



# 1Q 2019 Results Conference Call

May 9, 2019 at 15:00 CET

Good afternoon everyone. I am Péter Bauer, Head of Investor Relations at Magyar Telekom. I would like to welcome you to our first quarter 2019 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 Mr. János Szabó, our CFO, who will take you through the presentation and answer any questions you may have.

Now, it is my pleasure to turn the call to Tibor to open the presentation.

*Tibor Rékasi*

Thank you, Péter. Good afternoon everybody.

Let me start with a few words on the progress we've made against our strategic priorities so far this year on **Slide 3**. During the quarter, as planned, we accelerated our fibre rollout programme. As a result, more than a million access points are reached with fiber connection. At the same time, we continued to acquire smaller cable assets, adding a further 11,000 homes to our network. By the end of the first quarter 55% of our network was capable of delivering speeds of at least 100 megabits per second. The benefits of these are also reflected in the growing number of our fixed Triple Play and fixed-mobile convergent households. By the end of March this year, 75% of our fixed households had signed up for a Double or Triple Play package, while 38% of our residential customer subscriptions were part of an FMC package.



In a continuous effort to anticipate and **meet customer needs**, we revamped our post-paid portfolio from the end of April. One of the key features we introduced is the option for unlimited, within network calls, at a slightly lower price point, enabling customers to call more than 6 million numbers free of charge. We also applied the pricing approach used in fixed and FMC services, to mobile subscriptions, offering a 15% discount to the monthly fee when a new subscription is added to an existing account.

I am also pleased to report that we have made further progress in **enhancing our operational and service efficiency**. As we concluded the headcount reduction programme announced last year, we started the rollout of our agile, cross-functional working practices, with teams structured around the customer journey. The preliminary results of these changes are very promising with processes becoming more streamlined and colleagues more willing to initiate changes and take responsibility. We strongly believe that the continued rollout of this programme across additional operational functions will allow us to increase both customer and employee satisfaction going forward.

During the first quarter, we also further enhanced our **online** sales and customer care capabilities, in an effort to increase the share of online within our channel mix. In parallel, we further increased the attractiveness of our Telekom app by introducing new features that encourage greater usage.

At the same time, we sustained the positive momentum at our North Macedonian operations into 2019. Customer numbers continued to improve, supported by bundled and fixed-mobile convergent service offerings while financial performance remained broadly stable versus first quarter of 2018.

As shown on Slide 4, in the first quarter of 2019, we continued to grow revenues at both operations. In Hungary, revenue growth was mostly driven by high demand for smart devices, along with increasing data usage. Positive trends in both fixed and mobile service revenues in



North Macedonia were amplified by the weakening of the forint against the denar, resulting in a increase in revenue year-on-year. Group EBITDA excluding the impact of IFRS 16 adoption declined 3%, driven mostly by the 3 billion forint severance expense booked in relation to the Hungarian headcount reduction programme. However, the positive trend in profitability witnessed in the previous quarters continued in both countries and mitigated most of the increase in severance expenses. At the same time, EBITDA was favourably impacted by the implementation of IFRS 16 to the tune of 5 billion forints.

Looking at the **performance against our public targets** on Slide 5, our revenue growth has slowed somewhat versus last year. We expect that growth in IT revenues will decelerate further going forward, while the expected changes in our competitive landscape in the second half of the year may also put pressure on revenue performance. In terms of EBITDA, we expect that our efforts to increase operating efficiency across the Group will mitigate revenue and gross margin pressure. Meanwhile, the lower level of Capex, excluding the impact of IFRS 16 adoption versus last year, is purely down to the different timing of investments. Our free cashflow performance during the first quarter was negatively impacted by the 11 billion forint payment for the extension of the 2100 Megahertz frequency license. Excluding this, free cashflow declined by 5 billion forints versus the prior year, mostly on account of higher outpayments to suppliers. On a more positive note, we have seen an improvement in installment receivables and higher income from real estate sales, which will support cashflow performance going forward. Supplier balances are also expected to level out for the full year 2019, allowing us to achieve our annual free cashflow target .

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



Thank you, Tibor. Good afternoon.

Starting with **Hungary** on **Slide 6**, overall **revenue increased by 6% in the first quarter**, primarily due to significant growth in equipment sales, alongside higher mobile and fixed internet revenues.

As in the previous quarter, we achieved revenue growth across all our major business lines. We maintained our focus on pre- to postpaid customer migration which also positively affected our results in the previous quarter. Growth in non-voice revenues remained strong, thanks to continued customer migration towards higher value mobile data plans. The significant increase in equipment revenues was partly driven by higher third party export sales, as well as an increase in the average value of handsets sold.

Fixed service revenue declined moderately, as the continued expansion of the broadband and TV customer base could not fully offset the negative impacts from the decline in voice usage and the higher level of discounts offered, also in relation to IFRS 15 adoption. The strong growth in equipment sales reflects the introduction of a new pricing policy towards the end of last year, which allows customers to combine equipment discounts provided in relation to separate services.

System Integration and IT revenues witnessed further growth but at a lower rate versus the very strong performance in the same period last year. Majority of the revenues were still generated from the high demand for hardware and software delivery projects, especially in the public segment.

**EBITDA at our Hungarian operation, excluding the impact of IFRS 16 adoption, decreased by 2%** year-on-year, driven by severance expenses booked in relation to the previously mentioned headcount reduction programme. In Hungary, we reduced headcount by over 5% during the first quarter. At the same time, the moderate increase in gross profit, along with the savings realised in energy and marketing expenses, mitigated the level of the decline.



Slide 7 shows the key developments in the **Hungarian mobile market**. First, looking at the overall customer base, the continuous upward trend in the post-paid ratio reflects our focus on increasing the ratio of high value customers, as well as our ongoing efforts in the pre- to post-paid migration of our customers. Such initiatives are reinforced by the yearly regulatory registration of pre-paid SIM cards as well as the more favourable data packages we offer for post-paid customers.

These positive trends have translated into a 4% year-on-year improvement in our blended ARPU. While both our pre-paid and post-paid portfolio has experienced ARPU growth, the blended figure clearly demonstrates pre- to post-paid migration as we convert existing customers onto higher priced packages.

Mobile broadband subscriber growth continued into the first quarter, with a more than 25% increase in 4G subscribers. Over 80% of our customers are now using our state-of-the-art 4G network, thanks to our continuous efforts to drive equipment sales, providing 4G handsets to customers at an attractive price. As a result, our 4G network now transmits 90% of all mobile internet traffic. This is in line with global industry trends which show that data services are currently one of the most important growth drivers in the telecommunications sector. At Magyar Telekom, overall mobile data usage in the first quarter is up by 66% year-on-year. The gap between average data usage of non-4G and 4G customers continues to grow, with 4G subscribers now using more than five times the data of non-4G customers.

On Slide 8 you can see how our fixed segment performed. The first chart shows the continued growth in our two most important business lines - Broadband and TV, where we have managed to expand our customer numbers again in the first quarter of 2019. The decline in the size of our fixed voice customer base continues, in line with global industry trends. However, the growth in customer numbers within our **fixed segment** was supported by the expansion of our triple play subscriber base. In the first quarter we managed to grow both our Double Play and Triple Play customer base, as well as our total number of customers. This is a key factor in our fixed segment



strategy where, as you can see, there is visible ARPU growth with customers using more products as well as a decline in churn levels. In this quarter we grew fixed line ARPU across all of our multiplay categories, and with the growing percentage of our Triple Play customer base, our Blended ARPU has grown over 3% compared to the first quarter of 2018. However, with competitive pressures increasing, we experienced a slight decline in ARPU levels of our individual product lines.

**Slide 9** shows the developments in the **Hungarian System Integration and IT segment**. In the first quarter, we witnessed further growth in revenues, again mostly fueled by hardware and software deliveries, primarily in the public sector. At the same time, with the growing infrastructure base, we are now starting to see the first signs of rising demand for higher margin services in the fields of System Integration and IT implementation, which we plan to leverage by converting low margin hardware and software projects into higher margin service contracts. While this is equally true for both public and private enterprise customers, small and medium sized businesses continue to lag behind in terms of IT service penetration. By bundling IT services into Magenta Business packages, we now offer some attractive services free of charge to these customers with a view to increasing overall demand for IT services in the SME segment going forward.

Moving on to the performance of our **North Macedonian operations**, that is shown on **Slide 10** in local currency to better reflect underlying performance. Despite the competition on the market becoming even more intense, with Telekabel entering as an MVNO, revenues showed improvement in the first quarter of 2019 compared to a year earlier, thanks to our competitive service offerings.

In the **mobile segment**, revenue growth was primarily driven by higher data revenues and increase in equipment sales, both reflecting our continued focus on promoting mobile



broadband usage. Despite the increasingly competitive environment, we managed to further expand our subscriber base by 1% year-on-year with ratio of postpaid customers reaching over 51% thanks to our positive service quality and brand perception. At the same time, first quarter year-on-year comparison was distorted by the absence of one-off revenues related to the termination of prepaid loyalty program. The above tendencies combined led to an over 2% year-on-year increase in blended ARPU performance.

**Fixed line** also continued to perform positively, with a year-on-year 1% growth thanks to higher TV and retail broadband revenues, that could fully offset the structural decline of voice revenues and the decrease in equipment sales. This reflects the success of our bundling strategy, as number of subscribers of the double-play and triple-play packages as well as of the **FMC Magenta** offer increased further during the quarter. By the end of March this year more than 50% of our total household base did sign up for an integrated fixed-mobile plan. To promote further the sale of such packages we have introduced new add-ons, such as the advanced router option and smart-home services. We expect these to further support the expansion of digital services.

**System integration and IT** revenues declined by 15% year-on-year in the first quarter of 2019, caused by a temporarily revenue decrease in customised solutions projects but slightly compensated by increased revenue form cloud computing. Going forward we expect the declining trend to reverse and reach year-on-year increase is IT revenues.

**EBITDA** of the segment declined moderately as revenue increase and savings in employee related expenses were offset by higher costs related to equipment sales and lower other operating income. Looking forward we expect that we will be able to offset the adverse impacts of intense competition on profitability and deliver EBITDA improvements.



*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.*