The first nine months 2009 results conference call
30 October 2009 at 15:00 CET

Presenters

- Erika Kašpar
- Ivica Mudrinić
- Juergen Czapran

Operator: Thank you for standing by and welcome to the THT Q3 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 this conference is being recorded today, Friday, 30th October 2009. I would now like to hand over to your speaker today, Ms Erika Kaspar. Please go ahead.

Erika Kašpar: Thank you. Ladies and gentlemen, good afternoon and welcome from Zagreb where our CEO Mr Ivica Mudrinić and our CFO Mr Juergen Czapran will talk us through the highlights of our business and financial performance for the first nine months of this year using the presentation slides, which I hope you have in front of you. If you, please visit our website which is t.ht.hr where you can access the slides from our investor page. Before we begin, allow me to draw your attention to the harbour statements on page two of our presentation. And allow me now to introduce you to Mr Ivica Mudrinić our CEO to outline our company's performance this year.

Ivica Mudrinić: Thank you very much, Erika. Good afternoon to all of you on the line. It is nice to be here today. What I would like to do then is to take you through the slides, page by page. It will make things easier. The beginning here is the business environment and the economic outlook including the regulations. What we have seen as part of the global down turn is a drop or contraction in GDP in Croatia by roughly 6% in quarter two 2009. One other parameter that we have used as an indication of the household spending is the consumption expenditure of households has dropped by 9% in Q2 of this year.

We have also seen at the beginning of August this year, the government has introduced the new personal income tax. It is an additional levy, tax on the net income. They have also increased at the same time the VAT up from 22 to 23% and they have introduced a new tax on mobile communication services amounting to 6% of the telephony and messaging on the top line. The banking system however has remained stable and healthy and in addition the monetary situation, the exchange rate has been stable. You could argue that although the fiscal moves the additional taxation has been quite a burden, it has insured overall stability and so we have not seen probably the worst of two evils which means that we have avoided here in the country a monetary instability or a devaluation which we saw in many of the central European economies.

When you consider the regulatory aspects then one should highlight that in July 2009 market analysis based on the EU recommendations have been finalised and certain remedies were introduced. In addition we are obliged to give access to our competitors to other competing operators access to the optical network infrastructure, meaning access to the customer. We have also seen additional decreases of fixed and mobile interconnection charges from January 1st 2010, meaning the termination rates.

Turning to group highlights on page four, one could again hear what is most important is that we have of course maintained leadership in all of the segments of business that we operate in. Our performance is resilient despite the recession. Broadband and broadband related services like IP TV are growing quite well. You will see the data later. The mobile subscriber base has also increased. The balance sheet and cash reserves remain strong and we are well positioned for future growth. We continue to invest in the infrastructure. We have yesterday signed an agreement, a merger agreement between T-Mobile and HT inc, enabling a move to reintegrate the mobile part of the business into the company.

The reason for this—and this is in my opinion a very key enabler for future development: we believe that the era of technology based segregation is over and we believe that it is the right time for the telecom sector to move into what we are calling customer facing units. And the future organisation has foreseen chief operating officers for residential and business segments respectively. And not the traditional technology based access as definition, meaning T-Mobile and T-Com as we have had up to now. This should enable us to do a much better job in servicing the customer. This is of course coupled with the recent deployment of access and the realignment of the core networks, meaning that in the future we would have a single production facility that could be network managed which should give us a higher quality, more services and a lower cost base. So this is an important fact.

We chose this time to make this move because we believe that in this time of economic downturn, in times of pressure that you can in fact do these kinds of measures and that you, through this process, prepare the company for what is inevitably going to be an upturn in the next one to two years. And we have planned to complete this process during the course of 2010. The formal merger will take place on January 1st, but the process alignment and the optimisation will take place during the course of 2010.

I am sure if there are any questions I can elaborate on this later on, but on this same page on the group highlights, we have an indication of the flash results. Meaning that the revenue here you will see has dropped three quarters versus three quarters last year, 1.7%. So although we are seeing a significant drop or contraction in GDP, we have a slight downturn in revenue. We have also a drop in EBITDA, about 4.4%. Net profit is down 7.5% and the headcount is down 3.6%. Again we will hear a little more on the financials from Juergen Czapran our CFO and my colleague from the board.

But again, on the next page to take you briefly through the revenue development and the revenue breakdown and what we have prepared here is the January through September '08 and January through September '09 giving you an indication of where you are seeing a drop in revenue and where the increase is taking place. So for example on the right half of the slide, you will see there is a 9.9% drop in fixed telephony, traditional fixed telephony. A drop in the mobile services as well. Wholesale has dropped, however, internet services—meaning broadband and IPTV—are up significantly. And data and miscellaneous is up, giving a total net as I mentioned before of 1.7% below last year's result.

On the next page we move to the T-Com or fixed line business, including the internet services broadband and alike. We are the market leader in all of the services that we provide here. We have seen a significant growth in the broadband services, growth of course in IPTV as well and you will see the actual data in a minute. The EBITDA is down due to decreased revenue from fixed telephony, data and wholesale and an increase in merchandise and other expenses. The merchandise that we refer to here is IPTV and broadband or ADSL equipment. We also have pushed investments in network access, aggregation and core development. Again investment today prepares the company for the future upswing that we do expect in the next one to two years.

Key financials on the T-Com segment, the revenue is down 2.4%, EBITDA is down 6.8% and EBITDA margins before exceptional items are 1.9 percentage points down at 40%. CAPEX is up, meaning that we are better managing the distribution of CAPEX through the year and we are more aggressive in laying out this new platform. CAPEX to revenue ratio for the segment is 19.1% and the headcount at 5,169. The revenue by business segment is also indicated on the right hand of the slide. It is roughly what I mentioned up to know.

On page seven some physical information meaning the number of POTS for these mainlines that we have down 3.5%. Most of this is the ULL or those mainlines moving to our competitors and we are retaining them as wholesale. Total traffic is down 9.2%. You see the billions or thousands or millions of minutes. The ISDN lines down 10.7% which is usual because most of the customers were using ISDN for internet access, they have now moved to broadband and the average revenue per customers is down 8.2% at 138 kuna. So this is in the fixed telephony business.

In internet services on the next page, the revenue is up by 30.1% and amounting to 847 million. It is 22.2% of the T-Com revenue. MAXadsl continues to be the most popular choice; it is the leading broadband service not only in absolute trends but in net adds as well. We had 17,000 net adds in Q3 of '09. The average revenue has also increased because of the upgrade of speed and content improvements. Also we are diminishing some of the initial—or it is the end of some of the initial promotional periods and as that ends it has a positive impact on the average revenue. MAXtv is our IPTV service. It is by far the leading platform. It has been upgraded this year. It continues to be developed. We had nearly 19,000 net adds in Q3'09 so when you look at the net result, the ADSL or the broadband customer base grew by 22.7%. Dial up users is steady but this is again the base for future broadband customers. The ARPA is up by 3% and the IPTV customers grew twofold when you compare it to last year's September figures, nearly 190,000 customers at the end of September.

On the next page we have some information on the wholesale and data services. Slower growth of unbundled local loops which is you might say a positive reduction because the slower the ULL growth that means that we are not losing retail customers to our competitors. And number portability has increased and slight increase in usage of carrier preselect. We have also moving onto the data migration efforts to IP-based services. Meaning we are shutting down the old legacy platforms. Increased Metro Ethernet revenue. Wholesale revenue is down as you can see to 813 million kuna, 8.6%. And the number of ULLs again compared to last year September figure and this year September is up by 57%.

On T-Mobile Juergen Czapran our CFO and colleague on the board will take it from here and then I will come up with a summary and outlook at the end.

Juergen Czapran: Thank you, Ivica. As we have already mentioned the government introduced a 6% fee on mobile phone services on the 1st August this year and combined with the additional personal tax and increased VAT rate from 22 to 23% that were all introduced at the same time, this has impacted T-Mobile revenue to fall after several years of uninterrupted growth. However, impacted by these measures as well as by the recession itself, prepaid revenues are down by 12.2% caused by consumers tightening personal spending. Also total revenue fell down by 3.5%. We have compensated this with savings from increased efficiency so the EBITDA has fallen by about half that amount. I am pleased to say that we have actually increased our EBITDA margin by one percentage point to 47.3%, which is a good or even excellent performance.

In fact we actually reduced our cost by 6.2% and that has set us in a well position when revenues begin to grow again. As you will see on the next slide, we continue to increase our subscriber base and believe that mobile usage levels will recover at some stage when the economy picks up. In the meantime we are doing all we can to attract customers with deals that target specific segments of the market, such as young people and families. We also think mobile data services will become more important in the future and that is why we continue to invest in the network, so we can support the growth of products like the iPhone which are markets that really didn't exist a couple of years ago.

In the chart you can see that postpaid accounts still provide most of the revenue for T-Mobile and they have fallen slightly less than 2% in this period. Whereas prepaid revenue has fallen 12.2%. You can see that other revenue have increased quite a bit and that is mostly national roaming revenues we have gained from the contract with Tele2 which started last summer.

Looking at T-Mobile's operational data on slide 11, we can see that T-Mobile is the market leader in this segment. We have nearly 50% of the market share by revenue and about 47% by SIM and we serve 2.9 million subscribers which is 10% higher than last year and above 17,000 more than in the second quarter this year. Of this base, 31% are post paid subscribers who generate about 61% of revenue. So we continue to put a lot of marketing effort into converting people from prepaid to post paid. We are pleased to have managed to increase our prepaid accounts by 7.6% because in reality that is an extra 140,000 customers where we have a relationship that might not have been there before. As an impact of recession, subscribers controll their spending more. So it is clear that mobile usage is declining as a result. Decreased usage per average subscriber combined with increased penetration brought ARPU down nearly 16%. This time declining trend of ARPU was additionally impacted by newly introduced 6% contribution fee on mobile services.

Turning to the group financial highlights on slide 12, you can see the slight fall in revenue and the impact it has had on profitability at the EBITDA level which is partly due to higher employee expenses and a higher write down of assets. But obviously we remain committed to protecting our margins and as you can see we haven't given much margin away at the EBITDA level. Net profit is lower because we had slightly higher depreciation costs and lower income from investment in joint ventures. As you can see, CAPEX is higher this time but that is really down to the timing of projects because we actually anticipate CAPEX in 2009 at a slightly lower level than in 2008.

Now let me hand you back to Ivica to sum up.

Ivica Mudrinić: So, on the outlook now at the end considering revenue we have indicated consistently that we do expect a drop in revenue in 2009 due to the economic situation in Croatia and more recently because of the new taxes and levies imposed by the government. However, we believe that our revenue decline will be lower than the drop in the GDP and thereby confirming the resilience of the business in these difficult conditions.

The margin erosions will continue into the full year but we are committed to protect margins through cost efficiencies and reorganisation and as I mentioned at the beginning the reorganisation that we were planning for January 1st is actually—should be enabling future optimisation as well. As Juergen has just stated, the CAPEX has been reviewed in light of the drop in revenue due to the taxation and the overall environment and we believe it will be slightly lower than in 2008. We continue to monitor and evaluate expansion opportunities to increase shareholder value and hopefully to utilise some of the cash on the balance sheet in doing so as well, to create additional value of course and not just financial proceeds.