



TENIZ CAPITAL
INVESTMENT BANKING



ҚАЗАҚТЕЛЕКОМ

In anticipation of transformation of
Kazakhtelecom JSC:

Ecosystem of mobile provider and bank,
partnership with QazPost JSC, and
development of data centers and
Sovereign Artificial Intelligence



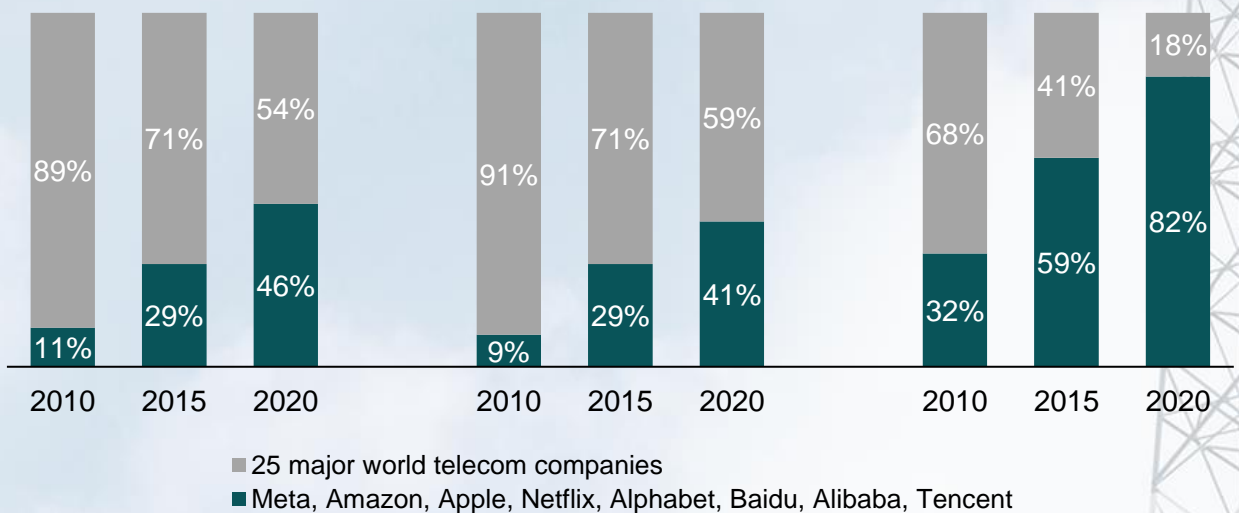
In this report, Teniz Capital Investment Banking shares its assumptions regarding transformation of Kazakhtelecom JSC, which will permit to increase the competitiveness and profitability of the company in conditions of the permanently changing telecommunication market.

Our assumptions are based on the development of a super-application for the ecosystem of digital services, expansion of business by introduction of marketplaces and partnership with QazPost JSC, streaming opportunities, and also investments in data centers and creation of Sovereign Artificial Intelligence. Special attention is drawn to necessity of diversification of activity and search for new sources of income, taking into account the slowing down of growth in traditional segments of telecommunications. This strategy will permit Kazakhtelecom company not only to strengthen its positions in the market, but also to hold a significant share in new and quickly growing sectors providing stable development of the company in the future.



Despite of huge capital investments during the last decade in the race for new technologies, the main business of providers becomes more and more commoditized and their growth becomes slower. A major part of the profit in technological sector was received by so called advanced players – by those who produce mobile phones, develop applications or create digital infrastructure. A big gap between communications providers and big companies providing digital services (for example, Netflix, Amazon, Meta, and Apple) is observed in such indices as proceeds, return on sales, and market capitalization (picture 1). It should be marked that this is a world trend and each big telecom provider tries to diversify its activity.

Telecom and technological companies



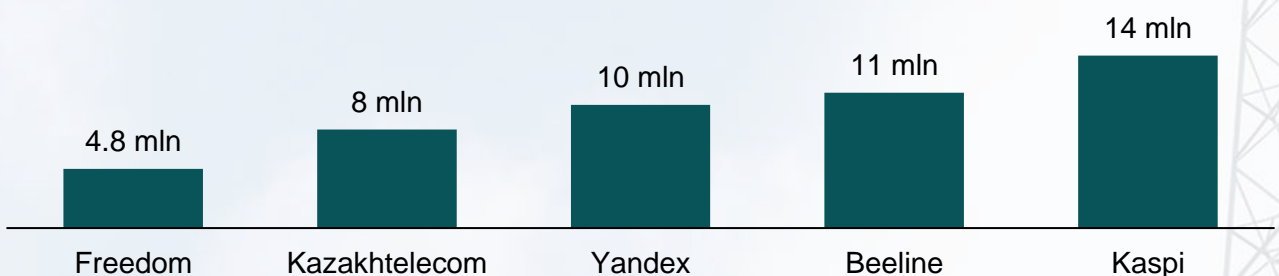
Picture 1: Dynamics of change of financial parameters from 2010 to 2020 of Telecom in relationship with major technological companies.¹ 25 companies include: AT&T, Deutsche Telekom, China Mobile, NTT, T-Mobile, China Telecom, Telefónica, Orange, América Móvil, Vodafone Group, KDDI, China Unicom, Softbank Corp, NTT DOCOMO, BT Group, KT, Telecom Italia, BCE, SK Telecom, Telstra, STC, Telenor, Etisalat, Swisscom

Before considering further potential ways of development of Kazakhtelecom JSC, it is important to take into account world trends of development of telecom providers:

- Ecosystem business:** Creation of ecosystem of digital services not only generates additional income, but strengthens competitiveness of the company. Turkcell company has developed a payment system Paycell and super application BiP, which integrates different services, including payments, news, and entertainments. Development of ecosystem inside Turkcell contributed to increase of incomes of the company and decrease of outflow of customer, and also rise of average income per user. According to data of McKinsey, in 2021 digital and financial services of Turkcell brought more than USD \$150 million (8% of the total revenue), outflow of users of mobile communication decreased by 5-12%, while the average revenue per user (ARPU) increased by 5-10% upon all services.¹
- Marketplaces:** Platforms of e-commerce such as 11Street from SK Telecom (Korean telecom provider) receive income from sale of goods or commission from transactions, that permits to providers to expand their services and make special offers for their users. Expansion of ecosystem increases loyalty of customers and incomes from main activity.

Development of ecosystem in Kazakhtelecom company. In our opinion, the most appropriate development of Kazakhtelecom JSC business is development of super-application which includes ecosystem of the mobile provider, financial services and marketplace. The company has a good jumping-off place for development a super-application – Kcell/Active mobile application. The application includes the financial product OGO Card. According to data of the company, by the end of 2022, over 150 thousand cards OGO were issued.² Taking into account the total number of Kcell users equaling to 8 million persons, the potential of growth of financial services is very big. When using attractive marketing campaigns, Kazakhtelecom has an opportunity to increase the number of OGO cards' users and accelerate the introduction of financial services. When converting more than half of users into users of super-application, for the following several years the application will have over 4 million users, that will give a good base for further competition with other Kazakhstani ecosystems, such as Kaspi with 14 million active users each month (picture 2).³ Thus, the company can take the significant share of the market within a relatively short time.

Quantity of users of different ecosystems

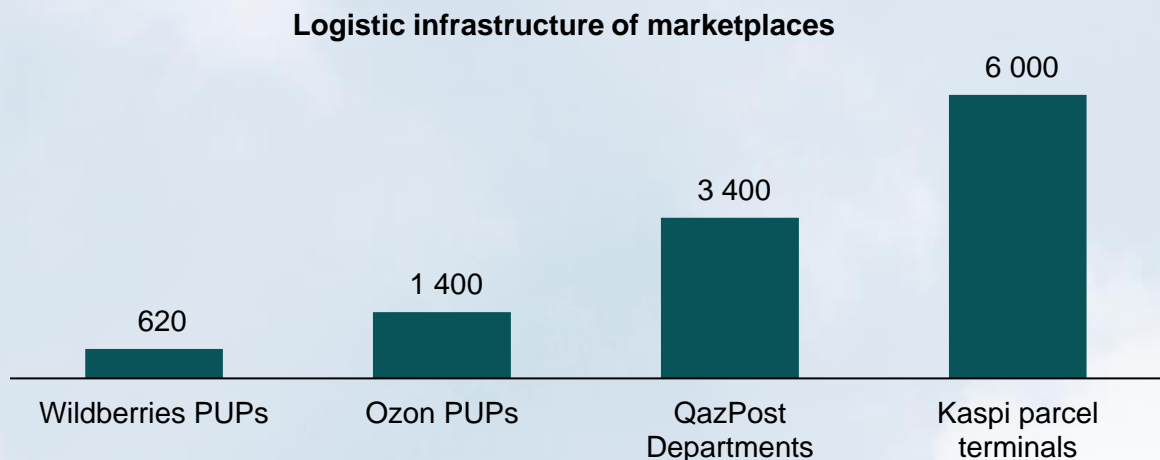


Picture 2. Quantity of active users of different ecosystems in Kazakhstan. For Beeline and Kazakhtelecom, quantity of users of mobile services was used.^{2, 3, 4, 5}

Marketplace development (e-commerce). The market of e-commerce moves into top gear. According to data of PwC, the e-commerce market grew by 79% in the first half of 2023 compared with similar period a year earlier.⁶ The e-commerce market has a long-term potential for growth, that is why Kazakhtelecom can become a major player. The company will significantly develop marketplace (now it operates as a separate website) within Kcell/Active super-application. Such step will accelerate users' mastering of the application platform. Also there is a possibility to offer discounts/privileged terms to users of special tariffs, that can increase ARPU of the main business.

For successful development of the marketplace, we assume partnership of Kazakhtelecom JSC with QazPost JSC, namely, purchase of QazPost JSC by Kazakhtelecom company. Technological infrastructure of Kazakhtelecom JSC and logistic infrastructure of QazPost JSC gives the required synergy for rapid development of the marketplace. 3,400 branches of QazPost JSC perform the role of distribution and pick-up points (PUPs). Integrated company represented by Kazakhtelecom JSC and QazPost JSC will become a major player, which logistic and technological infrastructure will be comparable with Kaspi (6,00 parcel terminals) and Ozon (1,400 puck-up points throughout the country) (picture 3).³

The important element of merger of these two companies is wide presence of department of QazPost JSC in regional and rural localities, giving access to the services for a big number of people.



Picture 3. Logistic infrastructure of marketplaces throughout the whole Kazakhstan by the beginning of 2023^{3,7}

Also for quick growth of the marketplace it is preferable to consider potential partnership with Chinese trade platform PinDuoDuo (PDD). PDD is one of the rapidly growing Chinese marketplaces with 870 million active users and 13 million sellers on the platform. PDD performs the processing of dozens of billions of parcels per year.⁸ The company mainly works inside China, and Kazakhstani consumers buy goods by means of logistic tools not connected with PDD. We consider that it is a distinctive opportunity for the integrated company to become an official partner of PDD and to use its logistic and technological infrastructure such as pick-up points throughout the whole country. According to some unofficial data, several hundreds of thousands Kazakhstani people make purchases on PDD platform on a monthly basis. This format of cooperation can be upscaled towards cooperation with other international marketplaces (Amazon, JD.com, Zalando.com).

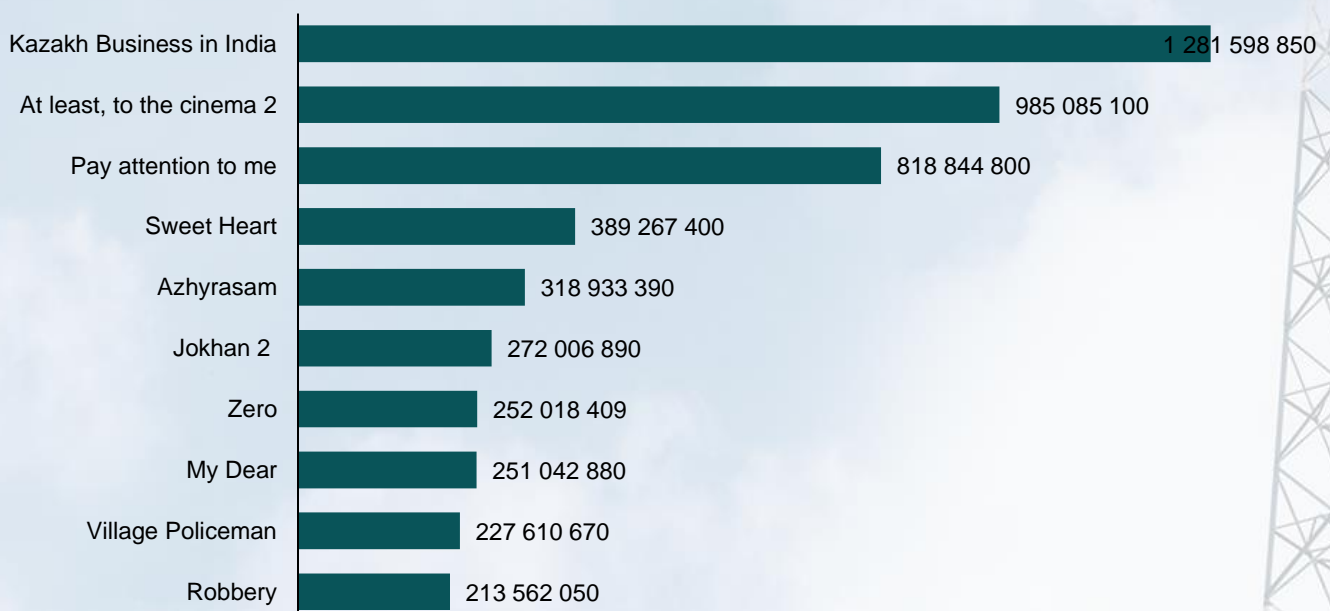
Additional synergies from merger with QazPost JSC. In addition to post services, QazPost offers customers financial and brokerage services. The company is in the process of elaboration and development of super-application QazPost. Possible integration of brokerage and financial services of QazPost JSC into Kcell/Active super-application will increase the attractiveness of ecosystem. This initiative will increase interaction of users with ecosystem of the integrated company.

The integrated company can extend the list of services for legal entities. In addition to Internet services the company will be able to offer payment solutions, financial products and also logistic (post) services. This solution will become one-shop solution for businesses and enterprises.

Streaming and digital TV. Recently, the model of subscription for streaming platforms has become widespread. Netflix is an absolute champion in the global market, but there are multiple local platforms focused on local content. We consider that Kazakhtelecom will actively develop existing streaming business, expand the assortment of movies, series, and sports broadcastings. A successful streaming platform will increase ARPU.

As of today, rapid development and demand for movies and series of local production is being observed. Recently, we observe previously unprecedented figures in Kazakhstani film production. Box office revenues of movie Kazakh Business in India nearly achieved the level of 1.3 billion tenge, and the movie At least to the cinema 2 nearly reached the figure of 1 billion tenge. This is to say that local movies are of high demand, in particular it is seen in box office revenues, as filmgoers vote by money.

Box office revenues of Kazakhstani films



Picture 4. Box office revenues of domestic films, KZT, as of June 1, 2023

At the same time this initiative has socially significant element – support of domestic media and film industry. Investments in Kazakhstani content and development of this industry by the national champion such as Kazakhtelecom will become not only profit-making, but a significant contribution to development of the culture in Kazakhstan.

Investments in data centers and Sovereign Artificial Intelligence (Sovereign AI). States of the whole world actively finance the development of own systems of Artificial Intelligence (AI) so that to stimulate economic growth and preserve the control over national data and advanced technologies in key spheres such as transport, communication and healthcare. AI is a catalyst of innovations stimulating the economic development and performance improvement.

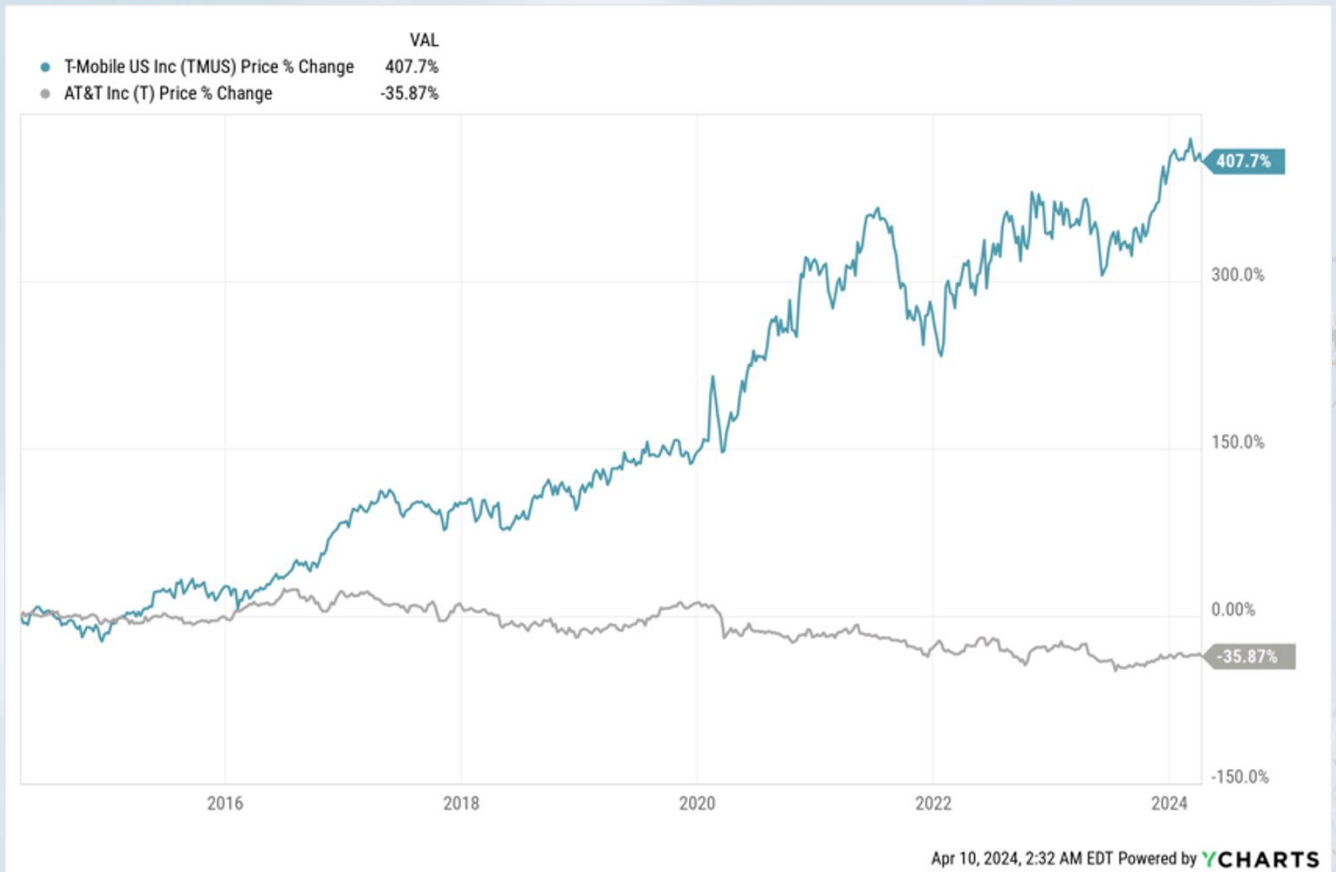


Initiative of NVIDIA AI Nations helps the countries to develop national AI possibilities including support of ecosystem and training of specialists. Scaleway in France is building a high-power cloud-based AI supercomputer. Swisscom in Italy – supercomputer on the basis of NVIDIA for development of the first Italian language model LLM. In India initiatives for development of computation powers have been launched. Japan cooperates with NVIDIA for introduction of AI in different sectors of economy. In Singapore, the national supercomputer center is being modernized (through SingTel provider).⁹

Kazakhtelecom is the most appropriate player for development of Sovereign AI in Kazakhstan. This initiative provides big opportunities for development of different sectors of economy in the country. For example, with cooperation with the Ministry of Enlightenment of the RK and Ministry of Science and Higher Education of the RK, it is possible to develop AI models for learning the Kazakh language and other disciplines in the Kazakh language.

Capital distribution. Development of 5G infrastructure and also business transformation demand high capital expenditures. Accordingly, we consider that the company is to de-prioritize payment of dividends, that will permit to develop the infrastructure and new directions of business for increase of the debt load. By the end of the third quarter of 2023, the consolidated net debt of the company was 239 billion tenge. With the company's operating profit of 137 billion tenge for the first 3 quarters of 2023, the company's debt load remains adequate.¹⁰ We consider that allocation of dividends to development of the company during the following several years will permit to transform the business and support sound financial standing.

For illustration of importance not to increase the debt load and not to be tied with payment of dividends, let's consider the case of AT&T and T-Mobile. 10 years ago it seemed that AT&T company was on the threshold of promising future, and T-Mobile was a relatively small company. However, the situation changed, as of this moment the market capitalization of T-Mobile exceeds capitalization of AT&T, and T-Mobile is to biggest telecom provider in the USA. AT&T is dividend aristocrat paying and regularly increasing dividends year in and year out. Dividends are not a single reason, but they are a key factor in growth of net debt, due to which the company is restricted in making strategic solutions. By the way, T-Mobile started to pay dividends only in 2023.



Possible listing on a new platform. With achievement of the first significant results, it is worth to think about listing on a new platform with high liquidity. We consider that telecom provider with growing segments of ecosystem and marketplace business will receive high multiplier and will be of demand among investors.

It is important to choose a platform with high liquidity. For example, shares of Kaspi (Kaspi was delisted from London stock exchange and now is trading on Nasdaq) demonstrated twelfold increase in liquidity.³

Strengthening of the role of Kazakhtelecom JSC as a quasi-regulator. As it is supposed, sale of Tele2/Altel to Qatari group Power International Holding W.L.L will impose certain restrictions on development of the telecommunication business of Kazakhtelecom JSC (for example, non-increase of the market share during a certain term).

The funds raised in the course of sale will strengthen the financial standing of Kazakhtelecom company. Also the company will be able to continue development of 5G infrastructure (construction of basic 5G stations) and will have capital for development of ecosystem business.



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