

**FASTWEB (FWB MI – €18.89 – Milan Stock Exchange)**

**Italian Connections - Buy**

<u>Year</u>	<u>EPS</u>	<u>P/E</u>	<u>PMV</u>	Dividend: None	Current Return: Nil
2010P	€1.00	18.9x	€32	Shares O/S: 79.5 million (a)	
2009E	0.40	47.2	31	52-Week Range: €22.66 – €12.60	
2008A	-0.25	N/A	30		
2007A	-2.10	N/A	25		

(a) 82% owned by Swisscom

**SUMMARY AND OPINION**

FASTWEB is the leading alternative operator of broadband services in Italy, organized in 1999 and listed on the Milan stock from March 2000. The company provides triple play voice, Internet connectivity and video services over an all IP platform. FASTWEB has invested in excess of €4.5 billion to date in its national fiber optic network that spans over 27,000 route kilometers and covers well over 50% of the Italian population. FASTWEB also operates as a mobile virtual network operator (MVNO), with over 120,000 active SIM card users. Swisscom acquired an 82% stake in FASTWEB in Italy for €3.1 billion cash (€47 per share) in May 2007. As of the June 30, 2009, FASTWEB had a total customer base of 1.6 million, a gain of 6% from the beginning of the year.

We recommend purchase of FASTWEB:

- Gaining market share in all segments of the under-penetrated (43% vs. >50% in EU) Italian broadband market
- Trading at 4.4x 2010 EBITDA
- Generating increasing free cash flow, having turned positive in 2008

The Italian broadband market remains attractive as the fourth-largest in Europe, with end user customer revenues of €16 billion in 2008. There are seven key national broadband players, with Telecom Italia holding more than a 60% share of total lines. From a below-average penetration level of 43%, Italian market is expected to surpass 60% broadband penetration by the end of 2012, with FASTWEB poised to take a disproportionate share of that growth.

The valuation case for FASTWEB can be made on the basis of an EV/EBITDA multiple of 4.4x 2010, with any prospect of a buy-in of minorities by Swisscom (despite repeated denials of such intent) further underpinning the price.

**Table 1**

**FASTWEB  
Private Market Value Analysis  
2006A-2012P**

	<u>2006A</u>	<u>2007A</u>	<u>2008A</u>	<u>2009E</u>	<u>2010P</u>	<u>2011P</u>	<u>2012P</u>	<u>CAGR</u>
Net Revenues	€ 1,251	€ 1,433	€ 1,705	€ 1,823	€ 1,906	€ 2,042	€ 2,167	8.6%
EBITDA	301	410	547	603	654	701	745	
Valuation Multiple	9.0	8.0	7.0	6.5	6.0	6.0	6.0	
Segment Value	€ 2,709	€ 3,280	€ 3,829	€ 3,920	€ 3,924	€ 4,206	€ 4,470	6.4%
Total Private Market Value	€ 2,709	€ 3,280	€ 3,829	€ 3,920	€ 3,924	€ 4,206	€ 4,470	
Less: Net Debt	1,081	1,265	1,458	1,422	1,359	1,226	1,104	
<b>Equity Private Market Value</b>	<b>€ 1,628</b>	<b>€ 2,015</b>	<b>€ 2,371</b>	<b>€ 2,498</b>	<b>€ 2,565</b>	<b>€ 2,980</b>	<b>€ 3,366</b>	
Shares Outstanding	79.5	79.5	79.5	79.5	79.5	79.5	79.5	
<b>PMV per share</b>	<b>€ 20</b>	<b>€ 25</b>	<b>€ 30</b>	<b>€ 31</b>	<b>€ 32</b>	<b>€ 37</b>	<b>€ 42</b>	10.8%
Current Market - Discount to PMV	5.9%	32.3%	58.8%	64.1%	69.4%	95.9%	122.2%	

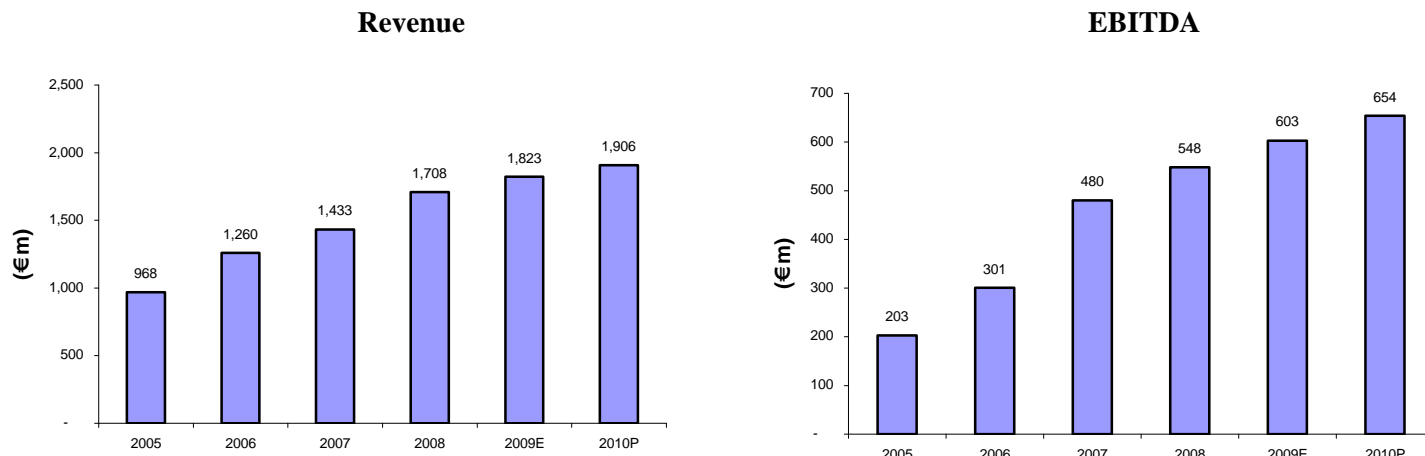
Source: Company reports and Gabelli & Company, Inc. estimates

## Continued Growth

FASTWEB has seen steady, consistent growth over the past four years as it extended its network infrastructure, marketing reach, and customer service and support operations. Its competitive approach is one of offering highest bandwidth and service quality, enabling the company to focus on high value customers and maintenance of a price premium to the low end, mass-market providers.

**Exhibit 1**

**Key Financial Performance Figures**



Source: Company data

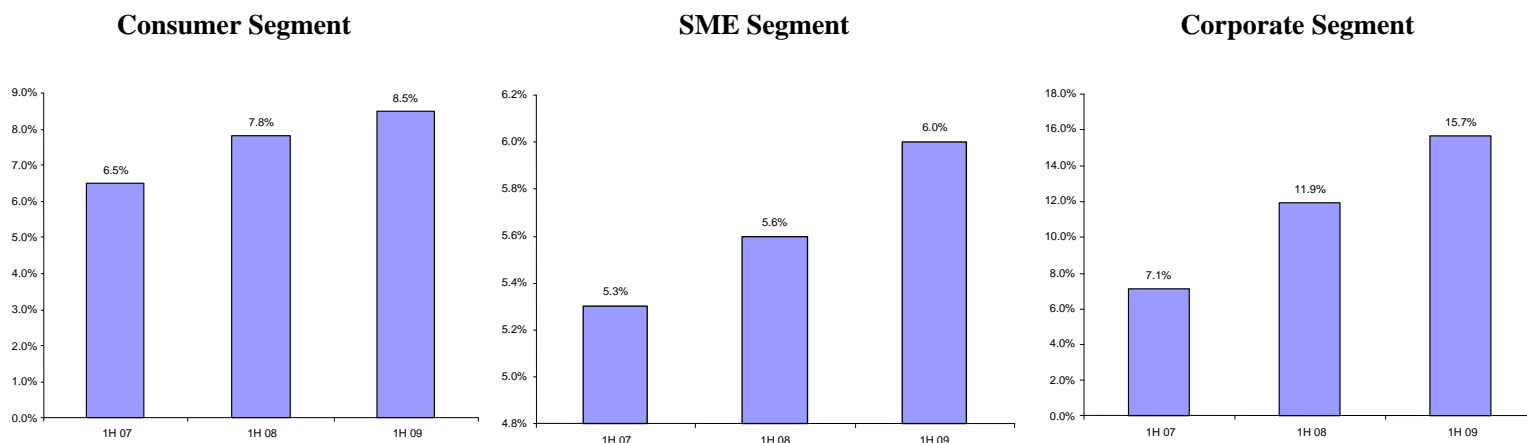
FASTWEB growth continues in 2009, albeit at a slower pace owing to the depth of the Italian recession. In 1H, revenue advanced by 13% to €19 million and EBITDA of €265 million was 8% up on 1H 2008. FASTWEB is active in three discrete market segments – residential, SME, and corporate/public administration (Executive), and has reorganized its commercial activities and service portfolios along these segmental lines.

The Executive business has been key to FASTWEB's recent performance, and contributed 42% of group revenues in 2Q 2008. This segment delivered 22% growth in the period, confounding those that were concerned about cancellation or deferrals of large, public contracts owing to spending constraints. The more-than doubling of market share in this segment to 15.7% over the past two years is notable.

The SME unit had revenue growth of 10% in 2Q and accounts for 22% of the group total. FASTWEB's position in the SME segment has been enhanced by the introduction of 100 Mb/s transmission speed from last year. This ultra broadband offering was the first available in Italy and among the first anywhere in Europe. The Consumer Business Unit appears the most heavily impacted by the economy, with 2Q revenue growth of only 2%. We view the slow growth in the segment as a temporary phenomenon only, with expanded IPTV content and mobile as drivers for continued subscriber and revenue gains.

**Exhibit 2**

**FASTWEB Market Share Gains  
Italian Broadband Market**



Source: Company data

### Mobile Service

FASTWEB entered the Italian mobile market in 2H 2008, following an agreement with 3 Italia to act as a mobile virtual network operator (MVNO). This enables FASTWEB to offer converged fixed-mobile services including high-speed Internet access, e-mail and voice messaging via mobiles. The company is actively promoting its mobile capability, with advertising targeted primarily at the existing broadband customer base. While mobile is not a critical success factor for FASTWEB, the current SIM penetration of less than 10% of the existing consumer and SME subscriber base suggests it will continue to grow.

### Video Service

FASTWEB was among the first in the world to offer an IPTV service when it launched the product in 2001. Today FASTWEB TV offers thousands of titles on analog channels, theme channels, SKY satellite channels, free DTT channels, video-on-demand and interactive services. At the end of 2006, the company introduced the first universal decoder (set-top box) for all current analog and digital TV content, as well as support for High Definition content.

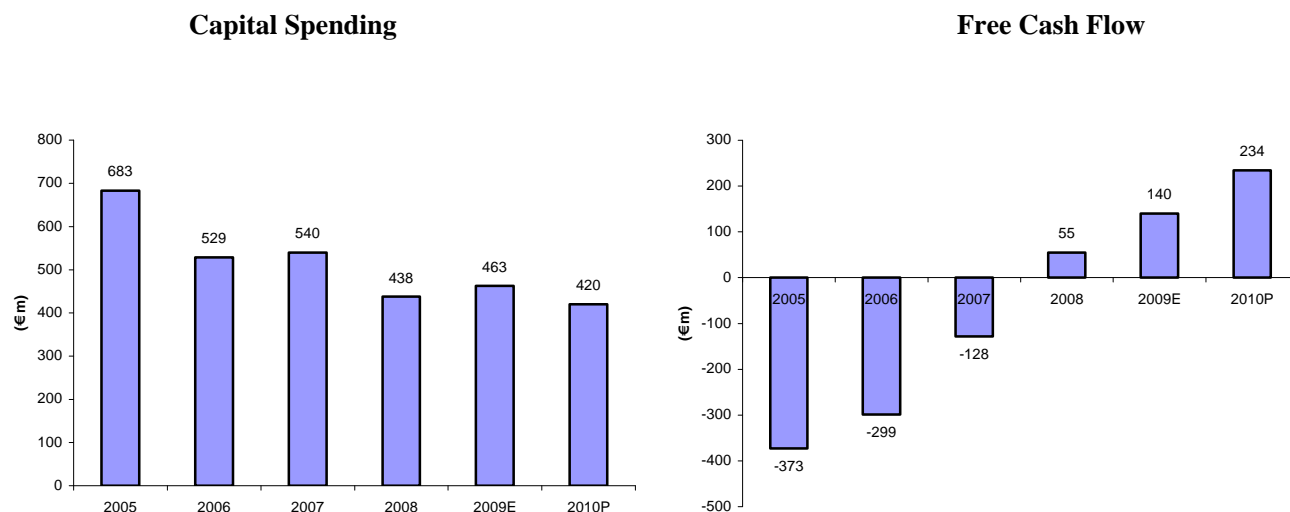
In July of this year, FASTWEB and Mediaset signed an agreement for the distribution and marketing of the Mediaset Premium digital terrestrial offer (broadcast and pay-per-view) on FASTWEB's IPTV platform. Two Mediaset Premium packages will be available from this month on FASTWEB TV – '*Premium Bouquet*' offering entertainment content and '*Premium Calcio*' that includes European and Italian football. Retail prices will match those charged by Mediaset.

### Capex and Cash Flow

FASTWEB is in the enviable position of having built the vast majority of its fiber network in the first-half of this decade. As a result, group capital expenditure has effectively been trending down since 2005. The combination of growing EBITDA and declining capital spending has enabled FASTWEB to achieve positive free cash flow for the first time in 2008.

#### Exhibit 3

#### Key Financial Performance Figures



Source: Company data

The lower capex trend, if anything, is now accelerating. 1H 2009 capex of €217 million was down 24% from the same period last year. Another metric that supports this view is the capex/sales ratio, which has fallen from 36% in 1H 2007, to 28% in 1H 2008 and stood at 24% for 1H 2009. The nature of the spend has also shifted over time from one of extending network coverage to additional cities and nodes, to customer, success-driven spend which constituted 59% of the 1H outlay.

### Outlook

FASTWEB provided broad guidance for the current year and confirmed the targets with the announcement of 2Q results:

- Revenue +5% (implies €1.8 billion)
- EBITDA +8% (implies €590 million)
- EBITDA – capex of €140 million
- Positive net income

On the basis of 1H performance, these targets look readily achievable, with the possible exception of the EBITDA-capex objective. In 1H, FASTWEB generated €48.5 million in operating free cash flow, suggesting that the 2H total will need to nearly double.

Nonetheless, if the primary use of the cash flow at this point is paying down debt, the June 30 net debt figure of €1.4 billion is not of great concern. This total should represent the peak of FASTWEB's borrowing (it is actually down fractionally from 1/1/09) and equates to 2.3x estimated 2009 EBITDA. Within the next 2-3 years, FASTWEB will certainly be in a position to start paying a dividend, with Swisscom no doubt keen to begin recouping its not insubstantial investment in FASTWEB. On our projections, net debt/EBITDA would fall to under 1.5x by 2012, absent a dividend.

**Other Companies Mentioned:**

Mediaset	(MS.MI)
Swisscom	(SWJ.HM)
Telecom Italia	(TQI.HM)

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I, **Evan Miller**, the Research Analyst who prepared this report, hereby certify that the views expressed in this report accurately reflect the analyst's personal views about the subject companies and their securities. The Research Analyst has not been, is not and will not be receiving direct or indirect compensation for expressing the specific recommendation or view in this report.

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**Important Disclosures**

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