The Q3 2018 results conference call

31 October 2018 at 11:00 CET

Presenters

Davor Tomašković
Hrvatski Telekom – President of the Management Board and CEO

Daniel Daub
Hrvatski Telekom - Member of the Management Board and CFO

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Operator: Good morning, ladies and gentlemen, thank you for standing by and welcome to the Hrvatski Telekom Results conference call for the nine months ended 30 September 2018.

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 Wednesday 31 October 2018. It is now my pleasure to hand you over to your first speaker today: Mr Elvis Knežević

Mr Elvis Knežević – please go ahead.

Elvis Knežević: Thank you

Ladies and gentlemen, good morning and welcome from Zagreb. Today our CEO Mr Davor Tomašković and Mr Daniel Daub, our CFO, will talk you through the highlights of our business and financial performance for the nine months ended 30 September 2018, 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 Tomašković 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 Davor Tomašković, our CEO, who will outline our company's performance during the nine months ended 30 September 2018.

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

It is my pleasure to present the results from Hrvatski Telekom for the nine months ended 30 September 2018. I will start the presentation with slide 3, which outlines the Group financial highlights for the period.

I am pleased to report an increase in EBITDA and net profit at both HT Group and HT Croatia while revenue remained stable in the first nine months of the year.

Revenue across the Group was flat at HRK 5.79 billion between January and September, reflecting a small decline in the revenue contribution from Crnogorski Telekom, offset by slight growth of 0.1% at HT Croatia. This broadly flat revenue at HT Croatia was achieved despite exiting some marginally profitable contracts in our energy business and the slowing of the extra high growth rates we have been seeing in visitors data traffic. Following a successful turnaround, revenue at Crnogorski Telekom has now fully stabilised, however it remains under pressure from aggressive competitive pricing in the local market and the regulatory environment.

EBITDA before exceptional items rose from HRK 2.35 billion to HRK 2.43 billion in the nine months to September 2018, along with improving margins.

We are reaping the rewards of our successful transformation program and cost savings measures implemented across the business and these initiatives, helped by the reduction in high spectrum fees and the implementation of IFRS 15, have lifted EBITDA margins to 41.9% from 40.5% in the prior year period.

HT Group net profit in the nine months to the end of September 2018 rose 18.6% to HRK 872 million, boosted by several factors including the rise in EBITDA before exceptionals, the absence of extraordinary receivables impairments and higher net financial income.

Please turn to slide 4 which covers the rest of financial highlights at HT Group in the first nine months of the year.

During the period, operating cash flow decreased but we continued to invest strongly in our network capabilities and our customer experience.

The decrease in cash flow from operating activities, which fell to HRK 1.80 billion from HRK 1.89 billion was largely due to unfavourable movements of working capital.

There was a slight decline of 0.8% in capital expenditure in the nine months to September, down to HRK 1.24 billion from HRK 1.25 billion.

Despite this marginal decline, we have continued to focus significant investment on mobile and fixed broadband networks, IT transformation, product development and regulatory related capex at HT Croatia, where capex expenditure fell 2.1% to HRK 1.13 billion.

Capex at Crnogorski Telekom rose by 14.7% or HRK 14 million due to investment focused on improving access to services.

Please turn now to slide 5 which shows the revenue performance for HT Croatia. We have maintained stable revenues despite exiting some marginally profitable contracts in our energy business and lower growth rates in visitors data traffic. Our mobile and system solutions businesses produced good performances in the period.

Total revenue in the nine months to September 2018 rose 0.1% to HRK 5.32 billion.

Mobile revenue was up 5.5% to HRK 2.36 billion due in large part to higher postpaid revenues when excluding the impact of IFRS 15, as well as more visitors to Croatia using our network and strong sales of handsets.

Fixed voice revenue fell 13.2% to HRK 560 million as mainline revenue, voice traffic and average revenue per user all declined. This decline is driven by the market trend of fixed to mobile substitution, regulation and enforced competition, but we continue to try and mitigate these effects with proactive and reactive churn prevention offers and activities.

Broadband and TV revenue fell 1.8% in the first nine months of the year, to HRK 975 million from HRK 993 million last year. While television revenue grew in the period, this was offset by a fall in broadband revenue which was affected by fierce competition and aggressively priced offers in the market.

Fixed wholesale revenue fell 16.2% to HRK 230 million mainly because of revenue deductions from H1 Telekom, which merged with Optima Telekom on 1 July 2017.

Other fixed revenue rose 7.1% to HRK 609 million on the back of an increase in Optima Telekom revenue following the consolidation of H1 Telekom.

Our system solutions business grew 1.7% in the nine months to September 30 to HRK 487 million as more projects came to fruition at both HT Croatia and Crnogorski Telekom, and we are on track to show good growth in the full year.

Finally, miscellaneous revenue fell 14.8% to HRK 96 million, reflecting the exit from some marginally profitable contracts in the first quarter of 2018 and the sale of Croatia Telecom's electric energy business to RWE Hrvatska in September 2018.

Energy revenue in the first nine months fell to HRK 80 million from HRK 105 million in the same period last year.

I would now like to hand over to our CFO Daniel Daub who will walk you through our operational performance during the first nine months of 2018 in more detail.

Daniel Daub: Thank you Davor and good morning everyone. Please turn to slide 6 which describes the performance of HT Croatia's mobile business, where we have maintained our leadership position in the market and in technology.

At the end of the third quarter 2018, HT Croatia's market share by subscribers was 45.2%. This is just a slight decline from the 45.8% reported at the end of September 2017 and we remain the market leader in mobile.

Total subscriber numbers were up 1.5% to 2.33 million at the end of the third quarter reflecting strong growth in postpaid customers offsetting a decline in the less profitable prepaid customers.

Postpaid customer numbers rose 6.8% to 1.31 million, while prepaid customers fell 4.5% to 1.03 billion.

Average revenue per user in the prepaid segment rose 2.2% to HRK 44. However, postpaid ARPU fell 3% to HRK 104, excluding the impact of IFRS 15, mainly due to a strong rise in M2M SIMs, which bring significantly lower revenues. Postpaid ARPU fell 19.2% to HRK 87 when the impact of IFRS 15 is taken into account.

Average minutes of use rose 3.2% to 223 minutes, and HT Croatia's smartphone proportion of total handset sales is now 91% in the postpaid segment, up from 80% in the first nine months of 2017. Smartphone customers account for 66% of HT Croatia's overall subscriber base.

By the end of the third quarter, HT Croatia's 4G network had reached 79% population coverage indoors and 98% coverage outdoors. We have started the modernization and capacity extension of our mobile network in preparation for the introduction of 5G.

Slide 7 shows the performance of HT Croatia’s fixed line and IP business, where TV customers have remained stable while their spending has risen, but fixed mainlines and broadband lines have decreased.

The number of fixed mainlines continues to decline, following the industry trend for fixed to mobile substitution. Fixed mainlines fell 6.7% to 888,000 at the end of the third quarter 2018 reflecting both wholesale and retail declines. We are managing this decline by developing innovative offers which appeal to the elderly, promoting attractive fixed line tariffs and providing connections for just HRK 1.

Fixed voice ARPU is also in decline because of fixed to mobile substitution, down 7.9% to HRK 73 in the third quarter, although it fell 7.1% when excluding the impact of IFRS 15.

The number of broadband access lines was down 1.4% to 748,000 in the nine months to the end of September, largely because of wholesale declines as more operators choose to use their own infrastructure. A slight decrease of 0.6% in the retail segment is the result of aggressively priced fixed to mobile substitution product offers from our competitors.

Broadband retail ARPU fell 5.4% to HRK 112 because of stronger competition and aggressively priced offers in the market. Excluding IFRS 15, broadband retail ARPU was HRK 113, a decline of 4.6%.

TV customers remained stable at the end of the third quarter compared to the same period last year at 413,000. We have managed to increase ARPU by 2.2% to HRK 83 (HRK 84 excluding IFRS 15) as we continue to provide the best premium television service on the market with our MAXtv product.

Next Generation Access speeds greater than 30 megabits per second have been enabled for 58.1% of Croatian households, while 399,000 households are now enabled for optical fiber network access with speeds of 100 megabits per second.

Please now turn to slide 8 which describes the standalone financial performance of Crnogorski Telekom. Revenue trends have stabilised after a good performance from mobile and system solutions, and our transformation initiatives are paying off with a boost to EBITDA margins.

This is a clear example of a successful turnaround story. To illustrate this achievement, we have also presented the growth rates the Company experienced just a year ago for comparable periods, that is Jan-Sep 2017 over Jan-Sep 2016.

At that time, as well as long period before that, growth was in negative territory and we have indicated this with the figures in black which sit above the actual growth rates for the reported period on the chart.

So, total revenue at Crnogorski Telekom fell slightly in the nine months to the end of September, down 0.4% to HRK 474 million. This compares to a fall of 7.7% a year ago. Mobile revenue was a strong performer, up 3.8% to HRK 248 million in the period driven by handset sales and postpaid customers, which offset the drag from prepaid customers and fewer visitors to Montenegro.

Crnogorski Telekom's fixed voice business is subject to the same fixed to mobile substitution issues that are affecting fixed line telephony worldwide, and revenue fell 10.3% to HRK 56 million.

Broadband and TV revenue also declined in the first nine months of the year, down 3% to HRK 88 million. The fall was largely due to lower Broadband ARPU which dragged broadband revenue down in the third quarter, offsetting a 2.3% rise in TV revenue in the period.

Fixed wholesale revenue fell 18.1% to HRK 15 million and other fixed revenue declined 8.7% to HRK 39 million.

System solutions revenue rose strongly to HRK 28 million from HRK 23 million last year.

An improvement in margins to 37.3% in the first nine months of 2018 from 35.3% in the same period last year helped boost EBITDA by 5.2% to HRK 177 million. This compares to a 5.8% decline a year ago.

Net profit at Crnogorski Telekom rose 53% to HRK 49 million, a significant upturn from the fall of 50.3% that was reported a year ago.

Slide 9 describes Crnogorski Telekom's mobile, fixed line and IP business, where we have seen a rise in all customer segments except fixed mainline.

The number of mobile subscribers at Crnogorski Telekom rose 3.8% to 384,000 at the end of the third quarter, reflecting a 10.8% increase in postpaid customers tempered by a 4.7% fall in prepaid customers.

Fixed retail mainlines were down 8.9% to 116,000 at the end of the third quarter.
In the same period the number of broadband retail access lines rose 0.5% to 71,000 and the number of TV customers was up 6.2% to 61,000.

I will now hand back to Davor, who will outline our outlook for 2018

Davor Tomašković: Thank you Daniel.

Please turn now to slide 10 for our Group outlook 2018.

There has been one adjustment to the outlook since the guidance was provided at the first quarter results in April.

We now expect revenue in the current year to be around the 2017 level of HRK 7.76 billion. Previous guidance had forecast ‘slightly higher’ revenue.

The rest of the outlook remains unchanged. We are anticipating an EBITDA margin before exceptional items of around 40%, compared with the 40.5% reported for 2017.

Capex in 2018 is expected to be slightly lower than the HRK 1.89 billion spent in 2017.

And we will again continue to monitor and evaluate potential M&A opportunities.

Thank you for your attention.

We are now ready to take your questions.