

# Emerging European Telecoms

11 December 2008

## Reality rings

### Recommendations

|               |                   | Price*  | Mkt.cap | EV/EBITDA (x) |       | Dividend Yld (%) |        | Fair  | Upside |
|---------------|-------------------|---------|---------|---------------|-------|------------------|--------|-------|--------|
|               |                   | (local) | (€ m)   | 2009F         | 2010F | 2009F            | 2010F  | Value | (%)    |
| Mtelekom      | Buy (upgraded)    | 560     | 2,539   | 3.2           | 3.3   | 13.90%           | 14.20% | 720   | 28.5%  |
| TPSA          | Buy (maintained)  | 18.6    | 7,947   | 3.7           | 3.5   | 8.80%            | 9.70%  | 26.5  | 42.5%  |
| Telefonica O2 | Buy (maintained)  | 432     | 5,952   | 4.7           | 4.7   | 11.60%           | 11.60% | 540   | 24.9%  |
| Netia         | Hold (maintained) | 2.74    | 333     | 3.6           | 2.4   | 4.70%            | 4.70%  | 3.0   | 9.5%   |
| Vimpelcom     | Buy (maintained)  | 9.3     | 5,895   | 2.2           | 1.9   | 7.80%            | 10.50% | 15.2  | 63.7%  |
| MTS           | Buy (maintained)  | 30.3    | 7,518   | 2.5           | 2.2   | 12.20%           | 12.20% | 35.2  | 16.2%  |
| Comstar       | Hold (maintained) | 2.7     | 705     | 2.2           | 1.9   | 0.20%            | 0.20%  | 3.0   | 9.3%   |
| Turkcell      | Hold (maintained) | 8.5     | 10,388  | 4.0           | 3.9   | 6.10%            | 5.90%  | 9.0   | 5.6%   |

Source: KBC Securities, Bloomberg

\*priced at COB 08/12/2008

We have reduced our earnings estimates for CEE telecoms by 10%-30% for 2009-2010 to factor-in the potential impact of a deeper economic contraction. Despite the 8.3% outperformance of MSCI EMEA Telecoms versus MSCI EMEA year-to-date, and the even larger outperformance of CEE operators, valuations remain attractive relative to Western European peers, and the market in general. Taking into account the sector's higher resilience to the economic downturn, relatively stable revenue streams, and high cash payout ratios, we expect it to continue to outperform in 1H09, albeit to a lesser extent than in 2008. Within our coverage universe, we continue to prefer TPSA for its growth and value.

### Rating update

- **Macro shock resistant:** MSCI EMEA Telecoms have outperformed the broader EMEA index by 8.3% year-to-date, in-line with the outperformance of global telecoms versus MSCI World. The sharp decline of the Russian operators has overshadowed a stellar outperformance in the remainder of the region.
- **Stable revenue streams:** We expect telecom spending to remain stable at some 2.5%-3.0% of GDP per capita across CEE. Core revenue streams of operators are relatively resilient to the economic slowdown, following the shift to standard tariff packages in the last five years.
- **Margin pressure from new services:** The bulk of our earnings downgrades come from margin reductions, as broadband and 3G services are expected to prove more vulnerable. We now expect EBITDA to grow 4.7% in 2009 and 5.2% in 2010, versus our previous estimates of 12.6% in 2009 and 6.3% in 2010.
- **Integrated operators offer the best hedge:** Integrated operators offer the safest investments during volatile times, as the potential slowdown in broadband, and to a lesser extent mobile, is more easily weathered, due to the stability of cashflows from the core fixed-line business. CEE incumbents offer the highest shareholder payouts, given resilient cashflows and the potential to downsize capital expenditures.
- **Outlook for mobile operators in Russia is better than in Turkey:** Russian and Turkish operators are vulnerable to currency devaluation, given macroeconomic pressures. However, lower Russian mobile tariffs provide a comfortable buffer for price adjustments to offset currency volatility. Russian mobile operators generate an average of US\$0.06 per minute, versus Turkcell's US\$ 0.16, and the CEE average of US\$ 0.13.
- **TPSA offers the most attractive growth and value prospects:** On a 2009F EV/EBITDA of 3.7x, versus CEE operators on an average of 3.9x, TPSA offers the best value. We expect a 2008-2011 CAGR of 9.3% in earnings, and 2009F cash and dividend yields of 15.5% and 8.8% respectively.

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## Definition of terms applied in the publication:

EBITDA = EBIT + amortization and depreciation

EPS = Net profit / No of shares outstanding

DPS = Dividend per Share

NBV per share = Net Book Value / No. of shares outstanding

EBITDA margin = EBITDA / Revenue

EBIT margin = EBIT / Revenue

CFPS = Cash flow / No. of shares outstanding

Net Financial Debt = Financial debt – Cash equivalents

ROE = Net profit / Average Equity

EV = Market Capitalization + Net Financial Debt

P/E = Stock Price / EPS

P/CF = Stock Price / (Net Profit + amortization and depreciation)

P/BV = Stock Price / NBV per share

P/S = Market Capitalization / Revenue

Gross Dividend Yield = Dividend per share / Stock

### List of recommendations concerning TPSA issued by KBC Securities NV Branch in Poland during the last 12 months

|      | Valuation | Market price | Recommendation | Date of issue    |
|------|-----------|--------------|----------------|------------------|
| TPSA | 24.1      | 20.5         | Buy            | 22 January 2008  |
| TPSA | 26.9      | 22.6         | Buy            | 07 February 2008 |
| TPSA | 26.9      | 21.8         | Buy            | 01 May 2008      |
| TPSA | 27.2      | 24.1         | Buy            | 11 August 2008   |
| TPSA | 26.5      | 18.6         | Buy            | 11 December 2008 |

### List of recommendations concerning Netia issued by KBC Securities NV Branch in Poland during the last 12 months

|       | Valuation | Market price | Recommendation | Date of issue    |
|-------|-----------|--------------|----------------|------------------|
| Netia | 4.0       | 3.8          | Hold           | 14 March 2008    |
| Netia | 3.0       | 2.74         | Hold           | 11 December 2008 |

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|         |     |
|---------|-----|
| 27 BUY  | 66% |
| 11 HOLD | 27% |
| 3 SELL  | 7%  |

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