IFRS 16 applied to MTN Group

Pre capital markets day workshop to sell-side analysts
24 May 2019

Hosted by Ralph Mupita Group CFO

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Agenda

Time	Presentation	Key speakers
09:00am	Welcome and Introduction	Ralph Mupita – MTN Group CFO
09:15am	Application of IFRS 16 in MTN Group	Sugen Perumal – MTN Group, Executive: Finance operations Ben Samwell – MTN Group, GM: Finance operations Lauren Gray – MTN Group, Manager: Technical accounting
11:00am	Nigeria deep dive	Adekunle Awobodu – MTN Nigeria CFO
11:30am	Q&A	
	Closing	Ralph Mupita – MTN Group CFO

Presenters

MTN Group
CFO
Ralph Mupita

BSc Engineering Hons (University of Cape Town), MBA (University of Cape Town), GMP (Harvard Business School)

Ralph is MTN's Group Chief Financial Officer. Prior to joining MTN in April 2017, Ralph was the Chief Executive of Old Mutual Emerging Markets. He has extensive experience in financial services, operating in emerging markets such as Africa, Latin America and Asia.

MTN Nigeria
CFO
Adekunle Awobodu

BSc Finance and Banking (University of Lagos), MSc Finance (University of Leicester), CPA, CIA, CMA, ACCA

Kunle is MTN Nigeria Chief Financial Officer and prior this, he was the Chief Financial Officer of MTN Irancell. He has over 22 years of professional experience and international exposure in finance, successfully leading financial system change management projects in two countries. He is adept at compliance with accounting standards and possess extensive knowledge of financial accounting, internal control processes and system effectiveness

Executive
Group Finance
Operations
Sugentharen Perumal

BCom Accounting Hons (University of Natal), CA (SA)

Sugen is MTN's Group Finance Operations Executive. Prior to joining MTN in 2014, Sugen was an audit director at SizweNtsalubaGobodo and initially joined MTN as the Chief Financial Officer in MTN Irancell. He has significant experience in leading the strategic and operational planning and management of various enterprises

GM
Financial Accounting
Ben Samwell

BCom Accounting Hons, MCom Enterprise Management (University of Johannesburg), CA (SA)

Ben is the General Manager Financial Accounting. Prior to joining MTN in 2011, Ben was the head of external financial reporting at Standard Bank Group. Ben has been leading IFRS implementations and the preparation of IFRS financial statements since IFRS adoption in South Africa in 2005. Ben is a member of SAICA's Accounting Practices Committee as well as the JSE's Financial Reporting Investigation Panel

Manager
Technical Accounting
Lauren Gray

BCom Accounting Hons (Nelson Mandela Metropolitan University), CA (SA)

Lauren is a manager in the MTN Group technical accounting division. Prior to joining MTN in 2017, Lauren was a senior manager in KPMG's Reporting Accounting and Assurance Solutions department. She has extensive experience in IFRS implementations, financial statement preparation and review and providing technical accounting advice

IFRS 16 – A new standard for lease contracts

Transition

Application date: 1 January 2019

Applied retrospectively, with no prior period restatement

IAS 17 pro forma information will be provided for comparative purposes

No change on lessor accounting

Regulator objectives

Improved transparency and comparability between companies

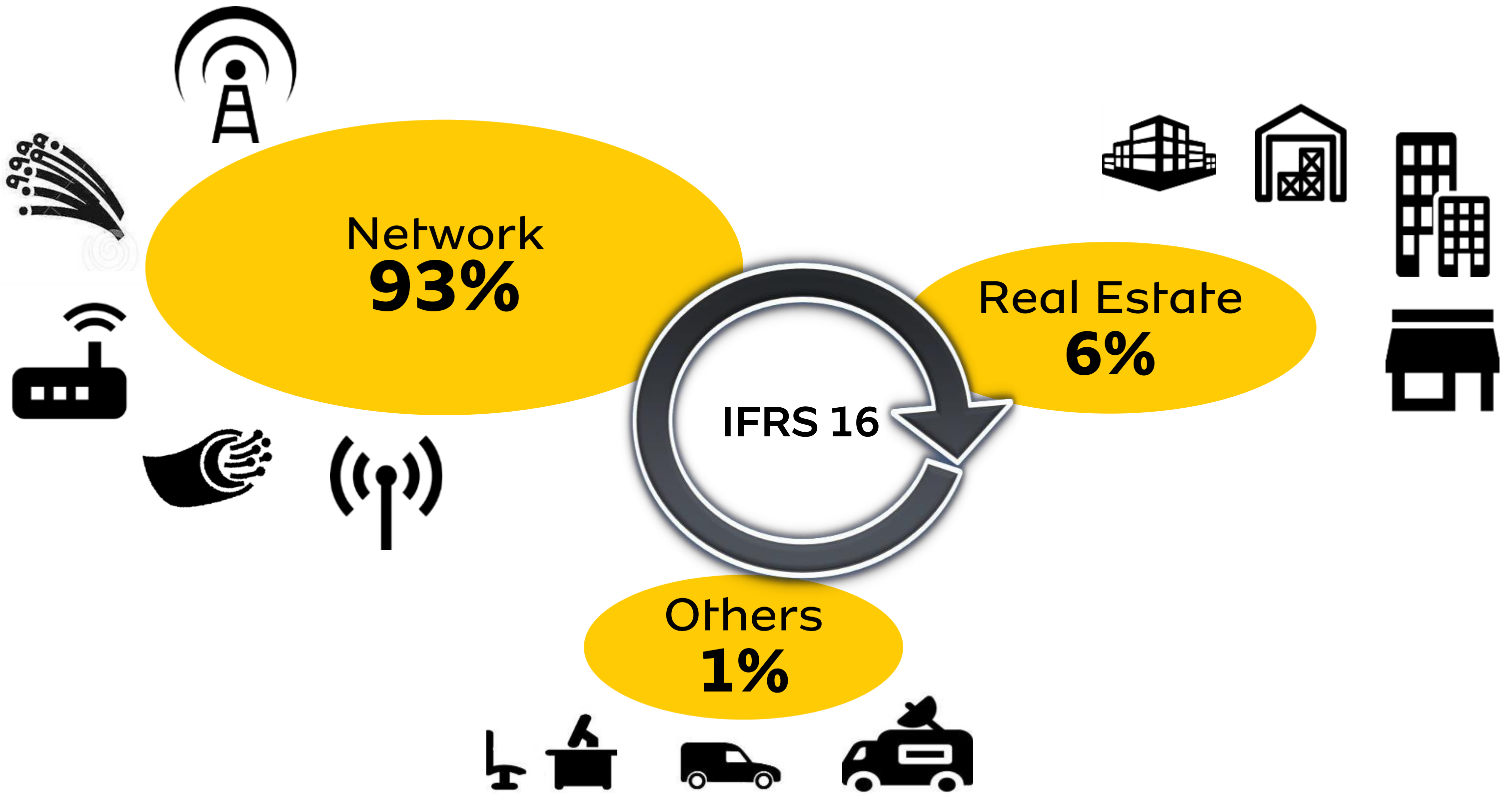
Integrating all the lease commitments on the statement of financial position (SOFP)

Major areas of impact on MTN

- Tower leases
- Network sites

A change applied to several categories of assets

Main lease activities at MTN

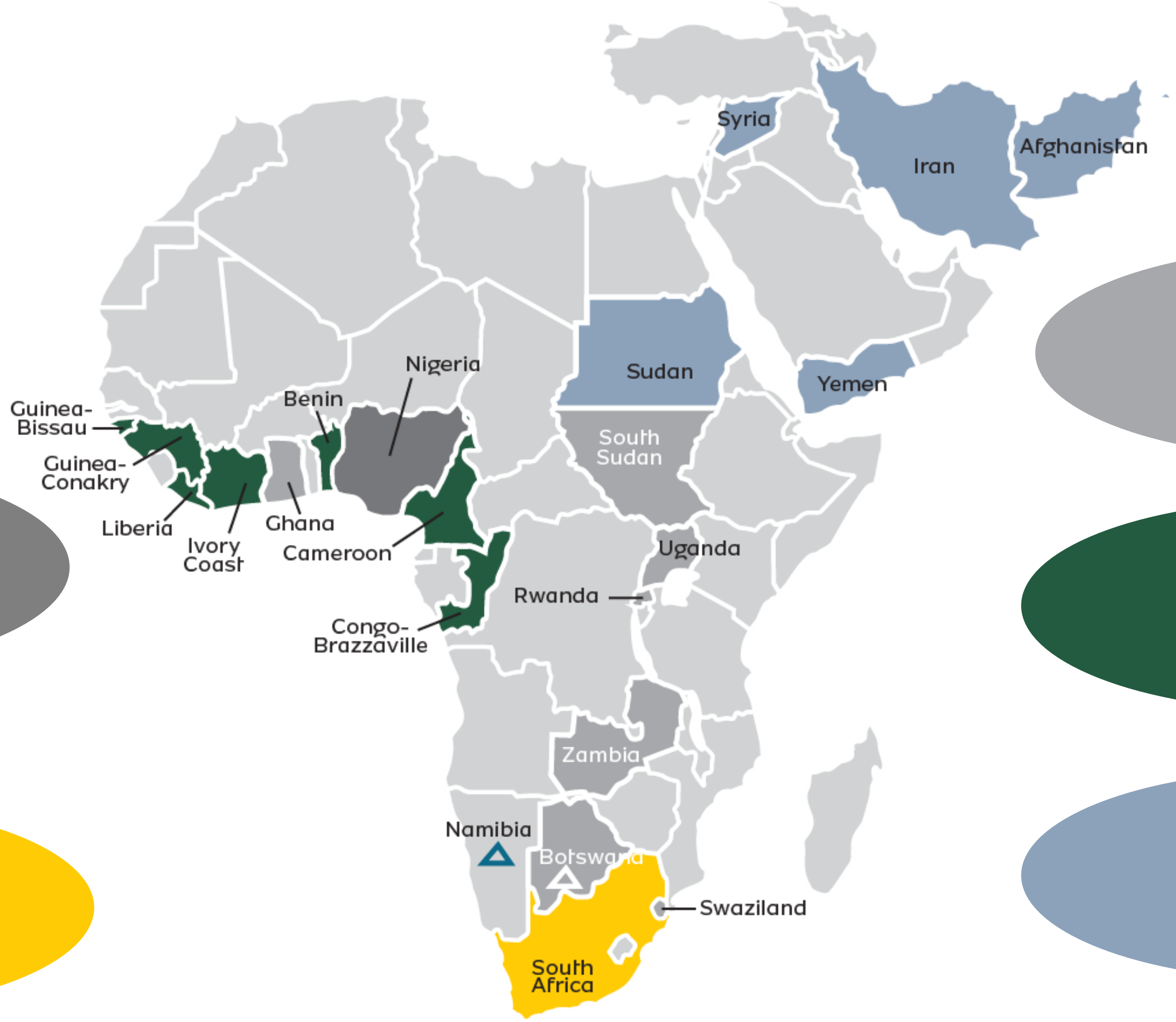


IFRS 16 Scope

Excluded from scope:
- Low value assets (<US$5 000 in value)
- Short-term leases

ROU assets geographically

Based on right of use (ROU) assets as at 1 January 2019



Nigeria
41% - 45%

South Africa
24% - 28%

SEAGHA
16% - 20%

WECA
8% - 12%

MENA
1% - 5%

Accounting concept : a single lease model

This new standard changes the accounting for leases in the lessee's financial statements by replacing the current dual accounting model (finance lease agreements on the statement of financial position and operating leases off-balance sheet) by a single model, on balance sheet accounting, for both finance and operating leases

Finance leases :
No change

Operating leases (lease component) :
change*

Operating leases (non-lease component) :
No change

Typical example of components in a lease contract.
What is **in vs out** IFRS 16:

Base transmission site

- Tower space – in scope
- Maintenance of equipment – out of scope
- Power supply (via generators) – out of scope

Non-lease components are items in a contract that do not give the right to use an identified asset for a period of time.

* Excluding short-term leases and leases of low value assets

Impact on statement of financial position (SOFP)

Before*

No asset or liability recognised

Off balance sheet commitments only for operating lease

Now*

Accounting of a ROU asset

Recognition of a liability for the NPV of the future lease payments

*Finance leases : no change

Illustrative example:

MTN signed on 1 January 2019 a commercial lease to rent towers for a period of 10 years for an annual rent of R500k (year end annual payment). The annual payment includes R100k for the maintenance services of the generators which has been identified as a non-lease component. The applicable interest rate is 12%.

IAS 17

Nothing on the statement of financial position
Undiscounted amount disclosed in the operating lease commitment note

IFRS 16

One single lease accounting model : Recognition of a ROU asset and lease liability (representing at contract inception the present value of future lease payments)

Assets	2019 R'000
Goodwill	
Other intangible assets	
Property, plant and equipment	
ROU assets	2 260
Associates and joint ventures	
…	
Total non-current assets	
Inventories	
Trade receivables	
…	
Total current assets	
Total assets	**2 260**

Liabilities	2019 R'000
Share capital	
…	
Total equity	
Non-current financial liabilities	
Non-current lease liabilities	2 131
Non-current derivative liabilities	
…	
Total non-current liabilities	
Current financial liabilities	
Current lease liabilities	129
…	
Total current liabilities	
Total equity and liabilities	**2 260**

The lease asset and liability calculated and accounted as of January 1st 2019 will be :

$$\text{R2 260k} = \sum_{n=1}^{10} \frac{(400)}{(1+12\%)^n}$$

Impact on income statement

Before*

Operating expense

Above EBITDA

Now*

ROU asset depreciation & interest expense below EBITDA

Additional foreign exchange gains/losses

*Finance leases : no change

Illustrative example:

MTN signed on 1 January 2019 a commercial lease to rent towers for a period of 10 years for an annual rent of R500k (year end annual payment). The annual payment includes R100k for the maintenance services of the generators which has been identified as a non-lease component. The applicable interest rate is 12%.

IAS 17

Operating lease expenses are booked above EBITDA

IFRS 16

Opex will be replaced by a depreciation of the ROU asset and an interest expense for the actualisation impact

	IFRS 16 2019 R'000	IAS 17 2019 R'000
Revenue		
Operating lease expense		(500)
Other operating income		
Other operating expense	(100)	
Labour expenses		
Operating taxes and levies		
EBITDA		
Depreciation and amortisation	(226)	
....		
Operating profit		
Finance costs		
Lease interest expense	(271)	
....		
Profit before tax	**(597)**	**(500)**
Income tax	167	140
Profit after tax	**(430)**	**(360)**

- **Depreciation of the ROU asset R226k: R2,260k / 10 years**
- **Interest expense on the first year : R271k: R2 260k * 12% (this interest expense will decrease over the years as the capital portion is repaid)**

Net decrease to profit after tax from applying IFRS 16: R70k

Total impact on cash flows : None

Before / Now

No change in cash flows

Change in classification of cash flows

Illustrative example:
MTN signed on 1 January 2019 a commercial lease to rent towers for a period of 10 years for an annual rent of R500k (year end annual payment). The annual payment includes R100k for the maintenance services of the generators which has been identified as a non-lease component. The applicable interest rate is 12%.

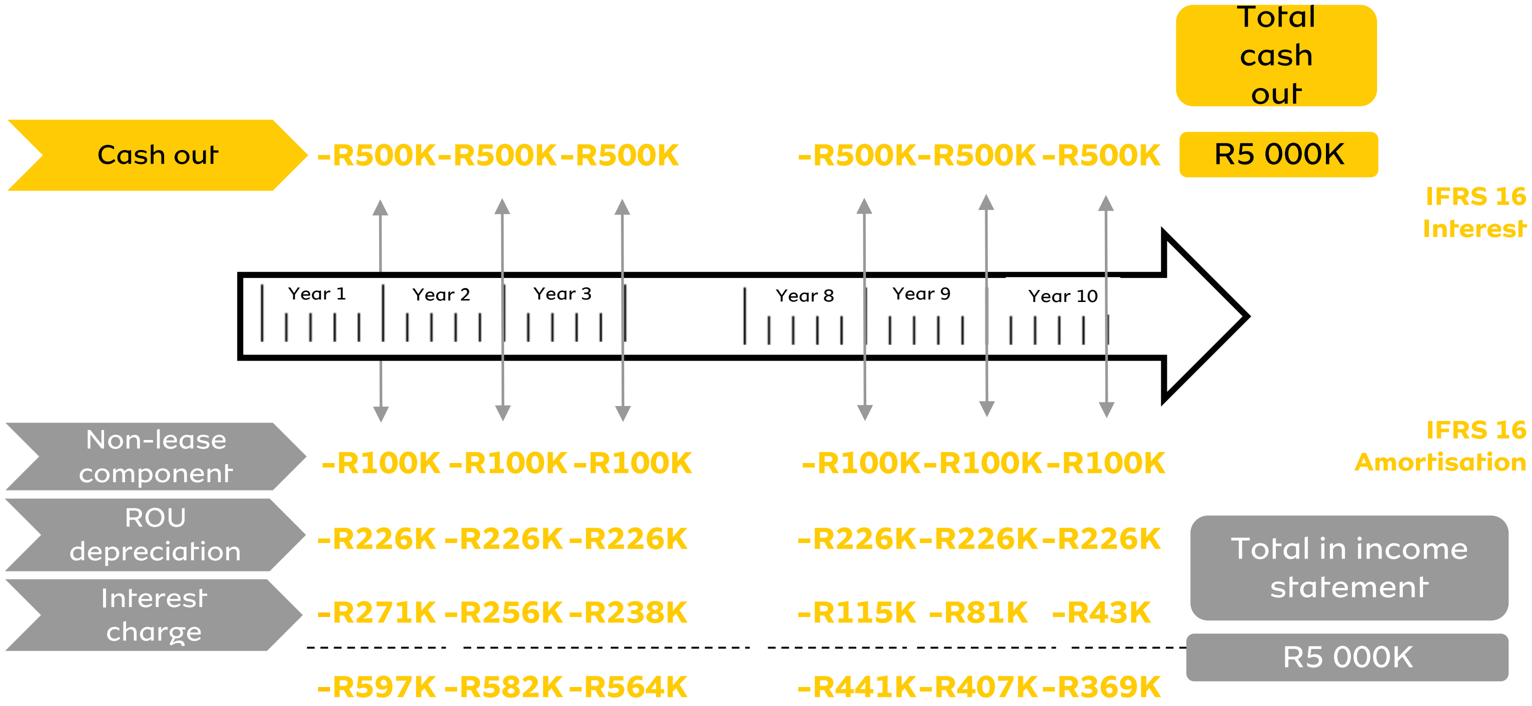
Total cash flows are the same under IFRS 16 as under IAS 17. However, operating lease payments were disclosed as operating cash flows. On adoption of IFRS 16, these cash flows will be split between operating cash flows for interest paid and financing cash flows for the repayment of the lease liability

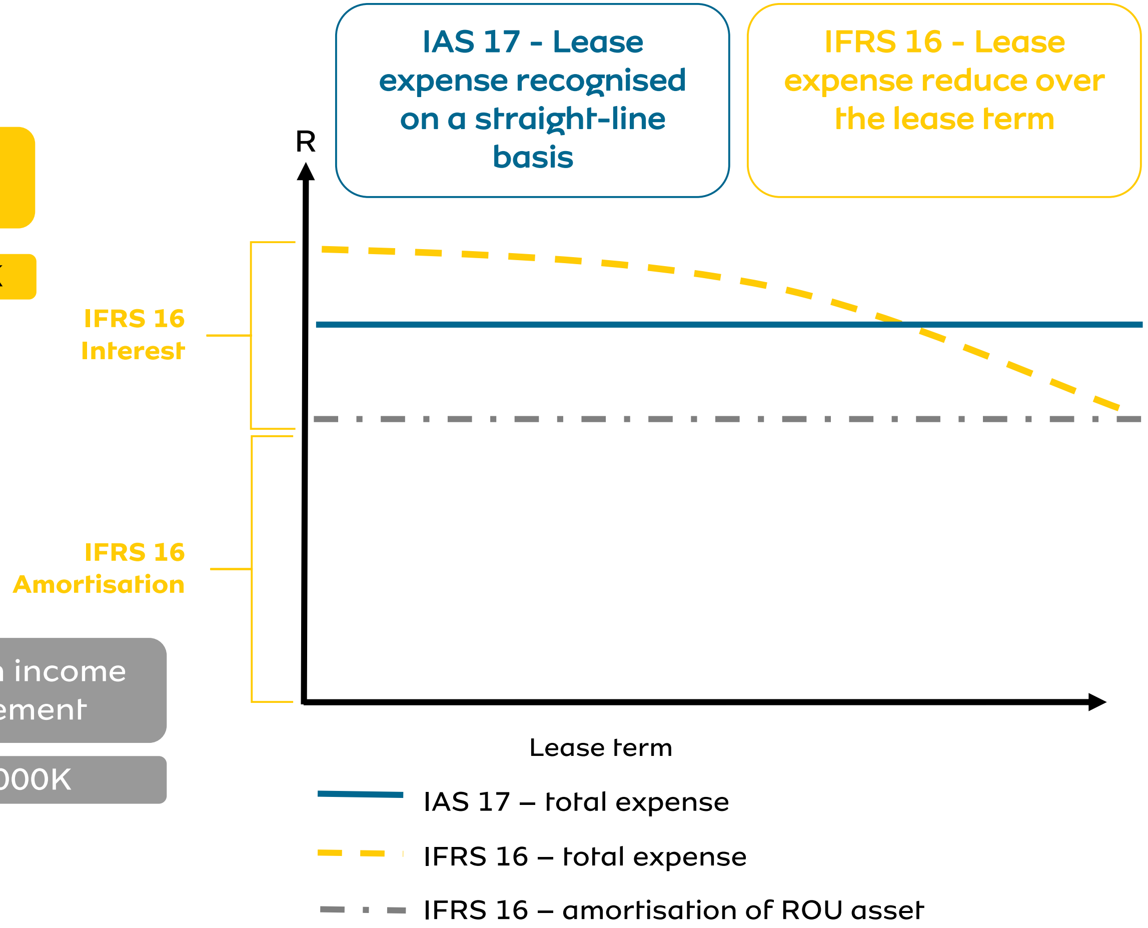
	IFRS 16 2019 R'000	IAS 17 2019 R'000
Cash flows from operating activities		
Cash generated from operations	(100)	(500)
….		
Interest received		
Interest paid	(271)	
Income tax paid		
Net cash generated from operating activities	(371)	(500)
Cash flows from financing activities		
….		
Proceeds from borrowings		
Repayment of borrowings	(129)	
Other financing activities		
Net cash used in financing activities	(129)	
Net cash and cash equivalents at end of the year		

Disconnect between cash flows and income statement

Over the contract period, the cumulated impact on profit before tax is the same under both standards.

A temporary difference will come from the decreasing interest expenses





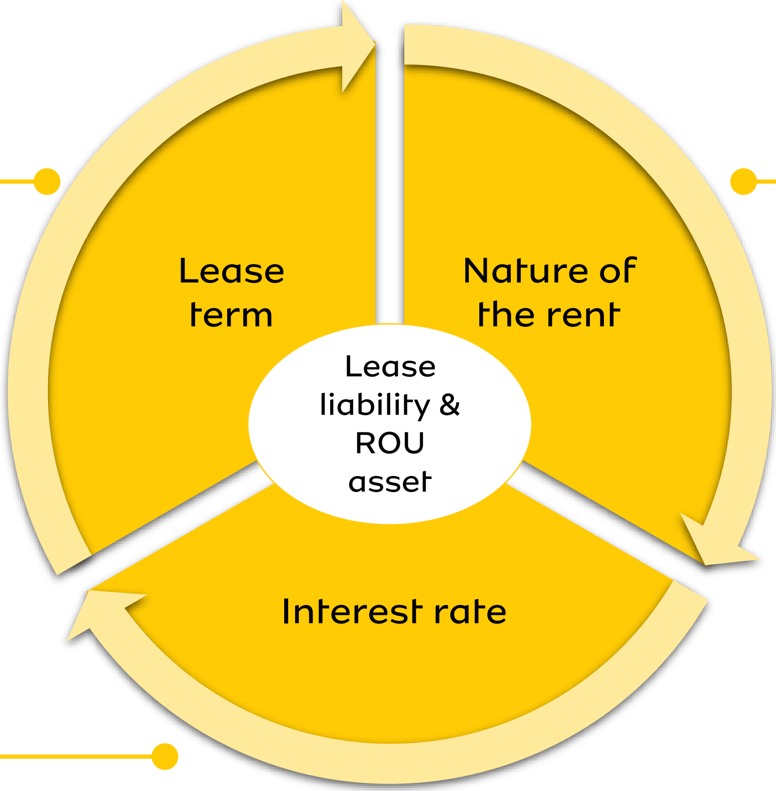
In FY 19, profit before tax is lower under IFRS 16 than under IAS 17. Profit before tax will be higher in later years, with an equal impact over the duration of the lease.

The valuation of the ROU asset and the lease liability

Lease liability and ROU asset will depend on 3 estimated inputs:

- The lease term is based on whether the lessee is reasonably certain to exercise an option to extend or terminate a lease
- The longer the lease term, the larger the ROU asset and the lease liability

Definition of lease perimeter



The interest rate is the incremental borrowing rate of the contracting entity:

- The higher the rate, the lower the ROU asset and the lease liability
- The higher the rate, the higher the interest charge

- The variable part of the lease payments is excluded from the lease liability calculation
- An option offered by the standard is to separate the lease components and services in the lease payment, which reduces the lease liability and the ROU asset. MTN has elected to only include lease components in the ROU asset and lease liability

Foreign currency exposure
The lease liability is subject to foreign exchange gains and losses due to lease contracts denominated in foreign currency

...thus leading to potential differences with our peers (see example in next slide)

Assumptions have a direct impact on lease valuation

The assessment of whether renewal options will be exercised directly impact the lease valuation.
Consider a lease with an annual payment of R3m

No renewal options considered

Contract duration of 3 years with an interest rate of 12%

2 renewal periods of 3 years each included

Contract duration of 9 years with an interest rate of 12%

SOFP

No renewal options considered

At inception

Capex every 3 years

Assets	Liabilities
R 7,2 m	R 7,2 m

2 renewal periods of 3 years each included

At inception

Capex every 9 years

Assets	Liabilities
R 16,0 m	R 16,0 m

Income statement

No renewal options considered

	Y1	Y2	Y3	Total
Lease interest expense	R 0,9 m	R 0,6 m	R 0,3 m	R 1,8 m
ROU Depreciation	R 2,4 m	R 2,4 m	R 2,4 m	R 7,2 m
Total	R 3,3 m	R 3,0 m	R 2,7 m	R 9,0 m

2 renewal periods of 3 years each included

	Y1	Y4	Y9	Total
Lease interest expense	R 1,9 m	R 1,5 m	R 0,3 m	R 11,0 m
ROU Depreciation	R 1,8 m	R 1,8 m	R 1,8 m	R 16,0 m
Total	R 3,7 m	R 3,3 m	R 2,1 m	R 27,0 m

ROU Depreciation | Lease interest expense | Total

Statement of financial position impact

31 Dec 2018

IAS 17

- Operating leases disclosed as off-balance sheet commitments

Minimum lease payments under non-cancellable operating lease arrangements = R129 billion

− Service component excluded

− Discounted

+ Cancellable leases included

+ Expected lease renewals

31 March 2019

IFRS 16

- All leases on the SOFP
- ROU assets and lease liabilities

	Unaudited 31 March 2019 Rbn
Assets	
ROU assets	44 - 48
Total assets	44 - 48
Liabilities	
Non-current lease liabilities	41,5 – 43,5
Current lease liabilities	2,5 – 4,5
Total equity and liabilities	44 - 48

Income statement Q1 2019

2018 – IAS 17	
Operating lease expense	R13,8bn

+ Lease expense saving, service component remains in opex
- Depreciation and interest expense

Q1 2019 – Impact of IFRS 16	Unaudited
Increase in MTN SA EBITDA margin	3.5%
Increase in MTN Nigeria EBITDA margin	9.1%
Weighted average depreciation period for ROU assets	6 – 10 years
Weighted average incremental borrowing rate of lease liability	10% - 15%

2019 is a transition year

No restatement of 2018

2019 IAS 17 pro forma figures will be provided for comparative purposes

Comparability to 2018 reported numbers

	2019 reported IFRS 16	2019 pro forma IAS 17	2018 Reported IAS 17
EBITDA	x	√	
Earnings	x	√	
AFCF (EBITDA less Capex)	x	√	

Loan covenants and ratings agencies

Financial institutions have confirmed that loan covenants for MTN will currently continue to be measured on an IAS 17 basis for existing facilities and facilities under negotiation

Under the terms of the major borrowing facilities, the group is required to comply with financial covenants relating to net debt: EBITDA and net interest: EBITDA

Debt cover

Net debt: EBITDA

- Net debt (excluding lease liabilities under IFRS 16)
- EBITDA (under IAS 17) 2019 pro forma

Interest cover

EBITDA: Net interest

- EBITDA (under IAS 17) 2019 pro forma
- Net interest (excluding lease liability interest expense under IFRS 16)

Ratings agencies previously adjusted MTN's metrics for operating lease commitments which were not recognised on the balance sheet when rating the Group. After the implementation of IFRS 16, ratings agencies will no longer have to adjust for these amounts as the impact of IFRS 16 will be included in MTN's metrics

MTN Nigeria - IFRS 16 Impact

- Major lease arrangements relates to the use of certain space on telecommunications towers owned by tower providers
- Main counterparties are INT Towers, IHS, Helios and ATC
- Other lease contracts are for equipment leases (printer/scanners/copiers) & property leases for office and residential properties
- Lease payments have been split into lease (47%) and non-lease components (53%)
- The tower leases have annual CPI escalation clauses
- The tower lease contracts have a periodic exchange rate reset
- Lease periods range between 3 – 11 years
- Approximately 69% of the lease liability is denominated in US$ (indexed to the CBN rates) & will give rise to foreign exchange gains and losses
- Incremental borrowing rates (22,7% - NGN, 9% - US$) used for the discounting of the lease liability on 1 January 2019

MTN Nigeria – Statement of financial position

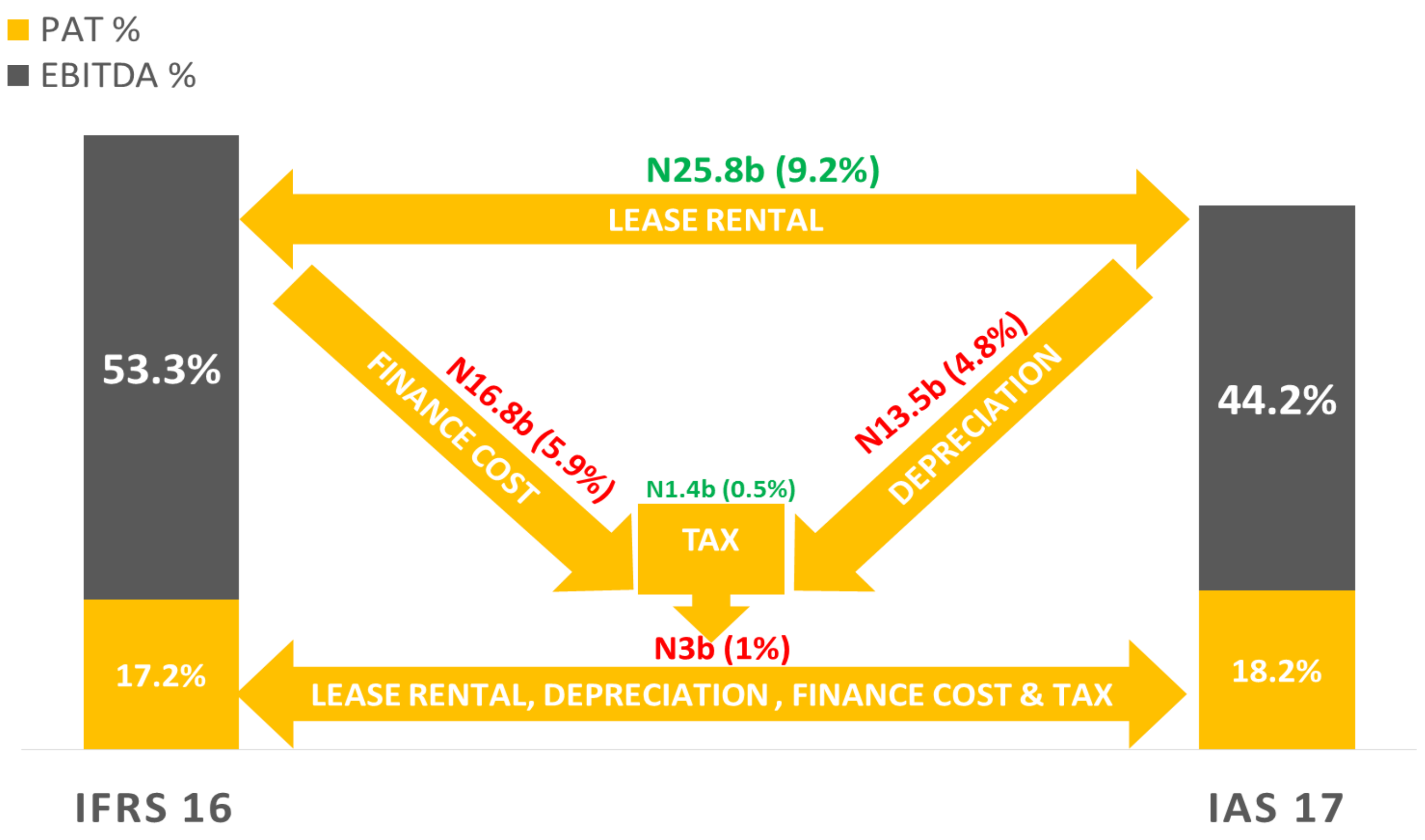
	Unaudited 31 March 2019 N'bn	Unaudited 31 March 2019 R'bn
Assets		
ROU assets*	507,1	20,3
Total assets	**507,1**	**20,3**
Liabilities		
Non-current lease liabilities	474,0	19,0
Current lease liabilities	29,2	1,2
Total equity and liabilities	**503,2**	**20,2**

IFRS 16
- All leases on the SOFP
- ROU assets and lease liabilities

*ROU assets includes reclassification of prepayments relating to property and BTS leases

MTN Nigeria - IFRS 16 recon to IAS 17 [EBITDA to PAT] - 31 March 2019

Total operating costs declined by N25.8 billion, improving EBITDA by same amount. On the other hand, depreciation and finance costs increased by N13.5 billion and N16.8 billion, following the adoption of IFRS 16, which depreciates the ROU asset as well as implicit finance cost charge on the ROU liability



Financial definitions

	Definition	Why?	Where to find?
Capex	Capital expenditure comprises of additions to property, plant and equipment; ROU assets and software included in intangible assets	ROU assets are similar to property, plant and equipment in nature and therefore, should be included in capex	**Financial statements:** Operating segments note
Capex intensity	Capex excluding ROU asset additions/ Revenue	MTN has defined capex intensity to be based on capex excluding ROU asset additions. Additions to ROU assets are recognised when management is reasonably certain that renewal options will be exercised. Including ROU additions in capex would result is significant volatility in capex on an annual basis that is not reflective of the annual investment in infrastructure	**Financial statements:** *Capex:* Operating segments note *ROU additions:* ROU asset note *Revenue:* Group income statement
Holdco leverage	Net debt*/ (MTN SA EBITDA* + dividends and management fees received by MTN Holdings) *IAS 17 basis	Financial institutions have confirmed that loan covenants will continue to be measured on an IAS 17 basis	**Financial statements:** Group statement of financial position *Net debt* is defined as borrowings and bank overdrafts less cash and cash equivalents, restricted cash and current investments (excluding investments in Insurance cell captives) **Results presentation** MTN SA EBITDA (IAS 17)
Adjusted ROE	Adjusted return on equity is based on adjusted headline earnings/equity attributable to equity holders of the company	MTN's previously issued medium-term guidance includes the impact of IFRS 16	**Results presentation:** Adjusted headline earnings **Financial statements:** Group statement of financial position

IFRS 16 timelines

9 May 2019

Q1 2019 results release under IFRS 16

First quarterly results under IFRS 16, with no Q1 2018 restated accounts but IAS 17 Q1 2019 pro forma information

Results unaudited

24 May 2019

Analyst presentation

IFRS 16 impacts

8 August 2019

Interim results

2019 interim results under IFRS 16 reviewed. Including H1 2019 IAS 17 pro forma financial information reviewed

March 2020

Year end results

2019 full year results under IFRS – audited

2019 full year IAS 17 pro forma financial info - audited

Enhanced medium-term guidance – IFRS 16 impact

Service revenue	Double digit growth	No impact
EBITDA margins	Improve margin	No impact- remains relevant
Group capex intensity	Reduce capex intensity post IFRS 16	No impact - capex intensity definition to exclude IFRS 16 impact
Holdco leverage	Reduce adjusted holdco leverage	No impact – covenants to exclude IFRS 16 impact as agreed with banks
Adjusted ROE	Improve adjusted ROE to >20%	Target set based on IFRS 16

Q&A

everywhere you go