



# ORANGE POLSKA Q1 2016 RESULTS CONFERENCE CALL

April 26, 2016, 11:00 AM CET

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Operator

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Good morning, ladies and gentlemen. Thank you for standing by. Welcome to the Orange Polska Q1 2016 results conference call on April 26. (Operator Instructions). I will now hand over the conference to Mr. Leszek Iwaszko. Please go ahead, sir.

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Leszek Iwaszko, Orange Polska SA - Head of IR

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Good morning everyone. Welcome to Orange Polska's results conference for the first quarter of 2016. My name is Leszek Iwaszko. I'm the Head of Investor Relations. Today we are joined by the management of Orange Polska starting from Bruno Duthoit, CEO; Maciej Nowohoński, CFO; Mariusz Gaca, responsible for the Business Market; Michal Paschalis-Jakubowicz, in charge of Marketing; Jolanta Dudek in charge of Customer Care and Bożena Leśniewska in charge of Sales. Piotr Muszyński will join us later. Our results have been published yesterday and they are available on our IR website.

I hand the floor to Bruno Duthoit to start the presentation.

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Bruno Duthoit, Orange Polska SA - CEO

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Thank you, Leszek. Good morning, ladies and gentlemen. The agenda for today is as follows. I will begin with highlights of the first quarter, financial and commercial and progress on our investments in connectivity. Maciej will follow with the financial review. Finally, I will conclude the presentation before opening the Q&A session.

Let's start with the introduction on slide 5. Our financial results in the first quarter were in line with our internal plans. We had much better customer additions in mobile, but our commercial expenses were lower. Top-line erosion was slightly lower than in Q4 thanks to better mobile.

Our restated EBITDA is on track with our plan, so we can reiterate our full-year guidance. Cash flow generation was impacted by payments to CapEx vendors as a consequence of big CapEx in Q4 2015. The results of our commercial actions were excellent which we present on the next page. In line with recently announced strategy, we continued strong commercial push in Q1, with great success especially in mobile. Our total mobile customer base increased by more than 2% in the first quarter.

Post-paid continued its very strong growth pace for another consecutive period. Over the last four quarters, we gained 130,000 net post-paid customers from our competitors. We continue to capitalize on family offers launched in Q3 2015 supported by promotional activities and effective communication. In fixed business, we are pleased with growth of our high speed broadband services. Net additions in Q1 were the highest ever, also thanks to gradual growth of fibre customers. On the next page, we show highlights of recent commercial actions.

On this slide we put a few examples of our ongoing marketing actions. We mainly focused on convergence and fibre which distinguish us from the competition. As you know, in February we launched new TV offer based on own aggregation of content in IPTV technology. It give us higher flexibility in the creation of TV product and enables development of additional services in the future. In the current promotion, fibre broadband with a speed of 300 MB/s and almost 100 TV channels is available for our customer for PLN80 a month.

Our most attractive convergent family package costs PLN164. It includes seven services, three fixed and four mobile. Within that are unlimited mobile and fixed call, 30 GB of mobile data and a package of roaming calls and data.

In March, we launched a new offer for small businesses. It is the first convergent hard bundle offer on the Polish market. It consists of fixed Internet access and two unlimited mobile voice SIM cards. It is priced at PLN85 which makes it the most competitive bundled offer in the market. We believe it sets a new standard. In the nearest future customers will be purchasing many such kinds of bundles. First commercial result are very promising.

Let's now look at our progress on the connectivity front, starting with fixed.

In the first quarter we added another 100,000 households to our FTTH network. Investment were continued in 16 cities all around Poland. In the next quarters, in line with our plans, investments will accelerate.

We confirm our full year target to add around 800,000 households this year. FTTH customer base increased by 10,000 in Q1. We plan higher quarterly take-up rates in the next quarters along with our promotional activities and growing experience of our sales force. In line with the strategy, we announced in February, we developed supporting technology that will help us to commercialize fiber network. In particular at the end of Q1 we started to offer in Warsaw fiber service based on MoCA, (Multimedia over Coax Alliance) technology. This technology allows to use concentric cable on last meters of installation if there is no possibility to put fiber directly in the customer apartment.

In a moment, you will hear us commenting on growth in mobile data usage. However, data usage also grows strongly in fixed network as you can see on the slide. This makes us absolutely confident that mobile-only network is not sufficient. Fast fixed network is necessary to digest demand for data and at the same time provide good customer experience on LTE.

You can see -- let's turn the page. You can see from the data on the slide that the growth rate of mobile data usage per user doesn't slow down. It continues to double in year-on-year terms. On top of that the number of smartphones keeps on increasing at a rate of around 20% year on year. To accommodate this booming traffic, we develop our LTE coverage and capacity based on the newly purchased spectrum.

LTE based on the 800/2600 megahertz frequency have been activated on over 200 base stations at the end of Q1. As of today it is already more than 300 base stations. Outdoor population coverage has approached 90% and indoor 70%. Already close to 50% of the data traffic in our networks goes through 4G.

Thank you very much. Now Maciej will walk you through the financial figures.

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Maciej Nowohoński - Orange Polska SA - CFO

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Thank you, Bruno. Good morning, everyone. Let's start the financial review on page 11.

Overall quarterly revenue trend was slightly better than in Q4 and was in line with our expectations. Fixed to mobile substitution and ADSL challenges stand behind fixed revenue evolution. We do no more infrastructure projects.

ICT revenue is strongly project-based and depends on timing of large projects.

Mobile business performance improved in Q1 thanks to strong customer base take-up and equipment sales.

Let's now look at mobile revenue in more detail on the next slide.

As Bruno already mentioned, Q1 was another very good quarter for us in customer acquisition. During past 12 months we have expanded our postpaid customer base by almost 850,000. Please remember that it was achieved in the environment of persistent and strong competition.

Significant portion of these acquisitions and retentions include handset purchase in instalment model which is prevailing market trend now in Poland. Financial consequence of this is that equipment revenue from such instalment contracts are recognized upfront at the moment of the contract is signed. This largely explains why performance of our reported mobile service revenue is not improving despite much higher number of customers.

Mobile ARPU trend in Q1 has deteriorated and one of the main reasons is growing base of customers with instalment offers. ARPU is diluted also by other factors including also growing number of customer with SIM-only contracts, family offers, convergent discounts and higher proportion of dedicated mobile broadband SIM cards in overall customer base. In the coming quarters, we expect further significant growth of mobile equipment sales.

Looking forward, please bear in mind that the Polish government is considering introduction of obligatory registration of prepaid cards users as a part of anti-terrorist activities. The draft regulation has just been published and we are analysing it. We do not know at this stage if the draft is the final version. Once we know more details we will work on appropriate actions and measures.

Let's now turn to fixed broadband on slide 13. In line with the strategy, our activities in fixed broadband are focused on connectivity improvement and market win-back in big cities, and on protection of our customer base in small cities and rural areas.

Actions in the first area progress well. Net additions to our fast broadband activities in Q1 were the highest ever. Two-thirds of the fibre customers acquired in Q1 were new clients for Orange Polska.

Outside of big cities, our customer base continues to be under pressure mainly from substitution to mobile technology. We are developing technical solutions and commercial actions to counteract, but it takes time before these bring effective results.

As you remember, we reduced prices of our broadband services in June last year by 10% to 20%. This gradually affects our ARPU level, but this effect is quite small relatively to the scale of price reduction thanks to effective bundling.

On the next page, we comment on fixed voice. In Q1 loss of fixed voice lines was similar to Q4 and slightly lower than in Q1 of last year. This is despite post-paid mobile services get more and more affordable and also despite marketing activity of competitors regarding wireless local loop.

One of the reasons is effective bundling. Already close to 20% of fixed voice services are in convergent bundles and the ratio keeps on increasing every quarter.

That concludes the review of our top line. Now let's turn to EBITDA on page 15. In Q1 we delivered around PLN870m of EBITDA. It decreased less than revenues. This means that our overall cost base was down. Cost evolution in Q1 reflects the pattern presented in our strategy, growing direct costs and optimization in indirect categories.

Direct costs were up only due to growing interconnect. Commercial spend, the largest component of direct category, was down year on year despite 4 times better net customer additions in postpaid. That is because compared to last year we increased the share of SIM-only sales acts especially in retention.

Results of our savings initiatives are visible mainly in labour, network and IT categories. In addition to cost savings, labour expenses in Q1 were also positively impacted by provision reversal following renegotiation of long-term employee benefits.

Let's now look at net income. Net income amounted to PLN98m in Q1 versus PLN171m a year ago. This evolution reflected lower EBITDA and higher financial costs following payments for new spectrum in February. These effects were partly mitigated by lower depreciation. Amortization of new spectrum was offset by positive effects from extension of useful life of some assets.

On slide 17, we review cash flow. In February when we commented Q4 results, we indicated that due to accumulation of CapEx at the end of last year, payments for the vendors will shift into Q1. This is what in fact happened. Our cash CapEx in Q1 amounted to more than PLN700m and was PLN185m higher year on year. This largely explains negative cash flow generation in the first quarter.

On the positive side, cash flow was helped by lower requirement for working capital. I mentioned earlier our expectations for significant growth of mobile equipment revenues that should result in further increase in receivables in quarters ahead.

Let's conclude the financial review taking a very quick look at our net debt on the next page. Following LTE spectrum acquisition, our net debt exceeded PLN7b at the end of March. Our net debt to restated EBITDA ratio is at 2.1. The leverage guidance is unchanged. We expect it to be not higher than 2.2.

Cost of debt was down in Q1 to 3.7% effectively and we expect further small cut in Q2 onwards.

Ladies and gentlemen, thank you for your attention. This concludes the financial review and I hand the floor back to Bruno.

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Bruno Duthoit - Orange Polska SA - President and CEO

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Thank you, Maciej. Our excellent commercial result in Q1 and in the first weeks of Q2 make us believe that the good appetite for our mobile offers will continue even though some competitors are visibly increasing their marketing activity.

We need to further improve performance in fixed which should be facilitated by more attractive offers supported by marketing activities, local approach and growing experience of our sales force. Our performance is on track with our plans and we reiterate our full year EBITDA and leverage guidance.

Taking a more long-term strategic perspective, I would like to stress that the position of Orange Polska in the Polish market is now better than it was one year ago. We have much more mobile customers, gaining market share from competition. Perception of Orange in the eyes of customer has significantly improved. We are able to offer our customers a much better connectivity both in fixed and mobile.

Finally, we still enjoy the position of the largest convergent telecom operator in the country. I am convinced that in the longer term this positive will translate into improved financial result and bring value to shareholders.

As you know, this was my last quarter at Orange Polska. At the end of this month, I will pass my duties as the CEO to Jean-Francois Fallacher, who will further on lead execution of Orange Polska's strategy. I would like to thank Orange Polska employees for their dedication to our customers and thank our shareholders for their trust and support.

Thank you very much for your attention. This concludes the presentation. We are now open to questions. Thank you.

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## Questions and Answers

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Leszek Iwaszko - Orange Polska SA - Head of IR

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As usual we will start with the questions from the floor. Are there any questions from the floor? Yes. In English please.

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Krzysztof Spirzewski, Bank Societe Generale

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You mentioned some disturbance that may come with regulations about the prepaid cards. Would you estimate -- did you estimate it, about the income or your volumes of sales, if it's kept a) the worst scenario.

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Bruno Duthoit - Orange Polska SA - CEO  
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I think it's too soon to comment on that because as explained by Maciej during the presentation, we are waiting in fact to know the project of the government. Today there is a draft ongoing which is under discussion and who we'll see later.

What we would like that we understand very much this rule of registration because there is an increase in anti-terrorist concern and it's really a benchmark in Europe that there is no issue from fundamental. The point is to make sure that the process will be let's say, a friendly process. The process of migration will be friendly focused and we are working on that.

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Leszek Iwaszko - Orange Polska SA - Head of IR  
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Other questions from the floor? Yes.

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Włodzimierz Giller - PKO BP - Analyst  
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Włodzimierz Giller, PKO BP. I have a question regarding slide number 8, FTTH network deployment progress. You seem to be quite successful in making more households connectable. However, if you - - we are looking at customer base, it looks like only pretty few households actually buy your service.

Aren't you afraid that the development of this service is a kind of, at least for now, waste of money?

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Bruno Duthoit - Orange Polska SA - CEO  
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Maybe Bożena who is in charge of Sales B2C will answer.

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Bożena Leśniewska - Orange Polska SA - Member of the Management Board in charge of Sales & Marketing  
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Well, in fact we are selling according to our expectations. I want to bring back the information which we passed some time ago that our first wave of investment was done in the area where our market share in fixed broadband is quite low. We have there at least two competitors, the cable competitors so we expect that it will not be the big explosion. But we are constantly doing what we plan.

We expect some acceleration during the next wave of investment also because we are diversifying our investment on area where we have our customer base. At this stage, 67% of the customers acquired are totally new customers for Orange Polska.

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Włodzimierz Giller - PKO BP - Analyst  
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Thank you.

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Leszek Iwaszko - Orange Polska SA - Head of IR  
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Any more questions? If not then I suggest switch to our teleconference listeners. Operator, please.

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Operator  
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(Operator Instructions). Vibhor Kumar, Citi.

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Vibhor Kumar - Citigroup - Analyst  
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Hi. Thank you so much for the opportunity. I have two questions. The first question is on EBITDA guidance for this year. So if I compare with this quarter performance wherein adjusted EBITDA is roughly 13% down year on year and your suggestive guidance range implies 6% to 10% kind of a range for EBITDA decline. So I'm just wondering do you -- should we expect further savings on commercial side going forward? And which of cost items should witness declines so that we can expect a middle range of the EBITDA? Thank you.

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Maciej Nowohoński - Orange Polska SA - CFO  
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Vibhor, actually -- Maciej Nowohoński speaking. Actually I'm not quite catching the question. Could you rephrase in one sentence your question?

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Vibhor Kumar - Citigroup - Analyst  
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Okay. See my question is on EBITDA guidance. Your EBITDA guidance implies 6% to 10% decline year on year. But the first quarter number implies 13% down year on year. So I'm just trying to understand how you are going to basically maintain the EBITDA and which all cost items will help to basically meet the guidance.

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Maciej Nowohoński - Orange Polska SA - CFO  
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Okay, the question is about how do we do the guidance in the context of Q1. In fact, the Q1 results from the perspective of the EBITDA are slightly better than what we have expected in our internal plans. So I do not see any reason not to do the guidance for EBITDA. We have just reiterated that we will do it. So PLN3.15b to PLN3.3b remains a valid guidance. And that will be supported by the combination of our efforts to acquire new customer base on the mobile front and FTTH together with savings efforts that are visible already in Q1 in our indirect costs. So, no reason not to repeat savings in indirect at the level of PLN300m as we have done in 2015 and in 2014.

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Leszek Iwaszko - Orange Polska SA - Head of IR  
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Vibhor, and just to be correct, EBITDA in Q1 was down 9%, not -- I think you mentioned 14%.

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Vibhor Kumar - Citigroup - Analyst  
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Sorry, I'm talking about the adjusted EBITDA.

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Leszek Iwaszko - Orange Polska SA - Head of IR  
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No, no, but the guidance is on EBITDA, it's not -- it's on restated. But this adjustment that you made implicitly it's not in the guidance. I mean -- It doesn't impact the guidance

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Vibhor Kumar - Citigroup - Analyst  
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Okay, okay. Fine. And the second question is rather an accounting-based question. If I look at mobile voice traffic revenue and the mobile data revenue, the voice revenue has declined quite a bit and the data revenue has jumped quite a bit. So I'm just trying to understand how -- has there been any changes in terms of accounting. How do you break the bundled revenue into voice and data in this quarter?

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Maciej Nowohoński - Orange Polska SA - CFO  
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Okay, so in fact there are two effects here which are impacting the exact split between the voice category and data category. First of all, we do from time to time promotions for data especially in the prepaid business and that is impacting positively data part. So from time to time it happens that the data is higher because of promotions and this time was the case.

And then the second trend is a global trend that we have seen since many quarters. That means that there are more and more abundant offers that we are selling to customers, especially unlimited on the voice and SMS front. And since that's becoming more and more a commodity, the component of the data is becoming much more important part of our ARPU than previously. So you will see it growing gradually quarter by quarter because of that factor. Data today is not unlimited. There is a price for 1 GB and this price is then a decisive factor for how do we price that component in our ARPU.

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Vibhor Kumar - Citigroup - Analyst  
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Okay. Thank you so much. Thank you.

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Maciej Nowohoński - Orange Polska SA - CFO [22]  
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You're welcome.

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Operator  
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There are no further questions on the telephone line.

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Leszek Iwaszko - Orange Polska SA - Head of IR  
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We have a follow-up from the floor.

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Paweł Puchalski - DM BZ WBK - Analyst  
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Hello. Paweł Puchalski, BZ WBK. A question on CapEx. I see your CapEx pretty low in the first quarter. Is it kind of OpEx -- sorry CapEx optimization you achieved or first quarter CapEx is a guidance for next quarters to come?

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Maciej Nowohoński - Orange Polska SA - CFO  
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If I may take this broad question, first of all this is the CapEx that we have had in our internal plans, so there is nothing unexpected here.

Second of all, we can expect that the CapEx will increase especially in the second semester because of the global targets that we are going to achieve on the fiber front. And in terms of specific fiber investments, you will see around PLN66m of fiber investments that we have done specifically in Q1. But everything is on track as planned.

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Paweł Puchalski - DM BZ WBK - Analyst  
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Thank you.

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Leszek Iwaszko - Orange Polska SA - Head of IR  
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There are no more questions. So if there are no more questions, then thank you very much for your presence, for your attention and see you again in July.

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Operator

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

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