Assumptions to prepare five years Financial Forecast
(2000/01 - 2004/5)

I. INTRODUCTION

We have prepared the forecast profit & loss and balance sheet under two alternatives (options) which are described below:

Alternative one

1. we have assumed that no change will be made to the existing tariff rates for each services in the coming five years except settlement rate is considered to be SDR 0.35 which is equivalent to USD 0.47.
2. We have assumed also that the net surplus will be reinvested to support the development programmes.

Alternative two

1 Tariff rates will be the same as under alternative one.
2. Here it is assumed the net surplus will be paid to the share holder (Government).

II. EXPECTED RESULTS

We have indicated here below some measures of growth, revenue per subscriber, returns, gearing, liquidity and financing. The measures calculated and comments made thereby are highly dependent on the following key point:

- The achievement of investment programs as planned and the assumed traffic under each service are critical to the financial position and performance of the corporation.

1) **Growth :**

An average growth rate in revenue gross operating surplus and profit after tax over the five years forecast has been determined as follows:-

Description	Alternative One*	Alternative Two*
Revenue	146%	146%
Gross operating surplus	147%	147%
Profit after tax	189%	164%

* Average amounts of the period from 2001 to 2005 have been compared with the 2000 amounts to arrive at the above figures.

2) **Revenue per subscriber**

The revenue per subscriber of fixed telephone under both alternatives is the same as shown in the following table. It is decreasing from Birr 2,845 in 1999 to Birr 2,357 in the year 2005. One explanation for the declining nature could be that the rate of increase in revenue is relatively lower than the rate of increase in connected lines (subscribers).

Year	**Revenue/subscriber**
1999	Birr 2,845
2000	2,261
2001	2,409
2002	2,395
2003	2,379
2004	2,367
2005	2,357

3) **Cash flow (Financing)** :-

Cash flow from operation (own funds) after covering profit tax payments and investment programs but before considering debt service payments and other sources of financing is:

In '000

YEAR	Alternative One	Alternative Two
2000	(131,345)	(131,345)
2001	(102,284)	(102,283)
2002	(447,323)	(496,590)
2003	56,957	(35,680)
2004	484,571	380,139
2005	771,766	658,048

The amounts shown under brackets represent cash deficits by which the own fund generated in each year falls short of the investment requirements. The extent of financing through own funds can be shown as follows.

YEAR	Alternative One	Alternative two
2000	72%	72%
2001	100%	100%
2002	65%	60%
2003	100%	97%
2004	100%	100%
2005	100%	100%

In the budget year, it is expected that 100% of the cash required for investment will be covered from own funds under both alternatives. In the year 2002, the coverage will be reduced to 65% under alternative one and 60% under the 2nd alternative. The cash requirements in the rest of the forecast years will be financed fully through internally generated funds with the exception of year 2003.

Though the investment requirements have been covered almost 100% in most of the forecast years, cash will be needed for repayment of long-term loan, net surplus to the share holder (alternative two) and to finance investment where it has not been covered through own funds.

The expected amount of additional cash required for these purposes will be:

	Alternative one	Alternative two
2002	29,214,000	439,749,000
2003	22,615,000	538,658,000
2004	-	277,776,000
2005	-	150,302,000
	51,829,000	1,406,485,000

The cumulative external cash required will be more than Birr 51 million and 1.4 billion under alternative one and two respectively over the forecast period.

All these financing requirements are assumed to be financed through commercial credits from local banks, suppliers credit, inter-governmental loans or capital injection from partners.

4) Returns, liquidity, gearing

4.1 Returns

As can be seen in the table below an average return on fixed assets of 33.4% and 34.8% has been achieved under alternative one and two respectively. Almost the same returns in both cases but in the average return on equity is 19% under alternative one and 33% under alternative two. The high return on equity under alternative two is because the equity amount has been reduced as it is assumed that the net surplus will be paid to the shareholder. At this point in time, it is very difficult to determine whether these results are satisfactory or not unless we have a predetermined target or sector averages.

Description	Alternative one	Alternative two
Return on fixed assets (average)	33.4%	34.8%
Return on equity (average)	19%	33%

4.2 Liquidity and gearing

The liquidity (current ratio) over the five-year period shows that current liabilities are covered more than one times by the current assets under alternative one. However, in the second alternative the current ratio is below standard. This is because the corporation is supposed to pay the net surplus to the share holders (Government) which is shown under current liabilities . Hence the, corporation will run in to short-term cash flow problems.(see the table on below)

	CURRENT RATIO		GEARING	
Year	**Alt-one**	**Alt-two**	**Alt-one**	**Alt-two**
1999	2.41	2.41	0.44	0.44
2000	1.83	1.71	0.37	0.37
2001	1.97	1.20	0.33	0.33
2002	1.06	0.68	0.29	0.50
2003	1.06	0.61	0.24	0.72
2004	1.45	0.54	0.19	0.79
2005	2.21	0.56	0.15	0.81

Under alternative one, the long-term debt to equity ratio (gearing) has shown a continuous decline from 0.44 in year 1999 to 0.15 in the year 2005 indicating that the dependency on long-term loan to finance investment programs is low. This is because the net surplus after tax have been retained and reinvested.

However, under alternative two, the net surplus will be repaid to the government (shareholder) and the equity base will be relatively lower. Hence, investment programmes will be financed through long-term loans. As can be seen from the table, these situations have lead to an increasing gearing ratio.

III. ASSUMPTIONS

A. PROFIT & LOSS

1) **Revenue from operation** :- is calculated based on traffic data received from Network Standard & Traffic Engineering Division. It is also assumed that there will not be devaluation of the local currency by the Government.

2) **Moves and changes** :- are assumed to be 2% of the urban telephone income. The rate has been determined based on data of 1999 accounting year.

3) **Other Revenue:-** is assumed to increase on an arithmetic progress increase of 1% over the previous year annual increment. The starting rate is taken as 16% Based on the three years actual data.

4) **Income from leased circuit:-** assumed to be 0.88% of operating revenue generated.

5) **Operating expenses:-**

5.1 Operating expenses other than depreciation is determined based on a percentage relationship of operating expense to operating revenue for each service during 1999 fiscal Year.

5.2 Depreciation expense is determined at composite rate of 3.55% and prorated into operation and administration by reference to the proportion of deprecation Expense in 1999 fiscal year

6) **administrative & general expenses** are assumed to increase by 12% from the previous year.

7) **Interest Expense** :- interest on Long Term loan is Determined at the agreed rate and translated in to birr at the expected prevailing exchange rate which is determined taking in to consideration the average rate of fluctuation.

8) **Bank charge**:- In each year bank charges are assumed to be 3% Of the interest based on 1999 reported figures.

9) **Provision for doubtful debts** :- Based on the accounting policy adopted by the corporation that is, the provision is raised by applying 1% of trade debtors.

10) **Exchange rate:-**
It is assumed that the exchange rate of the various currencies will increase by 5% every year constantly.

11) **Legal Reserve**:- 5% of net surplus after taxation is taken until the reserve reaches 20% of the authorized capital.

Note:- There will not be transfer of profit to paid up capital starting from 2001 Because the authorized level has been reached in year 2000.

B. BALANCE SHEET

1) **Fixed Asset** :- 50% of W.I.P is assumed to be transferred to Fixed Assets

2) **Investment**:- It is assumed that new investments on INTELSAT and SEA-ME-WE & others will not be acquired or existing investment will not be disposed in the coming five years.

3) **Deferred charge**:- Are stated net of amortization and amortization is established by dividing the deferred charge balance to the remaining life of related long term loans.

4) **Stock** :- Maintained 90% of the coming years material need. However, since the material need for 2006 was not established , 90% of the average need for the five years is taken as stock for 2005.

5) **Debtors** :- Are stated net of provisions for bad debts and the debtors shown comprises
   i) 20% of the billing of each year as trade
   ii) Advance to GSM which is established based on its expected clearance
   iii) Other debtors as 4% of trade debtors based on 1999 Accounting year .

6) **Cash** :- A minimum cash requirement of 100Million is assumed wherever there is deficit

7) **Creditors**:- Are assumed to be 54% of the material consumption under each year. The rate has been established by reference to the relationship existing in 1999 fiscal year.

8) **Long term Loan and its current portion**:- Determined as per loan Repayment schedule

9) **Financing**:- Where ever there is a cash deficit in each year , it is assumed to be financed through bank loan obtained at the beginning of the year with an interest rate of 12%. It is also assumed that there is a grace period of three years for principal.