

The Q1 2011 results conference call
28 April 2011 at 15:00 CET

Presenters

Dino Dogan

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Operator

Thank you for standing by and welcome to the T-HT Q1 Results call. At this time all participants are in a listen-only mode. There will be a presentation followed by a question and answer session at which time if you wish to ask a question you will need to press *1 on your telephone. I must advise you this conference is being recorded today, Thursday 28th April 2011. I would now like to hand over to your first speaker today, Ms Erika Kaspar. Please go ahead.

Erika Kaspar

Ladies and gentlemen, good afternoon and welcome from Zagreb. Today our Controlling Director, Irena Sekirica, is here with me and of course our IR team, Elvis and Anita. Our new CFO, Mr Dino Dogan, will join us over the phone from abroad. He will talk you through the highlights of our business and financial performance for the first quarter of this year, using the 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 Investors page. After the presentation, Mr Dogan will also be available for your questions.

Before we begin, allow me to draw your attention to the harbour statement on page 2 of our presentation. Now allow me to introduce you to Dino Dogan, to outline our Company's performance in the first quarter of 2011.

Dino Dogan

Thank you, Erika, and good afternoon to everybody wherever you are. So, let's start with slide 3, and what you can see there is that things haven't really picked up since we last reported in

February, which means that we are still confronted with a challenging macro-economic environment. The latest figures show that GDP fell by 1.2% in 2010 and, although that is an improvement on previous estimates, it's still taking some time to recover which is obviously affecting us.

The inflation rate is at 2.6% and that's the highest since May 2009, and this morning I also picked up, just for comparison reasons, the current inflation rate in Germany which is 2.4%. The unemployment in Croatia is still rising. It was at 19.3% at the end of March and worsening insolvency caused that one third of the active companies currently is insolvent. As I already said, we are facing several challenges and the recovery is taking longer than we hoped, so everybody is spending less and that is why our revenues are down in this quarter.

I'll now kindly ask you to switch to page 4, the Croatian Telecom Market. You can see that the competitive landscape is pretty much the same, although I would draw your attention to the fact that as of January 1st 2011 we have had lower fixed and mobile interconnection rates, which dropped by 29.3%, and from March the rates for ULL were reduced as well by some 16.4%. There were some other changes imposed by the Regulator in January too, which are related to the Reference Unbundling Offer, and earlier this month the Agency finalised its analyses on the retail market. You can read about it in more detail in the Results Statement we issued this morning.

Overall, you can see that Broadband and PayTV are still significant opportunities for us. As you will see later, they remain good drivers of revenue growth at the moment and, just to give you an indication, the Broadband connection: 55% of households in the EU have a broadband connection and you will see later on the figures in Croatia that there is still market potential to grow for us. We are also seeing continued growth in mobile data and that's being driven by smartphone growth and mobile broadband, either on tablets like the iPad, or on laptops.

So, if we now move to the Group highlights on slide 5, this shows that our revenue has fallen by 2.5% and, as before, we are still being affected by the recession and the special taxes imposed by the Government, so in this quarter the special 6% tax cost us around about HRK 34 million. Like this time last year, we had a HRK 68 million contribution from Combis in the ICT domain, so if you strip that out of the actual fall in revenue it would have been about 6%. So, it is clear that the recession is still impacting the Group's performance.

EBITDA was down by 6.4% and that has mostly to do with higher costs associated with very strong promotional campaigns we did in the mobile segment, but also with the higher copyright

fees payable as the Group's IPTV subscriber base expands. The EBITDA margin slipped a couple of percentage points to 40.5% and obviously this remains the focus for our cost-cutting measures so we can maintain a decent margin.

Looking at capex, capex has increased quite sharply and that is mostly to do with us picking up some internal projects that we had postponed following the reorganisation in the Group last year, plus the fact that we changed the accounting treatment of consumer equipment so it's now part of capital expenditure. We still don't have any clarity on the fibre situation from the Regulator, so this capex increase has nothing to do with starting fibre investments again.

Finally, we reorganised the Group into Residential and Business segments and it is their performance we'll be taking you through today. This split reflects indeed our governance model, too. To have a more inside view on our revenue development on page 6, we see the development of revenues and, as before, we are losing revenue from fixed telephony at a fairly predictable rate, and again we've lost some ground on mobile revenues for the reasons I have already mentioned. Data and wholesale are also down but, as you can see, our Internet business continues to do well, and that increased revenues 9% or HRK 29 million, and also you can see the contribution that Combis has made. We are pleased with the progress it has been making since we acquired it last year.

Let's have a more traditional look into fixed and mobile telephony as we and you are used to it so, turning to slide 7, this shows you how the mobile side of the business has performed across both the residential and business segments. You can see that we have increased our market share by 0.5% and in fact our subscriber numbers have gone up again by 7.4% to just over 3 million and this is because we have put a lot of effort into marketing, particularly in the first quarter where we gained about 100,000 new users. You can see, we have achieved good gains in both postpaid and prepaid numbers, too. Obviously the prepaid has been helped because we launched Bonbon, our second brand, in October.

When you look at residential mobile, this increased by 7.9% to just under 2.6 million accounts, and that's actually up 4.2% at the end of 2010, because of the promotional work we did in the first quarter of this year, particularly in relation to mobile broadband. What we also see is a lot of promotional work in the mobile for business customers at the same time, and in the business segment we have increased mobile numbers by 4.5% to currently 437,000, if compared with the first quarter of 2010 business. MOU, minutes of usage, per average subscriber fell slightly, while the blended ARPU fell by 12%, and this is down due to lower use but mostly because of the

pricing pressure we are under. As we saw in the previous slide, mobile revenues were down by 8.7% across the Group, which equals HRK 72 million.

Let's have a look at the situation in fixed telephony; slide 8 over the page shows us the performance of fixed telephony right across the Group and you can see a strong story that's pretty consistent with previous quarters in which the number of main lines is decreasing in line with global trends, which means fixed-to-mobile substitution for the fixed lines, so we are developing a lot of effort trying to reduce this by ensuring our services remain the best and the most keenly priced we can offer. As you can see, the ARPA is down 8.3% and total minutes down 10.6%. If we consider the residential segment of fixed telephony, we had about 1.2 million fixed lines, so that's the majority of the fixed line business in the Group, while the business segment has about 215,000 mainlines. If you recall, back on slide 6, fixed line revenues fell by HRK 64 million across the Group.

On page 9 the IP services – we have a new slide on the IP services and, again, this gives you a picture of what's happening right across the Group. What we see is that we are continuing to see strong growth in subscriber numbers and revenues from Internet services and overall we have increased ADSL mainlines by about 12% to 642,000 and of these 535,000 are residential broadband lines, which is about 83% of total broadband.

IPTV, both from MAXtv and Iskon's own service, contributes to be a big success story for us. You can see that IPTV numbers have increased by more than 23% since last year, so we now have 317,000 subscribers and that's up from less than 300,000 at the beginning of the year. In part this has been helped by the launch of MAXtv on satellite at the end of 2010. It turns out that MAXtv and Iskon's launch is one of the most successful IPTV launches worldwide. Of these, most are residential subscribers and we are continuing to provide them with new channel packages and new features in the product, like the ability to go onto our t-portal website and activate private media recording from the internet so they don't miss any programmes.

Clearly, what the growth of MAXtv is telling us is that we are having a lot of success selling it on to our ADSL subscriber base because we have 535,000 residential ADSL lines, and 300,000 of these homes are also taking our IPTV services, which is an attach rate of more than 55%. It is also telling us that, while people are making fewer voice calls and spending less on voice, what they are willing to increase is obviously broadband and television, so you can see how important these services are to our customer base and obviously to us as well. So, I think what is exciting about this is the fact that, while mobile and fixed telephony are pretty well penetrated across Croatia, broadband penetration is still less than 50%, which means we still have a big market to

go for in terms of getting ADSL lines connected and then selling the IPTV service once we are in. I already mentioned the reference level of EU with the 55% penetration.

Let's have a new look, let's say, into our business; slide 10, Residential, we are showing for the first time how the revenues are broken down in this segment. Because of the recession, residential revenue fell by about 5% and that was pretty much all voice revenues that were being lost, about HRK 92 million. Within Residential the revenue from mobile voice services were down 18.3% to HRK 265 million, which is a result of lower average revenue per usage and consistently downturn trend of prices, while the revenue from fixed voice service fell due to the continued fixed-to-mobile substitution already mentioned.

The decrease of voice revenue is being offset to some degree by gains in non-voice revenue and these increased by 5% from HRK 342 million to HRK 360 million. We also had some gains in what we term as 'other services' and this was due to changes in the mobile tariff structure. Revenue from terminal equipment went up by 14% to HRK 50 million, as a result of the already mentioned promotional campaigns we did in the mobile segment. On the EBITDA side you can see that was down 8.5%, to just under HRK 660 million and that fall is down primarily to the fall in revenue, as we have discussed before, affected by the increased merchandise costs, too.

The other new inside view into our business is the Business segment so, turning now to slide 11, this shows the business segment in more detail. Here you'll see that revenue actually went up by 1% to last year, to HRK 824 million, and this is obviously because we have added Combis since then, although EBITDA was down by 6.4% mostly because we've had higher cost of merchandise, associated with the mobile promotions we did for Business, and we've got some additional merchandising cost from Combis.

You can see that voice revenues were down about 10%, mainly for the reasons we have outlined, but in fact we have been quite successful in increasing the mobile base in the business segment, as we mentioned before. All the usual factors are there, including the decline of fixed revenue and the fall in termination rates. Non-voice revenues fell by 6% and that's largely wholesale and data, while Combis accounts for the large increase in the other revenues domain. One interesting fact to note is that we have about 18,000 IPTV subscribers in the business segment, which includes all sorts of business users and of course hotels, and we launched our hotel service last year.

Let me summarise, page 12; looking over the page at the financials in a bit more detail – we have already covered revenue and EBITDA – we can see that net profit fell by 8.5% to HRK 351

million, which is a result of the EBITDA development. Our net cash from operations was down 13% to HRK 471 million, driven by the lower EBITDA and partly because of higher investments in the mobile merchandise. Capex has risen, for the reasons we have already discussed, and you will see that the headcount is higher because of the integration of Combis into our result.

Let me continue and come to the last slide for today's presentation, which is the outlook for the entire year 2011. As I already mentioned, the recovery of the Croatian economy is progressing slower than anticipated, with the unfavourable development of some key indicators as high unemployment and falling disposable income, which is definitely impacting our Group's services. Subject to a strong tourist season in Croatia and recovery in the national economy, we expect to maintain our 2011 revenues at the 2010 level, by focusing on exploiting new growth opportunities and also maximising existing ones.

If we talk about EBITDA before exceptional items, based on the revenue strategies we have outlined above, the efficiencies that we have gained and we will continue to exploit from the success of restructuring in 2010, definitely continuing strong cost control, we expect – this is definitely subject to recovery in the national economy which is a major prerequisite – that the 2011 EBITDA for the year as a whole should be above the 2010 level.

Regarding capex, one thing we really have to emphasize is, while the current regulatory regime remains a disincentive to T-HT's potential investment in fibre infrastructure, we expect 2011 capital expenditure to be lower than 2010. Nevertheless, we will continue to invest in our fixed core network transformation and service platform development, and as well into the infrastructure which is necessary to support the growing demand for mobile broadband.

Last, but not least, looking into the region and potential expansion, our Group continues to monitor and evaluate expansion opportunities to increase shareholder value. Ladies and gentlemen, that's all from my side for the time-being.
