Q4 2021 Results Conference Call

February 24,2022

Good afternoon everyone. I am Diana Várkonyi, Head of Investor Relations at Magyar Telekom. It is my pleasure to welcome you to our fourth quarter 2021 results conference call.

Please note that today's presentation is also available on the Investor Relations section of our website. This event is being recorded, but the recording will not be redistributed outside Magyar Telekom. By joining the presentation, you give your consent to being recorded.

Throughout the presentation your lines will remain muted and once we have commenced the Q&A session, you will be able to ask a question using the "raise hand" function, after which your microphone will be open and you can unmute yourself to ask a question.

Before we start, I would like to draw your attention to the disclaimer on the second page of the presentation. 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 Ms. Darja Dodonova, our CFO, who will take you through the presentation and answer any questions you may have.

It is my pleasure to now hand over to Tibor to open the presentation.

Tibor Rékasi

Thank you, Dia. Good afternoon everybody.

Let me start by highlighting the progress we have made in each of our key strategic focus areas during 2021, as set out on **slide 3.**

First, we continued to pursue our goal of providing seamless connectivity to all our customers and completed the largest ever annual extension to our fiber network with over 400 thousand new access points added during 2021. Thanks to these efforts, we can now reach over 3 million households and businesses with our gigabit capable fixed network in Hungary. Customer satisfaction is clearly demonstrated by the significant increase in customers who opted to connect to the fixed network via these technologies. This is reflected by our fixed broadband and fixed TV market shares that continued to increase constantly throughout 2021.

With regards to the mobile infrastructure, our RAN modernization project progressed as planned with over one thousand base stations modernized by year-end, enabling us to provide increased capacity for around 40% of the population in Hungary. With mobile data usage continuing to rise sharply, reaching a rate of over 30% throughout 2021, this service is clearly in demand. Despite this strong increase in dataload, the quality and reliability of our services was maintained, something which was highly valued by our customers, with customer satisfaction scores, measured by the TRIM index, continuing to increase throughout the year.

In addition, the global mobile network ranking of the independent body, Open Signal, recently listed our network as a "global high performer" in 3 of the 6 categories, recognizing its competitiveness worldwide and also naming it the "best Hungarian mobile network" in 6 out of 7 categories.

Furthermore, while these investments in our networks are vital to providing the service level users are seeking, they are also major contributors to our efficiency enhancing goals. The technologies we have implemented ensure higher reliability, require much lower maintenance and fewer repair works and allow for more efficient energy usage, a crucial factor in light of surging usage levels and the sharp rise in global energy prices. These, coupled with other cost optimization measures, allowed us to deliver savings of 4 billion forint in indirect costs.

I would also like to draw your attention to our most recent sustainability efforts, with the CDP awarding a 'B' climate change score to Magyar Telekom and also naming us a CDP Supplier Engagement Leader with a SER score of A.

Slide 4 briefly summarizes our financial performance against 2021 guidance, with further details on actual performance shown later in the presentation. The factors I just mentioned, such as our commercial momentum and successful network monetization, allowed us to deliver year-on-year revenue and EBITDA after leases growth of 4.0% and 6.7%, respectively, ahead of our 3.0% target for the year. Our strong investment in the business, coupled with similar intensive investment uptake at our subsidiary in North Macedonia, is reflected in moderately higher Capex versus our initial targets. This, together with temporary unfavorable working capital developments, resulted in a lower-than-expected free cash flow of 56.2 billion forint.

Turning to our fourth quarter operational performance in more detail, let me outline key developments in the Hungarian mobile market, as summarized on **slide 5**.

The number of total SIM cards increased further, driven by continued expansion of our postpaid customer base, and also boosted by pre-to-post migration and higher machine-to-machine SIM card numbers. At the same time, the uptake of our mobile data plans has continued at pace, with the number of mobile data subscribers reaching over 3.6 million by the end of the year.

These positive trends, along with a strong rise in data usage levels and positive roaming revenue trajectories, led to positive ARPU development across all customer groups, with blended ARPU growing by over 4% year-on-year.

Favorable trends also continued in Hungary's fixed market, as shown on **slide 6**. Thanks to our customer-focused servicing approach and our efforts to provide prompt responses to our customers' constantly changing circumstances, we strengthened our position as the leading fixed service telecommunication provider in Hungary. While outperforming the market both in terms of fixed broadband and Pay TV customers, we also achieved increases in the ARPUs of these service lines, clearly reflecting customers' growing preference to the services offered on our gigabit networks. This strong demand for our high bandwidth broadband packages, combined with the success of our more-for-more pricing strategy, led to a more than 8% year-on-year increase in broadband ARPU. In addition, we were able to reverse the trend in TV ARPU development in 2021, achieving an increase of almost 2% year on year. We did this by successfully identifying and catering to changing customer habits by offering them services that meet these needs, such as additional HD channels, android based TV platform and the ability to simultaneously enjoy different content in the same homes using multiple set-top-boxes.

With regards to voice market developments, with the easing of pandemic-related restrictions, temporary increases in voice usage have reversed. Although the ratio of flat package subscriptions among residential customers is high and therefore has only mild implications for our financials, the reduction in corporate usage unfavorably impacted voice ARPU levels.

With that I'd like to hand over to Darja to take us through the financials in more detail.

Darja Dodonova

Thank you, Tibor. Good afternoon everyone.

Let me start with the major drivers of our quarterly and annual revenue performance, as shown on **slide 7**. The primary contributor to revenue growth in both periods was sharp growth in mobile data revenues, fueled by increasing data usage and expanding customer bases in both countries of operation. This, together with stronger mass SMS revenues in Hungary, offset the moderate decline in mobile voice retail revenues, resulting in overall rising mobile service contribution. As Tibor mentioned earlier, higher fixed service revenues were driven by increases in broadband and TV revenues, compensating for lower voice revenues.

With regards to equipment revenues, a year-on-year increase in the fourth quarter of 2021 was driven by stronger sales results at the Hungarian operation, as well as higher quarterly export sales to third parties in Slovenia, later levelling out on a full year basis.

SI/IT revenues in the fourth quarter were once again impacted by different in-year project distribution in Hungary, as well as the absence of some high value projects in both countries that negatively impacted year-on-year comparisons. However, on a full year basis, seasonality levelled out performance and we recorded a moderate 3% decline in SI/IT revenues, the combined result of lower Hungarian and North Macedonian contribution.

Turning to **slide 8**, let me now provide some detail on our profitability, starting with EBITDA after leases. The underlying improvement in gross profit continued, driven by increasing service revenue contribution, however, fourth quarter performance was impacted by a 3.2 billion forint bad debt impairment leading to an overall year-on-year decline in the quarterly gross profit amount. The impairment was booked at the Hungarian segment, reflecting a possible deterioration of the solvency of customers expected for mid-2022, driven by unfavorable macroeconomic tendencies and the impacts of the termination of a loan moratorium. Notwithstanding, we recorded year-on-year growth in EBITDA after leases of 3.4% for the quarter and 6.7% for the full year, as the strong decline we recorded in some indirect cost categories fully compensated for the impairment and absence of profit from real estate sales, supporting performance in the fourth quarter of 2020.

As mentioned earlier, we achieved significant savings across various maintenance costs, for example related to network, IT and real estate, and were also able to cut down on energy costs and some operational expenses as a result of efficiency improvements due to our digitalization efforts. At the same time, lower employee related expenses attributable to an over 5% reduction in group headcount and year-on-year lower severance expenses also contributed to the decline in indirect cost.

Looking at **slide 9**, we can see the development of net profit for both the fourth quarter and the full year 2021. In the fourth quarter, D&A expenses rose by 7%, mostly related to shortened useful life and accelerated depreciation relating to RAN modernization in North Macedonia. We also recorded once more a year-on-year improvement in financial results. Although interest expenses increased due to higher spectrum payment liabilities and the absence of the one-off interest provision reversal at the North Macedonian operation booked in the fourth quarter of 2020, results on the measurement of derivatives at fair value improved, reflecting different shifts in the relevant yield curves. This improvement, together with a year-on-year increase in EBITDA and lower profits allocated to minority owners of the North Macedonian subsidiary due to the higher one-off D&A costs, more than offset the increases booked in D&A and led to over 26% year-on-year growth in net income for the quarter.

Similar trends drove net income development for the full year, with even more pronounced EBITDA improvements and better financial results, the latter also supported by the absence of negative FX impact weighing on the 2020 results following considerable weakening of the forint in Q1 2020. Consequently, reported net income for the full year 2021 rose by 39% year-on-year.

Slide 10 provides further detail on Group capital expenditures and information about our gigabit capable fixed network rollout.

Capital expenditure after leases, without spectrum licenses, increased by 3% year-on-year in 2021 to 109.3 billion forints. At the Hungarian operation we recorded lower investment levels on the fixed network capacity expansion year-on-year, reflecting the elevated levels of such investments in 2020 to ensure network capacity and quality with rising data loads as a consequence of the pandemic. At the same time, the rollout of our gigabit network continued, and by year-end we had reached over 3 million access points in Hungary, allowing for gigabit speed across 69% of our network reach. Higher investment in the Hungarian mobile network is related to the RAN modernization program where we proceeded with the project throughout the year.

Investment in our North Macedonian operation increased significantly, driven by higher spending on the local radio network modernization program. In addition, in the fourth quarter of 2021, 1.1 billion forint was invested in a spectrum license related to usage rights for 15 megahertz douplex on the 2,100 megahertz frequency band for 8 years. This, in addition to the license investments in Q1 2021 at the Hungarian operation, resulted in a total of 193.4 billion forint capital expenditure after leases for the Group in 2021.

Slide 11 presents free cashflow developments in 2021 against 2020. Operating cash flow was higher year-on-year thanks to the combined impact of an increase in EBITDA and positive changes in other non-cash items, driven by the absence of significant foreign exchange rate movements leading to FX losses in the base period. These fully offset the less favorable working capital developments, which were primarily attributable to less favorable SI/IT receivable balance, driven by different in-year project dynamics and a different inventory management strategy as a result of supply chain difficulties that led to an increase in handset balances during 2021.

However, positive operating cashflow developments were offset by lower proceeds from real estate sales and higher capex related outpayments. Although booked capex was only moderately elevated in 2021 compared to a year earlier, capex outpayments, as presented on the chart, rose by 11 billion forint due to different in-year payment distributions. These, coupled with higher lease payments, driven by an increase in the frequency usage fee and network related rental payments led to free cashflow before spectrum payments of 56.2 billion forint for 2021.

Now, let me say a few words on the 2022 public guidance and outlook for 2023-24 announced yesterday and summarized on **slide 12**. Looking ahead, we expect to continue leveraging positive commercial momentum in 2022, supported by our customer centric operational approach, tailoring services to changing customer needs and striving to offer a seamless connectivity experience. This is forecast to deliver revenue growth of 1% to 3%, with EBITDA after leases growing by 3% to 5%, also supported by further cost control measures. We intend to maintain the steady pace of our fiber roll-out and mobile network modernization program as we strongly believe network quality remains a significant differentiator for the Group. Consequently, investment levels are expected to remain broadly stable year-on-year. Free cash flow, excluding spectrum license payments, is forecast to increase to at least HUF 70 billion in 2022, thanks to positive trends in EBITDA after leases and working capital.

Looking further ahead into 2023-2024, while there are significant uncertainties related to economic and business developments, demand for telecommunications services is expected to remain strong with digitalization continuing to be of vital importance. To ensure the reliability and security of our networks and our leading market position, management remains committed to investing in our infrastructure and continuing a customer centric operational approach going forward. Furthermore, internal process simplification and digitization initiatives are expected to enable us to maintain efficient operation. As a result, we expect to be able to maintain a growth trajectory both in terms of revenue, EBITDA after leases and free cashflow in that period.

Last but not least, let me say a few words about the Board of Directors' shareholder remuneration decisions and proposal. After careful consideration of the results and outlook of the Company, as well as received shareholder views, the Board of Directors believes that given improving profitability and free cash flow generation, a year-on-year increase in total shareholder remuneration of up to 29.6 billion forint is justified.

Consequently, it proposes for approval at the Annual General Meeting a total dividend payment of 15 billion forint for the 2021 financial year. Based on the number of outstanding shares, i.e. excluding treasury shares, as of today, the dividend will amount to an equivalent of 15.05 forint per share.

In addition, the Board intends to supplement the dividend with a share buyback program with a value of up to 14.6 billion forint. At this point, the execution of the buyback is subject to necessary authorization of the General Meeting scheduled for April 12, 2022.

Furthermore, to improve transparency and visibility with regards to the Company's shareholder remuneration, the Board of Directors has decided to set a new shareholder remuneration policy for the 2022-2024 period. The policy envisages growth in annual shareholder remuneration as a combination of dividend payments and share buybacks in line with improvements in the Company's financial performance. Going forward, the total value of annual shareholder remuneration is expected to be between 60% and 80% of the Company's annual adjusted "profit attributable to the owners of the parent" i.e. adjusted net income, generated during the preceding financial year.

That concludes our presentation, I will now hand back to Dia.

Dia Várkonyi

Thank you very much Darja.

We are now happy to take any questions you may have. Please use the "raise hand" function following which your microphone will be enabled and you can unmute yourself to ask a question.

(Take questions)

Thank you again for joining us today. Please note that the transcript of our conference call will shortly be available on our website. If you have any follow up question, please don't hesitate to contact us.