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KPN.AS - Q2 2013 Koninklijke KPN NV Earnings Presentation

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PRESENTATION

Hans Sohngen *- KPN Koninklijke NV - Head of IR*

Good afternoon, everyone. Welcome here at Merrill Lynch in the King Edward Hall. We would like to welcome you to KPN's half-year results 2013.

Today, our CEO Eelco Blok; CFO, Eric Hageman; Managing Director of the Netherlands, Joost Farwerck; and CEO of Mobile International, Thorsten Dirks, will take you through our half-year results and address your questions during Q&A.

Let me briefly point out that the Safe Harbor Statement applies to this presentation and that any forward-looking statements made in this presentation do not differ from those already made in the press release published this morning.

I would now like to hand over to Eelco Blok, CEO of KPN.

Eelco Blok *- KPN Koninklijke NV - Chairman and CEO*

Thank you, Hans. Good afternoon, everyone. With me today, as Hans already told you, is Eric Hageman, our CFO; Thorsten Dirks, Head of Mobile International; and Joost Farwerck, Head of the Netherlands.

Let's start with the announcement earlier this morning regarding the sale of E-Plus to Telefonica Deutschland.

KPN has said constantly that we will sell any asset for the right price that realizes the value we see in that asset. And that's what we have announced today, a transaction that unlocks large mobile synergies and, therefore, significant value for KPN.

Everybody was talking already for years in a row to make this deal. Everybody believed in it and now today, we have announced a very good transaction, creating value for the KPN shareholders. We have agreed to sell E-Plus to Telefonica Deutschland for an implied valuation of EUR8.1 billion.

Eric will in his part of the presentation discuss some more details of the transaction later in this presentation.

As you all know, today is our Q2 results presentation, so let's now move to the results for the first half of the year.

The financial results for Q2 and the first half were in line with our expectations. Market conditions remained challenging, which put pressure on top line. Our EBITDA reflects higher commercial investments, mainly to support our next strategy phase in Germany.

The free cash flow shows the usual intra-year phasing pattern, which the large majority expected to come in the second half of the year. Our financial position was strengthened by our capital raise, which was completed in May. This provides a healthy platform to continue to execute our strategy, strengthen, simplify, grow. I'm pleased to report that the strategy is delivering improvements in our operational performance.

In Dutch Mobile, we already announced in June that we are accelerating the 4G mobile network rollout. We expect to reach nationwide coverage by the end of the first quarter next year. We are the first mover on 4G in the Netherlands and we provide the best experience for customers, who increasingly want to use data-heavy devices on the move.

Our Dutch fixed networks have seen multi-year investments to improve customer experience, be able to offer HD TV and cope with the strong growth in [OTP base] services. Compared with our European peers, we are leading the way with rolling out [overtalking]-to-the-home; and also in upgrading the copper network, for example, by using vectoring.

In Germany, our data network is now fully competitive after the investments we have made in recent years. And in Belgium, we now have a leading network position in terms of voice and data quality.

Our customer-centric propositions are increasingly yielding operational results, demonstrated by growing triple play in the Netherlands and strong postpaid net adds in data growth in Germany and Belgium.

Bundle propositions are critical to reduce churn and optimize customer lifetime value. And more and more of our customers are moving to bundles, driven by continued growth in IPTV and fiber-to-the-home activations. At the end of Q2, we had more than 1.1 million Dutch triple play customers, up from 750,000 last year.

KPN Compleet quad play has had excellent take up in the initial target customer group. Joost and his team are already scaling up and speeding up by extending KPN Compleet into more of our brands. In time, we will reach out to all KPN and non-KPN customers.

In Germany, as Thorsten explained in February, we are focused on monetizing our competitive data network. We are investing in marketing and distribution, and those customer-centric investments are delivering strong results.

The take-up rates in underpenetrated regions in Germany are very good. In total, we won nearly 0.5 million postpaid net adds in Germany in the first half of the year, and we have seen our data revenues grow by 60% year on year.

We're also getting very good early results in Belgium for our new postpaid propositions, with over 50,000 net adds in Q2, the highest number since 2005.

While we are pursuing our network and commercial investment programs, we are also driving ahead with our efficiency improvements. The major FTE reduction program we launched in 2011 is on track to hit the upper end of the range by the end of this year.

The program is being achieved on time and without compromising service quality. This is already resulting in a structural decline of personnel costs in the Netherlands of around 10%.

Simplification of products, client processes, network and IT, will be the main driver of further efficiencies in 2014 and onwards. All in all, we continue to witness good operational performance across the Group and remain on track to realize our outlook.

The outlook we gave in February remains unchanged. Please note, however, that this excludes the sale of E-Plus, which we announced this morning.

We firmly expect to stabilize performance in the Netherlands towards 2014, and we are on track to return to underlying service revenue growth in Germany in the second half of this year.

Now I would like to hand over to Eric for the financial review and some of the details of the transaction we announced this morning. Eric.

Eric Hageman - *Royal KPN NV - CFO*

Thank you, Eelco. Good afternoon, everyone.

Earlier today, we announced the sale of E-Plus and provided further details regarding the transaction in the analyst call at 10.00. Let me briefly on this page summarize the transaction structure of the sale of E-Plus to Telefonica Deutschland.

The transaction includes EUR5 billion to EUR5.5 billion for the NPV of the future synergies. The implied valuation of E-Plus is EUR8.1 billion, which is 9 times the current analyst consensus for the full-year EBITDA in 2013.

The implied valuation of EUR8.1 billion consists of EUR5 billion in cash and a 17.6% stake in the E-Plus and Telefonica Deutschland combination, which is valued at EUR3.1 billion. Completion of the transaction is subject to EGM approval and regulatory clearance.

Our present intention is that the majority of the cash proceeds will be used to further increase our financial flexibility, reflecting our new Group profile. Depending on the timing of the closing of the deal, we aim to recommend dividend payments for 2014, a year earlier than we had planned.

I will now move on to our Q2 results, starting with our current financial profile.

On May 17, we successfully concluded our EUR3 billion rights issue, thereby completing the total EUR4 billion equity equivalent capital raise which we announced in February.

In the second quarter, our gross debt remains stable Q on Q at EUR13.5 billion. The cash position, however, increased by EUR3 billion to EUR4 billion because of the rights issue proceeds. The net effect is a significant decrease of our net debt position to EUR9.5 billion at the end of Q2.

We often get asked about what we intend to do with this cash balance. Let me, therefore, point out that as you can see in the redemption profile on the bottom left of this page that we have EUR1.9 billion of bond redemption in the coming 12 months and EUR2.9 billion in the next 23 months.

Please note that the cash on our balance sheet is invested with a large number of counterparties and with high liquidity, meaning maturities shorter than three months.

As you know, in March, we issued three hybrid bonds, all in different currencies, which following completion of the rights issue, are recognized at 50% equity by the rating agencies. In our net debt definition, we also include 50% of the hybrid capital instruments as equity. Under IFRS, the euro tranche is accounted for as equity, and the sterling and the US dollar tranches as liabilities.

Let me point out that for further details on the treatments of hybrids, you can refer to the information pack attached to this presentation.

Let's now move on to the next slide.

Net debt over EBITDA at the end of the second quarter was 2.2 times. The decrease illustrates the positive contribution of the EUR3 billion rights issue to this credit metric, partly offset by [EUR115] million lower twelve-months rolling EBITDA.

Looking at our current financial profile, pro forma, the EUR5 billion cash receipts for the sale of E-Plus and the loss of EBITDA, our net debt over EBITDA would be below 1.5 times.

As previously announced, we continue to target a net debt to EBITDA ratio between 2 times and 2.5 times for the end of 2013.

Furthermore, there have been no changes to our credit ratings, nor to the outlook of the rating agencies in the second quarter. We are still rated Baa2 and BBB minus.

Let's now move to the Q2 Group results.

Total revenues for the second quarter were down EUR257 million, or 8.1% year on year, including a EUR61 million regulatory impact. The revenue decline was in almost equal parts attributable to our Consumer Mobile, NetCo business and Germany segments. This was partly offset by the continued positive revenue increase of EUR23 million in Q2 in our Consumer Residential business.

Operating expenses, excluding D&A, were down EUR124 million, or 6.1% in the second quarter, due to EUR51 million lower personnel costs in the Netherlands, lower costs of materials, the sale of Getronics International in May last year. And this was partly offset by higher commercial investment in Germany to support postpaid and our data growth.

Group EBITDA, excluding restructuring costs, decreased by EUR136 million, or 11%, although this included a net positive impact from incidentals of EUR52 million, or 4.7%.

Our EBITDA, or operating result, decreased by EUR365 million year on year, resulting from lower EBITDA, and EUR232 million higher depreciation and amortization. Higher D&A is a reflection of the significant investments that have been made across the Group in 2012 and 2013, and two one-offs this second quarter.

These are impairments included in depreciation of EUR75 million in Germany in the second quarter relating mainly to obsolete technology as a result of network upgrades. And a EUR44 million impairment included in amortization, also in Germany, related to mobile platform technology.

Excluding these two impairments, our EBIT would have increased by EUR246 million.

Finally, please note on this page that we have recorded a positive income tax of EUR30 million in the second quarter. This is because of a positive one-off impact of the innovation tax facilities of previous years, and in addition, a EUR22 million tax benefit for a future deductible liquidation loss of a specific subsidiary.

Let's now skip one slide and move to the Q2 Group cash flow.

Mainly because of the lower EBITDA and higher capital expenditures, we generated a free cash flow of EUR139 million in this second quarter. This compares positively to the EUR85 million we generated in the first quarter of this year.

Let's now look at the cash flow year to date.

In the first half of 2013, we generated EUR224 million in free cash flow, EUR347 million less than the same period last year. The delta can be explained as follows.

EUR270 million lower EBITDA; EUR160 million higher CapEx due to increased customer-driven and 4G mobile network investments in the Netherlands; EUR72 million higher cash related to change in provisions, mainly related to FTE reductions; and EUR45 million higher interest paid, as we had to pay coupons in the first quarter related to two bonds last year.

These negative effects are partly offset by EUR140 million (sic - see press release "149 million") positive change in working capital year on year.

As Eelco indicated in his opening statement, the year-to-date free cash flow reflects the usual intra-year phasing. Historically, most of the free cash flow is generated towards the back end of the year.

I would now like to move to the financial review of the segment, starting with the Netherlands.

In the second quarter, revenues and other income in our Dutch division were down 9% year on year compared to 11% decline in the first quarter. EBITDA, excluding restructuring costs, decreased by EUR56 million, or 6.8% year on year, as a result of lower revenues. This resulted in an EBITDA margin of 44% in the second quarter compared to 43% a year ago.

The increase is mainly driven by the positive impact of our FTE-related cost reduction program, lower hardware sales, and the handset lease model in Consumer Mobile. These positive effects on the margin were partly offset by higher commercial costs at Consumer Residential, and lower high-margin revenues at NetCo and Business.

Let's now look at the Dutch segments in more detail.

Revenues at Consumer Residential increased again by 5% year on year in the second quarter. The increase was mainly driven by a positive contribution related to the acquisition of the fiber ISP in the fourth quarter of 2012, but also by the continued growth in triple play, supported by IPTV and fiber-to-the-home activations. On the face of it, and compared to the first quarter, our solid Q2 revenues and EBITDA at Residential appear to be lower. However, please note that Q1 was supported by an incidental of EUR13 million.

EBITDA margin, excluding restructuring costs at Consumer Residential was 18.5% in the second quarter, again lower compared to last year, but on par with the last couple of quarters. The margin downturn versus last year is due to increased distribution and marketing costs, higher content cost related to the strong IPTV growth, and a continued decline in higher-margin traditional services.

Several projects have been initiated in both 2012 and 2013 to improve profitability at our Residential business. Amongst other things, we have increased prices by an average of 3% as of July 1. We have increased efficiency through FTE reductions and quality programs, and continue to reduce churn by bundling services and fiber-to-the-home uptake.

Revenues of Consumer Mobile were down by 12% year on year. Underlying service revenues were down 7.2%, driven by lower traffic. The difference is explained by lower handset sales and a 1.4% regulatory impact.

The EBITDA margin, excluding restructuring cost at Consumer Mobile, was 35.2% in the second quarter, again supported by the handset lease model, and phasing of marketing spend.

Please note that EBITDA margin for Consumer Mobile will be impacted by the introduction on July 1 of new mobile propositions for the KPN brand which do not include handset lease any more.

Revenues and other income in the second quarter at our Business segment were down EUR46 million, or 6.1% year on year, due to lower hardware sales, decline in traditional services, and continued price pressure. The Business segment also experienced a reduced order intake of corporate customer projects due to continued adverse macroeconomic conditions.

This was partly offset, however, by a EUR23 million booking related to the sale of Infrastructure Services & Projects, which was completed subsequent to the approval of the ACM in April this year.

EBITDA margin, excluding restructuring costs, was 27.5%. 25% is corrected for the EUR23 million book gain and, therefore, below the 26.9% EBITDA margin in the same quarter last year, as lower personnel costs due to the FTE reduction program were offset by pressure on high-margin revenues.

Revenues at NetCo were down by 7.6% year on year, mainly driven by lower wholesale traffic revenues related to FTA declines, lower volumes as well as pricing, and a 1% negative impact, again from incidentals.

EBITDA margin at NetCo was 55.7%, driven by continued decline of high-margin, traditional services and higher fiber-to-the-home access costs, which were only partly compensated for by lower personnel costs due to the FTE reduction program.

Let's skip one slide now and move to the financial review for Germany.

In the second quarter, revenues and other income in Germany decreased by EUR39 million, or 4.6%, compared to the same quarter last year, mainly due to a regulatory impact of almost the same amount, and supported by a EUR13 million positive impact from incidentals.

The difference between underlying revenues and underlying service revenues can be explained by higher hardware sales, which supports the take-up of postpaid and our data proposition.

Following eight quarters of a worsening trend driven by the competitive nature of the German mobile market and changed consumer behavior, less voice and SMS, the underlying service revenue growth in Germany is now stabilizing. The stabilization in underlying service revenues is mainly due to the strong postpaid performance, as prepaid continued to be impacted by lower SMS and voice usage.

In the bottom left-hand graph you can see the key individual elements that explain the EBITDA movement compared to the same quarter last year.

First of all, correcting for the EUR22 million of regulatory impact and a EUR16 million incidental, you can derive the comparable EBITDA for Q2, 2012, which is EUR297 million.

The revenue decline I already explained. The underlying EBITDA decline is then largely attributable to the EUR50 million higher investment in growth compared to the same quarter last year.

These investments, however, will support growth in postpaid and data, and are mainly related to customer acquisition costs, such as dealer commissions to expand our addressable market, and marketing costs to expand our presence in under-penetrated regions.

E-plus also saw somewhat higher network costs related to our now larger scale and a more advanced network. As you can see, reported EBITDA was supported by EUR66 million positive incidentals.

We remain confident that these investments will lead to underlying service revenue growth, albeit at a slightly lower margin. As a result, the underlying EBITDA margin was 27% in the second quarter in Germany. The EBITDA margin is expected to improve in the second half of the year, towards our medium-term margin range of 30% to 35%.

Lastly, Belgium. Revenues in the second quarter in Belgium declined by 12% year on year, as increased competition in the mobile market impacted our top line. Also, regulations had a significant impact in the second quarter of EUR13 million.

Underlying service revenues declined by 3.6% in the second quarter. Having said that, BASE still estimates that it has outperformed the market again in the second quarter. More on that from Thorsten later.

The EBITDA margin in Belgium was 26.8%, negatively impacted by regulation, lower revenues and commercial costs related to the introduction of new mobile and fixed propositions in the second quarter.

I would now like to hand over to Joost for the operating review of the Netherlands.

Joost Farwerck - *Royal KPN NV - Managing Director of the Netherlands*

Thank you, Eric. Good afternoon, everyone.

In the Netherlands, we are fully focused on providing customers the best services on the best networks. And that's how we reduce churn and how we optimize customer-lifetime value.

As Eelco already indicated, we are seeing good operational results from the investments in our network and in our customer services. We are the first mover of 4G, and we are continuously increasing the available bandwidth for our customers on our fixed networks; but more on that later.

In order to reduce churn, we introduced the next phase of bundled services in the first half of this year. KPN Compleet, our quad play product for consumers, is based on benefits, not on discounts. KPN EEN is available for all our business clients, providing one integrated solution for all their services.

We are fully focused on simplification as well, simplification of our products, client processes, our IT and our networks, and the organization. And this is an important driver and it will be an important driver to support profitability in the Netherlands going forward.

So let's now look at the operational progress we are making with our Dutch networks, and you're already looking at the slide with respect to mobile.

Since the commercial launch of 4G at the start of February, coverage has now already reached over 50% of the Dutch population. Our 4G strategy is based on leveraging our first mover advantage and leadership in quality. We will be the benchmark for coverage and performance in the Netherlands.

And hand in hand with that, our new KPN All-in-One propositions, launched this month on July 1 give customers different 4G tariffs according to data allowance and speed, with transparent pricing.

So far. we are getting good early take up. Voice and SMS is all-inclusive within the tariff, and this increases the committed ARPU. And we are already seeing a significant increase of data usage, and that's by our 4G customers compared to 3G users.

We also understand the relevance of Wi-Fi as additional service, and we have the largest network of nationwide hotspots in the Netherlands. Beginning of this year, we announced a strategic partnership with Fon, the world's largest Wi-Fi network, also offering coverage outside the Netherlands; and we scheduled the pilot in Amsterdam later this year.

Our fixed networks are well positioned, not only on a national level, but also when comparing on a European level. We are clearly ahead of the curve with the investment we have done in the last two years.

And this year, we are launching vectoring. This gives a doubling of speeds for both uploads to 40 megabits, and downloads to 100 megabits on a copper network.

Also, starting in 2014 and ramping up in 2015, we will roll out bonded vectoring, and this is a combination of vectoring with pair bonding that allows a further doubling of speeds to 200 megabits.

As well as our copper network, we also lead in Europe with fiber-to-the-home. Both our copper and our fiber-to-the-home networks are point-to-point infrastructure, and they are highly future proof and able to handle increasing data consumption by our customers. And this is relevant for all the [top base] services such as YouTube and Netflix coming to the Netherlands soon.

I will now summarize the operational highlights for the different segments, and starting with Consumer Residential.

We've seen a continuation of good operational trends and revenue growth in Consumer Residential. RGUs and ARPU increased, driven by IPTV growth, which has now reached 1.2 million customers.

Cost reduction and price increases at the start of this month will help margins in the second half of the year. We made a relatively large price increase at Digitenne this month, but it is still the cheapest TV product in the market.

And at the same time, our broadband customer base is continuing to grow after bottoming out last year, and it's driven by triple play uptake.

As I said, we're focused on reducing churn and on optimizing customer lifetime value, and bundled services are at the heart of our strategy as we integrated XProvider.

Once we convert a single-product customer onto triple play, on copper, or better on fiber-to-the-home, the combination of quality, customer service and price is highly effective in building that customer's loyalty to KPN. And now, we aim to translate this success into mobile by means of converts to bundles.

And KPN Compleet quad play focuses on value, not on discounts, like I already said. It's on track, with 55,000 activations at the end of the second quarter, only targeted at the limited group of KPN brand customers. The next steps are to scale up by extending KPN Compleet to all our customers across all brands and by targeting new customers.

We have a differentiated market approach in our Mobile business. Through our KPN and high brands, we focus on maintaining value, and we approached the value for money customers via our Telfort and Simyo brands.

Underlying service revenues at Consumer Mobile remained under pressure in the second quarter and went down 7.2%. We held market share and ARPU relatively stable in a highly competitive market. And we see an upward trend in committed ARPU as a percentage of the total, which is a result of the flat rate tariffs we introduced.

Now let's move to Business markets. The tough conditions in the Dutch corporate and business market didn't improve, and as a result of that, our top line performance remained under pressure, but our market positions remained stable.

Our strategy is moving towards a one-stop shop model, and thereby protecting the value we get from our Business customers.

Last month in June we launched KPN EEN, and that offers a full range of fixed, 4G mobile and ICT services, and that's all in one bundle for our Business customers.

We realized around 2,000 FTE reduction in the first half of this year, and that's to reach the total of 3,900 since the start of this program in 2011. We now expect the total to reach the upper end of the 4,000 to 5,000 target by the end of 2013. The underlying structural decline in staff costs is now around 10% year on year, which we expect to continue in the second half of the year.

We've made significant steps by simplifying, and that's simplifying our propositions and by further simplifying products, processes, networks and IT, and this will drive efficiencies in 2014 and onwards.

So to conclude for the Netherlands, we continue to strengthen our fixed and mobile networks. Our commercial investments are increasingly delivering better operational performance, and simplification will support the next phase of improvements to our underlying cost structure.

Now I would like to hand over to Thorsten for a talk about Mobile International.

Thorsten Dirks - *Royal KPN NV - CEO Mobile International*

Thank you, Joost; and good afternoon, everyone. Like Joost, I will concentrate on the progress we have made at the first half of 2013 implementing our strategies in Belgium and in Germany.

For both countries, we have three overarching strategic priorities. First, is to strengthen our data networks, which are the essential foundation of everything we do. Then we have commercial strategies to monetize those networks. That means a clear focus on postpaid customers and on data-led propositions, as Eric and Eelco already pointed out.

It also means expansion into cities and regions where we are below our average market share -- we called it the under-penetrated region -- by expanding our distribution channel and targeted marketing. This all is based on our regionalization strategy I explained to you already in February.

Now let's look in Germany starting with the KPIs for the first two quarters.

The market environment stayed tough in Q2. There is pressure on prices. Customers continue to optimize their bundles. This is having the biggest impact in prepaid in terms of lower SMS and voice usage. This is what every operator is experiencing now.

E-Plus traditionally has a high relative proportion of prepaid customers. However, we are increasingly mitigating this was a very strong performance in postpaid, and this is why we have changed our strategy as of beginning of this year.

We added close to 0.5 million new postpaid customers in the last two quarters. In terms of market share, we expect to have stabilized at around 15% for Q2. And on service revenue, we see Q2 stabilizing on Q1 level at minus 2.4%.

Now you can see the changes in the components of Mobile service revenues in Germany comparing Q1 with Q1 a year ago. The total data revenue growth in Germany in Q1 was around 20%, and slowing down for all the other operators. Our data-led Challenger strategy is generating data growth 3 times faster than the market, and that underpins our belief that we will return to underlying service revenue growth in Germany towards the end of this year.

The strong postpaid performance supports a stabilizing underlying service revenue growth in Q2 already.

How have we managed to outgrow the market in data? As I said, the network is the foundation for everything, and we have made further improvement in coverage, capacity and in quality in the first half of this year.

We now have 3G HSPA+ coverage of nearly 90% of the German population. The dual carrier rollout and connecting a lot of sites to our IP backhaul has helped drive faster average throughput by the factor of 3 since a year ago, and we have expected -- and we are -- and we expect a further increase to 6 megabytes per second until Q4 this year. So we are really increasing the quality and the speed in our mobile broadband network.

So we are now the number three in the ranking of German networks by data speed and we are challenging the number two.

Last but not least, we also started our LTE deployment at 1,800 megahertz.

We added close to 0.5 million postpaid net adds in the first half. This is more than double our overall market share and over one-third of total post paid net adds in Germany looking at Q1 data.

This growth was driven by targeted investment in marketing and distribution. We were particularly successful in new regions where we had previously been under-represented. And again, this was part of and is part of our regionalization strategy.

We are pleased by the inflow ARPU for new [growth sets], and this justifies our strategic emphasis on winning new postpaid customers using our new innovative proposition.

So growing postpaid is one of the -- one part of the equation. The other is slowing down the decline on prepaid revenues. The main driver for that will be the competitive new tariff schemes we introduced this year, for example the new packages we just launched with Aldi, which already show a positive impact.

To give you some additional insights into prepaid, our average number of SMS per customer is falling in line with the market. Our average voice minutes per customer are stabilizing, but our average data revenue with our SMS customers are rising. So overall, we believe that our prepaid revenues are on path towards stabilizing.

Now let's have a look at Belgium. Here, the overall market service revenues are under heavy pressure from the increased competition facilitated by the telecom law that makes it easier for customers to optimize tariffs.

We are very pleased to have continued our market outperformance and that we increased our market share of service revenues despite these challenges.

In Belgium, we are already a leader in network quality. Now we are deploying dual carrier to help improve data speed up to 42 megabytes per second. Dual carrier coverage will reach 80% of [3G outdoor] population in Q3 already, and we have an ambition in Belgium to cover the majority of the country and the population with LTE by the end of next year.

Our commercial strategy is centered on new propositions aimed at postpaid in the same way we have done it in Germany; plus we are expanding into the south of the country, also based on our regionalization strategy, and this also we copied from Germany.

We launched new flat fee data-led propositions for the BASE brand in April. This has had very good early success, with 53,000 net adds compared to minus 8,000 the quarter before. And this compares also to negative postpaid net adds that we have seen with our competition, which is the best performance since 2005. We expect this positive momentum with the new proposition to continue in the coming quarters.

Thank you very much, and now back to Eelco.

Eelco Blok - *KPN Koninklijke NV - Chairman and CEO*

Thank you, Thorsten.

To conclude, we are strengthening our fixed and mobile networks, such as the accelerated 4G rollout and continued upgrade of our fixed network in the Netherlands.

Our customer-centric propositions are increasingly yielding results, demonstrated by growing triple play in the Netherlands, and strong postpaid net adds and data growth in Germany and Belgium. And we are driving ahead with simplifying our products, client processes, network and IT.

While we still have a lot of work to do, we are well on track with the execution of our strategy to strengthen, simplify and grow.

To finalize, as we have highlighted earlier this morning and in this presentation, we are unlocking significant German mobile synergies through the sale of E-Plus.

Thank you. And now we will take your questions.

QUESTIONS AND ANSWERS

Hans Sohngen - *KPN Koninklijke NV - Head of IR*

I would like to open the floor for Q&A. We've got two microphones. Please raise your hand if you have a question. A microphone will be brought to you.

Sam Morton - *Mizuho International Plc - Analyst*

Sam Morton, Mizuho. Just two questions on the balance sheet, please. So you talked about the liquidity position, the EUR4 billion and the EUR2.9 billion bonds coming due over the next 2.5 years. I just wondered whether you thought it made sense to pay those bonds as it comes due; or bearing in mind the windfall you're expecting from the E-Plus disposal, whether we should be expecting any bond tender exercises.

And secondly, so obviously on the E-Plus disposal, I just wondered if you could give us the breakdown of operating leases that existed within E-Plus. I think Moody's has you down as having EUR2.4 billion of operating leases in the adjustments. I just wondered what portion of that would sit at E-Plus rather than KPN in the Netherlands.

Thanks.

Eric Hageman - *Royal KPN NV - CFO*

Eric Hageman^ The operating leases are limited in Germany. I will make sure that you get the exact details via the colleagues of IR.

With regards to the bonds, I think we did an exercise with issuing the hybrids, and then subsequently the rights issue, which gave us EUR5 million of cash. I think this is why today we can show a very healthy 2.2 times net debt to EBITDA.

I think today we have also indicated that by year end, we expect to be comfortably within that range; and also that if you would look pro forma of the impact of this transaction, that we would be well below 1.5 times.

But we've also been in a very different period, and that is not that long ago. So what you should expect this team to do is to be very prudent with our cash, the cash that we've worked very hard for to get. But certainly what we're not going to do is already spend the cash that we haven't even received because we have yet to complete this transaction.

What we have said though today is that a portion of that cash of this transaction will be used to add to our balance sheet; that's one. Secondly, that we're also clearly communicating a use for that vis-a-vis our shareholders which would allow us to initiate a dividend again.

With regards to the current state, I think you should expect us to still come to the market to look at refinancing the bonds that we have outstanding. And I think if you look at the next 23 months, where indeed you have almost EUR3 billion of redemptions upcoming, that's the reason why we feel very comfortable with the current cash position that we have.

Dimitri Kallianiotis - *Citi - Analyst*

Dimitri Kallianiotis, Citi. Three questions, please. The first one is regarding Germany. In particular, at the beginning of the year, you commented that we should expect some improvement in margins in second half. Obviously, things are changing; you -- with [over that on] buying KDG, becoming more aggressive as well in the market. The same for Deutsche Telekom. You are now in the process of merging with Telefonica Deutschland.

I wanted to ask if that will change a bit the way you plan to run the business, because your competitors are likely to be more aggressive to try and take advantage of the transition period.

My second question is regarding Belgium which, as you said, you're performing better than the market, but the market is very, very tough, as we saw with Mobistar earlier this week. I wanted to ask you what -- if you intend to do any sort of M&A or anything like that to try to improve the situation, because you've launched that fixed offer. But we haven't heard much about it, so I was just wondering if that's performing in line with your expectations and if you can give us a little bit more color.

And my last question is regarding Dutch Mobile. [Vigor] seems to be planning on launching a bit earlier than expected, maybe end of Q3. I wanted to ask if that's changing a bit your view on quad play, in particular if you intend on accelerating the push towards quad play because the numbers are still relatively low in the grand scheme of things.

Thank you.

Eelco Blok - *KPN Koninklijke NV - Chairman and CEO*

Okay. Thorsten will take the first question. I will take the M&A question on Belgium. And Joost, of course, will take the Dutch Mobile question. Thorsten, perfect split?

Thorsten Dirks - *Royal KPN NV - CEO Mobile International*

Yes. The first question; as we have promised to you, we said we will see a real decrease in the EBITDA margin first quarter. You've seen it, 25%. Slight improvement the second quarter, 25% to 27%, you have seen it. And then you will see an improvement of the margin towards the midterm outlook, so to 30% to 35%; not saying that we will reach 30%, but that was what we said beginning of the year.

I don't see -- to be honest, looking at what happened, I don't see any reason to change our strategy, and this is exactly what we are doing. We have a clear strategy focused on postpaid, clear strategy focused on data, clear strategy to further roll out our networks. This is what we have done and this is -- by the way, so far we have done very successfully.

If you look at the numbers, I've just seen the Telefonica numbers, plus 60,000 I think postpaid net adds. It's the worst number I ever could think of in the last, I don't know, many years.

We are now at 210,000, and Vodafone, if I remember right, last Friday minus [14,000]. So we promised to you that we will outperform the market in postpaid net adds. We are doing.

Look at our data growth, plus 60%. Vodafone on Friday 6%; 6.8% to be very precise with you.

So, no, I don't see any reason to change our strategy.

Eelco Blok - *KPN Koninklijke NV - Chairman and CEO*

And maybe to add to this, to another part of your question related to Germany, Thorsten will continue to focus on executing the current plan, and given the performance Thorsten has shown to us and also the outside world, I'm really confident that he will not be distracted by the process that he [will] in. And, of course, Eric and I will support Thorsten in managing the Company as he has done before.

So we are really confident that what Thorsten has been saying about the performance of E-Plus, that he will deliver those results.

And on M&A in Belgium, as Thorsten has explained to you, we are doing really well in Belgium, outperforming the market, and we have no plans whatsoever to buy or sell activities in Belgium. We're really happy with the performance and we will continue to invest to be able to continue the current growth we are realizing in Belgium.

Joost Farwerck - *Royal KPN NV - Managing Director of the Netherlands*

And coming back to your question on Dutch Mobile, there's no change in our strategy. However, we accelerate it. At the beginning of this year, immediately after the auction of the frequencies, we executed the rollout of 4G, since this was already in preparation for a long time, and we accelerate the rollout of that. That's why we come to an 80% coverage of the Dutch population end of this year.

And on the other hand, we introduced quad play services. That's just launched the first of -- well, a month ago, only on a very limited target group, and now we open up for all KPN customers.

So we truly believe in the power of our 4G rollout and 4G services we're introducing. We also really believe in the power of quad play since we are the only Company in the Netherlands with both fixed and mobile assets, and the largest Wi-Fi hotspot network in between.

So you referred to an announcement of [Zero] on mobile, if I'm not mistaken. That's an MVNO they're going to do. To be quite honest, that's not unique in the market. I even think they already did it before.

So we know the MVNO model and I actually believe in our own strategy, our own 4G rollout and the propositions we put in the market, and the success of that.

Tim Boddy - *Goldman Sachs & Co. - Analyst*

Tim Boddy, Goldman. I just had a couple of questions about your strategy in fixed in the Netherlands. I guess it comes back to how you really understand your long-term ambition. You said you want at least 40% broadband share with a target of 45%. Obviously, you continue to press aggressively, particularly with the Telfort brand. And we've seen your cable competitors hurt by that and then reacting with more investment.

How does the market get out of this cycle which at the end of the day helps neither of the two infrastructure owners? And what are your real long-term ambitions for that?

Eric Hageman - *Royal KPN NV - CFO*

Yes. Well, to be quite honest, we think it's very important to maximize value on what you do and not see market share as an absolute holy target. That's why we are already for a couple of quarters stabilizing around 41% in the broadband market.

And we're not that aggressive currently, since we also introduced at the beginning of this month price increases on everything we do on fixed. TV, broadband, voice, everything has increased. And that we also believe that we really are responsible for making a good return on all the investments we do. So it's area to area a delicate approach, and that's where we are.

So we make good progress on fiber-to-the-home, but also there every year we decide on how far we roll out, what we invest. And it's all about return and the penetration we gain there. We invest in copper as well. We're very proud of our TV products. We especially grow strongly in TV, but we're not -- we do not have a strategy to push our market share to the limit.

Tim Boddy - *Goldman Sachs & Co. - Analyst*

And I guess related to that, if I could follow, you just say now you're six months further along the path. Could you just say a bit more about what's stabilizing EBITDA towards 2014 in the Netherlands? What does that really mean in terms of --? Is it a bottoming out in the second half? Is it stable in '14? How should we think about that?

Thank you.

Eelco Blok - *KPN Koninklijke NV - Chairman and CEO*

At this moment, we just keep it with the stabilizing towards 2014, that meaning bottoming out towards 2014. And, well, that's it, and we will share with your some more details beginning of next year.

Guy Peddy - *Macquarie Research - Analyst*

Guy Peddy, Macquarie. Just leading back on to Tim's question there quite nicely, what do you actually have to do in the second half of this year domestically and operationally to put you on track to stabilize in 2014? Because you're minus [9%], minus [6%] currently, so you've got a long way to travel. So what are you doing?

Eelco Blok - *KPN Koninklijke NV - Chairman and CEO*

Continue the operational performance improvements we have seen over the last couple of quarters; and next to that, continue the cost reduction programs, finalize the FTE reduction program. Joost is working on [next] program, mainly driven by simplification, and that are the main drivers behind the outlook that we have given for the Netherlands.

Polo Tang - *UBS - Analyst*

Polo Tang, UBS. I just have a couple of different questions. Could you maybe just expand in terms of where the opportunities are for cost savings, further cost savings in terms of such business? You briefly touched on it in terms of simplification, but I think previously, a couple of months ago, you talked about shop rationalization, etc. So could you maybe just talk about cost savings in a bit more detail?

Second point is could you clarify in terms of the E-Plus disposal are there any capital gains tax implications?

And the third question is really just in terms of German mobile. So you [showed] the charge in terms of the declines, in terms of prepaid service revenues. So the declines seem to be accelerating. So when can we see the inflection point there? Is it maybe in Q3 onwards as you start to lap the impact of competition in the FX segment? Can you maybe just talk about that?

Thanks.

Eelco Blok - *KPN Koninklijke NV - Chairman and CEO*

Eric, maybe you can start with the E-Plus capital gains tax.

Eric Hageman - *Royal KPN NV - CFO*

Unlike my usual self, I can be quite sure there are none.

Eelco Blok - *KPN Koninklijke NV - Chairman and CEO*

And, Joost, on the --

Joost Farwerck - *Royal KPN NV - Managing Director of the Netherlands*

There are (laughter). Yes. Now a very important part of my job is the simplification of the operating model in the Netherlands, as I call this. And you start with simplifying your portfolio, so what do you put in the market. That's what we're doing right now. And then you have to clean up everything that's out there in the market. So that's simplifying one.

Secondly, customer processes; we are migrating all these services in the volume market, the consumer market and in the value market, the business market who want IT environment, which will really clean up a lot of legacy.

Third, our distribution model. The shops you mentioned is -- we are optimizing that one. And then related to that we can also optimize the whole IT environment and the network environment.

And sounds complex. but the whole thing is connected to each other and that's what we're doing right now. And that's -- more incumbents do this, and that's really interesting from a simplification point of view and that will really gain reduction.

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Polo Tang - *UBS - Analyst*

Can you give us just an idea in terms of quantum? Is this going to be as big as the current program that you have which is going to yield EUR200 million in terms of synergies? Give us an idea of maybe scale.

Eric Hageman - *Royal KPN NV - CFO*

Yes, this is not only about FTE reduction, this is really about everything you do on spend.

Eelco Blok - *KPN Koninklijke NV - Chairman and CEO*

And to give you some more color, yes, we will also based on this program reduce the FTEs again, but it will not be the amount we announced in 2011 because continue to reduce 4,000 to 5,000 FTEs, then at the end you will end up with nobody and it will not be possible for Joost to design an operating model with no FTEs.

So percentage-wise, it will be an interesting amount, but in absolute numbers, it will be less than the program we announced in 2011. And we will give you some more information when we present the Q3 results.

Thorsten?

Thorsten Dirks - *Royal KPN NV - CEO Mobile International*

Yes. Last but not least on prepaid and bottoming out. That was your question. If you look at the prepaid business, if you look at the revenue drivers, it's active users. And on the volume side, on the usage side, it's voice, SMS and data.

Data is going up fast. Active users in some segments are increasing again; not in all. Voice is stabilizing; SMS is going down.

So to answer your question, we will see it most probably not already in Q2, but in Q4 ongoing.

The big question mark we have at the moment is SMS, because this is -- the big question I think all the operators at the moment have on SMS is how far will it go down.

I give you a number on Germany. The number of active [what's app] user, and active is what app user who at least wants [one] app per day, increased from October last year around 8 million to 9 million to 15 million/16 million now. And with this community increasing, people are sending less and less SMS, and this sum up to billions of SMS.

And especially in prepaid, these are pay-as-you-go SMS, so it immediately hits your top line. So and the big question for the overall market, we have seen SMS revenue go down for all the operators in average 14% in Q1. We will see the number in Q2 expected on the same level. How far it will go down, and this is then also -- this will also determine when we will see the bottoming out in prepaid.

Stuart Gordon - *Berenberg - Analyst*

Stuart Gordon, Berenberg; a couple of questions. First one is on the Netherlands. Obviously, you're doing a good job with the employee benefits, but it seems to be pretty much offset by increases in work contracted out from higher TV content and fiber-to-the-home access costs. I wonder if you could split out how that's working, because obviously, if you consolidate Reggefiber, a portion of that will, I assume, come back to you.

Secondly in Germany, I'm just struggling to get a grip of -- you're saying you're strongly outperforming when your share of service revenue isn't actually improving as part of the market. So I'd just be interested in some thoughts there.

And also in E-Plus, the EUR50 million of higher costs in the first half, could we get an idea for what was marketing and what was SAC and SRC within that split?

Thank you.

Eric Hageman - *Royal KPN NV - CFO*

Yes, so you're right. [We work this out] partly is the content we pay for customer on TV. That's a couple of euros. But we also pay Reggefiber for access to the fiber network. And indeed, after consolidation, we do not have to pay that any more to Reggefiber. It's consolidated in the Company.

So per connection to fiber, we have to pay an amount to Reggefiber. That's right.

Yes, so it's -- there it's now in the market of around EUR15/EUR16 per connection.

Thorsten Dirks - *Royal KPN NV - CEO Mobile International*

On Germany, you had two questions. One was on when we said we are performing well, looking at the trends. As I said before, also two of our competitors have reported the numbers so far. We see that they lose momentum on growth. One of them went down from minus 0.5% to minus 2.3%, so 1.8% absolute down. The same too for O2 from plus 0.5% to minus 1.3% down. So we are stabilizing.

So while we have lost market share in Q1, or service revenue market share-wise, because we were heavier impacted by MTRs. So the delta between reported and underlying, well, that is much heavier than or bigger than with our competitors, especially Deutsche Telekom and Vodafone. And that is something to do with the net balance of our terminations.

So we said that we will see a positive underlying service revenue growth towards the end of the year, and we are on our way. So this is why we believe that we are performing well according to the plan that we explained to you six months ago.

Second, you asked about the cost. Q2 this year, year over year compared with Q2 last year, as Eric explained, and his charts you've seen, the underlying EBITDA last year without regulation impact compared with this year, we were EUR88 million down. EUR22 million were driven by less revenue, so because (inaudible); and the rest was driven by -- EUR66 million was driven by additional costs.

EUR50 million out of them we call costs in growth, and this is SAC/SRCs, so subscriber acquisitions, subscriber retentions, and also marketing costs; so ATL, above-the-line spending. And [EUR16 million], an increased network cost around EUR5 million a month for our expanded network, broadband network.

Stuart Gordon - *Berenberg - Analyst*

(Inaudible - microphone inaccessible).

Thorsten Dirks - *Royal KPN NV - CEO Mobile International*

I could.

Stuart Gordon - *Berenberg - Analyst*

And will you?

Thorsten Dirks - *Royal KPN NV - CEO Mobile International*

No, sorry. No, I do not want to give our competition too many hints. That's the reason why we are not disclosing these numbers.

Eelco Blok - *KPN Koninklijke NV - Chairman and CEO*

With that, I officially conclude the Q&A session. I think there's still some room for a short chat. Thank you all for coming out.
