

# Eastern promise for telecoms

Having spent the last few years struggling to restore their balance sheets and creditworthiness, western European telecoms are back in the M&A hunt. Their main targets: central European mobile operators. **Oliver Holtaway** reports

**A**fter a long period of penitence, western European telecoms are finally moving on from their deleveraging phase and, with excess cash burning a hole in their pockets, starting to spend again. But, chastened by recent bad experiences, they are not chasing blockbuster mergers that might jeopardise hard-won credit rating upgrades.

**“Eastern Europe, primarily Russia and Ukraine, is the more promising space for investors”**

**Marcia Tarter, UBS**

Rather they are making modest, credit-neutral acquisitions – and central European mobile operators are the flavour of the month.

March was a busy time for central Europe investment activity. Vodafone dominated the headlines

with its acquisition of Telesystems International Wireless's Czech and Romanian mobile phone businesses, Oskar Mobil and MobiFon respectively.

At the time of press, Telefonica was close to securing a 51%, previously state-owned stake in the Czech Republic's Cesky Telecom, after submitting a €2.8 billion bid.

Meanwhile, Deutsche Telekom's Hungarian subsidiary Matav increased its stake in Montenegro. And Telekom Austria paid an €80 million call option price that took it one step closer to acquiring Bulgarian mobile provider MobilTel. Telekom Austria will be able to purchase all of MobilTel's share capital this year.

Telecoms paper from east of the Elbe was already in demand before this recent flurry of activity. Telecom bonds from EU accession countries usually yield around 7–8%, while telecoms from non-EU eastern Europe can yield up to 10–12%.

As a result of the M&A trend, high-yield paper issued by central European names has become even more popular among investors. When Telenor bought Hungarian mobile operator Pannon in 2001, the latter's bonds jumped from a Ba3 rating to A2, and the price rocketed. Investors cashed in again when Bulgaria's Mobitel issued a bond late last year. Within two weeks, Telekom Austria agreed a call option, and the bonds went through the roof. And despite being a third player in a completely saturated market, Oskar Mobil bonds traded up from 110 cents to 116 cents on the acquisition – great news for bondholders, who hope that Vodafone will buy the bonds back.

But those high-yield investors yet to get involved may find they have to park their bandwagons further east still. The completion of the Cesky Telecom auction seems to have marked the last of the big

## Remaining acquisition targets in central Europe

Company	Country	Est. value	Comment
Albtelecom	Albania	€250–300m	12 bidders for 76% govt stake
PTT BIH	Bosnia and Herz.	€400–500m	100% for sale
BH Telecom	Bosnia and Herz.	€400–500m	90% govt-owned
Zeptel	Bosnia and Herz.	€150m	100% management-owned
Eesti	Estonia	€1bn	TeliaSonera owns 49%
Lattelekom	Latvia	€150m	TeliaSonera owns 49%
ProMonte	Montenegro	€100m	Telenor owns 44%
Polkomtel	Poland	€2.6bn	TDC and VOD both own 19.6%
Zapp (Telemobil)	Romania	€300–400m	99.5% owned by Inquam
MobTel	Serbia	€700m	49% owned by PTT Serbia
Vega	Slovenia	€500–700m	Third-largest mobile

Source: UBS

## Telecoms operators in Belarus, Russia and Ukraine

Country	Operator	Major shareholders	%	Mkt Share
Belarus	Velcom*	SB Telecom	49%	46%
		Beltelcom*	31%	
		Beltekhexport	20%	
	Mobile TeleSystems LLC*	MTS	49%	50%
		State Owned Enterprises*	51%	
	BELCEL	Beltelcom	50%	4%
		Comstruct International	50%	
Russia	MTS	AFK Sistema JCSC	51%	36%
		T-Mobile	10%	
	Vimpelcom	Telenor	30%	35%
		Alfa Group	25%	
Russia	Megafon*	TeliaSonera	44%	18%
		Alfa Telecom	25%	
		OAO Telekominvest*	31%	
		IPOC	8%	
Ukraine	Kyivstar	Telenor	56.5%	45%
		Alfa Group (via Storm)	43.5%	
	Ukrainian Mobile Communications	MTS (10% held by T-Mobile)	100%	53%
	Digital Cellular Communications	Turkcell	51%	1%
		System Capital Management	49%	
Ukraine	Golden Telecom	Alfa	30%	1%
		Telenor	20%	
		Rostelecom	11%	
		EBRD	8%	
		Baring Vostok	7%	
Ukraine	Wellcom	Ukrfondinvest	31%	1%
		Interinvest	20%	
		Varkedge Ltd	24.5%	
		Occidental Management	24.5%	

\*state interest in company

Source: Barclays Capital

opportunities in central Europe. "There aren't actually many assets left to buy in central Europe," says Marcia Tarter, head of CEEMEA corporate research at UBS. "Eastern Europe, primarily Russia and Ukraine, is the more promising space for investors. Market penetration is much lower and there is more room for growth."

Russian telecom giants MTS, Vimpelcom and Megafon, and Ukraine's Kyivstar, are keen issuers of corporate debt, and have already attracted significant interest from Scandinavian telecoms such as Telenor and TeliaSonera.

### Russian roulette

Investors betting on Russian and Ukrainian telecoms will encounter greater political risk, however. Another sticking point is that many western European telecoms are pursuing 'control or exit' strategies, which is a barrier to entry. Laurence Watts, eastern European corporate bond analyst at Barclays Capital, says: "There is so much growth potential, local owners may be unwilling to sell controlling stakes at this point."

But if there are obstacles to Western ownership, then investors need to consider how eastern European telecoms look as stand-alone investments. UBS's Tarter argues that the importance of Western ownership is often overestimated. "There may be advantages from a marketing or operational perspective, but rarely from a cashflow perspective," says Tarter. "Eastern European telecoms are not little struggling subsidiaries that western European companies have to pour money into in the hope of long-term returns. If anything, they are performance boosters."

The lack of a change-of-control covenant on Vimpelcom's bonds is evidence that investors are not overly concerned with western European ownership. Deutsche Telekom recently cut its stake in MTS substantially; rating agencies affirmed the Russian telecom's credit rating.

Both central and eastern European telecoms carry much less leverage than a typical US high-yield name. If investors can stomach the political risk, they could well make tidy investments in their own right, with or without a western European parent. ■