

02 Mar 2020 | Affirmation

## Fitch Affirms Batelco at 'BB-'; Outlook Stable

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Fitch Ratings-London-02 March 2020:

Fitch Ratings has affirmed Bahrain Telecommunications Company's (Batelco) 'BB-' Long-Term Issuer Default Rating (IDR). The Outlook is Stable. Fitch has also affirmed the unsecured rating of Batelco International Finance No. 1 Limited at 'BB-'.

Batelco's 'BB-' IDR is constrained by Bahrain's 'BB-' sovereign rating as the Bahraini government owns 77% of the company and exerts strong control over it. Its standalone credit profile (SCP) is 'bb+', reflecting the company's leading domestic position in a competitive Bahraini market as well as the political and economic risks of the countries in which Batelco has international operations.

The regulatory-driven separation of Batelco's domestic fixed line network into two separate entities, one focusing on retail services, with the other concentrating on wholesale services, may put some pressure on retail broadband prices in the short- to medium-term. Batelco retains sufficient financial flexibility to manage these pressures should they occur.

### Key Rating Drivers

**Stable Underlying FYE19 Performance:** Batelco reported revenue growth (adjusted for the sale of Qualitynet) of 2% in FY19 and an EBITDA (adjusted for voluntary retirement payments, right of use asset depreciation and interest on lease liabilities) of BHD143 million, broadly flat compared with FY18. Batelco was able to offset revenue pressures in its subsidiaries, in Umniah and Sure Group, with growth in its domestic market and efficiency improvements across its operating subsidiaries.

**Domestic Market Key:** Bahrain is a key market for Batelco, accounting for 44.5% of total revenue in FY19. Its operating position in its domestic market is improving following the deployment of its fibre network. However, competition in the mobile segment remains intense as number-three mobile operator STC Bahrain tries to build revenue market share. Pursuing a convergence strategy, focused on a high-quality fixed and mobile infrastructure, is allowing Batelco to retain its strong market shares in the mid- to high-value consumer segment and the business segment.

**Bahrain Network Separation:** The separation of Batelco's network into two separate legal entities is a regulatory requirement. The separation (similar to BT Group in the UK) creates a separate fixed-line entity that has the obligation to serve both internal and external wholesale customers

equally without discrimination. The separation may create greater competitive pressure on retail broadband prices in the short- to medium-term. Should these pressures materialise, we do not expect them to have a significant impact on the rating given the level of wholesale prices, potential for growth in the wholesale division and the company's moderate leverage.

**Diverse International Operations:** Batelco's largest international operations are in the Maldives, Jordan and the Channel Islands. The Maldives business (of which Batelco owns 52%) generates healthy operating free cash flow (FCF), while reported revenue from the Channels Islands (and the Isle of Man) is exposed to sterling volatility. Jordan (22% of Batelco's consolidated FY19 revenue) has been a greater challenge due to its weak macroeconomic trends and intense competition. Batelco's capex in the market is expected to moderate over the coming years.

**Low Leverage:** Fitch views Batelco's financial profile as strong, underpinned by our expectation of a conservative leverage profile, and sound liquidity over the medium term. We expect funds from operations (FFO) adjusted net leverage to stabilise at around 1.5x over the medium term (versus 1.6x at end-2019), a level that is low for the 'BB-' rating.

**Strong State Influence:** Batelco is 77% directly and indirectly owned by the government of Bahrain. The Bahraini government is invested in Batelco via Bahrain Mumtalakat Holding Company (37%; BB-/Stable), Amber Holding (20%) and the Social Insurance Organisation (SIO; 20%). Bahrain-based diversified investment holding company, Mumtalakat, is 100%-owned by the Bahrain government and is the government's investment arm. Through these entities, the Bahraini government exerts strong control over Batelco, and is represented by six of 10 directors on the company's board: three from Mumtalakat (including the Chairman); one from SIO; and two from Amber Holding.

**GRE Criteria Application:** Batelco's IDR is constrained by the sovereign's based on Fitch's Government-Related Entities (GRE) Rating Criteria and Parent and Subsidiary Rating Linkage Criteria. We assess the company's SCP at 'bb+'. Under the GRE rating criteria we assess status, ownership and control; support track record and expectations as well as financial implications of a GRE default as strong. We view socio-political impact of a GRE default as moderate.

#### Derivation Summary

The SCP of 'bb+' of Batelco reflects its incumbent position in its domestic market, low leverage as well as risks to its international operations. We do not envisage Batelco being rated above the sovereign rating, especially given the government's significant shareholding in the company and strong ties between the company and the state. Oman Telecommunications Company S.A.O.G. (Omantel; BB+/Stable) is of similar size, with its rating similarly capped by the sovereign rating. Other telcos in the region such as Emirates Telecommunications Group Company PJSC (Etisalat;

A+/Stable) and Ooredoo Q.P.S.C. (A-/Stable) are much larger and can rely on domestic markets that are less competitive, as well as on government support.

## Key Assumptions

### Fitch's Key Assumptions Within Our Rating Case for the Issuer

- Reported revenue growth of 1%-2% in 2020, followed by about 1% per year until 2022
- EBITDA margin (pre-IFRS 16) slightly over 35% in 2020 and gradually increasing to 37% by 2022
- Stable right-of-use asset depreciation and interest on lease liabilities at BHD9.7 million
- Capex (excluding spectrum) of around 13% in 2020 and remaining broadly stable until 2022
- Broadly stable dividend per share till 2022

## RATING SENSITIVITIES

### Batelco

#### Developments That May, Individually or Collectively, Lead to Negative Rating Action

- Negative rating action on the sovereign
- Pressure on FCF driven by EBITDA margin erosion, consistently higher capex and shareholder distributions, or significant underperformance in the core domestic market and at other key subsidiaries may be negative for the SCP but not necessarily the IDR
- FFO net leverage remaining above 4.5x with failure to deleverage below such a threshold within the next 18 months may pressure the SCP but not necessarily the IDR

#### Developments That May, Individually or Collectively, Lead to Positive Rating Action

- An upgrade of the sovereign rating, or a change of the Outlook to Positive, with continued support from the government of Bahrain, without a weakening in the linkage with the sovereign.

### Bahrain Sovereign

The main factors that could lead to positive rating action are:

- Confidence in a narrowing of the budget deficit, consistent with placing government debt-to-GDP

on a downward path.

- A broadly accepted political solution to domestic political tensions.

The main factors that could lead to negative rating action are:

-Further significant deterioration of public debt dynamics, or increased financing constraints including a weakening of financial support from GCC partners.

- Severe deterioration of the domestic security environment.

#### Liquidity and Debt Structure

Adequate Liquidity: At FYE19 Batelco had BHD175.5 million of cash on its balance sheet, and BHD34.5 million of Bahrain sovereign bonds with maturities dates ranging from 2020 to 2023. Batelco has a USD473 million senior unsecured bond due May 2020. We see low refinancing risk for the partial refinancing of the maturing bond given the company's strong credit profile and strong linkage with the state.

#### Public Ratings with Credit Linkage to other ratings

The ratings are directly linked to the Sovereign Rating

#### ESG Considerations

ESG issues are credit neutral or have only a minimal credit impact on the entity(ies), either due to their nature or the way in which they are being managed by the entity(ies). For more information on Fitch's ESG Relevance Scores, visit [www.fitchratings.com/esg](http://www.fitchratings.com/esg).

Bahrain Telecommunications Company; Long Term Issuer Default Rating; Affirmed; BB-; RO:Sta  
Batelco International Finance No. 1 Limited

----senior unsecured; Long Term Rating; Affirmed; BB-

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### **Applicable Criteria**

[Corporate Rating Criteria \(pub. 19 Feb 2019\)](#)

[Corporates Notching and Recovery Ratings Criteria \(pub. 14 Oct 2019\)](#)

[Government-Related Entities Rating Criteria \(pub. 13 Nov 2019\)](#)

[Parent and Subsidiary Rating Linkage \(pub. 27 Sep 2019\)](#)

### **Additional Disclosures**

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