



3Q 2019 Results Conference Call

November 6, 2019 at 18:00 CET

Good evening everyone and welcome to the Magyar Telekom third quarter 2019 results conference call. I am Péter Bauer, Head of Investor Relations at Magyar Telekom, and with me today is Mr. Tibor Rékasi, our CEO, and Mr. János Szabó, our CFO, who will take you through the presentation and answer any questions you may have.

Please note that the Q3 results presentation can be accessed via the link provided in the conference call invitation, and is also available in the Investor Relations section of our website.

Before we begin, 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.

Now, it is my pleasure to hand over to Tibor who will begin the presentation.

Tibor Rékasi

Thank you, Péter. Good evening everybody.

Let me start again with an update on our key initiatives, as set out on **Slide 3**.

In Hungary, we progressed the delivery of our fibre rollout programme, adding more access points to our fiber network than ever before in a single quarter. This, coupled with the completion of the Docsis upgrade process that now enables us to offer gigabit speeds on the majority of our cable network, has notably strengthened the competitiveness of our fixed infrastructure. At the end of September, we became capable of providing gigabit speeds to 1.7 million households and businesses in Hungary.



With regards to our service portfolio, we continued the reshape of our offering to maximise potential household spend by offering higher value packages while maintaining attractive prices. Success of this strategy is reflected in the increase of mobile data ARPU attributable to the changes introduced in August to our mobile data portfolio, which promote subscriptions to packages with higher monthly data allowances.

In September, we launched new tariffs in our fixed segment to simplify the portfolio and capitalize on our improved network capabilities. The initial results of this are promising and overall sales volumes are up across all service categories. Furthermore, an increasing number of broadband customers are signing up for gigabit packages, equating to approximately one-third of sales in September.

From the third quarter, we provide Magenta customers with a single, combined bill for their telecommunication service portfolio. Not only does this help customers to track the discounts they benefit from more closely, but it also supports our internal processes by enabling us to better identify customer needs and demands.

Meanwhile, in North Macedonia, despite competitive pressures, favourable trends were sustained with customer numbers rising further, supported by bundled and fixed-mobile convergent service offerings. These contributed to our ability to maintain the positive financial performance with regards to both revenues and EBITDA.

Turning to the Group's results on **Slide 4, revenues** in the third quarter grew moderately due to telecommunication revenue increases in both Hungary and North Macedonia. The growth in both countries was fuelled by an expansion of the fixed broadband and TV subscriber bases, as well as the continued strong demand for mobile data. The continued positive trend in fixed equipment sales, supported by the opportunity to group equipment subsidies, fully offset the year-on-year decline in mobile equipment sales.



Group EBITDA, excluding the impact of IFRS 16 adoption, grew 4% year-on-year thanks to the improvement recorded in both countries of operation. In Hungary, the growth in gross profit reflects a one-off improvement in bad debt expenses, while the year-on-year reduction in indirect costs is attributable to savings in employee-related expenses. In North Macedonia, the gross profit increase is the result of higher revenues and a reduction in indirect costs attributable to lower employee and marketing expenses. It is also worth noting that Group EBITDA was favourably impacted by the implementation of IFRS 16 to the tune of 4.7 billion forints.

With regards to delivery against our **targets** set out on **Slide 5**. As forecasted, the revenue growth trend witnessed last year has slowed considerably, driven by the reduction in SI/IT and mobile equipment sale revenues. Looking ahead, we expect SI/IT revenues to decline further. However, we believe this will be largely compensated for by the positive dynamics of our core telecommunication revenues.

In line with our targets, we expect Group **EBITDA** to increase by 1 to 2% on an annual basis, thanks to efficiency enhancing measures we have been implementing across the business.

Capital expenditure, excluding the impact of IFRS 16 adoption, increased year-on-year, largely due to a ramp up in fixed infrastructure investments and more evenly timed investments compared to 2018.

In the third quarter, **free cashflow** improved, reflecting positive trends in our underlying performance. Excluding the 11 billion forint payment for the extension of the 2100 Megahertz frequency license, free cashflow by the end of September was broadly flat year-on-year. This is driven by higher EBITDA and an improvement in installment and other receivables which helped to offset increased outpayments to suppliers and capital expenditure.

Given our performance so far this year, we believe we are very well positioned to deliver on our full year targets for 2019.



I will now hand over to János to provide you with further details on the performance of our business segments

János Szabó

Thank you, Tibor. Good evening.

Turning first to the performance of our business in **Hungary** on **Slide 6**, **total revenues** increased marginally by 0.3%, in the third quarter, primarily due to a continued decline in SI/IT and mobile equipment revenues which was offset by an increase in data usage by our customers.

As reported in recent quarters, **mobile** service revenues continued to grow thanks to continued strong demand for data by our customers and changes in our mobile portfolio pricing. This year, we renewed both our postpaid voice and data packages with our 'more-for-more' strategy in mind, offering higher value packages to customers at a higher price point. Unfortunately, the growth of our mobile service revenues could not offset the continued decline in mobile equipment revenues, where customer spending has still not recovered from the second quarter of 2019.

Meanwhile, **fixed** revenues continued to grow both on the service revenue and equipment revenue lines. This is primarily due to fixed service revenue growth in the broadband segment where, like the mobile segment, we still encounter growing customer interest in data-related products. To ensure we take advantage of this opportunity, we restructured our fixed portfolio offering in Q3 with our more-for-more strategy in mind. In the fixed segment, equipment sales revenue continued to grow in the quarter, up approximately 38% versus last year.

In the **System Integration and IT** segment, we witnessed a continuing year-on-year decline in revenues, as we continue to operate against a particularly strong prior year, with revenues further impacted by a change in the seasonality of public sector projects.



EBITDA, excluding the impact of IFRS 16 adoption, increased by 4.7%. Including the impact of IFRS 16, EBITDA increased 15%.

Despite a reduction in System Integration and IT revenues, we successfully grew gross profit thanks to a higher contribution from our telecommunication services, both in the fixed and mobile segment, as well as a one-off improvement in bad debt expenses. The savings in our employee-related expenses reflect the effect of a lower headcount and a reduction in severance expenses which helped to offset wage increases to ensure salaries remain competitive in the Hungarian market.

Slide 7 illustrates the key developments within our **Hungarian mobile operations**. We have continued our ongoing efforts to convert our customers from pre- to postpaid packages. Attractiveness of postpaid packages was boosted by both the continued requirement to annually register prepaid customers as well as the rising demand for data. We also grew the total number of SIM cards compared to last year.

In 2019, in addition to focusing on the aforementioned pre-to postpaid migration and growing our SIM cards we also took the opportunity to review our mobile portfolio. This initiative commenced in Q1 with the introduction of our new pre-paid packages followed by a restructuring of the voice portfolio in Q2 and updates to our mobile data portfolio in Q3. Thanks to these portfolio changes, we grew our blended mobile ARPU by 2% this quarter.

In the third quarter we witnessed continued growth in customer data usage and a strong increase in the number of 4G customers using our networks. Despite a temporary decline in handset sales our focus on providing our customers with the latest 4G handsets show in our network usage, where over 88% of all data customers are using our award winning 4G network. The importance of our 4G network is even more visible when you look at the mobile broadband usage of our 4G and non-4G customers. By the third quarter 97% of all data consumed in our network was via a 4G connection. Total data consumption has also grown, by over 50%,



compared to the same quarter the last year. It is worth mentioning that 4G usage being more and more frequent 4G customers tend to use more data than the non-4G ones, over 6 times as much in the latest quarter.

Slide 8 shows the progression of the **fixed segment** in the third quarter. As we look at the fixed customer base it shows that besides the structural decline in the fixed voice customer base, we have managed to grow both our TV and fixed broadband customer base. In the TV segment, the growth came from the IPTV customer base reflecting our continued efforts to encourage our customers to adopt this technology, where we can leverage our ever-growing fixed network and offer the best products to our customers. In the fixed broadband segment, as mentioned by Tibor earlier, we upgraded our cable network to a gigabit capacity, meaning we can now reach 1.7 million households and businesses with gigabit connectivity.

The next chart illustrates the distribution of our multiplay subscriber base. In Q3, we recorded a decline in 1Play customers, as an increasing number of our subscribers discover the benefits of having 2 or 3 fixed services with us.

In addition to the structural decline in voice ARPU, we have experienced a decrease in TV ARPU, largely due to higher customer discounts, while fixed broadband ARPU continued to grow in the third quarter. This is in line with our efforts to upgrade our fixed network to be able to offer gigabit internet in every household in Hungary. The advantages of this strategy are clearly reflected in the fixed broadband ARPU figures, where we find that many of our customers opt for a higher data package if possible. Our ability to offer 1.7 million households with gigabit capable internet connections demonstrates our ability to create value for both customers and the Company with this strategy.

The final chart illustrates the advantages of customers having more than one service. In Q3, we successfully grew the blended ARPU of our fixed products, while also growing customer ARPU



figures across the board from 1Play to 3Play customers. As we focus on encouraging customers to use more of our products, we believe there is further growth potential in blended ARPU.

On Slide 9 we have outlined the developments in the **Hungarian System Integration and IT segment**. In the third quarter the revenue decline has continued in our SI/IT subsidiary which resulted in a lower gross profit for the period. This was driven primarily by a lower number of public sector projects being implemented in the Hungarian market compared to the prior year period.

Moving on to the performance of our **North Macedonian operations on Slide 10**. Our results are presented in local currency to better reflect our underlying performance. I am pleased to report a further year-on-year increase in revenues and EBITDA, despite the intensifying competitive pressure we are facing in both the fixed and mobile markets. Third quarter marked the start of a rebranding campaign of our major competitor, VIP, to A1 Macedonia with strong data and equipment promotions accompanying the process. Nonetheless, thanks to our strong service quality and attractive offerings we managed to sustain the positive performance in the period.

In the **mobile segment**, service revenue growth continues to be driven by higher data revenues thanks to the continued expansion of our mobile broadband customer base which grew approximately 6% year-on-year. To maintain competitiveness, we have introduced attractive smart equipment offers that led to higher equipment revenues and a 5% increase in the number of postpaid subscribers. The third quarter is also typically characterised by seasonally higher tourism, leading to higher prepaid customer numbers.

From July 1, the Balkan roaming agreement became effective which, like the EU directive, aims to minimize roaming charges within the six Balkan countries who have signed the agreement.



As a result, visitor traffic rose sharply, supporting other mobile revenues. Conversely, subscriber roaming revenues deteriorated compared to the third quarter of 2018.

Overall, this performance, coupled with the changing dynamics in the postpaid subscriber base, led to a slight decline in prepaid and postpaid ARPUs; whilst blended ARPU was up approximately 3% year-on-year.

Despite competitive pressures also characterizing the **fixed segment**, TV and retail broadband revenues increased. This reflects continued expansion of the relevant customer bases which helped to partly compensate for the decline in wholesale and retail voice revenues. Our continued efforts to cross sell bundled packages supported expansion of the customer base, including a 20% year-on-year increase in the double and triple play customer base.

Our **FMC Magenta** subscriber base also continued to grow and by the end of September, 45% of our home customers held an integrated package with us.

System integration and IT revenues witnessed a temporary decline, driven solely by year-on-year differences in the timing of project deliveries. Going forward, we expect continued growth in the segment.

EBITDA in North Macedonia, excluding the impact of IFRS 16 implementation, improved considerably, as a result of revenue growth and indirect cost savings, specifically in employee and marketing expenses.

Looking ahead, we believe that our attractive service offerings, coupled with our efforts to increase operational efficiency, will mitigate the negative impacts stemming from intensifying competition and support us in maintaining the positive financial performance delivered in the past quarters.



Tibor Rékasi remarks

Thank you very much, János.

That concludes the formal part of Magyar Telekom's conference call. Now, operator, when you are ready, we will take the first question.

(Take questions)

If you have any follow-up questions, please do contact our Investor Relations Department. 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.