

**Company:** Kcell

**Conference Title:** Kcell FY2016 Financial Results Announcement

**Moderator:** Irina Shol

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**Operator:** Good day and welcome to the Kcell Full Year 2016 Financial Results Announcement conference call. Today's conference is being recorded. At this time I would like to turn the conference over to Irina Shol, IR. Please go ahead.

**Irina Shol:** Thank you, operator. Ladies and gentlemen, good morning or good afternoon and thank you for dialling in to discuss Kcell's fourth quarter and full year 2016 results. During today's call we will go through the highlights of our business and financial performance for the reporting period, using presentation slides which I hope you have in front of you. If not, please visit our IR section on our website. Participants on the call today are Arti Ots, our CEO, Trond Moe, our Chief Financial Officer[?] and me, Irina Scholl, head of Investor Relations. Following our presentation there will be a Q&A session. And I will now hand over to our CEO, Mr Arti Ots, for his comments. Please, Arti.

**Arti Ots:** Okay, Irina, good morning and good afternoon also from my side, ladies and gentlemen, and thank you for joining our result call today. Firstly, let me start by highlighting some of the progress we made during the reporting periods as well as talking through some of the challenges we faced. To start with, 2016 was extremely challenging year for Kcell. Despite the challenges we saw also some of the signs of the market's recovery towards the end of the year and as expected overall revenue trends for the full year declined compared with the previous year. But that said, again, the fourth quarter, when revenue rose quarter on quarter making the third quarter consecutive increase. The revenue improvement though was driven by strong demand for contract phones and that said, the service revenue was slightly down. Overall, we can say that the market is – starts to improve, but it still remains very, very competitive. Our strategic network-sharing partnership we agreed a deal in Kazakhstan in 2016 August, has been

progressing very well, with both parties now fulfilling their commitments. The accelerated rollout for 4G services to our subscribers is well on track and now we cover 34% of the population with 4G services already. And also we have a significant growth in data traffic in our 4G network. And also we have very large proportion of our full traffic now in 4G network.

Also we did make a lot of technical improvements in Q4 to improve our quality both on the voice and data services side, and this is something that our customers really feel, especially in the bigger cities. Also, we fully finished the migration to our post-paid – of our post-paid customers to the new billing system, so now our customers can enjoy the enhanced functionality.

In the customer front, the fourth quarter we had increase by 81,000 subscribers, which is also already third quarter in a row where we have the positive subscriber numbers. However, we must mention that the customer growth came mainly from numerical entry level accent and that's why we don't see the impact on the revenues so significantly.

Lastly, also we need to announce that the company is currently undergoing tax inspections that cover period of 2011-2015 and I would like to stress that tax office has not been concluded yet and the company therefore has not received any official claims. But based on the preliminary assessments, we have made provision of 3.962 million – sorry, billion – tenge. Trond, later on, will answer the questions more thoroughly.

Moving to Slide 3 and 4, let's look now at the financial performance for the fourth quarter and also the full year 2016. Net take decreased by 3.5% year on year to 38.2 billion tenge in Q4 and 12.7% year on year. So the service revenue was down 8.1% and that's primarily related with the lower interconnects or driven by the lower interconnects from what we see already from first quarter this year, or last year, sorry. Data and [inaudible] revenues continue to develop quite an increase. We saw data revenue growing 11% year on year in Q4 and 5.2% year on year for the

full year of 2016, while B2B revenues were up 5.4% and close to 20% year on year respectively, so those two segments remain very strong also in Q4.

EBITDA excluding non-recurring items decline by 15.1% year on year in Q4 and 29.1% in 2016. And the EBITDA margin was 37.9% in Q4 and 39.4% over the full year.

So we can say it was very challenging year for Kcell and the market remains tough, but that said, we are seeing already number of quarters the stabilising trend on the financial results. And in today's call we actually focus very much on the revenue trends and I will pass over to our CFO, Trond Moe, who can go through more detail the financial results.

Trond Moe: Thank you, Arti, and a warm welcome from me as well, to everybody listening. On Slide 5 looking a bit closer at the revenue trends in Q4, where we are pleased to show that the net sales had a growth of 3.5% quarter on quarter. It's still a decrease year on year but you see the improvement of these numbers now for three consecutive quarters, so that is a good trend. Our service revenue broadly on the same level as the former quarter. After that we see also here that our B2B revenue actually increased by a full 19% year on year and 6.1% versus the previous quarter, so that's a good – a continued good trend on that segment.

On Slide 6 we look at revenues and the contribution to growth from our data services. We can see that in Q4 our data traffic grew by 75% year on year, and by 24% quarter on quarter. Our smartphone penetration continued to increase, reaching about 50% at the end of the last quarter. Kcell revenue was up 11% year on year, being partially offset by packages offering with lower tariffs per megabit, which led to a decrease in the average revenue per megabit.

On Slide 7 we take a closer look at our operational performance. Use increased to 245 in Q4 of 2016 compared to 229 in the corresponding quarter of 2015. Total voice traffic in Q4 rose marginally against Q3 but decreased versus Q4 of 2015. Blended RP[?] slightly decreased year

on year as average prices have decreased with more subscribers on bundled tariffs and we also see here a small RP reduction quarter on quarter. Partially this is an anti-effect[?] but also reflects some of the promotional activities in the more low-end segment of the market that Arti just mentioned. And our subscriber base, as Arti also mentioned, grew by 81,000 during the reporting quarter compared to Q3, which from one side is profiting but as I mentioned also contributed to some of the lowering of the average RP.

Then move to the financials on Slide 8, you will see a summary of the financial highlights for Q4 and for the full year 2016. I would like to focus a bit on the tax provision that Arti mentioned in the beginning. As we informed in the last quarterly call, the company is undergoing a comprehensive tax inspection that covers the period of 2011 to 2015. The tax audit has not been concluded yet and the company therefore has not received any official claims, but based on our preliminary assessment, we have now made a provision of 3.96 billion tenge, which we at this point believe is the most probable outcome of this audit.

When comparing full years here, please note that last year we had an extraordinary FX claim of 13.1 billion tenge on the positive side and extraordinary expenses mainly in the form a write-down of 4.6 billion tenge. If we remove these one-off effects, including the tax provision taken this year or last year's quarter, the underlying reduction of net income year on year is 49% and quarter on quarter, 27% reduction.

Then moving on to Slide 9, Kcell's EBITDA performance. As we have already discussed, our EBITDA and EBITDA margin decreased year on year, but the decrease is less than previous quarters and we are now on a positive trend year on year. Part of the tax provision that I mentioned on the previous slide actually impacts the EBITDA. This effect on EBITDA was 362 million tenge lost in Q4. If we remove this effect and look at the organic results, we actually delivered the best EBITDA this year in Q4, which in fact is slightly better than the guidance issued earlier.

Then on Slide 10 we can see that we delivered on our capex outlook of 25 billion tenge of normalised investments plus the 4G frequency spectrum acquisition of 26 billion tenge, which was a one off last year.

On Slide 11, dividends, I cannot, unfortunately, say too much on this call because that – this – the dividends for 2016 has not yet been decided, and as normal they will be proposed by the board of directors and approved by the AGM in March and April this year.

On Slide 12, just a small update on this data unlimited case. The only difference is that we have adjusted the amount paid out but this has been fully provisioned in the financial statement, so it has no impact as such.

One last clip, since we are now in the beginning of 2017, as normal we will give you our view on where we expect this year to end. We currently expect service revenue and EBITDA to stay flat this year, but with a possibility of a slight increase provided we get a regulatory possibility to increase prices and we see further market recovery. We expect our operational capex-to-sales ratio to stay at the low teens level for this year.

Thank you very much. Irina?

Irina Shol: Thank you, Trond. Now we are ready to take your questions.

Operator: Thank you. If you would like to ask a question, please press the star or asterisk key followed by the digit one. Please ensure the mute function on your telephone is switched off to allow your signal to reach our equipment. Again, please press star one to ask a question. We will now take our first question from Alex Kazbegi from Renaissance Capital. Please go ahead.

Alex Kazbegi: Yes, good afternoon there. Thank you for – thank you for presentation. My question is that your working capital increased also in 2016. Could you give us maybe some colour what was the – what was the reason behind it? Is it mostly handset sales that were driving it? And your outlook again, given your capex guidance you gave now, the working capital maybe outlook and possibility of Kaznet purchase, if you can also comment on that? What are the chances of that happening actually in '17? What is your view on the free cashflows for '17 and also on your net debt position with this regard? Thank you.

Arti Ots: Yes, thanks, Alex. On the working capital, the – it is correct, as you assume, that we are increasing the sales of handsets on instalment basis this year. So this path of course leads to a worsening of working capital, as we receive the cash after 12 or 18 or 24 months for this type of our subscribers. But also included in our cashflow is our blended financing, where we have now one year payment delay on certain equipment, mainly from Ericsson, especially the 4G roll out. So that improves the cashflow somewhat.

And on the debt level, we are now at the higher end of the net debt-to-EBITDA ratio, close to or around 1.0. So we will try not to go much higher than that. Funding is largely available now in Kazakhstan, so the main focus on the debt side is now to replace shorter term or expensive debt with somewhat longer and cheaper facilities.

Alex Kazbegi: So if I correctly understand that, I would assume that with your flat EBITDA guidance and pretty much probably similar capex, you would expect some improvement in the working capital and I guess the dividends – you know, you're not counting the dividends yet because you don't – you cannot focus them? That would be the view under which –

Arti Ots: Yes. Your assumption is correct.

Alex Kazbegi: Okay, so then less handset sales, basically, as well, probably?

Arti Ots: Sorry, can you repeat, Alex?

Alex Kazbegi: I said, less handset sales conversely as well?

Arti Ots: No. We have increase in handset sales.

Alex Kazbegi: You will. Okay. So it's just a rollover so working capital will not really stretch more than that?

Arti Ots: Yes. So we have an increase in handset sales so that worsens the working capital, so working in the other direction it's increased level of financing, which increases the cashflow. So overall, we should see a slight positive impact from this effect.

Alex Kazbegi: Okay, thank you. Maybe a quick second question. On your, so to say, EBITDA margin improvement predicated on the interconnect improving, are there any other areas where you could see improvement at all? I mean, your marketing increase in Q4, your SGMA grew, but that's kind of seasonal, so you don't see any more possibilities to decrease on those sides? So if any improvement will be, it's going to be through interconnect. Is that correct?

Arti Ots: Yes. We don't see any drastic changes on other issues, except on the interconnect level. So we now saw a positive interconnect balance on local calls in the summer for the first time in almost two years, so that is a trend that is positive at the moment. So, normally we should anticipate that we would be around zero on the interconnect balance. So it depends a little bit where the market will go in terms of off-net minutes included in the packages and so on. But that would be the normal level.

Alex Kazbegi: Okay, understood. Thank you very much.

Operator: Again, as a reminder, to ask a question today, please press star one. There are no further questions from the telephone.

We have another question from Anna Kazaryan from VTB Capital. Please go ahead.

Anna Kazaryan: Yes, hello. I would like to repeat Alex's question about Kaznet Media. So do you expect payments for these assets in this year? Or any news about it? Thank you.

Operator: Ladies and gentlemen, it appears we're experiencing a momentary interruption in today's conference. Thank you for your patience and please continue to hold.

Please go ahead.

Arti Ots: Yes, sorry. Arti here. Sorry, we had a small cut off. So, Ania, could you please ask your question again so we could hear it?

Anna Kazaryan: Yes. If – I missed your answer about Kaznet Media. So, do you expect to pay remaining part of the payment for these assets this year? Or do you have any news about it?

Arti Ots: Yes, thanks for the question. We don't see this happening in 2017, and the main reason, as you might recall, is that we said we will pay the remaining part of the fair market value of these frequency fees when the 4G becomes available on this frequency. So currently we don't see the progress enough with the regulator to foresee that happening in 2017.

Anna Kazaryan: And as far as I remember, Kaznet Media consolidation had negative impact on your EBITDA margin and you planned to eliminate this effect by the end of 2016. So have you



achieved your plans or you still see some upsides in 2017? Maybe you have some room to improve Kaznet Media effect on your EBITDA?

Arti Ots: So the plan is ongoing and it's actually exactly on track, so we will finish the optimisation of the network and also bringing customers to Kcell, or we have finished it by the year end. So no, it's only some technical work that we need to do in Kaznet Media and to make the company fully efficient. So definitely it will show improving tendency, have a little bit more positive impact to Kcell revenues. Sorry, EBITDA. That said, it still has somewhat impact. The fact we need to keep operations in order to keep the licences available for the future. Trond, do you want to comment more?

Trond Moe: No. We followed the plan as earlier reported exactly, so there is a slight negative effect in Q4 also but that effect should be neutralised or be completely gone during this year.

Anna Kazaryan: Thank you. And just about dividends. So, according to your policy, you plan to distribute at least 75% of net income. Will the basis for this dividend distribution be reported net income or you planned to do some adjustments on bottom line?

Arti Ots: Sorry, I didn't get the question on adjustments? What was it?

Anna Kazaryan: For example, you mentioned that there was some fixed effect on net income and so on and if we eliminate, if we adjust net income by these items we will have another dynamics of net income. So will you take as the basis for dividend payments reported net income or you plan to do some adjustments?

Arti Ots: So the policy is based on reported net income.

Anna Kazaryan: Okay. Thank you.

Operator: There are no further questions from the telephone. There are no further questions from the telephone. Please continue.

Arti Ots: Let's wait a few minutes, I guess.

Irina Shol: Yes.

Operator: Again, ladies and gentlemen, as a final reminder to ask a question today, please press star one.

There are no further questions from the telephone.

Irina Shol : If no questions, then thank you for joining our conference call. Thank you and bye-bye.

Operator: That would conclude today's conference call. Thank you for your participation, ladies and gentlemen. You may now disconnect.