

Group Interim Results

for the six months ended
30 September 2021



Telkom delivered strong earnings growth despite a challenging trading and economic environment. The first half of the year saw the economy struggle to recover from the consequences of COVID-19, which were compounded by the recent unrest in certain parts of South Africa. Group profitability continued to grow ahead of revenue, underpinned by our sustainable cost management, which seeks to ensure that cost to serve is optimised and operating expenditure (opex) growth is contained below inflation. Telkom remains resolute in executing its strategic goals, with the Value Unlock programme on track. The masts and towers business listing on the JSE is on target for the fourth quarter of the financial year. The effective management transition is in place, with the appointment of the Group Chief Executive Officer (CEO) Designate and the new CEO of Telkom Consumer. As the mobile business continues to grow, Telkom onboarded a second national roaming partner.

Highlights

EBITDA up 1.2%
with EBITDA margin
at 28.1%



HEPS up 30.4%
to 285.5 cents
BEPS up 27.3%
to 276.8 cents



Mobile data revenue
up 6.1%
to R6 374 million



Mobile customer base
up 18.8%
to 16.3 million



FTTH connectivity rate
at 46.9%



Operating environment

The pandemic continues to have an impact on lives, families and communities. Telkom has continued to prioritise the wellbeing of its employees. As the attention of the world moved to vaccines, we developed a proactive COVID-19 vaccination framework that supports an increased focus on mental and physical wellness and a need for greater resilience. Telkom supported the Business for South Africa initiatives to ensure access to vaccines for all South Africans. In July, we entered into an agreement with Dis-Chem that enabled us to prioritise vaccination for all employees who are eligible to get the COVID-19 vaccine, including up to five extended family members. We unveiled our hybrid work policy, which allows most employees to work remotely. We support government's national COVID-19 vaccination programme aimed at achieving population immunity in South Africa and in the workplace.

The pandemic and subsequent lockdowns continue to impact the South African economy. Customers remain under severe financial pressure due to loss of jobs and reduced income. Small and medium enterprises (SMEs) are also under strain, with some SMEs being liquidated as they were the hardest hit by the pandemic. The competitive environment has intensified with increased competitive activities in the first half of the year.

Group financial performance overview

The Group sustained its revenue performance

Group revenue was flat at R21 292 million, driven by the mobile business and the masts and towers business. Mobile revenue increased by 9.7% despite experiencing the COVID-19 bump in the prior period as a result of the stringent lockdown alert level that was implemented. The masts and towers business continued on its growth trajectory, with external revenue increasing by 4.6% as it commercialises its portfolio. The performance was offset by the IT business, which remains under pressure due to the challenging trading environment, and a decline in the fixed-line business as customers migrate to new technologies such as fibre and LTE. Although the fixed-line business declined by 9.5% in the period, we saw a significant slowdown in the rate of decline compared to the 18.2% reported in the prior period. The stability in the fixed-line business is attributable to a slowdown in fixed voice churn and an increase in usage, due to improved economic activity in the period compared to the prior period when South Africa was in lockdown level 5.

Solid EBITDA growth underpinned by sustainable cost management

Group EBITDA grew faster than revenue with an increase of 1.2% to R5 978 million and the EBITDA margin expanding by 0.5 ppts to 28.1%. This was underpinned by our effective sustainable cost management programme, which aims to contain opex growth below inflation and optimise cost to serve. Opex declined by 3.1% year on year despite an average Group-wide salary increase of 6%, which was effective from 1 April 2021. Mobile cost to serve was optimised despite the increase in certain costs associated with the post-paid market such as distribution channel costs following a year of lower distribution costs due to the impact of the strict lockdown. The cost to serve improvement was enabled by optimised roaming costs as we maintain stringent roaming traffic thresholds and migrate traffic to our network, supported by the ongoing network investment.

HEPS increase driven by lower finance charges and fair value movements

Reported HEPS increased by 30.4% to 285.5 cents while BEPS increased by 27.3% to 276.8 cents compared to the prior period. This was mainly due to a significant decline in finance charges and fair value movements compared to the prior period as well as the increase in Group EBITDA. Finance charges and fair value movements declined by 34.9% to R659 million. Finance charges reduced due to our funding strategy of ongoing settlement of maturing debt. Finance charges reduced by 25.2% to R541 million. Our funding strategy allowed us to balance our cost of debt ratio to 52:48 floating to fixed. This ensures that the risk to changes in interest rates remains balanced. Fair value movements and foreign exchange losses reduced significantly by 91.9% to R17 million from R209 million due to currency volatility and favourable foreign exchange hedging position.

Capital investment for growth accelerated in the first half of the year

We continued to invest in our key growth areas, fibre and mobile, with a capital investment increase of 22.7% to R3 610 million representing a capex to revenue intensity of 17.0%. The network rollout in the prior period was impacted by the lockdown in the first quarter of the prior year. With the highest FTTH connectivity rate of 46.9% in the market, we started accelerating our fibre rollout following a period of focusing on connectivity rate to improve returns. Going forward, we will focus on expanding our FTTH footprint while simultaneously focusing on connecting premises to ensure that we maintain a high connectivity rate.

Balance sheet remains stable with adequate capacity to fund our strategy

Our conservative funding approach enabled us to strengthen our balance sheet by repaying maturing debt of approximately R1.1 billion in the prior financial year, with R900 million repaid in the first half of the prior financial year. In the first half of the current year, we settled a further R100 million of debt in line with our debt maturity profile. We have adequate balance sheet capacity to effect our strategic funding requirements with net debt to EBITDA ratio stable at 1.1x driven by a 32.3% decrease in the cash balances at the end of the period and an increase of additional IFRS 16 lease liabilities to support mobile growth.

Free cash flow under pressure due to increased capex

In line with management expectations, we generated negative free cash flow (FCF) of R839 million due to an increase of R1.1 billion in capex paid in the period under review. During the period, we executed an off-balance sheet disposal of the handset receivable book amounting to approximately R300 million in line with management's cash release initiatives to improve working capital management.

Business performance overview

Telkom Consumer continued to be the driver of growth in the Group with revenue increasing by 2.1% to R12 960 million driven by the mobile business. This was partially offset by the decline in fixed-line business due to continued migration to next-generation technologies such as long-term evolution (LTE) and fibre, and ongoing pressure in the SME segment. Mobile service revenue grew by 6.8% to R8 847 million, supported by 18.8% year on year growth in active customers to 16.3 million. Mobile data revenue grew by 6.1% to R6 374 million, supported by 10.3% growth in mobile broadband customers to 10.6 million, which represents 65.5% of our active customer base. This performance was delivered against a strong first half of the prior year, which saw a surge in data demand due to the pandemic.

Driving the growth of adjacent revenue streams and opportunities remains a strategic imperative which we are actively investing in. Included in Telkom Consumer revenue is content and financial services revenue of R388 million, which grew 23% year on year. This revenue is expected to continue to grow and will be a solid base from which to grow as we look to diversify revenue.

BCX was the hardest hit by the challenging environment, as it serves all the sectors of the economy. Revenue declined by 6.1% to R7 461 million. We continue to see sluggish investments by corporates as the country battles with the impact of the pandemic and the effects of restrictions on parts of the economy. The Information technology (IT) business remains under pressure due to the lingering impact of the lockdown and the global supply chain constraints and shortages of semiconductor chips.

Openserve continued to stabilise with its topline revenue slightly down by 1.8% to R6 720 million, supported by the fibre ecosystem, including fibre to the base stations and fibre to the business. From a fibre to the home (FTTH) perspective, the number of homes passed increased by 54.2% to 707 399, and the number of homes connected with fibre increased by 34.3% to 331 735. The 331 735 number of homes connected with fibre surpassed the number of homes connected with copper of 230 817.

Gyro masts and towers (Swiftnet) continued to commercialise its masts and towers business, with revenue increasing by 7.3% to R674 million, supported by an increase in the productive portfolio tenancy ratio from 1.52x in the prior period to 1.55x. The business is being prepared for listing on the JSE.

Effective management transition is in place

The appointment of the Group CEO Designate and CEO of Telkom Consumer effective 1 October 2021 will ensure continued execution of Group strategy. Serame Taukobong was appointed Group CEO Designate and will take over the role of Group CEO on 1 July 2022. His successor in Telkom Consumer, Lunga Siyo, was appointed CEO of Telkom Consumer.

Telkom adds MTN South Africa as a second national roaming partner

Telkom has entered into a roaming agreement with MTN South Africa. MTN South Africa is Telkom's second roaming partner, effective 1 November 2021. The roaming agreement covers 2G, 3G and 4G, which will include seamless handover between Telkom and MTN networks. Telkom currently has a roaming agreement with Vodacom South Africa and has opted for two national roaming partners. Telkom's innovation in mobile network deployment has enabled flexibility to offer customers a better experience and optimise its existing roaming spend.

A separate listing of the masts and towers business (Swiftnet)

Telkom is pursuing a separate listing of its masts and towers business (Swiftnet) on the JSE before the end of the financial year. Significant progress has been made, including, but not limited to, formal engagements with the JSE. Telkom believes that a separate listing of Swiftnet will affirm the valuation of the masts and towers business and its contribution to the overall valuation of the Telkom business, thereby unlocking further value for Telkom.

Outlook statement

Given the challenges in the first half of the year, management will focus on growing the topline revenue and profitability in the second half of the year. Discipline in capital expenditure will continue to be exercised and we will focus on initiatives to improve cash generated from operations. Management expects FCF to normalise in the second half of the year and return to positive territory similar to the past two years. As the growth in the mobile business normalises and the fixed-line business is starting to stabilise following periods of decline subsequent to execution of a migration strategy, management will now focus on its IT business which has been under pressure due to various reasons. To this end, the Board is investigating a strategic intervention in the business which could include but not limited to introducing a strategic partnership in the business. This is aimed at addressing capacity and capabilities in BCX and ensure sustainable growth going forward.

The Board remains committed to the value unlock strategy, which is premised on Telkom's market capitalisation not representing its intrinsic value. Telkom has different classes of infrastructure assets such as data centres, a wholesale network business and masts and tower business, which are globally valued at higher multiples for separate individual businesses than telecommunications. Telkom has made progress in consolidating the data centres into Gyro, with the intention of building a carrier neutral data centre infrastructure business, while the legal separation of Openserve is on track. Significant progress has been made in respect of a separate listing of its masts and towers business (Swiftnet), including, but not limited to, formal engagements with the JSE. The listing is expected to be concluded before the end of the financial year subject to market and other conditions. The Board believes that a separate listing of Swiftnet will affirm the valuation of the masts and towers business and its contribution to the overall valuation of Telkom. The proceeds of the value unlock are expected to rebase the balance sheet and/or reinvest in the business and/or shareholder rewards.

Returning cash to shareholders remains a key element of our capital allocation framework. The Board remains committed to reinstate the dividend policy by the end of the current financial year. Given the advanced stage of the separate listing of Swiftnet which is expected to be concluded by end of the financial year and the management transition, the Board will be better placed to take a holistic view of the capital allocation and make an announcement on the dividend policy at the end of the financial year. The Board will deliberate on the dividend declaration at that stage.

Financial information summary

	Reviewed September 2021 Rm	Reviewed September 2020 Rm	Variance %
Gross operating revenue	21 292	21 396	(0.5)
EBITDA	5 978	5 908	1.2
EBITDA margin (%)	28.1	27.6	0.5
Capex	3 610	2 942	22.7
Free cash flow	(839)	211	(497.6)
BEPS (cents)	276.8	217.5	27.3
HEPS (cents)	285.5	219.0	30.4
Net debt to EBITDA (times)	1.1	0.9	0.2
Interim dividends (cents)	-	-	-

Sello Moloko
Chairman

Sipho Maseko
Group Chief Executive Officer

Dirk Reyneke
Group Chief Financial Officer

9 November 2021

Sponsor
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Further information: The short-form interim financial results announcement is the responsibility of the board of directors of Telkom. It is only a summary of the information contained in the long-form interim financial results announcement and does not contain full or complete details.

Any investment decisions should be based on the long-form interim financial results announcement published on the JSE's website on Tuesday, 09 November 2021 and also available on Telkom's website at www.telkom.co.za/ir.

The long-form interim financial results announcement, including the auditor's review opinion, is available on the company's website at: <https://www.telkom.co.za/ir/financial/financial-results-2022.shtml> and on the JSE's website at: <https://senspdfjse.co.za/documents/2021/jse/isse/TKG/ie2021.pdf>



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