

## **The Q2 2015 results conference call**

**30 July 2015 at 10:00 CET**

### **Presenters**

**Davor Tomašković**

Hrvatski Telekom – President of the Management Board and CEO

**Kai-Ulrich Deissner**

Hrvatski Telekom - CFO

**Elvis Knežević**

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Operator: Thank you for standing by, and welcome to the HT Q2 Results conference call.

At this time, all participants are in a listen-only mode. There will 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-1 on your telephone. I must advise you that this conference is being recorded today on Thursday, 30th of July 2015.

I now like to hand the conference over to your first speaker today, Mr. Elvis Knežević. Please go ahead, sir.

Elvis Knežević: Thank you. Ladies and gentlemen, good morning, and welcome from Zagreb.

Today, our CEO, Mr. Davor Tomašković, and our CFO, Kai-Ulrich Deissner, will talk you through the highlights of our business and financial performance for the six months ended 30 June 2015 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 investors' page. After the presentation, Mr. Tomašković and Mr. Deissner will be available for your questions.

Before we begin, allow me to draw your attention to the Harbor Statement on the 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 six months ended 30 June 2015.

Davor Tomašković: Good morning, ladies and gentlemen. Thank you for joining us today. It's my pleasure once again to present the results from Croatian Telecom for the six months ending 30th of June 2015.

I'll start the presentation with slide 3 which presents the financial highlights of the period. As you can see, we have seen positive developments in both revenue and the EBITDA in the first half of 2015. Revenue showed 0.5 percent over on increase. That is including Optima consolidation. If we exclude the Optima Telekom, revenue has a decline of 4.1 percent in the first half of 2015, demonstrating an improving trend from the first half of 2014 when revenue declined 5.2 percent.

EBITDA before exceptional items rose 2.1 percent in the first half. If we would exclude Optima, then EBITDA fell by 1.8 percent. That's still a substantial improvement on the 10 percent decline we have seen in the same period last year. Our pre-exceptional EBITDA margin improved to 39.6 percent compared with 38.9 percent in the first half of 2014.

Our transformation is also yielding good result and we are maintaining clear focus on improving efficiencies and optimizing operating costs. Our recently established HORIZONT strategic program is making good progress, delivering tangible outcomes and helping to consolidate the HT's long-term position as a leading player across all our markets. The effectiveness of our cost, transformation initiatives and HORIZONT program is evident in the further cost efficiency as achieved in the first half of 2015, with operating expenses showing HRK40 million decline year-on-year. Excluding Optima Telekom, operating expenses fell by HRK143 million showing almost 7 percent decrease year-on-year.

In light of this financial performance in the first half, our outlook for 2015 remains unchanged.

If we now turn to slide 4, we will outline our operational highlights for the first half of 2015. I'm pleased to report that we have maintained our leading position across all areas of our business against a lackluster, albeit slowly improving in economic backdrop. Enhancing the customer experience remains our central priority and we're investing a lot in mobile and fixed broadband networks to ensure that we provide technology leadership in the market.

We have also introduced a number of activities designed to enforce our position in both fixed and mobile markets which include new mobile subscription plans which aimed to minimize churn and monetize on the mobile data spectrum. Continued investment in our networks has ensured that we are on track to meet our ambitions end-of-year targets which is 40 percent of household now have Next Generation Access services and we're making good progress towards achieving our end-of-year target of 50 percent household coverage. At the same time, our 4G indoor coverage now is at 54 percent of the population, not far off the end-of-year target of 60 percent.

In addition, as testament to the improvements we have already undertaken in July, we were awarded the "Best in test" certificate for the highest speed mobile internet and the best mobile network in Croatia. Also, I'm pleased to report that our IP transformation is almost complete. 92 percent of retail customers have already migrated and we plan to migrate 100 percent by the end of year.

Also, we are very well pleased to participate in Deutsche Telekom's PAN IP Group initiative which aims to unify all of its PAN European production models under one IP base service production model.

Let's turn now to slide 5 which give an overview of the market in which we operate. For mobile, the trends have remained similar to the patterns we've seen in recent quarters. Customers are no longer finding the need for duplicate SIM cards, and therefore, the SIM penetration continues to decline. It's now down 3 percent year-on-year which is 114 percent at June 2015. Also, improved mobile deals mean more customers are choosing to take out contract rather pay-as-you-go so we see the prepaid to postpaid migration. We continue to see the growth in demand for mobile data. This is naturally dampening the growth of mobile minutes of use. Nevertheless, they grew 3.3. percent year-on-year in the first quarter of 2015 compared with 8.6 percent in the same period last year.

Fixed, on the other hand, voice minutes continue to decline, 12 percent year-on-year in the first quarter of 2015, which is a trend we see in the entire industry.

Fixed Broadband and PayTV market continue to buck the decline in fixed telecommunication trend. The market has seen some further consolidation amongst our competitors with the acquisition of Amis by Telekom Austria's Vipnet as part of

the strategy of providing a converged service across Croatia. The number of total fixed broadband lines at the end of the first quarter was 955,000 which is 2.4 percent increase year-on-year. Similarly, the number of total PayTV customers is up 4.7 percent and is now at almost 750,000 customers. Key drivers for this growth are convergent and bundled offers.

The ICT market is continuing to demonstrate growth. It grew in 2014 around 4.1 percent. You will note that we don't have the numbers for 2015 yet, but we expect further growth, although we expect the growth rate will decline to below 3 percent.

That is the overview of our markets and highlight on the performance both financial and operational. I'll now hand over to our CFO, Kai-Ulrich Deissner, to discuss our financial performance in more detail.

Kai-Ulrich Deissner: Thank you very much, Davor.

If you now turn to slide 6, we take a more detailed look at the breakdown of our revenues in the first half of this year. As already mentioned, our overall revenues in the first half grew by 0.5 percent. This was supported by the Optima contribution. Excluding this contribution, revenues would have declined by 4.1 percent which marks an improvement under this compared with the 5.2 percent decline which we saw in first half of 2014.

In the further breakdown, in fixed telephony revenues, this was down 13.4 percent. This is generally owing to the usage trends that we've seen in the telecom industry for many, many years with declines both in the number of lines and traffic and in revenue per line.

Mobile revenue also fell by 4.4 percent in the first half of this year and the positive momentum which we saw some part of last year, we see it negatively impacted by customers increasingly choosing lower value tariffs and lower-end handsets as well. However, of course, let me add, this was compensated in lower merchandise costs on the other hand as you would see there. Still, this decline of 4.4 percent in mobile was lower than the 5.5 percent decline that we saw in same period last year.

Wholesale was down 31 percent. This is mainly due to consolidation of Optima. It's an impact of about 33 million quarterly, which are now considered internal

transactions, and thus, are no longer reflected in our wholesale revenues. In addition to this negative Optima consolidation effect, general prices and traffic declined which was offset by the de-regulation of certain non-EU termination rates as of Q2.

ICT revenues grew by 3.2 percent. This was mainly driven by IP communications and ICT solutions as well as by cloud and managed services. In particular cloud and managed services, this new business model is seeing an increasing adoption by the market as there's more and more customers seem to avoid from their perspective, unnecessary capital investment in those IT assets.

Other revenues reported growth to HRK300 million from HRK63 million in the same period last year. Optima contributed to this 218 million. But taking into account the negative impact of the wholesale revenues which I described earlier, the net impact of the consolidation of Optima is HRK151 million.

We turn the page to slide 7. We're pleased to report that the transformation efforts which we have undertaken for the past year and a half have brought significant improvement in our operating expenses. This helped to improve EBITDA and net profit slightly while the EBITDA margin before exceptional items has risen to almost 40 percent. At the end of June, we're at 39.6 percent against 38.9 percent in the previous year. The first half of 2015, EBITDA before exceptional items rose 2.1 percent to HRK1.3 billion supported by this transformation initiatives, the lower operating expenses, and of course, the consolidation of Optima. As we said earlier, excluding Optima, the pre-exceptional EBITDA would have fallen 1.8 percent versus a 10 percent decline in the first half of last year.

Net profit rose slightly with an increase of 1.2 percent in the first half. This was driven by EBITDA growth as well as lower exceptional items and the higher net financial income. These positive contributions were offset slightly by higher depreciation in amortization; again, mainly driven by Optima.

Net cash fell almost 10 percent to HRK830 million. This was mainly due to adverse working capital movements.

Same time, CapEx rose more than 12 percent. This is reflecting our significant investments in mobile and fixed broadband networks and the IP transformation initiative which we already described.

We turn to page 8. where we provide the breakdown of revenues in the residential segment. In this segment, revenues fell almost 5 percent in the first half, with just about HRK1.8 billion. The key drivers of this decline were a fall of almost 14 percent in voice revenues and the 28 percent decline in terminal equipment revenues.

The voice revenues declined, driven mainly by usage in fixed and the fall of mobile revenues which is mainly coming from EU roaming regulation, termination rate cuts and increasing number of flat rate tariff offers on the market.

Terminal equipment revenues fell, as I mentioned, 28 percent because of lower prices of handsets and a greater number of customers who chose lower value tariffs; once again, compensated in merchandise costs.

These declines in revenue were only partially offset rising miscellaneous revenues. These miscellaneous revenues were strongly boosted by the price increase in mobile from July last year, that came from the new government fee for mobile services which we pass on to our customers. In addition, these miscellaneous revenues benefited from growth in revenue from energy.

Non-voice revenues fell only slightly down just about 1 percent, supported mainly growth in mobile data.

We turn to page 9. We'll review the performance of the business segment. The declining trend in business revenues, which fell almost 8 percent to HRK1.249 billion in the first half, continued to be seen both in voice and the non-voice revenues. Voice was down 18.3 percent, that's reflecting declines in fixed, mobile and wholesale.

Non-voice, down 11 percent. This is largely due to significantly lower wholesale revenues which was, as I said earlier, impacted by general decreases in prices and traffic, also by the negative consolidation effect of Optima where revenues are now considered internal rather than external.

ICT, our important growth segment, increased reported revenues by 3.2 percent.

I will close the overview of the revenues. I will now hand back to our CEO, Davor Tomašković, and talk us the main development in mobile, fixed and IP business and our outlook for 2015.

Davor Tomašković: Thanks, Kai.

If we move to slide 10, we'll give an outline of our mobile operations in first half of the year. Our market share by subscribers remained largely stable at the end of the first half. Subscriber numbers in the pre and postpaid segments declined by 2.9 percent, but the data subscribers were up strongly rising 6.1 percent to 1.45 million at the end of the period.

Average minutes of use per customer in the first half of 2015 rose by 4.1 percent compared to last year because more and more people are taking our flat offers on bundles which have a higher number inclusive minutes.

Blended ARPU decreased by 5.9 percent year-on-year as a result of highly competitive market. Croatia has also continued to have a challenging market economic situation and there are further EU regulations on roaming prices.

Smartphones as proportion of postpaid handset sales increased to 76 percent in the postpaid segment from 73 percent last year. Our HT's total smartphone penetration is at 43 percent.

HT's 4G coverage, as I mentioned, reached 54 percent in this period; while 3G availability indoors is at 77 percent of total population. This definitely helped us bring mobile data bundles to the market to remain competitive in this cut-throat market.

The focus of our mobile business has been and continues to be the improvement in the customer experience with speeds of up to 150 megabits per second available following the acquisition of new spectrum. So, we are the only operator in the market that can offer those speeds in mobile network.

Turning now to slide 11, we look at the progress of fixed line telephony. The fixed market continues to see a general decline in the number of mainlines and ARPA, in line with broader trends of substitution to mobile from fixed line services. The number of mainlines declined by 7 percent, while ARPA fell 7.1 percent to HRK89 by the end of the first half.

We have several marketing initiatives underway to stand these declines. We have put proactive and reactive churn prevention offers in place in our offer, for example, fixed line phone connection for just HRK1 on a term of 24-month minimum contract duration alongside the attractive fixed line tariffs. We also offer a range of double play and triple play services and we'll rely more on our multi-brand strategy opportunities as it unfolds.

If we move to slide 12, we keep the leading position in convergent offers and on content. As you can see on slide 12, we are seeing continued growth in broadband. The number of broadband access lines grew 2.5 percent and broadband retail ARPA showed a slight uplift rising 0.5 percent. We remain on track with our network broadband plans.

I'd like to first reiterate our target here: by the end of 2015, we plan to achieve 50 percent of household coverage with NGA, Next Generation Access, which means the speeds of more than 30 megabits per seconds. We currently have 40 percent coverage of NGA.

The TV-customer base fell by 1.7 percent to 387,000 customers in June from 394,000 customers in June 2014. It's a result of aggressively priced competitive bundle offers. However, we continue to build up a stronger offer in the exclusive TV content to attract and retain customers including Pickbox, Formula One, and HBO premium TV packages.

In response to the increased cost consciousness that we've observing amongst Croatian customers, in light again of the continued economic challenges, we are addressing challenges in low prices segment on the market and we're also repackaging some of our TV content. We're also undertaking marketing activities including the promotion of services combining direct to the home TV services and mobile.

Finally, we move to slide 13, and I'm pleased to reiterate our outlook for 2015 which remains unchanged since we last present those results in February this year. In 2014, revenue was HRK6.9 billion and we expect this remain stable in 2015.



In 2014, the group achieved pre-exceptional EBITDA margin of 40.3 percent and the outlook for 2015 is for the margin to be at the same level of around 40 percent. HT spent HRK1.07 billion in CapEx in 2014 and we'll increase this investment by around 25 percent to HRK1.35 billion in 2015. And this year, we continue to monitor and evaluate potential M&A opportunities.

Thank you for your attention, and we're now ready to take any questions you may have.