

First quarter 2008 Results Conference Call

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Conference call operator introduces call

Chris Mattheisen remarks

Good afternoon, ladies and gentlemen and welcome to Magyar Telekom's first quarter 2008 results conference call. I am Chris Mattheisen, Magyar Telekom's Chairman and Chief Executive Officer and I am hosting today's call together with Thilo Kusch, our CFO and member of the Board.

We are pleased to announce strong first quarter financials for 2008, with revenue growth of 1% and EBITDA growth of 9%, compared to the same period of last year. Even excluding the severance expenses accounted for last year and the investigation related costs, underlying EBITDA was up by 4% and the margin reached 43% in the first quarter. The high margin shows that our efforts to reduce costs and increase efficiency through headcount reductions and simplification of the organizational structure are gaining ground.

The large-scale headcount reduction program announced last year is progressing to plan with end-March Group headcount down 11% on the end-June 2007 figure. This means that we have already accomplished about 70% of our targeted 15% headcount reduction by year-end this year. Accordingly, positive effects of these cost savings and efficiency improvements are evident in our employee-related expenses and other operating costs.

However, in addition to the cost benefits as a result of the headcount reduction, profitability in the first quarter was also helped by some real estate gains. At Makedonski Telekom the sale of Montmak, a company which owns and operates a beach hotel facility in Montenegro, resulted in a significant gain. In Hungary, real estate sales also exceeded last year's level resulting in an improved margin at the Group Headquarters segment. All in all, due to these gains, EBITDA improved by 2 billion forints in the first quarter compared to the same period last year.

Before continuing with the segmental analysis, let me also mention that our Annual General Meeting held on the 25th of April approved a dividend payment of 74 forints per share for 2007 financials. The dividend payment will start on the 27th of May.

The increase in the dividend reflects the Group's solid financial position and strong cash flow generation last year, while our focus remains on finding value-accretive acquisition opportunities in the region.

Let me start the segmental analysis with the results of the **T-Com** segment. Revenue of the segment decreased by 3% in the first quarter this year compared to the same quarter last year due to voice revenue erosion in Hungary and Macedonia, partly offset by higher broadband revenues. EBITDA improvement was driven by lower severance expenses, a gain on real estate sales in Macedonia and of course by efficiency improvements.

Hungarian T-Com revenues were down by 5% in the first quarter of 2008 compared to the same period last year, this was driven mainly by a continued decrease in voice revenues. At the same time, due to a slowdown in the broadband market, internet revenues were up by only 2% compared to the first quarter of 2007.

To give you a little bit more detail, voice revenues actually fell by 12% in the first quarter. Key trends in this business remain unchanged with a continued decline in traffic and tariff levels, and pressure on voice revenues from cable competition, alternative operators and mobile substitution. Due to closed-user-group offers and free minutes within the network, average mobile tariff levels are already below those of the fixed tariffs. On the other hand, in the residential segment there has been a slight increase in usage thanks to discounts and flat rate packages offered.

In the broadband market we are witnessing a general slowdown in growth, as household penetration in Hungary approaches 30%. With broadband service providers trying to grab the mass market, customers are becoming more cost sensitive. In addition, our ADSL offering is facing increasing competition from new cable and mobile broadband offers. On the positive side, our cable company also benefited from the growing popularity of cable broadband offers, reaching 96,000 cable broadband customers by March-2008, a growth rate of over 40% year-on-year.

At the same time, broadband prices have been in a continuous decline and under continuous pressure. In order to tackle the changing competitive environment in the broadband market, we have introduced several new ADSL offers to foster customer acquisition and retention, and have lowered our ADSL prices by up to 25% from January 2008. We also continue to upgrade our IPTV network whilst focusing on

customer acquisition in this segment. By the end of the first quarter, the IPTV customer base reached close to 13,000 in Hungary.

On the expense side of our Hungarian T-Com business, the first results of our efforts to improve efficiency have started to come through. In addition to lower severance expenses, the 44% EBITDA margin also reflects increased efficiency thanks to the lower headcount number.

Continuing with the fixed line business in Macedonia, revenues slightly increased in the first quarter. Although mobile substitution and increasing competition from alternative operators put pressure on both wholesale and retail voice revenues, increasing internet, equipment sales and data revenues were able to offset this trend.

As a result of intense competition, Maktel's market share in international incoming traffic decreased further. In terms of international termination into the fixed network, alternative operators accounted for almost 70% of this traffic, while their market share in international traffic terminated at the mobile networks was above 40%.

We are, however, seeing continued growth in the broadband subscriber base in Macedonia. The number of customers here more than tripled compared to this time last year to over 67,000, mainly as a result of the ADSL campaign launched in September last year.

EBITDA increased by 18% and the margin reached 59% in the first quarter. The strong results were mainly driven by the sale of Montmak and lower consultancy costs. Excluding the approximately 1.3 billion forint gain on the Montmak sale, EBITDA margin was 47%.

Before moving on to Montenegro, I would like to inform you that the rebranding of our Macedonian subsidiary and the fixed line business announced in April is expected to be completed still in May 2008. During the rebranding process, new, innovative products and packages will be introduced under the T-Home brand, which we anticipate will have a positive impact on our business. All costs related to the rebranding will be covered by Deutsche Telekom.

In our Montenegrin fixed line business, internet revenues doubled in the first quarter compared to a year earlier, while voice revenues remained broadly unchanged. As a result, total fixed line revenues increased by 9%. Underlying EBITDA in the fixed line segment increased by 12% compared to the first quarter of 2007 and underlying

EBITDA margin increased by 1 percentage point to 36%. In addition to revenue growth, increased profitability was driven by lower operating expenses.

While the voice customer base in the Montenegrin T-Com business remained stable, due to decreasing usage, retail voice revenues in the first quarter declined by 5%. The drop was especially high in the international outgoing traffic, where alternative and mobile operators compete with lower tariff levels. On the other hand, wholesale revenues increased by 5% in the first quarter, mainly thanks to the higher interconnection rates for Serbian incoming calls since May 2007. Looking forward, we expect wholesale revenues to come under pressure, due to a decrease in transit traffic from the mobile operator ProMonte as a result of rerouting of most of its international traffic and the establishment of a direct link with Serbia through Telekom Serbia.

Declining retail voice revenues are more than offset by revenues generated in the fast growing Montenegrin broadband market. Thanks to our focus on ADSL and IPTV services, sales are increasing rapidly. In a year's time, our ADSL customer base more than tripled and we had more than 24,000 ADSL customers at the end of March this year. Our IPTV service continues to attract high customer demand; at the end of the first quarter the number of subscribers exceeded 9,000. In addition, more and more customers are subscribing to high-end packages and using our video-on-demand service.

Let me now hand over to Thilo who will provide further details on T-Systems and T-Mobile segment results.

Thilo Kusch remarks

Thank you, Chris.

Good afternoon everybody!

Let me continue with the results of our corporate segment. **T-Systems** revenues increased by more than 5% in the first quarter of 2008 compared to the same quarter last year. Revenues from our IT and system integration business more than offset the revenue decline in our traditional voice business. In addition to revenues, our profitability was also very strong in the first quarter. Underlying EBITDA increased by 20% and the margin reached 27%. Although our first quarter financial performance was very strong, for the full year we expect more balanced revenue growth and

profitability. We believe that last year's underlying EBITDA margin of close to 20% is a sustainable level for 2008.

Looking at this in a bit more detail, we continue to experience a significant decline in traditional fixed line voice revenues among corporate customers. This is driven mainly by mobile substitution as average mobile tariff levels in the business segment is around 40% lower than fixed line tariffs. In addition, cable operators have started to promote their offers for business customers.

On the other hand, in our IT and service integration business, our revenues increased by 18%, which reflects organic growth. T-Systems realized several big projects in the first quarter, mainly network upgrades and data warehousing projects for leading Hungarian banks. Despite the strong first quarter growth rate, we expect IT and system integration revenues to show a more balanced growth for the full year, but nevertheless exceeding the expected market growth rate of around 6%.

Thanks to the simplified and integrated structure of T-Systems in place since the beginning of this year, we introduced five new bundled products for our corporate customers, and set up a dedicated team to serve our TOP 30 customers supporting the full range of our services.

Having gone through the analysis of the T-Com and T-Systems segment, let us now look at the results of the mobile operations. Revenues of the **T-Mobile** segment were up by about 2%, driven by the international operations, as revenues in Hungary were almost flat. On the EBITDA level, the 3% improvement was driven by higher efficiency levels in Hungary and Macedonia, partly offset by competitive pressure in Montenegro.

Revenues at T-Mobile Hungary showed a moderate increase in the first quarter as higher voice retail and value added revenues were almost fully offset by the lower wholesale and visitor revenues. T-Mobile Hungary's mobile termination rates have been reduced twice since the beginning of last year: first in February 2007, and then from January 2008, each time the reduction was 15%, resulting in lower wholesale revenues. Another regulatory restriction which affected our financials relates to the lower EU roaming tariffs introduced in September 2007, which have a negative impact on our roaming and visitor revenues. On the other hand, lower mobile termination rates decreased voice related outpayments and the decreasing

asymmetry supported the overall profitability. This was coupled by lower severance-related expenses and resulted in a 43% EBITDA margin for the first quarter.

Regarding the Hungarian mobile market, penetration continued to expand at a slower pace reaching 112% by the end of March, with the strong competitive landscape remaining unchanged. T-Mobile Hungary maintained its market leading position with a market share based on the active customers of around 45%.

In terms of average revenue per user, we saw the same trends as in the previous quarter: the higher usage and improving customer mix could not offset the declining average per minute rates or the lower mobile termination fee and subscriber roaming tariffs. In addition, a considerable part of the 10% customer base increase has come from double or triple SIM cards with very low usage, which is a main driver behind the increasing inactive ratio and accelerating ARPU erosion.

In mobile broadband, which is an important area of growth for Magyar Telekom, the number of customers exceeded 164,000 by the end of March this year. T-Mobile Hungary's HSDPA network is already accessible in 143 cities with 55% population based coverage. Due to the improving quality of the mobile broadband network and the attractive offers, we already see signs of mobile broadband becoming a competitive product for ADSL and cable broadband. According to our latest surveys, however, only around 15% of the new mobile broadband subscribers have migrated from other internet connection sources to mobile internet.

Turning to Macedonia, the penetration growth in the mobile segment accelerated due to the entrance of the third mobile operator, exceeding at the end of March 2008 96%,. Although the SIM card-based market share of T-Mobile Macedonia decreased to 61%, the company continued to maintain its clear market leadership position.

Despite the intensifying competition putting pressure on ARPU with lower tariffs, revenues of T-Mobile Macedonia grew by 11%. The 27% increase in the customer base, the higher usage and the favourable customer mix offset the negative impacts of the lower tariffs. The revenues were also helped by higher voice wholesale revenues and value added services driven by the higher SMS usage. Although the larger subscriber base of all three mobile operators increased the voice-related payments and the higher postpaid gross additions drove equipment costs up, EBITDA increased by 6% with an EBITDA margin of 52%.

Moving on to Montenegro, mobile revenues were up by 15% in the first quarter compared to the same quarter last year, driven by the 35% increase in the customer base. However, due to the very intense competition and higher mobile termination rates, EBITDA declined by 25%. The new third mobile operator continued its very aggressive marketing campaign in 2008, resulting in price pressure and rapidly growing handset subsidies. As a result, the EBITDA margin was 18% in the first quarter of 2008.

Mobile operators' aggressive marketing strategy resulted in strong growth in the Montenegrin mobile customer base. Based on data reported by the Montenegrin Telecommunications Agency, mobile penetration was close to 180% in March 2008, while T-Mobile had a market share of 34%. Thanks to our promotions, we have stabilized our market share in a very competitive market. Due to our focus on postpaid customers, the customer mix in Montenegro is improving, and with our 45% postpaid market share we remain the market leader in this segment.

Our new Web'n'Walk service was launched in January 2008, and we started to offer 3G broadband mobile internet in March 2008. We are able to offer up to 3.6 Megabit per second download speed in the capital. Looking forward we intend to further increase mobile internet penetration and customer acquisition. In addition, we are planning a rollout of our 3G network in larger cities and at the seaside.

Chris Mattheisen remarks

Thanks Thilo.

That concludes the formal part of Magyar Telekom's conference call. We are now 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)

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@telekom.hu. I would like to inform you that the transcripts of our conference calls will be available on our official website.

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