



EFG - Hermes

Etisalat

Third Quarter Results Review

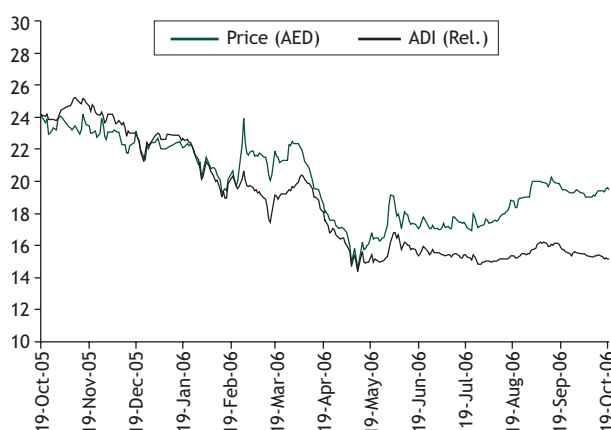
19 October 2006

UAE | Telecom

ST Rec. : Buy
LT Rec. : Buy

Current Price*: AED 19.55
LT Fair Value : AED 30.70

- Etisalat reported strong 3Q2006 results, with consolidated net revenues, EBITDA and net profits rising Y-o-Y by 29%, 38% and 42%, respectively. The UAE subscriber base grew 19% y-o-y with Etisalat achieving the highest number of mobile subscriber additions over the past 12 months in 3Q to reach 5.3 million, 22% up y-o-y.
- The EBITDA margin improved significantly, rising 10 pp to 76% in 3Q06 versus 3Q05. We attribute this to a 13% y-o-y decline in operating expenses as a result of Etisalat's cost saving strategy.
- Etisalat announced that it is bidding for controlling stakes in both Greece's third largest mobile operator and the Sri Lankan fixed line incumbent, Sri Lanka Telecom. Etisalat also mentioned that it is in advanced talks with the owners of Yemeni mobile operator Sabafon and several other deals.
- Etisalat paid its share in the license payment of the third Egyptian mobile license which was acquired in a consortium in July 2006. Etisalat owns a 66% stake in the consortium. We will be incorporating the Egyptian operations into our forecasts in our forthcoming update.
- We will be issuing an update shortly. Our forecasts will reflect the high growth in both the UAE and Saudi markets and the better-than-expected performance of Etisalat in both markets in 2006. Furthermore, we are revising our assumptions regarding the local competition in the UAE after the forthcoming entry of second operator Du and the implementation of number portability in Saudi Arabia, which we believe will benefit Mobily.
- Even though Etisalat is trading at a relatively high 2006e P/E of 16.5x compared to the MENA sector average of 14.6x, we are still positive on the prospects of the company, given the growing or steady stream of earnings the company is expecting from its Saudi/Pakistani operations in addition to the room for positive surprise on the acquisition front.



	2005a	2006e	2007e
EPS*	0.94	1.11	1.29
PER(x)	20.8	17.5	15.1
DPS	0.40	0.56	0.77
Div. Yield	2.1%	2.9%	4.0%
CFPS	1.1	1.7	1.8
PCF(x)	17.1	11.8	10.6
BVPS	3.5	4.0	4.5
PBV(x)	5.6	4.9	4.3

*Attributable

Stock Data:

Last Ex-Div Date	AED0.25 on 19 July 06
Mkt. Val. (mn)	AED88,481
Shares (mn)	4538
Av. Mthly Liqd. (mn)	AED407
52-Week High / Low	AED24.8 / 14.3
Bloomberg / Reuters	ETISALAT UH / ETEL.AD
Est. Free Float	40.0%

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*As at 19 October 2006

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3Q2006 RESULTS

Etisalat delivered a strong set of results in 3Q2006, showing strong Y-o-Y growth in consolidated net revenues, EBITDA and net profits of 29%, 38% and 42%, respectively. Consolidated net revenues came in at AED 4.1 billion in 3Q2006 versus AED3.2 billion for the same period last year, mostly on the back of growth in Etisalat's UAE subscriber base (fixed line, mobile and internet) of 19% Y-o-Y. By the end of September 2006, fixed lines grew 4% to 1.3 million, mobile subscribers grew 22% to 5.3 million and internet subscribers grew 34% to 0.6 million Y-o-Y, respectively. 3Q3006 was the best quarter in terms of mobile subscriber additions over the past twelve months, despite the penetration rate exceeding 100% since June 2006, with Etisalat gaining 264,000 subscribers in the three months ending September, representing growth of 15% Q-o-Q and 12% Y-o-Y.

EBITDA came in at AED3.5 billion, with the EBITDA margin improving significantly in 3Q2006 to reach an estimated 76%, up from 66% in 3Q2005. We attribute the rise in margins to the decline in operating expenses (opex), falling 13% Y-o-Y due to what we believe to be a cost saving strategy implemented by Etisalat over the past period. As a result, the opex/sales ratio fell to 24% in 3Q2006 down from 34% in 3Q2005. Among the expenses that have declined are outpayments to other telecom operators which fell 16% Y-o-Y and selling, general and other expenses which dropped 11% over the same period. Earnings after the royalty came in at AED1.6 billion in 3Q2006 compared to AED1.1 billion in 3Q2005. Information regarding the 3Q2006 performance of Etisalat's Saudi operation (Mobily) is currently not available.

Table 1: Etisalat Quarter Results

AED mn	3Q05	3Q06	Y-o-Y	9M05	9M06	Y-o-Y
Net Revenues	3,161	4,072	29%	9,362	11,815	26%
Gross Revenues	3,856	4,649	21%	11,338	13,537	19%
Cost of Sales	(1,293)	(1,124)	-13%	(3,887)	(3,942)	1%
EBITDA	2,563	3,525	38%	7,451	9,595	29%
EBITDA Margin	66%	76%		66%	71%	
Depreciation Expenses	(305)	(315)	3%	(914)	(957)	5%
Other Income (Expenses)	(34)	(49)	43%	(75)	152	
Profit before Royalty and MI	2,223	3,162	42%	6,462	8,791	36%
Royalty	(1,112)	(1,573)	41%	(3,231)	(4,386)	36%
Minority Interest	-	(15)		-	(19)	
Net Profit	1,112	1,574	42%	3,231	4,386	36%

Source: Etisalat

Recent Events

Payment of Egyptian 3rd Mobile License

In July 2006, an Etisalat-led consortium won the bid for the third mobile license in Egypt for a total consideration of USD2.9 billion. Etisalat holds a 66% stake in the consortium while the rest is divided among Egyptian partners. As per the terms of the license, the consortium paid the USD2.9 billion in the last quarter. This was divided among the members of the consortium on a pro rated basis. The payment by Etisalat was either made from its existing cash balance, which reached USD2.2 billion in 1H2006, or through the USD3 billion credit facility the company recently secured for future expansions.

Etisalat Expanding Globally

Etisalat announced on Reuters on 17 October 2006 that it is bidding to acquire both a controlling stake in TIM Hellas, Greece's third largest mobile operator and Sri Lanka Telecom, the country's incumbent fixed line operator. According to the press, TIM Hellas owners, private equity firms Texas Pacific Group and Apax Partners, hope to sell the operator for up to EUR4 billion. TIM Hellas has 2.3 million (2005) mobile subscribers, representing 19% market share of the Greek mobile market. The mobile penetration rate is currently estimated to be around 110% (2005) with four players in the market including TIM Hellas.

By the end of December 2005, Sri Lanka Telecom has 78% market share in the fixed line market and 9% in the mobile market through its mobile arm, Mobitel. Nippon Telegraph and Telephone Corporation of Japan owns a 35 % stake in Sri Lanka Telecom. Fixed line and mobile penetration rates in Sri Lanka reached 6% and 16% (2005), respectively, with seven players in the mobile market.

Etisalat also announced that it has reached an advanced stage in negotiations with the shareholders of privately owned Yemeni mobile operator Sabafon. Fixed and mobile penetration rates in Yemen are 4% and 11% respectively (2005). Etisalat mentioned that it is also in talks to acquire stakes in operators in Algeria, Ghana, Kenya and India.

Valuation and Recommendation

We are in the process of revising our forecasts to reflect the high growth in both the UAE and the Saudi markets and the better-than-expected performance of Etisalat in both markets in 2006. We will also revise our market share loss assumptions for Etisalat following the entry of the second mobile operator, Du, as we believe it will be higher than suggested by our current forecasts, especially with the imminent introduction of Mobile Number Portability. Furthermore, we will incorporate Etisalat's Egyptian mobile operation into our forecasts starting 2007.

We do not anticipate a significant negative impact on our fair value for Etisalat from the anticipated increase in competition in the UAE as we believe the negative impact in the UAE would be partially offset by an upgrade in our estimated fair value for Mobily.

Even though Etisalat is trading at a relatively high 2006e P/E multiple of 16.5x, while the MENA sector average is at 14.6x, we are still positive on the company. We believe that Etisalat is trying to position itself in relatively high growth/stable markets in order to secure a steady source of earnings in anticipation of saturation and the imminent introduction of competition in its home market. Going forward, the Saudi operation, Mobily, is expected to be a significant contributor to Etisalat's bottom line (13% of 2008e pre-royalty earnings), Mobily is expected to breakeven in 2006. Moreover, the steady stream of earnings from the Pakistani operation is expected to provide another cushion for earnings.

Furthermore, Etisalat's recent active stance on acquiring new licenses or existing stakes creates room for positive surprise should Etisalat win the bid(s) in one of the high growth markets, bearing in mind, of course the level of competition in each market. For the purpose of our valuation, these acquisitions are not yet accounted for, given the uncertainty of winning any of these bids and negotiations. We will shortly be issuing an update with new forecasts.

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