The Q3 2012 results conference call
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Presenters

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Operator
Thank you for standing by and welcome to the T-HT 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 30th October 2012. I would now like to hand over to your first speaker today, Erika Kaspar Head of IR. Please go ahead.

Erika Kaspar
Thank you. Ladies and gentlemen, good afternoon and welcome. Today our CEO Mr Ivica Mudrinic and CFO Mr Dino Dogan will talk you through the highlights of our business and financial performance for the nine months to 30th September this year using the presentation slides. I hope you have the presentation slides 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 Mudrinic 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.

Allow me now to introduce you to Mr Ivica Mudrinic our CEO who will outline our company's performance during the nine months to 30th September 2012.

Ivica Mudrinic

Thank you Erika, good afternoon to all of you listening, it is a pleasure to be here with you today. Let me start off with a brief overview of the Croatian economy and the performance thus far. Unfortunately the economy has not managed to make a fundamental turnaround, and as such since 2009 we have continued to be at a relatively low level with a total contraction in comparison to 2008 upwards of 7-8%. In 2012 Q2 we saw a contraction of 2.2%, the forecast to year-end for 2012 in total is a contraction of 1.8%. We are seeing a registered unemployment rate at 18.3% in September this year, versus 16.8 in September last year. The inflation is at 5% in September 2012, this is mainly due to energy cost increase, some prices in food and other goods as well. As a result we see a falling disposable income, and this affects directly of course the consumer behaviour and consumer spending habits. The business payment arrears are still extremely high at roughly HRK44 billion which is some 13/14% of total GDP. It peaked at 44.6 billion in May 2012.

We have seen on the flipside a successful tourist season. The tourist arrivals in January through August 2012 are up 4%, at 9.5 million. 90% of these are foreign tourists so this is helping the economy.

What we see also is that the government having come into power at the beginning of this year has done many things to manage the fiscal budget effectively and very well, as a result Fitch has maintained a long term rating at BBB- and revised the outlook from negative to stable, so this is a positive turnaround. It also somehow confirms that the government has managed the public finances effectively, not occurring any increase in further debt. They have some deficit but it is actually below the Maastricht level. Unfortunately we still did not see the far-reaching structural reforms of the economy and also the large public sector investments that were announced that should have fuelled some economic growth did not happen, at least not in the kind of numbers that we wanted or we were expecting to see. In addition to this, looking at the near future, Croatia is to become an EU member on 1st July 2013. There will be some structural funding and other funds available that should also fuel the economic turnaround. There is an expectation with this changing environment that certain foreign direct investments will increase and become increasingly present. The GDP in 2013 is forecast to be at least 0.5% growth. The members of the cabinet are actually talking about 1.5-2% growth but the 0.5% is from the independent economic analysts.

On slide 4 a brief overview of the Croatian telecom and ICT market. We have 19 licensed operators in fixed voice, nine of them are active, we have of course career pre-select, unbundled, local loop and wholesale line rental include naked bitstream and bitstream available. We are seeing similar trends in decline in the fixed voice as elsewhere on a worldwide scale having to do with the migration of some of the voice services to mobile, so it is a kind of a substitution. In addition we see mobile and VOIP substitution continue to undermine fixed voice increasingly, which means the new VOIP services available to the customer is using the mobile services is increasingly impacting the total usage. In fixed broadband what we have is a 47% household penetration versus a 65% average in Western

Europe, which means that we still have room to grow and you will see the numbers a little bit later. We do continue to see some uptake. Aggressively priced double play and triple play offers are now available, first integrated fixed-mobile offers and Naked DSL so this is now on the market, we are fully participating.

In the mobile part we have three operators with seven brands; we have commercially launched the LTE services mid spring this year, mobile penetration is at 123%. We see growth in mobile broadband, the penetration is at 8%, versus 9% in Western Europe, and of course this is fuelled by the smart phone development as well. Our smartphone penetration is at 21% versus 37% in Western Europe, again an indication of how much room there is to grow going forward. The PayTV part of the business satellite and cable TV is underdeveloped. PayTV I should say household penetration is at 39% versus 56% in Western Europe, again indicating room for growth. We have been regulated in the IPTV segment. We are the only regulated IPTV market in Europe; however on the flipside MAXtv is the most successful paid TV operation in our market, but it is one of the most successful PayTV operations anywhere.

In the ICT segment an area that we have entered in recent years, we have successfully positioned ourselves as a one-stop shop for all ICT services. The cloud concept or cloud as a concept gradually becoming accepted within the Croatian IT community, so our customers are increasingly welcoming this offering. In addition as we approach the EU membership we expect significant IT projects. There is an example that we have noted, it is the so-called fiscal registers where the Ministry of Finance is asking or is mandating the implementation of point of sale registers that are actually cash registers that are linked directly to their system. The economic malaise, difficulties in the economy and the limited Capex budgets have meant that the IT services has shrunk or the market has shrunk. We saw a decline of 2%; this is based on an IDC report. We also expect that in the future however we will see an increase upwards of 6.3% CAGR in the 2012-2016 period. This is room for growth as well.

On page 5 we have prepared some Group highlights, so again referring to the tough economic competitive and regulatory environments, we have in this period seen a decline of our revenue by 7.1%, totalling HRK5.66 billion. The EBITDA has decreased 6.7% to 2.611 billion, our EBITDA margin is at 46.1%, so we are maintaining as you can see a very high margin. The net profit is down to 6.4% to 1.388 billion and the Capex is lower by 8.3% at 581 million.

From an operational overview, we have of course maintained the leading position in all of the markets in which we are present. We have launched new bundles or bundled offers in the fixed segment; we continue the promotion of 4G mobile internet tariffs which is based on the network coverage and our network performance. We have in fact entered the test phase of mobile payments using near field communication or NFC technology. Our headcount is decreased to 5,725 employees compared to 6,066 on 30th September 2011. We have made a submission for the so-called digital dividend spectrum and we have applied for two blocks of 10 MHz yesterday we received an announcement by the regulator that we have been granted this license for the next 12 years. In addition to all of this we have also initiated a new strategic and transformation initiatives in order to prepare the company both for growth in areas where growth is possible, but in addition to ensure operational excellence. We are transforming our company in order to make sure that we maintain overall efficiency going forward.

On page 6 we have a revenue development breakdown and it is indicated best probably on this watershed chart, in comparison to 2011 cumulative January/September we show then a decrease in the fixed voice and fixed services, also a decrease in mobile services, increase in wholesale, increase in IT, some decrease in ICT and a decrease in other yielding a total as I mentioned before of 5.66 billion. Again to reiterate, it is pressure from the recession, certain regulatory measures, and intensifying competition. We also have been impacted by a regulatory measure introduced in August 2011 called wholesale line rental whereby our carrier pre-select customers were shifted to a complete wholesale relationship. This has impacted the fixed part of the business or the revenues from fixed. Mobile revenue declined primarily as a result of competitive pressures and continued recession. ICT revenues down due to lower public sector spending and certain seasonality as well. We see continued growth in IT revenue, wholesale revenue also positively impacted by the wholesale line rental, so those customers that were shifted from CPS to wholesale line rental relationships have caused an increase in the wholesale revenues.

Combis the ICT company that we bought has contributed 234 million in comparison to the 2011 same period where they were at 281. Iskon has contributed with 221 to this figure in comparison to 179 from last year.

Moving to slide 7, we give a brief overview of mobile telephony of the mobile segment. Again the market share by subscribers is stable, in fact increasing, as you can see at 46.1%. In total the number of subscribers has declined, however the data part of the subscriber base or those subscribers using the data services has increased by 25.1%. Clearly broadband and mobile data is a growth area. The ARPU in mobile is 1.6% lower at HRK92, period to period comparison, however at the same time the non-voice ARPU, blended non-voice ARPU has increased by 4.7%. Again I mentioned already the test phase of mobile payments, we believe that this is going to be an increasingly important segment for future development.

On slide number 8 we have a brief overview of the fixed telephony and here we see the decrease in the total number of main lines by 5.1%. The number of ULL lines has increased by 14%, so these are lines owned by us and they are bought on a wholesale basis by our competitors, alternate operators in fixed, totalling 164,000 at the end of September this year. The ARPA in the fixed telephony segment is down 2.9% again mostly due to the decreasing traffic and the shift of usage from fixed to mobile and fixed to alternate solutions, meaning VOIP primarily via mobile and also via fixed as well. Successful win back I should mention as well, we managed to significantly decrease the number of wholesale line rental customers in Q3 from 132,000 to 116,000, so this is a reversal of the earlier trend from the decision by the regulator.

On slide number 9 we have an overview of the IP services so we see here the number of broadband lines slightly increased by 0.6%. We also see the increase in the number of TV customers by 3.7%. In addition you see the broadband retail ARPA increased by 3.9%, so these are the key elements of the trends. I should mention that on our MAXtv platform we have the Croatian soccer league exclusively, we also have the Champions League, Europa League and so on, meaning that this has truly become a content business where we buy aggregate and sell the content to the customers using our service and our platform. We are a pioneer and this is not indicated on the charts, but we are a pioneer in IP transformation, meaning that we are migrating an increasing number of our customers to all IP paradigms, currently at roughly 20% targeting 30% in the next months, for the retail customer migration.

Now for the next session I would turn the floor over to Dino Dogan our CFO.

Dina Dogan

Thank you very much Ivica and good afternoon ladies and gentlemen from my side as well. I will continue on slide 10 with the residential segment. In the residential segment the revenue fell 7.3% in the first nine months of 2012, this was again due largely to lower voice revenue driven by the continued harsh economy, tough competition, mobile termination rate reductions and regulatory tightening, along with the ongoing industry wide shift from fixed voice to mobile and data services. Consequently the voice revenues fell 12.2%.

On the other hand growth has continued in fixed IP and mobile data revenue, however and residential non-voice revenue rose 2.6% in the first nine months of 2012. The division’s contribution to EBITDA fell 8.4% to 2.075 billion, however cost controls and consequently lower operating expenses offset the decline to some degree. The residential segment has continued to innovate in product and services. Our MAXtv service now has further features and promotions such as the Max 3 bundled packages. During this year’s tourist season in Croatia the Group has also offered attractive deals for visitors to Croatia providing flat rate internet access at HT hotspots. Meanwhile the Group also promoted its new 4G network services which provide support high-speed connectivity.

On slide 11 we explore the performance of the business segment. Revenues here fell 6.9% to 2.575 billion in the first nine months of 2012. Voice revenues 12.4% to 1.230 billion, owing to a lower number of fixed line mainlines and as we have seen in the residential segment the shift away from voice services, lower mobile revenues due to decreased usage and lower prices per minute and reduced MTRs and roaming rates. So for example, beginning of 2011 we had the MTRs at a level of 39.6 Lipa where as of today we are at 30.1 Lipa.

Non voice revenues rose 4.8% to 886 million and this increase was driven largely by higher infrastructure revenues due to wholesale line rental activation. Other service revenues was again lower falling 14.3% to 329 million. This fall resulted from changes to mobile tariff structures, seasonality in the ICT business and weaker demand for large public projects. The business segment contribution to EBITDA was down 3.7% to HRK1.618 billion.

The Group is continuing to develop product that addresses the evolving and complex needs of our business customers. We have introduced converged, fixed, mobile and ICT services and are also exploring the potential for services in the cloud that will allow our business customers to run their enterprises more efficiently and effectively.

Moving onto slide 12 I would like to conclude by outlining our financial highlights. Revenue was down 7.1% amidst a protracted economy downturn and in the face of regulatory factors that we have mentioned a number of times in recent years. At the same time competition in the domestic market continues to strengthen in all segments. EBITDA was also lower posting a 6.7% decrease to 2.611 billion, but our cost management continued to have a beneficial impact and the EBITDA margin rose slightly to 46.1% from 46% in the previous year. Our net profit fell 6.4% in the first nine months of 2012 to 1.388 billion. Capex was also lower against the previous year with projects to upgrade the fibre infrastructure still on hold and net cash from operations edged up 0.9% to 1.910 billion mainly due to improved working capital management.

Ladies and gentlemen that concludes our overview of the Group's results for the first nine months of 2012. It was indeed another tough period economically but in the face of this we have again maintained our market leadership and we will continue to implement a forward-looking strategy designed to position our group for growth in the years to come. I will hand you back to our CEO Ivica Mudrinic.

Ivica Mudrinic

Thank you Dino, so on slide 13 we give an outlook for 2012, the outlook to the end of the year and in fact from what we have said it is clear that Croatia is experiencing a protracted recession, with the GDP forecast to shrink by 1.8% in 2012. Added to this fiscal tightening, a 2-percentage point increase in VAT, rising unemployment and increasing energy and food prices have put further pressure on disposable income. At the same time the corporate sector faces further insolvencies and restructurings. Competition and stringent regulatory regime continue to exert pressure on the Group's business. In light of the factors outlined the Group now expects a greater than anticipated reduction in revenue indicating a mid-single digit percentage decline compared to 2011.

So far as the EBITDA is concerned, or EBITDA before exceptional items, the economic environment and revenue development explained above will impact EBITDA accordingly. However due to continuing cost management initiatives, the group expects to main a high EBITDA margin in 2012.

As far as the Capex is concerned, the current regulatory framework continues to deter investment in fibre infrastructure by the Group; however T-HT will continue investment in fibre infrastructure by the group.

However, T-HT will continue investment to transform its fixed core network and enhance its infrastructure to support further growth in fixed and mobile broadband demand. As a consequence, excluding investment in the spectrum licence, capex in 2012 is expected to be higher than the previous year.

In the Regional Expansion domain we continue to monitor and evaluate expansion opportunities to increase shareholder value.

Thank you for your attention and now I turn it back for questions.
