

Aug-17

OMANTEL

Event: Acquisition of 9.8% minority stake in Zain group valuing RO 326 million...



الخليجية بادر للأسواق المالية ش.م.ع.
GULF BAADER CAPITAL MARKETS S.A.O.C.

Omantel – Long term benefits seen, acquisition to be funded 100% through bridge loans...

Closing Price: RO 1.120

Rating: Accumulate (under review)

Fair Value: 1.360 (under review)

The Event- Omantel to acquire 9.8% stake in Zain Group

Omantel signed a Share Purchase Agreement (SPA) to purchase 425.7 million treasury shares in the Kuwaiti Mobile Telecommunications Co (Zain Group) which form 9.84% of outstanding common shares, subject to Kuwaiti regulatory bodies approval. **The purchase price of the treasury shares is KWD 0.6 per share (33% premium to the market closing), valuing the transaction at RO 325.6 million (USD 846.1 million).**

Omantel had an analyst conference call last Thursday (10-Aug-17) to update the strategy and rationale behind this acquisition. Find below the key highlights/ discussions of the conference call.

Acquisition strategy/ Rationale

- The acquisition of minority stake in Zain group is In line with the **Omantel's Corporate Strategy 3.0 launched in 2015** towards diversify and transforming all the business and become a leading digital services provider in the region by 2020
- The dynamics of the Telecom Industry are changing and the company need to get digitalization, increase in data requirements and other emerging trends seen.
- As per the management, the revenue growth is declining in the local telecom market along with intense competition (third mobile license and other over the top content providers)
- Revival of the company's strategy to become more international and the start looking at strategic alliances to support long term growth.
- Management is looking at synergies to strengthen their commercial offerings, customer experience, digitalization and shareholder value creation over the long term.
- Looking at cost saving on several future opportunities.
- Omantel always admire Zain for International and Innovative offers; leading technology player in MENA and in the World
- Zain has strong presence in well established markets and offers potential growth opportunities seen over the long term.
- Right partnership to project Omantel as a strong telecom player in the region
- As per the management, the deal valuations more within their acceptable levels (c. 6.5X of 2017E EBITDA) of the telecom industry, despite paying c. 33% premium to the current closing.
- Opex and Capex Synergies still at early stages
- **Omantel is not entitled for Board Seat with this acquisition and looking at commercial partnership for the long term**

Overall the management has stated that the acquisition is in line with Omantel's long term strategy. The acquisition of the minority stake is in line with the strategy and offer complimentary businesses. Omantel has strong fixed, mobile and capacities in its wholesale business. The acquisition would look at complimentary business expansions in Digital, Data acquisition and remain Competitive and presence in International markets. With this acquisition, management believes that they would have good usage of capital and this would help in **diversifying their businesses with exposure to nine markets with a total population of 175 million.** Turnaround seen in few of the markets Zain operates like Iraq, Sudan and Saudi Arabia

Added, as we know, Zain Group remain as one of the bidders and key contenders for the third mobile license in Oman. The management of Omantel doesn't want to comment on the current transaction and the Zain Group third mobile license bid in Oman. **The shortlist of qualified applications for the third license will be announced on August 14 by Oman Telecom Regulatory Authority, with the winning bid to be announced on September 4.**

Financing of the merger

- As per the management, acquisition bridge loans would be taken (100% financed by loans) and may look for other options as and when the market conditions improve
- Cost and the terms of the bridge loans are not going to be disclosed at this moment.
- No capital raising instruments proposed by the company
- With 100% debt financing assumed for acquisition, the Debt to Equity ratio of Omantel would increase to about 0.6X levels.
- While, the estimated cost of financing and dividend income (c. 5.8% yield) from Zain Group would neutralize the impact of interest costs for Omantel.

Transaction closing expected by end of this month – The company sees the notional process which needs to be taken place (Boursa Kuwait, may take 10 to 11 trading days). Expect to close the transaction by end of Aug 2017.

Dividend Outlook – As per the management, the short-term dividend policy of Omantel to remain the same, while long term value creation seen for the shareholders. The payback period and the return profile of this investment is not disclosed. Management sees this as a long-term value creating opportunity.

Our Preliminary Views on this deal- Zain Group winning Oman's third mobile license would be the turning point...

As per our view, Omantel would leverage its balance sheet considerably to invest in a strong and well-established telecom company based out of the GCC region, which operates in certain growth markets, which remains long term positive to the shareholders of Omantel. Added, the cost of financing the acquisition might be compensated by the dividend yield on the Zain Group investment. As we know, Oman Telecom market has matured and to remain highly competitive going forward, this acquisition would diversify the portfolio and benefit the company on a long term.

Key turning point would be the announcement of the third mobile license in Oman, if in case Zain won the bid, the strategic benefits on Infrastructure sharing and other synergies to enhance the presence in Oman to remain highly beneficial to Omantel. We would be keenly watching out for this final announcement by early Sep 2017. Post Correction of >25% YTD, at the current levels, Omantel trades at PE (2017E) of 9.5X and PBV (2017E) of 1.4X and provides dividend yield of 7%. We have an Accumulate rating on the stock. **The stock is under review and we would revise our rating and fair value soon.**

The reported Q2 2017 numbers of Omantel came below our estimates on economic slowdown, increase in royalty charges and the margin pressure due to intense competition. We would be revising our earnings estimates and fair value of the company post tomorrow's Q2 earnings conference call.



Stock Rating Methodology:

Buy - Upside more than 20%

Accumulate - Upside between 10% and 20%

Neutral - Upside or downside less than 10%

Reduce - Downside between 10% and 20%

Sell - Downside more than 20%

Not Rated - Stocks not in regular research coverage

Time Horizon

LT – Long Term rating with a 12 to 18 month horizon

ST – Short Term rating with a 3 to 6 month horizon

Disclaimer: This document has been prepared and issued by Gulf Baader Capital Markets SAOC ("the Company") on the basis of publicly available information, internally developed data and other sources believed to be reliable. While all care has been taken to ensure that the facts stated are accurate and the opinions given are reasonable, neither Gulf Baader Capital Markets SAOC nor any employee shall be in anyway responsible for the contents of this report. The Company may have a position and may perform buying/selling for itself or its clients in any security mentioned in this report. This is not an offer to buy or sell the investments referred therein.