Conference Call Transcript

1 February 2017

Q3 RESULTS ANALYST CONFERENCE

Operator

Good day ladies and gentlemen and welcome to the Vodacom Group Ltd results conference call for the three months ended 31 December 2016. Vodacom Group CEO, Shameel Joosub, will host the conference call. I will read the forward-looking disclaimer before handing over to Mr Joosub.

This announcement which sets out the third quarter results for Vodacom Group Ltd for the three months ended 31 December 2016 contains forward-looking statements. These statements have not been reviewed or reported on by the group's auditors with respect to the group's financial position, results of operations and businesses and certain of the group's plans and objectives.

In particular such forward-looking statements include statements relating to the group's future performance, future capital expenditures, acquisitions, divestitures, expenses, revenues, financial positions, dividend policy and future prospects, business and management strategies relating to the expansion and growth of the group, the effects of regulation on the group's businesses by governments in the countries in which it operates, the group's expectations as to the launch and rollout dates of products, services and technologies, expectations regarding the operating environment and market conditions, growth in customers and usage and the rate of dividend growth by the group.

If you do not have a copy of the results announcement it is available on the investor relations website www.vodacom.com. All participants are currently in listen-only mode and there will be an opportunity for you to ask questions later during the conference. If you need assistance from an operator please signal by pressing star and then zero. I would now like to turn the conference over to Mr Shameel Joosub. Please go ahead, sir.

Shameel Joosub

Thank you. Good afternoon everyone and good morning to those joining the call from the US. I'm joined by our CFO, Till Streichert, and Shaun Van Biljon, our Head of Investor Relations. As per our previous quarterly releases we will only focus on revenue and key performance indicators today. Before we look at the numbers let me tell you what stands out for me in this set of results.

Overall I'm pleased with the results with strong performance in South Africa and growth improving on a normalised basis for our international segment. South Africa continues to perform well in a challenging environment supported by strong customer gains with good progress in data as well as strong enterprise growth. Our international operations have shown sequential improvement on a normalised basis. This has been driven by a better growth in Tanzania on the disconnections in Q4, which were necessitated by ensuring that we comply with customer registration and avoid any fines, now showing better performance. And so we are seeing a recovery in the number of connections in the international space.

The continued improvement in our network has expanded coverage especially in relation to data and IT capabilities across all our markets. And finally our care programme has produced further innovation to drive improvement in customer experience with a better bundle depletion notification journey and improved My Vodacom app functionality and really more and more move into the digital space. Our customer satisfaction stores measured through NPS indicate that we are improving relative to our peers in most of our markets.

I will now unpack these results in a bit more detail for you. Fluctuation in exchange rate continues to play a role in our results both operationally and also in the translation of our non-Rand entities in the international segment, notably the strengthening of the Rand to the US Dollar and the continued weakness of the Mozambique Metical. When referencing normalised growth this excludes the impact of currency. Group revenue was up 1.2% and service revenue grew 1.3%. Normalised growth was 3.9% for revenue and 4.4% for service revenue. The growth in service revenue was supported by good growth in active customers and data revenue. Equipment revenue grew 0.2% as device sales volumes picked up in the quarter especially in South Africa. This now starts reversing the negative trend we have seen in the past three quarters as improvement of the Rand exchange rate allows us to bring pricing down, thereby reducing the barriers to entry and accelerating the volume of devices sold.

Overall customer numbers are now close to the levels we had before disconnection in the international operations in Q4. South Africa’s customer growth was strong at 6.7% while the international segment has seen two consecutive quarters of positive net additions. Net adds continued to improve and we should be able to recover the customers that we disconnected due to customer registration requirements in the prior year during the next quarter.

If we now move into the segments and starting with South Africa, the service revenue growth was sustained at strong levels of 5.5% which was supported by good customer growth and improved data revenue growth. Our superior network and our bundle pricing strategy continues to find resonance with the new as well as our existing customers. This has supported the net additions of 547,000 active prepaid customers and 143,000 contract customers in the quarter. We now have 16.3 million customers that are using bundles. These customers have bought 418 million bundles in this quarter alone. That is an increase of 34.8% in total bundles sold. The success of prepaid has been boosted by the take-up of our Just4You bundle offers. As a result we have attracted customers across all segments including value-seeking customers resulting in prepaid ARPU to decline by 3% but compensated for by a 6.8% increase in customers on the prior year.

Growth in contract ARPU of 1.2% was impacted by customer disconnections by Autopage and consequent revenue deferral release in the prior year, excluding which contract ARPU grew 3.6%. Our contract customers are up 5.9% and continue to show low levels of churn. I think it’s important to note that these numbers and these ARPU increases have been achieved without price increases which some of our competitors have put through in the financial year.

Our key area of growth is data. Data revenue now contributes 41% to service revenue and grew at 22%, an improvement on the previous quarter, whilst active data customers increased 4.9% to 19.3 million customers. The improved growth in data revenue stemmed from increased bundles sold, greater data coverage and improvement in device accessibility through better pricing. Data bundle sales continued to perform well as we sold over 136 million data bundles, up 49% year on year. The overall effective price per MB reduced 15.4% as we continue to move more and more customers to in-bundle usage through the improved out of bundle data notification journey. Data effective prices are down more than 60% over the last four years as we focus on improving the value offer to our customers. We added 1.1 million 4G customers to reach 4.8 million 4G customers on our network as we improved the price point of smart devices, even launching a sub R1,000 4G device. The average MB consumption per smart device remains strong, increasing 13.7% to 667 MB with high-end smartphone usage growing by 31% to 1.7 GB.

Another focus area for our growth is enterprise. Underlying enterprise revenue growth was strong at 13.6%. The growth was supported by our fixed line and business managed services as well as our cloud and hosting revenue growth, both of which grew at more than 20%. We spent R2.1 billion in the quarter to substantially widen 4G population coverage, now 70%, up from 54% a year ago, while 3G reaches pretty much the entire population at 99.2% coverage. I have spoken previously about taking a more segmented approach in addressing customers' different needs, wants and demands. The youth proposition known as NXT LVL continues to grow with close on a million customers now registered.

On to the international segment. Service revenue declined 8.2% year on year. Normalised for currency fluctuations on translation growth was 3.4%, an improvement from the previous quarter. Short-term pressure remained with the customer disconnections in Q4 last year not fully recovered. Customer registration processes continue to improve and we now have two consecutive quarters of positive net additions. In this quarter we added 876,000 customers. Our aim is to have customer numbers recovered to levels before the disconnections during the new financial year. Encouragingly Tanzania is showing signs of improvement with positive growth in the quarter. We saw a slowdown in the DRC which was driven by challenging economic and political conditions.

MPESA revenue grew 12.4%, normalised at 17.4%, with Tanzania contributing significantly. The number of customers in DRC has now more than doubled and 42.6% of customers are now using our MPESA service in Mozambique. With this critical mass we are seeing a positive increase in the number of transactions per customer. In total there are 12 million active MPESA customers across our international markets, up 23.6% on the prior year. I think it is worth reiterating how big the system is becoming for us. In Tanzania MPESA now transacts TSh 2.6 trillion a month, which is $1.2 billion per month.

Data demand remains positive in our international operations with data revenue increasing 12.8% on a normalised basis driven by 12.4% increase in active data customers to 12.6 million. This has resulted in data traffic increasing 61.7% year on year. We invested R612 million in infrastructure in these markets during the quarter. The focus remains on increasing both coverage and capacity. 2G sites increased 8.4% and 3G sites increased 32.1%. That concludes our highlights on the two segments. I will round up with our focus areas for the rest of the financial year.

Some comments on the white paper policy. Initial exploratory meetings for implementation of the policy paper between the Minister and the industry were held during November and December with the objective of finding a workable solution for the socio-economic objectives which the white paper seeks to achieve. Discussions are ongoing and I think we are encouraged by the level of engagement and probably more encouraged now by the willingness to find some kind of middle ground between industry and the Ministry. The court case on the other side, the court case between the regulator, ICASA, and the Minister of Communications is still pending. Only once this has been heard will we have communication as to whether or not ICASA can proceed with the auction for high demand spectrum. We do believe there are some efforts to also try and find some middle ground between the regulator and the Minister in this space.

Data continues to expand exponentially. In South Africa we signed a commercial roaming agreement with WBS to roam on their newly-built data network for additional capacity to be able to cater for this future demand and give customers wider access to new technologies such as 4G advanced or LTE advanced.

Some comments on the Tanzania listing. We have submitted our prospectus and we are awaiting feedback from the Capital Markets and Securities Authority in Tanzania. Once this approval is received we will be able to release the prospectus to the public. Our anticipation is for this to happen before the end of the financial year – so that is March.

We will focus on execution of our key areas of growth, enhancing our content offering through execution of [unclear], growing our enterprise space and product offers, and expansion of new revenues streams such as financial services and the Internet of Things. Till will continue to focus on delivering on our cost programme and optimise the returns on the investments that we have made over the past two financial years. Okay, that concludes my comments. Till and I are ready to take your questions.

Operator

Thank you very much, sir. Ladies and gentlemen, at this time if you wish to ask a question please press star and then one on your touchtone phone or on the keypad on the web phone screen. If you wish to remove your question please press star and then two. Again if you wish to ask a question please press star and then one. Our first question is from Chris Grundberg of UBS. Please go ahead.

Chris Grundberg

Thanks guys. Just a quick one or a couple of ones from me. Just on the South African landscape I wonder if you can comment on maybe the trends in the quarter in terms of the pricing moves from your major competitors. I understand MTN has been fairly aggressive but it looks like Cell C may have been less so, might even have raised some prices. I wonder if you can comment on how you see that landscape looking at the moment. And then the second question is actually on Tanzania. It sounds encouraging that you might be moving towards a period of maybe more rational pricing. Can you comment on exactly what shape that has taken? Has that been less competition from Halotel or how is that shaping up, and do you think it is sustainable or what should we be thinking for the year ahead? Thanks.

Shameel Joosub

Okay. Maybe just on the pricing in South Africa I think what we've seen firstly from Cell C is price increases that were introduced especially on data pricing and so on. There has been some price increases that have been put in from 1st January which is quite interesting because I would say the gap between us and the other competitors has narrowed almost completely now with the result that the premium operator is not priced premium, which I think is a very good space to be in. And I would venture to say that most of our tariffs are very competitive, specifically because we are targeting it on a segment basis. Clearly Cell C is not in the mode of reducing prices. I think one can say in the last three years price increases every year from Cell C. Clearly you are focussed on obviously delivering a profit and delivering strong EBITDA growth. And I think that doesn't change with the potential management buyout. If anything it probably becomes more centre stage would be my view.

From an MTN perspective, MTN hasn't made any big price changes. What MTN did was remember during the year they put prices up. So again the gap between us and them has narrowed completely. What they then did was a couple of tactical promotions where they ran one-day specials with big bundles. We understand from the market that it was for them to clear stock and so on. I'm not sure why they needed to do such dramatic things. I thought the days of giving free airline tickets had long gone. But this was that same context if you like. But very tactical, a couple of days only. They did it one or two days now in January and now they have stopped from what we pick up. One doesn't know whether they will do it again, but it is a short-term boost of just trying to get numbers to look better for that period. So interesting move, but my view is nonsensical because I think if you want to deal with it you have either got to deal with it on a more permanent basis to up your numbers than a week of extra connections. I don't particularly see the logic in that. But it does seem to be that they have stopped that.

And then lastly Telkom. I think Telkom with the FreeMe I think there are some offers out there. The limitation on FreeMe has basically been the fact that you need to finance the device on top of it. I think they gained a little bit of traction, but nothing to talk about and certainly nothing that is showing up in our migrations. They have managed to carve a bit of a niche for themselves in the fixed wireless space and that has worked well for them. Instead of replacing the copper as it gets stolen they are putting in LTE advanced. And that is working pretty well for them. So I think they have got a little bit of traction there. Certainly it is an area where I think we can be a bit more aggressive or more competitive, and we have addressed that during the last quarter.

In Tanzania I would say firstly I think the big knocks have been taken from a new competitor entering and so on. But I also think we are boxing smarter in that we have introduced Just4You and these products into the market, taking a more segment approach, protecting our base and so on. Not a dissimilar strategy to that we employed in South Africa, but it took a little longer to deploy because we needed to make sure that we had the IT capability systems and stuff in place which we now have. So that's helping and the intention is clearly that Tanzania does better in the new year.

Chris Grundberg
Great. Thank you very much.

Operator
Thank you. Our next question is from Paul Marsh of Berenberg. Please go ahead.

Paul Marsh
Yes. Thank you very much for taking the question. I really have three questions, and it is about the government white paper. Can you help me to understand the likely timing of this white paper becoming law and whether it is possible for the main proposals in the white paper to change significantly before they become law? Secondly, in broad brush terms – I'm not asking for numbers or percentages, but just in broad brush terms – what are the main financial implications of the white paper in its current form? It looks like no more spectrum auctions. So spectrum cost becomes opex on an annual basis. Does that affect your confidence to invest in PP&E? Would there be more pressure arising from MVNO competitors? These are the kinds of questions that I'm asking myself. And then finally can you remind us when each of your main spectrum licenses expires please?

Shameel Joosub
Okay. So firstly the spectrum licenses expire in 2028. Sorry? 2029. An extra year. So that's the one part. Those are all the spectrum. Remember spectrum is not technology dependent. So you can use it for any technology. That's the first part. I think the second thing is maybe just to explain the timelines and it becoming law. I think the big thing on the white paper itself is that for the white paper to take effect you have to rewrite the laws. The laws to rewrite would take you two to three years because it has got to go through parliament. It has got to go through all the different houses and so on and so on. There are certain things that you could put as a directive to ICASA where they comply with the current policy environment. So there are a few things. But those can also be challenged. So as you try and implement this into law that then provides the industry the opportunity to challenge. So you can challenge it upfront. You can challenge it as each piece is tried to be turned into law. So each of these concepts needs to find itself into law, which generally lands up having to take on more balanced views.

What happens with a white paper in general – I will just talk about white papers in general – they always have concepts in, but for those concepts to meet muster the constitution needs to be taken into account. The existing legislation needs to be taken into account. The regulatory frameworks and so on need to be taken into account. And the current licensing regime and the grandfathering of those rights all need to be considered before these things can be brought to fruition. As an example there is a constitutional part. If you say I want to take away spectrum, do we have a constitutional right to it, besides the fact that we have a license? There is a number of different parts. And as you can imagine all the operators would have spent a lot of money taking a lot of legal opinion on it comes into fruition. So this thing can be delayed for years if it gets challenged, or – and I think the modus operandi that we're trying to find because it doesn't benefit anyone for this to happen. It doesn't benefit industry, it certainly doesn't benefit the Ministry and it doesn't benefit ICASA if this thing gets tied up in court for the next ten years. So the big thing is that we find a workable solution that can work to be able to achieve the objectives. And I think there is more of a willingness to have that. The industry is also engaging on its own to reach common positions and so on before it starts to engage with the Ministry on the government side to be able to provide workable solutions.

The other thing to point out is that the spectrum that we're talking about is not readily available. So the 2.6 spectrum is there, which they can allocate. But the 700 and 800 which is the main sought-after spectrum is not available. It is still subject to digital migration. I think it is something like 60,000 households that have been done and you've still got to get to the majority of households. We've got 16 million households in the country with at least 14 million having access to TV. So there is a lot of work still. So we are actually fighting about spectrum that is actually not there. And it is not in the broadcasters' interest to stop all the court cases that they've got going on to make life easier for the mobile operators. So that conundrum you are stuck in as well. So that's the one part.

The financial consequences, maybe just to talk to it, there are a couple of parts to it. It depends. What's clear is that… Okay, so let's say what's good about the white paper is you won't pay for spectrum. Yes, you make a saving on the cost of spectrum. However, it creates other complexities. And then the other positive is it says you're going to build one network. Capex goes down. Those are the positives. The negatives are effectively there will be one network. We're not sure how that will essentially operate. Does that mean we each [unclear] on this network? So how exactly are we going to allocate the spectrum to various players? Who is going to fund it? What happens when the players around the table can't come up with the funding? Does that mean that the bigger players dilute the smaller players? These are the kinds of things that provide a lot of complexity.

That is why we are more for the mode of saying, look, build an open access network but also allocate spectrum to the existing operators. Remember the reference point that they're using is Mexico. And I think what they have discovered when they went to Mexico is that actually it is a hybrid model in Mexico. The existing players have got the spectrum and they have allocated spectrum to an open access network. So those are the parts. So what are the financial consequences? For us we've also built an alternative to the WBS roaming. That gives us more capacity. It is a little bit of an insurance policy. And to be very frank with you I think the industry regardless of what happens with the white paper needs to make an interim plan, because there isn't an end in sight or a clear end in sight of when the spectrum is available. So there is enough spectrum in the country with the existing players. So it requires some partnership or roaming or acquisitions or whatever modus operandi you want to use to be able to do it. But for us that way was roaming. So the roaming arrangement will work for us.

Longer term we think it is always better for an operator to hold on to his spectrum. But if it did come to pass we would then have to compete on the other elements. We would have to compete with our service, our pricing. The fact that we already have the customer base I think is obviously good for us. But I just think it is messy and it is messy for the country as a whole. That's why if we can come up with some kind of hybrid path including… There are concerns for example that if we did have a hybrid model and we couldn't leverage off the balance sheets of the existing operators that the new open access would suffer. Well, there is a solution which is that the current operators buy some capacity in addition to getting spectrum also from the [unclear]. So there is a multitude of ways in which we can try find a middle ground for this to work. I think one of the realisations for us is that there will be an open access network. Now, does that mean the introduction of more MVNOs and so on? It could be. But it really depends on the same thing. Who is willing to put the capital up? In this case it is not just an MVNO. Even in the WAN [?] is there they will have to buy capacity and invest in the network itself. So there is still a capital requirement, maybe just on a reduced basis.

Paul Marsh
Shameel, that's really helpful, a very comprehensive answer. Thank you very much.

Operator
Thank you very much. Ladies and gentlemen, again if you wish to ask a question please press star and then one. Our next question is from Jonathan Kennedy-Good of SBG Securities. Please go ahead.

Jonathan Kennedy-Good
Good afternoon. Just two from me. First of all a simpler question. Your contract customer growth seems to be accelerating quarter on quarter. I was just wondering whether you could definitively say that you're saying market share and from whom in the contract space, and whether you did anything specific to accelerate those net adds in Q3 with handset subsidies etc. And then just a quick one on the BEE deal. There have obviously been articles speculating that you're planning to buy that part of the PIC stake. And I wondered whether there was any target timeframe for the rollover of your existing deal and whether you could frame or contextualise the six of that deal at this point in time.

Shameel Joosub
Let me start off with the BEE one and I will come back to the contract one in a sec. On the BEE deal I think there are certain realities. The reality is that the current deal will basically expire in 2018, which will mean that we either roll over the deal, or the deal expires and then effectively people are free to sell or we buy back the shares. So that's the one part. So we're going to have to renew BEE. Let's put it that way. There is an opportunity to renew our BEE deal in some form. We are still currently working on the details of what form that could be, and obviously that is twofold. One is what do we get from it in terms of ownership and so on which then converts into points, and what does that mean into the scorecard, obviously versus the cost implications of doing that. The PIC part and the PIC wanting to do a deal or wanting to potentially sell its stake potentially to BEE partners is interesting. We are not in the position yet where we can comment on the deal save to say that we are talking. But let's be clear, the PIC is not looking to sell its entire stake. It is only looking to sell a portion of its stake. And obviously if those shares can either go into the market or those shares could go into BEE hands our preference would be that it goes into BEE hands. And should that require support from us in light of the fact that our current deal is expiring we would be open to that. But I think we are not yet at the point where we can provide further clarity on this.

Till Streichert
Shall I take the net additions so long? On the net additions, Jonathan, we are very pleased with the performance we have seen with 143,000 customers added in essence. Our net additions are a function of obviously our gross positions and the churn. And in essence churn was in fact… On the inflow side we have seen basically good growth in the enterprise sector which was quite pleasing. And equally we have seen on existing accounts add-on lines, which is basically a tablet or another phone which comes on top, another device which is pretty good. But in essence churn has stepped down again in the quarter. And that has in essence yielded a strong net additions growth.

Shameel Joosub

So maybe just to add, we are not doing anything strange or anything funny. We are definitely not giving away 10,000 minutes a month and 50 GB just to get the numbers up to look better. So that's not happening. I think what has also been a big positive, to be frank, is now that the service providers are gone and you have had that out of the system for a while now your gross adds have dropped but your net has improved, because all the fun and games as I like to call it on the contract side is better managed internally now. But also your churn is dropping, so we are not losing customers to Telkom and to Cell C. We are protecting our customer base well, so I think that's positive. And in corporate we keep winning. So that's been very positive as well. And these numbers still don't really have the impact of the National Treasury in, which only starts to come in the fourth quarter and into the new year.

Jonathan Kennedy-Good
Great. Thank you very much. Just a follow-up. Your churn was already at 5%. So it has dropped below that now?

Till Streichert
That's correct. During the quarter it actually dropped below that. It improved further. That's true.

Jonathan Kennedy-Good
Thank you.

Operator
Thank you very much. Our next question is from Michael Gresty of Citibank. Please go ahead.

Mike Gresty
Hello there guys. Just one from me. Can I just confirm, Shameel, that you mentioned that there had only been 12.4% increase in data customers in the international business? And if so, given the macro theme that we always hope for coming off a low base and able to show strong growth that looks a little disappointing. I was wondering if perhaps you can comment on that and where you see that going? It doesn't seem to be coming through as dramatically strongly as perhaps you would have liked to imagine it would.

Shameel Joosub
I think that's a fair comment. But I think you also just need to take into account that we deleted over 4.5 million customers due to customer registration, so it dampens the numbers as well. So we have had that impact. There have been a couple of impacts. There has been that impact. There has also been the impact of obviously the exchange rate in places like Mozambique and so on, which puts your price points up and your smartphone penetration down. So there was that impact. For me it is temporary to be honest. I think it continues to grow strongly into the future because it really is the future. So that's the one part. And I also think the one thing that I would say we need to focus on more and certainly the one that Till and I are pushing is we want to get a better monetisation of data. We are not happy with the monetisation of data in the international. Part of it is competition. But we want to make sure that we have implemented the same disciplines that we did in South Africa to be able to get that jaws to be closer.

Mike Gresty
Great. Thank you. That's all from my side.

Operator
Thank you very much. The next question is from Madhvendra Singh of Morgan Stanley. Please go ahead.

Madhvendra Singh
Yes hi. Thanks for the call. A couple of questions. Firstly on the South African performance. Very strong data revenue growth, it actually accelerated for the second time in the last three quarters. Do you think there is more upside to the data revenue growth trend going ahead? And just following up on that, in terms of out of bundle usage of data how big is that now? And given the focus on bringing the prices down do you think that there is a risk as you try to reduce out of bundle usage data revenue growth could actually get impacted because of that? Thank you.

Shameel Joosub
Okay, I think firstly on the data revenues and the upside, yes, there is always an upside on data. Let me give it to you. Well, not an upside, but there will be continued data growth. What do I mean by that? Essentially you've got 36.4 million customers in South Africa. 19.3 million are using data, of which 16.6 million have a smart device. So as you can see there is the opportunity of almost 3 million customers immediately who are using data with no smartphone. That is the first part that I would say is a potential uplift. The second thing is if you look at the number of customers that are using 4G we are still in a part where we need to get more 4G capable devices. So we have got 5.1 million customers using 4G. And remember we are getting an over 20% ARPU uplift when we convert them to 4G. So we need to continue to accelerate that. The price points we have managed to get down, so we are seeing an acceleration in 4G devices, which is part of the reason why we saw better growth in the December quarter.

So there are quite a few positives. The one big positive strategy that we're working on now is what we call reasons to consume. So we are trying to increase the reasons of why people consume data. Our strategy has been simple. One, increase the addressable market, build our coverage to more people. Two, make the network faster so that in the timeframe people are using more. Three is basically put the right device into people's hands. And conversion from 2G to 3G, and 3G to 4G, are giving us 20% ARPU uplift respectively, so a big part of the strategy. Four, stretch customers. Get them into bundles, give them better value and so on through upsides. And now we have built more [unclear] capability. You get pop-up screens. You get more notifications, that type of thing. So that is doing really well. The last part of the strategy is what we're focusing on now which is what we call reasons to consume. And the reasons to consume is things like video play, our on-demand services, our charge to bill, our ability to charge for data in an app, those types of things. So these are the new parts to keep the data growth at a high level. That's the strategy in a nutshell.

That said, we've just got to balance that against the fact that we are backing against a stronger and stronger data comparative as we go into the new year. And I think that becomes important for us. The absolute number because you are taking it over a bigger one will taper down the growth to under 20%, but purely because your comparative is so much bigger.

Till Streichert
And remember there is almost already 41% of our service revenue contribution which is talking to the point that it is off a lot bigger base as we basically grow data revenue every month, every quarter.

Shameel Joosub
Now, on the out of bundle risk I think what we are trying to do is to manage that carefully. When you look at the out of bundle issue there are really two elements to the out of bundle part. One element is customers that are exceeding their bundles. Now, to be frank with you on the one side it is bad that the customer has to experience out of bundle. On the other side we are missing an opportunity. If that person is exceeding his bundle then we had better sell him a bigger bundle. And that is why the notifications are becoming important. That's why we are trying to drive more people right-sizing

the bundles and so on. So that deals with more than half of the out of bundle problem, just getting that right. So we have a clear programme in place of trying to get people to right-size their bundles, put them on the right bundles, deal with the issue. That's part one. Part two is we're trying to come up with a clever way of dealing with the out of bundle by getting people that haven't used a bundle to adopt bundles and so on and to manage the risk in that form. What am I talking about? I will give you an example of what we did on voice without giving you all of our competitive parts. When Cell C dropped rates four and a half years ago now to 99c what we did was we came up with for R5 you get an hour, having calculated that the customer spends R2.50 a day. So in a similar construct we are now putting a product together which will deal with the out of bundle rate once and for all, but will also not cause a big dilution. It will be managed into our numbers into the new year. But a clear focus on dealing with the issue.

Till Streichert
Just adding to it, I would describe it as a very calculated move going forward which addresses exactly the issues which Shameel has described. Just as an indicator of us addressing that already quite successfully remember we have sold in the quarter more than 280 million data bundles. And in essence 90% of those data bundles are in essence very small size up to 100MB volume, which actually tells you that there is already a lot of move in particular in the income constrained segment of basically managing this transition into bundles and into a lot more control in terms of spend, and hence basically great customer experience.

Madhvendra Singh
When do you think voice becomes a free product? Or do you think actually the industry is moving in that direction given the offer from MTN of 10,000 minutes. Basically voice is free. Do you think this is where the industry is moving in South Africa as well?

Shameel Joosub
Look, I think you will have it on the bigger packages. I think you must not read too much into the MTN thing because if MTN went down the route of 10,000 minutes across the board you will have a very serious problem in terms of the MTN results going forward. That means everything reprices. So I think those were just tactical, almost like free flights to London type of thing to get the numbers up quickly, do a promotional activity, almost retail-type of thing. Just get the feet up in to the stores. And that is why they have not done it across the board. They did it in a select few shops on a select few days to bolster their numbers. And I mean we are monitoring closely to see if that starts to happen more. And of late we are seeing they are actually taking it away or are not continuing with that. So we are monitoring that quite closely. I do think however that your premium packages will step a level down and the next package up will become unlimited and those types of things will happen. Every couple of years that will change. So yes, in the longer term you will have those types of packages. But a lot of what we do today, if you think about Power Hour you are getting an hour for the day. So effectively if you buy a Power Hour every day you've got 30 hours of Power Hour, which is close to one of these free packages.

Madhvendra Singh
Sounds good. Thank you very much.

Operator
Thank you. Our next question is from Craig Hackney of NOAH Capital Markets. Please go ahead.

Craig Hackney
Thank you. Your on-demand video service that you announced in November last year, can you give us an update as to how the up-take of that has been please?

Shameel Joosub
Okay. The on-demand one hasn't launched yet. The video play one has obviously been going for a little while now or a couple of months. No big advertising, but I think there is something like 350,000 users already on the product, with some big advertising plans into the new year, and more content having been added, and a deal having been cut with Multichoice and so on. That one is going quite nicely and we are quite happy. But we have obviously got bigger plans for it as part of our reasons to consume.

Craig Hackney
Right. Okay. Thank you.

Operator
Thank you. The next question is from Ziyad Joosub of HSBC. Please go ahead.

Ziyad Joosub
Hi everyone. Two questions from me please. The first one is the enterprise segment. If you adjust out for Autopage you have had quite a nice step change. I think enterprise service revenue grew 13.6%. That's up from around 8.9% in H1. Given that the government contracts are only really going to be reflected in Q4. How should one be looking at the enterprise segment going forward? And then secondly, in this quarter you added 1.1 million 4G devices. That is effectively… it looks like a 30% increase quarterly sequentially. Do you expect that sort of growth in 4G going forward in terms of device adoption? Are pricing points dropping that fast? Thanks very much.

Shameel Joosub
Okay. So I think on the enterprise part you've just got to balance it out. Obviously there have been some wins in the quarter. I think your fixed services are growing over 20% plus. That has been strong growth in cloud, in hosting, in IP VPNs and so on. I think that continues to grow strongly because obviously it is a big opportunity. And obviously we are selling more and more into our base. So that's the one part. I think the mobile side probably outside the public sector will probably slow a bit, but then public sector will give you the boost. Why will it slow a bit on the mobile side? Because I think we already have a disproportionate market share in that space. So more of the revenue is now coming from new services I would say.

Ziyad Joosub
Okay.

Shameel Joosub
And then on the device strategy, look, I think what has been very positive in the last quarter is the fact that your price points held up and we managed to get a very good exchange rate. As the exchange rate holds up one is encouraged by the fact that we sell more 4G devices. That I would say is a positive. That said you might take into account December seasonality and Christmas seasonality as well. So it will step down a bit from that perspective. Remember over Christmas people do generally buy more. So it will step down, but I think we can look at a better number than you were seeing in the first two quarters. Not as high as December but somewhere in between.

Ziyad Joosub
Okay. And in your view your data conversion, your elasticity was excellent again. And there was quite a step change in data traffic. How much of this would you attribute to 4G? Is there a traffic concentration in a certain amount of subs that maybe provides [overtalking]?

Shameel Joosub

You're going to find this a bit strange, but what we're doing is we're actually investing in both. We are investing in 3G and we are investing in 4G, 3G in capacity in existing areas especially in low coverage. So we are putting a big focus on that. We call it QNPS900 which is effectively 3G in the 900 band which penetrates better indoors than your normal 3G. So we are bolstering the two and making sure that we're getting maximum on both. So it's a way of making sure that you get more data growth and the customer has a better experience. So we are not just doing blanket 4G. We are actually investing in both.

Ziyad Joosub
Okay. And both have got equivalent growth dynamics from a traffic perspective if you consider the traffic dynamic?

Shameel Joosub
Obviously you have got many more customers on 3G than you have on 4G. Of the 19.3 million users or 16.6 million smartphone users only a third are 4G. But they do contribute a disproportionate amount because your higher users are on those devices. So you are looking at 1.7 GB plus per customer whereas obviously on the low end to get to your average of 667 MB obviously on the lower end you're sitting at the 350 MB to 380 MB range.

Ziyad Joosub
Understood. Understood. Okay. Thanks very much.

Operator
Thank you very much. Our next question is from JP Davids of JP Morgan. Please go ahead.

JP Davids
Good afternoon guys. Shameel, you mentioned in your opening comments the success you're starting to see in segmentation. Can you talk us a little bit through some of the trends you are seeing from NEXT LVL? Are you seeing any step-up in ARPU from those customers as they move on to those segmented tariffs? And also maybe just discuss the profitability per customer, i.e. is the ARPU uplift offsetting the extra marketing that goes into that segmentation? Thank you.

Shameel Joosub
What I will do is I will just comment on the overall segmentation while they just give me some of the numbers on the NXT LVL. So basically the approach on it is to look at products and services that resonate with those particular customers. As an example you've got a high value segment, you've got a youth segment, you've got what we call the aspiring segment, which is first-time workers entering the workforce, that type of thing, and then you've got the bottom of the pyramid. And what you're trying to do to give you a good example is on the bottom of the pyramid we know customers are living hand to mouth. So as they are living hand to mouth part of it is that they need bite-sized type living. That is why we have smaller data bundles, small voice bundles and so on. And that is proving to be very successful.

But then when you back that up with Just4You, which does a personal recommendation for that customer and gives him more value, that is now helping to extract even more value from that particular segment. So it is making sure that that resonates more with a particular segment. How you speak to him is very different. That's the one side. Another example would be in high value one of the big things that we're going to be focussing on is roaming. So we are focussing a lot on travel saver, that type of thing in terms of making sure that our high-value customers are included. But we think that we need to do more in the roaming space, as an example. There is special focus on roaming bundles and stuff going into the future that we will be launching. So those types of things are more targeted products and services specifically to that. But also looking at the customers that fit into that high-value segment, are they all on 4G devices? And if they are not, why not? Should we add a little bit of subsidy? Should we move them across? So it is more targeted to get that customer across. In terms of…

Shaun Van Biljon
JP, I don't have the exact numbers with me, but if we look at overall ARPU from the NXT LVL side compared to the base that is not on those price plans we are seeing good ARPU uplift especially in the data space, because it is very much a data-focussed product for the youth. So we are already seeing quite a good uplift there. The good thing about NXT LVL is you create a community as well, because you can give some of your data to your friends and family. So we are seeing good uptick on that as well.

Shameel Joosub
Maybe just some of the offers on NXT LVL. There are about 1 million customers. They are buying more bundles. The products are specifically tailored for them. They have a flex product which now gives them the ability to buy X amount of flexes. One flex is one minute or one flex is 1 MB, two flexes is one minute, that type of thing. So the youth want that flexibility. They don't want you to give them free SMS and these types of things. They want to be able to convert seamlessly between the two. So that's one type of offering. The other offering is every time you buy a bundle of data you get 50 MB free to give to someone else. You can't use it. You have to give it to someone else. So the idea is give it to your bestie type of thing. So that creates this community part and really gets the youth to be part of the NXT LVL community. Then there are a whole lot of other activities. Music videos, music library on video play. So it is leveraging some of our existing products and services. And then again it has got its own Just4You type offering which also then provides better value, extracts more value and these types of things. And then there are a whole lot of below the line activations to create the excitement and so on. That is also working quite well. Bottom line is generating better ARPU.

JP Davids
Thanks very much guys.

Shaun Van Biljon
Thanks guys. We have run out of time. As always if there are any calls left you can always send it through to vodacomir@vodacom.co.za. Thanks for joining us.

Operator
Thank you very much, sir. Ladies and gentlemen, that concludes this conference. Thank you for joining us. You may now disconnect your lines.

END OF TRANSCRIPT