

## Conference call operator introduces call

### Elek Straub remarks

Good afternoon, ladies and gentlemen and welcome to Matáv's conference call for the first nine months of 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 Czenthe, Head of Investor Relations are also here with me today.

Let us begin with a brief overview of Matáv's performance in the first nine months of 2004, after which we will provide you with more details on our three reporting segments. We will then take you through the details of our headcount reduction plans and also say a few words about the privatisation of Telekom Montenegro. Following that, we will of course be happy to take your questions.

We announced today our financial results for the first three quarters of 2004 with broadly stable Group revenues and an above 40% EBITDA margin. We achieved continuing growth in the number of ADSL customers, in line with our plans. T-Mobile Hungary preserved its leading position with a 47.6% market share. Year-to-date mobile revenues increased by 4% while the EBITDA margin reached close to 40%, despite the intensifying competition. MakTel, our international subsidiary, also performed in line with our expectations in a difficult market environment, generating broadly stable revenues and a 53.5% EBITDA margin before the restructuring charges. As a result of these achievements, we are maintaining our public targets and guidances for 2004.

(Pause)

This year's regulatory changes led to more intense competition in practically all our markets. However, Matáv has also taken an active role in shaping the competitive landscape. As you may remember, in preparation for increasing competition and in order to reverse line erosion, we introduced a residential package called XL at the end of last year, allowing unlimited local calls in off-peak periods and at weekends for a supplementary monthly fee. Following the success of XL and in order to provide an attractive offer for domestic long distance callers, we introduced the XXL package in September. This is basically an expansion of XL to include domestic long distance calls for a monthly fee of around 7 euros. These packages will not only help us to keep or even win back customers but we also expect them to stimulate the usage of fixed-lines.

In conjunction with our efforts to preserve our position in all our markets, we are also launching initiatives in new areas. As carrier selection for local and Internet calls is now available, we extended our offerings on the service areas of other LTOs to include local calls from mid-September. Matáv's offers are now available for all call directions in Invitel, HTCC and Monortel areas through carrier preselection and call-by-call carrier selection, with attractive per minute fees.

The fixed-line geographical number portability introduced in January this year is certainly a threat to our business, especially for our corporate customer base. To date, however, the number of transferred lines is still low in proportion to the total lines. The proportion of ported mobile numbers has been even lower since the introduction of mobile number portability in May this year and in fact, the movement of customers has so far had a positive effect on our customer mix.

(Pause)

Let me now update you on the performance of the fixed line segment. As expected, the segment reported a drop in revenue and EBITDA due to the strengthening competitive pressure, partly imposed by regulatory changes of this year. The number of access lines fell slightly mainly due to seasonal effects in the third quarter but is expected to be back on track to reach zero line erosion in the fourth quarter.

Significant revenue erosion was caused by a 13% decline in domestic traffic revenues. This was mostly attributable to price decreases for fixed-to-mobile calls and discounted package offers. At the end of September, customised tariff packages represented the majority of the total number of lines. Our two new flat fee packages, XL and XXL, which were part of our efforts to retain customers and usage in a competitive market, prove to be very successful. Total residential minutes of use increased. However, the flat monthly fee, which offers unlimited off-peak calls in the given directions, is accounted for in subscription and other charges and therefore is not included in domestic traffic revenues. The decline in fixed-to-mobile termination fees brought in last September had to be passed onto the customers through a reduction in fixed-to-mobile tariffs, which also means lower revenues per fixed-line user. At the same time, the increased marketing spending has put some pressure on the fixed-line margin from the cost side.

Beside the price effect, traffic volume has also continued to fall, due not only to the general drop in minutes of use in the business segment but also to the loss of some heavy user business customers following the introduction of number portability. As for competition in the residential arena, the market entry of Tele2 has put a downward pressure on our revenues. Please bear in mind however that the decreasing traffic is partly compensated by the respective wholesale and interconnection revenues.

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The other main factor in fixed line revenue erosion is the drop in other usage revenues, with a 52% decrease compared to last year. As the majority of LTOs have signed interconnection agreements directly with the mobile operators, the revenue from LTOs and mobile operators has decreased. The LTO-mobile bypass is now nearly complete, resulting in a significant decrease in other usage revenues. In addition, significantly lower interconnection fees have also contributed to the decrease.

In the broadband business, ADSL has continued to gain ground in line with our expectations. The high, 22% increase in data and leased line transmission revenues is partly the result of this rapid growth and is also positively affected by the improving mix of Internet customers. As more and more narrowband Internet users tend to switch to broadband, our growing Internet revenue per user drives the rapid increase of data revenues. This positive trend will be supported by our efforts to significantly increase the maximum speed of our ADSL packages starting mid-November, without raising monthly fees. The higher bandwidth offers will not only contribute to the fast rollout of ADSL but will also encourage customers to download enriched broadband content. In order to support this trend, new content services will be introduced shortly: the launch of the "origo.play" service, which offers music download in cooperation with Warner and EMI, will soon be followed by a new video-on-demand service. Though it certainly takes time for these services to have a sizeable impact on our revenues, we expect that with the growing interest in broadband content, these new offerings will further drive data revenues. Increasing broadband revenues will this way serve as an important driver to the achievement of our strategic target of achieving 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 possibilities 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 surpassed 354 at the end of this September and the target for the end of 2006 is to even exceed 500 fixed lines per employee.

And now, I would like to hand over to Klaus, who will continue the analysis with the other two reporting segments.

## Dr. Klaus Hartmann remarks

Thank you, Elek.

Good afternoon!

Let me start with the mobile segment. As Hungary's dominant mobile player, T-Mobile Hungary had a customer base of almost 4 million at the end of the reporting period resulting in a 47.6% market share. Mobile segment revenues grew by 4% thanks to increased voice traffic and value-added service revenues as well as equipment sales. This was offset by the decrease in operating profit mainly due to 2 expense lines: year-to-date depreciation and amortisation increased by 26% compared to the same period last year due to the write-off of the Westel brand name this year, and in parallel, payments to other network operators grew by 14% as a result of the continuous increase in the number of mobile users and the traffic of all GSM providers.

As the market approaches saturation, the intensifying tariff competition resulting in deeply discounted prices puts pressure on our service margins. Previously, Vodafone had been the most assertive player in the market but this quarter, in line with our expectations, Pannon GSM started an intense campaign and is offering a substantial periodic discount on its prepaid package until end-December as well as lowering the prepaid entry barrier to less than 10,000 forints. Vodafone has launched a similar periodic offer available until the end of January.

As a result of the postpaid price competition, all three operators launched flat rate postpaid packages this year and Pannon GSM is also promoting non-voice traffic with a 50% discount on SMS and MMS messages. The low minute rate packages have had a positive effect on traffic, with minutes of use showing some increase. However, the cheaper per minute rates resulted in decreasing ARPU levels. 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 almost 28%. Despite mobile number portability from May this year, which has had a limited market impact so far, and highly competitive tariff offers, the postpaid churn rate is still favourable. Regarding the prepaid segment, year-to-date churn increased to nearly 15% and within this period, third-quarter churn grew to almost 24%. This is mainly attributable to a technical reason, namely the expiration of the extended lifetime period of the refill vouchers. Last December, the life of the smallest face value prepaid refill was extended, bringing it more in line with competitors' offers, which resulted in some distortion of prepaid churn from the fourth quarter of 2003. The churn rate was temporarily reduced, net additions looked higher and market share was also impacted. The extended one-year lifetime of the majority of these vouchers expired in the third quarter of this year, increasing previously low churn rates without any adverse impact on cash generation.

Gross additions increased considerably in the third quarter thanks to a mix of several positive factors in the rebranding period. As mentioned earlier, our Relax packages quickly became popular and further customers were attracted by our handset offerings. T-Mobile Hungary significantly decreased the price of a few selected handsets and extended the number of handsets offered with interest free credit and no immediate payment. The high number of new customers is also a result of strong marketing throughout the year, in connection with the rebranding campaign.

Let me now continue with the regulatory aspect of the mobile market. In line with EU regulation, the National Communications Authority has begun a series of analyses affecting the fixed-line and mobile market areas identified by the EU practice. Following the analysis of the mobile call termination market, the regulator determined that all three mobile providers had a 100% market share in terms of traffic terminated in their own networks, and therefore classified Vodafone Hungary as a significant market

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power in this market. If the draft decision is approved by the European Commission, Vodafone will have to submit a cost based price calculation model for fixed-to-mobile termination fees to the regulatory authority for approval.

Concluding the analysis of the mobile sector, let me give you some details on the UMTS tender. The National Communication Authority published the invitation for bids for the utilisation rights of UMTS frequency bands at the end of August. Pre-bid consultations lasted until the 30th of September, the deadline to file the bids was the 2nd of November. Results are expected in December this year. The tender notice offers four technically rather equivalent frequency blocks for a period of fifteen years, meaning that a new player may be able to enter the market. With the rollout of the third generation network, T-Mobile Hungary will offer much more comprehensive data contents than at present, enabling the fast transmission of high quality multimedia materials. Enhanced GSM will certainly remain a predominant service for a long time ahead, and during this time, T-Mobile will provide gateways for its customers between the two technologies.

(Pause)

I would now like to say a few more words on MakTel, our Macedonian operation. The economy remains difficult, with no obvious recovery as yet. GDP per capita is approximately 2,400 dollars and the unemployment rate is now close to 40%.

As a result, the company continues to suffer from limited revenue growth potential. Revenues remained broadly flat year-on-year, with increasing mobile revenues being offset by lower fixed line income. On the cost side, restructuring charges were the main driver behind the significantly lower EBITDA margin. These are related to the 3.4 billion forint provision made in the third quarter for the planned headcount reduction of 757 employees by the end of the year. Excluding this amount, the EBITDA margin would have been above 53% for the first nine months of 2004.

In the fixed line segment, tariff rebalancing in July and the associated change in the billing system caused some usage drop. However, this is a temporary effect, and we have already seen some signs of usage recovery. 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 is still the only ADSL service provider. The PC penetration is however very low, with the majority of PCs being owned by companies.

In the mobile sector, we saw very high penetration growth in the last quarters, mainly due to the increased activity of Cosmofon. Penetration reached 44% by the end of September. MobiMak is focusing on maintaining a high share in gross additions to protect its leading position against the new entrant Cosmofon. Based on SIM cards, MobiMak's market share was 77% by the end of the third quarter. However, its revenue share is somewhat greater, thanks to the higher portion of post-paid customers and the significantly higher market share in the business segment.

As you may know, liberalisation of the fix segment in Macedonia will commence next year. The New Telecom Law, which will be in line with the New Regulatory Framework of the EU, is expected to come into force in January 2005 at the earliest. The law is currently in preparation phase and will only create a framework for the regulation; the respective decrees will most probably be finalised later next year. MakTel does not expect major changes to the current price cap regime and number portability is not planned to be introduced in the first year of liberalisation. The new services that are expected to be launched due to the liberalisation are carrier selection, unbundling and voice-over IP. Fees paid to the government may also increase. Based on the current draft version of the law, MakTel anticipates some market share and revenue loss due to the increasing role of voice over IP services.

Before moving on, I would like to mention that our indirect stake in MakTel has again increased. As we announced in October, Matáv bought Cosmotelco's stake in Stonebridge, the majority owner of MakTel. As a result, Matáv's effective ownership in MakTel increased to 51% as of the end of October.

(Pause)

Let me now conclude my part by taking you through some group level items in our financial statements. You may notice an interesting contradiction in the evolution of our net debt ratio: while the net debt level decreased by 4.3%, the net debt ratio increased slightly from 32.8% to 33.1% compared to the end of the third quarter of 2003. The reason lies in the decrease of the shareholders equity, which results from the lower retained earnings due to the outpayment of a higher 2003-year dividend mainly in the second quarter of 2004.

Since the end of 2003, practically 100% of our loans have been denominated in forints, as a result of this, net forex loss decreased significantly. This was partly offset by increasing interest expenses due to higher Hungarian interest rates. Together, net interest and other charges decreased by around 5% on a year-on-year basis.

(Pause)

And now, I would like to hand over to Elek to update you on the details of our headcount reduction and our plans in Montenegro.

## Elek Straub remarks

Thank you, Klaus.

In line with our mid-term strategic plan announced in August, we have started to implement a major restructuring program to improve the efficiency of our operations. Following a lengthy negotiation period, Matáv recently reached an agreement with the Trade Union regarding the headcount reduction at the parent company. Based on the agreement, the parent company headcount is expected to be reduced by almost 2,600 employees by the end of 2006. This will result in a headcount of around 5,500 full time equivalent employees and a fixed lines per employee ratio in excess of 500. Please keep in mind though that of the total headcount reduction, some 800 people will be employed by companies operating outsourced activities. As some of these will be majority-owned by Matáv, a portion of the outsourced headcount will be re-consolidated in these new subsidiaries. As previously announced, our current subsidiaries will see a reduction in headcount of approximately 17%. This means that at Group level, a total of around 3,750 employees will be affected.

Finally, I am happy to let you know that we will participate in the tender process for the privatisation of Montenegro Telekom. The subject of the tender is a 51% share in Telekom Crne Gore, the remaining stake will stay in the hands of private shareholders. Following the publication of the sale offer on the 18th of October and the deadline to purchase tender documents expiring on the 5th of November, we now have access to the data room until the 3rd of December and, binding bids must be submitted by the 22nd of December this year. Applicants are required to be strategic investors. We are currently studying the details of the privatisation and will decide on further action according to the terms on offer and the outcome of our due diligence. Our intention to acquire the majority share of Montenegro Telekom is in line with our strategic priority to achieve growth through value-creating acquisitions.

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](mailto:investor.relations@ln.matav.hu).

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