



EFG - Hermes

Qatar Telecom

Last Player in the Queue of Liberalization

06 January 2007

Qatar | Telecom

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ST Rec. : Buy
LT Rec. : Buy

Current Price* : QAR 231.8 / AED 224.9
Fair Value : QAR 372.8 / AED 375.9

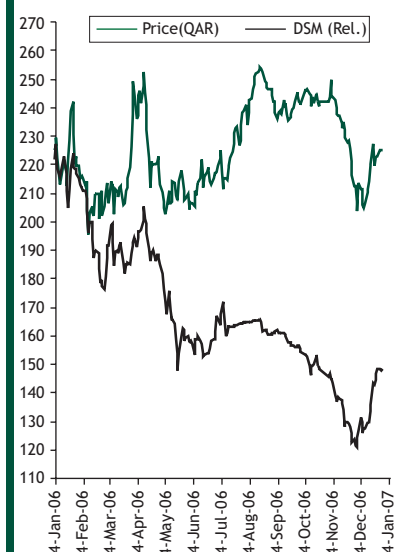
- Qtel's 9M2006 results came in better-than-expected, recording 44%, 47% and 39% Y-o-Y growth in revenue, EBITDA and post-royalty net profit respectively. The good results are mostly attributable to strong revenues in both the wireless and wireline businesses and the Omani subsidiary breaking even on an EBITDA level six months ahead of our expectations.
- Growth in wireless revenue has been mainly driven by robust mobile subscriber growth in both the local and Omani markets. Qtel's mobile subscriber base rose 57% Y-o-Y to reach 1.3 million by the end of September 2006, with Nawras subscribers in Oman accounting for 36%.
- Qatar's regulatory authority announced the liberalization of the telecom market in 2007. Details regarding the scope and timeframe have not yet been determined. We continue to assume partial liberalization of the telecom market, with Qtel remaining the sole provider in the fixed and international voice markets. We move the first year of competition and decline in the royalty payment as a result of the monopoly, from 2007 as previously assumed to 2008.
- We revise both our fixed line and mobile subscriber estimates in Qatar, forecasting 9% and 28% growth in 2006 subscribers, respectively. We also raise the Nawras subscriber estimate by 3% to reflect the strong subscriber uptake partially driven by MNP implementation in 2H2006 in Oman.
- We revise upwards estimates for Qtel's consolidated revenue and EBITDA for 2006 by 10% and 18% to reflect the strong growth in local wireless and wireline revenues in addition to a faster-than-expected improvement at Nawras at the EBITDA and bottom line levels. We forecast Nawras net profit will turn positive in 2007, one year ahead of our expectations.
- We upgrade our estimated fair value for Qtel by 25% to QAR372.8 to reflect the expected solid financial performance of Qtel from 2006 to 2008. We maintain our ST Buy and upgrade our LT recommendation to Buy, given the significant 61% upside to our FV and the attractive P/E multiples. Qtel is trading on a P/E 07e of 11.1x and 08e of 9.4x versus EMEA sector averages of 13.7x and 12.5x, respectively.

December year end	2005a	2006e	2007e	2008e
Operating Income	1,407	2,168	2,743	2,684
Net Attrib. Income	1,171	1,714	2,079	2,469
ROE	31.0%	37.8%	37.3%	35.9%
EPS	11.71	17.14	20.79	24.69
EPS Growth	-20.7%	46.4%	21.3%	18.8%
P/E* (Attrib.)	19.8	13.5	11.1	9.4
DPS	8.50	9.52	10.47	11.63
Dividend Yield	3.7%	4.1%	4.5%	5.0%
BVPS	37.76	45.39	55.70	68.76
P/BV	6.14	5.11	4.16	3.37
CFPS	18.65	23.54	26.65	25.41
P/CF	12.4	9.8	8.7	9.1
EBITDA	1,725	2,591	3,218	3,219
EBITDA Margin	57.8%	61.3%	62.8%	60.3%
EV/EBITDA	13.1	8.7	6.8	6.6
EV/Sub (Blended)	21,383	15,597	12,518	11,483
Net Debt (Cash)**	(586.9)	(518.8)	(1,434.4)	(1,982.4)
Net Debt (Cash)/ BV	-16%	-11%	-26%	-29%
Net Debt (Cash)/ Mkt cap	-3%	-2%	-6%	-9%

**Excluding Dividends

Figures are in QAR unless otherwise stated

Estimate Changes					
(QAR mn)	2005a	Old 2006e	New 2006e	Old 2007e	New 2007e
Revenues	2,982	3,840	4,223	4,396	5,126
EBITDA	1,725	2,204	2,591	2,575	3,218
EBITDA Margin	57.8%	57.4%	61.3%	58.6%	62.8%
Net Attrib. Inc. (mn)	1,171	1,460	1,714	2,068	2,079



Stock Data:

Last Ex-Div Date	QAR4.25 on 30 July 06
Mkt. Value (Local mn)	QAR23,180
Shares (mn)	100
Av. Mthly Liqd. (mn)	QAR105.3 mn
52-Week High/Low	QAR252.7 / 201.2
Bloomberg/Reuters	QATA BI / QTEL.QA
Est. Free Float	45.0%

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*As at 04 January 2007

KINDLY REFER TO THE IMPORTANT DISCLOSURES AND DISCLAIMER ON PAGE 11.

I. FINANCIAL ANALYSIS AND RECENT DEVELOPMENTS

9M2006 Overview

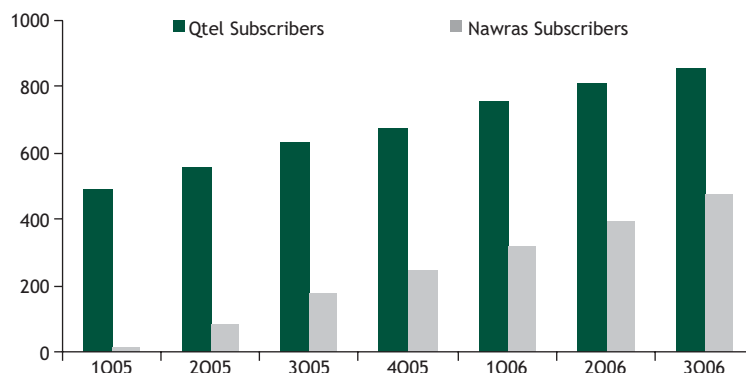
Qtel delivers stronger-than-expected results in both Qatar and Oman...

9M2006 results came in better-than-expected with Qtel recording Y-o-Y growth in revenues, EBITDA and post-royalty net profit of 44%, 47% and 39% to QAR 3.1 billion, QAR1.9 billion and QAR1.3 billion, respectively. Growth in Qtel revenues was mostly driven by growth in both its Qatari and Omani wireless operations. Qtel's mobile subscriber base rose 57% Y-o-Y to reach 1.3 million by the end of September 2006, with Nawras subscribers in Oman accounting for 36% of mobile subscribers versus 22% during the same period last year. 9M revenues and net profit accounted for 80% and 88% of our previous full year 2006 estimates of QAR3.8 billion and QAR1.5 billion, respectively.

...and strong subscriber uptake in 9M2006

Qatari mobile subscribers rose 35% Y-o-Y to reach 854,885 in the quarter ending September 2006, implying a penetration rate of 98%. As for the Omani subsidiary, Nawras continued its aggressive uptake in subscriber additions, adding 81,132 subscribers in 3Q2006 to reach 475,212, bringing its market share to 28% at the end of the quarter versus 25% in 2Q2006. The penetration rate in Oman is estimated to have reached 64% by year end. Wireless revenue rose 55% Y-o-Y to QAR2.2 billion in 9M2006, with Nawras revenues accounting for 15% of the wireless revenues versus 7% in 9M2005.

Figure 1.1: Qtel and Nawras Quarterly Mobile subscribers (000)



Sources: Qtel and Nawras

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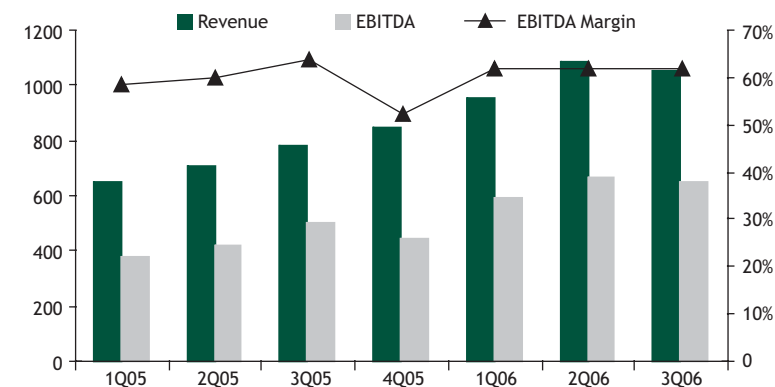
Gulf Sales

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By the end of September 2006, fixed lines and internet subscribers had grown 2% and 8% to 221,331 lines and 65,693 subscribers, respectively. Despite the slow fixed line growth, wireline revenue grew 26% Y-o-Y to QAR873 million in 9M2006, with internet revenue accounting for 19% of wireline revenue.

In 9M2006 the EBITDA margin rose 1 percentage point (pp) to 62% versus 61% in 9M2005. On a quarterly basis, the EBITDA margin remained flat in 3Q2006 at 62% but dropped 2 pp relative to the 3Q2005 margin. The decline in margin is attributable to one off expenses in Qatar, while Nawras's EBITDA margin continued improving, rising to 10% in 3Q2006 versus 1% in 2Q2006. In our previous forecasts we expected that the consolidated EBITDA margin would fall to 57% by the end of 2006 mostly as a result of the startup nature of the Nawras operations.

Figure 1.2: Qtel's Consolidated Revenue, EBITDA (QAR million) and EBITDA Margin



Source: Qtel

Recent Regulatory and Market Developments

Qatari Telecom market, which will open to competition in 2007, will be the last to liberalize in the GCC

ICT Qatar, the telecom regulator in Qatar, announced in November 2006 the liberalization of the telecom sector in 2007. The scope and the time frame of liberalization have not yet been declared. However, we continue to assume that the GSM and data markets will be the first market segments to open to competition in Qatar. Furthermore, we continue to forecast that Qtel will maintain its monopolistic hold over the fixed line and international voice markets in Qatar until further clarification becomes available. We also continue to assume a decline in the royalty paid by Qtel to the government from the current 25% of net profit to an estimated 7%, starting 2008 onwards.

Qtel launches 3G services in July 2006

In July 2006, Qtel announced the launch of its first 3G Video Calling service offered through its third generation (3G) network, which covers the Greater Doha city area. This service allows callers to see each others' images during a phone conversation through 3G handsets. We believe that similar to peers in the GCC, 3G services are still in their infancy and revenue generated from such services would remain small at least in the early years of introduction.

II. FORECASTS

A. Qtel (standalone)

Subscribers and ARPU

Fixed lines grow significantly and ARPL continues to rise...

We revise upwards our fixed line estimates to reflect the significant increase in lines in 9M2006, rising by 8%. We estimate that fixed lines in Qatar grew by 9% in 2006 to approximately 225,000, implying a penetration rate of 25%. Going forwards, we project that fixed lines will grow at a CAGR of 5% over the coming five years versus our previous estimate of 4%. Furthermore, we estimate that the average revenue per line (ARPL) grew in 2006 by 3% to QAR292 (USD80) as a result of the growth in fixed lines. We continue to forecast a five year CAGR of 3% in the ARPL.

Internet services booming on Qatar, we upgrade our subscriber and revenue estimates

We estimate that internet subscribers grew by 33% to 70,693 subscribers in 2006 with internet revenues rising 49% to QAR236 million. Despite our expectations of the entry of competition in the internet market, we revise our internet subscriber and revenue forecasts upwards to reflect the strong growth in internet services in 2005 and 9M2006. We project that internet subscribers and revenue will grow at a five year CAGR of 7% and 8%, respectively.

Mobile subscriber additions estimated to have picked up in 4Q

We estimate a 28% rise in mobile subscribers by the end of 2006 to approximately 920,570 subscribers, implying a penetration rate of 104%. We believe that subscriber additions temporarily picked up in the last quarter, versus the slight slowdown that occurred in 3Q2006, driven by the tourists and participants in the Asian Games that were hosted in Qatar and started at beginning of December of 2006.

We expect a second mobile operator to enter the market by early 2008

With the very recent announcement to liberalize the telecom market, and the as yet undefined timeframe for liberalization, we believe that the entry of competition would not be before 1H2008 versus our previous estimates of early 2007. We are forecasting that the second entrant would gain 8% market share in the first year of competition, rising to 15% in 2010.

Lower tariffs, churn and market segmentation are crucial to gain market share

With a mobile penetration rate exceeding 100%, Qatar, contrary to the UAE, still has one of the highest postpaid and prepaid mobile tariffs in the region. Therefore, we believe that even though Qtel might start lowering its tariffs in preparation for competition, there would still be room for price-based competition, at least in the early stages of competition, when the new entrant would want to gain ground rapidly.

With a fully saturated market and a declining number of subscriber additions, we also believe that churn from the existing operator would be important for the success of the second entrant. Furthermore, with Qtel currently offering its customers one package each for the post paid and the prepaid, the new operator could offer multiple packages to attract the different market segments in the Qatari market, which has a high percentage of expatriates (around 80%). Of course the extent of competition in this highly saturated market would very much depend on how the market would be regulated, an issue that has not yet been disclosed by the regulator.

Table 3.1: Qatar Telecom Market Indicators

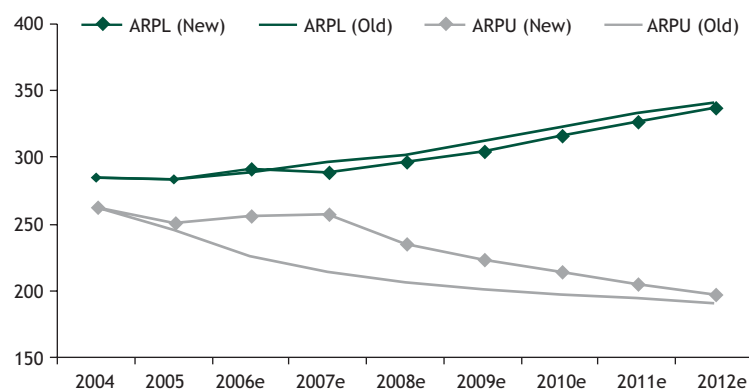
	2005a	2006e	2007e	2008e	2009e	2010e	2011e	2012e
Population (mn)	0.835	0.885	0.929	0.975	1.014	1.055	1.092	1.130
Teledensity	24.6%	25.4%	25.8%	26.0%	26.2%	26.3%	26.6%	26.8%
Fixed Line Subscriber Additions (mn)	0.015	0.019	0.014	0.014	0.012	0.013	0.012	0.013
Qtel Fixed Line Subscribers (mn)	0.205	0.225	0.239	0.254	0.265	0.278	0.290	0.303
Market Share of Qtel	100%	100%	100%	100%	100%	100%	100%	100%
Mobile Subscriber Additions (mn)	0.226	0.204	0.132	0.099	0.065	0.058	0.052	0.047
Total Mobile Subscribers (mn)	0.717	0.921	1.053	1.152	1.217	1.275	1.327	1.374
Growth in Mobile Subscribers	46%	28%	14%	9%	6%	5%	4%	4%
Penetration Rate (pop)	86%	104%	113%	118%	120%	121%	122%	122%
Qtel Mobile Subscribers (mn)	0.717	0.921	1.053	1.064	1.076	1.090	1.108	1.129
Qtel Share of Net Additions	100%	100%	100%	11%	18%	23%	35%	45%
Market Share of Qtel	100%	100%	100%	92%	88%	85%	83%	82%
New Entrant Subscribers	-	-	-	0.088	0.141	0.185	0.219	0.245
New Entrants Share of Net Additions	0%	0%	0%	89%	82%	77%	65%	55%
Market Share of New Entrants	0%	0%	0%	8%	12%	15%	17%	18%

Sources: Qtel and EFG-Hermes estimates

ARPU rose as a result of strong wireless business over the past two years

We revise our blended average revenue per user (ARPU) estimates upwards to reflect the better-than-expected performance in the wireless segment over 2005 and 2006. We estimate ARPU reached QAR256 in 2006, 13% above our previous estimate. We also forecast a five year CAGR decline of 5% to reflect the decline in tariffs as a result of the competition expected in the Qatari mobile market.

Figure 3.2: Old & New ARPL and ARPU Estimates



Source: EFG-Hermes estimates

We revise our revenue estimates upwards to reflect the better-than-expected performance in the local market

Revenue and EBITDA

Our new forecasts assume 10% and 15% rises in our wireless and wireline revenue estimates above our previous forecasts to QAR2.5 billion and QAR1.2 billion, respectively, in 2006. This is mostly the result of better-than-expected subscriber growth in 9M2006 and the continued strong performance estimated to have occurred in Q4, partially driven by the revenue expected to be generated from the Asian Games held in December 2006. We also revise our 2007 revenue estimates upwards by 17%, driven by the strong performance in 2006 and the expected delay in the entry of competition until 1H2008 from our old forecast of late 2007.

Furthermore, we estimate that Qtel's EBITDA for the local operation grew by 34% Y-o-Y in 2006 and 8% above our old estimates, implying an EBITDA margin of 67.4%, 1.2 pp over 2005 and 1.8pp below our old estimates. With Qtel losing its monopoly over the mobile and data markets in early 2008, we are forecasting that the EBITDA margin in 2007 will be flat, if not rise slightly as a result of the monopoly that Qtel is expected to enjoy until the end of 2007. However, going forwards, we expect that the EBITDA margin of the local operations will start declining and stabilize in the early-mid 50s over the coming five years.

Table 3.3: Qtel Financial Highlights for its Local Operations

(QAR mn)	2005		2006				2007			
	Est.	Actual	Old	New	Var.	Growth	Old	New	Var.	Growth
Wireline	939	947	1,007	1,161	15%	23%	1,080	1,275	18%	10%
Wireless	1,822	1,835	2,311	2,537	10%	38%	2,549	3,071	20%	21%
Special Business	68	63	66	50	-24%	-20%	67	46	-31%	-9%
Total Revenue	2,829	2,845	3,384	3,748	11%	32%	3,695	4,391	19%	17%
EBITDA	1,911	1,882	2,340	2,525	8%	34%	2,455	2,961	21%	17%
EBITDA Margin	67.5%	66.2%	69.2%	67.4%			66.5%	67.4%		
Royalty Fees	(444)	(397)	(541)	(593)	10%	49%	(158)	(683)	332%	15%
Net Profit	1,332	1,285	1,622	1,778	10%	38%	2,103	2,050	-3%	15%

Sources: Qtel and EFG-Hermes estimates

Royalty Payment

We had previously forecast a decline in the royalty paid by Qtel to the government upon the liberalization of the mobile and data markets. Our forecast was that Qtel would start paying 7% of net profit versus the 25% of net profit it currently pays, starting 2007. However, since we expect that the entry of competition will not be before the first half of 2008, we have shifted the decline in royalty to 2008. If one were to assume that the royalty payment was to remain, as in our previous forecasts, at 7% in 2007, net profit for Qtel's local operations would have grown by 43% to QAR2.5 billion instead of our new estimate of growth of 15% and net profit of QAR2.0 billion.

We forecast strong uptake of Nawras subscribers driven partially by MNP

B. Nawras

Subscribers and ARPU

We estimated that Nawras will have sustained its strong subscriber uptake in the fourth quarter of 2006, partially driven by the implementation of Mobile Number Portability (MNP) that was launched in 2H2006. We raise Nawras subscriber estimates by 3% to 559,000 subscribers by year end, securing 31% market share. We also forecast that Nawras will be able to achieve a 40% market share by 2008, to stabilize in the 40s going forwards. We maintain our ARPU assumptions and continue to forecast an annual 4% decline over our projection period.

Table 3.4: Omani Mobile Market Indicators

	2005a	2006e	2007e	2008e	2009e	2010e	2011e	2012e
Population (mn)	2.8	2.9	2.9	3.0	3.1	3.2	3.2	3.3
Addressable Market (mn)	1.8	2.0	2.2	2.4	2.6	2.7	2.8	2.8
Total Mobile Subscribers (000)	1,333	1,827	2,192	2,411	2,532	2,658	2,751	2,834
Growth in Subscribers	65%	37%	20%	10%	5%	5%	3%	3%
Net Additions (000)	527	493	365	219	121	127	93	83
Penetration to Addressable	75%	91%	99%	99%	99%	99%	100%	100%
Penetration Rate (pop)	48%	64%	75%	80%	82%	84%	85%	85%
Nawras Share of Net Additions	46%	64%	68%	69%	67%	65%	62%	60%
Nawras Net Subscribers (000)	244	558	808	960	1,041	1,123	1,181	1,230
Market Share of Nawras	18%	31%	37%	40%	41%	42%	43%	43%
Omantel Share of Net Additions	54%	36%	32%	31%	33%	35%	38%	40%
Omantel Net Subscribers (000)	1,089	1,268	1,383	1,451	1,491	1,535	1,570	1,603
Market Share of Omantel	82%	69%	63%	60%	59%	58%	57%	57%

Sources: Nawras, TRA in Oman, and EFG-Hermes estimates

Revenue and EBITDA

The slight estimated increase in subscribers in 2006 has led to a rise in our 2006 estimate of Nawras revenues of 4% over our old revenue estimate to reach OMR50.6 million in 2006. We believe that Nawras revenue will account for a growing portion of Qtel's top line going forward, reaching 18% of total revenues in 2009. Since Nawras surprised positively at the EBITDA level, turning positive six months ahead of our expectations, we revise our EBITDA figures upwards, to reflect the faster-than-expected improvement in Nawras operation. We estimated that Nawras closed the year at OMR2.4 million in EBITDA, implying an EBITDA margin of 5% for 2006. We also raise our terminal EBITDA margin to 50% up from our previous estimate of 40%.

Net Profit

Furthermore, we expect that Nawras will breakeven one year ahead of our previous expectations of it breaking even in 2008. This reflects the better-than-expected improvement in the company's operations and also implies that there could be room for positive surprise if MNP works faster in favor of Nawras than we currently anticipate.

Table 3.5: Nawras Telecom Financial Highlights (standalone)

(OMR)	2005	2006e	2007e	2008e	2009e	2010e	2011e	2012e
ARPU	10.2	9.7	9.2	8.9	8.6	8.3	8.1	7.9
Revenue (mn)	14.7	50.6	78.3	95.6	104.1	109.2	112.5	114.1
EBITDA (mn)*	(17.7)	2.4	19.9	38.1	46.6	54.4	56.0	56.8
EBITDA Margin	NR	5%	25%	40%	45%	50%	50%	50%
Dep. and Amort. Expenses (mn)	(4.4)	(10.3)	(11.0)	(11.7)	(12.2)	(12.7)	(13.2)	(13.7)
Other Income (Expenses) (mn)	(1.8)	(6.8)	(7.4)	(7.0)	(5.9)	(4.9)	(3.9)	(2.8)
Net Profit after Taxes (mn)	(21.7)	(11.8)	4.3	22.2	31.3	34.8	36.8	37.9

*EBITDA includes the royalty payment calculated as a percentage of net revenue
Sources: Qtel and EFG-Hermes estimates

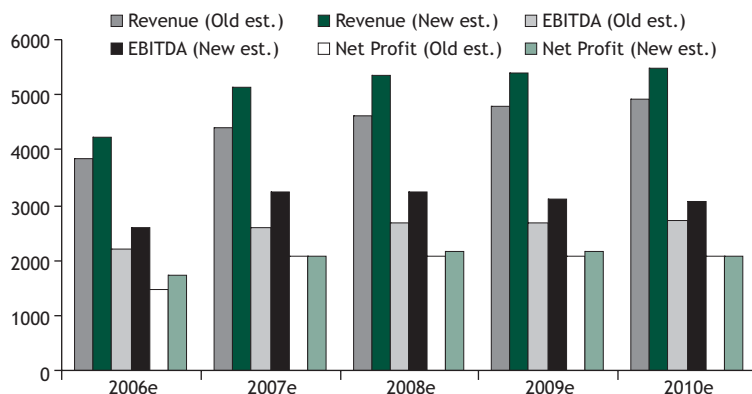
C. Consolidated Revenue, EBITDA and Net Profit

We estimate that consolidated revenue and EBITDA for Qtel in 2006 came in 10% and 18% higher than our previous estimates and 42% and 50% higher than 2005 figures. Furthermore, we revise the estimated 2006 EBITDA margin upwards by 4 percentage points over our previous estimates, to end the year at 61%. The estimated improvement in consolidated revenue and EBITDA comes as a result of the following: i) The strong top line results from Qtel's local operations, in both wireless and wireline. ii) The improvement in the EBITDA margin of Qtel's local operation, estimating it to rise by 1% over 2005 margin. iii) The faster-than-expected improvement in Nawras operations in 9M2006, breaking even on an EBITDA level six months earlier than we had previously anticipated.

Given that we believe Qtel will still be the only player in the market until the end of 2007, we are forecasting that the EBITDA margin will grow by 1pp that year to 62.8%, mostly as a result of the improvement in the Nawras EBITDA margin and Qtel maintaining its domestic margins. We forecast that by the end of 2008 the EBITDA margin will start declining as a result of competitive pressures. However, we believe that the decline would be partially offset by the continued improvement in Nawras margins. We forecast that the EBITDA margin of the whole Group will fall 2pp to 60.3% in 2008 versus our previous estimate of 54.9%, sliding to 57.6% in 2009 versus our previous estimate of 54.7%, and then continue declining to stabilize at the mid 50s over the following three years.

In light of the above, we estimate 2006 was a good year for Qtel with consolidated net profit growing a hefty 46% to QAR1.7 billion, 17% above our previous estimates. We also forecast that 2007 will also be a good year for Qtel but with growth slowing slightly as a result of the saturation in the mobile market and a decline in tariffs in preparation for competition. Since we shift the decline in the royalty paid by Qtel from 2007 to 2008, we expect to see positive growth in Qtel's bottom line in 2008, despite 2008 being the first year of competition.

Fig. 3.6: Qtel's Consolidated Revenue, EBITDA and Net Profit - Old and New Estimates (QAR mn)



Source: EFG-Hermes estimates

III. VALUATION

Discounted Cash Flow Valuation (DCF)

We revise upwards our estimated fair value for Qtel to QAR372.8 per share, 25% above our previous estimate, offering 61% upside over and above the current market price. The rise in fair value is mostly attributable to the better-than-expected growth in Qtel's wireless and wireline revenues in 9M2006 led by strong subscriber growth in both the local and Omani markets.

i) Local Operations: We revise our wireless and wireline revenue estimates upwards by 10% and 15%, respectively, versus our previous forecasts, to reflect the strong performance expected in 2006, mainly driven by robust subscriber growth. We also revise revenue and subscriber estimates for 2007 to reflect the late entry of competition in 1H2008 versus our old expectation of early 2007. Furthermore, we upgrade our EBITDA figures 8% and 21% above our estimates for 2006 and 2007, respectively.

ii) Omani Operations: We revisit our Nawras estimates due to the faster-than-expected improvement in the Omani operation, especially at the EBITDA level which turned positive in 2Q2006, ahead of our expectations. We forecast OMR2.4 million in EBITDA by the end of 2006, implying an EBITDA margin of 5%, versus a loss of OMR19.6 million previously estimated at the EBITDA level. Furthermore, we push upwards our terminal EBITDA margin from 40% to 50%. We also forecast that Nawras will breakeven in 2007, one year ahead of our previous estimate.

Royalty Scenarios

We perform a sensitivity analysis to demonstrate the effect of different royalty payments on Qtel's fair value. We choose three scenarios for the royalty presented below:

Scenario 1: the royalty payment continues at 25% over our six year projection period.

Scenario 2: the royalty decline gradually starting in 2008, to reach 15% in 2009 and onwards.

Scenario 3: the royalty would decline to 7% starting 2008 and thereafter.

It's worth noting that the extent of the decline in the royalty payment will affect the extent of tariff reductions by Qtel, assuming that Qtel passes on the benefit of the decline in royalty to its consumers. However, for the sake of simplicity, we did not change any of our ARPU assumptions in scenarios 1 and 2. We also continue to forecast that Qtel will maintain its monopoly over the fixed and international voice markets over our projection period in all three scenarios.

Table 4.1: A Summary of the Estimated Enterprise Value Under all Three Scenarios

(QAR mn)	Scenario 1	Scenario 2	Scenario 3
Estimated Enterprise Value	30,919	34,032	36,757
Net Debt (Cash)	(519)	(519)	(519)
DCF Value	31,438	34,551	37,276
Number of Shares	100	100	100
DCF Value per Share (QAR)	314.4	345.5	372.8
2007e P/E	11.1	11.1	11.1
2008e P/E	11.5	10.8	9.4

Source: EFG-Hermes estimates

We believe that our assumption of a decline in royalty to 7% is quite bullish (scenario 3), however, we will stick to our assumption until further information is released by the regulatory authority regarding the scope, timeframe of liberalization and other related regulatory issues.

Comparable Valuation

Qtel is slightly valued compared to the EMEA sector average on forward EV/EBITDA multiples. The company is trading on 07e and 08e EV/EBITDAs of 6.8x and 6.6x respectively, versus the EMEA sector average of 6.2x and 6.1x for 2007 and 2008. On the other hand, Qtel is trading at a discount on forward P/E multiples. The company is trading on 11.1x and 9.4x 2007e and 2008e P/E multiples, respectively, compared to the EMEA sector average of 13.7x and 12.5x, respectively. The low P/E multiples are partially attributable to the continued strong performance expected by Qtel in 2007, and the assumed royalty decline (from 25% to 7% of net profit) starting 2008. Its worth highlighting that even under scenarios 1 and 2, Qtel is still attractive, trading on 11.5x and 10.8x 08e P/Es, respectively.

We re-iterate our ST Buy recommendation on Qtel and upgrade our LT recommendation from Accumulate to Buy given the significant 61% upside to our estimated fair value and attractive forwards P/E multiples relative to its peers.

Downside Risk to Our Valuation

Partial liberalization or full liberalization...that is the question...?

We continue to assume a partial market liberalization scenario, with the mobile and data markets opening for competition in 2007. However, we do not exclude the possibility of the TRA opening the Qatari market to full competition, including the fixed and international voice markets. This would present a risk to our valuation, unless the decline in royalty paid by Qtel, more than offsets the expected decline in tariffs and the market share loss associated with the entry of competition in all of the aforementioned markets.

Royalty decline still to be determined...

Similarly to other TRAs in the region, we have assumed that once the telecom market opens, the TRA will lower the royalty/revenue share paid by the telecom operator to the TRA. Just recently the TRA in the UAE announced that it will lower the royalty paid by Etisalat, UAE's incumbent operator, currently at 50% of net profit, to 40% over the coming 3-4 years versus the 20% of net profit that Etisalat was hoping for and also versus our forecast decline to 30% over four years. We continue to forecast that the royalty will fall to 7% in 2008, as per our previous forecasts until further clarification from the regulatory authority.

DISCLOSURES

I, Daniyah Darwish, hereby certify that the views expressed in this document accurately reflect my personal views about the securities and companies that are the subject of this report. I also certify that neither I nor my spouse or dependants (if relevant) hold a beneficial interest in the securities that are the subject of this report.

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DISCLAIMER

Our investment recommendations take into account both risk and expected return. We base our long-term fair value estimate on a fundamental analysis of the company's future prospects, after having taken perceived risk into consideration. We have conducted extensive research to arrive at our investment recommendations and fair value estimates for the company or companies mentioned in this report. Although the information in this report has been obtained from sources that EFG-Hermes believes to be reliable, we do not guarantee its accuracy, and such information may be condensed or incomplete. Readers should understand that financial projections, fair value estimates and statements regarding future prospects may not be realized. All opinions and estimates included in this report constitute our judgment as of this date and are subject to change without notice. This research report is prepared for general circulation and is intended for general information purposes only. It is not intended as an offer or solicitation with respect to the purchase or sale of any security. It is not tailored to the specific investment objectives, financial situation or needs of any specific person that may receive this report. We strongly advise potential investors to seek financial guidance when determining whether an investment is appropriate to their needs. No part of this document may be reproduced without the written permission of EFG-Hermes.

Consolidated Financial Statements (December year end)

(QAR mn)	9M05	2005a	9M06	2006e	2007e	2008e	2009e
Balance Sheet							
Cash & Liquid Assets	1,645	1,645	1,665	1,821	2,809	3,238	4,001
Accounts Receivable & Prepayment	541.7	426.0	674.0	600.5	720.1	755.0	785.9
(Provision for Acc. Receivable)		(168.9)		(240.2)	(288.0)	(302.0)	(314.4)
Net Accounts Receivable	541.7	257.1	674.0	360.3	432	453.0	471.5
Due from Telecom Administrations		35.4		37.3	40	40.5	41.3
Non-trade Receivables		117.7		148.0	168.4	170.3	146.0
Inventory	23.9	23.9	24.3	25.4	25.5	26.1	26.5
Other Current Assets		131.5		154.0	168.4	158.2	146.0
Total Current Assets	2,211	2,211	2,363	2,546	3,643	4,086	4,833
Net Plant	2,491	2,491	2,875	3,788	4,218	4,533	4,613
Investments		178.6		178.6	178.6	178.6	178.6
Investments in Securities	1,199	1,020	1,245	1,064	1,110	1,159	1,212
License Costs (Net)	380.5	380.5	360.4	351.2	324.7	298.2	271.7
Other Assets	94.9	94.9	124.7	97.4	46.7	46.7	46.7
Total Assets	6,376	6,376	6,968	8,024	9,521	10,302	11,154
Current Portion of Long Term Debt		-		-	176.5	176.5	176.5
Accounts Payable		495.5		711.0	834.6	876.8	877.1
Due to Other telecom Admin.		66.5		89.8	103.1	108.1	112.2
Total Payables	-	562.0	-	800.8	937.7	984.9	989.3
Dividends Payables		485.0		527.0	579.7	637.7	701.4
Other Current Liabilities		832.3		1,132.9	1,274.6	789.6	800.7
Total Current Liabilities	1,387	1,879	1,623	2,461	2,969	2,589	2,668
Long Term Debt	573.4	573.4	647.7	775.1	617.8	441.3	264.8
Minority Interest	25.6	25.6	6.0	165.9	288.4	327.5	261.9
Employees' end of Service Benefits		73.8		41.5	37.3	33.6	30.2
Other Liabilities	128.8	47.3	142.6	42.6	38.3	34.5	31.0
Total Liabilities and Provisions	2,089	2,599	2,414	3,486	3,950	3,426	3,256
Net Worth	4,287	3,777	4,555	4,539	5,571	6,876	7,899
Income Statement							
Revenues	2,137	2,982	3,083	4,223	5,126	5,337	5,417
Cost of Services	(225.1)	(449.1)	(366.6)	(629.6)	(687.4)	(684.3)	(702.9)
SG and A	(612.2)	(808.7)	(806.4)	(1,003)	(1,221)	(1,434)	(1,596)
EBITDA	1,299	1,725	1,910	2,591	3,218	3,219	3,119
EBITDA Margin	60.8%	57.8%	62.0%	61.3%	62.8%	60.3%	57.6%
Depreciation and Amortization	(190.0)	(318.0)	(292.8)	(422.1)	(474.6)	(534.5)	(585.8)
Net Operating Profit	1,109	1,407	1,617	2,168	2,743	2,684	2,533
<i>NOP (EBIT) Margin</i>	51.9%	47.2%	52.5%	51.3%	53.5%	50.3%	46.8%
Net Interest Income (Expense)		46.4	(8.9)	(0.6)	11.0	37.9	69.1
Investment Income (incl. gain on sale of inv.)	58	30.3	96.2	118.2	69.6	70.6	71.6
Royalty Payment	(314.4)	(405.0)	(452.3)	(616.5)	(722.3)	(226.5)	(215.8)
Earnings before Minority Interest	852.9	1,078	1,252	1,670	2,102	2,566	2,458
Minority Interest		97.0	42.8	49.5	(17.8)	(92.8)	(130.8)
NPAUI	852.9	1,175	1,295	1,719	2,084	2,474	2,327
Net Attributable Income	852.9	1,171	1,295	1,714	2,079	2,469	2,322
Cash Flow Statement							
Cash Operating Profit after Tax		1,320		1,974	2,495	2,993	2,903
<i>Change Working Investment</i>		108.6		141.5	40.7	44.6	29.7
Cash Flow Post Chg in Working Investment		1,428		2,116	2,536	3,037	2,933
Capital Expenditure		(1,402.3)		(1,692.2)	(878.6)	(822.5)	(639.1)
Free Cash Flow		25.9		423.3	1,658	2,215	2,293
Non-operating Cash Flow		236.2		281.2	198.5	(478.8)	17.9
Cash Flow before Financing		262.1		704.5	1,856	1,736	2,311
Net Financing		0.8		(526)	(867)	(1,316)	(1,579)
Change in Cash		263		178.1	989.5	419.5	732.3

Sources: Qtel and EFG-Hermes

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