



**a Saudi Joint Stock Company**

**Interim Consolidated Financial Statements for the  
Second Quarter 2010**

**Interim Consolidated Financial Statements for the  
Three and Six-Month Periods Ended June 30, 2010  
(Unaudited)**

**Saudi Telecom Company**  
**(a Saudi Joint Stock Company)**  
**Index to the Interim Consolidated Financial Statements for the Three and Six-Month**  
**Periods Ended June 30, 2010(Unaudited)**

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**INDEPENDENT AUDITORS' LIMITED REVIEW REPORT**

To the shareholders  
Saudi Telecom Company  
Riyadh, Saudi Arabia

**Scope of Review**

We have reviewed the accompanying interim consolidated balance sheet of Saudi Telecom Company (a Saudi Joint Stock Company) as of June 30, 2010 and the related interim consolidated statements of income for the three-month and six-month periods ended June 30, 2010 and cash flows for the six-month period then ended and the related notes which form an integral part of these interim consolidated financial statements. These interim consolidated financial statements are the responsibility of the Company's management and have been prepared and presented to us with all the information and explanations which we requested.

We conducted our limited review in accordance with the interim financial statements review standard issued by the Saudi Organization for Certified Public Accountants. A limited review consists principally of applying analytical procedures to financial data and making inquiries of persons responsible for financial and accounting matters. Such limited review is substantially less in scope than an audit conducted in accordance with generally accepted auditing standard, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

**Review Result**

Based on our review, we are not aware of any material modifications that should be made to the accompanying interim consolidated financial statements for them to be in conformity with generally accepted accounting standards.

**Deloitte & Touche**  
**Bakr Abulkhair & Co.**



Bakr A. Abulkhair  
License No. 101



**Dr. M. Al-Amri & Co.**



Gihad Al-Amri  
License No. 362

Sha'ban 8, 1431 H  
July 20, 2010 G



**Saudi Telecom Company**  
**(a Saudi Joint Stock Company)**  
**Interim Consolidated Balance Sheet as of June 30, 2010 (Unaudited)**  
**(Saudi Riyals in thousands)**

	<u>Note</u>	<u>2010</u>	<u>2009</u>
<b><u>ASSETS</u></b>			
<b>Current assets:</b>			
Cash and cash equivalents		6,547,961	7,309,766
Accounts receivable, net		13,781,636	9,851,183
Prepayments and other current assets		<u>4,042,414</u>	<u>3,021,048</u>
<b>Total current assets</b>		<u>24,372,011</u>	<u>20,181,997</u>
<b>Non-current assets:</b>			
Property, plant and equipment, net		51,702,866	50,482,608
Intangible assets, net	3	31,074,914	29,470,312
Investments in equity and other		2,627,151	2,497,610
Other non-current assets		<u>2,382,788</u>	<u>2,154,789</u>
<b>Total non-current assets</b>		<u>87,787,719</u>	<u>84,605,319</u>
<b>Total assets</b>		<b><u>112,159,730</u></b>	<b><u>104,787,316</u></b>
<b><u>LIABILITIES AND EQUITY</u></b>			
<b>Current liabilities:</b>			
Accounts payable		10,877,516	6,656,437
Other credit balances		5,315,043	4,601,151
Accrued expenses		4,919,415	5,830,650
Deferred revenues – current portion		2,182,467	2,038,946
Borrowings – current portion	4	<u>8,197,976</u>	<u>7,143,370</u>
<b>Total current liabilities</b>		<u>31,492,417</u>	<u>26,270,554</u>
<b>Non-current liabilities:</b>			
Borrowings– non-current portion	4	22,584,274	25,527,569
End of service benefits		3,093,414	2,847,967
Other Credit balances		<u>4,653,555</u>	<u>3,804,907</u>
<b>Total non-current liabilities</b>		<u>30,331,243</u>	<u>32,180,443</u>
<b>Total liabilities</b>		<u>61,823,660</u>	<u>58,450,997</u>
<b>Equity:</b>			
<b>Shareholders' equity</b>			
Authorized, issued and outstanding shares:			
2,000,000,000 shares, par value SR 10 per share		20,000,000	20,000,000
Statutory reserve		9,773,916	8,787,435
Retained earnings		13,762,552	11,709,170
Other reserves	12	(683,303)	-
Financial statements' translation differences		<u>(606,816)</u>	<u>(984,120)</u>
<b>Total Shareholders' equity</b>		42,246,349	39,512,485
Non-controlling interest		<u>8,089,721</u>	<u>6,823,834</u>
<b>Total equity</b>		<u>50,336,070</u>	<u>46,336,319</u>
<b>Total liabilities and equity</b>		<b><u>112,159,730</u></b>	<b><u>104,787,316</u></b>

The accompanying notes from 1 to 14 form an integral part of these interim consolidated financial statements.

**Saudi Telecom Company**  
**(a Saudi Joint Stock Company)**  
**Interim Consolidated Statement of Income for the Three and Six-Month Periods Ended**  
**June 30, 2010 (Unaudited)**  
**(Saudi Riyals in thousands)**

	<u>Note</u>	<u>Three Months ended</u>		<u>Six Months ended</u>	
		<u>June 30,</u>		<u>June 30,</u>	
		<u>2010</u>	<u>2009</u>	<u>2010</u>	<u>2009</u>
Revenue from services		12,591,237	12,674,120	25,110,868	24,816,904
Cost of services	5	<u>(5,256,352)</u>	<u>(4,951,089)</u>	<u>(10,616,117)</u>	<u>(9,181,328)</u>
<b>Gross Profit</b>		<u>7,334,885</u>	<u>7,723,031</u>	<u>14,494,751</u>	<u>15,635,576</u>
<b>Operating Expenses</b>					
Selling and marketing expenses	6	(1,784,772)	(1,633,496)	(3,653,602)	(3,102,340)
Administrative and general expenses	7	(1,046,210)	(953,740)	(1,877,401)	(1,786,473)
Depreciation and amortization	8	<u>(2,159,067)</u>	<u>(1,907,391)</u>	<u>(4,265,633)</u>	<u>(3,681,868)</u>
<b>Total Operating Expenses</b>		<u>(4,990,049)</u>	<u>(4,494,627)</u>	<u>(9,796,636)</u>	<u>(8,570,681)</u>
<b>Operating Income</b>		<u>2,344,836</u>	<u>3,228,404</u>	<u>4,698,115</u>	<u>7,064,895</u>
<b>Other Income and Expenses</b>					
Cost of early retirement program		(2,340)	(443,520)	(2,340)	(593,520)
Finance cost		(338,525)	(326,759)	(765,312)	(690,656)
Commissions and interest		68,154	87,514	117,582	184,813
Other, net	9	<u>368,920</u>	<u>914,856</u>	<u>538,119</u>	<u>159,704</u>
<b>Other income and expenses, net</b>		<u>96,209</u>	<u>232,091</u>	<u>(111,951)</u>	<u>(939,659)</u>
<b>Net Income before Zakat, Tax and Non-controlling interest</b>		2,441,045	3,460,495	4,586,164	6,125,236
Provision for Zakat		(21,839)	(73,262)	(64,709)	(176,629)
Provision for Tax		<u>(211,578)</u>	<u>(157,857)</u>	<u>(412,789)</u>	<u>(274,589)</u>
<b>Net Income before Non-controlling interest</b>		2,207,628	3,229,376	4,108,666	5,674,018
Non-controlling interest		<u>(145,637)</u>	<u>(239,159)</u>	<u>(274,650)</u>	<u>(196,052)</u>
<b>Net Income</b>		<u>2,061,991</u>	<u>2,990,217</u>	<u>3,834,016</u>	<u>5,477,966</u>
<b>Basic earnings per share on Operating Income (in Saudi Riyals)</b>		<u>1.17</u>	<u>1.61</u>	<u>2.35</u>	<u>3.53</u>
<b>Basic Gain per share on Other Operations (in Saudi Riyals)</b>		<u>0.05</u>	<u>0.12</u>	<u>(0.06)</u>	<u>(0.47)</u>
<b>Basic earnings per share on Net Income (in Saudi Riyals)</b>		<u>1.03</u>	<u>1.50</u>	<u>1.92</u>	<u>2.74</u>

The accompanying notes from 1 to 14 form an integral part of these interim consolidated financial statements.

**Saudi Telecom Company**  
**(a Saudi Joint Stock Company)**  
**Interim Consolidated Statement of Cash Flows for the Six-Month Period Ended June 30,**  
**2010 (Unaudited)**  
**(Saudi Riyals in thousands)**

	<u>2010</u>	<u>2009</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	3,834,016	5,477,966
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	4,265,633	3,681,868
Doubtful debts expense	784,644	492,463
Earnings from investments accounted for under the equity method	(43,941)	(27,920)
Losses on sale/disposal of property, plant and equipment	31,658	117,234
Changes in:		
Accounts receivable	(3,105,055)	(2,223,609)
Prepayments and other current assets	(639,697)	(255,858)
Other non-current assets	58,600	132,561
Accounts payable	3,220,797	7,715
Other credit balances	699,425	587,089
Accrued expenses	(1,285,684)	68,330
Deferred revenues	59,115	(209,532)
End of service benefits	<u>249,545</u>	<u>109,942</u>
<b>Net cash provided by operating activities</b>	<u>8,129,056</u>	<u>7,958,249</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Capital expenditures	(2,838,186)	(9,669,256)
Intangible assets, net	(2,308,958)	1,176,909
Investments in equity and other	(50,284)	-
Dividends received from investments accounted for under the equity method	-	5,917
Proceeds from sale of property, plant and equipment	<u>91,543</u>	<u>189,648</u>
<b>Net cash used in investing activities</b>	<u>(5,105,885)</u>	<u>(8,296,782)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Dividends paid	(3,088,957)	(2,997,810)
Borrowings, net	(507,832)	685,005
Non-controlling interest	<u>(588,499)</u>	<u>1,899,935</u>
<b>Net cash used in financing activities</b>	<u>(4,185,288)</u>	<u>(412,870)</u>
<b>NET DECREASE IN CASH AND CASH EQUIVALENTS</b>	(1,162,117)	(751,403)
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD</b>	<u>7,710,078</u>	<u>8,061,169</u>
<b>CASH AND CASH EQUIVALENTS AT END OF PERIOD</b>	<u><b>6,547,961</b></u>	<u><b>7,309,766</b></u>
<b>Non-cash item:</b>		
Financial statements' translation differences	<u>209,449</u>	<u>(605,656)</u>
Other reserves (Note 12)	<u>(683,303)</u>	<u>-</u>

The accompanying notes from 1 to 14 form an integral part of these interim consolidated financial statements.

**Saudi Telecom Company**  
**(a Saudi Joint Stock Company)**  
**Notes to the Interim Consolidated Financial Statements for the Three and Six-Month**  
**Periods Ended June 30, 2010 (Unaudited)**

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**1 GENERAL**

Saudi Telecom Company (the “Company”) was established as a Saudi Joint Stock Company pursuant to Royal Decree No. M/35, dated 24 Dhul Hijja 1418 H (April 21, 1998) which authorized the transfer of the telegraph and telephone division of the Ministry of Post, Telegraph and Telephone (“MoPTT”) (hereinafter referred to as “Telecom Division”) with its various components and technical and administrative facilities to the Company, and in accordance with the Council of Ministers’ Resolution No. 213 dated 23 Dhul Hijja 1418 H (April 20, 1998) which approved the Company’s Articles of Association (the “Articles”). The Company was wholly owned by the Government of the Kingdom of Saudi Arabia (the “Government”). Pursuant to the Council of Ministers’ Resolution No. 171 dated 2 Rajab 1423 H (September 9, 2002), the Government sold 30% of its shares.

The Company commenced its operations as the provider of telecommunications services throughout the Kingdom of Saudi Arabia (the “Kingdom”) on 6 Muharram 1419 H (May 2, 1998), and received its Commercial Registration No. 1010150269 as a Saudi Joint Stock Company on 4 Rabi Awal 1419 H (June 29, 1998). The Company’s head office is located in Riyadh.

The Company has various investments in subsidiaries, associates and joint ventures collectively known for the financial statements purposes as (the “Group”). The details of these investments are as follows:

<u>Company Name</u>	<u>Ownership</u>	<u>Accounting Treatment</u>
Arabian Internet and Communications Services Co. - The Kingdom	100%	Full Consolidation
Telecom Investment Company Ltd – The Kingdom	100%	Full Consolidation
STC Bahrain ( BSCC) – Bahrain	100%	Full Consolidation
Gulf Digital Media Holding (BSCC) – Bahrain	51%	Full Consolidation
Kuwait Telecom Company Ltd. - Kuwait	26%	Full Consolidation
PT Natrindo Telepon Seluler (“NTS”) - Indonesia	51%	Proportionate Consolidation
Oger Telecom Ltd. - U.A.E.	35%	Proportionate Consolidation
Binariang GSM SDN BHD (“Binariang”) - Malaysia	25%	Proportionate Consolidation
Arab Submarine Cables Company Ltd. - The Kingdom	48.6%	Equity Method
Arab Satellite Communications Organization (“Arabsat”) - The Kingdom	36.66%	Equity Method

The main activities of the Group comprise the provision of a variety of telecommunications services which include mobile (second and third generations), fixed local national and international telephone services and data services such as data transmission, leased lines and internet services.

**2 SIGNIFICANT ACCOUNTING POLICIES**

The accompanying interim consolidated financial statements are prepared in accordance with accounting standards generally accepted in the Kingdom. The financial statements of the Group include the financial statements of the Company, its subsidiaries, associates and joint ventures for the period ended June 30, 2010.

The significant accounting policies used for the preparation of the interim consolidated financial statements mentioned below are in conformity with the accounting policies detailed in the audited consolidated financial statements for the year ended December 31, 2009.

Intra-Group balances and transactions and any unrealized gains arising from intra-group transactions, if material, are eliminated in preparing the consolidated financial statements.

**Saudi Telecom Company**  
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**Notes to the Interim Consolidated Financial Statements for the Three and Six-Month  
Periods Ended June 30, 2010 (Unaudited)**

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The preparation of the financial statements in conformity with accounting standards generally accepted in the Kingdom requires the use of accounting estimates and assumptions which affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the amounts of revenue and expenses during the financial period.

The significant accounting policies are summarized below:

**a) Period of the financial statements**

The Group's financial year begins on January 1 and ends on December 31 of each Gregorian year.

The interim consolidated financial statements are prepared on the basis of integrated periods, which views each interim period as an integral part of the financial year. Accordingly, revenues, gains, expenses and losses of the period are recognized during the period.

**b) Interim results**

The results of operations for the interim period may not represent a proper indication of the annual results of operations.

**c) Revenue recognition**

Revenue is recognized, net of discounts, when services are rendered based on the access to, or usage of, the exchange network and facilities. Usage revenues are based upon fractions of traffic minutes processed, applying rates approved by the Communications and Information Technology Commission ("CITC").

- Charges billed in advance are deferred and recognized over the period in which the services are rendered.
- Unbilled revenue is recognized in the period to which it relates.
- Revenue is recognized upon collection when collectability is highly uncertain.

**d) Cash and cash equivalents**

Cash and cash equivalents consist of cash on hand, balances with banks and all highly liquid investments with maturity of 90 days or less from the acquisition date.

**e) Accounts receivable**

Accounts receivable are shown at their net realizable values, which represent billings and unbilled usage revenues net of allowances for doubtful debts.

**f) Property, plant and equipment and depreciation**

1. Prior to May 2, 1998, the Telecom Division did not maintain sufficiently detailed historical information to record property, plant and equipment based on historical cost. Consequently all property, plant and equipment transferred by the Telecom Division on May 2, 1998 has been recorded based on a valuation performed by the Company with the assistance of independent international and local valuation experts. The principal bases used for valuation are as follows:

- Land	Appraised value
- Buildings, plant and equipment	Depreciated replacement cost

2. Other than what is mentioned in (1) above, property, plant and equipment acquired by the Group are recorded at historical cost.



**Saudi Telecom Company**  
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**Notes to the Interim Consolidated Financial Statements for the Three and Six-Month  
Periods Ended June 30, 2010 (Unaudited)**

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3. Cost of the network comprises all expenditures up to the customer connection point, including contractors' charges, direct materials and labor costs up to the date the relevant assets are placed in service.
4. Property, plant and equipment, excluding land, are depreciated on a straight line basis over the following estimated useful lives:

	<u>Years</u>
Buildings	20 – 50
Telecommunications plant and equipment	3 – 25
Other assets	2 – 8

5. Repairs and maintenance costs are expensed as incurred, except to the extent that they increase productivity or extend the useful life of an asset, in which case they are capitalized.
6. Gains and losses resulting from the disposal/sale of property, plant and equipment are determined by comparing the proceeds with the book values of disposed-off/sold assets, and the gains or losses are included in the interim consolidated statement of income.
7. Leases of property, plant and equipment where the Group assumes substantially all benefits and risks of ownership are classified as capital leases. Capital leases are recorded at the inception of the lease at the lower of the fair value and the present value of the minimum lease payments. Each lease payment is to be allocated between the finance charge, which is expensed in the current period and the reduction in the liability under the capital lease.

Assets leased under capital leases are depreciated over their estimated useful lives.

**g) Intangible assets**

**Goodwill**

- Goodwill arises on the acquisition of stakes in subsidiaries and joint ventures. It represents the excess of the cost of the acquisition over the Group' share in the fair value of the net assets of the subsidiary or the joint venture at the date of acquisition.
- Goodwill is recorded at cost and is to be reduced by impairment losses (if any).

**Spectrum rights and Second/Third Generation licenses**

These intangible assets are recorded upon acquisition at cost and are amortized starting from the date of service provisioning on a straight line basis over their useful lives or statutory durations, whichever is shorter.

**h) Impairment of non-current assets**

The Group reviews periodically non-current assets to determine whether there are indications that they may be impaired. When such indications are present the recoverable amount of the asset should be estimated. If the recoverable amount of the asset cannot be determined individually, then the cash generating unit to which the asset relates is to be used instead. The excess of the carrying amount of the asset over its recoverable amount is treated as impairment in its value to be recognized in the interim statement of income of the period in which it occurs. When it becomes evident that the circumstances which resulted in the impairment no longer exist, the impairment amount (except for goodwill) will be reversed and recorded as income in the interim consolidated statement of income of the period in which such reversal is determined. Reversal of an impairment loss shall not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset in previous financial periods.

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**Periods Ended June 30, 2010 (Unaudited)**

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**i) Investments**

**Subsidiaries**

Entities controlled by the Company are classified as subsidiaries. Control is defined as the power to use, or direct the use, of another entity's assets in order to gain economic benefits. The financial statements of subsidiaries are included in the consolidated financial statements of the Group from the date control commences until the date it ceases.

**Investments in joint ventures**

A joint venture is a contractual arrangement whereby the Group and other parties undertake an economic activity which is subject to joint control. That is when the strategic financial and operating policy decisions relating to the activities of the joint venture require the unanimous consent of all the parties sharing control.

Contractual arrangements that involve a separate entity in which each venture has an interest are referred to as jointly controlled entities.

In the interim consolidated financial statements the Group reports its interests in jointly controlled entities using proportionate consolidation, whereby the Company's share of the assets, liabilities, income and expenses of jointly controlled entities is combined on a line-by-line basis with the equivalent items in the Company's financial statements.

Goodwill arising on the acquisition of the Group's interest in a jointly controlled entity is accounted for in accordance with the Group's accounting policy for goodwill.

**Investments accounted for under the equity method (Associates)**

Associates are those corporations or other entities on which the Group exercises significant influence, but which it does not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Significant influence is the power to participate in the financial and operating policy decisions of the associate but not the power to exercise control over those policies.

The Company accounts for investments in entities in which it has a significant influence under the equity method. Under the equity method, the Company records the investment on acquisition at cost, which is adjusted subsequently by the Company's share in the net income (loss) of the investee, the investee's distributed dividends and any changes in the investee's equity, to reflect the Company's share in the investee's net assets. These investments are reflected in the interim consolidated balance sheet as non-current assets, and the Company's share in the net income (loss) of the investee is presented in the interim consolidated statement of income.

**j) Zakat**

The Company calculates and reports the zakat provision based on Shareholders' equity in its interim consolidated financial statements in accordance with Zakat rules and principles, and the instructions of the Department of Zakat and Income Taxes in the Kingdom. Adjustments arising from final zakat assessments are recorded in the period in which such assessments are approved.

**k) Taxes**

Taxes relating to entities invested in outside the Kingdom are calculated in accordance with tax laws applicable in their countries.

**Deferred tax assets**

Deferred tax assets of foreign entities are recognised only to the extent that it is probable that future taxable profits will be available against which the temporary differences of the foreign entities can be

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utilized. This involves judgement regarding the future financial performance of the particular entity in which the deferred tax asset has been recognised.

**l) End of service benefits**

The provision for employees' end of service benefits represents amounts due and payable to the employees upon the termination of their contracts, in accordance with the terms and conditions of the laws applicable in the Kingdom and the countries invested in.

**m) Foreign currency transactions**

**Functional and presentation currency**

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). These interim consolidated financial statements are presented in Saudi Riyals.

**Transactions and balances**

Balances of monetary assets and liabilities denominated in foreign currencies of specific amounts are translated using rates of exchange prevailing at the interim consolidated balance sheet date.

Gains and losses arising on the settlement of foreign currency transactions, and unrealized gains and losses resulting from the translation to Saudi Riyals of foreign currency denominated monetary balances are recorded in the interim consolidated statement of income.

**Entities of the Group (translation of financial statements)**

The results and financial position of all Group entities that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- Items of shareholders' equity (except retained earnings) are translated at the rate prevailing on the acquisition date.
- Retained earnings are translated as follows: retained earnings translated at the end of last year plus net income for the year as per the translated income statement less declared dividends translated at the rate prevailing on the date of declaration.
- Income statement items are translated using the weighted average rate for the period. Material gains and losses are translated at the rate prevailing on the date of their occurrence.
- All resulting exchange differences, if material, are recognised as a separate component of shareholders' equity.

When those entities are partially sold out or disposed of, exchange differences that were recorded in shareholders' equity should be recognized in the interim consolidated statement of income as part of the gains or losses on sale.

**n) Contingent liabilities**

A contingent liability is a possible obligation which may arise from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group, or a present obligation that is not recognized because it is not probable that an outflow of resources will be required to settle the obligation. If the amount of the obligation cannot be measured with sufficient reliability, then the Group does not recognize the contingent liability but discloses it in the interim consolidated financial statements.

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**Periods Ended June 30, 2010 (Unaudited)**

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**o) Cost of services**

Represents all costs incurred by the Group on rendering of services, which are directly related to revenues generated from the use of the network, including government charges and access charges.

**p) Selling and marketing expenses**

Represent all costs incurred by the Group, which are directly related to the marketing, distribution and sale of services. They are expensed as incurred when it is not possible to determine the relevant benefiting periods. Otherwise, they will be charged to the relevant periods.

**q) Administrative and general expenses**

Represent all the operating expenses incurred by the Group that cannot be directly linked to the costs of services or selling and marketing expenses. They are expensed as incurred when it is not possible to determine the relevant benefiting periods. Otherwise, they will be charged to the relevant periods.

**r) Earnings per share**

Earnings per share are calculated by dividing operating income and other operations before eliminating Non-controlling interest, and net income for the financial period, by the weighted average number of shares outstanding during the period.

**s) Financial derivatives**

The Group uses derivative financial instruments to hedge its exposure to certain parts of the risk of cost ratios resulting from financing activities, and designated these cash flow hedges for the protection of price risk loans. The Group does not use derivatives for speculative purposes. Financial derivatives are measured at fair value at the date of the contract, and re-measured at fair value at the date of subsequent financial periods. In the event of failure to comply fully with the requirements of hedge accounting in accordance with GAAP, the change in fair value of derivative financial instruments is included under finance cost in the interim consolidated statement of income.

**3 INTANGIBLE ASSETS, NET**

Intangible assets include the goodwill arising on the acquisition of the Group's shares in Binariang, NTS and Oger Telecom Ltd, in addition to the Company's share in the goodwill recorded in the financial statements of Binariang and Oger Telecom Ltd.

The companies invested in, which resulted in intangible assets, are:

**Binariang GSM SDN BHD "Binariang" – Malaysia**

Binariang is a Malaysian investment holding company that had owned 100% of Maxis, the then un-listed Malaysian holding group operating in the telecommunications sector in Malaysia. In November 2009, 30% of Maxis' shares were offered for public subscription and the company was subsequently listed in the Malaysian stock market. The percentage ownership of Binariang in Maxis has accordingly reduced to 70%.

Binariang has other investments in telecommunications companies in both of India and Indonesia, holding 74% of Aircel - India and 44% of NTS - Indonesia. The Company acquired 25% of Binariang in September 2007.

## **Saudi Telecom Company** **(a Saudi Joint Stock Company)**

### **Notes to the Interim Consolidated Financial Statements for the Three and Six-Month Periods Ended June 30, 2010 (Unaudited)**

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#### **PT Natrindo Telepon Seluler “NTS” - Indonesia**

NTS obtained the license to operate a third generation mobile network in Indonesia and it started the commercial provisioning of this service in the first of quarter 2008. The Company acquired 51% of NTS in September 2007.

#### **Oger Telecom Ltd. - U.A.E.**

Oger Telecom Ltd. is a company registered in Dubai, the United Arab Emirates, having investments in companies operating in the telecommunications sector in Turkey and South Africa. The Company acquired 35% of Oger Telecom Ltd in April 2008.

During 2009, Oger Telecom Ltd. changed the functional currency of one of its subsidiary companies in Turkey to the US Dollar, due to changes in events and circumstances following the acquisition by STC Group of 35% of its share capital, with prospective application in accordance with the accounting standards.

#### **Kuwait Telecom Company Ltd. – Kuwait**

In December 2007, the Company acquired 26% of the KD 50 million share capital of the Kuwait Telecom Company. This company operates in the field of mobile services, and has commenced commercial operations in December 2008.

#### **STC Bahrain (BSC Closed) – Bahrain**

STC Bahrain (BSC Closed) was established in the Kingdom of Bahrain in February 2009, and the Company owns 100% of its BHD 75 million share capital. This company operates in the field of mobile services, international telecommunications and other related services, and has commenced commercial operations in March 2010

Intangible assets consist of the following:

(Thousands of Saudi Riyals)	<u>2010</u>	<u>2009</u>
Licenses	15,455,943	14,787,575
Goodwill arising on the consolidation of financial statements	5,287,280	5,630,432
Trade marks and customer relations	3,866,104	4,409,789
Goodwill arising on the acquisition of 25% in Binariang	1,753,114	1,753,114
Goodwill arising on the acquisition of 35% in Oger Telecom Ltd.	826,395	826,395
Goodwill arising on the acquisition of 51% in NTS	713,191	713,191
Other	<u>3,172,887</u>	<u>1,349,816</u>
	<u>31,074,914</u>	<u>29,470,312</u>

#### **4 BORROWINGS**

They are composed of:

(Thousands of Saudi Riyals)	<u>2010</u>	<u>2009</u>
Short-term	8,197,976	7,143,370
Long-term	<u>22,584,274</u>	<u>25,527,569</u>
	<u>30,782,250</u>	<u>32,670,939</u>

As of June 30, 2010, the Group's share in the investees' borrowings amounted to SR 18,878 million.

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**5 COST OF SERVICES**

Cost of services consists of the following:

(Thousands of Saudi Riyals)	<u>Three Months ended</u>		<u>Six Months ended</u>	
	<u>June 30,</u>		<u>June 30,</u>	
	<u>2010</u>	<u>2009</u>	<u>2010</u>	<u>2009</u>
Access charges	2,183,275	1,928,097	4,086,831	3,230,744
Government charges (*)	1,355,251	1,413,887	2,783,004	2,803,301
Repairs and maintenance	315,586	394,981	1,161,073	812,279
Employee costs	804,579	844,795	1,560,988	1,608,366
Other	<u>597,661</u>	<u>369,329</u>	<u>1,024,221</u>	<u>726,638</u>
	<u>5,256,352</u>	<u>4,951,089</u>	<u>10,616,117</u>	<u>9,181,328</u>

“Other” comprises different items, the main ones being: rent of equipment, property and vehicles, utility expenses and consultancy fees.

(\*)The details of government charges are as follows:

(Thousands of Saudi Riyals)	<u>Three Months ended</u>		<u>Six Months ended</u>	
	<u>June 30,</u>		<u>June 30,</u>	
	<u>2010</u>	<u>2009</u>	<u>2010</u>	<u>2009</u>
The Company	1,134,838	1,155,610	2,216,815	2,365,001
Other Group’s companies	<u>220,413</u>	<u>258,277</u>	<u>566,189</u>	<u>438,300</u>
	<u>1,355,251</u>	<u>1,413,887</u>	<u>2,783,004</u>	<u>2,803,301</u>

**6 SELLING AND MARKETING EXPENSES**

Selling and marketing expenses consist of the following:

(Thousands of Saudi Riyals)	<u>Three Months ended</u>		<u>Six Months ended</u>	
	<u>June 30,</u>		<u>June 30,</u>	
	<u>2010</u>	<u>2009</u>	<u>2010</u>	<u>2009</u>
Advertising and publicity	673,887	569,259	1,280,536	1,151,960
Employee costs	522,957	492,637	1,005,713	957,216
Doubtful debts expense	317,379	252,384	784,644	501,626
Printing of telephone cards and stationery	65,523	133,611	170,955	166,024
Repairs and maintenance	29,510	30,368	57,350	56,897
Other	<u>175,516</u>	<u>155,237</u>	<u>354,404</u>	<u>268,617</u>
	<u>1,784,772</u>	<u>1,633,496</u>	<u>3,653,602</u>	<u>3,102,340</u>

“Other” comprises different items, the main ones being: rent of equipment, property and vehicles, and telecom, postage, courier, security and safety expenses.

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**7 ADMINISTRATIVE AND GENERAL EXPENSES**

Administrative and general expenses consist of the following:

(Thousands of Saudi Riyals)	<u>Three Months ended</u>		<u>Six Months ended</u>	
	<u>June 30,</u>		<u>June 30,</u>	
	<u>2010</u>	<u>2009</u>	<u>2010</u>	<u>2009</u>
Employee costs	530,167	510,078	966,084	947,995
Repairs and maintenance	122,796	95,043	207,805	192,563
Rent of equipment, property and vehicles	56,003	47,901	120,869	90,691
Consultancy & legal and professional fees	67,770	22,900	166,908	105,800
Utilities	60,651	43,990	88,176	85,028
Other	<u>208,823</u>	<u>233,828</u>	<u>327,559</u>	<u>364,396</u>
	<u>1,046,210</u>	<u>953,740</u>	<u>1,877,401</u>	<u>1,786,473</u>

“Other” comprises different items, the main ones being: insurance premiums, stationery, freight, handling, postage and courier expenses.

**8 DEPRECIATION AND AMORTIZATION**

(Thousands of Saudi Riyals)	<u>Three Months ended</u>		<u>Six Months ended</u>	
	<u>June 30,</u>		<u>June 30,</u>	
	<u>2010</u>	<u>2009</u>	<u>2010</u>	<u>2009</u>
Depreciation	1,904,090	1,719,314	3,748,812	3,318,257
Amortization	<u>254,977</u>	<u>188,077</u>	<u>516,821</u>	<u>363,611</u>
	<u>2,159,067</u>	<u>1,907,391</u>	<u>4,265,633</u>	<u>3,681,868</u>

**9 OTHER INCOME AND EXPENSES, NET**

Other income and expenses consist of the following:

(Thousands of Saudi Riyals)	<u>Three Months ended</u>		<u>Six Months ended</u>	
	<u>June 30,</u>		<u>June 30,</u>	
	<u>2010</u>	<u>2009</u>	<u>2010</u>	<u>2009</u>
Miscellaneous revenue	567,155	200,240	877,209	321,569
(Losses) / Gain on foreign currency exchange fluctuations	(10,186)	1,026,442	98,501	331,844
Miscellaneous expenses	<u>(188,049)</u>	<u>(311,826)</u>	<u>(437,591)</u>	<u>(493,709)</u>
	<u>368,920</u>	<u>914,856</u>	<u>538,119</u>	<u>159,704</u>

**10 COMMITMENTS AND CONTINGENCIES**

**Commitments**

- (a) The Group enters into commitments during the ordinary course of business for major capital expenditures, primarily in connection with its network expansion programs. Outstanding capital expenditure commitments approximated SR 2,229 million on June 30, 2010 (June 30, 2009: SR 4,340 million).
- (b) Certain land and buildings, for use in the Group’s operations, are leased under operating lease commitments expiring at various future dates. During the Second quarter and the Six-month periods

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ended June 30, 2010, total rent expense under operating leases amounted to SR 47 million and SR 224 million, respectively (Second quarter and the Six-month periods ended June 30, 2009: SR 134 million and SR 254 million, respectively).

**Contingencies**

The Group, in the normal course of business, is subject to proceedings, lawsuits and other claims. However, these matters are not expected to have a material impact neither on the Group's financial position nor on the results of its operations as reflected in the interim consolidated financial statements.

**11 SEGMENT INFORMATION**

The Group has identified its operating segments by the type of service provided by the Group and Transactions between operating segments occur in accordance with the normal trade provisions and terms. There are no other substantial revenues or expenses between segments.

The main operating segments of the Group comprise:

- GSM, for which the main services are: mobile, third generation services, prepaid cards, international roaming and messages.
- PSTN, for which the main services are: fixed line, card telephones, interconnect and international calls.
- DATA, for which the main services are: leased data transmission circuits, DSL and internet.
- Un-allocated, containing items which could not be linked with the main operating segments of the Group.

The following table shows the segmental information for the period:

(Thousands of Saudi Riyals)	<b><u>GSM</u></b>	<b><u>PSTN</u></b>	<b><u>DATA</u></b>	<b><u>Un-allocated</u></b>	<b><u>TOTAL</u></b>
Revenue from services	16,645,341	4,835,699	3,499,144	130,684	25,110,868
Interconnect revenues	1,074,278	2,950,115	456,703	-	4,481,096
Interconnect expenses	<u>(3,014,198)</u>	<u>(828,743)</u>	<u>(638,155)</u>	<u>-</u>	<u>(4,481,096)</u>
Net revenue from services	<u>14,705,421</u>	<u>6,957,071</u>	<u>3,317,692</u>	<u>130,684</u>	<u>25,110,868</u>
Depreciation and amortization	1,971,777	1,909,106	287,389	97,361	4,265,633
Net income	2,722,771	260,916	936,575	(86,246)	3,834,016
Total assets	41,989,991	37,636,519	6,455,455	26,077,765	112,159,730
Total liabilities	15,000,998	18,645,311	1,202,892	26,974,459	61,823,660



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The segmental information for the period ended June 30, 2009 was as follows:

(Thousands of Saudi Riyals)	<u>GSM</u>	<u>PSTN</u>	<u>DATA</u>	<u>Un-allocated</u>	<u>TOTAL</u>
Revenue from services	16,282,190	4,936,915	3,530,233	67,566	24,816,904
Interconnect revenues	819,319	3,133,660	249,066	-	4,202,045
Interconnect expenses	<u>(2,836,072)</u>	<u>(730,319)</u>	<u>(635,654)</u>	-	<u>(4,202,045)</u>
Net revenue from services	<u>14,265,437</u>	<u>7,340,256</u>	<u>3,143,645</u>	<u>67,566</u>	<u>24,816,904</u>
Depreciation and amortization	1,656,476	1,814,519	218,428	(7,555)	3,681,868
Net income	5,240,667	(491,403)	965,956	(237,254)	5,477,966
Total assets	37,006,493	39,596,926	5,153,754	23,030,143	104,787,316
Total liabilities	20,798,988	14,445,320	1,143,421	22,063,268	58,450,997

## 12 FINANCIAL DERIVATIVES

Hedging agreements have been concluded with a number of banks to hedge the cash flow risks of fluctuations in interest rates resulting from financing activities. The Group's share of the agreements amounted to USD 2,392 million (equivalent to SR 8,970 million). These agreements signed between the company and the banks are to swaps variables rates for fixed rates. The fair value of the effective Portion of these derivative amounted to SR 683 million as of June 30, 2010 recorded in the equity section of these interim consolidated financial statements.

The impact of these financial derivatives has been recorded in the interim consolidated financial statements of June 30, 2010, with no comparative effect due to lack of timely complete information. This reserve is the cumulative effect since inception of these contracts.

## 13 SUBSEQUENT EVENTS

The Board of Directors approved on July 20, 2010 interim dividends for the second quarter of the financial year 2010 amounting to SR 1,500 million, at the rate of SR 0.75 per share.

## 14 PRESENTATION IN THE INTERIM CONSOLIDATED STATEMENT OF INCOME

The Group has reclassified operating expenses to present cost of services, selling and marketing expenses, and administrative and general expenses. Accordingly, certain comparatives for the three and six –month periods ended June 30, 2009 have been reclassified to conform to the classifications used for the three and six –month periods ended June 30, 2010.