

The Q1 2018 results conference call

26 April 2018 at 12:00 CET

Presenters

Davor Tomašković

Hrvatski Telekom – President of the Management Board and CEO

Daniel Daub

Hrvatski Telekom - Member of the Management Board and CFO

Elvis Knežević

Hrvatski Telekom – Investor Relations

Operator: Good afternoon ladies and gentlemen and thank you for standing by. Welcome to today's HT Group Q1 results conference call.

All participants are in a listen only mode and if you wish to ask a question during today's question and answer session you will need to press star one on your telephone and wait for your name to be announced.

I must advise this conference is being recorded today on Thursday the 26th of April, 2018. I would now like to introduce and hand the conference over to you speaker today, Elvis Knežević. Please go ahead sir.

Elvis Knežević: Thank you. Ladies and gentlemen, good afternoon and welcome from Zagreb. Today our CEO Mr Davor Tomašković and Mr Daniel Daub, our CFO, will talk you through the highlights of our business and financial performance for the three months ended 31 March 2018, using presentation slides which I hope you have in front of you.

If not, please visit our website, at www.t.ht.hr where you can access the slides from our Investor's page. After the presentation Mr Tomašković and Mr Daub will be available for your questions.

Before we begin allow me to draw your attention to the harbour statements on page 2 of our presentation.

Allow me to introduce you to Mr Davor Tomašković, our CEO, who will outline our company's performance during the three months ended 31 March 2018.

Davor Tomašković: Good afternoon ladies and gentlemen and thank you for joining us today.

It is my pleasure to present the results from Hrvatski Telekom for the three months ended 31 March 2018. I will start the presentation with slide 3, which outlines the Group business highlights for the period.

We are pleased to report EBITDA and net profit growth at both HT Group and HT Croatia, despite a slight decline in revenue in the period.

Overall revenue was down 1.1% to HRK 1.80 billion, with HT Croatia revenue down 0.9% to HRK 1.66 billion.

This represents a broadly stable performance, although HT Croatia's revenue was impacted by a typically weak tourist period for mobile sales, as well as unfavorable project dynamics in our system solutions business. HT also exited some marginally profitable contracts in energy during the period.

Crnogorski Telekom, which was consolidated from 1 January 2017, remained under pressure, although the negative trends that have previously been seen have decreased significantly.

Crnogorski Telekom revenue fell almost 3% in the first quarter but EBITDA before exceptional items rose by more than 10%. We will provide further detail on this later in our presentation.

Despite the decline in revenue, HT Group EBITDA before exceptional items rose 1.6% to HRK 684 million in tandem with a 1 percentage point increase in margins to 38.1%.

The EBITDA growth is mainly a result of the continued successful transformation of the Group, as well as less intensive marketing initiatives. There has also been some impact from the implementation of the IFRS 15 accounting standard, which came into effect on 1 January 2018.

Net profit rose strongly, up 11.8% to HRK 166 million, largely due to EBITDA growth, lower redundancy costs compared to the same period last year, and a more favourable exchange rate compared to the first quarter of 2017, all related to HT Croatia.

On slide four we present two key developments: a decline in operating cash flow and continuation of our strong investments in our network and the core customer experience.

Net cash flow from operations was down 13.8% to HRK 563 million, mainly due to higher capex payments and adverse movements in working capital.

Capex in the three months to 31 March 2018 jumped 21% to HRK 442 million compared to the same period last year. This reflects a significant investment in our mobile and fixed broadband network, investments by HT Croatia in IT transformation and customer premises equipment, and greater capitalization of contracts for TV content rights in Crnogorski Telekom.

Our outlook for 2018 has not changed even accounting for the implementation of IFRS 15, which will have no material impact on our expectations.

Our share buyback program, started in July last year, will run until April 2021. Around 0.3% of total shares bought back by the end of 2017 were withdrawn in March 2018.

The international accounting standard IFRS 15 came into effect on 1 January 2018. HT Group has not restated the first quarter of 2017 as we have used the simplified initial application which means contracts that are not completed by 1 January 2018 are accounted for as if they had been recognized in accordance with IFRS 15 from the very beginning.

The net impact of the implementation of IFRS 15 on HT Group's main financials in the first quarter of 2018 are a negligible impact on revenue and a 1.2%, or HRK 8 million, increase in EBITDA before exceptional items.

Please turn now to slide 5 which details HT Croatia's revenue performance. During the three months to 31 March 2018, HT Croatia delivered a largely stable revenue performance despite the negative impact of seasonality on some businesses and the exit from marginally profitable contracts in our energy business.

HT Croatia total revenue was down 0.9% to HRK 1.66 billion in the first quarter of 2018. Within our mobile business, revenue rose 2.6% to HRK 693 million, helped by higher postpaid revenue when excluding IFRS 15, and higher handset sales.

However the growth was tempered somewhat by a slowing of visitor numbers, reversing a growth trend seen through 2017 and reflecting the low tourist season of the first quarter.

Fixed voice remained weak because of a fall in mainlines, traffic and average revenue per user, as people used their mobiles more and fixed lines less.

Fixed voice revenue fell 14.4% to HRK 188 million in the first quarter.

Broadband and TV revenue fell 2.2% in the period to HRK 320 million. This was due to a decline in broadband revenue caused by strong competition in the market. However, we delivered growth in TV sales, and have increased our customer base and enjoyed success with our Magenta 1 bundle of fixed, mobile and TV offers.

Fixed wholesale revenue fell 13.7% to HRK 84 million, largely because of revenue deductions from H1 Telekom after its merger with Optima Telekom in July 2017.

Other fixed revenue rose 11.8% to HRK 202 million. The rise reflects an increase in Optima Telekom revenue, resulting from the consolidation of H1 Telekom.

Our system solutions business remained largely stable, down only HRK 1 million to HRK 133 million in the first quarter. We have seen unfavorable yearly project

dynamics in the first quarter but expect that these will be compensated by improved dynamics in the remainder of the year. This business is growing revenue in all its portfolio segments.

Finally, miscellaneous revenue fell 3.8% to HRK 34 million largely because we exited some marginally profitable contracts. This impacted energy revenue, which fell to HRK 30 million in the first quarter 2018, from HRK 33 million in the same period last year.

I would now like to hand over to our CFO Daniel Daub who will walk you through our operational performance during the first quarter of 2018 in more detail.

Daniel Daub: Thank you Davor and good afternoon everyone. Please turn to slide 6 which describes the performance of HT Croatia's mobile business, where we have maintained our market and technology leadership position.

At the end of the first quarter 2018, HT Croatia's mobile market share by subscribers was 46.2%, only slightly down from the year earlier position of 47%. This is purely due to market development where FMS offers from our competition count their broadband customers as mobile subscribers.

Our mobile subscriber numbers rose 0.9% between the end of the first quarter 2017 and the end of the first quarter 2018, increasing by 19,000 as a 9.1% rise in postpaid subscribers offset an 8.3% decline in prepaid customer numbers.

Average revenue per user for the prepaid segment was unaffected by the introduction of IFRS 15, and rose 4.8% to HRK 42. However the introduction of IFRS 15 substantially impacted postpaid ARPU, which was down 19.9% to HRK 86. However, excluding the negative impact of IFRS 15, postpaid ARPU fell by a more moderate 5.3% to HRK 101.

In the three months to 31 March 2018, average minutes of use rose 5.3% to 220. The percentage of smartphones as a proportion of total handset sales was 90% in the postpaid segment in the first quarter, up 10 percentage points compared to the same period last year. HT Group's smartphone penetration was 57%.

At the end of the first quarter, our 4G network covered 76% of the population indoors and 98% outdoors.

At the end of 2017 we were recognized as the provider of the best mobile voice and data network in Croatia by P3 Communications, a network analytics and testing company, due to our ongoing efforts to improve our service quality.

Turning now to slide 7, our fixed line and IP business benefited from a rise in TV customers, although fixed mainlines and broadband lines decreased in the period.

At the end of the first quarter 2018, fixed mainlines were down 7.1% to 917,000 lines. Attractive mobile offers continue to persuade customers to substitute their fixed lines for mobiles, and regulation is also putting pressure on fixed lines.

We recognize that this is a trend that is unlikely to diminish, and we continue to develop churn prevention offers to mitigate this.

Broadband access lines at the end of the first quarter 2018 were 1.7% lower than the same period last year at 750,000 lines. Retail broadband access lines remained largely stable at 620,000, but the total number of lines was weighed down by an 8.4% decline in wholesale broadband access lines to 130,000. This decline can largely be attributed to more operators using their own infrastructure.

Meanwhile TV customers fared better, with 415,000 customers at the end of Q1 2018, compared with 408,000 at the end of the first quarter last year.

Fixed voice ARPU fell 9.5% to HRK 72, and broadband retail ARPU fell 6.1% to HRK 111 in the three months to March 31. Excluding the effect of IFRS 15, Fixed voice ARPU fell 8.6% to HRK 73 and broadband retail ARPU fell 4.9% to HRK 112.

TV ARPU remained stable at HRK 81, although it rose 1.9% to HRK 83 when the IFRS 15 effect is excluded.

Next Generation Access speeds greater than 30 megabits per second have been enabled for 58% of Croatian households, while 380,000 households are now enabled for FTTx access.

Following our acquisition of a majority stake in Crnogorski Telekom, we present standalone financial results for this business on slide 8.

Revenues at Crnogorski Telekom remained under pressure amidst onerous regulation and a highly competitive market.

However the negative trend in revenue has significantly abated, down 2.6% in Q1 2018 compared to the 8.1% decline we reported in the first quarter of 2017, and our transformation initiatives have strongly boosted EBITDA margins.

So, during the first quarter of 2018, revenue was down 2.6% to HRK 144 million as a 4.5% rise in mobile revenue to HRK 73 million failed to offset declines in all other areas of the business.

Fixed voice fell 7.5% to HRK 20 million, broadband and TV was down 5.6% to HRK 29 million, fixed wholesale slipped 10.5% to HRK 4 million, other fixed revenue was down 14.9% to HRK 13 million, and system solutions declined 13.1% to HRK 6 million.

Despite the downward trend in revenue, EBITDA before exceptionals rose strongly, up 10.6% to HRK 50 million on the back of lower operating expenses. This resulted in a strong rise in margin from 30.5% in Q1 2017 to 34.7% in Q1 2018.

Higher EBITDA helped Crnogorski Telekom report an 89.7% surge in net profit to HRK 8 million in the first quarter of 2018.

On slide 9, we outline the operational performance of Crnogorski Telekom, which shows a decline in customers and lines. However Crnogorski maintained its leading market position in mobile postpaid, fixed voice and broadband.

At the end of March 2018, mobile subscribers were 1.4% lower than the year earlier period, at 348,000. A rise in postpaid customers was insufficient to offset the decline in prepaid customer numbers.

The fall in fixed retail mainlines was more acute, down 10.4%% in the period to 119,000, while the number of broadband retail access lines fell 1.9% to 69,000. TV customers fell 3.3% to 56,000.

We are offering discounts to customers for adding broadband and IPTV components to their contracts, and we saw some positive development in fixed broadband and IPTV customer numbers in the first quarter. We are pleased to report an increase in customer satisfaction for both fixed and mobile services and for both consumer and business customer segments.

I will now hand back to Davor, who will outline our outlook for 2018

Davor Tomašković: Thank you Daniel. Please turn now to slide 10 for our Group outlook 2018.

The outlook remains unchanged from the guidance provided at the full year results in February, and the implementation of IFRS 15 has had no material impact on the published outlook.

We expect revenue in the current year to be slightly higher than last year's revenue of HRK 7.76 billion.

We are anticipating an EBITDA margin before exceptional items of around 40%, compared with the 40.5% reported for 2017.

Capex in 2018 is expected to be slightly lower than the HRK 1.89 billion spent in 2017.

And we will again continue to monitor and evaluate potential M&A opportunities.

Thank you for your attention. We are now ready to take your questions.