

The Q4 2016 results conference call

23 February 2017 at 14:00 CET

Presenters

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Operator: Good afternoon, ladies and gentlemen, and thank you for standing by. Welcome to today's HT Group Full Year 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 star one on your telephone and wait for your name to be announced.

I must advise you that this conference is being recorded today on Thursday the 23rd of February 2017. I would now like to hand the conference over your speaker today, Elvis Knežević. Please go ahead.

Elvis Knežević: Thank you. Ladies and gentlemen, good afternoon and welcome from Zagreb. Today, our CEO, Mr. Davor Tomašković and Josef Thuerriegl, our CFO, will talk you through the highlights of our business and financial performance for the 12 months ended 31st December 2016 using presentation slides which I hope you have in front of you.

If not please visit our website at www.t.ht.hr where you can access the slide from our investors page. After the presentation, Mr. Tomašković and Mr. Thuerriegl will be available for your questions.

Before we begin, allow me to draw your attention to the harbor statement on page two of our presentation. Allow me to introduce you to Mr. Tomašković, our CEO, will outline our company's performance during the 12 months ended 31st December 2016.

Davor Tomašković: Good afternoon ladies and gentlemen and thank you for joining us today. It is my pleasure once again to present the result from Hrvatski Telekom for the 12 months ended 31st December 2016.

I would start the presentation with slide four which outlines the highlights of the full year. The Croatian economy is now enjoying a steady recovery after many years of recession and GDP for the full year is expected to be around three percent with broad-based growth coming from industrial production, retail trades, tourism and construction activity. The Croatian telecommunication sector remains very competitive however, all the telecommunications companies are investing in the networks to keep up with data and internet demand and broadband, both mobile and fixed is the key driver of growth in this sector.

Against this backdrop, I'm pleased to report that we have delivered 2016 earnings in line with our previous reported outlook. Revenue in the 12 months to 31 December rose 0.7 percent to HRK6.97 billion even though there was no one of consolidation impact from Optima Telekom in 2016 as had been seen in the two preceding years.

Revenue was buoyed by encouraging trends in mobile, broadband, and TV and in sales of system solutions. Earnings before interest tax depreciation and amortization or EBITDA before exceptional items rose 1.4 percent to HRK2.82 billion, and we also saw a slight increase in the margin to 40.5 percent from 40.2 percent last year.

We expect 2017 revenue at a similar level to 2016 and we anticipate that we will maintain EBITDA margins before exceptional items at around 40 percent. The Board has proposed a dividend of HRK6 per share to be paid out of 2016 net profit equating to 54 percent payout ratio.

In addition, I'm pleased to announce that HT's intending to launch a share buyback program in 2017. Looking ahead, the Group expects to pay a dividend of no less than HRK6 per share out of 2017 net profit.

Operationally, we have again maintained our leading market position across all areas of the business. Magenta 1, our unique converged concept offering premium customer experience and benefits, continues to attract broadband and TV customers.

Our diversification into the energy segment is also displaying strong growth as consumers respond positively to our converged telco-energy proposition. In January, we completed the acquisition of Crnogorski Telekom in line with our strategy of growth through expansion and through regional markets.

We are now in the process of aligning strategy and taking operational control and the financials of Crnogorski Telekom will be added to the Group outlook for 2017 when we report our first quarter earnings in April.

Please turn now to slide five which shows our results for 2016 in relation to our forecast outlook for the year. Revenue was predicted to be around the 2015 level and we beat this forecast with the raise in revenue of 0.7 percent. The EBITDA margin before exceptional items had been forecast at around 40 percent and we outperformed here also with a margin of 40.5 percent.

We had expected to maintain CAPEX at the 2015 level of HRK1.47 billion. However, the final total was 9.1 percent higher. The increase was driven by intensive investment in fiber and the cost of fulfilling our regulatory requirements related to the electronic communications infrastructure.

We also continue to monitor and evaluate M&A opportunities throughout the year and these investigations and preparations led to our acquisition in January 2017 of Crnogorski Telekom. You will find further information on Crnogorski Telekom in appendix one of this presentation.

Please turn now to slide seven which describes the revenue breakdown in greater detail. We are very pleased to report a 0.7 percent rise in revenue in the full year 2016 to HRK6.97 billion beating our own forecast.

As I noted earlier, the key drivers of growth for mobile revenue, system solutions and energy sales, which helped to temper the drag from six points declines. Mobile revenue rose 3.3 percent as customers continue to use more data and bought larger

volumes of low-margin handsets. Sales grows to HRK2.82 billion from HRK2.73 billion in 2015.

The key drag on revenue continues to be fixed voice as fewer and fewer people use fixed line telephony and those that do so use it less regularly. Mainline sales, traffic and average revenue per account fell with revenue falling commensurately, down 12.7 percent to HRK953 million. This decline is in line with global telco trends.

Also, less pronounced, broadband and TV revenue also fell slightly down one percent to HRK1.315 billion despite a rise in customer numbers. The fall was due to stronger competition and aggressive offers in broadband which hit our ARPU. HT is mitigating the decline by promoting our Magenta 1 and Max 2, Max 3 and Ultra Max packages which are based on fiber to the home technology that enables much faster internet speeds.

The promotions have resulted in revenue momentum in the fourth quarter of 2016. Fixed wholesale revenue rose 7.5 percent in 2016 to HRK365 million, mainly due to higher infrastructure revenue while other fixed revenue rose 1.9 percent to HRK727 million on higher Optima Telekom consolidated revenue.

After disappointing third quarter hampered by public sector project deferral, we are pleased to report that system solutions revenue is back on track, following strong growth in the fourth quarter. System solutions within reach, the strongest area is customized ICT solutions, recorded annual revenue growth of 2.7 percent to HRK677 million.

Our most substantial growth has come from miscellaneous revenue which is largely derived from our increasingly popular energy products. Revenue more than double to HRK102 million boosted by a 12 percent jump in customer numbers and ongoing initiatives to increase customer loyalty.

Now we turn to slide eight which describes growth in EBITDA and net profit and outlines the strong investments we are making in our network. During 2016, EBITDA before exceptional items rose 1.4 percent to HRK2.82 billion. This growth can be attributed to increased revenue, the benefits of our restructuring measurements and sales of some assets including property and vehicles.

Net profit in the 12 months to 31st December rose one percent to HRK934 million reflecting high EBITDA, lower amortization of software licenses, lower exceptional items, and higher financial income. However, impairment losses and increased financial expenses impacted profit growth.

Net cash flow from operations was down 12.3 percent to HRK2.08 billion mainly due to negative moments in working capital. Meanwhile, CAPEX grows significantly up 9.1 percent to HRK1.61 billion after major investments in mobile and fixed broadband networks as well as higher ECI cost.

I will now hand over to Josef who will walk you through our performance during this period in more detail.

Josef Thuerriegl: Yes, thank you, Davor, and once again good afternoon to everybody. Please turn now to slide number nine which provides you a breakdown of the performance of our residential segments.

Sales in this segment were only slightly lower, down 0.7 percent to 3 billion 750 million in the full year 2016 as the rise in our mobile sales was almost fully offsetting the decline in fixed revenue. Contributing as a single most successful product to this residential revenue transformation, what our most innovative product Magenta 1 which includes converged customized office and other benefits for private customers and households.

Magenta 1 yielded strong results with 53,000 household signing up at the end of December 2016. We also continue besides Magenta 1 to promote our Max 2, Max 3 packages to residential customers who can enjoy exclusive TV content and premium TV packages.

The residential segment's contribution to EBITDA fell slightly by 1.8 percent to 2 billion – HRK2.56 billion as the revenue transformation was followed by somewhat higher operating expenses.

On slide 10, we review the performance from the business segment which posted better results of the rise in both revenue and the contribution to EBITDA. The sales in the business segment rose 2.3 percent to 2.78 billion reflecting growth in systems solutions and the energy business. This revenue growth was enough to offset the

somewhat higher direct cost by the nature of this business and the business segment thereby also showed a 0.5 percent rise in contribution to EBITDA of HRK1.36 billion.

Our efforts in the business segment are also focused like in residential on value management and customer retention. Also, here the Magenta 1, also for business clients includes flat fixed and mobile services with a highest available speed 4G backup network security and cloud storage of up to one terabyte capacity.

Continuing the converged theme, business customers are increasing return to our telco energy bundles as we offer attractive pricing and this is increasing our customer loyalty but also our ICT turnkey solutions were very much favored on the business segments.

Please turn now to slide 11 which details the progress we have made in our mobile business. Here we continue to focus on mobile data bundles and improving the customer experience centered on offering faster speeds. We are proud to report that we offer speeds of up to 262 megabits per second along some parts of the network.

We again maintained our market share by subscribing at 47 percent at the end of the fourth quarter with the number of subscribers largely flat at 2.23 million. This was made up of a slight increase in postpaid and a slight decrease in prepaid subscribers.

The average revenue per user showed similar trend with prepaid down and postpaid up. Prepaid ARPU fell 1.6 percent in the year from 43 to HRK42. Postpaid ARPU meanwhile rose by 0.9 percent to 110 from HRK109. Blended ARPU was up by 1.2 percent.

At the end of the year average minutes of use was up by 5.7 percent in line with the overall market trend of fixed to mobile substitution and free minutes included within our tariffs.

Supporting our value-driven strategy in mobile, the percentage of smart phone as a proportion of total handset sales was further up by nearly 80 percent in the postpaid segment in the 12 months to December 2016, largely flat on the previous year. HT Group smart phone penetration was reaching 67 percent.

As we continue to invest in our network, 4G coverage reached 68.2 percent of the population indoors and 96.9 percent outdoors. We had also enabled 51 percent of

the population to achieve 4G download speeds of up to 225 megabits per second which is an increase of 60 percent year over year.

We can now turn to slide 12 which describes our fixed line and IP business. Again, in 2016 the trend for declining fixed mainlines continues and broadband and TV customers remained the growth driver of the segment.

Customer base wise, the number of fixed main line fell 6.1 percent in 2016 reflecting declines across both wholesale and retail. However, the number of broadband access lines rose by a similar percentage. HT Group has put a strong focus on the further development of the network infrastructure increasing broadband capacity and availability to maintain our leading position as the largest fixed broadband operator in Croatia.

TV customers are also in the increase. At the end of 2016 we had 401,000 TV customers, a rise of 3.4 percent on the year earlier. On the ARPU's side as expected, fixed line ARPU was down by 6.8 percent to HRK84 as customers use the fixed line telephone less and less and switch to mobile.

But meanwhile, broadband retail is also under pressure fell down to 2.3 percent to 122 due to stronger competition and aggressive offers in the market. On the other hand side TV ARPU was up by 1.4 percent in the period to HRK82. The result was our concerted efforts to improve our services and program offers.

In total next generation access speeds have been enabled for 54 percent of Croatian household as a result of HT's efforts bringing Croatia by this closer to the target of the European digital agenda.

I will now hand back to the Davor who will outline for you our outlook for the forthcoming year.

Davor Tomašković: Thank you, Josef. To conclude this presentation of our full year performance I would like to focus on our outlook, for 2017, currently before the inclusion of Crnogorski Telekom, and our dividend proposals for 2016 and 2017.

The slide 14 shows we expect revenue in 2017 to remain at around a level we delivered in 2016 which was HRK6.97 billion. Having achieved the margin for

EBITDA before exceptional items of 40.5 percent in 2016 we expect this margin to be around 40 percent in the current financial year.

2016 was a particularly intensive year for investment in our network infrastructure and while we will continue to focus on building our network to keep up with the increasing data demand, we expect CAPEX in 2017 to be moderately lower than the 1.61 billion which is spent in 2016.

With regards to regional expansion, HT is again continuing to monitor and evaluate potential M&A opportunities.

And finally, on slide 15, let me outline for you the dividend in 2016 and 2017. The Board has arrived with the final dividend proposals of HRK6 per share after announcing a minimum target dividend of the same amount in February 2016. This equates to a payout ratio of 54 percent. In addition, HT intends to launch share buyback program once we have concluded the detailed market assessment. And looking forward to the current year, HT expects to pay out a dividend of no less than HRK6 per share for the year 2017.

Thank you for your attention this afternoon, we're now ready to take your questions.