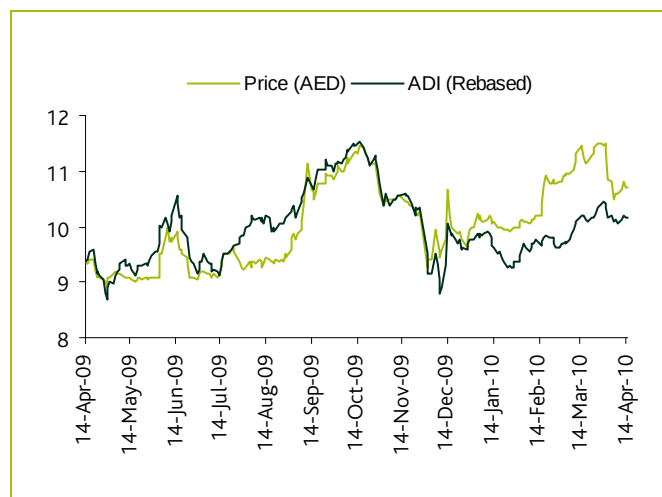




Current Price* : AED 10.7 Rating: Buy
Fair Value (FV): AED 14.5

- 4Q2009 Hit by One-Offs, 1Q2010 Should Look Better:** Management explained that 4Q2009's sharp decline in both the EBITDA margin and bottom line, despite strong top line growth, was the result of one-off provisions both above and below the EBITDA line that are typically booked at the year-end. These are unlikely to reoccur in 1Q2010.
- UAE Margins To Remain Under Pressure:** We think it doubtful that margins will return to previous levels, due to competition and pricing pressure in the UAE. Etisalat recently started to reduce its UAE effective tariffs through a number of different offers and promotions, with the aim of retaining its subscriber base and to try and attract as many new subscribers as possible given the slowdown in population growth and mobile market saturation. This has put pressure on its ARPU's and margins.
- Gearing Up for a Major Acquisition?** Etisalat has a bond programme ready that it is about to register and set aside for any potential investment opportunity. Etisalat already has a large cash position, of AED11.3 billion at the end of 2009, which could be further expanded by any potential future bond proceeds. This puts Etisalat in a strong position to snap up any potential opportunities in the region, with the ability to probably outbid any rivals. Etisalat is interested in operating in Libya where it has already submitted a bid for a license, and Syria where a new license is being formulated, in addition to the possibility of acquiring part of Korek Telecom in Iraq and Djezzy in Algeria.
- Mixed Operational Performance:** Despite its minimal contribution to Etisalat's consolidated revenue and earnings, Afghanistan was generally the top performing operation in 2009, with the highest revenue growth (163%) and highest subscriber growth (130%). Etisalat Misr's performance was also very strong, with revenue and subscribers more than doubling, and having broken even on earnings level in January 2010 ahead of our expectation (2014e). The UAE operation had stable revenues Y-o-Y although the UAE mobile revenue segment was down c8% Y-o-Y.
- Reiterate Buy, but Still Waiting For the Catalyst:** We continue to like Etisalat's diversified yet balanced portfolio of assets. Etisalat continues to trade at a discount to its regional peers (2010e P/E of 9.8x vs 11.6x and EV/EBITDA of 3.7x vs 5.7x), as it is still closed to foreign ownership. We reiterate our Buy recommendation, with our FV offering 35% upside potential over the current market price.

FLASH NOTE



*price as at 14 April 2010

	2010e	2011e	2012e
EPS	1.09	1.11	1.18
PER (x)	9.8	9.6	9.0
DPS	0.43	0.42	0.45
Div. Yield	4.1%	3.9%	4.2%
CFPS	1.31	1.54	1.55
PCF (x)	8.2	6.9	6.9
BVPS	3.84	3.83	3.85
PBV (x)	2.8	2.8	2.8

Figures in AED, unless otherwise stated

Stock Data

Last Dividend Date	AED0.35 on 1 Apr. 10
MCap./ Shares (mn)	AED84,596 / 7,906
Local Av. Mthly Liqd.	AED230.6 mn
52-Wk. High/Low	AED11.50 / AED8.92
Bloomberg / Reuters	ETISALAT.UH / ETEL.UH
Est. Free Float	40%

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We attended Etisalat's analyst day on Wednesday 7 April 2010 at the company's premises in Abu Dhabi, during which management presented key operational and financial highlights for the FY2009 results. Below are the main points and themes discussed.

A DEEPER GLIMPSE INTO 4Q2009 RESULTS

The weakness in 4Q2009's EBITDA margin was due to one-offs, according to management, as the EBITDA was hit by year-end provisions that are predominantly, if not all, booked in December. Etisalat's 4Q2009 consolidated EBITDA margin was 53.0%, significantly lower than the previous quarter's margin of 67.6%. According to management, the final quarter usually sees lower margins as certain company expenditure is back loaded to the end of the year. This implies that margins should recover again in 1Q2010. We expect a 1Q2010 EBITDA margin of 63.8%.

Finance costs during the quarter were also negatively impacted by some one-off items that were not related to interest expense. Total finance costs in 4Q2009 more than tripled Q-o-Q to AED292 million, from AED86 million in 3Q2009.

At the FY2009 level, management attributed the 85% Y-o-Y leap in capex to the deployment of the "Fibre To The Home" (FTTH) network in the UAE, as well as to the network rollout in India and other international operations, which served a total subscriber base of c108 million at the end of the year.

WHERE DOES ETISALAT'S STRATEGY STAND NOW?

One of the main pillars of the company's strategy is to continue growing the contribution of international operations to both its portfolio of assets and its operational results/performance. While management continues to look at all available investment opportunities that emerge, they confirmed that they will continue to be conservative regarding any acquisitions or investments, as well as in managing the company's financial resources. One of the most important criteria for selecting investments is the IRR, and management will not consider an investment with an IRR below 10%. However, this is not the only criteria assessed and some of them, such as synergies between different operations, may not be precisely quantifiable when considering a given opportunity.

The bond issuance: In order to remain prepared for any potential future opportunity, Etisalat has prepared a bond programme that it will soon register. However, in the near future (or the next few months) management does not have any intention of launching or selling these debt securities, they are instead preparing for any eventuality. Reuters had quoted CFO Salem Al-Sharhan back in October 2009 saying that the size of the planned issuance is around USD500 million (AED1.8 billion).

High-tech investment: Etisalat plans to continue investing in infrastructure that supports advanced technologies in its operations generally and in the UAE specifically, as it seeks to overcome the saturation of the more basic fixed and mobile telephony segments. Management is expecting to complete the deployment of the fibre optic network, which will enable FTTH, in 4Q2010. This will enable Etisalat to launch its new double and triple-play offers (a combination of high-quality fixed telephony, broadband internet, and advanced high-definition TV in a single package) under the name "eLife".

M&A UPDATE

In line with its regional expansionary strategy, Etisalat is considering a number of attractive investment opportunities. Amongst these are the following:

KSA: Media sources recently reported that Etisalat was planning to raise its stake in its 27%-owned Saudi Arabian unit, Mobily. Management clarified that they are indeed hoping to increase their stake in Mobily, to between 35% and 51%.

Algeria: Management reiterated their interest in Orascom Telecom's (OT) Algerian unit, Djazzy, and confirmed that they are looking at it. However, there has not as yet been any official communication with OT, nor with the Algerian government.

Sudan: In Sudan Etisalat is discussing the possibility of obtaining a 3G licence with the government.

Iraq: Management rebuffed recent media reports saying that Etisalat had signed a MoU to acquire a majority stake in Korek Telecom. However, they added that they have been in advanced discussions to acquire such a stake for two years, but these have been hampered by the difficulty of asset pricing due to the country's instability.

Libya: Etisalat has already submitted a bid for a Greenfield licence, but it is yet to receive details of the outcome of the bidding process.

Syria: The government is said to be in the process of drafting a licence and, once it is announced, Etisalat intends to bid for it.

India: Etisalat has applied for 3G licences in selected Indian circles, via the online bidding process which was launched on 9 April 2010 on a circle-by-circle basis.

Morocco: In Morocco, Etisalat is looking at all assets and have held discussions with all market players.

PERSPECTIVES ON THE SHIFTING DYNAMICS IN AFRICA

Following the acquisition of Zain Africa by Bharti Airtel, management expressed its pleasure at Bharti's entry into the African market. They believe that as a result of this deal, dynamics should shift in favour of Etisalat's operations in Africa through its subsidiary, Atlantique Telecom (AT). This is due to the following: i) Etisalat has written agreements with Bharti to compete on services, not prices, and to cooperate on technology; ii) agreements already exist with Bharti to share network infrastructure, which Etisalat has been trying to push for in Africa to reduce costs; and iii) Bharti is a rational competitor and is unlikely to seek aggressive price cutting to protect its market share.

Management feels that the entry of Bharti causes no significant threat as it is not present in Etisalat's two main countries of operation in Africa, Benin and Togo. In Africa, Etisalat and Bharti (after the Zain Africa deal) compete in Burkina Faso, Gabon, Niger, Nigeria, and Tanzania.

OPERATIONS' UPDATE

UAE - TOP LINE SLOWDOWN

The slight 1% Y-o-Y decline in revenue in the UAE operation in 2009 was expected by management, with the two main reasons for the decline being: i) the mass outflow of labour force during the year, and ii) the decline in international tariffs. The EBITDA margin was up to 70% in 2009 however, from 64% in 2008, due to cost optimisation measures that are due to continue into 2010.

Smart-phones supporting ARPU figures: With the smart-phone handset accessibility (prices/offers and availability) increasing, management say that smart-phone penetration into the UAE is between 12% and 15%. Although the number of devices was not disclosed, management said that the numbers are almost doubling every year, with ARPUs three to five times higher than for regular handsets.

MNP - Not this year: Management do not expect Mobile Number Portability (MNP) to materialise this year in the UAE. However, when it is introduced they are not worried about it, as they have a good experience from MNP in KSA (Mobily) and do not expect significant subscriber movement when introduced into the UAE. From other countries' experience, we do not expect a significant impact from the MNP service; usually the number of ported subscribers is high during the first few months after the introduction of the service, but afterwards the impact is minimal.

New subscriber reporting: Based on a new mandate from the Telecommunications Regulatory Authority (TRA), Etisalat has moved to an active subscriber reporting system. This implies that the 7.74 million subscribers as at December 2009 were active subscribers, not total, based on the 90-day definition. Management explained that the move took place in 2Q2009, which explains why the company had negative subscriber additions in that quarter, after which it returned to positive growth.

ETISALAT MISR (EGYPT) - BECOMES PROFITABLE, BUT SUBSCRIBER COUNT STILL UNCLEAR

Earnings Breakeven: The operation broke even on an earnings level in January 2010, considerably earlier than our expected 2014e. Management seem upbeat about the operation, which is the main contributor to revenue from international operations (63% of revenue from international operations in 2009).

Revenue & EBITDA Soar: Etisalat Misr's revenue jumped 112% Y-o-Y in 2009 to AED2,628 million, while its EBITDA margin reached 19% (vs just 1% in 2008). Its ARPU was stable Y-o-Y at AED21.

Subscribers - Mostly Data, we Believe: Subscribers more than doubled to 14.3 million at the end of 2009 (vs our estimate of 8.6 million and vs the Egyptian regulator's published figure of 6.67 million). The subscriber figures reported by Etisalat remain an issue of ambiguity for us: 14.3 million subscribers for Etisalat Misr would make a total of 62.9 million subscribers for the Egyptian mobile market at the end of December 2009. This implies a 78.4% penetration rate, which is much higher than our calculated 71.4% based on our estimate of only 8.6 million subscribers for Etisalat Misr.

We suspect that the majority of Etisalat's subscriber count is composed of USB internet devices (which are based on SIM cards). Anecdotal evidence also suggests that a large part of Etisalat Misr's active SIM cards are used for internet purposes in USB devices, not in mobile handsets. We attribute this to a quicker-than-expected uptake in USB internet devices for Etisalat Misr in 2009. This would also explain Etisalat Misr's ARPU level, which has remained almost stable for the past two years. However, until Etisalat discloses a breakdown of its SIM card mix in Egypt, it will remain very difficult to quantify actual mobile subscribers. One issue that remains very vague in our view is the gap between figures reported by Etisalat and those reported by the Egyptian regulator.

AT (AFRICA) - BACK ON TRACK

Etisalat resumed its capex spend on its African operations in 2009. Capex was up almost five-fold Y-o-Y at AED530 million (vs AED114 million in 2008) after a significant reduction in 2008 as a result of several obstacles at the level of various operations. The decision to resume capex spending was based mainly on: i) the successful extension of the licence in Togo, ii) solving a legal case in Benin, and iii) Etisalat increasing its stake in AT to 100% from 82%. These measures were also taken to address concerns raised by both lenders and vendors.

ZANTEL (TANZANIA) - UNDER PRESSURE FROM FIERCE COMPETITION AND HIGH COSTS

A price war was triggered by one of Tanzania's operators and resulted in damage to all operators. For Zantel, 2009 ARPU fell 35% Y-o-Y to AED16, resulting in a 23% Y-o-Y decline in revenue to AED130 million, and a corresponding EBITDA margin drop to -52% from -5% the year before. Operating costs remain very high, with 50% of the operation's headcount being security personnel (for every base station built, 16 security guards must be deployed).

ETISALAT AFGHANISTAN - THE FASTEST GROWING OPERATION

Out of the entire investment portfolio, management say that Etisalat Afghan is the only trouble-free operation and added that it is performing well, both operationally and financially. Revenue in 2009 jumped 161% Y-o-Y to AED218 million, with the EBITDA margin improving to -5% from -120% in 2008. The improving results are due to: i) a 15% Y-o-Y hike in ARPU to AED20, and ii) a 130% Y-o-Y surge in subscribers to 2.7 million in 2009.

NIGERIA - OPAQUE PICTURE

Management declined to provide any figures, but said that the operation missed its revenue target for 2009. Nigeria is experiencing aggressive competition, with the market ARPU falling to just above USD12 in 2009 from USD15-17 in 2008.

INDIA - UNDERTAKES A SOFT-LAUNCH

Etisalat DB India has recently entered into a controlled soft launch phase under the brand "Cheer". The company continues to outsource network infrastructure as the market is based on a low-cost model. Management does not see ARPUs falling any further on the back of competition, as margins are already very tight. Some of the operators' ARPUs are between INR60 and INR80, which management view as insufficient to sustain the business case in India.

GOING FORWARDS INTO 2010...

To a very limited extent, management shared some of their views of how the upcoming year would reflect on Etisalat's business, and they seem to feel that 2010 is going to be yet another tough year. Expressions such as "cost cutting" were used to describe 2010, as opposed to "cost optimisation" for 2009. This means, in our view, that Etisalat will be more aggressive in protecting its margins in 2010. Accordingly this carries an upside risk to our estimated FY2010 EBITDA margin of 66.2%.

With regards to capex, management said that the UAE's capex should remain approximately the same Y-o-Y at cAED2.3-2.5 billion in 2010e. The completion of the FTTH network will continue to weigh on the capex bill and, once completed, spending will focus on the deployment of the Long-Term Evolution (LTE) technology. This is likely to result in capex remaining at the same levels in the short to medium term.

Figure 1: FY2009 Operations' Results

	2008a	2009a	Y-o-Y
Subscribers (mn)			
Etisalat UAE	7.3	7.8	7.6%
Atlantique Telecom	3.7	4.8	27.5%
Etisalat Misr (Egypt)	6.8	14.3	109.2%
Zantel (Tanzania)	1.0	1.4	32.9%
Canar (Sudan)	0.2	0.1	-20.3%
Etisalat Afghan	1.2	2.7	129.6%
ARPU (AED)			
Etisalat UAE	166	139	-16.3%
Atlantique Telecom	40	28	-30.0%
Etisalat Misr (Egypt)	21	21	3.0%
Zantel (Tanzania)	25	16	-36.0%
Canar (Sudan)	146	195	33.6%
Etisalat Afghan	18	20	11.1%
Revenue (AED mn)			
Etisalat UAE	26,808	26,617	-0.7%
Atlantique Telecom	864	969	12.2%
Etisalat Misr (Egypt)	1,237	2,628	112.4%
Zantel (Tanzania)	169	130	-23.1%
Canar (Sudan)	193	195	1.0%
Etisalat Afghan	83	218	162.7%
EBITDA (AED mn)			
Etisalat UAE	17,134	18,449	7.7%
Atlantique Telecom	148	362	144.6%
Etisalat Misr (Egypt)	7	772	N/M
Zantel (Tanzania)	(9)	(67)	N/M
Canar (Sudan)	26	54	107.7%
Etisalat Afghan	(100)	(12)	N/M
EBITDA Margin			
Etisalat UAE	63.9%	69.3%	
Atlantique Telecom	17.1%	37.4%	
Etisalat Misr (Egypt)	0.6%	29.4%	
Zantel (Tanzania)	-5.3%	-51.5%	
Canar (Sudan)	13.5%	27.7%	
Etisalat Afghan	-120.5%	-5.5%	
Capex (AED mn)			
Etisalat UAE	1,985	2,545	28.2%
Atlantique Telecom	114	530	364.9%
Etisalat Misr (Egypt)	1,288	1,729	34.2%
Zantel (Tanzania)	314	91	-71.0%
Canar (Sudan)	15	42	180.0%
Etisalat Afghan	126	246	95.2%

Source: Etisalat

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