

Conference Call Transcript

25 July 2019

QUARTERLY RESULTS ANALYSTS

Operator

Good day ladies and gentlemen and welcome to the Vodacom Group Ltd results conference call for the quarter ended 30 June 2019. Vodacom Group CEO, Shameel Joosub, will host the conference call. I will read the forward-looking disclaimer before handing over to Shameel.

This announcement which sets out the annual results for Vodacom Group Ltd for the quarter ended 30 June 2019 contains forward looking statements. These statements have not been reviewed or reported on by the group's auditors with respect to the group's financial condition, results of operations and businesses and certain of the group's plans and objectives. In particular such forward-looking statements include statements relating to the group's future performance, future capital expenditures, acquisitions, divestitures, revenues, expenses, financial conditions, dividend policy and future prospects, business and management strategies relating to the expansion and growth of the group, the effects of regulation on the group's businesses by governments in the countries in which it operates, the group's expectations as to the launch and rollout dates of products, services or technologies, expectations regarding the operating environment and market conditions, growth in customers and usage and the rate of dividend growth by the group.

If you do not have a copy of the results announcement it is available on the investor relations website on www.vodacom.com. Please note all participants will currently in listen-only mode and there will be an opportunity for you to ask questions later during the conference. If you should need assistance during the call please signal an operator by pressing star and then zero. Please also note that this call is being recorded. I would now like to turn the conference over to Shameel Joosub. Please go ahead, sir.

Shameel Joosub

Thanks Chris. Good afternoon everyone and good morning to those joining the call in the US. I'm joined by Till Streichert, our CFO, and Sean van Biljon, our Head of Investor Relations. Being quarterly results we will only focus on revenue and key performance indicators today. In line with the listing requirements in Kenya Safaricom does not report on a quarterly basis. We will therefore not be disclosing an update on their performance during this call. None of these numbers have Safaricom included. Before we look at the numbers let me give you the key take-outs from the last three months.

Our international operations increased its contribution to group service revenue to 29.3% and are showing good growth across the portfolio. M-PESA in international and financial services businesses in South Africa are both showing good growth and are becoming a more material part of our business. We have close to 50 million customers now using financial services across the group with over R2 trillion being transacted annually across the M-PESA platform. We have over 14 million customers using M-PESA and continue to extend the M-PESA ecosystem thereby extending our reach and giving customers more ways in which to transact.

In South Africa we launched VodaPay this quarter which enables direct airtime purchases and bill payments for electricity, TV licenses and other payments. In South Africa our content platform is made up of our music services called My Muze, our gaming platform called PlayInc, and our video play product which delivers video services which are all growing very well. Service revenue growth in South Africa was impacted by new data usage regulations, significant proactive data price cuts and a subdued economy weighing on consumer spend. I will comment on this when we unpack the South African performance.

Looking at the numbers from a group perspective we have seen solid service revenue growth of 3.9% with revenue up 4.2%, with the international portfolio providing a good hedge against the weaker Rand during the quarter. We added 1.2 million group customers in the quarter to reach 79 million customers and 1.3 million group data customers were added to reach 38.9 million customers, with 49.3% of our customers now using data. We have spent R2.7 billion on expanding and improving all our networks and IT.

Let's look at the segments in more detail. In South Africa as expected we saw a service revenue decline of 1.2%. In March we implemented the End User and Subscriber Service Charter regulations relating mainly to the out of bundle data usage. At the same time we reduced out of bundle data rates by 50%. This now allows customers a worry-free experience. The bigger impact is obviously coming from the cut in the rates more so than the regulations. Service revenue was negatively impacted by a full three month impact from this regulation and the proactive price decreases which were slightly offset by price plan increases implemented on 1st April. Out of bundle data revenue is now only 3.7% of service revenue, impacting growth by 3.8%. I think it's important to note that it is now 3.7% of service revenue, a big decline obviously from last year and even year-end.

There was an ongoing impact from the transition between national roaming partners during the quarter. However, Telkom discontinued its roaming traffic with MTN at the end of the quarter and all Telkom's roaming traffic is now being directed through our network. As a result we expect national roaming revenue to recover to previous levels. The contact segment remains healthy. Contract customers grew 8.9% year on year. Revenue was impacted by data regulations, out of bundle rate cuts and continued proactive pricing transformation, most notably in the bigger data bundle segments.

The underlying data metrics remain strong with data traffic increasing 52% in the quarter, which is an acceleration from the previous quarter of 42%. Usage per smart device grew 52% to 1.2 GB per customer with 10.4 million 4G devices connected on our network, and we have sold 233 million data bundles this quarter. We are also seeing customers buying bigger data bundles with the proportion of bundles sold above 100 MB almost doubling. We are encouraged by this behaviour as it means that we are making data more affordable, but also that customers are truly growing into a higher usage.

As mentioned we launched My Muze and PlayInc, our music and gaming platforms. My Muze has seen good traction with 1.5 million downloads in the quarter. Video Play, our video on demand platform, continues to grow and now has just under 900,000 active users paying for the services. This remains a key strategy to drive data usage. Financial services has seen amazing success with revenue increasing 45% to R481 million. Customers have accessed R2.4 billion of airtime through our airtime advance platform. Insurance revenue increased 21.6% with 1.6 million policies driven by the introduction of new products and services. At the end of the quarter we launched a consumer IoT with a range of smart devices that lets you keep track of things that you love.



Moving on to our operations outside of South Africa. I'm pleased with the overall performance of our international operations particularly in Tanzania and the DRC. There was a slight slowdown in Mozambique which was as a result of the damage caused by the cyclones to our network. Despite this service revenue for the portfolio increased 19.6% or 8.1% normalised. We added 560,000 customers in the quarter, reaching 35.2 million, up 5.3%. Data increased 30.9%. We achieved this by focussing on segmented and bundle offerings. Data customers increased 15.2% in the quarter to reach 19 million. M-PESA customers increased by 11.6% to 14.2 million across all our international markets. M-PESA revenue grew strongly at 42.7%, representing 17.7% of service revenue in the internationals.

In Tanzania we have now launched an M-PESA overdraft service which gives customers instant access to credit to enable them to make money transfers, remit bills or purchase from merchants when they have insufficient funds in their accounts. The product gives the customers the convenience that when they run out of money they can continue with the purchase and pay back the funds on their next deposit. If they don't have money for a burger for instance they can now borrow money for the burger and pay later.

On the regulatory side in South Africa the president announced that a policy directive will be issued by the end of July. A recent update today is that they're saying it will be out in the next three days or so, and that cabinet has now approved a policy directive. That has just come out this afternoon. Once issued ICASA will start the ITA process. If the process is quick there could be an auction allocation by calendar year end or very early next year. We submitted comments on the Competition Commission's preliminary report regarding its data service market enquiry. Our submission highlights our range of pricing strategies which ensure that our services are accessible by all South Africans. We are also highlighting that our lack of spectrum increases our cost to produce a MB of data, thereby inflating retail prices. We also took the opportunity to update the pricing and facts used in this preliminary report as a number of these were outdated. We will continue to cooperate with the commission and expect their final findings to form part of the wider priority markets review initiated by ICASA. In the meantime we continue to proactively decrease pricing.

In the DRC we've resolved the long-standing dispute with the regulator over claims that our 2G license was not properly renewed. We will pay \$30 million and thereby extend our license by a further ten years to 2039. Looking ahead we expect to conclude the acquisition of an M-PESA branded platform. We are also encouraged by the growth potential from the IoT.nxt acquisition which only requires Competition Commission approval now. On our AWS partnership agreement announcement earlier this year we are making progress with the initial set-ups. We expect growth in the second half of the year to improve in South Africa with benefits from the completion of the national roaming partner switchover to flow through. Continued commercial momentum in financial services will also help the better growth and increase data demand to gradually help offset the impact of the regulatory changes will also help.

Finally, on behalf of our board and staff at Vodacom I extend our deepest condolences to Bob's family and all the staff of Safaricom. Bob previously indicated that he would like to retire. We as a board had started with a process to approve a successor and will be in a position to make an announcement soon in this regard. This concludes my comments and Till and I are now ready for any questions.

Operator

Thank you very much sir. Ladies and gentlemen, at this time if you do wish to ask a question please press star and then one on your touchtone phone. You will hear a confirmation tone that you have been added to the queue. If you wish to remove yourself from the question queue you can press

star and then two. Again if you wish to ask a question please press star and then one. Our first question then is from Jonathan Kennedy-Good of SBG Securities. Please go ahead.

Jonathan Kennedy-Good

Afternoon. Thanks for the call. Just two questions from me. Shameel, I would like to confirm your commentary on the out of bundle data revenue as a proportion of service revenue. I think you said it was 3.7% and that reduced service revenue by 3.8% in South Africa. Is that correct? And if so, should we expect a little bit of a bump up back into positive territory in second half service revenue despite the fact we haven't lapped the implementation of the data regs?

Till Streichert

Jonathan, just on that one, you are right. Out of bundle data revenue as a percentage of total service revenue is 3.7%. That is correct. And the effect of adopting the End User Subscriber Charter for the first quarter had been about 3.8% in terms of drag to our growth. Now, going forward I do expect in the second quarter a better result than in our first quarter. Where is this coming from? You know that the transition between our national roaming partners is completed, so we are having the entire Telkom traffic now on our network. That is an element of positive growth. And equally the underlying business obviously on the back of a step up in traffic, which you could see data traffic grew by about 10% quarter on quarter to 52%, we will be seeing elasticity and the opportunity to upsell as customer demand has grown.

Jonathan Kennedy-Good

Thank you. That's clear. Just one follow-up question in terms of the traffic growth. Obviously positive that you are seeing some policy directive come soon, but I'm just wondering if in the interim that traffic growth is manageable on the network and what kind of impact it could have on the utilisation of the Rain relationship and cost implications there.

Shameel Joosub

Okay. So it doesn't change any of the projections on the network. Of course every year we plan for capacity, and obviously most of the budget gets directed towards adding capacity anyway. So it is very much part of the plan. And also we have the capacity. If you take on the 4G network as an example there is 91% 4G coverage and only 10.4 million customers using 4G still – although growing quite nicely. I would say still some room to go in terms of fully utilising that capacity. And then what was the second question?

Jonathan Kennedy-Good

No, that was it. Thank you.

Shameel Joosub

Sorry, using Rain more. We are not still fully utilising the capacity that we bought from Rain. Remember we are trying to keep the traffic on our own network and just use it where it's cheaper for us to move it to Rain than to carry it on our own network. That is what we use smart capex for.

Jonathan Kennedy-Good

Thank you.

Operator

Thank you. Ladies and gentlemen, again if you wish to ask a question please press star and then one. Our next question is from Myuran Rajaratnam of MIBFA. Please go ahead.

Myuran Rajaratnam

Hi guys. Thanks for taking my call. I just wanted to follow up on Jonathan's question. Your data traffic is now accelerating and it's growing at 52% for this quarter. How much is the data traffic that you are roaming onto Rain growing by?

Shameel Joosub

It's growing nicely. Look, we don't obviously disclose how much.

Myuran Rajaratnam

Is it growing faster or slower than 52%?

Shameel Joosub

No, so remember there is nothing to compare it to because the traffic has been slowly cutting over. Effectively what has been happening is that from December slowly the traffic was coming across. At the end of June all the traffic is on. So now you will start to see the impacts of that going forward in terms of utilisation. The good part is that the roaming revenue that we lost last year is basically on a run rate basis fully recovered. So that's a positive part. And I would say logically that if you look at growth rates, let's say Telkom is the best of the two roaming partners in terms of growth.

Myuran Rajaratnam

Okay, fine. I understand you don't want to answer my question. The second question is... I've lost my train of thought because you didn't answer my question.

Shameel Joosub

Was it about the Rain traffic?

Myuran Rajaratnam

Yes, about the Rain traffic.

Shameel Joosub

Okay. So the Rain traffic...

Myuran Rajaratnam

Is it growing faster than 52% or slower than 52%? Because your own data traffic is growing at 52%.

Shameel Joosub

No. Remember on the Rain traffic specifically essentially we bought a certain level of capacity and we're not utilising that capacity in full. What they do on their part of the network I guess is up to them. But if you're asking me do we see Rain gaining a lot of market share the answer is no.

Myuran Rajaratnam

No, no, I'm not asking that. What I'm asking is your own traffic that you're carrying as a group in South Africa is growing at 52%. What is the growth rate of the traffic that you're roaming on to Rain? How much is that growing? Is it growing faster or slower than 52%?

Shameel Joosub

No, it's much slower than 52%.

Myuran Rajaratnam

Okay. Thank you.

Shameel Joosub

Most of it we are carrying on our network.

Myuran Rajaratnam

The second question I had was for you to tell us the out of bundle hit to growth was 3.8% means that you are still monitoring data revenue growth in the old metric. You don't disclose it now but you're still looking at it. So what is the data service revenue growth in South Africa? A question for Till I suppose.

Till Streichert

Let me just give you a bit of colour. We told everyone in our Q4 results, full year results, that we would be condensing our disclosure on data revenue, making it in essence more relevant, effectively aligning it to how we run the business. Data as a metric remains incredibly important. It's a key driver of our growth. But we have decided to condense it because ultimately on items like integrated price plans remember there is always an allocation key basically behind it. And with the market actually having moved on to more and more integrated tariff the reference point for it becomes meaningless. So what I can tell you is of course we are monitoring our MBB [?] traffic. That is data traffic that is directly measurable.

We equally monitor very carefully our data bundles generated, data revenue. And what I can tell you is that on those categories of our in bundle data revenue we have seen in the first quarter close to double-digit growth, which we are quite happy with. On the out of bundle data revenue side of course as you can expect there has been a significant step down which is driven by two actions. One is we have reduced our out of bundle data rate in the last quarter. You remember that. We've taken it down by 50%. And equally we adopted the End User Subscriber Charter. So actually on that side if you look at it from an in bundle point of view it's actually quite encouraging what we are seeing.

Myuran Rajaratnam

Wonderful. You've answered it perfectly. That gives me enough to go on. Thank you so much guys.

Operator

Thank you very much. Ladies and gentlemen, again if you wish to ask a question please press star and then one now. Sir, we have no further questions in the queue at the moment.

Shameel Joosub

There are no further questions. Thank you for joining the call. In the quarter ahead we look forward to seeing progress on the spectrum. We're focussed on continuing to improve results in the commercial execution in all our markets. And we are expecting a stronger Q2. Thank you.

Operator

Thank you very much sir. Ladies and gentlemen, that then concludes this conference call and you may now disconnect your lines.

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