

# MOODY'S

## RATINGS

### **Rating Action: Moody's affirms Telkom's Ba2 rating and downgrades national scale rating to Aa2.za; outlook stable**

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19 Dec 2023

DIFC - Dubai, December 19, 2023 -- Moody's Investors Service (Moody's) has today affirmed Telkom SA SOC Limited's (Telkom) Ba2 corporate family rating (CFR) and downgraded its national scale rating (NSR) CFR to Aa2.za from Aa1.za. The Baseline Credit Assessment (BCA) of ba2 was also affirmed. The outlook remains stable.

#### RATINGS RATIONALE

Today's rating action reflects Moody's expectation that Telkom's credit metrics will recover over the next 12-18 months to levels that the agency deems adequate for its Ba2 rating. At the same time, the downgrade of the NSR reflects that Telkom's rating is now weakly positioned at the Ba2 rating level, particularly compared to other Ba2-rated South African companies.

Moody's adjusted EBITDA declined by 19% during the financial year that ended March 2023 (FY2023) and did not recover in the six months that ended September 2023. At the same time the company's debt increased by 25% over the 18 months from March 2022 to September 2023 to fund negative free cash flow. Combined with rising interest rates that have increased the company's weighted average cost of debt, including leases, to 8.5% for the twelve months that ended September 2023 (September 2023 LTM) from 7.15% as of March 2022, this has led to a 54% increase in interest expense and a weakening of the (EBITDA – capex) / interest expense ratio to 1.0x as of September 2023 LTM, down from 2.4x 18 months earlier. Moody's deems a (EBITDA – capex) / interest ratio below 2x as weak for Telkom's Ba2 rating, even though it is partially mitigated by debt/ EBITDA leverage of 2.2x as of September 2023 LTM, which remains adequate despite weakening from 1.5x 18 months earlier.

The rating agency expects that Telkom's EBITDA will recover to around ZAR11 billion over the next 2 years from ZAR9.6 billion as of September 2023 LTM thanks to cost saving measures and the normalisation of expenses from the expansion of the postpaid book in FY2023. At the same time the company's debt/ EBITDA and interest

expense will reduce as the company has announced it will use some of the proceeds from the planned disposal of Swiftnet to reduce debt and interest expense.

Telkom falls under Moody's government related issuer (GRI) methodology given its 40.5% ownership by the Government of South Africa (Ba2 stable). The link between the company and the government is reflected by Moody's assumption of 'High' default dependence and 'Low' extraordinary support and results in no uplift to the BCA of ba2, which is in line with the rating of the Government of South Africa.

Telkom's BCA of ba2 is supported by (1) the company's leading market position in South Africa's fixed-line business and operator of the largest fibre network in the country; and (2) adequate financial policies with moderate, albeit weakening debt/ EBITDA leverage of 2.2x for the September 2023 LTM period. 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.

## STABLE OUTLOOK

The stable outlook reflects Moody's 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.

## FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

Moody's would consider an upgrade if operating performance sustainably improves, (EBITDA – capex)/ interest expense remains above 2.0x and debt/ EBITDA sustainably 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.

Moody's 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 Moody's will continue to monitor resilience of Telkom's credit profile against macro-economic shocks.

## PRINCIPAL METHODOLOGIES

The methodologies used in these ratings were Telecommunications Service Providers published in November 2023 and available at <https://ratings.moodys.com/rmc-documents/411275>, and Government-Related Issuers Methodology published in February 2020 and available at <https://ratings.moodys.com/rmc-documents/64864>.

Alternatively, please see the Rating Methodologies page on <https://ratings.moodys.com> for a copy of these methodologies.

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For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on <https://ratings.moodys.com/rating-definitions>.

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