



## **Telecom Egypt Announces First Quarter 2008 Results**

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### **Presenters**

- Mr. Akil Beshir, Chairman & CEO
- Mr. Tarek Tantawy, Vice President & CFO
- Mr. Mohamed Elnawawy, Vice President for Int'l, Wholesale & Regulatory Affairs
- Ms. Alia Allouba, Investor Relations Manager

### **Karim Khadr**

Hello, Good morning, and good afternoon everybody this is Karim Khadr from HSBC. I would like to welcome you all to Telecom Egypt First Quarter 2008 Results conference call that we are very happy to be hosting today.

From Telecom Egypt we have with us Mr. Akil Beshir, TE's Chairman and CEO, Mr. Tarek Tantawy, Vice President and CFO, Mr. Mohamed Elnawawy, Vice President for Int'l, Wholesale and Regulatory Affairs and Ms. Alia Allouba, Investor Relations Manager.

The conference call will start with a presentation on the operational and financial highlights for the first three months of the year followed by a Q&A session. I will now hand the call over to Telecom Egypt to Ms. Alia Allouba for a Safe Harbour Statement.

### **Alia Allouba**

Thank you, Karim, for the introduction and for hosting the conference call. Good morning and good afternoon everyone.

As a standard rule of Corporate Governance at Telecom Egypt I will first start by reading a Safe Harbour Statement.

We may make some forward-looking statements in the course of this conference call. These will be based on information available to us as of today and you should therefore not assume in the future that we continue to hold these views then. We do not commit to notify you if our views change. We refer to our public filings for some factors that may cause forward-looking statements to differ from actual future events or results. So that was the statement.

I would like now to hand over to Mr. Akil Beshir, Chairman and CEO of Telecom Egypt. Mr. Chairman.

### **Akil Beshir**

Thank you Alia and good morning and good afternoon everyone.

As usual, I welcome you to today's call and look forward to taking your questions in just a moment. First, I will comment briefly on today's consolidated results which are presented to you under Egyptian GAAP, Tarek will go into a little more detail on the numbers and Vodafone Egypt's performance and then we will move on to your questions.

As I reported to you last quarter, the emphasis of our business continues to shift. During the first three months of the year, we were focussed on capturing and optimising the increasing demand for wholesale services. Increased promotional activities by the mobile operators have accelerated the development of the mobile market in Egypt, resulting in heightened demand for access to our extensive, highly-modernized network. During the period under review, total wholesale revenues have increased by 12 percent year-on-year and now comprise 40 percent of our total revenue base.

As a result of this activity, we are seeing some effects of fixed-to-mobile substitution pressuring total retail revenues, in particular within the retail voice segment.

The year-on-year decline in total voice revenues, from EGP 836 million in the first quarter of 2007 to EGP 708 million in the first quarter of 2008, was directly related to the ramp-up in price promotions from mobile providers.

Presently, we are unable to compete fairly with such promotions, because of the structure of existing interconnection agreements.

I fully expect mobile operators in Egypt will continue to employ aggressive marketing techniques across all call types to capture market share. What is important here is to establish a level playing field for both new entrants and incumbent operators.

Our discussions with the mobile operators and the regulator in respect of a change in the interconnection agreement to allow for a reduction in the fixed-to-mobile termination rates are underway and an outcome is expected at the beginning of the third quarter this year.

An agreement on this will allow us to compete on a more equal footing and will be favourable to our consumers as reductions will be passed on directly.

You should view this as just one element of the next round of tariff rebalancing that we expect to come into effect on July 1<sup>st</sup> of this year. As most of you know the last round was successful in its implementation and we witnessed no real decline in usage.

Once the process of negotiation and rebalancing is complete we will focus on a broad campaign for boosting awareness of the value and quality that consumers can gain by using TE's network. The reliability of our network and service is a great asset.

I fully expect these initiatives to restore retail revenues and put us on track to achieve our full year guidance of top line growth of between 2 and 3 percent.

I should point out that, irrespective of this process and because of the significant reach of our network, the decline in our retail voice revenues experienced during the quarter has been partially offset by the uplift in wholesale revenues. Wholesale revenues are an important future item and already make up a growing component of our revenue base - one which, when domestic and international wholesale are combined, account for a significantly greater proportion of total revenues than our retail voice business.

Year-on-year comparisons show that, despite market pressures, total sales revenues were recorded at similar levels - EGP 2.4 billion. Within this total, retail revenues were EGP 1.4 billion and wholesale revenues were approximately EGP 1 billion.

Another point I would like make is that our business is seasonal and this has a notable bearing on both voice traffic, particularly in respect of international calls, and on revenues derived from new connections. Some of you have asked about the quarter-on-quarter progression, which we show clearly in our results. Because of seasonality effects, comparisons with the fourth quarter of 2007 are misleading.

International calls usually peak during the second half of the year due to seasonality, which spurs our customers to increase the overseas calls they make. The quieter first quarter for international traffic is borne out by today's results within Retail Voice revenues under fixed-to-international and within the International Wholesale segment, both of which increased year on year, but when observed quarter-on-quarter seemed to decline. We fully expect 2008 to be the same as any other year in respect of these seasonal trends and this does not impact our expectations for the year.

When I talk to our customers they are highly satisfied with the quality of our service. We continue to have one of the largest fixed-line subscriber bases in the region, with 11.25 million subscribers as at the end of March 2008. This is up 3 percent on the previous year, however, as we have explained before, our focus going forward is not on boosting this number further, but instead on ensuring subscribers are well serviced and profitable.

Our presence in the growing market for Internet and data services continues to be reinforced by the performance of TE Data. We are the Egyptian market leader and have established a market share that by the end of March 2008 stood at almost 54 percent. TE Data added more than 38 thousand Retail ADSL subscribers in the last three month, taking their subscriber base to close to 260 thousand which represents a 134% year on year increase.

While still a small component of total revenue, the increasing success of our internet offering is valuable in offsetting the pressure on retail voice revenues experienced during the period.

As ever, profitability is a key metric against which we judge our own performance. We continue to maintain an EBITDA margin that is within management expectations at 51 percent. EBITDA before provisions for the three months ended March was EGP 1.2 billion and has been impacted by the increased employee costs relating to annual pay awards and bonuses awarded at the start of the year. I view the question of total reward for our committed workforce as business critical as we seek to recruit and retain the highest caliber of telecommunications professional in an increasingly competitive market. Tarek will however focus on this item and its domestic market context a little more in just a moment.

Consolidated Net Profit for the period under review was EGP 557 million, a slight drop on the same period in 2007 because of the factors I have mentioned. This still translates into a Net Profit Margin of 23 percent, which is high by industry standards.

Finally, before I hand over to Tarek to talk through the numbers, I would like to comment on our strategic project, TE North.

As you know, last year was an important year for the progress of our submarine cable project TE North, designed to capitalize on the combination of our unique geographic position and the capacity of our infrastructure.

Spanning more than 3,000 km, TE North will be capable of delivering an ultimate capacity of 10 terabits per second on eight fibre pairs. This makes it one of the largest systems in the world in terms of density, if not the largest.

It is designed to capture a portion of the non-serviced demand for IP traffic capacity from Asia and India into the West, while simultaneously lowering the cost point for international bandwidth for TE and its subsidiaries.

During 2007, as you know, we announced two contracts with anchor customers, IMEWE, SEACOM and VSNL. I am pleased to say that subsequent to the close of the quarter we have signed an additional contract with Europe India Gateway (EIG) Submarine Cable System, worth USD 50 million. Together, the total value of contracts signed by TE in respect of the TE North project comes to US\$176 million. With anticipated capex for the entire project coming in at between \$150 and \$160 million over the next two years you can see that we have more than covered our build capex with these initial sales, meaning that this is a very safe project.

We expect to bring you further updates on TE North as 2008 progresses.

With that I would like to hand over to Tarek.

**Tarek Tantawy**

Thank you, Mr. Beshir.

As pointed out in our full year results conference call, Q1 2008 is the first quarter in which we started to report our revenue breakdown in a more compressed form and there has been some reclassification as well in terms of revenue reporting in our disclosure to better reflect our business lines as shown in note 23 to our financial statements.

We have maintained the same broad revenue reporting in terms of reporting retail and wholesale revenues. However, under retail revenues we now only report access revenue which includes connection and subscription revenues; voice revenue; Internet & Data and others. Under wholesale services we now report total domestic which includes mobile to fixed interconnection and infrastructure and facility leasing and total international which includes mobile to international and incoming international to fixed and mobile and capacity sales.

In terms of the reclassification that happened in revenue disclosure, we now report dial-up Internet revenues under Internet & Data instead of previously reporting it in voice revenues as part of local calls. We have also reclassified some of the items under other retail services to be included under domestic and international wholesale. Those items are mainly related to infrastructure and facility leasing as well as capacity sales.

Going back to our financial performance during the first quarter of 08, the year on year growth in wholesale revenues has certainly characterised the first quarter of 08 for TE.

Total revenues for the quarter were approximately EGP 2.4 billion, of which EGP 952 million were wholesale revenues. This represents a 40 percent contribution.

The increase in mobile traffic in Egypt means that domestic wholesale revenues now account for almost 28 percent of our total wholesale revenues, up from 26 percent in 07. This is also notable as it provides a balance to the revenues we derive from international voice services to mobile operators.

Within the retail segment, it is true that voice revenues have come under pressure, down 15 percent year on year. As expected the pressure on voice revenues is mainly coming from domestic long distance and fixed to mobile calls which are negatively impacted by the cheaper mobile to mobile rates. We expect that once changes happen to the existing interconnection agreements with mobile operators we can start offering more competitive rates and hence gain back some of the traffic that has migrated to the mobile operators networks.

As Mr Beshir has pointed out; the thing to bear in mind concerning fixed-to-mobile substitution is the fact that any revenue we lose to the mobile operators partially comes back to us in one of two ways. Firstly, through the investment income we receive from our stake in Vodafone Egypt and secondly through increasing revenues generated from increased third party traffic being directed over our network.

Moving on through the P&L line items.....

Our underlying EBITDA margin before provisions trend remains on target at low fifties – coming in at 51 percent for the quarter. EBITDA before provisions was impacted by increased employee costs Mr Beshir has mentioned. It is worth mentioning that our annual salary increase for 2008 was approximately 20%. 10% were effective from January and another 10% effective from the first of May. The reason for the subsequent 10% salary increase in May was to ensure that in a more competitive market for telecommunications professionals, we continue to attract and retain talent especially in light of the recent 30% increase in salaries of civil servants made by the government and indications that the private sector companies will follow. One thing to point out as well is that we would not be increasing salaries except in July 2009 and there will be no increase in January 2009.

The annual salary increase coupled with the flat revenues year on year as well as end of year bonuses has resulted in employee costs as a percentage of total sales increasing to 21 percent versus 18 percent during the same period in 2007.

In terms of other major cost points we strip out to arrive at our EBITDA calculations, interconnection costs were EGP 325 million an increase of 11% year on year, and other operating expenditure were EGP 363 million.

EBIT for the first quarter of 2008 was further impacted by increased foreign exchange losses, given the appreciation of the Euro and the depreciation of the US Dollar against the Egyptian pound. These losses were EGP 50 million in the first quarter of 2008, versus EGP 14 million in the first quarter of 2007. Correspondingly, EBIT actually came in at EGP 743 million versus EGP 860 million, a decline of 14 percent.

Despite these external pressures, we remain committed to profitability and have again delivered margins that are robust and within expectations.

As I reported to you in the fourth quarter, industry margins within the mobile industry in Egypt have come down as a result of customer numbers and minutes growing faster than revenues, compounded by aggressive price reductions.

Within this context, Vodafone Egypt continues to maintain the highest share of sector revenues and profits versus competition.

In this highly competitive environment, VE management continues to deliver against its strategic and financial objectives. Our investment in Vodafone Egypt has once again made a substantial contribution to our results, contributing EGP 277 million in investment income to our first quarter result.

Please remember that Vodafone Egypt reports a financial year ending on 31 March, so the numbers we are presenting to you today are for the year from 1<sup>st</sup> April 07 to 31 March 2008.

During this period, Vodafone Egypt recorded net additions of 4.4 million subscribers, taking its customer base to more than 14 million. This base generated a total of 6.4 billion minutes in the last three months to end of March 2008, and 22.7 billion over the course of the 12 months to 31 March 2008. Year-on-year for the 12 month number, this is an increase of 60 percent.

Financial performance was also strong for the 12 months period, Vodafone Egypt reached service revenue of EGP 10.4 billion, up 28 percent year-on-year. Correspondingly, Vodafone Egypt's net profit for the year to end of March 08 reached EGP 2.7 billion, representing a year-on-year increase of 7 per cent when compared with the same period in the previous year.

Vodafone Egypt's capex figures reached EGP 2.8 billion for the 12 month period, an increase of 33 per cent year-on-year.

Turning back to Telecom Egypt, the deleveraging work we completed in 2007 has been continued into the first quarter. Total debt position as of 31 March 2008 was EGP 4.5 billion, compared to EGP 5 billion at the end of December 2007. This represents a reduction of EGP 500 million during the first three months of 2008. Net debt at the end of March 08 was EGP 2 billion and you should expect our net debt position in 2<sup>nd</sup> quarter of 2008 to be higher than this due to the fact that dividends for the year 2007 totalling EGP 1.7 billion were paid in April 2008.

Capex during the period under review was EGP 232 million representing a reduction of 13% year on year.

So with that, I would now like to hand back to Mr. Beshir for his closing remarks.

**Akil Beshir**

Thank you, Tarek.

In many respects the first quarter has been challenging and these challenges will continue in the short term. However, we are doing all we can to ensure the wholesale opportunity is optimised and the current competitive imbalance is addressed through negotiation on interconnection agreements and tariff rebalancing in retail market. This is a key priority for 2008, and as I indicated earlier this is expected to happen 1st of July of 2008.

Once the next round of tariff rebalancing and interconnection rate negotiations are agreed, I believe that we will be in excellent shape to deliver on our objectives for the year.

I would once again remind you that as mobile penetration in Egypt continues to grow rapidly we stand to benefit, not only as a strategic investor in Vodafone Egypt, but also from the positive effect of mobile related income streams on our core business.

With that I would like to open up to your questions. Operator, please go ahead.

**(Coordinator)** Your first question comes from Cesar Tiron from JP Morgan, please go ahead.

**Cesar Tiron** Hi, I have two questions please. The first one can you please give us an update on the second fixed-line license and confirm that the 2nd operator will not be allowed to offer also international services in the first two years of operation? That's the first question.

The second question, can you please repeat what is the magnitude of the increase in salaries and when do you expect those to take place? And my third question is, if there is any reason that you will not be allowed to go ahead with the tariff rebalancing at the last minute just in light of the strong pressure of the inflation we're seeing in Egypt over the past month? Thank you very much.

**Akil Beshir** Thank you. Concerning the second fixed-line, as you know, the RFP was out in mid March and bids are supposed to be submitted on the 19th of June which was delayed to 29<sup>th</sup> of July. So far twelve companies bought the RFP documents.

The second operator as you mentioned will have international, however, first he'll be allowed, as of day one, to sell international to his own customers. However, after certain coverage obligations that are met he'll then be allowed to sell also international to other fixed line customers, our customers so all fixed line customers will have carrier selection options. However, he will not be allowed to sell to mobile customers before two years. And I have to mention here that right now about 70 percent of the international traffic is through mobile.

**Tarek Tantawy** On the salaries we have done an increase of 10 percent in January 2008 and we will do another 10 percent in May 2008. So if you're looking at the full year of 2008 versus '07 you can expect a salary increase in the range of 16 to 17 percent year-on-year.

The important thing to mention is that we usually have our increases done in January, but since we have done another increase in the middle

of 2008 we will not be increasing salaries again in January 2009 and will delay this until July 2009.

- Akil Beshir** And would go on July every year afterwards.
- Cesar Tiron** And in July 2009 do you expect the magnitude of the increase to be as high as in 2008?
- Tarek Tantawy** No, no we believe it should go back to, you know, the normal levels of 7 to 10 percent.
- Cesar Tiron** Okay.
- Akil Beshir** Concerning tariff rebalancing, as I said, no we do not see any chance that we will not be doing that and I have to remind you here that all previous tariff rebalancing were not really rebalancing they were just tariff increases. This is why it was delayed from April till July, so that we have a real rebalancing, meaning increasing subscription fee and subsequent minute charge and reducing the fixed to mobile tariff. So we're very confident and actually we confirmed this with the regulator today before this call just to make sure that there are no changes in the position.
- Cesar Tiron** Okay, thank you very much.
- Akil Beshir** You're welcome.
- (Coordinator)** Thank you. Your next question comes from Osman Zaki from Merrill Lynch, please go ahead.
- Osman Zaki** Thank you. I just have one question. Two of mine have been answered already. On the capex, i see what was only spent is 13 million in Q1? I believe your target for the full year was about 1.5 to 2 billion pounds. Are we still sticking to that same guidance on capex for the full year? Thanks.
- Tarek Tantawy** Yes, yes, we are sticking to the same guidance of 1.5 to 2 billion pounds.
- Osman Zaki** Great, thank you.
- (Coordinator)** Thank you. Your next question is now coming from Dirella McHenry, please go ahead.
- Dirella McHenry** Hi thanks for the call this morning. I was looking further on Vodafone Egypt. Can you share anything in terms of ARPU and specifically the percentage of ARPU which comes from non-voice deficits? And I was also wondering whether it's possible to know what percentage of the subscribers have with 3G enabled handsets?
- Tarek Tantawy** I'm sorry could you repeat the question again please.

**Dirella McHenry** Sure. I was wondering whether you can share on Vodafone Egypt ARPU. And in particular the percentage of their ARPU that come from non-voice also was wondering whether you can tell us what percentage of Vodafone Egypt subscribers have 3G enabled handsets?

**Tarek Tantawy** Unfortunately, we cannot, you know, address the last two questions. But on the first one in relation to ARPU – this is the something we can report and Vodafone Egypt’s Global ARPU was 64 pounds; prepaid is 47 and post paid is 287.

**Dirella McHenry** Okay. On the 3G question, I’m not necessarily asking how many subscribers you have but whether you can keep track of what percentage of users have enabled handsets.

**Tarek Tantawy** I’m sorry, I mean Vodafone Now is a private company and we would like to keep the privilege of not, you know, disclosing lots of details on their revenue break-down, so this is as far as we can disclose.

**Dirella McHenry** Okay, thank you. Could I ask you a few questions on the fixed side also?

**Tarek Tantawy** Go ahead

**Dirella McHenry** I wanted to check first of all the ARPU that you were reporting, results on the fixed side does that refers just to voice or DSL and dial up ARPU are also completed in that?

**Tarek Tantawy** Yes, it includes internet as well.

**Dirella McHenry** Okay and is there any way you could share what the most popular business and residential plans are for DSL?

**Mohamed Elnanawi** Yes, TE Data is our retail arm responsible for our internet services and the company has launched the first IPTV offering in Egypt back in 2006. Currently, the company is revamping this offering and they’re creating a whole new product that will include much more locally digitalized content and would be addressing a much, much larger spectrum of customers.

TE Data has presently 54 percent of the retail DSL markets Telecom Egypt of the wholesale level caters to 100 percent of this market. TE Data has been growing very well year end last year it had 52 percent and now it has 54 percent.

**Dirella McHenry** Okay. And can you tell us, I’m assuming on the residential side at least the 45 pound a month plan is the most popular? Is that correct, is there a particular plan for the business side?

**Mohamed Elnanawi** Yes, Approximately 70 percent of the customers take this plan, yes.

**Dirella McHenry** Okay. Great thank you.

**Mohamed Elnanawi** You're welcome.

**(Coordinator)** Okay, thank you. Your next question is coming from Osman Zaki from Merrill Lynch, please go ahead.

**Osman Zaki** Yes hi. Tarek can you please repeat ARPU of Vodafone Egypt again? Thank you.

**Tarek Tantawy** For Vodafone Egypt the Global ARPU is 64, prepaid is 47 and postpaid is 287.

**Osman Zaki** Is this for the quarter or for the full year?

**Tarek Tantawy** That's for the quarter.

**Osman Zaki** Okay great. Thank you.

**(Coordinator)** Thank you. At this time there are no more questions. Ladies and gentlemen at this point it seems that we do not have any further questions and I would like to end the call over back to Mr. Akil Beshir for his closing remarks.

**Akil Beshir** Thank you. Well, I'd like to thank you again for being with us on this call and as we explained the pressures we had on the retail revenues in this quarter, we're very confident that it will be properly addressed with the tariff rebalancing and reducing the mobile termination. And we're still confident that at the end of the year we'll be on target on our guidance for the revenues and for the profits.

So thank you very much again and talk to you again next quarter. Thank you.

**(Coordinator)** Again, a replay of the call will be available from the 15 of May and will be available for one week. To access this replay for international callers the number will be +44 207 1920 853 and for U.S. callers the number is +1 866 856 0170 with pass code 3151. Thank you very much.

**END**