

TELEKOM SLOVENIJE D.D.

29th October 2015

www.telekom.si

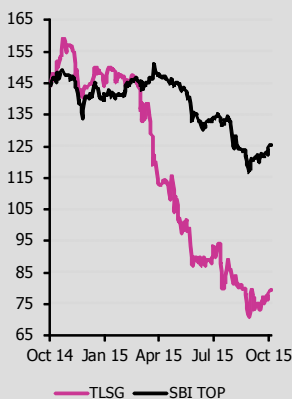
LJSE ticker: TLSG
Bloomberg: TLGS SV

Target price:
105 EUR

Previous target price:
105 EUR, BUY (28.8.2015)

Recommendation:
BUY

12 months stock performance in EUR



Stock data as of 29.10.2015

Market price (EUR)	78.0	Market Cap (EUR)	507.4
52 week range (EUR)	71.0-159.1	No. of Shares	6.5
Avg. daily trade vol., EUR(k)	111.06	Free float	26%
Average daily % of stock traded	0.014%	Dividend yield	12.8%

Price performance	3 months	12 months	Multiples:	TTM
			P/E	neg.
price change in %	-17.0%	-46.6%	EV/Sales	1.2
SBI TOP index change in %	-7.8%	-13.9%	EV/EBITDA	4.3
relative to SBI TOP index in %	-10.0%	-37.9%	EV/EBIT	283.9

Key figures (According to International Accounting Standards) Consolidated data in EURm

Income statement:				Balance sheet:			
million €	FY2013	FY2014	TTM	million €	FY2013	FY2014	TTM
Sales	799.2	764.9	745.2	Investments	30.6	18.8	8.8
Growth yoy	0.5%	-4.3%	-2.6%	Cash	59.2	23.9	9.3
EBITDA	237.8	218.2	212.4	Debt	411.6	369.3	394.3
Margin	29.8%	28.5%	28.5%	Net debt	321.7	326.6	376.3
EBIT	72.0	11.5	9.2	Equity	759.9	693.9	701.7
Margin	9.0%	1.5%	1.2%	Assets	1,389.8	1,343.4	1,328.6
Net income	52.7	1.7	34.5	D/E	54.2%	53.2%	56.2%
Growth	18.3%	-96.8%	1940.1%	ROE	6.9%	0.2%	4.9%
EPS	8.0	0.2	5.3	ND/EBITDA	1.4	1.5	1.8

Recent news and outlook revision:

- As expected, but not as we hoped, government (or SSH) still did not provide a strong message regarding what will they do with Telekom Slovenije stake after faltered privatization process in August-September. Possibly all are awaiting the completion of Telekom Srbije privatization for which Telekom Slovenije is bidding although it's not publicly known how they would finance it.
- Telekom Slovenije received a lawsuit by The Association for the European Collective Management of Audiovisual Works for EUR 2.4m due to obligations for the years 2010 and 2011. Telekom Slovenije believes claim is completely unfounded.
- Moody's international rating agency confirmed the credit rating of Telekom Slovenije at »Ba2« level with outlook still being negative. While Moody expected December 2016 bond refinancing will be done successfully and acknowledges strong market position and relatively low debt levels, Moody also recognizes adverse competitive environment which is expected to persist. We agree that bond refinancing will be successfully done in 2016.
- Several pending group structure changes were completed in Autumn. Firstly, merger of its Macedonian operations with Telekom Austria operations into ONE.VIP company. We note Telekom Slovenije owns 45% share (with option for an exit) while Telekom Austria 55% share. As net operating profit of One amounted to EUR 1.0m in 2013 and EUR 4.0m in 2014 we believe this will actually improve the bottom line. Secondly, Telekom Slovenije took over Debitel for EUR 15.8m. With this they gained 90,000 user and basically got back the stake in mobile domestic market that it lost in the last few years. Namely Debitel has a 3.9% stake while Telekom Slovenije 47.3%, while it had a 51.8% stake at end 2011. All in all both we view both transactions as positive.

Valuation commentary:

- Valuation is now hard to gauge due to pending changes, like preparation of exit from Macedonia, lawsuit provisioning etc. However main catalyst is completely unchanged, as lack of revenue growth potential and ASP pressures dictate Telekom Slovenije must step up the pressure for cost optimization. If this materializes, we can see profit even increasing from current levels despite negative top-line dynamic. But if states grip prevents economic measures to be deployed, then profit and with it future dividends is under downward risk.
- 9M15 results show EBITDA will surpass management guidance (EUR 198m) and likely also our estimate (EUR 209.1m). It seems revenue and price pressure will be less pronoun, although group changes are also making any estimation difficult. This is even more seen at bottom line, where EUR 50.1m in 3Q15 is likely under these effects. Again results will be above expectations as net profit in 9M15 now stands at high EUR 70.6m, more than we expected (but with unclear one-offs).
- Nevertheless we will for now maintain our price target of EUR 105 per share as upside is vast and warrants a buy recommendation. Implied EV/EBITDA is 5.0. After more detailed 2015 report is out we will be in a better position to give a forward estimate.

Privatisation disappointment.

High dividend yield.

Dominant market shares on the domestic market.

Substantial room for rationalization.

Mature domestic market.

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9M15 Results

Group changes limits the comparability, but all in all results above expectations

million €	9M14	9M15	YoY	3Q14	2Q15	3Q15	QoQ	YoY
Sales	579.3	559.7	-3.4%	194.5	184.5	192.0	4.1%	-1.3%
EBITDA	166.0	160.2	-3.5%	53.6	52.8	55.8	5.8%	4.1%
Margin	28.7%	28.6%		27.6%	28.6%	29.1%		
EBIT	47.8	45.5	-4.9%	13.5	13.6	19.6	43.3%	44.5%
Margin	8.3%	8.1%		7.0%	7.4%	10.2%		
Net income	37.8	70.6	86.9%	6.7	13.3	50.1	275.7%	643.1%
Margin	6.5%	12.6%		3.5%	7.2%	26.1%		

- Broadband connections stayed are now at 325,854 as the group no longer reports Macedonian data (38,039 users on 30.6.2015). Adjusted for this, number of connections is up by 3.3% due to foreign markets as number of connections on the domestic market stagnated. On the other hand mobile connections are down 2.2% YoY in Slovenia while fixed line is down by 4.8% YoY. Again foreign markets (ex Macedonia) achieved a growth of connections. Telekom Slovenije continues to bleed market share on the domestic market, although it remains the dominant player.
- Operating revenues are down 3.4% YoY with 3Q15 revenues down by lower level, namely by 1.3%. It is true however sales revenues are down more, since other operating income almost doubled versus the same period last year. Sales revenues are down 4.3% YoY. However Telekom Slovenia noted that we should take into consideration Macedonian One operations are excluded from recent months and contributed to revenues 2 months less than in 9M14 (One is excluded from 31st July 2015). On the other hand they recognize pricing pressure continued.
- Opex is down 3.9% YoY as well, again also due to group structure changes. Labor costs are down 9.9% to EUR 89.6m due to headcount. Namely headcount is down by 10% to 3,990, but this is due to exclusion of Macedonian operations which had 420 employees at end 2014. Without this effect number of employees is down by 21 versus end 2014. Cost of services is down 1.7% YoY while D&A charges are down by 3.0% YoY to EUR 114.7m. We note GibTelecom was divested therefore operating profit no longer accounts for its contribution, which stood at EUR 3.3m for 9M14.
- EBITDA is down 3.5% in 9M15 however up by 4.1% in 3Q15. This is encouraging. Also given the 9M15 numbers management guidance of EBITDA slightly below EUR 200m for 2015 will now almost surely be surpassed. This is very positive.

REVENUE (in EUR 000)	1Q14	2Q14	3Q14	4Q14	1Q15	2Q15	3Q15	Q YoY	9M YoY
Telekom Slovenije	166.231	162.754	163.491	156.606	156.513	157.409	167.361	2.4%	-2.3%
Other companies in Slovenia	11.262	13.690	13.572	17.953	9.822	11.281	11.639	-14.2%	-15.0%
IPKO-Kosovo	15.475	16.655	19.819	17.632	16.544	16.578	19.367	-2.3%	1.0%
Macedonia	17.472	19.376	20.151	19.313	18.181	20.490	6.770	-66.4%	-20.3%
Other SEE companies	6.841	5.274	4.644	5.957	4.892	5.332	5.716	23.1%	-4.9%
Total	217.281	217.749	221.677	217.461	205.952	211.090	210.853	-4.9%	-4.4%

EBITDA (in EUR 000)	1Q14	2Q14	3Q14	4Q14	1Q15	2Q15	3Q15	Q YoY	9M YoY
Telekom Slovenije	50.053	45.116	40.405	35.380	42.355	44.438	44.931	11.2%	-2.8%
Other companies in Slovenia	-0.147	0.636	0.443	0.674	0.301	0.487	0.945	113.3%	85.9%
IPKO-Kosovo	5.854	6.298	7.943	6.057	5.809	5.228	7.972	0.4%	-5.4%
Macedonia	2.068	2.369	3.913	1.802	2.058	2.668	1.053	-73.1%	-30.8%
Other SEE companies	0.739	0.645	0.985	2.262	1.133	1.200	1.259	27.8%	51.6%
Gibtelecom	1.077	1.309	0.853	0.819	0.000	0.000	0.000		
Total	59.644	56.373	54.542	46.994	51.656	54.021	56.160	3.0%	-5.1%

Net operating profit (in EUR 000)	1Q14	2Q14	3Q14	4Q14	1Q15	2Q15	3Q15	Q YoY	9M YoY
Telekom Slovenije	16.670	24.272	6.785	-29.801	11.265	18.192	40.057	490.4%	45.6%
Other companies in Slovenia	-0.851	-0.089	-0.286	-0.233	-0.512	-0.356	0.027		
IPKO-Kosovo	-0.528	-0.208	1.775	-0.475	-0.526	-1.139	1.512		
Macedonia	-1.586	-2.788	0.319	0.049	-2.087	-1.574	-0.272		
Other SEE companies	-0.013	-0.096	0.126	1.128	0.262	0.259	0.262		
Gibtelecom	1.077	1.309	0.853	0.819	0.000	0.000	0.000		
Total	14.769	22.400	9.572	-28.513	8.402	15.382	41.586	334.5%	39.9%

- All of the group changes and divestments have likely boosted net financial result. Namely finance income is up 183% to EUR 38.5m with financial costs down 22% to EUR 13.8m. On the other hand share of loss of associates and Joint Ventures increased to EUR 4.4m.
- All in all EBT surged by 64% to EUR 65.8m. Effective tax rate additionally boosted bottom line to EUR 70.648 or by EUR 4.8m due to deferred taxes.
- CAPEX amounted to EUR 64.5m down 4% on the year with majority spent in Slovenia.
- Net cash from operations amounted to EUR 108.1m in 9M15 versus EUR 129.9m in 9M14.
- Equity stands at EUR 701.7m with retained earnings of EUR 29.3m and reserves at EUR 218.5m, out of which EUR 112.1m other reserves. Provisions are now at EUR 57.7m.
- Debt stands at EUR 394.3m with cash item at 9.3m and ST investments at EUR 3.6m. Reported net debt is therefore at EUR 381.5m, up by 11% versus end 2014. However we should note that Telekom Slovenije has EUR 5.0m of investment property and now also EUR 120.6m of LT investments versus EUR 13.4m at 2014 yearend. This is due to Macedonian operations where it has a 45% stake. We believe it's likely a further exit will happen and that would substantially lower the debt. Balance sheet is therefore still healthy.

Market share dynamic on the domestic market is still negative.

Revenues down 3.4% YoY but up in 3Q15 if adjusted for Macedonia.

Also Opex is down as well YoY.

Therefore while EBITDA is down, it's still above expectations.

Change in status of Macedonian operation is severely affection comparability.

Net profit boosted severely by deferred tax and net financial result.

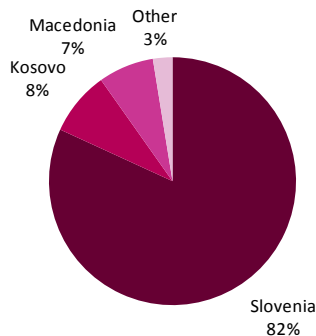
While LT investments are now at EUR 120.6m.

Top5 shareholders:	
Republic of Slovenia	62.5%
KAD	5.6%
SDH	4.3%
Perspektiva FT	1.5%
Modra Zavarovalnica	1.4%

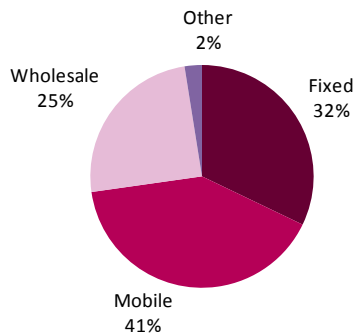
Brief Company profile

Telekom Slovenije Group is Slovenia's leading provider of telecommunications services in domestic and international fixed telephony, mobile telephony, VoIP, IPTV and broadband internet services. The Group also offers telecommunication network construction and maintenance services through its subsidiary GVO d.o.o. and owns a stake in a media company. Telekom Slovenije also operates in Bosnia and Herzegovina, Kosovo and Macedonia (but now in joint company with Telekom Austria) while it exited from a 50% stake in Gibtelecom during 2014.

Group sales by region (1H15)



Group sales by product (1H15)



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Sašo Stanovnik, Head of research. On the day of the public release, the author of the recommendation did not hold securities of the issuer.

First release of the recommendation was performed on 13.04.2010.

Quarterly updates are planned for data, valuation, target price and recommendation.

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