

### Key Data

<b>Closing Price*</b> EGP 18.43	<b>Avg. Value Traded per Day</b> EGP 32.59 mln
<b>52-Week High</b> EGP 19.20	<b>Market Cap</b> EGP 31.5 bln
<b>52-Week Low</b> EGP 13.60	<b>Current Number of Shares</b> 1,707 mln
<b>Reuters</b> ETEL.CA	<b>Bloomberg</b> ETEL EY
<b>Ownership Structure</b>	
Government 80%	Public 20%

\*As of December 21, 2009. Sources: Bloomberg, Zawya, and NBK Capital

### Rebased Performance



Sources: MSCI, Reuter, and NBK Capital

### Key Ratios

	2008a	2009 f	2010 f	2011 f	2012 f	2013 f
P/E	12.9	11.0	10.0	9.9	9.5	9.0
EPS Growth	3%	17%	10%	1%	4%	5%
EV/ EBITDA	6.9	6.5	6.2	6.2	6.1	6.0
EBITDA Margin	44%	46%	46%	45%	44%	43%
EBITDA Growth	-9%	6%	6%	-1%	2%	2%
Dividend Yield	7.1%	8.7%	9.5%	10.1%	10.6%	11.1%
ROAE	10%	11%	12%	12%	12%	13%

<b>1Q2009 EBITDA a</b> EGP 1,257 mln	<b>3Q2009 EBITDA a</b> EGP 1,187 mln
<b>2Q2009 EBITDA a</b> EGP 1,244 mln	<b>4Q2009 EBITDA f</b> EGP 1,042 mln

a=actual, f = forecast. Sources: Reuters and NBK Capital

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### Highlights

**12-Month Fair Value: EGP 23.32**

**Recommendation: Buy-Risk Level\*\*: 4**

**Reason for Report: Initiation of Coverage**

- Telecom Egypt is a fully integrated operator: it is the sole fixed-line service provider in Egypt; the company provides mobile services through its subsidiary Vodafone Egypt and data services through its unit TE Data.
- Aggressive competition in the mobile market increased the fixed-to-mobile substitution. Thus, Telecom Egypt's revenue growth was affected negatively. In 2008, total revenue increased by only 1%. As for the company's EBITDA, according to the IFRS financial statements at the end of 2008, it decreased by 9% over 2007. This pushed the EBITDA margin down from 49% at the end of 2007 to 44% at the end of 2008. The main reasons behind the decline are salary increases during 2008 and slower growth in revenue. As for 9M2009, total revenue grew by 3% YoY; this was primarily due to the growth in the company's wholesale segment, which has benefited from the increase in mobile traffic. On the back of an increase in the top line, an improvement in cost management, and a reduction in interconnection fees, EBITDA in 9M2009 grew by 4% YoY; as a result, the EBITDA margin reached 48%.
- We expect that Telecom Egypt will remain the only player in Egypt over our forecasted horizon as the government decided to halt the granting of a second fixed-line license. With the new credit policy that Telecom Egypt introduced, we believe that the company will close the year with negative net additions in the fixed-line segment, reflecting a penetration rate of 11.7% at the end of 2009. As for the coming years, we believe that Telecom Egypt will be able to increase its subscribers' base, especially since management is focusing on a segmented market approach. We estimate the penetration rate will reach 12.3% in 2013.
- We forecast that Telecom Egypt's total revenue will increase at a CAGR of 4% between 2008 and 2013. On the other hand, in this competitive environment, Telecom Egypt will have to increase its offers along with marketing and advertising campaigns. Thus, we expect Telecom Egypt's EBITDA margin to decrease to 43% in 2013.
- We arrived at a 12-month fair value for Telecom Egypt of EGP 23.32 per share using a discounted cash flow based on a sum of the parts and a peer comparison based on forward PEG (price-to-earnings ratio to growth) and EV/EBITDA multiples. With an upside potential of 27% compared to the closing share price on December 21, 2009, we initiate coverage on Telecom Egypt with a "Buy" recommendation.

\*\* Please refer to page 18 for recommendations and risk ratings.

**CONTENTS**

EXECUTIVE SUMMARY ..... 3

VALUATION..... 4

BULLS VS. BEARS ..... 6

TELECOM EGYPT OVERVIEW ..... 7

TELECOM EGYPT FINANCIAL ANALYSIS AND FORECAST ..... 11

FINANCIAL STATEMENTS..... 17

## EXECUTIVE SUMMARY

Telecom Egypt is a fully integrated operator: it is the sole fixed-line service provider in Egypt; the company provides mobile services through its subsidiary Vodafone Egypt and data services through its unit TE Data. The fixed-line market in Egypt has been anticipating the end of Telecom Egypt's monopoly; however, with the current financial crisis, the government decided to halt the granting of a second fixed-line license. Hence, we believe that Telecom Egypt will remain the only player in Egypt over our forecasted horizon.

With the entry of Etisalat in the Egyptian market, the telecom sector witnessed increased competition between the mobile operators that affected fixed-line growth. The fixed-line sector grew at a very modest CAGR of 5% between 2004 and 2008, which translated into a penetration rate of 15% at the end of 2008. Moreover, with the current financial crisis, the level of subscriber default in paying bills on time increased. Thus, Telecom Egypt amended its credit policy for disconnection from 12 months to 90 days. This led to a decrease in the fixed-line base to 9.6 million as of September 2009. According to the company, the disconnected subscribers did not have a material impact on revenue growth as those subscribers spent less than EGP 23 per month. Based on 9M2009 numbers, we believe that the company will end the year with negative net additions, reflecting a penetration rate of 11.7% at the end of 2009. As for the coming years, we believe that Telecom Egypt will be able to increase its fixed-line subscribers especially since management is focusing on a segmented market approach. We estimate the penetration rate will reach 12.3% by 2013.

Aggressive competition in the mobile market increased the fixed-to-mobile substitution. Thus, Telecom Egypt's revenue growth was affected negatively. In 2008, total revenue increased by only 1%. As for the company's earnings before interest, taxes, depreciation and amortization (EBITDA), according to the International Financial Reporting Standards (IFRS) financial statements at the end of 2008, it decreased by 9% over 2007. This pushed the EBITDA margin down from 49% at the end of 2007 to 44% at the end of 2008. The main reasons behind the decline are salary increases during 2008 and slower growth in revenue. As for 9M2009, total revenue grew by 3% year on year (YoY); this was primarily due to the growth in the company's wholesale segment, which has benefited from the increase in mobile traffic. On the back of an increase in the top line, an improvement in cost management, and a reduction in interconnection fees, EBITDA in 9M2009 grew by 4% YoY; as a result, the EBITDA margin reached 48%. We forecast that Telecom Egypt's total revenue will increase at a CAGR of 4% between 2008 and 2013. On the other hand, in this competitive environment, Telecom Egypt will have to keep up with its offers along with marketing and advertising campaigns. Thus, we expect Telecom Egypt's EBITDA margin to decrease to 43% in 2013.

We arrived at a 12-month fair value for Telecom Egypt of EGP 23.32 per share using two valuation methods: discounted cash flow (DCF) based on a sum of parts (SOTP) and a peer comparison based on forward price-to-earnings ratio to growth (PEG) and EV/EBITDA multiples. With an upside potential of 27%, we are initiating coverage on Telecom Egypt with a "Buy" recommendation

## VALUATION

The purpose of this valuation exercise is to use fundamental analysis to arrive at a fair value estimate for the share price of Telecom Egypt. To arrive at this fair value, we used a combination of two valuation methods: DCF based on a SOTP and a peer comparison based on PEG and EV/EBITDA multiples. However, this does not represent a guarantee that this value is achievable within our time frame, as a wide range of variables and market dynamics can ultimately affect the market price of an asset. Each investor must use his or her favorite mix of fundamental research, technical analysis, and market intelligence to arrive at an investment decision that matches his or her objectives and tolerance for risk.

We arrived at a 12-month fair value for Telecom Egypt of EGP 23.32 per share by allocating a greater weight (70%) to the SOTP DCF valuation, a methodology that examines the fundamentals of the company to determine its future cash-generating ability. This fair value is 27% above Telecom Egypt's last price, hence our "Buy" recommendation.

**Figure 1 Fair Value per Share**

*Our 12-month fair value for Telecom Egypt is EGP 23.32*

Valuation Method	Value	Weight
Discounted cash flow - SOTP	EGP 23.54	70%
Peer comparison	EGP 22.80	30%
<b>Weighted Average Fair Value</b>	<b>EGP 23.32</b>	<b>100%</b>

Source: NBK Capital

## SOTP DCF Valuation

To value Telecom Egypt using an SOTP DCF, we separately forecasted—through to 2014—the financial results for Telecom Egypt and Vodafone Egypt (Telecom Egypt owns 44.95% of Vodafone Egypt). From the forecast financial statements, we extracted free cash flows that were used in our valuation of each operation. We discounted the cash flows to the end of December 2010 (12 months from now) to obtain an estimate of the value of each of Telecom Egypt's operations. We assigned a separate risk rating for each of the operations, which resulted in each having its own unique cost of equity. In addition, we assigned different debt and equity weightings for each operation depending on our outlook for the capital structure of each operation moving forward. Our SOTP DCF model resulted in a fair value of EGP 23.54 for Telecom Egypt's share price. The per-share valuation of each operation helps shed light on the source of the value.

**Figure 2 Sum-of-the-Parts Valuation**

	Telecom Egypt's operations		Total
	Telecom Egypt	Vodafone Egypt	
DCF Value (EGP million)	27,425	28,371	
Ownership	100%	44.95%	
Value (EGP million)	27,425	12,753	40,178
% of EV			
<b>Per Share (EGP)</b>	<b>16.07</b>	<b>7.47</b>	<b>23.54</b>

Source: NBK Capital

### Sensitivity Analysis

We performed a sensitivity analysis (Figure 3) on two important inputs to our SOTP DCF valuation model: the cost of equity and the perpetual growth rate used in computing the terminal value.

**Figure 3 Sensitivity Analysis**

*We performed a sensitivity analysis on two major inputs to our SOTP DCF valuation model*

		Cost of Equity Increments				
		-1.00%	-0.50%	Base Case	0.50%	1.00%
Growth Increments	-1.00%	23.48	23.32	23.17	23.03	22.89
	-0.50%	23.67	23.51	23.35	23.19	23.05
	Base case	23.89	23.71	23.54	23.37	23.22
	0.5%	24.12	23.93	23.74	23.57	23.40
	+1%	24.38	24.17	23.97	23.78	23.60

Source: NBK Capital

### Peer Group Comparison

We compared Telecom Egypt to five telecom operators that share similar characteristics (Figure 4). We obtained the consensus forward earnings per share (EPS) and the consensus earnings growth estimates for each of the peer group members for the next three years. The simple average PEG for the sample, excluding the highest and lowest values, was 3.05. Telecom Egypt, in contrast, currently trades at a lower PEG of 1.96, based on our 2010 forecast EPS and next-two-years earnings growth rate.

We also valued Telecom Egypt relative to the EV/2010EBITDA for the same sample. The simple average EV/2010EBITDA for the sample, excluding the highest and lowest values, was 4.48. Telecom Egypt, in contrast, currently trades at an EV/ 2010EBITDA of 5, based on our 2010 forecast EBITDA and net debt levels.

Using a simple average of the two multiples, and excluding outliers among the five companies in the sample, we estimate the value of a Telecom Egypt share is EGP 22.80. This implies that Telecom Egypt is currently undervalued, considering Telecom Egypt's current market price of EGP 18.43.

**Figure 4 Forward PEG and EV/EBITDA Multiples Comparison**

Company	Market Data		EV / 2010 EBITDA	2010 Forecast EPS	PEG
	Price* (Local Currency)	Market Cap (USD Millions)			
Telekomunikacja Polska	16	6,881	4.32	1.02	1.6
Turk Telekom	5	10,583	4.30	0.6	3.1
Magyar Telekom	715	3,678	4.29	76	4.7
Maroc Telecom	138	14,885	6.95	10.90	3.7
France Telecom	17	62,834	4.82	1.82	2.4
<b>Weighted average</b>			<b>5.03</b>		<b>2.70</b>
<b>Simple average</b>			<b>4.94</b>		<b>3.10</b>
<b>Simple average excluding outliers</b>			<b>4.48</b>		<b>3.05</b>
<b>Median</b>			<b>4.32</b>		<b>3.05</b>

*The average EV/EBITDA for the sample, excluding outliers, stands at 4.48*

\*Prices as of last close. Sources: Reuters Knowledge and NBK Capital

## BULLS VS. BEARS

### Bull Story

- Egypt has a favorable demographic outlook, as 31% of Egypt's population is under the age of 15 and the total Egyptian population is expected to grow at around 2% per year.
- Telecom Egypt is a fully integrated operator: it is the sole fixed-line service provider in Egypt; the company provides mobile services through its subsidiary Vodafone Egypt and data services through its unit TE Data.
- Telecom Egypt provides connectivity to all mobile operators, and the company completely controls the wholesale and data business in the country.
- Telecom Egypt has one of the largest fixed-line subscriber bases in the MENA region.
- During the third quarter, Telecom Egypt signed a wholesale telecommunications agreement with Vodafone Egypt that should generate EGP 4 billion in revenue for Telecom Egypt over the next three years. According to this agreement, Vodafone Egypt will use Telecom Egypt's international gateway and will rely on Telecom Egypt's domestic network for all infrastructure leasing needs.
- Telecom Egypt is considered one of the largest employers in Egypt; hence, the company has the full support of the government.
- The mobile penetration rate in Egypt stood at 69% at the end of September 2009, implying room for further growth, especially since the average penetration rate in peer countries has reached 73%. Hence, Telecom Egypt will benefit from this potential growth as the company owns 44.95% of Vodafone Egypt (the second mobile player in Egypt).
- Capitalizing on Egypt's exceptional geographical location, Telecom Egypt is investing in a submarine cable. Through TE North, Telecom Egypt can capture the growth in bandwidth demand in Asia.

### Bear Story

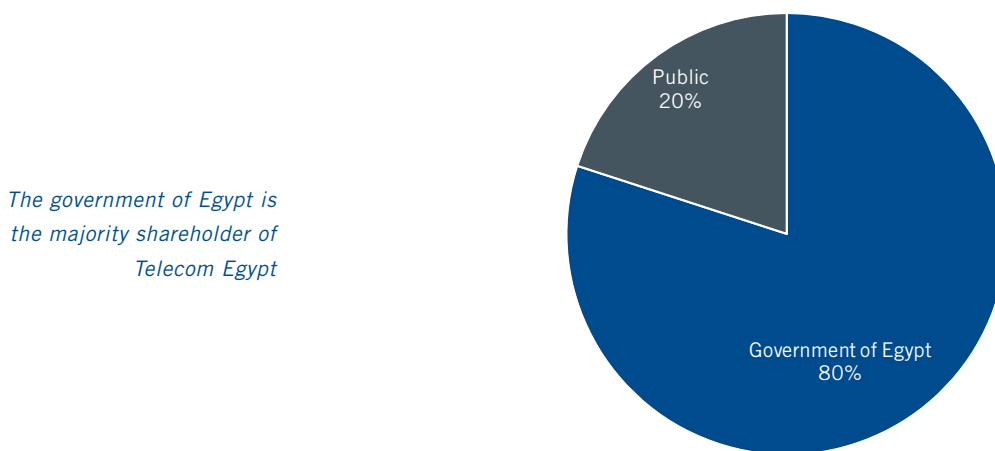
- Telecom Egypt's main line of business, the fixed-line operation, is facing tough competition from the mobile sector. The three mobile operators are offering competitive tariffs and packages that are adding to the fixed-to-mobile substitution.
- Mobinil announced that it will apply for an international gateway license in case the company fails to reach an agreement with Telecom Egypt regarding international interconnection rates and the cost of the leasing infrastructure. If this happens, Telecom Egypt's wholesale international revenue will be at risk.
- Illegal VoIP international calls are putting pressure on the company's revenues.
- During 3Q2009, a price war started among the three mobile operators with Etisalat's re-launch of the EGP 0.19 cross-net tariffs. To curb market share loss, Mobinil and Vodafone Egypt had to respond with similarly aggressive promotions. This price war has taken its toll on Vodafone Egypt's ARPU, which will negatively impact Telecom Egypt's dividend income from its subsidiary.

## TELECOM EGYPT OVERVIEW

### Basic Information

Telecom Egypt was separated from the ARNETO in 1998, when the process of telecom liberalization started to take shape. Telecom Egypt was formed to provide telecom services and establish, maintain, and operate the telecom network. In 1998, Telecom Egypt was transformed into a joint stock company, with the government of Egypt maintaining full ownership. In November 2005, the government launched an initial public offering of Telecom Egypt's shares; this offer represented 20% of Telecom Egypt's outstanding share capital, and raised around USD 890 million (Figure 5).

**Figure 5 Ownership Structure**



Source: Zawya

### Telecom Egypt Business Lines

Telecom Egypt is a fully integrated operator: it is the sole fixed-line service provider in Egypt; the company provides mobile services through its subsidiary Vodafone Egypt and data services through the unit TE Data.

Telecom Egypt has different lines of business divided as follows:

#### Retail

- **Telephony:** This represents the voice services, and it contributes to around 80% of total retail revenue. The growth in this line of business is based on Egypt's growing and young population.
- **Home:** The company offers services over a broadband connection such as Internet and IPTV. This line of business is considered to be very important to Telecom Egypt as home services represent the future of the company.
- **Enterprise:** The company offers enterprise-managed Internet access, managed network services, and outsourcing of information and communication technologies (ICT) services. For years, this segment was ignored by Telecom Egypt; however, according to management, the company has started to focus on this segment, and is planning to organize the institution's base.

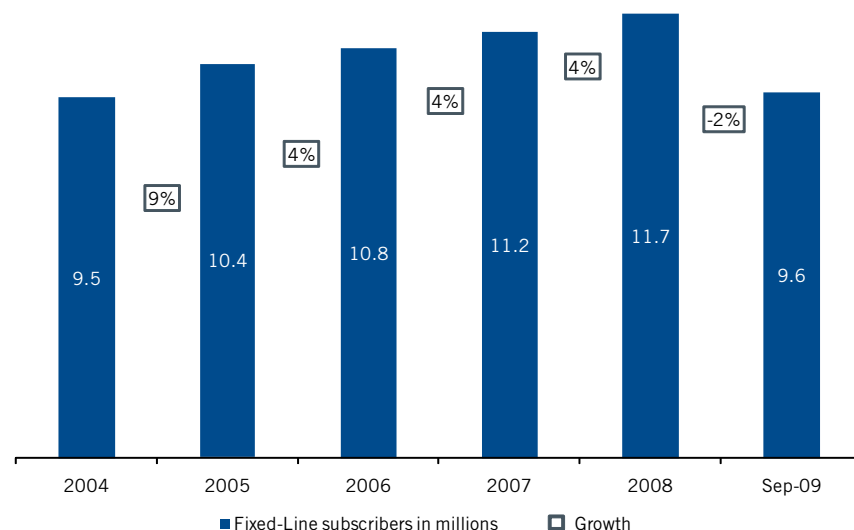
### Wholesale

- Domestic Customers:** The main customers for this segment are the existing mobile operators who rely on Telecom Egypt's infrastructure and network to offer services such as international and wholesale calling. Neither Vodafone Egypt nor Mobinil has bought an international gateway yet as the telecom regulator has set a high price for this license (EGP 100 per existing subscriber and EGP 60 per new subscriber). Vodafone Egypt was the first to sign a three-year agreement for EGP 4 billion with Telecom Egypt to use its international gateway. The agreement covers the following: Vodafone Egypt will utilize Telecom Egypt's international gateway to transit all Vodafone Egypt incoming and outgoing international traffic, and Vodafone Egypt will rely on Telecom Egypt's domestic network for all infrastructure leasing needs.
- International Customers:** Telecom Egypt is counting on its unique geographic position (Egypt) to grow this segment line. Egypt is considered one of the preferred countries for connecting Asia to Europe. Hence, all the growth expected in Asia will reach Europe through Egypt.

### Fixed-line Services

With the entry of Etisalat in the Egyptian market, the telecom sector witnessed increased competition between the mobile operators that affected fixed-line growth. The fixed-line sector grew at a very modest CAGR of 5% between 2004 and 2008, which translated into a penetration rate of 15% at the end of 2008 (Figure 6). Moreover, with the current financial crisis, the level of subscriber default in paying bills on time has increased. Thus, Telecom Egypt amended its credit policy for disconnection from 12 months to 90 days. This led to a decrease in the fixed-line base to 9.6 million as of September 2009. According to the company, the disconnected subscribers did not have a material impact on revenue growth as those subscribers spent less than EGP 23 per month.

**Figure 6 Fixed-line Growth in Egypt**



Source: Telecom Egypt's presentation

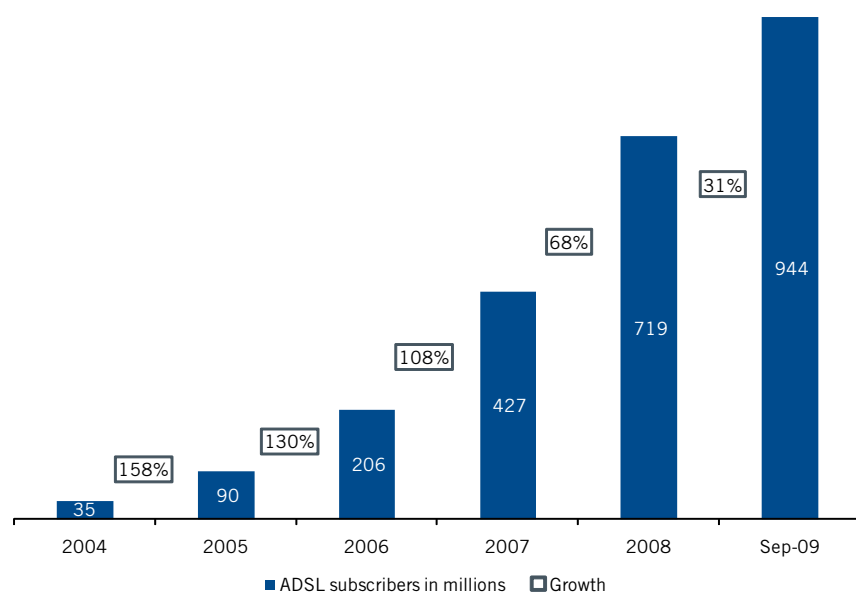
As a counteraction to the fixed-to-mobile substitution effect, Telecom Egypt submitted a request to the regulator for fair competition. Hence, the NTRA authorized a landline tariff rebalancing on July 1, 2008: connection fees, tariffs for phone calls from landlines to mobiles (and vice versa), and paging services fees were reduced. However, monthly subscription fees, tariffs for local phone calls, and the tariff for initiating a local call and paging service were increased. With the current aggressive telecom market background, and the short-term tactical strategy that is being followed in the market, Telecom Egypt is responding with promotions that should help the company retain its position in the market. For example, during this quarter, the company introduced two promotions that should run until the end of December: reduction of connection fees and reduction of long distance rates. Moreover, the medium- and long-term strategy of the company is to focus on customers by having a segmented customer approach.

On the other hand, in October 2009, the NTRA invited bids for two triple-play licenses, which will be offered in closed communities in Egypt that include housing of up to 5,000 units. The winning consortiums will have to build and operate the fiber optic networks but will not have the right to offer voice services as only Telecom Egypt will offer such services. The newcomers will have to be very creative in their value-added services to be profitable. Companies are expected to present their bids in March 2010. According to the Ministry of Communications and Information Technology (MCIT), this network is expected to generate around USD 1 billion within a five-year time frame.

### Internet and Data Services

In 2001, Telecom Egypt established an Internet and data communications subsidiary, TE Data, which is 95.04% owned by Telecom Egypt. The NTRA awarded TE Data a Class A license, which permits the company to build its own national network and to operate its own international data gateway. TE Data is the market leader in Egypt with a market share of 60%. Total Internet subscribers have grown at a CAGR of 15% between 2002 and 2008; during this same period, the ADSL connections grew by a CAGR of 23%. At the end of September 2009, the number of ADSL subscribers in Egypt reached around 944 thousand (Figure 7).

**Figure 7 ADSL Subscribers in Egypt**



Source: Telecom Egypt's presentation

Telecom Egypt plans on rolling out a fiber-optic network in new suburbs around Cairo and Alexandria in Egypt; this rollout will not be across Egypt, and will be focused on areas where demand for high-speed broadband access is high. In October 2009, the company launched its first fiber-to-the-home (FTTH) service, which includes basic services such as voice, data, and IPTV in one bundle.

### Mobile Services through Vodafone Egypt

In 2001, Telecom Egypt was awarded the country's third mobile license; however, in 2003, the company decided not to participate directly in the mobile market, and returned the GSM license to the MCIT. In 2003, Telecom Egypt bought an 8.6% stake in Vodafone Egypt, the second mobile service provider in the country. By the end of 2008, the company had increased its stake to 44.95%. For further details on the mobile sector in Egypt, please refer to our initiation of coverage report on Mobinil dated November 24, 2009.

### TE North Cable System

Telecom Egypt's TE North cable system is a project undertaken by Telecom Egypt to deploy a new submarine cable network linking Sidi Krir in Egypt to Marseille in France and Pentaskhinos in Cyprus. The TE North cable system is currently under construction, and according to the company, the delivery of the TE North cable is expected to take place at the end of 2009. This system will have underwater branching units, which will form a MedGateway, a bridge between Mediterranean countries, Europe, and Asia; in turn, these extensions will provide Telecom Egypt with access to new markets.

According to Telecom Egypt, the strategic rationale behind this project is:

- It will capitalize on Egypt's unique geographic position.
- Telecom Egypt's route is the resilient "route of choice" from the Red Sea to the Mediterranean Sea submarine cable crossing.
- TE North allows Telecom Egypt to increase the footprint of the existing transit corridor.
- It will capture the growth in bandwidth demand in Asia without the need to invest outside the home market.
- It will reduce the cost base of Telecom Egypt and its subsidiaries by lowering international bandwidth costs.
- The company will be in a more competitive position to capture national and regional opportunities.

According to management, the company is on track to launch the TE North cable project during the first quarter of 2010.

**Figure 8 TE North Cable Contractual Progress in USD Millions**

Cable	IRU Value/ TE Transit Corridor	Asset Transfer/TEN
IMEWE "2009"	36	
Seacom/TATA "2009"	40	43
EIG "2010"	50	
CYTA "2010"		50
<b>Total</b>	<b>126</b>	<b>93</b>

Source: TE's half-year investor presentation

## TELECOM EGYPT FINANCIAL ANALYSIS AND FORECAST

## Fixed-line Market Forecast

The fixed-line market in Egypt has been expecting the end of Telecom Egypt's monopoly in 2009; however, due to the financial crisis, the government decided to halt the granting of a second fixed-line license. No information was made public on whether this license will be made available again or not. Hence, we believe that Telecom Egypt will remain the only player in Egypt over our forecast horizon.

With the new credit policy that Telecom Egypt introduced, we believe that the company will end the year with negative net additions, reflecting a penetration rate of 11.7% at the end of 2009. As for the coming years, we believe that Telecom Egypt will be able to grab more subscribers, especially since management is focusing on a segmented market approach. We estimate the penetration rate will reach 12.3% by 2013 (Figure 9).

Figure 9 Fixed-line Market in Egypt

(000's)	2008a	2009f	2010f	2011f	2012f	2013f
<b>Penetration Rate</b>	14.8%	11.7%	11.7%	11.9%	12.1%	12.3%
<b>Total Fixed-Line</b>	11,703	9,400	9,629	9,989	10,360	10,742
<b>Market Share:</b>						
<i>Telecom Egypt</i>	100%	100%	100%	100%	100%	100%
<i>Others</i>	0%	0%	0%	0%	0%	0%

*We expect the fixed-line penetration rate in Egypt to reach 12.3% by 2013*

Sources: Annual reports, IMF, Informa database, and NBK Capital

## Mobile Market Forecast

With the current stiff competition between mobile operators, we believe that the mobile market in Egypt will continue to grow, and based on the peer country analysis, we forecast that the penetration rate in Egypt will reach 90% by 2013 (Figure 10). We forecast that the total subscribers will grow at a CAGR of 13% over the next five years, and Vodafone Egypt's market share will decrease to around 38% by 2013. For further details on the mobile sector in Egypt, please refer to our initiation of coverage report on Mobinil dated November 24, 2009.

Figure 10 Mobile Market in Egypt

(000's)	2008a	2009f	2010f	2011f	2012f	2013f
<b>Penetration Rate</b>	54%	72%	78%	83%	87%	90%
<b>Peers' Penetration Rate</b>	66%	82%	92%	99%	104%	107%
<b>Total Subscribers (millions)</b>	43.0	57.7	64.2	69.7	74.5	78.6
<b>Market Share:</b>						
<i>Vodafone Egypt</i>	41%	39%	39%	39%	38%	38%
<i>Others</i>	59%	61%	61%	61%	62%	62%
<b>Vodafone Egypt's ARPU (USD)</b>						
<i>Total Blended</i>	11.3	9.3	8.4	7.9	7.5	7.3

*We expect the mobile penetration rate in Egypt to reach 90% by 2013*

Sources: Annual reports, IMF, Informa database, and NBK Capital

The mobile market in Egypt has been witnessing a price war, and we believe that the price war, if it continues, will further dilute the ARPU; thus, we forecast that Vodafone Egypt's blended ARPU will drop from USD 11.3 in 2008 to USD 7.3 in 2013.

## Revenue

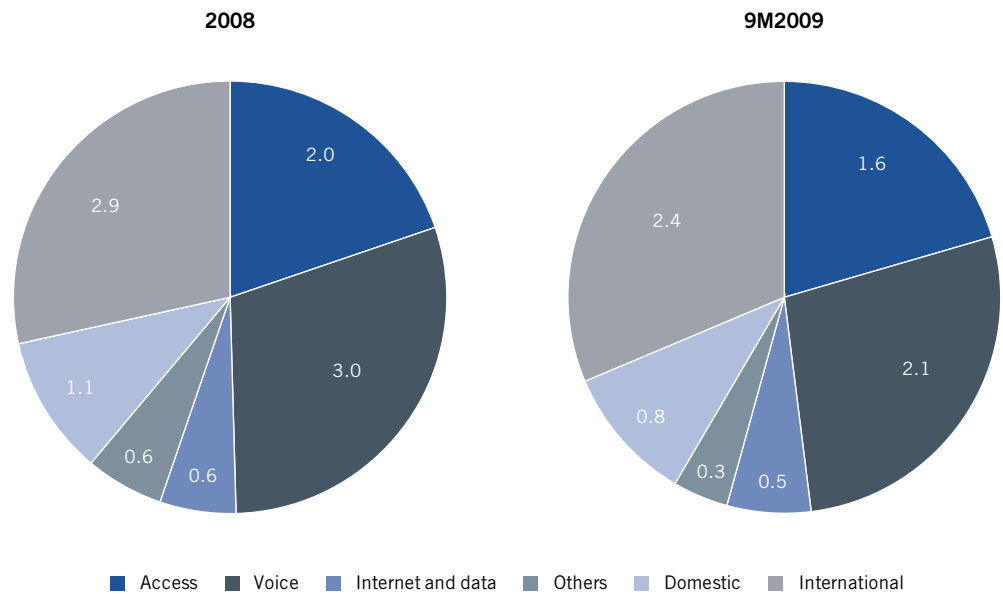
With increasing competition between the telecom operators, the growth of revenue has narrowed. At the end of 2008, Telecom Egypt's consolidated revenue grew by 1% YoY, and reached around EGP 10 billion. As for 9M2009, consolidated revenue amounted to EGP 7.7 billion, a growth of 3% YoY. Telecom Egypt's divides its revenue into two categories: retail and wholesale services.

**Retail Services:** The aggressive competition in the mobile market encouraged many subscribers to use mobile services instead of fixed-line services. Thus, Telecom Egypt's retail segment growth was affected negatively. During 2008, this segment witnessed almost no growth, while in 9M2009, mobile services saw a decline of around 1% compared to the same period last year. Retail services are still the main contributor to total revenue (58.4% during 9M2009) and are divided as follows:

- *Access revenues:* Representing revenue generated through connections and subscriptions, access revenues grew by 6% YoY to reach around EGP 2 billion in 2008. As for 9M2009, this revenue segment increased by 9% YoY.
- *Voice revenues:* In 2008, this revenue segment declined by 5% YoY and reached around EGP 3 billion; the positive outcome of the implementation of tariff rebalancing on the local call revenue was diminished due to the pressure resulting from increasing competition from mobile operators. During the summer and Ramadan of 2009, competition intensified, leading to more pressure on voice revenue, which declined by 6% in 9M2009 compared to the same period last year.
- *Internet and data revenue:* During 2008, Internet and data revenue witnessed 26% YoY growth, with broadband revenue growing by 54% YoY. In 9M2009, this revenue segment increased by 18% and reached EGP 485 million.

**Wholesale Services:** Being the network of choice and having control over the international gateway have created a different source of revenue for Telecom Egypt. According to management, the growth in Telecom Egypt's total consolidated revenue in 9M2009 was primarily due the growth in the company's wholesale segment, which has benefited from the increase in mobile traffic; this revenue line witnessed a 10% increase YoY during 9M2009 and accounted for 42% of the total revenue. However, if we look at quarter-on-quarter growth, the wholesale revenue declined by 8%; this drop was partly related to the new wholesale agreement with Vodafone Egypt (according to management, Telecom Egypt gave Vodafone Egypt some discounts due to its long-term commitment) as well as the seasonality effect witnessed on international revenue.

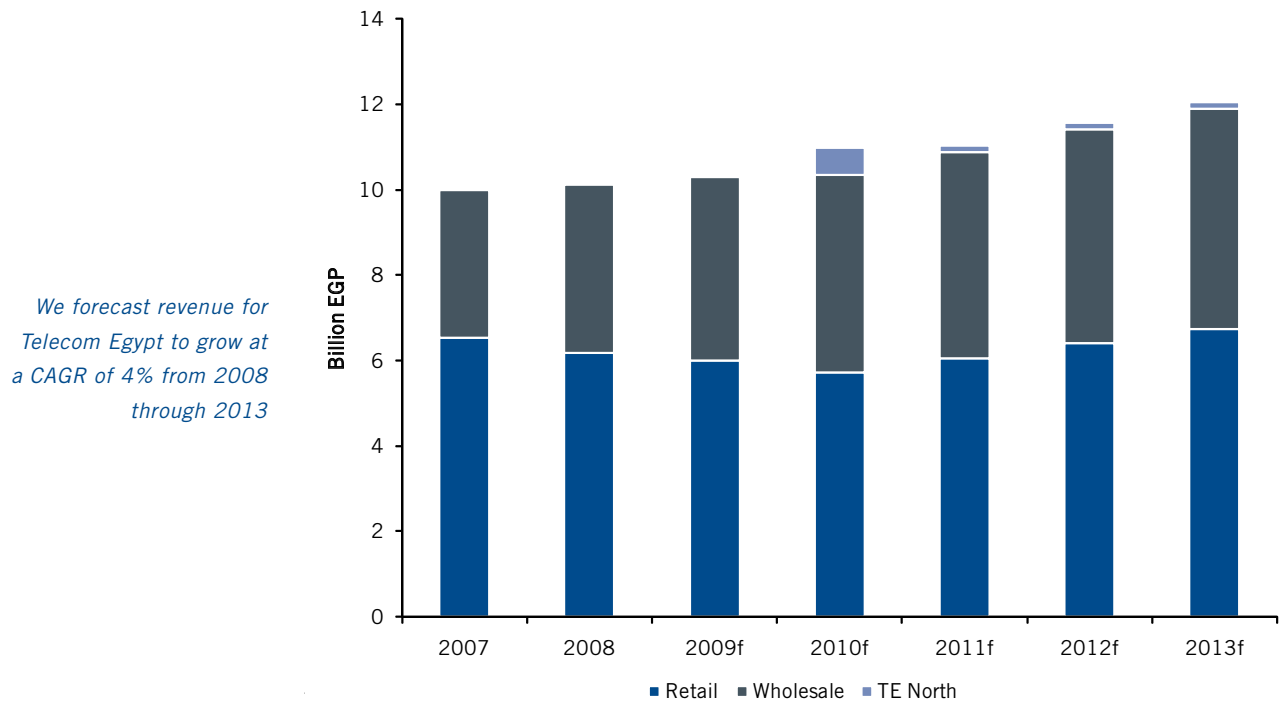
**Figure 11 Breakdown of Telecom Egypt's Revenues in EGP Million for 2008 and 9M2009**



Sources: Annual report and NBK Capital

Based on the performance of Telecom Egypt and the challenges in the telecom market, we forecast total revenue to grow at a CAGR of 4% between 2008 and 2013. We believe that retail revenue will continue to be the highest contributor to total revenue (56% by 2013), and will grow at a CAGR of 2% between 2008 and 2013. As for wholesale services, we believe that this business line will grow at a CAGR of 6% between 2008 and 2013 and will contribute to 43% of total revenue by 2013. On the other hand, starting in 2010, the company will start to recognize revenue from the TE North project. According to management, the project is expected to contribute around EGP 2.75 billion over the coming 15 years. During 2010, 18% of this amount will be one-off revenue recognized as an asset sale. As for the coming years, the project will contribute to 1% of total revenues and will be booked as capacity sales.

Figure 11 Telecom Egypt's Actual and Forecast Revenue



Sources: Annual report and NBK Capital

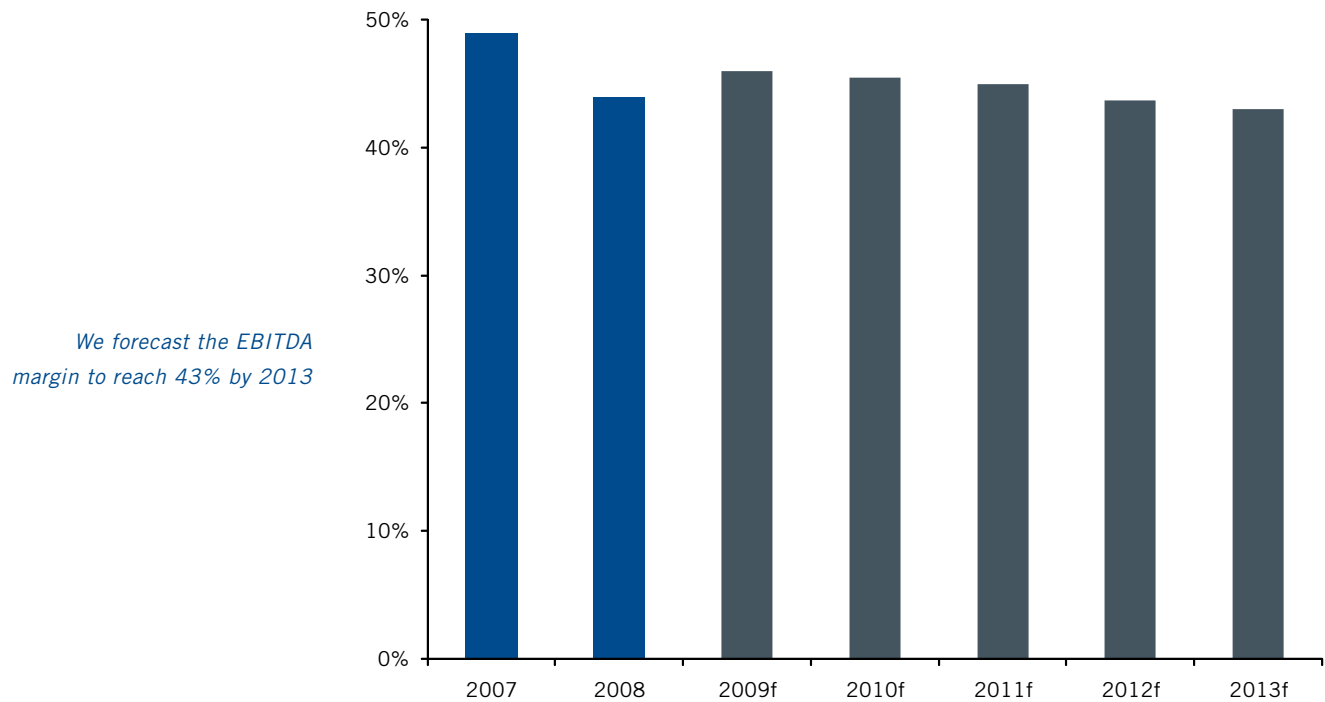
### Profitability

According to the IFRS financial statements, at the end of 2008, EBITDA amounted to EGP 4.4 billion, a decrease of 9% over 2007. The EBITDA margin decreased from 49% at the end of 2007 to 44% at the end of 2008. The main reason behind the decline is due to the increase in employee costs in January and May 2008 and slower growth in revenue.

As for 9M2009, on the back of an increase in the top line, an improvement in cost management, and a reduction in interconnection fees by 27% YoY (the reduced cost is attributed to the NTRA reducing interconnection costs during 2008), EBITDA grew by 4% YoY; as a result, the EBITDA margin reached 48%, compared to 47% in 9M2008. Furthermore, the annual salary increase was implemented on July 1, 2009, and the increase stood at 8%, thus increasing employee costs starting 3Q2009.

The company signed a new three-year agreement with Vodafone Egypt to continue to provide infrastructure and international gateway service that will have a negative impact on margins because of the additional discounts given. On the other hand, the increased competition will push Telecom Egypt to introduce more offers and increase advertising and marketing expenses. As a result, we estimate that the EBITDA margin at the end of 2009 will be 46%, and will reach 43% at the end of 2013.

Figure 12 Telecom Egypt's Actual and Forecast EBITDA Margin



Sources: Annual report and NBK Capital

Telecom Egypt's bottom line increased by 3% to EGP 2.44 billion in 2008, compared to 2007. This resulted in a net profit margin of 24%. As for 9M2009, net profit increased by around 20% and amounted to EGP 2.41 billion, with a net profit margin of 31%. This significant increase is due to a 29% increase in other income YoY (we do not have further details about this line item) and a 56% drop in financial expenses YoY (Telecom Egypt paid back part of its loan during this year).

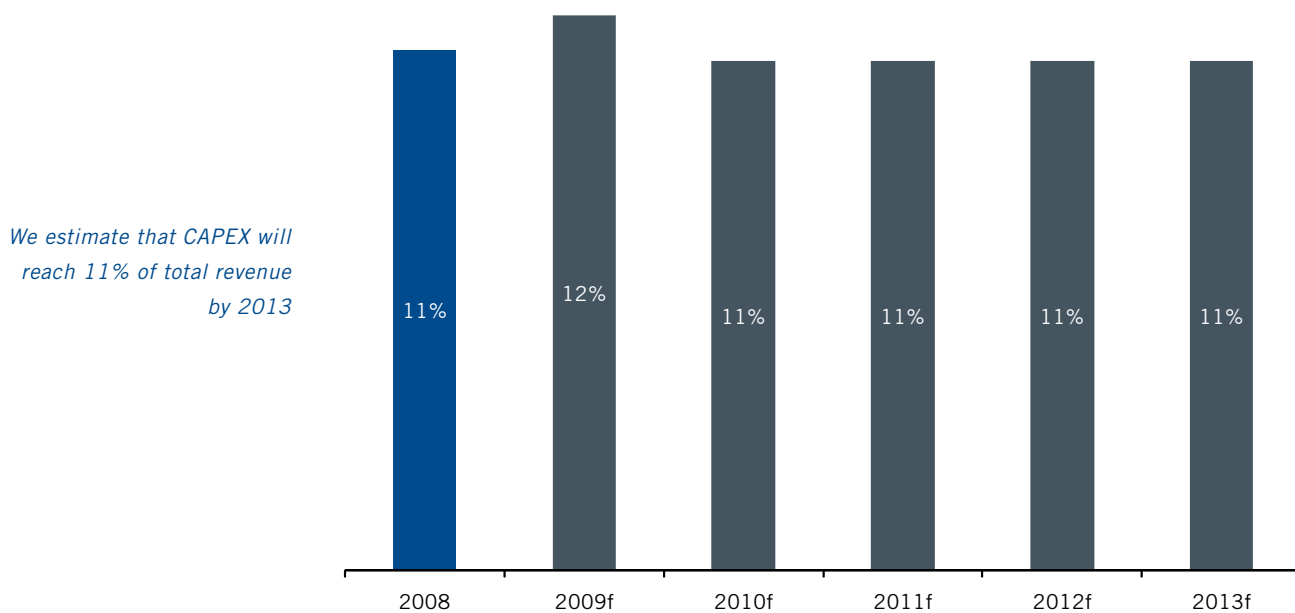
Vodafone Egypt has historically paid Telecom Egypt a dividend during the third quarter; however, during 3Q2009, the company delayed paying the dividend to Telecom Egypt, on the grounds of the ongoing interconnection dispute.

### Capital Expenditure

During the first nine months of 2009, CAPEX witnessed an increase of 6% in comparison to 9M2008 and amounted to EGP 697 million. According to management, this CAPEX was directed toward the development of the TE North project, the ongoing maintenance of Telecom Egypt's infrastructure, and the continuing commitment to increasing broadband capacity.

Based on the guidance of Telecom Egypt's management for a CAPEX of EGP 1 to 1.3 billion for 2009 and based on our forecast, we expect CAPEX to account for around 12% of total revenue in 2009. As for the coming years, we believe that CAPEX will settle at 11% of the total revenue (Figure 13).

Figure 13 Capital Expenditure as a % of Total Revenue



Sources: Annual report and NBK Capital

### Financial Health

At the end of September 2009, Telecom Egypt had a low debt-to-equity ratio of 0.06x. During 9M2009, Telecom Egypt paid part of its outstanding loan, which amounted to around EGP 1.6 billion. According to management, the company is planning to pay an additional debt of EGP 400 million before year-end.

## FINANCIAL STATEMENTS

Balance Sheet (EGP Thousands)		Historical		Forecast			
Fiscal Year Ends December	2007	2008	2009	2010	2011	2012	2013
<b>ASSETS</b>							
Cash and Short-Term Investments	1,396,833	2,734,662	3,474,386	5,070,918	7,020,683	8,225,608	9,453,785
Total Receivables, Net	4,756,435	4,853,444	4,935,706	5,267,944	5,296,053	5,554,650	5,783,313
Total Inventory	508,416	473,015	359,895	403,327	405,479	445,529	484,955
<b>Total Current Assets</b>	<b>6,661,684</b>	<b>8,061,121</b>	<b>8,769,987</b>	<b>10,742,189</b>	<b>12,722,215</b>	<b>14,225,788</b>	<b>15,722,053</b>
Property/Plant/Equipment, Total - Net	19,737,481	18,212,656	16,818,240	15,321,441	13,754,986	12,167,980	10,550,276
Intangibles, Net	223,722	154,991	133,598	110,781	87,254	63,494	39,400
<b>TOTAL ASSETS</b>	<b>34,266,304</b>	<b>33,438,080</b>	<b>32,731,137</b>	<b>33,183,723</b>	<b>33,573,767</b>	<b>33,466,573</b>	<b>33,321,041</b>
<b>LIABILITIES &amp; EQUITY</b>							
Accounts Payable	130,348	215,836	164,524	184,378	185,362	203,671	221,694
Accrued Expenses	462,427	589,477	514,136	548,744	551,672	578,609	602,428
Current Port. of LT Debt/Capital Leases	1,866,321	1,547,179	1,512,781	375,352	391,701	459,126	-
Other Current Liabilities	2,969,812	3,132,376	3,226,347	3,323,138	3,422,832	3,525,517	3,631,282
<b>Total Current Liabilities</b>	<b>5,428,908</b>	<b>5,484,868</b>	<b>5,417,788</b>	<b>4,431,612</b>	<b>4,551,567</b>	<b>4,766,923</b>	<b>4,455,404</b>
Long-term Debt	3,208,271	1,662,722	375,352	1,391,701	1,459,126	1,000,000	1,000,000
Other Liabilities, Total	62,045	62,718	62,718	62,718	62,718	62,718	62,718
<b>Total Liabilities</b>	<b>9,241,185</b>	<b>7,671,949</b>	<b>6,317,499</b>	<b>6,347,672</b>	<b>6,535,052</b>	<b>6,291,282</b>	<b>5,979,763</b>
<b>Total Equity</b>	<b>25,025,119</b>	<b>25,766,131</b>	<b>26,413,638</b>	<b>26,836,051</b>	<b>27,038,715</b>	<b>27,175,291</b>	<b>27,341,278</b>
<b>TOTAL LIABILITIES AND EQUITY</b>	<b>34,266,304</b>	<b>33,438,080</b>	<b>32,731,137</b>	<b>33,183,723</b>	<b>33,573,767</b>	<b>33,466,573</b>	<b>33,321,041</b>
Income Statement (EGP Thousands)		Historical		Forecast			
Fiscal Year Ends December	2007	2008	2009	2010	2011	2012	2013
Total Revenue	9,993,147	10,116,896	10,282,720	10,974,883	11,033,444	11,572,188	12,048,570
Cost of Revenue	1,388,221	1,270,345	1,028,272	1,152,363	1,158,512	1,272,941	1,385,586
<b>Gross Profit</b>	<b>8,604,927</b>	<b>8,846,551</b>	<b>9,254,448</b>	<b>9,822,520</b>	<b>9,874,932</b>	<b>10,299,247</b>	<b>10,662,984</b>
Selling/General/Admin. Expenses	3,379,890	3,895,837	4,113,088	4,389,953	4,468,545	4,779,314	5,000,156
Depreciation/Amortization	2,870,625	2,695,933	2,662,134	2,738,596	2,815,466	2,896,090	2,980,032
Other Operating Expenses	332,887	508,899	411,309	438,995	441,338	462,888	481,943
<b>Operating Income</b>	<b>2,021,525</b>	<b>1,745,882</b>	<b>2,067,917</b>	<b>2,254,975</b>	<b>2,149,584</b>	<b>2,160,956</b>	<b>2,200,853</b>
Interest Income (Exp), Net Non-Operating	(478,725)	(117,543)	(88,220)	33,206	122,979	215,255	313,609
Equity In Affiliates	1,022,910	1,179,771	1,267,611	1,286,228	1,350,577	1,404,071	1,457,811
Other, Net	335,299	157,771	172,264	177,432	182,755	188,238	193,885
<b>Net Income before Taxes</b>	<b>2,901,009</b>	<b>2,965,881</b>	<b>3,419,572</b>	<b>3,751,842</b>	<b>3,805,895</b>	<b>3,968,520</b>	<b>4,166,157</b>
Provision for Income Taxes	513,331	512,313	547,132	600,295	608,943	634,963	666,585
<b>Net Income After Taxes</b>	<b>2,387,678</b>	<b>2,453,568</b>	<b>2,872,440</b>	<b>3,151,547</b>	<b>3,196,952</b>	<b>3,333,557</b>	<b>3,499,572</b>
Minority Interest	(6,725)	(5,712)	(5,741)	(5,769)	(5,798)	(5,827)	(5,856)
<b>Net Income</b>	<b>2,380,953</b>	<b>2,447,856</b>	<b>2,866,700</b>	<b>3,145,778</b>	<b>3,191,153</b>	<b>3,327,730</b>	<b>3,493,716</b>
Cash Flow (EGP Thousands)		Historical		Forecast			
Fiscal Year Ends December	2007	2008	2009	2010	2011	2012	2013
Cash from Operating Activities	4,639,633	4,347,941	4,439,069	4,454,501	4,745,512	4,616,267	4,768,790
Cash from Investing Activities	(149,183)	636,033	32,983	125,342	246,503	297,867	341,646
Cash from Financing Activities	(3,805,583)	(3,645,762)	(3,732,328)	(2,983,310)	(3,042,251)	(3,709,209)	(3,882,259)
Foreign Exchange Effect	31	(383)					
<b>Net Change in Cash</b>	<b>684,898</b>	<b>1,337,829</b>	<b>739,724</b>	<b>1,596,532</b>	<b>1,949,765</b>	<b>1,204,925</b>	<b>1,228,177</b>

Sources: Annual reports and NBK Capital

## RISK AND RECOMMENDATION GUIDE

Recommendation		Upside (Downside) Potential				
Buy		more than 20%				
Accumulate		between 10% and 20%				
Hold		between -5% and 10%				
Reduce		between -10% and -5%				
Sell		less than -10%				
RISK LEVEL						
Low Risk					High Risk	
1	2	3	4	5		

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