Paratus Namibia Holdings
FY21 Results Review
November 2021

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Paratus Namibia Holdings Ltd

FY21 Results Review

Target Price (c) ***1,326***

Current Price (c) 1,275

Year End 30 June	FY19	*FY20	FY21	FY22E	FY23E
Revenue (N$ m)	5	152	341	378	436
EBITDA (N$ m)	7	41	95	118	150
Profit after tax (N$ m)	7	20	29	39	53
HEPS (c)	30.7	50.5	57.9	79.0	110
DPS (c)	0.0	10.0	20.0	26.1	36.2
DY (%)	0.0	0.9	1.7	2.1	2.8
P/E (x)	35.9	19.8	20.1	16.1	11.6
EV/EBITDA	45.2	10.9	8.1	7.1	6.0

Recommendation	BUY
NSX Code	PNH
Market Cap (N$ m)	585
Shares in Issue (m)	48.7
Free float (%)	94.3
52-week high	1,275
52-week low	1,125
Expected Total Return (%)	6.1%

Source: PNH, IJG Securities

**IJG has restated FY20 results to include 12 months, instead of the 16 months reported by PNH for comparability purposes.*

FY21 Results Review

Paratus Namibia Holdings (PNH) released results for the year ended 30 June 2021 (FY21). FY21 marked the reporting company's first full year as the 100% shareholder of its operating company, Paratus Telecommunications (Pty) Ltd Namibia (PTNA). Despite challenging economic conditions, PTNA continued to report impressive growth in its fibre customer base, which increased by 108.9% y/y to approximately 2,500 subscribers.

Given that PTNA is the main performance driver for the group, and management now releases financial results for PTNA, this report analyses and discusses PTNA's operations extensively. Despite virtually identical income statements, PNH and PTNA have significantly different financial positions. The reader is hereby cautioned that PNH's performance ultimately determines prospective investment returns.

PNH's top line increased by 123.4% y/y to N$340.6m, with the majority of the increase attributable to PNH increasing its stake in PTNA from 51.4% to 100% in August 2019. PTNA's revenue, which constitutes 98.7% of PNH's top line increased by 3.7% y/y to N$336.1m.

PTNA's EBITDA rose by 21.6% y/y to N$92.4m, partially due to the N$12.1m increase in revenue. Furthermore, the company achieved a N$24.0m reduction in cost of sales (before depreciation and amortization.) Overall, PTNA's EBITDA margin rose from 23.4% in FY20 to 27.5% in FY21.

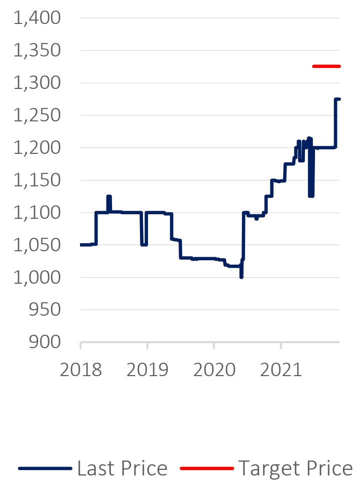
PNH's total assets increased by 25.3% y/y to N$921.9m, with property, plant, and equipment (PPE) increasing by 53.4% y/y to N$390.0m. In comparison, PTNA realised a 54.5% y/y increase in total assets, which totalled N$608.4m in FY21. PTNA's PPE increased by 66.3% y/y to N$339.6m, which is N$50.4m below that of PNH. The difference is due to PNH owning properties in Prosperita and Swakopmund valued at a combined N$38.6m and capital work in progress with a book value of N$10.6m. PNH currently has a N$170.9m cash and cash equivalents position, which includes a N$159.9m money market investment, which is substantially higher than PTNA's N$132.6m cash position. Although PNH's large cash position is expected to be invested into capital projects in FY22, it has created a drag on the company's return potential, and resulted in sub-optimal leverage levels, evidenced by the low ROE in FY21 of 5.4%. In comparison, PTNA recorded an ROE of 16.3% in FY21.

PNH allocated a N$195.6m investment into capital expenditure for FY22, with the majority earmarked for Fibre-to-the-X (FTTx) rollout, as it looks to increase its market share in the Namibian fibre space. The company completed the acquisition of an erf to construct its new tier-3 data centre, with construction expected to be completed in the third quarter of 2022 at a total cost of N$123m.

Valuation

IJG has used a sum of the parts free cash flow to equity model to value PNH. Given that PNH is still in its growth phase, fixed capital investment is expected to accelerate to N$350.8m by FY23 for the group. Fixed capital investment is forecast to average N$204.2m a year over the forecast horizon. EBITDA has been forecast to increase from N$94.5m in FY21 to N$120.2m in FY22 and N$392.3m in our FY30 terminal year, due to a strong national fibre roll-out as well as the introduction of the data centre in the third quarter of 2022. Using a cost of equity of 17.6% and a long-term ROE of 13.1%, we derive a target price of N$13.26 per share. Paired with an expected dividend of 26 cents per share, we forecast a total return of 6.1%. Despite the relatively low return, there is room for further upside if the company can successfully execute its national fibre roll-out. We initiate coverage on PNH with a **BUY** recommendation.

PNH Share Price (c)



Dividends

A final dividend of 10 cents per ordinary share was declared for the period ended 30 June 2021.

- Last day to trade: 22 Oct 2021
- Record date: 29 Oct 2021
- Payment date: 12 Nov 2021

Background

Paratus Namibia Holdings (PNH), formerly Nimbus Infrastructure Limited, was originally established as a capital pool company, with the aim of acquiring viable assets that satisfy the ICT sector investment criteria.

Nimbus appointed Cirrus Capital as the investment manager, who was responsible for identifying viable assets. The tenor of the investment management agreement was for 24 months, with Cirrus entitled to a 2.0% transaction fee for every acquisition made by Nimbus, as well as a 0.5% management fee for the total value of all assets acquired or invested in by Nimbus.

Nimbus issued 10,220,850 shares valued at N$10.00 each in its initial private placement in September 2017, raising a total of N$102,208,500, before listing on the NSX in October 2017. Institutional investors accounted for about 79.0% of the total capital raised, with Capricorn Investment Group emerging as the largest shareholder at the time, holding 33.3% of Nimbus.

In November 2017, Nimbus released a circular, proposing Paratus Telecommunications Namibia Limited (PTNA) as a viable asset for acquisition. PTNA holds the head office from which Paratus Africa Group's operations are overseen and managed. It is important to note that the PTNA acquisition by PNH only gained exposure to PTNA and not the Paratus Africa Group. PTNA offers services such as mobile LTE, fixed-line internet, as well as a variety of other telecommunications services including point of sale devices, cloud services, voice over IP and traditional voice calls. In 2014 PTNA launched a privately owned fibre ring in Windhoek, a first for the country. Nimbus' rationale for the PTNA acquisition was to gain exposure to PTNA's revenue and profit stream, in addition to its asset base, consisting of terrestrial and urban infrastructure. Additionally, PTNA was in the process of constructing the Trans-Kalahari Fibre Line (TKF), spanning from Swakopmund, via Windhoek to the Buitepos border with Botswana. The acquisition entailed a N$20m cash payment to Cuvelei Investments in exchange for an 8.0% holding in PTNA. An additional N$75m was paid to PTNA for the allotment and issue of PTNA shares. The total consideration of N$95m resulted in a 26.5% shareholding of PTNA by Nimbus, effectively valuing PTNA at N$358.5m. It was further determined that Canocopy, a subsidiary of PTNA, would be removed as a wholly-owned subsidiary of PTNA as it was not a core operating component.

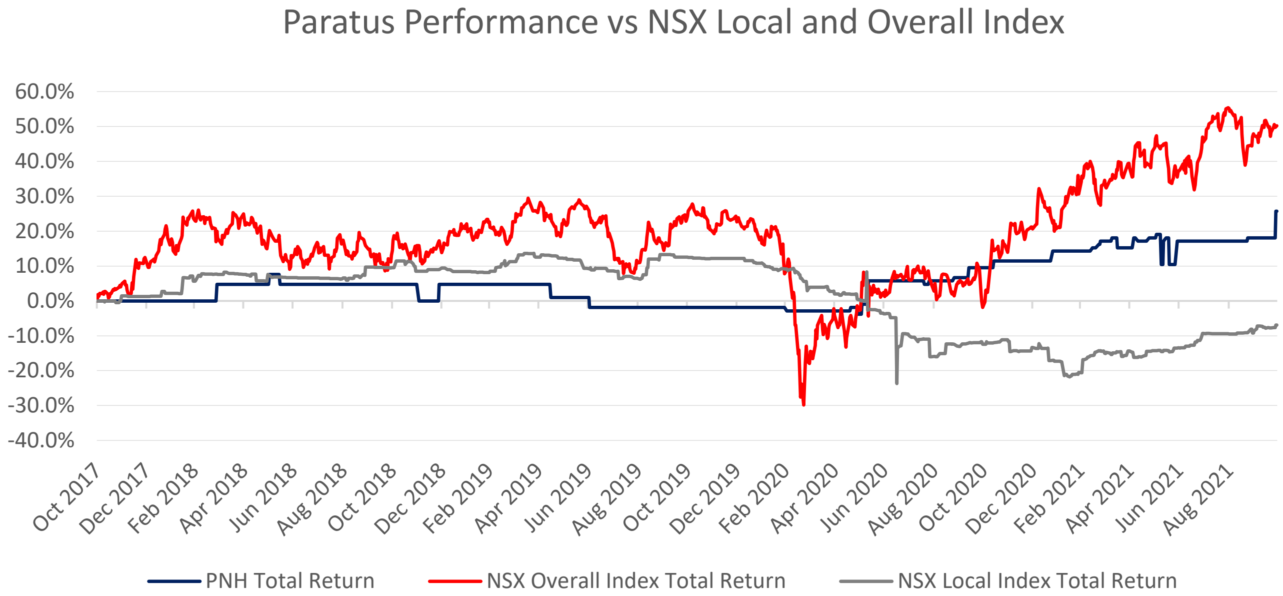
The construction of the TKF Line was a strategic move by PTNA as the Paratus Africa Group's operations source the majority of its bandwidth from South Africa via Zimbabwe or Botswana, as transit prices via Telecom Namibia were multiples more expensive. The TKF Line would offer a cheaper alternative for the Paratus Africa Group to source bandwidth from Namibia via Botswana. The TKF Line consists of 48 single fibre cables or cores, which are paired into 24 pairs, offering 40 x 10 Gbps wavelengths per pair, called an STM-64 connection. At a total of 960 STM-64 connections, the TKF Line's capacity is about 320 times that of Namibia's current internet utilisation.

In June 2017, PTNA signed a commercial agreement with BoFiNet, a telecommunications company based in Botswana. BoFiNet purchased access to 2 of the 24 dark fibre pairs in a 20-year Dark Fibre Indefeasible Right of Use agreement on the Ngoma-Sesheke fibre line. In exchange for transit capacity, equivalent to an STM-64 connection from Buitepos to Ngoma for the duration of the agreement, PTNA offered BoFiNet a 35% discount, bringing the contract value to US$981,000. In September 2017, PTNA entered into a Super Indefeasible Right of Use agreement with BoFiNet. BoFiNet purchased 10 x 10Gbps wavelengths for 20 years, for a total cost of N$87.9m. This bandwidth sale represents a mere 1.0% of the total capacity of the TKF Line.

Trans Kalahari Fibre Line, Source: Paratus Telecommunications (Pty) Ltd

In a circular released in March 2018, Nimbus announced its intent to increase its stake in PTNA to 51.4% via a proposed share swap. Nimbus issued 8.5 million new ordinary shares at a predetermined value of N$89.2m in exchange for 8,815 ordinary PTNA shares (18.6%) held by Cuvelei Investments and 3,000 ordinary shares (6.3%) held by B. Harmse, the current Paratus Africa group CEO. A 15:10 rights issue was combined with the share swap, with the intention to raise additional capital, as well as to mitigate a 24.7% dilution to existing shareholders. A total of 15.5m rights issue shares were made available at a subscription price of N$10.50. 9.9m rights issue shares were subscribed for, resulting in an additional capital raise of N$103.4m for Nimbus. The company stated two potential investments in the share swap circular. Firstly, to acquire a shareholding in Lightstruck Operating Company, which specialises in the rollout of fibre to the home and office. And secondly, the construction and operating of co-location hubs, which would enhance the cloud service offering.

Nimbus released a circular in August 2019, announcing a proposed share swap transaction to increase its stake in PTNA from 51.4% to 100%. The swap transaction entailed the issue of 20.0m ordinary Nimbus shares, valued at N$210.1m in exchange for 46,168 ordinary PTNA shares. PTNA's implied valuation was N$432.4m, 20.6% higher than the first acquisition of the 26.5% stake in 2017. The transaction would cement Nimbus's exposure to PTNA's revenue streams while aligning interests between Nimbus and PTNA. Furthermore, access to capital for PTNA would be simplified via the 100% shareholding, allowing for an aggressive infrastructure rollout. Finally, Nimbus would be able to terminate the management agreement with PTNA and the investment management agreement with Cirrus. Following the swap, Nimbus changed its name to Paratus Namibia Holdings (PNH) and its year-end was changed to 30 June, to coincide with that of Capricorn Group, which had a 17.68% stake in PNH after the swap deal. Although PNH acquired a 100% stake in PTNA from Paratus Group Holdings, the share swap transaction resulted in Paratus Group Holdings emerging as the majority shareholder of PNH, with a 41.07% stake.

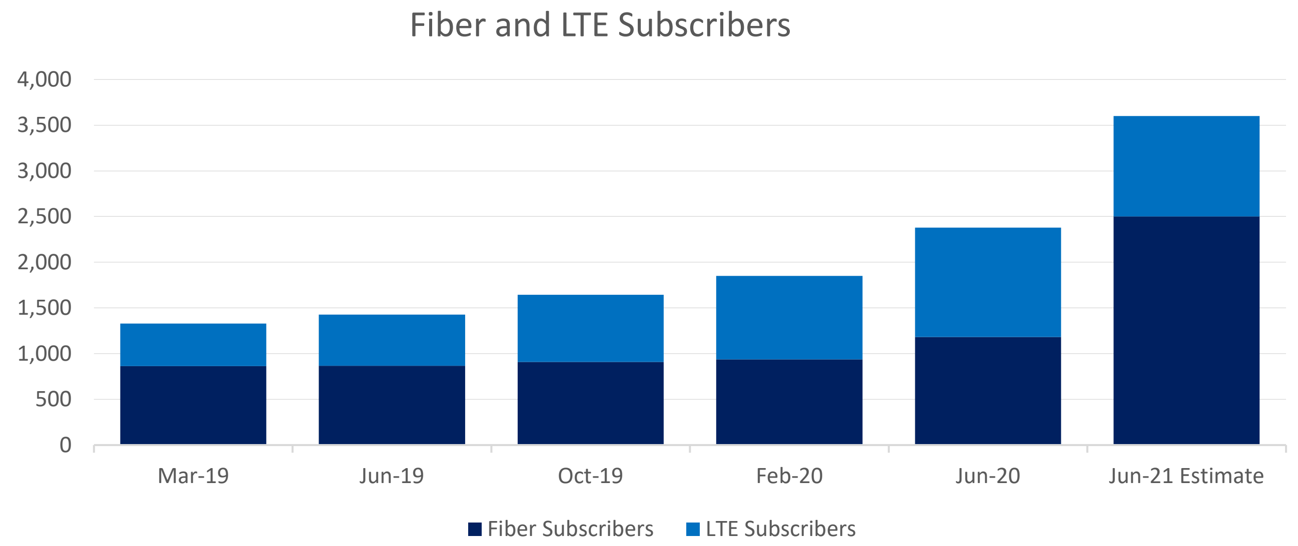


Source: Bloomberg, IJG

Since listing on the NSX in October 2017, PNH has grown its market cap from N$102.4m to N$586.1m in October 2021. The cumulative holding period return for PNH shareholders at the end of these four years stood at 25.2%, with the price rising from N$c1,050 to N$c1,275. PNH's performance has been more stable compared to the NSX local and overall index, which has displayed a great amount of volatility since the beginning of the Covid-19 pandemic.

Performance Drivers

Connectivity, which includes internet connectivity through Fiber, WiMax and 4G LTE, and services such as virtual private networks (VPN) have been the main driver in PTNA's financial performance, accounting for 81% of total revenue in FY21, and averaging 86.8% of recurring revenue over the past two years. Evident in the graph below, fibre subscribers have grown exponentially, from 557 subscribers as at June 2019, to 1,197 in FY20 and up to about 2,500 in FY21. This translates to a compounded annual growth rate of 111.9% in fibre subscribers (retail and corporate).



Source: Paratus Namibia Holdings, IJG

PTNA has aggressively rolled out its fibre infrastructure since 2014, which now covers Windhoek, Swakopmund, Walvis Bay, Gobabis, Otjiwarongo, Okahandja and Grootfontein. Capital expenditure on fibre infrastructure totalled N$72.6m in FY20, constituting 72.0% of the N$100.8m capital expenditure for the year. In FY21, capital expenditure increased to N$178.0m, with the majority invested into Fibre-to-the-X (FTTx) rollout. During FY21, 342km of new fibre ducts were installed in Windhoek's suburbs, in addition to rollouts in Swakopmund, Walvis Bay, and Grootfontein.

In addition to its private fibre infrastructure, PTNA also utilises capacity from Telecom Namibia as well as NamPower. Management noted that they prefer NamPower's "GridOnline" service offering, as it is cheaper than Telecom's rates.

Presently, PTNA's fibre infrastructure passes an estimated 21,000 residential units, with 2,500 current subscribers, translating to a penetration rate of 11.90%. The current average revenue per fibre user (ARPU) is about N$1,250, which is significantly higher than similar services in South Africa where ARPU's tend to be in the region of R500. As a result of superior ARPU, PTNA is able to achieve breakeven at a far lower penetration rate than in South Africa where breakeven penetration rates currently range between 40%-65%.

Management noted that competition in the fibre space is expected to intensify as Telecom and MTC in particular look to grow their top-line. As such, the current trend in capital expenditure towards the rollout of FTTx is likely to persist, with the company's current strategy to gain the first-mover advantage in suburbs across the country, while looking to increase its penetration rate over time.

PTNA has experienced additional success in its LTE network offering, with total subscribers rising from 869 in June 2019, to 1,181 in FY20, which translates to a 35.9% y/y increase. Management did not provide an exact figure for FY21 but did note that the aggressive fibre rollout did have a cannibalisation effect on the LTE customer base. This is an issue that is unlikely to persist, as LTE expansion projects are set for areas that do not have fibre, meaning the LTE target market and customer base will largely be mutually exclusive from fibre.

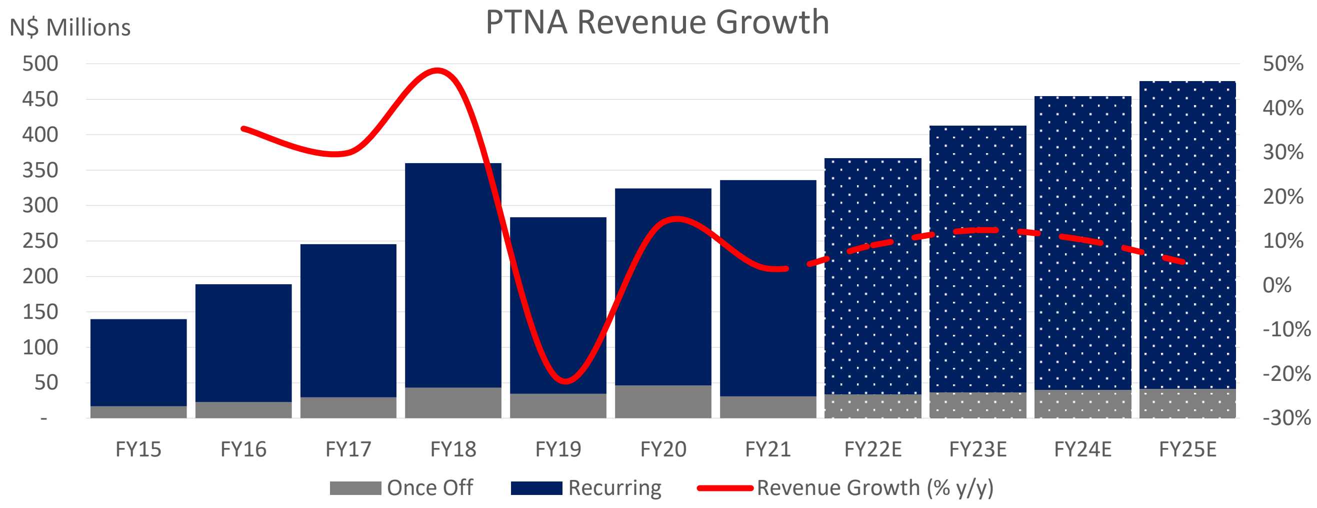
PTNA possesses 1,800 MHz and 2,600 MHz spectrum licences and leases tower space from Powercom, a subsidiary of Telecom Namibia. PTNA is not pursuing the rollout of 5G at the moment as 5G legislation is still pending and 5G spectrum bands travel far shorter distances than LTE spectrum bands, making 4G LTE a cheaper and more viable option as it requires fewer towers.

A critical component in achieving success in a fibre rollout is to be the first mover in a suburb. Achieving this entails two different possible routes. On the one hand, it involves developing fibre infrastructure in established residential areas. This is an expensive and laborious process that involves digging trenches through rigid surfaces such as tar and concrete. Once the fibre ring is set up, it will take another four weeks to connect a prospective client, which could serve to dissuade prospective clients from signing up for fibre in the first place. This time process does shorten however, as the fibre network matures.

On the other hand, the company could pursue connectivity agreements with pre-construction phase developments. This process integrates the fibre installation with the construction of residential properties, solving the issue of trenching through resistant surfaces. Furthermore, since the infrastructure is ready for the new resident, it takes up to a week to connect them to the network, which is significantly faster than the former.

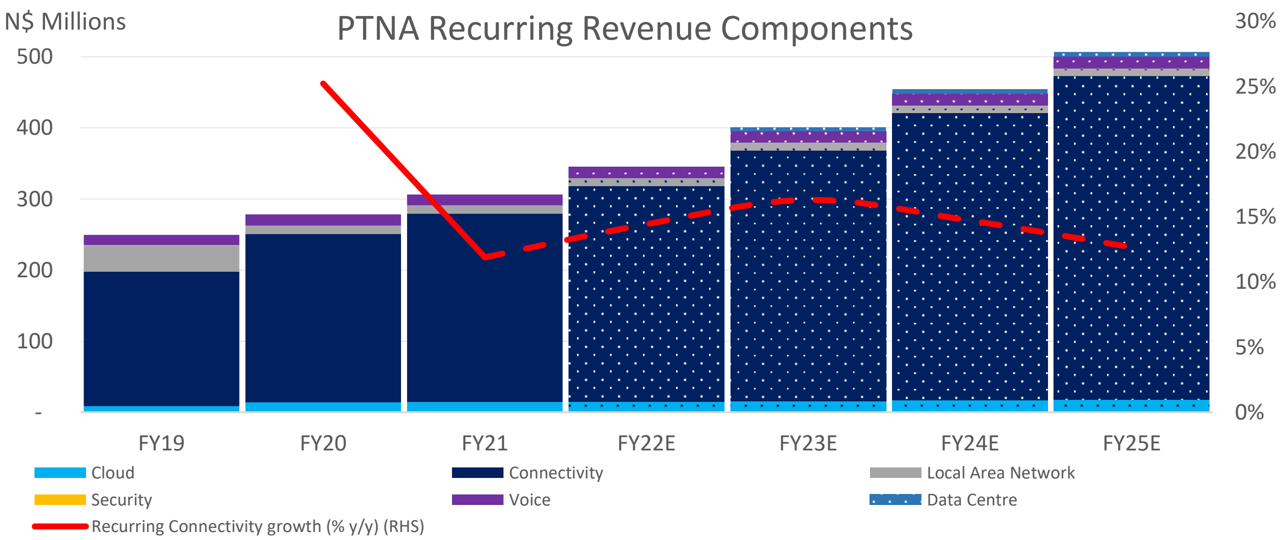
Given that Namibia is characterised by a relatively low population and low income, the construction of large residential estates is rare. Therefore, most of PNH's fibre rollout has and will continue to entail the more strenuous approach. That said, PNH announced on 16 November 2021, that it entered into a commercial connectivity agreement with Ongos Connect, which will provide fibre connectivity to over 4,500 housing units in Ongos Valley phase 1. This is an opportunity for PNH to increase its revenues at a lower cost, thus improving profitability margins in the future. The first homes are expected to be completed in November 2021, with phase 1 culminating in 2023 according to the latest estimates.

Revenue



Source: Paratus Namibia Holdings, IJG

PTNA reported revenue of N$245.5m in FY17. Since then, revenue growth has averaged 10.8% y/y, increasing to N$336.1m in FY21. However, revenue growth slowed in FY21, increasing by 3.7% y/y, compared to the 14.2% y/y growth recorded the year before. The slower revenue growth was attributable to lower demand amongst the corporate sector, which has been under tremendous pressure during the Covid-19 pandemic. This was reflected in revenue growth from connectivity, which slowed from 25.2% y/y in FY20 to 11.9% y/y in FY21. Further declines were experienced in revenue collections from local area networks, which contracted by 3.1% y/y, coming off an already low base after it contracted by 67.9% y/y in FY20.



Source: Paratus Namibia Holdings, IJG

As previously mentioned, connectivity has been a driving force behind PTNA's success. Growth in revenue collections from this category averaged 18.6% y/y over the last two years, and we expect this double-digit growth to persist in the medium term, at an expected average rate of 13.6% y/y over the next five years. This is based on the assumption that the company will continue its fibre rollout to cover

30,000 urban units by the end of FY24, after which we expect growth in the network to drop to more organic levels. We further expect fibre penetration to rise steadily from the current 11.9% to 26.0% by the end of FY25 as the conversion to fibre lags the infrastructure rollout. We model revenue on the assumption of an ARPU of N$1,400. Further, the company's current strategy to be the first-mover in the fibre space, and then increase subscribers has the potential to improve the company’s margins in the future, as the variable costs involved with fibre rollouts are rather low, and as more subscribers opt for PNH’s fibre, the fixed costs will be spread over a larger subscriber base.

A major difference between PNH and its state-owned competitors is that PNH is focused on gaining customers, while the mature companies look to retain their customer base. Whether MTC and Telecom will pursue fibre as an avenue for customer retention remains uncertain. Interestingly, in South Africa, the telecommunications market leaders have been wary in terms of rolling out fibre to the home (FTTH) and the global trend amongst mature telecommunications providers as well as MTC has been to pursue financial technology product offerings such as mobile financial services. Further upside potential exists for PNH if this trend applies to the Namibian telecommunications market, allowing it to become the dominant player in the country’s fibre market.

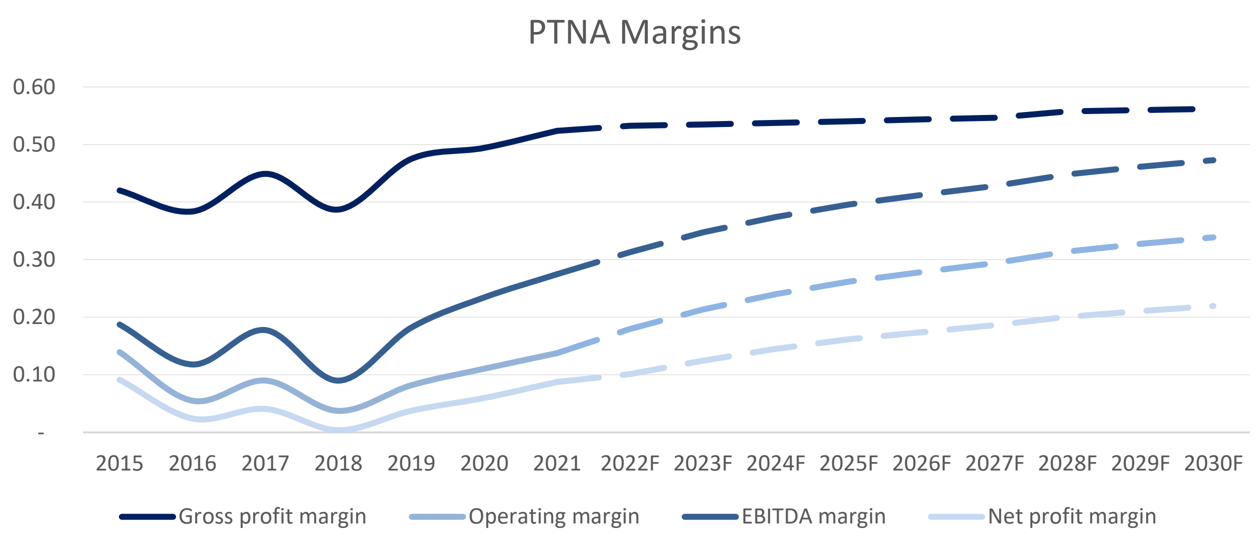
The sale of bandwidth capacity on the TKF line in the form of indefeasible right-of-use agreements continues to provide PNH with a constant revenue stream. The sale is recognised as revenue received in advance and recorded on the balance sheet as a contract liability and amortized over the life of the contract. The agreement with BoFiNet has a book value of N$79.9m, with 18.2 years remaining. The amortization of this contract translates to yearly revenue of N$4.8m for PNH. Furthermore, the TKF line has effectively connected Namibia to Botswana, DRC, Malawi, Zambia, Tanzania, Zimbabwe and Mozambique. As noted in all three Nimbus circulars, one of the motivations behind the TKF Line was to provide cheaper bandwidth to the Paratus Africa Group’s operations. Consequently, revenue from related parties totalled N$11.6m in FY21, bringing total revenue generated by the TKF line to N$16.0m. With the TKF currently valued at N$60.3m, this translates to a return on asset of 26.5% per annum.

Voice revenue fell by 1.2% y/y to N$15.6m in FY21, accounting for 5.1% of recurring revenue. We do not expect voice services to be a major income driver going forward. Cloud services accounted for N$14.5m of recurring revenue, up 3.8% from FY20, which in turn was up 64.6% y/y from FY19. This category is largely dependent on demand from the corporate sector, which is likely to remain gloomy in the medium-term, and as such, this category will also likely remain stagnant.

During the year, PNH concluded the acquisition of the erf to construct the Armada Data Centre, which will be tier-3 by design, which, according to PNH’s marketing material, offers superior efficiency with 99.8% uptime and 72 hours of protection from power outages. The data centre will also offer additional business facilities for business continuity, such as video conferencing and boardroom equipment. The data centre offers a total of 30 uncaged racks, 20 uncaged half-racks in addition to a 2x4 and 2x6 caged rack configuration. PNH is currently running a pre-launch special, however, management has noted that it is difficult to sell a product on which construction is still taking place. We believe that the data centre will be an attractive investment for the commercial banks, which will likely become future anchor tenants. Capital expenditure towards the project totalled N$18.0m in FY21. The project is expected to be completed in the third quarter of 2022 and total cost is expected to come in at N$123.0m. We have included an estimate for revenue from the data centre in our forecasts and expect it to total N$5.4m in FY23, before picking up to N$6.7m in FY24. In our view, the data centre is a strategic move, that will benefit beyond income received from the data centre. The data centre serves as an opportunity for

PNH to secure large corporates, such as the banks, that will serve as their anchor tenants. This could result in greater penetration in the corporate space for the provision of other services such as fibre and local area networks. In our view, this provides potential for future revenue growth.

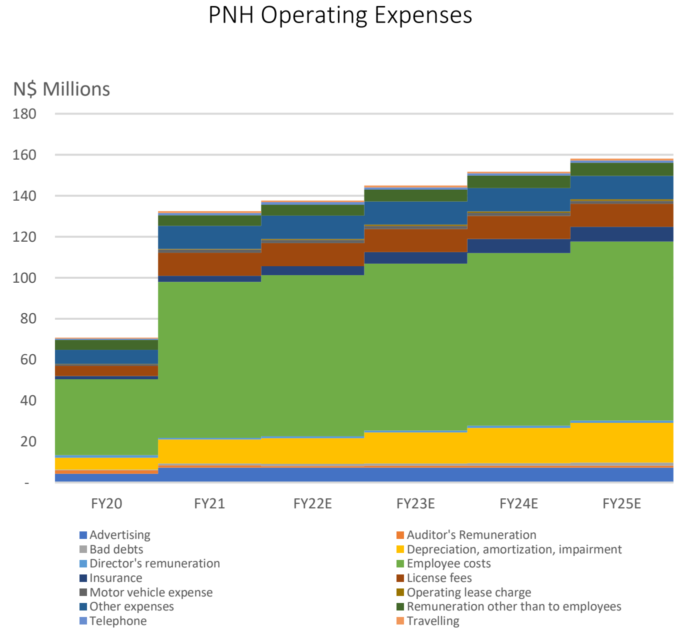
Margins

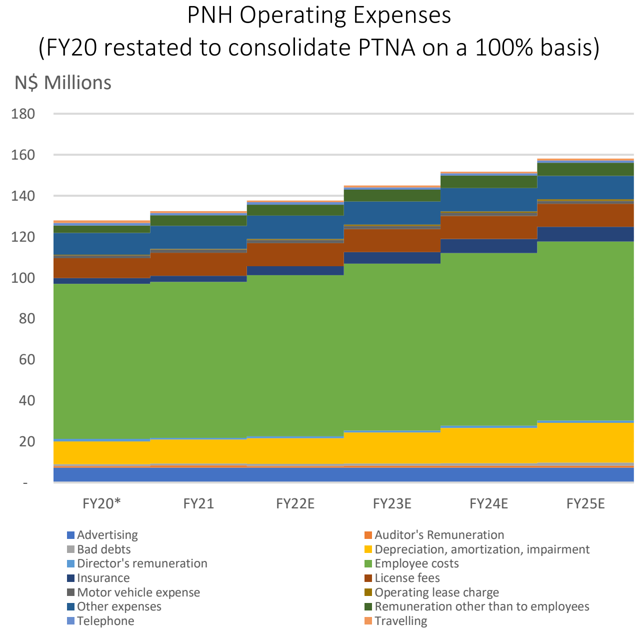


Source: Paratus Namibia Holdings, IJG

Despite increasing the company's revenue-generating potential, another motivation behind the construction of the TKF line was to increase PTNA's competitiveness by internalising a substantial proportion of its backhaul capacity, thus decreasing its cost of sales profile. Evident in the above graph, this strategy has paid off, with the average gross profit margin rising from an average of 41.0% before the conclusion of the TKF line to 47.5% the year thereafter. The company's gross profit margin continued to tick up, increasing to 52.4% in FY21. PTNA also recorded increases in its operating margin, which rose from 11.1% in FY20 to 13.8% in FY21. Due to the capital-intensive nature of PTNA's operations, paired with widening profitability margins, its EBITDA margin widened from 27.5% in FY20 to 31.3% in FY21. Finally, prior to the Nimbus acquisition, PTNA's net profit margin averaged 5.2% and increased to 6.0% in FY20, before rising to 8.8% in FY21. We forecast the company to achieve its first double-digit net profit margin in FY22 at 10.1% and expect it to reach 20% by FY28.

Operating Expenses



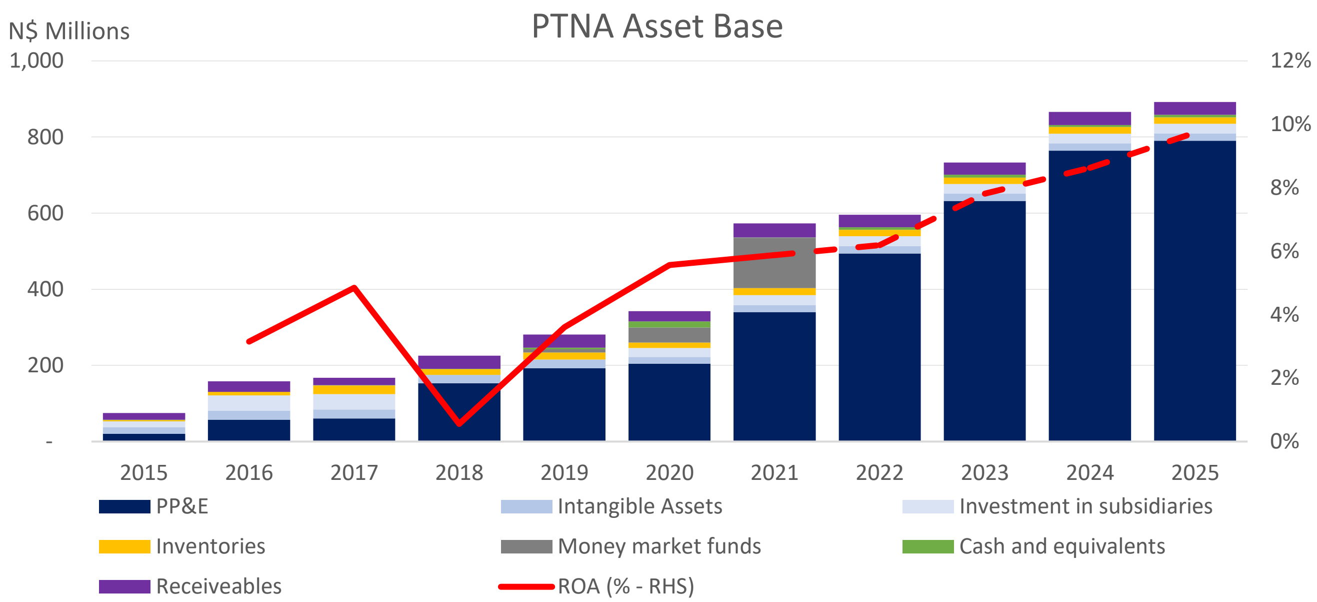


Source: Paratus Namibia Holdings, IJG

PNH's operating expenses rose by 87.3% y/y to N$132.4m, the increase is largely attributable to the fact that FY21 was the first full financial year in which PTNA is 100% consolidated in the holding company's financial statements. For comparative purposes, IJG has normalised PNH's FY20 operating expenses by including PTNA on a 100% basis. Based on the restated values, operating expensed rose by N$4.5m or 3.5% y/y in FY21. Employee costs, comprising of salaries, wages, bonuses, and other benefits made up N$76.0m or 57.4% of total expenses in FY21. Employees are vital for carrying out the company's strategy to provide superior services to the Namibian market, therefore, the company has a large employee base across various departments. Licence fees paid annually to CRAN totalled 8.50% or N$11.2m of operating expenses. It is worth noting that the company's spectrum licences have an indefinite life, as long as these fees are paid, and the spectrum is utilised. Advertising is an important component in PNH's mission to increase its market penetration, totalling N$7.2m in FY21.

Funding and Asset Base

In June 2021, PNH raised two floating rate notes with a total face value of N$200m. This forms the first tranche of its N$1.0bn domestic medium-term note programme. The first note is a N$175m senior unsecured floating rate note, maturing on 24 June 2024, bearing interest at 3-month Jibar plus 300 basis points. The second note has a face value of N$25m, matures on 18 June 2026, and bears interest at 325 basis points above 3-month Jibar. The weighted cost of this issue currently stands at 6.7%. The medium-term note programme replaced PNH's loan with the Development Bank of Namibia, which had a book value of N$79.6m, priced at 7.75%. Overall, the net issuance was N$120.4m and resulted in a 69.8 basis point decrease in PNH's after-tax cost of debt.

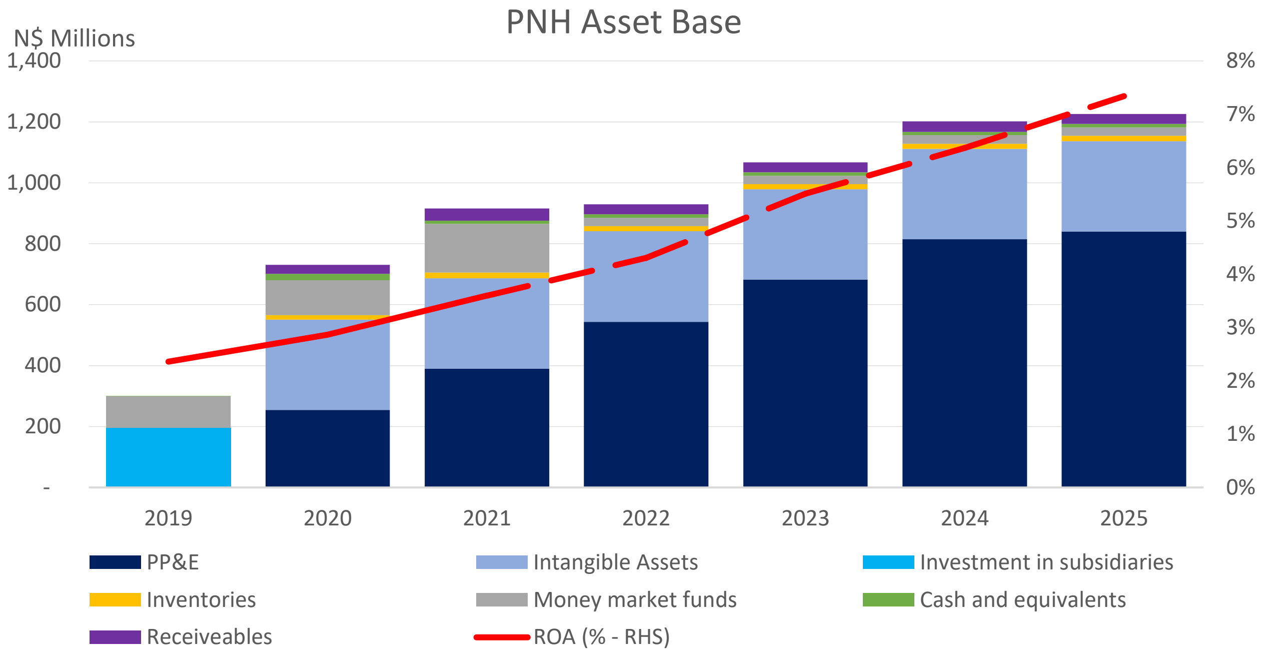


Source: Paratus Namibia Holdings, IJG

Since selling its first stake to Nimbus, PTNA has more than doubled its asset base from N$207.0m in FY17 to N$608.4m in FY21. Investments into property, plant, and equipment (PPE) has been the main contributor to this growth, increasing by 66.3% y/y in FY21, and at a compound rate of 60.5% per year over the last six years. Currently PPE accounts for 55.8% of PTNA's total asset base. Given the capital-intensive nature of the business, as well as management's current infrastructure roll-out strategy, we expect PPE to grow at an average of 24.4% y/y over the next four years.

At the end of FY21, the company had a total of N$132.6m in cash and cash equivalents, of which N$132.0m was invested in money market accounts. This large cash position is largely a result of the company's debt issuance earlier this year and should be invested in the company's capital projects by the end of the next financial year.

Despite the significant growth in the company's balance sheet in FY21, and the inflated cash position, PTNA managed to increase its return on assets (ROA) by 31.2 basis points to 5.9%. Given that the company is still in its growth stage, fixed capital investment will remain aggressive, thus ROA is expected to remain flat in FY22, before increasing to 7.8% in FY23, as PTNA increases its market penetration.



Source: Paratus Namibia Holdings, IJG

There is a clear disparity between PTNA's asset constituents and that of PNH. Firstly, PNH's asset base is considerably larger than that of PTNA, by a total of N$313.5m, with the disparity driven by two factors. Firstly, PNH recognises N$296.5m in intangible assets with the major constituent being its spectrum licence with a book value of N$241.4m, which has an indefinite life. Goodwill and the free right-of-use agreement with BoFiNet, which has a useful life of 18.2 years add a combined value of N$35.4m. PTNA, the operating entity, does not recognise the spectrum licence or the free right-of-use agreement in its goodwill, which totals N$19.3m. Therefore, PTNA's asset base is significantly lower than that of PNH.

Another significant difference is PNH has held a significant cash position over the last 3 financial years since the rights issue in March 2018 averaging a total of N$133.2m a year, which increased to N$170.9m in FY21. Money market investments classified as "investments at fair value" makes up the majority of this position. We view this cash drag on PNH's portfolio as a downside, inflating the balance sheet, while PPE, which comprise the majority of the company's cash-generating assets makes up 42.3% of total assets. Overall, this has resulted in a significantly lower ROA for PNH, at 3.6% in FY21, although it did increase from 2.9% in FY20. Despite this downside, as with PTNA, we expect PNH to draw down this large cash position throughout FY22, which will be invested into capital projects such as its FTTx rollout and data centre, which will increase PPE and provide an improved rate of return on assets We estimate PNH's ROA to increase to 4.3% in FY22, and average 6.4% thereafter.

Outlook

PNH has cemented itself as a serious player in the Namibia telecommunications space, producing a third consecutive year of triple-digit net profit growth. Evidenced by its ever-expanding customer base, the company has disrupted the Namibian market, a trend that is likely to persist going forward.

The PNH's national fibre roll-out continues to gain momentum, which will likely continue to drive the company's performance. We have been somewhat conservative in our forecasts for PNH's fibre rollout, remaining wary of Telecom and MTC's stance on retail fibre rollouts. However, it seems as if MTC is currently focused on its "Spectra" product offering, as well as the rollout of its own fintech, which could result in PNH's future fibre performance benefitting from lack of competition.

Furthermore, management noted that it intends to sign infrastructure sharing agreements, in which it will lease LTE and fibre capacity to smaller players in the market, at an affordable rate. The first agreement of this kind has been signed with MTN, in a national roaming agreement, integrating both companies' LTE networks across the country. Given that the Namibian incumbents have been largely uncompetitive in terms of infrastructure sharing, PNH will likely attract new market entrants in the future, which will indirectly increase its customer base.

To the downside, we view the large cash position that resulted from the conclusion of the rights issue in 2019 as a drag on the balance sheet, which has resulted in sub-optimal leverage levels. The cash position as a proportion of total assets grew from 14.2% in FY20 to 21.8% in FY21, suppressing the company's return potential. This has ultimately resulted in a very low return on shareholder's equity in the past. Furthermore, PNH paid a dividend of 20 cents per share in FY21, which equates to a pay-out ratio of 33.4%. Management admitted that the rationale behind the dividend is to cater for the demand for dividends amongst Namibian retail investors. The sub-optimal ROE, combined with a relatively high pay-out ratio for a company in the growth stage of its lifecycle has resulted in a relatively low sustainable growth rate for PNH. However, given the company's capital-intensive strategy, the cash position should be substantially smaller by the end of FY22, which could unlock greater shareholder value if invested successfully.

Valuation

We make use of a sum of the parts free cash flow to equity model to value PNH. Given that PNH is still in its growth phase, fixed capital investment is expected to accelerate to N$350.8m by FY23 for the group. Fixed capital investment is forecast to average N$204.2m per annum over the forecast horizon. EBITDA has been forecast to increase from N$94.5m in FY21 to N$120.2m in FY22 and N$392.3m in our terminal year of FY30, due to a strong national fibre roll-out as well as the introduction of the data centre in the third quarter of 2022. We have used a cost of equity of 17.6% and a long-term ROE of 13.1% in our valuation.

	Value (N$'000)	Price per Share	Price to Earnings	Forward PE	Price to Book	Forward PB	Dividend Yield	Forward Dividend Yield
FCFE	650,956	13.26	21.32	16.29	1.14	1.15	1.6%	2.1%

Source: IJG

Based on the table above, we derive a **target price of N$c1326** per share. Coupled with an expected full-year dividend of 26cps, we derive an **expected total return of 6.1%.** Despite the relatively low return, there is room for further upside if the company can successfully execute its national fibre roll-out. We initiate coverage on PNH with a **BUY** recommendation.

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