



Zagreb – 28 July 2016

## Hrvatski Telekom Results for the first six months ended 30 June 2016

### Hrvatski Telekom: All financial indicators are up, higher revenue and net profit

Hrvatski Telekom (Reuters: HT.ZA; Bloomberg: HTRA CZ), Croatia's leading telecommunications services provider, announces its unaudited consolidated results for the six months ended 30 June 2016.

In H1 2016, Hrvatski Telekom saw a 3% revenue increase to a HRK 3.4 billion compared to the same period 2015. The first two quarters also recorded a 1.4% growth in earnings before interest, tax, depreciation, and amortisation (EBITDA before exceptional items). EBITDA amounted to HRK 1.34 billion with a 39.3% EBITDA margin. H1 2016 net profit was HRK 417 million, which was 2.7% above H1 2015.

### Continued investment cycle, increased investment in innovative services and infrastructure

H1 2016 was marked by intensive activities focusing on customer experience improvement, innovative service, and continued investment in infrastructure. The strong investment cycle was continued, leading to a 10% increase in CAPEX to HRK 645 million compared to H1 2015 with a focus on fixed and mobile network development, especially increase of the broadband Internet access capacity.

Access speeds in 4G network increased from 150 Mbit/s to 225 Mbit/s, in certain areas even to 262.5 Mbit/s. Indoor coverage increased from 65.2 per cent to 67.4 per cent of the population. In the fixed network, the possibility of fibre optic access was extended to more than 227 thousand households.

In H1 2016, Hrvatski Telekom presented a new, unique concept of service offering on the Croatian telecommunications market – Magenta 1. Innovative in its concept and the main idea, Magenta 1 integrates all fixed and mobile services in a single package. The fact that Magenta 1 has been accepted by more than 20,000 customers shows that with this innovation HT has recognised their needs.

The projects implemented in the first wave of the HorizonT programme have yielded the expected results in the areas of customer experience, business improvement, and financial performance.

Commenting on the half-year performance, **Davor Tomašković, President of the Management Board of Hrvatski Telekom**, pointed out: *“We can be very satisfied with the financial performance for the first six months as it shows that customers have recognised all the benefits of our fixed and mobile offers. We have recorded an increase in the average revenue per customer, inflow of new customers in the mobile network, and a growth in the ICT and energy segments. Therefore, we will continue investing in network infrastructure and innovative services, in maintaining and strengthening our position of a technological leader on the Croatian market, and in improving customer experience.”*

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A conference call for analysts and investors will be held at 10:00 UK time / 11:00 CET on the same day.

The conference call dial in details are as follows:

International Dial In +44 (0) 1452 555 566  
Conference ID 54269368

A replay of the call will be available until Thursday, 4 August 2016 using the following details:

International Dial In +44 (0)1452 550 000  
Conference ID 54269368

A presentation covering results for the first six months of 2016 can be downloaded from the HT web site ([www.t.ht.hr/eng/investors/](http://www.t.ht.hr/eng/investors/)).

# 1. Review

## 1.1 Introduction

### HT Group's good performance in H1 2016

HT Group has successfully responded to market challenges and maintained a leading position in the Croatian telecommunications market across all business segments in the first half of 2016. Differentiation of HT Group offers and positioning of brands contributed to strengthen position on the market.

## 1.2 Market overview

### All key players continue with investments in networks; integrated fixed/mobile/ICT offers available in the market

Investments in telecommunications grew by 18% in the first quarter of 2016 compared to the first quarter of 2015. The major part of the investments was into modernization of networks and NGA infrastructure, particularly in high-speed internet access.<sup>1</sup>

Croatian mobile market has been determined by strong competition and regulatory measures that impact mobile revenue. Mobile SIM market contraction has been slowing down in 2016 vs. 2015. Estimated mobile SIM penetration rate was 114.7% at the end of June 2016. The estimated Company's share of total mobile customers is 46.9% at the end of June 2016.

All three mobile operators offer 4G services with favourable data packages and attractive smartphones/ tablets that additionally encourage usage of OTT services. As a result, mobile data traffic recorded significant growth.<sup>2</sup> Total Croatian mobile market minutes of use (MOU) grew by 0.3% yoy in Q1 2016 while the total number of sent SMS messages continued to decrease on annual basis by 9.1% in Q1 2016.<sup>2</sup>

Amount of fixed originating voice minutes declined by 11.5% yoy in Q1 2016. Total broadband traffic grew by 39.7% in Q1 2016 compared to total traffic in Q1 2015.<sup>2</sup>

Besides classic telecommunication services offers, HT Group introduced Magenta1, a unique concept of integrated services offering, in March 2016.

According to the Croatian Post and Electronic Communications Agency, Croatian fixed broadband market continued to grow yearly by 4.3% in Q1 2016. There were more than 996 thousand fixed broadband connections in use at the end of Q1 2016. Out of them, 44% had access speed over 10 Mbit/s.<sup>2</sup>

HT Group has set a strong focus on further development of the network infrastructure, increasing broadband access capacity and availability to maintain a leading position as the largest fixed broadband operator in Croatia. HT Group had 607 thousand of broadband access lines at the end of June 2016.

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<sup>1</sup> Source: Croatian Post and Electronic Communications Agency

The Croatian Pay TV market continues with growth and grew by 3.2% yoy in Q1 2016 reaching 771 thousand customers. The leading Pay TV technology is IPTV, although DTT has the highest growth rate compared to Q1 2015 (19.1%).<sup>2</sup>

### **Wholesale**

Following liberalization of the fixed line market, demand for infrastructure services requested by alternative operators remains high in H1 2016 with major focus on broadband services. The number of broadband wholesale customers (BSA and Naked BSA) increased to 123 thousand at the end of June 2016 that is increase of 35.2% compared to end of June 2015. Due to high churn and migration to broadband services, number of Unbundled Local Loops (ULL) and Wholesale Rental Lines (WLR) is decreasing which resulted with 153 thousand of ULL access and 96 thousand of WLRs at the end of June 2016.

### **IT market**

According to IDC Adriatics<sup>2</sup>, Croatian IT market is expected to grow by 4.8% yearly in 2016. The strongest growth is projected for IT services (5.7%), followed by Packaged Software (5.4%) and Hardware (4.0%). HT Group is positioned in all three segments by providing standard and customized services with strategic focus on Cloud and Managed services.

### **Energy market**

Business retail energy market is entering consolidation phase after three years experiencing tough price war. Incumbent has tried to win back lost market share, but still app. 40% of business customers are held by alternative suppliers. The profit margins on supply in business are suppressed due to competition.

Unlike all other energy suppliers, who are running business as primary activity, HT is seeking to exploit synergy effect from telco-energy convergent proposition which is launched for the first time in June 2016 as highly innovative offer.

## **1.3 Economic background**

### **Domestic demand becomes the main driver of moderate growth**

Croatian GDP grew by 2.7% on a yearly basis in Q1 2016. The largest positive contribution to the GDP's growth came from the increase of personal consumption.<sup>3</sup> The recovery of personal consumption is supported by mild employment growth and more available net income due to the absence of inflation and reduced interest rates on loans.

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<sup>2</sup> Source: IDC Adriatics, May 2016

<sup>3</sup> Source: Croatian Bureau of Statistics

With a growth rate of 1.6% yoy, the industrial production data for May 2016 confirmed positive movements for the 16th month in a row.<sup>1</sup>

Coming closer to the peak of the tourist season, the usual seasonal decline in the unemployment rate is additionally supported by positive movements in the economy. The registered unemployment rate in May stood at 14.4% (down by 2.7pp in annual terms).<sup>1</sup>

Reported average net income for April 2016 amounted to HRK 5,633 (up by 2.4pp in annual terms).<sup>1</sup> Average annual inflation rate in May 2016, calculated by Consumer Prices Index (CPI), was -1.8%.<sup>1</sup>

## **1.4 Regulatory environment**

### **Determining the reasonable return on investment rate (WACC)**

On May 31<sup>st</sup>, 2016, Croatian Regulatory Authority for Network Industries (HAKOM) adopted decision related to a decrease in the weighted average cost of capital (WACC) rate in order to implement the regulatory obligation of price control and cost accounting in mobile and fixed network. New WACC rates are:

1. 8.73% for services in fixed public communications network
2. 9.13% for services in mobile public communications network

WACC rate for services in fixed public communications network will be increased by the additional WACC rate (WACC surplus) of 3.33% for services based on FTTH/FTTB concept.

New WACC rates will be applicable in the period from January 1<sup>st</sup>, 2017 until January 1<sup>st</sup>, 2020. HT is obliged to use the above mentioned WACC rate under 1, including the possibility to use WACC surplus for FTTH/FTTB concept, in its regulatory financial statements for the years 2016, 2017 and 2018.

### **Determining the monthly fee for the fully unbundled local loop (ULL) service on the basis of a copper pair**

On May 31<sup>st</sup>, 2016, HAKOM adopted a decision on reduction of the monthly fee (price) for ULL based on BU-LRAIC+ cost model. New ULL price is set at the level of HRK 49.53 and will start to apply from January 1<sup>st</sup>, 2017.

### **Determining new fees for the wholesale broadband access service (BSA)**

On June 29<sup>th</sup>, 2016 HAKOM initiated public consultation regarding the decision proposal on reduction of fees for BSA and NBSA access on copper (BSA access where the network access is realized via services provided by the alternative operator) and BSA service on FTTH, and the introduction of a new category of BSA prices, the price for NBSA on ADSL/VDSL technology for the speeds of 30 Mbit/s and above. Decision proposal is based on BU-LRAIC+ cost model of HAKOM.

### **Amendment to the Reference Offer for Wholesale Broadband Access (BSA)**

Pursuant to HAKOM's decision as of March 15<sup>th</sup> 2016, HT amended its BSA Reference Offer in order to make the BSA (bitstream access) service on VDSL available to customers on loops longer than 1.000 m, but shorter than 1.500 m.

Pursuant to HAKOM's decision from June 29<sup>th</sup> 2016, HT amended its BSA Reference Offer in order to include prices for BSA access in case where fibre optics in-house installation is not included in the provision of BSA service. These cases will occur in situations where HT will provide BSA services via newly built fibre optics access network (built according to the Ordinance on fibre optics distribution networks).

## 1.5 Changes in reporting

### Optima Telekom

In 2014 Croatian Competition Agency has conditionally allowed the concentration of HT with Optima Telekom based on the proposal of financial and operational restructuring of Optima Telekom within the pre-bankruptcy settlement procedure. Croatian Competition Agency has determined a set of measures defining the rules of conduct for HT with regard to management and control over Optima Telekom, among which is the implementation of so called "Chinese wall" between Optima Telekom's and HT employees involved in Optima Telekom's business, in relation to all sensitive business information, with the exception of reporting of financial data necessary for consolidation. Respectively only financial statements are consolidated while due to limited access to Optima Telekom's information, non financial KPIs are not consolidated in the Group results.

### Costs related to the electronic communication infrastructure (ECI)

In 2015, the Company voluntary changed its accounting policy in regard to costs related to the electronic communication infrastructure (ECI) rights of servitude and rights of way. It determined that ECI contracts meet the criteria for capitalization as intangible assets. The effects of the accounting policy change on financial information for 2015 are recognized at year end, respectively restatement of financial data for the first half of 2015 was done as follows: EBITDA before EI increase of HRK 13 million, increase in Capex of HRK 34 million and increase in cash flow from operating activities of HRK 13 million.

## 1.6 Summary of key financial indicators

in HRK million	Q2 2015	Q2 2016	change	Jan-Jun 2015	Jan-Jun 2016	change
Revenue	1,686	1,729	2.6%	3,304	3,402	3.0%
Mobile	644	696	8.1%	1,267	1,350	6.6%
Fixed voice	277	241	-12.7%	560	488	-12.8%
Broadband & TV	335	328	-1.9%	668	652	-2.4%
Fixed wholesale	88	87	-0.9%	161	172	6.8%
Other fixed	186	186	0.0%	364	363	-0.4%
System solutions	145	165	14.2%	258	330	27.9%
Miscellaneous	12	25	110.0%	26	46	80.2%
EBITDA before exceptional items	692	711	2.8%	1,320	1,339	1.4%
Exceptional items	8	2	-70.4%	81	62	-23.8%

EBITDA after exceptional items	684	709	3.6%	1,239	1,277	3.1%
EBIT (Operating profit)	328	367	12.0%	520	586	12.6%
Net profit	255	282	10.3%	406	417	2.7%
EBITDA margin before exceptional items	41.1%	41.1%	0.1 p.p.	39.9%	39.3%	-0.6 p.p.
EBITDA margin after exceptional items	40.6%	41.0%	0.4 p.p.	37.5%	37.5%	0.0 p.p.
EBIT margin	19.4%	21.2%	1.8 p.p.	15.7%	17.2%	1.5 p.p.
Net profit margin	15.1%	16.3%	1.1 p.p.	12.3%	12.3%	0.0 p.p.

in HRK million	At 31 Dec 2015	At 30 Jun 2016	change
Cash and cash equivalents	3,175	2,916	-8.2%
Total assets	14,079	13,676	-2.9%
Total issued capital and reserves	11,641	11,589	-0.5%

in HRK million	Q2 2015	Q2 2016	change	Jan-Jun 2015	Jan-Jun 2016	change
Net cash flow from operating activities	400	359	-10.2%	826	934	13.1%

#### RESIDENTIAL SEGMENT

in HRK million	Q2 2015	Q2 2016	change	Jan-Jun 2015	Jan-Jun 2016	change
Revenue	917	939	2.5%	1,838	1,853	0.8%
Contribution to EBITDA before EI	653	640	-2.0%	1,293	1,264	-2.2%

#### BUSINESS SEGMENT

in HRK million	Q2 2015	Q2 2016	change	Jan-Jun 2015	Jan-Jun 2016	change
Revenue	656	677	3.1%	1,249	1,328	6.3%
Contribution to EBITDA before EI	340	339	-0.3%	636	643	1.2%

#### NETWORK & SUPPORT FUNCTIONS

in HRK million	Q2 2015	Q2 2016	change	Jan-Jun 2015	Jan-Jun 2016	change
Contribution to EBITDA before EI	-359	-327	8.9%	-720	-682	5.2%

#### SEGMENT OPTIMA TELEKOM CONSOLIDATED

in HRK million	Q2 2015	Q2 2016	change	Jan-Jun 2015	Jan-Jun 2016	change
Revenue	113	113	0.3%	218	221	1.7%
Contribution to EBITDA before EI	58	60	2.1%	111	113	2.2%

### 1.7 Exchange rate information

	Kuna per EURO		Kuna per U.S dollar	
	Average	Period end	Average	Period end
Six months to 30 Jun 2015	7.62583	7.58066	6.84113	6.82942
Six months to 30 Jun 2016	7.55801	7.51274	6.77402	6.79148

## 2. Business Review

Key operational data	Q2 2015	Q2 2016	change	Jan-Jun 2015	Jan-Jun 2016	change
<b>Mobile customers in 000</b>						
Number of customers	2,241	2,246	0.2%	2,241	2,246	0.2%
- Prepaid	1,136	1,119	-1.5%	1,136	1,119	-1.5%
- Postpaid	1,105	1,128	2.0%	1,105	1,128	2.0%
Minutes of use (MOU) per average customer	200	214	7.1%	194	205	6.0%
Blended ARPU (monthly average for the period in HRK)	76	77	1.2%	74	75	1.6%
- Prepaid	44	42	-3.2%	42	41	-1.6%
- Postpaid	108	110	1.8%	107	109	1.4%
SAC per gross add in HRK	91	103	12.8%	97	103	5.3%
Churn rate (%)	2.3	2.2	-0.1 p.p.	2.3	2.4	0.1 p.p.
Penetration (%) <sup>1)</sup>	114	115	0.6 p.p.	115	115	0.0 p.p.
Market share of customers (%) <sup>1)</sup>	47	47	0.5 p.p.	47	47	0.4 p.p.
Smartphone customers (%) <sup>2)</sup>	43	56	13.8 p.p.	43	56	13.8 p.p.
Smartphones sold (%) <sup>3)</sup>	76	80	4.0 p.p.	76	81	5.0 p.p.

1) Internal estimations

2) Number of customers using a smartphone handsets in total number of mobile customers

3) Number of smartphones sold in total number of handsets sold (postpaid only)

Key operational data	Q2 2015	Q2 2016	change	Jan-Jun 2015	Jan-Jun 2016	change
<b>Fixed mainlines in 000</b>						
Fixed mainlines - retail <sup>1)</sup>	1,012	945	-6.7%	1,012	945	-6.7%
Fixed mainlines - wholesale (WLR)	109	96	-12.4%	109	96	-12.4%
ARPU voice per user (monthly average for the period in HRK) <sup>2)</sup>	90	85	-6.3%	91	85	-6.2%
<b>IP mainlines/customers in 000</b>						
Broadband access lines - retail <sup>3)</sup>	606	607	0.1%	606	607	0.1%
Broadband access lines - wholesale <sup>4)</sup>	91	123	35.2%	91	123	35.2%

TV customers	387	391	1.1%	387	391	1.1%
Broadband retail ARPU (monthly average for the period in HRK)	126	123	-2.5%	125	122	-2.6%
TV ARPU (monthly average for the period in HRK)	81	82	0.9%	81	82	1.3%
<b>Wholesale customers in 000</b>						
ULL (Unbundled Local Loop)	162	153	-5.0%	162	153	-5.0%

<sup>1)</sup> Includes PSTN, FGSM and old PSTN Voice customers migrated to IP platform; payphones excluded

<sup>2)</sup> Payphones excluded

<sup>3)</sup> Includes ADSL, VDSL, FTTH and Naked DSL

<sup>4)</sup> Includes Naked Bitstream + Bitstream

Note: Optima Telekom's non financial KPIs not integrated into Group results due to limited access to Optima Telekom's information as a result of "Chinese wall" introduced by regulator

## MAJOR ACHIEVEMENTS

- Significant efforts taken to maintain position in the market
  - HT managed to keep the leading mobile market share with stable estimated portion of 46.9%
  - HT Group increasing broadband access capacity and availability to maintain a leading position as the largest fixed broadband operator in Croatia which has started to offer LTE throughput of 262.5 Mbit/s in selected areas
  - HT has launched Magenta 1 as fixed and mobile convergent offer that defines trend of new market drive.
- The main financial KPIs stabilized
  - Revenue is above H1 2015 by HRK 98 million or 3.0% driven by growing mobile, system solution, energy business and fixed wholesale
  - EBITDA is above H1 2015 by HRK 19 million or 1.4%
- Key strategic milestone for 2016 developing
  - The strategic program Horizont 2016 is sequenced into three waves out of which two have already started. First wave projects have already delivered expected results in areas of defined strategies, enhanced customer experience, process improvements and targeted financial impact. Projects from second wave (B2B Market Strategy, NT Rejuvenation, etc) have been launched in April and are progressing according to plan.
  - Magenta 1 results confirm FMC as the main market driver, in 3 months 20 thousand customers achieved
- Significant investment in network driven by integrated network strategy and regulatory demand
  - Capex is above H1 2015 by HRK 59 million or 10.0%

- 4G population coverage increased from 65.2% at the end of 2015 to 67.4% at the end of H1 2016
- Optical access network FTTX access is enabled for 227 thousand households at the end of H1 2016

### **Mobile telecommunications**

Mobile customer base increased by 0.2%, to 2,246 thousand customers at the end of H1 2016 in comparison to H1 2015 mainly as a result of launch of new mobile attractive tariffs “Najbolja” in second half of 2015, growth in M2M and mobile internet and launch of Magenta 1 convergent offers in March 2016. Increase was partially offset by overall aggressive competitors offers on the market and decrease of customers with double SIM cards due to continuing trend of favorable flat and cross net offers.

Number of postpaid customers was higher by 2.0% than at the end of H1 2015 as a result of overall push of successful and attractive tariffs and handsets as well as Mobile Net offers.

End of March HT presented its new unique concept of premium customer experience and benefits called Magenta1 which offers HT private and business customers numerous free benefits such as TV packages, fastest internet speed, additional international and national minutes, discounts on mobile tariffs for all household, attractive smartphones including Samsung J3.

The goal of Magenta 1 is to ensure complete services for the household and the best mobile and fixed services to all customers. All private customers will enter the Magenta1 world immediately if they use HT’s internet line in their household and at least one mobile HT line and will become a part of whole new world of special, custom-made offers and benefits. On the occasion of presenting Magenta1, in April 2016, HT organized a free concert of popular Croatian artists Gibonni and Oliver as a gift to citizens. Second wave Magenta1 campaign was launched in Q2 prior to European Football championship together with giveaway on social networks that invited everyone to support the Croatian national football team.

In March, HT launched sales of Samsung Galaxy S7 and Samsung Galaxy S7 Edge, the new generation of Samsung’s most popular smartphone. The phones are available in the “Najbolja” tariffs plans which include the highest 4G speed with the highest 4G coverage in Croatia. Furthermore, new iPhone SE, Apple’s response to the customers’ wishes for smaller screen dimensions, started selling in Croatia in April through HT web shop.

Number of prepaid customers was 1.5% lower than in H1 2015 due to overall decline of prepaid market and strong competition. On-going MNP and retention efforts in prepaid segment as well as focusing on additional value for HT prepaid customers are being undertaken to mitigate the on-going decline. HT prepared a special offer for tourists this summer including 7 days of flat mobile internet at 4G speed (up to 75 Mbit/s) in Croatia for HRK 85.

Bonbon continued with bringing its customers additional value, this time through media campaign “Moćni noćni paket” with additional number of minutes, messages and MB from 19pm to 7am for only HRK 10. Furthermore, all customers are able to set their own combination of smartphones/gadgets with additional discounts available. Among other well-known Bonbon benefits, new postpaid users are still able to get discounts on L and XL packages, 1,000 minutes and 1,000 SMS until 2020 and can set their spending limit according to their possibilities.

HT innovative mobile advertising service, Kupon2go, which sends users text messages or push notification informing them about sales and discounts at stores near their location, was further improved with developed mobile application for Apple's and Android devices.

At the end of H1 2016, minutes of usage per average customer increased by 6.0% compared to the H1 2015 and it is in line with overall market trends of fixed to mobile substitution and free minutes included in tariff.

Blended ARPU increased by 1.6% compared to H1 2015 as a result of postpaid ARPU overachievement resulted from better tariff mix and good results of "Najbolje" tariffs.

### **Fixed line**

By the end of H1 2016, total fixed access mainlines of 945 thousand were by 6.7% lower than at the end of H1 2015. Decline is driven by the market trend of fixed to mobile and IP substitution, regulation and enforced competition but HT further continues with pro - and reactive churn prevention offers and activities.

To mitigate the on-going decline promo offer for fixed line was introduced offering phone connection for HRK 1 with 24 MCD accompanied by new attractive fixed line tariffs.

Fixed voice ARPU decreased by 6.2% compared to H1 2015 as a result of mentioned general market trends and lower usage.

### **Broadband**

At the end of H1 2016 broadband customer base was higher by 0.1% in the comparison to the end of H1 2015 reaching 607 thousand, due to Magenta 1 proposition offer results.

At the same time broadband retail ARPU was 2.6% below H1 2015 at the level of HRK 122 due to stronger competition and aggressive offers in the market. To mitigate the decrease HT continues with push of MAX2/MAX3 packages and Ultra MAX packages on FTTH. The offer was accompanied by attractive promo options included in the price and MAXtv for all new Ultra MAX customers for HRK 1 for first 9 months of usage. These packages are based on FTTH technology which enables ten times higher speed than the standard ADSL. In addition, at the end of March 2016 new convergent Magenta 1 Business packages were launched, consists of flat fixed and mobile service with highest available speeds, 4G backup, network security and Cloud storage of 1 Terabyte capacity. HT will continue to invest in the development of the fiber network and plans to expand the fiber optical internet zones.

H1 2016 result was influenced by contribution of Smart office packages launched in Q4 2015 for small and medium business customers with high speed flat internet and fixed line, including antivirus protection, Business Connect application and possibility of 4G backup, making it unique and most reliable connection for business customers on Croatian market.

## TV

TV customer base increased by 1.1% in comparison to H1 2015 year as a result of continuous service and program offer improvements which resulted with higher TV ARPU by 1.3% in comparison to H1 2015 driven by premium content and enriched exclusive TV content. Moreover, HT continued with promotion of MAXtv package Pickbox which contains more than 70 hit series and 300 movies and covers the majority of Hollywood productions. Furthermore, Pickbox can be used in the same time on TV and other devices – mobile phone, tablet or laptop without any additional fee.

Satellite TV, which is an extension of classical IPTV service, continues to grow with further improvements in offerings providing more value for the customers and is expected to contribute significantly to the overall TV success. It continued with attractive promo offering 50% discount on Basic or Basic Extra package monthly fee for first 9 months for activations during promo period.

## Wholesale

At the end of H1 2016 there were 153 thousands of active ULL lines, which was lower by 5.0% in comparison to the same period last year. Number of ULL lines decreased due to higher focus of alternative operators to broadband services.

Broadband wholesale access lines (BSA and naked BSA lines) reached 123 thousands, which was 35.2% above number of lines at the end of same period in 2015 with main contributor being increase of number of naked BSA lines.

Number of WLR lines at the end of H1 2016 decreased by 12.4% and reached 96 thousands compared to the end of H1 2015 as a result of declining voice market. As a consequence of WLR offer, the number of “pure” CPS customers was reduced comparing to the same period last year.

In H1 2016 successful sales continued in spite of competitive domestic wholesale market of data and IP services. Especially successful was sale of IP upstream services with growth of 123.3% in volume comparing to the same period last year.

In the international wholesale market total capacity of sold IP and data services increased by 17.5% where only sales of IP services grew by 41.6% contributing to stability of international wholesale revenue.

Visitor roaming services are significant source of international wholesale revenue. Roaming traffic shows further growth in 2016, both from foreign visitors in HT mobile network and by HT retail users abroad. Visitors generated 27.4% more voice originating minutes and 143.5% more data traffic than in the same period last year. At the same time, on the wholesale cost side, HT's mobile customers generated 26.6% more roaming voice traffic in foreign countries and 400.7% more data traffic. During H1 2016, additional 4G (LTE) international roaming services with foreign partners were set up reaching 81 4G worldwide roaming interconnections in total.

Another significant contributor to wholesale international revenue is termination and transit of international voice traffic. Total international voice traffic volume terminating in HT mobile network increased by 24.4% compared to the same period 2015. On the wholesale cost side, international outgoing traffic from HT fixed network users decreased by 15.2% and from HT mobile network users increased by 19.0%.

## **System solutions**

Continuous growth in all portfolio segments was driven by HT Group's strategic focus in the area of Cloud and Managed Solutions. The strongest growth was recorded in the area of customized ICT solutions.

Focus continues to be on market education and customer experience to further strengthen leading position of HT Group on the market. Additionally, high focus is on development of telco and ICT converged proposition. The biggest projects were recorded in the banking, real and telecommunication sector in all production/service segments, but primarily in the IP communication and security, IT infrastructure and professional solutions segment.

## **Energy**

Revenue from energy was higher by HRK 19 million or 91.5% compared to H1 2015 due to higher number of customers by 24.2%. Growth is present in both residential and business segment with even more positive outlook in the future. Telco-energy convergent proposition is in focus with intention to increase customer loyalty.

# **3. Group financial performance**

## **3.1 Revenue**

In order to maintain consistency with the 2016 year presentation of revenues in new structure, previous year items were reclassified for comparative purposes. The main revenue items used in the past for the revenue presentation: voice revenue, non voice revenue, other service revenue, terminal equipment revenue and miscellaneous revenue are changed to new categories: mobile revenue, fixed revenue, system solution revenue and miscellaneous. This change makes the financial data of HT Group more comparable with other market participants.

Total consolidated revenue increased by HRK 98 million or 3.0% to HRK 3,402 million in H1 2016 in comparison to H1 2015. Increase is driven by higher mobile revenue (HRK 84 million or 6.6%), system solution revenue (HRK 72 million or 27.9%) and miscellaneous revenue (HRK 21 million or 80.2%), but this increase is partially offset by decrease in fixed revenue (HRK 78 million or 4.5%).

Optima Telekom contribution to HT Group was in line with H1 2015 and amounted to HRK 151 million in H1 2016 and consisted of HRK 221 million of Optima Telekom third party contribution (H1 2015: HRK 218 million) that was presented in the whole amount under fixed other revenue and HRK 71 million of inter-company relations that decreased mainly fixed wholesale revenue (H1 2015: HRK 66 million).

Contribution of subsidiaries in Group revenue in H1 2016 amounted for Iskon HRK 186 million (H1 2015: HRK 188 million) and for Combis HRK 237 million (H1 2015: HRK 194 million).

## **Mobile revenue**

Mobile revenue rose by HRK 84 million or 6.6% to HRK 1,350 million in H1 2016 in comparison to H1 2015. The growth resulted mainly from higher handset revenue, postpaid revenue and other mobile revenue, while prepaid revenue decreased.

From total deviation, HRK 86 million or 10.4% came from residential segment, while business segment contributed negatively (HRK 2 million or 0.5%).

The handset revenue growth was driven by the increased sales volume of smartphones, higher number of contract prolongations taking handsets and higher share of more valuable handsets mainly in residential segment additionally supported by growing convergent offers.

Postpaid revenue increased primarily due to higher mobile data revenue as both number of subscribers and usage increased as a result of continuous substitution trend of traditional voice and SMS services with data, higher number of data traffic included in tariff bundles and increasing share of customers having smartphones. Tariffs "Najbolje" introduced in 2015 contributed to higher data revenue with focus on 4G network services included in tariffs.

SMS revenue increased by HRK 6 million or 9.9% as a result of higher number of messages sent by 0.9% both in business and residential segment.

MTC revenue increased as a result of deregulation of non EU international termination rate from April 2015. Rate was increased from 0.063 HRK/min in H1 2015 to 1.73 HRK/min in H1 2016.

This revenue increase was offset by decline in voice revenue due to fierce price competition.

Prepaid revenue decrease was a result of lower retail revenue and MTC. The retail prepaid was lower (HRK 8 million or 3.2%) due to lower customer base (1.5%) that resulted with lower voice and SMS revenue. Revenue decline was partially compensated by mobile data growth as a result of continuous promotional offers with focus on data traffic and 4G speed.

## **Fixed revenue**

Fixed revenue dropped by HRK 78 million or 4.5% to HRK 1,675 million in H1 2016 in comparison to H1 2015. The fall resulted mainly from lower voice revenue, broadband revenue, terminal equipment revenue and other fixed revenue but it was partially compensated by higher wholesale revenue, data communication revenue and TV revenue.

From total deviation, HRK 73 million or 7.3% came from residential segment and HRK 9 million or 1.7% came from business segment while Optima consolidated segment contributed more.

In H1 2016, fixed line voice retail revenue decreased in comparison to H1 2015 mainly as a result of continuous decline in the number of fixed mainlines (6.7%) due to ongoing fixed to mobile substitution trend coming from strong mobile offers which are much more attractive than fixed voice propositions and strong regulatory environment. Consequently, number of minutes dropped and ARPU voice per user declined by 6.2%. ARPU decline is a result of more low value residential customers using fixed voice services (mostly elderly population).

To slow down erosion of customer base, pro- and reactive churn prevention actions are taken. In residential segment new attractive fixed line tariffs were introduced, accompanied with phone connection for HRK 1 with 24 MCD. In business segment, new Smart Office packages were introduced in order to ensure stable customer base development.

Decrease in broadband revenue was a result of lower broadband retail ARPU despite of slightly higher broadband customer base. ARPA decline in residential segment is a result of stronger competition and aggressive offers in the market. To mitigate the decrease HT continues with push of MAX2/MAX3 packages and Ultra MAX on FTTH. Customer base slightly higher as a result of Magenta 1 proposition offer results. In business segment, lower customer base together with lower ARPU is driving lower revenue result.

Other fixed revenue decrease was driven by lower installation revenue and value added services due to lower number of acquired customers and overall customer base decline. This decline was partially offset by higher contribution of Optima consolidated segment.

Fixed wholesale revenue increased mainly due to higher infrastructure wholesale revenue driven by NBSA growth while IP and data services decreased due to lower prices. Positive contribution from deregulation of international prices as of April 1, 2015 was offset by lower termination traffic in H1 2016.

Fixed retail data revenue increase mainly came from higher Ethernet service ARPU.

TV revenue increased in comparison to the same period last year due to increased TV customer base by 1.1% and higher ARPU by 1.3%. In residential segment TV customer base increase is a result of continuous service and program offer improvements which also resulted with TV ARPU 0.7% above H1 2015 driven by premium content and enriched exclusive TV content. Moreover, HT continued with promotion of MAXtv package Pickbox which contains more than 70 hit series and 300 movies and covers the majority of Hollywood productions.

### **System Solutions**

System solution stream is becoming significant source of HT Group revenue growth. System solution revenue increased by HRK 72 million or 27.9% to HRK 330 million in H1 2016 in comparison to H1 2015.

Higher Combis contribution is the result of higher realization in most segments, but primarily in IP communication part (network and security projects) and application development/professional services. HT Inc contributed to growth mostly in sale of ICT equipment, licenses, specific IP communication and safety equipment, enterprise software/professional solutions, but also in providing consulting services.

### **Miscellaneous revenue**

Miscellaneous revenue increased by HRK 21 million or 80.2% to HRK 46 million in H1 2016 in comparison to H1 2015.

Increase in miscellaneous revenue mainly comes from energy business due to higher customer base (24.2%). Efforts to increase customer loyalty are being undertaken constantly.

### **Other operating income**

Other operating income increased by HRK 31 million or 81.0% compared to HRK 69 million in H1 2015 mainly as a result of higher sale of fixed assets mainly coming from sale of lands in Rijeka and Požega as well as sale of vehicles, and commitment write off related to obligation for antenna poles retirement.

## **3.2 Operating expenses**

Total consolidated operating expenses increased by HRK 91 million or 4.3% to HRK 2,195 million in H1 2016.

This increase was a result of higher material expenses and other expenses compensated with lower employee benefits expenses, write down of assets and higher work performed by the Group and capitalized.

Excluding redundancy costs of HRK 62 million (H1 2015: HRK 81 million), operating expenses increased by HRK 110 million or 5.4% to HRK 2,133 million in H1 2016.

### **3.2.1 Material expenses**

Material expenses increased by HRK 136 million or 15.3% to HRK 1,023 million in H1 2016 as a result of higher merchandise, material and energy expenses and services expenses.

Merchandise costs increase was mainly driven by higher mobile merchandise and system solution merchandise that is in line with system solution revenue growth while fixed merchandise was lower compared to H1 2015.

Mobile merchandise cost increase was mainly driven by residential segment as a result of increased sales volume of smartphones, higher number of contract prolongations taking handsets and higher share of more valuable handsets additionally supported by growing convergent offers. Fixed merchandise decrease is a result of lower focus on fixed only services.

Increase of energy sales costs is in line with energy revenue growth.

Services expenses increase was driven by higher telecommunication costs and online costs.

Telecommunication cost increased mainly due to higher incoming non EU traffic towards domestic fixed and mobile operators while online costs increase was mainly related to increase of system solution standard portfolio following revenue development.

### **3.2.2 Employee benefits expenses**

Total employee benefits expenses decreased by HRK 34 million or 6.4% to HRK 503 million in H1 2016 as a result of lower redundancy costs and lower personnel costs due to lower number of employees and lower rights from collective agreement.

Number of FTE decreased from 4,719 in H1 2015 to 4,443 in H1 2016 mainly due Headcount Restructuring program partially compensated by new employments.

### **3.2.3 Other expenses**

Other expenses increased by HRK 15 million or 2.2% to HRK 688 million in H1 2016 mainly due to higher external employment costs, selling commissions and advertising expenses that were compensated by lower maintenance costs, ex-patriot costs and consulting fees.

Increase in external employment cost mainly came from additional engagement of agency technicians and agents in call center, as well as additional sales activities in residential segment.

Increase in selling commissions come from more transactions in indirect sales channel coming from door2door and telesales activities.

Advertising costs increased as a result of marketing campaign that supported Magenta1 launch.

Decrease in maintenance was a result of lower cost in network due to better conditions negotiated with vendors related SLA contracts and vouchers.

## **3.3 Write down of assets**

The assets write down decreased by 16 million or 39.8% to HRK 24 million in H1 2016 mainly due to lower value adjustment of receivables. This decrease was mainly driven by residential segment both in mobile and fixed part. Drop was partially offset with increase in business segment mostly due to lower collection of value adjusted receivables and higher new bad debt in retail part in 2016 and receivables value adjustment related to Metronet and Amis in wholesale part in H1 2016.

## **3.4 Depreciation and amortization**

Depreciation and amortization decreased by HRK 28 million or 3.9% to HRK 691 million in H1 2016 mainly due to lower amortization of software licences.

## **3.5 HT Group profitability**

### **EBITDA before exceptional items**

EBITDA before exceptional items increased by HRK 19 million or 1.4% to HRK 1,339 million in H1 2016. This increase was a result of higher revenue (HRK 98 million or 3.0%), driven by mobile revenues and system solutions, and other operating income (HRK 31 million or 81.0%), partially compensated by higher operating expenses (HRK 110 million or 5.4%).

Optima Telekom contribution to H1 2016 Group EBITDA was in line with H1 2015. It was amounted to HRK 49 million (H1 2015: HRK 49 million) and consisted of HRK 113 million of Optima Telekom third party contribution (H1 2015: HRK 111 million) and HRK 65 million of inter-company relations (H1 2015: HRK 62 million).

### **Net profit after non controlling interests**

In comparison to H1 2015, consolidated net profit after non controlling interests increased by HRK 11 million or 2.7% to HRK 417 million in H1 2016. Net profit after non controlling interests increased due to lower depreciation and amortization, higher EBITDA and lower exceptional items that were partially offset by higher financial expenses lower financial income, higher taxation and lower non controlling interests.

Negative contribution of financial expenses by HRK 38 million mainly due to net negative exchange rate differences coming from EUR exchange rate decline. Financial income decline of HRK 3 million is mainly driven by lower contribution from investment in joint ventures, partially offset by higher interest income and exchange rate gain.

Optima Telekom contributed to HT Group net profit by loss of HRK 1 million (H1 2015: loss of HRK 3 million).

## **3.6 Balance sheet**

Total value of assets decreased by HRK 403 million or 2.9% to HRK 13,676 million in comparison to end of year 2015. This is mainly caused by decrease within current financial assets and cash and cash equivalents resulted from dividend payment in May 2016.

Total issued capital and reserves decreased from HRK 11,641 million at 31 December 2015 to HRK 11,589 million at 30 June 2016. This is due to net profit for H1 2016 in the amount of HRK 417 million that is offset with dividend payment of HRK 491 million.

Total current liabilities decreased by HRK 362 million or 19.3% to HRK 1,520 million at 30 June 2016 mainly due to the settlement of higher payables for capital expenditures at 2015 year end.

## **3.7 Cash flow**

Cash flow from operating activities is HT Group's principal source of funds enabling the Company to finance capital investments and dividend distributions.

Net cash flow from operating activities increased by HRK 108 million or 13.1% to HRK 934 million mainly due improvements on working capital management and lower tax paid compared to H1 2015.

Net cash flow from investing activities decreased by HRK 857 million 242.2% to HRK -503 million mainly due to significant maturity of financial assets, mostly from time deposits and REPO arrangements in H1 2015 and higher capex paid and financial assets purchase in H1 2016 compared to H1 2015.

Net cash flow from financing activities increased by HRK 34 million or 4.9% to HRK -664 million mainly due to lower dividend paid in H1 2016.

### 3.8 Capital expenditure

in HRK million	Q2 2015	Q2 2016	<i>change</i>	Jan-Jun 2015	Jan-Jun 2016	<i>change</i>
<b>HT Group</b>	314	332	<i>5.5%</i>	587	645	<i>10.0%</i>
Capex / Revenue ratio	18.6%	19.2%	<i>0.5 p.p.</i>	17.8%	19.0%	<i>1.2 p.p.</i>

Capital expenditure realization is increased by HRK 59 million or 10.0% to HRK 645 million in H1 2016 in comparison to H1 2015 mostly due to investment resulted from integrated network strategy.

INS (Integrated Network Strategy) is focused on development of next generation fixed and mobile network. One of the main contribution in fixed network by the end of H1 2016 was enabled FTTx access for 226,972 households (increase of 28% compared to EOY 2015).

Coverage, capacity and performance are still increasing in mobile network with 4G network download throughput increased from 150 Mbit/s to 225 Mbit/s, in certain areas even to 262.5 Mbit/s and "Indoor" 4G population coverage increased from 65.2% at the beginning of 2016 to 67.4%.

Next TV, legacy TV platform replacement project with a unified converged platform, will increase service quality and expand MAXtv portfolio with additional functionalities. Platform has been installed and configured. Integration and software development for STB receivers is ongoing.

Changes on core and services platforms have been implemented in order to support requests within roaming regulation IV (EuRegIV).

Focus was on technology realization of 'digital company' business model and business transformation to ensure cost optimization.

HT continues with improvements of product and services security within cyber and data security area. PCI DSS certificate L1 received and certificate ISO 27001: 2013 for information security was renewed.

## 4. Overview of segment profitability

After financial consolidation of Optima Telekom into Group results as of Q3 2014, the Group's operating segments are Residential business unit, Business business unit, Network and support functions and Optima consolidated unit.

The Residential business unit (RBU) includes marketing, sales and customer care activities, focused on providing mobile, fixed line telecommunications and TV distribution services to residential customers.

The Business business unit (BBU) includes marketing, sales and customer care activities, focused on providing mobile and fixed line telecommunications, system integration services to corporate customers, small and medium business and public sector. In addition, BBU is responsible for wholesale business for both, fixed and mobile services.

The Network and support function (NSF) performs cross-segment management and support functions, including Technology department, Procurement, Accounting, Treasury, Legal and other central functions.

Companies in the HT's full ownership Iskon, Combis, KDS and E-tours are part of above mentioned segments, following the same structure as Mother Company.

Optima consolidated unit includes contribution of all Optima Telekom's functions to the HT Group financial results following the same reporting structure as used for other operating segments, except revenue details that are only reported in whole amount on Fixed revenue line. According to "Chinese wall" introduced by regulator, access to Optima Telekom figures is limited. So only financial consolidation is performed, while Optima Telekom non financial KPIs are not included into HT Group achievements.

In the financial reports, the HT Group's segments are reported on contribution to EBITDA before exceptional items level. The revenue and expenses of the segments include primary results.

Depreciation is not allocated to the segments, except the part related to Optima Telekom, as the majority is related to the fixed and mobile network, which is part of NSF.

### 4.1 Residential Segment

in HRK million	Q2 2015	Q2 2016	<i>change</i>	Jan-Jun 2015	Jan-Jun 2016	<i>change</i>
Mobile revenue	415	467	12.6%	825	911	10.4%
Fixed revenue	494	462	-6.5%	994	921	-7.3%
System solutions	0	0	-	0	0	-
Miscellaneous	8	10	31.4%	18	20	12.9%
<b>Total Revenue</b>	<b>917</b>	<b>939</b>	<b>2.5%</b>	<b>1,838</b>	<b>1,853</b>	<b>0.8%</b>
<b>Operating expenses</b>	<b>264</b>	<b>299</b>	<b>13.4%</b>	<b>545</b>	<b>589</b>	<b>8.1%</b>
<b>Contribution to EBITDA before EI</b>	<b>653</b>	<b>640</b>	<b>-2.0%</b>	<b>1,293</b>	<b>1,264</b>	<b>-2.2%</b>

## 4.2 Business Segment

in HRK million	Q2 2015	Q2 2016	<i>change</i>	Jan-Jun 2015	Jan-Jun 2016	<i>change</i>
Mobile revenue	229	229	-0.1%	441	439	-0.5%
Fixed revenue	278	268	-3.8%	541	532	-1.7%
System solutions	145	165	14.2%	258	330	27.9%
Miscellaneous	4	15	-	8	26	232.0%
<b>Total Revenue</b>	<b>656</b>	<b>677</b>	<b>3.1%</b>	<b>1,249</b>	<b>1,328</b>	<b>6.3%</b>
<b>Operating expenses</b>	<b>317</b>	<b>338</b>	<b>6.8%</b>	<b>613</b>	<b>685</b>	<b>11.7%</b>
<b>Contribution to EBITDA before EI</b>	<b>340</b>	<b>339</b>	<b>-0.3%</b>	<b>636</b>	<b>643</b>	<b>1.2%</b>

## 4.3 Network and support functions

in HRK million	Q2 2015	Q2 2016	<i>change</i>	Jan-Jun 2015	Jan-Jun 2016	<i>change</i>
Other operating income	16	27	65.8%	38	69	82.3%
Operating expenses <sup>1)</sup>	375	354	-5.6%	758	751	-0.9%
<b>Contribution to EBITDA before EI</b>	<b>-359</b>	<b>-327</b>	<b>8.9%</b>	<b>-720</b>	<b>-682</b>	<b>5.2%</b>

<sup>1)</sup> Operating expenses are restated for H1 2015 due to voluntary change of accounting policy related to Electronic Communication Infrastructure (ECI) costs at 2015 year end

## 4.4. Segment Optima Telekom consolidated\*

in HRK million	Q2 2015	Q2 2016	<i>change</i>	Jan-Jun 2015	Jan-Jun 2016	<i>change</i>
Fixed revenue	113	113	0.3%	218	221	1.7%
<b>Revenue</b>	<b>113</b>	<b>113</b>	<b>0.3%</b>	<b>218</b>	<b>221</b>	<b>1.7%</b>
Other operating income	0	0	-	1	1	15.1%
Operating expenses	54	54	-0.6%	108	109	1.3%
<b>Contribution to EBITDA before EI</b>	<b>58</b>	<b>60</b>	<b>2.1%</b>	<b>111</b>	<b>113</b>	<b>2.2%</b>

## 5. Hrvatski Telekom Inc. financial highlights

### Revenue

Revenue increased by HRK 57 million or 2.0% to HRK 2,877 million in H1 2016 when compared to H1 2015. Increase was driven by higher mobile revenue (HRK 86 million or 6.8%) coming from mobile data and handset revenues, system solution revenue (HRK 27 million or 42.5%) and miscellaneous revenue (HRK 20 million or 91.1%) coming from energy business. This increase was partially

compensated with decrease in fixed revenue (HRK 76 million or 5.2%) mostly resulting from lower voice and broadband revenues compensated by higher wholesale revenue.

#### **EBITDA before exceptional items**

EBITDA before exceptional items increased by HRK 10 million or 0.8% to HRK 1,226 million in H1 2016, mainly as a result of higher revenue (HRK 57 million or 2.0%) and higher other operating income (HRK 31 million or 89.7%) driven by sales of fixed assets and write down of commitments. This increase was partially compensated by higher operating expenses (HRK 78 million or 4.7%) driven mainly by higher merchandise costs related to growing system solution business and retention activities taken in mobile segment.

#### **Net profit**

Net profit increased by HRK 22 million or 5.8% to HRK 410 million in H1 2016. This increase was primarily a result of lower depreciation and amortization (HRK 24 million), lower personnel redundancy costs (HRK 17 million), higher financial income (HRK 15 million) and higher EBITDA before exceptional items (HRK 10 million), partially offset by higher financial expenses (HRK 38 million) mainly related to negative exchange rate differences and higher taxation (HRK 5 million).

## **6. Risk management**

Besides the business and regulatory developments detailed in this statement, and in audited financial statements for 2015 made public, there were no material changes to the Group's risk profile in the period under review.

## **7. Group 2016 outlook**

### **Revenue**

Following a lengthy period of severe recession, Croatia's 2015 GDP was up 1.6% and 2016 forecast shows similar trend, while high levels of unemployment still persist and adverse movements in both public debt and the budget deficit continue.

Telecommunication spending in both the residential and corporate sectors remains subdued, while the competitive environment and a stringent domestic and EU regulatory regime continue to exert pressure on the Group's business.

In light of the environment described above, with Optima Telekom now consolidated for the full 12 months of 2015 and 2016, alongside the contribution from growth areas within the Group, the Board expects 2016 revenue to decline slightly, within the range of 0% to -2%.

However, the Group now anticipates that system solutions will be broadly at 2015 levels, as some Government and public sector projects are expected to be deferred.

### EBITDA before exceptional items

The economic environment and revenue trends outlined above, along with further changes in the revenue structure, will impact EBITDA accordingly. However, the Group's continued focus on transformation initiatives will help maintain a high level of profitability, and consequently the Board expects an EBITDA margin in 2016 of around 40%.

### Investments

As previously announced, total Group investments for 2015 amounted to HRK 1,473 million, which represents a one-off increase of around 35% compared to 2014.

This was mainly due to the need for a significant strategic shift with respect to investment, aimed at both enhancing the Group's market position through the provision of high quality customer services whilst supporting the overall health and competitiveness of the Croatian economy.

In particular, the Group invested significantly in infrastructure in 2015, with an emphasis on fixed and mobile broadband, and, as previously discussed, achieved its year-end 2015 targets of household coverage by Next Generation Access (NGA) >30Mbps fixed broadband of around 50% and LTE (4G) indoor coverage of around 60% of the population.

In 2016, the Group plans to continue significant investment; these are now expected to be slightly lower than in 2015.

## 8. HT Group Financial statements

### 8.1 Consolidated Income Statement

in HRK million (IFRS)	Q2 2015	Q2 2016	<i>change</i>	Jan-Jun 2015	Jan-Jun 2016	<i>change</i>
Mobile revenue	644	696	8.1%	1,267	1,350	6.6%
Fixed revenue	885	843	-4.8%	1,753	1,675	-4.5%
System solutions	145	165	14.2%	258	330	27.9%
Miscellaneous	12	25	110.0%	26	46	80.2%
<b>Revenue</b>	<b>1,686</b>	<b>1,729</b>	<b>2.6%</b>	<b>3,304</b>	<b>3,402</b>	<b>3.0%</b>
Other operating income	16	28	70.1%	38	69	81.0%
<b>Total operating revenue</b>	<b>1,702</b>	<b>1,757</b>	<b>3.2%</b>	<b>3,343</b>	<b>3,472</b>	<b>3.9%</b>

<b>Operating expenses</b>	<b>1,018</b>	<b>1,048</b>	<b>3.0%</b>	<b>2,104</b>	<b>2,195</b>	<b>4.3%</b>
Material expenses	451	514	14.1%	887	1,023	15.3%
Merchandise, material and energy expenses	269	325	20.8%	530	658	24.1%
Services expenses	182	190	4.1%	357	366	2.4%
Employee benefits expenses	233	214	-8.2%	538	503	-6.4%
Other expenses <sup>1)</sup>	336	340	1.4%	673	688	2.2%
Work undertaken by the Group and capitalised	-21	-30	-45.4%	-34	-44	-28.9%
Write down of assets	19	10	-49.3%	40	24	-39.8%
<b>EBITDA</b>	<b>684</b>	<b>709</b>	<b>3.6%</b>	<b>1,239</b>	<b>1,277</b>	<b>3.1%</b>
Depreciation and amortization <sup>1)</sup>	357	342	-4.1%	719	691	-3.9%
<b>EBIT</b>	<b>328</b>	<b>367</b>	<b>12.0%</b>	<b>520</b>	<b>586</b>	<b>12.6%</b>
Financial income	5	11	120.4%	23	30	27.7%
Income/loss from investment in joint ventures	9	1	-90.1%	7	-2	-126.2%
Financial expenses <sup>1)</sup>	31	28	-8.2%	59	98	64.8%
<b>Profit before taxes</b>	<b>311</b>	<b>350</b>	<b>12.6%</b>	<b>491</b>	<b>516</b>	<b>5.1%</b>
Taxation	60	71	19.4%	98	105	7.7%
<b>Net profit</b>	<b>251</b>	<b>279</b>	<b>11.0%</b>	<b>394</b>	<b>411</b>	<b>4.5%</b>
Non controlling interest	-4	-3	35.8%	-12	-6	52.9%
<b>Net profit after non controlling interest</b>	<b>255</b>	<b>282</b>	<b>10.3%</b>	<b>406</b>	<b>417</b>	<b>2.7%</b>
Exceptional items <sup>2)</sup>	8	2	-70.4%	81	62	-23.8%
<b>EBITDA before exceptional items</b>	<b>692</b>	<b>711</b>	<b>2.8%</b>	<b>1,320</b>	<b>1,339</b>	<b>1.4%</b>

<sup>1)</sup> Other expenses, Depreciation and amortization, as well as Financial expenses are restated for H1 2015 due to voluntary change of accounting policy related to Electronic Communication Infrastructure (ECI) costs

<sup>2)</sup> Exceptional items refer to redundancy costs

## 8.2 Consolidated Balance Sheet

in HRK million (IFRS)	At 31 Dec 2015	At 30 Jun 2016	Change
Intangible assets	1,651	1,608	-2.6%
Property, plant and equipment	5,616	5,595	-0.4%
Non-current financial assets	1,033	1,061	2.7%
Receivables	98	103	5.0%
Deferred tax asset	46	56	21.9%
<b>Total non-current assets</b>	<b>8,444</b>	<b>8,422</b>	<b>-0.3%</b>
Inventories	104	120	15.1%
Receivables	1,215	1,309	7.7%
Current financial assets	869	727	-16.4%

Cash and cash equivalents	3,175	2,916	-8.2%
Prepayments and accrued income	272	182	-33.1%
<b>Total current assets</b>	<b>5,636</b>	<b>5,254</b>	<b>-6.8%</b>
<b>TOTAL ASSETS</b>	<b>14,079</b>	<b>13,676</b>	<b>-2.9%</b>
Subscribed share capital	9,823	9,823	0.0%
Reserves	445	492	10.6%
Revaluation reserves	4	39	-
Retained earnings	268	655	143.9%
Net profit for the period	925	417	-54.9%
Non controlling interest	177	163	-8.0%
<b>Total issued capital and reserves</b>	<b>11,641</b>	<b>11,589</b>	<b>-0.5%</b>
Provisions	68	57	-16.6%
Non-current liabilities	443	469	5.8%
Deferred tax liability	45	42	-6.0%
<b>Total non-current liabilities</b>	<b>556</b>	<b>568</b>	<b>2.1%</b>
Current liabilities	1,775	1,420	-20.0%
Deferred income	103	94	-8.2%
Provisions for redundancy	4	5	32.4%
<b>Total current liabilities</b>	<b>1,882</b>	<b>1,520</b>	<b>-19.3%</b>
<b>Total liabilities</b>	<b>2,438</b>	<b>2,088</b>	<b>-14.4%</b>
<b>TOTAL EQUITY AND LIABILITIES</b>	<b>14,079</b>	<b>13,676</b>	<b>-2.9%</b>

### 8.3 Consolidated Cash Flow Statement

in HRK million (IFRS)	Jan-Jun 2015	Jan-Jun 2016	change
Profit before tax	491	516	5.1%
Depreciation and amortization	719	691	-3.9%
Increase / (decrease) of current liabilities	-251	-128	49.0%
(Increase) / decrease of current receivables	47	-6	-113.4%
(Increase) / decrease of inventories	-7	-16	-112.7%
Other cash flow increases/ decreases	-173	-123	28.7%
<b>Net cash inflow/outflow from operating activities</b>	<b>826</b>	<b>934</b>	<b>13.1%</b>
Proceeds from sale of non-current assets	4	44	-
Proceeds from sale of non-current financial assets	1	1	-12.9%
Interest received	10	9	-6.3%
Dividend received	0	3	-
Other cash inflows from investing activities	1,521	991	-34.8%

<b>Total increase of cash flow from investing activities</b>	<b>1,535</b>	<b>1,048</b>	<b>-31.7%</b>
Purchase of non-current assets	-526	-696	-32.5%
Purchase of non-current financial assets	-75	-75	1.2%
Other cash outflows from investing activities	-580	-781	-34.5%
<b>Total decrease of cash flow from investing activities</b>	<b>-1,181</b>	<b>-1,551</b>	<b>-31.3%</b>
<b>Net cash inflow/outflow from investing activities</b>	<b>354</b>	<b>-503</b>	<b>-242.2%</b>
<b>Total increase of cash flow from financing activities</b>	<b>-</b>	<b>-</b>	<b>-</b>
Repayment of loans and bonds	-13	-14	-3.9%
Dividends paid	-573	-491	14.3%
Repayment of finance lease	-4	-4	-4.1%
Other cash outflows from financing activities	-108	-155	-43.4%
<b>Total decrease in cash flow from financing activities</b>	<b>-698</b>	<b>-664</b>	<b>4.9%</b>
<b>Net cash inflow/outflow from financing activities</b>	<b>-698</b>	<b>-664</b>	<b>4.9%</b>
<b>Exchange gains/losses on cash and cash equivalents</b>	<b>1</b>	<b>-26</b>	
Cash and cash equivalents at the beginning of period	2,192	3,175	44.8%
Net cash (outflow) / inflow	482	-259	-153.8%
<b>Cash and cash equivalents at the end of period</b>	<b>2,674</b>	<b>2,916</b>	<b>9.1%</b>

Note: H1 2015 Cash flow restated, changes were made on Net cash inflow/ outflow from operating activities and Net cash inflow/ outflow from financing activities due to voluntary change of accounting policy related to Electronic Communication Infrastructure (ECI) costs at 2015 year end

#### 8.4 Consolidated EBITDA reconciliation

in HRK million	Q2 2015	Q2 2016	change	Jan-Jun 2015	Jan-Jun 2016	change
<b>Segment Result (Contribution to EBITDA)</b>						
Residential Segment	653	640	-2.0%	1,293	1,264	-2.2%
Business Segment	340	339	-0.3%	636	643	1.2%
Network and Support Functions	-359	-327	8.9%	-720	-682	5.2%
Segment Optima consolidated	58	60	2.1%	111	113	2.2%
<b>Total Contribution to EBITDA before EI of the Segments</b>	<b>692</b>	<b>711</b>	<b>2.8%</b>	<b>1,320</b>	<b>1,339</b>	<b>1.4%</b>
Exceptional items	8	2	-70.4%	81	62	-23.8%
<b>Total EBITDA</b>	<b>684</b>	<b>709</b>	<b>3.6%</b>	<b>1,239</b>	<b>1,277</b>	<b>3.1%</b>

## **8.5 Notes to the condensed consolidated financial statements for the six months ended on 30 June 2016**

### **Basis of preparation**

The condensed consolidated financial statements as of 30 June 2016 and for the six months then ended, have been prepared using accounting policies consistent with International Financial Reporting Standards.

### **Significant Accounting Policies**

The consolidated financial statements have been prepared under the historical cost convention, except for investments available-for-sale stated at fair value.

The same accounting policies, presentation and methods of computation are followed in these condensed consolidated financial statements as were applied in the preparation of HT's consolidated financial statements for the year ended 31 December 2015.

### **Dividends**

On 21 April 2016 General Assembly of Hrvatski Telekom d.d. reached a decision on dividend distribution for 2015 in amount of HRK 491,307,624.00 (6.00 HRK per share).

Dividend was paid in May 2016.

A part of the net profit for 2015 amounting to HRK 47,000,000.00 was used to increase legal reserves.

### **Segment information**

After financial consolidation of Optima Telekom into Group results as of Q3 2014, the Group's operating segments are Residential business unit, Business business unit, Network and support functions and Optima consolidated unit.

The Residential business unit (RBU) includes marketing, sales and customer care activities, focused on providing mobile, fixed line telecommunications and TV distribution services to residential customers.

The Business business unit (BBU) includes marketing, sales and customer care activities, focused on providing mobile and fixed line telecommunications, system integration services to corporate customers, small and medium business and public sector. In addition, BBU is responsible for wholesale business for both, fixed and mobile services.

The Network and support function (NSF) performs cross-segment management and support functions, including Technology department, Procurement, Accounting, Treasury, Legal and other central functions.

Companies in the HT's full ownership Iskon, Combis, KDS and E-tours are part of above mentioned segments, following the same structure as Mother Company.

Optima consolidated unit includes contribution of all Optima Telekom's functions to the HT Group financial results following the same reporting structure as used for other operating segments, except revenue details that are only reported in whole amount on Fixed revenue line. According to "Chinese wall" introduced by regulator, access to Optima Telekom figures is limited.

In the financial reports, the HT Group's segments are reported on contribution to EBITDA before exceptional items level. The revenue and expenses of the segments include primary results.

Depreciation is not allocated to the segments, except the part related to Optima Telekom, as the majority is related to the fixed and mobile network, which is part of NSF.

Management of the Group does not monitor assets and liabilities by segments and therefore this information has not been disclosed.

The following tables present revenue and direct cost information regarding the Group's segments:

Period ended 30 June 2015	Residential HRK millions	Business HRK millions	Network & Support functions HRK millions	Optima Telekom consolidated HRK millions	Total HRK millions
Segment revenue	1,838	1,249	-	218	3,305
<i>Mobile revenue</i>	825	442	-	-	1,267
<i>Fixed revenue</i>	995	541	-	218	1,754
<i>System solution revenue</i>	-	258	-	-	258
<i>Miscellaneous revenue</i>	18	8	-	-	26
Usage related direct costs	(105)	(90)	-	(48)	(243)
Income and losses on accounts receivable	(22)	(12)	-	(3)	(37)
Contribution margin I	1,711	1,147	-	167	3,025
Non-usage related direct costs	(225)	(327)	-	(3)	(555)
Segment result	1,486	820	-	164	2,470
Other income	-	-	38	-	38
Other operating expenses, restated	(210)	(196)	(804)	(57)	(1,267)
Depreciation, amortisation and impairment of non-current assets, restated	-	-	(719)	-	(719)
Operating profit, restated	1,276	624	(1,485)	107	522
1 April 2015 to 30 June 2015	Residential HRK millions	Business HRK millions	Network & Support functions HRK millions	Optima Telekom consolidated HRK millions	Total HRK millions
Segment revenue	916	657	-	114	1,687
<i>Mobile revenue</i>	414	230	-	-	644
<i>Fixed revenue</i>	494	278	-	114	886
<i>System solution revenue</i>	-	145	-	-	145
<i>Miscellaneous revenue</i>	8	4	-	-	12
Usage related direct costs	(54)	(48)	-	(26)	(128)
Income and losses on accounts receivable	(9)	(7)	-	(1)	(17)

Contribution margin I	853	602	-	87	1,542
Non-usage related direct costs	(108)	(173)	-	(1)	(282)
Segment result	<u>745</u>	<u>429</u>	<u>-</u>	<u>86</u>	<u>1,260</u>
Other income	-	-	17	-	17
Other operating expenses, restated	(92)	(90)	(381)	(29)	(592)
Depreciation, amortisation and impairment of non-current assets, restated	-	-	(357)	-	(357)
Operating profit, restated	<u>653</u>	<u>339</u>	<u>(721)</u>	<u>57</u>	<u>328</u>

Period ended 30 June 2016	Residential HRK millions	Business HRK millions	Network & Support functions HRK millions	Optima Telekom consolidated HRK millions	Total HRK millions
Segment revenue	1,853	1,328	-	221	3,402
<i>Mobile revenue</i>	911	439	-	-	1,350
<i>Fixed revenue</i>	922	533	-	221	1,676
<i>System solution revenue</i>	-	330	-	-	330
<i>Miscellaneous revenue</i>	20	26	-	-	46
Usage related direct costs	(104)	(96)	-	(49)	(249)
Income and losses on accounts receivable	(1)	(19)	-	(2)	(22)
Contribution margin I	1,748	1,212	-	171	3,131
Non-usage related direct costs	(296)	(396)	-	(6)	(698)
Segment result	1,452	816	-	165	2,433
Other income	-	-	69	-	69
Other operating expenses	(202)	(185)	(785)	(53)	(1,225)
Depreciation, amortisation and impairment of non-current assets	-	-	(691)	-	(691)
Operating profit	1,250	631	(1,407)	112	586
1 April 2016 to 30 June 2016	Residential HRK millions	Business HRK millions	Network & Support functions HRK millions	Optima Telekom consolidated HRK millions	Total HRK millions
Segment revenue	939	677	-	113	1,729
<i>Mobile revenue</i>	467	229	-	-	696
<i>Fixed revenue</i>	462	268	-	113	843
<i>System solution revenue</i>	-	165	-	-	165
<i>Miscellaneous revenue</i>	10	15	-	-	25
Usage related direct costs	(53)	(51)	-	(25)	(129)
Income and losses on accounts receivable	2	(11)	-	-	(9)
Contribution margin I	888	615	-	88	1,591
Non-usage related direct costs	(155)	(193)	-	(3)	(351)
Segment result	733	422	-	85	1,240
Other income	-	-	28	-	28
Other operating expenses	(93)	(85)	(355)	(26)	(559)
Depreciation, amortisation and impairment of non-current assets	-	-	(342)	-	(342)
Operating profit,	640	337	(669)	59	367

## **Relations with the governing company and its affiliated companies**

In the first six months of 2016 there were no transactions among related parties with a significant impact on the financial position and operations of the Group in the given period.

In the first six months of 2016 there were no changes in transactions among related parties which were specified in the annual financial report for 2015 and which had a significant impact on the financial position and operations of the Group in the first six months of 2016.

Business relations transacted between HT d.d. and affiliated companies thereof (hereinafter referred to as: Group) in the first six months of 2016 and the governing company and affiliated companies thereof can be classified as follows:

### *Transactions with related companies*

Transactions with related companies primarily relate to the transactions with the companies owned by Deutsche Telekom AG (hereinafter referred to as: DTAG). The Group enters into transactions in the normal course of business on an arm's length basis. These transactions included the sending and receiving of international traffic to/from these companies.

In the first six months of 2016 the Group generated total revenue from related companies from international traffic to the amount of HRK 29 million (the first six months of 2015: HRK 34 million), while total costs of international traffic amounted to HRK 33 million (the first six months of 2015: HRK 31 million).

DTAG companies provided technical assistance to the Group in the amount of HRK 4 million in the first six months of 2016 (the first six months of 2015: HRK 6 million).

### *Compensation of the Supervisory Board*

The chairman of the Supervisory Board receives remuneration in the amount of 1.5 times of the average net salary of the employees of the Company paid in the preceding month. To the deputy chairman, remuneration is the amount of 1.25 times of the average net salary of the employees of the Company paid in the preceding month is paid, while any other member receives the amount of one average net salary of the employees of the Company paid in the preceding month. To a member of the Supervisory Board, who is in the same time the Chairman of the Audit Committee of the Supervisory Board, remuneration is the amount of 1.5 times of the average monthly net salary of the employees of the Company paid in the preceding month. To a member of the Supervisory Board, who is in the same time a Member of the Audit Committee of the Supervisory Board, remuneration is the amount of 1.25 times of the average monthly net salary of the employees of the Company paid in the preceding month. To a member of the Supervisory Board, who is in the same time a Member of the Compensation and Nomination Committee of the Supervisory Board, remuneration is the amount of 1.25 times of the average monthly net salary of the employees of the Company paid in the preceding month. DT AG representatives do not receive any remuneration for the membership in the Supervisory Board due to a respective policy of DT AG.

In the first six months of 2016 the Company paid a total amount of HRK 0.4 million (the first six months of 2015: HRK 0.4 million) to the Members of its Supervisory Board. No loans were granted to the Members of the Supervisory Board.

*Compensation to key management personnel*

In the first six months of 2016 the total compensation paid to key management personnel of the Group amounted to HRK 23 million (first six months of 2015: HRK 21 million). Compensation paid to key management personnel relates to short-term employee benefits. Key management personnel include members of the Management Boards of the Company and its subsidiaries and the operating directors of the Company, who are employed by the Group.

## **9. Statement of the Management Board of Hrvatski Telekom d.d**

To the best of our knowledge, unaudited financial statements of the company Hrvatski Telekom d.d. (hereinafter: "Company") and unaudited consolidated financial statements of the Company and affiliated companies thereof (hereinafter: "Group"), which are prepared in accordance with International Financial Reporting Standards (IFRS), give a true and fair view of assets and obligations, profit and loss, financial position, and operations of both the Company and the Group.

The management report for the first six months of 2016 contains a true presentation of development and results of operations and position of the Group, with description of significant risks and uncertainties for the Group as a whole.

Mr. Davor Tomašković, President of the Management Board (CEO)

Mr. Josef Thürriegl, Member of the Management Board and Chief Financial Officer

Ms. Nataša Rapaić, Member of the Management Board and Chief Operating Officer Residential

Mr. Saša Kramar, Member of the Management Board and Chief Operating Officer Business

Mr. Boris Batelić, Member of the Management Board and Chief Customer Experience Officer

Ms. Marija Felkel, Member of the Management Board and Chief Human Resources Officer

Zagreb, 28 July 2016

## 10. Presentation of information

Unless the context otherwise requires, references in this publication to “HT Group” or “the Group” or “HT” are to the Company Hrvatski Telekom d.d., together with its subsidiaries.

References to “HT” or the “Company” are to the Company Hrvatski Telekom d.d. Following the merger of T-Mobile d.o.o. with Hrvatski Telekom (HT d.d.), effective 1 January 2010, the Group is now organized into two business units: Business and Residential.

Therefore, references to “Business” are to business operations performed within the Company’s Business Segment.

References to “Residential” are to business operations performed within the Company’s Residential Segment.

References to “Iskon” are to the Company’s wholly-owned subsidiary, Iskon Internet d.d.

References to “Combis” are to the Company’s wholly-owned subsidiary, Combis d.o.o.

References to “KDS” are to the Company’s wholly-owned subsidiary, KDS d.o.o.

References to “E-tours” are to the Company’s wholly-owned subsidiary, E-tours d.o.o.

References to “Optima” are to Optima Telekom, the company fully consolidated into the Group’s financial statements as of 1 July 2014.

References in this publication to “Agency” are to the Croatian National Regulatory Authority, the Agency for Post and Electronic Communications.

## 11. Disclaimer

This release contains certain forward-looking statements with respect to the financial condition, results of operations and business of the Group. These forward-looking statements represent the Company's expectations or beliefs concerning future events and involve known and unknown risks and uncertainties that could cause actual results, performance or events to differ materially from those expressed or implied in such statements. Additional information concerning important factors that could cause actual results to differ materially is available in the Group's reports which may be found at [www.t.ht.hr](http://www.t.ht.hr)