012 Smile.Communications, Ltd. SMLC (NAS)

Last Close	Industry	Sector
31.04 USD	Diversified Communication Services	Telecommunications

Profile

Pricing data through 16 Mar 2010

In addition to this comprehensive company profile, Morningstar offers in-depth analyst research and ratings on selected companies.

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012 Smile.Communications Ltd. is a communications services provider in Israel and offers a range of broadband and traditional voice services.

The company offers broadband access at speeds of up to 6 Megabits per second. Its broadband services include broadband Internet access with a suite of value-added services, data services and server hosting, as well as new innovative services such as local telephony via voice over broadband, or VoB, and a WiFi network of hotspots across Israel.

Its traditional voice services include outgoing and incoming international telephony, hubbing, roaming and signaling and calling card services. Its data services to bandwidth organizations and international carriers, allows them to transmit electronic data from point to point or from point to multi-points. Its IP-TRUNKING services provide interconnections between service providers using session initiation protocol, to business customers.

It currently operates a network of hotspots covering hotels, hospitals, other public areas and all commercial airports throughout Israel. 012 Smile provides global international telephony services through direct connections with over 100 carriers. Its outgoing international telephony services for its residential and business customers include direct international dialing services, international and domestic pre-paid and post-paid calling cards and call-back services. It provides hubbing-traffic routing between approximately 100 network operators. 012 Smile provides roaming and signaling services for cellular operators.

The company offers its services to residential and business customers, as well as to Israeli cellular operators and international communication services providers, or carriers through its integrated multipurpose network, which allow it to provide services to almost all homes and businesses in Israel. It provides these services through its integrated multipurpose network that is deployed through points of presence, throughout Israel and in England, Germany and the United States.

012 Smile.Communications, Ltd. SMLC

Sales ILS Mil	Mkt Cap USD Mil	Industry	Sector
292	787	Diversified Communication Services	Telecommunications

012 Smile.Communications provides communication services to Israel, offering voice over broadband (VoB) and traditional voice services, as well as broadband and WiFi internet services. The company serves residential and business customers in Israel, along with Israeli cellular operators and international communication services providers. The company changed its name from Smile.Communications to 012 Smile.Communications in 2007 following its acquisition of 012 Golden Lines.

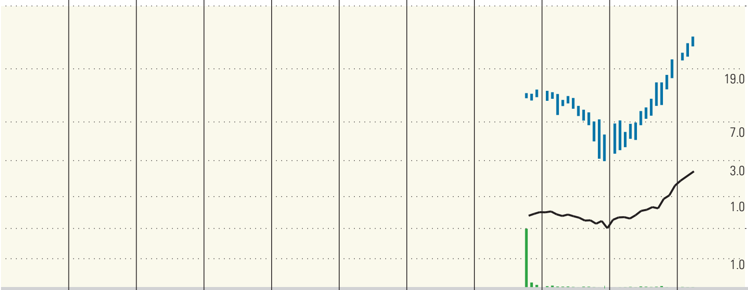
25 Hasavim St.
Petach-Tikva, IS 49170
Phone: 1 972722002111
Website: http://www.012.net

Employees: 1715

Morningstar Rating	Last Price	Fair Value	Uncertainty	Economic Moat™	Stewardship Grade
-	31.04	-	-	-	-

per share prices in USD

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	YTD
Annual Price High								13.47	13.17	22.91	33.94
Low								11.06	3.40	3.98	22.49
Recent Splits											



Price Volatility
Monthly High/Low
Rel Strength to S&P 500
52 week High/Low
33.94 - 4.72
10 Year High/Low
33.94 - 3.40
Bear-Market Rank
0 (10=worst)
Trading Volume Million

2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	YTD	Stock Performance
—	—	—	—	—	—	—	—	-69.3	440.4	44.3	Total Return %
—	—	—	—	—	—	—	—	-30.8	417.0	40.3	+/- Market
—	—	—	—	—	—	—	—	-14.6	400.6	40.9	+/- Industry
—	—	—	—	—	—	—	—	—	—	0.0	Dividend Yield %
—	—	—	—	—	—	—	325	101	545	787	Market Cap USD Mil

1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	TTM	Financials
—	—	—	—	—	41	55	76	269	307	292	Revenue ILS Mil
—	—	—	—	—	—	44.0	34.5	30.9	31.9	30.7	Gross Margin %
—	—	—	—	—	—	5	6	28	36	37	Oper Income ILS Mil
—	—	—	—	—	—	9.8	7.5	10.6	11.6	12.8	Operating Margin %
—	—	—	—	—	3	3	0	10	13	29	Net Income ILS Mil
—	—	—	—	—	0.17	0.14	-0.02	0.50	0.53	1.14	Earnings Per Share ILS
—	—	—	—	—	—	—	—	—	—	—	Dividends ILS
—	—	—	—	—	18	18	18	19	25	25	Shares Mil
—	—	—	—	—	—	—	6.78	7.19	8.65	8.68	Book Value Per Share ILS
—	—	—	—	—	—	4	8	54	58	98	Oper Cash Flow ILS Mil
—	—	—	—	—	—	-3	-2	-12	-16	—	Cap Spending ILS Mil
—	—	—	—	—	—	1	6	42	42	—	Free Cash Flow ILS Mil

1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	TTM	Profitability
—	—	—	—	—	—	5.3	-0.3	2.7	3.1	7.0	Return on Assets %
—	—	—	—	—	—	8.6	-1.4	10.0	7.2	15.2	Return on Equity %
—	—	—	—	—	7.9	4.8	-0.6	3.6	4.4	9.9	Net Margin %
—	—	—	—	—	—	1.09	0.43	0.76	0.70	0.70	Asset Turnover
—	—	—	—	—	—	1.6	9.5	2.4	2.3	2.0	Financial Leverage

1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	09-09	Financial Health
—	—	—	—	—	—	—	-208	22	-24	38	Working Capital ILS Mil
—	—	—	—	—	—	2	1	114	102	91	Long-Term Debt ILS Mil
—	—	—	—	—	—	30	34	170	182	220	Total Equity ILS Mil
—	—	—	—	—	—	0.07	0.02	0.67	0.56	0.41	Debt/Equity

2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	TTM	Valuation
—	—	—	—	—	—	—	24.3	7.9	18.0	25.6	Price/Earnings
—	—	—	—	—	—	—	1.5	0.7	1.0	1.3	P/E vs. Market
—	—	—	—	—	—	—	0.9	0.3	1.8	2.5	Price/Sales
—	—	—	—	—	—	—	1.9	0.6	2.5	3.5	Price/Book
—	—	—	—	—	—	—	4.4	1.8	8.3	7.5	Price/Cash Flow

Growth Rates Compound Annual

	1 Yr	3 Yr	5 Yr	10 Yr
Revenue %	0.2	65.3	—	—
Operating Income %	9.7	74.4	—	—
Earnings/Share %	-6.8	43.9	—	—
Dividends %	—	—	—	—
Book Value/Share %	3.9	53.9	—	—
Stock Total Return %	520.8	—	—	—
+/- Industry	447.9	—	—	—
+/- Market	467.0	—	—	—

Profitability Analysis

	Current	5 Yr Avg	Ind	Mkt
Return on Equity %	15.2	—	6.6	19.0
Return on Assets %	7.0	—	2.2	7.3
Fixed Asset Turns	6.8	—	1.7	6.8
Inventory Turns	—	—	24.9	12.1
Revenue/Employee ILS K	170.2	125.7*	—	669.4
Gross Margin %	30.7	—	51.5	41.1
Operating Margin %	12.8	—	15.5	12.2
Net Margin %	9.9	4.0	5.0	8.2
Free Cash Flow/Rev %	—	—	14.6	0.1
R&D/Rev %	—	—	—	10.7

Financial Position

	12-08 ILS Mil	09-09 ILS Mil
Cash	16	17
Inventories	—	—
Receivables	54	50
Current Assets	101	156
Fixed Assets	45	46
Intangibles	155	150
Total Assets	424	444
Payables	50	37
Short-Term Debt	56	48
Current Liabilities	125	118
Long-Term Debt	102	91
Total Liabilities	242	224
Total Equity	182	220

Valuation Analysis

	Current	5 Yr Avg	Ind	Mkt
Price/Earnings	25.6	—	22.4	19.3
Forward P/E	25.0	—	—	14.3
Price/Cash Flow	7.5	—	8.8	7.1
Price/Free Cash Flow	—	—	13.3	17.6
Dividend Yield %	—	—	0.5	1.8
Price/Book	3.5	—	2.3	2.2
Price/Sales	2.5	—	1.9	1.3
PEG Ratio	1.7	—	—	1.7

*3Yr Avg data is displayed in place of 5Yr Avg

Quarterly Results

Revenue ILS Mil	Dec 08	Mar 09	Jun 09	Sep 09
Most Recent Period	77.0	70.0	71.6	77.0
Prior Year Period	68.6	70.8	77.0	82.4

Rev Growth %	Dec 08	Mar 09	Jun 09	Sep 09
Most Recent Period	12.3	-1.1	-7.0	-6.6
Prior Year Period	-14.0	-73.8	-72.1	-70.6

Earnings Per Share ILS	Dec 08	Mar 09	Jun 09	Sep 09
Most Recent Period	0.26	0.48	0.25	0.15
Prior Year Period	0.06	0.06	0.06	0.14

Industry Peers by Market Cap

	Mkt Cap USD Mil	Rev ILS Mil	P/E	ROE%
012 Smile.Communicat	787	292	25.6	15.2
Hutchison Whampoa, L	—	—	—	—
TeliaSonera AB	—	—	—	—

Major Fund Holders

	% of shares
Fidelity Nasdaq Composite Index	0.01
	—
	—

TTM data based on rolling quarterly data if available; otherwise most recent annual data shown.

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Management & Ownership

Management Activity

Name	Position	Shares Held	Report Date*	InsiderActivity
NA	NA	NA	NA	NA

*Report date represents the date on which the owner's common shares held was audited.

Fund Ownership

Top Owners	Morningstar Rating	% of Shares Held	% of Fund Assets	Change (k)	Portfolio Date
Fidelity Nasdaq Composite Index	QQQ	0.01	0.02	0	31 Dec 2009

Concentrated Holders	Morningstar Rating	% of Shares Held	% of Fund Assets	Change (k)	Portfolio Date
NA		NA	NA	NA	NA

Institutional Transactions

Top 5 Buyers	Morningstar Rating	% of Shares Held	% of Fund Assets	Shares Bought/ Sold (k)	Portfolio Date
NA		NA	NA	NA	NA

Top 5 Sellers	Morningstar Rating	% of Shares Held	% of Fund Assets	Shares Bought/ Sold (k)	Portfolio Date
NA		NA	NA	NA	NA

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Industry Focus: Communication Services

Imari Love
Stock Analyst

We assess the Brazilian wireless sector's quarterly performance so far.

Dialing into Earnings for Brazilian Wireless

03 March 2010

Now that Vivo VIV and Claro (America Movil 's AMX Brazilian unit) have reported fourth-quarter results, we pause to take stock of the Brazilian wireless sector's earnings season. Given the ever-changing economic and competitive landscape of the country, we thought it worthwhile to examine some of the key performance indicators that we've witnessed thus far for the fourth quarter of 2009.

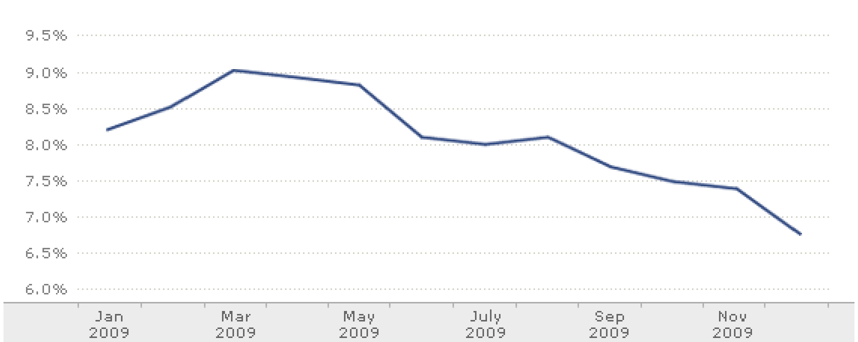
On the macro front, Brazil once again has things going in the right direction. Over the course of the past year, unemployment in Brazil has gone from multiyear highs to a multiyear low.

The economy has now witnessed 10 consecutive months of credit expansion, lower loan rates, and tax cuts, thanks to President Lula's government stimulus package. Even better, Finance Minister Guido Mantega expects Brazil to create an additional 1.6 million jobs during 2010. However, Lula's policies aren't the only ones benefiting Brazil's economy. Brazil is getting a boost from China's stimulus package as well. In 2009, China surpassed the United States as Brazil's top trading partner, thanks to its insatiable appetite for iron ore. This has driven a recovery in Brazil's industrial production, which filters down into more jobs and disposable income for its workforce.

Thanks in part to the lower loan rates, consumers are opening their wallets once again. Sales of passenger cars and light trucks grew by 13% in 2009, and could rise by double digits again in 2010. Foreign Direct Investment (FDI) is projected to rise by 80% in 2010, and there are plenty of infrastructure projects underway as the country prepares to host the World Cup (2014) and Summer Olympics (2016).

The competitive landscape in Brazil has also been a bit of a roller coaster ride. Oi TNE and Claro have been very aggressive over the past year in terms of handset subsidies. This has eroded sector profitability, pinched margins, and increased churn. The early returns from the fourth-quarter results, however, hint that things might be improving.

Brazil Unemployment



Source: Brazilian Institute of Geography and Statistics (IBGE)

As we start to ponder the prospects of new players entering the fray after next quarter's spectrum auction, it's important to note that Brazil is one of the only wireless markets with more than three players with substantial scale. With a penetration rate exceeding 90%, it will be an extremely difficult investment case for new entrants. Some of the early takeaways from Vivo and Claro are highlighted in the charts below. We include just Vivo, Claro, and TIM TSU because Oi doesn't report these wireless metrics on a proforma basis.

ARPU

Both Vivo and Claro saw their ARPU decline on a year-over-year basis for the eighth consecutive quarter. Data growth has been strong, up 51.4% in the quarter for Claro, and up

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65% for Vivo. However, this strong showing hasn't been enough to offset competitive pricing pressures.

As we go into 2010, we expect the sector's blended local-currency ARPU to continue to decline, because of strong subscriber growth and steady pricing pressure.

Usage

Not much of a read-across here. The two firms went in opposite directions during the quarter. Claro had a 6% year-over-year drop in minutes of use (MOU), while Vivo set a multiyear high after a 40% jump, to 119 average minutes of use per month. Vivo's uptick was driven by new promotional campaigns the firm launched last fall, namely, "Recharge and Win," that focused on stimulating traffic.

Subscriber Growth and Retention

Very solid. Both firms registered 15% growth for the quarter. As we mentioned earlier, the penetration rate is now over 90%, so as subscriber growth inevitably slows, the firms' ability to retain customers becomes more important. Vivo held its churn rate flat at 2.5%, while Claro saw a 40-basis-point jump from the fourth quarter of 2008, to 3%. For the record, of the major players, Vivo recorded the fewest complaints to Anatel, the Brazilian telecommunications regulator.

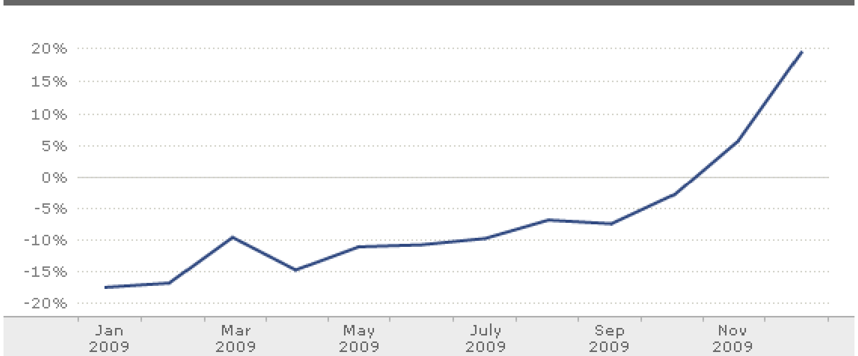
Profitability

This is probably the most important metric of all when trying to gauge the fundamental health of the sector. Last quarter, Claro saw EBITDA (earnings before interest, taxes, depreciation, and amortization) margins widen by nearly 5 percentage points year over year, to 24.5%. This pushed its full-year margin to 24.2%, versus 23.6% in 2008. Vivo also generated margin expansion in 2009, with EBITDA widening by a more modest 1 percentage point, to 32%. However, Vivo's fourth-quarter margin remained flat, at 32.7%. It seems that subscriber acquisition costs are finally dropping off, thanks to more SIM-only sales and lower handset subsidies. However, we note that only Vivo has reported this metric, showing a 22% decline year over year, and 25% drop sequentially. In fact, Vivo reported handset subsidies were down 65% year over year during the fourth quarter, or 57% sequentially. This is a positive precursor for 2010, where we expect all four firms to expand their margins further.

Outlook

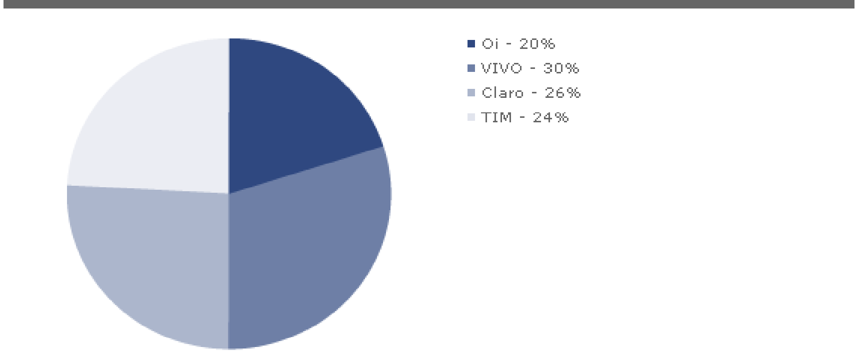
Neither firm offered 2010 guidance, probably because there

Brazil Industrial Production (YoY Growth)



Source: Brazilian Institute of Geography and Statistics (IBGE)

Brazilian Wireless Market Share



Source: Anatel

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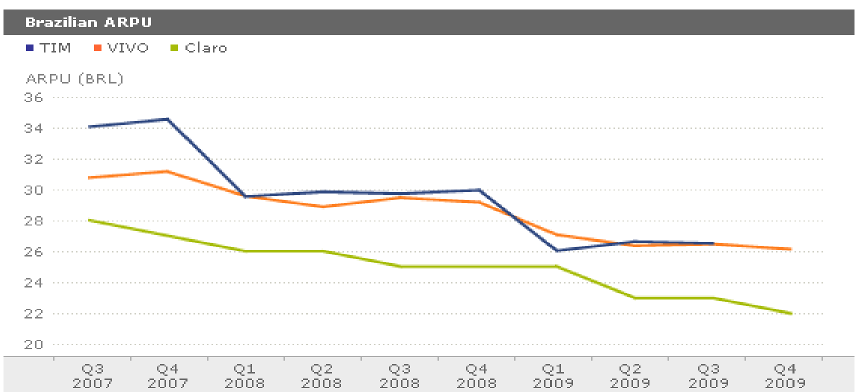
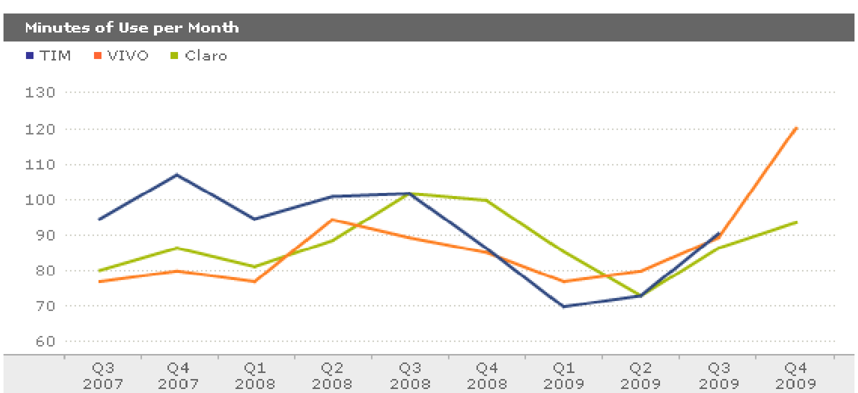
Industry Focus: Communication Services

is not a lot of visibility right now. After all, we aren't sure if the market will be consolidating (possibly through a VIV and TIM merger) or expanding (possibly by GVT or NII joining the sector). What we do know is that we are now more concerned with the quality of the incremental subscriber than the quantity. The hope is that collectively, management will prioritize market share of profits over the share of subscribers. Thankfully, the four carriers seem to be on the same page and have begun building their promotional initiatives around higher-quality customers. We expect Oi and TIM to post solid fourth-quarter results, but after that, the sector's 2010 share price fate will hinge on how many players will be in the mix and how rational they will be.



Source: Company filings, Morningstar



Source: Company Reports

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