

Bahrain Telecommunications Sector

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1. Summary

Bahrain's economy has been growing at a robust rate since the past few years. The strong economic growth was primarily led by higher oil and gas prices which boosted revenues of the state and increased liquidity in the system. The provisional data for the national accounts indicate that Bahrain's Gross Domestic Product (GDP) in year 2005 rose by 7.8% compared with 5.6% in the previous year. In 2005, GDP at constant prices increased to BD3.49bn from BD3.24bn recorded during the previous year. This vigorous growth is ascribed to the improvement in most of the non oil sectors and economic activities, particularly financial co-operation, manufacturing, construction, government services, education and health services and real estate & business activities. The GDP at current prices increased from BD4.2bn in year 2004 to BD5.03bn in year 2005, up by a healthy 19.7% due to the rise in world oil prices and a noticeable improvement in performance of the financial co-operation sector, manufacturing and construction, real estate and business activities.

The population of Bahrain grew at a CAGR of 2.64% during the period 1991-2005. As per the figures available from the Central Informatics Organisation the total population of Bahrain stood at 724,645 at the end of 2005. We expect the population of Bahrain to grow at a rate of 2.5% per annum in 2006 and is expected to reach 742,761.

The sharp rise in economic activity has multiplier effect on various sectors of the economy and telecommunication sector was one of the biggest beneficiaries. The rapid growth in telecommunication space led to the emergence of number of players in the market. In 2002, there were only 20 mobile operators in the Arab world while in 2005 number of mobile operators increased to 38. With the sharp growth in mobile communication, the number of fixed-line operators remained almost half of the mobile operators.

Liberalisation and openness in the telecommunication sector has become the buzzword in the MENA region for the past few years. Privatisation in the telecommunication sector has opened up lot of opportunities for the telecom operators from the region as well as from outside. Egypt recently offered its third mobile telecoms license to a consortium led by UAE operator, Etisalat for a price of US\$2.9bn which was much above the minimum bid price of US\$411mn.

Within the cellular mobile communication market in the GCC region, pre-paid segment is growing much faster than the post-paid segment. Bahrain has witnessed the same phenomenon in recent years. As at the end of Apr-06, prepaid cellular mobile subscribers in Bahrain stood at 671,892 a growth of 5.7% over Dec-05. Pre-paid mobile subscribers grew at a rate of 21.6% in 2005 over the previous year. Pre-paid mobile subscribers comprised 83.2% as at the end of Apr 05 while post-paid subscribers were at 16.8%. Bahrain has mobile penetration rate of 107% at the end of 2005, which was closely followed by UAE with the penetration rate of 104%. Bahrain and UAE both have a fixed line penetration rate of 27%. Bahrain's fixed line subscribers comprised around 23.6% of the total mobile subscribers at the end of April 2006. In 2005, fixed line subscribers in Bahrain stood at 193,520 as compared to 191,553 during the previous year thereby registering a miniscule growth of 1%. As at the end of Apr 06, fixed line telephony subscribers stood at 190,894 there by recording a decline of 1.4% over Dec 05 figures. Bahrain accounted for the highest number of internet subscribers in the GCC region with 10% subscribers' base followed by UAE with 9% and Kuwait with 7%.

In case of mobile telephony, as volumes expand and pricing ceases to be an effective competitive tool, operators need to provide value-added services to differentiate with their peers. We believe that future of mobile communication would rely largely on value added services offered by the operators. Although basic voice communication will remain the major source of revenue for telecom operators, data services and other value-added services will be the future growth drivers of the operators. As mobile telephone sets become more sophisticated, users are likely to expect more from their phones in terms of information as well as entertainment. Going forward, technology will be the driving force in helping telecom companies achieves greater diversification.

Consolidation and joint ventures in the telecommunication space has been occurring in the past as well. MTCs alliance with the Vodafone is testimony to this phenomenon. However, since the past few years there has been a sharp upsurge in consolidation and joint ventures in the MENA region. Some players are bidding aggressively to acquire telecom licenses while others are forming alliances or consortiums to bid for the telecom licenses. This is necessary as some of the markets in the GCC like Bahrain are at a saturation stage in terms of mobile penetration rate and mobile operators are forced to look beyond their shores to augment revenue base. Some of the players which have emerged as the key players in the telecommunication space in the MENA region comprised Orascom Telecom, Etisalat, MTC, Investcom, and Wataniya.

The Government of Bahrain formulated its telecommunications policy in May 2002 and enacted the Telecommunications Law in October 2002. The new law fully liberalised the telecommunications markets in Bahrain from July 2004, and created an independent authority, the Telecommunication Regulatory Authority, to regulate the sector. Telecommunications Regulatory Authority (TRA) acts as a regulator responsible for ensuring both fair competitions between market players and the ability of consumers to choose freely between competitors. In 2005, a total of 62 new licenses were granted by TRA for various service providers in Bahrain. Such a large number of new licenses were a record number so far as not so many licenses were issued in the past.

Bahrain Telecommunications Company (Batelco) was established as a monopoly in 1981 to provide telecommunication services in Bahrain. In an effort to expand its services, Batelco has entered into several joint ventures in the region to provide data services to multinationals through Batelco Middle East Co (BMEC). In an effort to transform the company into a customer-oriented and commercially driven institution, Batelco has embarked on a "Project Get Ready" program in 2002. The project focuses on areas that require major improvement such as customer service, network efficiency, human resource allocation, mobile services, sales and marketing including a change in the corporate identity.

Mobile telecommunication services is one of the major revenue contributors to Batelco in view of the high ARPU levels in the country. Mobile services contributed BD98.17mn to the total revenue of the company in 2005 as compared to BD95.37mn in the previous year, recording a growth of 2.9%. With the surge in mobile users, substantial part of Batelco's subscriber's base comprised mobile users rather than fixed telephone users. As a result, revenue from fixed line telephony has also witnessed substantial decline since the past few years. Revenue from fixed line telephony was BD51.6mn in 2003 which declined to BD47.5mn in 2005. In percentage terms revenue from fixed line telephony declined from 26.9% of the total revenue in 2003 to 22.4% in 2005.

Leased circuits segment is the rapidly growing segment of Batelco. It contributed BD23.6mn to the total revenue of the company in 2005 as compared to BD21.3mn in the previous year, recording a growth of 10.6% over the previous year. Revenue from internet services grew at a robust rate of 22% in 2005 and reached BD32.5mn as compared to BD26.5mn in the previous year. Internet services recorded highest year-on-

year growth in 2005. It is the third highest contributor to the total revenue of the company in 2005 as its contribution to the total revenue stood at 15.3%.

During the first nine months of 2006, total assets of the company stood at BD450.5mn, representing a growth of 16.4% over Dec 05 figures. Non-current assets comprised 83.6% of the total assets in Sep 06 as compared to 48.1% as of Dec 05. Current assets of the company declined substantially to BD74mn as at the end of Sep 06 as compared to BD200.8mn as at the end of Dec 05. The substantial decline in current assets was mainly due to sharp reduction in cash and cash equivalents of the company which decreased from BD162.7mn at the end of Dec 05 to BD29.1mn in Sep 06. The company borrowed BD8mn during the first nine months of 2006.

The total revenue of the company rose by 6.3% to BD170.14mn during the first nine months of 2006 as compared to the same period previous fiscal. Total earnings of Batelco was up by 8.7% to BD71.7mn as of Sep 2006 over Sep 05 figures. The company reported an Earnings Per Share of 59 fils as at the end of Sep 06 as compared to 54 fils in Sep 05.

Mobile Telecommunications Company (MTC) was established in 1983. MTC is the pioneer of mobile telecommunications in the Middle East and now a major player in the African continent. The company has initiated “3x3x3” expansion strategy in 2002 and has expanded rapidly since then. MTC now operates across 6 Middle Eastern and 14 sub-Saharan African countries with 12,000 employees providing a comprehensive range of mobile voice and data services to over 24.9mn (September 30, 2006) individual and business customers. MTC operates in Kuwait and Bahrain as MTC-Vodafone, in Jordan as Fastlink, in Iraq as MTC atheer, in Lebanon as MTC touch, in Sudan as Mobitel and in 14 sub-Saharan countries in Africa as Celtel.

MTC won the Bahrain license to develop the second GSM network in April 2003. In 2005, the company expanded its network capacity and enlarged its 3G network to cover 100% of Bahrain. MTC-Vodafone Bahrain continued to launch new and innovative products and services to its clientele in Bahrain throughout 2005. MTC-Vodafone Bahrain’s revenues totaled US\$69.6mn, up by 101% from the previous year. It accounted for 5.4% of the Middle East operations’ proceeds and for 3.5% of the group’s total revenues. EBITDA of the company in Bahrain improved by 171.2% to US\$15.9mn in 2005 compared to a negative EBIDTA of US\$22.3mn in 2004. EBIDTA margin was 23% compared to EBIDTA margin of -64% in the previous year.

2. Bahrain's Economic Overview

Bahrain's economy has been growing at a robust rate since the past few years. The strong economic growth was primarily led by higher oil and gas prices which boosted revenues of the state and increased liquidity in the system. In 2005, economy surged at even more robust rate as compared to its past five year performance.

The provisional data for the national accounts indicate that Bahrain's economic growth rate in year 2005 rose by 7.8% compared with 5.6% in the previous year. In 2005, the Gross Domestic Product (GDP) at constant prices increased to BD3.49bn from BD3.24bn recorded during the previous year. This vigorous growth is ascribed to the improvement in most of the non oil sectors and economic activities, particularly financial co-operation, manufacturing, construction, government services, education and health services and real estate & business activities. The GDP at current prices increased from BD4.2bn in year 2004 to BD5.03bn in year 2005, up by a healthy 19.7% due to the rise in world oil prices and a noticeable improvement in performance of the financial co-operation sector, manufacturing and construction, real estate and business activities.

Table 1: Gross Domestic Product

BD mn	2001	2002	2003	2004	2005
GDP at Current Prices	2,981.5	3,176.5	3,647.0	4,204.6	5,031.2
Growth Rate	-0.5%	6.5%	14.8%	15.3%	19.7%
GDP per Head (BD)	4,554.5	4,726.0	5,289.9	5,945.7	6,943.0
GDP at Constant Prices	2,723.8	2,866.2	3,071.4	3,242.5	3,496.2
Growth Rate	4.6%	5.2%	7.2%	5.6%	7.8%

Source: Ministry of Finance, Bahrain

As a result of the rise in oil prices, the value added in the mining activity increased to BD1.27bn in year 2005 from BD963mn in the previous year, thereby accounting for 25.2% of the GDP at current prices in 2005. The value added in the financial co-operation sector rose to BD1.24bn in year 2005, against BD1.01bn in year 2004, resulting in a growth of 21.5% compared with 31.9% the year before. This increase resulted from the rise in the net interest income, dealing in foreign currencies, investment in fund, the sale of corporate banking and retail banking services, and share of profit in associated companies. The relative importance of this sector in the GDP at current price stood at 24.6% in 2005.

The contribution of the government services sector in the GDP accounted for BD628.3mn in year 2005 against BD580.8mn in year 2004 thus representing a growth of 8.2%. This growth is ascribed to the increase in the wages and salaries by 8.7%. From a structural stand point, this sector contributed about 12.5% to the GDP. The value added of private and government education reached BD209.3mn in year 2005, up from BD193.1mn in 2004 registering a growth of 7.7%. This increase resulted from the rise in wages and salaries at the Ministry of Education, increase in number of private universities and educational institutions. Health services activity both private and public witnessed a remarkable improvement of 14.1%, as the value added reached BD103.4mn in year 2005 compared to BD90.6mn in the pervious year. This growth resulted essentially from the increase in wages and salaries at the Ministry of Health and the increase in the number of private hospitals and clinics.

The value added in manufacturing rose by 47.4% to BD655.8mn in year 2005 against BD445mn in the year before. This growth was essentially due to the increase in value added in aluminium, refinery, petrochemical, gas liquidation, metal industries, building materials and food industries. The relative contribution of this activity to GDP increased from 10.6% in year 2004 to 13.1% in year 2005. With regards to real estate and business, the value added in these activities grew by 4.8% to BD393.3mn in year 2005 compared with BD375.2mn during the year 2004. This growth is attributed to the increase in the number of residential and commercial buildings as well as the relative increase in rents. In the same direction, the value added in the transport and communications, rose by 5.8% to BD312.5mn in the year 2005 from BD295.4mn in the pervious year as a result of the increase in value added of wireless communications and land transportation activities. The value added in the wholesale & retail trade sector increased to BD504.2mn in 2005 compared to BD426.1mn in the year 2004 i.e. growth of 18.3%. Meanwhile, the value added in the rest of non oil sector recorded an increase in 2005, as the value added in construction increased by 23.1% to BD188.4mn during that year against BD153.1mn in year 2004.

Regarding items of expenditure on GDP, provisional data indicate that the final government expenditure in year 2005 increased by 9.9% to BD775.9mn from BD705.8mn in the year 2004. Private consumption expenditure reached BD2.19bn in 2005 compared to BD1.85bn in 2004. Also, its ratio to the GDP slightly decreased from 43.5% in year 2004 to 44.0% in 2005. Government expenditure on gross capital formation reached BD278.1mn during 2005, decreased by BD25.3mn or 10%.

Meanwhile, the private expenditure on gross capital formation (public, joint and private investment) declined to BD615.2mn during 2004, compared to BD654.5mn in the previous year, representing 12.24% of GDP in 2005.

The value of exports of goods and services rose by 28.7% to BD4.4bn in 2005 against BD3.41bn in 2004. This was a result of the increase in the value of oil exports from BD2.09bn in year 2004 to BD2.92bn in year 2005. The value of imports of goods and services registered an increase of 21.2% to BD.26b in 2005 compared with BD2.7bn in 2004. This rise is essentially attributed to the increase in value of oil imports from BD1.04bn in year 2004 to BD1.57bn in year 2005.

Total revenue of the government has also been increasing at a stronger rate. In 2004, total revenue of the government increased by 13.5% to BD1.3bn. Oil revenue contributed 72.6% or BD944mn to the total revenue of the government in 2004 while non-oil contributed the rest. Total expenditure of the government stood at BD1.1bn registering a growth rate of 2.2% over the previous year. Bahrain recorded a net surplus of BD60mn in 2004 as compared to a surplus of BD13.6mn during the previous year.

Table 2: Public Finance

BD mn	2000	2001	2002	2003	2004*
Revenues	1,047.3	980.9	1,026.9	1,145.5	1,300.4
Oil and Gas	764.6	672.1	691.4	836.1	943.8
Non-Oil	282.7	308.8	335.5	309.4	356.6
Expenditures	787.0	832.8	1,031.0	1,080.4	1,104.6
Current	664.1	669.8	740.0	821.2	864.0
Project	122.9	163.0	291.0	259.2	240.6
Strategic Projects	255.0	145.0	0.0	0.0	50.6
Surplus/Deficit Before Rollover	5.3	3.1	-4.1	65.1	145.2
Rollover for the Period					
Projects	0.0	0.0	0.0	45.0	85.2
Current	0.0	0.0	0.0	6.5	0.0
Total Rollover				51.5	85.2
Net Surplus/Deficit After Rollover	5.3	3.1	-4.1	13.6	60.0
As % of GDP	0.2	0.1	0.1	0.4	1.4

Source: Ministry of Finance, * Provisional 2004 GDP

As mentioned earlier, oil and gas is the backbone of Bahrain's economy. Bahrain has reported stellar economic performance in recent years due to higher oil and gas prices. Though oil and gas is the key revenue driver of the government, crude oil production has

been declining since the past three years. In 2003, Bahrain's crude oil production was 87,481 thousand US barrels which declined substantially to 68,096 thousand US barrels in 2005. In 2006, crude oil production is likely to fall further. At the same time, gas production has been rising at a steady rate and stood at 470,413 MMCF at the end of 2005. Most of the oil produced in Bahrain is from the Abu Saafa Oilfield while oil produced from Bahrain's oilfield is miniscule and comprised less than one third of total oil production.

Table 3: Main Products of Bahrain

	2001	2002	2003	2004	2005	Q1 2006
Crude Oil (US Barrels Thousands)	85,380	86,500	87,481	76,337	68,096	16,882
Bahrain Oilfield	13,656	13,800	13,720	13,647	13,348	3,280
Abu Saafa Oilfield	71,724	72,700	73,761	62,690	54,748	13,602
Production of Refined Oil (US Barrels 000)	87,765	91,122	92,350	92,669	97,716	24,212
Petrochemicals (Thousand Metric Tonnes)	1,477	1,496	1,317	1,287	1,338	405
Gas (Million Cubic Feet-MMCF)	424,358	429,169	434,537	428,375	470,413	107,398
Electricity (GWH)	6,779.4	7,279.2	7,767.6	8,267.3	8,904.4	1,375.3
Aluminum (Metric Tonnes)	522,749	518,924	531,991	531,626	750,710	208,536

Source: Ministry of Oil & Gas, Ministry of Electric & Water, Alba

3. Bahrain's Population

Size and quality of the population is the most important factor while analysing the telecommunication market in any country. We have analysed the population of Bahrain both from the nationality point of view as well as from the gender perspective.

Bahrain is a small island nation with a smaller population. The population of Bahrain grew at a CAGR of 2.64% during the period 1991-2005. For the period 1993-2002, Bahrain's population grew at a constant rate of 2.67% while in subsequent years population growth declined to 2.57% in 2003 and 2004 while in 2005 population grew at a rate of 2.47%. As per the figures available from the Central Informatics Organisation the total population of Bahrain stood at 724,645 at the end of 2005. We expect the population of Bahrain to grow at a rate of 2.5% per annum in 2006 and is expected to reach 742,761.

Table 4: Population of Bahrain

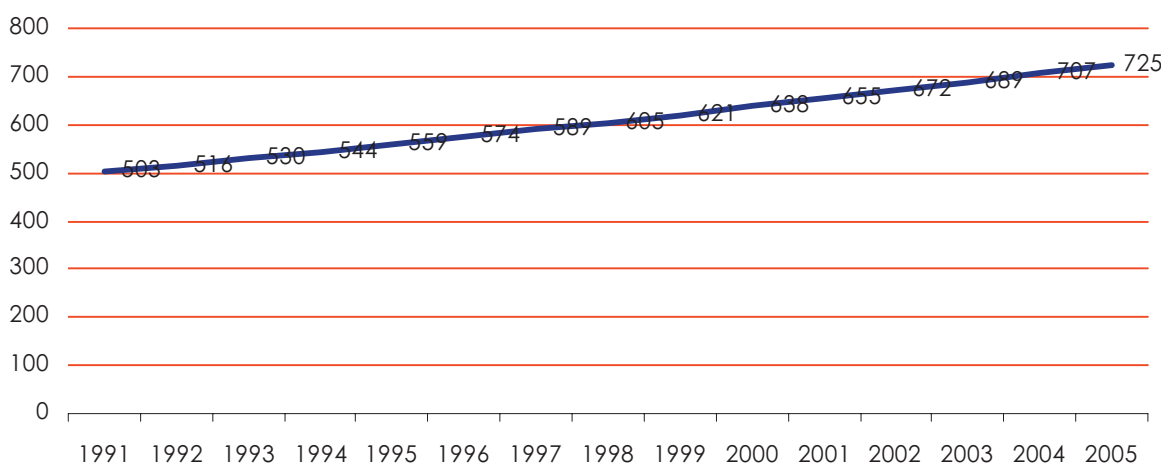
Year	Bahraini	% Growth	Non-Bahraini	% Growth	Total	% Growth
1992	328,226	2.45%	188,232	3.05%	516,458	2.66%
1993	336,251	2.44%	193,974	3.05%	530,225	2.67%
1994	344,479	2.45%	199,887	3.05%	544,366	2.67%
1995	352,900	2.44%	205,979	3.05%	558,879	2.67%
1996	361,530	2.45%	212,262	3.05%	573,792	2.67%
1997	370,377	2.45%	218,738	3.05%	589,115	2.67%
1998	379,435	2.45%	225,407	3.05%	604,842	2.67%
1999	388,714	2.45%	232,275	3.05%	620,989	2.67%
2000	398,221	2.45%	239,361	3.05%	637,582	2.67%
2001	407,959	2.45%	246,660	3.05%	654,619	2.67%
2002	417,940	2.45%	254,184	3.05%	672,124	2.67%
2003	427,955	2.40%	261,463	2.86%	689,418	2.57%
2004	438,209	2.40%	268,951	2.86%	707,160	2.57%
2005	448,491	2.35%	276,154	2.68%	724,645	2.47%

Source: Central Informatics Organisation

The local Bahraini comprised 61.9% of the population while non-Bahraini comprised the rest. Non-Bahraini population of the country has been growing at a more robust rate since the past fifteen years while growth of local Bahraini's has been a modest as compared to expatriates. Bahraini population grew at a rate of 2.45% since the period 1992 to 2002 (except in 2003 when it rose by 2.44%) while in 2003 and 2004 growth rate declined to 2.4%. In 2005, Bahraini population recorded a growth of 2.35% over the previous year,

which is also the lowest growth recorded by Bahraini population since 1991. Bahraini population stood at 448,491 at the end of 2005. In case of expatriates or non-Bahraini population growth rate was robust at 3.05% during the period 1992 – 2002. Subsequently, the growth receded to 2.86% during 2003 and 2004. In 2005, non-Bahraini population stood at 276,154 recording a growth rate of 2.68% over the previous year.

Chart 1: Historical Trend - Population of Bahrain (in 000)



Source: Central Informatics Organisation

The local Bahraini comprised to 448,491 or 61.9% of the total population in 2005. The percentage of local Bahraini's to the total population of the country has been declining consistently over the last few years. Bahraini's comprised 63.6% of the total population in 1992 while in 2005, this percentage declined to 61.9%. During the same period, population of expatriates has been rising as it rose from 36.4% in 1992 to 38.1% in 2005.

Table 5: Demographic Profile of Bahrain's Population

	2000	2001	2002	2003	2004	2005
Population Under Age 14	180,974	182,440	187,105	190,108	194,828	197,800
Population Above Age 65	15,975	16,457	16,869	17,375	17,798	18,321

Source: Central Informatics Organisation

The demographic profile of Bahrain's population indicates that around 27.3% of the total Bahraini population is below 14 years of age while 2.53% of the population is above 65 years of age.

Table 6: Population of Bahrain by Nationality

Year	Bahraini		Total Bahraini	Non-Bahraini		Total Non-Bahraini	Total
	Males	Females		Males	Females		
1991	161,959	158,430	320,389	128,862	53,801	182,663	503,052
1992	165,932	162,294	328,226	132,967	55,265	188,232	516,458
1993	169,973	166,278	336,251	136,615	57,359	193,974	530,225
1994	174,108	170,371	344,479	140,366	59,521	199,887	544,366
1995	178,328	174,572	352,900	144,227	61,752	205,979	558,879
1996	182,648	178,882	361,530	148,207	64,055	212,262	573,792
1997	187,065	183,312	370,377	152,307	66,431	218,738	589,115
1998	191,577	187,858	379,435	156,523	68,884	225,407	604,842
1999	196,190	192,524	388,714	160,866	71,409	232,275	620,989
2000	200,903	197,318	398,221	165,344	74,017	239,361	637,582
2001	205,720	202,239	407,959	169,954	76,706	246,660	654,619
2002	210,814	207,126	417,940	175,407	78,777	254,184	672,124
2003	215,848	212,107	427,955	180,430	81,033	261,463	689,418
2004	221,019	217,190	438,209	185,598	83,353	268,951	707,160
2005	226,187	222,304	448,491	190,568	85,586	276,154	724,645

Source: Central Informatics Organisation

Bahrain's overall population is still dominated by males as percentage of male population to the total population of the country remained in the range of 57.4% to 57.9% during the period 1992 to 2005. In 2005, male population of the country was 416,755 or 57.5% of the total population while female population comprised 42.5%. The percentage of males among the non-Bahraini population is 69%, whereas among the Bahraini population the percentage of males is around 50.4% in 2005.

Table 7: Population of Bahrain by Gender

Year	Males	% of Total	Females	% of Total	Total
1991	290,821	57.8%	212,231	42.2%	503,052
1992	298,899	57.9%	217,559	42.1%	516,458
1993	306,588	57.8%	223,637	42.2%	530,225
1994	314,474	57.8%	229,892	42.2%	544,366
1995	322,555	57.7%	236,324	42.3%	558,879
1996	330,855	57.7%	242,937	42.3%	573,792
1997	339,372	57.6%	249,743	42.4%	589,115
1998	348,100	57.6%	256,742	42.4%	604,842
1999	357,056	57.5%	263,933	42.5%	620,989
2000	366,247	57.4%	271,335	42.6%	637,582
2001	375,674	57.4%	278,945	42.6%	654,619
2002	386,221	57.5%	285,903	42.5%	672,124
2003	396,278	57.5%	293,140	42.5%	689,418
2004	406,617	57.5%	300,543	42.5%	707,160
2005	416,755	57.5%	307,890	42.5%	724,645

Source: Central Informatics Organisation

Bahrain's population is expected to grow at a more modest rate going forward. However, population of expatriates is expected to grow at a more robust rate since the country offers number of employment opportunities for the non-Bahrainis.

4. Telecommunication Industry Scenario

The telecommunications sector in the Middle East and North Africa region is one of the fastest growing sectors in the region. The process of liberalisation and privatisation has resulted in the telecommunication sector undergoing a rapid transformation. In addition, the strong economic growth in the region fuelled by high oil prices has led to unprecedented growth in the region. The overall economic growth has multiplier effect on various other sectors of the business and telecommunication sector was one of the largest beneficiaries of this. In the telecommunication space, growth is more visible in the mobile space rather than in the fixed line segment, which saw aggressive strategies by both incumbent operators and the new licenses holders fighting for market share in respective countries.

Preponderance of Mobile Communication

Communication technology and connectivity has been evolving over the years and is the backbone of modern economies. Most of the emerging countries are focusing heavily on developing their communication infrastructure. GCC countries are no exception to this phenomenon. GCC countries are currently focusing intensely on mobile telecommunications to address today's communication needs. With the rapid and cost-effective deployment of mobile communication networks, fixed-line penetration has been left far behind in the race to wrest market share. Most of the people and especially expatriates rely heavily on mobile network for their communication requirements. Within the spiralling mobile penetration facility, the pre-paid segment is experiencing faster growth than the post-paid.

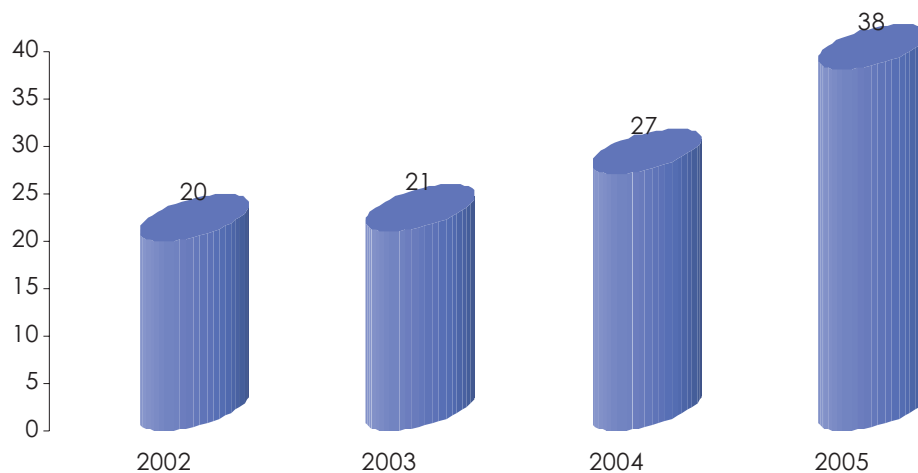
Rapid Rise in Number of Mobile Operators

The rapid growth in telecommunications market in recent years can be attributed to the number of liberalisation measures initiated by the respective governments since 2003.

Liberalisation along with the privatisation of several governments owned monopolies witnessed the emergence of new telecom operators in the region. The government allowed the entry of new players in the market place while the impending competition forced the incumbent players to entered into joint ventures with global telecom majors to offer mobile telecommunications services.

The rapid growth in telecommunication space led to the emergence of number of players in the market. In 2002, there were only 20 mobile operators in the Arab world. As per the figures available from Mobile Telecommunication Company (MTC) of Kuwait in association with Zawya, the number of mobile telecom operators in the GCC region stood at 38 at the end of 2005. Going forward, we believe that there is expected to be consolidation in the telecommunication space as the operators bid aggressively for mobile licenses in other countries. New mobile operators have been granted international gateway rights in several countries, resulting in lower prices for international phone calls. By early 2006, Saudi Arabia, Oman and Qatar were testing 3G services, following its introduction in Bahrain.

Chart 2: Number of Mobile Operators in the Arab World



Source: MTC, Zawya

With the sharp growth in mobile communication, the number of fixed-line operators remained almost half of the mobile operators. In the fixed line category there is a predominance of government owned monopolies. The future growth in telecommunication space will be driven to a large extent by mobile communication rather than fixed line telephony. As a result, most of the operators in the region are focusing on

mobile telephony as a future growth driver. Viewed from this perspective, the number of mobile operators is expected to rise further in the next few years in some of the countries in the Middle East and North Africa region.

Historically, the trend has been for domestic mobile operators to collaborate with major multinational companies, as licenses are being awarded to indigenous operators. There is also expected to be consolidation in the telecommunication space as the companies with deep pockets look for opportunities elsewhere in the region. For example, the UAE-based Etisalat owns 35% in a mobile telecom venture in Saudi Arabia's Etihad Etisalat, while MTC has stakes in several mobile operators in Jordan, Bahrain and Iraq. Bahrain Telecommunications Company (Batelco) has also become very active in overseas market with the acquisition of Umniah in Jordan. The cross border deals within the MENA region also indicates that most of the funding required for the new initiatives in the telecommunication space is also being generated from the region.

Pre-paid segment growing faster than the post-paid

Within the cellular mobile communication market in the GCC region, pre-paid segment is growing much faster than the post-paid segment. Bahrain has witnessed the same phenomenon in recent years. As at the end of Apr-06, prepaid cellular mobile subscribers in Bahrain stood at 671,892 a growth of 5.7% over Dec-05. Pre-paid mobile subscribers grew at a rate of 21.6% in 2005 over the previous year. Pre-paid mobile subscribers comprised 83.2% as at the end of Apr 05 while post-paid subscribers were at 16.8%. As at the end of 2005, total mobile subscribers in Bahrain stood at 807,428, representing a growth of 18.1% over the previous year. Going forward, pre-paid segment is expected to maintain its growth momentum.

Table 8: Mobile Subscribers in Bahrain

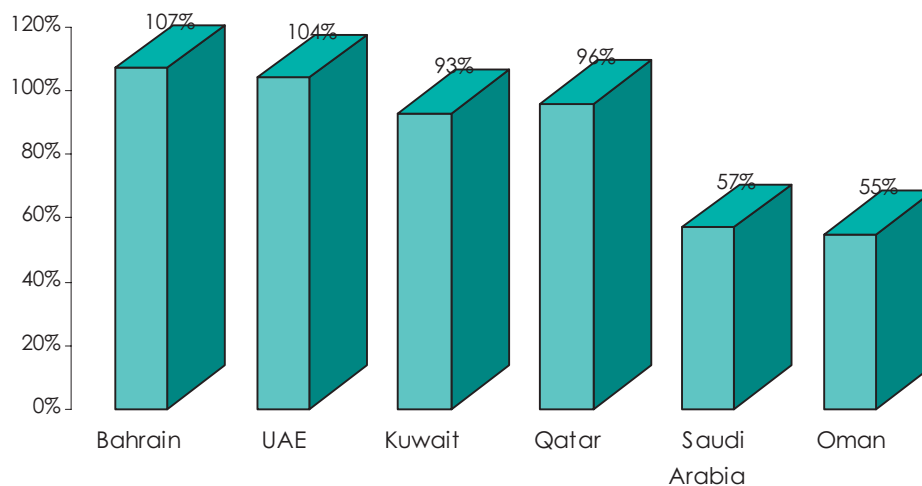
	Dec-04	Dec-05	Apr-06
Prepaid Cellular Mobile Telephone Subscribers	522,190	635,277	671,892
Postpaid Cellular Mobile Telephone Subscribers	127,574	131,826	135,536
Total Cellular Mobile Telephone Subscribers	649,764	767,103	807,428

Source: TRA, Bahrain

Mobile Penetration Rate

As indicated in the figure below, Bahrain has the highest mobile penetration rate in the entire GCC region. Bahrain has mobile penetration rate of 107% at the end of 2005, which was closely followed by UAE with the penetration rate of 104%. Oman is having the lowest penetration rate of 55% while Saudi Arabia has a mobile penetration rate of 57% as of 2005. In its newly released '2006 Middle Eastern Mobile Communications and Mobile Data Markets', Research and Markets announced that Bahrain has the highest mobile penetration rate in the region at 117%.

Chart 3: Mobile Penetration Rate in the GCC region



Source: Company Data, Various Sources

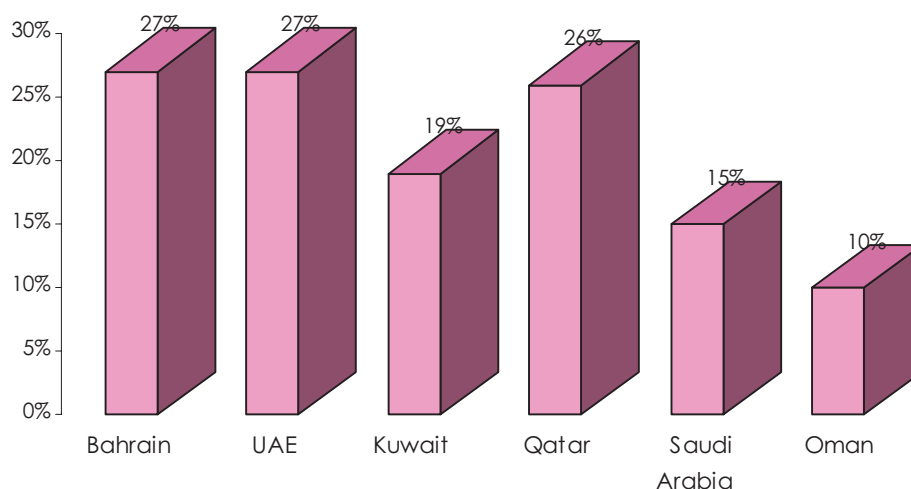
If we compare the mobile penetration rate in the GCC region to that of the MENA region, there is a wide disparity prevalent. The mobile penetration rate in the MENA region with a population of over 300mn is around 28% while it is above 55% in the GCC region. The penetration rates in the GCC countries have reached saturation levels in most of the countries while it remains still low in the other countries of the MENA region. A major part of the current mobile users were added in 2005, when the number of subscribers in the region increased by about 75% to reach just over 86mn.

In Bahrain, Batelco has been offering mobile telephony services since the GSM network was launched in 1995. As the sole mobile operator in the country till recently, the

company was able to build a strong customer base. Batelco introduced prepaid services in 1999 under the brand name SimSim. Prepaid subscribers represented over 80% of the total mobile subscribers at the end of 2005. In April 2003, the TRA granted the second mobile license to Mobile Telecommunications Company (MTC), the incumbent mobile operator in Kuwait, together with UK's Vodafone, ending the monopoly of Batelco. With the entry of competition, Batelco became more aggressive and attuned to customers' demands, increasing its advertising campaigns, and developing customized packages to appeal to all market segments. As a result, the mobile market grew significantly, as can be seen from the evolution of subscriber numbers over the past few years.

Fixed Line Penetration Rate

As mentioned earlier, with the advent of mobile communication fixed line telephony remained in the backburner as numbers of fixed line users are diminishing. Mobile telecommunication becomes the cost-effective way to meet the communication needs of the customers. The lack of innovative approach and liberalization in fixed line services has limited the expansion possibilities in the fixed line telephony. As a result, the number subscribers in the fixed line telephony and penetration rates remained much lower than that of mobile services. Bahrain continued to lead in fixed line penetration as well in the GCC region. Bahrain and UAE both have a fixed line penetration rate of 27% followed closely by Qatar with 26% and Kuwait with 19%. Oman continued to lag behind in the fixed line telephony with the penetration rate of just 10%. In early 2006, the ratio of mobile penetration to fixed-line penetration was 365% in Jordan and 400% in Bahrain.

Chart 4: Fixed Line Penetration Rate in the GCC region

Source: Company Data, Various Sources

Batelco has been the sole provider of telecom services in Bahrain since 1981. The company offers fixed line telephony including national, international voice services, public phones and toll free services among others. Growth in the fixed line segment has been slow over the past years mostly due to the migration of subscribers to mobile services.

As mentioned earlier, fixed line telephony is lagging behind the mobile telephony by a wide margin in most of the GCC countries. Bahrain's fixed line subscribers comprised around 23.6% of the total mobile subscribers at the end of April 2006. In 2005, fixed line subscribers in Bahrain stood at 193,520 as compared to 191,553 during the previous year thereby registering a miniscule growth of 1%. As at the end of Apr 06, fixed line telephony subscribers stood at 190,894 there by recording a decline of 1.4% over Dec 05 figures. The year 2006 is expected to see further decline in fixed line subscribers as the mobile operators start offering innovative and cost-effective communication technology.

Table 9: Fixed Line Subscribers in Bahrain

	Dec-01	Dec-02	Dec-03	Dec-04	Dec-05	Apr-06
Fixed Exchange Lines	173,900	175,644	185,756	191,553	193,520	190,894

Source: TRA, Bahrain

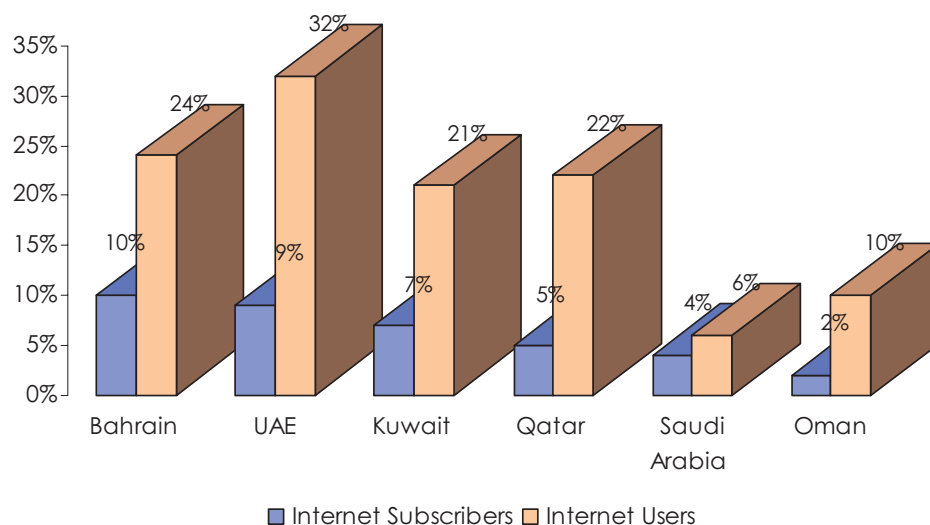
In 2003 Batelco adjusted the manner of reporting subscriber statistics. Figures for 2003 may not therefore be directly comparable to earlier years.

Due to the small population in Bahrain, we do not expect the entry of competition into the national fixed line market. However, we believe that international carriers will have their eyes set on the international telephony market especially that around 38.1% of the population in Bahrain is expatriates. Subscribers will have the ability to make calls using different call providers. This is called Carrier Pre-Selection (CPS). Batelco's subscribers will have the choice to conduct international calls either through Batelco or other international carriers providing attractive packages.

Internet Penetration

Internet services are one of the fastest growing services within the telecommunication space in the region. Bahrain accounted for the highest number of internet subscribers in the GCC region with 10% subscribers' base followed by UAE with 9% and Kuwait with 7%. UAE leads in internet users with 32% penetration rate while internet users' penetration in Bahrain stood at 24%.

Chart 5: Internet Penetration Rates in the GCC region



Source: Telecom operators in respective countries

As per the figures available from TRA, internet subscribers in Bahrain stood at 45,933 at the end of Dec 05, registering a decline of 8.8% over the previous year. Internet subscribers in Bahrain grew rapidly during the first four months of the current year as it stood at 52,492 at the end of Apr 06, up by 14.3% over Dec 05 figures. Internet subscribers are expected to go up sharply in the years to come.

Table 10: Internet Subscribers in Bahrain

	Dec-01	Dec-02	Dec-03	Dec-04	Dec-05	Apr-06
Internet Subscribers	29,325	32,000	52,889	50,382	45,933	52,492

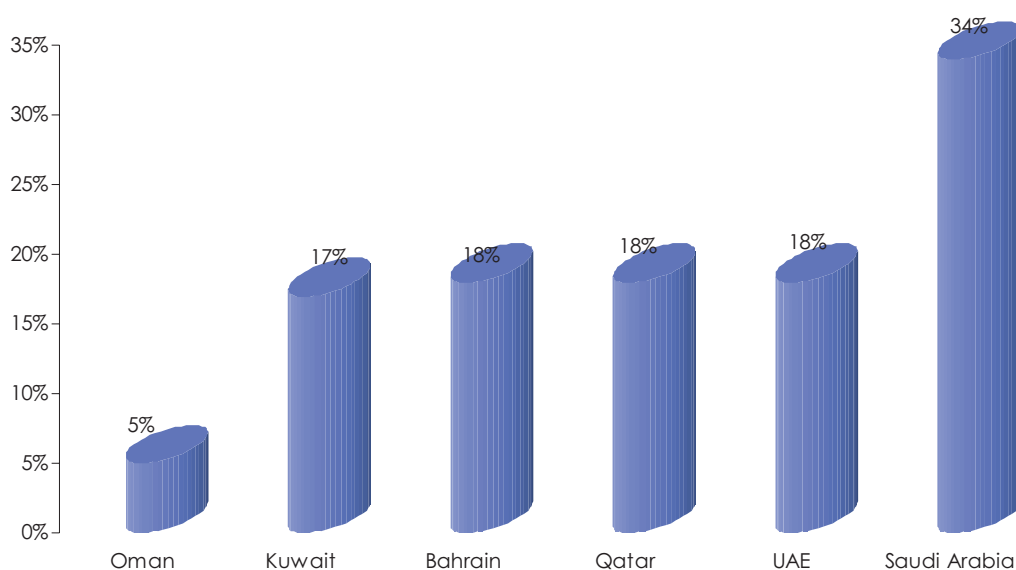
Source: TRA, Bahrain

In 2003 Batelco adjusted the manner of reporting subscriber statistics. Figures for 2003 may not therefore be directly comparable to earlier years.

PC Penetration

PC penetration in the region still remains on the lower side though it is increasing at a rapid pace. In Bahrain, UAE and Qatar PC penetration was 18% while in Kuwait it was 17%. Saudi Arabia has the highest PC penetration rate of 34%. However, the lower penetration of personal computers may limit the growth prospects of internet use in the near future. We believe that penetration rate of personal computers and internet users are set to grow exponentially in the near future.

Chart 6: PC Penetration Rates in the GCC region



Source: Telecom operators in respective countries

Operators Looking Beyond Their Shores

Domestic market remains the key focus area for most of the operators in the Middle East though some are also looking beyond their shores for expansion. It's relatively easy for the local operators to penetrate the domestic market rather than to create strong brand equity in comparatively newer markets. In almost all the markets in the Middle East, competition is driving new service providers to use aggressive strategies to expand volumes. We believe that the local operators may try to boost their topline by offering value added services to the customers. However, as the domestic market saturates for most of the GCC countries, incumbent players are looking for other markets in the MENA region to expand business.

Value Added Services to be the Future Growth Driver

Mobile users in emerging countries generally tend to be price sensitive. As a result, most of the telecom operators compete on the pricing front. However, there is a limit to which operators can compete on the pricing front. As volumes expand and pricing ceases to be an effective competitive tool, operators need to provide value-added services to differentiate with their peers. We believe that future of mobile communication would rely largely on value added services offered by the operators. Although basic voice communication will remain the major source of revenue for telecom operators, data services and other value-added services will be the future growth drivers of the operators. As mobile telephone sets become more sophisticated, users are likely to expect more from their phones in terms of information as well as entertainment. Going forward, technology will be the driving force in helping telecom companies achieves greater diversification.

Regional Markets Opening Up

Liberalisation and openness in the telecommunication sector has become the buzzword in the emerging countries for the past few years. Privatisation in the telecommunication sector has opened up lot of opportunities for the telecom operators from the region as well as from outside. Egypt recently offered its third mobile telecoms license to a

consortium led by UAE operator, Etisalat for a price of US\$2.9bn which was much above the minimum bid price of US\$411mn. Customers have benefited immensely from the liberalization and privatization initiatives of the respective governments as these forces incumbent players to reduce tariffs on number of mobile services offered to customers.

Qatar is the only country in the region to have telecommunication monopoly. However, Qatar recently announced its intention to liberalize the sector and allow the entry of foreign operators. In addition, Saudi Arabia, and Iraq are also looking forward to allow mobile license auctions in due course to other telecom operators. Other countries from the region such as Bahrain, Kuwait, and Palestine are exploring the option of granting additional licenses to other telecom operators. Lebanon also intends to privatize two mobile phone companies operating in the country buoyed by the success of Egypt's third mobile licenses bid and the huge price tag.

Consolidation and Joint Ventures

Consolidation and joint ventures in the telecommunication space has been occurring in the past as well. MTCs alliance with the Vodafone is testimony to this phenomenon. However, since the past few years there has been a sharp upsurge in consolidation and joint ventures in the MENA region. Some players are bidding aggressively to acquire telecom licenses while others are forming alliances or consortiums to bid for the telecom licenses. This is necessary as some of the markets in the GCC like Bahrain are at a saturation stage in terms of mobile penetration rate and mobile operators are forced to look beyond their shores to augment revenue base.

Some of the players which have emerged as the key players in the telecommunication space in the MENA region comprised Orascom Telecom, Etisalat, MTC, Investcom, and Wataniya. Most of these players have already captured substantial market share in their respective countries. This makes task difficult of new entrants to the market. As it's not very easy to penetrate the market and create a strong brand value to acquire substantial chunk of the customers. In addition to these factors, smaller companies will find it increasingly difficult to sustain their operations in view of high competition and falling tariffs. We are also expected to see some action in this space as well as the cash rich companies will use aggressive strategies to acquire some of the telecom operators or other companies in the telecommunication space.

Technology

Modern and innovative technology is the mainstay of the mobile communication. GSM technology is the dominant technology for mobile telecommunication. GSM technology continued to rule the mobile telecommunication in the GCC region as well. However, mobile communication is not limited to 2G alone; in fact, along with the rapid expansion of operation and coverage areas operators are upgrading their networks to provide latest range of technologies to customers. The migration to latest technologies has become absolutely necessary to offer customers value added products and services in line with other operators. In future, value added products and services based on latest technologies will play a crucial role in augmenting revenue mix of the mobile operators.

Table 11: Mobile Technologies in GCC Countries

Country	2G	3G	EDGE	GPRS
Bahrain	√	√	√	√
UAE	√	√		√
Kuwait	√		√	√
Saudi Arabia	√			√
Qatar	√			√
Oman	√			√

Source: Telecom operators in respective countries

The upgradation in technology is expected to continue with latest technologies such as 3G, EDGE and mobile broadband emerging and becoming sine qua non for mobile communication. Mobile broadband holds immense potential and operators may look forward to provide Internet Protocol Television (IPTV) services to its customers. Presently, lot of operators have migrated to 3G and EDGE technologies at least partly to serve the more sophisticated customers located in key locations. Bahrain is at the forefront in offering latest technologies to its customers as it offers most of the latest technologies including 3G and EDGE services.

New Operators in Bahrain

In 2005, competition took a major step forward in Bahrain with competing operators launching their services, for the first time, in two segments of the market. By the end of December 2005, three operators were providing internet services, via satellite, for

corporate customers. They are North Star Technology Company W.L.L., Mena Broadband Services W.L.L. and Orbit Communications Company W.L.L. A further three operators – Arabian Network Information Services W.L.L. (a subsidiary of Batelco), Business Communications Networks and Kalaam Telecom Bahrain B.S.C. – also started offering international calls, some of them using voice-over-internet protocol (VoIP). Customers use calling cards to access these services. The call rates are currently lower than the international direct dial rates offered by the mobile and fixed line operators.

5. Regulatory Environment

The winds of liberalisation have been flowing through the telecommunication sector in the GCC region for quite some time now. All the countries except Qatar have liberalized their telecommunication sector in recent times. Qatar has also announced its intention to liberalise this sector in due course. Bahrain is one of the first countries in the GCC region to liberalise the telecom sector.

Telecommunications Regulatory Authority, Bahrain

The Government of Bahrain formulated its telecommunications policy in May 2002 and enacted the Telecommunications Law in October 2002. The new law fully liberalised the telecommunications markets in Bahrain from July 2004, and created an independent authority, the Telecommunication Regulatory Authority, to regulate the sector. Telecommunications Regulatory Authority (TRA) acts as a regulator responsible for ensuring both fair competitions between market players and the ability of consumers to choose freely between competitors.

The TRA is charged with encouraging the development and availability of the widest possible range of information and communications technologies and services within Bahrain. It is the intention that these services are provided in an open environment, which allows private sector companies the necessary flexibility to best meet user needs.

The Government also adopted a Telecommunications Plan to provide a policy framework within which the TRA would operate. The telecommunication plan is likely to be updated in the near future. With the enactment of the TRA and liberalisation of the telecommunication sector, the government allowed the second mobile operator, MTC Vodafone to start operations in Dec 2003. Since then TRA has been quite aggressive in

granting various licenses and has given number of licenses to various service providers. Following are the landmark decisions taken by the Bahrain government in the telecommunication space since year 2002.

2002

- The bringing into effect of the Telecommunications Law.
- The creation of a telecommunications regulator called the Telecommunications Regulatory Authority (TRA), headed by a General Director.

2003

- A second license to provide Mobile Services.
- Opening the Value Added Services and Internet Service Provision sectors for competition.
- Establishing the Bahrain Internet Exchange.

2004

- Opening the National Fixed Service sector for competition.
- Opening the International Facilities and International Services sectors for competition opening the VSAT, Paging and PAMR sectors for competition.

Liberalisation

Bahrain is a member of WTO since 1995. Being the member of WTO, the country was committed to full liberalization of the telecom sector by 2004. Currently, there is only one service provider for fixed line telephony, namely Batelco. The company also provides mobile and Value Added Services (VAS) in a competitive environment. MTC-Vodafone Bahrain (MTC-VB) began operations in December 2003 offering mobile telephony services and mobile-enabled internet connectivity services. The TRA has the right to issue a third GSM license. TRA is actively considering the issue of third mobile licenses in Bahraini market; however, the small size of the market might force TRA to reconsider its decision. The third license will likely be used as leverage by the TRA should the two existing players become involved in what it regards to be anti-competitive behavior.

In the first quarter of 2004, licenses for Very Small Aperture Terminal (VSAT) services were made available, followed by licenses for national and international fixed voice and data services by the third quarter of 2004.

Licenses

In 2005, a total of 62 new licenses were granted by TRA for various service providers in Bahrain. Such a large number of new licenses were a record number so far as not so many licenses were issued in the past. Table below shows the types of license issued excluding the three temporary WiFi (wireless network) frequency licenses, which are discussed separately. In 2005, maximum 21 licenses were issued for individual international telecommunication services while 8 licenses were provided for Internet Service Providers.

Table 12: Licenses Issued in 2005

Licence	Service covered	Number issued
Individual License for National Fixed Services	Provision of national voice and data services via a fixed network owned and operated by the licensee	4
Individual License for International Telecommunications Services (ISL)	Provision of international voice and data services with specified bundling of traffic	21
Individual License for International Telecommunications Facilities (IFL)	Provision of facilities including termination, landing, international connection and connection to Bahrain licensed networks for international services	7
Individual License for Very Small Aperture Terminal (VSAT)	Provision of a digital satellite data network using an antenna with small diameter – for private use only	3
Class License for Internet Service Provider (ISP)	Provision of Internet services, not including voice	8
Class License for Value Added Services (VAS)	Provision of additional services over an existing network (eg. card transactions)	16

Source: TRA - Bahrain

WiFi Frequency Licenses

Recently, the TRA of Bahrain announced that it would be accepting applications for temporary WiFi frequency licenses. Holders of these licenses would be able to use the allocated frequencies for wireless internet services. Using this technology, customers can log into the web at ‘hot spots’ without using any wires or cords for the connection. This

step was taken to enable organizations and individuals providing this type of service to do so legally, while future policy on spectrum related issues in Bahrain was being decided. Three temporary licenses were issued to Batelco, Kalaam Telecom and 2Connect.

National Fixed Wireless Services (NFWS) Licenses Auction

The Board of Directors of the Telecommunications Regulatory Authority (TRA) approved on 6 July 2006 to conduct auctions for the award of the Fixed Wireless Access licenses. The two frequency licenses to be granted with the NFWS licenses authorize use of the following spectrum:

Frequency License I: 3410 MHz – 3455 MHz paired with 3500 MHz – 3545 MHz

Frequency License II: 3455 MHz – 3500 MHz paired with 3545 MHz – 3590 MHz

Spectrum Policy

TRA along with Ministry of Transportation recently published the spectrum policy for Bahrain. This outlined the availability of spectrum for additional mobile licenses showing available spectrums for both 2G and 3G.

In the world of modern telecommunications many services depend wholly or in part on wireless connections from mobile phone services to WiFi, and from public networks to private connections. New uses are being developed all the time. This makes the use and management of spectrum critical to the success of the telecommunications market. The Ministry of Transportation (MoT), Bahrain and the TRA published a joint consultation document on the future policy for the use and management of spectrum in the Kingdom of Bahrain. This took account of recent developments such as WiMax, fixed wireless access and the latest requirements for public and private mobile communications. It aimed to set a long-term policy which encourages the development of new technologies and promotes a fair market for operators and consumers.

The document covered issues such as the overall principles of spectrum management, spectrum pricing – including the issue of whether there should be auctions or ‘beauty contests’, for example – and likely demand for spectrum now and in the future. The MoT/TRA approach does not favour one technology over another – it is ‘technology

neutral’ – but does seek to stimulate innovation and growth in the market. Comments from both the industry and consumers were invited by December 21. After the end of the comments period, TRA and MoT will consider the responses received and then issue the final policy on spectrum for the Kingdom of Bahrain.

Third Mobile License

There is a wide discussion in the media regarding the issue of third mobile license in Bahrain. TRA has already initiated discussion about the viability of a third mobile operator in Bahrain. However, the existing mobile operators are expected to oppose this proposal of TRA by tooth and nail. In addition to this, small size of the Bahraini telecommunication market might also force TRA to rethink its decision of issuing third mobile operator license. With the issue of third mobile licenses, we don’t expect immediate threat to Batelco as the new entrant will have to fight hard to acquire substantial market share. It will also not very easy for the new player to penetrate the market in view of the strong competition from the incumbent operators.

Regarding the issue of new mobile licenses, TRA is exploring various options. TRA is looking for whether to issue one or more further licenses or whether such a license would be for a Mobile Network Operator or a Mobile Virtual Network Operator or both. TRA has fixed an aggressive time schedule for coming out with a final conclusion.

Licenses to Operate Wireless Telecommunications Networks

Bahrain's telecommunications regulatory authority, or TRA, fixed Nov. 28 as the date by which companies can bid for two licenses to operate wireless telecommunications networks. In an invitation to tender document, TRA said successful bidders will be announced on Dec. 13. The TRA has set the starting price of the auction of each National Fixed Wireless Services, or NFWS, license at BD20,000. The prospective licensees will also have to pay annual fees of BD28,000 to the Ministry of Transportation for the use of the 3.5 GHz wireless spectrum.

Successful bidders will be able to offer services directly to customers including local voice telephony, and subject to obtaining the additional relevant licenses, private internet services and international calls. Bahrain currently has one company offering the entire spectrum of telecommunications facilities, the incumbent Batelco. A second mobile

operator, MTC Vodafone-Bahrain, and three other companies, Kalaam, Menataalk and Startalk, also offer carrier pre-select options for cheaper international calls.

TRA-UAE and TRA-Bahrain Signed MoU

The UAE Telecommunications Regulatory Authority (TRA-UAE) signed a Memorandum of Understanding (MoU) with the Telecommunications Regulatory Authority of Bahrain (TRA - Bahrain) in early 2006 formalising cooperation between the two independent regulatory organisations. The MoU ushers in an era of co-operation between UAE and Bahrain, in the increasingly competitive world of telecommunications. In a globally interlinked world, communication technology is crucial to economic development and public governance. This MoU will go a long way in strengthening the regional telecommunications sector and will result in better services for the regional consumer.

The memorandum sets the grounds for TRA-UAE and TRA-Bahrain to exchange operational expertise and also share the use of each other's regulatory instruments. The telecommunications industry is increasingly vital to the Middle East's rapidly expanding economies and techno-savvy society. Regulators of both the countries aim to establish a regulatory framework that is robust and addresses the needs of the industry. The MoU is a progressive initiative that complements the already strong ties between Bahrain and UAE and will allow two authorities to benefit from each other's regulatory know-how and resources. Through the MoU, the two agencies have agreed to cooperate in areas such as licensing; Internet; telecommunications spectrum management; dealing with competition in fix net, mobile and Internet services markets; promotion of infrastructure development; laying down procedures for rules and the public process; determining regulatory approaches to anti-competitive behaviour in the marketplace; universal services; policies and interconnection. The MoU states that representatives of TRA-UAE and TRA-Bahrain will meet regularly and at least once a year in order to exchange data, research findings and technical information. These meetings will be held alternately in the UAE and in Bahrain. Under the terms of the MoU, the two authorities may exchange specialist staff and conduct training and development programmes for enhancing the level of expertise and skills of personnel from their respective organisations. Additionally, both the agencies have agreed to liaise with each other in their day-to-day operations.

6. Operators Profile

6.1 Bahrain Telecommunications Company

Overview

Bahrain Telecommunications Company (Batelco) was established as a monopoly in 1981 to provide telecommunication services in Bahrain. Batelco provides fixed line and mobile telephony services in Bahrain and data communication services in Bahrain and overseas. The company was one of the first companies in the region to reach full digitalization of its national and international public telephone switched network in 1992. In 1995, Batelco launched GSM and internet services (inet) and became the first telecom company in the Middle East to receive an ISO 9002 accreditation one year later. In 2000, the company provided Wireless Application Protocol (WAP). Batelco also provides Multimedia Messaging Service (MMS) and Global Packet Radio Service (GPRS), targeting both services to the younger population of the country.

In 2004, the company launched WiFi services allowing wireless high speed internet access through laptops and PDA's. Through its copper wire telephone lines, Batelco can also provide households with TV programs, internet access and telephone services all at the same time. This can be done through DSL technology that allows the bundling of these services at high speed. Batelco can provide around 93% of the Bahraini houses with this service. During 2004, Batelco started deploying Enhanced Data for Global Evolution (EDGE) technology through which customers can enjoy high speed data transfer, MMS and internet on their mobiles.

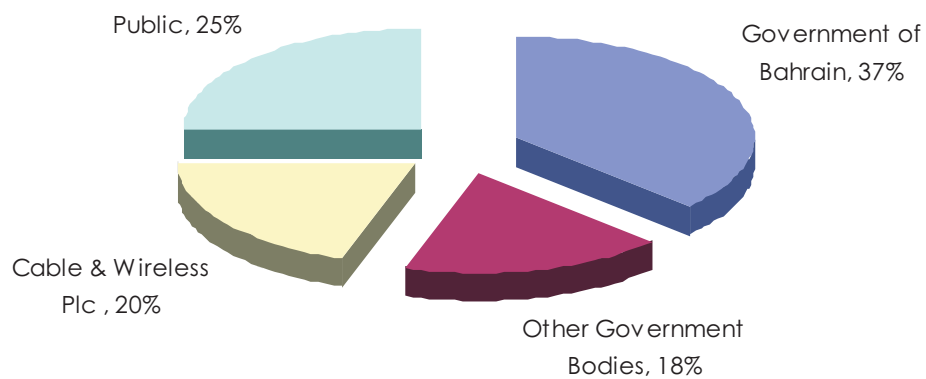
Management

The Board of Directors of the company comprised 10 members and is headed by Mr. Hassan Ali Juma. Batelco witnessed change in two key top management positions during the last one year. Mr. Tony Hart, Chief Executive Officer, left Batelco paving way for Mr. Peter Kaliaropoulos to the helm of Batelco. Soon after joining Batelco, Mr. Kaliaropoulos also brought his former colleague Mr. Chris Gabriel onboard as Chief Financial Officer forming the first non C&W team in Batelco.

Shareholding Pattern

As at the end of 2005, the Government of Bahrain held 37% stake in the company while other related government bodies held 18% of the company's shares. The global network operator Cable & Wireless Plc owns 20% stake in the company and the remaining 25% are accounted for by the public. Batelco was listed on the Bahrain Stock Exchange in June 1989. The company has joint ventures (JVs) to provide data services in other countries in the region such as Jordan, Egypt and Kuwait. Batelco operates in a duopolistic mobile market with MTC Vodafone Bahrain (MTC-VB) that entered the market at the end of 2003.

Chart 7: Shareholding Pattern of Batelco



Source: Company

Key Business Segments

Batelco is an integrated telecommunication service provider and provides wide range of mobile telecommunication services. Key business segments of the company included mobile telecommunication services, fixed line telephone services, data communications and internet services and messaging. Some of its major business segments are enumerated below:

a) Mobile Telecommunication Services

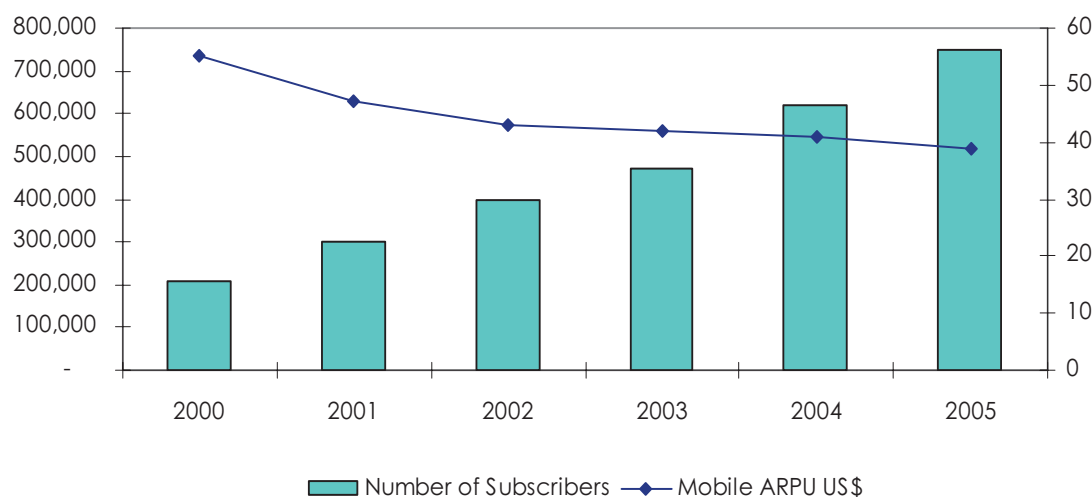
Under the mobile telecommunication services, Batelco provides following services:

- GSM PostPaid
- International Roaming
- Short Messaging Service (SMS)
- Prepaid Mobile Services (SimSim)
- Twin Sim Card GSM
- Paging
- Trunked Mobile Radio
- Mobile Fax and Data Services
- Mobile VoiceMail
- Mobile FaxMail
- Wireless Application Protocol (WAP)
- Thunaii (Two SIMs one number)
- Multimedia Messaging Service (MMS)
- International Multimedia Messaging Service (IMMS)
- General Packet Radio Services (GPRS)
- MSN Chat
- Freedata (Data Card)
- Bulk SMS
- SMS2TV
- Family & Friends Scheme
- GPRS International Roaming

- aywah Portal
- Prepaid International Roaming (2-way)

As mentioned above, Batelco offers comprehensive mobile services to its customers. Mobile telecommunication services is one of the major revenue contributors to Batelco in view of the high ARPU levels in the country. Mobile services contributed BD98.17mn to the total revenue of the company in 2005 as compared to BD95.37mn in the previous year, recording a growth of 2.9%. In 2004, revenue from mobile services rose by 9% over 2003. The number of mobile subscribers increased by about 37% in 2004 as compared to 2003 despite the onset of competition in 2004. Batelco also benefited from the increased subscriber base in 2004 as 43% of the new additions preferred Batelco as co. However, as MTC starts rolling out its mobile telephony in Bahrain customers get attracted towards it as a whopping 83% of the new subscribers preferred MTC over Batelco. Mobile subscribers are expected to continue to contribute substantially to the topline of Batelco. Large and increasing expatriate's population prefers mobile segment rather than fixed line telephones for their communication requirements.

Chart 8: Mobile Telephony and ARPU Levels



Source: Company Data

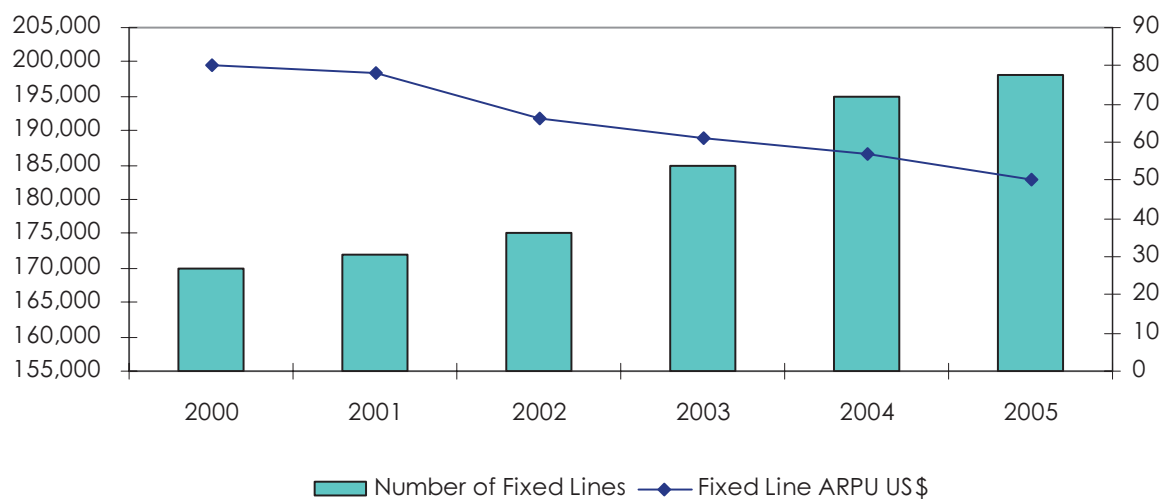
b) Fixed Line Telephony Services

Batelco offers the following services under the fixed line telephony category:

- International Direct Dialing (IDD)

- IDD Paid 800 Access
- International Operator Assist Services
- (151 and 191)
- National Telephony
- VoiceMail
- StarDial
- Fax Plus Services
- Caller Line Identification (CLI)
- Messaging Switching System (MSS)
- SMS on Fixed Line Service
- Prepaid Calling Cards
- Smart and Public Payphones
- Bahrain Direct (access to Bahrain from overseas)
- Home Direct (international access from Bahrain)
- Freeline (8000xxxx toll-free services)
- Audiotex (9000xxxx)
- PABX (Small, Medium and Large)
- Batelco Mobile Satellite Service

Cost-effective and innovative mobile services have forced customers to switch from fixed line telephony to mobile telephony. With the surge in mobile users, substantial part of Batelco's subscriber's base comprised mobile users rather than fixed telephone users. As a result, revenue from fixed line telephony has also witnessed substantial decline since the past few years. Revenue from fixed line telephony was BD51.6mn in 2003 which declined to BD47.5mn in 2005. In percentage terms revenue from fixed line telephony declined from 26.9% of the total revenue in 2003 to 22.4% in 2005. We expect the pace of decline in revenues from fixed line telephony to stabilize going forward. Batelco's decision to reduce international call charges from fixed lines is expected to enhance the outlook for this sector. In addition to this, other factors which can be potential revenue driver for this segment includes increase in personal computers and internet penetration in the country and the huge addition of office space. Both these factors are expected to contribute positively to the topline as well as bottomline of the company in future. Batelco is the only operator in the fixed line telephony in Bahrain and we do not see any serious threat in the fixed line market to Batelco in the near future.

Chart 9: Fixed Line Telephony and ARPU Levels

Source: Company Data

Batelco has recently launched a campaign for introducing access deficit charges and rate hike for compensating the losses which it is claiming to have while running fixed line services. Batelco may get a marginal rate increase in near future.

c) Data Communications and Internet Services

Batelco provides following broad services under the data communications category.

- LANConnect Service (Frame Relay)
- Local Leased Circuits
- Global Frame Relay
- Very Small Aperture Terminal (Vsat)
- Global Managed Private Line (GMPL)
- International Private Leased Circuits (IPLC)
- Datacenter
- Customer Premise Equipment (CPE)
- Broadcast
- Managed LAN Connect
- Integrated Service Digital Network (ISDN)

- Multi-Protocol Label Switching (MPLS)
- Global Multi-Protocol Label Switching
- (Global MPLS)

Under the Internet services and messaging segment, Batelco's services includes following services:

- Dial Direct
- inet ISD
- inet 900
- Internet Broadband
- inet Roaming
- inet PrePaid
- Integrated Messaging Services (IMS)
- Broadband PC
- Web hosting
- inet Dedicated Access
- WiFi Services
- Telex and Telegrams
- Maritime Services
- inet Advertisement

Leased Circuits

Leased circuits segment is the rapidly growing segment of Batelco. It contributed BD23.6mn to the total revenue of the company in 2005 as compared to BD21.3mn in the previous year, recording a growth of 10.6% over the previous year. In percentage terms, leased circuits contributed 11.2% to the total revenue of Batelco as compared to 10.5% in 2004. Thus, leased circuit segment becomes the fourth largest contributor to the total revenue of the company in 2005. We expect the growth in revenue from leased circuits to remain in double digits at least for next couple of years. The booming real estate commercial sector and the new companies that are coming up in Bahrain will keep the demand for these segments higher.

Internet Services

Internet segment of the telecommunication industry is one of the major growth drivers globally for telecom operators. Aware of this Batelco also see this segment as the future growth engine and which needs to be tap in to penetrate the market. Revenue from internet services grew at a robust rate of 22% in 2005 and reached BD32.5mn as compared to BD26.5mn in the previous year. Internet services recorded highest year-on-year growth in 2005. It is the third highest contributor to the total revenue of the company in 2005 as its contribution to the total revenue stood at 15.3%.

In its efforts to tap this segment and enhance the penetration levels as well as revenues from this segment, Batelco recently restructured its packages and lowered the price of entry-level packages to make internet more affordable for large part of the population. Batelco eliminated the unlimited usage ADSL packages from their offering, and forced everyone to migrate to the new packages and risk paying additional fees. However Batelco's effort to bring in download limits met with strong opposition from existing high user customers and even saw a widely publicised "Boycott Batelco" campaign which substantially damaged the brand equity and loyalty created by the company over the years. Batelco is also fighting with TRA to get approval for its entry package. However, TRA see this as pre-emptive strategy by Batelco to prevent competition coming in this category when new players are trying in to enter this area. Most of the new players may find it difficult to enter into a price war at early stages.

Wholesale and Interconnect Services

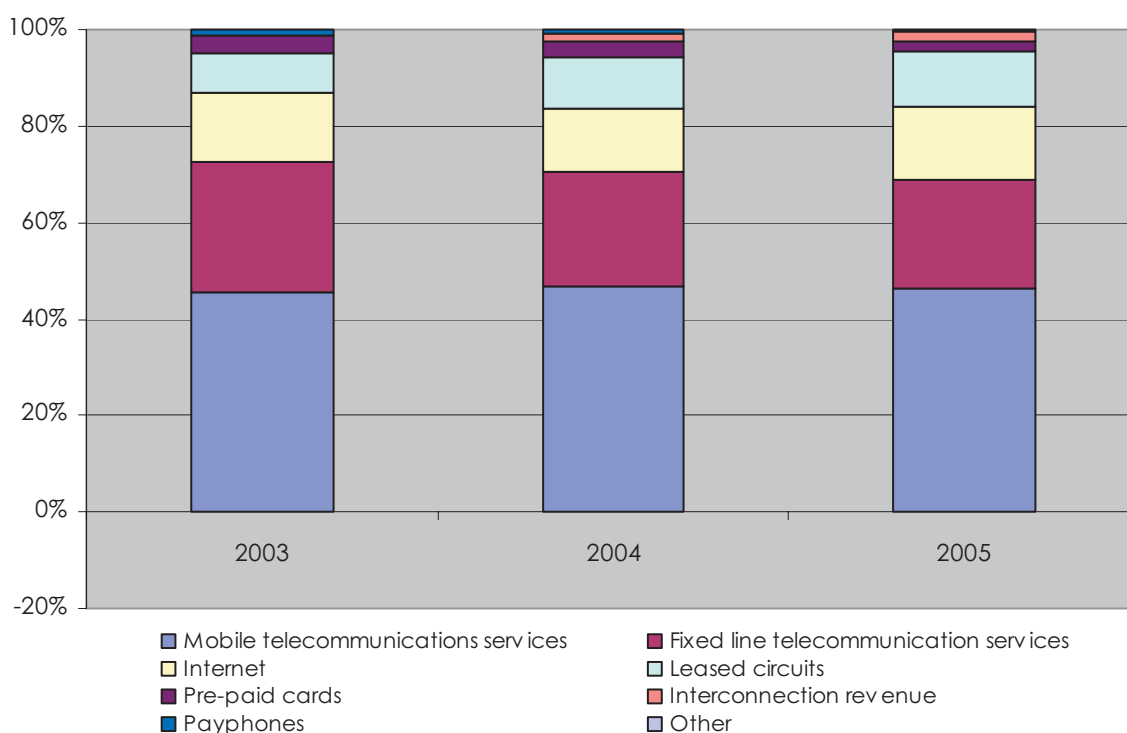
Wholesale and interconnect services is the new segment, which has started contributing to the revenue stream of the company since the past two years. Batelco is the dominant player in most of the services offerings in Bahrain. This segment contributed BD4.6mn to the total revenue of the company in 2005 as compared to BD3.75mn in the previous thus recording a growth of 22.2%. This contributed around 2.2% of total revenues of Batelco in 2005. Batelco is expected to offer wholesales products to other licenses holders and interconnection with its network to ensure competition. This revenue stream is expected to increase further.

Pre-Paid Cards and Payphones

Pre-paid cards and payphones segment of the company is losing its popularity. The increased use of mobile services and competition from VoIP services has reduced the revenue from these services considerably. The revenue from this segment has been declining consistently since the past few years. Revenue from pre-paid cards declined by 36.1% in 2005 over the previous year and stood at BD4.3mn as at the end of 2005. Revenue from pay phones has also been declining since the past few years. It declined by 14.5% in 2005 over the previous year and stood at BD0.95mn. We expect further decline in revenues from pre-paid card and payphone segment.

During the last few years the importance of various segments in Batelco's operation has changed significantly. Fixed line services, which used to contribute a major part of the revenues earlier, have given way for fast growing mobile services. The new services such as internet and leased circuits have started contributing significantly to top line. As seen in the chart, during 2003-2005, major part of growth came from Mobile services, followed by leased circuits and internet and data communications.

Chart 10: Revenue mix of Batelco



Source: Company

Joint Ventures

In an effort to expand its services, Batelco has entered into several joint ventures in the region to provide data services to multinationals through Batelco Middle East Co (BMEC). BMEC is the holding company through which Batelco manages its operations in the region. The company's aim is to be the no. 1 choice service provider for multinationals in the region capitalising on its global partner's experience in data communications services. The four JVs are discussed briefly below.

a) QualityNet – Kuwait

QualityNet is the most established of Batelco's joint-venture operations. Batelco held 44% stake in the company. QualityNet was established in 1998 in response to a public offering by Kuwait's Ministry of Communication, as part of a strategy to privatise internet and data communication services in Kuwait. QualityNet seized the opportunities offered by the emerging new telecommunications technologies to provide a total solution for new generation networks with strategic partnerships and innovative solutions. A rich pedigree and an impressive depth of expertise have allowed the company to move swiftly and nimbly, repositioning itself to meet the challenges of an era of convergence.

Despite the introduction of three competitors in the marketplace, QualityNet remains the market leader in terms of both its internet business and data communications services and continues to be the main service provider to government and the business community in Kuwait City. Major achievements include a project with the Ministry of Education in Kuwait to establish a network initially linking 300 schools. QualityNet also delivers services to the US Embassy by providing an International Private Leased Circuit service to the UK.

b) Batelco Jordan – Jordan

Batelco Jordan was formed in 2001, following the merger of National Equipment Telecommunications Systems (NETS) and First Telecommunications Group (FTG) with Batelco. The company capitalised on the experience by NETS for internet content, the provision of data communications services by FTG and Batelco's experience worldwide. Batelco Jordan has emerged as the country's industry leader since the past few years.

Batelco Jordan's services extend beyond dial-up subscribers to include Broadband Internet, managed data services, leased lines, online solutions, interactive content, web design/hosting and Internet-based solutions and technologies for both individuals and corporations. During 2005, Batelco Jordan started to provide Voice over Internet Protocol (VoIP services) by introducing 'Donya' an international calling card, the first of its kind since the liberalisation of the telecoms market in Jordan.

c) Batelco Egypt Communications – Egypt

Batelco Egypt Communications (S.A.E.) is a wholly owned subsidiary of Batelco Middle East and was established in August 2003 in Cairo as an Egyptian Joint Stock Closed Company. The company was established with an authorised and paid-in capital of EGP30mn and EGP3mn, respectively. The company obtained a public data network license from the Telecommunications Regulatory Authority in October 2003. Initially, the focus was on providing worldwide telecommunications services to corporate and multinational customers that already used the Cable & Wireless Global Frame Relay service and that have a presence in Egypt. The managed global frame relay service, managed international private lines service and a global Internet access service, combine to form part of the company's one-stop shop service, in a bid to cater for all of its customers' global needs.

d) Arabian Network Information Service (ANIS)

Arabian Network Information Services (anis) is a leading regional systems and network integrator that is solely owned by Batelco and is the vehicle through which Batelco approaches the ICT market in Bahrain and in the region. The company's expanding client list includes the banking and finance industry, government, oil and large enterprise sectors, hospitality groups and major real estate projects in Bahrain. By developing core offerings in selling solutions that straddle the telecoms and IT markets, anis aims to service the ICT requirements of Batelco's existing business customers and new 'greenfield' site developments.

By entering into partnerships with communication companies in the region and world, Batelco reaps significant dividends in terms of technological know-how, shared best practice and market-leading new products. Batelco's vast experience gained over many years in the telecommunications industry coupled with its unrivalled and ever increasing

list of new products and services places it in prime position to be the communication provider of choice for individual customers, for business clients and multi national companies in the region.

By enhancing its market position at home and in combination with its joint ventures in Egypt, Kuwait and Jordan, the company can establish a solid platform to support its regional offerings. Batelco's unique ongoing working relationship with global network operator, Cable & Wireless provides the company with a clear advantage over the competition and guarantees that its customers continue to enjoy global reach using one of the world's most advanced networks. Batelco's wholly owned subsidiary, Arabian Network Information Services (anis) which provides state-of-the-art customised Internet, Intranet, extranet and e-business solutions is a new bow in its arrow that aims to become a trusted name in the business world.

Strategic Initiatives

In an effort to transform the company into a customer-oriented and commercially driven institution, Batelco has embarked on a "Project Get Ready" program in 2002 with the aid of an international management consultancy firm, AT Kearney. The project focuses on areas that require major improvement such as customer service, network efficiency, human resource allocation, mobile services, sales and marketing including a change in the corporate identity. This move to restructure the company is similar to those of other telecom peers in the region who embarked on their restructuring programs way before competition started in their markets. Batelco started slashing tariffs and becoming more aggressive at the marketing level only in 2003. Batelco was a late mover in responding to the competition. However, the market responded very strongly to both mobile operators' efforts to expand the market. With the onset of competition, Batelco has initiated number of measures to stay on course and has initiated aggressive strategies to penetrate the market further and to boost the revenues.

Competitive Strength

Telecom operators in the MENA region adopted two pronged strategy to thwart the competition with the liberalisation of the sector. The first part of the strategy was concentrated on improving their domestic operations while the second part of the strategy was to explore emerging opportunities in the region in an effort to expand its footprint

beyond their domestic operations. Batelco also used the same strategy to drive its growth. The restructuring efforts and the “Project Get Ready” program undertaken by Batelco in 2003 and 2004 helped Batelco to increase efficiencies and helped margins in the short term however the company needed a much required face lift and change in attitude to win in a competitive world. Batelco undertook an extensive re-branding exercise projecting as a “home grown brand” and stressing on its changing face to become more customer friendly. The pain of competition was most felt in the mobile telephony services with the entry of MTC.

Batelco’s efforts to grow beyond the borders of Bahrain did not produce any encouraging results. The conservative management style and the focus on organic growth limited its capacity to tap various opportunities that came up in the region. While its peers in the region moved ahead with aggressive strategies, Batelco was confined to Bahrain and its joint ventures.

The management of Batelco plans to transform the company’s competitiveness in the market and to deliver better technologies at more reasonable prices. This initiative of the company is well under way and is now the driving force within every department of Batelco. In a rapidly changing economic environment and one in which innovations in technology is a routine occurrence, Batelco trying to meet its targets, rising above any obstacles to offer a world class basket of products that caters to the needs of residential and business customers. Batelco’s continuing performance is attributable to a combination of strategic vision and inspired planning.

New Investment

Batelco continued to invest in new initiatives and during 2005 the company committed substantial investment to upgrade its current offerings and introduce new ones. A sum of around BD21mn has been earmarked toward Batelco’s broadband Bahrain initiative which is designed to ensure that the enormous potential of the worldwide web of information is available to the residents of the Kingdom, with faster and more affordable internet access.

The company’s investment of BD35mn in the new FLAG Telecom’s FALCON cable system will also contribute in a big way to delivering a better product for its customers by providing a superior connectivity than is possible currently. In addition, the extension of the MPLS networks, mobile network upgrade, major Data Centre Project, the company’s

desire to extend its VoIP services and a range of additional products and services are all designed to ensure that the company continue to add value for customers and remain a driving force in the success of the Kingdom's economy.

More Affordable Charges

The company reduced the charges for broadband business packages and usage towards the end of last year. Broadband business packages were reduced by up to 43% and broadband business usage slashed by 50%. The company believes that the reduced prices are the most competitive in the GCC market and which is in line with the Batelco's aim to transform the company's competitiveness, while continuing to deliver a better customer experience. In recent years, the company delivered significant product and service enhancements to its customers and during 2006 through key strategic imperatives the company is expected to continue to build on that solid foundation.

Customer Service – Critical Priority

To improve customers' satisfaction and loyalty the company is embarking on continuous process improvement based on Lean Sigma and Six Sigma initiatives. Prime objective of the company is to simplify all its processes allowing customers to acquire new services and transact with the company for support in a responsive, convenient and effective way. A sound relationship with the customers is also based on innovation and better value. The company is delivering innovative products and services such as Mobile Office and has introduced very competitive price plans for IDD, mobile and broadband - among the most competitive in the Gulf region.

Innovation and investment – fundamental to success

By continuing to invest in state-of-the-art telecommunications infrastructure, Batelco is providing the digital backbone of the Kingdom. Initiatives such as the new e-Government portal based on leading edge IP technology is an example of Batelco's commitment to further enable electronic commerce. Other major projects, with a commitment of over BD70mn investment, critical to the continued development of Bahrain's national economy, include investing in Mobile Office wireless email solutions, new Data Centre facilities, Broadband Bahrain – increasing Bahrain's broadband penetration, mobile coverage upgrade and the FALCON Cable project to provide diverse access and high rate transmission from Bahrain to major cities and business centres around the world.

Broadening Horizons to Accelerate Growth

Batelco's growth overseas continues to evolve with its joint ventures in Kuwait, Egypt and Jordan flourishing. A key achievement in recent years was Batelco Jordan being awarded the country's first individual fixed license in a move that kick-started the liberalisation of Jordan's telecoms market. Currently, the company is deploying its infrastructure and is offering voice services to complement its data solutions. QualityNet in Kuwait recorded another strong performance in recent years and is poised to enter a new growth phase by its entry into ICT services in Kuwait. Batelco Egypt is currently exploring various possibilities resulting from further imminent liberalisation in Egypt.

ANIS has evolved from a web development operation into a network centric, ICT services and solutions company, leveraging opportunities based on VoIP technologies and managed services. ANIS is expected to focus on developing strong partnerships with leading IT companies to deliver network management and systems integration services. Batelco is expected to continue to explore appropriate investment opportunities across the MENA region for new licenses as the market deregulates and to acquire existing business operations.

Improving Operational Effectiveness

In the last quarter of 2005, Batelco launched a series of initiatives to improve its overall operational performance. "Reaching Peak Performance" initiatives are designed to transform Batelco into one of the most competitive and high performing companies in the Gulf region. One such initiative resulted in the re-alignment of Batelco into customer focused operating divisions aimed at delivering end-to-end services to consumer, business and government and wholesale customers.

Hi-Tech Business Solutions

Batelco launched the Batelco Mobile Office (BMO) service, which offers customers a high-tech solution, providing people on the move, secure and wireless access to their corporate e-mail while they are out of the office. BMO is designed to give customers access to business critical information such as e-mail and documents while they are on the move, enabling companies to benefit from a workforce that is flexible, more

productive and better connected. Organisations using Lotus Notes or Microsoft Exchange environments can make use of this service, which is also known as ‘Push Technology’.

A new unit called Batelco Business Solutions (BBS) was also launched in 2005. BBS is designed to help meet customers’ Information Communication Technology needs and offers a full range of professional services from presale business and technical consultancy to post-sale implementation and management. The service was launched in direct response to market needs and has already been given big thumbs up by one of the country’s most high profile organisations. Through Batelco Business Solutions, Batelco is again providing Bahrain’s telecommunications market with a unique, high-tech comprehensive service that will help customers meet their business objectives.

Collaborations

Batelco has joined a group of five Bahraini companies to set up a new M-Commerce service, which is designed to enable customers to conduct financial transactions using their mobile phones together with the telecoms infrastructure and banking systems. Batelco, Ahli United Bank, American Express, The Benefit Company and On Air Commerce Company have joined hands in a partnership. The project will ultimately enable customers to use their mobile devices to pay utility bills and settle credit card statements, along with offering the ease and convenience of conducting ATM and banking transactions such as balance checking and fund transfers while on the move. In line with its commitment to offer world-class and innovative services to customers, Batelco has selected Ericsson to upgrade its GSM Core, Radio and Service Networks. Under the agreement, Ericsson will enhance Batelco’s GSM network coverage and capacity for both voice and data services, boosting their existing nationwide high speed EDGE data access capabilities. The expansion of the mobile network’s capacity and the launch of new mobile services such as video streaming are also part of the agreement. These new offerings will allow Batelco to fulfill the ever changing needs of subscribers.

New Retail Outlets

In addition to the University of Bahrain Batelco Student Centre shop, Batelco also opened its newly transformed Isa Town Shop, the eighth newly branded retail unit opened by Batelco over the last two years. The development programme started with the opening of Batelco’s Seef Mall outlet in February 2004 and has been followed by

openings at Bahrain International Airport, Al Alawi Complex, Hamad Town, Arad, the Batelco Commercial Centre outlet in the heart of the Manama souq, and the UOB Student Centre.

New Services

Batelco launched its new GPRS and MMS roaming service, giving customers who are travelling abroad the ability to stay in touch with others via a host of extra mobile services including pictures, video clips, e-mail and access to the Internet. Postpaid customers who have MMS enabled handsets with MMS/GPRS settings are able to use the full service while travelling to a range of popular regional and global destinations. Old public phones have been replaced with brand new high-tech payphones throughout the Kingdom. The new phones use Smartcard technology and offer the very latest advances in payphone communications options. New high-tech multimedia phones have also been installed in key areas including Bahrain International Airport. The cutting edge multi-lingual multimedia touch-screen phones allow users to make phone calls, send faxes and emails, utilise SMS messaging facilities, check out international news and browse the Internet - all in a quick and easy to use format with the aim of making communications better, quicker and more reliable for the Kingdom's payphone users.

DataCentre Project on Course

Batelco signed a new BD3mn initiative which will provide customers with secure off-site data storage, complete with national and international connectivity. Batelco's DataCentre is designed to help meet a growing requirement for businesses to secure their data and ensure access to vital records via a state-of-the-art facility that offers disaster recovery services. The world-class Batelco DataCentre will allow business customers to host their own equipment and electronic records within a secure environmentally controlled fire safe facility that ensures round the clock access all year long.

Expanding across the Border

Batelco Jordan was awarded the country's first individual license in a move that kick-started the liberalisation of Jordan's telecoms market and paved the way for further developments in the Middle East's communications industry. Batelco Jordan is now poised to provide a cutting edge service to its new customers by capitalising on the latest

technological developments to build a state-of-the-art infrastructure that integrates voice, video and data and provides a host of new and exciting services. At present, Batelco Jordan is the country's leading data communications and web development and hosting provider, serving tens of thousands of Jordanians and catering to all sectors of the economy, ranging from individual prepaid Internet subscribers to the largest multi-nationals. Batelco customers can now receive up to the minute breaking, business and sports news through the new Al Jazeera Mobile Short Messaging Service, thanks to a new partnership with Qatar's Al Jazeera Channel and Al Majaz Telecom.

Strategic imperatives for the future

Batelco's strategic imperatives for the future included the following:

- Continually improve and lead market in customer satisfaction
- Accelerate growth by focusing on broadband and mobile services
- Expand into new markets across Middle East and North Africa (MENA) region
- Create and deliver network centric ICT services and solutions
- Improve competitive advantage through cost leadership and process re-engineering
- Create high performance culture based on personal leadership where everyone is motivated to succeed

Batelco Dominates the Market Player

Despite the onset of competition, Batelco continues to be the dominant player in Bahrain having operations in most of the product categories. Being incumbent player in Bahrain, Batelco was at advantageous position as compared to MTC. Even though Batelco faced serious threat from MTC it was able to continue as the market leader with close to 75% market share. In fixed line services Batelco continued to be the only player and there is no immediate threat to Batelco in this category. Batelco faced serious threat mostly from companies providing calling cards for making international calls at significantly lower rates compared to Batelco. This has affected Batelco's revenue from international calls as majority of expatriates from Indian subcontinent, East Asia and African countries used these cards substantially. Despite the recent reductions of tariffs on international calls, calling cards are still the cheaper. Batelco need to come up with alternate strategies to counter this if the company is eager to acquire additional customers. Batelco's effort to increase internet penetration by slashing entry level rates met with opposition from TRA

as it viewed this as anti competitive move by Batelco to eliminate possible competition in the future.

Batelco buys Jordan's Umniah

Batelco acquired a majority shareholding in Umniah Mobile Communications, holder of Jordan's third mobile license, for US\$415mn. Umniah was awarded its license in 2004 and started commercial operations in June 2005. Umniah has about 500,000 subscribers and a market share of around 13%. Batelco acquired the 96% stake from a group of Kuwaiti investors including Alghanim Group and Global Investment House.

The acquisition is Batelco's company's first major venture overseas. The acquisition will take Batelco head-to-head in a second market with Kuwait's MTC, which owns Jordan's second mobile operator, Fastlink. MTC is also the second GSM license-holder in Bahrain. The other Jordanian provider is Mobilcom, a subsidiary of state-owned Jordan Telecom. Batelco already operates limited fixed-line services in Jordan. Regional expansion is high on Batelco's agenda as it responds to the introduction of competition at home. Umniah will contribute positively to Batelco's revenues and profits.

Financial Performance of Batelco

Asset Structure

The total assets of Batelco stood at BD396.8mn at the end of 2005, representing a jump of 9.5% over the previous year. Current assets comprised 52.33% of the total assets while non-current assets comprised the rest. The composition of current assets was heavily tilted towards cash and cash equivalents, while property, plant & equipment dominated non-current assets. Investments accounted for less than 10% on the company's Balance Sheet.

Analysis of the current assets reveals that cash and cash equivalents accounted for 78.9% of total current assets, while accounts receivable and prepayments comprised 19%. As a percentage of total assets cash and cash equivalents accounted for 41.3% at the end of 2005. Inventories and amounts due from other telecom operators were virtually insignificant. The structure of current assets remained almost the same as in 2004, though in absolute terms, they grew by 20.1%. Property, plant and equipment comprised over 80% of non-current assets and 38.8% of total assets. If intangible assets, of nominal value, are ignored, the rest of the non-current assets were made up of investments. At the end of 2005, investments stood at 8.8% of total assets, up from 6.6% in 2004. Meanwhile, the structure of non-current assets remained stable through 2005.

Share Capital and Shareholders Equity

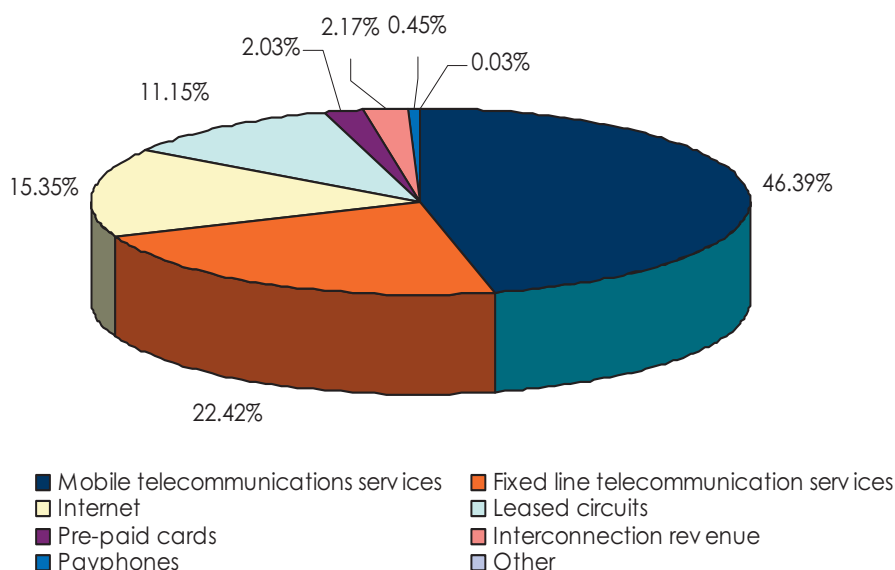
Total share capital of the company stood at BD100mn at the end of 2005. Total shareholders equity of the company stood at BD335.6mn at the end of 2005 as compared to BD299.8mn in the previous year representing a growth of 11.9%. Growth in shareholders' equity was principally due to an increase in retained earnings. During 2005,

retained earnings climbed to BD168.7mn from BD141.3mn a year ago. As of Dec 05, Batelco was a zero-debt company with a capital structure consisting of only equity. In February 2006, Batelco made a bonus issue of one share for every five shares, as part of its dividend for 2005; pushing its share capital further to BD120mn. The company also obtained an approval from its shareholders to increase authorized capital to BD200mn.

Income Statement

Batelco recorded modest performance in 2004 and continued its growth momentum in 2005 as well. In 2005, the total revenue of the company grew by 3.9% to BD211.6mn as compared to BD203.7mn in 2004. Other income of the company rose sharply by 158.2% in 2005 and stood at BD14.4mn. The sharp rise in other income was primarily due to sharp rise in investment income, interest income and gain on sale of investments. Total expenses of Batelco grew by 9.4% in 2005 to reach BD137.3mn. The net profit of the Batelco group before appropriations amounted to BD87.5mn in 2005 as compared to BD83.7mn in 2004, representing a growth of 5.85%. Basic Earnings Per Share (EPS) of the company rose from 83 fils in 2004 to 88 fils in 2005.

As net profit grew, net profit margin moved up to 41.9% in 2005, marginally higher than the 41.1% registered the year ago. However, return on assets and return on equity declined during the year. Return on assets fell to 22.3% in 2005 from 23.1% reported a year ago, while return on equity dropped to 26.4% in 2005 from 27.4% in 2004. Batelco rewarded its shareholders with a dividend of 45 fils a share and a bonus issue of one share for every five shares held.

Chart 11: Revenue Mix of Batelco for FY2005

Source: Consultia Analysis, Company Data

Financials Results – First Nine Months 2006

During the first nine months of 2006, total assets of the company stood at BD450.5mn, representing a growth of 16.4% over Dec 05 figures. Non-current assets comprised 83.6% of the total assets in Sep 06 as compared to 48.1% as of Dec 05. Current assets of the company declined substantially to BD74mn as at the end of Sep 06 as compared to BD200.8mn as at the end of Dec 05. The substantial decline in current assets was mainly due to sharp reduction in cash and cash equivalents of the company which decreased from BD162.7mn at the end of Dec 05 to BD29.1mn in Sep 06. The company borrowed BD8mn during the first nine months of 2006.

The total revenue of the company rose by 6.3% to BD170.14mn during the first nine months of 2006 as compared to the same period previous fiscal. Total earnings of Batelco was up by 8.7% to BD71.7mn as of Sep 2006 over Sep 05 figures. The company reported an Earnings Per Share of 59 fils as at the end of Sep 06 as compared to 54 fils in Sep 05.

Table 13: Balance Sheet of Batelco

BD '000	2004	2005	% Change
Property, plant and equipment	153,277	154,084	0.5%
Intangible assets	623	-	
Investments	23,821	35,039	47.1%
Total non-current assets	177,721	189,123	6.4%
Inventories	590	587	-0.5%
Accounts receivable and prepayments	40,170	39,494	-1.7%
Amounts due from telecommunications operators	7,513	3,786	-49.6%
Cash and cash equivalents	136,369	163,822	20.1%
Total current assets	184,642	207,689	12.5%
Accounts payable and accruals	49,342	49,981	1.3%
Amounts due to telecommunications operators	7,095	4,847	-31.7%
Total current liabilities	56,437	54,828	-2.9%
Net current assets	128,205	152,861	19.2%
Net assets	305,926	341,984	11.8%
EQUITY			
Share capital	100,000	100,000	0.0%
Statutory reserve	43,518	51,746	18.9%
Other reserves	15,070	15,146	0.5%
Retained earnings	141,251	168,713	19.4%
Total equity attributable to shareholders of the parent company	299,839	335,605	11.9%
Minority interest	6,087	6,379	4.8%
Total Equity	305,926	341,984	11.8%

Source: Company

Table 14: Income Statement of Batelco

BD '000	2004	2005	% Change
Revenue	203,764	211,616	3.9%
Other income	5,581	14,411	158.2%
	209,345	226,027	8.0%
Expenses			
General and administrative	99,002	95,208	-3.8%
Other expenses	26,561	42,134	58.6%
Total Expenses	125,563	137,342	9.4%
Profit for the year	83,782	88,685	5.9%
Attributable to :			
Shareholders of the parent company	82,584	87,502	6.0%
Minority interest	1,198	1,183	-1.3%
	83,782	88,685	5.9%
Basic earnings per share	83	88	6.0%

Source: Company

Table 15: Ratio Analysis

	2004	2005
Return on assets (%)	23.1	22.3
Return on equity (%)	27.4	26.4
Earnings per share (fils)	83.0	88.0
Total assets turnover (x)	0.56	0.53
Net profit margin (%)	41.1	41.9

Source: Consultia Analysis, Company Data

6.2 Mobile Telecommunications Company (MTC)

Mobile Telecommunications Company (MTC) was established in 1983 in Kuwait as a joint venture between the government of Kuwait (49%) and private sector investors (51%). Listed on the Kuwait Stock Exchange, MTC's market capitalization exceeded US\$14.5bn as of September 30, 2006. There are no restrictions on MTC shares as the company's capital is 100% free float and publicly traded. The largest shareholders are the Kuwait Investment Authority (24.6%) which is a government controlled entity, and National Investment Company (18.5%).

MTC is the pioneer of mobile telecommunications in the Middle East and now a major player in the African continent. The company started providing mobile and paging services in Kuwait in 1985. MTC launched GSM services in Kuwait in 1994 and was privatized in 2001. MTC offers the entire range of mobile telecom services with the latest and technologically advanced services in order to maintain a competitive edge and retain its strong brand image. In December 1999, MTC monopoly in Kuwait came to an end with the launch of mobile services by National Mobile Telecommunications Company (Wataniya Telecom). In view of maturing mobile market in Kuwait and helped by on going deregulation in the region, MTC has expanded operations organically and by acquisitions to become a truly regional operator. In March 2005, MTC acquired Celtel International, a Dutch communications network company with major interests in 13 Sub-Saharan African countries, in one of the biggest telecom deals in the Middle East and Africa worth US\$3.36bn.

Management

At the 2005 annual assembly of shareholders in March 2005, a new Board of Directors was elected. Mr Asa'ad Al Banwan has taken the reigns as Chairman and replaces Mr Ahmed Al-Nassar who completed his many years of successful service in MTC. Headed by Dr Saad Al-Barrak the executive management team is entrusted with carrying out and implementing the necessary reforms in order to meet the targets and vision that is set by the Board of Directors and shareholders. The team closely oversees all MTC operations as well as seeking out new growth opportunities.

Strong Regional Presence

The company began operation in 1983 in Kuwait as the region's first mobile operator, and since the initiation of its "3x3x3" expansion strategy in 2002, it has expanded rapidly. MTC now operates across 6 Middle Eastern and 14 sub-Saharan African countries with 12,000 employees providing a comprehensive range of mobile voice and data services to over 24.9mn (September 30, 2006) individual and business customers. MTC operates in Kuwait and Bahrain as MTC-Vodafone, in Jordan as Fastlink, in Iraq as MTC atheer, in Lebanon as MTC touch, in Sudan as Mobitel and in 14 sub-Saharan countries in Africa as Celtel : Burkina Faso, Chad, Democratic Republic of the Congo, Republic of the Congo, Gabon, Kenya, Madagascar, Malawi, Niger, Nigeria, Sierra Leone, Tanzania, Uganda and Zambia.

Corporate Strategy

The business strategy of MTC focuses on combining value creation and internal growth from existing operations with aggressive expansion into new geographies. To pursue this strategy MTC is building on four strategic elements:

1. Mass market focus and segmented customer strategy

MTC is focusing on the mass market addressing at least 70% of the market – both in terms of subscribers as well as segment value. The subscriber growth will be generated through aggressively targeting under-penetrated segments, whereas value growth will come from the existing customer base. The aim of the company is to reach 50% market share in markets where MTC is a "leader" and a minimum of 30% market share in markets where MTC is a "challenger."

2. Competitive positioning and differentiation strategy

MTC's differentiation approach is not only focused on pricing, but a combination of differentiated elements of value proposition. The company believes that its competitiveness derives from the adoption of a fully segmented market approach. This approach clusters customers into value segments and addresses all of them - both high-end as well as low-end customers - with distinguished propositions. To further build out its competitive positioning, the company also selectively expands into new businesses within the wireless value chain while focusing on areas that generate value for MTC.

3. High-value technology strategy

The company constantly explores latest technologies. The company only invests in commercially viable wireless technologies that enable the provision of a full range of services that at the same time add value both internally and to end-customers. While using technology as one of the key enablers of differentiation, the company ensures that innovation is not only technology driven, but also an internal philosophy adopted throughout the organization.

4. Company management strategy

The company adopted a people-oriented culture and organisation where it promotes collaboration among the group, local operations and functional areas – aiming at synergy realisation and excellence. MTC provides a merit-based working environment which rewards and empowers employees in line with their performance.

Global Strategy

MTC's corporate strategy can simply be summarized as "3x3x3", an ambitious, sustainable expansion strategy that is expected to see MTC become a leading mobile and lifestyle services provider on the global stage by the end of the year 2011. This strategy was initiated in year 2002. The company believes that this strategy will make MTC a global player in three stages: regional, international and global, with each stage completed in three years, with an aim of reaching a subscriber base in excess of 50mn. In essence, through acquisitions, partnerships and green-field opportunities, MTC aims to achieve in nine years what other companies have taken more than 27 years to achieve.

Association with Vodafone

MTC's relationship with Vodafone extends only to two countries, Kuwait and Bahrain. The agreement allows MTC Kuwait and Bahrain customers to access their home services when roaming abroad on any of Vodafone's networks and to access Vodafone's global products and services. The Partner Network Agreement established in September 2002 with Vodafone fully supports the MTC's vision. Vodafone is the world's largest mobile community with over 451 million venture customers across five continents. By partnering with the leading, world-class operator Vodafone, MTC is able to gain invaluable business knowledge and practices. Elsewhere MTC is competing with Vodafone for new markets.

MTC is constantly seeking to forge partnerships with key global companies to bring the best products and services to its customers.

At the end of September 2005, MTC embarked upon an extended and modified co-branding agreement. The new one-year renewable contract between the two parties has put in place a 'segmented dual branding' leading to a co-branding only at the points of entry of the country (such as the airport) and for co-launched products. MTC's partial exit from its relationship with Vodafone is part its global strategy to re-brand all the group's entities under MTC brand name. The group will first start in the Middle East with Kuwait, Bahrain, Iraq and Jordan and then will continue with Celtel. The total re-branding should take up to three years with the integration of Celtel taking place not before two years.

Customer Base

MTC is having customer base of around 24.9mn as at the end of Sep 2006 in the Middle East and Africa region. The company's customer base grew at a robust rate during the past one year and it showed a growth of 100% over Sep 05 figures. In Bahrain, MTC has a subscriber base of 279,000 at the end of Sep 06 as compared to 190,000 during the same period last year, thus recording a growth rate of 47% during the period. In the Middle East, MTC has a subscriber base of 9.62mn at the end of Sep 2006. Following is the customer base of the company as at the end of Sep 06.

Table 16: Customer Base of MTC

Managed Customers (000s)	Q3 2006	Q3 2005	Growth
Bahrain	279	190	47.0%
Iraq	2,441	925	164.0%
Jordan	2,364	1,732	36.0%
Kuwait	1,513	1,394	9.0%
Lebanon	568	501	13.0%
Sudan	2,462	-	
Middle East Total	9,626	4,742	103.0%
Burkina Faso	441	238	86.0%
Chad	308	182	70.0%
Congo Brazzaville	570	304	87.0%
Democratic Republic of Congo	1,705	949	80.0%
Gabon	479	288	66.0%
Kenya	1,743	1,461	19.0%
Madagascar*	302	-	
Malawi	312	151	107.0%
Niger	343	166	107.0%
Nigeria**	5,993	-	
Sierra Leone	202	137	48.0%
Tanzania	1,349	738	83.0%
Uganda	381	233	64.0%
Zambia	1,144	530	116.0%
Celtel Total	15,270	5,375	184.0%
MTC Group Total	24,897	12,451	100.0%

Source: MTC

*MTC acquired Madacom in December 2005

** MTC acquired V-Mobile in May 2006

Financial Performance - 2005

MTC recorded consolidated revenues of KD579.5mn (USD1.982bn) for the year ended December 31, 2005, an increase of 80% over the same period in 2004. During the year, the consolidated EBITDA increased by 90% to reach KD333.83mn (USD1.142bn), a margin of 58%. MTC has announced consolidated net income of KD185.92mn (USD636mn), an increase of 55% compared to the same period last year, representing earnings of 222 fils (USD0.76) per share, 74 fils higher than the EPS for 2004.

First Nine Months Results – 2006

MTC recorded consolidated revenues of KD849.15mn (USD2.92bn) for the nine months ended September 30, 2006, an increase of 115% over the same period in 2005. During the nine months, the consolidated EBITDA increased by 78% over same period last year to reach KD416.57mn (USD1.43bn), a margin of 49%. Consolidated net income stood at KD223.18mn (USD767.46mn), an increase of 64% compared to the same period last year, representing earnings of 180 fils (USD 0.62) per share.

MTC Vodafone - Bahrain

MTC won the Bahrain license to develop the second GSM network in April 2003 and officially launched its services in December 2003, at the time, the fastest deployment in the Middle East. The company has a three year co-branding agreement with Vodafone that includes a full branding deal and cooperation arrangement on products and services. The company became an extension of MTC's Partner Network Agreement with Vodafone thus branded as MTC-Vodafone. The company was capitalised at BD20mn and around 40% of the shares were owned by Bahraini investors. MTC-Vodafone Bahrain is expected to list on the Bahrain Stock Exchange in due course. The network ranks highly worldwide for coverage quality and the operation is at the forefront of technological development in the Middle East. In just over 2 years of operation, at 30 September 2006 - the operation had gained 279,000 subscribers and taken an approximate 25% market share in a short time.

Some distinctive highlights of the Bahrain operation included the following:

- First 3G nation wide network in the Middle East – December 2004
- First 3G Network in the Middle East – 15 December 2003
- First EDGE nation wide network in the Middle East – December 2003
- First mobile entertainment services “World of WoW” in the Kingdom of Bahrain – July 2004
- First Live TV to Mobile in the Middle East – July 2004
- First Virtual Private Network services in Bahrain – October 2004
- GPRS roaming with 29 countries including 3G with Japan

Technical Overview

MTC-Vodafone Bahrain is at the forefront of technological development in the Middle East. In 2005, the company expanded its network capacity and enlarged its 3G network to cover 100% of Bahrain. It also signed 3G roaming service agreements with 13 global mobile operators and now has roaming contracts with 137 countries and 3G roaming with 6 operators and GPRS roaming with more than 32 operators in 24 countries. Further, MTC-Vodafone Bahrain and VeriSign started to work together to offer high-end security services to customers, while MTC-Vodafone was awarded ISO 9001:2000 and BS7799-2:2002 certifications in 2005.

Commercial Overview

MTC-Vodafone Bahrain continued to launch new and innovative products and services to its clientele in Bahrain throughout 2005. It introduced a new prepaid calling plan named eeZee International, launched new post-paid Hewan calling plans with free minutes/ bundled MMS/ bundled 3G video calls, and enhanced its M-Chat service by adding new features. Moreover, it introduced special calling packages to Bahraini journalists, and offered for the first time in Bahrain a new method of seasonal greetings with its Talky Messages service, Wifi roaming and Bulk MMS messaging. Also, MTC-Vodafone Bahrain teamed up with Smartner Information Systems to bring leading edge mobile office solutions to the enterprise and residential markets in Bahrain, while it partnered with Al Ayam newspaper to offer direct classified advertising via SMS messaging. Further, MTC-Vodafone and BBC World agreed to provide full time access to BBC World for all mobile customers via the Live TV service.

Financial Performance

MTC-Vodafone Bahrain's revenues totaled US\$69.6mn, up by 101% from the previous year. It accounted for 5.4% of the Middle East operations' proceeds and for 3.5% of the group's total revenues. EBITDA of the company in Bahrain improved by 171.2% to US\$15.9mn in 2005 compared to a negative EBIDTA of US\$22.3mn in 2004. EBIDTA margin was 23% compared to EBIDTA margin of -64% in the previous year.

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