

Valuation Summary

- We have placed Safaricom Limited under review as we update the valuation following release of its H1'2018 results
- Safaricom Limited is currently trading at a P/E of 20.3x and a dividend yield of 4.1% at the current price of Kshs 25.8, as at 3rd November 2017

Key highlights during the year

- Safaricom Limited registered a growth in their subscriber market share to 72.6% as at June 2017 from 65.2% in June 2016. Total customer base grew by 10.8% to 29.5 mn as at September 2017 from 26.6 mn as at September 2016,
- Safaricom enhanced the quality and coverage of its network currently at 96% population coverage with 4G at 32% and 3G at 85%,
- Safaricom launched an innovation hub, accelerated the roll out of their Fibre To The Home (FTTH) network, upgraded the M-PESA platform and extended the M-PESA 1-tap. The firm is also on course with an E-commerce platform in readiness for its launch,

Financial Performance:

- Normalised EBITDA grew by 14.4% to Kshs 54.3 bn from Kshs 47.5 bn in H1'2017 after adjusting for a one-off item in 2016 of Kshs 3.4 bn. Core earnings per share grew by 9.0% to Kshs 0.65 from Kshs 0.6 in H1'2017. Adjusting for the one-off item in 2016, core earnings per share grew by 21.4% to Kshs 0.65 from Kshs 0.54 in H1'2017. The earnings growth was supported by a 12.0% growth in service revenue (M-PESA, messaging, mobile data, fixed service) to Kshs 109.7 bn from Kshs 98.0 bn in H1'2017 due to growth in active users and increased usage of non-voice services. Key highlights for the half year performance include:
- Core earnings per share grew by 9.0% to Kshs 0.65 per share from Kshs 0.60 per share in H1'2017. This performance was driven by a 12.0% growth in service revenue (M-PESA, messaging, mobile data, fixed service) to Kshs 109.7 bn from Kshs 98.0 bn in H1'2017 due to growth in active users and increased usage of non-voice services;
- Voice revenue grew by 3.6% to Kshs 47.4 bn from Kshs 45.7 bn in H1'2017, while messaging revenue grew by 3.4% y/y to Kshs 8.9 bn from Kshs 8.6 bn. This growth was supported by a 10.8% y/y growth in the number of total customers to 29.5 mn from 26.6 mn in H1'2017. However, the voice monthly average revenue per user (ARPU), declined by 7.8% to Kshs 271.2 per user from Kshs 294.0 per user, indicating that the traditional revenue streams are not benefitting as much from the increasing customer base. Voice revenue now accounts for 43.2% of service revenue, down from 46.6% in H1'2017;
- M-Pesa revenue rose 16.2% to Kshs 30.1 bn from Kshs 25.9 bn in H1'2017. This was supported by the 12.1% growth in registered M-Pesa customers to 27.8 mn, and an increase in activity as measured by users who were active in the last 30 days by 9.5% to 19.3 mn from 17.6 mn. M-Pesa currently accounts for 27.4% of total revenue, a slight improvement from 26.4% in H1'2017. The cashless platform, Lipa na M-Pesa, continues to be adopted by firms and currently has over 70,000 merchants on a 30-day active basis;
- Mobile data revenue grew by 31.0% y/y to Kshs 17.6 bn from Kshs 13.4 bn, driven by a 13.5% increase in 30-day active mobile data customers to 17.0 mn from 14.9 mn in H1'2017 and increased smartphone penetration. Currently there are over 90,000 homes and 1,670 commercial buildings with FTTH network, further driving the growth in data usage;
- Fixed service revenue grew by 34.7% to Kshs 3.2 bn from Kshs 2.4 bn driven by a 24.9% growth in 30-day active fixed service customers to 14.1 mn from 11.3 mn;
- Normalised EBITDA grew by 14.4% to Kshs 54.3 bn from Kshs 47.5bn in H1'2017, after adjusting for a one-off item in 2016 of Kshs 3.4 bn;
- Return on Average Assets improved to 26.0% in H1'2018 from 24.2% in H1'2017 while Return on Average Equity increased to 57.1% in H1'2018 from 51.2% in H1'2017,
- The board of directors did not recommend payment of an interim dividend;
- EBIT guidance for FY'18 has remained in the range Kshs 71-75 bn, while capex guidance is Kshs 35-38 bn. The telco is carefully monitoring their CAPEX as they set up 4G sites to 40 out of 47 counties;

Key take-out:

- The mobile money segment continues to experience increased competition with latest data from the Communications Authority showing that Safaricom's market share by value of transactions declined to 74.2% for the quarter ended June 2017 from 76.1% in the previous quarter. The decline in market share could be attributed to increased adoption of Equitel, M-PESA's main competitor, with its market share growing to 25.6% from 23.2% in the previous quarter,
- With regards to revenue streams, the non-voice service revenue (M-pesa, SMS, mobile data) continues to be the main growth driver currently accounting for 56.8% of service revenue and recording a growth of 19.3% to Kshs 62.4 bn.

Safaricom's strategy going forward will be driven by:

- Investing in their network to enhance capacity, coverage and quality, including the rolling out of 4G network to additional sites in 40 out of 47 counties
- Improving customer experience by investing in additional call centres. Safaricom has started the creation of additional 300 customer care jobs and opening a new centre in Eldoret
- Increased localization as the company subdivides the business into regions each with its own head to provide tailor-made regional promotions and offers with the strategy being driven forward by the new Regional Operations division

The company has maintained their target estimates for FY'2018 as below;

- EBIT to range between Kshs 71-75 bn,
- Capital expenditure to range between Kshs 35-38 bn. Safaricom has invested Kshs 17.4 bn on capital expenditure in H1'2018.

Below is a summary of the key line items in the balance sheet and income statement

Figures in Kshs billions unless otherwise stated

Revenue Source	H1'2018	H1'2017	% Contribution to Total Revenue	y/y change	Number of active users (mn)
Voice	47.4	45.7	41.3%	3.6%	22.2
M-Pesa	30.1	25.9	26.2%	16.2%	19.3
Mobile data	17.6	13.4	15.3%	31.0%	17.0
Messaging	8.9	8.6	7.8%	3.4%	16.8
Fixed service	3.2	2.4	2.8%	34.6%	
Other service	2.6	2.0	2.3%	30.8%	
Non-service revenue	5.0	6.4	4.4%	(21.4%)	
Operating Revenue	114.7	104.4	100.0%	9.9%	

Income Statement	H1'2018	H1'2017	y/y change
Service revenue	109.7	98.0	12.0%
Non-service revenue	5.0	6.4	(21.4%)
Total Operating revenue	114.7	104.4	9.9%
Total Operating expenses	60.5	53.6	12.9%
EBITDA	54.3	50.8	6.8%
Profit after tax	26.2	23.9	9.5%
Core EPS	0.7	0.6	9.0%

Key Ratios	H1'2018	H1'2017	y/y change
EBITDA Margin	32.8%	33.0%	(0.2%)
Return on average equity	57.1%	51.2%	5.9%
Return on average assets	26.0%	24.2%	1.8%

Balance Sheet	H1'2018	H1'2017	y/y change
Equity	94.8	82.9	14.3%
Non-Current assets	138.6	135.1	2.6%
Current assets	47.6	68.8	(30.9%)
Current liabilities	91.3	120.9	(24.5%)