Event transcript

KPN Q3 2021 Results

Tuesday, 26 October 2021

Operator: Good day, ladies and gentlemen. Welcome to KPN's third quarter 2021 earnings webcast and conference call. Please note that this event is being recorded. At this time, all participants are in listen-only mode. We will be facilitating a question-and-answer session towards the end of today's prepared remarks. If you would like to ask a question, you may do so by pressing *1 on your telephone.

I will now turn the call over to your host for today, Reinout van Ierschot, Head of Investor Relations. You may begin.

Reinout van Ierschot (Head of IR, KPN): Thank you and good afternoon, ladies and gentlemen. Thanks for joining us. Welcome to KPN's third 2021 results webcast. With me today are Joost Farwerck, our CEO, and Chris Figee, our CFO.

As usual, before turning to our presentation, I would like to remind you of the Safe Harbor on page 2 of the slides, which also applies to any statements made during this presentation. In particular, today's presentation may include forward-looking statements including KPN's expectations with respect to its outlook and ambitions, which were also included in the press release published this morning. All such statements are subjects to the Safe Harbor.

Let me now hand over to our CEO, Joost Farwerck.

Joost Farwerck (CEO, KPN): Thank you, Reinout, and good afternoon everyone.

Today's results show another important proof point of our strategic progress. Mass-market service revenues grew again in the third quarter, supporting service revenue growth for the group as a whole and this time growth was visible in all our mass-market segments, most notably in SME segment.

We delivered service revenue growth in SME ahead of our commitment to stabilize before year-end and this is an important milestone for us, as it provides confidence to deliver the turnaround for the entire business segment during our current strategic period.

We have seen strong momentum of mobile inflow in recent quarters and this accelerated further to 67,000 net adds across Consumer and Business this quarter.

Consumer mobile service revenues continued to grow, supported by strong performance of our Unlimited propositions. With solid adjusted EBITDA growth in the third quarter and a strong year-to-date Free Cash Flow, we remain on track and confident that we will deliver on our full-year 2021 outlook.

At the second quarter results we announced a € 200m share buyback, reflecting our confidence in the successful execution of our strategy. We have nearly completed this leg of our share buyback program, which we see as the first step to structurally return additional capital to our shareholders in the coming years.

We continued to make good progress against the strategic and financial ambitions of our strategy ‘Accelerate to grow’. And we remain confident that the strategy will create long-term sustainable value for all our stakeholders.

We rolled out fiber to 93,000 households in the third quarter, a figure slightly lower than other quarters as a result of the August holiday period. This year, we have rolled out to 313,000 homes and over the last twelve months we have added 424,000 homes. We continue to successfully add new fiber customers and upgrade existing copper customers in fiber areas. This will be a key driver for sustainable revenue growth.

The joint venture Glaspoort is now fully up and running and has recently started its wholesale broadband access services for wholesale providers. Together with Glaspoort, we are going to jointly reach 80% of Dutch households by the end of 2026. After reaching that point, Capex will come down to a lower, more sustainable level.

After returning to growth in the second quarter, we have been able to show continued growth in Mobile service revenues this quarter. This was mainly driven by an acceleration of the commercial performance over the last quarter and a higher ARPU level.

Fixed mobile revenues increased 3.5% and total Consumer service revenues grew slightly by € 2m.

Customer satisfaction remains one of our top priorities and the progress in the last two quarters has been encouraging, following a few tougher quarters. It has been pleasing to see our efforts in this area are paying off.

Consumer NPS recovered strongly to +15 and this is a reflection of the success of our attractive KPN and Simyo line-up, the quality of our products and services, the customer journey improvement in several areas, such as customers moving into new homes, complementary fiber upgrades of copper, customers in fiber areas and the new KPN Wi-Fi manager we introduced for our customers.

Now let's take a deeper look into our Consumer KPIs. Broadband net adds were again relatively stable this quarter. Within the mix, we see a positive inflow on our KPN brand. This was supported by solid fiber inflow, which level was seasonally lower at 36,000 fiber households, but fully in line with our expectations.

Our fiber ARPA remains significantly higher compared to copper due to the take-up of higher speeds, more Value Added Services and more SIMs per household. Importantly, for the first time, our fiber service revenue growth was higher than the copper decline. We delivered 27,000 postpaid net adds in the third quarter in the consumer market and together with 1.7% higher postpaid ARPU this led to mobile service revenue growth of 2.4%.

Let's now move to the B2B segment. This year we started to run the Business segment by focussing on three distinct customer segments: SME, LCE and Tailored Solutions. At our strategy update last November, we committed to stabilization of SME service revenues by the end of this year. We have delivered on that commitment well ahead of plan, driven by solid commercial momentum in both broadband and mobile. This was the main driver for the improvement in our Business service revenue trend to a decline of 2.7% year-on-year compared to a level of around minus 5% in previous quarters.

The performance in LCE and Tailored Solutions was in line with our expectations. And, as we highlighted earlier, it will us some more time than in SME to deliver the turnaround there.

Business NPS remained at the positive level of +3, as customers continued to value KPN for the stability, reliability and quality of our network and services.

Let's dive a little bit deeper into the drivers of the SME turnaround. Our strong focus on acquiring new and retaining existing customers by migrating to KPN EEN is paying off with a solid based fence. This in turn, provides a strong platform to increase density of product take-up by our customers, as we leverage up and cross sell opportunities.

Looking at the revenue development of the three product groups within SME we can conclude the following. We see healthy broadband base developments, also supported by fiber and self-employed inflow and this resulted in strong growth of Broadband and Network Service revenues. The Mobile market remains competitive, resulting in continued price pressure. However, the strong inflow of new Mobile customers, among others driven by Unlimited, is now offsetting that effect. This led to stabilization of mobile service revenues in SME in the third quarter, an improving trend compared to -11% in Q1 and -4% in Q2.

And finally, in Fixed Voice the pace of the decline here moderated from around -20% to approximately -10%. This is partly due to the annualization of the phase out of ISDN-2 last year, which reduced the year-on-year headwind.

All in all, good performance in SME, which gives me confidence that we will also deliver a similar turnaround in LCE and Tailored Solutions, the other parts of B2B.

In Wholesale, revenues increased by more than 7% in the third quarter, supported by our successful open access policy. In Mobile, we added 33,000 customers and that is making a total postpaid growth for the Group, including Consumer and B2B, of 100,000 this quarter. Wholesale providers continued to strongly outperform the two incumbents in terms of broadband base growth. In this third quarter, 18,000 broadband lines were added, reflecting the attractive access terms we offer to service providers. Recently, we entered into several long-term agreements with some of the larger broadband service providers in the Dutch market.

ACM is currently conducting its fixed access review and we strongly believe that we are operating a highly competitive market. With our open Wholesale access model, we guarantee sufficient room for wholesale providers to grow and to compete. Customers in the Dutch market get high quality services, can easily switch and choose from a wide range of service providers that offer value for money.

Now over to Chris for our financial performance.

Chris Figee (CFO, KPN): Thank you, Joost. The financial performance of KPN. Well, overall I am pleased with the development of our key financial metrics this quarter. Let me start by summarizing some of these. Our adjusted revenues increased 1% year-on-year, supported by growth in mass-market service revenues. Our adjusted EBITDA after leases increased 1.4%, at a margin of 46.3% for the quarter, despite a tough comparison base in terms of opex. Free Cash Flow was more or less flat versus last year in Q3, year-to-date however, our Free Cash Flow increased 7.1% despite higher Capex and taxes paid.

Our indirect cost savings run rate this quarter was impacted by several factors. First, the comparable base for the third quarter last year was a tough benchmark to beat this quarter, so this quarter year-on-year is not a good proxy for a normalized run-rate. Second, we continue to see some less tailwind from COVID-related savings. Finally, some other elements affected our staff cost performance this quarter, certainly when compared to last year. These include our recent CLA-increase, dotations to employee related provisions, lower Capex charging, and importantly, large restructurings in B2B and TDO. These were effectuated per the first of October, with the full impact visible in Q4, not in Q3.

If we look through these specific effects, we see a continued, structural decline in our cost base, evidenced by the continued decline of FTEs employed at KPN. For example, our own employee numbers are now significantly and structurally lower, even below 9,800, where we started with 10,100 in the beginning of the year. Our total staff, own staff and third-party external staff is now 30% lower than Q1 2020, for example, as testimony to our continuous restructuring and structural cost improvements.

We expect to pick up the pace of our reported cost savings run-rate by Q4 this year, which together with our mass-market service revenue performance will drive EBITDA growth well into 2022.

Finally, please know that our Capex spend is well under control. Fiber spend is up, as we planned to do, and non-fiber Capex is down versus last year, testimony to our enhanced Capex vigilance.

If we dive into revenue growth, we see we delivered mass-market service revenue growth again this quarter, which also add to growth in the Group's overall service revenues. This is an important proof point for the success of our strategy and the first step towards sustainable top-line growth for KPN.

All three mass-market segments contributed to the 2.2% growth in the third quarter. Wholesale grew by 9.4%, mainly driven by broadband and mobile business and some support from seasonality and several smaller incidentals.

SME service revenues inflected the 2.9% growth, driven by the success of our KPN EEN portfolio; and in Consumer, mobile service revenues continued to grow. As Joost said, Fiber broadband service revenues were higher this quarter than decline in copper but again, there was some offsetting effect by declining Legacy services.

Albeit small, it is important to note that our mass-market segment is now no longer depending on Wholesale to show stable to small growth from here on. Also excluding Wholesale there is some growth. Our growth base is widening.

In terms of revenue growth going forward, we expect some technical headwinds in the year-on-year comparison in Q4. We will still grow our mass-market service revenues but due to technical comparisons, at a slightly slower pace than in Q3. Notably, B2B will face a tougher revenue comp due to a spike in Q4 last year, which is mainly related to pass-through revenues in LCE and Tailored

Solutions. And in B2C, more than half of the € 8m revenue correction we booked in the first quarter was actually related to the fourth quarter of last year, providing a more difficult comp for Fixed Service revenues next quarter. We expect both effects to be technical in nature and temporary and fade again in Q1 next year, after which our top-line growth will resume at the current pace. So in summary, our revenue will continue to grow. The base comparisons will prove difficult to read in Q4 and Q1 but underlying there is a solid growth rate in mass-market service revenues.

In terms of cash, we have seen strong cash generation this year, despite higher Capex and taxes. The higher Capex related to the accelerated fiber rollout caused our operational free cash flow to decline, but it was counted by several other line items. More favourable developments in working capital as our continued effort to reduce working capital intensity is paying off. € 38m lower cash interest paid as a result of bond redemptions last year and lower cash restructuring impact. Our Free Cash Flow margin improved to 13.7% of revenues and is on the clear path to improve further, in line with our guidance.

Our balance sheet continues to be resilient. Committed liquidity consisting of over € 700m of cash and short-term investments and a € 1bn undrawn sustainability linked RCF, cover debt maturities well through to 2023. In the quarter, we extended our RCF, but added a sustainability-linked feature to it. This underlines our commitment to sustainable operations and sustainability-oriented financing strategies. Versus Q2, net debt increased by € 92m, mainly driven by the 4.5 cents per share interim dividend in August for a total of € 189m and € 90m worth of share repurchases in August and September as part of the € 200m share buyback program for 2021, which is, as we speak, now nearly completed. And again, these were partly offset by Free Cash Flow generated during the quarter.

Our leverage ratio of 2.3 times is 1 notch higher compared to last quarter, but still comfortably below our ceiling of 2.5 times.

Reassured by our current financial performance and good strategic progress, we confidently reiterate our 2021 outlook and our ambitions for 2023.

So, to summarize, as we noted in our statement this morning, the successful execution of our strategic plan enables us to return additional capital to our shareholders worth € 200m share buyback this year, which has nearly been completed at this point in time.

Execution of our strategy is on track and we remain focused on delivering long-term value to all our stakeholders. Today's results show another important proof point of success and impact of our strategy. After returning to mass-market service revenue growth in Q2, we have delivered growth in SME service revenues this quarter. The number of business segments that have inflected increased gradually. Our margins, both in EBITDA and Free Cash Flow terms, developed favourably, and we feel confident about the cash generating related to Group. And we remain fully on track to deliver our full year 2021 guidance and commitments.

Thank you for listening. Now, let’s turn to your questions.

Q&A

Operator: Ladies and gentlemen, we will start the question-and-answer session now. If you would like to ask a question, you may do so by pressing *1 on your telephone.

The first question is from Mr. Keval Khiroya, Deutsche Bank. Go ahead, please.

Keval Khiroya (Deutsche Bank): Thank you. Two questions, please, the first one being the revenue growth trend is obviously very impressive but Chris, as you highlighted, the Q3 opex reduction was a bit weaker. Can you help quantify the level of improvement we should expect for Q4? On my numbers, I was expecting € 25m to €30m of opex reduction in Q4 based on the full EBITDA guidance. Does that seem reasonable to you?

And secondly, how should we think about Opex reduction for 2022? On the one hand, you have had slower progress in 2021, but on the other hand, it could help the 2022 trend as well. So both those questions on opex, please. Thank you.

Chris Figee (CFO, KPN): Well, Keval, two questions on costs. First, let me outline again on costs. I mean we are seeing structural improvement in costs. As I said, the FTE levels are continuously declining. On our own staff, we are less than 300 since the beginning of the year, external staff also less than 300 and those are structural. Attrition is also good, with 40 to 50 FTEs leaving the company. We are hiring a bit back, but net-net, we are declining our staff level structurally. And again, there are some technical comparisons to Q3 last year, Covid, CLA, employment provisions, opex Capex charging, some investments in commercial success. Those make for a slightly more difficult comparison to last year. So, the number we present for Q3 is a bit unflattering and distorted by the comparison. Finally, as I said, the restructurings that we planned for this year are more back-end loaded and are kicking in in Q4. Long story short, you asked what is the guidance and outlook for Q4? You said you have € 25m to € 30m in your models. That is at a reasonable model. If I had such a model, I would keep that model up and running. It seems like a reasonable estimate to me.

As far as next year is concerned, our program is running. We have our target and commitments. We see FTE levels declining, restructuring kicking in. So we will give you the full year guidance for 2021 when that moment is due. That is going to be done at the full year results, but at this point in time, we stick to our overall commitments and we keep the cost program running.

Keval Khiroya (Deutsche Bank): That is it. Thanks, Chris.

Operator: The next question is from Mr. Joshua Mills, Exane. Go ahead, please.

Joshua Mills (Exane): Hi, guys, thanks very much. A couple of questions from me. The first is on regulations. You mentioned the ACM review, but it would be great just get to a bit more of an overview in detail as to how you see the potential timing, the areas that could be impacted and in what way those might be impacted. Finally, you can talk about extending some wholesale deals with larger customers. My question was, have you changed terms with T-Mobile before or after the recent announcement of the business sale?

The second question was just around inflation. You have talked about how the FTE reductions you are making can deliver longer-term cost savings. Are there any areas within your cost base, which are subject to inflation and how are the payroll contracts set up to reflect that as well? Thank you.

Joost Farwerck (CEO, KPN): Well, Joshua, let me first cover the ACM question you raised. Yes, our regulator is investigating the fixed market. It is a review they do every three years. So that is not a surprise. The latest was in 2018, which was annulled by the highest court in the Netherlands last year. So we currently are not regulated. In the whole discussion around market analysis on fixed broadband, we believe we have a strong position and a solid case. The market with our consumer broadband share of 38% against Ziggo with 42% did not really change compared to last year. We follow an open wholesale policy. We did not change after we were deregulated. And that is dynamic reflecting competitive dynamics in the market, you could say. So we see wholesale providers actually gaining substantial market share, which proves the model is working. Now, our regulator indicated it expects to publish a draft consultation document as it is called, the coming month, at the end of November we expect it. And after that, the process will take at least a couple of months until mid of next year. They also have to ask the market for consultation, make the final document, pass it through the EU, so it will take some time. There is a belief at the ACM side that there may be a risk that KPN’s access conditions will get less attractive for the market and complicate the possibility for competitors to grow. We do not recognize that, and we look forward to share our ideas with ACM, like we did with the providers in the market. And like I said, we were able to close longer-term contracts with those providers. Of course, there is a claim of T-Mobile in the market, but well, let’s hope that the new owners of T-Mobile are more reasonable and that we can sit together and work it out like we do with the other providers. I am looking forward to having a good discussion with ACM and to understand the real worries. But like I said, we believe we have a strong position.

Chris Figee (CFO, KPN): On costs, Joshua, you think about inflation. If you think about the different cost factors, I mean, the staff is one thing. We have an annual CLA increase and our CLA runs into next year. Then we renegotiate a new one. For the moment, I think it is not just about wage increases, other factors are at play. So, let’s see how these negotiations work out. For now, I think continuation of our current wage policy is probably fair to assume. We are structurally declining the amount of labour capacity at KPN.

Let me quickly touch on other components. Energy is a question that is being raised to us sometimes. The input of that is still limited because we actually forward bought most of our energy. So I think the energy headwind next year is probably up to € 5m, not more than that, simply because we have actually pre or bought forward much of our energy. When energy stays elevated, at some point, the higher price will kick in, but not for next year. We see some inflation in technology prices, but it is still limited and to also some extent, compensated by the fact we have also forward-procured quite some of our materials. And on the rest, it means that we have to be smarter in procurement. That means consolidation of procurement, for example, in active and mid- and long tail of our spend to consolidate suppliers. We focus more on catalogue buying, more standard buying to counter all these effects. So in summary, is there some inflation? Yes, there is. So far, it feels manageable and we can counter it by volume assignments and other measures. Costs or energy inflation will no longer be a tailwind, is a bit of a headwind, but nothing that would keep us awake at night from where we are today.

Joshua Mills (Exane): That is very clear, thank you.

Operator: The next question is from Mr. Ulrich Rathe, Jefferies. Go ahead, please.

Ulrich Rathe (Jefferies): Thank you. I have two questions, please. My first one is on the inflection of mass-market service revenue. You are reporting a further expansion of the growth rate, which is good to see. Would you go as far as committing to that remaining in growth really on a quarterly basis over the foreseeable future? Obviously, there is a sort of pandemic help in there, I suppose, at the moment. So the question is, is this something that you can commit to on a quarterly basis and will it remain in growth?

My second question is the broadband RGU picture. Is this still a sort of slight leakage of broadband customers net-net, I suppose, as you lock customers into your own fiber network? But then the copper customers, who are in competitive fiber areas, say they get sucked up by the competitors. So I was wondering, is there a point at which you think the broadband customer base shrinkage can be stopped? I understand a bit about the higher ARPU and the revenue growth that comes with the dynamics, but simply on the volume side, can it be stopped? Thank you.

Joost Farwerck (CEO, KPN): Ulrich, to start with your second question, of course, our strategy is not only focused on fiber, but also on broadband in general. The more fiber we rollout, the better it gets because we strengthen our weakest areas first. Because on the one hand, we have low quality on copper; on the other hand, we have high quality on copper in certain areas. Especially in the larger cities, we can do 200 to 500 megabits per household via a double copper line. So what we now saw is that for the first time, we were able to more than compensate the loss on copper by fiber, and by pushing this further and by focusing even more on our copper steering as well, we think in the quarters to come we will have to grow in broadband, both in business and in the customers by the strategy. So, there is a churn on copper, on one hand, and there is a growth on fiber on the other hand and it is our focus area to run that balance and optimize that balance better along the road. So that is what our strategy is about. Last quarter or a couple of quarters ago, we were still in the decline. The copper loss was much higher than the fiber gain. Now it is more or less breakeven. And on the revenue side, we do better. So yes, step by step, we improved this run-rate, I would say.

On mass-market growth rate, I would say before I hand over to Chris, that it is also was step-by-step run-rate we run here. We identified mass-market as the most important focus point for this year because that is where 90% of our EBITDA comes from, Consumer, Wholesale and SME. Looking at the run-rate, we saw the growth coming in SME, but I am of course, happy that it is really visible now. It is our job there to run the run-rate in a better way in the quarters to come as well. Chris?

Chris Figee (CFO, KPN): To your point on the pandemic impact, the pandemic impact on revenues has actually been limited on the mass-market. We gained something on interconnect revenues. On interconnect mobile calls, people calling 0800 Covid numbers. And then at the same time, due to the pandemic, we lost roaming revenues, without argue. And that is, of course, a much more higher-margin business. I would argue that revenue-wise it has been flat to slightly negative, EBITDA margin probably slightly negative. Perhaps, a bit of a cost benefits due to Covid, but the revenue has not been that much affected by the pandemic. If you look at the coming quarters and If I look at where we are today and the upcoming comparisons, I think we are well set to grow well into next year. So we will show year-on-year growth numbers well into next year, simply looking at the current run-rate of service revenues, the underlying growth rate and then the upcoming comparables. As I said, Q4 will be a bit funny because, for example, this revenue correction that we booked was an unfortunate event in Q4 last year and a correction in Q1 this year. In Q4, we expect mass-market service revenue growth to be by 0.3% to 0.4%, simply because of that comparison and going back to 2% or even a bit higher in Q1, simply because of those technicalities. But the underlying growth is probably around 1.5% to 2% in the coming two quarters, and I can see it growing well to the next year.

Ulrich Rathe (Jefferies): Very helpful. Thank you very much.

Operator: The next question is from Mr. Konrad Zomer, ABN AMRO. Go ahead, please.

Konrad Zomer (ABNAMRO): Hi, good afternoon. My first question is on the healthy immigration to KPN ONE. I think you did a great job on migrating SME. I can imagine that to migrate large customers, it is going to take more time while simply more complex. What gives you confidence that that is running about one year behind the migration of SME? And in particular, what should we expect in terms of revenue loss initially because we did see that with SME. You turned it around very quickly, but I can imagine it can be a little bit bigger in LCE.

My other question is on your statement about shareholder remuneration. We have nearly completed the € 200m. I know from talking to several investors that they were looking for another announcement this quarter. It looks like maybe at the start of 2022, you might announce another buyback. You have used the word ‘structural’ a few times, but can you maybe be a bit more specific combined with your leverage ratio, your cash flow profile, but in particular, what that could impact for the share buybacks going forward? Thank you.

Joost Farwerck (CEO, KPN): Yes, Konrad, I will do the first question. Yes, we migrated all our customers to KPN ONE in the SME segment. That was not done quickly, but took a long time, too long as far as I am concerned, by the way, but we are there now. And by doing that, migrating them to the future-proof portfolio. Enabling ourselves to sell-up again to that customer base now makes it possible and doable to grow in the SME segment. The dynamics in LCE are completely different, although the idea is the same. In LCE, we will migrate the larger customers to a new environment. And once they are there, we are in a much better shape to up-sell and make our business grow. It is not that we have to start on that. We already migrated 80% of our LCE base to that new environment. The difference between how we will follow the last 20% compared to SME is that we found out that the last 20% is the most difficult part, and the first 20% is the most easiest part to migrate when it comes to customers. So on LCE, we are following a more delicate migration scheme to avoid that we really move customers against their wishes to a new kind of platform. So the dynamics are different. We are the largest workspace provider in the Netherlands. There is a lot of workspace for large customers in that base. It is not only migrating customers, but also really moving them up to a better protected, higher quality, safer, faster surface. Maybe it will take some more time, but we are super focused on not losing too much business there when we have to migrate the last 20%, but already 80% has been done on LCE.

Chris Figee (CFO, KPN): And on the share buyback, as you pointed out correctly, the 2021 program is nearly finished. I guess it will happen probably in the coming weeks. That standard 2021 program, as in this year, we effectively returned the Free Cash Flow that we generated to our shareholders. We said this is a structural part of our shareholder remuneration policy. That means we are going to continue this. It does not mean we are going to announce another one every quarter, but we have announced the 2021 version. It is the continuous and a constant part of our reward program, in which we take Free Cash Flow into account, our balance sheet into account with the objective to make this a structural repetitive part of our shareholder reward and we will design it like that. The exact number, I have to keep the spirits up and the tension high, we will let you know when we get there. It will probably be communicated with our full year results when we give the outlook for next year.

Konrad Zomer (ABNAMRO): Okay, thank you very much.

Operator: The next question is from Mr. Polo Tang, UBS. Go ahead, please.

Polo Tang (UBS): Hi, thanks for taking the question, I just have one. It is really just about EBITDA. So your EBITDA growth year-to-date is plus 0.3% and to achieve your guidance for the full year, you need close to 4% EBITDA growth in Q4. Can you just talk about what makes you so confident that you can achieve this step-up in growth? Can you talk us through some of the key moving parts? And what does this mean for the trajectory of EBITDA growth into 2022? Thanks.

Chris Figee (CFO, KPN): Yes. Polo, it is Chris here. For Q4, it is easy to talk about the earnings that you need rather than the growth, and we have given a guidance for the year. If you go back, you can almost like backwards sold, the amount of EBITDA you need to get there, which will then be a growth over last year. And again, last year, if you remember, Q4, we had relatively low EBITDA. So the growth will look good. It is about the absolute level of EBITDA. And I then look what we need or we guide for Q4 and compare that to Q3, for example, the Q3 EBITDA level, September of Q3 is always high, the classical release of the holiday provision and some other elements. If you strip those out, we need to continue to run at the current underlying earnings rate to do a bit better, and then we will hit the number that we are required to meet to meet our full year guidance. And the growth is a function of that. So to me, it is more about confident on the euros we will make in the quarter, and that actually is a continuation of the current structural earnings rate of the Group, where we have some slight improvement. That we think is actually feasible. And then the growth number comes out of that, but it is the euro number that should drive the guidance, and we have got all comfort in that.

Polo Tang (UBS): Okay, thanks.

Operator: The next question is from Mr. Andrew Lee, Goldman Sachs. Go ahead, please.

Andrew Lee (Goldman Sachs): Yes. Good afternoon, everyone. I have two questions. The first was another question just around the pandemic impact on your top-line growth. Obviously, you have had a successful period up-selling, which is driving your strong growth in the quarter. Just how confident are you that this is not just a temporary phenomenon caused by a pull-forward of demand for higher speeds, given the work-from-home, etc. as set up across Europe in the Netherlands for you guys, we are just seeing like an acceleration of people’s willingness to pay more for more right now that does not necessarily continue? So that is question number one.

My second question was just on B2B. Given your success in inflecting the revenue growth of SME, where does that put you or does that pull forward your inflection on B2B altogether and timeline on that? Thank you.

Joost Farwerck (CEO, KPN): Well, when it comes to the COVID effect on our top line, we are not benefiting that much from Covid. We think there is a lot more upgrade to do in the Netherlands than we currently see. This is the Netherlands. So, when we started on fiber, people started to buy 50 megabits. Currently, 100 megabits is more the average. So, we do not think that during the pandemic people asked for an upgrade, and later in the time, they will ask for a downgrade again. Once you are up on 100 megabits or 200 megabits and you found out the difference, people will not move back. By the way, we also priced the higher speeds on fiber more attractively last quarter, because we really try to motivate our customers to do an upgrade. But we did not see a real relation between the pandemic, Covid kicking in and upgrades being asked. It is a more delicate line that we see there. So, we think, now we rollout fiber and we move to XGS PON, which is enabling us to upgrade to 10 gigabits per household, we think there is far more potential in upgrading our customers in the years to come.

On B2B, we announced that we were going to stabilize our SME business in the second half of this year. So, we are a bit ahead of track with a slight growth in that segment, so that is good. And of course, now the jury is out, first of all, keep the growth in SME and secondly, how to inflect the other parts of that B2B business? We aim for that, and we are ready for an update on that when we release our annual figures next year. For us, that of course is a super important milestone because then we have a full top line growing again, but we are convinced we are going to do it. But we do not want to over promise now. It is the first quarter we see the SME market growing. So first, keep that under control and then soon, we will come back to you on how to inflect the other part of B2B.

Andrew Lee (Goldman Sachs): Thank you.

Operator: The next question is from Mr. Luigi Minerva, HSBC. Go ahead please.

Luigi Minerva (HSBC): Good afternoon. Thanks for taking my two questions. So, the first one is on Capex. I was wondering how do you see the Capex profile evolving in the medium-term? I think Joost, you signalled Capex normalization starting from 2022 but then when the 5G network densification kicks off, what sort of impact will it have? Do you think that the capital intensity eventually will start growing again if you think about the next five years? And related to that, but moving to the shareholders' remuneration, how do you make the share buyback a structural component? Obviously, you create a very strong signalling system. And I was wondering whether Capex at some point becomes subordinate to the shareholder remuneration? So, in other words, whether the Capex number becomes even more discretionary for the sake of keeping a gradually increasing shareholder remuneration? Thank you.

Joost Farwerck (CEO, KPN): Luigi, last year, when we announced our strategic plan, we were fully aware of the fact that we were increasing our Capex to a level of between 1.1 and 1.2, related to the rollout of more fiber in the Netherlands. With that Capex envelope, we think we stretched the level of investments in the Netherlands. It is a huge amount of Capex for a country like the Netherlands. After 2026, when we are done, because then we rolled out 80%, we expect other initiatives to cover the other 20% in the Netherlands. So, the whole Netherlands is connected to fiber then. It makes sense to put in the program that we will step down significantly on Capex. Now in our industry, there is always a promise of a short-term step up in Capex and a longer-term step down, and we are aware of that as well. So it is, for us, super important that we stick to the program and we keep our promise.

5G is something we really are very prudent on. There is an auction coming up next year. We already rolled out the network. The network is 5G ready on 5,000 sites, which covers the Netherlands. But we are not trigger happy to start rolling out to a more dense network, thousands of sites in the Netherlands because we really are working there business case based. So, we have some field trials out there and we are scanning all over the world, what is happening on 5G. It is super fantastic what one can do on 5G on certain locations, but it really should pay back before we do the investments. We have seen in other countries so many investments in such doubtful business cases that we really are prudent there. I do not think we will start to work on a network that is covering the 5G 3.5 gigahertz spectrum kind of speeds through the Netherlands. It really is going to be business case by business case.

Chris Figee (CFO, KPN): Luigi, to add to that, if you think about the Capex ratio, our fiber, we are spending between 8% and 10% of our revenues on fiber. It depends a bit on what quarter you look at. Non-fiber is between 12% to 14%. It fluctuates a bit per quarter, but you get 22%, 23% of revenues on Capex. We are fully aware that is a significant spend. And as Joost said, as soon as the fiber program is done, the diction of the fiber program will obviously fade away and you get to an underlying fiber Capex profile, which is probably more in line with where the European telcos are, much more in line with our non-fiber spend. And that is the way we look at it. If you think is it subordinate to shareholder returns, look, the way we think about it is this, you look at your Capex that you can structure into different buckets. There is the bucket that has to do with maintenance, life cycle management, dealing with increased traffic, security. That is your license to operate that you will always have to invest to make sure we keep our business running. There is Capex that relates to customer Capex. In general, that good Capex provided, of course, you sell profitable products, but assuming that these are business profitable, consumer Capex tends to be good Capex. And then there is Capex, which is more growth oriented, which I would qualify fiber at some point growth-oriented Capex. It is really clear that, that needs to make an attractive return. And then of course look at the ROI, the IRR of the Capex you invest there. And of course, you always keep in mind how does the IRR of that Capex stack up to, for example, buying back your own shares. We could swing Capex of € 100m every year and buy back shares back and forth, but it is a good disciplining factor to make sure that the return that you make on the Capex stacks up to the alternative of buying back your own shares. And that to me is a very disciplining factor in determining how much you spend in growth and innovation and new products, new initiatives.

When it comes to our shareholder remuneration policy, I think ultimately, I think you and me want our shareholder returns to be found at continuously growing Free Cash Flows. And we designed a program that our cash flows can grow in the coming years. You will see it according to our guidance, and you can top up that with whatever room you got on your balance sheet. In the long term it is important that your cash flow will grow. Capex is an important element to it. And as Joost alluded at some point, the fiber part will become less and then your Capex will come down and Free Cash Flow will step up. That will obviously have positive repercussions for shareholder returns.

Luigi Minerva (HSBC): That is great. Thank you.

Operator: The next question is from Mr. Usman Ghazi, Berenberg. Go ahead please.

Usman Ghazi (Berenberg): Hello. Thank you. I have a few questions, please. The first one is on the extension of wholesale agreement that you have announced this quarter. Could you perhaps illustrate whether these were tough negotiations and what were some of the puts and takes that you had to concede to or to get these agreements done? And over what period are these agreements? Are they similar to the previous agreements you used to do with about seven years ago or are these shorter? Some colour there would be helpful.

And then just on the topic of fiber as well, [sound distorted].

Joost Farwerck (CEO, KPN): I am afraid we are losing you a bit when it comes to the quality of the line. It can't be KPN so probably something on your side.

Usman Ghazi (Berenberg): Okay. Sorry. Is it better now?

Joost Farwerck (CEO, KPN): Yes, it sounds better. Sorry. Would you please repeat your second question?

Usman Ghazi (Berenberg): The second question was just on the copper shutdown that you did in six areas in the Netherlands this quarter. I believe it was 40,000 connections. During that process, it would be great to know what your experience was, whether there was a situation where there had to be any forced migrations of remaining customers, or whether it was just the demand for fiber led to a natural kind of migration in that process? Thanks.

Joost Farwerck (CEO, KPN): Yes. Usman, thanks for your question. Good to hear you speak a bit Dutch as well nowadays. When we come to wholesale agreements, we have these long-term relationships with several service providers out there in the Dutch markets, not only T-Mobile, but a lot more. And the reason why we have a good relationship is that we try to optimize the business model on both sides. So, we make it doable for the smaller service providers to plug in on one or two locations in The Netherlands and via that, we can serve them on broadband through the whole country, which makes it far more efficient on their side and for us a bit better as well because it is on the active layer of the network and therefore, we are generating a bit more margin. So, it is a win-win situation. And that is why it is not only a storyline we tell to convince our regulator that everything is working in the Dutch market, but that open network model, that open access network model is really working quite well for both our customers and ourselves. Yes, the copper switch-off and the migration to fiber in those areas is of course very important for us. We have been talking on that topic for years now. Also there, we use ACM's guidance to announce switch-off in certain areas three years in advance, if I am not mistaken. But also these areas are not new, they are all our areas, so already five years to eight years old in some cases. So, it is known that we of course, have to, at the end, switch off the legacy network. It used to be tougher, but we have changed our fiber model a bit. So, when we rollout fiber, we are more focusing on migrating our customer base to fiber in the early stage, sell up and migrate, complementary fiber upgrades early in the process than we did in the past to make that migration possible. Also the other providers, the wholesale providers, most of them are following that because it is also of course, important to sell fiber in five areas. So, we did the switch off, I think you are right, 40,000 lines something like that, and that was more a pilot in a couple of areas. We are very satisfied that we really switched off the whole MDF and the number exchange in those areas. In 2023, the real program kicks off and then we are really going to disconnect several areas with a large base of copper. That is important because of the costs related to the copper network. The service tickets on copper are much higher than on fiber. It is more expensive to maintain the copper network in general in the Netherlands than fiber. So, when it comes to efficiency, it is important to do the copper switch off and we really will start the real program in 2023.

Chris Figee (CFO, KPN): And o your point on, what are forced migrations, I mean not really. We learned from this copper pilot that it is very important to start early on, communicate early and frequently to customers. If you communicate early on that it is going to happen, are very clear and we repeat that, that customer eventually will move from copper to fiber. And as you know, we have an offer where for the same speed from copper to fiber, you do not pay extra for the same speed. So, for a client, for customers actually, if he or she wants to stay at that current speed level, there is actually no additional cost. You have to make sure that there are always customers who do not respond, then you have to chase and make sure you connect with them. It is not the unwillingness of the customer; sometimes customers do not pick up the phone, do not read their e-mails, do not read their letters. So, it is more that pointing them to it and then having the last bunch of customers that you actually have to personally connect, go door-to-door rather than the forced migration. It is about making sure you connect with customers on time, and it is all about preparation. We see the way prepared well early on those transitions actually go pretty smooth. And that is where you are late or later, you have got much more work to do to migrate those customers.

Usman Ghazi (Berenberg): Great. Thank you. Just one follow-up, just on the length of the wholesale agreements that you have recently signed. Are these 7-years length deals, similar to what you used to have or are these shorter in length?

Chris Figee (CFO, KPN): No, they are multiyear contracts. They vary by customer, but they tend to be multiyear contracts.

Usman Ghazi (Berenberg): Great. Thank you.

Operator: The next question is from Mr. Jakob Bluestone, Credit Suisse. Go ahead please.

Jakob Bluestone (Crédit Suisse): Hi. Thanks for taking the questions, they are fairly quick. Firstly, just on the business segment, you mentioned the challenge of migrating the last 20%, they are the hardest ones. Just to be clear, do you think you can actually see some of the non-SME revenue segments worsen as you try to migrate those? If I look, for example, your Tailored Solutions revenues that went from -4 to -5 and the LCE looks like it is fairly unchanged at -6% year-on-year. So, I am interested whether you think it could actually get worse before it gets better, just so we understand the glide path.

Secondly, I see there was some press coverage that Vodafone Netherlands has had three service disruptions in October, and it is a little bit difficult for us to gage from outside the Netherlands how significant that is. I am interested in hearing, is that significant from your point of view? Is that something you should materially benefit from? Thank you.

Joost Farwerck (CEO, KPN): So, on B2B, what I mentioned when I said the last 20% is difficult that there are always customers that just do not want us to touch anything. Sometimes they are right, by the way. So, that is always the toughest part of the whole migration program. It doesn’t mean that we are going to push our business additionally down. I do not see the trend worsening related to the migration in B2B. We are not super happy with the current developments. It is our aim to inflect to positive growth. So, the whole migration will be built around improving the run-rate at the end and keep it where it is in the short-term. So, I do not see the trend worsening.

On Vodafone and the outages in the Dutch market, there is an old habit of not making jokes about competitional failures because before you know, it bites you in your neck. But the only thing I can say that it is super important to invest in quality of your network and that is what we are doing. So, we are focused on our end. We decided to upgrade our core mobile network to migrate it to Ericsson or investing in our core and access networks intensively. And we are focused on that, but we never think that we can benefit from bad news on competition. That is a negative business model and not good for the business in general, I would say.

Jakob Bluestone (Crédit Suisse): Very clear. Thank you.

Reinout van Ierschot (Head of IR, KPN): Okay. Thank you very much. Thank you Joost, Chris. That concludes the Q3 call. If there are any further questions, please contact the Investor Relations team. Operator, over to you.

Operator: Thank you. Ladies and gentlemen, this concludes today's presentation. Thank you for participating. You may now disconnect your lines.

[End of call]