

The Q2 2016 results conference call

28 July 2016 at 11:00 CET

Presenters

Davor Tomašković

Hrvatski Telekom – President of the Management Board and CEO

Josef Thürriegl

Hrvatski Telekom - Member of the Management Board and CFO

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Operator: Thank you for standing by and welcome to the HT H1 results.

At this time, all participants are in listen-only mode. There'll be a presentation followed by a question-and-answer session at which time, if you wish to ask a question, you'll need to press star one on your telephone. I must advise you that this conference is being recorded today, Thursday, the 28th of July 2016.

And I now like to hand the conference over to your speaker today, 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 Mr. Josef Thürriegl, our new CFO who joined us in June, will talk you through the highlights of our business and financial performance for the six month period ended 30th June 2016, using presentation slides which I hope you have in front of you. If not, please visit our Web Site at www.t.ht.hr where you can access the slides from our investors' page. After the presentation, Mr. Tomašković and Mr. Thürriegl will be available for your questions.

Before we begin, allow me to draw your attention to the harbor statement on page two of our presentation. Allow me to introduce you to Mr. Davor Tomašković, our CEO, who will outline our company's performance during the six month ended 30 of June 2016.

Davor Tomašković: Good morning, ladies and gentlemen, and thank you for joining us this morning.

It is my pleasure once again to present the results from Hrvatski Telekom for the six months ended 30th of June 2016. I will start the presentation with slide three which outlines the highlights of the first half of this year.

Let me start by outlining the macro-economic environment we are experiencing. After many years of recession, the Croatian economy is now showing further signs of recovery with GDP growth of 2.7 percent year on year recorded in the first quarter of 2016. There's also been a notable recovery on personal consumption supported by a rise in employment and greater availability of disposable income with the absence of inflation and thanks to reduced interest rates.

However, this is unfortunately still not sufficient evidence to point to a tangible turnaround in the economy. While the telecommunication marketing creation remains highly competitive, HT Group continues to innovate in order to provide a differentiated quality offering and ensure that we are well placed to benefit from this nascent recovery in the economy and then consumption.

I'm pleased to report that revenue for the period rose 3 percent to HRK 3.4 billion. This was underpinned by increased sales of more valuable handsets, better wholesale and energy revenue, and an above-average number of completed system solution projects.

The revenue rise has boost EBITDA before exceptional items by 1.4 percent to HRK 1.4 billion with margin largely maintained at 39.3 percent. In terms of our output for 2016, our revenue and EBITDA margin expectations remain unchanged. However, we now are anticipating that system solutions will be broadly at 2015 levels as we are seeing some government and public sector projects being deferred.

It's worth reminding you all that the further round of parliamentary elections within less than a year of the previous ones are now scheduled for September 11, 2016 and

for the last two months, our country has been run by so-called technical government. We have also modified our CapEx expectation for 2016 from moderately lower to slightly lower than 2015.

From our operational perspective, we continue to maintain our leadership position across all areas of the business as we push ahead with our transformation initiatives. In particular, Magenta 1, our converged premium customer offer, has boosted the number of broadband and TV customers.

We're also seeing growth in the take-up of our energy services. And in June this year, we launched for the first time a converged telco-energy proposition for our business customers, another product that differentiates us from our competitors and provides quality services and convenience with aim of increasing customer loyalty.

We have also benefited from an influx of visitors roaming onto our network in the six months to June 30th with visitors generating 27 percent more voice originating minutes and 143.5 percent more data traffic than in the same period last year. Our strategic Horizont 2016 program is progressing well. Two of the three phases have already commenced and are on track to deliver.

First phase projects have already delivered the expected results in the areas of defined strategies, enhanced customer experience, process improvements, and targeted financial impact. Project from second phase including B2B market strategy, network rejuvenation, and PAN NET, were launched in April and are progressing according to plan.

Please turn now to slide four where we will look at the breakdown of revenue growth. We have seen positive development in our low margin system solutions and energy segments, wholesale and handset sales. Mobile revenue, as you can see, rose 6.6 percent to HRK 1.35 billion largely due to sales of higher value Smartphones, increased data revenue, and the rise in wholesale revenue after to certain non-EU termination rates were deregulated in April 2015.

Fixed voice continued to decline amid fixed to mobile substitution, down 12.8 percent to HRK 488 million because of fewer mainlines, fewer calls, and lower average revenue per account. Broadband and TV revenue declined 2.4 percent in the first

half. Intense competition in the broadband market has impacted revenue and ARPU when this was only partially upset by an increase in TV revenue and related ARPU.

Fixed wholesale revenue rose 6.8 percent owing to the deregulation of non-EU termination rate discussed earlier as well as high infrastructure revenue. Our system solutions revenue rose strongly up to almost 28 percent to HRK 330 million as more projects were completed in the first half of 2016 compared to the same period last year.

ICT equipment sales also has lift system solutions revenue as did demand for our consulting services. The 80 percent jump in miscellaneous revenue reflect a strong rise in energy sales as HT Group wins more customers in both the residential and business segments. The company's focused on offering a converged proposition and we anticipate that customers who take both telecom and energy services are likely to remain more loyal.

Slide five describes the increases in EBITDA, net profit and cash flow during the first half as we continue to invest strongly in our network. EBITDA before exceptional items increased by HRK 90 million or 1.4 percent year on year in the six months to 30 of June 2016. This reflects rising revenue as well as profits on the sale of certain assets and the impact of the cost disciplines we have introduced. This increase in EBITDA was a factor in the 2.7 percent rise in net profit to HRK 470 million alongside lower depreciation and redundancy costs.

The net profit improvement was offset to a degree by the adverse effect of exchange rate fluctuations, most of which occurred in the first quarter of 2016 which we reported at the end of Q1. Net cash flow from operations rose 13.1 percent in the first half of 2016 to HRK 934 million mainly due to positive working capital movements and lower tax paid. Meanwhile, capital expenditure was up 10 percent following significant investments in developing the next generation fixed and mobile network.

We have also implemented changes to our services platforms to support roaming regulations, for example, and the grouped internal IT infrastructure has been updated adding to the CapEx outlay.

I will now hand over to our CFO, Josef Thürriegl, who we welcomed back to the Group in June in his new role as CFO to walk you through our performance during the period in more detail. Josef?

Josef Thürriegl: Yes, thank you, Davor. First of all, also, good morning from my side, and let me tell you how delighted I am to be working again within HT Group and to be able to present this set of results as the group CFO for half year.

Please turn first to slide six where we take a closer look at the residential segment. Here, revenue was up by 0.8 percent points during the first half, and the contribution of EBITDA was slightly down by 2.2 percent. This revenue was supported to some degree by the success of our Magenta 1 offer which is household-focused and therefore aims to tap into the fixed and mobile convergent trends.

So, Magenta 1's customized offers and numerous benefits for private customers and households have attracted meanwhile 20,000 customers since its launch in March. But we have also continued to actively promote our MAX2 and MAX3 packages which provide exclusive TV content and premium TV packages.

Turning to slide number seven, we will also take a look at the business segment where in the first half of 2016, the Group delivered a positive business segment performance. The revenue, for example, was up by 6.3 percent points in the segment which was underpinned by system solutions, wholesale and energy products. The rise in operating expenses have impacted the business segment's contribution to EBITDA. However, it was still 1.2 percent higher at HRK 643 million.

Within this segment, HT Group continues to focus on value management and customer retention so our flagship Magenta 1 proposition offers specific business to business benefits including the highest available Internet speeds, 4G backup, network security, and secure cloud storage. From June onwards, we're also going to offer energy bundles at attractive prices and we intend to focus on converged telco-energy bundle to further encourage our customer loyalty.

Turning now to slide eight, as you will see, the Group is focused on mobile data bundles and on improving the experience of its mobile customers, so, offering speeds meanwhile of up to 262 megabits per second. Here, HT Group's market share by

number of subscribers rose slightly to 46.9 percent at the end of the first half 2016 coming from 46.5 percent at the end of same period last year.

Meanwhile, the total number of subscribers remains largely unchanged at the end of the period as an increase in postpaid customers was offset by a decrease in prepaid users. Here, the postpaid customer ARPU was up by 1.4 percent while the prepaid customer ARPU slipped by 1.6 percent.

At the end of the period, average minutes was up by 6 percent in line with the overall market trends of fixed to mobile substitution and free minutes included within the tariffs. During the first half, the proportion of the total handset sales that were Smartphones increased up to 81 percent in the postpaid segment from 76 percent in the same period last year while HT Smartphone penetration still stood at 56 percent. We now reached 67 percent of the population with our 4G coverage indoors that even achieved the 95 percent outdoor coverage.

On slide number nine, we will take a look at our fixed line and IP business. The number of fixed lines was 7.1 percent lower at the end of the first half compared with the same period in '15, reflecting declines in both wholesale and retail lines. The fixed line ARPU was also lower, falling at 6.2 percent to HRK 85.

The broadband lines, however, were up 4.7 percent to 730,000 at the end of the first half, reflecting a 35 percent increase in wholesale broadband access lines. Still, broadband's retail ARPU was down 2.6 percent to HRK 122, reflecting the tough competition and aggressive offers that we see in the broadband market.

However, on a quarter-on-quarter basis, you would have noticed that we saw relatively strong growth of 6,000 broadband retail lines supported also mainly by the Magenta 1 bundled offerings. The number of TV customers increased to 395,000 at the end of the first half from 387,000 in the same period last year, and TV ARPU rose by 1.3 percent to HRK 82 driven mainly, again, by premium content and enhanced exclusive TV contents.

Having said this, I will now hand back to Davor who'll bring this presentation to a close with a preview of our output for the remainder of 2016.

Davor Tomašković: Thank you, Josef. To conclude this presentation of our first half 2016 performance on slide ten, I would like to largely reiterate our outlook for the full year. As I said at the beginning of the year and then later when we reported our first quarter results, we expect revenue for 2016 to be in a range of flat to minus 2 percent compared with last year.

As mentioned earlier today, we now expect the system solutions business to deliver a broadly stable performance. This will, along with other factors taken into account at the beginning of the year, have an adverse impact on H2 2016 revenue development.

EBITDA margin before exceptional items, however, should remain at around 40 percent. We now expect CapEx to be slightly lower in 2016 compared to the HRK 1.47 billion spent last year. With regard to regional expansion, HT is continuing to monitor and evaluate potential M&A opportunities. So, we will inform you in due course if there is any new development.

Thank you for your attention this morning. We are now ready to take any questions.

Operator: Thank you. As a reminder, if you wish to ask a question, please press star one on your telephone and wait for your name to be announced. If you wish to cancel your question, please press the hash key. (Slap) star one for any questions.

Thank you. Your first question comes from the line of (Jacob Carowitz) from RCB. Please ask your question.