The 2011 results conference call
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Presenters

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Operator

Thank you for standing by and welcome to the T-HT Q4 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 *1 on your telephone. I must advise you this conference is being recorded today, Tuesday 14th February 2012. I would now like to hand the conference over to your first speaker today, Miss Erika Kaspar. Please go ahead.

Erika Kašpar

Thank you. Ladies and gentlemen good afternoon and welcome from Zagreb where our CEO Mr Ivica Mudrinić and our CFO Mr Dino Dogan will talk you through the highlights of our business and financial performance for the year to 31st December 2011, using the presentation slides which I hope you have in front of you, if not please visit our website www.t.ht.hr where you can access the slides from our investors page. After the presentation Mr Mudrinić and Mr Dogan will also be available for your questions. Before we begin allow me to draw your attention to the harbour statements on page 2 of our presentation, and now allow me to introduce you to Mr Ivica Mudrinić our CEO who will outline our company's performance in the full year to 31st December 2011

Ivica Mudrinić

Thank you Erika, good afternoon to everyone, sorry for the delay. As I understand we had some technical difficulties. On this Valentines Day we are announcing our results for 2011, starting on slide 3 just a brief overview of the environment in which we operated in. The economy continued to have some difficulties and what we have done here is provided you the GDP level in comparison to 2008 and the GDP level in absolute amounts. As you can see in 2011 we continued to be roughly 7% below the 2008 level. Again just as an indication of the difficulties in the environment.

The second point that I would like to make is that the unemployment level continues to be very high, at 18.7% in December 2011 and a very high arrears amount in the business segment, roughly HRK40 billion which is quite significant. On the positive note related to the environment, Croatia has signed the agreement with the EU member states and has held a referendum in which two-thirds of those voting have voted in favour of the EU accession, and now the ratification process has begun in the EU member countries, some have already ratified the Croatian accession and mid next year, 1st July 2013 Croatia is going to become a full fledged member of the European Union, which again will determine the environment or have a significant impact on the environment going forward.

On slide 4 a few words and an indication of the telecoms and ICT markets in which we operate. In the fixed line business we have 19 licensed operators of which 10 are active. In July 2011 the regulator has introduced the wholesale line rental modality for our competitors to access our access network and also naked bitstream has been introduced. The market has been liberalised since 2005 and the local loop and bundling started in 2006. What we are seeing in fixed telephony further is also a typical decline in usage that we are seeing in all of the market. Fixed mobile substitution and other effects are influencing the fixed telephony market.

On the other side mobile telephony in our market has three operators, ourselves plus two competitors, six brands, no MVNOs at this time. Mobile penetration is at 120% which is actually a decline in comparison to pervious year's figures but this is because the regulator has determined finally the activity rate for the prepaid segment and therefore has brought the presentation level to 120. Growth in mobile broadband and smartphones is both significant and it is the growing segment of the mobile market.

In the internet segment we have a fixed line broadband household penetration of 45%. We have also the implementation of what is called naked DSL, significant growth opportunity in the internet. This is as a result of the 45% penetration and in comparison to roughly 62 or so on average in the western part of the European Union. We saw further consolidation – the number two mobile operator has acquired the largest cable TV operation.

On the paid TV side we continue to have a satellite and cable TV underdeveloped. The paid TV household penetration is at 39%. Our MAXtv IPTV platform holds a significant part of the market and it is the most successful paid TV player, also one of the top ranking IPTV launches on a worldwide basis measured by density or penetration rate in the market.

On the ICT segment – what we saw in 2010, this is the last reference here we have that the IT market declined 1.3% year-on-year to HRK 5.8 billion. The IT services segment represents 35% of the total IT market, also declined by 2.3% in 2010. We saw also continued economic difficulties and the shrinking of the Capex budget of the largest IT services spenders in the country. However ICT is an important segment as you will see later, one in which we have made significant in-roads during the course of 2011.

On slide 5 a few words about the regulatory framework – as I mentioned already the wholesale line rental has been introduced and also naked DSL. We saw also the imposition of automatic migration to wholesale line rental of those customers that had been on carrier pre-select. Decreased wholesale prices, both unbundled, local loop, wholesale bitstream access and interconnection prices as well – this is in alignment with the EU regulatory framework. We have had a defined concept for the provision of wholesale bid access on copper and limited bid access on FttH for speeds of 20 MB and higher. In this what we wanted to actually say is that we have cleared the path for offering FttH at the higher speeds. It means that we have resolved the impasse related to the wholesale offer of the FttH product.

We have also the initiative by our regulator HAKOM to regulate the IPTV market which is a decision that is now under investigation. However we believe – well maybe not to comment it – but this would be a precedent when the EU provides a basis. Also we have seen the regulator adopt an ordinance on what is called the certificate and fee for the right of way and other regulatory framework elements, all impacting our business in this fixed line, especially fixed line access part of the business.

Cost accounting and cost modelling prices continue of course during 2012 and 2013, and we are also seeing a cost model developed for fixed and mobile network and universal services by our regulator.

When we look at page 6 briefly and we compare what we have committed and our promise let's say to the capital markets and delivery, we have essentially delivered on all of our commitments during the course of last year, having to do both on revenue, EBITDA, Capex and regional expansion issues.

On the Group highlights page on page 7 – of course we have maintained a leading market position in all business segments as we have previously. Our revenue decreased 3.6% to HRK 8.067 billion as a result primarily of the difficult economic environment that I mentioned already, as well as stronger competition and certain regulatory measures. The EBITDA is down 1.2% to HRK 3.619 billion, and the margin is at 44.9%. Before exceptional items, EBITDA is up 2.4% or HRK 3.78 billion. The net profit decrease 1.1% to HRK 1.811 billion. The Capex was lower in 2011 in comparison to 2010 by 23.9%, mostly due to certain regulatory hindrances related to fixed line investments. Headcount has been decreased to 6,032 employees. We have a proposed dividend in the amount of HRK 22.14 which is a 100% payout ratio. One thing worth noting is also that the parliament had originally last year abolished the 6% special fee on mobile services, because we have had a change of government in Croatia, the fee has been reinstated effective 26th January this year and it is to remain in effect until 30th June 2013 or the date on which we become an EU member.

On the next slide on page 8 we have a revenue development – again indicating that the traditional fixed telephony has declined by 9.9%, mobile has declined by 9.5%, wholesale by 8%, whereas IP has grown by 10.5%, ICT by 85%, here we have the consolidation impact of a company we have acquired, Combis, again an ICT company so we look at the ICT business in its entirety together with Combis, and other revenues are down by 15%, so you see the 3.6% decline year-on-year for the full year period, and having a revenue of 8.067 billion in 2011.

On slide 9 we have an overview of the mobile telephony part of the business where you see the subscriber share – 47%, so it is up 0.3% from the previous year. The subscriber numbers in absolute terms are lower by 0.8%, but here we have seen a change in the activity rate definition, so 2,418,000 is the total number of subscribers. The blended ARPU is down by 10% at HRK 94, and the average minutes of use have dropped by 1.2% to 134.

On the fixed telephony side which is on slide 10 we have a decline in the number of active mainlines. This is because we saw the shift to wholesale line rental of those customers that were previously on CPS and on the bottom right hand you can see the 123,819 wholesale line rental customers or lines and this is mostly what impacted the total number of mainlines in our customer base. The traffic is down by 12.2% at 2.8 billion minutes. The average revenue per customer is down 7.3% to HRK 121.

Now I would like to then on page 11 a brief overview of the IT services – the number of fixed broadband customers or ADSL lines has increased by 3.4% to 651,000. Similarly the ADSL average revenue has declined 31.% to HRK 123. On the TV subscriber side however we saw the growth of total number of TV customers grow by 12.3% or 341,000.

At this time I would like to pass the microphone to Mr Dino Dogan our CFO who will take you through the next set of slides.

Dino Dogan
Thank you very much Ivica. Ladies and gentlemen on slide number 13 we would like to give you a breakdown of the revenues in the residential segment. The residential revenue fell due largely to lower voice revenues as a result of the economic downturn. The competitive pressure on the pricing we are facing, lower mobile termination rates and the already mentioned regulatory measures. During 2011 the voice revenues fell 12.6% to HRK 2.582 billion. This result was slightly offset by an increase in non-voice revenue thanks to growth in the fixed IP and mobile data revenue, although other non-voice mobile revenues were lower. On the service revenue – this was higher due to the higher revenue from usage bundled tariffs, while revenue from terminal equipment declined largely due to reduced investments in the prepaid customer segment.

The division's contribution to EBITDA in fact rose 1% to HRK 3.025, however on the back of tight cost controls and lower operating expenses and here I would highlight the SACs, the interconnection costs and lower losses on receivables. During the year, this division continued to innovate and introduce new products and services, including mobile post-paid tariffs with unlimited data usage, a storage service for multimedia content on TV, mobile and PC laptops. The Group also acquired the rights to the Croatian Premier Football League matches on MAXtv exclusively, and as I mentioned before whilst the prepaid brand "bonbon", mobile brand reached more than 100,000 users after just a year in existence. We also re-launched our Simpa mobile tariff with attractive rates for calls to all networks in Croatia.

Let's move to the business segment on slide number 13. The business segment as well experienced a decline in revenue, which was 2.7% lower at HRK 3.635 billion. The voice revenue was down 12.2% at HRK 1.763 billion, largely on a falling number of main lines, a decline in fixed network traffic and mobile revenue lower mainly due to lower prices and lower usage. On the non-voice side – the revenues fell 2.6% to HRK 1.095 billion mainly due to lower revenues from traditional data and national leased lines, although higher infrastructure revenues were reported due to the wholesale line rental activation.

Other service revenues were significantly higher, up 61.1%, mainly due to the contribution from Combis, but the revenue from terminal equipment fell 6.6% due to the lower fixed parts revenue and miscellaneous revenue was pushed some 31.5% lower by decreased national roaming prices, lower usage and mobile disconnection fee revenue designated as service revenue as of 2011. The entire contribution from the business segment to the EBITDA fell 5.8% primarily as a result of lower usage but we also have to face that there is also an impact from the lower margin ICT business as such. Nevertheless we remained innovative and proactive, in ICT we also launched a number of new services to expand our product range including cloud based services, like tCloud virtual desktops, tCloud human resources, tCloud ERP, tCloud virtual private service and e-book store our Planet 9. We also launched mobile phone tariffs that were specifically designed to meet the needs of the SMEs and moved into the emerging area of geolocation marketing with our HotHot product.

Ladies and gentlemen lets recap on the financial highlights. Our revenue is down 3.6% due to the reasons we already mentioned, however when the impact of the contribution from Combis and the accounting change related to the useful life of a customer relationship so called SAB101 excluded the underlying revenue in effect declined 6.9%. Our EBITDA before exceptional items increased by 2.4% to HRK 3.782 billion with a margin of 46.9%. In 2011 exceptional items referred to the redundancy provisions totalling HRK 162 million. At the same time positive effect of the change in accounting treatment of consumer premises equipment was shown. The change was introduced from September 2010 and it resulted in the fall of the corresponding merchandise costs of HRK 136 million in 2011 versus HRK 75 million in 2010. In 2011 this fall more than offsets the consolidation of Combis expenses and increased copyright fees. Out net profit was HRK 1.811 billion, down just 1.1% from 1.831 billion for the previous year, as a result of lower operating profit and slightly higher net finance income, which is a result of FX and interest gains. Capex was lower than the previous year, down 23.9% in 2011, largely as a result of the slower realisation of backbone and backhold projects. Regulatory issues that we have discussed on many occasions in the past, a few years remained disincentive to investment by the group in the fibre infrastructure network. Our net cash from operations fell 8.5%. This is a result of the decrease in the current liabilities and impact of the already mentioned redundancy payments.

After we have presented results of the previous year, let me outline the outlook for the year 2012. In terms of revenues, what we can see is the Croatian economy has shown no sign of recovery since entering recession in 2009 and according to the recent forecasts growth is still not expected to emerge in 2012. In a business environment characterised by a protracted economic recession, domestic regulatory tightening and progress towards alignment with EU telecoms regulation as well as intensifying competition, last year's trend in Group revenue decline is expected to continue. This will be additionally impacted by the recently introduced increase in the VAT rate and the reinstatement of the 6% fee on the mobile services.

Regarding the EBITDA before exceptional items, the Group will continue its transformation program measures throughout the year. It already showed positive impacts on the 2011 results. Nevertheless, due to continued severe economic and market conditions in Croatia, leading to lower expectations for revenue, combined with the absence of some already mentioned one-off items reported the previous year, the Group expects 2012 EBITDA to be somewhat below the 2011 level.

Regarding our Capex, the current regulatory regime continues to deter investment in fibre infrastructure by the Group. However, we will continue investment to transform our fixed core network and enhance our infrastructure to support further growth in mobile broadband demand. As a consequence, Capex in 2012 is expected to be higher than in the previous years.

Last but not least, ladies and gentlemen, regarding the regional expansion, we will continue to monitor and evaluate expansion opportunities to increase the shareholder value.
