Helios Towers Q2 2018 Results

Wednesday, 15 August 2018

Kash Pandya Good afternoon, everybody; thank you so much for making the time to join us for our H1 and Q2 trading update. As always, I am going to take you through an executive summary, then we will discuss the detailed financials, then there will be ample time at the end of the presentation for Q&A. Let me introduce, on slide two, the two individuals who are on the call with me, as always, Tom Greenwood, our CFO, and Manjit Dhillon, our Head of Corporate Finance.

Let me start with our key highlights on slide four.

We continue to deliver growth in revenue and adjusted EBITDA, driven by organic demand, and reinforced by our business excellence strategy that is driving margin growth as we continue to grow.

Our EBITDA has grown by 27% year over year, and our margin has improved by nine percentage points, now approaching the 50% mark with 49% in Q2. We are excited about breaking through the 50% mark during the course of this year, and we have a culture to drive efficiency in our business and, through our technology investments, reduce the cost base meaning the flow-through from our new revenue is becoming bigger and bigger.

Moving on to slide five, here we just demonstrate 14 consecutive quarters of EBITDA growth, and hopefully this gives you confidence in our business to continue to drive the EBITDA margin and the EBITDA quantum. And particularly knowing that the macro drivers in our markets are so strong and the levels of penetration for mobile services are relatively low, that future growth is ahead of us and still to be captured.

If I take you on to slide six, here we will see modest growth in our tenancies year over year, by 2%, and our tenancy ratio in Q2 is just under two, a fraction drop from where we were in Q1. There is a logical reason to explain this; partly, it is driven by the year-end cycle for our customers. Some of our customers do not start their new year until April and therefore the first quarter of their budget year is relatively slow, which happens to be our second quarter.

Secondly, we have been very successful through an open public tender in Ghana with the new entity, formed through the Airtel and Tigo merger. This merger created a strong number two player in Ghana, moving from number four and three, respectively. We were successful in re-negotiating our contract and extending the contract life from 5 years to 15 years, with a slight increase in lease rate per tenancy, which maintains our EBITDA at a neutral level for that contract.

However, part of the agreement was to allow them cancellation rights for 140 net tenancies. This was predominantly driven by the fact that the two mobile operators coming together had a degree of overlap in their network coverage. As a good partner, we felt that it was the right thing to allow that flexibility in the contracts, with no revenue or EBITDA impact.

This is one of the key driving forces for our tenancy ratio not improving as much as we would have liked. However, looking forward, we are still confident of continued growth in colos, amendment revenues, and built-to-suits.

You may have seen our backbone press release this morning as well, an example of investment that is helping to drive our margins and revenue.

Moving on to slide seven, let me provide more detail about the backbone for our customers, which is expanding into new territories in DRC.

DRC is the 11th largest country in the world with a land mass that is equivalent to Western Europe. This backbone of 1800 kilometres represents the distance between London and Rome through the virgin jungle, in which we have been rolling out and building up to 100-metre towers, effectively providing line of sight over the forest canopy.

We are excited about this investment. It allows our customers to provide service to six million additional individuals. As you will be aware, only half of the DRC population today has a network coverage where they can access mobile services and this step by a couple of our big MNO customers means that they are going to obviously invest in further last-mile connectivity through smaller towers to access further population centres.

We will have this project completed by the end of the year. The build programme is well on its way and we will be posting some of the photographs of the sites on our website shortly. Now, the other exciting aspect to DRC is that in the last three months, three of the four core MNOs in DRC have secured and purchased 4G licences, with the fourth MNO currently in negotiations to also acquire a 4G licence.

We believe that this is going to increase the offering of 3G and the rollout of 4G, particularly as mobile smartphone prices continue to drop. This will be a huge facilitator for further growth for our customers on the back of our infrastructure capability, and therefore we will be continuing to grow.

Regarding embedding our business excellence strategy, in addition to the 70 Lean Sig Sigma specialists trained last year, we are in the process of training a further 80 individuals in our business. This will result in almost 50% of the payroll workforce having received training, and we are already seeing a huge benefit from efficiency and productivity gains in our business.

I am pleased to say that our ultimate and main driver is delivering exceptional customer service, and pleased to recognise that 90% of our towers are performing at Lean Sig Sigma levels of less than two seconds downtime per tower per week. We believe we are leading the way in our industry in Africa, in delivering this level of power uptime for our customers.

In addition to customer service, we are seeing good margin growth as indicated earlier.

The other aspect I want to highlight is that we developed a digitised application over the last 12 months, and have been rolling it out this year. 87% of our sites now use this application, allowing us to monitor and track the real time performance of our field service teams, and ensure they are efficient and more importantly, are able to do the work at hand in a responsive way. We should have the remainder of our portfolio completed by the year-end. This will drive further productivity efficiencies in our business, particularly in managing our supply chain.

Finally, we are very active on the business development front. We believe that there is opportunity outside of our four core markets. Of course, we remain focused continuing on our organic and inorganic potential in our four existing markets. However, we have added an extra vigour in looking for opportunities outside of our existing four markets in Africa.

Specifically, we are looking at further tower acquisitions, but also on adjacent technologies mentioned before, i.e. small cell, fibre, and data centres. There is a good amount of time spent by myself, Tom, and our business development team to try to bring something about over the next coming months.

So, on that, let me hand over to Tom, to talk in more detail on the financials.

Tom Greenwood Thanks, Kash. I am now on page nine, the key highlights.

As Kash mentioned, we have achieved very strong year-on-year growth with revenues up 5% and EBITDA growing 27%, which equates to us reaching the 49% margin point at Q2, and we very much hope and expect that we can grow that further through this year.

Even in the quarter-on-quarter from Q1 to Q2, our EBITDA has grown 5%. That growth is on a backdrop of a slightly slower tenancy rollout through the quarter and the Airtel-Tigo merger, for which the new contract became live for us on April 1st, so right at the beginning of Q2.

On the capex side, we have invested $34 million in Q2, a fair amount of that being in relation to the investment in the backbone sites in DRC. I will come onto that capex guidance in a few slides time.

Net debt was reasonably flat quarter-on-quarter, touching up slightly due to capex investment, which I will come on to in a few slides.

Turning now to page ten, the revenue breakdown.

It is very much the same position as we have been seeing over the past few quarters and years. The vast majority of our revenue, 86% in fact, is coming from Africa's big five mobile operators, being Vodacom, Tigo, MTN, Orange, and Airtel, and we anticipate that kind of trend to continue, virtually all of this revenue being under long-term contracts.

In terms of foreign exchange, again, similar to previous quarters and years, with around 56% of our revenues in dollars or euro-pegged currency, and this translates down to an EBITDA line of around 70% because we have a natural hedge in our P&L with the local currency operating costs. And, again, the revenue breakdown by country is very similar as before, around 40% coming from each of Tanzania and DRC, with the balance coming from Ghana and Congo Brazzaville.

Turning now to page eleven, the costs and margin analysis.

The chart on the top left illustrates the margin growth of EBITDA since Q1 15. We have virtually doubled margin over that time, from 25% in Q1 15 to 49% in Q2 18, and again we aim for that to continue growing through the rest of this year and beyond.

That is of course being driven by top line growth, but also by operational efficiencies, we have been driving through the business as well, with the solar rollout and other power-saving initiatives. That is illustrated on the bottom left-hand chart, where you can see the cost of sales per quarter trending down nicely.

So you can really see the impact there of some of the opex savings projects we have been pushing over the last year coming through.

Now, turning to page twelve, capital expenditure.

Our capex for the half-year was around $70 million, around $11 million of that being maintenance and corporate capex, and the remainder being growth and upgrade capex. We are revising slightly our capex expectations for the year, which has been driven by additional growth capex that either we have secured through orders, or we think we might by the year-end. The prior FY18 guidance was $90 million and the updated guidance for the year is now $105 to $120 million.

The first additional $15 million is driven mainly by projects or contracts we have secured, being the Airtel-Tigo contract in Ghana and the backbone projects in DRC, and then there is an additional $15 million of potential growth capex, which may come in by the year-end, or may be a 2019 event. We do not know the exact timing on those because, of course, it is dependent on third parties and the customers we are negotiating with.

We hope to give some more colour or update on that in our Q3 call, which will be in November. Final point on this slide is that maintenance and corporate capex guidance is still $20 to $25 million, so unchanged on that.

Moving now to the financial debt on slide thirteen.

Continued de-leveraging on a gross leverage basis was driven by the growth in EBITDA, ending Q2 at 4.1x times, which is down from 4.2x in Q1, and down from 4.9x across the whole of FY17. On a net basis, we are still in the same range as before, this time at 3.7x, slightly up from last quarter but really within the range that we typically expect; being between 3.5x to 4.0x.

And with that, I will hand back to Kash.

Kash Pandya Thanks, Tom. So we are on slide fourteen, just to summarise before we move to Q&A.

We have continued to maintain a strong position in our core markets. As you know, in three of the four markets we operate in, we are the only independent tower company, but we are particularly pleased in Ghana, where there are other independent tower companies. We have been successful with the Airtel-Tigo joint venture, through the open tender process. This has extended our contract life from 5 years to 15 years and established our future in Ghana, while continuing to serve our customers in Ghana and across the other three markets.

Our revenue growth has been 4% year-over-year, and we delivered 27% EBITDA growth year-over-year.

Our contract life still is around $3.3 billion, with close to nine years of average contract life remaining for our business, so a strong pipeline ahead of us. Importantly, 56% of our revenue is in USD or euro-pegged currencies, hard currencies, and close to 70% of our EBITDA is in hard currencies.

Our margin continues to improve, over 14 consecutive quarters, and we have seen a nine-percentage point improvement year-over-year in our EBITDA margin evolution. In terms of our re-occurring free cash flow, we delivered $75.1 million for the first half of the year. That is an improvement of 41% year-over-year. The team and the business have really focused and are driving a number of different matrices in the right direction.

Looking forward, the fundamental macro drivers are solid in our four markets. We see continued momentum across all four markets, particularly reinforced by the strength of the new joint ventures from operators both in DRC and in Ghana. This is particularly reinforced by the fact that our big customers are investing and buying 4G licences to rollout new technologies, investing in new territories in the markets we operate in, and we are the choice infrastructure builders for our customers.

Finally, of course, we have a culture established in our business over the last three years. The business excellence strategy and Lean Sig Sigma capabilities continue to drive efficiencies to improve our margins. So, exciting times, and we are focused on continuing to improve shareholder and bondholder returns.

On that note, I am going to hand over, back to Laura, for taking our questions.

Operator Thank you, Kash. Ladies and gentlemen, if you would like to ask a question please press star followed by one on your telephone keypad now. If you change your mind, please press star followed by two. And when preparing to ask your question, please ensure your phone is unmuted locally. As a reminder, that is star followed by one to ask a question.

Our first question today comes from Kojo Amoo-Gottfried from Enko; please go ahead.

Kojo AmooGottfried Hi, thanks for the presentation. In the last call we had, you stated that you thought you were going to be free cash flow neutral by the end of this year. Now, given the jump in capex, do you still think that is likely to happen? Or do you want to revise that guidance?

Tom Greenwood The guidance on that would be impacted by the capex increase, so we would be slightly negative for this year, in the same quantum as the capex increase. Again, on the capex, as I mentioned, some of it we are not sure if it will happen by the year-end or not, so we are giving a range on that. But as the capex is higher, then there will be some negativity on the free cash flow, as you imply.

Kojo AmooGottfried Great, thanks.

Operator Our next question today comes from the Simon Cooke from Insight Investment; please go ahead.

Simon Cooke Hi, thank you for taking the questions. A few, if possible; I will drop back if you want me to. Firstly, on DRC; it looks like there is a bit of weakness versus the prior quarter, so could you just touch on a bit more about what is going on in DRC, and whether it is structural or whether it is just temporary slow-down? And then, secondly, on the Airtel-Tigo impact; I don ot know if it is related, but it looks like your overall contracted revenue has dipped a bit from the first quarter, from $3.43 billion down to $3.28 billion, could you just talk through what is going on there and how we should think about the impact of the Airtel-Tigo merger for financials going forwards?

Kash Pandya Yes, of course. Hi, Simon, good to have you on the call. On the first part of your question, on DRC; we have seen a little bit of a slowdown, partly driven, actually, by the ZTE issue. That has been resolved now. I think you are aware, in the public domain, the challenges there. Vodacom has predominantly ZTE active equipment in DRC and that issue has now freed up the supply chain and so we expect to see more activity from Vodacom. And obviously we are building the backbone, as we discussed, there.

With regard to Airtel and Tigo and the contract life, I think overall our revenue for that contract has stayed equal because our lease rate improved, and that was offsetting the reduction in the tenancies that we agreed with them. And I think the reduction overall in contract volume to $3.3 billion is just a matter that we have had another three to six months go by and we have eaten up some of the months.

Simon Cooke Okay. And then one other before I drop back in the queue; just in terms of you talk about potential for expansion and M&A, or organic expansion into other geographies, in terms of funding that, how are you guys thinking about funding it? Right now your cash balance is $70-odd million, $74 million, so if you want to burn a significant amount of cash expanding somewhere, I presume you are going to need funding, rather than going down to $10, $20 million of cash? So is this a case of raising more debt, or do you raise equity, or a combination?

Tom Greenwood Hi, Simon. I think we will always look at all options, whether that is cash on balance sheet, raising more debt, raising more equity. I think from where we stand today, there is a little bit of debt capacity in the business. So if we needed to, we would look to raise a little bit more debt, and that may come in the form of a bond tap, dependent on the market, or may come in the form of a loan from a bank, which medium-term, we would look to re-finance through bonds anyway.

And then equity, as well, is always an option and whether that is cash equity, or in fact issuing shares in our Group in return for assets, or whether it is a part-cash, part-share deal. So these are all options we would consider, and I think the order of priority is always cash on balance sheet first, then debt, then equity, and raising the debt needs to be within the confines, of course, of the covenants and what we feel comfortable with. So we will look at each case on a case by case basis, based on those parameters.

Simon Cooke Okay, just a quick follow-up, if I can, on that? In terms of the potential scale of expansion, because obviously you are talking about all the options you have on the table; are you guys talking about potentially very large-scale M&A, or is this more sort of bolt-on, so are we talking a small tap to the bonds, or is this potentially transformative M&A?

Tom Greenwood I think what we are looking at is more bolt-on, rather than super-transformative.

Simon Cooke Okay, thanks.

Operator As a reminder, ladies and gentlemen, that is star followed by one to ask any further questions. We currently have no further questions registered on the line, so I will hand back to you, Kash.

Kash Pandya That is great. Thanks, Laura. Well look, thank you very much, everybody, for joining the call. We look forward to speaking to you for our Q3 update, in November. Thank you.