المتحدة للأوراق المالية ش.م.م
UNITED SECURITIES LLC

INVESTMENT RESEARCH | OMAN

Sector Note: Telecom

BUY Omani Telecos; Mix of Value & Yield

Omantel — STRONG BUY

Stock data			
Price target (RO)			**1.000**
CMP (RO)			0.724
Potential Upside (%)			38%
Free Float (%)			49%
Beta			1.6
Shares O/S (mn)			750
Valuation	**2017**	**2018E**	**2019E**
P/E Ratio (x)	12.0	7.9	5.0
P/B Ration (x)	1.7	0.9	0.8
P/S Ratio (x)	1.3	0.3	0.3
EV/EBITDA (x)	12.3	4.7	4.3
Dividend Yield (%)	6.9%	4.7%	7.2%
		RO	**USD**
Market Cap		543	1,410
Enterprise Value		2,890	7,506
Price Performanc	**6M**	**12M**	**YTD**
Omantel	-40.9	-42.3	-39.9
MSM30 Index	-10.3	-15.5	-10.5

Ooredoo Oman — BUY

Stock data			
Price target (RO)			**0.572**
CMP (RO)			0.506
Potential Upside (%)			13%
Free Float (%)			45%
Beta			1.3
Shares O/S (mn)			651
Valuation	**2017**	**2018E**	**2019E**
P/E Ratio (x)	11.1	10.1	8.5
P/B Ration (x)	1.4	1.4	1.3
P/S Ratio (x)	1.3	1.2	1.1
EV/EBITDA (x)	3.1	2.9	2.6
Dividend Yield (%)	8.3%	-8.9%	-10.6%
		RO	**USD**
Market Cap		329	856
Enterprise Value		360	936
Price Performanc	**6M**	**12M**	**YTD**
Ooredoo Oman	-7.7	1.6	-3.8
MSM30 Index	-10.3	-15.5	-10.5

Oman's telecom sector is undergoing a fundamental shift on both at the regulatory as well as operating side, leading to a revisit on the sector story. We upgrade Omantel to STRONG BUY after its recent sell-off created value buying opportunity and assign 12M TP of RO 1.000/Share, implying upside potential of 38% from current levels, while we maintain our BUY rating on Ooredoo Oman with 12M TP of RO 0.572, c.13% upside. Both telecom companies are trading at discount to their GCC peers, offering an attractive valuation sweet spot compared to GCC peers. Our positive stance in OTEL is stemming from its focus on wholesale business growth driven by Zain acquisition and submarine cable capacity enhancements, while ORDS is expected to maintain lower earnings volatility and stable payout leading to high dividend yield. We expect OTEL's domestic voice business to witness decline due to competition from OTT apps and expected award of third mobile operator in the country. Yet, the company is estimated to deliver profitability growth by leveraging on its growing Submarine Cable System, wholesale and ICT segments in addition to synergy gains from Zain acquisition. We see ORDS maintaining its superior FCF generating capability with reduced capex and relatively lower revenue impact from the introduction of third operator. Companies are losing on conventional revenue streams while data becomes the key revenue contributor. OTEL is establishing itself as a key wholesale player in the region's telecom landscape while ORDS is further building its profitability on efficiency gains.

Revenue growth from Data, ICT & wholesale business to offset voice revenue decline; Omantel to be a key regional player in the emerging segments: With mobile penetration of 145% and smart phone penetration of close to 80%, decline in conventional voice revenue streams, and data segment growth rates falling to low double digits while companies are facing macro headwinds in the form of low oil prices, declining expat population growth rates, and regulatory changes, Omani mobile telecom market is turning from a mature to declining phase. Companies are seeking further revenue growth opportunities from wholesale and ICT segments and also via cross border acquisitions. Challenging macro conditions and reduction in expat population have reduced the mobile penetration growth and we expect domestic penetration growth to remain muted until the next 5G growth cycle kicks in. In the recent times, companies have been busy bundling smartphone equipment with long term postpaid subscriptions, which has resulted in 6.5% growth in postpaid subscriber base to 669K in 1Q18. OTEL has been the aggressive player in smart phone offering, which saw 10% y/y growth in postpaid customers. This trend is likely to continue in the future, driving down the ARPU gap between prepaid and postpaid customers.

Risks: The threat of third mobile operator still lingers in the air, the materialization of which could negatively impact the performance of existing players. Our scenario analysis suggests OTEL could face the major threat from third operator while impact on ORDS could be relatively lower. The increase in telecom royalty have negatively impacted the telecom sector profitability and margins. The Implementation of new Access and Interconnection Tariff regime as suggested by the TRA is likely to impact revenue and margins of OTEL going forward. Despite these challenges, our positive stance on the sector is coming from the new revenue streams that are being opened up for OTEL and view it as a deep value stock.

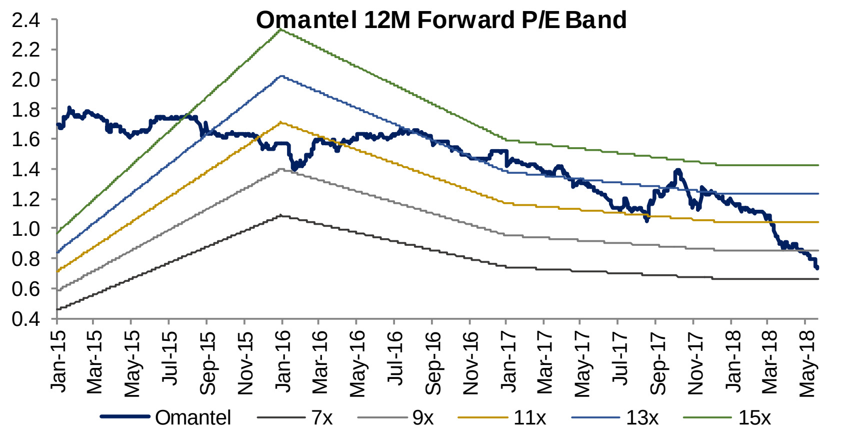
Subscriber growth to slow down; data revenue growth to continue, while Domestic ARPU remains under pressure: In the past five years mobile telephone subscribers have grown at a moderate 5%. Though fixed telephony grew by 9%, the level of subscribers continues to be low. Internet subscribers on the other hand has grown at a strong 15-20%. Going forward we expect voice growth to continue to be moderate, while data growth will grow at double digit. Growth in data is likely to be aided by the strong demographic profile in Oman. ARPUs on the other has been under pressure across segment and the same is expected to continue. However, we also note that the ARPU's in Oman is one of the lowest in the region and as a result could have only a limited downside from the current level.

Entry of third operators is likely to make the market more challenging: Telecom regulators have been considering giving third operator license in Oman since 2016. We expect this to be finalized in the next two years. This in turn is likely to put further pressure on the incumbents. Given the relatively matured nature of the market, the introduction of third party will be value depraving for both the incumbents, OTEL and Ooredoo.

Regulatory changes on interconnection charges negative for OTEL: With an aim of opening up of the current Telecom infrastructure to all operators, the Telecom regulator has proposed to calculate interconnection charges on a cost-plus basis, compared to the current process of calculating the same on a commercial basis. This in turn is expected to reduce the entry barriers for new operators. Added to this, this regulation will also reduce the cost of access to Ooredoo, which in turn can help the company gain market share in areas where it is currently not present. Overall, we feel that the current regulation is a negative for OTEL.

Recent selloff in OTEL provides attractive entry point; STRONG BUY rating with target price of RO 1.000: OTEL has a strong financial profile, leading market position in the domestic telecom market and has recently achieved a diversified market position across Middle East through Zain acquisition. The company is constrained by an already competitive market in Oman, the potential entry of a third operator and adverse regulatory reforms, which are likely to pose challenges to its financial position and margins. However, we expect OTEL's acquisition of Zain, though slightly overpaid, to add value in the long run. Zain's operations in Iraq and Sudan, which has thus far been weighing on its performance, is showing signs of recovery, which could provide further upside. Apart from this, OTEL has estimated cash synergy of RO 30 million to accrue annually. We expect to see the full benefits of synergy to accrue from 2020E. We have valued the company using a blended DCF-Relative Valuation technique and arrived at 12M target price of RO 1.000/Share, which is 38% higher than the current price. We believe that the recent selloff in the stock has opened up an attractive entry point for long term value oriented investors. We estimate the company to distribute DPS of RO 0.035/Share in 2018E, which should grow to RO 0.073/Share by 2022E. The stock is currently trading at FY19E P/E of 5.0x and EV/EBITDA of 4.3x, which we see as highly undervalued. We assign a STRONG BUY rating on the stock and recommend investors to BUY OTEL shares.

Stable performance and attractive strong FCF generation makes Ooredoo Oman an yield play; BUY with TP of RO 0.565/Share: Our positive stance on ORDS is derived from its unleveraged balance sheet, high growth profile of FBB segment and strong FCF generation capabilities. Even though the potential entry of third operator will be detrimental to the performance of both the existing players, we estimate ORDS will have a relatively lower damage as compared to OTEL. Additionally, we believe the new RAIO regime at the present form of cost plus basis would be advantageous to ORDS in expanding its service coverage and product offerings. We estimate significant cost advantages to the company from group procurement strategies result in lower capex and high FCF generation possibilities. This should lead to the company maintaining its payout ratio at close to 90%, resulting in high DPS and yield. Our blended DCF-Relative Valuation has resulted in 12M target price of RO 0.572/Share, offering 13% upside potential from current levels. The shares of ORDS are currently trading at FY19E P/E of 8.5x and offer 2018E dividend yield of 8.9%, which is the highest among all GCC telecom operators. We assign BUY rating on the stock and recommend it for income seeking investors.



Key Modelling Assumptions	
Core Forecasting Assumptions	We have modelled the financials of OTEL based on a 5% subscribers growth in fixed telephony for 2017-19E. Muted mobile subscriber growth during the period is assumed. Fixed line ARPU has been projected to fall at an average 5% for the forecast period. Fixed line internet ARPU is expected to fall 10% on pricing pressure on data. Mobile ARPU is expected to be flat for 2018 and fall by 2.5% for thereon. Zain revenue is estimated to grow by 1% CAGR between 2017 and 2022. We have modelled double digit CAGR for revenue from Enterprise data and wholesale segments, driven by ICT demand and acquisition synergies. We assumed that OTEL would be servicing lion's part of its finance cost annual dividend receipts from Zain, while it will try to divest investments and passive assets during the forecast period. We have assumed maximum payout levels of 50%, where DPS reaching RO 0.073 by 2022E from RO 0.035/Share in 2018E, aided by deleveraging and improvements in FCF generation.

BBB - Bull, Bear, Base case approach of valuation	
Bull case valuation @ RO 1.400	Revenue of OTEL to grow at a CAGR of 6.15% and that of Zain by 5.30% during FY17-22E, while net income growing by 19.2% and 10.6% for OTEL and Zain respectively.
Base case valuation @ RO 1.000	Revenue of OTEL to remain flat, while that of Zain growing by 1% between 2017 and 2022, while net income growing by 8.6% between 2017 and 2022 for OTEL and by 3.7% for Zain. Consolidated net income to grow at CAGR of 14.9% during FY18-22E
Bear case valuation @ RO 0.666	Revenue of OTEL to fall at a CAGR of 5.72% and that of Zain by 4% between 2017 and 2022, while net income falling by 5% between 2017 and 2022 for OTEL and by 8% for Zain. OTEL consolidated net profit to reach RO 72 million in 2022E, from RO 55 million in 2018E

Key Investment Positives

• The acquisition of Zain, though slightly overvalued, will provide OTEL with diversification benefits. It will also make OTEL the third largest Telcom player in the Middle East, providing them with scale of operations.

• The acquisition will provide OTEL with a pre-tax synergy benefit of USD80 million every year. Full synergy monetization is expected to be realized from 2020E

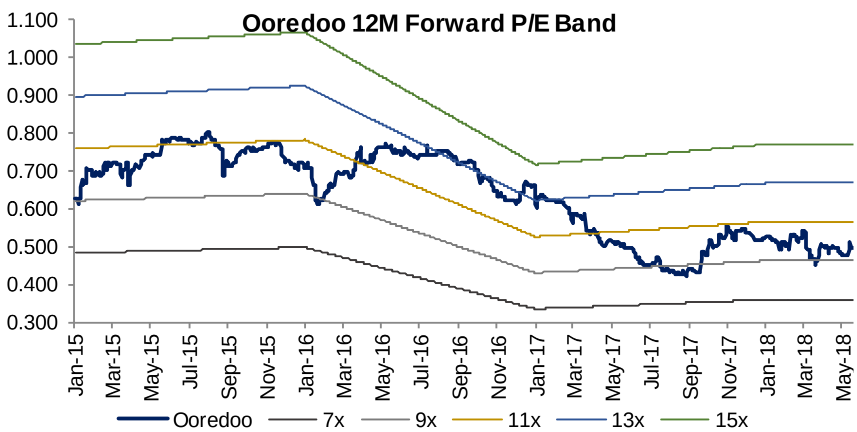
• With a high penetration rate, adverse regulatory changes and the potential entry of third player makes the Oman Telcom market stagnant and highly competitive.

• Post-acquisition, the leverage of OTEL is expected to increase to 2.6x debt to EBITDA for 2018, from being nearly debt free prior to this. However, leverage is manageable and comes at the back of benefits from increased diversification and increased scale.

• Dividend payments to come under pressure, as we expect dividend received from Zain to be less than the finance cost of the acquisition.

• OTEL is currently quoting at 5.0x its estimated 20189E EPS and 4.3x it 2019E EBITDA.

• Key risks include, potential third operator in Oman, further deterioration in Iraq and Sudan market of Zain and loss of OTEL market share in Oman due to changes in interconnection charges regulations.



Key Modelling Assumptions	
Core Forecasting Assumptions	We have modelled Oredoo based on a 15% subscribers growth in fixed telephony for 2018 and 2019 and 10% growth for 2020 and 5% growth thereafter. Mobile subscribers to grow at 5% for 2018 and 2019 and then fall at an average rate of between 1-2% thereon. Mobile ARPU to remain flat at 2017 levels for the forecast period. Fixed telephone ARPU to fall by 10% p.a. for the forecast period.

BBB - Bull, Bear, Base case approach of valuation	
Bull case valuation @ RO 0.711	Revenue to grow by 6% CAGR between 2017 and 2018, while net income is estimated to grow at a CAGR of 17%.
Base case valuation @ RO 0.572	Revenue to grow by 1% CAGR between 2017 and 2018, while net income is estimated to grow at a CAGR of 8%.
Bear case valuation @ RO 0.475	Revenue to fall by 4% CAGR between 2017 and 2018, while net income is estimated to fall at a CAGR of 2%.

Ooredoo Oman Valuation Snapshot			
Discounted Cash Flow	0.538	40%	0.215
EV/EBITDA	0.669	30%	0.201
P/E	0.520	30%	0.156
Blended DCF-RV Target Price		**100%**	**0.572**
CMP			0.506
Potential upside			**13%**

Key Investment Positives

• With a high penetration rate, adverse regulatory changes and the potential entry of third player makes the Oman Telcom market stagnant and highly competitive.

• Changes in regulations of interconnection charges could help Oredoo to gain market share in markets and segment untapped by the company currently.

• A relatively debt free balance sheet and consistent cash flow generation, the financial profile of Oredoo continues to be strong.

• Capex as a proportion of revenue has fallen from its historical average of 25% to 17% in 2017. Aided by group sourcing and the resultant benefit of scale, we expect capex spending going forward to remain at 2017 levels of 17% of revenue.

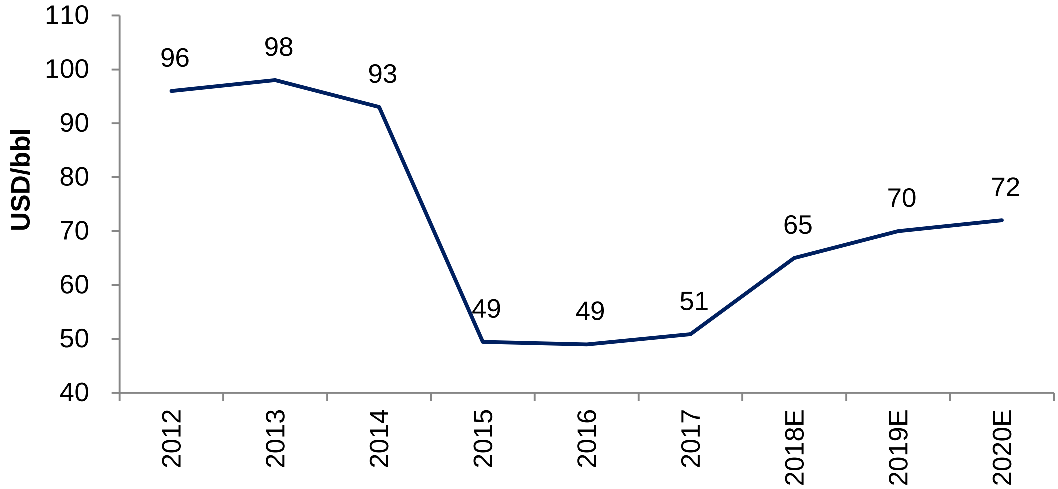
• Oredoo is quoting at 10.1x 2018E net income and a dividend yield of 9%. The high dividend yield of the company aids in relatively lower downside risk to the price of Oredoo.

• Risk to the recommendation include potential entry of third operator in Oman, nonimplementation of interconnection charges in the current form and failure in accrual of benefit of reduction in capex.

We estimate average oil price in the range of USD 65-72/bbl during FY2018-20E

Oil prices recovered in 2017, a trend that is expected to continue in the medium term: In 2017, WTI averaged USD 50.85/bbl. compared to USD 43.47/bbl in 2016, an increase of around 17% YoY. Going forward we expect this trend to continue, as we expect oil prices to average USD 65/bbl in 2018, USD 70/bbl in 2019 and USD 72/bbl for 2020.

Figure - 1 Trends in WTI – Average oil price estimates

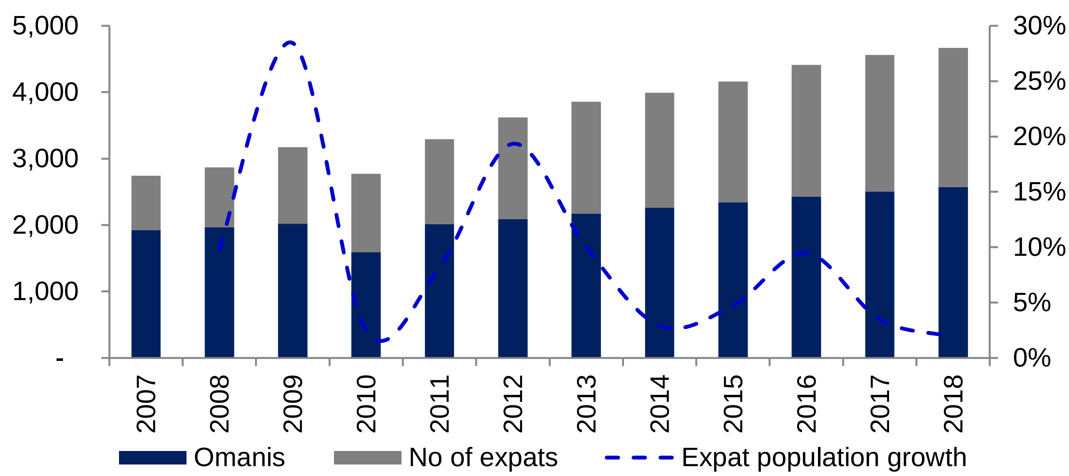


Source: Bloomberg, US Research

Oman population to grow steadily; expatriate population growth to decline as Omanization drive gathers further momentum

Oman population grows in a steady manner; expat population growth declines: Between 2013 and 2017 population growth in Oman averaged 4%, though the growth rates have slowed down in the past few years to 3% YoY in 2017. A significant contributor to this growth was the increase in expat population. We are seeing a marked decline in expat population growth during the past three years as a result of large outflow of highly educated expats leaving the country in search of better employment opportunities elsewhere. While the expat population grew at a CAGR of 13.3% during the 5 years ended 2013, the growth rate plummeted to 4.5% during the 5 years to 2018. It has to be noted that this increase comes despite the Omanization steps taken by the government. There seems to be no perceptible change in expat population thus far, which we perceive as positive for domestic telecom companies, as it does not have an impact on the subscriber base of the companies.

Figure - 2 Oman population increases at a steady rate

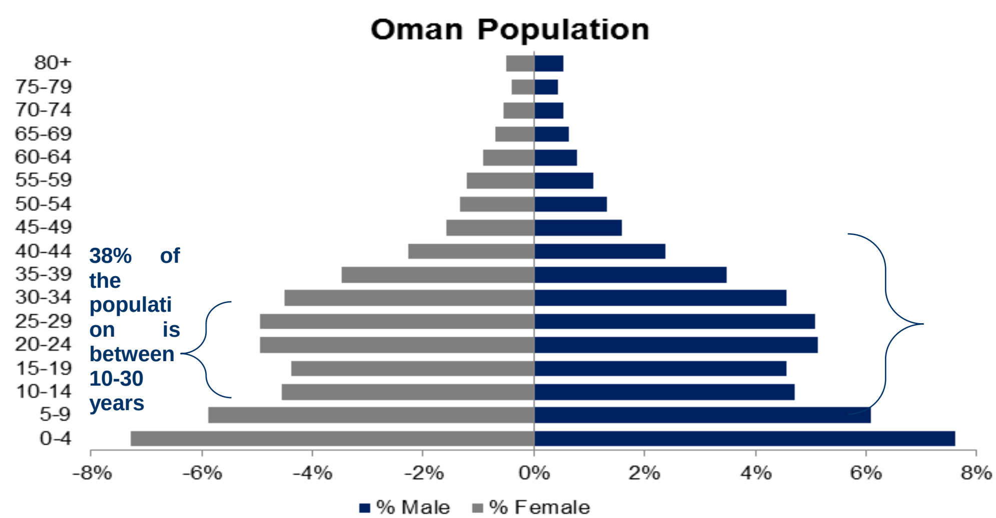


Source: NCSI, US Research

Oman's favourable demographics with a high proportion of population below the age of thirty years.

Favourable demographics for ARPU growth; but disposable income growth remain muted: The demographics of Oman has improved over the past five years, with the proportion of population below 30 years growing by 9% between 2013 and 2017, with its proportion to total population increasing to 67% in 2017 from 56% in 2013. The number of population above 40 years on the other hand fell by 4% between 2013 and 2017, as their proportion fell to 15% as of 2017 from 21% in 2013. We feel that this is a major positive for Telecom industry, given that the higher proportion of younger population means higher potential for earning growth and also higher proportion of customer base for the Telecom companies.

Figure - 3 Oman's demographics is conducive for long term growth of Telecom



Source: NCSI, US Research

New regulations on interconnection charges, will make it easy for new entrants

New access and interconnection regulations to put pressure on incumbents and lowers the entry barrier for new entrants: In 2016, the TRA of Oman passed a comprehensive regulation, mandating all Telecom companies operating in Oman to share their existing physical infrastructure and other facilities to requesting parties and wholesale customers on a cost-plus basis, compared to the current practice of charging a fee on a commercial basis. The regulation also differentiates between dominant and non-dominant service providers and imposes more restrictions on the dominant service providers. This regulation has been issued to increase competition and improve access, especially broadband access, in rural areas.

The regulator is also proposing to impose penalties, ranging from RO 10,000 to RO 100,000 for noncompliance under this regulation. In addition to this, a penalty of not less than RO 1,000 shall be imposed for each day the violation continues beyond the date on which penalty is imposed. In case of reoccurrence of the violation, the fine will be doubled.

OTEL has more to lose, given its market dominance; Oredoo will have a chance to capture market

The impact of the regulation will be that of increased competition among existing players and removal of a major entry barrier for a new entrant. OTEL, given its market dominance in fixed line segment, has strong Telecom infrastructure across the country, especially in the rural areas. Given this, it has a virtual monopoly in some of the areas it operates, especially in fixed telephony and broadband, since it is cost prohibitive for new entrants to set up fresh infrastructure. As of 2017, OTEL had a market share of c.65% in both fixed line subscribers and fixed line broadband.

If and once the new fee structures in its current form is confirmed, OTEL would have to share these networks to other operators at a cost substantially lower that the current price being charged for network sharing. This in turn is likely to result in increased competition and a resultant pressure on fixed line ARPUs. The regulation is also likely to make it easy for a potential third player, as it would limit cost restrictive investments in infrastructure, thereby removing a key entry barrier. However, it also has to be noted that this move may also limit further investments in infrastructure, as the incumbent has no incentive towards the same. Overall, we feel that this new regulation will be a major negative for OTEL, and revenue neutral to positive for ORDS.

OTEL appeals RAIO order passed by TRA. Oredoo on the other hand has filed its RAIOs, which is under consideration

In Jan 2018, OTEL has filed a review petition before the TRA, on the orders passed by the agency on RAIOs. TRA has accepted the review petition by OTEL and has temporarily suspended its order on RAIO, until the final hearing of the review. It has to be noted that ORDS has filed its final RAIOs with the TRA and the same is under consideration. We feel that the final decision taken by TRA to be unlikely to be materially different from its initial decision and the same is likely to continue to be a negative for OTEL.

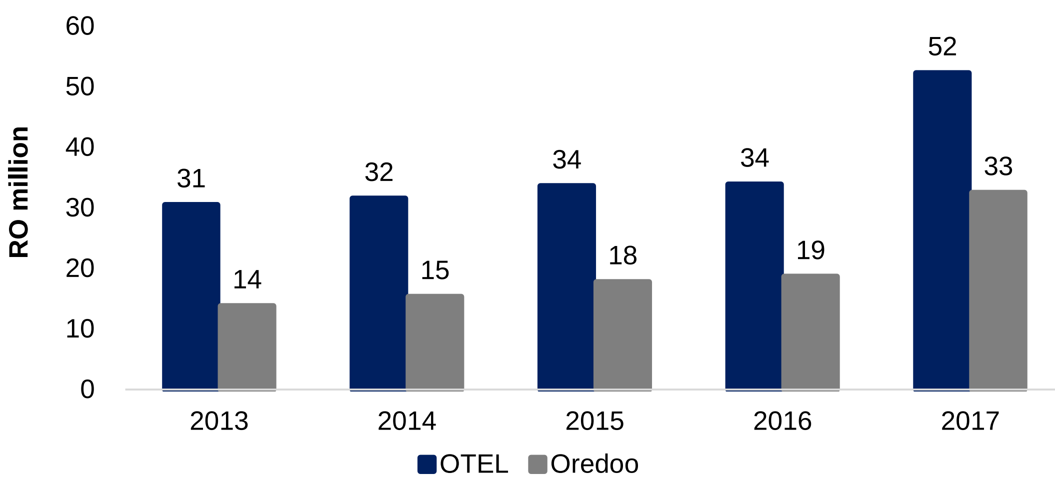
Monetizing assets could provide some respite to OTEL

One of the ways that OTEL could manage this risk is to monetise its infrastructure, which in turn could place it in par with the potential new comers. Despite this, at an operating level, this move is likely to be negative for OTEL, as it could likely cede market share to ORDS and resellers. It is a marginally positive for ORDS, as the company will be able to enlarge its customer base and start servicing clients across Oman. However, it also has to be noted that this optimism has to be tempered with the fact that this move is also likely to make it easy for new entrants in the market, which in turn would impact the market share and profitability of ORDS.

Royalty increased from 7% of revenue to 12% of revenue

Change in royalties to hit profitability and margins: In Dec-2016, royalty charges to be paid by the Telecom companies was increased from 7% of revenue to 12% of revenue, effective from Jan-2017. However there seems to be some doubt as to whether the increase applies to both mobile or only fixed line revenue. Currently both OTEL and ORDS are deducting royalty at the rate of 12% only for mobile calls, while for fixed line telephone, royalty is being provided at 7%. The higher rates for mobile in turn had resulted in a more than 50% YoY increase in OTEL's royalty for 2017, while the same for ORDS increased by close to 75% for the same period. We expect this increase, along with the increase in corporate tax to 15% from 12%, to continue to put pressure on the profitability of both ORDS and OTEL

Figure - 4 60% increase in total royalty expenses



Source: Company filings, US Research

Entry of third player will put further operating pressure on incumbents

TRA proposes to invite bidding for third operator. This will impact both OTEL and ORDS

In 2016, TRA had invited bidding for third mobile operator in Oman, with a view of introducing the same in 2017. However, the agency cancelled the bids and announced its intention of offering the same to a local company, owned by investment funds and a global partner. However, it is unclear, if and when, this bidding will happen.

The introduction of third player will have a negative impact on the financial and operating performance of both OTEL and ORDS. Among its peers, across companies within the region, OTEL and ORDS had one of the highest ROIC (calculated on EV).

We also see the road for the new entrant to be easier, even when compared to the entry of ORDS, given the changes in the interconnection regulations. As a result of these changes, a new entrant's capital investments are likely to be substantially lower.

If ORDS can capture fixed line voice and broadband market, this could alleviate some pain of third operator

Once the operations of the third player stabilise, after introduction, there could be a reduction of around 9% each in the market share of mobile subscribers for both OTEL and ORDS. At current ARPU levels, this could mean c.20% reduction in the revenue for both OTEL and ORDS. However, in terms of overall revenue, we feel that OTEL has more to lose, given its high market share in fixed line and broadband subscribers. ORDS, on the other hand could restrict the fall in revenue to a certain extent by gaining market share in fixed line and broadband subscribers.

It has to be noted that in Kuwait, which has population levels close to Oman and is served by three operators, Zain (market share of 37%, Ooredoo (market share of 31%) and Viva (market share of 32%), the average blended ARPU was USD24, close to Oman's ARPU of USD23.5. Also, we feel that the ARPU levels in Oman is lower than its peers in the region, given this, there may not be substantial fall in the ARPU from the current levels due to the fresh entrant. However, the secular fall that has been witnessed in the past years is likely to continue.

Source of revenue	2017A		Post third operator entry		
	OTEL	**Ooredoo**	**3rd party**	**OTEL**	**Oredoo**
Mobile revenue (RO mn)	290	231	181	181	181
subscribers (mn)	3.99	2.95	2.31	2.31	2.31
market share (incl resellers)	57.5%	42.5%	33.3%	33.3%	33.3%
ARPU (RO)	6.06	6.52	6.52	6.52	6.52
Fixed line revenue (RO mn)	131	42	66	66	66
subscribers (,000)	329	118	165.91	165.91	165.91
market share	66.1%	23.6%	33.3%	33.3%	33.3%
ARPU (RO)	33.26	30.01	33.26	33.26	33.26
Total revenue (RO mn)	528	274		353	247
% reduction				*-33%*	*-10%*

Source: Company reports, US Research

We have conducted a sensitivity on change in revenue to a fall in the market share of both mobile and fixed line for both OTEL and ORDS. We feel that OTEL has the most to lose, in case of the entry of new player, with the new interconnection norms. We estimate a fall in total revenue of close to 33% from the levels of 2017, assuming the same ARPU, in case of OTEL's mobile and fixed line market share falling to around 33% from their current levels. However, ORDS's fall in revenue could be restricted to c.10%, if they are able to improve their market share in the fixed line telephone market.

Sensitivity of OTEL and Oredoo revenue to changes in market share of fixed telephony (voice and broadband)

OTEL market share in fixed	66.1%	61.1%	56.1%	51.1%	46.1%	41.1%	33.3%
ORDS market share	16.9%	19.4%	21.9%	24.4%	26.9%	29.4%	33.3%
New Entrant	16.9%	19.4%	21.9%	24.4%	26.9%	29.4%	33.3%
OTEL revenue (RO mn)	131	121	111	102	92	82	66
Total revenue (RO mn)	528	408	399	389	379	369	353
% Change		*-22.6%*	*-24.4%*	*-26.3%*	*-28.2%*	*-30.1%*	*-33.0%*
ORDS revenue (RO mn)	34	39	44	49	54	58	66
Total revenue (RO mn)	274	220	225	230	235	240	247
% Change		*-19.6%*	*-17.8%*	*-16.0%*	*-14.2%*	*-12.4%*	*-9.6%*

Source: Company reports, US Research

Formation of OTC, both a threat and opportunity

Value unlocking through separate tower company: In Jan-2018, an agreement was signed to establish Oman Tower Company (OTC) to build standardized telecommunications infrastructure to be utilised by all licensed operators in Oman. Oman 70 Holding Company will have 56% stake in OTC, while ActivCo, which enjoys global experience specialised in the management, operation and maintenance of telecommunication towers, will own 34% stake, with the balance 10% being held by Oman Broadband Company, which will be representing the government. In the first phase, OTC will invest RO 15 million towards building new towers, to expand the existing telecom infrastructure of the country. In the second stage the company is planning to reach an agreement with the existing operators to manage their portfolio of assets.

We feel that this is both a threat and opportunity to the existing operators, especially OTEL. The establishment of this company could result in the breaking of near monopoly enjoyed by OTEL in certain areas in the country, thereby providing access to other players. Again, this move will benefit new entrants, given that the company can enter into agreement with tower companies, instead of investing in own infrastructure, that could be cost prohibitive in a market like Oman.

OTC could help both Oredoo and OTEL to monetize its tower assets

However, we also see this is as a positive for OTEL, which could use this opportunity to sell its tower portfolio, thereby generating cash flows for debt repayment and making the company more asset light. The prospects for the telecom industry in Oman are competitive, with limited opportunity to grow. With high penetration and slow population growth, added to the potential reduction in expat population are already putting pressure on the financials of the incumbents. Added to this, higher royalty and tax rates and the potential entry of new player in the industry, is likely to make the environment even tougher. Given this, any move by the company to unlock value will aid the company to utilize the funds for either reduction of existing debt or to make potential investments to diversify its exposure.

Overall the number of towers in Oman is pegged at c.4,000, of which OTEL is estimated to own c.2,500 and Oredoo at c.1,500. Based on the analysis of past transactions, the average realization per tower can be between USD 100K to 150K, or a potential value of around RO 200 million, with RO 125 million for OTEL and RO 75 million for Ooredoo. We note that these are average numbers and the actual realization may vary substantially from these and will vary based on the technical specifications of each of these towers.

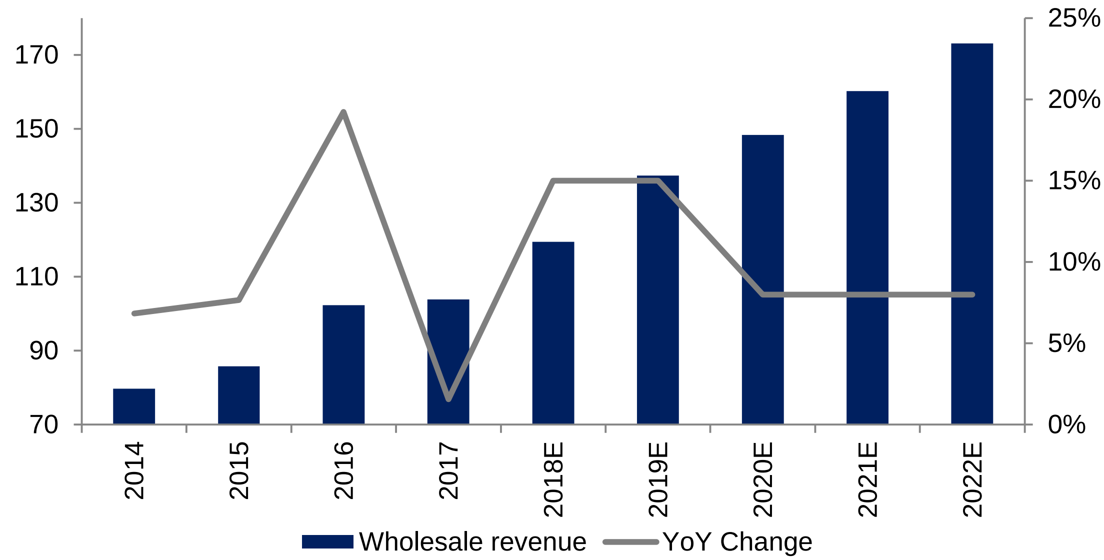
Wholesale revenue to witness consistent growth

Growth in wholesale revenue support total revenue of OTEL: OTEL's wholesale service includes income from mobile services, income from access services provided to local and international operators, income from interconnection services and revenue from carrier services. OTEL has an integral advantage in this segment given its locational advantage and extensive infrastructure across the country. This in turn aids the company to act as gateway for international players to Oman and the MENA region. With 12 cable landing stations in Oman, four terrestrial networks and access to 20 submarine cable systems, OTEL aims to become a regional hub between Asia, Africa and Europe.

OTEL has entered into various agreements with international service providers and carriers to provide dedicated capacity. These agreements in turn aid in stable revenue growth from this segment. The domestic revenue from this segment is primarily through revenue from resellers. Apart from this, the revenue sources also include interconnection charges, connectivity, national roaming charges, etc. currently, OTEL services two resellers, Renna and FRIENDi.

Between 2013 and 2017, wholesale revenue of OTEL increased at a CAGR of 9%, with its proportion to total revenue increasing from c.16.5% in 2013 to c.20% in 2017. We expect the company to maintain this growth trajectory going forward, as revenue from this segment is considered to be stable, with high visibility. We estimate OTEL's wholesale revenue to grow by 10.7% during FY17-22E, contributed by Zain call aggregation revenue and increase capacity and IRU sales.

Figure - 5 OTEL wholesale revenue show a consistent increase



Source: Company reports, US Research

Zain acquisition to aid in pooling of technology and clientele, aiding in revenue growth

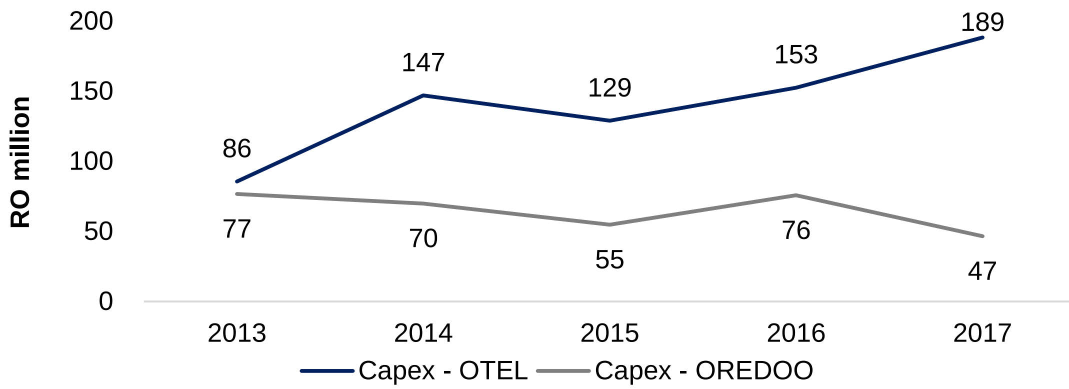
OTEL management sees substantial opportunity for growth on wholesale revenue through its partnership with Zain. OTEL is looking to leverage its existing capacity and capabilities and provide service across Zain's extensive network. To achieve this, OTEL is looking to tap into both Zain's infrastructure and customer base. Through this OTEL aims to improve the quality of services being provided and also aid in lower cost.

Steady capex spending by Omani telecos in the past; we estimate capex spending of ORDS to decline on efficiency gains: Capex outlay of both OTEL and Oredoo grew by a CAGR of 10% between 2013 and 2017, mainly due to a 22% CAGR increase in capex spending of OTEL during the same period. Capex spending of ORDS, on the other hand, fell by 12% per annum. Capex outlay mainly pertained to improvement in the telecom

Capex outlay of ORDS to fall as a result of efficiency gains from Group level sourcing of equipment

infrastructure. Capex to revenue of OTEL averaged c.26% during 2013 to 2017, while the same for ORDS has fallen from c.38% in 2013 to c.17% in 2017. The main reason for the fall in capex of ORDS was the full roll out of its WiMax network, and efficiency gains from group sourcing with the parent company, Ooredoo Qatar. We expect potential savings in the similar lines for OTEL once its integration with Zain is complete. It has to be noted that a 1% fall in capex to revenue, will result in an average 4% reduction in capex (2017 as base).

Figure - 6 OTEL capex spending continue to raise, even as ORDS's fell in 2017

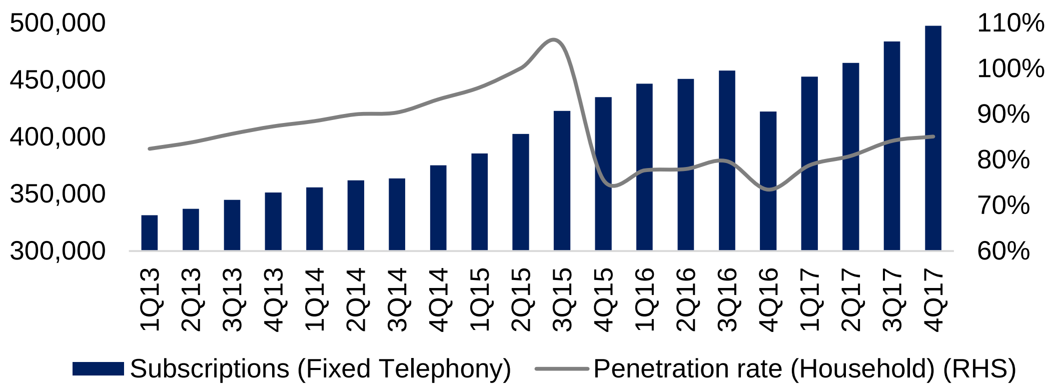


Source: Company reports, US Research

Fixed telephony grows at a steady rate

Steady subscriber's growth in fixed line telephony: Between 2013 and 2017, fixed line subscribers grew at a CAGR of 9% from 351,411 as of Dec-13 to 497,716 as of Dec-17. OTEL was the market leader in this segment with a market share of c.66% and grew at CAGR of 6%. High base and high market share was the main reason for the relatively low growth, vis-à-vis the market. Ooredoo on the other hand grew at a higher rate of 16% between 2013 and 2017. Lower base was the main reason for this.

Figure - 7 Steady growth in fixed line subscribers

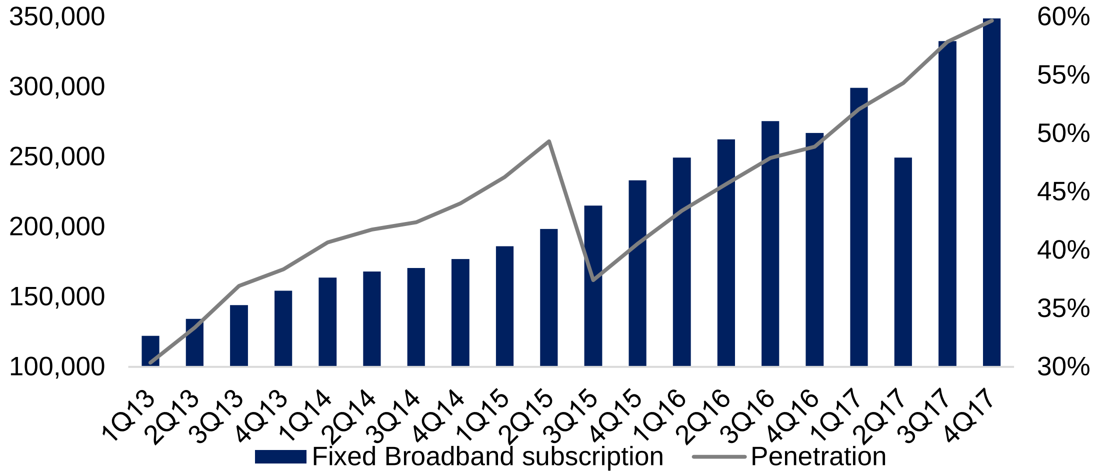


Source: TRA, NCSI, US Research

ORDS registers higher growth in fixed line telephony aided by lower base

Fixed line penetration per household was high 85% as of Dec-17, slightly lower than 87% in 2013. Given the high penetration, we do not expect substantial upside from the current growth rates in fixed line. Going forward, we expect subscriber's growth to average close to 6%, in line with historical average. While we expect ORDS to continue to grow at double digits, we expect the market share of the company to trail OTEL due to superior infrastructure facility in possession with OTEL, due to its first mover advantage. However, if the proposed interconnection sharing law goes through, we expect the same to be a major boost for ORDS. This would entail ORDS to offer fixed line services to a wider range of customers, using the network of OTEL, at a relatively lower cost.

Figure - 8 Steady growth in FBB and its penetration levels.



Source: TRA, NCSI, US Research

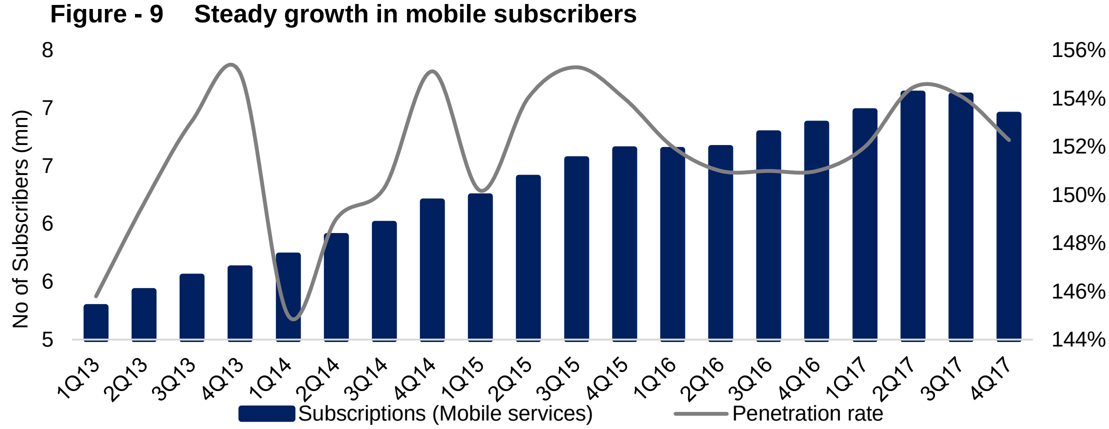
Fixed line telephony continues to offer strong growth

Fixed line broadband, consistently strong growth: Fixed line broadband grew at a CAGR of 23% to 348,926 as of FY17, compared to 154,290 as of FY14. Again, OTEL was the market leader in this segment, with a market share of 65% and grew at a CAGR of 24%, for the same period. Average penetration of fixed broadband in Oman was 60% per household and 8% in terms of total population. This in turn offers strong growth prospect for future growth. Given this we expect fixed broadband connections to grow at double digit growth for the next three to five years. Similar to growth in fixed line telephone, an opening up of interconnection in this segment could offer strong potential growth of Ooredoo, while eroding the potential growth rates and market share of OTEL.

Mobile telephony grows at a stable growth, despite high penetration.

Mobile phone subscribers registered a CAGR of 5% between 2013 and 2017 to 6.9 million. OTEL subscribers grew at 5% between 2013 and 2017, at a rate in line with the industry growth. ORDS on the other hand registered a slightly higher than industry growth of 6% for the same period. Both OTEL and ORDS had nearly equal market share of 42.2% and 42.5%, respectively, as of Dec-17. Resellers on the other hand cornered a market share of the balance 15.2%. Currently the entire resellers operate under OTEL. Mobile penetration rate to 152.3% as of Dec-17 and was one of the highest in the region. Given this, we expect mobile subscribers to grow at around 2.5-5% for the next three to five years. We expect the competitive industry landscape in Oman in the mobile segment to continue, especially if/when the regulator decides to introduce the third mobile operator.

Figure - 9 Steady growth in mobile subscribers

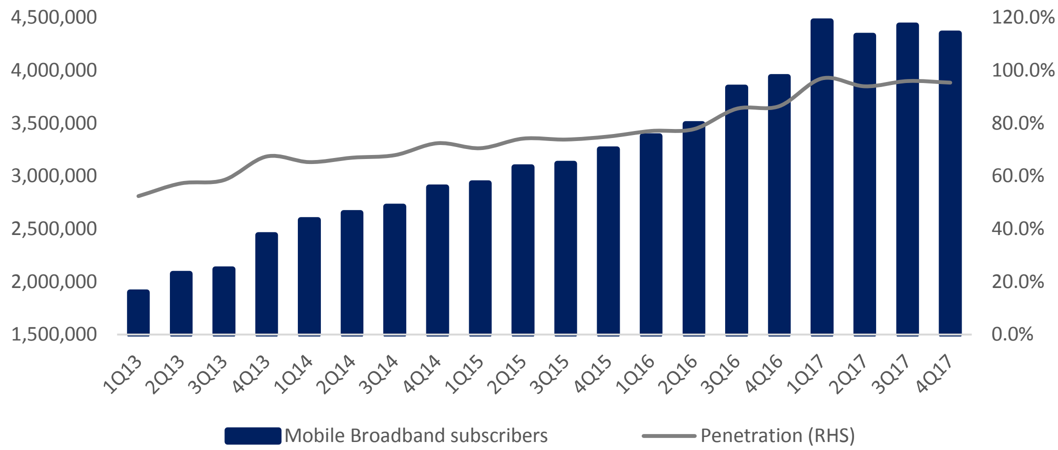


Source: TRA, Company reports, US Research

Mobile data growth continues to offer growth opportunity

Mobile data registers strong growth: Mobile broadband subscribers grew by 20% between 2013 and 2017 to 18 million subscribers as of Dec-17 from 9 million subscribers as of Dec-13. Penetration on the other hand increased to 95.4% per inhabitants as of Dec-17 from 67.4% as of Dec-13. Despite the high penetration, we expect the growth to continue, though the same is likely to be lower than historical average. It has to be noted that growth rates had fallen to 10.5% YoY as of Dec-17. We expect his to be a more representative of the expected growth rate in the medium term.

Figure - 10 Steady growth in mobile subscribers

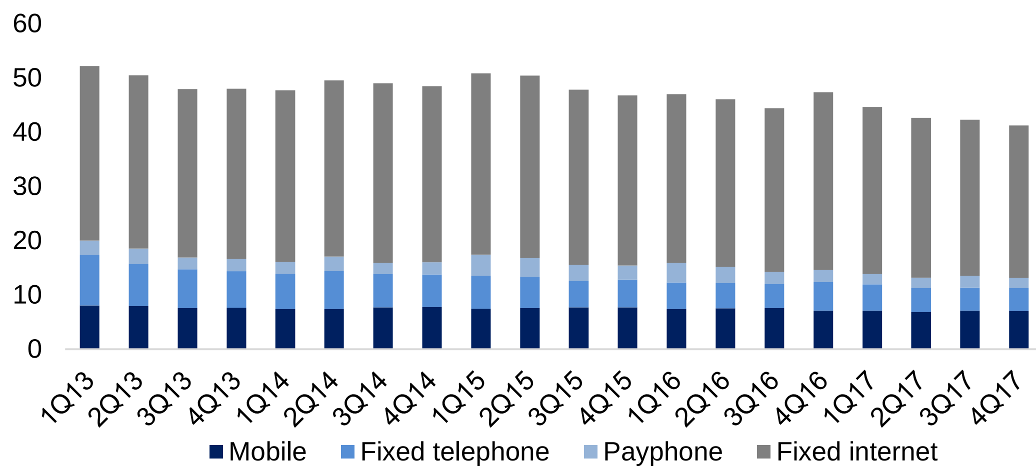


Source: TRA, Company reports, US Research

ARPUs across segment comes under pressure

ARPU's across the board comes under pressure: Given the highly competitive industry scenario, ARPUS across the segment has come under pressure, ARPUs of fixed telephony fell the most, -11% CAGR between 2013 and 2017. Payphone's ARPU on the other hand fell by 5% for the same period, while fixed internet fell by 3%. Surprisingly, despite the heavy competition, the ARPU of mobile fell by a much lower 2% CAGR between 2013 and 2017. Given the heavy competition in the industry, we expect this trend to continue. However, it has to be noted that Oman has one of the lowest ARPU's in the region and given this, further fall in ARPU could be limited. We feel that even in the event of the entry of a third operator, there could be limited opportunity to start a price war, given the existing ARPU's in the industry, without substantially eroding the ROI.

Figure - 11 Telecom sector ARPU Trends

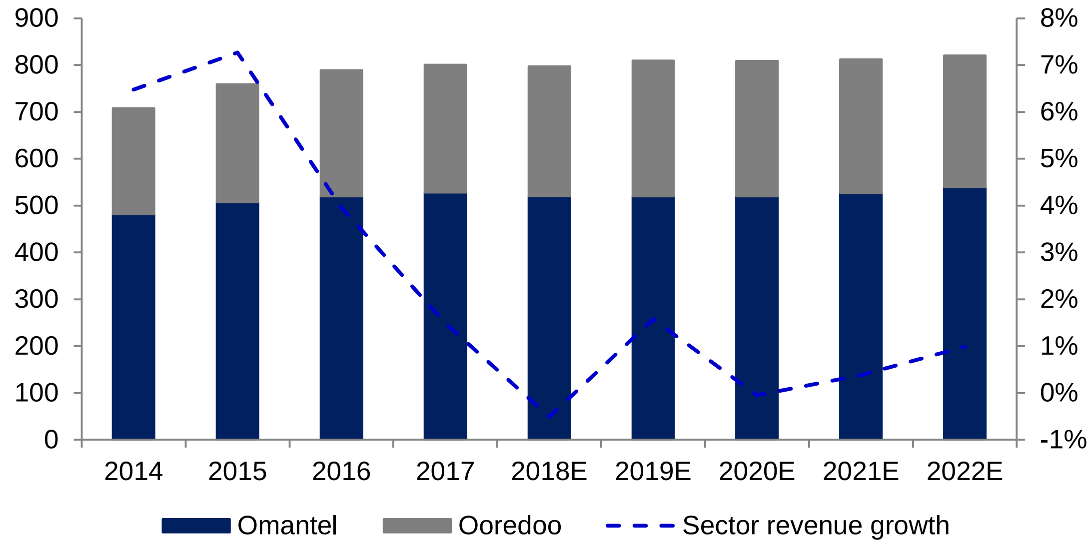


Source: TRA, Company reports, US Research

Moderate revenue growth aided by subscriber additions. Declining ARPU was the limiting factor

Revenue growth moderate: OTEL revenue grew at a CAGR of 4% between 2013 and 2017 and was aided by a 12% and 9% growth in fixed line broadband and wholesale revenue for the same period. Mobile revenue on the other hand grew by 1% CAGR between 2013 and 2017, though fixed line revenue fell by 12% CAGR for the same period. Fixed telephony broadband revenue increase was aided by a 24% CAGR between 2013 and 2017 in subscribers, which more than made up for a consistent fall in ARPU (10% fall for the same period). Mobile revenue increase was aided by a 5% CAGR in subscribers between 2013 and 2017, which made up for a 4% CAGR fall in ARPU during the same period. Fixed line telephony revenue on the other hand was impacted by a 11% CAGR fall in ARPU's. While subscriber's growth averaged 6% for the same period, the same was not sufficient to support revenue.

Figure - 12 Oman telecom sector revenue trends



Source: TRA, Company reports, US Research

Ooredoo reports growth better than OTEL aided by lower base

Ooredoo revenue between 2013 and 2017, registered an 8% CAGR and was aided by a substantial 17% CAGR in fixed telephony revenue for the same period. Revenue from mobile telephony on the other hand grew by 7% CAGR between 2013 and 2017. Mobile subscribers between 2013 and 2017 registered a CAGR of 6%, while ARPU was flat for the period. Going forward, we expect revenue of OTEL and Ooredoo to come under pressure. While we expect wholesale revenue to support revenue growth of OTEL, a more liberal interconnection regime is likely to affect OTEL more than Ooredoo. In fact, we expect this move to benefit Ooredoo, though the entry of third operator is likely to put pressure on the revenue of both the companies.

Higher royalty impacts profitability growth

Operating expenses and EBITDA growth impacted by increase in royalty: OTEL's cash operating expenses, at the standalone level, grew by a CAGR of 7% between 2013 and 2017. One of the main reason for the higher cash operating expenses was the more than 50% increase in royalty, due to increase in the royalty charged by the government of Oman from 7% (prior to 2017) to 12% in 2017. Depreciation on the other hand increased at a CAGR of 12% between 2013 and 2017. Despite pressure on revenue, capex outlay of OTEL has been steady and averaged close to OMR 140 million, between 2014 and 2017. Most of the capex was towards improvement of existing infrastructure to upgrade for latest technology. Going forward, we expect growth in operating expense of OTEL to come down, aided by benefits of synergy derived from the company's acquisition of Zain. Most of these are expected to come from lower sourcing cost. Apart from cash operating cost, we also see a potential in the reduction in capex cost of OTEL, aided by the larger scale of OTEL post acquisition. OTEL management has projected for pre-tax synergy benefits of USD80 million p.a. We expect the same to start accruing from 2019, 70-75%, with close to 100% of the same from 2020 onwards.

Ooredoo depreciation to come down aided by savings in capex

Cash operating expenses of Ooredoo grew at a CAGR of 8% between 2013 and 2017, which was in line with growth in cash operating expenses of OTEL. In 2017, royalty cost of Ooredoo increased by 74% Y0Y, mainly due to higher royalty charges. Depreciation on the other hand registered by 14% CAGR and was mainly due to consistent capex growth. It has to be noted that the capex requirement, at least in the initial period, of Ooredoo was higher than OTEL, though the same has been coming down since 2015 and has bottomed in 2017. The main reason for the lower capex was the benefit accrued by the unified sourcing of group, aiding in advantage of scale. Given this, we expect depreciation charges of Ooredoo to come down, despite consistent investment in capex in the medium term.

EBITDA of OTEL between 2013 and 2017 has been flat, varying between RO 205 million to RO 230 million. EBITDA margins on the other hand has been consistently coming down from 45.4% in 2013 to 39.2% in 2017. EBITDA margins of Ooredoo on the other hand moved in a similar fashion, though EBITDA in terms of value increased by an 8% CAGR between 2013 and 2017. Higher growth in revenue, compared to OTEL, due to consistent growth in fixed telephony at the back of lower base and higher growth in mobile telephony, was the main reason for higher EBITDA growth. Going forward, we expect EBITDA of both OTEL and Ooredoo to come under pressure, while we expect synergy benefits to aid EBITDA of OTEL, increasing competition due to a more open interconnection and entry of third operator is likely to cast more pressure on OTEL than Ooredoo.

Increase in finance cost of OTEL, due to Zain acquisition puts further pressure on the company's profitability

Historically both OTEL and Ooredoo have been debt light, with most of the finance cost coming from short term working capital requirement. However, with the acquisition, debt of OTEL increased from RO 8 million in 2016 to RO 2 billion by 2017, resulting in finance cost increasing to RO 11 million at a standalone level and RO 20 million at the consolidated level. Overall net income (excluding minority interest) of OTEL fell by more than 30% and was impacted mainly due to increase in operating cost, driven by higher royalty, and higher finance cost. Net income of Ooredoo too fell by more than 30% and was impacted mainly by higher operating cost, due to higher royalty.

Zain's acquisition puts pressure on leverage

Gearing of OTEL increased due to Zain acquisition: Borrowings of OTEL (standalone) increased to 867 million as of 2017, compared to net cash position as of 2016. The increase in debt was entirely attributed to the acquisition of Zain. Consolidated debt levels on the other hand increased to OMR1.97 billion, mainly due to acquisition debt of OTEL and the debt of Zain. Debt to EBITDA increased to 6.8x as of 2017, at the consolidated level, though we feel that this is not a true representation of the company's leverage, given that less than two months of financial performance of Zain was consolidated. Debt to EBITDA at the standalone level on the other hand at 4.2x, was more representative of the company's leverage as of 2017. We expect the leverage to fall steadily, with the consolidated leverage falling to 2.6x for 2018, when full consolidation happens. At the standalone level, we expect the leverage to fall more gradually, to 3.8x for 2018 and 3.3x for 2019 and to below 3.0x post 2020.

In terms of revenue OTEL and Ooredoo one of the smallest

Peer Group Analysis: In terms of revenue and overall size, both OTEL and Ooredoo were the smallest. Etisalat and Saudi Telecom were the biggest companies in the region. In terms of profitability (EBITDA margins), OTEL and Ooredoo were in line with the peer average. EBIT margins of Ooredoo was however, substantially lower than both its peers and OTEL. Higher than proportionate depreciation charges were the main reason for the same. Net margin of Ooredoo on the other hand was more in line with both industry average and OTEL. While net income margins of OTEL was weighed in by borrowings to finance Zain. Among the peers, Saudi Telecom had the highest profitability (net income), followed by Etisalat and Zain Kuwait.

Name	Country	CMP (USD)	Market Cap (USD mn)	EV USD (mn)	Revenue (USD mn)	EBITDA (USD mn)	EBIT (USD mn)	Net income (USD mn)	Net debt (USD mn)
Omantel	Oman	1.9	1,410	7,506	4,949	1,821	1,023	166	4,117
Ooredoo Oman	Oman	1.3	856	936	731	284	106	87	-26
Etisalat	UAE	4.3	37,647	41,010	14,438	7,106	4,050	2,486	-528
Du	UAE	1.3	5,974	5,162	3,612	1,503	1,050	494	-642
Batelco	Bahrain	0.6	1,048	1,349	1,006	331	155	9	211
Saudi Telecom	Saudi Arabia	23.0	46,096	42,735	13,633	5,226	3,034	2,763	-4,028
Mobily	Saudi Arabia	5.3	4,112	7,360	3,045	1,041	99	-113	3,246
Zain KSA	Saudi Arabia	1.8	1,035	3,596	1,954	677	239	21	4,368
Vodafone Qatar	Qatar	2.3	1,975	2,140	543	157	-58	-58	163
Ooredoo Qatar	Qatar	18.4	5,909	13,854	9,346	3,813	1,613	732	6,164
Ooredoo Kuwait	Kuwait	2.9	1,449	1,909	2,301	794	326	150	24
Zain Kuwait	Kuwait	1.3	5,452	7,968	3,525	1,388	780	536	43
VIVA Kuwait	Kuwait	2.3	1,171	1,050	913	232	132	126	-77

Source: Bloomberg Professional®, US Research

OTEL and Ooredoo have one of the best return on M-Cap.

Return on Market cap of OTEL was, at 5%, in line with the peer average. However, post consolidation of Zain, we expect OTEL's return on Market cap to increase to close to 7%. The return on Market Cap at 10% of Ooredoo was substantially higher than the industry average. Overall, both OTEL and Ooredoo had one of the highest return on Market cap among its peers, which indicates under valuation of the stocks

Name	Country	CMP (USD)	EV/ EBITDA	EV/EBIT	P/E	Net debt/ EBITDA	EBITDA margin	EBIT margin	Net margin	Net income/ Mcap
Omantel	Oman	1.9	4.1	7.3	8.5	2.3	37%	21%	3%	12%
Ooredoo Oman	Oman	1.3	3.3	8.8	9.9	-0.1	39%	15%	12%	10%
Etisalat	UAE	4.3	5.8	10.1	15.1	-0.1	49%	28%	17%	7%
Du	UAE	1.3	3.4	4.9	12.1	-0.4	42%	29%	14%	8%
Batelco	Bahrain	0.6	4.1	8.7	113.2	0.6	33%	15%	1%	1%
Saudi Telecom	Saudi Arabia	23.0	8.2	14.1	16.7	-0.8	38%	22%	20%	6%
Mobily	Saudi Arabia	5.3	7.1	74.5	NM	3.1	34%	3%	-4%	-3%
Zain KSA	Saudi Arabia	1.8	5.3	15.0	50.2	6.5	35%	12%	1%	2%
Vodafone Qatar	Qatar	2.3	13.6	NM	NM	1.0	29%	-11%	-11%	-3%
Ooredoo Qatar	Qatar	18.4	3.6	8.6	8.1	1.6	41%	17%	8%	12%
Ooredoo Kuwait	Kuwait	2.9	2.4	5.9	9.7	0.0	34%	14%	7%	10%
Zain Kuwait	Kuwait	1.3	5.7	10.2	10.2	0.0	39%	22%	15%	10%
VIVA Kuwait	Kuwait	2.3	4.5	7.9	9.3	-0.3	25%	14%	14%	11%

Ooredoo has one of the lowest leverage among its peers. OTEL leverage increase was due to acquisition

In terms of leverage, the average leverage of peers at 0.5x (net debt to EBTIDA), reflecting the relatively mature market in the region. OTEL, however, had a above leverage of 5.5x. However, it has to be noted that the leverage is not reflective of the true leverage, due to EBITDA reflecting only around two months of profitability of Zain. Net debt to EBITDA as of 2018E at 2.0x we feel is a better indicator of OTEL's leverage, though the same is still higher than peer average.

In terms of valuations, Ooredoo' was one of the cheapest among its peers, across parameters. OTEL on the other hand had a higher than average valuations, across parameters. However, as mentioned earlier, the financial statements consist of only c.2 months of financial performance of Zain. Including Zain's performance, 2018E P/E at 7.9x and EV/EBITDA of 4.3x, was closer to OTEL's true valuations, though it continues to be richer than Ooredoo in terms of EV/EBITDA.

INVESTMENT RESEARCH | OMAN

Telecom

Omantel – Offers deep value

BUY: TP @ RO 1.000

Valuation Summary (TTM)			
Price (OM)			0.724
PER (x)			7.7
P/Book (x)			1.1
P/Sales (x)			0.5
EV/Sales (x)			2.8
EV/EBITDA (x)			7.8
Dividend Yield (%)			6.9
Free Float (%)			39%
Shares O/S (mn)			750
YTD Return (%)			-40%
Beta			1.6
(mn)		**OMR**	**USD**
Market Cap		543	1,410
EV		2,890	7,506
Price performance (%)	**1M**	**3M**	**12M**
OTEL	-15	-33%	-42%
MSM 30 Index	-4%	-8%	-16%
Services Index	-3%	-6%	-11%
Trading liquidity (,000)	**1M**	**3M**	**6M**
Avg daily turnover (RO ,000)	0.24	0.42	0.25
Avg Daily Volume (,000)	270	325	198
52 week	**High**	**Low**	**CTL***
Price (RO)	1.410	0.720	0.56
* CTL is % change in CMP to 52wk low			
Major shareholders			
United Telecom Investments			51.0%
SGRF			6.0%
PASI			4.4%
Others			38.6%
Other details			
Exchange			MSM
Sector			Telecom
Index weight (%)			6.8
Key ratios	**2017**	**2018E**	**2019E**
EPS (RO)	0.106	0.092	0.144
BVPS (RO)	0.757	0.802	0.892
DPS (RO)	0.050	0.035	0.052
Payout ratio (%)	47	38	36
Valuation	**2017**	**2018E**	**2019E**
P/E Ratio (x)	6.8	7.9	5.0
Price/Book (x)	1.0	0.9	0.8
Dividend Yield	6.9%	4.8%	7.2%

OTEL has a strong financial profile, leading market position in the domestic telecom market and has recently achieved a diversified market position across Middle East through Zain acquisition. The company is constrained by an already competitive market in Oman, the potential entry of a third operator and adverse regulatory reforms, which are likely to pose challenges to its financial position and margins. However, we expect OTEL's acquisition of Zain, though slightly overpaid, to add value in the long run. Zain's operations in Iraq and Sudan, which has thus far been weighing on its performance, is showing signs of recovery, which could provide further upside. Apart from this, OTEL has estimated cash synergy of RO 30 million to accrue annually. We expect to see the full benefits of synergy to accrue from 2020E. We have valued the company using a blended DCF-Relative Valuation technique and arrived at 12M target price of RO 1.000/Share, which is 38% higher than the current price. We believe that the recent selloff in the stock has opened up an attractive entry point for long term value oriented investors. We estimate the company to distribute DPS of RO 0.035/Share in 2018E, which should grow to RO 0.073/Share by 2022E. The stock is currently trading at FY19E P/E of 5.0x and EV/EBITDA of 4.3x, which we see as highly undervalued. We assign a STRONG BUY rating on the stock and recommend investors to BUY OTEL shares.

Challenging market conditions in Oman: With a penetration rate in excess of 150% in the mobile telephony, one of the highest globally and in the region, and a stagnant fixed telephony, Oman telecom market is highly competitive, with ARPU's across services coming under pressure in the past five years. While we expect revenue from broadband to continue to grow, regulatory changes, in interconnection charges, and the potential entry of third operator in Oman, could result in erosion of OTEL's market share.

Zain acquisition to provide diversification benefits: The acquisition of Zain provides OTEL diversification to a wider market in the Middle East. Apart from this, the acquisition is also expected to provide synergies to the extent of USD80 million, prior tax annually, as guided by the management. Also, post integration, OTEL will be able to pool the combined infrastructure and clientele, thereby providing growth opportunities in wholesale revenue.

Financial pressure to continue in the medium term: Post-acquisition of Zain, OTEL's leverage has increased from its historically insignificant levels to a debt to equity of 123% for 2017 and a debt to EBITDA of 2.6x for 2018E. Though we feel that this level of leverage in manageable, dividend payment by OTEL is likely to come under pressure in the medium term, due to finance cost and repayment of term loan. While dividend receipt from Zain and synergy benefits could aid in managing this to a certain extent, we expect reduced dividend payments till 2022. However, any reduction in capex, through joint sourcing, will aid the company to restore its dividend payments to historical levels at a faster rate.

Risks

- Third operator entry, resulting in higher than expected deterioration in market share
- Further deterioration in Iraq and Sudan markets (Zain)
- Slower than expected integration resulting in synergy benefits accruing later than 2019
- Deterioration in fixed line and fixed broad band market share of OTEL due to changes in regulations

Despite the overvaluation, the acquisition to benefit OTEL in the long run

Omantel overpaid for acquiring Zain stake; market overreacted, and that creates long term value opportunity: Our calculations suggest Omantel paid RO 253 million as control premium for Zain acquisition, which is 56% higher than the 6 months average price of Zain prior to the deal announcement. We believed this was too high a premium paid for Zain, which has significant exposure to high risk geographies such as Iraq and Sudan. The acquisition will make OTEL the third largest player in Middle East and also offer diversification opportunities to OTEL. Given the stagnant nature of the Oman Telcom market, the potential entry of the third operator and potential threat of changes in interconnection charges, the acquisition provides OTEL with channels to diversify its exposures and channelize its investments in a better way. Added to this, the recovery of Iraq and Sudan market will provide upside to Zain's valuation. Overall, despite the slightly overvalued nature of the acquisition, we feel that Zain is likely to provide long term benefits to OTEL.

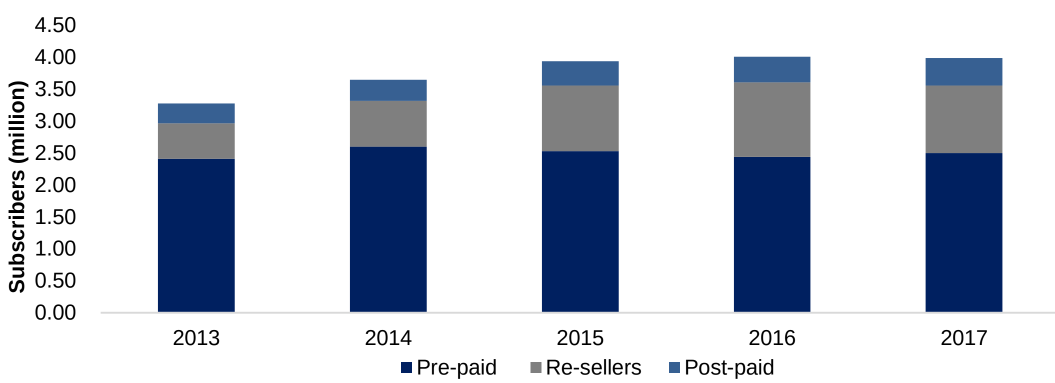
Recovery of Iraq, Sudan and Saudi market of Zain could provide upside to OTEL's acquisition

The shareholders are wary of the over-payment for Zain and the regulatory challenges in the domestic market in the form of potential third operator license in an over penetrated market, and the implantation of new RAIO of OTEL on the cost plus basis. The stock is down 40% YTD and 35% following the Zain deal and TRA announcements. We feel the shareholders are completely ignoring the growth opportunities that come along with Zain acquisition and are overreacting to the company's balance sheet leverage (1.63x market cap and 1.74x equity) and potential reduction in dividend distribution over the medium term. We believe the recent sell-off in OTEL shares have created excellent value opportunity for long term investors. We estimate OTEL's profit to reach RO 120 million by 2022E, registering CAGR of 14% during FY2018E-22E. The shares are trading at FY19 P/E of 5.0x and P/B of 0.81x. We estimate OTEL to distribute DPS of RO 0.035/Share in 2018, which is expected to grow to 0.073 by 2022E as the company deleverages in a steady manner. We have arrived at a blended DCF-RV target price of RO 1.000, which offers 42% upside potential from current levels. Owing to the significant return potential, we assign a STRONG BUY rating on the stock.

Fixed line subscribers grow in 2017, while mobile subscribers come under pressure

Fixed line and fixed broadband subscribers continue to grow, even as mobile subscribers fall marginally: Fixed line subscribers grew by 7.9% YoY to 329 thousand subscribers in 2017, while fixed line broadband subscribers continued to grow at a strong rate, 16.5% YoY to 226 thousand in 2017. However, the proportion of fixed line and broadband subscriber continued to be lower in proportion relative to mobile subscriber. Mobile subscribers, continued to come under pressure, as the number of mobile subscribers fell marginally by 0.5% to 4 million in 2017. We expect subscriber's growth to come under pressure from 2019, when by all probability, the third operator is likely to come under operation.

Figure - 13 OTEL Mobile subscribers report subdued growth

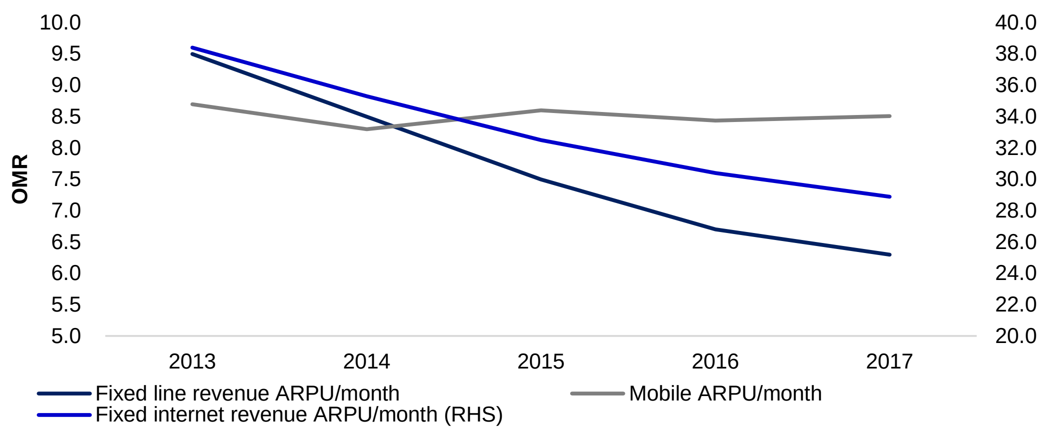


Source: Company reports, US Research

ARPU's across segment comes under pressure

ARPUs under pressure across segment: Average mobile ARPU of OTEL fixed line revenue fell by 9% YoY, while the same for fixed line broadband fell by 10% YoY in 2017. Mobile ARPU on the other hand increased marginally by 1.9% YoY for 2017. This increase comes as a marginal relief, after four years of consecutive fall in ARPU. Going forward, however, we do not expect this trend to continue as we expect it to fall by c.2.5% in the medium term.

Figure - 14 ARPUs come under pressure across the segment

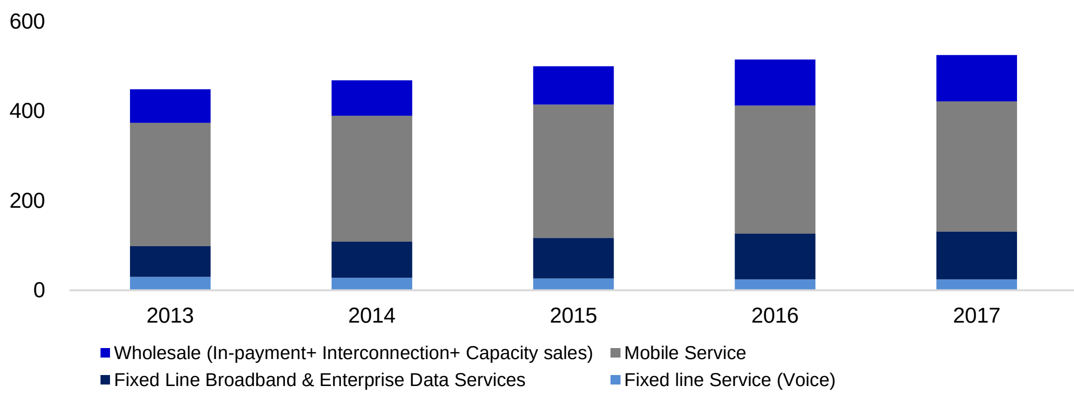


Source: Company reports, US Research

Wholesale and fixed line revenue support overall growth of OTEL

Fixed line subscriber growth and higher wholesale revenue aid in marginal sales growth: Standalone sales of OTEL increased by 2% YoY and was aided by strong growth in fixed line subscribers, both voice and broadband, and a 2% YoY growth in wholesale revenue. Going forward, we expect wholesale revenue to be aided by the synergies from Zain. However, overall standalone revenue of OTEL is likely to come under pressure from 2019, due to the potential entry of the third operator.

Figure - 15 Steady and consistent growth of wholesale revenue



Source: Company reports, US Research

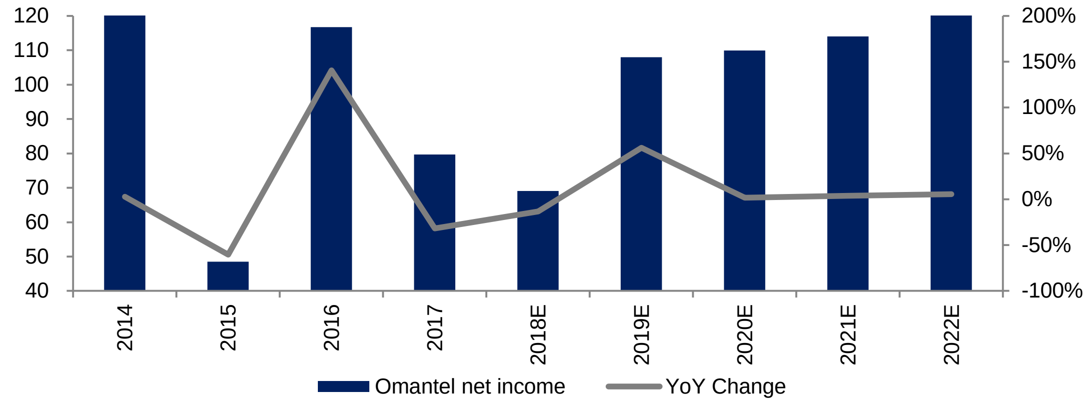
Consolidation of c.2 months Zain result aid in 2017 revenue growth

Consolidated revenue for 2017 grew by 45%, mainly due to the addition of c.2 months of Zain revenue in 2017. 2018 consolidated revenue on the other hand is expected to more than double, vis-à-vis, revenue of 2017 and will be aided by full consolidation of Zain revenue during the year. We have estimated, Zain's revenue growth to average around 2% between 2017 and 2022. However, there could be potential upside from the potential recovery of growth rates in Iraq, Sudan and the recovery of growth and full consolidation of Saudi operations of Zain.

Increase in royalty impacts profitability

Standalone profitability under pressure due to higher royalty: OTEL EBITDA at the standalone level, fell by 10% YoY and was impacted by a more than 50% increase in royalty due to royalty increasing from 7% till 2016 to 12% in 2017. EBIT on the other hand fell by 28% YoY. Apart from higher royalty, EBIT was also impacted by higher depreciation, as capex requirements continued to be high at around 25% of revenue. Finance cost on the other hand was RO 11 million, compared to no finance cost in the previous periods, as earnings before tax fell by 38% YoY. Increase in debt to finance Zain acquisition was the main reason for the higher interest. Overall standalone net income of OTEL fell by 40% YoY, higher royalty, depreciation and finance cost were the main reason for this.

Figure - 16 Net income under pressure over the medium term; Profit to grow from 2019E



Source: Company reports, US Research Estimates

Consolidated net income attributable to OTEL fell by 32% YoY and was impacted by higher interest rates, while only partial consolidation of Zain was made during the year. Net income attributable to OTEL is expected to increase at a CAGR of 8% between 2017 and 2022. Full consolidation of Zain and benefits of synergy, estimated at around USD80 million p.a. from 2019 will aid in this growth of consolidated profitability. Again, growth in profitability could be higher, if the recovery of Zain Iraq and Sudan happens at a faster rate.

Zain acquisition gives OTEL exposure to countries across Middle East and makes it the third largest player in the region

Zain acquisition to ensue long term benefits: In 2017, OTEL acquired 21.9% stake in Kuwait based Zain Group for a total consideration of RO 845 million. Through this acquisition, OTEL became the second largest shareholder in Zain and also acquired control of board. A Kuwait based telecom major, the group has diversified presence across middle east, including Kuwait, Iraq, Jordan, Sudan, Bahrain and Saudi Arabia. In most of the market it operates, Zain has either a leadership or number two position. With this acquisition, OTEL became the third largest player in the Middle East.

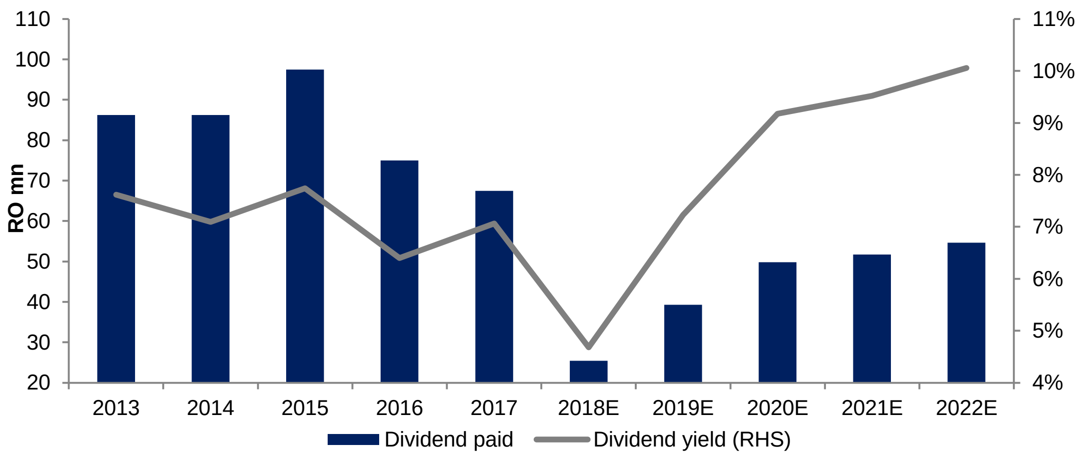
Between 2013 and 2017 revenue of Zain fell by 5% CAGR and was impacted by substantial fall in revenue in Sudan and Iraq. EBITDA on the other hand fell at a CAGR of 6% for the same period, mirroring the fall in revenue. However, it has to be noted that the operations in most of the regions that Zain is operating is recovering, with Iraq leading the way. Revenue from Sudan and Iraq fell between 8% and 9% CAGR during 2013 and 2017.

Overall, we feel that the valuations paid by OTEL for the acquisition of Zain appear to be stretched, with a discount of 9.4x EV/EBITDA and 18.4x P/E based on 2017 financials. However, if we include the estimated synergies, the same reduces to 7.0x EV/EBITDA and 13.6x P/E. Despite this we feel that the valuations appear to be stretched.

Zain acquisition likely to put pressure on medium term dividend payments

The entire acquisition cost of Zain has been financed through debt by OTEL at an average cost of close to 5.6%. We expect annual interest cost from these debts to average RO 50 million. Zain on the other hand has paid an average annual dividend of KD 151 million or OTEL share of RO 42 million. Given this, it appears that dividend alone may not be sufficient to service the new debts issued by the company for the purpose of acquisition, unless pay-out of Zain increases significantly going forward. This would necessitate the company to fund the interest service deficit from its operating cash flow or cash from sale of investments during the first two years. From 2019E, we estimate the reduced debt levels and full monetization of synergies to the tune of RO 30 million would be sufficient for servicing the debt. For principal repayments, we estimate the company will have to monetize from some its assets such as investments, the upcoming head office, and tower assets. We are estimating a sale and lease back arrangement for OTEL's head office, while the Oman Tower Company is likely to take over the tower assets from the company's balance sheet, helping in value unlocking.

Figure - 17 Lower dividend through 2019E, and expected to pick up as asset monetization gathers momentum

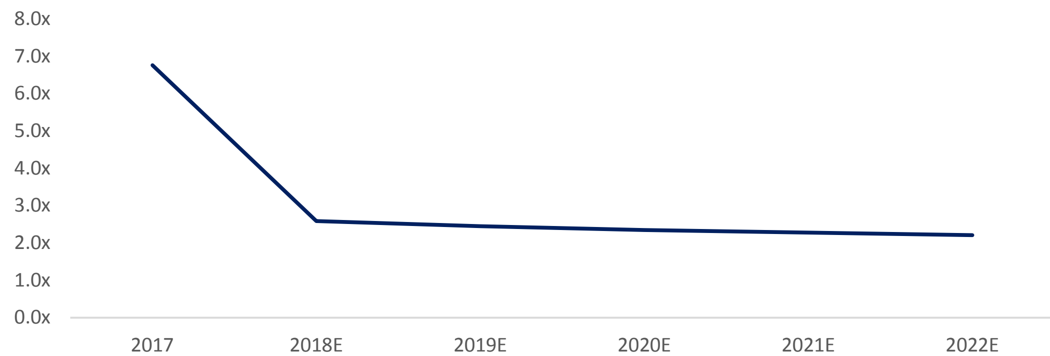


Source: Company reports, US Research Estimates

Leverage increase, though the same under control

Despite increase in debt, Omantel maintains a strong financial position: In line with lower profitability, standalone cash flow from operations of OTEL fell by 12% and was impacted by higher royalty and taxes. Capex continued to be high, averaging close to 25% of revenue. Once OTEL is able to fully integrate its operations with Zain, there could be substantial savings in the amount of capex, aided by integrated sourcing. Cash flow from financing on the other hand showed a positive flow of OMR850 million, reflecting the debt issued to finance the acquisition. This along with the expected repayment of term loan over the next five years, is expected to put pressure on the dividend payments, with the same recovering to current levels in the next five years.

Figure - 18 Leverage likely to come down from 2017 levels, though it is likely to average close to 2x for the next five years



Source: Company reports, US Research Estimates

Debt to equity for 2017 was around 123%, while we estimate a consolidated debt to EBITDA of close to 2.6x for 2018. This in turn is likely to fall at a slow rate in the next six years. However, we expect the leverage to continue at around 2.0x in the medium term.

DCF valuation of RO 1.156/Share; 60% upside potential

OTEL's DCF valuation resulted in RO 1.156/Share: We have employed SOTP FCFE valuation of OTEL to arrive at the intrinsic valuation of the company. We have used cost of equity of 15% derived from risk free rate of 5%, equity risk premium of 6.5%, and equity beta of 1.5. Our base case valuation assumed that the company's cash flow would remain stable beyond the forecasted period. As for valuation of Zain, we have employed cost of equity of 10.8% derived from risk free rate of 5%, equity risk premium of 6.5%, and equity beta of 0.9. In our base case scenario, we further assumed that the FCFE of Zain would grow at terminal growth rate of 2% beyond our forecast period. We have arrived at a DCF value of RO 1.156/Share of OTEL, which is 60% higher than the current price of RO 0.724/Share.

Figure - 19 DCF Valuation - OTEL

Discounted cash flow valuation	**2018E**	**2019E**	**2020E**	**2021E**	**2022E**
Net changes in cash flow	-17	6	-2	1	5
Less: dividend from Zain	-34	-33	-35	-36	-38
Add: Dividend paid	25	39	50	52	55
Net FCFE	-26	12	13	17	22
Cost of Equity (%)	15%	15%	15%	15%	15%
PV of FCFE	-22	9	8	10	11
Sum of PV					87
Value of OTEL - Standalone					221
DCF value of Zain					2,949
OTEL's share of Zain					646
Market value of OTEL+Zain					867
Shares outstanding					750
Value per share (RO)					**1.156**
CMP (RO)					0.724
Upside/downside					60%
Implied P/E (2019E)					8.0x

Source: Company reports, US Research Estimates

Relative valuation in the range of RO 0.788-0.848/Share

Our relative valuation of OTEL shares involved 3 year average EV/EBITDA of 4.9x, which was employed to FY2018E EBITDA of the company. The EV/EBITDA valuation thus arrived was RO 0.788/Share, implying upside potential of 9% from the current price of the stock. Additionally, we have employed P/E based valuation, in which we have used 3 year average P/E of 9.2x to the FY2018E earnings of OTEL. Our P/E based valuation resulted in a relative value of RO 0.848/Share.

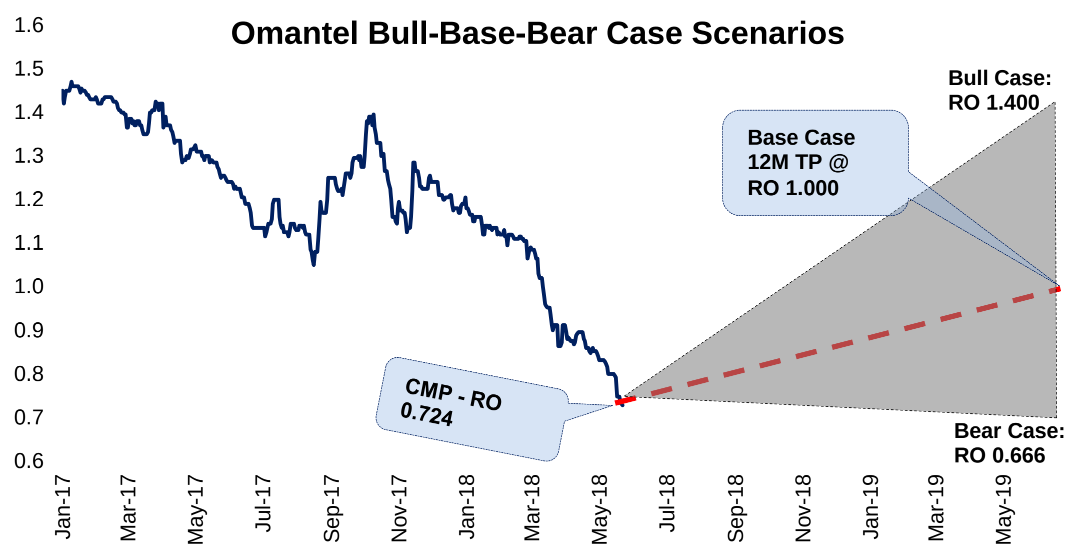
Our base case blended weighted DCF-Relative valuation of OTEL resulted in 12-Month target price of RO 1.000/Share for the stock. We have applied 55% weight to DCF while the relative valuation techniques were given an equal weight of 22.5% each. The target price thus arrived is 38% higher than the current price of OTEL, and hence we rate the stock as STRONG BUY.

Figure - 20 Weighted DCF-Relative Valuation of Omantel

Omantel Valuation Snapshot			
Discounted Cash Flow	1.156	55%	0.636
EV/EBITDA	0.788	23%	0.177
P/E	0.848	23%	0.191
Blended DCF-RV Target Price		**100%**	**1.000**
CMP			0.724
Potential upside			**38%**

Source: Company reports, US Research Estimates

Our Bull-Base-Bear Case valuation of the stock resulted in a valuation range of RO 0.666 to RO 1.400/Share.



Income Statement (RO mn)	2013	2014	2015	2016	2017	2018E	2019E	2020E	2021E	2022E
Revenue	463	481	507	519	752	1,845	1,864	1,876	1,896	1,923
Cash operating cost	-263	-270	-284	-289	-461	-1,188	-1,164	-1,174	-1,189	-1,208
EBITDA	200	212	224	230	291	657	700	702	707	715
Depreciation and Amortization	-78	-81	-88	-103	-152	-322	-320	-318	-316	-315
Operating profit	121	130	135	127	139	335	379	384	391	400
Finance and investment income	7	9	4	5	13	5	4	5	5	5
Finance cost	-5	-8	-0	-1	-20	-106	-98	-96	-94	-92
Other income/(expences)	4	4	-8	3	-16	35	41	44	47	54
Profit before tax	128	135	131	134	116	269	327	336	350	368
Tax	-12	-19	-16	-16	-9	-36	-43	-44	-46	-49
Net income	115	116	115	118	107	233	283	292	304	319
Net income - Omantel share	119	122	48	117	80	69	108	110	114	120
Cash flow from operations	189	224	221	212	260	655	702	706	725	737
Funds from operation	189	201	208	215	268	661	702	706	713	725
FCF	104	77	92	60	72	365	412	416	433	443
Capex	-86	-147	-129	-153	-189	-290	-290	-290	-292	-294
Working capital	32	19	-28	-59	-54	-52	-52	-52	-63	-75
Changes in working capital	1	23	13	-2	-7	-6	0	0	11	12
CMP (RO)	1.5094	1.6209	1.6794	1.5631	1.2742	0.724	0.724	0.724	0.724	0.724
Market Cap	1,132	1,216	1,260	1,172	956	543	543	543	543	543
Debt	36	36	38	8	1,966	1,958	1,908	1,858	1,810	1,764
Minority interest	0	0	0	-35	1,030	1,050	1,085	1,121	1,159	1,199
EV	1,096	1,202	1,252	1,077	3,571	3,096	2,992	2,900	2,808	2,716
Number of shares	750	750	750	750	750	750	750	750	750	750
Adj EPS (RO)	0.159	0.163	0.065	0.156	0.106	0.092	0.144	0.147	0.152	0.160
Adj. P/E (x)	9.5x	9.9x	26.0x	10.0x	12.0x	7.9x	5.0x	4.9x	4.8x	4.5x
EV/EBITDA (x)	5.5x	5.7x	5.6x	4.7x	12.3x	4.7x	4.3x	4.1x	4.0x	3.8x

Balance Sheet (RO mn)	2013	2014	2015	2016	2017	2018E	2019E	2020E	2021E	2022E
Assets										
Current assets										
Cash and bank balance	72	49	45	69	381	455	543	622	704	790
Trade and other receivables	72	89	85	97	694	704	712	718	725	734
Inventories	11	10	8	9	52	59	60	60	61	61
Other financial assets	86	90	74	30	24	24	24	24	14	4
Prepayments and other non-current assets	12	13	17	0	0	0	0	0	0	0
Dues from subsidiaries	0	0	0	0	0	2	2	2	2	2
Total current assets	**252**	**252**	**229**	**205**	**1,151**	**1,243**	**1,341**	**1,426**	**1,506**	**1,591**
Non-current assets										
Other financial assets	40	46	53	51	58	48	38	28	28	28
Other assets	10	13	9	9	19	19	19	19	19	19
Investments in JV and associates	7	9	9	10	245	245	245	245	245	245
Due from an associates	0	0	0	0	521	521	521	521	521	521
Investements in subsidiaries	0	0	0	0	0	0	0	0	0	0
Property, plant and equipments	396	465	463	517	1,468	1,442	1,418	1,396	1,377	1,363
Intangible assets and goodwill	51	45	29	25	1,005	1,005	1,005	1,005	1,005	1,005
Total non-current assets	**504**	**578**	**564**	**612**	**3,317**	**3,282**	**3,247**	**3,216**	**3,197**	**3,183**
Assets classified as held for sale	0	4	0	9	10	10	10	10	10	10
Total assets	**756**	**834**	**793**	**826**	**4,478**	**4,534**	**4,598**	**4,651**	**4,712**	**4,783**
Current liabilities										
Trade and other payables	119	166	191	202	855	867	876	883	892	904
Borrowings	7	14	23	2	855	304	304	302	301	331
Royalty payable	30	32	34	0	0	0	0	0	0	0
Tax payable	20	20	18	0	0	0	0	0	0	0
Total current liabilities	**177**	**232**	**265**	**205**	**1,710**	**1,171**	**1,180**	**1,185**	**1,192**	**1,235**
Non-current liabilities										
Borrowings	29	21	15	6	1,111	1,653	1,604	1,556	1,510	1,433
Retirement benefit obligations	6	5	6	0	0	0	0	0	0	0
Provisions	0	0	0	0	0	0	0	0	0	0
Other liabilities	5	6	2	10	59	59	59	59	59	59
Total non-current liabilities	**40**	**32**	**23**	**15**	**1,170**	**1,712**	**1,663**	**1,615**	**1,568**	**1,491**
Liabilities classified as held for sale	0	0	0	59	0	0	0	0	0	0
Total liabilities	**217**	**264**	**288**	**279**	**2,880**	**2,884**	**2,843**	**2,800**	**2,761**	**2,726**
Equity - Parent	**533**	**570**	**540**	**582**	**568**	**601**	**670**	**730**	**792**	**858**
Non controlling interest - discontinued operations	6	-0	-35	0	0	0	0	0	0	0
Discontinued operations	0	0	0	-1	0	0	0	0	0	0
Non controlling interest - continuing operations	0	0	0	-35	1,030	1,050	1,085	1,121	1,159	1,199
Total equity	**539**	**570**	**505**	**547**	**1,598**	**1,651**	**1,755**	**1,851**	**1,951**	**2,057**
Total equity and liabilities	**756**	**834**	**793**	**826**	**4,478**	**4,534**	**4,598**	**4,651**	**4,712**	**4,783**

Key Ratios	2013	2014	2015	2016	2017	2018E	2019E	2020E	2021E	2022E
Valuations										
P/E	9.5x	9.9x	26.0x	10.0x	12.0x	7.9x	5.0x	4.9x	4.8x	4.5x
EV/EBITDA	5.5x	5.7x	5.6x	4.7x	12.3x	4.7x	4.3x	4.1x	4.0x	3.8x
Price to book value	2.1x	2.1x	2.3x	2.0x	1.7x	0.9x	0.8x	0.7x	0.7x	0.6x
Price to sales	2.4x	2.5x	2.5x	2.3x	1.3x	0.3x	0.3x	0.3x	0.3x	0.3x
Capex										
Capex to sales	18.5%	30.5%	25.4%	29.4%	25.1%	15.7%	15.6%	15.5%	15.4%	15.3%
Capex to depreciation	91.1%	55.2%	68.5%	67.3%	80.5%	111.1%	110.4%	109.6%	108.4%	106.9%
Liquidity										
Current ratio	1.4x	1.1x	0.9x	1.0x	0.7x	1.1x	1.1x	1.2x	1.3x	1.3x
Quick ratio	1.4x	1.0x	0.8x	1.0x	0.6x	1.0x	1.1x	1.2x	1.2x	1.2x
Cash ratio	40.7%	21.1%	17.0%	33.5%	22.3%	38.8%	46.0%	52.5%	59.1%	64.0%
Cash cycle										
Inventory turnover	42.7x	46.5x	60.9x	55.6x	14.3x	31.4x	31.3x	31.3x	31.3x	31.3x
Receivables turnover	6.4x	5.4x	5.9x	5.3x	1.1x	2.6x	2.6x	2.6x	2.6x	2.6x
Accounts payable turnover	3.9x	2.9x	2.7x	2.6x	0.9x	2.1x	2.1x	2.1x	2.1x	2.1x
Inventory days	8	8	6	6	25	11	11	12	12	11
Receivables days	56	67	61	67	332	137	138	138	138	137
Accounts payable days	93	124	135	140	409	169	169	169	169	169
Cash cycle	-29	-50	-69	-66	-52	-20	-20	-20	-20	-20
Leverage										
Debt to equity	6.7%	6.2%	7.5%	1.5%	123.1%	118.6%	108.7%	100.4%	92.8%	85.8%
Debt to EBITDA	0.2x	0.2x	0.2x	0.0x	6.8x	3.0x	2.7x	2.6x	2.6x	2.5x
Net debt to EBITDA	0.0x	0.0x	0.0x	0.0x	5.5x	2.3x	2.0x	1.8x	1.6x	1.4x
Interest coverage	41.5x	25.2x	514.2x	177.8x	14.5x	6.2x	7.1x	7.3x	7.5x	7.8x
Return Ratio										
ROE	21.4%	20.3%	22.8%	21.5%	6.7%	14.1%	16.1%	15.8%	15.6%	15.5%
ROA	15.2%	13.9%	14.5%	14.2%	2.4%	5.1%	6.2%	6.3%	6.4%	6.7%
ROIC	16.1%	15.6%	17.1%	15.4%	3.1%	7.4%	8.3%	8.3%	8.3%	8.4%
DUPONT analysis										
Total assets to equity	1.4x	1.5x	1.6x	1.5x	2.8x	2.7x	2.6x	2.5x	2.4x	2.3x
Net income to sales	24.9%	24.0%	22.7%	22.6%	14.3%	12.6%	15.2%	15.6%	16.0%	16.6%
Sales to total assets	61.2%	57.7%	64.0%	62.9%	16.8%	40.7%	40.5%	40.3%	40.2%	40.2%
ROE	21.4%	20.3%	22.8%	21.5%	6.7%	14.1%	16.1%	15.8%	15.6%	15.5%
Profitability ratio										
EBITDA margin	43.1%	44.0%	44.1%	44.3%	38.7%	35.6%	37.5%	37.4%	37.3%	37.2%
EBIT margin	26.2%	27.1%	26.7%	24.5%	18.5%	18.1%	20.4%	20.5%	20.6%	20.8%
PBT margins	27.6%	28.0%	25.9%	25.7%	15.4%	14.6%	17.5%	17.9%	18.4%	19.1%
PAT margins	25.8%	25.4%	9.6%	22.5%	10.6%	3.7%	5.8%	5.9%	6.0%	6.3%
Effective tax rate	10.8%	16.6%	14.1%	13.8%	8.4%	15.3%	15.3%	15.2%	15.2%	15.2%
Cash flow ratio										
CFO to EBITDA	94.9%	105.6%	98.7%	92.2%	89.6%	99.7%	100.3%	100.6%	102.4%	103.1%
Debt to CFO	19.1%	15.9%	17.1%	3.9%	754.9%	298.9%	271.8%	263.1%	249.8%	239.2%
Debt to FFO	19.2%	17.7%	18.1%	3.8%	733.9%	296.2%	271.9%	263.2%	253.8%	243.3%
Debt to FCF	34.9%	46.4%	41.0%	13.7%	2732.7%	536.9%	463.2%	446.6%	418.0%	398.1%
EV to FCF	10.6x	15.7x	13.6x	18.1x	49.6x	8.5x	7.3x	7.0x	6.5x	6.1x

Telecom

Ooredoo Oman - FCF growth and high yield

BUY: TP @ RO 0.572

Valuation Summary (TTM)			
Price (OM)			0.506
PER (x)			10.5
P/Book (x)			1.5
P/Sales (x)			1.2
EV/Sales (x)			1.3
EV/EBITDA (x)			3.4
Dividend Yield (%)			8.3
Free Float (%)			36%
Shares O/S (mn)			651
YTD Return (%)			-4%
Beta			1.3
(mn)		**OMR**	**USD**
Market Cap		329	856
EV		360	936
Price performance (%)	**1M**	**3M**	**12M**
ORDS	4	-5%	2%
MSM 30 Index	-4%	-8%	-16%
Services Index	-3%	-6%	-11%
Trading liquidity (,000)	**1M**	**3M**	**6M**
Avg daily turnover (RO ,000)	0.07	0.10	0.10
Avg Daily Volume (,000)	130	198	191
52 week	**High**	**Low**	**CTL***
Price (RO)	0.554	0.420	20.48
* CTL is % change in CMP to 52wk low			
Major shareholders			
MENA Investco			55.0%
PASI			4.5%
Civil Servants Pension Fund			4.0%
Others			36.4%
Other details			
Exchange			MSM
Sector			Telecom
Index weight (%)			7.8
Key ratios	**2017**	**2018E**	**2019E**
EPS (RO)	0.048	0.050	0.059
BVPS (RO)	0.368	0.373	0.379
DPS (RO)	0.042	0.042	0.053
Payout ratio (%)	88	84	91
Valuation	**2017**	**2018E**	**2019E**
P/E Ratio (x)	10.5	10.1	8.6
Price/Book (x)	1.4	1.4	1.3
Dividend Yield	8.3%	8.3%	10.6%

Stable performance and attractive strong FCF generation makes Ooredoo Oman an yield play; BUY with TP of RO 0.565/Share: Our positive stance on ORDS is derived from its unleveraged balance sheet, high growth profile of FBB segment and strong FCF generation capabilities. Even though the potential entry of third operator will be detrimental to the performance of both the existing players, we estimate ORDS will have a relatively lower damage as compared to OTEL. Additionally, we believe the new RAIO regime at the present form of cost plus basis would be advantageous to ORDS in expanding its service coverage and product offerings. We estimate significant cost advantages to the company from group procurement strategies result in lower capex and high FCF generation possibilities. This should lead to the company maintaining its payout ratio at close to 90%, resulting in high DPS and yield. Our blended DCF-Relative Valuation has resulted in 12M target price of RO 0.572/Share, offering 13% upside potential from current levels. The shares of ORDS are currently trading at FY19E P/E of 8.5x and offer 2018E dividend yield of 8.9%, which is the highest among all GCC telecom operators. We assign BUY rating on the stock and recommend it for income seeking investors.

ORDS's strong financial position is expected to be maintained over the medium term: With virtually no debt in the balance sheet and consistent cash generation, the financial position of Oredoo continues to be strong. Dividend payment averaged close to RO 25 million in the past five years and we expect dividend payment to continue to be strong. At current market price, the company is quoting at attractive dividend yield of close to 9%.

Group procurement strategy helped in efficiency enhancement and reducing capex spending: Capex spending's of ORDS fell from historical levels of c.25% of revenue to close to 17% in 2017, mainly due to scale benefits gained by the company from group sourcing. This in turn, will help the company to limit the pressure on cash generation post the entry of third operator, to a certain extent.

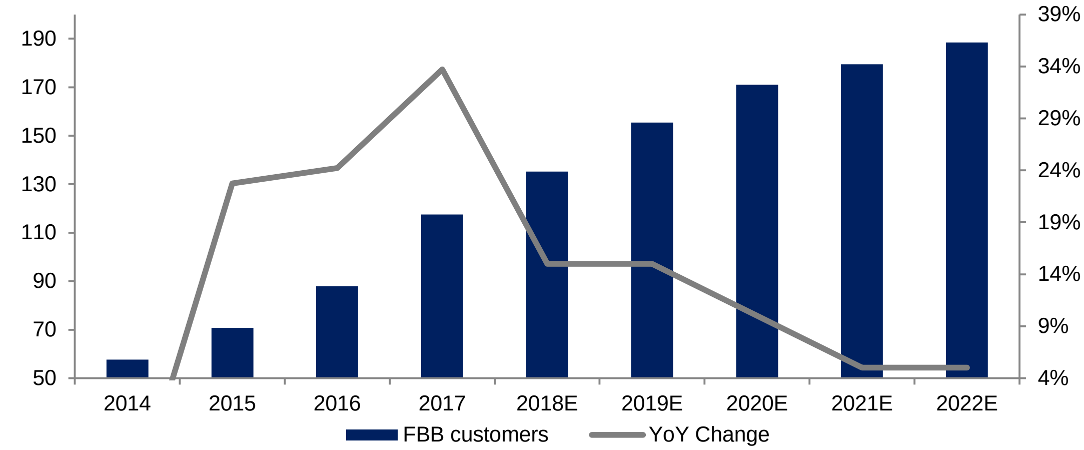
Oman's telecom market to come under pressure with the eminent entry of third operator: With the Omani government likely to make way for third operator and given the stagnant telecom market in the country, we expect market share of Ooredoo to come under pressure. While there appears some growth opportunity, in the form a more liberalized interconnection charges, which could help them shore up their market share in fixed broadband telephony and the wholesale market, it could at best limit the damages of the entry of third operator.

Risks

- Third operator entry, resulting in higher than expected deterioration in market share
- Non-implementation of interconnection charges in the current form
- Failure of the accrual of benefits of group sourcing of capex

Customer growth aided by both fixed and mobile telephony growth

Figure - 21 Fixed Telecom subscriber grow steadily

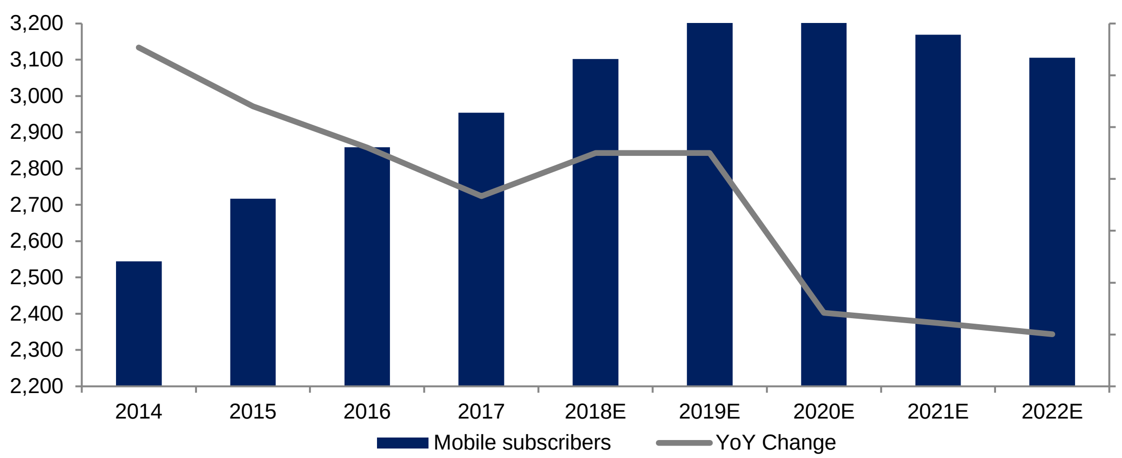


Source: Company reports, US Research Estimates

Fixed line subscribers register strong growth aided by lower base

Total customers of Ooredoo grew by 4% YoY to 3 million and the growth was aided by a 34% YoY growth in fixed telephony subscribers. Growth in fixed telephony was aided by a lower base and despite the strong growth, contributed to a mere 4% of total subscribers. Mobile telephony on the other hand grew by a moderate 3% YoY and was aided by 3% YoY growth in pre-paid subscribers, which accounted for 92% of total subscribers. Post paid subscribers on the other hand grew by 2% YoY. Going forward we expect mobile subscribers to grow by 5% for the next two years, with the same coming under pressure from 2020, with the introduction of third operator.

Figure - 22 Mobile subscriber base to peak in 2019E

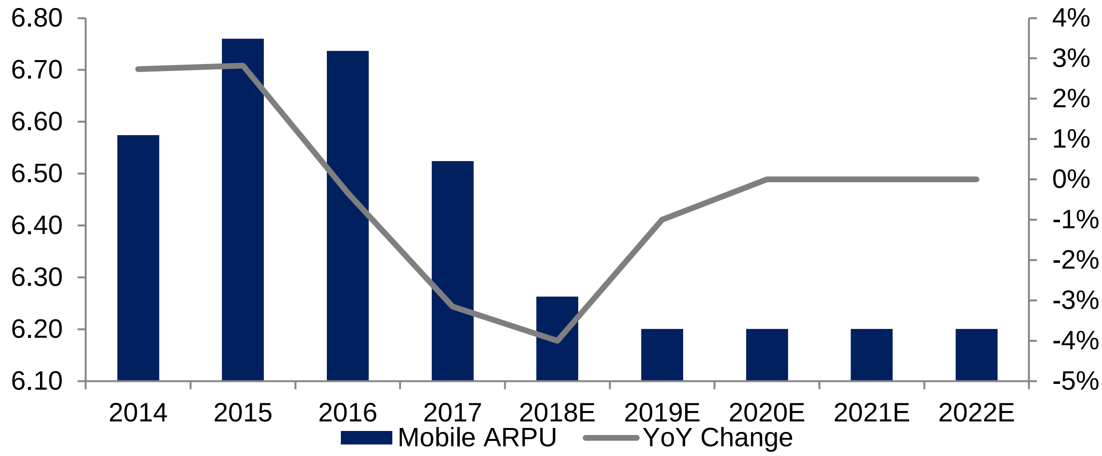


Source: Company reports, US Research Estimates

ARPU estimated to be under pressure

ARPU continues to remain under pressure: Blended ARPU of Ooredoo fell by 3% YoY and was impacted by lower ARPU from both mobile and fixed telephony. Revenue from fixed telephony fell by 19% YoY, while the same for mobile telephony fell by 3%. Going forward we expect this trend to continue and we expect ARPU's to continue to come under pressure. However, we also note that, the average ARPU in Oman is one of the lowest in the region and downside to the same is limited.

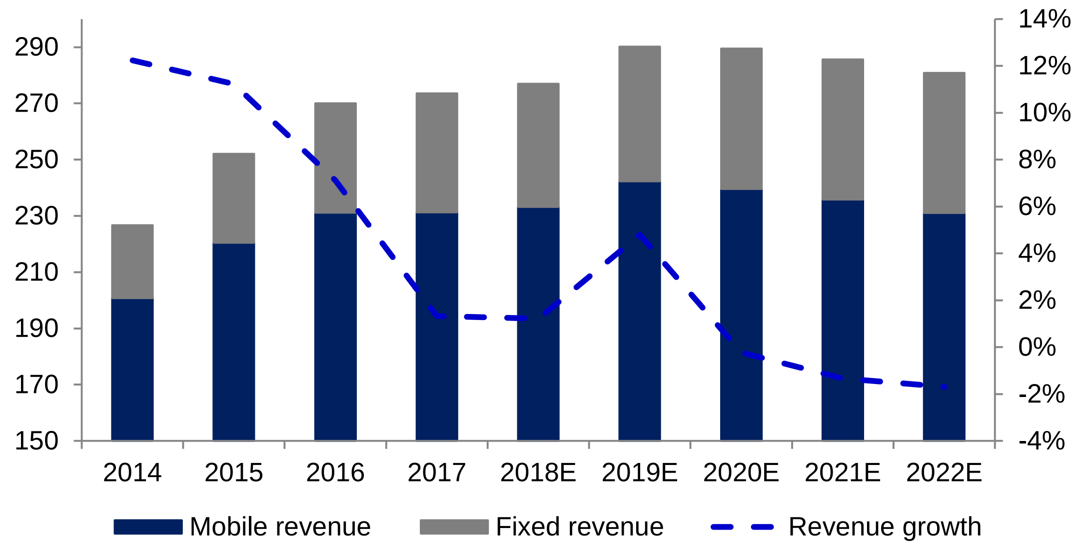
Figure - 23 Mobile ARPU under pressure



Source: Company reports, US Research Estimates

Revenue growth to moderate

Figure - 24 Mobile revenue aid in total revenue growth



Source: Company reports, US Research Estimates

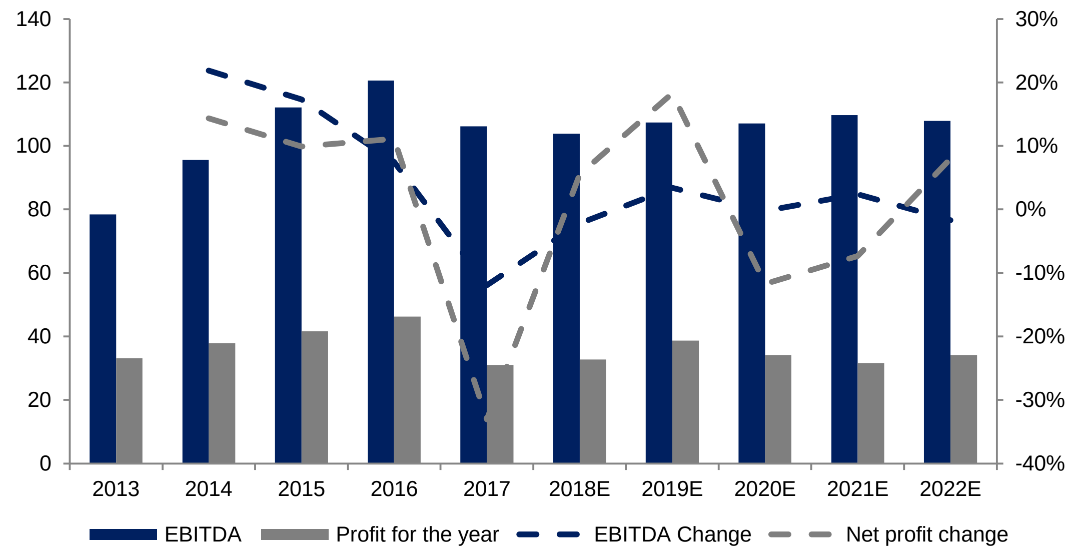
Subscriber additions to drive revenue growth

Total revenue of Ooredoo grew by 1% YoY and was aided by a 9% YoY growth in fixed telephony, while mobile revenue was flat in 2017, compared to 2016 levels. Improvement in subscribers, both fixed and mobile telephony aided in revenue growth, while lower ARPU limited the same. Going forward, we expect revenue growth average 5% for the next two years and start to fall from then on. While moderate growth in subscriber's growth will aid revenue, pressure on ARPUs will continue to check revenue growth. We expect revenue to fall from 2020 onwards, when we expect the purported third operator to likely commence full-fledged operations.

High royalty impacts profitability growth

Profitability under pressure due to higher royalty: EBITDA of OTEL fell by 12% YoY to RO 106 million and was impacted by a 74% YoY increase in royalty. Increase in royalty charges from 7% prior 2017 to 12% of revenue from 2017. Overall net income fell by 33%, owing mainly due to lower EBITDA. Going forward, we expect Ooredoo EBITDA to grow by between 4% and 5% p.a. for the next two years, post which, we expect the same to come under pressure at the back of pressure on revenue. Depreciation is expected to fall from 2018, with the company's capex spending coming down, aided by scale benefits from joint acquisition by the group.

Figure - 25 EBITDA to grow at 1% CAGR through 2022E while net income to grow 2% upon savings from lower depreciation expenses



Source: Company reports, US Research Estimates

Strong financial profile supported by consistent cash flow and low debt

Strong financial position of ORDS is aided by net cash balance sheet: Strong cash flows in the previous years coupled with moderate payout ratios have helped ORDS in faster deleveraging of its balance sheet. This has prompted the management to increase the payout ratio to 90% in 2017. We expect the company to maintain similar payout ratio in the absence of any extraordinary capex requirements. The company's mobile license will fall due for renewal in 2020E, and we expect ORDS to issue debt for payment of license fee. Our model envisages new debt of RO 50 million to this effect. Better working capital management has helped the company to generate superior cash flow in 2017. We estimate the trend to continue, leading to level of dividend payout through 2020E.

Capex on the other hand fell by 38% YoY and averaged close to 17% of revenue, compared to historical average of 25%. We infer this was a result of ORDS's group procurement strategy. Management was vocal about equipment deployment in 2017 that is similar to that of 2016, which was a high capex year. We expect this trend to continue, as we expect ORDS to continue to benefit from scale efficiencies of the group, aiding in lower capex. Dividends averaged close to RO 25 million and we expect the same to increase, as we expect the company to pass on the benefit of lower capex to shareholders.

DCF Valuation of RO 0.538/Share: We have discounted Ooredoo's FCFE using cost of equity of 13.4% derived from risk free rate of 5%, equity risk premium of 6.5%, and stock beta of 1.3. We did not assume any terminal growth rate in FCFE beyond our forecast period. The value arrived was RO 0.538, which is 6% higher than ORDS' current market price.

Figure - 26 DCF VALUATION – OOREDOO OMAN

DCF Valuation	**2018E**	**2019E**	**2020E**	**2021E**	**2022E**
Net change in cash flow	10	3	12	16	13
Add: Dividend	29	35	31	28	31
Net FCFE	40	38	43	45	43
Cost of equity	13.4%	13.4%	13.4%	13.4%	13.4%
PV of FCFE	35	30	29	27	23
Sum of PV + TV					317
Cash					33
Value of ORDS					350
Shares outstanding					651
DCF Value per share					**0.538**
CMP (RO)					0.506
Upside/downside					6%
Implied P/E					10.7x

Source: Company reports, US Research Estimates

Our relative valuation of ORDS shares involved 3 year average EV/EBITDA of 4.5x, which was employed to FY2018E EBITDA of the company. The EV/EBITDA valuation thus arrived was RO 0.725/Share, implying upside potential of 43% from the current price of the stock. Additionally, we have employed P/E based valuation, in which we have used 3 year average P/E of 10.0x to the FY2018E earnings of ORDS. Our P/E based valuation resulted in a stock valuation of RO 0.502, which is 1% below the current market price of the stock.

Our base case blended weighted DCF-Relative valuation of ORDS resulted in 12-Month target price of RO 0.572/Share for the company. We have applied 55% weight to DCF while the relative valuation techniques were given an equal weight of 22.5% each. The target price thus arrived is 13% higher than the current price of ORDS, and hence we rate the stock as BUY. In addition to the intrinsic valuation of the company, the stock offers one of the highest dividend yield of 9% among regional telecom players. We find the stock as an attractive investment proposition for an income oriented portfolio for the medium term.

Figure - 27 Ooredoo Oman Valuation Snapshot

Ooredoo Oman Valuation Snapshot			
Discounted Cash Flow	0.538	55%	0.296
EV/EBITDA	0.725	23%	0.163
P/E	0.502	23%	0.113
Blended DCF-RV Target Price		**100%**	**0.572**
CMP			0.506
Potential upside			**13%**

Source: Company reports, US Research Estimates

Income statement	2013	2014	2015	2016	2017	2018E	2019E	2020E	2021E	2022E
Revenue	202	227	252	270	274	277	290	290	286	281
Cash operating cost	-123	-131	-140	-149	-167	-173	-183	-182	-176	-173
EBITDA	78	96	112	121	106	104	107	107	110	108
Depreciation and Amortization	-40	-50	-57	-66	-68	-64	-62	-63	-69	-65
Operating profit	39	46	55	55	38	40	46	44	41	43
Finance and investment income	0	0	0	0	0	0	0	0	0	0
Finance cost	-2	-2	-2	-2	-2	-1	0	-3	-3	-3
Other income/(expences)	1	-0	-4	0	-0	-0	-0	-0	-0	-0
Profit before tax	38	43	49	53	36	38	45	40	37	40
Tax	-4	-5	-7	-7	-5	-6	-7	-6	-6	-6
Net income	33	38	42	46	31	33	39	34	32	34
Net income - Oredoo share	33	38	42	46	31	33	39	34	32	34
Cash flow from operations	82	98	93	118	106	98	103	97	100	98
Funds from operation	75	88	105	113	96	97	100	97	101	99
FCF	-2	18	51	37	50	50	48	-7	51	50
Capex	-77	-70	-55	-76	-47	-47	-52	-104	-50	-49
Changes in working capital	7	10	-13	4	10	1	3	-0	-1	-1
CMP	0.600	0.628	0.708	0.660	0.526	0.506	0.506	0.506	0.506	0.506
Market Cap	391	409	461	430	342	329	329	329	329	329
Debt	37	46	53	26	23	13	0	50	45	40
Minority interest	0	0	0	0	0	0	0	0	0	0
EV	413	428	485	440	333	298	282	320	299	281
Number of shares	651	651	651	651	651	651	651	651	651	651
Adj EPS	0.051	0.058	0.064	0.071	0.048	0.050	0.059	0.052	0.049	0.052
Adj. P/E	11.8x	10.8x	11.1x	9.3x	11.1x	10.1x	8.5x	9.7x	10.4x	9.6x
EV/EBITDA	5.3x	4.5x	4.3x	3.6x	3.1x	2.9x	2.6x	3.0x	2.7x	2.6x

Balance Sheet	2013	2014	2015	2016	2017	2018E	2019E	2020E	2021E	2022E
Assets										
Non-current assets										
Property and equipment	256	294	281	304	279	262	253	294	275	259
Licence fee	35	32	37	32	26	26	26	26	26	26
Other intangible assets	0	0	23	3	14	14	14	14	14	14
Investment in a subsidiary	0	0	0	0	0	0	0	0	0	0
Positive fair value of derivatives	0	0	0	0	0	0	0	0	0	0
Deferred tax asset	0	0	0	1	2	2	2	2	2	2
Total non-current assets	**291**	**326**	**342**	**340**	**321**	**304**	**294**	**335**	**316**	**301**
Current assets										
Inventories	0	1	2	1	2	2	2	2	2	2
Receivables and prepayments	33	32	38	42	42	42	44	44	44	43
Bank balances and cash	15	27	28	16	33	44	47	59	76	88
Total current assets	**48**	**60**	**68**	**59**	**77**	**88**	**93**	**106**	**121**	**133**
Total Assets	**340**	**386**	**410**	**398**	**398**	**392**	**388**	**441**	**438**	**434**
Equity and liabilities										
Total equity	**185**	**199**	**215**	**236**	**239**	**243**	**247**	**250**	**253**	**256**
Total equity and non-controlling interests	**185**	**199**	**215**	**236**	**240**	**243**	**247**	**250**	**253**	**257**
Non-current liabilities										
Interest bearing borrowings	27	30	26	4	13	0	0	45	40	40
Site restoration provision	3	4	5	5	5	5	5	5	5	5
Employee benefits	3	2	3	3	2	2	2	2	2	2
Total non-current liabilities	**34**	**37**	**34**	**13**	**20**	**8**	**8**	**53**	**48**	**48**
Current liabilities										
Payables and accruals	89	112	108	102	103	104	109	109	107	105
Interest bearing borrowings	10	17	27	22	11	13	0	5	5	0
Deferred revenue	16	17	19	18	17	17	17	17	17	17
Income tax payable	5	5	7	8	8	8	8	8	8	8
Total current liabilities	**121**	**151**	**161**	**150**	**138**	**141**	**133**	**138**	**137**	**130**
Total liabilities	**154**	**188**	**195**	**163**	**158**	**149**	**141**	**191**	**184**	**178**
Total equity and liabilities	**340**	**386**	**410**	**398**	**398**	**392**	**388**	**441**	**438**	**434**

Key Ratios	2013	2014	2015	2016	2017	2018E	2019E	2020E	2021E	2022E
Valuations										
P/E	11.8x	10.8x	11.1x	9.3x	11.1x	10.1x	8.5x	9.7x	10.4x	9.6x
EV/EBITDA	5.3x	4.5x	4.3x	3.6x	3.1x	2.9x	2.6x	3.0x	2.7x	2.6x
Price to book value	2.1x	2.1x	2.1x	1.8x	1.4x	1.4x	1.3x	1.3x	1.3x	1.3x
Price to sales	1.9x	1.8x	1.8x	1.6x	1.3x	1.2x	1.1x	1.1x	1.2x	1.2x
Capex										
Capex to sales	38.0%	30.9%	21.8%	28.1%	17.1%	17.0%	18.0%	36.0%	17.5%	17.5%
Capex to depreciation	51.5%	71.2%	104.5%	86.6%	145.1%	136.3%	117.8%	60.6%	138.0%	131.3%
Liquidity										
Current ratio	0.4x	0.4x	0.4x	0.4x	0.6x	0.6x	0.7x	0.8x	0.9x	1.0x
Quick ratio	0.4x	0.4x	0.4x	0.4x	0.5x	0.6x	0.7x	0.7x	0.9x	1.0x
Cash ratio	12.7%	18.1%	17.6%	10.5%	24.3%	31.0%	35.3%	42.9%	55.3%	68.0%
Cash cycle										
Inventory turnover	427.9x	236.8x	115.4x	362.9x	137.2x	137.2x	137.2x	137.2x	137.2x	137.2x
Receivables turnover	6.2x	7.1x	6.7x	6.4x	6.6x	6.6x	6.6x	6.6x	6.6x	6.6x
Accounts payable turnover	2.3x	2.0x	2.3x	2.6x	2.7x	2.7x	2.7x	2.7x	2.7x	2.7x
Inventory days	1	2	3	1	3	3	3	3	3	3
Receivables days	58	51	54	56	55	55	55	55	55	55
Accounts payable days	159	178	155	136	135	135	135	135	135	135
Cash cycle	-99	-125	-98	-79	-77	-77	-77	-77	-77	-77
Leverage										
Debt to equity	20.1%	23.4%	24.4%	11.0%	9.8%	5.2%	0.0%	20.0%	17.8%	15.6%
Debt to EBITDA	0.5x	0.5x	0.5x	0.2x	0.2x	0.1x	0.0x	0.5x	0.4x	0.4x
Net debt to EBITDA	0.3x	0.2x	0.2x	0.1x	-0.1x	-0.3x	-0.4x	-0.1x	-0.3x	-0.4x
Interest coverage	40.2x	41.4x	48.9x	56.5x	64.9x	117.3x	NA	30.7x	35.0x	38.7x
Return Ratio										
ROE	17.9%	19.1%	19.3%	19.6%	12.9%	13.5%	15.7%	13.6%	12.5%	13.3%
ROA	9.8%	9.8%	10.2%	11.6%	7.8%	8.3%	10.0%	7.7%	7.2%	7.9%
ROIC	11.5%	11.9%	13.4%	13.8%	9.7%	10.1%	11.8%	10.0%	9.3%	10.0%
DUPONT analysis										
Total assets to equity	1.8x	1.9x	1.9x	1.7x	1.7x	1.6x	1.6x	1.8x	1.7x	1.7x
Net income to sales	16.4%	16.7%	16.5%	17.1%	11.3%	11.8%	13.3%	11.8%	11.1%	12.2%
Sales to total assets	59.4%	58.7%	61.5%	67.8%	68.8%	70.7%	74.9%	65.7%	65.3%	64.7%
ROE	17.9%	19.1%	19.3%	19.6%	12.9%	13.5%	15.7%	13.6%	12.5%	13.3%
Profitability ratio										
EBITDA margin	38.8%	42.2%	44.5%	44.7%	38.8%	37.5%	37.0%	37.0%	38.4%	38.4%
EBIT margin	19.3%	20.2%	21.8%	20.3%	14.0%	14.3%	15.8%	15.2%	14.2%	15.4%
PBT margins	18.6%	19.1%	19.3%	19.5%	13.3%	13.9%	15.7%	13.9%	13.0%	14.3%
PAT margins	16.4%	16.7%	16.5%	17.1%	11.3%	11.8%	13.3%	11.8%	11.1%	12.2%
Effective tax rate	11.7%	12.3%	14.3%	12.3%	15.0%	15.0%	15.0%	15.0%	15.0%	15.0%
Cash flow ratio										
Cash flow from operations to EBITDA	105.0%	102.2%	82.8%	97.5%	100.3%	93.9%	96.0%	90.7%	91.0%	90.5%
Debt to Cash flow from operations	45.3%	47.5%	56.7%	22.1%	22.1%	13.0%	0.0%	51.5%	45.1%	41.0%
Debt to funds from operations	49.9%	52.8%	49.9%	23.0%	24.4%	13.1%	0.0%	51.4%	44.7%	40.5%
Debt to FCF	0.0%	261.3%	104.0%	69.7%	47.3%	25.5%	0.0%	0.0%	88.9%	80.8%
EV to FCF	0.0x	24.1x	9.6x	11.8x	6.7x	6.0x	5.9x	0.0x	5.9x	5.7x

Key Contacts

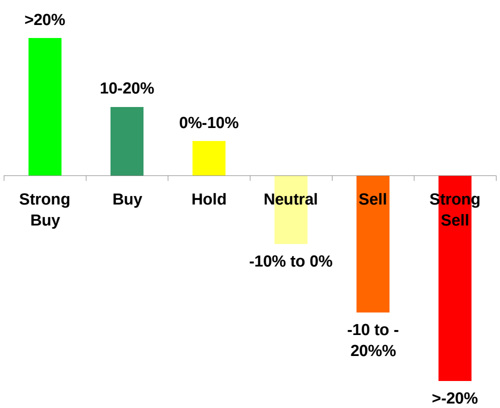
Research Team

Joice Mathew
Senior Manager - Research
E-Mail: joice@usoman.com
Tel: +968 2476 3311

Contact Address
P.O BOX 2566, PC 112
Next to Ruwi Hotel
Ruwi, Muscat
Tel: +968 2476 3300

Rating Criteria and Definitions

Rating



Rating Definitions

Strong Buy	This recommendation is used for stocks whose current market price offers a deep discount to our 12-Month target price and has an upside potential in excess of 20%
Buy	This recommendation is used for stocks whose current market price offers a discount to our 12-Month target price and has an upside potential between 10% to 20%
Hold	This recommendation is used for stocks whose current market price offers a discount to our 12-Month target price and has an upside potential between 0% to 10%
Neutral	This recommendation is used for stocks whose current market price offers a premium to our 12-Month target price and has a downside side potential between 0% to -10%
Sell	This recommendation is used for stocks whose current market price offers a premium to our 12-Month target price and has a downside side potential between -10% to -20%
Strong Sell	This recommendation is used for stocks whose current market price offers a premium to our 12-Month target price and has a downside side potential in excess of 20%
Not rated	This recommendation used for stocks which does not form part of Coverage Universe

Disclaimer

This document is not for public distribution and has been furnished to you solely for your information and must not be reproduced or redistributed to any other person. Persons into whose possession this document may come are required to observe these restrictions. Opinion expressed is our current opinion as of the date appearing on this material only. We do not undertake to advise you as to any change of our views expressed in this document. While we endeavor to update on a reasonable basis the information discussed in this material, United Securities, its subsidiaries and associated companies, their directors and employees are under no obligation to update or keep the information current. Also, there may be regulatory, compliance, or other reasons that prevent us from doing so. Prospective investors and others are cautioned that any forward-looking statements are not predictions and may be subject to change without notice. Our proprietary trading and investment businesses may make investment decisions that are inconsistent with the recommendations expressed herein. The information in this document has been printed on the basis of publicly available information, internal data and other reliable sources believed to be true and are for general guidance only. While every effort is made to ensure the accuracy and completeness of information contained, the company takes no guarantee and assumes no liability for any errors or omissions of the information. No one can use the information as the basis for any claim, demand or cause of action.

Recipients of this material should rely on their own investigations and take their own professional advice. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult their own advisors to determine the merits and risks of such an investment. Price and value of the investments referred to in this material may go up or down. Past performance is not a guide for future performance. United Securities LLC, and affiliates, including the analyst who has issued this report, may, on the date of this report, and from time to time, have long or short positions in, and buy or sell the securities of the companies mentioned herein or engage in any other transaction involving such securities and earn brokerage or compensation or act as advisor or have other potential conflict of interest with respect to company/ies mentioned herein or inconsistent with any recommendation and related information and opinions. United Securities LLC and affiliates may seek to provide or have engaged in providing corporate finance, investment banking or other advisory services in a merger or specific transaction to the companies referred to in this report, as on the date of this report or in the past.