MAKEDONSKI TELEKOM AD - SKOPJE
Kej 13 Noemvri No. 6, 1000 Skopje, R. North Makedonija

To:	Macedonian Stock Exchange AD Skopje Orce Nikolov 75, 1000 Skopje
Date:	February 2019
Subject:	Explanation on the operation of Makedonski Telekom AD - Skopje for the period from 01.01.2018 until 31.12.2018

The following analysis refers to the unaudited financial statements of Makedonski Telekom (MKT) for the period 01.01.2018 - 31.12.2018, prepared in accordance with the International Financial Reporting Standards (IFRSs).

The application of the new standard IFRS 15 Revenue from Contracts with Customers is effective for periods beginning on or after 1 January 2018. IFRS 15 has superseded IAS 11 Construction contracts and IAS 18 Revenue for periods beginning on or after 1 January 2018. The adoption of the new standard resulted in significant changes in the financial statements of MKT, primarily in respect of the timing of revenue recognition and in respect of capitalization of costs of obtaining a contract with a customer. In the case of multiple-element arrangements (e.g., mobile contract plus handset) with subsidized products delivered in advance, a larger portion of the total remuneration is attributable to the component delivered in advance (mobile handset), requiring earlier recognition of revenue in future. This leads to the recognition of what is known as a contract asset – a receivable arising from the customer contract that has not yet legally come into existence – in the Balance sheet. At the same time, it results in higher revenue from the sale of goods and merchandise and to lower revenue from the provision of services. Under the new standard, expenses for sales commissions (customer acquisition costs) must be capitalized and recognized over the estimated customer retention period. MKT utilized the option for modified retrospective approach initial application, i.e., contracts that were not completed by 1 January 2018 have been accounted for as if they had been recognized in accordance with IFRS 15 from the very beginning. The cumulative effect arising from the transition has been recognized as an adjustment to the opening balance of retained earnings in 2018.

The application of the new standard IFRS 9 Financial Instruments is effective for periods beginning on or after 1 January 2018. The standard addresses the classification, measurement and derecognition of financial assets and financial liabilities and introduces new rules for hedge accounting. In December 2011, in November 2013 and in July 2014, the IASB amended the standard in order to make further changes to the classification and measurement rules and also introduced a new impairment model. These latest amendments completed the new financial instruments standard. As of 1 January 2018, MKT classifies its financial assets in the following measurement categories: those to be measured subsequently at fair value and those to be measured at amortized cost. The classification depends on the entity's business model for managing the financial assets and the contractual terms of the cash flows. As of 1 January 2018, with the transition to IFRS 9, loss allowance is recognized in respect of not only losses already incurred as of the reporting date (incurred losses) but also losses which have not yet incurred as of the reporting date but which are expected to be incurred in the future (expected losses). The adoption of the new standard and its amendments did not result in material changes in the MKT’s financial statements. The new provisions on the classification of financial assets will not give rise to changes in measurement and presentation of financial assets.

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Company Reg. No. 5168660 | Principal capital MKD 9.583.887.733,00

The effects from operations for 2018 presented below, for the purposes of the comparative analysis with the previous year are given without the influence from the International Financial Reporting Standard 15 Revenue from Contracts with Customers and the International Financial Reporting Standard 9 Financial Instruments.

I Revenues

The sales revenues in 2018 amounted to MKD 10,462,121 thousand, which represents an increase of 2.0% (excluding IFRS 15 impact) compared to the previous year.

The implementation of IFRS 15 has positive effect of MKD 37,191 thousands on total revenues.

Voice services

Fixed line voice services

MKT has managed to maintain the **leading position on the fixed voice market with 56.1%** (internal estimation) or 212.3 thousand customers at the end of 2018.

The voice revenues in 2018 in the fixed segment services have decreased by 8.1% (excluding IFRS 15 impact) compared to the previous year due to decreased outgoing traffic by 10.6% as well as the decreased international and national incoming traffic. At the end of 2018 the number of customers in the fixed voice marked a slight increase of 0.7% compared to the previous year.

The implementation of IFRS 15 has negative effect of MKD 21,347 thousands on fix voice revenues.

Mobile voice services

On the mobile market, the MKT has a **market share of 49.7%** (internal estimation). The subscribers' base at the end of 2018 amounts to 1,206 thousand subscribers and it is slightly increased by 0.2% compared to the previous year.

At the end of 2018, the **mobile voice revenues** (including voice wholesale revenue - incoming) are decreased by 1.8% (excluding IFRS 15 impact) compared to the previous year. The decrease is due to lower volume in international incoming mobile terminating traffic. The blended ARPU (Average Revenue Per User) has increased by 6.3% compared to the previous year amounting to MKD 354 mostly driven by the increase of post-paid subscribers' portion in the total subscribers' base.

The implementation of IFRS 15 has negative effect of MKD 236,748 thousands on mobile voice revenues.

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Internet, TV and other non-voice services

Fixed Internet and TV

At the end of 2018, the number of total BB accesses is increased by 1.2% and amounts 196.3 thousand compared to 194.0 thousand at the end of the previous year, while the **broadband Internet market share** at the end of 2018 **amounts to 45.5%** (internal estimation). The investments in the optic network have resulted in an increase by 7.1% of Households passed with access to the optic network compared to the previous year. At the end of 2018 the total coverage of the Households with access to the optic network has reached 30.5%.

Regarding the **TV market**, MKT has a **market share of 30.6%** (internal estimation) of the total TV market. The IPTV (digital television via Internet protocol) service, with its high quality, interactivity and the unique TV experience, is excellently accepted on the market and MKT achieved an increase of the number of IPTV customers (including Magenta1, 3 Play and other TV services) by 9.3% compared to the previous year, which has resulted in a customer base of 128.4 thousand customers at the end of 2018.

The **revenues from digital television via Internet protocol ("IPTV")** at the end of 2018 have increased by 14.5% (excluding IFRS 15 impact) compared to the previous year. While positive growth in TV ARPU (Average Revenue Per User) could be sustained, the intense competition continued to put a pressure on broadband ARPU. Therefore the **Revenues from retail Internet** at the end of 2018 have declined by 1.1% (excluding IFRS 15 impact) compared to the previous year.

The implementation of IFRS 15 has negative effect of MKD 51,119 thousands on Internet and TV revenue.

Mobile non-voice services

The non-voice revenues in 2018 have increased by 11.0% (excluding IFRS 15 impact) compared to the previous year, as a result of the increased mobile internet revenue due to the higher GPRS traffic and increased usage of data tariff plans.

The implementation of IFRS 15 has negative effect of MKD 119,372 thousands on Mobile non-voice services.

Other revenues

Other revenues in the fixed and mobile segment

The **revenues from the sale of equipment** at the end of 2018 have increased by 8.8% (excluding IFRS 15 impact) compared to the previous year, due to the higher average selling price of handsets as well as the higher number of sold handsets.

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The implementation of IFRS 15 has positive effect of MKD 466,406 thousands on revenues from sale of equipment.

System integration and IT revenues at the end of 2018 continued to grow dynamically after the last year's temporary decline and the same have increased by 41.6% compared to the same period of the previous year. The higher revenues are result of the larger number of customised ICT projects.

II Expenses

Operating expenses

On the cost side, at the end of 2018, the operating expenses are increased by 1.8% (excluding IFRS 9 and IFRS 15 impact) compared to the previous year.

The implementation of IFRS 9 and IFRS 15 has negative effect in amount of MKD 30,524 thousand on the operating expenses.

The employee related expenses have increased by 5.9% (excluding IFRS 15 impact) at the end of 2018 compared to the previous year. The increase is due to the severance cost for employees who left the Company in accordance with the Programme for voluntary leave, The implementation of IFRS 15 has positive effect in amount of MKD 11,769 thousand on the employee related expenses.

The cost of trading goods sold have increased by 11.2% at the end of 2018 compared to the previous year.

The cost for depreciation and amortization at the end of 2018 has increased by 5.5% compared to the previous year.

Capital expenditures

The amount of total Capital expenditures (CAPEX), at the end of 2018 is MKD 2,037,713 thousand.

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III Operating and Net profit

The above-stated movements of the revenues and costs resulted in an increase of the Earnings before interest, taxation, depreciation and amortization (EBITDA) for the 2018 by 3.3% (excluding IFRS 15 and IFRS 9 impact) compared to the previous year. Implicitly the EBITDA margin for the 2018 amounts 39.2% (excluding IFRS 15 impact and IFRS 9 impact).

Operating profit (Earnings before interest and taxation - EBIT) for the 2018 is stable (excluding IFRS 15 and IFRS 9 impact) compared to the previous year.

Net profit for the 2018 has increased by 2.5% (excluding IFRS 15 and IFRS 9 impact) compared to the previous year, while the net profit in accordance with IFRS 15 and IFRS 9 has been increased by 2.9% and amounts MKD 1,421,564 thousand. The implementation of IFRS 15 and IFRS 9 have impacted the net profit and resulted in the positive net effect of MKD 6,000 thousands including the negative effect on deferred tax in amount of MKD 667 thousand.

In MKD thousands	*2017 Dec YTD in accordance with IAS 11 and IAS 18*	*2018 Dec YTD in accordance with IFRS 15 and IFRS 9*	*Change YoY*	*IFRS 15 and IFRS 9 effect*	*2018 Dec YTD in accordance with IAS 11 and IAS 18*	*Change YoY*
Total Operating revenues	10.368.035	10.564.528	1,9%	-37.191	10.527.337	1,5%
Sales revenues	10.221.094	10.462.121	2,4%		10.424.930	2,0%
Total Operating expenses	8.754.428	8.945.789	2,2%	30.524	8.915.265	1,8%
Deapreciation and amortization	2.387.440	2.519.279	5,5%	0	2.519.279	5,5%
Earning before interest, taxation, depreciation and amortization (EBITDA)	**4.001.047**	**4.138.018**	**3,4%**	**-6.667**	**4.131.351**	**3,3%**
EBITDA margin in %	38,6%	39,2%			39,2%	
Operating Profit (Earning before interest and taxation - EBIT)	**1.613.607**	**1.618.739**	**0,3%**	**-6.667**	**1.612.072**	**-0,1%**
Deferred tax effect				**667**		
Net Profit	**1.380.848**	**1.421.564**	**2,9%**	**-6.000**	**1.415.564**	**2,5%**

IV Paid dividends

The Shareholders' Assembly of MKT, at its meeting, held on 16 April 2018 adopted a Resolution for the dividend payment for the year 2017 and determination of the dividend calendar. In accordance with this Resolution the dividend for 2017 is in total gross amount of MKD 1,584,851 thousand.

The gross amount of dividend per share for 2017 is MKD 18.37. The dividend was paid out in September 2018.

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V Plan and expectations for the next period

The plan for 2018 was prepared based on the assumptions for relatively stable macroeconomic environment and already consolidated market, with overall anticipated total market decline of 0.6% in 2018 compared to the previous year. The actual result are in line with the expectation.

The achievement of higher actual revenues compared to the planned revenues is result of Growth Strategy on the targeted growth areas i.e. growing the value of base, further penetration of FMC (fix to mobile convergence) / FMCC (fix to mobile cloud convergence), build ICT as new stream.

Respectively, higher revenue related cost resulted with lower direct margin. Other operating expenses/income are below the plan due to constant cost optimization of the employee related expenses, maintenance etc.

The expectations for the next period can be summarized as follows:

- Continuation of the positive development in market structure – improvement of the postpaid/prepaid ratio, positive ARPU development
- Premium TV content - one of main drivers for positioning on the market
- Improving infrastructure investments, continue with Further fiber rollout
- Smart Cities, ICT & Cloud growth opportunities

MKT also plans to maintain leading position in FMC & ensure positive value generation from convergent households.

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On 13 February 2006, Magyar Telekom Plc., the controlling owner of the Company, (via Stonebridge Communications AD - Skopje, majority shareholder of the Company), announced that it was investigating certain contracts entered into by another subsidiary of Magyar Telekom Plc. to determine whether the contracts were entered into in violation of Magyar Telekom Plc. policy or applicable law or regulation. Magyar Telekom's Audit Committee retained White & Case, as its independent legal counsel to conduct the internal investigation. Subsequent to this, on 19 February 2007, the Board of Directors of the Company, based on the recommendation of the Audit Committee of the Company and the Audit Committee of Magyar Telekom Plc., adopted a resolution to conduct an independent internal investigation regarding certain contracts in Republic of North Macedonia.

Based on publicly available information, as well as information obtained from Magyar Telekom and as previously disclosed, Magyar Telekom's Audit Committee conducted an internal investigation regarding certain contracts relating to the activities of Magyar Telekom and/or its affiliates in Montenegro and Republic of North Macedonia that totalled more than EUR 31 million. In particular, the internal investigation examined whether Magyar Telekom and/or its Montenegrin and Macedonian affiliates had made payments prohibited by U.S. laws or regulations, including the U.S. Foreign Corrupt Practices Act (the "FCPA"). The Company has previously disclosed the results of the internal investigation.

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Magyar Telekom's Audit Committee informed the U.S. Department of Justice (the "DOJ") and the U.S. Securities and Exchange Commission (the "SEC") of the internal investigation. The DOJ and the SEC commenced investigations into the activities that were the subject of the internal investigation. On 29 December 2011, Magyar Telekom announced that it had entered into final settlements with the DOJ and the SEC to resolve the DOJ's and the SEC's investigations relating to Magyar Telekom. The settlements concluded the DOJ's and the SEC's investigations. Magyar Telekom disclosed the key terms of the settlements with the DOJ and the SEC on 29 December 2011. In particular, Magyar Telekom disclosed that it had entered into a two-year deferred prosecution agreement (the "DPA") with the DOJ. The DPA expired on 5 January 2014, and further to the DOJ's request filed in accordance with the DPA, the U.S. District Court for the Eastern District of Virginia dismissed the charges against Magyar Telekom on 5 February 2014.

In relation to the local investigation by the state authorities in Republic of North Macedonia and further to the previously disclosed information in the Financial Statements of the Company for the preceding years, the criminal procedure at the basic court is on-going.

We have not become aware of any information as a result of a request from any regulators or other external parties, other than the previously disclosed, from which we have concluded that the financial statements may be misstated, including from the effects of a possible illegal act.

Nikola Ljusev
Chief Executive Officer

Slavko Projkoski
Chief Financial Officer

Proofreading by Lingva Ekspert

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