

## **The Q1 2019 results conference call**

**26 April 2019 at 13:00 CET**

### **Presenters**

#### **Kostas Nebis**

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

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### **Operator**

Thank you for standing by and welcome to the Hrvatski Telekom Results conference call for the three months ended 31 March 2019.

At this time, all participants are in a listen-only mode. Today, there will be a presentation followed by a question and answer session at which time, should you wish to ask a question, you will need to press the <star> 1 on your telephone.

I must advise you that this conference is being recorded today Friday 26 April 2019. It is now my pleasure to hand you over to your first speaker today: Mr Elvis Knežević

Mr Elvis Knežević – please go ahead.

### **Elvis Knežević**

Thank you.

Ladies and gentlemen, good afternoon and welcome from Zagreb. Today our CEO Mr Kostas Nebis 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 2019, using presentation slides which I hope you have in front of you.

If not, please visit our website, at [www.t.ht.hr](http://www.t.ht.hr) where you can access the slides from our Investor's page. After the presentation, Mr Nembis 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 Kostas Nebis, our CEO, who joined us at the beginning of April. He will outline our company's performance during the three months ended 31 March 2019.

## **Kostas Nebis**

Thank you Elvis.

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

I'm delighted to have joined Hrvatski Telekom as CEO, and it is my pleasure to present for the first time the results from Hrvatski Telekom Group for the three months ended 31 March 2019.

I will start the presentation with slide 4, which outlines the business and financial highlights for the period.

Magenta1, our premium customer experience and benefits proposition, continues to attract broadband and TV customers, and we now have 209,000 households and 21,000 business accounts in Croatia.

We have maintained our leading market position across all areas of the business, underpinned by strong investments in mobile and fixed broadband networks, which have ensured our customers get the best experience.

The investment has increased superfast broadband coverage and access speeds across our fixed broadband network as well as helping us to modernise the mobile network throughout Croatia.

The latest 5G mobile technology is being introduced through a pilot network and data sessions within a real network environment. This pilot will be extended during 2019 to cover further locations.

During the period, Hrvatski Telekom participated in the 2600Mhz spectrum award and we acquired a block of two 20Mhz spectrum lots which will allow us to improve our network performance.

Following our announcement of the acquisition of HP Produkcija in November last year, we have now completed the process of buying the Evotv service provider.

Hrvatski Telekom is in the final stages of preparations to launch our Telekom Banking service in cooperation with Zagrebacka Bank, and there will be an official launch soon.

Finally for the operational review, our One App digital service now has 113,000 monthly active users.

Financially, we have delivered strong revenue and EBITDA performance and we are supporting our strong investment strategy with a high 21.8% capex to sales ratio.

The Group has applied new IFRS 16 accounting standards as of 1 January 2019, and we will be providing an 'after leases' comparison in our financial results.

The outlook for 2019 remains unchanged and our share buyback program is proceeding at an accelerated pace.

I would now like to hand over to our CFO Daniel Daub who will talk you through the accounting changes made as a result of the implementation of new IFRS accounting standards to our accounts.

### **Daniel Daub**

Thank you Kostas and good afternoon everyone. Slide 6 explains the accounting changes we have made by applying the new IFRS 16 standards to our accounts, eliminating the different treatment of finance and operating leases. To ensure comparability we have introduced 'AL' or 'after leases' steering KPIs.

The IFRS 16 lease accounting change became effective from 1 January 2019 and has a major impact on telecoms from the side of the lessee. Lease contracts usually relate to the rental of buildings, retail shops, collocation spaces, rooftops for cell sites, network infrastructure and vehicles, for example.

The application of IFRS 16 will mean that relevant leases will be recognised as finance leases where they were previously recognized as operating leases.

HT Group has not restated its 2018 accounts to reflect the IFRS 16 changes, only the income statement, cash flow and the respective KPIs are adjusted for the effect of IFRS 16.

We have stated our 2019 outlook on an 'after lease' basis.

As of 2019, the steering logic will be based on an 'after lease' view, which means that all the financials which are impacted by IFRS 16 will be proforma adjusted to eliminate the impact of IFRS 16.

The relevant 'after lease' KPIs for 2018 and 2019 are EBITDA AL and Capex AL.

I will now hand back to Kostas, who will outline HT Group financial highlights.

## **Kostas Nebis**

Thank you Daniel. Let's now move to slide 8, where the Group financial highlights for the first quarter show a rise in EBITDA and net profit, although revenue was slightly down.

Revenue in the three months to 31 March 2019 amounted to HRK 1.78 billion, 1.3% lower compared to the prior year period, reflecting a decline at both Hrvatski Telekom and Crnogorski Telekom.

Croatia's revenue, which was down 1.3% to HRK 1.63 billion, was impacted by the decision to exit our energy business in September last year. This year however, we consolidated the acquisition of Evotv as of 1 March 2019.

The decline at Crnogorski Telekom, where revenue fell by 1.4% to HRK 141 million, reflects the tough competitive and regulatory environment in Montenegro. But even though this pressure remains, the negative trends from previous years have significantly decreased.

EBITDA, adjusted for the 'after lease' accounting change, rose 3.4% to HRK 673 million in the first quarter of 2019, partially influenced by the one-off positive impact from the Evotv transaction. However, if we take into consideration some other one-off impacts we see that underlying EBITDA development was more modest, showing growth of around 1%.

We will provide additional details on the "after lease" concept with regards to our EBITDA on the next slide in this presentation.

EBITDA margin for the Group rose 1.7 percentage points to 37.9%.

We reported a 14.1% rise in net profit to HRK 190 million in the first quarter. This reflects higher EBITDA AL and lower redundancy costs.

I will now hand back to Daniel, who will talk you through details of accounting changes and performance of the whole Group, Hrvatski Telekom in Croatia and Crnogorski Telekom.

## **Daniel Daub**

Thank you Kostas. Now let's turn to slide 9 where we will take a more detailed look at the new accounting treatment and its impact on HT Croatia's EBITDA.

First of all, I'd like to say a few words about the basic principles of the "after lease" concept. In essence, the new IFRS 16 accounting standard increases EBITDA significantly due to the elimination of operating lease expenses.

In order to add transparency in the year on year development and ensure comparability of EBITDA before and after IFRS 16 we have introduced the AL ("after lease") concept.

Lease depreciation and interest are added back to EBITDA, and by doing this the IFRS 16 impact is eliminated.

Typically, this adjustment would bring EBITDA AL to around the same level as EBITDA before IFRS 16.

However, due to circumstances specific to Electronic Communication Infrastructure - or ECI - this is not case for HT.

This is because ECI contracts were already capitalized before the implementation of IFRS 16. Depreciation and lease interest are included in the AL concept, resulting in EBITDA AL being at a lower level compared to EBITDA before IFRS 16, or reported EBITDA.

2018 is not restated but the proforma adjusted on a “like for like” comparison reasons with 2019 effect

IFRS 16 and the AL concept have no material impact on Net revenue and net profit.

Let's also take a closer look at the numbers on left hand side - and starting from 2019:

- After elimination of operating lease expenses, Q1 2019 EBITDA including IFRS 16 is amounting to HRK 707 million.
- When adding lease depreciation and interest in, we are coming to EBITDA AL in amount of HRK 627 million
- When adjusting 2018 for completely the same amount of 2019 IFRS 16 impact (in order to have comparable EBITDA AL view) – we arrive to HRK 601 million which is lower than old reported EBITDA (or EBITDA before IFRS 16 impact) as already explained.

Please turn to slide 10 which describes our operating cash flow position and the continued investment in our network and improvements to customer experience.

Net cash flow from operations fell 8.4% to HRK 559 million mainly because of adverse movements in working capital. Meanwhile capital expenditure was 12.7% lower in the first quarter at HRK 386 million. This decline reflects lower content capitalisation, and has not impacted the significant investment we continue to make in our mobile and fixed broadband networks.

Slide 11 explains HT Croatia revenue performance for the period, which was impacted by our exit from the energy business last year. Total revenue across the Group fell 1.2% to HRK 1.64 billion.

Broken down by segment, mobile revenue in the first quarter rose 4.7% to HRK 725 million. This reflects strong growth in the postpaid market as a result of our successful prepaid to postpaid migration strategy.

In addition, convergent offers helped lift volumes of smartphone sales while also driving smartphone penetration across our subscriber base.

Fixed voice revenue continued its downward trend, with revenue falling 10.3% to HRK 169 million as mainline sales, traffic and average revenue per user all declined as a result of competitive pressures and fixed to mobile substitution.

Broadband and TV revenue fell slightly, down 0.9% to HRK 317 million, dragged down by a slide in broadband revenue. This offsets growth in TV revenue which was boosted by our premium Magenta1 offers, more TV customers and one month of revenue from our Evotv acquisition.

Fixed wholesale revenue fell 7.9% to HRK 78 million mainly due to lower transit traffic.

We saw an improvement in revenue in our system solutions segment, up 2.1% to HRK 136 million reflecting more favourable yearly project dynamics in the first quarter of 2019 compared to the same period last year.

Miscellaneous revenue fell to HRK 3 million from HRK 34 million in Q1 2018 because of the sale of the energy business last year, which accounted for HRK 31 million of revenues in the first quarter of 2018.

Slide 12 describes our mobile business in Croatia, where we maintained leadership in the overall market and in mobile technology.

At the end of the first quarter 2019, HT maintained its leading market position with a share of 45.6%, down slightly from the 46.2% reported in the first quarter of 2018 due to competitors' active promotion of their FMS offers.

Despite this slight decline, we increased the number of subscribers across HT Croatia by 1.5%, largely driven by a 4.5% increase in postpaid customers to 1.33 million. This more than offset a 2.6% decline in prepaid customers to 933,000 at the end of the first quarter.

Average revenue per user fell 5.3% to HRK 40 in the prepaid segment and slipped 0.6% to HRK 85 in the postpaid customer Group as higher value prepaid customers migrated to the postpaid portfolio.

HT Croatia's smartphone proportion of total handset sales is now 94% in the postpaid segment, up from 90% in the first quarter of 2018. Smartphone customers account for 66% of HT Croatia's overall subscriber base which grew from 63% in Q1 2018.

By the end of the first quarter 2019, HT Croatia's 4G network had reached 99% coverage outdoors and 84% population coverage indoors. We continued the modernization of our mobile network throughout Croatia as we build the foundations for the introduction of 5G.

I'm also proud to report that we again received the P3 award for best mobile data and crowdsourcing network in Croatia for the second consecutive year.

Please now turn to slide 13 for details of HT Croatia's fixed line and IP business. Here the acquisition of Evotv boosted the number of TV customers, but fixed mainlines and broadband lines decreased.

Fixed mainlines, which have been in decline for many years due to fixed to mobile substitution, regulation and enforced competition, declined 6.7% to 856,000. Retail fixed mainlines were down 6.2% to 805,000 and wholesale fixed mainlines fell 13.6% to 51,000 in the first quarter of the year. We continue our endeavours to mitigate these declines through the introduction of a range of tailor made propositions and customer base management activities.

Fixed voice ARPU was down 4.2% to HRK 69.

In addition, broadband access lines declined 0.7% to 745,000 in the period, with retail lines down 0.6% to 617,000 and wholesale broadband access lines down 1.3% to 128,000. Competition for broadband customers is fierce and we are focused on value-added offers like our Ultra MAX packages to attract new customers. Strong competition and aggressive offers in the market also dragged average revenue per account (ARPA) down 6.4% to HRK 104 in the first quarter.

While fixed and broadband lines were depressed, TV customers rose strongly, up 17.8% to 488,000 by the end of the first quarter. This boost mainly came from the acquisition of Evotv which uses DVBT technology. TV ARPU was also up 6.7% to HRK 87.

As a result of investments into the fixed infrastructure, NGA coverage for speeds above 30 Mbps reached the level of 59% and coverage for above 100 Mbps reached 22% of Croatia's total 1.5 million households.

Slide 14 describes the standalone performance of Crnogorski Telekom, which has come under pressure mainly because of a steep decline in fixed voice revenue.

Revenue fell by 2.5%. This was largely the result of negative trends in Fixed Voice and Mobile Prepaid, which was partly offset by higher year on year mobile postpaid revenues and an increase in System Solutions revenue.

Broadband and TV revenue have remained broadly stable.

However, we have seen a decline in EBITDA of 9.1%. This was mainly the result of the absence of some positive one-off impacts reported in Q1 2018, including the sale of real estate and a change in accounting standards. In addition, we saw lower revenues from fixed voice.

I will now hand back to Kostas, who will outline our outlook for 2019

**Kostas Nebis**

Thank you Daniel.

Please turn to slide 15 for our Group outlook 2019 which remains unchanged but is now reported on an 'after leases' basis.

We expect to maintain revenue at around the 2018 level of HRK 7,783 million, with a margin for EBITDA AL before exceptionals of around 38% in 2019, against the 38.6% achieved in 2018.

Capex AL is also expected to remain around the 2018 level of HRK 1,826 million.

In 2019, we will again continue to monitor and evaluate M&A opportunities following the completion of our acquisition of Evotv in the first quarter.

We are now ready to take any questions.