

The H1 2019 results conference call

25 July 2019 at 12:00 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

Operator

Thank you for standing by and welcome to the Hrvatski Telekom Results conference call for the six months ended 30 June 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 Thursday 25 July 2019. It is now my pleasure to hand you over to your first speaker today: Mr Elvis Knežević

Mr Elvis Knežević – please go ahead.

Mr 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 six months ended 30 June 2019, 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 Nebis 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. He will outline our company's performance during the six months ended 30 June 2019.

Mr Kostas Nebis

Thank you Elvis.

Good afternoon ladies and gentlemen and thank you for joining us today. It is my pleasure to present the results from Hrvatski Telekom Group for the six months ended 30 June 2019.

I will start the presentation with slide 3, which outlines the business and financial highlights for the period.

Before I go into the detail of our financial performance, I'd like to outline our overarching strategy as a business, and as the leading telecoms provider in Croatia.

We have identified for Hrvatski Telekom a key role in connecting all citizens across Croatia – including consumers, businesses and the public sector – with the opportunities that digitization brings across all aspects of our lives.

To drive this core objective, we have established a new brand positioning under the “Svijet boljih mogućnosti” or “A world of better opportunities”, pay off statement as we continue to empower every part of our society with the products, tools and skills to truly benefit from digital innovation and progress.

We play an integral role in paving the way for the technology and digital revolution that is changing the landscape of our country.

We need to ensure that the opportunity to connect businesses and people is available to everyone across the country, including those in rural communities, elderly people and others who have in the past been unable to access the clear benefits that digital skills and connectivity can provide.

At the same time, we need to educate the youth on the opportunities of new technology, while enabling innovation and competitiveness in the Croatian economy.

We've set out these aims in our manifesto on “Building a World of Better Opportunities”, and we are investing around HRK 1.8 billion this year alone to drive this strategy forward.

Indeed, we have for many years been investing strongly in our mobile and fixed broadband networks, with the aim of maintaining and building on our leadership in the industry, providing superior customer experience and best in class connectivity.

And while mobile is a large part of our business, we are equally focused on ensuring more people can access and enjoy our fixed broadband service.

Over the next two and a half years, we plan to make significant investments in our fiber network to enable 1.2 million of the 1.5 million Croatian households to get access to Next Generation Networks, with broadband speeds above 30 Mbps.

From July this year, HT introduced Hybrid access to customers in rural areas enabling significantly higher speeds through the combination of fixed and mobile technologies.

Our investments across the board are paying off and we are achieving strong industry recognition, having been awarded certificates by OOKLA, the global leader in internet testing, data and analysis, for the fastest mobile network and best mobile coverage in Croatia, based on real customer experiences.

Our focus on improving our services and converged offers also continue to bear fruit. Magenta1, our premium customer experience and benefits proposition, continues to attract broadband and TV customers. We now have 227,000 households and 30,000 business accounts, a penetration on BB base of 53% and 38% respectively.

Our One App application provides a digital hub for our customers to manage all their fixed and mobile services including paying bills and managing tariffs. 21% of our user base, or 233,000 customers, are now using it on a monthly basis.

HT's market leading mobile services allow us to innovate and develop new services for our customers. As a result, we are very pleased to be leading a new smart parking initiative in Dubrovnik. Using our Narrowband Internet of Things network, the Dubrovnik Smart City umbrella project, makes it easier for drivers to find parking in the city and eases congestion. It is one of the biggest smart city projects in the world.

We have also been recognised as Microsoft's partner of the year in Croatia for developing and delivering outstanding Microsoft-based solutions.

Meanwhile following the acquisition late last year, Evotv services are now incorporated into the HT portfolio, and being offered through DVBT technology.

On the financial side, we have continued to deliver strong financial performance. Our CAPEX to sales ratio is high at 19.7%, illustrating our commitment to investment in the future of the business and the wider economy.

We paid out a dividend of HRK 10 per share, representing an 82% payout ratio, and our share buyback continues at an accelerated pace. Around 0.6% of total shares bought back in 2018 were recently withdrawn.

Looking forward, our outlook for the full year remains unchanged.

Moving to slide 4, just a reminder that we introduced the new IFRS 16 standards to our accounts at the start of the year, eliminating the different treatment of finance and operating leases.

To ensure comparability we have introduced 'AL' or 'after leases' steering KPIs. The relevant 'after lease' KPIs for 2018 and 2019 are EBITDA AL and Capex AL. Slides 12 to 14 in the Appendix section of this presentation set out the changes and impact of these changes on our financial reporting.

In the first half of 2019, revenue and net profit have risen while EBITDA AL is slightly down, impacted by higher operating expenses, including write down of assets.

Total revenue across the group rose by 0.4% in the first half of 2019 to HRK 3.7 billion from HRK 3.68 billion last year. This is the result of a 4.1% decline in revenue at Crnogorski Telekom to HRK 288 million, which was offset by a 0.8% rise in revenue at HT Croatia to HRK 3.41 billion.

Crnogorski Telekom remains under pressure reflecting the tough competitive and regulatory environment in Montenegro. But even though this pressure remains, the negative trends from previous years have significantly improved.

EBIDTA AL was down 1.3% to HRK 1.40 billion. This fall is attributed to higher merchandise and roaming costs, and the higher cost of employee benefits, all of which offset a one-off positive impact from the Evotv transaction. EBITDA AL margins fell 0.7 percentage points to 38%.

Despite the small decline in EBITDA AL, we have reported net profit up 1.2% to HRK 438 million in the first half of the year. The EBITDA decline and higher taxation was offset by better net financial results, lower depreciation and less onerous redundancy costs.

Please now turn to slide 5 which describes our operating cash flow performance and the continued investment in our network and improvements to customer experience.

Net cash flow from operations fell 2.0% to HRK 1.07 billion in the first half mainly because of adverse movements in working capital. Meanwhile capital expenditure was 18.6% lower in the period at HRK 729 million. This decline merely reflects a difference in the yearly distribution of funds and does not impact the significant investment we continue to make in our mobile and fixed broadband networks.

I would now like to hand over to our CFO Daniel Daub who will talk you through the details of Group financial and operating performance.

Mr Daniel Daub

Thank you Kostas and good afternoon everyone.

On slide 6 you will see that HT Croatia revenue has increased in the first half despite our exit from the energy business. This rise was underpinned by a good performance from the mobile and system solutions businesses.

Total revenue rose 0.8% to HRK 3.41 billion, and the large contributor is mobile revenue which was up 2.9% to HRK 1.49 billion in the first half. This increase in mobile revenue came from higher postpaid revenue as a result of our successful prepaid to postpaid migration strategy. This strategy has both increased customer numbers and the amount they spend with us. 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 10.4% to HRK 336 million as mainline sales, traffic and average revenue per user all declined because of competitive pressures and fixed to mobile substitution.

Broadband and TV revenue rose slightly, up 0.5% to HRK 649 million. Within this figure, TV revenue was boosted by more TV customers and higher ARPU as well as the positive impact of four months of revenue from our Evotv acquisition. This was enough to offset a fall in broadband revenue.

Fixed wholesale revenue fell 0.7% to HRK 156 million mainly due to lower transit traffic.

Other fixed revenue rose 1.3% to HRK 411 million due, among other things, to higher terminal equipment and digital advertising revenue.

We saw a strong improvement in revenue in our system solutions segment, up 27.8% to HRK 355 million reflecting more favourable yearly project dynamics in the first half of 2019 compared to the same period last year.

Miscellaneous revenue fell to HRK 8 million from HRK 68 million in H1 2018 because of the sale of the energy business last year, which accounted for HRK 58 million of revenues in the first half of 2018.

Slide 7 describes our mobile business in Croatia, where we maintained leadership in the overall market and in mobile technology.

At the end of the first half 2019, HT maintained its leading market position with a share of 44.9%, down slightly from the 45.8% reported in the first half of 2018 mainly due to competitors' active promotion of their FMS offers where they count their broadband customers as mobile subscribers

Despite this slight decline, we increased the number of subscribers across HT Croatia by 0.8%, largely driven by a 4.8% increase in postpaid customers to 1.35 million. This offset a 4.6% decline in prepaid customers to 936,000 at the end of the first half.

Average revenue per user rose 0.4% to HRK 43 in the prepaid segment and was also up 0.6% to HRK 86 in the postpaid customer segment.

HT Croatia's smartphone proportion of total handset sales is now 92% in the postpaid segment, up from 90% in the first half of 2018. Smartphone customers account for 68% of HT Croatia's overall subscriber base which grew from 65% in H1 2018.

By the end of the first half of 2019, HT Croatia's 4G network had reached 99% coverage outdoors and 85% population coverage indoors. We are continuing the modernization of our mobile network throughout Croatia as we build the foundations for the introduction of 5G and at the same time we are supporting increased traffic through our 4G network sites.

I'm also proud to report that we recently won the OOKLA certificates for fastest mobile network and best mobile coverage in Croatia.

Please now turn to slide 8 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 6.2% to 847,000 at the end of the first half. Retail fixed mainlines were down 5.8% to 798,000 and wholesale fixed mainlines fell 12.3% to 50,000. 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 4.5% to HRK 69.

In addition, broadband access lines declined 1.2% to 741,000 at the end of the first half, with retail lines down 0.4% to 619,000 and wholesale broadband access lines down 5.4% to

122,000. 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 aggressively priced offers in the market also dragged broadband retail ARPU down 6.9% to HRK 104 in the first half.

While fixed and broadband lines were depressed, TV customers rose strongly, up 18% to 490,000 by the end of the first half. This boost mainly came from the acquisition of Evotv which uses DVBT technology. TV ARPU was also up 4% to HRK 86.

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

Customers in more rural areas are being upgraded to higher speed broadband through Hybrid access. Thanks to the innovative hybrid technology, Hrvatski Telekom has secured up to 30 megabits per second in rural and less populated areas of Croatia. It is a combination of fixed and best mobile network in a unique service that provides stable and fast Internet access. We are the only provider of telecommunication services in the market that delivers high speeds of up to 30 megabits per second into the rural areas of Croatia using this innovative hybrid approach.

Turning now to slide 9, we describe the standalone performance of Crnogorski Telekom, which has come under pressure mainly because of a steep decline in fixed voice revenue.

Revenue fell by 3.4% in the first half of 2019. This was largely the result of negative trends in the fixed voice and mobile prepaid segments, which was only partly offset by an increase in system solutions revenue.

Broadband and TV revenue have remained broadly stable.

We have seen a decline in EBITDA AL of 5.7%, to HRK 101 million. This was mainly the result of the absence of some positive one-off impacts reported in H1 2018, including the sale of real estate and a change in accounting standards. In addition, we saw lower revenues from fixed voice.

Finally, please turn to slide 10 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.

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.