

Wataniya

Company Note

27 May 2010



Hold Until Liquidity Improves

- **Good subscriber growth in Kuwait, window of opportunity in Algeria, and increased competition in Tunisia**
- **Possible listing on the DFM is one of the main future catalysts**
- **Increase our TP by 10% and maintain Hold recommendation; continuous deteriorating liquidity weighs on the stock**

Wataniya reported mixed 1Q10 results. Despite a 9% QoQ drop in ARPU, Wataniya's 1Q10 revenue grew 2% QoQ mainly on the back of a 4% QoQ subscriber growth. EBITDA margin came in significantly lower than previous quarters at 37% due to an exceptional drop in Kuwait's margin (47% of total EBITDA). Net income increased 45% QoQ and 4% YoY. We attribute the huge QoQ net income growth to a one-off item that negatively impacted 4Q09's net income.

Kuwait's top line rebounding driven by higher net adds due to higher-than-expected market growth. Kuwait mobile penetration increased by an impressive 7.5% QoQ, which led Wataniya's net adds to increase QoQ although it barely held its market share. As a result, subscribers increased for the second quarter, jumping 5.6% QoQ from the previous average of 2.8%. Despite a larger drop in ARPU of 7% QoQ, revenue grew 3.5% QoQ due to the higher net adds. EBITDA margin decreased by 800bps, partly because 4Q09's margin was exceptionally high and also due to (i) a reclassification of license fees, (ii) Fono, the retail chain shop acquired in 4Q09 was included in 1Q10 results (retail margins are lower than mobile services' margins), and (iii) a bad debt allowance of KWD800,000. We have revised our EBITDA margin estimate for Kuwait downwards going forward to reflect the permanent factors behind the drop in EBITDA margin.

Algeria is experiencing a "window of opportunity" and Tunisia is preparing for the third entrant. Nedejma benefited from Djezzy's turmoil, which led to a 35% QoQ growth in subscribers in 4Q09, but this didn't filter through to the top line since some of the new SIMs pushed in the distribution channel in 4Q09 are still stuck. Distribution costs pressured EBITDA margin to 31% in 4Q09, but rebounded to 34% in 1Q10 due to cost efficiencies and revenue growth. In Tunisia, operators are being aggressive ahead of the entrance of the third player which is due in 2Q10, which negatively reflected on ARPU and revenue of the last two quarters.

We increase TP by 10% but maintained our Hold recommendation. Kuwait continues to be the main driver of our fair value and the rebound in revenue increases it. We are positive on the other operations, except for Tunisia due to the expected increase in competition. Algeria is benefiting from the window of opportunity, Palestine's EBITDA is expected to turn positive this year, Saudi Arabia is growing its subscriber base, and Maldives' top line has been witnessing double digit growth for two consecutive quarters. Despite this, Wataniya's stock continues to be illiquid and liquidity deteriorated over the past six months. As a result, we maintain our 20% illiquidity discount. There is a plan to list Wataniya on the DFM, which would increase the stock's liquidity, making us reconsider the discount.

KPIs (KWD mn)	New		Old		Consensus	
	2010e	2011e	2010e	2011e	2010c	2011c
Revenue	498	543	513	561	530	562
EBITDA Margin	37.1%	34.9%	37.8%	35.9%	38.5%	38.1%
EPS (KWD)	0.14	0.13	0.16	0.16	0.18	0.19
Net debt/EBITDA (x)	-0.28	-0.45	-0.18	-0.45	-0.16	-0.45
PER (x)	12.9	13.9	10.9	11.1	9.6	8.9
EV/EBITDA (x)	5.4	5.1	6.9	6.5	4.3	4.1
Dividend Yield	2.3%	2.2%	2.7%	2.7%	3.3%	4.1%
Free Cash Flow Yield	5.9%	6.5%	9.4%	8.0%	NA	NA

Hold

Target Price (KWD)	2.02
Market Price (KWD)	1.75*
Upside	15.1%

Listed on	KWSE
Bloomberg Code	NMTC KK
Reuters Code	NMTC.KW

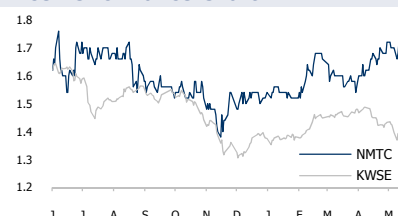
Ent. Val. (KWD mn)	981
Net Debt (KWD mn)	-19
Minorities (KWD mn)	120
Mark. Cap (KWD mn)	879

Market Cap (USD mn)	3,014
Num. of Shares	501
Daily Turn. (KWD mn)	0.24
Daily Turn. (USD mn)	0.82

Shareholders Structure

Free Float	24.0%
Qtel	52.5%
Kuwait Inv. Auth.	23.5%

Price Performance Chart



* Price as of 18 May 2010

NematAllah Choucri

- ▶ +202 3332-8610
- ▶ nchoucri@hc-si.com

Sarah Shabayek

- ▶ +202 3332-8640
- ▶ sshabayek@hc-si.com

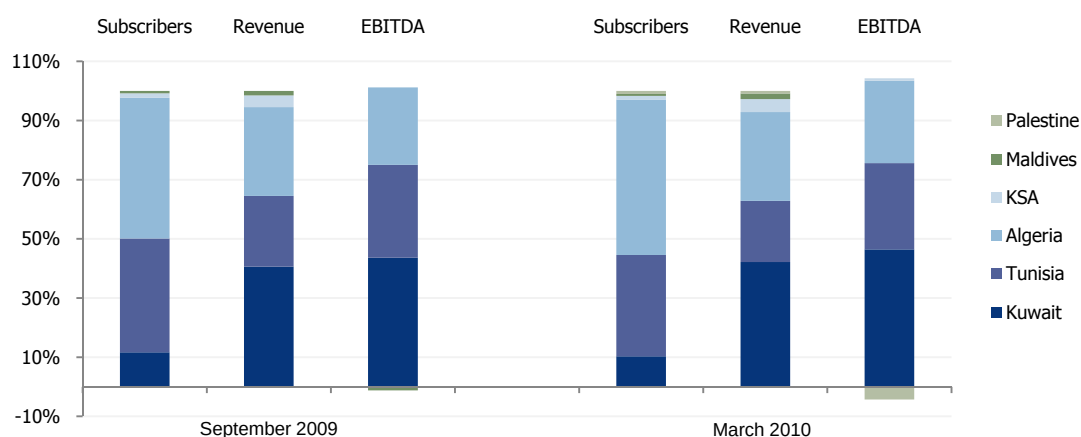
* Disclaimer: See page 5

Table 1: 1Q10 Results

KWD Million	1Q10a	4Q09a	Δ QoQ	1Q09a	Δ YoY
Subscribers (000)	15,759	15,179	3.8%	11,519	36.8%
Net Adds (000)	580	2,689	-78.4%	584	-0.7%
Blended Mob. ARPU (USD)	2.7	3.0	-9.2%	3.3	-18.2%
Revenue	125.7	123.8	1.5%	111.5	12.7%
EBITDA	47	48	-3.3%	44	6.4%
EBITDA Margin	37.1%	38.9%		39.3%	
Net Income	16	11	45.2%	15	4.4%
NPM	12.7%	8.9%		13.7%	
CAPEX	17	29	-43.0%	32	-47.4%
CAPEX/Sales	13.2%	23.6%		28.3%	

Source: Wataniya, HC Research

Chart 1: Wataniya Subsidiaries' Contribution Comparison Between September 2009 (our last update) and March 2010



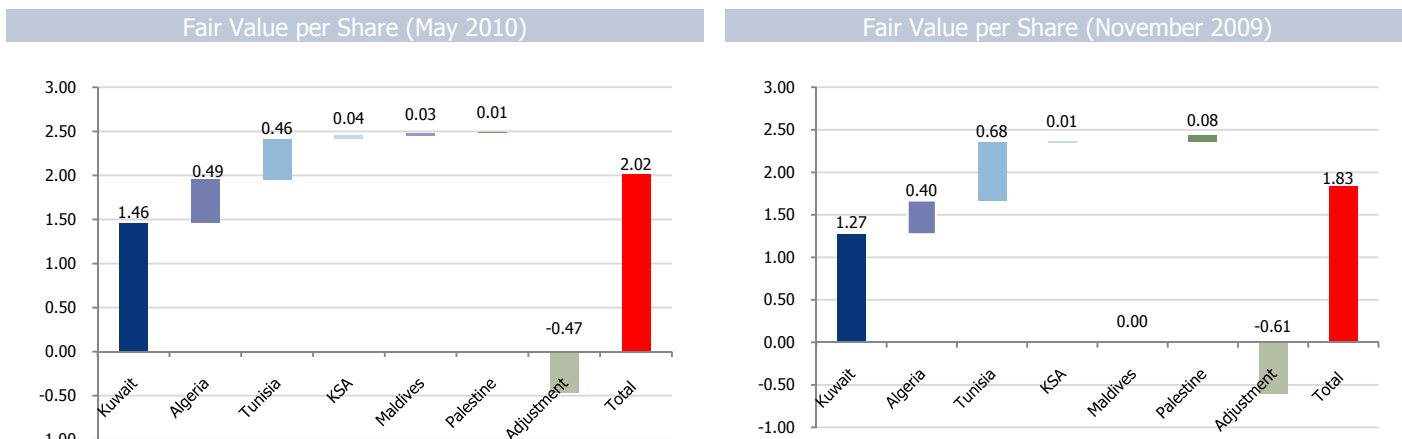
Source: Wataniya, HC Research

Table 2: Updated Estimates per Subsidiary

KWD Million	New		Old	
	2010e	2011e	2010E	2011e
Kuwait Revenue	212	227	208	220
Kuwait EBITDA Margin	42.8%	39.8%	43.8%	41.8%
Tunisia Revenue (Proportionate)	98	96	112	114
Tunisia EBITDA Margin	47.4%	44.4%	52.0%	50.0%
Algeria Revenue	148	152	158	170
Algeria EBITDA Margin	33.6%	33.6%	31.4%	32.5%
KSA Revenue	23	25	24	29
KSA EBITDA Margin	1.5%	9.5%	-4.8%	3.2%
Maldives Revenue	9	10	8	9
Maldives EBITDA Margin	16.8%	20.8%	7.6%	12.6%
Palestine Revenue	8	32	4	19
Palestine EBITDA Margin	-46.7%	3.3%	-10.0%	-5.0%
Consolidated Revenue	498	543	513	561
Consolidated EBITDA Margin	37.1%	34.9%	37.8%	35.9%
Consolidated Net Income	68	63	80	79

Source: Wataniya and HC Research

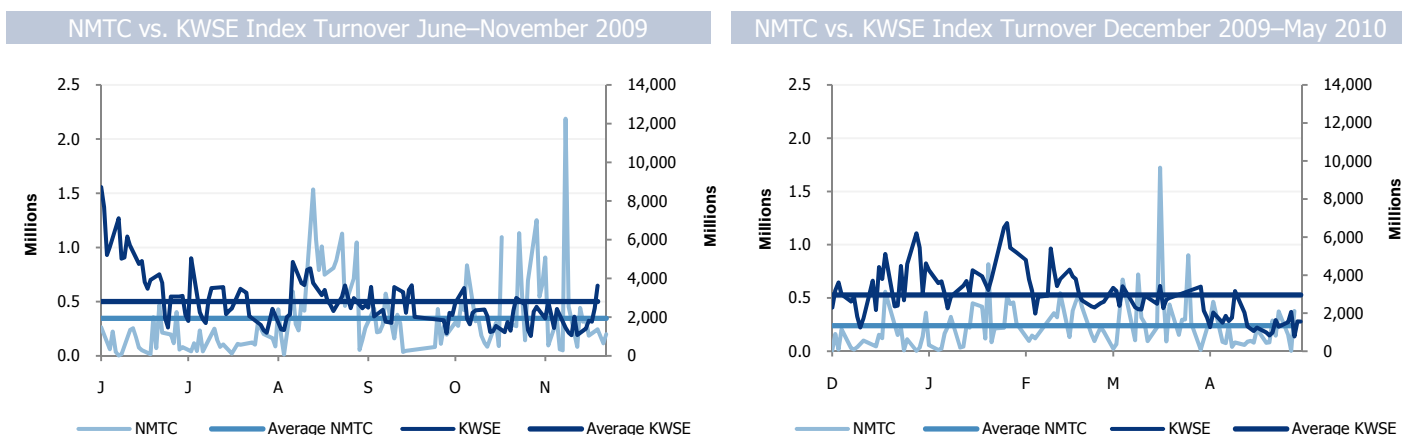
Chart 2: Updating our Valuation: Increase in all operations' value except of Palestine and Tunisia



Adjustment is the addition of book value of some investments, the subtraction of debt, the addition of cash and the addition of a discounted difference between reported and calculated EBITDA

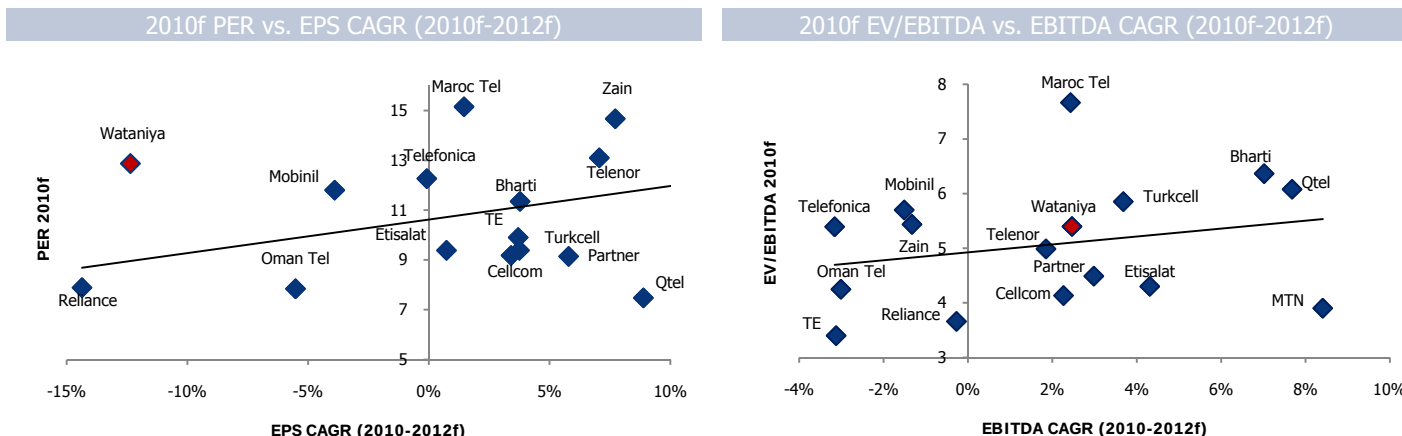
Source: HC Research

Chart 3: While Kuwaiti market's liquidity slightly improved, Wataniya's liquidity deteriorated



Source: Bloomberg , HC Research

Chart 4: Wataniya trades at a premium of 50.0% on 2010f PER and of 5.3% on 2010f EV/EBITDA



Source: Wataniya, Bloomberg, Reuters Knowledge , HC Research

Financial Statements

KWD Million	2009a	2010f	2011f	2012f	2013f	2014f
Income Statement						
Kuwait	201	212	227	247	271	297
Tunisia	102	98	96	97	97	97
Algeria	141	148	152	154	157	163
Maldives	8	9	10	11	12	13
Ksa	20	23	25	28	30	31
Palestine	1	8	32	53	75	96
Total Group Revenue	475	498	543	590	642	697
<i>Growth In Revenue (%)</i>	<i>-0.1%</i>	<i>4.7%</i>	<i>9.1%</i>	<i>8.7%</i>	<i>8.9%</i>	<i>8.5%</i>
Calculated EBITDA	179	176	180	194	215	241
<i>Calc. EBITDA Margin</i>	<i>37.6%</i>	<i>35.4%</i>	<i>33.1%</i>	<i>32.9%</i>	<i>33.5%</i>	<i>34.5%</i>
Reported EBITDA	190	185	189	205	227	253
<i>Rep. EBITDA Margin</i>	<i>40.0%</i>	<i>37.1%</i>	<i>34.9%</i>	<i>34.7%</i>	<i>35.3%</i>	<i>36.3%</i>
Depreciation and Amortization	(82)	(97)	(105)	(107)	(107)	(109)
Operating Profit	97	79	75	87	108	131
<i>Operating Margin</i>	<i>20.4%</i>	<i>15.9%</i>	<i>13.8%</i>	<i>14.8%</i>	<i>16.8%</i>	<i>18.9%</i>
Other Non-Oper. Income	32	0	0	0	0	0
Net Interest Expense	(10)	(6)	(5)	(3)	(2)	(3)
Taxes	(18)	(13)	(12)	(13)	(14)	(17)
Minorities	11	12	9	5	4	3
Contribution To Zakat, KFAS, NLST	(5)	(3)	(3)	(4)	(5)	(6)
Directors' Remuneration	(0)	(0)	(0)	(0)	(1)	(1)
Net Profit	108	68	63	73	91	109
<i>Net Margin (%)</i>	<i>22.8%</i>	<i>13.7%</i>	<i>11.6%</i>	<i>12.4%</i>	<i>14.1%</i>	<i>15.6%</i>
Earnings Per Share (EPS)	0.22	0.14	0.13	0.15	0.18	0.22
<i>Growth In EPS (%)</i>	<i>31.4%</i>	<i>-37.0%</i>	<i>-7.7%</i>	<i>15.7%</i>	<i>24.6%</i>	<i>19.5%</i>
Dividends Per Share	0.00	0.04	0.04	0.04	0.05	0.06
Dividends Pay-Out (%)	0.0%	30.0%	30.0%	30.0%	30.0%	30.0%
Balance Sheet						
Intangible Assets	205	174	159	121	119	79
Tangible Assets	413	453	469	477	480	476
Investments & Other Assets	41	38	38	38	38	38
Total Fixed Assets	659	665	665	636	637	593
Total Current Assets	229	264	266	363	469	599
Total Current Liabilities	259	277	280	286	295	303
Total LT Liabilities	145	112	76	91	130	134
Minority Interest	33	22	13	8	4	1
Shareholders' Equity	452	519	564	615	678	754
Cash Flow Statement						
C/F From Ops	171	169	162	174	191	212
Dividends Received	0	0	0	0	0	0
Interest and Minority Divs.	(10)	(6)	(5)	(3)	(2)	(3)
CAPEX + Investment	(85)	(125)	(105)	(78)	(109)	(65)
Acquisitions and Disposals	(2)	0	0	0	0	0
Dividends Paid	(24)	0	(20)	(19)	(22)	(27)
Net C/F Pre Financing	50	38	31	74	59	118
Liquid Resources	8	1	0	0	0	0
Financing	(11)	(28)	(39)	12	36	0
Change In Cash	47	10	(8)	86	95	118
Key Ratios						
Net Debt/EBITDA	0.06	-0.28	-0.45	-0.80	-0.99	-1.38
CAPEX To Sales	23.5%	21.1%	15.3%	13.2%	11.1%	9.3%

**Rating Scale**

Recommendation	Upside
Buy	Greater than 20%
Hold	-5% to 20%
Sell	Less than -5%

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HC Research

research@hc-si.com

Karim Khadr	Regional Head of Research	karim.khadr@af-hc.com	+971 4 2935381
Tudor Allin-Khan, CFA	Chief Economist/Strategist	tudor.allin-khan@af-hc.com	+971 4 2935386
Amr Abdel Khalek	Economist	aabdelkhalek@hc-si.com	+202 3332 8638
Nadine Weheba	Economist	nweheba@hc-si.com	+202 3332 8644
NematAllah Choucri	Telecoms	nchoucri@hc-si.com	+202 3332 8610
Sarah Shabayek	Telecoms	sshabayek@hc-si.com	+202 3332 8640
Germaine Benyamin	Banks & Financials	germaine.benyamin@af-hc.com	+971 4 2935382
Janany Vamadeva	Banks & Financials	janany.vamadeva@af-hc.com	+971 4 2935384
Hatem Alaa	Industrials	halaa@hc-si.com	+202 3332 8614
Mennatallah El Hefnawy	Industrials	melhefnawy@hc-si.com	+202 3332 8632
Mai Nehad	Industrials	mnehad@hc-si.com	+202 3332 8626
Majed Azzam	Real Estate	majed.azzam@af-hc.com	+971 4 2935385
Ankur Khetawat	Real Estate	ankur.khetawat@af-hc.com	+971 4 2935387
Nermeen Abdel Gawad	Real Estate	ngawad@hc-si.com	+202 3332 8628
Lovetesh Singh	Petrochemicals & Fertilizers	lovetesh.singh@af-hc.com	+91 9772 755 777
Rehaam Romero	Editor	rromero@hc-si.com	+202 3332 8634
Mohamed El Saiid, MFTA	Head of TA Research	msaeed@hc-si.com	+202 37496008 (Ext. 175)
Wael Atta, CFTE	Senior Technical Analyst	wael.atta@af-hc.com	+971 4 2935388
Sameh Khalil, CFTE	Technical Analyst	skhalil@hc-si.com	+202 37496008 (Ext. 361)

HC Brokerage – Cairo, Egypt

salesandtrading@hc-si.com

Shawkat El-Maraghy	Managing Director	selmaraghy@hc-si.com	Ext. 200
Khaled Abdelrahman	Managing Director	kabdelrahman@hc-si.com	Ext. 402
Mostafa Saad	Local & Gulf Sales	msaad@hc-si.com	Ext. 213
Yasser Mansour	Local & Gulf Sales	ymansour@hc-si.com	Ext. 217
Hossam Wahid	Local & Gulf Sales	hwahid@hc-si.com	Ext. 206
Hassan Kenawi	Local & Gulf Sales	hkenawi@hc-si.com	Ext. 300
Abou Bakr Shaaban	Local & Gulf Sales	ashaaban@hc-si.com	Ext. 238
Nihal Hany	Local & Gulf Sales	nhany@hc-si.com	Ext. 219
Mohamed Helmy	Foreign Sales	mhelmy@hc-si.com	Ext. 207
Ahmed Nabil	Fixed Income Trader	anabil@hc-si.com	Ext. 218

HC Brokerage – Dubai, UAE

Hassan Aly Choucri	General Manager	hassan.choucri@af-hc.com	+971 4 293 5305
Mohamed Hegazy	Head of Sales	mohamed.hegazy@af-hc.com	+971 4 293 5365
Mohamed Galal	Head of Sales Trading	mohammed.galal@af-hc.com	+971 4 293 5309
Anne Marie Browne	Foreign Institutional Sales	annemarie.browne@af-hc.com	+971 4 293 5301