

20<sup>th</sup> April 2010

# Etisalat

## 1Q10 earnings miss consensus

Etisalat posted its 1Q10 financials, showing 8% lower earnings year-on-year (YoY), falling short of consensus estimates by 11%. Lower UAE revenues (driven in part by lower fixed-line subscribers) muted international revenue growth. Margins have narrowed due to start-up opex in new markets (e.g. India), which also explains the jump in capex to 19% of revenues in 1Q10. The recently acquired 14% stake in Zantel is too small to affect our valuation. We will revise our model following the results release in view of recent market trends in both the UAE and overseas. We maintain our LTFV and TP (adjusted for the company's stock dividend) at AED22 and AED18, respectively. Our Strong Buy rating stands, given a 70% upside to our TP of AED18.

**Earnings 8% lower YoY, flat QoQ – missing consensus by 11%:** Etisalat's 1Q10 net income fell by 8% YoY to AED1.99bn, versus an average consensus estimate (four analysts) of AED2.25bn. We did not have an estimate for 1Q10. The lower earnings came in despite revenue growth of 5% to AED7.94bn on the back of higher mobile subs (+5% to 7.71mn reported; 7.25mn active based on an assumed activity rate of 94%) and higher internet subs (+15% to 1.38mn). Revenue growth was negatively affected by an 8% drop in UAE revenues (79% of total revenues) to AED6.3bn, while international revenues (21% of total revenues) grew 138% to AED1.6bn. Fixed-line subs declined by 4% to 1.3mn. We estimate EBIT margin has contracted around 9%, from 54.4% to 45.5%, due to opex for new start-ups such as India's **Etisalat DB Telecom**. 1Q10 EPS reached AED0.25 (1Q09: AED0.28, -8%). Capex reached AED1.54bn (19% of revenues) in 1Q10 vs. AED320mn (4% of revenues) a year ago, as Etisalat has invested both at home and in new start-up operations. The internet segment continues to grow, but not fast enough to drive revenue growth up further. Meanwhile, Etisalat's net cash position reached AED7.8bn, 5.5% higher than the AED7.4bn recorded in 4Q09.

**Increasing stake in Zantel – minimal effect:** Etisalat raised its stake in Tanzania's **Zantel** from 51% to 65% for USD16mn, valuing the company's equity at around USD114mn. This is a premium to our DCF-based LTFV and multiple-based TP. Given the investment's minimal size relative to Etisalat, we believe Etisalat is justified in further consolidating its existing operations.

**Valuation and recommendation:** We will revise our model following the release of both 2009 and 1Q10 results, in view of recent market trends in both Etisalat's home market (the UAE) and in international markets. We think the additional 14% stake in Zantel is too small to have a significant effect on valuation, and we therefore maintain our LTFV and TP (adjusted for the recent 10% stock dividend) at AED22 and AED18, respectively. Our **Strong Buy** rating stands, given the 70% upside to our TP.

| AED mn            | 2008 A        | 2009 A        | 2010 F        | 2011 F        | 2012 F        |
|-------------------|---------------|---------------|---------------|---------------|---------------|
| <b>Revenues</b>   | <b>29,360</b> | <b>30,831</b> | <b>32,027</b> | <b>34,456</b> | <b>36,800</b> |
| Growth rate       |               | 5.0%          | 3.9%          | 7.6%          | 6.8%          |
| <b>EBITDA</b>     | <b>17,228</b> | <b>19,504</b> | <b>21,998</b> | <b>23,124</b> | <b>24,476</b> |
| Growth rate       |               | 13.2%         | 12.8%         | 5.1%          | 5.8%          |
| EBITDA margin     | 58.7%         | 63.3%         | 68.7%         | 67.1%         | 66.5%         |
| <b>Net income</b> | <b>8,511</b>  | <b>8,836</b>  | <b>9,920</b>  | <b>10,363</b> | <b>10,863</b> |
| Growth rate       |               | 3.8%          | 12.3%         | 4.5%          | 4.8%          |
| Net margin        | 29.0%         | 28.7%         | 31.0%         | 30.1%         | 29.5%         |
| PER               | 9.8x          | 9.5x          | 8.4x          | 8.1x          | 7.7x          |
| P/BV              | 2.7x          | 2.3x          | 2.6x          | 2.3x          | 2.0x          |
| EV/EBITDA         | 3.9x          | 3.6x          | 3.2x          | 3.0x          | 2.8x          |
| Net debt/EBITDA   | -0.5x         | -0.3x         | -0.4x         | -0.4x         | -0.4x         |
| Dividend yield    | 4.3%          | 5.6%          | 5.7%          | 6.0%          | 6.2%          |

Note: EV/EBITDA is proportionate; forecast does not include recently-acquired Tigo (Sri Lanka)

Source: Etisalat and CICR estimates

**STRONG BUY** (MAINTAINED)  
**LT FAIR VALUE | AED22**  
**TARGET PRICE | AED18**

### COMPANY SYNOPSIS

Emirates Telecommunications Corporation (Etisalat) was established in 1976 as UAE's sole telecommunications service provider, under UAE Federal Government decree No.78 which was finally amended by Decretal Federal Code No.3/2003 stipulating the liberalization of the telecom sector. Etisalat's monopoly came to an end in 2005, when Emirates Integrated Telecommunications Company (du) won the second integrated telecom license. Despite the end of its service monopoly, Etisalat continues to submit 50% of its earnings to the UAE's government as royalties, making it a major contributor to the UAE's budget.

Etisalat established itself as a regional pioneer by introducing advanced technologies: mobile phone services (1982); GSM technology (1994); 3G and MMS (2003) and most recently BlackBerry service (2006). Driven by the vision to become one of the top 10 global telecom operators in 2010 and supported by a cash-generating saturated telecom market in the UAE, Etisalat expanded its service footprint to the global market. Currently, Etisalat possessed a portfolio of investments in West Asia, South Asia, and Africa markets in 18 countries with an aggregate subscriber base of around 85mn. Etisalat stands 140<sup>th</sup> among the Financial Times Top 500 Corporations in the world in terms of market capitalization, and is ranked by The Middle East magazine as the 6<sup>th</sup> largest company in the Middle East in terms of capitalization and revenues.

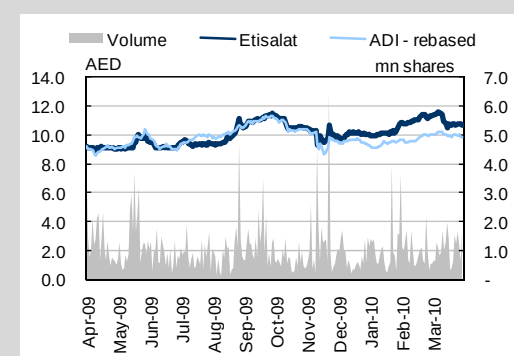
### SHAREHOLDER STRUCTURE

|                   |               |
|-------------------|---------------|
| Government of UAE | 60.0%         |
| Free float        | 40.0%         |
| <b>Total</b>      | <b>100.0%</b> |

### STOCK DATA

|                              |                        |
|------------------------------|------------------------|
| Reuters; Bloomberg           | ETEL.AD; ETISALAT DH   |
| Recent price as of 19-Apr-10 | AED 10.60              |
| No. of O/S shares            | 7,906.1 mn             |
| Market cap                   | AED 83,805 mn          |
| 52-wk high / low             | AED 11.59/ AED 8.64    |
| Avg. daily volume / turnover | 1.05 mn / AED 10.59 mn |

### STOCK PERFORMANCE | 52 WEEKS



Source: Reuters

**AMR HUSSEIN ELALFY, CFA**  
**AMR.ELALFY@CICH.COM.EG**

**NORAN ALI**  
**NORAN.ALI@CICH.COM.EG**

20<sup>th</sup> April 2010

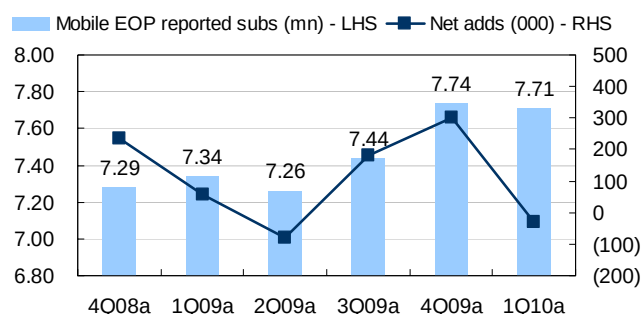
**Figure 1 | Etisalat's major KPIs (1Q10 actual vs. 1Q09 and 4Q09 and forecasts)**

|                                                 | 1Q09             | 4Q09             | 1Q10             |               |               |                     |                 |                    |
|-------------------------------------------------|------------------|------------------|------------------|---------------|---------------|---------------------|-----------------|--------------------|
|                                                 | Actual<br>Mar-09 | Actual<br>Dec-09 | Actual<br>Mar-10 | YoY<br>change | QoQ<br>change | Consensus<br>Mar-10 | Var.<br>a vs. e | No. of<br>analysts |
| (All figures in AED mn, unless otherwise noted) |                  |                  |                  |               |               |                     |                 |                    |
| UAE subscribers (mn)                            |                  |                  |                  |               |               |                     |                 |                    |
| Mobile subscribers (mn) - Reported              | 7.34             | 7.74             | 7.71             | 5.0%          | -0.4%         |                     |                 |                    |
| Mobile subscribers (mn) - Active *              | 6.90             | 7.28             | 7.25             | 5.0%          | -0.4%         |                     |                 |                    |
| Fixed subscribers (mn)                          | 1.35             | 1.31             | 1.30             | -3.7%         | -0.8%         |                     |                 |                    |
| Internet subscribers (mn)                       | 1.20             | 1.35             | 1.38             | 15.0%         | 2.2%          |                     |                 |                    |
| UAE net adds (000)                              |                  |                  |                  |               |               |                     |                 |                    |
| Mobile subscribers (000) - Reported             |                  |                  |                  | 369           | (30)          |                     |                 |                    |
| Mobile subscribers (000) - Active               |                  |                  |                  | 347           | (28)          |                     |                 |                    |
| Fixed subscribers (000)                         |                  |                  |                  | (50)          | (10)          |                     |                 |                    |
| Internet subscribers (000)                      |                  |                  |                  | 180           | 30            |                     |                 |                    |
| Revenues                                        | 7,566            | 8,724            | 7,945            | 5.0%          | -8.9%         | 8,286               | -4.1%           | 2                  |
| UAE                                             | 6,877            | 7,454            | 6,311            | -8.2%         | -15.3%        |                     |                 |                    |
| % of total revenues                             | 91%              | 85%              | 79%              |               |               |                     |                 |                    |
| International                                   | 688              | 1,270            | 1,634            | 137.5%        | 28.7%         |                     |                 |                    |
| % of total revenues                             | 9%               | 15%              | 21%              |               |               |                     |                 |                    |
| Opex                                            | (3,451)          | (4,815)          | (4,331)          |               |               |                     |                 |                    |
| EBIT                                            | 4,115            | 3,909            | 3,614            | -12.2%        | -7.5%         |                     |                 |                    |
| EBIT margin %                                   | 54.4%            | 44.8%            | 45.5%            | -8.9pp        | 0.7pp         |                     |                 |                    |
| Income/(loss) from associates                   | 12               | 314              | 98               |               |               |                     |                 |                    |
| Financing income                                | 184              | 191              | 282              |               |               |                     |                 |                    |
| Financing cost                                  | (62)             | (292)            | (10)             |               |               |                     |                 |                    |
| Net financing income/(cost)                     | 122              | (101)            | 272              |               |               |                     |                 |                    |
| Pretax income                                   | 4,249            | 4,122            | 3,984            | -6.2%         | -3.3%         |                     |                 |                    |
| Income taxes                                    | (52)             | (98)             | (19)             |               |               |                     |                 |                    |
| Effective tax rate %                            | 1.2%             | 2.4%             | 0.5%             |               |               |                     |                 |                    |
| Minority interest expense                       | 159              | (44)             | 24               |               |               |                     |                 |                    |
| Net income (before royalty fees)                | 4,356            | 3,979            | 3,989            | -8.4%         | 0.2%          |                     |                 |                    |
| Royalty fees                                    | (2,178)          | (1,990)          | (1,994)          |               |               |                     |                 |                    |
| Net income (after royalty fees)                 | 2,178            | 1,990            | 1,994            | -8.4%         | 0.2%          | 2,251               | -11.4%          | 4                  |
| Net margin %                                    | 28.8%            | 22.8%            | 25.1%            | -3.7pp        | 2.3pp         | 27.2%               | -2.1pp          |                    |
| No. of O/S shares (mn) **                       | 7,906            | 7,906            | 7,906            |               |               | 7,906               |                 |                    |
| EPS **                                          | 0.28             | 0.25             | 0.25             | -8.4%         | 0.2%          | 0.28                | -11.4%          | 4                  |
| Capex                                           | 320              | 3,291            | 1,540            | 380.7%        | -53.2%        |                     |                 |                    |
| Capex/revenues                                  | 4%               | 38%              | 19%              | 15.1pp        | -18.3pp       |                     |                 |                    |
| Cash                                            | 14,613           | 11,309           | 12,856           | -12.0%        | 13.7%         |                     |                 |                    |
| Total debt                                      | 2,736            | 3,900            | 5,037            | 84.1%         | 29.1%         |                     |                 |                    |
| Net debt / (cash)                               | (11,877)         | (7,409)          | (7,819)          | -34.2%        | 5.5%          |                     |                 |                    |

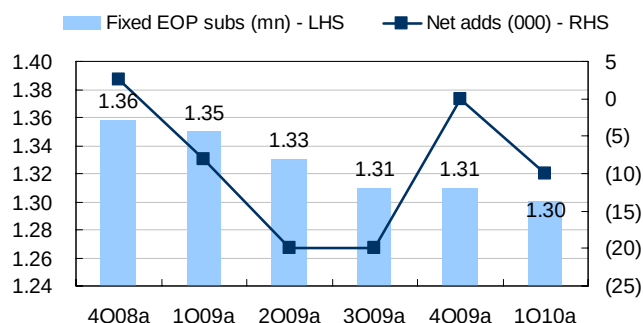
\* Based on an assumed 94% activity ratio.

\*\* 2009 number of shares and EPS are adjusted for bonus shares issued in 2010.

Source: Etisalat financials, Zawya, Bloomberg, and CICR estimates

**Figure 2 | Etisalat's mobile subs growth – quarterly**


Source: Etisalat and CICR database

**Figure 3 | Etisalat's fixed-line subs growth – quarterly**


Source: Etisalat and CICR database

## Contacts and Disclaimer:

### CI CAPITAL RESEARCH

**Mark Rorison | Group Director, Head of Research**  
Mark.Rorison@cich.com.eg

**Amr Hussein Elalfy, CFA | Director**  
Amr.Elalfy@cich.com.eg

**Mona Mansour | Director**  
Mona.Mansour@cich.com.eg



### CI CAPITAL SECURITIES BROKERAGE (EGYPT & UAE)

**Amr Mostafa | Managing Director**  
Amr.Mostafa@cich.com.eg

### DYNAMIC SECURITIES

**Ahmed Roushdy | Managing Director**  
Ahmed.Roushdy@cich.com.eg

### CI CAPITAL HOLDING

8, Nadi El-Seid Street, Third Floor  
Dokki, Giza  
Egypt

Reuters pages: COIW, COIX, COIY, and  
COIZ

Bloomberg page: COIB <GO>

For more information,  
please contact CI Capital Research on +2  
(02) 33 38 62 59,  
send e-mail to Research@cich.com.eg  
or visit our website at www.cich.com.eg

## RATING SYSTEM

In February 2009, CI Capital Research (CICR) launched a new rating system to give analysts more freedom to be market responsive. This is to make one element of our research more dynamic, namely the advertising of target prices and recommendations. What we did not change is our assessment of the Long Term Fair Value (LTFV), nor have we stopped our detailed industry and company research. What we did is changing the target price to trade in the balance of where a share should trade and where we think it will trade.

**LTFV:** As before we continue to estimate a fundamental valuation, largely DCF and/or NAV based.

**Target Price:** The target price, which is not necessarily the LTFV, is where the analyst, given all (qualitative as well as financial) information available, thinks the share price can get to within the next 3-12 months. This can be changed at any time on changing facts, and perceptions.

**Recommendations:** Our new rating system falls out from the total return relating to the share price performance to the target price, and including any distributions as may not be included in the target price calculation. This is shown in the table below, and to be BUY must return over 19%, an arbitrary hurdle rate we think reasonable given prevailing interest rates and risks. (Please see table below.)

#### Recommendation structure:

|             | Change to Target Price |                   |
|-------------|------------------------|-------------------|
| Strong BUY  | > 30%                  | Strong Conviction |
| BUY         | > 20% < 30%            |                   |
| Hold        | > 10% < 20%            |                   |
| Underweight | > 0% < 10%             |                   |
| SELL        | < 0%                   |                   |

## DISCLAIMER

The information used to produce this market commentary is based on sources that CI Capital Research (CICR) believes to be reliable and accurate. This information has not been independently verified and may be condensed or incomplete. CICR does not make any guarantee, representation or warranty and accepts no responsibility or liability to the accuracy and completeness of such information. Expression of opinion contained herein is based on certain assumptions and with the use of specific financial techniques that reflect the personal opinion of the authors of the commentary and is subject to change without notice. It is acknowledged that different assumptions can always be made and that there is a wide choice of techniques that can be adopted each of which can lead to a different conclusion. Therefore, all that is stated herein is of an indicative and informative nature as forward-looking statements, projections, and fair values quoted may not be realized. Accordingly, CICR does not take any responsibility for decisions made on the basis of the content of this commentary. This commentary is made for the sole use of CICR's customers and no part or excerpt of its content may be redistributed, reproduced or conveyed in any form, written or oral, to any third party without the prior written consent of CICR. This commentary does not constitute a solicitation or an offer to buy or sell securities.