

**CREDIT OPINION**

11 July 2024

Update

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**RATINGS**

**Telkom SA SOC Limited**

Domicile	Pretoria, South Africa
Long Term Rating	Ba2
Type	LT Corporate Family Ratings
Outlook	Stable

Please see the [ratings section](#) at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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**Telkom SA SOC Limited**

Credit update

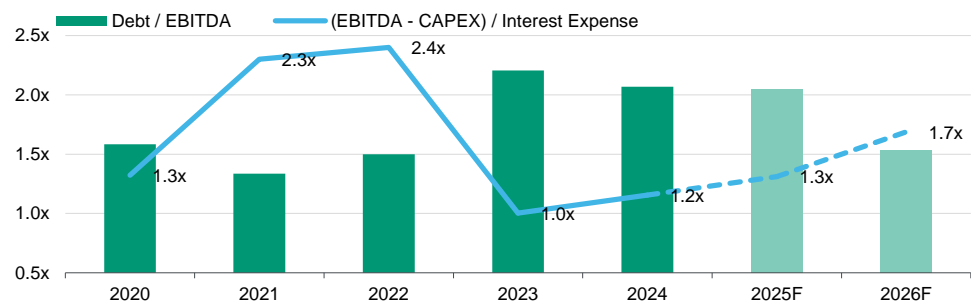
**Summary**

[Telkom SA SOC Limited's](#) (Telkom) Ba2 corporate family rating (CFR) and Aa2.za national scale CFR reflect our view of the fundamental credit quality of Telkom, represented by its Baseline Credit Assessment (BCA) of ba2, combined with our assumptions of high default dependence with- and low support from the South African government. We classify Telkom as a government related issuer (GRI) because it is 40.5% owned by the [Government of South Africa](#) (Ba2 stable). Telkom derives all of its revenue from South Africa and therefore its credit standing is strongly correlated to the economic and regulatory environment in the country. The low growth environment and intense competition between mobile network operators is a growth constraint to Telkom.

Telkom's BCA of ba2 is supported by (1) the company's leading market position in South Africa's fixed-line business as operator of the largest fibre network in the country; and (2) adequate financial policies with moderate debt/ EBITDA leverage of 2.1x as of March 2024, which we expect to reduce to around 1.5x by March 2026, mainly because the company will apply most of the proceeds from the sale of Swiftnet towards debt reduction. The rating is constrained by (1) operational concentration in South Africa and exposure to the country's economic, social, political, legal and regulatory environment; (2) the company's position as the third largest operator in a highly competitive South African mobile market; and (3) low growth prospects with continued, albeit slowing decline of fixed line business and mature mobile market.

Exhibit 1

**We expect Telkom's credit metrics to recover over the next 12-18 months as proceeds from the Swiftnet sale are used for debt reduction**



All figures and ratios are based on adjusted financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.

Periods are financial year-end unless indicated. The company's financial year ended 31 March.

Moody's forecasts are Moody's opinion and do not represent the views of the issuer.

Sources: Moody's Financial Metrics™ and Moody's Ratings forecasts

## Credit strengths

- » Successfully completed transition towards integrated telecommunications business model to mitigate declining fixed voice revenue
- » Leading market position in South Africa's fixed-line business, with the largest fibre network in South Africa based on fibre kilometres

## Credit challenges

- » Geographic concentration in South Africa
- » Continued, albeit slower decline of fixed line business
- » Number 3 mobile operator in highly competitive and mature South African mobile market
- » Weak interest coverage, when taking into account capex needs

## Rating outlook

The stable outlook reflects our expectation that Telkom's credit metrics will strengthen again over the next 12-18 months, and that in particular (EBITDA – capex)/ interest expense will trend towards 2.0x, while debt/ EBITDA will trend below 2.0x as disposal proceeds from Swiftnet are applied towards debt reduction.

## Factors that could lead to an upgrade

We would consider an upgrade if operating performance sustainably improves, (EBITDA – capex)/ interest expense exceeds 2.0x and debt/ EBITDA remains below 2.0x, both on a sustainable basis. An upgrade would also be conditional upon an upgrade of the sovereign rating of the Government of South Africa.

## Factors that could lead to a downgrade

We would consider a downgrade if (EBITDA – capex) / interest expense remains close to 1.0x for a prolonged period of time or debt/ EBITDA sustainably remains above 2.5x. Telkom's ratings are also likely to be downgraded in case of a downgrade of South Africa's sovereign ratings, although we will continue to monitor resilience of Telkom's credit profile against macro-economic shocks.

## Key indicators

Exhibit 2

### Telkom SA SOC Limited

(in ZAR billions)	2020	2021	2022	2023	2024	2025F	2026F
Revenue	43.0	43.2	42.8	41.8	42.5	43.3	44.2
Debt / EBITDA	1.6x	1.3x	1.5x	2.2x	2.1x	2.0x	1.5x
RCF / Net Debt	55.1%	86.9%	71.9%	49.4%	56.0%	44.2%	82.4%
(EBITDA - CAPEX) / Interest Expense	1.3x	2.3x	2.4x	1.0x	1.2x	1.3x	1.7x
EBITDA Margin %	24.7%	27.9%	27.8%	21.9%	23.5%	23.4%	24.3%
EBITA / Interest Expense	2.9x	4.7x	4.8x	1.9x	2.4x	2.0x	3.0x
FCF / Debt	0.4%	11.0%	-5.5%	-12.7%	2.3%	-1.7%	-2.3%

For 2024, revenue represents revenue from continuing operations

All figures and ratios are based on adjusted financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.

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## Profile

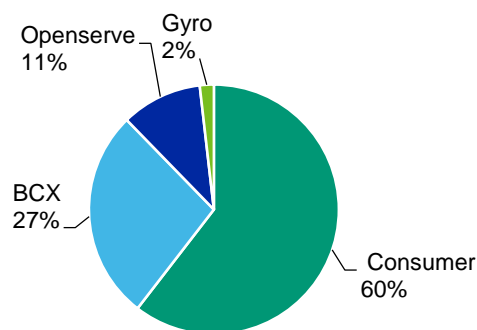
Telkom is the leading South African fixed-line operator, the third incumbent mobile operator and also a leading provider of information and communications technology services. The company controls around 609,000 fixed telephone access lines, most of which are connected to digital exchanges, and has 20 million active mobile subscribers in South Africa, making it the third largest mobile operator in the country by number of subscribers. As of 31 March 2024, the company had the largest national fibre network across South Africa.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the issuer/deal page on <https://ratings.moody's.com> for the most updated credit rating action information and rating history.

Telkom operates across four segments: Consumer (mobile, fixed-line and broadband), Business Connection Group (BCX, offering information and communication technology services, ICT), Openserve (wholesale connectivity), and Gyro (property portfolio). On 22 March 2024 the company announced it had agreed to sell its entire portfolio of around 4,000 productive telecom towers in its Swiftnet business to infrastructure investment company Actis and a Black Economic Empowerment (BEE) entity for ZAR6.75 billion. Telkom expects the transaction to close towards the end of financial year 2025 (FY2025) or at the beginning of FY2026.

Telkom is listed on the Johannesburg Stock Exchange (JSE) and is 40.5% owned by the South African government, 13.5% by the Public Investment Corporation, a South African state-owned investment management company, and the remaining 46.0% is free float, as of 31 March 2024.

Exhibit 3

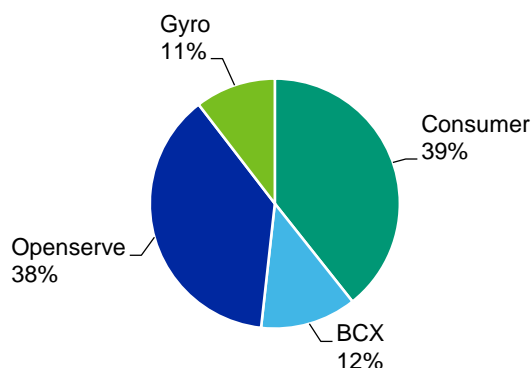
**Revenue by business segment (2024)**

Note: Includes revenue from external customers and intersegmental operating revenue, before intracompany eliminations.

The company's financial year ended 31 March.

Sources: Company filings and Moody's Ratings

Exhibit 4

**EBITDA by business segment (2024)**

Note: Based on company reported EBITDA, before intracompany eliminations and excluding other losses.

The company's financial year ended 31 March.

Sources: Company filings and Moody's Ratings

## Detailed credit considerations

### Geographic concentration in South Africa, which has a weak economic environment and weighs on Telkom's performance

Telkom's revenue and EBITDA are exclusively generated in South Africa, which exposes the company to the economic, political, social, legal and regulatory environment of the country. Growth of the South African economy remains structurally weak. We expect real GDP growth of 1.3% for 2024 and medium term growth of only around 1.0-1.5% due to constraints from a malfunctioning labour market, decaying infrastructure and slow progress on economic and social reforms. Against this backdrop Telkom's performance has also been weak over the past 4 years and we expect recovery to remain slow over the next 1 to 2 years, as consumer spending power remains under pressure and load shedding persists.

### Transition to integrated telecommunications business model, but decline of fixed services continues to be a drag on growth

Over time Telkom's business model has become increasingly diversified and integrated (see exhibit 5). To offset the steady decline in demand for fixed voice services, which used to be Telkom's main product, the company embarked on a turnaround strategy in 2013 to broaden its service offering. After completion of the strategic turnaround, Telkom remains the leader in fixed telephony and broadband in South Africa, but the company has also built out a sizeable mobile service offering in its consumer division and added enterprise services for businesses and public sector entities through the acquisition of BCX in 2015. Its ICT services include hosting, managed solutions, cloud and data center services. Telkom also has an infrastructure business, including its wholesale broadband network in the Openserve division, and Gyro, its property investment and property services business. The infrastructure businesses derive a substantial portion of their revenue from leasing network capacity to other mobile operators and third party clients.

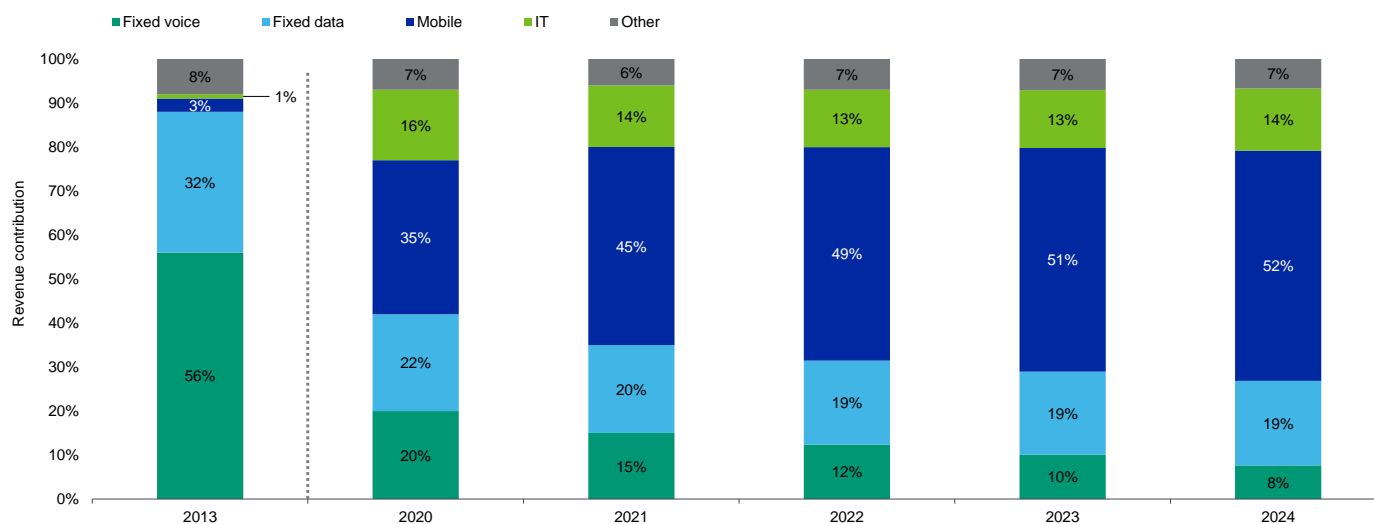
The integrated business model has allowed Telkom to successfully diversify its income streams away from the declining fixed line voice business and positions the company well as a convergent telecom operator. Convergent offerings allow the company to serve a wider range of customers and to provide bundled packages with opportunities to upsell and increase customer loyalty.

Nevertheless, the company's performance has been weak following the pandemic. From FY2021 to FY2023, revenue and Moody's adjusted EBITDA dropped by a combined 3.2% and 23.8%, respectively. This slow revenue growth and decline in profitability was driven by the combination of continued decline of Telkom's fixed voice service, some cyclical in the BCX business and a highly competitive and relatively mature mobile market in South Africa, that limit the growth of the mobile business. Operating costs increased due to more frequent planned power outages (load shedding) that increased the need to use diesel back up generators to maintain network availability as well as increased usage of roaming on other operators' networks.

In FY2024 the company achieved its first year of growth since FY2021, with 1.5% revenue growth and also managed to improve Moody's adjusted EBITDA by 8.9% against a year earlier. This turnaround was achieved through refocusing sales of its mobile business on its pre-paid data packages, which helped increase subscribers 11.9% against a year earlier to 20.4 million. Profitability improved mainly because of a cost saving program implemented in FY2023 that reduced headcount by 15% as well as investments into network resilience that allowed to reduce the use of back-up power and roaming, despite continued high load shedding.

Exhibit 5

#### Evolution of Telkom's revenue mix from financial year 2013 to financial year 2024



Periods are financial year-end unless indicated. The company's financial year ended 31 March.

Sources: Company filings and Moody's Ratings

#### After rapid growth of mobile business, growth has slowed and now depends on data demand

The mobile business, comprising both voice and data services, has become Telkom's primary revenue driver and accounted for 52% of group operating revenue of continuing operations in FY2024. Telkom's mobile business has grown rapidly over the past 10 years, from 1.8 million subscribers in March 2014, generating around ZAR350 million in revenue to 20.4 million subscribers and ZAR22.6 billion of revenue in March 2024. Telkom was able to generate this rapid growth despite competition from three larger, more established mobile operators Vodacom (majority owned by [Vodafone Group plc](#), Baa2 stable), [MTN Group Limited](#) (Ba2 stable) and Cell C. Telkom overtook Cell C in terms of subscriber numbers in 2020, becoming the third largest mobile operator in South Africa.

Telkom's market share however still significantly lags behind the 29% market share of the second largest operator MTN and its profitability is also significantly lower at a mobile business EBITDA margin of 22.2% in FY2024 against margins generally around 40% for MTN's and Vodacom's South African operations. We expect growth of the mobile market in South Africa will slow over the next years as it is mature, as indicated by a penetration rate of 167% as of 2022 according to the World Bank, meaning there are 167 mobile subscriptions for every 100 residents, which is amongst the highest levels in the world.

Telkom could however benefit from increasing data usage, data penetration amongst its mobile customers is already higher at 62% than penetration at MTN, where it stands at 55%. During FY2024, Telkom gained 2.1 million additional mobile subscribers, including 1.1 million data subscribers as it focused on offering competitive data packages. Telkom's mobile network runs primarily on 4G and 4.5G whereas competitors Vodacom and MTN still service more customers on 2G and 3G networks. As more customers migrate to

smartphones with 4G capabilities, demand for Telkom's network is likely to grow and could offset some of the otherwise slowing down growth of the mobile segment.

#### Focus on cost savings and network commercialization

Telkom's Moody's adjusted EBITDA margin improved over FY2024 to 23.5% from 21.9% a year earlier. Nevertheless it remains significantly below its pre-pandemic margin of around 30%. For profitability to improve, efficiencies and cost savings are crucial. Telkom is focussed on streamlining and has significantly reduced its workforce in recent years. The company has conducted another restructuring program during FY2023 that has started yielding significant cost savings. We expect EBITDA margin will recover to around 25% over the next 2 years.

With growth of the mobile business overall slowing, Telkom is focussing on cementing its leadership in broadband and fixed data, which contributes to revenue across its Consumer, BCX and Openserve divisions and which accounts for most of the EBITDA generated by the Openserve division. Openserve accounted for 39% of Telkom's EBITDA FY2024 and therefore already constitutes a substantial part of the company's profitability.

Telkom has the largest fibre and broadband network across South Africa and continued investment in the network is one of Telkom's key priorities, accounting for 35% of total investments during FY2024. During this period, the company increased homes passed with fibre by 17% to 1.2 million compared to a year earlier and increased the number of homes connected by 20% to 590,000. Telkom sees particular demand growth from other carriers for use of its strong backhaul capacity. As the company continues its investments in the network and mobile customers' demand for speed and data consumption increases, we expect that demand from other mobile carriers for Telkom's network will continue to grow strongly. At the same time the decline in demand for fixed voice services will level off as the contribution to Telkom's revenues has already reduced substantially. The combination of growth in fixed data and slower decline of fixed voice should over the next 2-3 years lead to a stabilization and sustained growth of revenue and EBITDA from Openserve.

#### Prudent financial policies and credit metrics will improve following Swiftnet sale

Telkom has prudent financial policies with target net leverage of 1.5x to 1.9x and a good track record of adhering to this leverage target over time. For FY2024 company reported net leverage stood at 1.7x and Moody's adjusted debt to EBITDA was 2.1x, which we view as adequate.

Even though net leverage remained within the target range, the higher interest rate environment led to a 45% increase in interest expense in FY2024 compared to a year earlier. This has led to a weakening in the company's interest coverage, as measured by  $(\text{EBITDA} - \text{capex}) / \text{interest expense}$  to 1.2x as of FY2024, down from 2.4x two years earlier in FY2022. An  $(\text{EBITDA} - \text{capex}) / \text{interest}$  ratio below 2x is weak for Telkom's Ba2 rating and only partially mitigated by the adequate leverage of 2.1x.

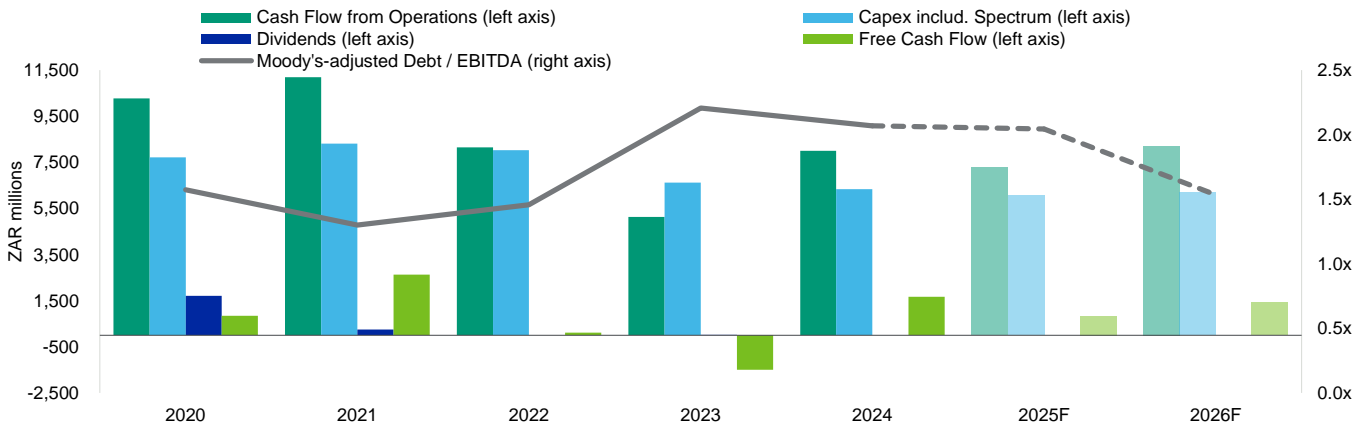
We expect however that interest coverage will improve again over the next 3 years and trend towards 2.0x as the company has announced that it is looking to apply most of the proceeds from the sale of Swiftnet towards debt reduction, with the aim of reducing reported net leverage well below 1.5x. Assuming that the transaction will only close at the beginning of FY2026, we expect that this will lead to a reduction in Moody's adjusted debt to EBITDA to 1.5x by FY2026 and an improvement in  $(\text{EBITDA} - \text{capex}) / \text{interest expense}$  to 1.7x.

Telkom has not paid a dividend in the past 5 years and does not plan to resume paying one while free cash flow generation remains negative. In 2024, it announced a new dividend policy that links dividend payments to free cash flow and targets a payout ratio of 30% to 40% of free cash flow. We expect that dividends will be resumed after closing of the Swiftnet sale and that the company will remain prudent when allocating cash flow between shareholder returns, investments and adhering to its leverage target.

Free cash flow should also improve going forward through a slight reduction in capex to 14% of revenues from previously more than 17%.

Exhibit 6

**We expect cash flow generation to recover over the next 1-2 years**



Moody's-adjusted debt/EBITDA is based on adjusted financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. Periods are financial year-end unless indicated. The company's financial year ended 31 March. Cash flow from operations shown excluding dividend payments. Moody's-adjusted debt/EBITDA forecasts are Moody's opinion and do not represent the views of the issuer. Sources: Company filings, Moody's Financial Metrics™ and Moody's Ratings forecasts

**South African government support and dependence assumptions result in no rating uplift**

Moody's default dependence assessment reflects the degree of correlation of a government-related issuer, such as Telkom, and its supporting government to being jointly susceptible to adverse circumstances that simultaneously move them closer to default. The "high" default dependence assumption reflects our view that both the South African government and Telkom's performance are highly correlated to the general business cycle in South Africa. In addition, it factors the moderate link between the government and Telkom, given the firm's partial privatisation during the past decade. Despite its 40.5% stake in Telkom, the South African government has no board representation, which limits its influence over the strategic direction of the company.

The "low" support assessment reflects the fact that the company is run independently with no interventionist tendencies from the government. We also do not view Telkom to be a strategic entity for the government.

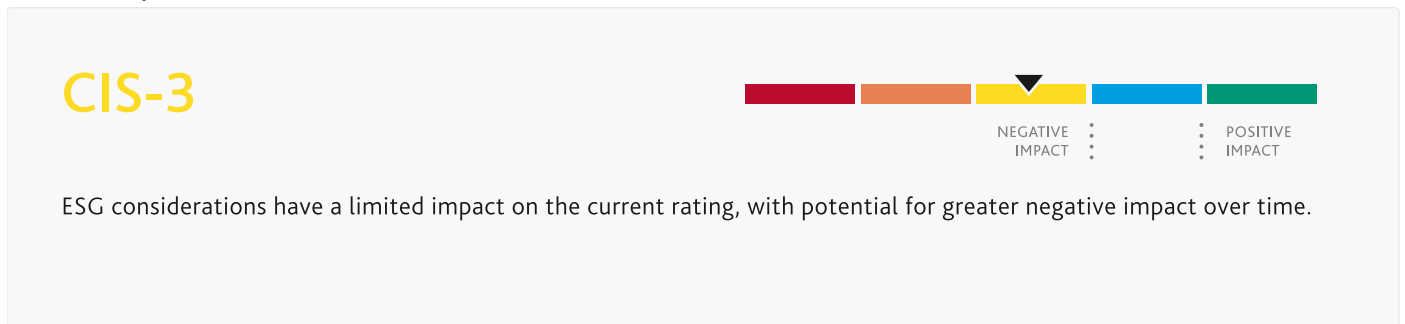
Our default dependence and support assumptions lead to no uplift to the BCA of ba2, which is in line with the rating of the Government of South Africa.

**ESG considerations**

**Telkom SA SOC Limited's ESG credit impact score is CIS-3**

Exhibit 7

**ESG credit impact score**



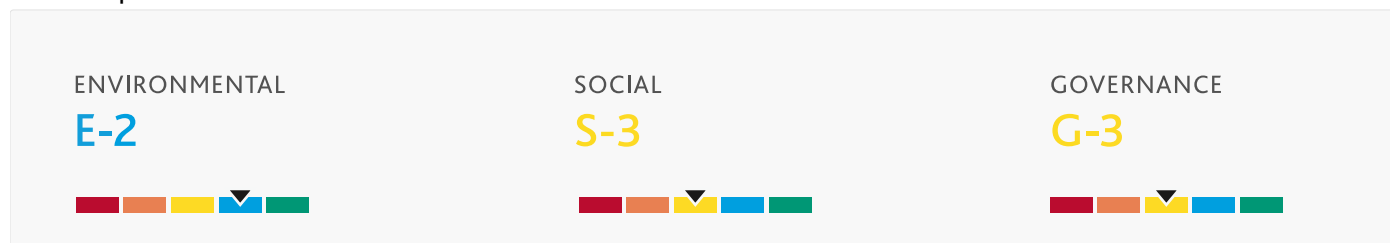
Source: Moody's Ratings

Telkom's **CIS-3** indicates that ESG considerations have a limited impact on the current credit rating with potential for greater negative impact over time especially through exposure to social and governance risks. Social risks that Telkom is exposed to mainly comprise

of exposure to labour unions, changing societal trends in using mobile communication and the risk of data breaches. Governance risks Telkom is exposed to mainly comprise its 40.5% ownership by the government of South Africa and risk of interference, as well as its adequate but weakened credit metrics.

Exhibit 8

#### ESG issuer profile scores



Source: Moody's Ratings

#### Environmental

The company's exposure to environmental risks is low and in line with the overall industry. Telkom is mostly focussed on energy efficient projects to reduce energy consumption.

#### Social

Telkom faces some social risks as it is exposed to well entrenched labour unions with rigid employee regulations and changing demographic and societal trends towards the use of telecom related technology. This is partially mitigated by Telkom's good track record over the past few years in reducing its overall work force, in particular in its declining fixed voice business and of successfully growing mobile voice and data businesses to offset declining fixed voice revenues. Data security and data privacy issues are prominent in the sector. Telecommunications providers exchange large amounts of data, and a breach could cause legal, regulatory or reputation issues. In addition, a breach could result in increased operational costs to mitigate cyberattacks and reduce exposure to the loss of private data. Electromagnetic radiation (for example, from mobile antennas or mobile handsets) has repeatedly been said to be potentially harmful to the environment and health. While the need for higher mobile data speeds will increase electromagnetic radiation, we do not see it as a significant environmental risk for global telecommunication providers, given the existing regulatory radiation limits and ongoing technology improvements.

#### Governance

Telkom faces some governance risks as the government of South Africa is the largest shareholder with 40.5% ownership. The risk of government interference is low as the government has no board representation and has no track record of active interference in the company's management. Telkom has adequate financial policies. While interest coverage, as measured by (EBITDA-capex)/ interest expense has significantly weakened since the beginning of financial year 2023, we expect it to recover to an adequate level over the next 1-2 years as Telkom reduces debt from proceeds of its sale of Swiftnet.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click [here](#) to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

#### Liquidity analysis

Telkom has adequate liquidity. As of 31 March 2024, the company's internal liquidity sources included ZAR3.7 billion of cash and around ZAR14.0 billion of operating cash flow, which we project the company to generate through September 2025. In addition, Telkom had available facilities of ZAR5.5 billion. While we note ZAR5.0 billion of these are reviewed annually, Telkom has a good track record of rolling facilities over at the time of review. Together, this should be sufficient to cover the company's capital spending (including lease payments) and debt maturities of ZAR4.4 billion through March 2025. Disposal proceeds from Swiftnet provide an additional liquidity source that Telkom plans to use mostly towards reducing debt. Some of Telkom's facilities include financial covenants, including interest cover and net leverage, which the company will be able to meet comfortably.

## Rating methodology and scorecard factors

The principal methodology used in rating the company was our Telecommunications Service Providers. The scorecard indicated outcome of Ba2 as of March 2024 is in line with the assigned rating of Ba2.

Exhibit 9

### Rating factors

Telkom SA SOC Limited

Telecommunications Service Providers Industry Scorecard [1][2]	Current FY 03/31/2024		Moody's 12-18 Month Forward View As of 7/3/2024 [3]	
	Measure	Score	Measure	Score
<b>Factor 1 : Scale (10%)</b>				
a) Revenue (USD Billion)	\$2.3	B	\$2.3 - \$2.4	B
<b>Factor 2 : Business Profile (25%)</b>				
a) Competitive Position	Ba	Ba	Ba	Ba
b) Market Share	Ba	Ba	Ba	Ba
<b>Factor 3 : Profitability and Efficiency (10%)</b>				
a) Revenue and Margin Sustainability	B	B	B	B
<b>Factor 4 : Leverage and Coverage (40%)</b>				
a) Debt / EBITDA	2.1x	Baa	1.5x - 2x	A
b) RCF / Net Debt	56.0%	A	44% - 82%	A
c) (EBITDA - CAPEX) / Interest Expense	1.2x	B	1.3x - 1.7x	B
<b>Factor 5 : Financial Policy (15%)</b>				
a) Financial Policy	Ba	Ba	Ba	Ba
<b>Rating:</b>				
a) Scorecard-Indicated Outcome		Ba2		Ba1
b) Actual Rating Assigned				Ba2
<b>Government-Related Issuer</b>		<b>Factor</b>		
a) Baseline Credit Assessment		ba2		
b) Government Local Currency Rating		Ba2		
c) Default Dependence		Hi		
d) Support		Lo		
e) Actual Rating Assigned		Ba2		

All figures and ratios are based on adjusted financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.

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Sources: Moody's Financial Metrics™ and Moody's Ratings forecasts



## Appendix

Exhibit 10

### Peer Comparison

#### Telkom SA SOC Limited

(in \$ millions)	Telkom SA SOC Limited			MTN Group Limited			Millicom International Cellular S.A.			LTM
	Ba2 Stable			Ba2 Stable			Ba2 Stable			
	FY Mar-22	FY Mar-23	FY Mar-24	FY Dec-21	FY Dec-22	FY Dec-23	FY Dec-22	FY Dec-23	FY Mar-24	
Revenue	2,884	2,472	2,268	12,304	12,700	11,996	5,624	5,661	5,779	
EBITDA	801	542	534	5,584	5,539	4,007	2,225	2,110	2,231	
Total Debt	1,184	1,141	1,092	8,071	8,101	8,117	7,820	7,739	7,683	
Cash & Cash Equivalents	222	196	198	2,474	2,607	2,053	1,039	831	675	
EBITDA margin %	27.8%	21.9%	23.5%	45.4%	43.6%	33.4%	39.6%	37.3%	38.6%	
(EBITDA - Capex) / Interest Expense	2.4x	1.0x	1.2x	3.1x	2.6x	1.1x	1.8x	1.3x	1.6x	
Debt / EBITDA	1.5x	2.2x	2.1x	1.6x	1.5x	2.0x	3.5x	3.7x	3.4x	
FCF / Debt	-5.5%	-12.7%	2.3%	18.7%	4.7%	0.4%	0.8%	-1.8%	-0.5%	
RCF / Net Debt	71.9%	49.4%	56.0%	64.5%	59.6%	51.3%	21.7%	19.4%	20.4%	

All figures and ratios are based on adjusted financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.

LTM = Last 12 months.

Source: Moody's Financial Metrics™

Exhibit 11

### Moody's-adjusted debt reconciliation

#### Telkom SA SOC Limited

(in ZAR millions)	2020	2021	2022	2023	2024
<b>As reported debt</b>	<b>16,782.0</b>	<b>15,839.0</b>	<b>17,306.0</b>	<b>20,245.0</b>	<b>20,678.0</b>
Pensions	-	255.0	-	-	-
<b>Moody's-adjusted debt</b>	<b>16,782.0</b>	<b>16,094.0</b>	<b>17,306.0</b>	<b>20,245.0</b>	<b>20,678.0</b>

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Periods are financial year-end unless indicated. The company's financial year ended March 31.

Source: Moody's Financial Metrics™

Exhibit 12

### Moody's-adjusted EBITDA reconciliation

#### Telkom SA SOC Limited

(in ZAR millions)	2020	2021	2022	2023	2024
<b>As reported EBITDA</b>	<b>9,391.0</b>	<b>11,614.0</b>	<b>11,885.0</b>	<b>8,142.0</b>	<b>9,603.0</b>
Pensions	37.0	35.0	(8.0)	(31.0)	87.0
Unusual Items	1,187.0	395.0	-	1,065.0	305.0
<b>Moody's-adjusted EBITDA</b>	<b>10,615.0</b>	<b>12,044.0</b>	<b>11,877.0</b>	<b>9,176.0</b>	<b>9,995.0</b>

All figures and ratios are based on adjusted financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.

Periods are financial year-end unless indicated. The company's financial year ended March 31.

Source: Moody's Financial Metrics™

## Ratings

Exhibit 13

Category	Moody's Rating
<b>TELKOM SA SOC LIMITED</b>	
Outlook	Stable
Corporate Family Rating	Ba2
NSR Corporate Family Rating	Aa2.za

Source: Moody's Ratings

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