

The Q2 2011 results conference call
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Presenters

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Operator

Thank you for standing by and welcome to the T-HT Results conference call. At this time all participants are in a listen-only mode. There will be a presentation followed by a question and answer session at which time if you wish to ask a question you will need to press *1 on your telephone. I must advise you that this conference is being recorded today, Friday 29th July 2011. I would now like to hand the conference over to your first speaker today, Erika Kaspar. Please go ahead.

Erika Kaspar

Ladies and gentlemen, good afternoon and welcome from Zagreb. Our CEO, Mr Ivica Mudrinić, is here in Zagreb with us and our CFO, Mr Dino Dogan will join us over the phone. Our CEO and CFO will talk you through the highlights of our business and financial performance for the first half of this year using the presentation slides, which I hope you have in front of you. If not, please visit our website, which is www.t.ht.hr where you can access the slides from our investors' page. After the presentation Mr Mudrinić and Mr. Dogan will also be available for your questions.

Before we begin, allow me to draw your attention to the harbour statements on page 2 of our presentation. Now allow me to introduce you to Ivica Mudrinić, our CEO, to outline our company's performance in the first half of this year.

Ivica Mudrinić

Thank you, Erika. Good afternoon to all of you on the line. Both, Mr Dogan, our CFO, and I will take you through the key highlights. I would like to lead off with a few words related to the overall economic environment in Croatia. We had earlier anticipated and the key reference points in Croatia were giving an indication that we should expect a growth of the GDP starting some time in Q2 or even earlier. This has not materialised, so the anticipated expected GDP growth did not materialise unfortunately. There is some expectation that it will happen now in Q3 following a rather successful or expected successful tourism season in Croatia. The economic issues in Croatia are complex and I would not dwell on them.

I think we are merely referring to the point that the expectations that we had earlier this year did not materialise. We are currently roughly 7 or so per cent below the 2008 GDP levels. The inflation rate has slowed, it's at 2%. The registered unemployment rate is at 16.9% in June of this year compared to a 16.6% in June of 2010. This further confirms that the economy has not recovered and that we are still suffering as a result of this recession.

In addition, the overdue payments are at a record level of roughly HRK 39.9 billion, which means that we have significant solvency issues in the business segment, so the unemployment rate is in a sense linked to our residential segment of our business and the overdue payments and arrears that have accumulated are linked to the business segment directly. There are graphs on page 3 which you can refer to and maybe if you have got a question I would be happy to answer related to the economic development.

On the telecoms sector itself we have a quick overview. What's most important to note is we have in the fixed telephony 21 licence operators out of which 10 are active. We have the introduction in July of this year of this wholesale line rental and naked bitstream. Liberalisation has been in place since 2005; local loop unbundling since 2006. I would say that what we are seeing in fixed telephony in general is similar to the global trends.

On the mobile telephony we have three operators, no MVNOs. The penetration rate based on the current census on the population in Croatia is set at 151% or 151 SIMs per 100 population. We're seeing a growing demand for mobile data, driven by smartphones and mobile broadband. This segment continues to grow.

Internet penetration is at about 64% of population and the broadband household penetration at about 45%. Here we see a significant growth opportunity. This is also confirmed by the result which you'll see later on in this presentation.

PayTV, satellite and cable TV are underdeveloped. The cable TV household penetration is at about 12% of households and TV broadband using the cable infrastructure is at 4%. MAXtv, our IPTV platform, is the most successful payTV in the market. We are by far a leader in this segment and as far as IPTV launches on a world-wide scale are concerned we are one of the top 3 in the ranking.

The regulatory framework as far as the telecoms market is concerned we saw amendments to the Law on Electronic Communication. It is a further alignment with the EU. It took place in 2009 and maybe a note, Croatia – for those that are not following the country very closely - a few weeks back Croatia completed a negotiations process for accession to the European Union. The actual accession is expected mid-year 2013, so two years from now. In addition to the regulatory framework, HAKOM decision on the automatic migration of carrier pre-select customers to the wholesale line rental is impacting our business. We also have a ban on us. It's actually an inability for HT to charge the activation costs of this wholesale line rental. This is changing the relationship between us and the alternative operators. I think we'll touch on that a little bit later. We're also facing a mandatory prepaid

registration, but it has been postponed from the earlier timeline, so now we have, let's say, a reprieve on this segment.

On page 5 we have the Group highlights. We have maintained a leading market position in all of the business segments. The revenue decreased 4% to 3.883 billion due to the continuing recession. As I mentioned before, in addition we see a strong competitive pressure and of course we continue to carry the impact of the 6% mobile telephony and messaging tax, which is a top line taxation introduced two years ago. The EBITDA is down 3.1% to 1.668 billion with the margin increased to 43%. Capex increased period-to-period 73% to HRK 499 million. We paid a dividend in May of this year, HRK 22.76 per share. We launched the ICT services: tCloud, first cloud-based service in Croatia. We also launched an eBook store called Planet9. Further participation in the privatisation process in Post and Telecommunications of Kosovo is under review currently. I think we can maybe touch on that later under the outlook section.

On page 6 we have a revenue development showing both a breakdown between fixed telephony, wholesale, data, miscellaneous, mobile, IP and ICT and here you can see segment by segment how we performed. We saw a 4% decline period-to-period comparison 2010 versus 2011. What we see here is that fixed telephony is down 11.7%, mobile 9.9, wholesale 7.1. IP is up 9%; ICT grew significantly, but in absolute terms it's not huge, 200% is not huge in absolute terms; and data and miscellaneous down by 12.5%.

In summary, so far as revenue is concerned, we are still significantly impacted by the recession and the fact that we did not recover from the significant decline. Again, as a reminder, Croatia dropped in absolute terms by 5.8% in 2009, a further 1.5, 1.6% in 2010 giving a total decline which we still have today of roughly 7% in comparison to the 2008 figures. We saw internet revenues continues to grow. You can see this, as I mentioned, a minute ago, in the IP and also ICT segment. Combis, which is a company we bought and consolidated in May of last year, they contributed significantly both to revenue and EBITDA as well.

On slide 7 we have an overview of the mobile telephony. You can see that the market share by subscribers is being maintained and what we see in absolute terms, a growth both in prepaid and post paid. The blended ARPU is down, mostly caused by the recession and the new tariff bundles that are being opted for. The minutes of use are slightly up, but in a totally changing environment, the total blended ARPU is down 14.2% to HRK 75 in this period.

On fixed telephony on slide 8, the number of main lines is down due to the migration to some of our competitors under the ULL model. The total traffic is down 11.4% as you see in the upper right. ARPU is down 8.7% to HRK 120 and the number of ULLs is up by 12.1% to a total of 141,000. The IP services, the number of ADSL mainlines that we have is up by 10%. The ADSL mainline ARPU is down 5.9%, so here we are seeing the impact of both promotions and the increase in the number of households connected. The number of IPTV customers grew significantly by 22.7% and this puts us, as I said before, into the category of one of the leading providers of IPTV services on a global scale.

Now I would like to turn the floor to Dino Dogan, our CFO, for the segment overview.

Dino Dogan

Ladies and gentlemen, good afternoon from my side as well. Let's move on to page 10 where we show you the first half year residential results. You can see how we have recognised our revenues accordingly. The continuing recession meant that the residential revenues fell about 6% and that was largely due to a fall in voice revenue of about HRK 203 million, which means they are down almost 14%. Within the residential segment, revenues from the mobile voice services were down roughly 19% as a result of lower average revenue per usage and consistently downwards trend of prices while the revenues from fixed voice services fell due to continued fixed to mobile substitution. that is also a phenomenon visible on the Croatian telecommunication market. Nevertheless, the fall in the voice revenue is being offset to some degree by gains in the non-voice revenues. These rose by 5.6% up to HRK 730 million coming from previously HRK 691 million. We also had some gains in what we term as other services and this was due to changes in the mobile tariff structures that we have performed. The revenues from terminal equipment went down by 11% to HRK 82 million, which is the result of different tariff structures in the mobile segment. On the Contribution to EBITDA you can see that this was down by some 2.2% just to under HRK 1.429 million and that is primarily due to lower revenue.

Let's have a look on the business segment on page 11, which shows the business segment in more detail. Here you can see that the revenue fell by 1.3% on last year to HRK 1.714 million, although the fall was offset to some degree by revenues from the acquisition of Combis that we already mentioned. You can see that the voice revenues were down about 11.5% mainly for the reasons we have outlined, namely the recession in the macroeconomic environment, but also, let's say, the competition and the corresponding price declines, but we have increased the mobile base in the business segment on the other hand as well.

We are seeing all the usual factors, as I mentioned, including decline of fixed revenues and the fall in termination rates. Non-voice revenues fell by 5.7% and that's largely in wholesale and data, while Combis accounts for the large increase in the category of other revenues. The contribution to EBITDA in the business segment was down by 11.3% largely due to higher cost of merchandise which are associated with the mobile promotions in the earlier part of the year. We named that one "front loading" and on the other hand we had some merchandise costs from Combis as well as a contribution of Combis' indirect costs. Our IPTV subscribers in the business segment have grown by 23% to around 18,000 over the previous year and we also launched our Hotel TV service in March this year.

Let's move to page 12, the Group highlights from a financial perspective and looking over the page at the financials in a bit more detail. We have already covered, I think, the revenues and the EBITDA part, so we can see that the net profit rose slightly to HRK 828 million due to lower EBITDA, being more than offset by the absence of the last year HT Mostar related charge; moreover, higher financial income and a lower taxation. Our net cash from operations was down by 12.5% at HRK 979 million and this is a result of lower profitability which we have already mentioned and higher redundancy payments. Our

capex has risen for the reasons we have already discussed and you will see that the headcount is down by 2.3% as we continue to keep a tight rein on our costs.

That would be all from my side and may I now hand over back to our CEO.

Ivica Mudrinić

In the outlook at the end of this presentation on page 13, what we have stated is that the Group's revenues are going to be influenced by the strength of the tourism season in Croatia and the recovery of the national economy. The economic turnaround that has been predicted earlier this year has not materialised, while the unemployment remains high and the amount of overdue payments also at record levels. We therefore and in addition having in mind that the Government's 6% tax on mobile services originally imposed two years ago, has not been removed, and in addition to that the regulations governing wholesale line rental and naked DSL, all of this will impact the Group's business and our total revenues. Therefore we continue to be focused on exploiting new revenue opportunities and maximising existing ones. However, given this tough economic environment and accelerated regulatory pressure on the Group, we expect the revenues to be moderately lower than the 2010 level.

EBITDA; in light of the continued challenging economic environment, the regulatory impact, and as I stated earlier the lower expected revenues, we no longer expect 2011 EBITDA to be above the 2010 level. However, we, the Group are committed to maintaining the year-on-year EBITDA margin through efficiencies gained so far in continued strong cost control.

On the capex side, while the regulatory regime remains a disincentive as it is today to our potential investment in fibre infrastructure, we expect the capital expenditure to be lower than the 2010 level. However, we will continue to invest in the fixed core network transformation and service platform development, as well as to ensure that we have and we can maintain the demand for mobile broadband at a sufficiently high level.

On the regional expansion, we will continue to monitor and evaluate expansion opportunities to as always increase shareholder value.