



Rostelecom

CONFERENCE CALL TO DISCUSS ACQUISITION OF TELE2 RUSSIA

Company: Rostelecom

Conference Title: Acquisition of Tele2 Russia

Presenter: Ekaterina Ustinova, Head of IR

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Participants:

Mikhail Oseevskiy – President and CEO

This English language transcript has been generated from a simultaneous translation of a Russian language call.

**Represents remarks corrected or inserted to reflect the content of the Russian language call*

Ekaterina Ustinova, IR: Good afternoon, ladies and gentlemen. We are happy to welcome you again for the second time this month. Just last week, we updated you about our performance of Rostelecom for nine months of this year. And today's conference call is perhaps about one of the landmark events, not just for the company but for the industry in general. That is the acquisition of our control over Tele2 and creation of an integrated digital telecom services provider.

The main speaker on this call is our CEO, Mikhail Oseevskiy. We will, as usual, start with a presentation, that will be followed by a Q&A session. This time you will have an opportunity to ask questions through webcast. So please either during the presentation or after it, you are welcome to do it if you so wish. And we are asking

the analysts as ever to ask the questions in the language of the lines for which they are connected.

Let me once again remind you about our disclaimer. Certain statements made on today's call may contain forward-looking statements about future events and such statements are subject to risks and uncertainties, and as such, actual results may differ from the ones discussed today. A lot of such factors are outside of the company's control and with a view to the above, we do not recommend to unduly rely on today's statements and we do not undertake to publicly review such statements except when provided for by the legislation.

We're now ready to start. Mikhail, over to you.

Mikhail Oseevskiy, CEO: Good afternoon, colleagues. And I guess that today's discussion should have a motto that everything that should happen, happens at right time. The transaction of Tele2 consolidation has long been in discussion in preparation, and today we would like to share with you all the details, given that all the mandatory documents and all directives have been passed and we are now proceeding to the implementation phase.

We have circulated quite a busy, quite a detailed presentation that explains why we are buying Tele2 and what would be the benefits in the joint company? What synergies we are expecting to see?

And in my short discussion, I would like to focus on the structure of the transaction because it's an important aspect of that transaction. We consolidate 55% of Tele2 as a company, as a corporate entity. And with that, we have obtained an independent evaluation of Tele2 and Rostelecom itself. That was done by Price Waterhouse Coopers. Our financial advisor on this transaction was Citibank.

Following the valuation, 100% of equity in Tele2 was valued at RUB240.5 billion, given the price of one ordinary share at RUB92.87. And the total share price of Rostelecom's ordinary shares is RUB239.1 billion. And as agreed with our appraiser, we decided to see or to take the evaluations as equal as RUB240 billion. So, we somewhat increased that the value of ordinary share of Rostelecom and reduced the value of the 100% of equity in Tele2.

So, for the transaction, one share in Rostelecom, its price is at RUB93.21. The consolidation transaction comprises three elements. First, the swap of 10% of ordinary shares of Rostelecom for 10% of shares in Tele2. The shares sit in the

balance sheet of our subsidiary, Mobitel, that's our legacy entity that came about as a result of some past transactions, and I'm sure that those of you have been following Rostelecom for a while are well aware of how that subsidiary and that stake happens to be.

In accordance with president's decree and government's resolution there will be an additional share issue of Tele2 versus the shares of Rostelecom that will be offered in a private placement to VTB at the price that I've already mentioned RUB93.21.

That transaction should help us consolidate in Rostelecom's balance sheet from RUB66 billion worth of assets, and again, all the shareholders of Rostelecom in accordance with the existing legislation may exercise their pre-emptive rights and participate in the share issue. So hypothetically the situation is possible, whereby Rostelecom will receive additional cash when other shareholders, other than VTB, acquire these new shares. And the cash obtained from that additional share issue as well as any additional cash that we will consolidate in the amount of RUB42 billion. So all of that will be the funds and means to acquire the remaining shares in Tele2.

So in general, the cash components of the transaction will be RUB108 billion. Apparently, that is a very substantial transaction for the market and for Rostelecom. We have been preparing this transaction for a long time. We have discussed it with the government, with the existing Tele2 shareholders. And during the discussion, Tele2 has made an enormous progress having transformed itself from an outsider and a discounter to one of the market leaders that demonstrates very strong pace of development of its operational and financial results.

It's now a profit-generating company, demonstrates quite good profits and EBITDA. It has got good customer base at the federal level and it's got very high NPS score. So we believe this is a very timely move for us to increase our ownership in that company to make it wholly-owned.

That's it from my side. I'm now prepared to answer your questions.

Ekaterina Ustinova, IR: Okay, thank you. We're now ready to open up the Q&A session. Let me once again remind to the analysts to please ask the questions in the language of the lines for which you are connected. And you're also welcome to ask your questions through the chat.

Operator: Ladies and gentlemen, to ask a question please press star one on your telephone keypads. Please make sure that your mute button is off. If you want to remove yourself from the queue, please press star two. Again, please press star one to ask a question. Our first question comes from and Anna Kurbatova, Alfa Bank. Please go ahead.

Anna Kurbatova, Alfa Bank: Good afternoon. Thank you for this conference call and congratulations on completing this long journey and this onerous process of preparation. I would like to have some more color about the current state of affairs at Tele2. And in your presentation and press release, you mentioned valuation based on EBITDA multiples. So, can you please share your expectations in terms of 2019 and 2020 EBITDA? I'm also interested in the potential CapEx that is expected in 2019 as well as in 2020 that would be also very helpful. And also, it would be very useful to understand the net debt level and the structure of that net debt of Tele2 at the time of the transaction? Thank you.

Mikhail Oseevskiy, CEO: We have a bit of a unique event today. Tele2 EBITDA for 2019 could be some RUB64 billion, well, given the new IFRS standards. And this is a good result. There will be a substantial increase year-on-year. And we expect 2020 EBITDA on a standalone basis to be at least RUB70 billion.

In terms of net debt, today it is RUB120 billion. And if we, for accuracy, add here leasing liabilities and the other adjustments required by the IFRS, that would bring the number up to some RUB140 billion.

Ekaterina Ustinova, IR: Thank you. Next question please?

Operator: Our next question comes from Maria Sukhanova of BCS.

Maria Sukhanova, BCS: Good afternoon. I have two questions. First, the transaction when you swap your 10% of quarterly treasury shares in exchange for the shares of Tele2, who do you transfer them to? Who would be the shareholder – the holder of that treasury stock? And my second question is a bit of a more technical nature. Maybe you're not prepared to comment at this point. In terms of Tele2 consolidation, I understand you've got a lot of business with Tele2. And if you're going to consolidate Tele2 revenue, I really wanted to understand what would be the impact of that. There wouldn't be a direct addition, if you will. There will be some elimination. So, I'd like to understand the magnitude of that elimination.

Mikhail Oseevskiy, CEO: The swap of the 10% of shares held in Mobitel's balance sheets will happen with SPV Telecom investments. That's a Russian company that represents the interests of the existing shareholders in Tele2. The structure of that company is something we cannot share with you because it is up to our partners to decide on that.

In terms of the intra-group trade, if you will, and the elimination, that will be carried out in the IFRS financial statements. I guess we will be able to update the market on that early next year. But the total intra-group turnover is at the level of some RUB10 million to RUB15 billion.

Maria Sukhanova of BCS: Thanks.

Operator: Our next question comes from Igor Goncharov, Gazprombank.

Igor Goncharov, Gazprombank: Yes, thank you. I have a follow-up on Tele2. Indeed, we have seen some very strong growth rates, growth in revenue and EBITDA in particular in 2019. But the growth rates that the company has been demonstrated in – demonstrating in its press releases in terms of EBITDA in particular have been, in part, due to the implementation of the new IFRS standards, and I understand that the comparison basis was under the previous standard. So, could you please give any guidance in terms of 2019 EBITDA growth in terms of 2018. You gave us a guidance in terms of absolute EBITDA numbers. But if we were to compare apples to apples, so if we were to compare the 2019 versus 2018, where both periods are either under new standards or under old standards, that would be very useful.

Mikhail Oseevskiy, CEO: Indeed, having to live in two worlds for a long time is something that we don't like and something we wouldn't advise anybody to do so. In terms of Tele2 EBITDA in 2018, that was RUB43 billion apparently under other the then applicable standards. And now for 2019 is, as I mentioned, the guidance is RUB64 billion.

In terms of how to adjust, well, you are professional in that I guess, and you can make your own adjustments. As far as I remember, it is something around Rub 6-8 billion.

Igor Goncharov, Gazprombank: Well, the reason I'm asking is that because sadly up until now Tele2 disclosures have been quite ascetic, so it was quite challenging to understand the potential effect.

Mikhail Oseevskiy, CEO: Yes, the company was not quite public. And post-consolidation, you would certainly have much more public information that will be disclosed, as I mentioned during the first quarter 2020 disclosure.

Igor Goncharov, Gazprombank: Thank you. And my next question is whether this transaction creates any obligation for Rostelecom or its shareholders to make a mandatory offer for a buyout for Rostelecom minorities?

Mikhail Oseevskiy, CEO: Well, given the target shareholder structure, we don't see any need under the legislation to make any mandatory offers, but that's less a question to us, more the question to VTB that will be big shareholder in the future shareholder structure of Rostelecom. Thank you. Next question please?

Operator: As a reminder, if you wish to ask a question, please press star one. And the next question comes from Ivan Kim.

Ivan Kim, Xtellus Capital: Yes, hi. Couple of questions from my side. First about the dividend policy. Is it your intention to continue with the dividend policy where you guide for a particular payment per share? So now there will be more shares and do you still intent to pay RUB5 per the increased number of shares? And my second question is about synergy. Have you looked at the cost synergies with Tele2? Thank you.

Mikhail Oseevskiy, CEO: Our strategy is to ensure consistency in dividend policies. So, I would like to emphasize once again that all the base principles that have been formulated previously, such as targeting up the payout of at least 75% of free cash flow and at least RUB5 per share. We reaffirm that we will seek to observe those guiding principles in the future.

And since this question hasn't been asked but I guess it's somewhere in the queue, let me preempt that the hypothetical question by saying that we have discussed in considerable level of detail our approaches to dividend payments because we've got to consolidate a considerable cash amount of RUB42 billion by the middle of next quarter, we made that decision, a one-off decision not to pay dividends for 2019 and to pay the dividends in full compliance with the dividend policy that I've now just mentioned in the summer of 2020.

I would like to, once again, emphasize that this is a one-off decision related uniquely to this particular transaction and the timing of it. We believe that the

payment of dividends twice a year is quite beneficial for both the company and our shareholders and we intend to maintain this approach going forward.

In terms of the synergy, an integration – or the integration committee has already started its operation that consists of senior executives of both companies as well as our advisors from McKinsey. And among other things, we intend to look at the synergies both on the additional revenue side and the reducing cost side, that is the usual expectation of such a transaction.

I don't want to give you any numbers at this point in time because we're only starting with a separate. But I guess that by the time of completing that transaction and we are targeting to complete this at the end of February, early March, we should have some guidance there.

Today, the Boards of Directors approved the date of the EGM to approve the additional share issue and that's 18th December. After that, the offering circular will be registered with the Central Bank and the share ratio will take place. The existing shareholders will be able to exercise their pre-emptive rights if they so wish.

And again, as I said, in the middle of the first quarter next year, we are targeting to complete all the legal and technical actions. Thank you. Let's take a question from the English line. Let's take a question from the English lines.

Operator: There are no questions in English at this time.

Ekaterina Ustinova, IR: Okay. Then we'll take questions from the webcast.

Operator: Next question comes from Denis Kuskov of TelecomDaily.

Denis Kuskov, TelecomDaily: Hi. How will this transaction impact the plans of 5G developments in Russia? Now in the M2M, Tele2 doesn't play the leading role unlike MTS and MegaFon. Would it be able to take a more active stance after the transaction?

Mikhail Oseevskiy, CEO: Well, it's worth of saying that the M2M segment, the machine-to-machine segment is almost non-existent in this country. The projects developed by Rostelecom together with Tele2, now mostly are focused on data collection from various sensors and meters, energy meters such as heat, electricity and other power meters and energy meters.

We are a key provider under the contract for heat metering in Moscow, where we collect that information from all the meters and sensors that are installed and will be installed in Moscow homes. And we are discussing similar projects in other areas. So, making statements that some other companies are leaders while others are outsiders is perhaps not entirely appropriate.

Operator: Your next question comes from Tatyana Belyakova, Russia Today.

Tatyana Belyakova, Russia Today: Will Invintel B.V. of Alexei Mordashov and Rossiya Bank, will they get shares or cash in exchange of their stake?

Mikhail Oseevskiy, CEO: We can't answer this question at the moment. As I explained, 10% of Rostelecom's shares were being swapped for Tele2 shares. And our shareholder will be an SPV called Telecom investments and which legal entities will be the shareholders in that SPV is something that we don't know. This is a question to be addressed to those other parties.

Julia Tishina, Kommersant: Why the shareholder agreements with VTB about retaining control in Rostelecom is for four years? Why exactly this period of time? After that period, VTB will be able to sell down. So why is it four years for preserving the government control?

Mikhail Oseevskiy, CEO: Well, again it's a question to the government, to the state that is the period determined by the president and the government. We, as management of private corporate entity, cannot address these issues of our state significance.

Anastasia Skrinnikova: How will the Tele2 company be managed? Who would be the management and what joint projects will there be?

Mikhail Oseevskiy, CEO: Well, we have explained already that Tele2 will continue as a standalone subsidiary. We will preserve its management in place and Rostelecom will exercise its management through corporate procedures. The current Tele2 team demonstrated its efficiency while operating in a challenging environment, while having to catch-up and the fact being a challenger company, we don't see any needs for any replacements in its management. But, of course, we'll discuss any opportunities to leverage on the experience of both Tele2 management and

Rostelecom management. There might be additional synergies there also at the level of managing the holding.

Operator: Next question from Julia Tishina of Kommersant.

Julia Tishina, Kommersant: What would be the sources for the RUB42 billion?

Mikhail Oseevskiy, CEO: Well, to be fair, we already have a queue of banks who want to lend to us.

Ekaterina Ustinova, IR: Now we would like to take a question from the English line.

Operator: We will now take our first question in English from Ondrej Cabejsek from UBS. Please go ahead. Your line is open.

Ondrej Cabejsek, UBS: Hi. Thank you. Two questions for me please. Just to clarify on the dividend. Do I understand it correctly that you are cancelling the second dividend for 2019 or are you just postponing it into 2020? I didn't quite understand. And the second question for me please in terms of the transaction value is it – do I understand correctly that you are basically paying this multiple or this enterprise value without having done any due diligence at this stage on synergies? Thank you.

Mikhail Oseevskiy, CEO: About your first question regarding the interim dividend. For 2018, the company paid in early 2019, the company paid an interim dividend. We believe that this is the right approach and we continue to observe it in the longer term. But at the same time, given the need to consolidate quite substantial cash to pay for Tele2, the company made a temporary decision not to pay interim dividends for 2019, in respect of 2019, but it will be paid in full observing our dividend policy, so at least RUB5 per share in the summer of 2020.

Okay. And regarding the synergies and whether they have been accounted for in the valuation. The answer is yes, it has been included by the appraiser into both evaluation of Rostelecom and Tele2, but we will continue our efforts. We believe that there may be some potential for further refinement.

Ekaterina Ustinova, IR: Thank you. We have more questions from the Russian line.

Operator: Yes, we have an additional question from Anna Kurbatova of Alfa Bank.

Anna Kurbatova, Alfa Bank: Yes, hi. Thank you once again. Thank you for taking my follow-up. In fact, I have a couple with your permission. First, the shareholder agreements. Will you disclose any details, any highlights of that to investors or publicly, so if it's not the full text of the shareholder agreement but at least the key points. My second question is regarding the presentation. On page 13, it says that the maximum size of share issue is up to 1.2 billion ordinary shares. Can you please explain this number as well? So why this amount? Is that potential reserve for the potential exercise of the pre-emptive rights? And also, on the next slide, you provide the target shareholder structure, which has ranges in it. So why the ranges there and what influences that?

Mikhail Oseevskiy, CEO: Yes, let me start with your last question indeed. The maximum amount of shares to be offered is just under 1.2 billion. We proceeded from the existing shareholder structure. If all of them were to exercise their pre-emptive rights, then the size of the share issue would be as mentioned on that slide.

Apparently, it is not likely to happen. However, the legislation requires that we follow this approach. That is why, our after-transaction shareholder structure, as we presented following the share issue, will depend on whether the shareholders be willing to exercise the pre-emptive rights or not and which of them will be willing to do so.

The transaction envisages that the state plus VTB plus VEB shares. So those combined stakes will ensure the next real level of ownership for the company. As far as the Rosimushchestvo agreements or the Federal Property Management Agency, that agreement with Rostelecom is not a part of it, so I cannot disclose the details of that.

But the logic is clear. The government clearly believes that Rostelecom remains key player in the development of the national digital infrastructure and through various means, including through the shareholder agreement we want to continue to influence its operation.

Operator: Thank you. And we'll take another question from the Russian line. And that's Igor Goncharov.

Igor Goncharov, Gazprombank: Yes, hi. Thank you for taking my follow-up. I've got a couple. First, continuing on dividends. And I understand that you will continue to

calculate those based on your free cash flow of the combined company as I understand. Can you please give us any guidance in terms of Tele2's free cash flow historically or for some future periods, as I can see for 2018 at least they did not disclose this number. That was my first question. My second question is about the level of net debt in the consolidated company. Again, as I understand, with the net debt to – or the net debt to EBITDA may come close to the 2.5x, which only recently you mentioned that the maximum leverage. So, are you envisaging any steps to reduce the net debt and leverage, or do you believe that the net debt post the merger will be comfortable for you? And my third question is of a technical nature. You mentioned that Tele2's net debt is RUB120 billion, but I don't think I was able to hear about the non-financial lease obligations. Can you please repeat those answer?

Mikhail Oseevskiy, CEO: In terms of the free cash flow, well, I suggest that you wait for the consolidated financial statements in the first quarter of 2020 and there you will be able to see the potential guidance for the merged company. But again, all the dividend policy provisions will be supported by the financial results.

For us, as the senior executives of the merged group, it is important that we continue with our conservative debt policy. So even though we will have to raise our debt of approximately RUB42 billion, we will remain within the band, the leverage band that we believe to be the maximum for our company of our size, which is 2.5x of net debt to EBITDA will still be under that maximum, even if close to it.

And various other obligations, the lease obligations and other such obligations, we believe to be at the level of RUB17 billion to RUB18 billion in addition to the net debt of RUB120 billion.

Ekaterina Ustinova, IR: Thank you. We will once again take questions from webcast. And now Anna Balashova, RBC.

Anna Balashova, RBC: The Board of Directors was thinking of terminating the framework agreements between Tele2 – T2's holding and Rostelecom. Can you please explain what that topic was about?

Mikhail Oseevskiy, CEO: Well, in the creation of Tele2 in early 2014, there was an agreement signed on the integration of certain assets between Rostelecom, Tele2 Russia Holdings, that's a Dutch company and Tele2 Russia. And certain directives were issued by the government. To terminate that agreement, we need to obtain

reverse directives from the government because from a formal standpoint, this is not an item that requires a directive. We will send a request signed by the Chairperson of the Board of Directors. Well, that's a technical question that doesn't have much impact on the transaction.

Operator: Okay. Next question from Anastasia Skrinnikova of Vedomosti.

Anastasia Skrinnikova, Vedomosti: What would happen to Tele2's debt? Will it be bought out?

Mikhail Oseevskiy, CEO: Of course not. It will remain in the balance sheet of Tele2 and in accordance with the IFRS standards, we consolidated into Rostelecom's Group. In the future, we will naturally follow a single – a consistent policy to manage the debt to minimize the debt servicing costs and to build the appropriate duration structure.

Operator: Next question from Anna Ustinova, ComNews.

Anna Ustinova, ComNews: Given the consolidation of Tele2, do you plan to go into the regions where that mobile operator is not yet represented?

Mikhail Oseevskiy, CEO: Well, that's – it's a very technical question in terms of working in the mobile communications markets. Tele2 management team have their own vision that they will implement. I guess, they have such an objective on their table and it's a question of how they go about it. It is up to them.

Ekaterina Ustinova, IR: We have a question from Antonio de la Hoz. We don't know from which organization. And it will now be back translated into English.

Antonio de la Hoz: Tele2 will be managed as a standalone entity or will it be fully integrated into Rostelecom? And will the dividend policy of Rostelecom hold? Will it be preserved?

Mikhail Oseevskiy, CEO: As already explained, Tele2 will continue its operations as a standalone business.

Operator: And we'll now take, I guess, a final question from the Russian line. And that's Sergey Libin, Raiffeisen Bank. Please go ahead.

Sergey Libin, Raiffeisen Bank: Yes, good afternoon. Question, telecom investments, will it have any limitations in terms of sale of its stake?

Mikhail Oseevskiy, CEO: The answer is no. Thank you.

Operator: We have a follow-up from Igor Goncharov, Gazprombank. Please go ahead.

Igor Goncharov, Goncharov, Gazprombank: Yes, hi. Thank you. Thank you for taking another follow-up. So, what would happen to the Tele2 brands following the consolidation? Do you intend to maintain that brand or change it?

Mikhail Oseevskiy, CEO: Well, apparently Tele2 is a very strong brand today as already explained. The company has a very strong NPS, in fact the highest in their industry. So, we will certainly continue developing that brand and expanding the product range that we will be offering under the Tele2 brand. Thank you.

Operator: Thank you. We have no further questions.

Ekaterina Ustinova, IR: Okay, colleagues, thank you for participating in today's conference call. As ever, we are eager to receive your further questions. We hope we were able to answer all of the questions that you have. But if not, you can approach IR or PR and ask your questions and we will try to give you a prompt response. Thank you for your attention and wish you a good day.