

Short-Term Rec.: Accumulate
Long-Term Rec.: Buy

Current Price*: AED 10.6
LT Fair Value : AED 16.7

• **A Good Quarter, Strong Usage Saves the Day:** Consolidated figures were overall better-than-expected, especially at the level of the EBITDA margin. Strong usage experienced during the quarter has more than compensated for the decline in the subscriber base and provided some comfort with regard to revenue performance in upcoming quarters. Mobily, the Saudi subsidiary, continues to beat our estimates. The operation is the second biggest contributor to our valuation for Etisalat (9.7%). The better-than-expected results support our positive stance on the stock and we reiterate our ST Accumulate / LT Buy recommendation on the stock with an unchanged fair value of AED16.7.

• **Negative Additions in the UAE, For the First Time:** Mobile net additions have turned negative for the first time, while negative additions in fixed-line subscribers continued for the second consecutive quarter. This is an area of concern given that the UAE operation constitutes 85.5% of our estimated equity value for Etisalat. We expect further decline in the subscriber base during 3Q (after the summer) but strong revenue suggests that the subscriber loss is mostly at the level of lower spending subscribers.

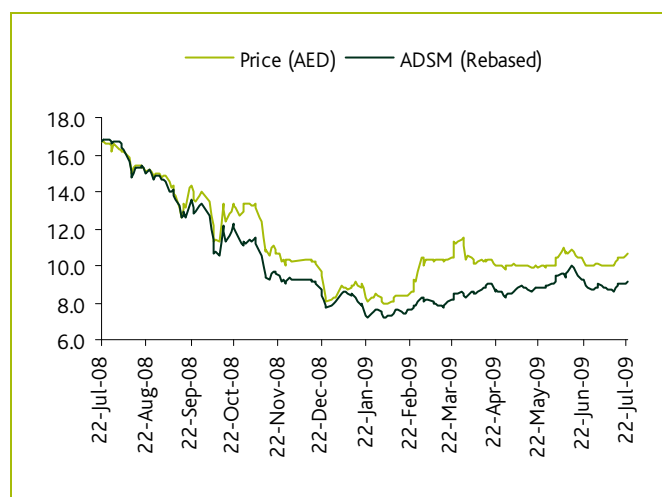
• **Local Revenue Ahead:** Consolidated net revenue came in at AED7,625 million, only 2.6% ahead of our estimate. Revenue generated from the UAE during 2Q2009a exceeded our estimate by 3.6%, which indicates that usage in the UAE was better-than-expected and better than last quarter, given a decline in the subscriber base for both mobile and fixed-line (-2%), which also came lower than 1Q2009a (-1%).

• **EBITDA Margin Surprises After Four Quarters of Deterioration:** The consolidated EBITDA margin was 69.5%, (2Q2009e: 63.0%, 1Q2009a: 64.6%). This improvement in margin comes after four consecutive quarters of deterioration, mainly on lower start-up margins and pressure on the UAE margin. The improvement is due to operating expenses optimization strategies. According to management, this level of margins is sustainable for the rest of the year. This is in line with our FY2009e EBITDA margin estimate of 67.4%.

• **Associates Surprise Positively:** Associates contributed with AED191 million to Etisalat's bottom line in 2Q2009a, higher than our estimate of AED127 million. The better-than-expected figure was mainly due to better-than-expected earnings at Mobily and XL (Indonesia).

• **Earnings Beat Estimates:** Earnings came in at AED2,415 million, up 11% Q-o-Q and 11% above our estimate of AED2,167 million. Higher-than-expected earnings are due to the better-than-expected EBITDA margin and better-than-expected income from associates.

FLASH NOTE



	2009e	2010e	2011e
EPS*	1.20	1.23	1.27
PER(x)	8.8	8.6	8.3
DPS	0.48	0.47	0.49
Div. Yield	4.5%	4.5%	4.6%
CFPS	1.34	1.57	1.61
PCF(x)	7.9	6.8	6.6
BVPS	4.03	4.27	4.52
PBV(x)	2.6	2.5	2.3

* Attributable

Stock Data

Last Ex-Div Date	AED0.35 on 01 Apr 09
Mkt. Val. / Shares (mn)	AED76,186 / 7,187
Av. Monthly Liqd. (mn)	AED341.6
52-Week High / Low	AED16.79 / 7.75
Bloomberg / Reuters	ETISALAT UH / ETEL.AD
Est. Free Float	40.0%

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SUBSCRIBERS – UAE POPULATION SHRINKS

Etisalat's total subscriber base has grown c27% Y-o-Y in 2Q2009 to 61.7 million subscribers (excluding XL subscribers in Indonesia as the figure is not yet reported). Including the 16%-owned Indonesian subsidiary, we estimate Etisalat's total subscriber base will reach 104.3 million by year-end. As per our FY2009e estimates, Indonesia is the largest contributor to Etisalat's subscriber base with 34% of the total, followed by Pakistan with 26% and Saudi Arabia 14%.

For the first time, Etisalat posted negative additions in the UAE losing 81,000 mobile subscribers during 2Q2009 versus our estimate for positive additions of 70,000. We believe this is a direct impact of the population decline in the UAE. Etisalat reached 7.26 million mobile subscribers in the UAE at the end of June. On the fixed-line front, and for the second consecutive quarter, Etisalat lost some of its fixed-line subscribers in the UAE, reporting negative additions of 19,000 in 2Q2009, worse than the 15,000 lost in 1Q2009, and lower than our estimate for positive additions of just 5,000 subscribers. The total fixed-line subscriber base in the UAE reached 1.33 million at the end of June.

Figure 1: Etisalat Subscribers Breakdown by Operation

	June 2008a	June 2009a	FY2009e
UAE	8.18	8.59	9.08
Egypt	4.52	10.26	8.03
Atlantique	3.57	3.93	5.85
Zantel	1.08	1.00	N/A
Canar	0.18	0.17	N/A
Afghanistan	0.67	1.95	1.15
Nigeria	-	1.30	3.53
Saudi Arabia	11.14	13.40	14.25
Indonesia	-	N/A	35.17
Pakistan	19.24	21.14*	27.28
Total	48.56	61.74	104.33

*Until end of May 2009

Source: Etisalat, Regulators, and EFG-Hermes estimates

REVENUE – STRONG USAGE IN THE UAE

We calculate 2Q2009 consolidated net revenue (excluding in-payments, but including out-payments and discounts) came in at AED7,625 million (+7.1% Q-o-Q, +7.0% Y-o-Y), 2.6% ahead of our estimate.

Revenue generated from the UAE constituted 89% of the quarter's total revenue, coming in at AED6,779 million (+5.5% Q-o-Q, +2.4% Y-o-Y), exceeding our estimate by 3.6%. This indicates that usage in the UAE was better-than-expected and better than last quarter, given a decline in the subscriber base for both mobile and fixed-line (-2%), which also came lower than 1Q2009a (-1%). This leaves revenue from international operations (mainly Egypt, Afghanistan and Atlantique Telecom) at cAED846 million, growing 21.4% Q-o-Q, missing our estimate by 4.2%.

During the analysts' meeting on 20 July 2009, management stated that the solid growth in UAE revenue is attributable to the diversification in revenue sources the company has been following in order to offset subscribers' negative growth. Management specifically underlined the surge in data and internet revenues in the UAE, which, combined, have contributed 25% of UAE revenues in 1H2009 as opposed to 20% in 1H2008. Management also said the decline in international traffic on mobile phones is responsible for the slowing mobile revenues as opposed to the fast-growing data and internet revenues.

Figure 2: Revenue Breakdown by Fully Consolidated Operations

AED million, unless otherwise stated

	1H2009a	Contribution	FY2009e
UAE	13,212	89.6%	23,918
Egypt	799	5.4%	1,722
Atlantique	475	3.2%	2,062
Zantel	77	0.5%	222
Canar	106	0.7%	271
Afghanistan	75	0.5%	267
Total	14,744	100%	28,462

Source: Etisalat, EFG-Hermes estimates

Figure 3: ARPU Breakdown by Fully Consolidated Operations

AED, unless otherwise stated

	1H2008a	1H2009a	FY2009e
UAE*	197.5	178.4	170.3
Egypt	21.0	19.0	21.5
Atlantique	40.0	29.0	33.9
Zantel	16.0	16.0	N/A
Canar	141.0	156.0	N/A
Afghanistan	17.0	13.0	25.2

*UAE actual ARPU is based on our calculations

Source: Etisalat, EFG-Hermes estimates

EBITDA MARGIN PICKS UP ON COST OPTIMIZATION, TO PERSIST

The consolidated EBITDA margin in 2Q2009a stood at 69.5%, as per our calculations, much better than our estimate of 63.0% and better than the 1Q2009a margin of 64.6%. This improvement in margin comes after four consecutive quarters of deterioration, mainly as a result of lower margin at the level of start-ups as well as pressure on the UAE margin.

Etisalat's management attributed the remarkable EBITDA margin mainly to the cost optimization plan which was implemented across the group. Also, management believes the high margin to remain sustainable at this level for the rest of the year 2009 with 2H2009e margin coming higher than that of 1H2009a (67.5%), as the Opex optimization strategies are maintained. We therefore believe that Etisalat could beat our FY2009e EBITDA margin of 67.4%.

Consolidated EBITDA for 2Q2009a, according to our calculation, was AED5,299 million (+15.2% Q-o-Q, +13.4% Y-o-Y), 13.2% ahead of our estimate.

Figure 4: Etisalat EBITDA and EBITDA Margin Breakdown by Operation During 1H2009

AED million, unless otherwise stated

	EBITDA	Contribution	EBITDA Margin
UAE	9,748	98.0%	73.8%
Egypt	146	1.5%	18.3%
Atlantique	178	1.8%	37.5%
Zantel	(32)	-0.3%	-41.5%
Canar	40	0.4%	37.5%
Afghanistan	(42)	-0.4%	-55.6%
India	(92)	-0.9%	
Total	9,947	100%	67.5%

Source: Etisalat

ASSOCIATES – MOBILY AND XL SURPRISE POSITIVELY

Associates, which are consolidated under the equity method, surprised positively during 2Q2009, contributing with AED191 million to Etisalat's bottom line, higher than our estimate of AED127 million. Associates include mainly Pakistan Telecommunication Company Limited PTCL in Pakistan (26% owned), Etihad Etisalat (Mobily) in Saudi Arabia (27.4% owned), Etisalat Nigeria in Nigeria (40% owned) and Excelcomindo (XL) in Indonesia (15.97% owned). The better-than-expected figure was mainly due to better-than-expected earnings at Mobily and XL. Mobily reported 2Q2009a earnings of SAR675 million (AED662 million), 23% ahead of our estimates.

EARNINGS BEAT ESTIMATES

Earnings for 2Q2009a came in at AED2,415 million, 11% higher than last quarter and 11% higher than our estimate of AED2,167 million. Etisalat's better-than-expected earnings came on the back of the stronger-than-expected EBITDA margin as well as the strong performance of the associates.

INTERIM DIVIDEND

Etisalat board of directors announced an interim cash dividend for 1H2009 of AED0.25 per share for shareholders till 27 July 2009 to be paid on 6 August. This implies a payout ratio of 39% based on 1H2009a earnings. We have an estimate of AED0.48 for FY2009e, which implies a payout ratio of 40% and a dividend yield of 4.5% based on today's closing price.

Figure 5: Etisalat 2Q2009 Historical and Forecast Income Statement
AED million, unless otherwise stated

KPIs (000's)	2Q08a*	3Q08a	4Q08a	1Q09a	2Q09a	Y-o-Y	Q-o-Q	2Q09e	Var.
Mobile Subs (UAE)	6,830	7,050	7,285	7,341	7,260	6.3%	-1.1%	7,411	-2.0%
Mobile Additions	200	220	235	56	(81)			70	
FL Subs (UAE)	1,350	1,360	1,364	1,349	1,330	-1.5%	-1.4%	1,354	-1.8%
FL Additions	20	10	4	(15)	(19)			5	
Income Statement									
Net Revenue	7,128	6,626	7,050	7,119	7,625	7.0%	7.1%	7,428	2.6%
Total Costs	(2,453)	(2,050)	(3,546)	(2,519)	(2,162)			(2,751)	
EBITDA	4,675	4,576	3,504	4,601	5,299	13.4%	15.2%	4,677	13.3%
<i>EBITDA Margin</i>	65.6%	69.1%	49.7%	64.6%	69.5%			63.0%	
Depreciation & Amortization	(610)	(555)	(755)	(486)	(668)			(587)	
EBIT	4,065	4,021	2,748	4,115	4,631	13.9%	12.6%	4,090	13.2%
<i>Margin</i>	57.0%	60.7%	39.0%	57.8%	60.7%			55.1%	
Net Interest Income (Expenses)	(170)	5	83	122	(55)			86	
Other Income (Expenses)	1,784	22	(55)	-	-			-	
Associates	140	180	34	12	191	36.3%	1521.2%	127	51.0%
EBMI	5,819	4,228	2,810	4,249	4,767	-18.1%	12.2%	4,303	10.8%
Minority Interest	157	106	65	159	90			80	
EBTR	5,976	4,334	2,876	4,408	4,857	-18.7%	10.2%	4,383	10.8%
Deferred Taxes	(32)	(65)	(51)	(52)	(27)			(49)	
EBR	5,944	4,270	2,825	4,356	4,830	-18.7%	10.9%	4,334	11.4%
Royalty Fees	(2,995)	(2,135)	(1,413)	(2,178)	(2,415)			(2,167)	
Net Profit	2,949	2,135	1,413	2,178	2,415	-18.1%	10.9%	2,167	11.4%

*Restated

Source: Etisalat, EFG-Hermes estimates

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