Turk Telecom

Moderator: Gozde Cullas
25 October 2017
2:00 p.m. GMT

Operator: This is Conference # 963042.

Operator: Good afternoon ladies and gentleman and thank you for standing by. Welcome to the Turk Telecom 2017 Q3 conference call. I must advise you that this conference is being recorded today, Wednesday the 25th of October 2017. I would now like to turn the conference over to your speaker today, Gozde Cullas. Thank you. Please go ahead.

Gozde Cullas: Welcome to 2017 Third Quarter Results Conference Call. Today's speakers are our CEO, Paul Doany; and our CFO, Kaan Aktan. Before we start, I would again remind you kindly to review our notice of our presentation. I will now hand over the call to Paul Doany.

Boulos H. B. Doany: Thank you. Good afternoon, everybody. I am delighted to discuss our third quarter results. We have strong financial performance and real operating momentum across each and every one of our main business segments. During the quarter, we remained focused on executing our strategic, operational and financial plans and there are several areas I would like to highlight.

First of all, we're progressing with our mobile active network sharing, which is strategic to us. We're starting a pilot project in the first city where all items of this agreement are now in place. And we will be updating you further as we progress along the slide. We believe that mobile network sharing opportunities will pave the way for more efficient deployment of our LTE network CapEx and OpEx going forward as well as future 5G deployments on the same principle.

Secondly, we signed a Memorandum of Understanding with GE Digital to provide industrial companies in Turkey, especially the top 500 with digital transformation consulting services. And these will be followed by a digital transformation execution projects. This is a good example of our new win-win collaborations with world-class companies, in this regard targeting the top industrial companies. And for the execution stage, we will be participating through the Türk Telekom corporate offerings as well as GE digital industrial solutions unit.

Additionally, we also for midsize corporate customers., we have signed an agreement with SAP. This is targeting and pre-accountancy and ERP applications customized for SMEs through our subsidiary Innova and will be presented to SMEs through cloud technology. Our subsidiaries, especially Innova, are very well positioned to grow through such initiatives. We will be again updating you on how this is going in the next quarter.

The third quarter was an important quarter for us in the sector. A revision proposal for taxation of telecom services to equalize special communication tax at 7.5 percent for major telco services, both fixed and mobile, was submitted to parliament. We welcome this proposal because it provides clarity, transparency for all stakeholders under a unified tax rate without the uncertainty of what is voice and what is data. And this will reduce future dispute risks that we have seen earlier, such as treasury share issues, which again I'm sure we will update you on the course of Q&A.

Now turning to Slide 3 on financial performance among. During the third quarter, consolidated revenues increased 10 percent year-on-year to TRY 4.5 billion. EBITDA grew 16 percent, TRY 1.7 billion. EBITDA margin 37 percent versus 35 percent in the third quarter last year. Capital expenditure TRY 554 million in the quarter. These results reflect our ongoing focus on profitable growth as well as improved OpEx control and disciplined cost management.

As planned, commercial expense growth accelerated 21 percent year-on-year this quarter based on strong net add performance as well as diminishing base impact of last year's first half LTE launch and brand unification related marketing expenses. We added almost 2 million net subscribers over the last 12 months out of which 930,000 this third quarter.

At the same time, we continue to extract efficiencies from our operations through streamlined organization structure, which has been visible through our personnel expense trajectory.

During the quarter, we generated a net income of TRY 293 million, a strong increase compared to last year, primarily as a result of stronger operational results. Year-to-date net income at TRY 1.25 billion, 88 percent up on the same period last year.

I would like to stress that the total number of telecom subscribers now exceeds 40 million at 40.5 million. We posted better performance across every one of our main products, including fixed voice driven by accelerated commercial activities and successful execution.

Now I turn to Slide 4 on fixed broadband. Broadband business posted strong subscriber growth with customer base reaching 9.4 million at the end of third quarter. Quarterly net adds reached 289,000, 2.5x higher than the third quarter last year. Broadband subscriber base expanded by 952,000 in the last 12 months.

We had a strong back-school offering starting September. And also, we had a good push with our Internet Bizden, which is the penetration focus entry-level 20 Giga Internet with impressive results, making around a quarter of our net adds in this quarter.

We're confident that there is plenty of room for growth in the broadband segment and we're looking ahead. We see a real opportunity to target new customers in this area, the entry-level packages as well as upgrading existing customers with further packages as well as obviously cross-selling TV, mobile and other value-added services.

We have achieved progress with our target to expand our sales channels with electricity distribution companies and we will be announcing this very soon. These discussions are progressing very well. Similarly, we delivered good results in fiber. We reached total fiber base of 2.5 million, adding 182,000 subscribers, during this last quarter, up 72 percent on last year's performance. At the same time, broadband ARPU is at a healthy level of TRY 44.1 reflecting continued upsells and price adjustments.

Turning to Slide 5. I would like to highlight some of the dynamics in the fixed broadband. As shown in these charts, we continue to see more customers taking up our highest speed and higher capacity packages. At the end of the third quarter, 27 percent of our broadband customers took 75 Gigabyte or above packages, which was 13 percent a year ago.

Meanwhile, percentage of our customers in the high-speed fiber/hipernet packages is now 31 percent, up from 26 percent last year.

This increasing demand obviously requires a strong network. The fixed network offers the most efficient technology to deliver this high capacity. Our superior fiber network now is 4.3 million FTTH /FTTB - fiber-to-the-home or building. And 11.1 million FTTC homes passed, which gives us plenty of room for further growth in the sector.

Turning to Slide 6. On mobile, we've added 414,000 subscribers in the third quarter, our best quarterly performance yet this year. And as we had initial planned, we accelerated our mobile marketing activity and communications in this quarter compared to the midyear and refocused these plans for further -- with further successful tariffs aiming for further market share growth.

The increase in mobile subscriber base was driven by postpaid segment, which expanded by 237,000, which is 57 percent of the mobile net adds in this quarter, plus the prepaid segment which increased by 176,000. Regarding ARPU, mobile business delivered an impressive third quarter ARPU of TRY 28.8, increasing 11 percent compared to the same period of last year driven by healthy mix in our customer base as well as growing data consumption, further explained in the next slide.

Monetizing data, Slide 7. Mobile data revenues continued to enjoy strong momentum with 80 percent year-on-year growth, accounting for 54 percent of mobile service revenue in the third quarter.

Increase in mobile data usage, LTE adoption, smartphone penetration and postpaid conversion were the key elements of data revenue growth. Tariff change and data pack upsells continued at full force in this third quarter.

Our postpaid ratio increased 54 percent, 9 percent year-on-year growth in postpaid subscribers. Base smartphone penetration is up 5 percentage points, 78 percent. And parallel average monthly use of smartphone users in our base reached 3.9 Gigabyte, up from 2.7 Gigabyte a year ago. Additionally, LTE-compatible devices among the smartphone users continue to make progress, reaching a penetration of 64 percent from 48 percent a year ago, demonstrating increasing demand for LTE.

Average monthly data of LTE users was 4.7 Gigabyte, up from 3.5 last year. And share of LTE registered customers with compatible devices and SIMs increased from 18 percent last year to around the third in this quarter. Therefore, there is still a substantial upside ahead of us to convert more customers to LTE.

Now the next slide on TV performance on Slide 8. In this quarter, TV business gains momentum in line with our new strategy of focusing in this area, posting the highest net adds yet. The number of TV subscribers exceeded 2.5 million with more than 200,000 net adds in the quarter.

In particular, Home TV continued gathering momentum exceeding 1 million subscribers. Quarterly net adds in Home TV reached 135,000, 3x higher year-on-year.

We're now positioning TV as an affordable service with the target of reaching as many homes as possible. So, this is a penetration gain. The current level of Pay TV penetration is low in Turkey, with more than 15 million underpenetrated homes.

These are the homes that receive now free-to-air through obviously DTH satellite TV. This provides also future opportunity for Türk Telekom in these specific homes that we can build for potential up-sells into home wireless broadband projects.

So, these we call them Wireless Homes. Initially they will get entertainment by satellite-TV and then we will upgrade them into a home broadband unit. But also serve those using mobile network because that would be sufficient for the needs of this particular homes we believe. And we can do much more cost-effective that way in terms of price.

So that's a very important part of our strategy in order to drive mobile data service growth. This will be there WiFi hotspots, but driven from our mobile network in the home.

In Pay TV, we're the only player with content delivery platforms that position ourselves across all these platforms and this puts us in a unique position, not only to serve the tail, but also to serve from the top end.

Now in relation to content. Now clearly when the company decided to boost its Tivibu offering to the market, the company acquired some premium sports content, which is the Champions League and through the UEFA. Now this, of course, the strategy going forward is more around sharing of premium content. There is no point in this company investing or overpaying for exclusive content.

So the strategy that worked 3 years ago, going forward we need to be more focused on having lower costs and therefore more open to sharing, but rather to go for penetration. And that's why we need to go for the lowest possible price to grow the base as much as we can. So, we added 738,000 Home TV subscribers since second quarter. And this is expanded now 3.5x and this has served its purpose.

So, therefore, we're no longer, if you like, attached to any specific exclusive content. And we're -- we have been discussion even in sharing content that we already have with other operators. And we will see how the next round goes in relation to UEFA tender in addition. Because there we are also engaged on a sharing approach. And as you may remember, we also offered to be a form of a channel of sharing for the Football League. And that's how the strategy would going forward.

Slide 9 on fixed voice performance. In fixed voice, we experienced a clear turnaround with positive net adds in the traditional fixed voice services for the first time since the IPO. We added 24,000 net fixed lines in this quarter, a significant improvement from the net loss of 170,000 in the same period last year. Fixed voice and NDSL combined number of total fixed lines increased now to 13.4 million with 186,000 net additions, the highest net adds in fixed line since the IPO.

So we achieved this result as a consequence of increased variety of synergy campaigns within the offerings of the company. As an example now, the Internet Bizden – this 20 Giga entry package. We're focused on penetration and obviously this can be supported by fixed voice and vice versa. People who have fixed voice can now have it at a very low incremental cost to them, and we can also reactivate previously canceled lines for future upsell.

This can complement the earlier wireless homes that I described. So, wireless homes are homes we enter first for entertainment and then we upgrade to our wireless data offerings over our mobile network. And these are fixed homes that are connected by a fixed since there already connected. We're trying to extract value from what is already there.

Remember that these are very heavily priced in favor of any wholesale retail basement. And that's why these are not only for TTNET but also will be going to market through other operators. And this is the reason why we're also investing in the electricity sector. Because Turkcell, Vodafone and other players in the market are not really that strong into entering that segment for the growth part.

So while the pace of that subscriber losses in fixed voice segment has slowed, ARPU continue to remain healthy at TRY 23. And all-in-all, the annual decline in fixed voice revenue decelerated.

So the last point I would like to say on this slide is that the new reduced tax of 7.5 percent on fixed voice, which we expect to be in place as of next year, as I indicated earlier, this is the new offering 7.5 percent flat across the segment, we believe will be a very helpful for growing the Internet penetration by TTNET or any other operators that would like to focus on this segment.

To the extent other current players are not doing it, we're going to open an alternative to the electricity companies in order to make sure that this is shared with the sector and not taken up by TTNET entirely.

On digital transformation, I don't want to say too much on this slide other than to highlight - this is Slide 10, other than to highlight that the strategy of the company when we refer to anything called Digital Services must mean something more than services we are giving to our own customers. It must mean more than that for it to have a value for the company.

Now that focus is on technology, on marketing, on branding and communications and also sales and customer care aspects of digital strategy. Because that impacts everything. The first item I had mentioned here is that building on Argela's R&D efforts in both SDN, software defined networks, and also virtualization - NFV, network function virtualization. They have worked for 5 years on a very intensive R&D program. And now this is paying dividends. What this has allowed us to do is for Türk Telekom now to have joined the Open Network Forum, the U.S.-based open platform. And, as you know, this includes important members as AT&T, one of the leading operators who are moving in this direction; Deutsche Telekom; and also Verizon.

This puts us in that setting where we're benefiting from what other operators have done. But also we have been pleasantly surprised that Argela USA and their operating name there Netsia is actually standing up to what other operators are doing and this is putting us and Argela in a very interesting position in relation to the network of the future to be part of what the future will be like.

Because the future will not be as we're now relying totally on vendors without the ability of differentiating what the customer wants over a mobile network. This allows people to price quality on mobile business which now we can do on fixed, but is very hard to do on mobile. So that's a very important thing for the sector all-in-all.

In addition, on business service product, we're building now Argela up not only for R&D, but also to be commercial entity. So we're putting our consumer digital service offerings under Argela. The first of these is Tambu, which is our keyboard platform, which is now -- which obviously is fully owned by the company. And this -- the call is being put under Argela.

The initial management team worked on this, about 50 people working on this project from within Türk Telekom. But we will be transferring all this into Argela and seeking to use this as a service that can be sold as a managed service to other operators globally.

Obviously, I don't want to go into the normal stuff of 200 value-added service and mobile applications. You are very well aware of that. I would just like to mention that the relaunch of Türk Telekom music brand under the name Muud has been very successful I believe. And that's also a direction that we will be taking in relation to what we offer our services and am I would like to hand over to my friend Kaan. Thank you.

Kaan Aktan: Thank you, Paul. Hi, everyone. Let me now move to the financial performance. This is on Slide 12.

In the third quarter, we continue to deliver solid set of results. Consolidated revenues sustained double digits growth momentum. Quarterly revenue reached to TRY 4.5 billion. Operational revenue growth, which is, excluding, IFRIC which is the construction adjustment, was 12 percent. Mobile revenue was the largest contributor to our consolidated revenue growth in this quarter, with 15 percent year-over-year increase. This is driven by data monetization firstly, and focus on increasing smartphone, postpaid and LTE penetration through our integrated tariffs.
Broadband revenue growth revenue was 14 percent supported by consistent base growth and higher value revenue in the existing base, which came with upsells and price adjustment.

We also had our corporate data business growing 15 percent year-on-year in the third quarter. This is coming through our best-in-class products like TTVPN and TTUNEL for our corporate and public sector customers. On top of that, we saw an accelerated growth in international revenues this quarter. This is partly the result of appreciation of Euro and US dollars against Turkish lira.

Annual revenue decline in fixed voice decelerated to 6 percent now, compared to high single or low double digits rate in the previous quarters. This came with the exceptional strength in fixed voice metrics as previously explained by Paul. Our revenue performance is coupled with ongoing cost efficiencies on the successful execution of integration process, synergies and cost control initiatives. This moved EBITDA up by 16 percent to TRY 1.7 billion. This also means 2 percentage points year-on-year improvements in the margin, which is now at 37 percent. Our EBIT also increased by 33 percent in this quarter. This is the natural result of higher EBITDA, but also rather normalized depreciation, amortization level.

Personnel expenses remained flat year-on-year in this quarter. The impact of organizational streamlining is the major driver here. Our headcount excluding the call center employees declined by around 5 percent in average versus last year. Overall, we forecast personnel expenses for the full year to grow at low single digits.

Commercial expense growth accelerated in this quarter as a result of much higher subscriber gains and intense commercial activity. In the last 12 months, we gained 2 million subscribers and out of these number, close to 1 million came in the third quarter.

Before moving towards the financial metrics, let me say that we will keep our EBITDA guidance unchanged. So obviously, the first 9 months performance gave us a lot of confidence for the delivery of the guidance in EBITDA. We should expect the delivery to be at the higher end of the range close or around to TRY 6.4 billion.

At net income levels, the number for the quarter is close to TRY 300 million. For the first 9 months, this is TRY 1.25 billion. This is 88 percent higher compared to last year.

Finally, capital expenditures in the quarter was TRY 554 million. Our 9 months CapEx is now at TRY 1.5 billion. We spent less than our normal run rate in the first 9 months. We always had investment activities skewed towards the year end. And you would also remember that we increased our CapEx guidance in midyear based on strong market dynamics and internal needs. That also creates some further concentration on the last quarter. Having said that, we still target to finish the year in the vicinity of our CapEx guidance.

Now we're moving to Slide 13 with the debt profile. Net debt-to-EBITDA multiple is now below 2. To be exact, this is 1.96. This shows an improvement compared to, for example, 2.23 of the first quarter. The decline driven both by a strong operational performance and the completion of payments related to LTE license fees.

We had some cash outflow in our trade payables if you look at our balance sheet, as a result of newly establishing payment cycles of our supplier finance programs. Our total debt is TRY 15.4 billion. We have a 3.1 years average maturity on the debt. 13 percent of total debt is short-term, which is around TRY 2 billion. Our total cash balance at the end of the quarter is TRY 2.8 billion. This is fairly higher than our short-term debt. The majority of our debt, in other words, 70 percent of it has a maturity beyond 2 years.

In this quarter, we executed some hedging transactions. We acquired additional USD 100 million to Turkish lira participating swap contracts. These are attached to our 2024 bonds and with this recent transaction 95 percent of our USD 1 billion Eurobond is now swapped to Turkish lira under different hedging structures. We may execute other hedging transactions in the coming period, depending on the markets condition.

At the same time, we will continue to use cash as a tool for managing the currency risk. We're accumulating cash and we are keeping a higher percentage of the cash in Euro or Dollar. At the end of this quarter, 61 percent of the cash was in foreign currency, which is up from 24 percent of end of last year.

All-in-all, Türk Telekom's leverage level continue to be at the low end in comparison to major global peers. And one last remark for this, in the third quarter S&P and Fitch completed their annual reviews and they both confirmed our investment grade credit rating.

Well, thank you very much for listening. We will now initiate the Q&A session.

Operator: We have a question for you. Your first question comes from the line of Can Oztoprak of Unlu&Co.

Can Oztoprak: Can Oztoprak from Unlu&Co. My question is on the PSTN side. Net addition is pretty encouraging obviously. Given the fact that this line of business has already completed its investment, are you seeing any further potential for more value extraction from this line of business?

Boulos H. B. Doany: Thank you for that. This is not a question of what one would normally do. This is an opportunistic strategy. So the opportunistic strategy is based upon that the broadband penetration in Turkey is currently below what it can be in terms of affordability and also in terms of availability of infrastructure. And so when we say we have homes passed, we also have homes connected.

So if you have home connected, which cancel the fixed voice when mobile voice became more appealing and cheaper and, et cetera, but the line is still there. So what we managed to get is the ability to provide a very low priced wholesale charge, which actually is 0 for that type of customers who have fixed line so they can retail at TRY 15.

Now that is a very low price for an entry package Internet, which a person of that level would not normally consider, simply because it's not available. So the issue is to make it available where we can, which by the way is quite a large number.

If you take the fixed voice currently that they don't have broadband, that's a nice easy target for them to get broadband 20 Gig in that location, but at 4 Mega speeds. So this is more opportunistic in order to build the possibility of those homes, upgrading in the future for a fixed broadband, whereas otherwise they would simply stay wireless. If they stay wireless, they are under using their data potential and probably we will never be able to get them in the future. That's the idea.

Operator: And your next question comes from the line of Vyacheslav Degtyarev of Goldman Sachs.

Vyacheslav Degtyarev: You have done very good job in terms of cost control and margin improvement in the company this year. So how should we be thinking for the next year? Do you think that you have already picked most of the low-hanging fruit and you have a limited margin improvement potential for 2018? Or maybe you see some particular tailwinds in terms of your cost performance for the next year?

Boulos H. B. Doany: OK. What I would like to say is, I would like to say that now the strategy of the company which will go towards answering your question in a more general way and I use this opportunity to explain it further.

So I have covered now the fixed voice parts and when the tax 7.5 percent starts as of next year which coming down from 15 percent, it provides for a further opportunity to drive, if you like, fixed data over an existing voice line or over a previously canceled voice line. So there is a very high potential growth here. But it may not provide a high revenue.

In fact, it will provide very little revenue to us. But the importance of those are potential future growth. So once we connect those customers, they will be an easy upsell in the future. If we don't connect them now, we will not have that revenue opportunity in the future.

This is why we have the special agreement with the regulator that we will not net revenue out of this. Retail, will net some. And that's why also we need to build that, if you like through, alternative carriers. On the remaining part of broadband today, if we take the total penetration in Turkey, it's still below 50 percent, in the high 40s. And Turkey can easily reach 70 percent by all its providers. So that means us. It also means the cable-TV. It means Turkcell what they currently have by themselves. And Vodafone and what they use over Telekom. So there is a huge growth potential that can be served cost-effectively by fixed line, where fixed line is available, and justify fixed line investments where the incremental CapEx can be justified.

That's key and critical, if you like, for this company and also for the country in general. And that's an area that we now have no further obstacles in our way to realize that. Meaning, regulatory obstacle or a pricing obstacle, et cetera.

Then in relation to mobile growth, how do we sustain continued mobile growth? Well, one of the ideas to maintain the mobile growth is that we see now that based on the structure of SCT that you're now seen come down to a total of 7.5 plus 5, so total of 12.5, if you add the TRX to the current cost of SCT average between voice and data, you see that there is an actual trend going downwards.

So the government basically in a position of losing or getting less proceeds from the operators. So what this now does allows the government to maintain, let me say, a flat level going forward at least in percentage and the operators to remove any further uncertainty as what is data and what is voice, you see, because we would all we have any risk in the future.

The treasury share was a matter of dispute on a discounted price. So they were taxing us on a discount. So imagine us in the future discussing what is voice and data legally as opposed to what would that be for the purposes of tax application. So what this does for us is that we're now above the 12.5 percent in total in mobile.

So next year that will be 12.5 percent. So that's an opportunity that we can use to grow or definitely to grow our net revenue. Out of that, obviously our margin. The same thing would apply to Vodafone. Turkcell would be motivated to go for more quality and increasing price, which is I think is very important for the sector to move in that direction. And they have the natural ability to do that. So that sector would develop the way we see it.

What would be remaining out of that picture is the wireless -- what we call the wireless homes for us is the one that we can easily now serve by satellite-TV. What that does, it gives us a very high penetration opportunity simply because Digiturk is a premium player, which, therefore, by nature has to be high priced because they have a lot of exclusive content. And D-Smart is cash strapped, so they cannot grow very much from where they are. They are important customers of ours in the wholesale terms. So we, therefore, have an opportunity here since we already have satellite-TV. Again, very opportunistic. If you ask me whether we would do it if we didn’t have it, that would be an academic discussion, but I wouldn't be as tempted to do it since now we have it, if you see what I mean.

That also provides a unique opportunity to this company. So, therefore, the sustainability of what they are now presenting to you goes well beyond 1 year, if that is your question. We're looking at the 5-year sustainable story.

Kaan Aktan: And for the OpEx part, I mean we're sure, that we harvested a lot of benefits from restructuring throughout year. For the next year, it's a bit early. We would like to discuss in more detail when the time comes for the guidance. We still see that it may not be across the board, but we may some OpEx benefit here and there. We're working on those items. And also, let me also remind you that if that new law passes through the parliament there will be some additional OpEx, because the rebalancing at the special consumption tax in mobile was done with some more OpEx as TRX and more revenues with lower taxes. But we will give you the details so that doesn't get confusing for the analysts.

Operator: Your next question comes from the line of Walid Bellaha from Barclays.

Walid Bellaha: I have 2 questions if I may. Just to clarify on the special tax for telecoms. So my understanding is that there is a 15 percent for fixed telecom, 25 percent for voice and SMS for mobile and 5 percent for data. So what you're saying is that this will be equalized to 7.5 percent starting from next year, is that correct?

Boulos H. B. Doany: Well, I mean the proposal that has -- that went to parliament -- and by the way I mean this particular aspect of the proposal is very easy for the government to pass. So, therefore, you can assume that this is going to happen. So what it is that today on mobile, the voice is 25 percent and the data is 5 percent. OK? Now that will become 7.5 percent.

However, just be careful on one point, that we have a -- we were potentially going to have a future dispute on TRX, which now will be capped at 5 percent. Why this is important for all the sector, for all of us, because that TRX should be 0 actually. But concession has a number in it and that was lack of clarity on how that would be implemented, which means that we would have had a major dispute with the government in a year or 2 on a very high number, which we think is unfair, which we think should be 0 even.

But we started paying all of us a certain amount. So what this results is, if you like, we're protected now. The uncertainty became 5 and the average of 25 and 5 became 7.5. So it's a very important development for the full sector, all operators, very, very important.

Walid Bellaha: Understood. So how should we then look at the margins, if this measure is passed next year? Will that imply some improvement in your margins going into next year or the amounts that are owned to the treasury?

Boulos H. B. Doany: OK. In relation to our mobile play, right, today we have certain average of SCT, which you may be able to work out between what you now see as base of our voice and our data. And you have to make an estimation of what TRX is, because we normally don't disclose what that is. But now luckily for all of us, that will become 5. We are now below 5 on that. I can give you a clue on that. And we're definitely way over 7.5 today on the balance of 25 and 5.

So that means going forward, that gives us an ability to be more competitive if there is price competition or to be able to build up additional revenue or margin from our current base through further upsell of data. So, we have the opportunity of both. And we hope and believe it will be more of a revenue growth and margin improvement, which is basically what all operators have done so far.

Walid Bellaha: Thank you. And my second question is regarding your hedging of the balance sheet of FX debt. So, in September you increased your hedging you mentioned that in the call. Could you just comment on your target of how much of your FX debt you would like to be able to hedge against currency variations.

Kaan Aktan: Well, I can only say that we will increase the exposure to Turkish lira, meaning that will come with further hedging transactions. But I cannot give you a target for the time being. It will really depend on how the market, how the internal thinking will move. But it will be something higher than today.

But also that we remind you that the fourth quarter will be, in terms of cash generation, to be a strong quarter, as well as the first quarter next year. So, in line with our strategy to keep our cash in dollar and euro, that will also contribute. So I can tell you from today that we will be close or more than 75 percent of our cash in hard currencies as we move on. So that's the decision we already made.

Walid Bellaha: Just lastly, on the shareholder structure, could you update us on what's the stage -- what's the current stage regarding the government involvement in the shareholding structure?

Boulos H. B. Doany: OK. Just to be very clear. What the government did, the government served notice to the defaulting party, which they are entitled to do, to introduce a change in the board members, which currently the Ojer Side has 7 members out of 12. So they have served the notice first on 20 working days and then followed by 60 calendar days which expired early October.

Now we're now at the stage where the notice period has been -- has lapsed. And this allows the replacement request to be done by agreement between the parties, because there is an agreement on how this will be executed. There has been recent press in relation to the references to a request for an extension on this.

In fact, there was such a request for an extension, but that is -- that doesn't deny STC the ability to continue talking to the banks. And in any case, they are still on the board right now. So the reason the government provided that notice to the Ojer side is to be able to have a replacement instantaneously as opposed to then going through a notice. So that's the reason it was done.

And if you ask me how it will be done, it will be done by agreement between the 2 sides. And this relates to board change, not ownership change. On ownership change, I cannot comment because that's not something that we're related to. In other words, has nothing to do with us.

Operator: And your next question comes from the line of Maddy Singh from Morgan Stanley.

Maddy Singh Good set of numbers. Can you please give some color around the competitive dynamics in the market, on both mobile side as well as on the rest of the business? And secondly, on the CapEx side given that you already have this network sharing agreement with Vodafone, is it fair to presume that most of the CapEx then will go into the fixed side?

Boulos H. B. Doany: Let me take the second part and then I will hand over to Hakan on the competition dynamics. So now the agreement or let me say the basis of what we have now by way of sharing with Vodafone as you may remember, was a passive sharing of a 1-1. What we're doing now is we're changing that model into active sharing, which we're allowed to by LTE.

So that form of operation allows us to get a value in coverage to us that would be much more costly if we were to do it ourselves. So in the sharing form, we can get more coverage than we have now at a much lower incremental CapEx than we would otherwise. That's the value to us.

The value they get of course is they need more capacity, which they can only get by having more stations and therefore, they end up sharing some of ours in the same way. So that doesn't actually reduce the potential CapEx that we need to invest. It allows us to get a lot of more value for the CapEx we invest.

So the idea is not that we invest less, the idea is that we bridge the quality gap between us and Turkcell over time in a cost-effective way. If we were individually to try to do that, a lot more expensive for us to do it. So, therefore, again this is -- and again this will take time obviously. So, therefore, the idea isn't that now we don't invest in mobile, we invest in fixed.

So, these are 2 separate optimization approaches. We're trying to get best value for every incremental CapEx we put in mobile. We can achieve it this way. And on the fixed, it's more about utilization. So, every incremental we do should be valuing or benefiting from what we have already build.

And if we're providing for an additional facility, it means cases where the incremental CapEx has to be again recoverable from the targeted customer we're seeking. So we have to be very disciplined in how we invest. And therefore, these are totally independent sets of approaches, Hakan. Mobile market structure.

Hakan Dursun: Hakan Dursun, Chief Marketing Officer. So, very briefly, the competition on different segments of the market. Actually, we have a unique position because we're not a mobile only operator. We're a multiplay operator.

Therefore, we have a solid strategy, which is not even for 1 year, which is for 5 years, and we are following our strategy in a very financially disciplined way. We make markets, we grow our market share, we grow our ARPUs and also subscribers according to our plan. So, in this respect, maybe I have to touch some of those segments very quickly. For fixed voice, we already discussed this.

So fixed voice is a record performance this quarter both in terms of ARPU revenue and also in terms of subscriber growth. Then we talk about mobile in general. The first half in mobile market was a very aggressive half. Especially Turkcell and Vodafone were very aggressive on entry-level and also retention offers. While we prefer to focus on other sides of our business, because we're a multiplay operator, and we were focusing on value increase in the first half in mobile.

Starting with third quarter, we also focused on acquiring additional customers on mobile segment, again in a disciplined way. And we see that our net adds performance increased from 50,000 mobile net adds to 414,000 mobile net adds in this quarter. Now when we look at the dynamics especially towards the end of Q3, we're seeing some price adjustments in the market.

And going forward, we are going to act in line with the general competitive dynamic of the markets in line with our plans. On fixed broadband side. Basically we have a very solid revenue performance and subscriber performance in Q3. And all the trends in all fronts, including ARPU are in line with expectations.

Not only we're increasing our ARPU and subscribers, but also we are making market as Paul explained very well. So, it is securing our future not only for our retail business, but also for all ISP players in the market. And also TV side is very strategic for us.

Now we have penetration approach for TV in order to be present in as many homes as possible, which is in the future very strategic for us in order to provide wireless -- what you call wireless broadband. When 5G arrives over a mobile network.

And now over we have exceeded 2.5 million subscribers in TV, whereas 1 million is on big screen. And we're proceeding very well according to our plans on TV side as well. Also in TV business, we're by far the most preferred Pay-TV operator in the market in the last couple of quarters.

Maddy Singh: OK. So is it fair to say that if you are also going to act in line with the competition in mobile space, especially there is a risk of some kind of price war.

Hakan Dursun: Actually, there was very aggressive price war by competition, we were not involved, in the first half of 2017. We decided to focus on other sides of our business, as Paul explained very well. We were focusing on growing fixed broadband market, retaining fixed voice customers, focusing on TV, coming up with mobile subscriptions. So, we had a different game plan.

We were not engaged in competition at all, we focused on value and market making. And in third quarter, again in line with our plans, we focused on acquiring mobile customers, where also the aggressiveness in the market eased. So it did not come at a very high cost to us, which was very rational and according to our plans. Now we're following the markets. And we will be financially disciplined and also following our strategy.

Boulos H. B. Doany: Yes because -- I can give you a little bit more explanation on this is that in the first half of the year we were working on this market-making opportunity. And we wanted to understand what we will be able to do in order to grow the broadband. And that required some discussion internally and also with the regulator and also with the ministry.

So, as we were studying this and we were very hopeful, we hope that we would be able to come up with something that can work, the market was getting a little bit hot in the mobile and we deliberately held back. Because Turkcell and Vodafone, were, let me say, were getting a little bit more competitive. And this started making a bit overly competitive offers we believe. So, we focus on areas where we did not need to play that game while to understand if we can get our strategy to work.

Now in the first part, we now obviously on the entry Internet, that is now done. The port transmission uncertainty pricing with regulator is now done. So, everybody knows what that is. A way for us to be able to grow that segment now and get up to that broadband penetration which will take time. But that's the whole point is that we have a sustainable revenue growth would becoming from that.

Now obviously we now know that can be done and we progressed a lot with the electricity companies. As you can well imagine, that will take some time. We will be announcing that in the next couple of weeks or so. We thought that we will be even able to manage it this week.

So we were more focused on these things, rather than fighting it out with the other 2 mobile operators. And then in this quarter, we decided now it's time for us to start to recover our, if you like, penetration or mobile market share growth. Because that is obviously very key for us.

I mean some people may have the impression that we're gonna turn inward and try to be profitable mobile without growth. Our strategy is not that. Our strategy is to be -- get our fair market share in mobile and profitably. And that's why the issue of sharing is very key. And that's why we go from just 2,000 passive sharing into full active sharing.

Operator: And your next question comes from the line of Ondrej Cabejsek of Berenberg.

Ondrej Cabejsek: Two things I would like to ask about. The first is following up on the tax issue. As in my understanding -- or is my understanding correct? that you sort of look at potentially passing of these savings on the tax side to the customers on the fixed side? But in order to sort of drive penetration especially of the TV product you mentioned Digiturk and DSmart are sort of trapped in the premium segments.

So would be thinking on passing these taxes -- or rather absorbing these taxes and passing the savings on to the customers? And then mobile that depends on what the market allows you to do. That's my first question.

Second question: In terms of the digital transformation, I just would like to understand whether your partnership with GE also serves as a sort of learning tool for you. And how far down this road you are? Whether you already have some visibility on potential OpEx cuts from the likes of digital customers journeys, lower commissions paid, lower network cost, et cetera.

Boulos H. B. Doany: Thank you. Let me start with the second one, because it is difficult to sort of, answer that one in a very direct way because GE isn't it really the right partner for us in relation to our own internal digital transformation. But rather they jointly -- we can target large companies in areas that they are strong in. And we're going to focus actually with them on the number of verticals.

I mean health seems to be a very important one for both of us where we have joint effort on a go-to-market in that direction. Also, we see energy could be the second one. Others will be opportunistic entries into mostly industrial groups in the country and they have already a list of, let me say, 2 serious customers out of a short list of 10. And therefore would be an ideal partner to jointly go-to-market.

So they are not really -- GE is really not a good party for what we do as a business. It's more looking outward. In relation to what we will be doing, I think we will have more to say on that perhaps on the next call because we're doing something also through Innova, which is a better partner for that part. And I'd leave that for another call. But definitely we will be moving in the that digital direction in 2 to 3 months we will have more something more serious to say than just to give generalities.

Now in relation to the further explanation on the tax now, now clearly on the fixed voice we will pass all the value to the customer. On the broadband, the tax is going up from 5 to 7.5. So those who have fixed, meaning voice and broadband, they will be flat. Those who have only fixed, is an opportunity for us to upsell the cheap Internet to them, very, very cheap.

That would be helpful for us. The limited ones who have only broadband. This is a very small amount, but we will be passing it on to the customers. It is important by the way that we actually do that because we're a retailer of those and in wholesale, that would be squeezing the margin. And therefore, we would definitely have to pass it on to the customers and that's exactly what we will do. Because we're always increased prices whenever we can in that relationship.

On the mobile, I think you also said it perfectly, if we turn into a price competitive situation, we will have a lot more room to play. But I don't think that the other operators are going to playing in that because they are seeking to improve their financial performance, both of them. And that's exactly also what we intend to do.

So I think that we will be reaping the benefit of the lead that Turkcell build for everybody. They showed, let me say the government where the sector would be, being ahead obviously and then the government said, look, I'm losing tax. But then, of course, we also said that TRX is a nightmare for us and we don't want to go to court or something like that. So this was a negotiation between us and them.

So that's how the balance adds up to that 12.5 percent. So just consider that TRX uncertainty could have been a very major headache. So that total of 12.5 actually is the right balance for all sides. That's why even Turkcell benefits, Vodafone benefits and perhaps we benefit a bit more on the mobile side. But that may give us more room to target the segments we want to target.

Ondrej Cabejsek: OK. So if I understand correctly, it sounds like you sort of, overall impact, and I apologize if you commented on this already. But the overall impact from your what you're saying it seems to be that you would be targeting for sort of neutral impact taking the benefit you potentially might have. instead of reinvesting it into the fixed subscriber platform? Is that correct?

Boulos H. B. Doany: Actually, while not exactly. I mean that sounds a bit too intelligent and I'm not trying to be too intelligent, to be honest with you. So we look at each segment separately, absolutely separately. So we are not going to cross subsidize.

So in mobile, it has to stack up as it is. We have to increase our mobile market share and the only way you can do that is to have a lower cost of CapEx and OpEx that justifies this growth. And we don't want to do it by lowering prices. So we have a gap in the tax, which gives us value.

Now we want to do that through satellite-TV. So, we're offering satellite-TV near free if a customer buys our mobile at a normal price. That's how we're playing it. We're not -- so don't mix it with the fixed. We don't play that game between fixed and mobile. We can play with satellite-TV because we have full freedom on pricing. If we start to try to bundle on fixed, we lose.

So what we do is we cross-sell, upsell, we don't bundle. Bundle never works. And also it puts us in a situation where your targeting a different part of the home. And mobile customer is a mobile customer. He's not a home customer. That's why he's very key for us. And that's why the satellite-TV is key because that can be a future mobile subscriber.

How I can get a mobile market share, fair share of getting to the 1/3, let's say, or a bit below that. That's the only way we can do it without just lowering prices. You see the point on the mobile. So we're very disciplined and we have to be that way. We cannot just merge the two together saying I will take a hit on mobile to get fixed. It doesn't work that way. Every single element has to justify. Any money going in, has to provide the return. That's how we're operating.

Operator: And your final question comes from the line of Mitch Reznick of Hermes.

Mitch Reznick Just follow-up on ownership question. I've got 2 questions. On the ownership structure, I mean obviously the bonds are trading at or above par. Is there any kind of change in ownership that would lead to change of control event on the securities to be puttable to you I would guess would be par?

And second question is related to just a little bit, you've talked about the what's going on? But what is the kind of Optical outcome for you as you fast forward 3 to 6 months time for this whole affair?

Boulos H. B. Doany: The last part again?

Mitch Reznick: And just asking what is the optical outcome for you in terms board structure, ownership, everything that's going on with the restructuring of the loans?

Boulos H. B. Doany: OK. Let me take the second part and then Kaan gone will take the first one. So the first thing that we need to recognize is that we're isolating totally the OTAS lender situation, regardless who owns the shares from the operation of the company. I mean in fact my main mission is to make sure that, that isolation is absolutely complete.

So we're now operating through a board that is helpful. Ojer side is helpful in all decisions that we need to raise, that require board consent. So we're fully operational in that regard. We have built our own management case now. By October, we will be taking that as the business plan with the new 5-year plan. Along the lines, I have given you some indication of. So you can build your own models of it. So that's where we're.

Now, as a first step, the government indicated that they would look at changing the board. That could be an important thing to do at a certain point. If STC, for example, cannot agree with the banks and other party wants to talk to the banks. Again this is not an issue for us.

So all we need is for the board to operate. If the government have 5 members and then they increase that 5 up to a number, 7 is a number we need for any decision, Ojer have been very helpful. From Oger side said that there are 5 members plus 2 from STC. So we're still operating with this board.

At a certain point we would want to do what the lenders intend to do, be that with STC or with any other party that would end up getting the shares. And if and when at that point there will be a new owner of that 55 percent, that would be something to discuss at that time. And Kaan can relate to you what we've done actually at the level of TT lenders and you ask specifically on the matter of bondholders.

So, my role was specifically to decouple completely and this is something Ojer have consented to. And that is why in fact we're able to operate this way. So, of course, we not going to operate like this forever, right. So the government is now have the tools that enable it without further delay to institute a change in the board because they have served notices. And this again is done with an agreement with Ojer and STC. So Kaan on second question.

Kaan Aktan: For the impact of a change of control on the bonds, so there are 2 steps or there are 2 different things that have been discussed here. First is the change in the composition of the board. So would it trigger a change of the control in terms of the rules. For the change in the board composition, Fitch made an announcement saying that they would not consider this as a change of control. But also let me remind you that a change of control is not enough for the bonds -- for the rules under the bond issuance to be applied as a change of control. It should also trigger a change in our rating.

So, there are 2 steps to go to a change of control for the bond. So for the change at the board level, Fitch said they are not considering this as a change of control. Or they don't think that would trigger any change in their evaluation of the company.

When it comes to the real change in the shareholding structure, which means transaction at the shareholder level, I mean the rating agencies says they will evaluate the case when it comes, depending on the structure on who is buying the shares and what will be the governance structure between the new shareholder and Türk Telekom, they will do their evaluation at the time.

Boulos H. B. Doany: To give you a brutal answer to your question. Based up on the discussion with Fitch and S&P, I can give you CEO answer as well in the sense that there is no reason to expect any change in the rating for the scenarios of ownership change that we think may happen. There is no reason to worry about it. So that is as clear as I can be.

Mitch Reznick: I guess, if there was a change in controlling shareholders that would trigger the change of control?

Boulos H. B. Doany: Just the rating.

Mitch Reznick: OK, just the rating.

Gozde Cullas: Thank you. This ends our conference call.

Operator: Ladies and gentlemen, thanks for participating. You may now disconnect.

END