

Vodafone Qatar (VFQS)

Recommendation	MARKET PERFORM	Risk Rating	R-4
Share Price	QR18.15	Target Price	QR17.20
Implied Upside	(5.2%)		

Raising Price Target & Changing Rating to Market Perform

Revising price target to QR17.20 from QR13.95 post strong March 2014 quarter results and model changes. Concurrently, we are also raising our recommendation on VFQS shares to Market Perform from Underperform.

Highlights

- Adjusting model and raising dividend expectations significantly.** Factoring in recent results, we have adjusted our model and boosted our revenue/EBITDA estimates by an average of 3%-4% going forward. We continue to expect EBITDA margins to grow to 36% by FY2018 versus 25% in FY2014. Our net income and EPS estimates increase significantly beyond FY2015 due to the low base effect; we continue to expect the company to turn profitable in FY2016. In term of capex, we further increase our expectations boosting capital spending to QR500mn (20% of revenue) in FY2015 and QR432mn (15%) in FY2016 vs. QR338mn (17%) in FY2014. We continue to expect the near-term peak in capex to be driven by 4G along with continued network expansion and enhancements. On the dividend front, given the FY2014 surprise, we now expect VFQS to up its DPS to QR0.33 in FY2015 and QR0.53 in FY2016. Our DPS estimates assume VFQS management will opt to distribute the maximum allowable 95% of the company's distributable profit over the next two fiscal years. *More details on our model changes are available on Page 2.*

Catalysts

- Continued improvement in quarterly KPIs, including growing profitability, should act as catalysts.** VFQS has garnered a substantial market share within a short span of time and positioned itself as a strong alternative to the incumbent (Ooredoo or ORDS). Mobile network improvements and growth in data services, along with focus on new higher-value segments such as mobile postpaid, enterprise and nationwide fixed-line, should drive the next leg of growth. Prospects of higher dividends also remain a positive catalyst.

Recommendation, Valuation and Risks

- Recommendation and valuation: We upgrade VFQS to Market Perform and raise our price target to QR17.20 from QR13.95 previously.** Our DCF-based valuation benefits from a lower CoE assumption of 10.3% (vs. 11.1% previously) that leads to a revised WACC of 9.5% (vs. 10.7% before). Our terminal growth rate assumption remains unchanged at 2.5%.
- Risks: Besides significant equity market volatility, as seen of late,** other risks include – 1) ARPU pressure due to promotional activity/unlicensed VoIP; 2) Lack of postpaid traction/stickiness and 3) Slow growth and penetration in fixed line.

Key Financial Data and Estimates

	FY2013	FY2014	FY2015e	FY2016e
Revenue (QR mn)	1,527	1,982	2,475	2,879
Revenue Growth	25.0%	29.8%	24.9%	16.3%
EPS (QR)	(0.47)	(0.29)	(0.13)	0.08
EV/EBITDA (x)	57.5	32.6	22.9	17.1
DPS (QR)		0.17	0.33	0.53
Dividend Yield	0.0%	0.9%	1.8%	2.9%

Source: Company data, QNBFS estimates; Note: All data based on current number of shares

Key Data

Bloomberg Ticker	VFQS QD
ADR/GDR Ticker	N/A
Reuters Ticker	VFQS.QA
ISIN	QA000A0Q5NE9
Sector	Telecoms
52wk High/52wk Low (QR)	23.00/8.70
3-m Avg. Volume ('000)	3,918
Mkt. Cap. (\$ bn/QR bn)	4.2/15.3
Shares Outstanding (mn)	845.4
FO Limit* (%)	No Limit
Current FO* (%)	6.8
1-Year Total Return (%)	101.6
Fiscal Year End	March 31

Source: Bloomberg (as of July 02, 2014), *Qatar Exchange (as of July 01, 2014); Note: FO is foreign ownership

Saugata Sarkar

+974 4476 6534

saugata.sarkar@qnbfs.com.qa

Revising Estimates and Target Price

Adjusting model and raising dividend expectations significantly. Factoring in recent results, we have adjusted our model and boosted our revenue/EBITDA estimates by an average of 3%-4% going forward.

- **We are modeling in a 25% growth in total revenue for FY2015.** Our mobile revenue growth estimate is driven by a 5% increase in average revenue per user (ARPU) and a 16% increase in mobile subscribers. For FY2016, we pencil in another 16% top-line expansion as VFQS' mobile base expands another 13% while ARPU grows by 2%. Our ARPU growth estimates blend in traction in the postpaid segment (where ARPUs are running at 2.5x prepaid levels). The company's subscriber base should continue to benefit from strong overall population growth and gains in market share; we model mobile customer market share to grow from 33.8% in FY2014 to 35.1% in FY2015 and 36.3% in FY2016.
- **We continue to expect EBITDA margins to grow to 36% by FY2018 vs. 25% in FY2014.** For FY2015 and FY2016, we expect EBITDA margins to expand to 28.6% and 32.6%, respectively.
- **Our net income and EPS estimates increase significantly beyond FY2015 due to the low base effect.** We continue to expect the company to turn profitable in FY2016.
- **In term of capex, we further increase our expectations boosting capital spending to QR500mn (20% of revenue) in FY2015 and QR432mn (15%) in FY2016 vs. QR338mn (17%) in FY2014.** We continue to expect the near-term peak in capex to be driven by 4G along with continued network expansion and enhancements.
- **On the dividend front, given the FY2014 surprise, we now expect VFQS to up its DPS to QR0.33 in FY2015 and QR0.53 in FY2016.** Our DPS estimates assume VFQS management will opt to distribute the maximum allowable 95% of the company's distributable profit over the next two fiscal years.

We upgrade VFQS to Market Perform and raise our price target to QR17.20 from QR13.95 previously. Our DCF-based valuation benefits from a lower cost of equity (CoE) assumption of 10.3% (vs.11.1% previously) that leads to a revised WACC of 9.5% (vs. 10.7% before). Our terminal growth rate assumption remains unchanged at 2.5%.

Major Estimate Changes

In QR mn	FY2015e			FY2016e			FY2017e			FY2018e		
	New	Old	Change (%)	New	Old	Change (%)	New	Old	Change (%)	New	Old	Change (%)
Revenue	2,475	2,448	1.1	2,879	2,811	2.4	3,280	3,155	4.0	3,631	3,460	4.9
EBITDA	707	685	3.2	937	906	3.4	1,122	1,079	4.0	1,307	1,246	4.9
EBITDA Margin (%)	28.6	28.0		32.6	32.3		34.2	34.2		36.0	36.0	
Net Income	(112)	(116)	(3.3)	69	51	36.1	268	177	51.6	462	300	53.8
Net Margin (%)	(4.5)	(4.7)		2.4	1.8		8.2	5.6		12.7	8.7	
EPS (QR)	(0.13)	(0.14)	(3.3)	0.08	0.06	36.1	0.32	0.21	51.6	0.55	0.35	53.8
Dividend/Share (QR)	0.33	0.20	59.7	0.53	0.30	76.0	0.75	0.50	50.2	0.92	0.70	32.3
Dividend Yield (%)	1.8	1.1		2.9	1.7		4.2	2.8		5.1	3.8	
Capex	500	486	2.9	432	393	9.7	410	379	8.3	390	346	12.8
Capital Intensity (%)	20.2	19.8		15.0	14.0		12.5	12.0		10.8	10.0	

Source: Company data, QNBFS estimates

FY2014 and March 2014 Quarter Review

Recent results: VFQS posts narrower March 2014 loss on increase in customer base; declares maiden QR0.17 in cash DPS (0.9% yield). In 4QFY2014, Vodafone Qatar's (VFQS) net loss narrowed by 39% on a QoQ basis and 56% on a YoY basis and stood at QR33mn. We were expecting a net loss of QR50mn (Bloomberg consensus: QR49mn). Results were driven by an increase in revenue with 4QFY2014 revenue up 8% QoQ and 26% YoY to QR550mn. Reported revenue was in line with our estimate of QR543mn (Bloomberg consensus: QR517mn). VFQS' mobile customers grew by 22% YoY (4% QoQ) to reach 1.33mn as of March 31, 2014 (QNBFS estimate: 1.34mn), while quarterly ARPU improved 0.8% sequentially (4.9% YoY) to QR128. The company reported a quarterly EBITDA margin of 27.7% (around 27% on a normalized basis) vs. our estimate of 26.2% and December 2013 quarter's 26.4%. VFQS' FY2014 loss narrowed by 39% to QR246mn, compared to a net loss of QR401mn a year earlier. The improved results were driven by a strong 30% YoY growth in FY2014 revenue to QR1.98bn. The mobile revenue market share grew to 33.6% by the end of 4QFY2014 as compared to 30.4% in the same period last year. Postpaid revenue contributed around 17% of total revenue for the quarter and represented 9.6% of VFQS' customer base. This enabled VFQS to further increase its profitability with EBITDA margin improving 644bps over the year to reach 25% in FY2014. The company declared QR0.17 in DPS for FY2014 (subsequently approved by shareholders) vs. our estimate of QR0.10 (Bloomberg consensus: QR0.08).

Detailed Financial Statements

Income Statement (In QR mn)	FY2013	FY2014	FY2015e	FY2016e
Revenue	1,527	1,982	2,475	2,879
Direct Costs	(689)	(872)	(1,054)	(1,123)
Gross Profit	837	1,110	1,421	1,756
Other Expenses, Excluding D&A	(553)	(613)	(714)	(819)
EBITDA	284	496	707	937
Depreciation & Amortization	(659)	(717)	(796)	(845)
EBIT	(375)	(220)	(90)	92
Interest Income	0	0	0	0
Interest Expense	(27)	(26)	(23)	(23)
Profit Before Tax	(401)	(246)	(112)	69
Income Tax Expense	0	0	0	0
Profit for Shareholders	(401)	(246)	(112)	69
EPS (QR)	(0.47)	(0.29)	(0.13)	0.08

Source: Company data, QNBFS estimates

Balance Sheet (In QR mn)	FY2013	FY2014	FY2015e	FY2016e
Non-Current Assets				
Property, Plant and Equipment	1,095	1,136	1,298	1,340
Intangible Assets	6,555	6,136	5,678	5,222
Trade and Other Receivables	11	9	9	9
Total Non-Current Assets	7,660	7,281	6,985	6,571
Current Assets				
Inventory	17	14	18	20
Trade and Other Receivables	218	304	366	402
Cash and Cash Equivalents	162	97	111	286
Total Current Assets	396	415	496	707
Total Assets	8,056	7,696	7,481	7,279
Equity				
Share Capital	8,454	8,454	8,454	8,454
Legal Reserve	12	19	34	58
Accumulated Other Comprehensive Income	0	0	0	0
Accumulated Deficit	(2,294)	(2,548)	(2,818)	(3,048)
Total Equity	6,172	5,926	5,670	5,463
Non-Current Liabilities				
Trade and Other Payables	37	41	41	41
Provisions	36	34	34	34
Long-Term Borrowings	1,160	951	951	951
Total Non-Current Liabilities	1,233	1,026	1,026	1,026
Current Liabilities				
Trade and Other Payables	651	744	785	790
Short-Term Borrowings	0	0	0	0
Total Current Liabilities	651	744	785	790
Total Liabilities	1,884	1,770	1,811	1,816
Equity and Liabilities	8,056	7,696	7,481	7,279

Source: Company data, QNBFS estimates

Recommendations

Based on the range for the upside / downside offered by the 12-month target price of a stock versus the current market price

OUTPERFORM	Greater than +20%
ACCUMULATE	Between +10% to +20%
MARKET PERFORM	Between -10% to +10%
REDUCE	Between -10% to -20%
UNDERPERFORM	Lower than -20%

Risk Ratings

Reflecting historic and expected price volatility versus the local market average and qualitative risk analysis of fundamentals

R-1	Significantly lower than average
R-2	Lower than average
R-3	Medium / In-line with the average
R-4	Above average
R-5	Significantly above average

Contacts

Saugata Sarkar

Head of Research

Tel: (+974) 4476 6534

saugata.sarkar@qnbfs.com.qa

Abdullah Amin, CFA

Senior Research Analyst

Tel: (+974) 4476 6569

abdullah.amin@qnbfs.com.qa

Shahan Keushgerian

Senior Research Analyst

Tel: (+974) 4476 6509

shahan.keushgerian@qnbfs.com.qa

Sahbi Kasraoui

Manager – HNWI

Tel: (+974) 4476 6544

sahbi.alkasraoui@qnbfs.com.qa

Ahmed Al-Khoudary

Head of Sales Trading – Institutional

Tel: (+974) 4476 6548

ahmed.alkhoudary@qnbfs.com.qa

QNB Financial Services SPC

Contact Center: (+974) 4476 6666

PO Box 24025

Doha, Qatar

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