Türk Telekom Q4 2018 Financial & Operational Results Conference Call

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Conductors:

Dr. Paul Doany, CEO

Mr. Kaan Aktan, CFO

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Ms. Gözde Cullas, Head of Investor Relations

OPERATOR: Ladies and Gentlemen, thank you for standing by. I am Gelly, your Chorus Call operator.

Welcome and thank you for joining the Turk Telekom conference call for the Fourth Quarter 2018 Financial & Operational Results.

At this time, I would like to turn the conference over to Ms. Gözde Cullas, Head of Investor Relations, Dr. Paul Doany, CEO and Mr. Kaan Aktan, CFO of Türk Telekom.

Madam and Gentlemen, you may now proceed.

ÇULLAS G: Hello, welcome to 2018 Year End Results Conference Call. We are here with the Management team and today's speakers are our CEO, Dr. Paul Doany and our CFO, Kaan Aktan. Before we start, I kindly remind you to review the notice on our earnings presentation.

Paul, you can go ahead.

DOANY P: Thank you. Hi everyone, I'd like to thank you for joining this call. Before I start the presentation, I would like to start with a few words about our recent changes in the Corporate structure. In December the 55% block shares were taken over by the special purpose vehicle Levent. Following this, we had the related board changes and we also held an Extraordinary General Assembly. We now have a more agile board structure with nine members from the previous twelve. And with the valuable contribution of our new board members, we will be continuing to implement our long-term business plan in a more determined manner and grow the Company creating value for all the stakeholders. I'll continue with strategic highlights of this quarter on Slide 3.

In this quarter we continue to deliver on our strategic objectives after a challenging third quarter, the early actions undertaken by both the Government and the Company started to deliver results enabling our outstanding performance across all KPIs in the fourth quarter of 2018. The team managed excellent execution of our primary strategic imperatives of driving fixed broadband penetration growth with defensive fixed voice, as well as, increasing mobile market share along with our opportunistic move into the Pay TV growth segment benefiting from the state of play in the TV market, which I will explain a bit later on.

In terms of fixed broadband, we got almost 40% of our fixed broadband net additions in the fourth quarter through our affordable penetration campaign entry package İnternet Bizden. Regional campaigns, as well as partnerships with electricity companies, are also continuing to grow through these new channels. We are well positioned to deliver value with digital and ICT solutions in addition to core services. We continue to drive digital services through our Tivibu GO which is our next generation, new generation TV platform, Muud which is our digital music platform and e-dergi which is the digital reading platform and Tambu our national keyboard.

Tambu has reached 8.3 million downloads by the end of last year, more than double its nearest competitor. Tambu was viewed 17 billion times. 36 billion interactions were generated over it is applications since its launch. We renewed in December new features in Tambu with a new customer interface. The new features include location-based food and beverage venue search, web search engine and keyword search from domestic content with stronger basis for monetization and we will be elaborating on this more in the next quarterly reporting.

Our other customer-focused platform which is the online service app, Online Islemler was downloaded 23.8 million times since its launch, supporting our strategy of providing best-in-class self-service customer experience and driving operational efficiency. TT mobile subscribers using the app exceeded 10 million in 2018.

In the fourth quarter, we integrated our corporate security services under the largest cyber security center in Turkey, addressing increased cyber security threats. We target to provide end-to-end solutions and global standard to our customers, leveraging on our strong position in telecommunication space and strong brand position. We continued our initiatives to drive efficiency by utilizing infrastructure effectively. We value infrastructure sharing opportunities to minimize duplication of infrastructure and unnecessary duplication.

As you may recall we announced the signature of our corporation protocol with Turkcell, Vodafone, Turksat and TELKODER. The protocol aims efficient use of existing infrastructure and acceleration of new business. Within the scope of this protocol, we recently completed the pilot project with Vodafone in Sincan, Ankara.

While the incremental CAPEX of the project is financed by Vodafone, Türk Telekom will own that infrastructure. We believe this leasing model with a built in capital contribution can form the basis of our Next Generation networks, such as slicing radio over 4.5G and getting ready for 5G where we can be the fiber to the most economic point of the other operators' network. In this case obviously would be Turkcell and Vodafone who are the mobile network operators in these markets. This is what we call actually Fiber to the Site, FTTS we have more to say about this in the next quarter.

We are also evaluating sharing opportunities with all players in the mobile sector including active sharing as you may have seen with Vodafone in Zonguldak, passive sharing we have had with Vodafone for a long time and

RAN leasing options which will be more cost effective to do with Turkcell in the larger cities, so we are looking really at all alternatives and we have now at least one working model that works very well in low population density, which is where we had a coverage challenge and we cannot obviously monetize on that investment.

For sustainable subscriber growth, we continue our focus on cross sells benefiting from our integrated structure. Share of customers providing consent for sharing their information within the TT group companies increased to 72% from 66% a year ago. Triple Play drives the increase in multiple ownership and among the constant universal customers who consented a year ago our multi-play product ownership increased from 58% to 63% in the fourth quarter last year.

Our corporate venture capital strategy to invest in scalable ventures in priority verticals is moving forward. Our stake in Doctor Turkey 5% is moving forward and we have made a recent transaction at 6.9% first tranche in MentalUP and education vertical. MentalUP or app is a game based learning platform for K12 students that provides educational and developmental brain training web and also for students but also for adults. We will continue to invest in such type of opportunistic openings in verticals such as health, education and possibly also in energy and in any other viable horizontal.

On Slide 4, net subscriber additions. We delivered strong subscriber growth in the fourth quarter across all business lines with our integrated business model and our unmatched diversified portfolio and penetration increase initiatives. We cost-effectively executed our strategy of growing our customer base seizing opportunities for cross selling and effective retention management.

Leveraging on our attractive multi product offers, total number of Türk Telekom subscribers reached 46 million with 1.2 million net adds in the fourth quarter last year. For the full year, net subscriber gain was 4.3 million by far outperforming the previous year of 2.8 million. Mobile subscriber base reached 21.5 million with 718,000 net additions in the fourth quarter of 2018, the highest fourth quarter. For the full year net subscriber gains reached 1.9 million, the best annual net add since the IPOs.

Importantly our quarterly mobile churn rate decreased to 6%, the lowest churn achieved again since the IPO. We added 1.2 million net new mobile subscribers in 2018, again the best performance over the last decade on the back of our penetration growth initiatives across all channels and in the fourth quarter net additions was 308,000.

Home TV subscribers reached 1.7 million with a record full year net add 492,000. Tivibu Home moved from the fourth player position in 2016 to the second position in Q1 2018 in the Pay TV market and this position was reinforced throughout 2018 strengthening our base for the wireless home strategy.

Lastly, the positive trend in fixed voice subscriber additions continued supporting by momentum of our fixed broadband entry package penetration campaign. The number of total fixed voice subscribers continue to sustain growth for six consecutive quarters with 108,000 net additions in the fourth quarter.

Slide 5 financial performance. I would briefly present because Kaan will give you more detail. During the quarter we continued our balanced focus on subscriber growth and ARPU growth executing with financial discipline. Our TL 8.4 billion EBITDA exceeded the high end of our EBITDA guidance range of

TL 8 to 8.2 billion. Our 2018 EBITDA margin was outstanding at 41.3 on the back of our efficiency program executed across the entire company.

We delivered a turnaround in underlying EBITDA margin with 4.2 percentage point improvement over the past two years supported by a more streamlined organization, effective cost control, scaled advantages, integrated synergies and enhanced efficiencies on the back of data growth and some digitalization. While FX rates impacted our net income negatively in the first nine months of 2018, we have a strong recovery in the fourth quarter. Our fourth quarter net income was TL 2.2 billion, a significant improvement compared to net loss of TL 113 million last year thanks to stronger operating performance and improved FX environments.

Fixed broadband performance on Slide 6. Our strategy to increase fixed broadband penetration continues to bear fruit, driving strong growth in the fixed broadband market. We have 308,000 net new subscribers in the fourth quarter out of which around 40% came from our affordable entry package. Moreover, regional penetration campaigns also supported our growth with the best performance over the last decade. Net subscriber additions in 2018 were 1,163,000 and our fixed broadband base reached 10.9 million. The contribution of partnerships with electricity companies in our net additions is increasing in line with our strategies to drive penetration through a more diverse distribution channel. In addition to our channels covering whole Turkey, we also cover 70% of households through these companies.

Fiber and upsells are also driving our growth where customers enjoy superfast speeds, our fiber subscribers exceeded 3.6 million, increasing 254,000 in the fourth quarter, more than 80% of the total broadband subscriber net additions came via fiber offers. Share of our subscribers who prefer over 20 megabytes per second increased to 37% in the fourth quarter which was 31% a year before.

In September, we had a price increases in the range of 12% to 15% for existing campaign prices for new activation. Overall with tariff changes, the existing share of fiber product upsell from entry packages, we see an acceleration in the ARPU growth. Our ARPU increased to 45.9 lira in the fourth quarter by 3.3% quarter-on-quarter and we expect further momentum in this year. We provide our customers with a wide variety of offerings building on our strength to provide abundant capacity efficiency.

Starting from 2019, we lifted fair usage quotas for unlimited tariffs and launched high capacity offers. We also included 6 megabyte per second and 12 megabyte per second in our portfolio to add affordable pricing points during the transition to unlimited world.

As a customer-oriented company, we continue to invest for better connectivity and best-in-class customer service in every city in the country. We continued to strengthen our position in fiber ownership, increasing our fiber network to 282,000 kilometers and fiber homepasses to 18.6 million as of the end of last year.

Mobile performance on Slide 7. We also delivered excellent mobile results. We gained almost 2 million net subscribers in 2018 which is a record supported by our cross-selling activities and synergy offers including for example our mobile TV cross-sell, as well as our improved network quality and coverage benefiting from our full spectrum.

Number of total subscribers exceeded 21.5 million by year-end. We added 718,000 subscribers in the fourth quarter. Based on the limited reporting from competition, we believe we are outperforming them in terms of market share growth as we are better able to maximize our differentiation ability in particular cross-selling. Overall, 2018 results show that we are on track to increasing our mobile market share to our desired fair share towards the one-third.

In the fourth quarter with our customer-oriented initiatives and effective retention management, we have the lowest churn rate ever in mobile at 6% which also shows that we can grow our subscribers effectively. In addition to our solid fundamentals, our online transactions at our loyalty campaign Sil Süpür and new touch points within our customers had a major contribution to our strong retention performance. While accelerating the pace of subscriber growth, we also had a strong ARPU. Our mobile ARPU increased by 11% year-on-year with higher data consumption combined with inflationary price decreases.

The market continues to be more rational in the fourth quarter. In the beginning of the quarter, that quarter we closed our aggressive tariffs in line with the market. We launched new headline acquisition campaigns with around 15% -20% higher prices. In December, we launched new tariffs with another 10% increase. Supported by these actions, our service revenue growth accelerated to around 20% year-on-year in the fourth quarter from 12% at the beginning of the year. However, our reported mobile revenue growth at 14%, lower than the service revenue growth due to one-off provision and our more prudent strategy in relation to device business.

Mobile data on Slide 8. In the fourth quarter last year, LTE population coverage expanded to 91% from 83%. Meanwhile, the share of LTE users continued to grow to reach 46% share among our mobile subscribers, up by 11% from a year ago. Average monthly data usage increased from 4.8 gigabytes last year to 6.1 gigabytes in the fourth quarter with LTE compatible smartphone penetration reaching 75%. Similarly, our leadership in smartphone penetration continued with 83% of our total mobile subscriber base. With strong consumption growth and price increases, our data revenue increased by 25% in the fourth quarter last year.

On the other hand, in the fourth quarter, we offered less free data via our loyalty campaign Sil Süpür compared to Q3 when we offered more substantial data to certain customers. As such or data usage decreased slightly while revenues per gigabyte increased quarter-on-quarter.

TV performance Slide 9. We would like to remind you that is an opportunistic strategy in relation to pushing for Pay TV targeting the mass market benefiting from, firstly, limited penetration due to high prices of the main Pay TV players as well as a very high free-to-air customer base aimed to penetrate as many as homes as possible using satellite television for our growth market as we happened to have satellite television as well as our fixed broadband offering over broadband for a top up price over a main FBB price.

At the end of the fourth quarter, we reached 1.6 million Tivibu Home customers with the best annual performance in net adds increasing our Home TV base by 492,000. During the year, satellite net additions were particularly strong as we focused on our wireless home strategy addressing the mass TV market at affordable prices. And again these are very easy to install and incur less customer experience issues enhanced, of course, now by our Tivibu GO offer which means we can provide additional features and that can drive either additional WiFi demand or hopefully also some mobile data.

As we are now the #2 player with 23% market share in the large screen market, surpassing both Cable TV and D-Smart, we are now increasing prices to cover for our increased set-top box FX exposure. Therefore while continuing to focus on wireless home strategy, we will also target to monetize our existing customer base with a more cost effective approach. Building on our cost effective content strategy, we will continue to broadcast Turkish Basketball League for 3 years. We also decided just focus not only exclusive outsourced TV channels, in-house cinema channels in line with our content cost optimization strategy as there is very little differentiation in the market in Turkey. And also we have to recognize that there are very lax copyright enforcement in this area of service so investments in content are not an option to any of the current TV players such as Bein, D-Smart or the online players.

Now all of which fixed broadband and wireless data where we gained from their growth through fixed broadband wholesale and WiFi access.

Accordingly, our ARPU started to increase quarter-on-quarter. Nevertheless, we will keep our prices at attractive levels compared to the premium players in the market especially with regards to our synergy of bundling this or cross-selling this with mobile Plus, especially our Tivibu campaign and driving Tivibu GO across the entire market. Meanwhile, the number subscribers of our OTT TV platform Tivibu GO has now reached 2 million with 394,000 net additions during the year. Our focus is to continue to increase Tivibu GO subscribers and building on this platform.

Fixed voice finally on Slide 10. The results of fixed voice segment in the last year show the clear sign of success on executing on well-designed strategy. The fixed voice is an important component of our integrated offering and obviously an important revenue source. For Türk Telekom fixed voice subscribers we provide additional benefits in other services such as İnternet Bizden, the entry package. This also supports our retention acquisition performance in the fixed voice. This strategy enabled our strong results for the last 6 quarters with subscriber growth in this legacy voice services despite many substitutes. In 2018, we increased our fixed voice subscribers by 338,000, and by 108,000 in the fourth quarter. This performance is clearly outstanding.

We not only increased our subscribers, but we also increased our fixed voice revenues raising this through a tariff structure. In 2018, fixed ARPU also increased to 22.5 lira in the fourth quarter. We also are re-contracting higher prices. With these initiatives, the fixed voice revenues posted annual growth of 5%.

And I would like to now to handover to Kaan Aktan.

AKTAN K: Good afternoon, ladies and gentlemen. We are now on Slide 12, to discuss our financials in more details. Fourth quarter consolidated revenues reached close to TL 5.4 billion, growing 12.5% year-on-year. When we exclude IFRIC 12, top-line growth was close to 14%. Mobile and fixed broadband segments were the main contributors which both grew at strong double-digit rates of 14% to 15% respectively. In the fourth quarter of 2018, the increase in mobile service revenues was actually around 20% year-over-year, while we reported mobile revenue growth of 14%. This was impacted with lower commissions on device sales and also one-off provision of TL 32 million which is related to the regulation on excess usage charges.

As you might remember, we have a decline in our device commissions due to our more prudent approach in device sales and this also led to lower receivable costs. It is important to note here that this impact will be mostly in the base of 2019. With reduced exposure to device business, we are also comfortably positioned considering the discussions on limiting the number of installments in device sales.

Our international revenues growing 46% year-on-year in the fourth quarter. This is driven by higher FX rate and higher volumes especially Türk Telekom

International, our international arm in Wholesale Data, Voice and Roaming services.

We are very satisfied with the performance of our Fixed Voice revenues, which increased by 5% year-over-year after many years of decline. But still fixed revenues still dilute to revenue growth to some extent. When we exclude the fixed voice revenues from our underlying revenues, revenue growth is around 15% instead of 13.8% in the last quarter. With respect to pricing dynamics, we continue to execute pricing action in a disciplined manner without sacrificing our strategy of driving penetration and data consumption. We adjust our pricing plans according to the macro environment, at the same times, we are not ignoring market dynamics.

In Fixed Voice, we increased some tariff components, such as transfer and transport fee in the last quarter. We also increased tariff prices by 10% to 15% in January. In fixed broadband, we increased our prices to new customers by 12% to 15% in September last year. Additionally, we increased our prices for uncommitted subscribers by around 25% in mid-January.

In mobile, in the beginning of last quarter, we closed our aggressive tariffs and announced new headline prices with 15% to 20% increase. In December, in addition to that, we launched new tariffs with another 10% price increase. All these pricing actions will impact revenue growth with a lag, due to committed subscriber base.

The next excellent development is the turnaround in the EBITDA margin continued throughout the year, including last quarter. In the whole year, we delivered TL 8.4 billion EBITDA, you know, which is well above the high end of our EBITDA guidance. The EBITDA margin was 41.3%, which is 7.3 percentage points higher than prior year. This is supported by both scale economy, due to growing customer base, efficiency measures undertaken in opex management including organizational realignment, integration synergies, digitalization and prudent receivable management. Even when we exclude IFRS impact which was implemented first time last year; the EBITDA margin is still at 38%.

EBITDA margin in the last quarter was also excellent and it was at 41.3%. When we exclude the IFRS 15 impact, the margin was at 37.8%, and again 6 percentage point higher than the same quarter of last year, or prior year. One of the key success factors for us is to make the turnaround in EBITDA margin sustainable. And I believe that the company's perfectly positioned to deliver this outcome. If you check our full financial disclosure, you will also see that the contribution of our mobile operations to the consolidated EBITDA is now above 30%. This came on the back of 56% year-over-year increase in mobile contributive EBITDA.

In the fourth quarter of last year, operating expenses decreased by 3.2%. Excluding IFRS 15 and IFRIC 12 impact, I know that all these are complicating our numbers, but growth in operating expenses without these impacts was 4.1% year-over-year. It is well below revenue growth or inflation or devaluation. With respect to all these references points our disciplined opex management had clearly its impacts on our financial delivery.

In the fourth quarter, we continued to have another optimized commercial spending. Commercial costs declined by 6.7% year-over-year. There is still room for continued efficiency on commercial expenses through enhanced digitalization, the way we interact with our potential and existing customers.

Considering the successful commercial performance of the last year, we also proved that we can have an efficient and also effective commercial infrastructure. The availability of well-addressed offers improved upsell/crossell capability of our integrated sales channel; these are all contributing to this sustainable performance.

Another factor in opex performance is the positive impact of the device-related risk management policy and segmented approach in receivable management. As such provision for doubtful receivables declined by 71.1% year-over-year. Personal expenses increased by only 2.3% year-over-year in the last quarter. This is the result of simplification efforts. Share of personnel expense in total revenue is now declined from 17% in 2016 to 14.8% in 2018.

On the other hand, with the higher FX rate, the utilities prices increased our network expenses in the fourth quarter, while we also had an increase in tax expense in relation to strong growth in mobile revenues. There is also a change in calculation methodology in frequency taxes for mobile. Accordingly, you know, network and technology expenses combined with tax expenses increased 28% year-on-year in the last quarter.

As I said we already expected to see some negative impact especially from FX-related network expenses. And for this quarter, we also experienced relative energy prices which were around 40% of total increase in this specific opex item. We tend to be more optimistic going forward, therefore we have rather stable trend in energy prices. Growth of interconnection expense was at 20% year-over-year in the last quarter, this is mostly due to an increase in Türk Telekom International sales volume, and also with the FX impact. We had TL 1.4 billion net financial income in the fourth quarter. This is due to appreciation in Turkish lira. So with fundamental in the underlying business, we've been able to report TL 2.2 billion of net income.

CAPEX in the fourth quarter was at TL 1.5 million, CAPEX in the full-year of 2018 was TL 4.1 billion, and this is in line with our plans despite the challenging FX environment. Excluding the impact of IFRS 15 underlying

CAPEX was TL 3.4 billion, vame with the CAPEX to sales ratio of 16.8%, which is down by around 1 percentage point compared to 2017.

We are now on Slide 13. At the end of fourth quarter our net debt decreased to TL 15.8 billion from TL 18.1 billion and we have 1.86 times net debt to EBITDA and this is also down from 2.3 times in the prior quarter. The decrease is due to Turkish Lira appreciation as well as some cash flow. We have a strong liquidity of TL 4.5 billion cash at the end of the quarter.

We are comfortable with financing even our strong cash flow generation. We have alternative financing instruments such as vendor financing. At the same time, you probably heard we decided to carry out preparation for the issuance of debt instrument of up to a total amount of USD 500 million depending on market conditions and we already applied to Capital Markets Board for this purpose.

We are now on Slide 14. I would like to give you some highlights on our hedge position. We executed additional participating cross currency swap transactions of around USD 445 million during the fourth quarter. We now reached to USD 1.9 billion equivalent of participating cross currency swap position in total.

Our FX portion of cash was slightly down to 73% at the end of year; this is due to debt repayment, as well as, operational necessities for keeping Turkish lira for the early January settlements. But we will continue using cash to hedge our FX base. Including FX based cash at around USD 600 million, our hedge ratio significantly increased to 67% in the last quarter and this is up from 41% in the first quarter of 2018. We may continue executing new hedging transactions when we feel that we have the right market condition. And let me also tell you that our balance sheet is now especially compared to a year ago, it's far more resilient to any potential hikes in FX rates.

Looking at our cash flow generation, our unlevered cash flow in 2018 was TL 3.5 billion. This is more than double compared to 2017. Our impressive EBITDA growth normalized CAPEX cycle following the payments for LTE licenses and also sound working capital management drove an outstanding cash flow performance. We anticipate strong cash flow generation will continue over the next 12 months, as there will be no license fee payment similar to last year. Strong EBITDA generation together with disciplined CAPEX will also support our cash flow generation positively.

As we all know, level of cash flow is a very critical KPI for a telco. This is really very end results of everything we do and a brutally honest indication for sustainability of the business model. Our ability on cash flow generation, we hope that will enable us to deleverage to our comfort zone of 1.5 times net debt to EBITDA within the next one to two years.

Another remark here our mobile operation has also contributed to the cash flow generation in 2018, which was what we expected. But we're also excited to seeing this to happen.

We are now finally on Slide 15 with our 2019 guidance. We are expecting consolidated revenue growth, excluding IFRIC 12 to be at 15% to 16% year-on-year, EBITDA to be at TL 10 -10.2 billion level, CAPEX will be at TL 5.5 billion to TL 5.7 billion, again these are all including I have to mention the impact of IFRS 16, which will be implemented first time in 2019.

In terms of topline, we expect an accelerated growth supported by price increases as well as ongoing subscriber growth. We will have balanced focus between ARPU subscriber performance, so that we ensure sustained growth of our business. The positive momentum in subscribers in entering 2019 gives us high confidence for delivering our revenue guidance. Our guidance now implies around 40% EBITDA margin when we adjust for IFRS 16 impact which will be unchanged versus last year. CAPEX to sales ratio adjusted again for IFRS 16 is also unchanged.

On the opex front, we will continue our focus on optimization and it will ensure that we manage the impacts of high inflation. In commercial spendings, we will prioritize the projects with the highest return in the short-term and also minimize the expenses that are not linked with revenue directly.

From sales side, we are optimizing promotions, tax subsidy and similar expenditures for efficiency. Moreover, we plan to use our online sales channels including our online customer care platform more effectively. We will focus on the improvement in content expenses. For TV, we will also focus on monetizing our existing subscriber base. For personnel expenses, we are also focusing on improving quality and capacity in field operations together with structural improvement. We already launched an early retirement incentive program. This will increase efficiency in the coming periods. Overall, we expect another strong year in 2019. And we are… we believe that we are very well positioned for leveraging the current momentum in our business.

Now, I will hand over the call to…

ÇULLAS G: For the Q&A, we can now start Q&A.

Q&A

OPERATOR: The first question is from the line of Bintcliffe, Jordan with Reorg. Please go ahead.

BINTLCIFFE J: Hi, good afternoon. Thanks very much for hosting the call and I was just hoping to get a bit more information on the EBITDA increase, as very substantial figures, if you could provide a bit more color on what drove that and likewise the cash, cash equivalents dropped quite significantly. Would you be able to shed a bit more color on that, that'd be much appreciated? Thank you.

AKTAN K: For the EBITDA performance, I tried to briefly mention that initially, but there are basically two basic factors, one is the gross margin improvement, which comes from price increases as well as we are now growing the size of the customer base. Obviously there is an impact coming from that front. And the other thing is definitely the reduced share of opex within the revenue that… and we have clear initiatives throughout the year, which will lead to a better and more efficient opex spending, which is a combination of control, well controlled opex and impact of growing business, having a better pricing environment and growing the subscriber number.

And I think the second question was the reduced cash balance at the end of the year, I suppose. There are again two factors. Naturally, we try to… we said we are keeping high percentage of cash in hard currency, any move, download movement in FX rates from one quarter to another is impacting our cash balance that is converted to Turkish Lira. The other factor is we are now starting amortization of our club loan and the first installment was in the last quarter of last year. That also impacted our cash balance.

BINTLCIFFE J: Excellent. Thank you.

OPERATOR: The next question is from the line of Drouet Hervé with HSBC. Please go ahead.

DROUET H: Yes. Good afternoon. Thank you, as well for the presentations. Two questions on my side. Firstly, on employee expenses, there has been only a mid-single digit growth. I was wondering with the high inflation we have, should we expect more inflation on the expense of employees in 2019 and from which quarter do you think we may have that effect. And secondly, on CAPEX, I mean if we clean…if we look at your guidance for 2019 and we removed the impact of the accounting change in IFRS 16, it still points to a relatively quite significant increase of CAPEX for '19. Could you give us a bit more… light on where do you think this increase of CAPEX will come and if you have plugged in any assumption of currency movement that may impact the CAPEX. Thank you.

AKTAN K: For the first question, the impact of inflation on people related first obviously, we will adjust the wages and salaries in line with the inflation but it doesn't start from January, it is partially adjusted until the mid-year. We have different terms during the year for salary increases. It should give us a higher increase in people related costs compared to last year, that's for sure. But we will try to keep the total growth under the level of the inflation by executing the synergy and optimization program.

And for the CAPEX side, actually we don't specifically assume a very aggressive FX scenario for 2019, meaning we don't assume a negative or increased CAPEX due to the FX rate. We didn't assume any significant one-off large items to stand on CAPEX, it will be for a business as usual and if you look at the last 2 years especially, we tried to increase the percentage of CAPEX that we are spending in the infrastructure, not very significantly but still more than the other year and this came on the back of increased revenues and increased return on those services. So it's a growing market, it has growing customer base and we feel like it's the best return that we really get on our CAPEX will be spend on our basic infrastructure projects. So we will continue executing this program throughout the year but again we don't assume any major one off item.

DROUET H: All right. Yes, thank you very much.

OPERATOR: We will continue with the next question from Mr. Özbek Mete from Unlu and Company. Please go ahead.

ÖZBEK M: Thank you very much for the presentation. I just wanted to make clear something about your guidance. You are guiding TL 10 billion to TL 10.1 billion of EBITDA including the impact of the IFRS 16 reconciliation I think which you expect to have a positive impact of TL 650 million to TL 700 million. If we convert it to the comparable EBITDA, it should be more or slightly lower than TL 9.5 billion.

And if I make the calculation and assumption correct, it points out to around 40% EBITDA margin guidance at the comparable level with 2018 reporting standards. So if it is correct…if my calculation is correct, where do you see the reason of declining EBITDA margin on a year-over-year basis for 2019?

AKTAN K: Well, to be honest, we tend to see this as a slight, you know, performance compared to 2018. It was 41%. You're right. When we make the calculation by excluding IFRS 16, it comes something like 40%. But you should also consider that we will be growing the revenue by mid-teen numbers which means there will be in absolute terms significant improvement in EBITDA, and we would have mentioned the impact of the inflationary adjustment in our cost base. We try to be more cautious on providing around 40% like-for-like...40% EBITDA margin on this guidance.

ÖZBEK M: Thank you very much. That's clear.

OPERATOR: The next question is from Rishad, Ahmed with Goldentree Asset Management. Please go ahead.

RISHAD A: Hi, there. Just on the point of CAPEX. Could you maybe talk a little bit about the outlook for the rollout of 5G? What the timing potentially is for spectrum auctions and when you are, you know, when you and… thinking about rolling that out, and what sort of magnitude in terms of cost we should factor for that? Then if... are there any costs in your mind for, let's say, concession extension over the next year or two that we should consider as well? Thank you.

DOANY P: Thank you Rishad; actually or Ahmed. Now, let me start by concession subject first. As you know, the earliest renewal dates on the concessions are 2023 for the 2G license which in this state is Turkcell. 2026 on the 2G would be this Company, I believe Vodafone as well. And then we have the fixed concessions in the same time, 2026, the 3G and 4G expire on 2029.

Now, first let's look at 5G expectation, the 5G expectation, firstly, would require that the 4.5G or 4G LTE license be minimum 15 years from the date of the issuance of the 5G. So we're talking 2029 in itself would need an extension, otherwise the 5G would necessarily have to be spotty type coverage realistically and the issue with 5G mostly, as you know very well now, is that people are mostly concerned on their coverage obligations.

So the way we are approaching this here in this country and the way we are talking to decision makers and also sector wide is that we need to see that the mobile investments that will be made in 5G benefits from the 4.5G license terms. The 4.5G license terms are technologically neutral, they're not specific in terms of technology, but they have, of course, the spectrum band associated with each party's license in the 800 megahertz band, etc., all the way up.

And going forward with 5G, whatever the new bands would be, it is logically possible to expand the existing licenses, 4.5G with additional spectra bands, obviously for payment and receivables payments. We are seeing examples now where countries are not overcharging for this; we are seeing countries that are overcharging. And then, of course, will be the term, the term would have to extend, obviously, towards the mid-2030.

So if we look at the markets' expectation in this particular country and how the licensing may fit within this, we can see now that the mobile licensing needs to cater to, let's say, mid-30 to end-30s as a duration, defining the coverage obligation of 4.5G is frankly sufficient to provide for the government interests relating to coverage… their coverage, for example, and there are, as you know, that universal service network, for example, to provide areas that are uneconomic to cover. So you can say that the public interest has been mostly covered to over 4.5G. Therefore, it is our hope that 5G will be a lot more opportunistic rather than obligatory and that should be done by competition.

Now, if this assumption is right, and there's no reason for it you know, not to be right, I haven't seen any negativities in this regard. We would like to see the market actually, that the market should be looked at in terms of what bandwidth you are providing for customer which takes you to the 5G level, where you can monetize much higher bandwidth if the customer wants it. And then you can monetize capacity which is the gigabytes that the customers use. That, of course, will be very helpfully done over a 4.5G, and of course, we still also have 3G licenses and so on over that, the value of which is uncertain and what bands will be needed.

So you can see here that one advantage, we are very keen on, is a form of radio slicing in the 4.5G capacity. What this means is that operators will be able to slice that capacity because we really have good spectrum in this band, all the operators and we can then provide fiber to the most economic point to any operator. This is what we call fiber to the site, which I alluded to, partly, in my introductory statement.

What this would mean is that the other operators will be able to have constant access, fiber access, to their radio access points whether they are 4.5G access point or even 5G or even, by the way, advance wise, regardless of what the customer's needs. This seems to be the direction… at least this is the last discussion we had at the center just 2 days ago at the level of the CEOs of the companies and the related departments.

So going in this way, as we now have a model also as to how this can be done. We see that we can have minimal replication, minimum duplication of unnecessary infrastructure. They benefit from the extensive duct bank of this company. How the fiber itself will be financed of course also there are two models FTTS is one model. So we see this market direction is important. Then Argela is one of our subsidiary companies have invested 5 years of R&D in radio slicing and Software Defined Network are active now in the Open Network Forum and ONAP and have done successful installations with Verizon and Telefónica, for example, and Orange.

So we see that the direction operators may take here in this market we will offer this to both Vodafone and to Turkcell. We will be the offering partner with something that covers the ULAK you know, which is the local base station. The obligations on our 4.5G is 45% of our base stations to be local, but of course that could not be met, while we are still as the primary provider they have practically all of Vodafone, most of Turkcell and a good part of ours.

So going forward, we see the opportunity of slice with a fiber access, extend 5G through 5G new spectrum on the 4.5G authorization agreement, extend its term. This seems to be a practical way of doing it which is not overly expensive to the sector and allows us to serve the market and have some you know, reasonable level of competition but with minimization of duplication. This is also why, by the way, our sharing over 4.5G, for example, active sharing, I think that I mentioned earlier, are also very important for all of us.

And the fixed mobile of CAPEX contribution will work very well on our fiber to the site FTTS model, which is very key for this type of direction that the sector can take. So we have had this level of discussion with all the operators and we think that if we offer this solution, the government side of course are fully aware of all of this, find that this is a win-win all the way around situation. So we are, as we say, seeing the markets… the existing authorization agreement and benefiting from the local content obligation. By that, I mean, ULAK to extend it to our Argela solution. We find this can be a workable approach, of course, so long as the other parties who are using Argela can get it on a fair price.

And that's the basis that we are working with; they will get the same price we would pay. This will also support ULAK. They cannot go beyond the 4G or 4.5G, whatever, LTE standard, you see? That's kind of like what we expect. So we are very...as an operator, we may benefit from this. We can lower the cost of the other operators, so they also don't need to unnecessarily invest. In that sense, we are optimistic as to where this market may go, especially if we are able to provide a near 5G experience over 4.5G with slicing which means people can use their existing handsets but get a spectrum... rather, get a bandwidth that they're paying for.

Operators can then monetize bandwidth, not only capacity. I mean, today if you have a high ARPU customer that is getting very cheap gigabytes but just happens to pay more if he wants to make sure that he gets more bandwidth secured, that can give a very good opening, for example, to Turkcell as they are leading in that segment of the market and we can enable that through technology which we are developing and is now working, plus of course our extensive fiber where they need it.

Clearly, where they can use their own fiber, they will be using that. So when it is cheaper, they would use ours. So in that sense, that's the basic state of play. At least I can tell you as a sector.

RISHAD A: It's just… if you were to do all of this, I guess, how much would it cost? And is this a 2020 cost? Is it a 2021 cost? Or when should we expect it?

DOANY P: I don't think that we will see any high demand or expectation from the government side for a very early type 5G licensing. More importantly, we will be ensuring the 4.5G and perhaps some level of slicing that we can do in the next let's say, 1 or 2 years. So I mean, more than that, I don't see an immediate expectation for a license or a network obligation, this is how I can answer you. And we don't think that it will be overbearing on us if and when it comes.

RISHAD A: Thank you. And then with regards to just the concession extension, is that something that you would expect to have any cash outflow for over the course of the next couple of years?

DOANY P: Well, on the mobile side, the examples that I gave...the government will have the choice of putting a formulation on to, for example, if you are extending your 2G license, what is the value of that license today other than, frankly, the powers of it? So Turkcell, for example, would benefit from having those powers extended. Ours peaks in 2026. So that's why we are looking at this really totally as a sector. So Turkcell would be able to unlock value earlier. And then this idea of a tower company they become more viable.

As you notice from the way I'm giving you the answer is that we are really looking at this all together as a sector to see how this may work. Then on the fiber part, the solution would be the one FTTS that I gave you. And frankly, between these 2 with active sharing, it doesn't really matter when anything, mobile comes so long as the renewal terms are defined by a formulation, which we have now proposed a formulation that we are all happy with.

And so I'm kind of like optimistic on that level in relation to a payment. The other option, of course, is to alter the month… the revenue share as we now pay, for example, 7.5% plus 5% at the moment. That's another way for the government to consider charging us. They will be charging our revenue rather than charging money upfront.

On the fixed concession 2026, that one can also operate in the same way, by the way. And that's 2026 so it's a bit further out but we would like in the course of this year and next year to get actually clarity on this. We have shared let me say, I can call it a realistic expectation of what this model would be and we have not seen any negative signs on it. So again, even on that, we are optimistic.

RISHAD A: Thank you.

OPERATOR: The next question is from the line of Kazaryan Anna with VTB Capital. Please go ahead.

KAZARYAN A: Yes. Hello, thank you for taking my questions. Sorry, I was disconnected. Sorry if I missed something. So my first question is about consumer behavior during fourth quarter and January this year. So due to these recent upward price adjustments, do you see any change in the customers' behavior? Do you expect that customers' additions might slow down significantly in 2019? Or consumer traffic consumption will slow down? And my second question is about the cost of hedging. So due to the fact that you have expanded your hedge ratio, could you update what's the current cost of your… average cost of debt, including hedging?

DOANY P: Okay. Thanks, Anna. Look, the strategy of the company under the current market conditions are...really not affected that much in the sense that, first of all, as you know that we have entry packages, for example, especially on the broadband part, where we need to increase the Internet penetration. So that's an absolute must and necessity, a strategic requirement for this company. And we have a cost-effective way of doing that, that the regulatory authority have approved. It is not of course exclusive to TTNET, it's actually going to the entire market. This one, for example, definitely is not affected by inflation.

On the fixed voice, of course, that's more of a defensive strategy to keep something going, we have been a bit more careful in that sense and we have executed, I think, successfully in that regard because this is more of a protective approach.

In relation to going to up sells, for example, where we have to provide levels of inflationary increase, we have to consider one thing. That if you compare an inflationary increase between, let's say, a telecom service and electricity… home electricity service, in your home, for example, when the bill increases, you're not actually using much more electricity, you're not consuming more kilowatt hours where you are. So when they increase the price per kilowatt hour, so what happens is that you are paying a higher price and consuming the same amount of electricity. So you can choose to consume less, that's your choice. But in reality, most people are consuming what they need.

The difference with a telecom is that they are getting a lot more data, which is the new demand. Voice, most people have more voice than… they're paying for, more voice than they are using, the same applies to message. So the thing really is about data. And in this type of a market, people are happy to pay for that additional data with an inflationary increase because it is an inflationary market.

But we have been sensitive to the government's objective of limiting the inflation increases. And in this regard, we are in a good situation because we are actually giving our customers more. So all operators kind of.. like.., gave the right thing to the customers at the time that suited them. That's how the… call it, let's say, we manage the expectations of the customers.

So what you actually are giving your customers is more capacity, they get more capacity. What we have to be careful with is when we give them bandwidth. So, you know, it means that if someone wants capacity in broadband and they take, for example, a cheaper package because it has lower speed, the one who can afford to pay more would then use with a full inflation as you should because your costs are also going up.

That's basically how it is managed between us. And the inflation increase expectations, meaning that we are careful with inflationary increases. In fact, we passed that test as well. So we have no concerns as well as that regards.

AKTAN K: That is Kaan, yes. The cost of debt and cost of hedges. I will try to give you some numbers and I think it will help you to make a calculation on the cost of overall financing. At the end of the quarter, we had roughly USD 3.8 billion gross debt, which is purely dollars and euro-denominated loans. And our total hedge portfolio, the value of it is USD 1.9 billion, in dollar terms, so which is 50% of the total gross debt. Our… normally, our debt in original terms, the cost of it is between 3% to 4%. The cost of that 50%, which is hedged on a different instrument, the average cost as of the year end is low to mid-teens level. This is, obviously…some of it was executed in the fourth quarter where we had higher costs. And some of it was executed in the prior quarters which had lower cost. But the latest average cost, is as I said, low to mid-teens.

If we are to execute as of today new transaction, it will come at mid-teens or slightly higher than mid-teens. But again, we will try to give similar data information going forward in every quarter if we have other transaction to be be executed.

KAZARYAN A: Okay, thank you.

OPERATOR: Ladies and Gentlemen, there are no further questions at this time. I will now turn the conference over to Ms. Gözde Çullas for any closing comments. Thank you.

ÇULLAS G: This concludes the conference. Thank you a lot for participating.

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