May 2022. These developments bode well for Nigeria's unbanked population as it would serve as a gateway into the financial services sector. Taking cognizance of its existing customer base and its significant presence in the country, we are quite optimistic about the impact these two telco giants (MTNN & Airtel Africa) would have on its widespread usage.

In terms of constituting a threat to the traditional banks, we hold the view that the services are going to be complementary. Already, MTNN alluded to some form of partnership with deposit money banks in its 2022FY financial results press release.



Introducing Fifth Generation (5G) Technology – An End to Low Broadband Penetration?

MTNN launched the Fifth Generation (5G) services in Q3:2022 following the successful bid of the 3.5 Gigahertz (GHz) spectrum license. The two awardees of the license were MTN Communications Nigeria Plc and Mafab Communications Limited, each paying USD273.6 million for the license.

In December, 2022, NCC auctioned the remaining lots of 2 x 100MHz in the 3.5GHz spectrum band. However, Airtel Africa emerged the only bidder, after another company, Standard Network, failed to pay the necessary deposit to make a bid. On 9th January, 2023, Airtel Africa announced that it had acquired the 4G and 5G spectrum for a consideration of USD316.7million.

The MTN launch, placed Nigeria as the third African nation to roll out a 5G network after South Africa and Kenya. However, despite the increasing infrastructure investment, there exists a threat of a slow adoption as the country and the continent (Africa) is laced with low penetration of 5G devices, with its focus currently on 4G support.

Elon Musk's Starlink – A threat to Existing Players?

In May 2022, Elon Musk announced that Starlink, the satellite internet service launched by SpaceX, has been approved in Nigeria and Mozambique. Its launch in Nigeria has been in the works since 2021, gaining approval to operate a year later.

Starlink is currently modelled to operate as a non-mobile internet provider, a fixed broad-band service. Although the mobile telecoms players offer fixed broad band service along with their mobile (GSM) service, it constitutes a small portion of their revenue. Starlink operates with a speed of over 100 mbps, almost five (5) times higher than the highest median download speed recorded in Nigeria for fixed broad band (iPNX: 21.34 mbps).

Considering this development, we opine that the key players in the fixed broad band service would need to improve their internet speed to compete favourably in the



market. In terms of pricing, Starlink is expensive to the average Nigerian household, costing USD600 (about NGN276,554 based on official⁶ rate and NGN447,000 based on parallel⁷ market rate) for its hardware and USD43 monthly subscription. We have found that the nature of the cost (the majority being fixed) would still allow some sizable adoptions. On the other hand, we might witness a low adoption rate for some completely different reason, which is the issue around the uncertainties of the climatic condition in Nigeria. Overall, it is a welcomed development as it would help with delivering a wider broad band coverage.

Google's Equiano Subsea Cable – A Much Needed Infrastructure

Sometime in April 2022, Google's Equiano subsea cable landed in Lagos, Nigeria. The subsea internet cable project is expected to ensure that the unserved and underserved, especially in Africa, have a high-speed affordable internet. In terms of connectivity, it is expected to increase internet speed, reduce internet retail price, and increase internet penetration. This aligns well with the broadband plan of the nation and we opine it could set the country up for success in reaching its 70% broadband penetration goal by 2025.

⁶ I & E rate of NGN461.09 to USD1 as of 15th March 2023

⁷ NGN745 to USD1 as of 15th March 2023





Company Analyses



Company Analyses

MTN NIGERIA COMMUNICATIONS PLC (MTNN)

MTN Nigeria Communications Plc is part of the MTN Group - MTN International (Mauritius) Limited, incorporated in the Republic of Mauritius, which operates in 21 countries in Africa and the Middle East. MTN Nigeria since its debut in 2001, have maintained its leadership status in the market.

The company derives most of its revenue from Voice and Data service. Other service offerings include SMS⁸, roaming, handset & accessories, Digital, ICT, cloud, and infrastructure services. Although voice revenue represents the bulk of its total revenue, data revenue has grown at a faster pace over time. We allude this to the increasing internet penetration and the favourable demographics of the country.

In its recently released financial results, data revenue accounted for 69.23% of the total growth in revenue. Given a society that is becoming more digitalized as businesses and people evolve, we opine that MTNN would continue to leverage on increased data traffic (consequently data revenue) and fintech revenue to drive overall revenue growth.

Its recent MoMo PSB license allows the company to scale its fintech and digital service business, while aiding the growth of financial inclusion in Nigeria. As of 2022FY, the company reported approximately 14.9 million active users and 2 million active MoMo agents. The 5G rollout is also expected to scale its data service revenue in 2023FY.

⁸ Short Message Service



Price	NGN236
52-week range	NGN185-NGN270
TP	NGN352.96
Rating	STRONG BUY
Market Cap	NGN5.05trn

MTNN 2022FY Performance- Ahead of the Pack

In its recently released 2022FY financials, MTN Nigeria Communications Plc (MTNN) posted an impressive topline performance, making it the first quoted company on the Nigeria Stock Exchange to post a NGN2trn revenue. Total Revenue grew by 21.64% YoY to NGN2.01trn. The impressive revenue performance rode on the faster growth in Data revenue (+48.02% YoY to NGN763.94bn) and a recovery in its Voice revenue (+6.01% YoY to NGN864.61bn) in 2022FY. Despite the macroeconomic challenges which has engulfed the operation of businesses across the country, as evidenced by the surge in Operating Expenses (+18.79% YoY to NGN600.30bn), the telco giant was able to grow its Profit After Tax (PAT) by 20.16% YoY to NGN358.87bn.

MTNN-Share Price Trend



Analyst

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MTNN defied the odds and posted an impressive 2022FY financial performance despite the challenges faced in the immediate business environment as well as global headwinds. We arrived at a target price of NGN352.96 for 2023FY using a blend of absolute (Discounted Cash Flow) and relative (P/E multiple and EV/EBITDA multiple) valuations. This represents a 50% upside from its current closing price of NGN236 as of 16th March, 2023. Thus, we rate MTNN a STRONG BUY.

Topline Performance Boosted by Data Revenue

Total Revenue grew by 21.64% YoY to NGN2.01trn on the back of improved Data Revenue (+48.02% YoY to NGN763.94bn). For context, Data revenue in the period accounted for 69.23% of total revenue growth. This is largely supported by improved data traffic in 2022FY (+66.6%) as the telco giant continues to drive expansion in its 4G network (79.1% coverage in 2022 vs 70.3% in December 2021). Furthermore, we note a continued recovery in Voice revenue, growing by 6.01% YoY to NGN864.61bn in the period.



Rising Cost of Operation Amid Macroeconomic Headwinds

Cost of Sales rose by 25.64% YoY to NGN341.61bn, an offshoot of improved gross connections in the period as well as base effect from 2021FY, a period where sales of new SIM was suspended. Similarly, OPEX⁹ rose by 18.79% YoY to NGN600.3bn due to exacerbated energy costs, acceleration in site rollout and the impact of Naira depreciation in the period. As a result, BTS lease cost (power and maintenance) rose by 14.86% YoY to NGN331.85bn in the period.

Impressive Bottomline Performance Amid Rising Finance and Depreciation Costs

Earnings Before Tax (EBT) grew by 22.28% YoY to NGN533.97bn despite the momentous surge in finance cost (+33.19% YoY to NGN213.09bn) and depreciation and amortization (+15.31% YoY to NGN337.07bn). We attribute the sharp increase in finance cost to higher borrowings (+39.92% YoY) amidst rising interest rate environment. The higher depreciation cost reflects the increased site rollout in the period. Taxation for the period surged 26.85% YoY to NGN175.10bn partly due to the increase in the education tax rate to 2.5% and the tax paid on investments in government securities following the expiration of the 10-year tax exemption period. Overall, Profit After Tax (PAT) grew by 20.16% YoY to NGN358.88bn.

Outlook: Impressive Outing Ahead

Despite the rising operation cost environment, we expect MTNN to post higher growth in its topline performance as the company continues to maintain its current position as the market leader. We opine that Voice revenue would witness a considerable growth in 2023FY barring any regulatory glitch in the sector. We arrived at a target price of **NGN352.96** for 2023FY using a blend of absolute (Discounted Cash Flow) and relative (P/E multiple and EV/EBITDA multiple) valuations. This represents a 50% upside from its current closing price of NGN236 as of 16th March, 2023. Thus, we rate MTNN a **STRONG BUY**.

⁹ Operating Expenses



MTNN- 2022FY Financial Highlights

NGN'million	2022FY	2021FY	YoY
Total Revenue	2,012,272	1,654,299	21.6%
Cost of sale	(341,607)	(271,884)	25.6%
Opex	(600,300)	(505,344)	18.8%
EBITDA	1,070,365	877,071	22.0%
Operating Profit	733,298	584,747	25.4%
PBT	533,972	436,687	22.3%
PAT	358,877	298,654	20.2%
EPS	17.8	14.7	21.3%
EBITDA Margin	53.2%	53.0%	0.4%

NGN'million	2021FY	2022FY	2023F	2024F	2025F
Total Revenue	1,654,299	2,012,272	2,414,726	2,897,672	3,477,206
Cost of sale	(271,884)	(341,607)	(424,992)	(521,581)	(625,897)
Opex	(505,344)	(600,300)	(702,351)	(821,751)	(961,448)
EBITDA	877,071	1,070,365	1,287,384	1,554,340	1,889,861
Operating Profit	584,747	733,298	916,610	1,146,489	1,441,224
PBT	436,687	533,972	674,803	853,678	1,087,183
PAT	298,654	358,877	453,528	573,748	730,684
EPS	14.7	17.8	19.7	19.8	22.1
EBITDA Margin	53.0%	53.2%	53.3%	53.6%	54.3%



AIRTEL AFRICA (AIRTELAFRI)

Airtel Africa is the second largest mobile telecommunications operator (by market share) in Nigeria. Airtel Africa derives its major revenue from voice, data and mobile money revenue. Airtel Africa currently operates in 14 countries across Africa.

Like its peer (MTNN), data revenue has grown at a faster pace in recent times as the economy gradually embrace technology. In its 9M:2023 financial result, data revenue accounted for 43.41% of the total growth in revenue. In a quest to improve internet penetration, the company invested heavily on spectrum acquisition in 2022. Airtel DRC¹⁰ purchased 58 MHz¹¹ of additional spectrum, spread across 900, 1,800, 2,100 and 2,600 MHz bands, for a gross consideration of USD42mn in June 2022. Airtel Kenya Networks Limited purchased 60 MHz of additional spectrum in the 2,600 MHz band for a gross consideration of USD40mn in July 2022.

Airtel Tanzania plc also purchased 110 MHz spectrum spread across the 2,600 MHz (2 blocks of 2x15MHz) and 3,500 MHz bands for a gross consideration of USD60mn in October 2022. Airtel Zambia purchased 60 MHz of additional spectrum spread across the 800 MHz and 2600 MHz bands for a gross consideration of USD29mn in November 2022. Finally, on 9th January 2023, the company announced it had purchased 4G and 5G spectrum for a gross consideration of USD316.7mn in Nigeria.

We expect the company to continue to leverage on its large customer base, and increase data traffic even as it deploys these spectrums.

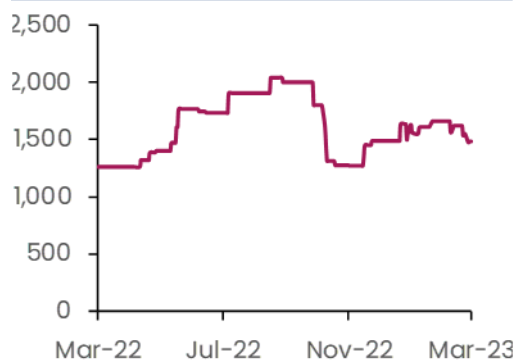
¹⁰ Democratic Republic of Congo

¹¹ megahertz



Price	NGN1,548.7
52-week range	NGN1,147.5-NGN2,095.9
TP	NGN1,340.86
Rating	SELL
Market Cap	NGN2.26trn

AIRTELAFRI-Share Price Trend



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9M:2023 Performance- Impacted by Macroeconomic Headwinds

In its 9M:2023 financials, Airtel Africa posted a growth in its total revenue (+12.08% YoY to USD3.9bn) mainly driven by its Data Revenue. On the flip side, Total expenses (excl. depreciation and amortization) rose by 11.69% YoY to USD2.01bn, an offshoot of rising energy costs in the period. Overall, Profit After Tax (PAT) grew marginally by 1.75% YoY to USD523mn.

We arrived at a 12-month target price of NGN1,340.86 using a blend of absolute (Discounted Cash Flow) and relative (P/E multiple and EV/EBITDA multiple) valuations. This represents a 13% downside from its current closing price of NGN1,548.7 as of 16th March, 2023. Thus, we rate AIRTELAFRI a SELL.

Topline Performance Boosted by Data Revenue

Total Revenue grew by 12.08% YoY to USD3.9bn on the back of improved Data Revenue (+16.95% YoY to USD1.32bn) and Mobile Money Revenue (+26.85% YoY to USD515mn). Data revenue continues to take the lead in total revenue growth, an offshoot of improved data traffic. Voice revenue grew slightly by 7.16% YoY to USD1.87bn in 9M:2023. Overall, the slower growth in total revenue is alluded to the NIN-SIM effect on voice revenue in Nigeria and the loss of tower sharing revenues following the sale of towers in Tanzania, Madagascar and Malawi in H2:2022.

Rising Expenses Impacted by Macroeconomic Environment

Total expenses (excl. depreciation and amortization) in the period rose by 11.69% YoY to USD2.01bn. The surge in total expenses is not surprising, as higher energy costs continues to take its toll on network operating expenses. Net Finance cost spiked (78.35% YoY) to USD519mn on the back of higher derivative losses and foreign exchange losses arising from Naira devaluation (USD70mn), Malawian Kwacha,



Ugandan and Kenyan shilling (USD53mn). Interest cost in the period was higher, an offshoot of higher lease liabilities and increasing interest rates.

Bottomline Performances Constrained by Higher Finance Cost

Airtel Africa grew its Earnings Before Interest, Depreciation and Tax (EBITDA) by 12.57% YoY to USD1.92bn and slightly improved its EBITDA margin by 20bps to 49%. Profit Before Tax (PBT) declined by 7.29% YoY due to the spike in net finance cost. Taxation tapered by 2.86% YoY due to the recognition of a deferred tax credit of USD62mn in Kenya. Overall, Profit After Tax (PAT) grew marginally by 1.75% YoY to USD523mn.

Strong Revenue Performance Alluded to Nigeria Segment

We recognize that Nigeria remains the largest market for Airtel Africa as it constitutes a sizable chunk in its overall performance. For context, Nigeria contributed 40.50% to total revenue in the period. Revenue in Nigeria grew at a faster pace compared to the Group, rising by 15.69% to USD1.59bn in the nine (9) month period.

The impressive outing follows a surge (+21.15% YoY to USD653mn) in Data Revenue and a recovery in Voice revenue (+10.32% YoY to USD791mn) in the period. This growth is driven by growth in its overall customer base (+13%) and data customer base (+16%) in the period. On profitability, EBITDA grew by 7.52% YoY to USD815mn. However, due to rising operating costs amidst rising energy costs, the EBITDA margin declined by 388bps to 51.42% in the period.

Outlook: Better Days Ahead

Despite macroeconomic headwinds, we expect Airtel Africa to post decent 2023FY performance. We expect to see more recovery in voice revenue in its Q4:2023 earnings result. We arrived at a 12-month target price of **NGN1,340.86** using a blend of absolute (Discounted Cash Flow) and relative (P/E multiple and EV/EBITDA multiple) valuations. This represents a 13% downside from its current closing price of NGN1,548.7 as of 16th March, 2023. Thus, we rate AIRTELAFRI a **SELL**.



AIRTEL AFRICA- 9M:2023 Financial Highlights

USD'million	9M:2023	9M:2022	YoY
Total Revenue	3,914	3,492	12.1%
Expenses excl. Depreciation	(2,007)	(1,797)	11.7%
EBITDA	1,916	1,702	12.6%
Operating Profit	1,318	1,146	15.0%
PBT	801	864	-7.3%
PAT	523	514	1.8%
Basic EPS	12.5	11.7	6.8%
EBITDA Margin	49.0%	48.8%	0.4%

USD'million	2021FY	2022FY	2023F	2024F	2025F
Total Revenue	3,919	4,724	5,218	5,845	6,546
Expenses excl. Depreciation	(2,119)	(2,445)	(2,680)	(3,118)	(3,601)
EBITDA	1,800	2,279	2,539	2,727	2,945
Operating Profit	1,119	1,535	1,735	1,859	2,008
PBT	697	1,224	1,043	1,133	1,245
PAT	415	755	590	680	747
EPS (cents)	9.0	16.8	16.7	17.5	18.4
EBITDA Margin	45.9%	48.2%	48.6%	46.7%	45.0%



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 buy 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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