

Orange Polska

CONFERENCE CALL TO DISCUSS ORANGE POLSKA FINANCIAL AND OPERATIONAL RESULTS FOR THE FIRST QUARTER OF 2021.

Company: Orange Polska

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Participants:

- Julien Ducarroz, Chief Executive Officer
- Jacek Kunicki, Chief Financial Officer
- Leszek Iwaszko, Head of Investor Relations

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Hello, welcome everyone to our conference summarizing first quarter of 2021 results. Speakers for today's conference will be Julien Ducarroz, CEO of Orange Polska; and Jacek Kunicki, our CFO. Let me hand the floor to Julien to begin the presentation.

Julien Ducarroz, Chief Executive Officer

Good morning, everyone and welcome to our Q1 results. Today I will highlight what we did in Q1, Jacek will follow with our financial, and I will summarize our main actions for the rest of the year, and then we will gladly take your questions.

Moving on the next slide highlighting the main events of Q1. Obviously FiberCo has been a big achievement, although, technically it was not in Q1, but we believe that this is very important and structural event for Orange Polska. I remind you that it will enable us to expand the footprint while allocating our capex towards the project and as well as you have seen it allows us to take advantage of high valuation of assets. Regarding commercial, I would say that we had solid result when we compare it to last year Q1, but I have as well to share that those results are bit below our expectation. And when I refer to expectation, I will say our plan and we will see in more detail after, but the main reason is because of lockdown and the demand on the market that we have seen across all the product line has been a bit lower than we expected. On the financial side, I think we are posting some strong results and it's an illustration that our value strategy is the right one and as well we will see that this growth pattern is a sustainable one, it's an important one. And the last point I will cover which is very important for me and we have seen as well inside the company a great mobilization and engagement is that yesterday we published our commitments regarding our green targets and our climate policy, and I will come back a bit more detail on this.

Let's start the discussion around the financial result. As I said, strong results and here you see the different lines. So, on the revenue, we posted 4% growth year-on-year. And when we look at the component of it, they are strong because they are driven by convergence and ICT and as well equipment; we had a good quarter following as well a strong Q4, and Q1 continue on this area. When we look at EBITDAaL, the EBITDAaL grew even faster, by 5% compared to last Q1 and this is coming both from our direct margin, which is very important, because this is what we are looking at and as well our continuous effort on cost savings. On the commercial side, we see as well that thanks to last year strong performance, you remember we commented 2020 especially H2 and combination with ARPO growth is delivering this nice growth. We can say that we are now confident on full-year trajectory. Obviously, it will depend as well as we see in Q1 on the macroeconomic situation and as well on I would say the pandemic, but I'm getting more positive on this side. The last comment on the financial, on the capex, you see that we are above and this is due to the fact that we had to reverse a real estate transaction in Q1, but it's a matter of phasing as well and we don't see any issue on our ambition for e-capex.

So, going to the first zoom which is back to the FiberCo and I do know that you had already a quite extensive discussion with Jacek, so, I will not go back to the detail. But just to remind everyone the reason we did this move and why we believe this is the right move. So, obviously, fiber, we are at more than 5 million connectable households in Poland. This is by far not the entire Poland. As you know, there is 15 million, and so our journey in the fiber must continue and we are strongly convinced. And when we see the result, we see that this is a right thing. So, fiber must go on for us and we know as well that there is still plenty of potential to be covered. So, first point fiber must continue. And we came with this model of FiberCo obviously for the reason that we need capex as well to fuel other part of the business, upcoming business, one of it being a 5G, but not the only one. And clearly the market condition as you have seen on the valuation that we got out of this exercise which is PLN 1.4 billion for the 50% sales of this FiberCo. It is obviously a very good moment to have done it and we are very pleased with the result. I want as well to remind you that this is the first step, we need now to walk toward the closing and as well to operationalize it. As you know we will be the, I will say, the engine behind to deploy these 1.7 million households over the next five years.

So, going now on more commercial result and starting with fiber. So, in Q1, we added 54,000 new fiber customers. This is lower than in Q4, but this is a bit of seasonality. And as I commented as well, the overall market situation related to the pandemic and closing of malls and this is clearly a bit pushing down our result, but we are confident that the dynamic is there. And as soon as the shops will open or the economy will more widely open, we will benefit and continue our strong growth. But as you see 54 is a very strong result. And I think what is important and we wanted as well to show you that it's not only because we are deploying, but it's as well because we are becoming month after month more, I will say, agile and precise in exploiting the previous deployment, because you see that our penetration and what we call utilization is increasing quarter after quarter. We can share that even if on average it's getting close to 16%, we have cities where it's higher than 20% and even on the top 10 cities, we have more than 30% utilization of our infrastructure. So, a very healthy one that is

driven by new deployment, but as well on the existing footprint that we continue to better and better utilizing.

When we look at the value, you can see on the bottom left chart that fiber customers on ARPO level are generating 20% higher ARPO than the fixed broadband. So, when we are growing fiber, we are growing the value. And when we look and analyse where this value is coming from, we have a strong driver that we have seen especially since last year is the adoption of highest speed. As you know, we have a tiered strategy pricing for fiber 300, 600 and 1 gigabyte. And we see that quarter after quarter and you see that on the bottom right chart, the adoption of the high speed is increasing, which mechanically increases the ARPO. And here this is as well not only sustained by the demand of the customer for better speed, but as well a great innovation that we launched in Q1, which is our Funbox 6, which is leveraging new Wi-Fi technology, which allows the customer to have a much faster Wi-Fi. So, this is a good combination of delivering fiber high speed, but as well providing it in Wi-Fi at a high speed. Because most of the time if you don't have this technology of the Funbox 6, even if you have a very good fiber to your home, if you are using Wi-Fi, you might not get all the speed we are providing because the Wi-Fi is limited and that was a great innovation we had in Q1.

Moving to the next one, obviously our main axis of the commercial is convergence. So, convergence as well growing versus Q1 last year. Again, same comment as before, we are a bit below our ambition due to the demand, but nevertheless, you see the growth is there and it's encouraging. As well we can see that when we compare convergence and fixed broadband, both are growing in term of ARPO, so, we are growing volume and we are growing value. So, I think those are very good signals of healthy growth of our business. I can tell you as well that if I look at the convergence segment as a revenue line, we are growing by 14% in Q1.

So, going now on the mobile side. As well very strong Q1 in terms of net adds with 88,000. As well you probably follow the portability and market and we are very happy to report that we were positive, one of the highest volumes over the last period, which is as well showing us that when I'm commenting that we have a bit of a slowdown versus our ambition, we cannot say this is due to the competition, at least not through the portability. But we strongly believe that by the decrease of traffic that has been in March almost 40% in our retail, that once the economy will be open again on a wider basis, we will see back strong momentum like we have seen last year.

This time I wanted as well to share with you some insight on the prepaid that we don't usually comment. You probably know, as an industry, prepaid has been very much affected across all Europe. This is a segment that is very volatile by nature, but as well it's a segment that most of the dynamic is driven by seasonal, whether it is visitor roaming, whether it is a worker coming from abroad; and in the case of Poland, obviously, there is a lot of people coming from abroad on a seasonal basis, which are usually the part of the prepaid base. And as you understand that mobility has been very much constrained over the last 12 months. This is reflected in our prepaid. But nevertheless, you see here that we are showing you the ARPO, and for those customers that are here because our base is decreasing, they have a better ARPO. So, this is encouraging for us that the day when again the economy and specially the workers from abroad will come back, we are well-positioned. I remind you as well that

we had noticed that as a headwind for this year that the new regulation was implemented regarding prepaid in February and will impact our revenue as it's related to the recognition of the top up fund.

Going to the next one about our green ambition. So, we published yesterday and I'm very happy that today on the special day of Earth Day, we can talk about this topic, it's a very important topic for me and for Orange. So, just to give you a bit of our story and our ambition on this topic, first of all Orange Group on which Orange Polska is fully subscribed to, we had a bold ambition to be a net carbon neutral by 2040 on all the scope, so internal and external and as well all our suppliers. So, this is Scope 1, 2 and 3. This is the clear ambition we have, but obviously 2040 is a bit far away and the climate situation, we cannot afford to wait and just project in such a long your perspective, so we published a strong commitment towards 2025 and that commitment is that we will reduce by 65% our carbon emission compared to 2015, which I believe is a very strong commitment. So, the way we will do it, and this is for Scope 1 and 2; Scope 3 we will start to address it, but the main I will say effect and result will take more time to be visible. So, we focus for 2025 to commit on a reduction of 65% of the carbon emission.

And when we are looking at our business, obviously, the main impact is coming from energy. Therefore, we want by 2025 to have 60% of our energy coming from renewable sources. And this is all our strategy that we started already last year by getting almost 10% of our energy coming from renewable sources as through PPA that we will implement before summer. So, this is where we want to go. And obviously we believe as well as a telecom and technology company is not only about what we do inside the company, which clearly we have taken as I just said strong commitment, but we have a great role to play in the economy to help with our technology other players, other business partner to engage into their green transformation, I can mention a few, like smart cities, but as well 5G and fiber are great I will say transformation of our green. If I look at the fiber compared to copper, you have to know that the fiber is consuming 80% less energy than copper. So, as we are engaged in this transformation from copper to fiber, we will mechanically as well contribute to our main objective of reduction. I do believe as well that we have a great role to play with our customers when it comes to devices and equipment material that we need to enable more circular economy, that you will see more and more that we will come back on this topic. So, I'm very pleased today to share that with you that we have committed, and we are going along all our report to be transparent with you and show where we are and the progress we are making in this very important topic.

So now let me hand over to Jacek.

Jacek Kunicki, Chief Financial Officer

Thank you, Julien. Good morning, everyone. Let's start the financial review on slide 13. We will present the highlights of the quarter. As you can see the financial results of Q1 were strong and in line with our expectations. Revenue growth was fuelled by expanding revenues of convergence and ICT as well as by a rebound in equipment sales and in our energy business. The revenue increase was a key driver of the 5% EBITDA growth. This was possible as direct margin from core telecom services is now

offsetting the structural decline of legacy. This is a key change in our EBITDA dynamics, and it makes this growth much more sustainable.

The year-on-year increase of economic capex results mainly from phasing. Please note that last year in the light of the outbreak of the pandemic we were slowing down capex projects as part of the mitigating measures. In addition, proceeds from real estate sales are much lower in 2021. This reflects a tough business environment and also a change in accounting estimates relating to a consideration from previous periods. Finally, cash generation was much higher than in Q1 of last year, driven by EBITDA growth and by timing of working capital requirements.

Let's review this in more detail, starting with revenues on the next slide. So, as we've mentioned, the revenues expanded by 4.1% in Q1. There were four main reasons to this very satisfactory performance. Firstly, convergence. Revenues from these services grew by 14%. This is a strong performance with a pace of the increase even accelerating in comparison to previous quarters. It results from a solid customer base growth coupled with an expanding ARPO. Secondly, ICT revenues were 7% up year-on-year. The key driver of this growth was the contribution of Craftware, which we acquired in December last year. It generated over 20 million revenues in the first quarter of the year posting a satisfactory growth year-on-year. Excluding Craftware, ICT revenues matched their level in the Q1 of last year when we realized a large contract to enable the digitalization of the Polish post. Thirdly, revenues from equipment were 12% up year-on-year. We have been able to adapt to the new environment and this year's lockdown did not affect equipment sales as severely as the one in the first quarter of last year. Finally, our energy resale business is regaining momentum after a difficult 2019 and 2020. It should continue to support our top-line development in the next quarters. The resulting revenue growth is a solid start to year.

Let's now see how this translated into EBITDA on slide 15. We're happy to report a 5% EBITDA growth in Q1. This is a strong achievement. I am also pleased with the structure of this growth. It is almost equally driven by the expansion of the direct margin and by cost optimization. This means that our growth is becoming much more sustainable. Growing direct margin demonstrates that our future proof revenues generate higher value for us and we're able to offset the burden of legacy decline. At the same time, we continue to pursue further cost optimization. In Q1, we report another sequential 2% reduction of indirect costs. This came mostly from workforce costs as well as from property and general expenses as we have continued to save due to remote work.

The Q1 EBITDA performance was in line with our expectations. We are confident to deliver on a full-year objective to grow the EBITDA in 2021. Obviously, as the pandemic is not over, we will continue to monitor the pace of the economic recovery and its impact particularly on the credit situation of our B2B customers. Also, looking forward to Q2, please remember that we posted a very high EBITDA last year when it was boosted by the curtailment of jubilee awards a non-recurring development.

Let's now look at the next page to see on the net income. We posted a PLN 39 million net income in Q1, a marked improvement versus the net loss that we have generated a year ago. The main drivers of this improvement were growing EBITDA, lower depreciation and less finance costs. We already discussed the EBITDA development. Depreciation costs decreased year-over-year as we've extended the economic useful

life of certain assets. We mentioned this already in our financial statements for the full year of 2020. It impacted Q1 by about PLN 33 million and we expect a similar year-on-year impact for the next quarters. Finance costs were PLN 66 million below last year when they were heavily impacted by significant weakening of the Polish zloty.

Finally, over to cash generation on page 17. We generated almost PLN 200 million of organic cash flows in Q1, significantly higher results than in the Q1 of last year. We're pleased that the expansion of EBITDA has translated into growth of operating cash flow before working capital. As for working capital itself, its evolution was influenced by three elements: firstly, by different timing of payments between quarter four and quarter one in both years; secondly, by good receivables collection; and thirdly, by a more favourable change in inventory balance resulting from better handset sales this quarter.

Working capital evolution is by nature tends to be volatile from period to period and an extrapolation of this result and trend should be made with quite caution. Let me also remind you that in the quarter two of last year, working capital was exceptionally positive as we shifted over 100 million of social security payments from Q2 to Q3 as this was allowed by the anti-COVID legislation.

I think this concludes the financial review. You can see that we've had quite solid satisfactory financial results. Thank you very much and let me hand the floor back to Julien.

Julien Ducarroz, Chief Executive Officer

Thank you, Jacek. Let me just summarize what we just presented and give you a bit of our perspective for the remaining of the year. Obviously, you have seen that we had a good start of the year, which is a result of a very good H2 commercially last year and all the effort of the team in terms of the transformation and cost optimization that now are visible on our Q1 result. Obviously, we are looking as well to have a bit more dynamic in our commercial performance and I do expect, and we will get ready, we are preparing for this moment, so, we have seen last year that as soon as there was a bit more opening, the commercial dynamics went back very quickly and we must be ready for this moment. As well, we are preparing our new operating model, which will be important for the future, which is related mainly to how are we going to work and it will have an impact on our offices because we plan to optimize offices under the assumption that we will go back on hybrid model between working home and working in the office.

As we commented FiberCo now need to be going full speed. We aim to go to the closing in Q3 and we have to do that because our deployment will depend now on FiberCo. So, we need to be ready in Q3. Regarding 5G auction, we are still on waiting position. You probably know that the cyber security law is still in discussion and that will be the trigger for the license process. But I hope it will start soon, so it will give us more visibility on some of the topics that we have been as well as discussing in the past.

Globally I'm optimistic. I'm looking forward with confidence together with the team about our full-year target as long as we see in the short term a better evolution of the

pandemic situation and as well that we will see a macroeconomic environment favourable for us.

To conclude, I will invite you towards the end of June to present our new strategy. And as I was telling you, we finished .One and we will start a new cycle, and I'm very excited and looking forward to meet you at this occasion.

Thank you very much. And we will take the questions.

Operator

Thank you very much for the presentation. I would like to now turn to the Q&A session. [Operator Instructions]. Our first question comes from Titus Krahn from Barclays. Please go ahead. Your line is open.

Titus Krahn, Barclays

Good morning, everyone, and thanks for taking my question. Just two from my side, the first one on your inorganic growth. So, with PLN 21 million Craftware it has been growing quite nicely over the quarter. Could you please elaborate on how much the EBITDA after leases contribution was? And similarly, could you please quantify the revenue impact from energy's resale over the quarter? Is it also likely to continue over the next couple of quarters?

And the second question is more strategic. So, a number of your peers in Poland have already decided to sell their mobile infrastructure. Does this have any impact on your strategy regarding tower ownership? And also, how do you expect to work together with the TowerCo that has now entered the market, would this impact your investment needs and to what extent could this be actually beneficial for you?

Jacek Kunicki, Chief Financial Officer

Thank you very much, thank you for your questions. Taking the first two ones. I will start with the energy business; the growth of revenues was about PLN 26 million year-over-year for energy. I would expect that we should have at least this kind of benefits for the year-on-year evolution for the next quarters, if we can do better, we will try to do better, but I would say at least this level of contribution for the year-on-year growth. Regarding the inorganic growth, so the revenues of Craftware were about PLN 20 million. As you can imagine the EBITDA is much, much smaller, I would say single millions, and we don't guide per subsidiary, but you can imagine that this is not a significant impact when you analyse the overall performance of Orange Polska which was much more driven by the good growth of convergent revenues as the percentage margin coming from convergent is much, much higher than from ICT. That's for the first two questions.

Julien Ducarroz, Chief Executive Officer

Now the second one around the move on the TowerCo, I would say sector in Poland, for us obviously, we are about to close, not yet closed FiberCo, and as we indicated in the past and you know that, our Group is active now in Spain and France via Totem

Company, that we said after the team will start to get less busy with FiberCo we will progressively look at the different options. And obviously one of it will be to look together with our Group on what we can do. I remind you as well that we have Networks together with T-Mobile, so I will say our situation is a bit different than the one who have already did a move on the market, and we need to look carefully on the option. But obviously I can say that all scenarios are on the table and we are going to look what makes more sense for Orange Polska and the stakeholders. But at the moment we have no decision or any indication in which direction it will go, so I will come back on this point probably in Q3.

Titus Krahn, Barclays

Thanks. That's very helpful. And does it impact something kind of from an operational standpoint in terms of you having a new TowerCo, you can negotiate with about additional sites potentially?

Julien Ducarroz, Chief Executive Officer

It will, but obviously we are mainly active with our networks that we had already by getting together with T-Mobile done already a lot of optimization and cross utilization. So, remain to be seen, it's not yet operational and we will see. But I would say we have already done a lot on our side, on our perimeters together with Network. So, we are not dependent, highly dependent on this new entity.

Titus Krahn, Barclays

Great. That's very-very helpful. Thank you.

Operator

Thank you very much. [Operator Instructions]

Leszek Iwaszko, Head of Investor Relations

While we are waiting for more voice questions let me go through some questions that we have received online from Santander. First question, could you add more colour on volumes below your expectations? What line represents key negative surprise to you in the first quarter?

Julien Ducarroz, Chief Executive Officer

I would say as you have seen we are higher than last quarter in Q1. So, I could have commented that we are happy with our performance because it's growing but I wanted as well to be transparent and you probably know that obviously in Poland we started, January was quite good, probably prolongation of the Christmas offer and dynamism on the market. And then it went slowly down in traffic. You probably know that if you were shopping, the traffic is extremely low for us, it was in the range of 40% less traffic. And if you ask me on, how much I consider or versus our ambition, we are probably in the range of 10% to 15% below our ambition. But once again, when I look at portability, I clearly see that this is not an issue of competition. But this is an issue of

demand and I have good hope that the moment the opening will happen, we will see like last year very strong dynamics. That's why one of the focus I have in the short term is to make sure that we have the right offer once the market will reopen.

Jacek Kunicki, Chief Financial Officer

And I think it's fair to say that, while obviously, mobile is slightly below expectations and through lower mobile volumes also convergence, fiber on the other hand, is where we wanted it to be. So, that just shows how remarkably resilient fiber is to any crisis. And in fact, I think it's fair to say that increase of home office and remote schooling has fuelled the demand for fiber and we're benefiting from that.

Leszek Iwaszko, Head of Investor Relations

The next question from Santander is about real estate. Do you expect real estate disposals to accelerate in coming quarters? What may be the total positive impact of real estate in 2021?

Jacek Kunicki, Chief Financial Officer

Thanks for your question, Pawel. I definitely expect us to accelerate in real estate sales starting from Q2. I think Q1 was not a particularly favourable period for this. One, because generally the environment was tough, secondly, as we commented we had to reverse the transaction. So, definitely expect to accelerate. I will not comment on the overall amount that we will wish to sell this year, as we integrate real estate proceeds and capex spending into e-capex. But everyone is aware of the range that we are targeting for this year and we are quite determined to keep e-capex to this amount. We will keep you posted when we have more progress. Thank you.

Leszek Iwaszko, Head of Investor Relations

And the third question from Santander is about capex. You mentioned some extra capex for other businesses going forward. This would be on top of your 5G deployment outlays? What scale of extra capex do you expect? Any early view on your 2022 e-capex?

Julien Ducarroz, Chief Executive Officer

I will let Jacek to comment on the numbers, but to give you a bit of where I foresee the need of how to allocate capex, because we are not talking about on top of but in term of allocation of capex for sure 5G will be in the center stage in terms of spending. But we need as well in the area of digitalization, transformation, automatization, which in our plan to deliver optimization in the long run. But at the beginning, you need to invest. It's unrealistic to believe we can continue to transform the business without investment. So, there is no major other I will say surprise or idea of spending. But mainly to continue to invest in order to have in two, three years' time, real impact on our operating model.

Jacek Kunicki, Chief Financial Officer

I will not comment extensively on the financial figures, because we will deal with this, when we will communicate to you our three-year strategy. From the main directions I think it's clear we will spend less capex on fiber. And we commented before that thanks to FiberCo we could expect PLN 250 up to even PLN 300 million benefits of lower capex than if we were to invest by ourselves. But on the other hand, clearly there will be capex linked with 5G spectrum. Clearly, there will be capex linked with 5G rollout. And we will need to initiate a network renewal for our mobile, radio access network. So, definitely, there will be a pivot towards mobile and towards 5G. I think that's all that we can say right now for the main directions. Thank you.

Leszek Iwaszko, Head of Investor Relations

And then another question that came online is, will the company pay dividends for 2020?

Jacek Kunicki, Chief Financial Officer

Well, this is the question that is coming up frequently. I will comment as the last time we commented, it was in February. I believe that we then mentioned that on one hand, we really would like to come back to paying a dividend. However, there are three items that we need to clear and we need to be more certain about. One was the sustainable growth of our results and our EBITDA. I think Q1 shows that we are well progressing on this path. We have mentioned FiberCo as one of the unknowns and now we see that we've been able to sign the transaction not yet conclude, but we've been able to sign the transaction with a good inflow for our balance sheet. I think the two elements that we're still missing today is, first of all, more clarity on the 5G auction. Because this is quite a considerable spending that is coming up and we don't know neither the timing nor the conditions today. And we are observing still quite rigorously the pace of the economic recovery, because we are under lockdown as we speak right now. And we are observing how well the economy and especially our business clients, how will they, in what condition will they come out from this crisis? So, obviously, we will address this soon. We will address the dividend policy together with a strategy. We will address the 2020 dividend decision before the AGM. But you need to appreciate, we need a bit more time to try and get more clarity on those. Thank you.

Leszek Iwaszko, Head of Investor Relations

As it appears, we have more questions. But I think this is a question of the dividend that has just been addressed, so no need to repeat. Operator, can you please confirm we have no other questions in the queue?

Operator

Confirmed, Leszek. We have no further voice questions. I'll pass the line back to you.

Leszek Iwaszko, Head of Investor Relations

Okay. Thank you very much for your attention and you will hear from us soon, hopefully. Thank you, bye-bye.

Jacek Kunicki, Chief Financial Officer

Thank you.

Julien Ducarroz, Chief Executive Officer

Thank you very much.