



1Q 2020 Results Conference Call

May 14, 2020 at 13:00 CET

Good afternoon everyone. I am Melinda Modok, Head of Investor Relations at Magyar Telekom. I would like to welcome you to our first quarter 2020 results conference call. Please note that our presentation can be accessed via the link within the conference call invitation, and is also available in the Investor Relations section of our website.

Before we get started, I would like to draw your attention to the disclaimer on the second page. Information in this presentation contains statements about expected future events and financial results that are forward-looking and subject to risks and uncertainties.

With me today is Mr. Tibor Rékasi, our CEO, and Ms. Darja Dodonova, our CFO, who will take you through the presentation and answer any questions you may have.

Now, it is my pleasure to hand over to Tibor to open the presentation.

Tibor Rékasi

Thank you, Melinda. Good afternoon everybody.

Let me start with a short update on how we are **responding to the COVID-19 pandemic** and the impact this is having on our operations, our people and our customers.

Our main focus since the outbreak of coronavirus has been on the swift implementation of measures to safeguard the health and safety of our employees and customers. Following the introduction of strict social distancing across the Group, around 80% of our employees continue to work remotely. While the majority of our points of sale remain open, we have highly limited traffic within stores. However, I am pleased to report that our call centres and online support services are successfully handling increased volumes of customer requests.

This crisis is having an unprecedented impact on our society and, as a Group, we are actively supporting the communities in which we operate.



For example, we were the first in Hungary to offer free mobile data to our customers. Furthermore, to facilitate online learning, we have introduced complimentary educational content, additional TV content, and a range of attractively priced laptops and tablets. In addition, we are providing free voice usage to the most vulnerable in our society as well as payment restructuring for customers in financial difficulties.

Digitalisation has been of vital importance in these times of unprecedented crisis and our networks are playing a critical role in keeping businesses and families connected. To ensure the reliability and security of our networks, we continue to invest in our infrastructure. Usage levels have increased to pre-crisis peak levels across the market with voice usage over our network up by more than 50% and data usage by almost 30%. I am extremely proud that, despite these extraordinary capacity demands, we continued to provide seamless services to both our residential and business customers.

Slide 4 shows the progress we've made against our **strategic priorities during the first quarter**. The rollout of our fibre network remains a key priority and capex dedicated to such investments has doubled versus the first quarter of 2019. As a result, more than two million access points are now connected to our gigabit speed capable network, covering almost half of our footprint. The importance of these developments, which serve as a cornerstone to the digitalization of households and business in Hungary, has never been higher, and I strongly believe that our industry is playing a vital role in the current crisis and will continue to do so as we restart our economy.

The successful acquisition of spectrum licences related to 5G and mobile broadband services at the end of March, was a very important step for us to be able to offer the full range of infrastructure necessary for the digital environment. We commenced commercial 5G services in early April and intend to steadily expand our coverage over the coming months.



These efforts have been welcomed by our customers. We see an increasing number of subscribers opting for higher bandwidth fixed packages, even more so since the introduction of social distancing measures. On the mobile network, average data usage is increasing rapidly and this trend is expected to accelerate with growing take up of products and services leveraging 5G features.

I am also pleased to report that we have made further progress in enhancing our operational efficiency. We concluded both the headcount reduction programme announced last year at the Hungarian operation and the voluntary programme in North Macedonia. These programmes, coupled with other restructuring efforts, led to a 9% reduction in the Group's employees in the first quarter of 2020. We also progressed the rollout of our agile, cross-functional working practices. This is proving highly beneficial in this rapidly changing environment as, thanks to our more streamlined processes and operation, we are able to respond to customer needs in a more flexible and timely manner.

At the same time, we sustained positive operational momentum at our North Macedonian operations. Customer numbers continued to improve, supported by bundled and fixed-mobile convergent service offerings. As a result, we successfully maintained our number one position in the fixed market despite the continued intense competitive pressures.

Moving on to **our financial performance** in the first quarter of 2020 and our public targets on **Slide 5**. Total Group revenues remained broadly stable compared to a year earlier. While we successfully continued to grow telecommunication service revenues at both operations, these were offset by the decline in System integration and IT revenues in Hungary coupled with the slowdown in equipment sales. The latter reflects the lower transaction volumes witnessed across all segments since the outbreak of COVID-19. Looking ahead, the global pandemic is expected to negatively impact our roaming and visitor revenues along with equipment sales and reshape demand for System Integration and IT services. Nevertheless, we expect demand for our core telecommunication services to remain strong, making the delivery of broadly stable revenues achievable.



EBITDA also remained stable year-on-year in the first quarter of 2020 with EBITDA after leases increasing moderately by 1%, driven by lower IFRS 16 related expenses. Our EBITDA performance was the combined result of higher gross profit contribution from telecommunication services and positive results from cost optimization measures, offset by lower SI/IT gross profit and negative impacts stemming from the weakening of the forint. Going forward, we expect profitability to come under pressure from unfavourable exchange rates as well as the negative effects of the recessionary environment. To mitigate the impact of such trends on our performance, we intend to pursue further cost optimization measures that will support us in our efforts to reach our target for the full year.

Our Capex - excluding the impact of IFRS 16 - in the first quarter of 2020 rose strongly versus last year, driven by differences in the timing of investments. The increase, as mentioned, is mostly due to the acceleration of the fibre rollout program in Hungary and one-off increases in North Macedonia related to TV content fee capitalization. Although the weakening of the forint is expected to have some effect on our overall capital expenditures going forward, with the necessary adjustments and optimization measures, we currently do not foresee any major deviation from our original full year target.

Our free cashflow performance, excluding the 11-billion-forint payment for the extension of the 2100 Megahertz frequency license in Q1 2019, declined by 4 billion forints year-on-year. This reflects the increase in capital expenditures, as well as lower proceeds from real-estate sales that could only be partly offset by improvements in working capital. Looking ahead, we expect the favourable trend in working capital and levelling out of capex volumes to support us in meeting our guidance of an annual 5% increase.

I will now hand over to Darja to run through the performance of our business segments in more detail.



Thank you, Tibor. Good afternoon everyone.

Starting with **Hungary** on **Slide 6**, overall revenue recorded a moderate decline in the first quarter, primarily due to the significant decline in System integration and IT sales coupled with lower equipment sales.

As in previous quarters, we achieved growth in both mobile and fixed service revenues. In both segments, data revenues remained the most important driver of growth, with TV revenues also positively contributing towards the positive momentum. The structural decline in voice revenues continued into 2020, although the outbreak of COVID-19 has led to elevated voice usage levels since mid-March. As customer transactions declined sharply following the introduction of social distancing measures, the overall volume of equipment sales also declined leading to a moderate contraction versus the previous quarter. Other revenues were negatively impacted by lower dunning fees in the mobile segment coupled with a higher level of discounts provided for fixed line customers in relation to online bill payments.

System Integration and IT revenues contracted due to lower income from Hungarian public and corporate sector projects, especially in the large volume implementation segment. Social distancing measures have also been reshaping demand for IT services. Projects facilitating digitalization are becoming more-and-more vital for the long-term success of businesses in all sectors of the economy. However, these projects, while of great significance longer term, have a lower contribution to our profitability today.

EBITDA after leases at our Hungarian operation contracted slightly year-on-year, as savings in indirect costs could not fully offset lower gross profit and declines in other operating income. The gross profit decline reflects higher expenses in relation to elevated voice usage levels; both interconnect outpayments and telecom tax are up compared to previous quarters. These increases were coupled with higher bad debt and TV content related outpayments, the latter also reflecting the weaker forint. Savings were the most prominent in employee-related expenses, thanks to the decline in the company's headcount which fully offset the effect of higher severance expenses in relation to the headcount reduction programme.



Further savings were also achieved in advisory and maintenance expenses. However, the absence of income from real-estate sales, that positively impacted results in the first quarter of 2019, led to lower other operating income.

Slide 7 shows **customer developments** at the Hungarian operations. The make-up of our customer base continues to improve in both the mobile and fixed segments. In the mobile segment, the number of total SIM cards has grown further, with most of the increase driven by growth in the postpaid customer base. Please note that, to provide a more transparent account of our mobile SIM base, as of this quarter we report machine-to-machine SIM cards separately. These were previously included in the postpaid base. This will allow you to more closely track the development of this segment which is expected to become a key growth driver going forward. In parallel, our mobile data customer base registered a significant increase which we expect to be further intensified by the favourable offers we introduced, partly in response to social distancing measures.

In the fixed line market, the ratio of customers choosing bundled packages has increased further, albeit with growth driven by 2-play offers. You can see this trend on the charts that show customer developments by service. While the fixed voice customer base shows a steady decline, broadband and pay TV customer bases are increasing dynamically thanks to our competitive service and product offerings.

Slide 8 shows the strong increase in **usage** volumes since the outbreak of COVID-19. Although the pandemic hit Hungary only in the last 2 weeks of the quarter, its impact on voice usage is already visible in our numbers. Mobile voice usage rose by 14% versus mid-single digit increases in previous quarters, while the earlier sharp decline in the average fixed usage has now been flattened. Positive momentum in mobile data usage continued with 50% growth year-on-year.



However, these increases could only partially be translated to **APRU** improvement due to the growing portion of unlimited and semi-flat packages. Nevertheless, thanks to the success of our more-for-more strategy, our postpaid segment delivered a strong performance, leading to a positive trend in our blended mobile ARPU. In addition, we witnessed favourable developments in fixed broadband ARPU supported by the increasing demand for higher bandwidth packages. While the full impact of the current crisis on our performance remains highly uncertain, we currently expect continued strong demand for our services. We will continue to closely monitor the impact of the pandemic on our operations and, if necessary, adjust the measures implemented throughout the year.

Moving on to the performance of our **North Macedonian operations**, shown on **Slide 9** in local currency to better reflect underlying performance. For most of the first quarter, the positive trend in underlying revenue witnessed over the previous quarters continued. However, towards the end of the period, we saw a negative impact of COVID-19.

The overall improvement in mobile revenues slowed to 1% as continued growth in mobile data and equipment revenues was offset by lower roaming and visitor revenues. These declines were primarily attributable to the reduction in roaming price levels following the introduction of the Balkan roaming agreement in July 2019, while the decline in tourism activity due to COVID-19 also had an unfavourable impact. Nevertheless, the positive underlying trends were successfully maintained. The overall customer base increased moderately with the number of mobile data subscriptions growing by 7% year-on-year and the postpaid share in the total SIM base advancing further. Please note that, similarly to the Hungarian operation, machine-to-machine SIM cards are now reported separately. Blended ARPU development shows a moderate decline, driven by the aforementioned cut in roaming prices coupled with lower spending in the prepaid segment. This could not be fully offset by higher mobile data revenues.



Fixed revenues continued to perform positively, growing 2% year-on-year, as higher TV and retail broadband revenues fully offset the structural decline in voice revenues. With price levels under sustained competitive pressure, ARPU trends in the fixed market remained unchanged. However, thanks to the success of our bundling strategy, customer numbers continued to grow across all three service lines leading to overall service revenue improvement.

System integration and IT revenues almost tripled in the first quarter, reflecting a recovery in public sector demand, mainly in the fields of customized solution projects, cloud computing and internet protection.

EBITDA after leases temporarily declined. This was driven by the negative effect of one-off termination expenses which offset a higher gross profit and improvements in other operating expenses, most notably the cost of raw materials and marketing.

Looking ahead, while the precise impact of the current crisis on Makedonski Telekom's financial performance remains uncertain, we expect sales to be negatively impacted, especially in the prepaid segment. Equipment sales, roaming and visitor revenues are also expected to decline.

At the same time, in line with our Group approach, Makedonski Telekom is also engaged in supporting the North Macedonian society throughout the crisis. At present, the company is providing additional benefits such as more mobile data and TV content. In addition, Makedonski Telekom has donated mobile internet for distance learning to children from families at social risk until the end of the school year.

Tibor Rékasi remarks

Thank you very much, Darja.

That concludes our presentation. We are now happy to take any questions you may have. Operator, when you are ready, we will take the first question.

(Take questions)



LIFE IS FOR SHARING.

If you have any follow-up questions, please do contact our Investor Relations team. Please also note that the transcript of our conference call will shortly be available on our website. Thank you again for joining us today and your continued interest in Magyar Telekom.