The Q2 2018 results conference call
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Presenters

Davor Tomašković
Hrvatski Telekom – President of the Management Board and CEO

Daniel Daub
Hrvatski Telekom - Member of the Management Board and CFO

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Hrvatski Telekom – Investor Relations

Operator: Thank you for standing by, and welcome to the HT Group H1 2018 Analyst Conference Call.

At this time, all participants are in a listen-only mode. There'll be a presentation, followed by a question and answer session, at which time, if you wish to ask a question, you will need to press "star" and "one" on your telephone. I must advise this conference is being recorded today, Thursday, the 26th of July, 2018.

I would now like to introduce and hand the conference over to your first speaker, 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 six months ended 30th June, 2018, using the 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 investors 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 Harbor statement on page two of our presentations.

Allow me to introduce you to Mr. Davor Tomašković, our CEO, who will outline our company's performance during the six months ended 30th June, 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 six months ended 30 June 2018. I will start the presentation with slide 3, which outlines the Group business highlights for the period.

We have achieved net profit and EBITDA growth at both HT Group and HT Croatia against a backdrop of broadly stable revenue. Across the Group, revenue in the first half was HRK 3.68 billion, down slightly from HRK 3.69 billion in the same period last year.

Revenue at HT Croatia was HRK 3.38 billion in the first half, from HRK 3.39 billion in the first half of 2017, remaining largely stable despite the exit from marginally profitable contracts in energy. Meanwhile Crnogorski Telekom revenue was 1.5% lower at HRK 300 million from HRK 305 million in H1 2017, as the business remained under pressure, although the negative trends have significantly decreased.

Earnings before interest, tax, depreciation and amortisation before exceptional items rose 0.9% in the first half to HRK 1.47 billion reflecting a rise in earnings at both HT Croatia and Crnogorski Telekom. HT Croatia earnings were up 0.6% in the six months to the end of June at HRK 1.36 billion, reflecting the success of transformation efforts that we have put in place as well as recently reduced spectrum fees and the positive impact of IFRS 15.

EBITDA before exceptionals at Crnogorski Telekom rose 4.7% to HRK 109 million, from HRK 104 million last year, as a result of lower operating costs and higher other operating income. Margin across the Group was up slightly to 40% from 39.5% in the first half of last year.

Net profit rose strongly to HRK 447 million from HRK 410 million, reflecting the EBITDA uplift, lower redundancy costs and a better exchange rate, all in HT Croatia.

Please turn to slide 4 which covers the financial and operational highlights at HT Group in the first half.

As you can see net cash flow from operations has decreased, but we continue to invest in our network and the customer experience. Operating cash flow was down 17.9% to HRK 1.01 billion in the six months to the end of June, mainly due to adverse movements in working capital.

HT Croatia operating cashflow fell 14% to HRK 964 million, and Crnogorski Telekom operating cashflow fell 58% to HRK 45 million.

Capital expenditure in the first half reflects our significant investment in mobile and fixed broadband networks, along with IT transformation investment and new product development in HT Croatia. Capex across the group was HRK 895 million in the first half, up 8.7% on last year. This breaks down as an 8.3% rise in capex at HT Croatia to HRK 822 million, and a 12.6% increase at Crnogorski Telekom to HRK 73 million.

Our outlook remains unchanged following the implementation of IFRS 15.
The international accounting standard IFRS 15 came into effect on 1 January 2018. HT Group has not restated the first half 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 recognised in accordance with IFRS 15 from the very beginning.

The net impacts of the implementation of IFRS 15 on HT Group's main financials in the first half of 2018 are a decrease in revenue of HRK 13 million or 0.3%, and an increase in EBITDA before exceptional items of HRK 25 million or 1.7%.

Please turn now to slide 5 which shows the standalone financial revenue performance for HT Croatia. We are reporting stable revenues despite exiting some marginally profitable contracts in our energy business, and it is also worth noting that our mobile and system solutions businesses produced good performances in the period.

Mobile revenue at HT Croatia was up 4.1% in the first half of 2018 to HRK 1.45 billion reflecting higher postpaid revenue (excluding IFRS), more revenue from visitors to Croatia, as well as strong handset sales.

Fixed voice fell 13.9% to HRK 375 million as mainlines, traffic and average revenue per user declined. This fixed decline is an industry-wide trend and we continue to try and mitigate the fixed to mobile substitution with proactive and reactive churn prevention offers and activities.

Broadband and TV revenues were slightly lower in the first half, falling 2% to HRK 646 million, dragged down by a fall in broadband which offset growth in TV revenue. Our Magenta 1 bundled offer helped boost the success of our TV business, with customer numbers rising in the period. However TV growth failed to overcome declines in our broadband revenues, which were impacted by the highly competitive broadband market and the need to compete with aggressively priced offers.

Fixed wholesale revenue fell 19.3% to HRK 158 million in the first six months of the year mainly due to revenue deductions from H1 Telekom, which merged with Optima Telekom on 1 July 2017.

Other fixed revenue rose 13.2% to HRK 406 million largely because of an increase in revenue at Optima Telekom following the first half consolidation of the Company.

We are pleased to report that system solutions revenue has reversed the trend seen in the first quarter and is now on track to show good growth for the full year 2018. Revenue in this segment rose 0.7% to HRK 278 million in the first half.

Finally, miscellaneous revenue, which includes our energy business and other non-telecoms services, reported a 0.8% decline in revenue to HRK 68 million. This was largely because we exited marginally profitable contracts in our energy business, lowering revenue slightly to HRK 59 million from HRK 64 million in the first half of 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.

HT Croatia's estimated market share by subscribers was 45.8% at the end of the first half, slightly down from the 46.3% at the end of June 2017, but still enough to maintain our leadership position in the mobile market. This is due to market development where FMS offers from our competition count their broadband customers as mobile subscribers.

We have increased the number of subscribers by 1.4% to 2.27 billion at the end of the first half. This increase reflects strong growth in postpaid customers, where subscriber numbers rose 6.7% to 1.29 billion, which offset a 4.8% decline in prepaid subscribers to 981 million.

Average revenue per user in the prepaid segment rose 2.5% to HRK 43 per month. However postpaid ARPU fell 21.2% to HRK 85 per month, due to the impact of the change to IFRS 15 accounting standards. Excluding the HRK 15 per month impact of IFRS 15, postpaid ARPU fell 4.8% to HRK 103 per month. This fall is mainly due to introduction of our Hybrid tariffs and RL@H impact. Average minutes of use rose 5.6% to 226.

Smartphone penetration continues to grow, with the smartphone proportion of total handset sales now 90% in the postpaid segment, up from 81% in the first half of 2017.

By the end of the first half, HT Croatia's 4G network had reached 78% population coverage indoors and 98% coverage outdoors. We have started the modernization of our mobile network in preparation for the introduction of 5G.

Slide 7 shows the performance of HT Croatia's fixed line and IP business, where TV customers and ARPU has risen but fixed mainlines and broadband lines have decreased.

The number of fixed mainlines continues to decline amid fixed to mobile substitution as customers are drawn to attractive mobile offers. Retail mainlines fell 5.9% to 846,000, while wholesale mainlines declined 21.2% to 57,000 at the end of the first half.

The effect of the general market trend towards mobile substitution pushed fixed voice ARPU down 8.7% to HRK 72.7, which includes a slight impact of IFRS 15. Excluding IFRS 15, fixed voice ARPU was down 7.8% to HRK 73.4.

Broadband access lines were also lower at the end of June 2018, down 2.1% to 750,000. Retail broadband access lines fell only slightly to 621,000 from 624,000 last year, but wholesale broadband customers dropped 9.1% to 129,000 due to the higher usage of operators' own infrastructure.

Broadband retail ARPU was down 5.7% to HRK 111, hit by stronger competition and aggressive offers in the market, as well as the impact of IFRS 15. Excluding IFRS 15 broadband retail ARPU was down 4.8% to HRK 112.

Encouragingly we attracted 4,000 new TV customers during the first half, ending the period with 415,000 customers. Consumers responded well to the continuous improvement of our service and program offers, especially through premium content and enriched exclusive TV content. This helped lift TV ARPU 1.5% to HRK 83. Excluding IFRS 15, TV ARPU rose healthy 2.8% to HRK 84.

Next Generation Access speeds greater than 30 megabits per second have been enabled for 58% of Croatian households, while 388,000 households are now enabled for optical fiber access with speeds of 100 megabits per second.

Please now turn to slide 8 which describes the standalone financial performance of Crnogorski Telekom. We are pleased to see that the revenue trend is stabilising and our transformation initiatives are paying off with a boost to EBITDA margins.

Total revenue fell 1.6% to HRK 302 million in the first half of 2018. The breakdown shows that mobile revenue rose 3.5% to HRK 154 million, boosted by handset sales and customer growth in the postpaid segment, which offset a decline in prepaid revenue.

Fixed voice fell 8.8% to HRK 38 million, continuing the trend towards declining fixed telephony.

Broadband and TV revenue in the first half fell 3.7% to HRK 58 million, as gains in TV revenues failed to offset the impact of lower ARPU on broadband revenues.

Meanwhile fixed wholesale revenue fell 12.9% to HRK 9 million and other fixed revenue was down 13% at HRK 25 million. System solutions revenue increased 6.0% in the first half to HRK 18 million, driven by changes in project seasonality.

EBITDA before exceptional items at Crnogorski Telekom rose 4.7% to HRK 109 million in the first half of 2018 as initiatives we have implemented to transform the business helped boost margins to 36.2% from 34% in the first half of 2017.

Net profit at Crnogorski Telekom jumped 54.2% to HRK 26 million in the first half of 2018.

Slide 9 describes Crnogorski Telekom’s mobile, fixed line and IP business, where customer numbers have risen in the mobile segment but declined in other key areas including fixed mainlines, broadband and TV.

Mobile subscriber numbers increased 1.6% to 359,000 at the end of June 2018, as successful efforts to attract postpaid customers with a renewed tariff portfolio offset a decline in prepaid subscribers. Postpaid subscribers rose 12.4% to 221,000 while prepaid subscribers fell 11.9% to 138,000. Crnogorski Telekom has already initiated new measures in the prepaid segment and is seeing some positive developments.

Fixed retail mainlines declined by 10.3% to 117,000 at the end of the first half, although sales efforts resulted in net additional fixed voice customers in June.
The number of broadband retail access lines has declined 0.6% to 70,000 at the end of the first half, and TV customers also showed a decline, down 1.8% to 57,000 in the same period.

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 first quarter results in April, 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.