

Final version

Conference call operator introduces call

Elek Straub remarks

Good afternoon, ladies and gentlemen and welcome to Matáv's conference call for the full year 2004 results. I am Elek Straub, Matáv's Chairman and Chief Executive Officer. Dr. Klaus Hartmann, our CFO and member of the Board and Szabolcs Czente, Head of Investor Relations are also here with me today.

Let us begin with a summary of Matáv's full year 2004 performance, after which we will provide you with more details on our three reporting segments. We will conclude the call with an outlook for the year 2005 by taking you through our public targets, the details of the potential Telekom Montenegro deal, a further update on dividend payment and finally the planned name change for Matáv.

I would like to start with a brief overview of Matáv's 2004 public targets and the performance against them. I am pleased to say that Matáv achieved and in some cases even overperformed last year's goals. The 2004 full year revenue was in line with our target of around 600 billion forints, while EBITDA margin before restructuring charges stood at 40.4%, meeting the around 40% targeted level. Reported Group EBITDA margin, however, fell to 37.1% as 2004 financials were affected by restructuring charges and additional employee benefits relating to future terminations in the amount of 20.7 billion forints, within this, restructuring charges amounted to 20.2 billion forints. We expect to incur some minor additional charges throughout the duration of the program but the total expense of the restructuring is expected to stay below the earlier communicated 22.7 billion forints.

The target for gross additions to tangible and intangible assets without UMTS spending was around 90 billion forints. The actual number was somewhat lower at 85 billion forints mainly because some investments were delayed at MakTel due to the uncertainties in the upcoming Macedonian telecommunication market liberalisation. In addition procurement related savings were realised, for example on ADSL-related assets. As for the operational targets, let me mention that one of the year's greatest achievements was the fact that we were able to minimise the erosion of fixed lines. A main driver behind this success was the fast rollout of ADSL: Matáv surpassed the targeted 200 thousand ADSL lines at the end of December.

Beyond these figures, the year was characterised by substantial achievements and measures determining the future of many aspects of the Matáv Group. Among the milestones of 2004, let me cite the successful rebranding of Westel to T-Mobile, the announcement of our mid-term strategy along with the restructuring plans, the winning of a UMTS licence – and this is not all as further milestones followed in January 2005: we were selected to enter exclusive negotiations to acquire Telekom Montenegro and have also taken the conceptual decision to rename Matáv as Magyar Telekom.

(Pause)

First, I would like to take you through the analysis of the performance of the fixed line segment. As expected, the segment reported a drop in revenue and EBITDA. Revenues fell by 7% mainly due to the strengthening competitive pressure and regulatory changes. Regulatory impacts include reduced interconnection fees as well as a revenue fallout of around 6 billion forints primarily due to the reduced role of the Universal Telecommunications Support Fund. Revenues were also hit by decreasing transit revenues. Although data revenues show continuous growth, they cannot counterbalance these factors. Reported EBITDA margin stood at 28.4%, reflecting last year's headcount reduction expenses and the severance provision made for the expected expenses in 2005-2006 in the amount of 16.7 billion forints in total. EBITDA margin before restructuring charges was 33.9%

As mentioned earlier, we are proud to have minimised the erosion of the fixed-line segment by the end of last year and even managed to increase the number of residential PSTN customers. In the Matáv service area, new customised packages were introduced, by now their proportion of the total number of lines grew to 58%. Furthermore, with the availability of carrier selection for local and Internet calls, we extended our offerings in the service areas of other LTOs to include local calls through carrier preselection and call-by-call carrier selection from mid-September, with attractive per-minute fees.

At the same time, some of these actions have put pressure on our revenues. The increased proportion of customised tariff packages partly reduces traffic revenues as the monthly flat fee of XL, XXL supplementary packages and bundled minutes of Halving are accounted for in subscription revenues. The discounted offers stimulate usage but also cause traffic revenue fallout as higher usage is offset by the lower minute rates. Fixed-to-mobile termination fees were lowered in September 2003 and in June 2004. In addition, the loss of some heavy user business customers also resulted in traffic fallout, which the increase in the residential customer base could not compensate for. As a combined effect of all these factors domestic traffic revenues decreased by 15% year-on-year. In parallel, international traffic revenues also fell by 19% compared to the end of 2003 as a result of lower outgoing and incoming traffic as well as lower average settlement rates.

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Another main factor in fixed line revenue erosion was the drop in other usage revenues, with 47% decrease compared to the previous year. Not only were interconnection fees significantly lowered but the drop in transit volumes due to the direct interconnection of mobile service providers and LTOs also caused a significant decrease in other usage revenues. Please note though that at the same time, payments to other network operators were also lower thus limiting the EBITDA impact.

Last year we witnessed intensifying competition, partly imposed by regulatory changes. The fixed-line number portability introduced in January last year is certainly a threat, especially for our corporate customer base. In the residential business, competitors also took advantage of the regulatory changes such as number portability and decreasing interconnection fees. Tele2 entered the Hungarian market in April 2004. UPC followed suit in September introducing voice over cable services.

Although competition certainly puts a downward pressure on our revenues, please bear in mind that this is partially compensated by respective interconnection revenues. Another positive factor is that at the residential segment, usage is still increasing despite the entrance of new competitors.

In the broadband business, the number of ADSL lines almost doubled during 2004, and as a result, we even outperformed our year-end target and closed the year with over 203 thousand ADSL connections. The high, 21% increase in data and leased line transmission revenues is partly a result of this rapid growth. In Matáv's service area, every third internet subscriber already accesses the web via an ADSL line and a rising share of new residential customers selects ADSL as their first internet access line. This positive trend has been supported by the free of charge upgrade of the ADSL access rates since November last year as well as the introduction of new broadband content services. Considering last year's results we are confident that we can fulfil our earlier commitment of reaching 400 thousand ADSL connections by the end of next year. Increasing broadband revenues will also serve as an important driver in the achievement of our strategic target of producing low single digit revenue growth at Group level by 2006.

In order to further increase fixed line productivity, we continue to focus on cost-cutting opportunities and are continuously implementing efficiency measures. The consistent increase in the line per employee ratio at the parent company reflects our efforts to minimise fixed line erosion and to maximise headcount efficiency. The ratio stood at 365 at the end of last year and we set an ambitious target of exceeding 500 fixed lines per employee by the end of 2006 at the parent company.

Let me now hand over to Klaus who will continue with the analysis of the mobile segment.

(Pause)

Dr. Klaus Hartmann remarks

Thank you, Elek.

Good afternoon!

Hungary's leading mobile player, T-Mobile Hungary had a customer base of over 4 million at the end of last year resulting in a 46% market share in a market with 86% penetration. Mobile segment revenues grew slightly due to increased voice traffic and value-added service revenues as well as equipment sales. Full-year segmental EBITDA margin increased by 2 percentage points to 39.4% in 2004.

As the market approaches saturation, the intensifying tariff competition has resulted in deeply discounted prices, putting pressure on our service margins. As a result of the postpaid price competition, all three operators introduced flat-rate postpaid packages in 2004. The rapid acceptance of T-Mobile Hungary's flat rate postpaid package, Relax, contributed to the positive change in our customer mix. Thanks to the migration of a significant number of prepaid customers to postpaid packages, the proportion of postpaid customers increased to 29%. In addition, the percentage of postpaid customers in net sales grew to almost 70% by the last quarter of the year, compared to 36% in 2003 and practically zero two years earlier, reflecting the success of our efforts to increase the proportion of postpaid subscribers. Tariff reductions and the growing customer base of flat-rate packages increased the usage. However, usage growth could not counterbalance the fact that the migration to the postpaid flat-rate Relax packages caused a lower average tariff level, which has put downward pressure on both ARPU and margins.

In the prepaid segment, both competitors introduced substantial periodic discounts, which are now being extended. T-Mobile did not enter into this new step of tariff competition, and in fact raised prepaid peak minute fees. Other measures to protect traffic revenues were the increase of the billing increment of all public postpaid packages to 30 seconds and the rise in international call fees as well as roaming charges in non Freemove alliance networks. In parallel, to offset competitors' lower tariff levels, T-Mobile launched discounted fees and bundled minutes to members of the loyalty program, supported by a strong campaign.

The postpaid churn rate remains favourable despite competing tariff offers, the high market saturation and the introduction of mobile number portability in May last year. In fact, number portability has had a limited impact on both our customer base and revenues so far. In the prepaid segment, year-to-date churn increased to 17%, and within this period, fourth quarter churn grew to 25%. This is mainly attributable to a technical reason, namely the expiry of the extended validity period of the prepaid refill vouchers.

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Let me now continue with the regulatory aspect of the mobile market. In line with the EU practice, the National Communications Authority has performed a series of analyses of the fixed-line and mobile market areas. Following the analysis of the mobile call termination market, all three Hungarian mobile operators were identified as significant market powers in this market. Vodafone Hungary will therefore also have to submit a cost-based price calculation model for mobile termination fees to the regulatory authority for approval. In 2005, mobile companies are offered the choice to apply a 15% minus CPI decrease instead of the decrease resulting from the LRIC model, therefore the expected maximum decrease of mobile termination fees will be 10%. This is most likely to become applicable from June this year. The regulator also expressed its intention to converge the termination fees of the individual operators to eliminate the significant differences which exist today.

Concluding the analysis of the mobile sector, allow me to give you some details on the outcome of the recent UMTS tender. The National Communication Authority has granted three technically rather equivalent frequency blocks to the existing three mobile operators for a period of 15 years. T-Mobile Hungary won the so called "A" block, which is a UMTS only licence. The license fee will be net 17 billion forints in total, of which 5.5 billion forints were paid in December 2004. A second instalment of 6 billion forints is due in June and the remaining amount in December 2005. Coverage obligations include the launch of the service in central Budapest by January 1, next year and to reach 30% population coverage by January 1, 2008. The related asset based capex is forecasted to be around 15 billion forints in 2005. It will certainly take some time for UMTS to generate significant demand, and in the first years, revenues will be mostly offset by operating expenses, mainly network support fees. However, with a broader rollout and an anticipated fall in handset prices, the service is expected to generate a positive margin in a few years' time.

T-Mobile Hungary will continue its balanced focus on keeping high profitability and preserving its leading market share. We expect slight growth in revenues from value added services, while on the expense side, – given the high market saturation – total acquisition costs are expected to decrease. In addition, T-Mobile will implement major cost cutting initiatives to further increase the profitability of the segment including renegotiation of contracts, a growing focus on e-procurement and decreased marketing expenditure.

(Pause)

I would now like to say a few more words on MakTel, our Macedonian operation. The macroeconomic situation remains difficult, with no signs of recovery as yet. Foreign direct investments are very low, GDP per capita is approximately 2,500 dollars with low growth rates, and the unemployment rate is stagnating, and is still as high as 37%.

As a result, the company continues to suffer from limited revenue growth potential. Revenues decreased slightly, by 2% year-on-year, with increasing mobile revenues offset by lower fixed line revenues. On the cost side, in line with the framework of the restructuring program, MakTel's headcount was reduced by 756 last year resulting in a severance payment of 3.3 billion forints. As a result, reported EBITDA margin was 49.1%, while before restructuring charges the figure stood at 54%.

MakTel's fixed segment revenues fell in 2004 due to mobile cannibalisation, the unfavourable development of the peak and off peak usage mix and some usage drop mainly attributable to domestic tariff rebalancing in July 2004. International traffic revenues also stood lower than in 2003. This was mainly attributable to decreased tariff levels and increased mobile substitution in outgoing calls as well as illegal competition driven voice-over-IP and a reduction in incoming traffic revenues as a result of lower average settlement rates. On the positive side, demand for internet services has increased and internet penetration in Macedonia is approaching 5%. MakTel has a strong leading position in the dial-up market, and still remains the only ADSL service provider.

Liberalisation of the fixed-line segment will start this year, the new telecom law will be in line with the New Regulatory Framework of the EU. Following the liberalisation, new services like carrier selection, unbundling and number portability are expected to be launched gradually. Based on the current draft version of the law, MakTel anticipates increasing competition, especially in long distance and international calls.

The Macedonian mobile market is continuously gaining ground, penetration reached 49% by the end of 2004. MobiMak's subscriber base grew by 44% year-on-year, the company has managed to preserve a strong leading position with 76% market share and mobile revenues also increased. Revenue based market share was even higher as MobiMak has a larger portion of post-paid customers and a significantly higher market share in the business segment than its competitor, Cosmofon.

The future profitability of the MakTel Group is expected to be driven by further revenue growth in mobile while fixed-line revenue generation will be affected by liberalisation and mobile substitution. However, on the cost side, the restructuring program and additional cost-cutting initiatives will help to improve efficiency. As a combined result, we expect to maintain the high profitability of the company.

(Pause)

And now, I would like to hand over to Elek.

Elek Straub remarks

Thank you, Klaus.

Having gone through the analysis of Matáv's 2004 performance, let us now look at our targets for 2005. In line with our strategic announcement we expect low single digit revenue growth and an above 40% EBITDA margin before restructuring charges and potential acquisitions such as Telekom Montenegro. As for gross additions to tangible and intangible assets, we target a maximum of 105 billion forints excluding potential acquisitions, which includes UMTS expenditure of roughly 15 billion forint in 2005.

As announced in our mid-term strategy, Matáv Group's priority remains growth through further value-enhancing acquisitions. I am pleased to say that following the submission of our bid for the privatisation of Telekom Montenegro last December, Matáv was chosen to enter into exclusive negotiations to acquire the company. Upon conclusion of the share purchase agreement, we intend to acquire the company for a maximum price of 165 million euro offered for the 100% stake. Financial closure is expected to take place in the first half of 2005, and the acquisition will mainly be financed from debt. We anticipate that this acquisition will enable Matáv to create further growth opportunities for our shareholders in line with our mid-term strategic targets.

Let me draw your attention to the fact that although the potential acquisition of Telekom Montenegro, the restructuring charges as well as the UMTS license fee and service launch will temporarily reduce the free cashflow of Matáv, this will not result in a change in our dividend policy. The 2004 dividend payment to be proposed by the Board of Directors to the Annual General Meeting will be published in the second half of March. The General Meeting will make the final decision on April 27th and the payment of the dividend is expected to start in the first week of June.

Let me conclude with an important milestone, which will have a significant imprint on this year for the Group, the name change of Matáv. Following a positive perception of the rebranding of Westel to T-Mobile Hungary, on January 20th, the Board of Directors made a conceptual decision to rebrand Matáv as Magyar Telekom and continue its operations under the global T-brand structure, with the General Meeting due to make the final decision on February 22nd. The rebranding is expected to have a positive impact on Matáv's competitive positioning in the Hungarian market. Deutsche Telekom will bear the direct operational expenses related to the rebranding. The name change does not signify any intention to change the ownership of Matáv, with Deutsche Telekom remaining the 59% owner of the company.

(Pause)

That concludes the formal part of Matáv's conference call. I would like to inform you, that the transcripts of our conference calls will be available on our official website.

Now we are happy to open the floor for questions. Operator, when you are ready, we will take the first question.

(Take questions)

I believe we have time for one more question.

(Take final question)

This is all the time we have. If there are follow-up questions, I encourage you to contact our Investor Relations Department. The telephone number is +36 1 458 0437 or if you want to send an e-mail you can address it to investor.relations@ln.matav.hu.

Thank you again for joining us today, and for your continued interest in Matáv.