

Qatar Telecom

Neutral

Target price (QAR)	295
Share price (QAR)	280
Potential total return (%)	4.6

Dec	2006a	2007e	2008e
HSBC EPS	15.58	16.35	17.71
HSBC PE	18.1	17.3	15.9
Performance	1M	3M	12M
Absolute (%)	14.5	13.1	13.5

11 February 2008

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Tough road ahead; we initiate with a target price of QAR295 and a Neutral rating

- **Domestic market could become saturated; limited financial flexibility could make it difficult to fund future expansions**
- **Wataniya Telecom, a subsidiary of Qatar Telecom, is driving group profitability; Qtel ex Wataniya looks expensive to us**
- **We initiate coverage with a target price of QAR295, implying 5.4% potential total return, and a Neutral rating**

Qatar Telecom, or Qtel, is Qatar's incumbent diversified telecom operator. It launched in 1987 and operated solely in Qatar until 2004, since when it has expanded via acquisitions to have a presence in 16 countries. Qtel's core markets are Qatar and Kuwait, accounting for c72% of the group's current EV. However, increased competition in either market could dampen the company's growth prospects, and it looks likely, after Vodafone paid a high price for the mobile licence in Qatar, that aggressive competition will come from that quarter. However, we expect the Qatar government to reduce royalties in Qatar from 25% of pre-tax profit to c12.5% from 2008 onwards on account of new competition in the market, while in Oman it has already been reduced from c12% of net revenue to c7% following the liberalisation of the telecom market. This should offset some of the pressure on bottom-line growth. Besides its core markets, the company also operates in the growth markets of Algeria, Tunisia, Iraq and Oman.

The company is highly leveraged, at c40% of its total assets, which at current prices implies a high net debt-to-EBITDA of 3.5x. Therefore, its ability to finance further expansion is limited, as taking on more debt would erode profitability substantially. Additionally, a secondary issuance would dilute earnings for the current shareholders.

Qtel's growth is mainly driven by its Wataniya operations. We estimate the 2009 EV/EBITDA of Wataniya Telecom at 6.9x versus 6.2x for Qtel and 7.9x for Qtel ex Wataniya. This compares with the 2007-12e EBITDA CAGR of 12.4% for Wataniya Telecom, 7.3% for Qtel and 2.8% for Qtel ex Wataniya. These figures illustrate our view that Wataniya's growth is more sustainable. In addition, Qtel's core market is on the verge of saturation, and Qtel ex Wataniya looks expensive to us. Therefore, we prefer Wataniya. We initiate on Qtel with a Neutral rating, on a target price of QAR295, implying a potential total return of 5.4%. In a separate report published today, we initiate coverage of Wataniya with a target price of KWD4.00, implying 36% potential total return, and an Overweight rating.

Index^	ABU DHABI INDEX
Index level	4777.86
RIC	QTEL.QA
Bloomberg	QTEL QD

Source: HSBC

Enterprise value (QARm)	45340
Free float (%)	45%
Market cap (USDm)	7,760
Market cap (QARm)	28,200

Source: HSBC

Financials & valuation

Financial statements

Year to	12/2006a	12/2007e	12/2008e	12/2009e
Profit & loss summary (QARm)				
Revenue	4,420	10,068	13,229	14,168
EBITDA	2,630	4,978	6,416	6,829
Depreciation & amortisation	-503	-1,363	-1,905	-1,998
Operating profit/EBIT	2,127	3,615	4,511	4,832
Net interest	-18	-998	-1,316	-1,259
PBT	2,252	2,980	3,570	3,923
HSBC PBT	2,109	2,696	3,282	3,664
Taxation	-598	-691	-396	-392
Net profit	1,700	1,919	2,190	2,435
HSBC net profit	1,558	1,635	1,771	2,175

Cash flow summary (QARm)

Cash flow from operations	2,205	5,222	4,775	5,413
Capex	-1,028	-1,740	-2,453	-2,324
Cash flow from investment	-1,745	-19,445	-2,453	-2,324
Dividends	-910	-1,065	-1,078	-1,235
Change in net debt	24	18,091	-1,162	-1,854
FCF equity	1,124	3,494	2,246	2,834

Balance sheet summary (QARm)

Intangible fixed assets	354	17,532	17,532	17,532
Tangible fixed assets	3,043	8,965	9,513	9,839
Current assets	2,405	6,196	6,224	6,337
Cash & others	1,417	4,000	4,000	4,000
Total assets	7,802	37,838	38,491	39,022
Operating liabilities	1,957	5,868	5,865	6,179
Gross debt	766	21,441	20,278	18,425
Net debt	-651	17,441	16,278	14,425
Shareholders funds	4,992	5,898	6,721	7,695
Invested capital	2,428	22,825	23,404	23,529

Ratio, growth and per share analysis

Year to	12/2006a	12/2007e	12/2008e	12/2009e
Y-o-y % change				
Revenue	48.2	127.8	31.4	7.1
EBITDA	51.2	89.3	28.9	6.4
Operating profit	49.6	69.9	24.8	7.1
PBT	50.3	32.3	19.8	9.9
HSBC EPS	34.3	4.9	8.3	22.8

Ratios (%)

Revenue/IC (x)	1.8	0.8	0.6	0.6
ROIC	62.5	21.3	17.2	18.4
ROE	33.7	30.0	28.1	30.2
ROA	23.5	13.4	11.7	12.4
EBITDA margin	59.5	49.4	48.5	48.2
Operating profit margin	48.1	35.9	34.1	34.1
EBITDA/net interest (x)	147.3	5.0	4.9	5.4
Net debt/equity	-12.9	196.7	152.5	113.2
Net debt/EBITDA (x)	-0.2	3.5	2.5	2.1
CF from operations/net debt		29.9	29.3	37.5

Per share data (QAR)

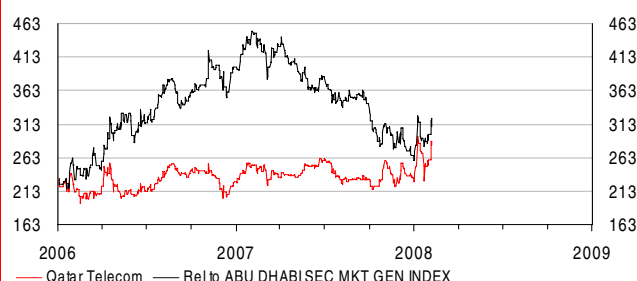
EPS reported (fully diluted)	17.00	19.19	21.90	24.35
HSBC EPS (fully diluted)	15.58	16.35	17.71	21.75
DPS	10.00	10.78	12.35	14.61
NAV	49.92	58.98	67.21	76.95

Valuation data

Year to	12/2006a	12/2007e	12/2008e	12/2009e
EV/sales	6.3	4.5	3.4	3.0
EV/EBITDA	10.6	9.2	7.0	6.3
EV/IC	11.5	2.0	1.9	1.8
PE*	18.4	17.5	16.2	13.2
P/NAV	5.7	4.9	4.3	3.7
FCF yield (%)	3.9	12.3	7.9	10.0
Dividend yield (%)	3.5	3.8	4.3	5.1

Note: * = Based on HSBC EPS (fully diluted)

Price relative



Note: price at close of 06 Feb 2008

Investment summary

- ▶ Qatar remains the key market, accounting for c47% of the group's EV. However, we think growth there will slower
- ▶ Wataniya Telecom is driving the group's growth; funding remains problematic, with net debt-to-EBITDA at 3.5x
- ▶ Qtel ex Wataniya looks expensive. We initiate coverage with a Neutral rating and a target price of QAR295

Following the herd

The MENA region has witnessed a huge surge in mergers and acquisitions in recent years. Until 2004, Qtel operated only in Qatar, where it until this year has enjoyed a monopoly. However, the prospect of market liberalisation and saturation led Qtel to follow many other operators' lead and start expanding into other regions. Over the last four years, the company has expanded via acquisitions to have a presence in 16 countries. Its portfolio comprises assets that we think provide both value and growth in the long term. While Qatar and Kuwait offer value, Oman, Algeria, Tunisia and Iraq provide it with growth

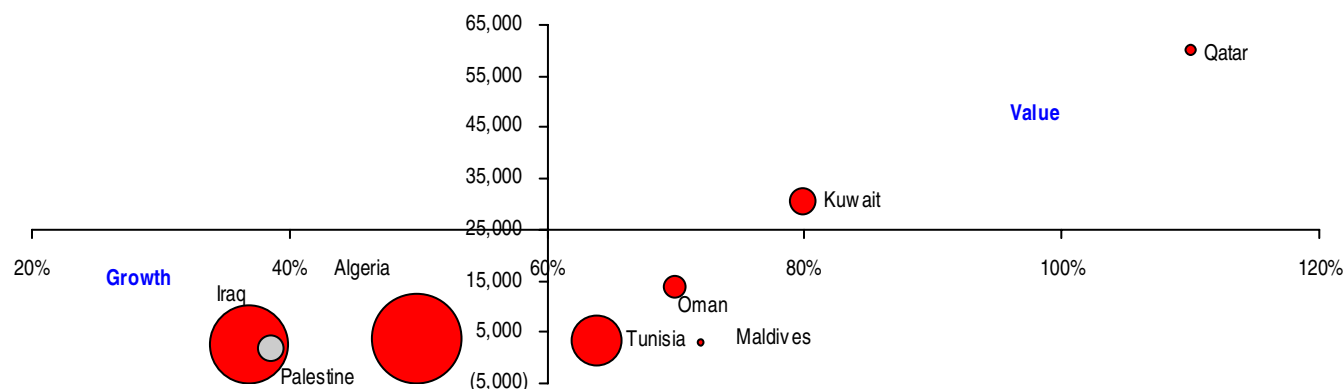
opportunities. Additionally, the investment in Asia Mobile Holdings (AMH) exposes Qtel to the high-growth Asian markets.

Core markets to come under pressure

Qatar and Kuwait are Qtel's biggest markets, contributing c72% to the group's EV.

Until end-2007, Qtel was the sole telecoms service provider in Qatar. Its monopoly recently ended when a second wireless licence was awarded to a Vodafone-led consortium. The company is expected to start its operations in late 2008.

Qtel's portfolio: GDP per capita (Y axis), penetration levels as at end-2006 (X axis) and population size (size of the bubble).



Source: HSBC, Company reports

We believe the entrance of Vodafone rather than a regional player to the Qatari market is more negative for Qtel, because:

- ▶ Of Qatar's population, 82% reside in just two cities (Doha and Al Rayyan) and therefore Vodafone's network rollout is likely to be fast. Therefore, Qtel is unlikely to profit from Vodafone needing to share the existing infrastructure.
- ▶ The large number of expats living in Qatar could help Vodafone to capitalise on its roaming services, particularly as it has wide coverage, with operations in the Western developed markets and now, since the acquisition of Hutch, also in India. Since most of the expats in Qatar are Indians, this could be crucial for Vodafone.
- ▶ Vodafone won the international gateway licence, which is likely to be negative for Qtel's international interconnect revenues.

In addition, pricing pressure in Qatar appears set to continue. Mobile tariffs in Qatar are among the highest in the region in terms of per minute call rates and connection fees. We don't expect a price war in Qatar following the opening up of the market; however, we do expect some pricing pressure to continue, diluting ARPU. We don't believe that price elasticity in Qatar is high, as it is a rich country, so any reduction in prices may not lead to an increase in MOUs.

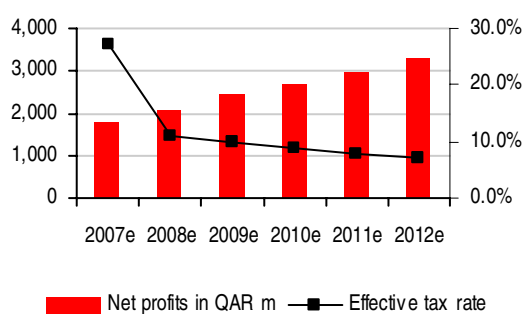
The examples of other GCC countries have been similar, for example Mobily in Saudi Arabia, Du in UAE and Nawras in Oman, have all been able to capture a high market share very rapidly. The same is likely to be case for fixed line in Qatar, where a licence is up for grabs in 2008. Qatar has one of the highest ARPUs (cUSD72 in 2006) and EBITDA margins (over 60%) in the GCC region. However, we believe they are going to come under pressure as Qtel's monopoly comes to an end.

Similarly, we think Qtel's ARPU and EBITDA margins in Kuwait – where Wataniya is one of only two telecom operators currently – will be negatively affected by the arrival of STC in Kuwait by late 2008, with its market share falling from c42% to c36% in the long run. However, population growth coupled with the fact that STC is going to share infrastructure with Wataniya should allow Qtel to maintain its growth in Kuwait.

Royalty reduction to provide some relief to the bottom line

We expect Qtel's earnings to grow at a compound annual rate over 2007-12e of c12.8%. This is higher than top-line and EBITDA growth, because of the reduction of royalties in Qatar and Oman. The Omani government has already announced it is to reduce the royalty from c12.5% of net revenue to c7% from 2008 onwards and we expect the royalty in Qatar to fall from c25% of profit before tax to c12.5% of profit before tax. This should reduce the effective tax rate for the company from c27.3% in 2007 to c7.3% in 2012e.

Bottom line to grow by 12.8% in next five years, driven by the reduction in the tax rate (in QAR m)



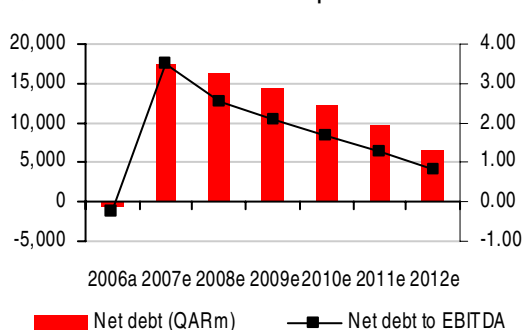
Source: HSBC estimates

Promising plans, but can they be capitalised on?

Qtel intends to become one of the top 20 telecom operators globally by market capitalisation, with inorganic growth one of the main ways through which it is intending to achieve its goal. Since most of the markets in which Qtel operates are

small in terms of population, we think it not only needs to make another round of strategic acquisitions, but also that it needs to target bigger markets if it wants to meet its goal. One option we think the company might pursue is an increase its stake in AMH, a subsidiary of Temasek-owned Singapore Technologies Telemedia (STT), or buy out the minorities in Wataniya. Further, Qtel has expressed its desire to expand in the Middle East, especially in Lebanon, Syria or Iran, which are effectively closed to Western operators. Qtel is also looking for opportunities in Africa, but its main interest remains in the North African region, where the company has experience and more understanding of the market. Management might consider acquiring new licenses or existing operators. However, given the current state of Qtel's balance sheet, we believe the ability of the company to make further acquisitions in the near term is limited. The company's net debt-to-EBITDA ratio is currently around 3.5x, making it difficult to increase debt to fund further acquisitions. Additionally, telco assets are becoming more and more expensive globally, thereby making it more and more difficult as time goes by for Qtel to consolidate further and create shareholder value.

Qtel's net debt and net debt/EBITDA position



Source: HSBC estimates

We prefer Wataniya to the slow-growing Qtel ex Wataniya

We use a sum-of-the-parts (SOTP) methodology based on discounted cash flow to value each of Qtel's operations separately. Our SOTP analysis gives us a fair equity value of QAR29.5bn or QAR295 per share. Therefore, we initiate coverage with a Neutral rating, based on a 12-month target price of QAR295, which implies a potential total return of 5.4%.

Qtel's growth is driven mostly by Wataniya. We have assessed the effect of Wataniya on Qtel's valuation. To find out the effective EV of Qtel without Wataniya, we removed the price paid for Wataniya (fully financed by debt) from Qtel's current EV. We then derived the multiples of Qtel ex Wataniya, which effectively is Qtel's wireless and wireline operations in Qatar and its business in Iraq and Oman.

Comparing the multiples of Qtel, Qtel ex Wataniya and Wataniya, we find that Qtel ex Wataniya offers limited growth, while trading at higher multiples (see the table below). We expect Qtel's EBITDA to grow at a compound annual rate of 11.3% while Qtel ex Wataniya will grow at c5.8% between (2007-09e)

Another important factor to consider is that we expect Wataniya growth to be more sustained Qtel's. This is because Wataniya's operations in Algeria, the Maldives and Palestine are likely to continue to expand margins and so experience higher growth rates over a longer period.

Wataniya's growth is coming in later years...Qtel ex Wataniya expected to remain flat

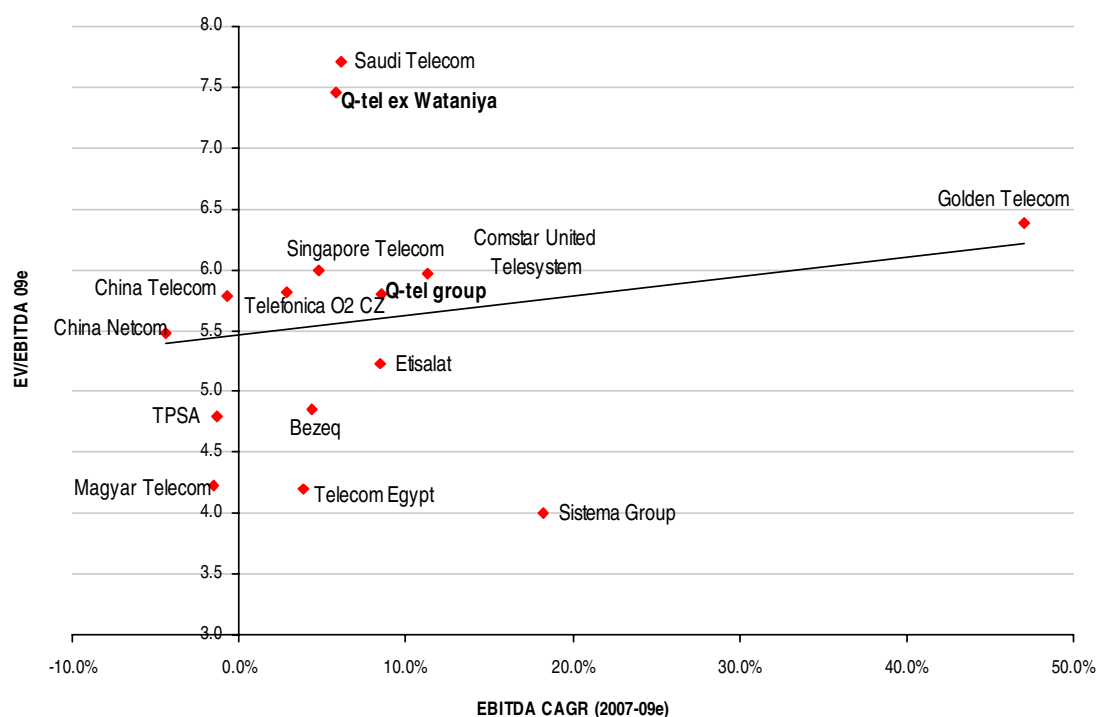
	EV/EBITDA						EBITDA CAGR (2007-12e)
	2007e	2008e	2009e	2010e	2011e	2012e	
Wataniya Telecom	9.8	8.5	6.9	5.8	5.0	4.3	12.4%
Qtel Group	9.1	6.9	6.2	5.6	5.0	4.4	7.30%
Qtel ex Wataniya	8.8	8.0	7.9	7.9	7.8	7.7	2.8%

Source: HSCB estimates

The EBITDA CAGR (2007-12e) for Wataniya Telecom is 12.4%, Qtel is 7.3% and Qtel ex Wataniya is 2.8%, implying Wataniya Telecom's growth is more sustainable.

On account of this our ratings are Overweight Wataniya and Neutral Qtel, as Wataniya offers better value and growth, in our view. The multiples for Wataniya may not indicate its true potential, as most of the growth is coming in later years on account of fast growth in Algeria. Though our valuation of Qtel benefits from the growth of Wataniya, the holding company suffers from the risk that its core market, Qatar, will become saturated.

EV/EBITDA 2009e vs EBITDA CAGR (2007-09e) for EMEA/Asia diversified telco operators



Source: HSBC estimates

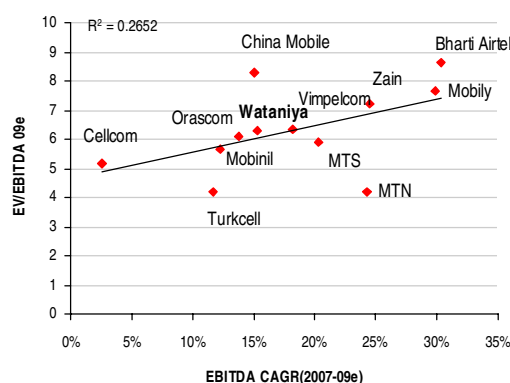
We initiate on Qtel group with a Neutral rating, based on our target price of QAR295, which implies a potential total return of 5.4%. In our report on Wataniya Telecom published alongside this note, we initiate coverage of Wataniya with a target price of KWD4.00 per share, implying 36% potential total return, and an Overweight rating.

Qtel ex Wataniya does not look like an attractive investment

Qtel's investment in Wataniya net of Iraq (in USDm)	3,600
Qtel's investment in Wataniya net of Iraq (in QARm)	12,981.6
Qtel's EV (in QARm)	45,541
Qtel's EV without Wataniya	32,459
Net debt of Qtel without Wataniya	4,459
Wataniya EV/EBITDA 2009e	6.9x
Wataniya EBITDA CAGR (2007-09e)	15.30%
Qtel EV/EBITDA 2009e	6.2x
Qtel EBITDA CAGR (2007-09e)	11.30%
Qtel ex Wataniya EV/EBITDA 2009e	7.9x
Qtel ex Wataniya EBITDA CAGR (2007-09e)	5.80%

Source: HSBC estimates

EBITDA CAGR (2007-09e) vs EV/EBITDA 2009e for pure mobile operators in EMEA/Asia



Source: HSBC estimates

Qtel becoming a key regional player

- ▶ Monopoly in Qatar ended recently when a new mobile licence in Qatar was awarded to Vodafone
- ▶ Qtel has expanded into a total of 16 countries by acquiring existing operations (eg Wataniya Telecom) and by winning new licences (eg in Oman)
- ▶ However, its stretched balance sheet could make further expansion difficult in the near future

The company

Qatar Telecom (Qtel) is the integrated telecommunication services provider in Qatar and is the country's third-biggest public company in terms of market capitalisation. It launched on the Doha Securities Market (DSM) in 1998 and also listed on the London Stock Exchange in 1999, on the Bahrain Stock Exchange in 2001 and on the Abu Dhabi Securities Market 2002. However, most of its liquidity is in the DSM.

Until recently, the company was the incumbent and only telco company in its domestic market of Qatar, when Vodafone was awarded the second mobile licence.

Qtel is majority-owned by the Qatar government, which has a 55% stake. The rest is free float, of which around 10% is held by the long-term investor Abu Dhabi Investment Authority (ADIA).

Qtel's other operations

Name of subsidiary	Country	Qtel's effective stake
Nawras	Oman	55.6%
NavLink	United States, Europe and Middle East	38.2%
Wataniya Kuwait	Kuwait	51.0%
PCT Saudi	Saudi Arabia	28.6%
Tunisian	Tunisia	25.5%
Wataniya Maldives	Maldives	51.0%
Nedjma	Algeria	32.6%
Wataniya Telco Palestine	Palestine	29.1%
Asiacell Iraq	Iraq	29.9%
ACT- Jordan	Jordan	78.0%
Burraq – Pakistan	Pakistan	58.5%
Asia Mobile Holdings	South East Asia	25.0%
LCT Laos	Laos	6.0%
Shinwatra	Cambodia	12.3%
Starhub	Singapore	12.3%
Indosat	Indonesia	10.3%

Source: Company report, HSBC

Expansion was necessary

Anticipating that competition would increase in its home market, the company decided to expand abroad, winning the second mobile licence in Oman in 2004. This was followed by a series of acquisitions, including a 38% stake in NavLink (a provider of managed data services), Atco Clearwire

(with coverage in Pakistan and Jordan), Asiamobile Holdings (Singapore, Indonesia, Cambodia and Laos), Wataniya Telecom (Kuwait, Algeria, Tunisia, Maldives, Palestine and Saudi Arabia) and Iraq. Operations in Qatar, Oman, Iraq, Kuwait, Tunisia and Algeria are explained later.

NavLink

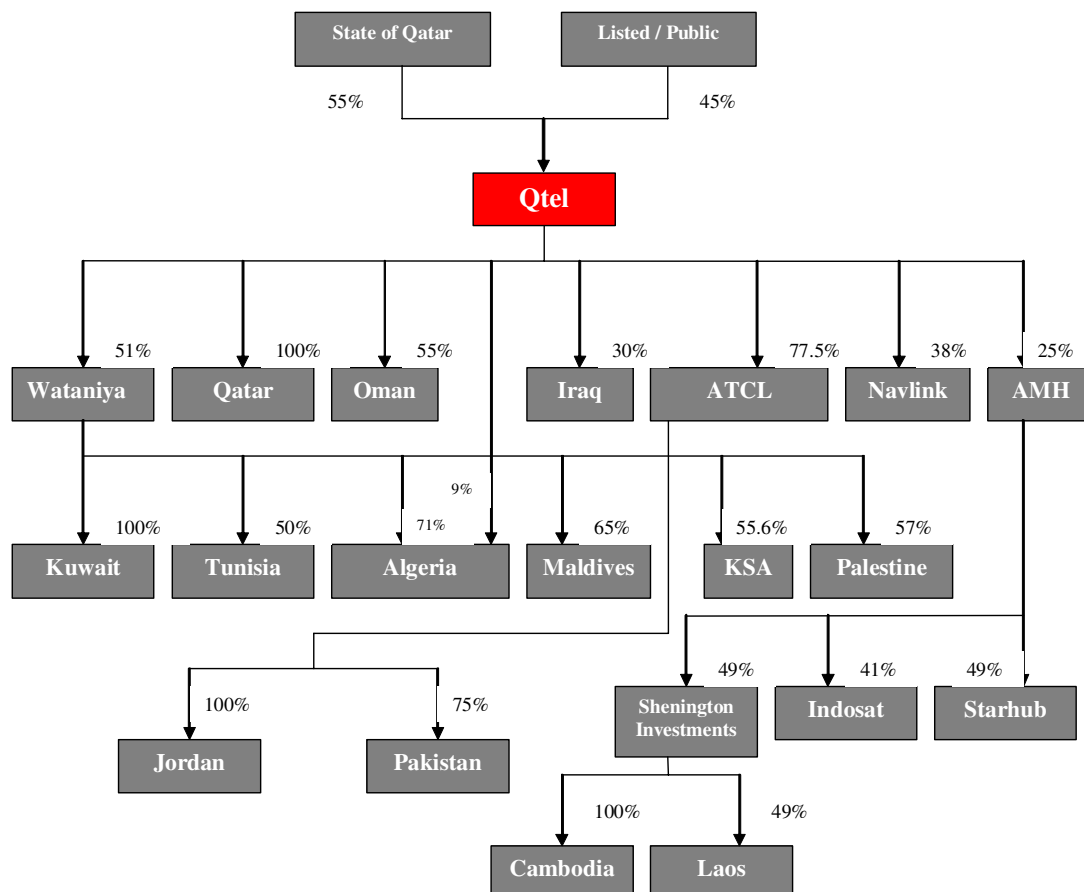
In late 2006, Qtel acquired a 38% stake in NavLink for USD28m. It is a subsidiary of NavLink Switzerland, which is jointly owned by AT&T and two Lebanese shareholders, Laurent Delfer and George N Chammas. NavLink is a provider of managed data services, delivering enterprise information technology solutions, including web hosting, messaging and wireless services. NavLink has operations in the US, Europe and the Middle

East and serves both businesses enterprises and governments. Qtel integrates the numbers for NavLink as an associate.

ATCO Clearwire (ACTL)

Qtel owns around 77.5% of ATCO Clearwire, which has stakes in Jordan (100%) and Burraq Telecom in Pakistan (75%). The company focuses on providing WiMAX services in the region. We believe WiMAX is an important technology in the emerging markets (for more details on WiMAX, refer to our thematic research *WiMAX- Anti climax* January 2006). We believe that it is a good investment in terms of exploring potential opportunities in these countries; however, it does not add any material value to Qtel, in our view.

Company structure (as of end 2007)



Source: Company data

Asia Mobile Holdings (AMH)

In January 2007, Qtel acquired a 25% stake in Asia Mobile Holdings (AMH) for USD635m in cash. AMH is a mobile-focused investment vehicle of Temasek-owned Singapore Technologies Telemedia (STT). AMH has a 49.28% stake in Starhub (Temasek has a controlling stake) and a 40.81% stake in Indosat. StarHub's shares are listed on the Singapore Stock Exchange, while Indosat's shares are listed on the Jakarta and Surabaya Stock Exchanges, and its American Depositary Receipts are listed on the New York Stock Exchange.

In July 2007, AMH completed the acquisition of a 49% stake in Singapore-registered Shenington Investments for USD200m. Shenington, previously a wholly owned subsidiary of Shin Satellite, owns 100% of Cambodia Shinawatra (CamShin), as well as 49% of Lao Telecom (LTC) in Laos. Thus, the acquisition gave Qtel indirect exposure to Singapore, Indonesia, Cambodia and Laos. The deal looked attractive from Qtel's perspective when it acquired the stake in AMH.

In contrast to recent telecoms M&A generally, Qtel's 25% stake in AMH was acquired at a discount (of 16%) to the underlying holdings' market value. The transaction implied an equity value of USD2.54bn for AMH, while the market value of AMH holding at that time was USD3.016bn. Based on current market prices, we believe the value of AMH is around QAR3.1bn, compared with a book value of QAR2.3bn, implying a return on equity of around 30% to the shareholders of Qtel. However, the impact of the AMH acquisition is not material enough to justify a valuation premium for Qtel in our view.

Wataniya Telecom – acquisition of 51% stake

In March 2007, in what has been dubbed one of the most important M&A transactions in the Middle East, Qtel acquired a controlling 51% stake in

Wataniya Telecom for USD3.8bn or KWD4.6 per share when the stock was trading at around KWD3.02 per share. The sellers of the 51% stake were KIPCO and other parties related to KIPCO. The acquisition included additional direct stakes of 9% each in operations in Algeria and Iraq.

At the time, the acquisition implied an EV/sales of 5.0x, EV/EBITDA of 11.9x and PE of 28.9x on a trailing 12-month basis. The transaction was fully financed by debt, resulting in Qtel's net debt rising to QAR15.3bn at the end of Q1 2007. The company was net cash positive at the end of 2006.

Analysis of Qtel-Wataniya deal

Total value of the deal (USDm)	3,818
Less: value paid for additional stakes in Iraq and Algeria (USDm)	100
Total value for 51% stake in Wataniya (in USDm)	3,718
Implied value for 100% Wataniya (in USD)	7,290
Implied value for 100% Wataniya (in KWD)	2,107
No. of shares outstanding in Wataniya	458
Value per share for Wataniya (KWD)	4.60
Share price on the day of acquisition (KWD)	3.02
Premium	52.3%
Amount received from Iraq sale by Wataniya (in USDm)	107
Net implied value of 100% Wataniya excluding Iraq (in USDm)	7,183
Net implied value of 100% Wataniya, excluding Iraq (in KWDm)	2075.87
Implied value per share for Wataniya excluding Iraq for Qtel (in KWD)	4.53

Source: Company reports, HSBC

We believe the premium paid in acquiring the controlling stake in Wataniya Telecom was much too high; even the expected synergies may not be enough to make the deal value-enhancing for shareholders. Wataniya Telecom is currently trading at KWD2.94 per share, excluding its Iraqi operations, now sold. We have arrived at a fair value of KWD4.00 for Wataniya Telecom. This is still far below the price paid by Qtel (implied price per share excluding Iraq is around KWD4.53 per share). We believe that Wataniya will benefit more than Qtel from the expected synergies from the deal in terms of roaming and equipment procurement. This is because Wataniya can piggy back on Qtel's scale benefits.

Forecasts – Wataniya is driving growth

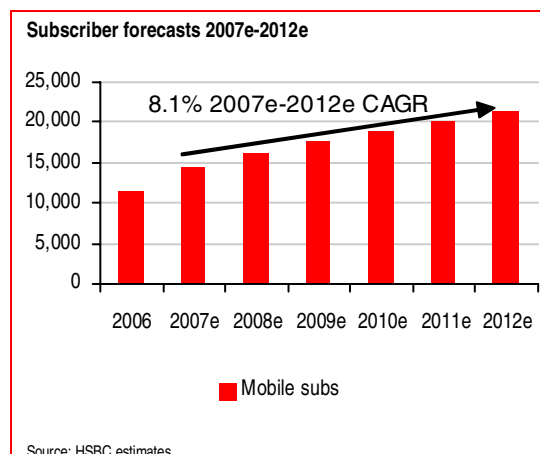
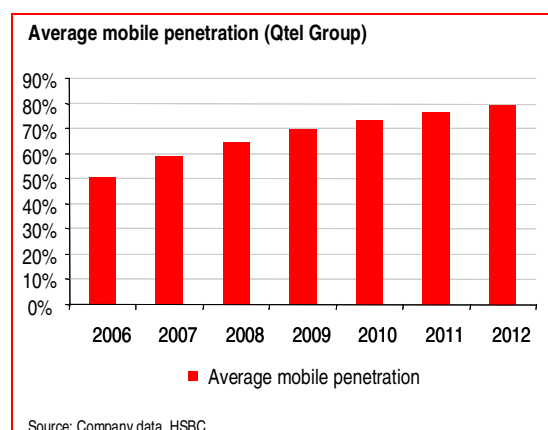
- ▶ 21 million mobile subs by 2012e; 2007-12e subs CAGR of 8.1%, mainly driven by Wataniya
- ▶ Of Qtel's EV, 88% comes from its mobile operations; it is one of the slowest-growing EMEA/Asian mobile operators in terms of revenues and EBITDA
- ▶ Royalty reduction to drive profitability; high gearing leads to less financial flexibility to fund further inorganic growth

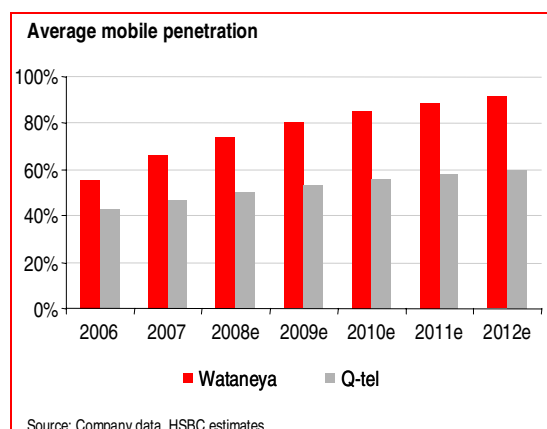
Mobile penetration reaching 80% by 2012e

Qtel Group operates in 16 countries, of which we include nine in our estimates. This is because its operations in Pakistan, Jordan, Singapore, Indonesia, Cambodia, Laos are associates and are not material to the overall valuation of the group. In any case, six of these are held by Qtel's 51%-owned subsidiary, Wataniya. Qtel began life as a fixed-line player, but its focus has since shifted to mobile, with it representing 88% of our valuation

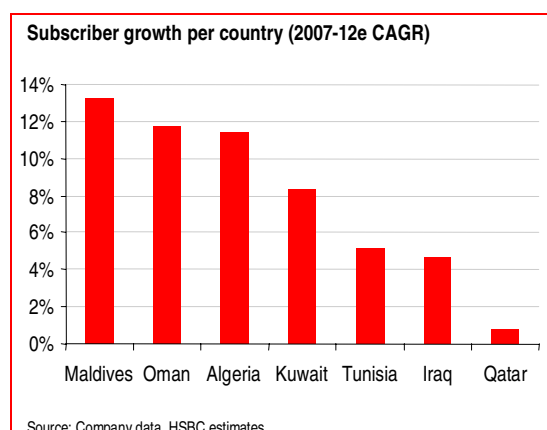
of the company. The company has also mentioned that it is only interested in mobile opportunities, rather than fixed.

Qtel is present in four GCC countries (Qatar, Kuwait, Oman and Saudi Arabia), two Middle Eastern countries (Iraq and Palestine) and two North African countries (Algeria and Tunisia). Qtel is also present in the Maldives.



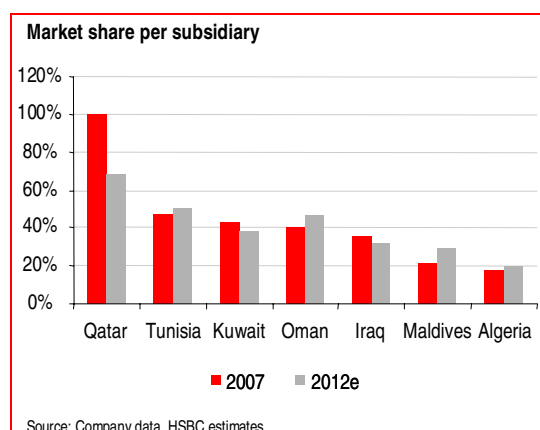


The average mobile penetration of Qtel's portfolio of countries stood at 51% at the end of 2006 and we expect it to approach 80% by 2012e. We expect Wataneya's average mobile penetration in its portfolio of countries will reach 92% and for Qtel will reach 60% by 2012e. We forecast limited growth for Qtel, as we remain concerned about the deteriorating security situation in the Iraq and the fact that Zain has emerged as the dominant player in the market, following its acquisition of Orascom Telecom's Iraqi subsidiary, Iraqna in 2007.



Market share erosion in key markets of Qatar and Kuwait

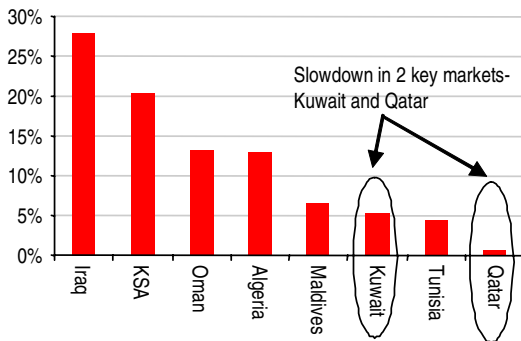
Competition in Qatar from Vodafone and additional competition in Kuwait from STC, the third mobile operator there, could reduce Qtel's market share in its two key markets, which combined contribute more than 70% to the group's EV. However, we expect this to be offset somewhat from Qtel increasing its market share in Oman, Tunisia and Algeria.



Revenue growth mainly driven by Algeria and Iraq

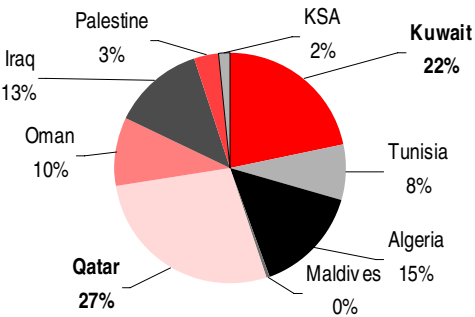
Qtel is one of the slowest-growing companies in terms of revenues when compared with its other Asian/EMEA mobile peers. Since 88% of the group's value of coming from mobile, we consider the group as a mobile operator. Iraq and Algeria is the key contributor to the growth, driven by subs growth and stable ARPUs in the two countries. However, the key thing to note is that we think growth in Qatar and Kuwait will slow, with revenue growing at a compound annual rate over 2007-12e of c5% and c1%, respectively, against our estimate for the group as a whole of c10.2%.

Revenue CAGR (2007-12e) for each operations



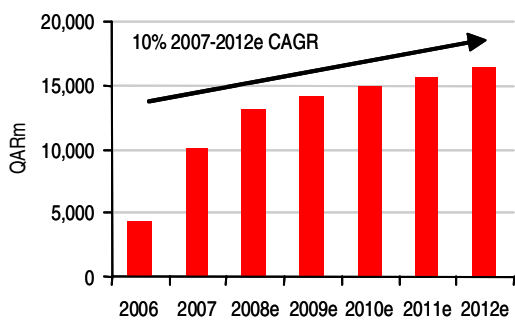
Source: HSBC estimates

Revenue contribution per subsidiary 2012e



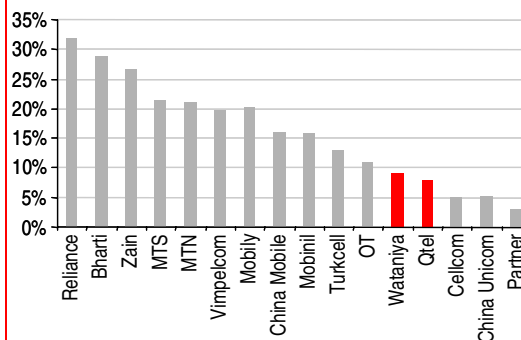
Source: HSBC estimates

Revenue forecasts 2007-12e



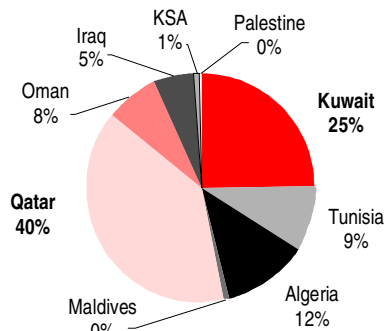
Source: Company data, HSBC

Projected revenue growth for EMEA/Asian mobile operators – 2007-09e CAGR



Source: HSBC estimates

Revenue contribution per subsidiary 2007e



Source: Company data, HSBC

ARPUs to remain stable; however, Qatar likely to see the most pressure

We expect ARPUs to remain stable in all of the key markets. We expect Qatar to see the fastest decline at a CAGR over 2007-12e of c4.4% on account of competition.

ARPUs in USD

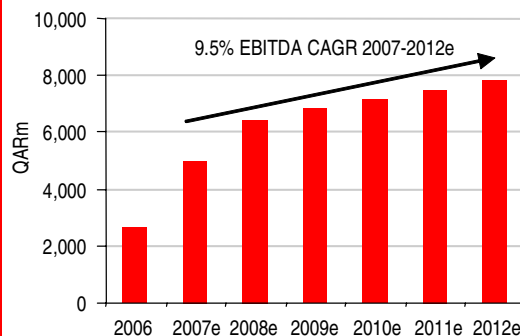
	2007e	2008e	2009e	2010e	2011e	2012e	CAGR (2007-12e)
Kuwait	50.9	49.5	47.0	45.3	44.2	43.5	-3.1%
Tunisia	13.1	13.0	12.6	12.9	12.9	12.7	-0.6%
Algeria	9.0	8.6	8.6	8.7	8.8	9.0	-0.1%
Maldives	14.8	14.2	13.9	13.8	13.9	14.1	-1.0%
Palestine	0.0	13.9	14.6	14.9	15.2	15.4	n/a
Qatar	67.7	62.9	60.1	57.3	55.3	54.0	-4.4%
Oman	26.5	24.8	24.2	23.9	23.7	23.7	-2.2%
Iraq	9.7	9.8	9.9	10.0	10.2	10.4	1.5%

Source: HSBC estimates

EBITDA to grow at a 2007-12e CAGR of c9.5%

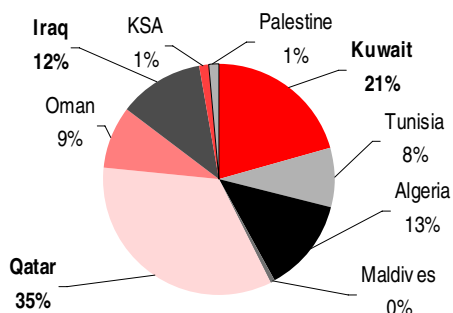
Qtel's Qatari operation has high EBITDA margins (c69% for the first nine months of 2007), which we expect to come under pressure as the market opens up to competition. We don't expect Vodafone to enter into a price war, as it would be detrimental for both companies and would be likely to increase their SAC (subscriber acquisition costs). We believe product differentiation and quality of service will be key to gaining share in Qatar. We expect Qtel will

Qtel Group EBITDA forecasts 2007-12e



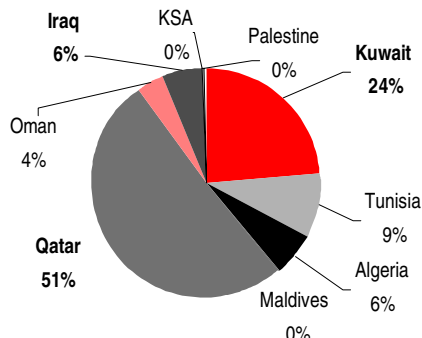
Source: Company data, HSBC estimates

Contribution to EBITDA per subsidiary 2012e



Source: HSBC estimates

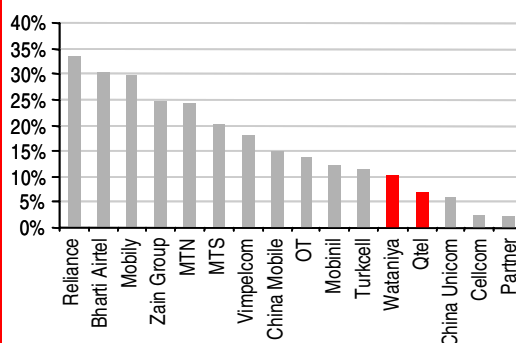
Contribution to EBITDA per subsidiary 2007e



Source: HSBC

suffer gradual margin declines, with wireless margins dropping to c67% from c75% currently, while we see wireline margins falling to 46% in 2012e from 48% currently. For the group, we expect margins to stabilise at around 46% in the long run (by 2016e).

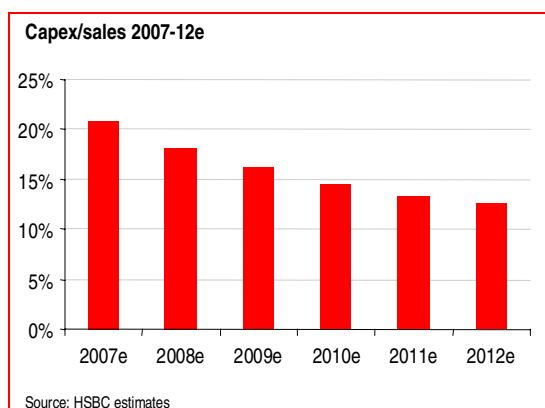
Projected EBITDA growth for EMEA/Asian mobile operators 2007-09e CAGR



Source: HSBC estimates

Capex to sales to stabilise at c13% by 2012e from c21% currently

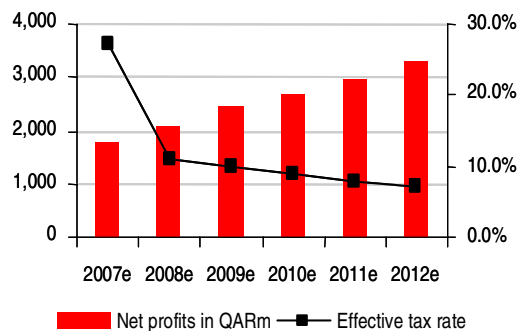
The company's high capex is currently being driven by its start-up operations, for example in Palestine, the Maldives, Algeria and Iraq, but should stabilise in next five years, we think. We expect the group's capex-to-sales ratio to decline from c21% currently to c11% in the long run (2016e).



Royalty reduction in Qatar and Oman to offset the interest cost pressure on bottom-line

We expect Qtel's earnings to grow at a compound annual rate over 2007-12e of c12.8%, higher than both top-line and EBITDA growth because of the reduction of royalties in Qatar and Oman. The Omani government has already announced a reduction in royalty from c12.5% of net revenue to c7% and we expect a royalty reduction in Qatar from c25% of profit before tax to c12.5%. This should reduce the effective tax rate for the company from 27.3% in 2007 to 7.3% in 2012e. The high level of debt on the balance sheet has resulted in higher interest expenses. However, we believe that the lower tax rate should offset the higher interest expenses, resulting in bottom-line growth increasing.

Bottom line to grow by 12.8% in the next five years, driven by reduction in tax rates

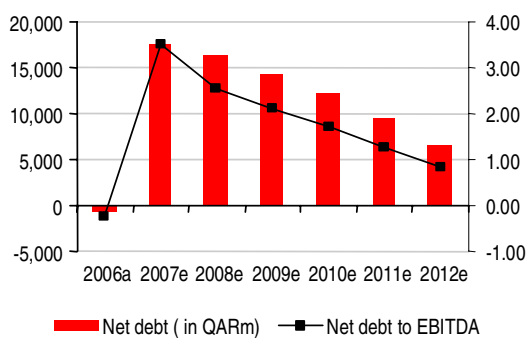


Higher leverage resulting high net debt/EBITDA

Qtel has a strong cash flows from its operations in Qatar and Kuwait. Both these operations are cash cows for the company and management is utilising the cash generated from these assets to generate growth in markets like Algeria, Iraq, the Maldives and Palestine. The company paid a dividend of 60% of earnings in 2006 and c70% in 2005. We expect a payout ratio of c60% in 2007, implying a dividend yield of c4.2% and c4.8% in 2008 at current prices.

The company has been borrowing heavily recently to finance its acquisitions. The company's net debt-to-EBITDA ratio is currently around c3.5x, which makes it difficult for Qtel to increase its level of borrowing to fund further acquisitions. We don't expect the company to become net cash positive before 2014e.

Qtel net debt and net debt/EBITDA position



Qtel group P&L summary (Year end December)

In QARm	2006a	2007e	2008e	2009e	2010e	2011e	2012e
Wireless revenue	3,032	8,769	11,861	12,681	13,333	14,000	14,681
Wireline revenue	1,388	1,299	1,369	1,487	1,567	1,612	1,658
Reported revenue	4,420	10,068	13,229	14,168	14,900	15,612	16,339
Y-o-y change	48%	128%	31%	7%	5%	5%	5%
EBITDA	2,630	4,978	6,416	6,829	7,171	7,504	7,845
EBITDA margins	59.5%	49.4%	48.5%	48.2%	48.1%	48.1%	48.0%
Change	51%	89%	29%	6%	5%	5%	5%
Capex	-991	- 2,101	- 2,453	- 2,324	- 2,206	- 2,124	- 2,075
Capex/sales	22.4%	20.9%	18.5%	16.4%	14.8%	13.6%	12.7%
TFA	3,043	8,965	9,513	9,839	9,998	10,058	10,071
Depreciation	-503	- 1,363	- 1,905	- 1,998	- 2,047	- 2,064	- 2,063
Depn/opening TFA	20.2%	44.8%	21.2%	21.0%	20.8%	20.6%	20.5%
Amortisation	0	0	0	0	0	0	0
Operating profit	2,127	3,615	4,511	4,832	5,125	5,441	5,781
Non-op. exceptional	143	284	288	259	233	210	189
Associate	0	79	87	91	96	101	106
PBIT	2,270	3,978	4,886	5,182	5,454	5,751	6,076
Interest paid	- 18	- 1,036	- 1,476	- 1,419	- 1,290	- 1,136	-954
Interest received	-	38	160	160	160	160	160
Net interest	- 18	-998	- 1,316	- 1,259	- 1,130	-976	-794
PBT	2,252	2,980	3,570	3,923	4,324	4,775	5,283
Tax	-598	-814	-396	-392	-379	-374	-376
Tax rate	26.5%	27.3%	11.1%	10.0%	8.8%	7.8%	7.1%
Minorities	46	-370	-985	- 1,096	- 1,273	- 1,454	- 1,626
Net profit	1,700	1,796	2,059	2,435	2,672	2,948	3,281
Number of shares	100	100	100	100	100	100	100
EPS	17.0	18.0	20.6	24.3	26.7	29.5	32.8
Change	42.8%	5.6%	14.6%	18.2%	9.8%	10.3%	11.3%
DPS	10.0	10.8	12.4	14.6	16.0	17.7	19.7
Change	18%	8%	15%	18%	10%	10%	11%

Source: Company reports, HSBC estimates

Balance sheet summary (year-end December)

QARm	2006a	2007e	2008e	2009e	2010e	2011e	2012e
Intangible assets	354	17,532	17,532	17,532	17,532	17,532	17,532
Tangible assets	3,043	8,965	9,513	9,839	9,998	10,058	10,071
Investments	2,000	5,144	5,222	5,313	5,409	5,510	5,616
Fixed assets	5,396	31,642	32,266	32,684	32,939	33,100	33,218
Stocks	27	134	139	158	172	187	201
Debtors	962	2,062	2,086	2,179	2,253	2,324	2,397
Investments + cash	1,417	4,000	4,000	4,000	4,000	4,000	4,593
Current assets	2,405	6,196	6,224	6,337	6,425	6,510	7,191
Loans & borrowings	0	-3,224	-3,224	-3,224	-3,224	-3,224	-3,224
Other creditors	-1,957	-5,868	-5,865	-6,179	-6,375	-6,595	-6,855
Creditors < 1 year	-1,957	-9,092	-9,089	-9,404	-9,599	-9,819	-10,079
Net current assets	448	-2,896	-2,865	-3,066	-3,174	-3,308	-2,888
Assets less current liabs	5,845	28,745	29,401	29,618	29,765	29,792	30,331
Creditors > 1 year	766	18,216	17,054	15,200	13,006	10,400	8,000
Provisions	26	1,662	1,672	1,672	1,672	1,672	1,672
Minority interests	61	2,969	3,954	5,050	6,323	7,777	9,403
Equity shareholder funds	4,992	5,898	6,721	7,695	8,764	9,943	11,256
Total	5,845	28,745	29,401	29,618	29,765	29,792	30,331
Total assets	7,802	37,838	38,491	39,022	39,364	39,611	40,409

Source: Company reports, HSBC estimates

Cash flow summary (Year end December)

QARm	2006a	2007e	2008e	2009e	2010e	2011e	2012e
Op. profit excl depn + amort	2,773	5,262	6,574	7,088	7,405	7,714	8,034
C/f from operations	2,820	6,928	6,578	7,069	7,383	7,688	8,004
Interest + minority divs	-18	-998	-1,316	-1,259	-1,130	-976	-794
Tax	-598	-708	-497	-396	-392	-379	-374
Capex	-1,028	-1,740	-2,453	-2,324	-2,206	-2,124	-2,075
Investments net	-617	187	0	0	0	0	0
Intangibles net	0	-2,278	0	0	0	0	0
Capex + investment	-1,644	-3,813	-2,453	-2,324	-2,206	-2,124	-2,075
Subsidiaries bought	0	-12,938	0	0	0	0	0
Associates bought	-102	-2,693	0	0	0	0	0
Associates sold	0	0	0	0	0	0	0
Acquisitions + disposals	-102	-15,632	0	0	0	0	0
Dividends paid	-910	-1,065	-1,078	-1,235	-1,461	-1,603	-1,769
Net c/f pre financing	-451	-15,287	1,244	1,854	2,195	2,606	2,993
Loans new	75	17,341	0	0	0	0	0
Loans repaid	0	0	-1,162	-1,854	-2,195	-2,606	-2,400
Financing	75	17,341	-1,162	-1,854	-2,195	-2,606	-2,400
Change in cash	-229	2,210	82	0	0	0	593

Source: Company reports, HSBC estimates

Valuation

- ▶ DCF-based sum-of-the-parts leads to a target price of QAR295 per share
- ▶ We prefer Wataniya over Qtel, as Qtel ex Wataniya trades at a premium to its peers on lower growth forecasts
- ▶ We initiate coverage with a Neutral rating, based on a target price of QAR295, implying a potential total return of 5.4%

DCF-based SOTP is our preferred methodology

We use a DCF-based SOTP based on discounted cash flow to value each of Qtel's operations separately. We use discounted cash flow, as it best allows us to incorporate the imminent changes to the structure of the industry and to the competitive landscape.

Our SOTP analysis of Qtel gives us a fair equity value of QAR29.5bn or QAR295 per share. It implies a 2009e EV/EBITDA of 6.4x and PE of c12x. This is against an EBITDA CAGR for 2007-09e of 17.1% and earnings CAGR of 16.4%. However, this growth is inorganic, as Wataniya is not fully consolidated in the full-year 2007 numbers. If we look solely at the company's organic growth, ie Qatar and Oman, then the EBITDA CAGR for 2007-09e stands at 3.9%. While if we add Wataniya's operations for full year of 2007 then EBITDA CAGR (2007-09e) stands at 11.3%

Qatar and Kuwait constitutes 72% of the group's EV

Qatar wireless accounts for 35% of the group's EV, while wireline comprises 12% of the

valuation. Kuwait constitutes c25% of the group's value. Thus, our valuation is highly sensitive to the assumptions for these countries.

SOTP key assumptions

Operation	Cost of capital	Terminal growth rate
Qatar-Wireless	9.0%	2.5%
Qatar-Wireline	9.0%	1.5%
Oman	10.8%	3.0%
Iraq	23.0%	4.0%
Kuwait	10.8%	2.5%
Tunisia	10.5%	2.0%
Algeria	11.5%	3.0%
Maldives	10.5%	3.0%
Saudi Arabia	10.8%	3.0%
Palestine	18.0%	4.0%

Source: HSBC estimates

We use a WACC of 9% for Qatar based on a debt-to-asset ratio of 35% (derived from current debt divided by target EV). We also use an unlevered cost of equity of 11.05% for Qatar, derived from a risk-free rate of 5%, market risk premium of 5.5% for emerging markets and unlevered asset beta of 1.1x. This is based on an explicit forecast period to 2017, followed by a terminal growth rate ranging from 2.5% for wireless and 1.5% for wireline, depending on free cash flow growth in the last 3 years of free cash flow forecasts. Our SOTP valuation estimates are highly sensitive to the cost of capital and terminal growth rate assumptions.

Sum of the parts valuation summary for Qatar Telecom (in QARm)

Qtel sum of the parts valuation	Total EV	Qtel/Wataniya Holding	Subsidiary(S)/Joint Venture(J)	Qtel proportionate share	proportion of total operating EV	Method	Implied EV/Sales 2009e	Implied EV/EBITDA 2009e
Qatar-Wireless	18839	100%	S	18,839	35%	DCF	6.0	8.7
Qatar-Wireline	6331	100%	S	6,331	12%	DCF	4.3	9.2
Oman	4348	55%	S	4,348	8%	DCF	3.5	9.9
Iraq	3230	30%	J	969	2%	DCF	1.8	3.9
Kuwait	13175	100%	S	13,175	25%	DCF	4.1	8.9
Tunisia	8150	50%	J	4,075	8%	DCF	3.6	7.2
Algeria	6251	71%	S	6,251	12%	DCF	3.5	10.3
Maldives	164	100%	S	164	0%	DCF	3.1	17.7
Saudi Arabia	575	56%	S	575	1%	DCF	2.9	14.0
Palestine	365	57%	S	365	1%	DCF	2.5	N/A
Wataniya EV	28680	51%	S	24,605				
Wataniya Minorities	(2223)			(2223)	-4%			
Wataniya EV ex minority	26457			22,382				
Algeria direct 9% stake	6251	9%		563	1%			
Total EV	59204			53,431				
Group proportional net debt	(17441)			(17,441)				
Minorities	(12924)			(12924)				
Non Core assets	3270			3,270				
Equity value	32110			26,336				
Shares (fully diluted)	100			100				
Value per share	321			263.4				
12 months price target				295.4				

Source: HSBC estimates

The company is highly geared currently and we expect net debt at the end of 2007 to be at around QAR17.4bn. A minority of QAR12.9bn needs to be wiped out from the EV to arrive at our equity value of QAR26.3bn by the start of 2008. The minority is equal to the sum of 45% of the EV of Oman and 49% of the EV of Wataniya ex minorities.

Our valuation of Wataniya operations is based on our calculated EVs for each of its subsidiaries (for details refer to Wataniya Telecom initiation report published alongside this report. We use an average

of a SOTP value of KWD3.97 and a DCF value of KWD4.05 to derive our KWD4.00 target price).

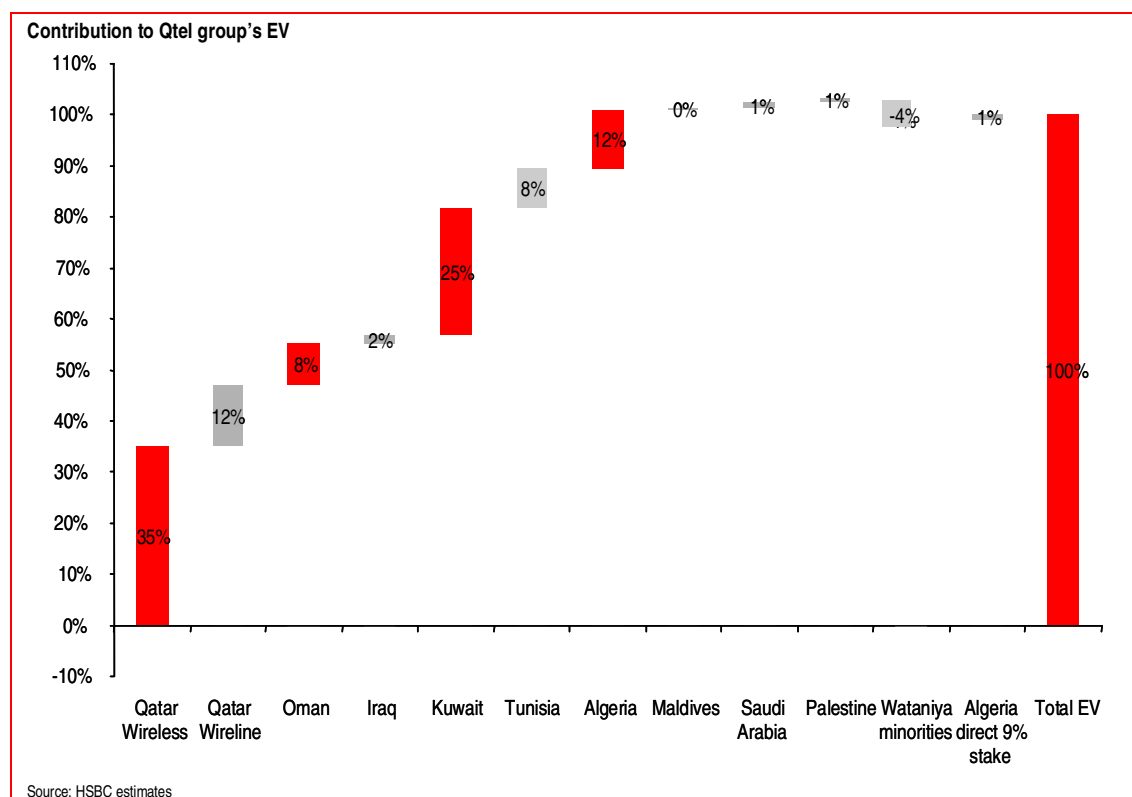
Associate valuation

The book value of Qtel's associates and investments stood at QAR2.486bn at the end of Q3 2007. Asia Mobile Holdings (25%) and NavLink (38%) are the investments in associates for Qtel. We have valued Indosat and Starhub based on their market capitalisation, since they are listed entities. We have assigned an EV/sub of USD250 for Qtel's Laos and Cambodian operations. Our implied valuation of these associates gives us a value of QAR3.27bn.

Investments in associates

Investments	effective stake	Trading status	Market value (in QARm)	Method of valuation	Qtel's share (QARm)
NavLink	38.2%	Unlisted		Book value	175.4
Indosat	10.3%	Listed	13,736	Market value	1,408
Starhub	12.3%	Listed	13,223	Market value	1,620
Laos	6.0%	Unlisted	738	Multiples (EV/subs)	44
Cambodia	12.3%	Unlisted	182	Multiples (EV/subs)	22
Total					3269.8

Source: HSBC estimates



Relative valuation – Qtel ex Wataniya looks expensive

We have assessed the effect of Wataniya on our valuation of Qtel. We subtracted the price paid for Wataniya (fully funded by debt) from Qtel's current EV to discover the effective EV of Qtel without Wataniya. We then derived the relative multiples of Qtel group ex Wataniya, which is effectively Qatar wireless and wireline and Qtel's operations in Iraq and Oman. When we compared the multiples to those of Wataniya, we found that Qtel ex Wataniya offers limited growth, while trading at higher multiples. We expect Qtel's EBITDA to grow at a compound annual rate of 11.3% versus c5.8% for Qtel ex Wataniya (2007-09e)

Another important factor to take into consideration is that we expect the growth of Wataniya to be more sustained than Qtel's. This is because Wataniya's operations in Algeria, the Maldives and Palestine should show higher growth rates in later years on account of margin expansion.

Qtel ex Wataniya does not look attractive...

Qtel's investment in Wataniya net of Iraq (in USDm)	3,600
Qtel's investment in Wataniya net of Iraq (in QARm)	12,981.6
Qtel's EV (in QARm)	45,441
Qtel's EV without Wataniya	32,459
Net debt of Qtel without Wataniya	4,459
Wataniya EV/EBITDA 2009e	6.9
Wataniya EBITDA CAGR (2007-09e)	15.30%
Qtel group EV/EBITDA 2009e	6.2
Qtel group EBITDA CAGR (2007-09e)	11.30%
Qtel ex Wataniya EV/EBITDA 2009e	7.9
Qtel ex Wataniya EBITDA CAGR (2007-09e)	5.80%

Source: HSBC estimates

As shown in the table below, Wataniya is expected to experience growth for a longer period of time than Qtel ex Wataniya. This is evident from the forward multiples of Wataniya Telecom, Qtel and Qtel ex Wataniya. We estimate the EBITDA CAGR over 2007-12 for Wataniya Telecom at 12.4%, Qtel at 7.3% and Qtel ex Wataniya at 2.8%, implying growth for Wataniya Telecom is more sustainable.

Wataniya's growth is coming in later years...Qtel ex Wataniya expected to remain flat

	EV/EBITDA						EBITDA CAGR(2007-12e)
	2007e	2008e	2009e	2010e	2011e	2012e	
Wataniya Telecom	9.8	8.5	6.9	5.8	5.0	4.3	12.4%
Qtel Group	9.1	6.9	6.2	5.6	5.0	4.4	7.30%
Qtel ex Wataniya	8.8	8.0	7.9	7.9	7.8	7.7	2.8%

Source: HSBC estimates

On account of this, we advise investors to Overweight Wataniya and be Neutral Qtel, as we think Wataniya offers better value and growth. Also, Qtel could suffer from the possibility that the Qatari market becomes saturated and our valuation of Qtel includes Wataniya at our implied target price.

We initiate on Qtel with a target price of QAR295, implying a potential upside of c5.4%, versus our Neutral band for non-volatile Qatari stocks of 5.3%-15.3% potential total return. Therefore, we rate the stock Neutral. Our valuation of Wataniya gives us a target price of KWD4.00 per share, implying 36.1% potential total return. Therefore, we rate the stock Overweight.

Valuation sensitivity

Since 35% of Qtel's value is coming from Qatar wireless, our valuation is highly sensitive to WACC and terminal growth rate assumptions, as shown in the table below. Our base-case assumption incorporates a WACC of 9% and a terminal growth rate of 2.5% for wireless.

Qtel's target price sensitivity to changes in WACC and terminal growth rate assumptions for Qatar wireless

WACC	Terminal growth rate				
	0.5%	1.5%	2.50%	3.50%	4.50%
7%	324.9	350.5	387.4	445.5	550
8%	292.2	309.5	333	367	420.4
9%	267.3	279.5	295.0	317	348.3
10%	247.7	256.6	267.7	282.4	302.3
11%	231.9	238.5	246.6	256.9	270.4

Source: HSBC estimates

Risks to our view

Downside risks to our rating for Qtel include:

- ▶ A better-than-expected competitive scenario in Qatar for both wireless and wireline.
- ▶ Our base-case numbers include a reduction in royalty to 12.5% in Qatar from 2008 onwards. The government has not yet announced this.
- ▶ The introduction of corporate taxes in Qatar might have a negative impact on Qtel's valuation.
- ▶ Overpayment for any future acquisitions.
- ▶ Competition in Kuwait could be worse than our base-case assumption for Wataniya. If STC manages to gain a higher market share or should an aggressive price war in the country start, then Qtel's ARPU and margins could be depressed. Since Kuwait constitutes c25% of our base-case valuation, we believe this scenario would have a material impact on our overall valuation.
- ▶ The privatisation of Algerie Telecom is important to our base-case assumptions. If Etisalat were to secure the bid, then it might lead to aggressive competition in the Algerian market.
- ▶ The conflict between Orascom Telecom and Wataniya in the Tunisian joint venture may lead to operational and management inefficiency at the Tunisian operations.

Upside risks to our rating include:

- ▶ An improvement in the situation in Iraq could lead us to upgrade our numbers. Currently, we incorporate a WACC of 23% for the Iraqi operations.
- ▶ The potential IPO of Nawras in Oman might unlock further value for the company. Currently Oman contributes around c8% to the group's value.

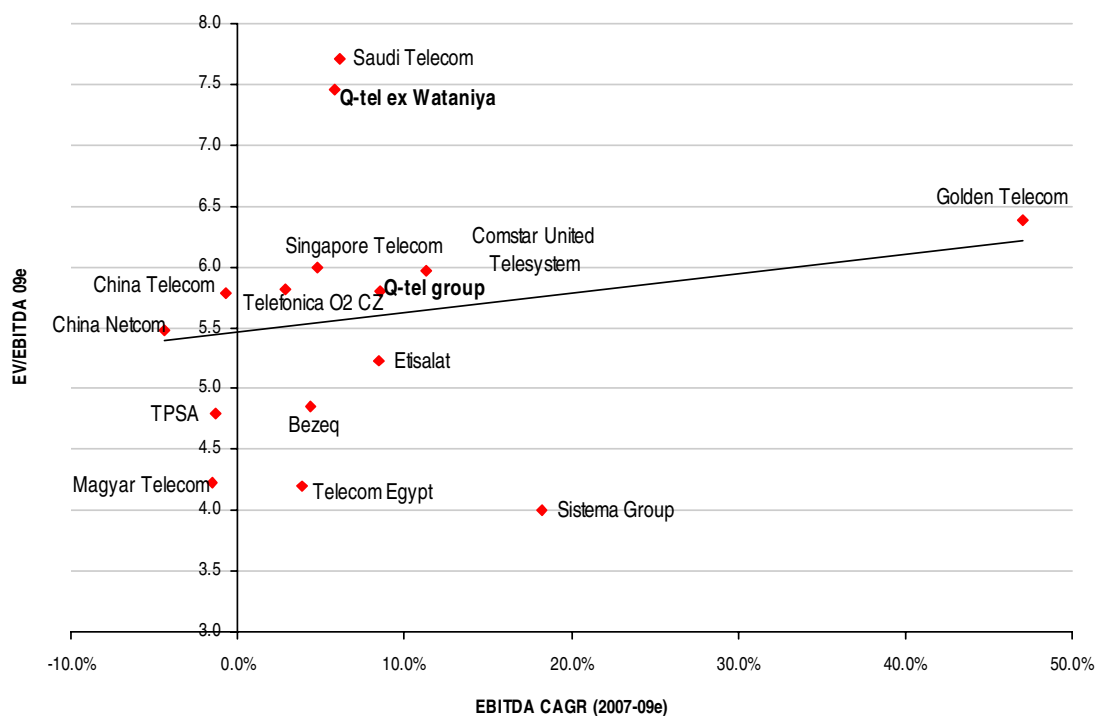
Risks to our view – Wataniya (OW, target KWD4.00)

- ▶ Competition in Kuwait could be worse than we currently expect. If STC managed to generate higher market share than we forecast, or if an aggressive price war took hold in the country, this could depress ARPU and margins. Given that Kuwait accounts for c54% of our base-case valuation, we believe this would have a material impact on the

overall valuation.

- ▶ The privatisation of Algerie Telecom is significant for our base-case assumptions. If Etisalat managed to secure the bid, this could lead to aggressive competition in the Algerian market.
- ▶ Any conflicts between Orascom Telecom and Wataniya in their management of the Tunisian JV could lead to operational and management inefficiency at Tunisiana.
- ▶ Political instability in the region could lead to a slowdown in the regional economies.
- ▶ Overpayment for any acquisition – either by Wataniya or by Qtel using Wataniya as acquisition vehicle – could be value dilutive for Wataniya's shareholders.

EV/EBITDA 2009e vs EBITDA CAGR (2007-09e) for EMEA/Asia diversified telcoms operators



Source: HSBC estimates

Qatar: close to saturation

- ▶ Highest GDP per capita in the region (USD60,000); strong rise in population is driving value and growth...
- ▶ ...but competition will bring change
- ▶ Qatar contributes c47% of Qtel's EV

Rich country – high GDP per capita

At current prices Qatar has the highest nominal GDP per capita of any GCC country (and one of the highest levels in the world). We expect the real GDP growth rate in Qatar to be the highest in the region for the next five years, followed by the UAE. Oil and gas contribute more than 60% of the country's GDP (85% of export earnings).

Furthermore, Qatar has proven natural gas reserves of more than 25 trillion cubic metres (15% of the world total) and its gas exports have grown substantially in recent times. In the past few years the government has undertaken an industrialisation programme that has increased foreign direct investment through the liberalisation of the economy; this has also contributed significantly to

the high GDP growth of recent times. The country's mobile ARPUs are now among the highest globally, at USD72 in 2006.

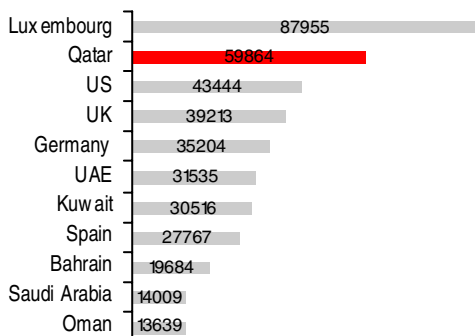
Monopoly in the region until late 2007

Until 2007, Qtel was the sole telecoms service provider in Qatar. Its monopoly recently ended in December 2007 when a second wireless licence was awarded to a Vodafone-led consortium.

Drivers of subscriber numbers

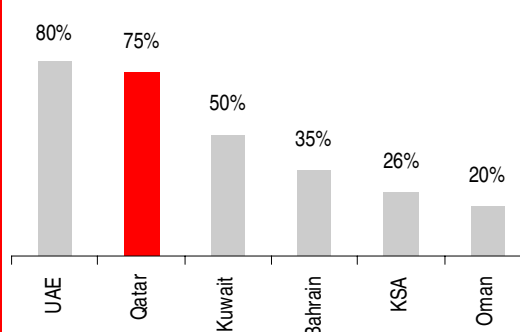
Qtel launched its wireless operations in 1994. Subscriber numbers grew only slowly until it introduced its pre-paid offers in 2000, after which, they grew at a CAGR of c43% to end 2006. Pre-paid now accounts for c82% of total subscribers to Qtel's Qatar operations.

GDP per capita (USD) – 2006



Source: HSBC estimates, ICT Qatar

High ratio of expats as a % of total population – 2006



Source: ICT Qatar

Population growth to boost wireless subscribers...

Qatar has one of the highest wireless penetration levels in the GCC region and future growth cannot, therefore, come from higher penetration levels alone. Rather, it will be driven mainly by high population growth and the large number of expatriates in the country. We expect the population to grow at a CAGR of 5.3% for the next 10 years, implying that it will double in that period – which represents a huge potential base for the mobile operators. Consequently, despite high mobile penetration in the region, Vodafone still has a huge future population base. Furthermore, around 24% of the population is under 14 years of age, implying good future growth potential for the telecoms services. The relatively young population implies that it will be easier for operators to launch more value-added services (VAS) and new technologies in the future.

...aided by a high proportion of expatriates

There is a large inflow of foreign nationals in Qatar. The high percentage of expatriates in Qatar (75%) implies that there will be strong demand for telecoms services for calls international telecoms services. In addition, it brings the double-SIM factor into the equation: since most

expatriates come for business purposes, they tend to have two connections, one for business and the other for personal use. We expect mobile penetration to reach c165% at the end of our forecast period, 2017e, up from c130% currently, mainly on the back of the high double-counting factor in the market.

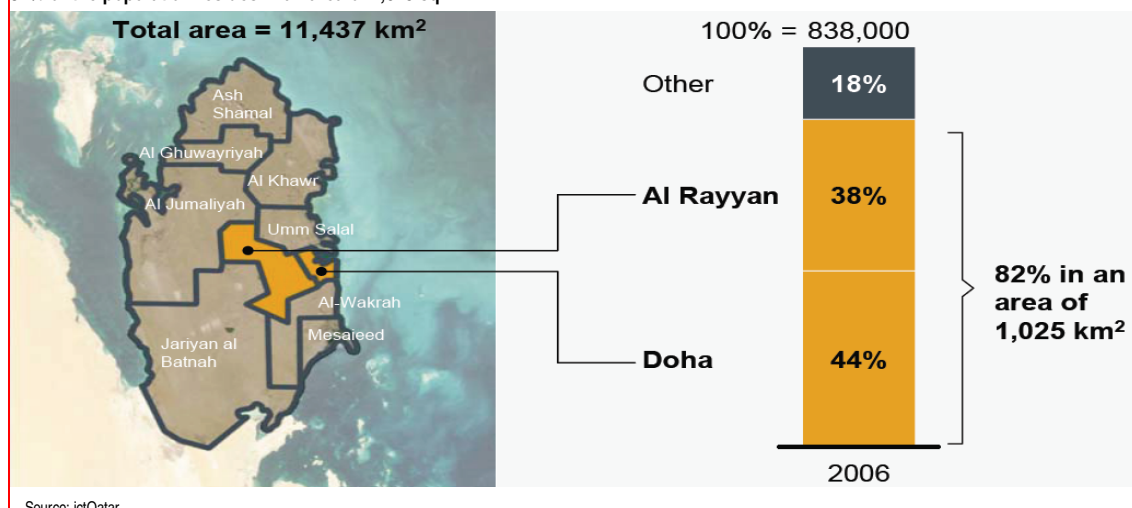
Looking at the double-counting factor in other markets, we saw that most of the markets are characterised by massive double counting of SIM cards. At its Milan Investor Day, (last year), Vodafone said that the ratio of SIMs to human users had reached 1.7x in Italy. A survey conducted by the Arab Advisor group in 2006 indicated that around 40% of cellular users in Saudi Arabia had more than one SIM card; we have adopted a slightly conservative view and estimate the double-counting factor there to be 1.3x, versus 1.25x in Oman and 1.5x in Jordan.

Here comes the competition

First it was wireless...

In December 2007, a consortium led by UK-based Vodafone Group won Qatar's second mobile network operating licence. Qtel will now face competition in its strongest market, which accounts for around 47% of its total EV.

82% of the population resides in an area of 1,025 sq km.



Vodafone has been aggressively expanding into emerging markets to generate growth, as the developed markets are reaching to saturation. We expect the entry of a new operator to further boost wireless penetration in the region, as prices are likely to come down and the two operators will introduce more customer-focused offers.

It may prove to be easier than expected for Vodafone to roll out operations in Qatar

Some 82% of Qatar's population inhabits two of its municipalities, Doha and Al Rayyan. With most of the population concentrated in an area of 1,025 km², we believe, it will take little time for Vodafone to build its network and bring a large chunk of population under its coverage area. This high concentration will also help it build and roll out its wireless services network rapidly, providing services to a large number of people. The speedy rollout of the network will also help Vodafone save on interconnection expense. We expect its market share to reach 45% in the next 10 years, with high growth in the initial period. The high expatriate population presents a good opportunity for Vodafone, which has operations in a large number of countries and will therefore be able to offer this client group competitive international rates. Vodafone's entry into the Indian market via the acquisition of the Hutch operations should enable it to generate substantial

roaming synergies, as a very high percentage of the total population in Qatar is Indian. The company also won the country's international gateway licence, which is likely to further dampen Qtel's revenue stream.

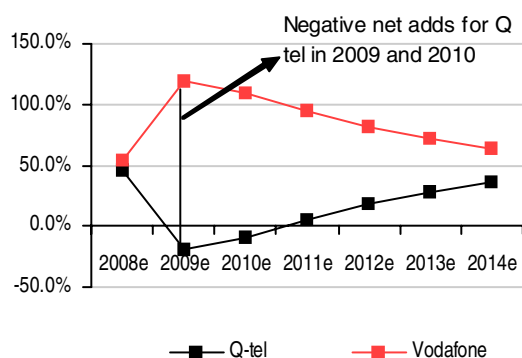
We believe competition from Vodafone poses more of a threat to Qtel than the entry of a regional operator, for the following reasons:

- ▶ since 82% of population resides in two cities, network rollout will be relatively rapid, causing Qtel to lose out on prospective infrastructure-sharing revenues early on.
- ▶ roaming synergies related to the country's high expat population could help Vodafone, whose operations range from developed markets in the west to the recently acquired Hutch operations in India – a crucial factor, since most expats in Qatar are Indian;
- ▶ Vodafone also won the international gateway licence, which will eat into Qtel's international interconnect revenues.

Now it's the turn of wireline

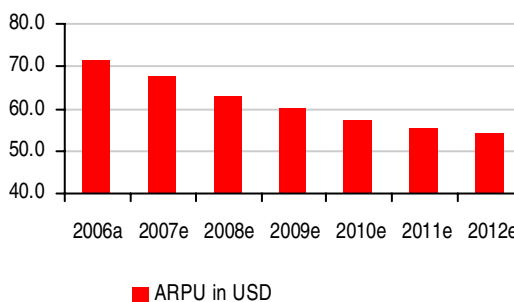
Qtel's monopoly in Qatar's fixed-line market is set to end in 2008. The telecoms regulator, ictQatar, has launched an auction for the country's second fixed-line network operating licence, to be awarded in April 2008, and five parties have

Share of net adds in wireless space in Qatar



Source: HSBC estimates

ARPU dilution in wireless – we expect ARPU to reach USD54 by 2012e



Source: HSBC estimates

already shown interest. The licence will cost a fixed fee of QAR10m (USD2.75m), and will allow the winning bidder to provide facilities-based domestic and international services, including authorisation to operate an international gateway. Factoring in the future competition in the fixed-line business, we expect Qtel's wireline market share to drop to 65% at the end of our explicit forecast period, ie 2017e.

Fixed voice reaching saturation...

Fixed-line penetration is higher in Qatar than in other GCC countries. We believe future growth in the telecoms sector will mainly come from wireless as the fixed-line market is saturated. Fixed penetration currently stands at 27% of the population and we believe it will reach to 26% in the next 10 years. We expect it to decline with fixed to mobile substitution (F2M), but believe total fixed-line subscribers will continue to grow, mainly on the back of population growth and higher demand from the corporate segment (which accounts for c30% of fixed-line connections). One major growth factor for this business will be a sharp rise in broadband subscriptions. As broadband penetration increases, people will require more fixed-line connections – a prerequisite for obtaining an internet connection in the region. ictQatar expects broadband subscriptions to increase at a CAGR of 26% during the five-year

period from 2007 to 2011.

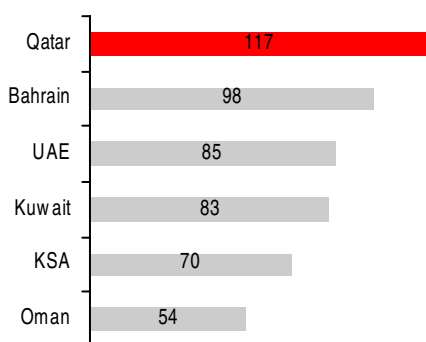
At the same time, the high proportion of expatriates means that the new fixed-line operator is likely to target the international long-distance segment aggressively. This will put pressure on the price per minute for Qtel's international long-distance business, which accounts for the majority of its fixed-line business, as its fixed-line-to-fixed-line calls are currently free.

Internet and data services

According to ictQatar, household internet penetration (total internet accounts including both dial-up and broadband divided by the number of households) was 53% at end-2006. In the same period, its neighbouring state, Kuwait, had internet penetration of 82%, implying that more scope for growth in data services remains in Qatar. As the voice business approaches saturation, the data segment will become the driver of future revenues (see *Data Accelerator*, published in May 2007). Data revenues are generally higher than voice revenues on a per-minute basis, so higher data usage will help drive the future ARPUs of Qatar's telecoms operators.

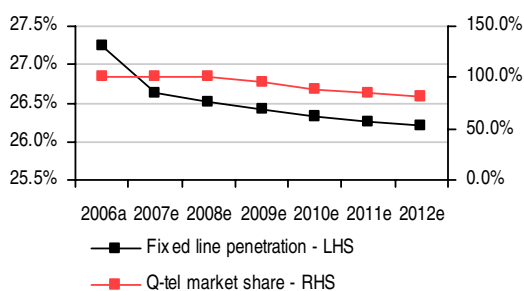
Internet accounts grew at a CAGR of 39% during the 2001-06 period (rising to 70,000 at end-2006) and the number of personal computers grew at a CAGR of 7% during the same period (to 140,000 at end-2006). Qatar's internet – and especially its

Fixed-line penetration per household in GCC in 2006



Source: ictQatar

Fixed-line penetration as a % of population and Qtel's market share



Source: HSBCestimates

broadband – penetration is lower than in some other developed countries. Potential growth in penetration will play a critical role in offsetting the negative impact of competition on ARPUs.

ictQatar is taking various steps to increase internet (and particularly broadband) usage in the country. Its initiatives include encouraging the new player in the fixed-line market to introduce WiMAX broadband services, and it is ready to allocate the appropriate wireless frequencies. Qtel already has WiMAX frequencies, and rolled out WiMAX services during the Asian Games in Doha in December 2006. With the introduction of competition in the fixed-line market, we expect monthly DSL subscription rates to fall from current levels, which are well above the international average. The monthly rate for a 512kbps DSL subscription in Qatar last year was nearly USD55, which is considerably higher than the EU average of USD25. According to ictQatar, broadband subscriptions are set to increase at a CAGR of 26% during the five-year period 2007-11e.

3.5G arrives

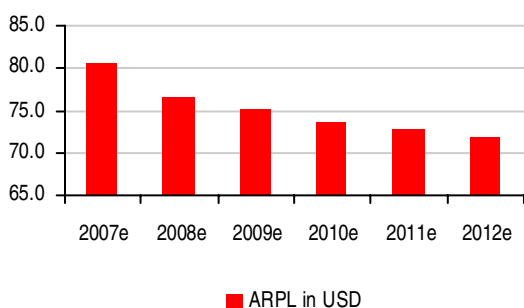
We believe higher internet and data usage will be helped by the deployment of 3.5G HSDPA technology, which is expected to be commercially available from H1 2008. Currently Qtel offers a full range of 2G and 2.5G (fully GPRS- and mostly EDGE-enabled) services on a nationwide scale. Its 3G coverage zone also covers the

majority of Qatar's population. Deployment of 3.5G HSDPA will take the market to the next level of technology and help increase regional internet and data usage.

Pricing pressure to continue

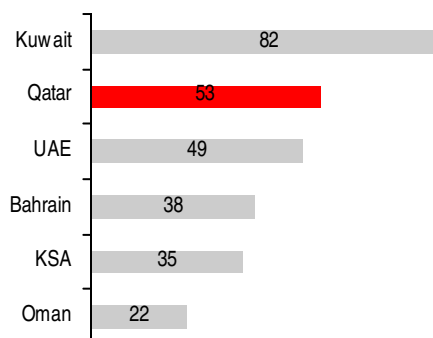
Mobile tariffs in Qatar are among the highest in the region in terms of per-minute call and connection fees. In the pre-paid segment, the average mobile tariff currently stands at USD0.15 per minute in Qatar compared with averages of USD0.08 in the UAE and USD0.13 in the GCC. In the post-paid segment it stands at USD0.10 per minute, the highest rate in the GCC. The connection fee is the highest in the region in both the pre-paid and post-paid segments, at USD50 and USD70, respectively.

ARPL for fixed line to remain stable



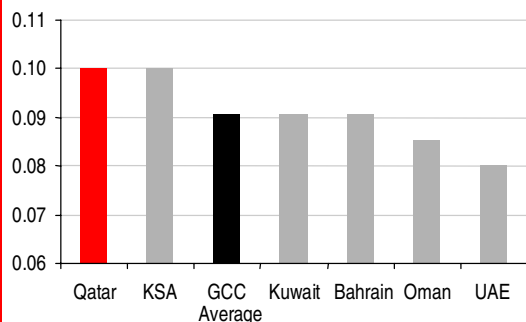
Source: HSBC estimates

Internet penetration as a % of households in 2006



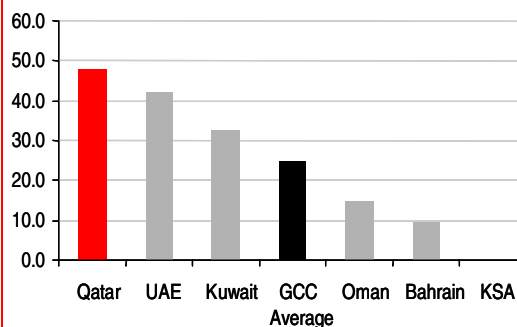
Source: ictQatar

Average post-paid tariff in USD per minute in 2006



Source: Note: average published tariffs for basic post-paid plans in each country (excluding special and promotional offers)
Source: Saudi Arabian telecoms regulator (CITC).

Average connection fees in USD for pre-paid mobile service in 2006



NOTE: Average of basic pre-paid offers by all operators in each country (does not include special and promotional offers)
Source: Saudi Arabian telecoms regulator (CITC);

We believe the monopolistic market is among the key reasons for high connection fees in Qatar and, previously, the UAE. Although we do not expect a price war in Qatar post liberalisation, we do expect some pricing pressure to continue in the country, further diluting the ARPU. We do not believe price elasticity in Qatar is high as it is a rich country, so any reduction in prices might not necessarily be offset by an increase in minutes of usage (MOU) to same extent as in other, less wealthy, countries.

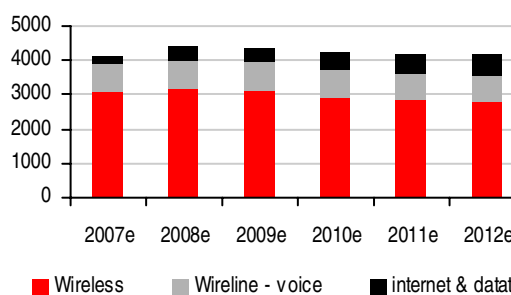
EBITDA margins

Qtel's Qatar operation has high EBITDA margins (c69% for the first nine months of 2007), which we expect to come under pressure with the entry of competition. We do not expect Vodafone to adopt an irrational approach and embark on a price war – which would increase the SAC for both companies. Rather, we believe product differentiation and quality of service will be the key considerations in the Qatari markets. We expect EBITDA margins to decline in response to competition, falling from c75% to c67% in wireless and from 48% to c46% in wireline by 2012e.

Forecasts and valuation

We expect negative revenue growth in wireless over the next five years as a result of competition and pressure on ARPU. We project that revenue will decline at a CAGR of c1.8% in the 2007-12 period. However, we expect a c5% CAGR (2007-12) in the wireline segment, driven by the data and internet segment, which we believe will post growth at a 2007-12 CAGR of 18.9%, whereas the wireline voice segment looks set to decline by c1.7% during the same period. Overall we expect revenues in Qatar to remain flat over the next five years.

Revenue breakdown in Qatar (in QARm)



Source: HSBC estimates

Qatar Wireless Sum-of-the-parts valuation summary

In QARm	2008e	2009e	2010e	2011e	2012e	2013e	2014e	2015e	2016e	2017e
EBITDA	2,293	2,174	2,009	1,911	1,867	1,863	1,891	1,943	2,015	2,104
Less: Depreciation	-251	-285	-308	-323	-332	-337	-341	-343	-346	-349
Pre Tax NOPLAT	2,042	1,890	1,701	1,588	1,535	1,526	1,550	1,600	1,669	1,755
Tax 12.5%	255	236	213	198	192	191	194	200	209	219
NOPLAT	1,787	1,654	1,488	1,389	1,343	1,335	1,357	1,400	1,461	1,536
Depreciation	-251	-285	-308	-323	-332	-337	-341	-343	-346	-349
Capex	-567	-508	-446	-406	-382	-370	-365	-367	-374	-385
Free cash flow	1,471	1,431	1,350	1,306	1,293	1,303	1,332	1,376	1,432	1,499
Terminal Value										23646
Terminal Growth Rate 2.5%										
Discount Rate 9.0%										
Discount Factors	0.92	0.84	0.77	0.71	0.65	0.60	0.55	0.50	0.46	0.42
PV of Cash Flow	1349.5	1204.1	1042.8	925.3	840.2	776.9	728.5	690.4	659.4	633.4
PV of continuing Value	9988									
Enterprise Value	18839									
Implied EV/EBITDA	8.2	8.7	9.4	9.9	10.1	10.1	10.0	9.7	9.3	9.0

Source: HSBC estimates

SOTP valuation

We have assumed that royalties in Qatar will fall from the current level of 25% to c12.5% of pre-tax profits from 2008 onwards – mainly owing to the introduction of competition. In addition a licence fee equivalent to c1% of net revenue is payable to the government, and we have adjusted our EBITDA margin calculations accordingly. Qatar is Qtel's most important market, accounting for c47% of EV (c35% from wireless and c12% from wireline). Our

SOTP valuation method incorporates a WACC of c9% as well as terminal growth rates of 2.5% in wireless and 1.5% in wireline.

Qatar Wireline Sum-of-the-parts valuation summary

In QAR m	2008e	2009e	2010e	2011e	2012e	2013e	2014e	2015e	2016e	2017e
EBITDA	641	692	724	741	759	780	803	830	860	892
Less: Depreciation	-136	-151	-164	-176	-186	-194	-201	-206	-211	-215
Pre Tax NOPLAT	505	541	560	565	573	586	603	624	649	677
Tax 12.5%	63	68	70	71	72	73	75	78	81	85
NOPLAT	442	473	490	494	502	513	527	546	568	592
Depreciation	-136	-151	-164	-176	-186	-194	-201	-206	-211	-215
Capex	-237	-235	-230	-221	-215	-212	-210	-211	-213	-216
Free cash flow	342	389	424	449	472	495	518	541	566	591
Terminal Value										7999
Terminal Growth Rate 1.5%										
Discount Rate 9.0%										
Discount Factors	0.92	0.84	0.77	0.71	0.65	0.60	0.55	0.50	0.46	0.42
PV of Cash Flow	313.5	327.0	327.4	317.9	306.7	294.9	283.1	271.6	260.5	249.7
PV of continuing Value	3379									
Enterprise Value	6331									
Implied EV/EBITDA	9.9	9.2	8.7	8.5	8.3	8.1	7.9	7.6	7.4	7.1

Source: HSBC estimates

Qatar – KPIs and P&L summary

In QAR mn	2006a	2007e	2008e	2009e	2010e	2011e	2012e
Population ('000)	838	880	924	973	1,024	1,077	1,134
Wireless Penetration	110%	130%	137%	142%	147%	150%	153%
Wireless Market subs('000)	920	1,146	1,263	1,384	1,503	1,621	1,739
Qtel Market share	100%	100%	95%	85%	78%	72%	69%
Qtel wireless subs('000)	920	1,146	1,200	1,177	1,165	1,171	1,193
Wireless ARPU in QAR	261	246	229	219	209	201	197
Change	3%	-6%	-7%	-4%	-5%	-3%	-2%
Wireless ARPU in USD	72	68	63	60	57	55	54
Wireless Revenue	2,563	3,055	3,224	3,120	2,930	2,824	2,789
Wireless EBITDA	1,926	2,227	2,293	2,174	2,009	1,911	1,867
EBITDA Margins	75%	73%	71%	70%	69%	68%	67%
Wireless Capex	-546	-588	-567	-508	-446	-406	-382
Capex/Sales	21%	19%	18%	16%	15%	14%	14%
Wireline penetration	27.2%	26.6%	26.5%	26.4%	26.3%	26.3%	26.2%
Wireline Market subs('000)	228	234	245	244	240	238	239
Market share	100%	100%	100%	95%	89%	84%	80%
Wireline Revenues	1,388	1,299	1,369	1,487	1,567	1,612	1,658
Wireline EBITDA	665	615	641	692	724	741	759
EBITDA Margins	48%	47%	47%	46%	46%	46%	46%
Wireline Capex	-297	-248	-237	-235	-230	-221	-215
Capex/Sales	21%	19%	17%	16%	15%	14%	13%

Source: HSBC estimates

Oman – growth story

- ▶ Least penetrated market in GCC, with inactivity level estimated at 1.25x by the regulator, suggesting further growth potential
- ▶ Qtel owns 55% of Nawras, which gained a c40% market share in its three years of operation
- ▶ Contributes c8% to our valuation of Qtel; royalty reduction has added to the overall valuation; proposed IPO in 2008 could unlock further value for the group

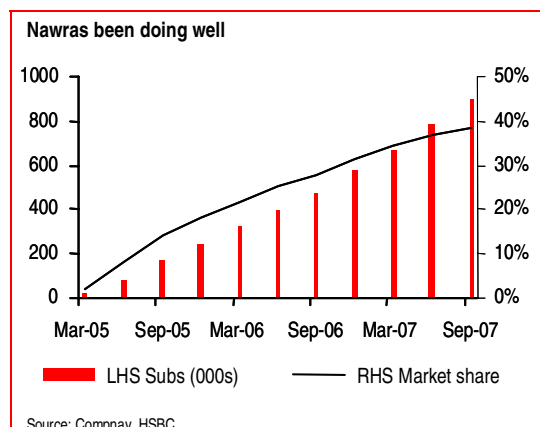
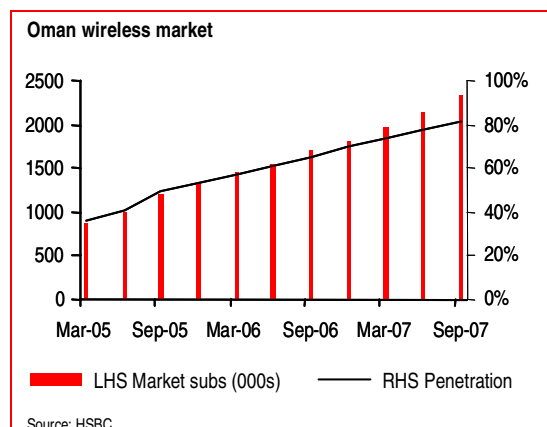
Telecommunications in Oman

Wireless subscriber boom

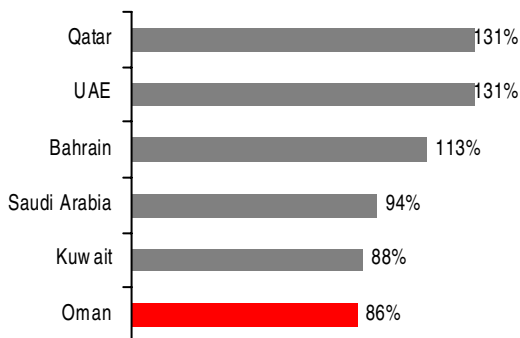
The Oman market is a duopoly between incumbent, Omantel's subsidiary, Oman Mobile, and Qtel's subsidiary, Nawras. The Omani government invited bids for the country's second mobile licence in January 2004. The government short-listed six firms from the 10 bidders. Qtel's consortium was the winning bidder (OMR40m). Nawras is 55%-owned by Qtel, 15% by Danish company TDC and 30% by Omani investors.

Mousbak is Nawras' pre-paid package, while its

post-paid package is called Ajel. More than 90% of its customers are on pre-paid contracts. After the entry of Nawras (Qatari Omani mobile company), the Oman market has seen huge growth in the wireless sector. Penetration has reached 82% (c30% before Nawras started its operations) and subscriber has grown by a compound annual rate of 70% over the same period. Nawras has captured a market share of c40% in its three years of operation. Its growth was helped by the introduction of mobile number portability (MNP) in August 2006. We expect Nawras to gain a market share of c47% by 2012.

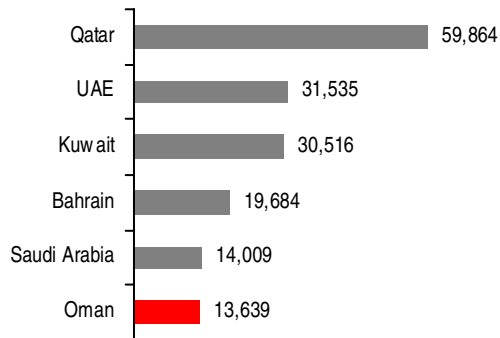


Low wireless penetration means growth potential 2007



Source: HSBC 2007 estimates

But at the same time low GDP per capita (USD) 2006



Source: HSBC estimates

Mobile penetration in Oman to catch up with its peers

We forecast 106% mobile penetration by 2010e in Oman. Mobile penetration in the GCC region already exceeds 100% in three countries (Qatar, Bahrain and UAE), owing to the double SIM-card phenomena as SIM-card penetration has now surpassed human penetration (please refer to our thematic report, *Oh Behave*, September 2005). The double-counting factor varies between 1.3x in Saudi Arabia and 1.5x in Jordan, and results in declining tariffs, special offers and promotions by mobile operators targeting the pre-paid segment, which encourages subscribers to switch to different networks. The Omani telecom regulator recently announced that the level of inactive subscribers out of the total subs market stands at 25%, which implies real human penetration of 52.5% versus SIM-card penetration of 70% as at end-December 2006.

Mobile penetration in Oman lags behind other GCC markets. Given the GCC's high GDP per capita and the presence of at least two operators in each country, we believe average mobile penetration in the region could follow the example set by Bahrain, Qatar and the UAE (whose mobile penetration was between 113% and 119% at end-2006) and exceed 100%. The current high mobile penetration in the three countries can be attributed to their high GDP per capita, as is the case in

Bahrain, and the large number of expatriates as a percentage of the population, 80% on average in the UAE and 75% in Qatar. Based on our forecasts for the remaining three markets (Saudi Arabia, Oman and Kuwait), we expect mobile penetration to cross over 100% by 2009e.

The main drivers for our subscriber growth forecast in Oman are declining tariffs (because of increasing competition and market liberalisation), falling handset prices and growing disposable incomes, which is a function of the domestic economies' growth.

Entry of MVNOs to boost growth further

Oman's TRA is inviting applicants to bid for licences to re-sell basic public mobile communication services in the country. This will enable the existing operators to better utilise their networks and will provide a source of additional income. MVNOs (Mobile Virtual Network Operators) or resellers buy airtime from existing operators (who have their own network, Omantel and Nawras in Oman) at wholesale rates, then reselling them at retail rates. Also the entry of MVNOs to a market generally lead to additional consumer-centric offers and accelerate wireless penetration.

ARPUs are set to improve ...

Nawras has seen its ARPUs decline from cQAR130 (USD36) to cQAR88 (USD24) during its three years of operations. This is around a c40% discount to the

incumbent Omantel on account of pre-paid post-paid user mix differential. Already ARPUs have begun to stabilise and are expected to grow in future mainly on back of higher internet and data usage. Data services usually have higher ARPUs than do voice services, and with the market becoming more mature, it is expected that the proportion of data revenues to total revenues is going to increase.

... given technological superiority

Nawras has launched third generation (3G W-CDMA) services in Oman. This will allow Nawras to provide high-speed mobile internet access to its customers. It has also made headway in offering 3.5G (HSDPA) services in Oman. This should also strengthen its technological superiority over Omantel, which currently operates 2.5G services in Oman (although Omantel has started offering blackberry mobile in association with Research in Motion, RIM).

Oman still lags behind other GCC countries in terms of technological evolution and we believe this represents an opportunity for both the mobile operators to improve their ARPUs in future, through increased usage of data services among subscribers. For this, they will need to invest more in technology and infrastructure.

EBITDA margins

EBITDA margins for Nawras have been increasing and we expect margins to reach c42% by 2012.

As Nawras' operations mature (and costs decline as a percentage of sales, as a result), we expect EBITDA margins are expected to improve significantly in the next few years.

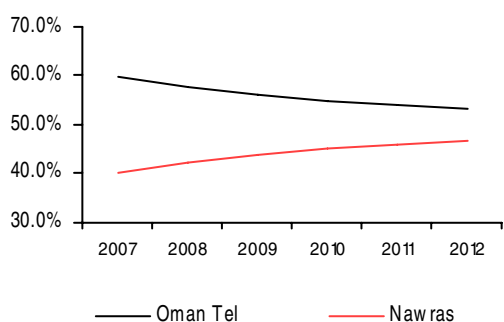
Regulatory environment

The liberalisation of the Omani telcoms sector is mandated by the commitments given by the government to the WTO.

Following the issuance of the second mobile licence, the TRA has announced its intention to issue a licence to provide fixed-line services, long-distance and international carriage and to set up an additional public data network. Oman Mobile and Nawras have an exclusivity period for three years, which is due to end on 19 February 2008. So far we haven't heard of any plans from the TRA with regard to issuing a new mobile licence. The country's mobile licences oblige the operator to pay an annual royalty of 12% of gross revenues to the government. The government has recently announced that it will be cut to a 7% flat rate from 2008 onwards.

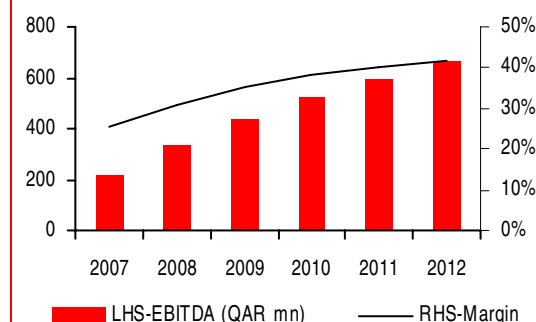
We believe there is regulatory risk for the existing operators, as the terms of the mobile licences state that the TRA may modify the licence, should it be in the public interest. However, the licences may not be modified within three years of their issuance or last modification.

Nawras to gain c47% market share by 2012



Source: HSBC

Margins to improve in the next few years



Source: HSBC

Forecasts and valuation

Oman is a growth story for Qtel and adds c8% to the group's valuation, on our estimates. We expect revenues to grow at a compound annual rate over 2007-12e of c13.1%, adding 9% to Qtel's revenue by 2012e. However, the key factor remains Nawras' margin expansion, which we expect should go up to around c42% from 26% currently. As the operations mature, we expect margin expansion on account of lower SAC, higher on net calls (on account of higher market share), fixed costs getting absorbed on higher revenue numbers. Nawras currently doesn't have its own international gateway, but we expect this to change in near future, and for it to have a further positive impact on EBITDA margins.

Our SOTP valuation for Qtel's operations in Oman results in an EV of QAR4,348m for the 100% of the Omani operations. We use a cost of capital of 10.8% and a terminal growth rate of 3%.

Are we conservative in our valuation for Nawras?

We compared our valuation for Nawras with the implied valuation of the mobile segment for Omantel based on our target price of OMR2.26 for Omantel. We believe around c60% of Omantel's value comes from its mobile segment.

Hence, the implied valuation for Omantel mobile segment comes to around USD2.6bn.

Our valuation of Nawras implies a one-year forward EV of USD1.3bn. We believe this discount for Nawras compared with mobile division of Omantel is justified for the following reasons:

Nawras valuation comparison to Omantel mobile valuation

Omantel EV based on our target price (in Omani riyal)	1,696.0
Omantel EV based on our target price (in USD)	4,412.0
Omantel Mobile – 60% of EV (in USD)	2,647.2
Nawras EV for 100% in USD	1,312.7

Source: HSBC estimates

- ▶ ARPU for Omantel mobile was around USD38 at the end of 2006 and we expect it remain at around USD39 during our forecast period. Nawras' ARPU was c32% below that of Omantel at around USD26 by the end of 2006 and we expect it to remain stable at USD25, implying a 35% discount to Omantel over our forecast period. This is mainly on account of better quality customers that the incumbent enjoys, which is evident from the pre-paid/post-paid mix. Omantel has around 22% of subs at post-paid compared with 7% for Nawras.

Omani operations – SOTP valuation summary

In QARm	2008e	2009e	2010e	2011e	2012e	2013e	2014e	2015e	2016e	2017e
EBITDA	340	441	524	600	666	725	780	831	881	930
Less: depreciation	-137	-157	-173	-185	-193	-200	-204	-208	-211	-214
Pre-tax NOPLAT	203	284	351	415	473	526	576	623	670	716
Tax 7.0%	77	88	96	105	112	119	126	133	140	147
NOPLAT	126	196	255	311	361	407	450	491	530	569
Depreciation	-137	-157	-173	-185	-193	-200	-204	-208	-211	-214
Capex	-270	-253	-236	-224	-216	-212	-211	-212	-216	-222
Free cash flow	-7	100	192	272	338	395	443	486	525	562
Terminal value										7467
Terminal growth rate 3.0%										
Discount rate 10.8%										
Discount factors	0.90	0.82	0.74	0.66	0.60	0.54	0.49	0.44	0.40	0.36
PV of cash flow	-6.4	81.5	141.7	180.6	203.0	213.9	216.9	214.8	209.6	202.4
PV of continuing value	2690									
Enterprise value	4,348									
Implied EV/EBITDA	12.8	9.9	8.3	7.2	6.5	6.0	5.6	5.2	4.9	4.7

Source: HSBC estimates

- ▶ Unlike Nawras, Omantel owns its own international gateway, thus saving on international interconnect expenses.
- ▶ We expect the EBITDA margins of Nawras are expected to be around 44% in the long run compared with 50% for Omantel, which includes wireline.
- ▶ Upside potential to our valuation includes the possibility of an IPO of Nawras, later in 2008, which might unlock value for Nawras and so for Qtel.

Nawras KPIs and P&L summary

In QARm	2006a	2007e	2008e	2009e	2010e	2011e	2012e
Population ('000)	2600	2672	2745	2820	2898	2978	3060
growth	3.6%	2.8%	2.8%	2.8%	2.8%	2.8%	2.7%
Penetration (%)	70%	86%	95%	101%	106%	109%	112%
Market subs	1,818	2,297	2,594	2,845	3,062	3,253	3,425
Change	36.4%	26.4%	12.9%	9.7%	7.6%	6.2%	5.3%
Net adds ('000)	485	479	297	251	217	191	172
Oman Tel market share	68.5%	60.0%	57.6%	55.9%	54.7%	53.9%	53.3%
Nawras market Share	31.5%	40.0%	42.4%	44.1%	45.3%	46.1%	46.7%
Nawras subs ('000)	572	919	1,120	1,254	1,386	1,499	1,598
Net adds	328	347	201	134	132	113	99
% fo total							
Post-paid	4.0%	7.0%	6.6%	6.3%	6.0%	5.8%	5.7%
Pre-paid	96.0%	93.0%	93.4%	93.7%	94.0%	94.2%	94.3%
Implied ARPU (QAR)	96	97	90	88	87	86	86
Change	1.9%	0.7%	-6.6%	-2.2%	-1.4%	-0.7%	-0.2%
Implied ARPU (USD)	26	27	25	24	24	24	24
Revenue	470	864	1103	1257	1378	1495	1602
Change	240.7%	83.9%	27.8%	13.9%	9.6%	8.5%	7.1%
EBITDA	36	220	340	441	524	600	666
Margins	7.7%	25.5%	30.8%	35.1%	38.1%	40.1%	41.6%
Change		511.5%	54.6%	29.6%	18.9%	14.4%	11.0%
Capex	-186	-265	-270	-253	-236	-224	-216
Capex as a % of sales	40%	31%	24%	20%	17%	15%	13%

Source: HSBC estimates

Iraq – important, but not adding value

- ▶ Qtel holds 29.9% in the operations via holding in Asiacell communications
- ▶ Zain is the dominant player in the market, with a 65% market share
- ▶ Qtel's Iraqi operations contribute only c2% to the group's valuation, mainly on account of the country's higher discount rate

Who's in, who's out in wireless?

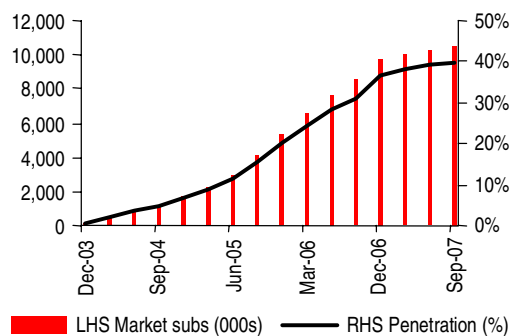
In 2003, three regional mobile licences were issued in Iraq to Asiacell in northern Iraq, Orascom Telecom (branded Iraqna) in central Iraq (including the capital city of Baghdad) and MTC Atheer Telecommunications in southern Iraq. A tender of national licences was planned for December 2005, but the deadline was missed. In December 2006, Orascom Telecom and MTC were awarded a temporary extension on

operations, but Asiacell wasn't. The national level licences were finally sold in August 2007 for USD1.25bn to Asiacell, Zain and Korek Telecom.

In the following months, Qtel bought a 29.9% stake in Asiacell operations. Also, Orascom Telecom was planning to form a joint venture with Korek Telecom, which was also awarded a licence.

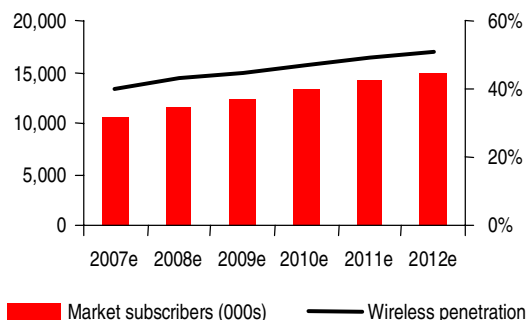
Now Zain is operating in the central and southern regions and Qtel is operating in northern area of Iraq. Both have national level licences to operate

Huge subscriber growth in recent time



Source: Company reports

...but subscriber growth to slow down unless operators start national level services



Source: HSBC estimates

wireless services. Zain, now, commands a market share of 65%, with a subscriber base of around 7 million. The rest of the market is covered by Qtel.

Economy

Iraq's economy is dominated by the oil sector, which has historically provided c95% of its foreign exchange earnings. There was drop in oil exports because of the war, but exports have now picked up and are back to pre-war levels. Iraq has a young population, with c40% estimated to be below 15 years of age. The overall population is expected to grow by c2.6% during 2007 (source: *CIA Factbook*).

High-growth market

The Iraq war led to a widespread disruption of communication services in the country. The Coalition Provisional Authority took control of the communications sector in Iraq in 2003 before passing on control to the newly formed Communications and Media Commission in 2004. Since the first three telecoms licences were issued in 2003, Iraq has seen phenomenal growth in subscriber numbers, which passed the 10 million mark in 2007. Mobile Penetration levels stood at 37% as at end-2006.

Now players have national level licences, they will try to expand their wireless coverage and thus competition is set to rise. This should provide impetus to the telecoms market in Iraq. However,

in case they do not expand their network to national level and the status quo is maintained then wireless growth may not be as strong as it has been in past. Operating at a regional level means neither operator has to worry about competition, but equally the potential for wireless services is not fully realised.

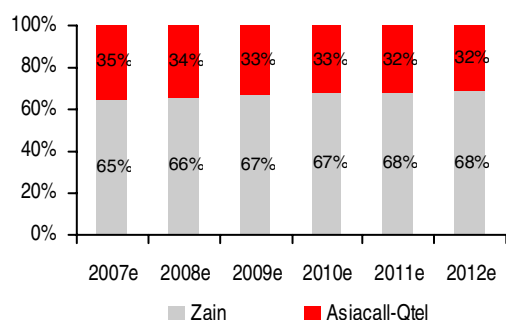
Also, the high growth of the Iraq market should to continue given the young population, which bodes well for future growth of telecom market in Iraq. We expect wireless penetration to reach 51% by 2012.

It's going to be a tough road

Expansion is the only option

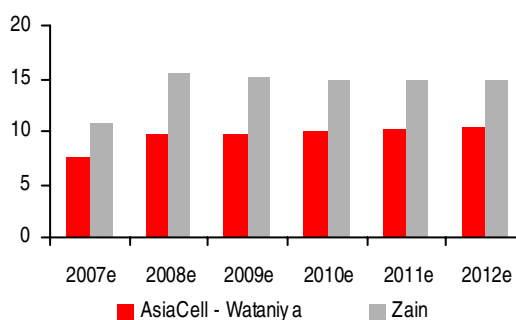
The Iraq market may prove to be a tough one for Qtel. With Zain in the dominant position, covering a large geographical area (Zain currently covers almost all of the major population centres of Iraq), it's probable that it would like to expand into the northern market to grow its base and coverage. We think Qtel will now have to expand fast to cover a larger area. It paid USD1.25bn for a national level licence and to get the required return on the investment it has no option but to expand, we believe. We expect Zain to consolidate its position further and emerge as an even stronger player in the market. This is mainly on the back of synergies that Zain should generate through its Iraqna operations. The synergies will include lower staff and security costs, better pricing flexibility and better service to the customers.

Market share- Zain to consolidate position



Source: HSBC estimates

ARPU differential between Zain and Asiacell – lot to catch up...



Source: HSBC estimates

Lower ARPUs than its competitor

The ARPUs of Qtel are lower than Zain's (USD10 versus USD13 during Q3 2007). Qtel controls the northern region whereas Zain has the central and southern regions. The main reason for Qtel's lower ARPU is that the northern region does not include many major population hubs, so revenues are poorer as a consequence. It is not just important for Qtel to expand fast and grow its subscriber base, but also to improve its ARPU, which can either be done by having a more favourable post-paid to pre-paid proportion or by pushing value-added services (content and data), which generate higher ARPUs than voice.

Margins to remain stable

We expect margins to remain at the current levels. EBITDA margins are currently at c49% and we expect them to fall to c48% in the long run by 2016e

Forecasts and valuation

Qtel holds around c30% of Asiacell. However, the numbers are fully consolidated on account of management control with Qtel. Our mobile penetration forecasts remain conservative on account of the local population escaping to neighbouring countries because of the war. We

expect cleaning up of the subscriber numbers in next couple of years, which in turn should have positive impact on industry ARPU. As Asiacell has majority Iraqi ownership, the revenue sharing with the government stands at 15% (compared with 18% for Zain). Moreover, unlike its other competitors, Asiacell has a tax holiday for 10 years starting in 2007, as it was established in a special tax zone.

Our base-case valuation gives us an EV of QAR3.2bn for 100% of Qtel's Iraqi operations. This excludes the licence fee of USD1.25bn (QAR4.6bn) to be paid in 2007 and 2008. If we add the present value of the licence fee then it indicates that the operations would be value negative.

Qtel's 30% stake implies that the Iraqi operations add an enterprise value of QAR969m to the group. This is around c2% of the group's valuation, which excludes further payments on account of licence fee. We have not factored in further licence fee in our valuation yet. Our base-case valuation incorporates a WACC of 23% and a terminal growth rate of 4%.

Iraqi operations – SOTP valuation summary for 100% operations

In QARm	2008e	2009e	2010e	2011e	2012e	2013e	2014e	2015e	2016e	2017e
EBITDA	800	818	848	892	944	999	1,057	1,121	1,193	1,269
Less: depreciation	-15	-50	-83	-111	-135	-156	-175	-191	-206	-221
Pre-tax NOPLAT	785	768	765	781	808	842	882	931	987	1,048
Tax	0.0%	0	0	0	0	0	0	0	0	0
NOPLAT	785	768	765	781	808	842	882	931	987	1,048
Depreciation	-15	-50	-83	-111	-135	-156	-175	-191	-206	-221
Capex	-263	-238	-225	-222	-225	-232	-241	-253	-268	-284
Free cash flow	537	580	623	670	719	767	816	868	926	985
Terminal value										5394
Terminal growth rate	4.0%									
Discount rate	23.0%									
Discount factors	0.81	0.66	0.54	0.44	0.36	0.29	0.23	0.19	0.16	0.13
PV of cash flow	436.4	383.7	334.9	292.8	255.3	221.4	191.5	165.7	143.6	124.3
PV of continuing value	680									
Enterprise value	3230									
Implied EV/EBITDA	4.0	3.9	3.8	3.6	3.4	3.2	3.1	2.9	2.7	2.5

Source: HSBC estimates

Sensitivity to cost of capital and terminal growth rate

We have used a conservative discount rate because of Iraq's high political risk. Our base-case valuation incorporates a WACC of 23%, which gave us an EV of QAR3.2bn for the operations. We have run a sensitivity table with respect to the cost of capital and terminal growth rate. Keeping the same terminal growth rate of 4%, while reducing the discount rate by 400bp, the EV for Asiacell comes to around QAR4.1bn (around c25% higher than our base case). Upside potential to our valuation could result from the risk profile of Iraq become more positive.

Sensitivity to cost of capital and terminal growth rate for 100% operations

WACC	Terminal growth rate				
	2%	3%	4%	5%	6%
19%	3,998	4,074	4,160	4,258	4,371
21%	3,529	3,581	3,639	3,704	3,778
23%	3,153	3,190	3,230	3,275	3,325
25%	2,847	2,873	2,902	2,933	2,968
27%	2,592	2,611	2,632	2,655	2,680

Source: HSBC estimates

Qtel's Iraqi operations – KPIs and P&L summary

In QAR mn	2007e	2008e	2009e	2010e	2011e	2012e
Population (000)	26,530	27,061	27,602	28,154	28,717	29,291
Market Subscribers	10,612	11,636	12,421	13,232	14,071	14,836
Market Penetration	40.0%	43.0%	45.0%	47.0%	49.0%	50.7%
Asia Cell - Wataniya Subscribers	3,756	3,993	4,155	4,335	4,532	4,713
Asia Cell Market share	35.4%	34.3%	33.4%	32.8%	32.2%	31.8%
ARPU in QAR	27.3	35.7	36.1	36.6	37.2	37.9
YoY Change	0.0%	30.7%	1.0%	1.4%	1.7%	2.0%
ARPU in USD	7.5	9.8	9.9	10.0	10.2	10.4
Revenue	611	1,646	1,748	1,847	1,962	2,086
Change	0.0%	169.6%	6.2%	5.7%	6.2%	6.3%
EBITDA clean	312	800	818	848	892	944
Change	0.0%	156.8%	2.3%	3.6%	5.2%	5.8%
Margin	51.0%	48.6%	46.8%	45.9%	45.5%	45.2%
Capex	(122)	(263)	(238)	(225)	(222)	(225)
Capex/sales	20.0%	16.0%	13.6%	12.2%	11.3%	10.8%

Source: HSBC estimates

Kuwait – still the big Daddy

- ▶ Lagging behind Zain in a hitherto duopoly market; high ARPU (USD50) and EBITDA margins in the late-40s make it an attractive market
- ▶ Competition heating up, with STC scheduled to start operations in late 2008
- ▶ High-value market, forming c54% of Wataniya's EV and c25% for Qtel

High-value market...

The two players...

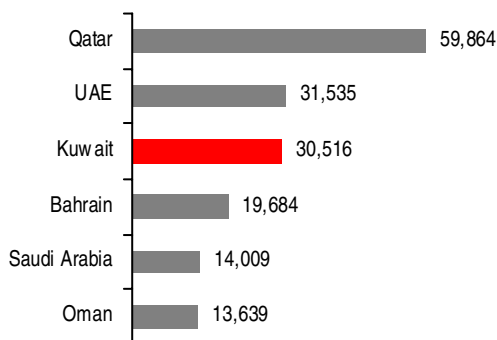
Kuwait was one of the first Gulf countries to open up its telecoms sector, which it did back in 1999 by issuing the second mobile licence to NMTC. This ended the 13-year monopoly of Zain. With the arrival of Wataniya, tariffs began to fall and wireless coverage extended to more segments of the population. In 2003, Wataniya surpassed Zain in terms of market share, but this was short-lived, as Zain again took the dominant position and has

been consolidating its position ever since.

The arrival of Wataniya also marked the start of a huge growth in wireless subscribers, which has since continued. Both players started pushing pre-paid plans, which also proved to be a catalyst in subscriber growth, as it encouraged younger people to purchase mobiles.

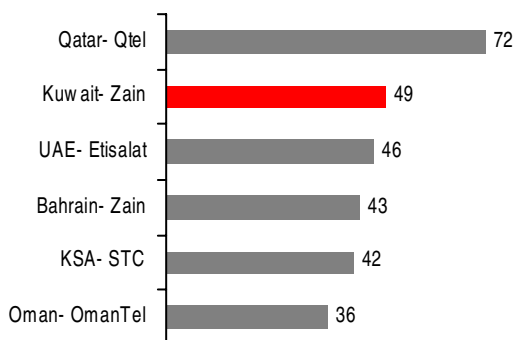
The market has witnessed a high level of competition between the two players, though Zain has been able to maintain its market leadership.

GDP per capita (USD) - 2006



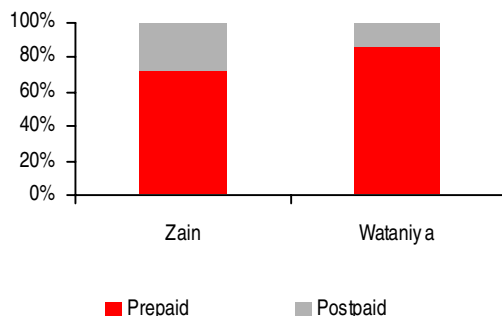
Source: HSBC

...translating to high ARPUs (2006)



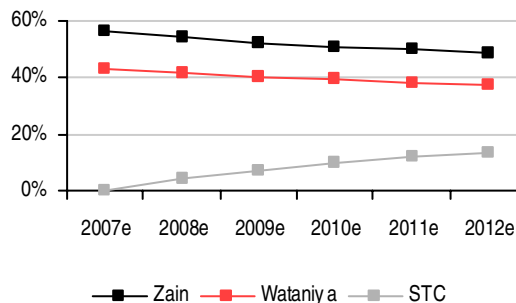
Source: Company reports

Higher pre-paid to post-paid ratio...



Source: Companies (first-half 2007)

Market-share change in Kuwait



Source: HSBC estimates

...and its going to be three now...

In November 2007, Saudi Telecom Company (STC) won the Kuwaiti Government's auction of a 26% stake in a yet-to-be-launched third mobile operator. Its successful bid was KWD248.7m (USD908m). It beat eight other rivals in the bidding process. The Government will retain a 24% stake in the company and the remaining 50% is scheduled to be issued in an IPO in late 2008.

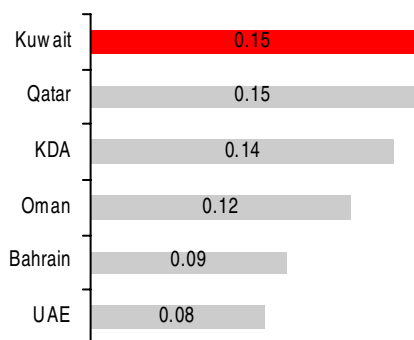
...and KPIs are going to come under pressure

We expect competition in the market to intensify following the entry of STC, which could lead to a drop in ARPUs and EBITDA margins for both Zain and Wataniya. Kuwait has the highest average national price per minute and second-highest activation fees in GCC region. This has resulted in high ARPUs of USD49 for the market leader Zain. Kuwait's economy is largely

dependent on oil. It has 10% of the world's reserves and petroleum accounts for nearly 50% of its GDP. High oil prices in recent years have positively affected the economy and have led to a growth in GDP per capita, which stands at USD31,051 currently, and has been one of the factors behind the high ARPUs.

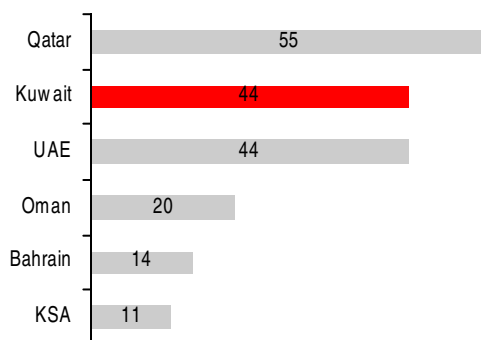
We expect tariffs to drop after the entry of the new operator, directly affecting ARPUs. We believe ARPUs will fall initially, stabilising at around USD45 in the long term. ARPUs are also going to take a hit because Wataniya has lowered its international call rates by 20%, effective January 2008 (on the back of pressure from the regulator). However, at the same time, the entry of third player and the more intense competition is expected to give a further boost to the mobile penetration in the region.

High average national price per minute (USD, 2006)

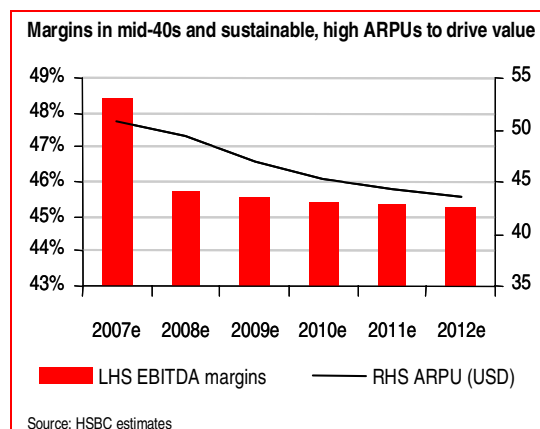
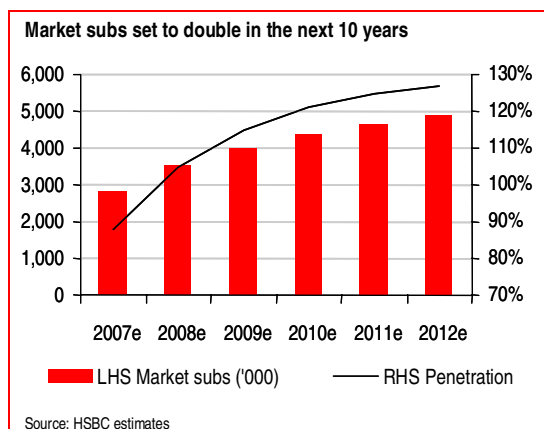


Source: ictQatar

High activation fees (USD, 2006)



Source: ictQatar



We expect mobile penetration to exceed 120% by the end of 2010, as we think the increased competition will boost penetration as tariffs go down. However, Wataniya has more to lose from increased competition, as it has higher number of pre-paid customers, who are more susceptible to churn. Zain, the market leader, has a higher percentage of post-paid customers and thus we expect it will suffer less churn. Overall we expect numbers of subscribers in the market to go up, with population expected to grow at a compound annual rate of c3.5% on the back of high proportion of expatriates in the region (c50%). Also, we think the level of competition is going to affect EBITDA margins for both Zain and Wataniya. In the long term, we expect the margins in the region to stabilise at c45%. Currently Zain has higher EBITDA margins than Wataniya, mainly because it has better quality customers (ie postpaid) and a higher market share (meaning net interconnect income).

Regulatory environment

Despite being the first market to liberalise its mobile market in the GCC, there is no independent telecom regulator in Kuwait. The Ministry of Communications is acting as the regulator. The 1961 MoC Law sets the general guidelines for the regulation of the market.

Technology

Kuwait is one of the most advanced Middle-Eastern countries in terms of wireless technology. With the market becoming more saturated and because the pre-paid segment (which has lower ARPUs than the post-paid segment) dominates, both operators began implementing next generation voice and data services to attract more contract customers and improve ARPUs. By 2005, both operators had added GPRS and EDGE to their wireless services portfolio. By 2006 they had upgraded their networks to 3.5G HSDPA. The impact of the technology is illustrated by the fact that Kuwait has the highest number of households with internet connections among the GCC countries.

So where is the value coming from?

- ▶ We expect market subs in Kuwait to double from around 2.8 million at the end of 2007 to 5.9 million by 2017e, mainly driven by high population growth.
- ▶ Despite Wataniya losing market share, with it falling from 43% in 2007 to 36% by 2017e, its subscriber base should go up from 1.2 million to around 2.1 million by the end of 2017, we think.
- ▶ STC has announced its intention to share infrastructure with Wataniya initially, which should boost Wataniya's EBITDA margins.

- ▶ Around 50% of the population are expats, which should result in sustainable ARPU in the mid-40s (in USD), we think.
- ▶ The company is already in a maintenance capex stage, with capex spending as a percentage of sales in single digits in 2006.

We expect Kuwait to contribute 23% to Qtel's revenue by 2010e, while we think its EBITDA contribution will be around c22%.

Our valuation for Qtel's Kuwaiti operations incorporates a WACC of c10.76%, a bit higher than Zain on account of Zain's higher level of debt. Our terminal growth rate assumption stands at 2.5%.

Valuation sensitivity of WACC and terminal growth rate

Our base-case valuation for Qtel's Kuwaiti operations gives us an EV of KWD992m. We note that the region is marked currently with change in interest rates leading to changes in discount rates for the companies. Interest rates in this region are being revised, leading to changes in the discount rates for the companies. We have run a sensitivity analysis to find out sensitivity of

the valuation to changes in WACC and terminal growth rates (see table below).

Kuwait valuation sensitivity to WACC and terminal growth rates

WACC	Terminal growth rate				
	0.5%	1.5%	2.5%	3.5%	4.5%
8.76%	1,122	1,202	1,307	1,452	1,665
9.76%	997	1,054	1,128	1,224	1,358
10.76%	896	939	992	1,059	1,149
11.76%	814	846	885	934	997
12.76%	745	770	800	836	881

Source: HSBC estimates

Kuwait SOTP valuation summary

In KWDm	2008e	2009e	2010e	2011e	2012e	2013e	2014e	2015e	2016e	2017e
EBITDA	103	111	115	118	121	123	126	130	134	138
Less: depreciation	-11	-13	-15	-16	-18	-20	-22	-23	-25	-26
Pre-tax NOPLAT	92	99	101	102	103	103	105	107	109	112
NOPLAT	92	99	101	102	103	103	105	107	109	112
Depreciation	-11	-13	-15	-16	-18	-20	-22	-23	-25	-26
Capex	-21	-25	-27	-29	-30	-31	-33	-34	-35	-36
Free cash flow	83	87	88	89	91	92	94	96	99	102
Terminal value										1261
Terminal growth rate	2.5%									
Discount rate	10.76%									
Discount factors	0.90	0.82	0.74	0.66	0.60	0.54	0.49	0.44	0.40	0.36
PV of cash flow	74.5	70.7	65.1	59.4	54.3	49.8	45.8	42.3	39.3	36.6
PV of continuing value	454									
Enterprise value	992									
Implied EV/EBITDA	9.6	8.9	8.6	8.4	8.2	8.0	7.9	7.6	7.4	7.2

Source: HSBC estimates

Kuwaiti operations – KPIs and P&L summary

In KWDm	2006a	2007e	2008e	2009e	2010e	2011e	2012e
Population (000)	3,180	3,256	3,370	3,489	3,612	3,739	3,871
Market subscribers	2,530	2,859	3,528	4,006	4,366	4,656	4,905
Market penetration	79.5%	87.8%	104.7%	114.8%	120.9%	124.5%	126.7%
Wataniya subs ('000)	1,069	1,240	1,471	1,616	1,715	1,789	1,851
Mix							
Post-paid as a % of total subs	12.5%	13.6%	13.0%	12.4%	11.9%	11.5%	11.2%
Pre-paid as a % of total subs	87.5%	86.4%	87.0%	87.6%	88.1%	88.5%	88.8%
Market share							
Zain	58%	57%	54%	52%	51%	50%	49%
Wataniya	42%	43%	42%	40%	39%	38%	38%
Saudi Telecom	0%	0%	4%	7%	10%	12%	13%
ARPU (KWD)	14.0	14.3	13.9	13.2	12.7	12.4	12.2
Y-o-y change	1.7%	2.2%	-2.8%	-5.1%	-3.6%	-2.5%	-1.6%
Blended ARPU in USD	49.8	50.9	49.5	47.0	45.3	44.2	43.5
Total revenue	178.5	206.2	226.0	244.3	254.1	260.7	266.5
Change	14.9%	15.5%	9.6%	8.1%	4.0%	2.6%	2.2%
EBITDA clean	86.1	99.7	103.3	111.3	115.4	118.2	120.7
Change	22.0%	15.9%	3.5%	7.7%	3.8%	2.4%	2.1%
Margin	48.2%	48.4%	45.7%	45.6%	45.4%	45.4%	45.3%
Capex	-12.8	-16.4	-20.7	-24.5	-27.0	-28.7	-30.1
Capex/sales	7.2%	8.0%	9.2%	10.0%	10.6%	11.0%	11.3%

Source: Company data, HSBC estimates

Algeria – value and growth market

- ▶ Market with high growth potential, as subscribers set to double in the next 10 years
- ▶ Nedjma has been showing significant improvements on the KPI front; becoming a strong No.2 player; ARPU and margins look set to improve in the long run
- ▶ Algeria represents 25% of Wataniya's EV and 13% of Qtel's group's EV

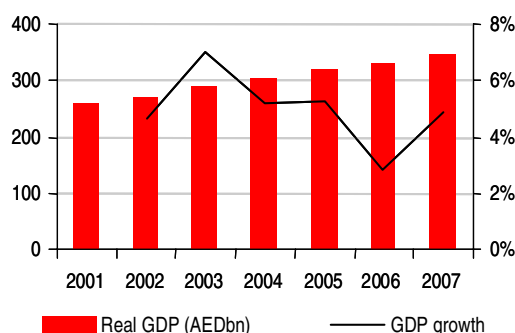
Fast-track market...

The Algerian market is Wataniya's largest market, with 33.5 million population representing 44% of population under coverage. It has a low market share of around 17% currently and only represents 24% of Qtel's total subscriber base. We expect market share to go up to around 20% in next 5 years. The opening up of the Algerian economy to foreign interests could act as a key catalyst for future growth in the telecommunication sector.

GDP growth is strong

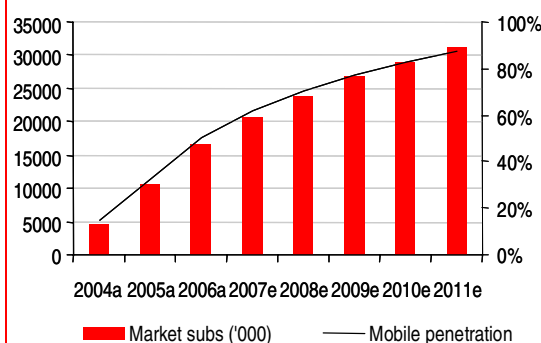
Algeria has a young and growing population, of which 27% is under the age of 14 and 95% is under 65. The population has grown at a compound annual rate of 1.5% between 2001 and 2006, rising from 31 million to 33 million. Real GDP (in local currency terms) has grown at a compound annual rate of 5% from AED 259bn in 2001 to AED346bn in 2007e and per capita GDP stands at USD3,100.

Strong GDP growth



Source: IMF

Wireless market evolution



Source: Company report, HSBC estimates

Exponential growth in subscribers

Algeria has seen an exponential growth in subscriber numbers recently. The penetration rate in the country has grown from 1.4% in 2002 to 61.5% in 2006. The main trigger for the rise was the increase in competition following the entry of Orascom Telecom and Wataniya. The Algerian market is the 'Jewel in the Crown' for Orascom Telecom, the largest mobile operator in Algeria, with a 65% market share. Hence, competition is very tough in the market for Nedjma, especially as it is fighting head to head with the incumbent's mobile operator, Mobilis, which has a 17% market share.

...but competition is tough

State-owned Algeria Telecom's subsidiary, Mobilis, lost its monopoly in the Algerian market in 2002, when Orascom Telecom Algeria (under the brand name Djezzy) entered the market. This triggered an increase in subscribers and a period of high, sustainable growth for the market, from which Orascom benefited.

The competition in the market increased further when the third mobile licence was granted to Wataniya Telecom in 2003, which beat South Africa's MTN and Telefonica Moviles in the bidding process. This forced Mobilis to transform itself into a more efficient and customer-oriented player. This increased competition was reflected

in the growth in the number of subscribers for the market. The number of mobile subscribers in Algeria has grown by a compound annual rate of 183% over 2001-06, with mobile penetration reaching 50% by end-2006 versus 0.3% in 2001.

Orascom Telecom's capex for 2003-06 exceeded USD1.5bn, which it used to expand its network coverage and to deploy its own backbone. The lack of competition from Algeria Telecom's mobile arm and growing network coverage helped the company to cement its position in the market.

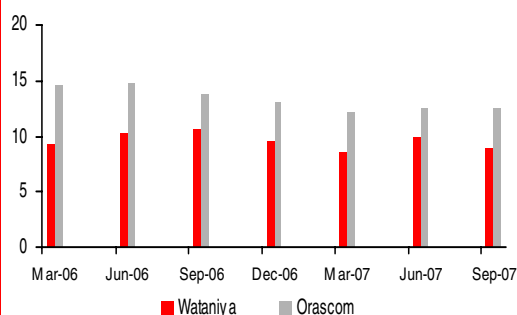
Lower KPIs

Currently Nedjma has lower KPIs than the market leader, Djezzy. We expect Djezzy to maintain its EBITDA margin and ARPU premium over its competitors, on the back of higher quality (postpaid) subscribers, high on-net traffic and low leased line costs.

Nedjma only spent USD515m between 2004 and 2006, far less than OT. Its post-paid ARPU of USD12 in 2006 equals OT's Djezzy blended ARPU. Unlike OT, we believe most of Nedjma's traffic is off-net, which exposes the company to the change in the interconnect regime. Also, we believe that Nedjma's costs will remain high, as the company continues to have leased line costs.

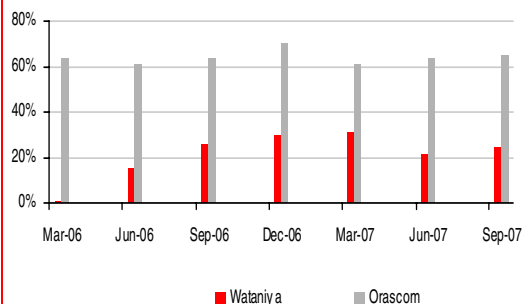
Having said that, the privatisation of Algeria Telecom, which has been under discussion for a couple of years now, is important for Wataniya's

ARPUs (USD) lower than competitor



Source: Company report

EBITDA margins gap is very high compared to Orascom



Source: Company report

subsidiary, as it could imply that costs will rise, which would be likely to affect the company's pricing strategy.

An upside risk to our valuation of Qtel's Algerian operations would be if the government were to open up the economy, as it would result in growing consumer spending, which would help raise the overall ARPU in the market, in our view.

Etisalat enters the frame

According to a Reuters report (December 31 2007), UAE-based Emirates Telecommunications (Etisalat) is considering bidding for a 51% stake in Algerian PTO Algerie Telecom. Etisalat has been looking to expand abroad since it lost its monopoly position in the UAE following the entry of Du. Should Etisalat enter the Algerian market, then the competition in wireless is likely to become even more intense.

Regulations

ARPT was founded as an independent regulatory authority in August 2000, under the Telecom Law 03-2000. The Algerian president nominates all seven members of the ARPT's council who have the right to award licences. The licences have a

term of 15 years and oblige the owner to provide wireless services in all towns with more than 2,000 inhabitants. In return, ARPT only issues additional wireless licences every 30 months at most.

Technology

Currently all three players in the market provide wireless services on a 2.5G platform (GPRS+EDGE). ARPT is considering issuing 3G licences. It has already carried out studies to see whether the Algerian market is ready for 3G services.

Forecasts and valuation

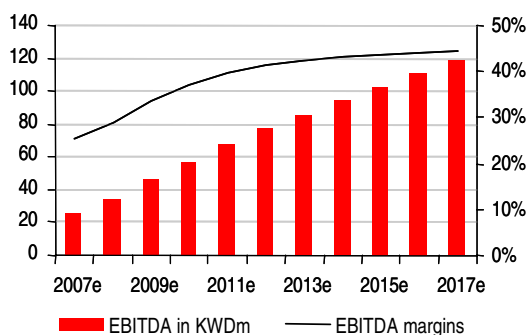
- ▶ We expect market penetration in the market to continue on its growth path, reaching 100% by end-2017e.
- ▶ Nedjma has been steadily increasing its market share, mainly at the expense of Algerie Telecom and we expect it to continue growing until its market share stabilises at 20% (from 17.3%).
- ▶ We expect ARPUs to fall for the next couple of years, as Nedjma tries to acquire more market share through pricing. However, as the

Algeria SOTP valuation summary

KWDm	2008e	2009e	2010e	2011e	2012e	2013e	2014e	2015e	2016e	2017e
EBITDA	34	46	57	67	77	86	95	103	111	118
Less: depreciation	-22	-23	-24	-25	-25	-26	-26	-26	-26	-27
Pre-tax NOPLAT	12	22	32	42	51	60	69	77	84	92
Tax	3	6	8	11	13	15	17	19	21	23
NOPLAT	9	17	24	32	39	45	51	57	63	69
Depreciation	-22	-23	-24	-25	-25	-26	-26	-26	-26	-27
Capex	-26	-25	-25	-24	-24	-25	-25	-26	-27	-28
Free cash flow	4	15	24	32	40	46	52	58	63	67
Terminal value										817
Terminal growth rate	3.0%									
Discount rate	11.5%									
Discount factors	0.90	0.80	0.72	0.65	0.58	0.52	0.47	0.42	0.38	0.34
PV of cash flow	3.9	11.7	17.2	20.8	23.0	24.1	24.4	24.1	23.5	22.7
PV of continuing value	275									
Enterprise value	471									
Implied EV/EBITDA	13.9	10.3	8.3	7.0	6.1	5.5	5.0	4.6	4.2	4.0

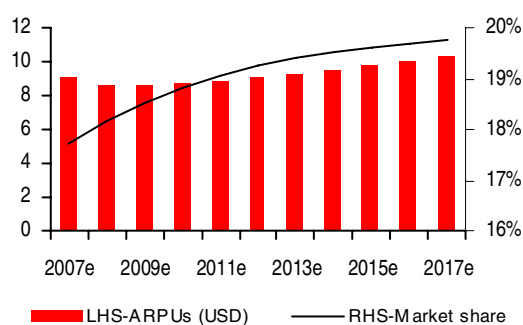
Source: HSBC estimates

Growth coming in mainly from EBITDA margins expansion...



Source: HSBC estimates

...at the same time, Nedjma's market share and ARPUs are set to improve



Source: HSBC estimates

market stabilises and more data revenues pour in, we expect the company's ARPUs to steadily increase to USD10.

- ▶ EBITDA margin expansion driven by more on net traffic and, as the operations mature, we expect it to reach at c44% in the long run.

Algeria KPIs and P&L forecasts

KWDm	2006a	2007e	2008e	2009e	2010e	2011e	2012e
Population (000)	32,926	33,452	33,988	34,531	35,084	35,645	36,216
Penetration	50.1%	62.0%	70.6%	77.5%	83.0%	87.4%	90.9%
Market subscribers	16,506	20,740	23,995	26,755	29,114	31,149	32,924
Nedjma subscribers	2,991	3,679	4,357	4,957	5,479	5,936	6,336
Post-paid	47	111	167	219	258	288	312
Pre-paid	2,944	3,568	4,190	4,737	5,221	5,648	6,024
Mix							
Post-paid as a % of total subs	2%	3%	4%	4%	5%	5%	5%
Pre-paid as a % of total subs	98%	97%	96%	96%	95%	95%	95%
Nedjma market share	18.1%	17.7%	18.2%	18.5%	18.8%	19.1%	19.2%
Blended ARPU (KD)	2.758	2.540	2.417	2.410	2.434	2.477	2.533
Y-o-y change	-31%	-8%	-5%	0%	1%	2%	2%
Blended ARPU in USD	9.8	9.0	8.6	8.6	8.7	8.8	9.0
Total revenue	74	102	117	135	152	170	187
Change	76%	38%	15%	16%	13%	11%	10%
EBITDA clean	15	26	34	46	57	67	77
Change		73.2%	31.1%	34.6%	24.4%	18.4%	14.5%
Margin	20.2%	25.4%	29.0%	33.8%	37.2%	39.5%	41.2%
Capex	(27)	(29)	(26)	(25)	(25)	(24)	(24)
Capex/sales	35.9%	28.1%	22.7%	18.9%	16.2%	14.4%	13.0%
Net profit	(17)	(10)	6	13	23	27	31
Margin	-23%	-9%	5%	10%	15%	16%	16%

Source: Company reports, HSBC estimates

Tunisia – a stable market

- ▶ Saturated market in terms of subs growth; focus remains on enhancing usage and hence ARPU
- ▶ A concern would be further disagreements between Wataniya and its partner Orascom about the size of their stakes in Tunisiana
- ▶ Tunisia represents 17% of Wataniya Telecom's EV and 8% of Qtel's

Young market, but with limited growth opportunities

Tunisia has a burgeoning telecoms market. It contributes significantly to Wataniya's subscriber numbers. At the end of Q3 2007, its Tunisian subsidiary, Tunisiana, had around 3.5 million subscribers and accounted for 42% of Wataniya's total subscriber base. Of Tunisia's population, around 24% is under 14 years of age and the overall population is expected to grow at a rate of 1.2% in the long run (2016e)

GDP is growing strongly

GDP has grown at a compound annual rate of 5%

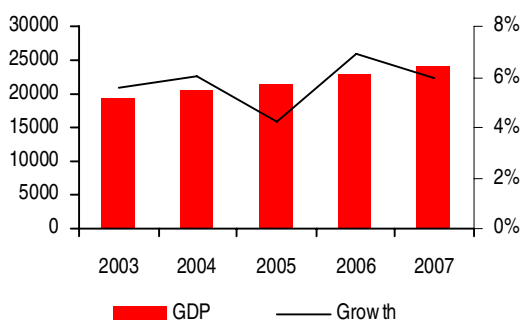
over the past five years. Liberalisation process and the government's progressive social policies have resulted in raising the living standards of the local population relative to the region. GDP per capita was around USD2,800 and real GDP growth was at 5.2% as at end-2006. In the 2007 edition of the *Global Competitiveness Report* (published by World Economic Forum), Tunisia was ranked the most competitive economy in Africa and the whole of the Arab world.

The telecommunications market

Duopoly market: opportunity...

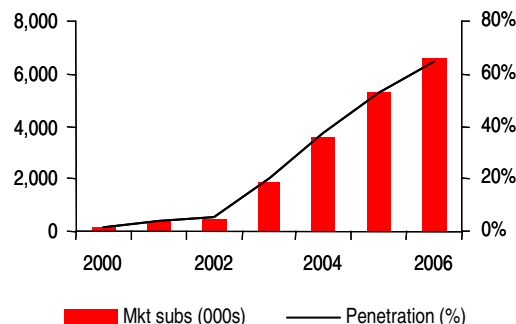
In May 2002, Tunicell's monopoly came to an end when the government awarded a 15-year GSM

Real GDP (in local currency, million) and GDP growth



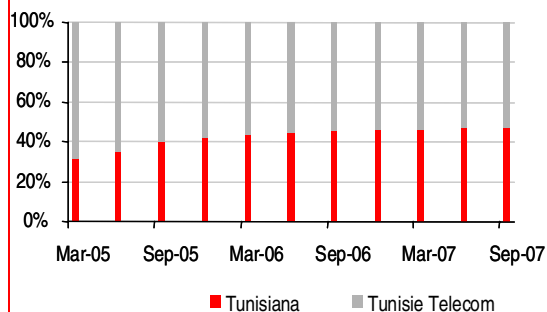
Source: Thomson Financial Datastream

Tunisia market has witnessed huge growth



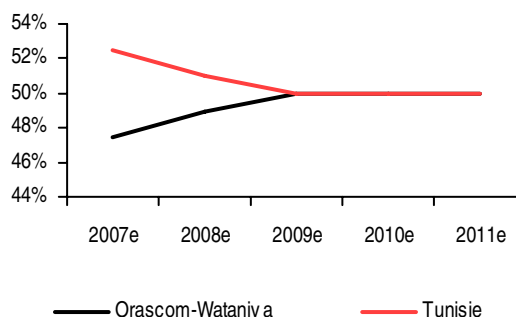
Source: HSBC

Market share: Tunisiana catching up with Tunisie Telecom...



Source: Company, HSBC

... and we expect it to catch up soon



Source: HSBC estimates

licence to Orascom Telecom Tunisia (now Tunisiana) for USD454m. Tunisiana is now jointly and equally controlled by Orascom Telecom of Egypt and Wataniya Telecom. In October 2002, Wataniya paid USD113.5m for a 50% stake in Tunisiana. Tunisia is a stable market and both Orascom Telecom and Wataniya have said they would like to have a higher share in the joint venture.

...have a disagreement

In May 2006, Orascom filed a request for arbitration against Wataniya with the International Court of Arbitration. Orascom claims that Wataniya had 'materially breached the agreement', and thus Orascom argued that it has a contractual right to acquire Wataniya's 50% stake in the company. However, the court ruled that the breach was not sufficient to require Wataniya to sell its stake.

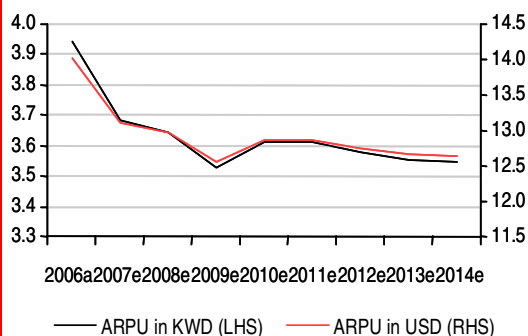
High wireless subscriber growth

Subscriber growth in Tunisia picked up rapidly between 2000 and 2006 with wireless penetration rising from 1.2% to 64%. The number of subscribers has grown at a compound annual rate of 53% during 2004-07. We expect penetration in this market to start stabilising at around 88% in next 10 years, as market starts to become saturated.

Market share up, ARPUs down

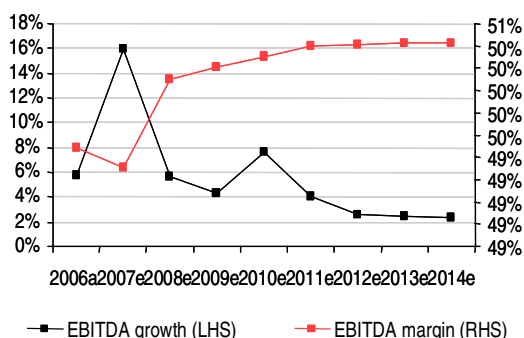
The gap between Tunisiana and Tunisie Telecom has steadily been closing. It is gaining higher market share with the passing of each quarter. And we expect it to catch up with Tunisie Telecom by 2009e, with both players having an equal share of the market. Tunisiana has aggressively sought market share at the cost of ARPUs. So, as market share stabilises after 2009 and pricing pressure reduces, we expect ARPUs also to stabilise.

With market share, ARPUs are expected to stabilise, too



Source: Company, HSBC estimates

EBITDA growth and margins



Source: Company, HSBC estimates

Tunisiana's EBITDA margin has hovered around the mid- to late 40s for the last three years and we expect the margins to remain stable at 45% in the long term (to 2016e).

Regulations

The Telecommunications Act of 2001 led to the creation of two new regulatory bodies – the National Telecommunications Commission (NTT) and the Agence Nationale des Frequences (ANF).

Both Tunicell and Tunisiana use a 2.5G platform for their wireless services. The Tunisian Government is considering issuing 3G licences, but nothing is clear on how many or when they will be issued.

Forecasts and valuation

Wataniya treats its Tunisian operations as a joint venture for accounting purposes. Wataniya's 50% stake implies a proportionate consolidation of 50% to the group's numbers. We expect revenues from Tunisia to grow at a compound annual rate of 4% over 2007-12e, while EBITDA should grow at a compound annual rate of 5%, implying that the business is relatively stable.

Our SOTP valuation for Tunisia incorporates a cost of capital of c10.5%, in line with Orascom's Tunisian operations and a terminal growth rate of 2%.

Tunisia SOTP valuation summary

KWDm	2008e	2009e	2010e	2011e	2012e	2013e	2014e	2015e	2016e	2017e
EBITDA	81	85	91	95	97	100	102	104	107	109
Less: depreciation	-36	-37	-38	-37	-36	-35	-34	-33	-32	-31
Pre-tax NOPLAT	45	47	54	58	61	65	68	71	75	78
Tax	14	14	16	17	18	19	20	21	22	23
NOPLAT	32	33	38	40	43	45	48	50	52	55
Depreciation	-36	-37	-38	-37	-36	-35	-34	-33	-32	-31
Capex	-25	-22	-22	-20	-19	-20	-20	-21	-21	-22
Free cash flow	43	48	53	58	60	61	61	62	63	64
Terminal value										767
Terminal growth rate	2.0%									
Discount rate	10.5%									
Discount factors	0.90	0.82	0.74	0.67	0.61	0.55	0.50	0.45	0.41	0.37
PV of cash flow	38.5	39.5	39.1	38.9	36.3	33.3	30.5	28.0	25.7	23.5
PV of continuing value	283									
Enterprise value	613									
Implied EV/EBITDA	7.54	7.23	6.72	6.46	6.30	6.15	6.01	5.88	5.75	5.63

Source: HSBC estimates

Tunisia KPIs and P&L forecasts

KWDm	2006a	2007e	2008e	2009e	2010e	2011e	2012e
Population (000)	10,292	10,415	10,540	10,667	10,795	10,924	11,055
Market subscribers	6,601	7,499	7,905	8,213	8,528	8,849	9,148
Market penetration	64.1%	72.0%	75.0%	77.0%	79.0%	81.0%	82.8%
Subscribers (000)							
Orascom-Wataniya	3,069	3,562	3,874	4,107	4,264	4,424	4,574
Tunisie Telecom	3,531	3,937	4,032	4,107	4,264	4,424	4,574
Market subscribers	6,601	7,499	7,905	8,213	8,528	8,849	9,148
Market share							
Orascom-Wataniya	46.5%	47.5%	49.0%	50.0%	50.0%	50.0%	50.0%
Tunisie Telecom	53.5%	52.5%	51.0%	50.0%	50.0%	50.0%	50.0%
Net adds (000)							
Orascom-Wataniya	812	493	312	233	157	160	150
Tunisie Telecom	514	406	95	75	157	160	150
Market net adds	1,326	898	406	308	314	321	300
Revenue	67.1	78.1	81.2	84.5	90.7	94.2	96.6
Change	-0.9%	16.4%	4.0%	4.0%	7.4%	3.8%	2.5%
EBITDA	33.2	38.5	40.7	42.4	45.6	47.5	48.7
Change	5.7%	16.0%	5.7%	4.2%	7.6%	4.0%	2.6%
Margin	49.5%	49.3%	50.1%	50.2%	50.3%	50.4%	50.4%
Capex	(13.7)	(14.9)	(12.6)	(11.2)	(11.2)	(9.8)	(9.7)
Capex/sales	20.4%	19.1%	15.5%	13.3%	12.3%	10.4%	10.0%

Source: HSBC estimates, Company data

Notes

Notes

Notes

Disclosure appendix

Analyst certification

The following analyst(s), who is(are) primarily responsible for this report, certifies(y) that the opinion(s) on the subject security(ies) or issuer(s) and any other views or forecasts expressed herein accurately reflect their personal view(s) and that no part of their compensation was, is or will be directly or indirectly related to the specific recommendation(s) or views contained in this research report: Kunal Bajaj and Karim Khadr

Important disclosures

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For each stock we set a required rate of return calculated from the risk free rate for that stock's domestic, or as appropriate, regional market and the relevant equity risk premium established by our strategy team. The price target for a stock represents the value the analyst expects the stock to reach over our performance horizon. The performance horizon is 12 months. For a stock to be classified as Overweight, the implied return must exceed the required return by at least 5 percentage points over the next 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock must be expected to underperform its required return by at least 5 percentage points over the next 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands are classified as Neutral.

Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation of coverage, change of volatility status or change in price target). Notwithstanding this, and although ratings are subject to ongoing management review, expected returns will be permitted to move outside the bands as a result of normal share price fluctuations without necessarily triggering a rating change.

*A stock will be classified as volatile if its historical volatility has exceeded 40%, if the stock has been listed for less than 12 months (unless it is in an industry or sector where volatility is low) or if the analyst expects significant volatility. However, stocks which we do not consider volatile may in fact also behave in such a way. Historical volatility is defined as the past

month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility has to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

Prior to this, from 7 June 2005 HSBC applied a ratings structure which ranked the stocks according to their notional target price vs current market price and then categorised (approximately) the top 40% as Overweight, the next 40% as Neutral and the last 20% as Underweight. The performance horizon is 2 years. The notional target price was defined as the mid-point of the analysts' valuation for a stock.

From 15 November 2004 to 7 June 2005, HSBC carried no ratings and concentrated on long-term thematic reports which identified themes and trends in industries, but did not make a conclusion as to the investment action that potential investors should take.

Prior to 15 November 2004, HSBC's ratings system was based upon a two-stage recommendation structure: a combination of the analysts' view on the stock relative to its sector and the sector call relative to the market, together giving a view on the stock relative to the market. The sector call was the responsibility of the strategy team, set in co-operation with the analysts. For other companies, HSBC showed a recommendation relative to the market. The performance horizon was 6-12 months. The target price was the level the stock should have traded at if the market accepted the analysts' view of the stock.

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As of 08 February 2008, the distribution of all ratings published is as follows:

Overweight (Buy)	55%	(22% of these provided with Investment Banking Services)
Neutral (Hold)	30%	(24% of these provided with Investment Banking Services)
Underweight (Sell)	15%	(15% of these provided with Investment Banking Services)

HSBC & Analyst disclosures

Disclosure checklist

Company	Ticker	Recent price	Price Date	Disclosure
QATAR TELECOM	QTEL.QA	282.00	07-Feb-2008	2

Source: HSBC

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