

17 February 2014

The Manager

Company Announcements Office
Australian Securities Exchange
4th Floor, 20 Bridge Street
SYDNEY NSW 2000

Office of the Company Secretary

Level 41
242 Exhibition Street
MELBOURNE VIC 3000
AUSTRALIA

General Enquiries 08 8308 1721
Facsimile 03 9632 3215

ELECTRONIC LODGEMENT

Dear Sir or Madam

Transcript from Analyst Briefing – Half-Year Financial Results for the year ended 31 December 2013

I attach a copy of the transcript from the analyst briefing held on Thursday 13 February 2014 – Half-Year Financial Results for the year ended 31 December 2013, for release to the market.

Yours faithfully



Damien Coleman
Company Secretary

Telstra Half-Year Results Presentation, 13 February 2014 - Transcript

MR A. KEYS: Good morning. I'm Andrew Keys. Head of Investor Relations at Telstra. On behalf of the company welcome to today's investor and analyst briefing for our half year financial results. After presentations from CEO David Thodey and CFO Andy Penn, we will be taking questions from investors and analysts. I will now hand over to David Thodey. Good morning, David.

MR D. THODEY: Thanks, Andrew. Yes. Good morning. Great to have you here and it's good to go through the first half results for 2014. What we thought we would do is pretty much follow the same format we always do. I am going to give you a quick update on some of the highlights and then Andy is going to come up and take you through more detail. Just an analysis of the numbers and a bit of a perspective. And then I will come up at the end and just try to take you through, I guess, our strategic priorities just the relevant bits in terms of the results and then we will take your questions.

So, firstly, to the highlights of the first half. Well, I think the results really do reflect the continuing focus we've had around those strategic priorities of improving customer efficacy, you know, really driving, you know, value from the wonderful domestic core business that we have but also, you know, spending time around growing our new business opportunities. Very important to note that our customers really do remain our number one priority and we are committed to improving the way we serve our customers and providing them with the access to the best networks in Australia. And the real measure of that is whether more Australians choose to come to Telstra and I am pleased to say that they are.

During the half we added 739,000 new domestic retail mobile customers. 75,000 new retail fixed broadband customers. 117,000 new customers on a fixed bundle and 2189 new IP services which are mainly in the business and enterprise markets. Now, over the last six months, the business has continued to grow. On a reported basis, revenue or income is up 4.1 per cent to \$12.8 billion. EBITDA grew by seven per cent to \$5.3 billion and net profit after tax increased by 9.7 per cent to \$1.7 billion.

I am also pleased to announce that the Board has increased Telstra's interim dividend to 14 and a half cents per share. Very importantly, as well, is that we are confirming that we're on track to meet our full year guidance.

But let me just look for a moment at the product revenues. Revenue in our mobile's business was up 6.4 per cent. A strong result. Revenue in fixed data was also up 6 per cent. And revenue in our network applications and services business was up 29.3 per cent which was a very strong result. And the international business was up 28.3 per cent. I think you would agree with me they are a strong set of results.

We're also very committed to maintaining our technology and product leadership. This is really at the heart of so much of what we do. During the half we invested \$1.8 billion to maintain that leadership and we really do believe that that investment is delivering real tangible results in terms of both top line and bottom line. For example, by Christmas, around the 4G network, we committed to covering, you know, 85 per cent of all Australians and we're pleased to say that we delivered on that.

Over the past six months, we've upgraded 1500 base stations to have 4G capability and we now have 3500 4G mobile base stations switched on and working around Australia. I want to stress, that 4G network is four times – four times larger - than any other comparable network in Australia. Besides investing in core network, we've also been investing in new business initiatives and, of course, this is so important for us in driving out the portfolio and also driving innovation. These investments included, you know, companies like North Shore Communications and O2 Networks that are really bolt-ons to improve our capabilities in the NAS business. We also continue our interests in the health industry and we acquired 50 per cent of Fred IT, which I will talk about a little bit about later on.

Now, to fund this growth, operating expenses are up 2.1 per cent on the half. These are largely driven by the costs supporting this revenue growth. Especially the very large contracts like Department of Defence and Department of Health Services as well as driving out new initiatives in customer service. Revenue growth has translated, pleasingly, into growth at the bottom line. This half, earnings per share grew by 8.7 per cent. These are a solid set of results and I think it sets us up well for the future. Let me now hand over to Andy, who is going to take you through more of the details. So, Andy, over to you.

MR A. PENN: Thank you very much, David, and good morning everybody. In my presentation this morning I will firstly take you through the overall results and comment on how we tracked against guidance. Secondly, I will take you through our product and business line performance. Thirdly, I will comment on our expenses and productivity program. Fourthly, I will provide you with an update in relation to our key balance sheet movements and capital position. And, finally, I will conclude with some comments on guidance for the balance of 2014.

Before I take you through the results and following the execution of agreements for the sale of both Sensis and CSL, I would like to clarify how we are required to account for these transactions in these results. We are required to record both businesses as held for sale. In the case for Sensis, we expect to book a loss on the sale of approximately \$150 million subject to the timing of completion and \$100 million of that has been booked at the half year. In the case of CSL, we expect to book a profit on the sale of approximately \$600 million and this will be accounted for in the second half of the year when we anticipate the transaction will consummate.

In the case for Sensis, we are also required to treat this business as a discontinued operation. The effect of this, it has been deconsolidated from the current period and the prior comparative period. And then the net profit after tax and depreciation and amortisation of Sensis is recorded as a discontinued operation in the accounts of Telstra after net profit after tax for Telstra. CSL is not treated as a discontinued operation because unlike Sensis, where we are exiting the print advertising business completely, mobiles continues to obviously be a very core business for Telstra.

With those clarifying points made, I will now move to the results. Sales revenue for the half year was up 3.6 per cent to \$12.6 billion. Total income was up 4.1 per cent to \$12.8 billion and EBITDA was up 7 per cent to \$5.3 billion. On a guidance basis, excluding the impacts of M&A, total income and EBITDA were up 3.3 per cent and 6.6 per cent respectively. There was a small decrease in depreciation and amortisation of 2.7 per cent reflecting some minor changes to asset lives. EBIT was up 14 per cent to \$3.3 billion. After accounting for the loss from the Sensis discontinued operations, including the impairment, net profit after tax was up 9.7 per cent to \$1.7 billion.

Commenting further on some of our key financial measures, accrued capex decreased slightly down 2.1 per cent and the capex for sales ratio for the half was 14.4 per cent. Free cashflow declined 23.4 per cent to 1.7 billion. However, the first half of 2013 included the proceeds from the sale of Telstra clear. Excluding these, free cashflow was up 11.2 per cent. Earning per share increased 8.7 per cent to 13.7 cents per share and, as David mentioned, the board has declared a fully-franked interim dividend of 14.5 cents per share. Return on equity was broadly flat as the increase in profit was matched by equity gains from the superannuation fund which strongly returned to surplus. Return on invested capital was up 1.7 percentage points to 15.2 per cent, reflecting strong returns from our investments in the mobiles business in particular.

Turning to the group sales. In the first half of 2014 we saw continued growth in sales revenue. Sales revenue was up 3.6 per cent to \$12.6 billion. We saw small declines in fixed media, data and IP which I will cover in a moment however these were more than offset by strong growth in mobiles, NAS and international, up 6.4 per cent, 29.3 per cent and 28.3 per cent respectively.

I will now walk through our product and business line performance, firstly fixed. Fixed revenues were down 1.5 per cent, an improved performance on previous periods. This was due to slower declines in PSTN, growth in fixed broadband and revenue from the NBN Infrastructure Services Agreement. Fixed voice was down 7.3 per cent with a number of retail lines down 155,000 to 6.4 million. Fixed data revenue was up 6 per cent and retail fixed data revenue was up 7.8 per cent. A further 75,000 new retail fixed data customers were added in the period while ARPU increased 1 per cent to just under \$55. We continue to see strong performance in bundles, up 117,000 due in part to the success of our entertainer bundle. EBITDA margins trended in line with expectations with fixed voice declining one percentage point as the portfolio declined in size and fixed broadband, excluding the early NBN connections, increased one percentage point as we continue to expand the scale of this business.

The mobiles business continued to perform very strongly. Overall, revenues were up 6.4 per cent and mobile services revenues were up 7.3 per cent. This follows strong growth that we have experienced in SIOs over recent periods. In fact, our total number of services has increased 50 per cent in the last

three and a half years. During the period, we added 739,000 retail Australian mobile customer services to take our total number of services to 15.8 million. This included particularly strong growth in pre-paid while net adds in post-paid was lower than in the first half of 2013 reflecting a slowdown in the market overall. We estimate that we still took market share in post-paid.

Revenues were up 5 per cent in post-paid handheld and 19.4 per cent in pre-paid. The pre-paid performance was driven by an 11.7 per cent increase in unique users and a 6.2 per cent increase in ARPU. In post-paid handheld, ARPU, excluding the MRO impacts, this was up 2.1 per cent to just over \$66. With more than 4 million customer services now on the 4G network, we are seeing increased demand for data. This is driving ARPU and assisting with further improvements in the EBITDA margin which for mobiles expanded by two percentage points to 39 per cent. We have invested a further \$650 million in the half and, having achieved 85 per cent coverage of Australia with LTE, we remain committed to continue to invest in Australia's best mobile network.

In the second half of the year, we will be further deepening our LTE coverage, investing in additional capacity and a number of other innovative trials and preparations for the digital dividends spectrum which will become available in 2015. Overall, another very strong performance from our mobiles business.

In data and IP, IP access revenue did not fully offset the declines in ISDN calling and data products. We have seen strong customer growth with IP MAN SIOs growing 14 per cent, increases in volume, span width upgrades and IP access revenues up 3.9 per cent to \$581 million. This has been offset by intensified competition on large contract renewals and ISDN revenues declining 8.8 per cent, really driven by calling substitution and the movements from legacy to new IP-based products.

In NAS, we saw another very strong period of growth with revenues up 29.3 per cent to \$821 million. Revenue growth has accelerated due to the number of large contracts that we have signed in recent times including with the Department of Defence. Performance was also assisted by the acquisition of O2 and North Shore Communications. The latter added \$17 million to revenue in the first half. As with previous periods, we saw strong revenue growth across all major product categories with Cloud up 28.6 per cent, unified communications up 27.6 per cent and management network services up 64.8 per cent. To support this very strong growth in NAS, we have increased our operating costs and increased our head count by more than 700 for the on-boarding of the major new contracts that we have signed and also to scale it for further growth in the future. Notwithstanding these drivers of cost, we have more work to do to improve the efficiency of our NAS business and further improve margins.

Looking at the results from a channel perspective, Telstra retail income for the first half was up 3.9 per cent. This includes consumer and business. Consumer was up 5 per cent underpinned by growth in mobile services revenue and ARPU as well as fixed data revenue, which was up 7.8 per cent. Business was up 0.9 per cent underpinned by fixed data, up 6.9 per cent, and offset by lower fixed voice and mobile services revenue. In November, we announced the creation of our Global Enterprise and Services business unit led by Brendon Riley consolidating Enterprise and Government, the Telstra Global submarine cable business and NAS. Global Enterprise Services was up 3.2 per cent underpinned by the strong growth in NAS and partly offset by weaker mobile services revenue. Wholesale revenue was up 9.8 per cent, driven mainly by the NBN Infrastructure Services Agreement revenues and a growing pre-paid 3G wholesale mobile business.

Turning now to media and firstly Sensis. I will make a couple of comments on the operational performance of Sensis in the first half and then speak later about the transaction. Overall, sales revenue for the half was down 13 per cent with print revenues declining 31.7 per cent and digital revenues up 7.5 per cent. Part of the decline in print revenues was due to the Adelaide books where the revenue recognition will move to the second half of the year due to the timing of book deliveries. The Sensis EBITDA margin for the half year held up well at 20 per cent, although the seasonality of this business is that most of the earnings are recorded in the second half.

Foxtel's revenue was up 0.6 per cent for the half year and EBITDA was up 6.1 per cent. The EBITDA performance was partly driven by the continued flow through of the cost synergies from the acquisition of Austar. EBIT was up 23.5 per cent to \$273 million. Whilst revenue was only up 0.6 per cent, customer numbers were up 5.2 per cent underpinned by strong sales of Foxtel on T-Box and reduced churn which was down 1.8 percentage points to 12.4 per cent. In Telstra's books, the interim

Telstra Half-Year Results Presentation, 13 February 2014 - Transcript

dividend received from Foxtel was down slightly to \$50 million and cable revenues down 1.6 per cent. There is considerable product development at Foxtel to stimulate further customer growth. Foxtel Play and Foxtel Go have already been launched with Presto the new SVOD platform due to be launched soon. The team are also working on plans for the launch of a new set-top box iQ3 and a triple play offering.

In our other media businesses, revenue was up 2.7 per cent to \$379 million. Pay TV was up 4.5 per cent to \$348 million with very strong contribution from pay light, up 64.5 per cent to \$51 million. The success of the entertainer bundle has driven significant growth in Paylite revenue. In the first half, we sold 124,000 T-boxes. In addition, we saw a 12 per cent increase in movie downloads with more than 300,000 users now streaming on average over three movies per month. Digital content services revenue declined notwithstanding growth in subscription revenue from NRL, AFL and MOG but these were offset by the continued decline in feature phone services.

Turning, finally, to our international portfolio. Overall, revenues were up 28.3 per cent or 15.5 per cent on a local currency basis. CSL revenues were up 27.5 per cent or 13.2 per cent in local currency as we added a further 227,000 customers. Revenue from our China digital media businesses was up 53.8 per cent in local currency with a very strong performance from Autohome.

Finally, global connectivity and NAS were up 9.7 per cent to \$323 million as we added over 50 new customers. In conjunction with our strategy to further expand global enterprise services into Asia, we also launched new cloud platforms in Hong Kong, London and Singapore.

Before making a couple of comments on productivity, I will take you through the key elements of the income from our NBN. Global NBN revenue in the period was \$294 million. This included \$136 million from the Commonwealth government agreement and other government policy agreements, \$139 million from the Infrastructure Services Agreement, and \$19 million in PSAA payments. We continued to amortise the revenue previously received for the Retraining Deed and the Information Campaign and Migration Deed. In relation to the latter, the amortisation will conclude in the second half of the year. TUSMA net revenue increased in line with expectations. Income received under the Infrastructure Services Agreement relates to the transit network which we expect to complete the build of in the second half of the calendar year, and access payments which will continue to increase over time in conjunction with the rollout of NBN.

Let me now turn to our expenses. Total costs grew 2.1 per cent to \$7.51 billion. Excluding TelstraClear and the impact of foreign exchange, expenses increased 4 per cent. In the period, our additional investments in DVCs and business growth were \$230 million and \$210 million respectively. FX impacts added a further \$110 million to our costs.

As mentioned earlier, one of the key drivers of costs in the first half have been those to support NAS, although we clearly have more work to do to improve the efficiency of NAS and further improve margins. Against these increases, our productivity and simplification plan delivered \$230 million in net benefits to our expense position for the half year.

Turning now to capital management: I refer to the strategic framework for capital management which we presented to the market for the first time two years ago, and this remains the key benchmark against which we make all capital decisions. The framework has the joint objectives of maximising returns to shareholders, maintaining our financial strength, and retaining financial flexibility for investing in the future.

In this regard, we continue to manage the balance sheet consistent with a single A credit rating, whilst we have just announced the board has declared a 0.5 cent increase to the interim dividend to 14.5 cents per share on a fully franked basis. As mentioned previously, our capex to sales ratio in the first half was 14.4 per cent as we applied the additional investments to rolling out the LTE network. And we ended the half year with cumulative excess free cash flow of \$1.8 billion. In relation to some of the more detailed capital movements, our total accrued capex decreased by 2.1 per cent to 1.8 billion, and this included the \$650 million investment in the mobile network that I mentioned before. Our net debt position increased slightly to 13.9 billion following the successful half a billion dollar Aussie issue in October.

We have also reduced our average borrowing costs from 6.4 to 6.1 per cent. During the half we were particularly active in portfolio management. We announced investments totalling \$226 million. These included increasing our investment in Ooyala, the acquisitions of NSC and O2 Networks to further enhance our NAS capabilities, DCA and Fred IT in the eHealth space, and in Box, a US cloud-based file storage provider which we invested via Telstra Ventures. We also slightly increased our investment in Autohome, before very successfully listing this business in December on the New York Stock Exchange. Finally, subsequent to the year end, we announced the signing of an important memorandum of understanding to develop a joint NAS business with Telkom Indonesia. We also made two significant announcements in relation to the sale of our 76.4 per cent interest in CSL and 70 per cent of our interest in Sensis. I have already mentioned to you how these have been treated in the results from an accounting point of view.

The conditions precedent that need to be satisfied in relation to both transactions are progressing as expected. To CSL, this is subject to regulatory and purchasing shareholder approval. OFCA, the relevant regulator in Hong Kong, has been through a public enquiry process, and is now in the process of reviewing submissions pending a decision which we expect on this matter will be before the end of March. On Sensis, the financing and further approval conditions precedent are progressing as expected, and we expect this transaction also to complete by the end of the first calendar quarter.

Before handing back to David, let me make a couple of comments on guidance for the rest of the year. Our guidance for 2014 remains low single digit growth for both total income and EBITDA and a capex to sales ratio of around 15 per cent. We expect free cash flow to be in the range of \$4.6 to \$5.1 billion, excluding the impact of M&A activities that we have announced. Thank you, and I will now hand back to David.

MR THODEY: Thanks, Andy. I think it's good to get a good feel for, you know, the details behind some of the numbers, and we can take questions after I take you through just a little bit of an update on our strategy and how it really relates to the results. As you know, we have got three core strategies that, sort of, really guide our every decision. Firstly, around customers: improving customer advocacy, and that is a very simple but very complex set of things to do; driving value from our core business; and building new growth businesses. So let me give a quick update on each of those, and I will just give you a quick update on NBN as well; just a very quick update.

So, firstly, to improving customer advocacy, as I continually say, it is our number one priority, because it drives value for the company and shareholders.

And we really are focused on creating sustainable differentiation through customer service. And we focus on four areas: NPS, you know, product differentiation, process improvement, and then how do we create unique service experiences. So let me go through each one of those. I mean, in terms of this NPS system, it's very important to understand that it isn't just one metric. It's – we measure NPS on every customer interaction, every episode – that is when, you know, people do something with Telstra – every product, every process, and it really instils everything in the company. We also measure it at what we call a strategic level is, sort of, this perception level of what customers say when you ask them, "Would you recommend Telstra to a family associate or a friend?" And that is a very telling and very hard metric when you're only going to count them as an advocate when they score you a nine or a 10.

And every person who works at Telstra has a target. Every person from me all the way down to a field technician – I should say across to a field technician or to a – you know, someone at the front of house. And so this is the way we run our business. So I'm not going to say much more about it. I just want you to understand that it's core to who we are.

In terms of products, we continue to invest in a wide range of new products and drive differentiation. Just a few highlights: we have introduced the Telstra StayConnected product, which allows you to swap out your mobile device or replace it should you lose it. It also restores all the data on the device and it helps people to get back online very quickly. That has been a very successful launch. We have had about 175,000 customers take up the service, and the attachment rate is about a third, so it has been very good.

We also introduced a new Telstra Platinum service. It's a premium service. It offers customers end-to-end technical support, both for connectivity but also for devices and applications, and the early signs in that area is very positive. We also continue to enhance a number of our products, you know, trying to address excess data usage, international roaming charges, and we believe that we are really offering some great products in that area.

Thirdly, customers do want simplicity. Therefore, driving process improvement is very, very important. And we do this in association with NPS, but every process in Telstra has an owner. We measure it and we try to understand how we can, you know, take costs out while actually creating a better customer experience. So if you're talking an area like the online space, we have now increased the number of online service transactions to 44 per cent of the total, and that's across all segments, and that's basically digital interaction. We now have a third of our customers who have chosen a paperless bill, and we also now have paperless contracts in the shops. We also provide 24 by 7 support, so customer contact is 24 hours a day, seven days a week. You can either use the app on your mobile phone, or you can call us, you can use live chat, get onto Facebook, get onto Twitter. These are innovative good ways in which we can interact with our customers, but you have got to change your processes to do that.

Also, we are trying to build unique customer service experiences; things that, what we say, money can't buy. Since launching our 'Thanks' loyalty program in March 2013, we have had over a million people who have enjoyed unique service experiences. Things, like, you can enjoy Brad Pitt or you can go to Michael Bubl  or Jessica Mauboy. These are things that normally we – you know, a Telco wouldn't offer but we do now. So it has been, you know, quite impressive. Also, we offer movies, sports and tickets. Movies. Sports. Music. Tickets. And also we're going to continue to provide some really great experiences.

So when it is all said and done, what you've really got to do, you've got to both lead in product network innovation and we've always been known for that but we've also got to be known for great customer service and experience and, of course, if you get both right it really creates value for our shareholders and for our customers.

The other areas around driving value from a core business – and we often talk about our key domestic products and services because they do make up the bulk of our business. And in this area we really try top focus on three areas. One is customer and revenue growth because that's what drives good core businesses. Network leadership and then this whole costs simplification focus that we've had for the last four years.

Let me briefly touch on each of those. So I think Andy has really taken you through some of the great results we've had across mobiles and fixed data. But let me just quickly remind you of those. So even though we think the market probably went backwards in the September quarter, we've seen one of the fastest take ups of 4G mobile of any operator in the world at 4.1 million 4G mobile devices on the network. We've also seen good growth in mobile services, which we have already taken you through, at 739,000. We've seen, you know, good handset ARPU growth at 2.1 per cent. That's excluding MRO. And churn remains at near record lows at only 10.6 per cent.

Also, as the NBN, you know, changes come we're very pleased that we've continued to grow our fixed data services at 75,000 and so we're continuing in this – improving the experience on the ADSL network. We have done a number of upgrades that – across 4400 suburbs and also upgraded the cable network, 49 nodes at 134 suburbs. So we're keeping those networks and the customer experience at the right level.

Also, as we've often talked about, bundling is very important because when you sell a bundle a customer signs up to a two year service and we're now a total of 1.7 million customers on a bundle plan. This is a very important part of our business as we bundle in entertainment because we see this as a real differentiator. Both today and in the future. So I think from a customer and revenue growth perspective, you know, good results and we will continue that focus.

In terms of network leadership, Andy touched on this as well but, again, 1.8 billion dollars we have investment. It's very important we keep our leadership in 4G. Andy also mentioned that we're not stopping. We're going to continue to drive out further investments in those networks to improve

Telstra Half-Year Results Presentation, 13 February 2014 - Transcript

customer experience and, also, to continue to drive more efficient capital allocation. And then lastly driving productivity to simplifying the business, the productivity program remains on track. This is hard work and we've got a great team led by Robert Nason doing that with all the business units. We've seen benefits of \$225 million dollars in the first half.

It's important to understand that driving productivity benefits really gives us the right to invest in new growth opportunities and customer service initiatives. And that's really what we do. Process and service improvements led to a 9 per cent – 9 per cent reduction in December quarter call volumes for our consumer business. That's very impressive. A 9 per cent reduction. So driving value from the core is critical. Given the scale of our core business, you drive enormous shareholder value and I do believe that the potential to grow this business remains, you know, exciting. So that's driving value from the core.

Let me now turn to building new growth businesses and I really want to focus more on NAS and Asia, at least initially. We have a clear strategy in place designed to realise the opportunities that we believe exist across these portfolios. So let's talk briefly to NAS. You know, the results, I think, speak for themselves. We've got significant capability in this business and it is a capability driven business. And we're enhanced that with North Shore Communications and O2 Networks.

But the changing nature of our business means that there's a changing mix in our expense base to support this very fast growing business. Over the six months, we have successfully transitioned in two of the largest managed services contracts in the history of Telstra. I have already mentioned Defence and Health Services. But this includes the upfront transition which includes significant equipment, etcetera, so that there usually is a bit of a front ended cost base in terms of these large contracts. So that's NAS.

Turning now to Asia. We really have continued to focus in on what will we do in Asia. I am very pleased about the restructuring of the business around the global enterprise services division, which will run our enterprise and government division here in Australia and, also, right across Asia and the NAS business. We're also looking for an opportunity to leverage our core capabilities and optimise value in mobiles. And that wording is very important. Is really looking for opportunities to leverage our core capabilities and optimise value across mobiles. And we will continue to look for longer term growth opportunities in that market.

We do have significant scale and scope in Asia and many people don't understand just how big it is. If you – just a few quick points on that, in the last 18 months we have opened 15 new points of presence internationally. So Telstra now provides customers access to 1900 – 1900 points of presence and we operate it in 230 countries and territories. 230. We've invested in two new submarine cables bringing the total number of cables in which we have an investment to more than 20. We've opened data centres, as Andy mentioned, in Singapore and we now have seven data centres that we directly operate and we have another 11 that we have some involvement with. Which brings us to a total of 18.

So these assets position us well as we look to grow the NAS business beyond Australia and expand our global footprint. Andy also mentioned the Memorandum of Understanding with Telkom Indonesia. And it will form a new joint venture to provide network application and services in Indonesia which, as you know, is a very fast growing market. Under the terms of the MoU, the joint venture will be the exclusive provider of these services in Indonesia for Telstra and Telkom Indonesia giving both companies the opportunity to build market share in that fast growing market. It is a Memorandum of Understanding now and we will move to final contracts as soon as possible.

Also last year, we increased our stake in Autohome. And that is the leading online marketplace for cars in China. It was listed on the New York Stock Exchange last December. Telstra has a 65.4 per cent stake in Autohome. Which has a market cap of around about 3.25 billion US dollars based on the current share price. That has been an impressive investment.

Our strategy in mobiles is also to optimise value. Our decision to sell CSL is consistent with this strategy. In our view, the nature of the Hong Kong market is such that consolidation is important for long-term economic reasons. So we feel comfortable with that decision.

I also want to mention briefly the emerging opportunities we've identified in health, global applications and digital media. Over the six months we have undertaken a significant amount of work in these areas. Firstly, health, our decision to take a 50 per cent interest in Fred IT Group is, I think, a good example. The company offers eHealth solutions to the community. That's to general practitioners and pharmacists. And is helping to overcome some of the issues that result from the fragmentation that we all know exists in the health industry. And it connects over 15,000 doctors and 3900 pharmacies through its script exchange service. So this is all about driving efficiency of information flow.

In the applications area, I am pleased to say that we continue to focus in on that area. We increased our equity stake in Ooyala. We launched our start-up accelerator program called Muru-D. And we've also continued to look for – and evaluate a large number of new opportunities in Australia and globally.

In digital media, we believe in the multi-screen experience. We think that this is a growing and exciting opportunity. Over the past six months we have had 54,000 new customers take up the new entertainment bundle and we now have 360,000 households registered for Foxtel Go. And that's a 15 per cent increase for the half.

We strongly support Foxtel's commitment to bring subscription, video on demand, service to the market and we've got a team working on that new platform capability right now. Which we hope will soon be available. The technology is built on a leading edge software platform of which Ooyala really is at the heart. So building new growth businesses is an ongoing priority for the company.

Let me now move on to make a few brief comments about the National Broadband Network. I just want to keep it pretty brief because we have commenced negotiations with NBN Co and the government. And what we're going to do is as we achieve milestones, we will update you. As you know, we're ready to assist the government in achieving its objectives to move to a multi-technology NBN rollout. But we're very mindful of achieving our objectives which are as follows: we will act in the best interests of our shareholders, number 1; number 2: we are going to maintain the value of the current agreements; number 3: we're going to move to drive certainty of outcomes as soon as reasonably possible and our intent is to try to enhance regulatory certainty.

As for any additional role Telstra could play in the NBN build, for example, doing more work in design and construction. We're very happy to consider any opportunity should they become available and prove commercially attractive. NBN Co and the government continue to work through their process. They have completed their strategic review of which the results were released last December. NBN Co and the government and now considering the view and they will issue a new corporate plan. NBN Co has also gained acceptance for their SAU, which is their special access undertaking, and that has been approved by the ACCC and, on our side, we've signed a two year wholesale broadband agreement with NBN Co and we continue to be focussed on building the transit network which will be completed by the end of this year.

So, let me just summarise, we've delivered revenue, profit and customer growth. Which we're very pleased with. We've increased the dividends for the first time in eight years. We continue to invest in our core business driving productivity and network leadership. And we continue to focus on new growth initiatives. Having made several strategic investments in the first half of the year. And we are on track to meet our full year guidance.

Thanks for your time this morning. Andy and I would be delighted to take any of your questions and I would just like to finish by thanking the team that I work with. They are a great team and while we've got still a lot to do, we are very pleased with our results at the half. Thank you.

MR KEYS: Okay. We will take questions here in Melbourne first and then over the phone. Good morning, Ian.

MR MARTIN: Good morning. Strong results. Well done. I think that strategy seems to be working in terms of, you know, the things you're putting in place to help exploit the fantastic operating leverage your company has.

MR KEYS: Yes.

MR MARTIN: I just wonder why the guidance is still so low when you're clearly – are beating that, the first question. Second, just in terms of that operating leverage, the one area where it's a little bit tricky, given declines in volumes is the fixed margin. But you seem to be, at least, largely making up the decline in margin on voice with gains in fixed data. Can you just – now we've got a – you know, a half year of subscribers from NBN. I think a few months ago you suggested a 20 per cent gross margin for NBN customers - it seems very low to me. And I wonder what the experience of that first half is, whether there's enough to go on there in terms of guiding margins.

MR THODEY: Yes. Why don't I just pick up that last one, Mark, and then I will get Andy to talk about some of the specifics and the half-to-half. Yes, look, on the NBN, still really early days, I mean, we're only talking about tens of thousands of connections and remember the amount of work that we have to do to get all our systems right and processes – and it's a very complicated interaction with NBN in terms of provisioning systems, you know, transferring customers from their copper or cable across to the new NBN system. So in terms of margins, you won't see a, you know, ongoing predictable margin. I don't think for about probably another year and a half, two years. You've really got to be in the hundreds of thousands, millions of services before you get any stable sort of run rate on it.

So, at the moment, we've still got a lot of work to do to really smooth out that process and get the customer experience better as well as managing costs. So that's why you're not seeing a whole lot on the margins at the moment. Do you want to talk to the half-to-half and some of those other questions that - - -

MR MARTIN: Sure. Yes. 20 per cent margin – I think you mentioned gross margin at Investor Day is that still....

MR THODEY: Yes. I did. Yes. I think – look, I think that's about where we should target – 20/25, actually, is where I would like to be and – but, you know, as you know, this has got, you know, market forces, etcetera, in it but we've really got to drive a really efficient great customer experience and that's what a lot of the thinking is going into at the moment. How you ought to make the process. How you make it easier for the customer so you don't have to truck roll and it's a lot of hard work to be honest. And, of course, remember the way the NBN is rolled out, it is not done street-by-street. It's FSAM. And so you've got teams working, you know, one end of a suburb, another end of the suburb and so we think there's some better ways we might be able to do it. But we're working that one through.

MR MARTIN.: Okay. Andy.

MR PENN: Okay. Look, thanks very much, Ian. The question on guidance is that, well, if you look at our guidance result for the half year, it's 3.3 per cent on income and 6.6 per cent EBITDA. So I assume you're sort of referencing the EBITDA rather than income. A couple of things: I mean, firstly, as you know, our guidance basis basically excludes the impact of M&A in the current period, and it's based of the FY13 base number, so you might recall in the first half of FY13 we had the impairments for the sale of TelstraClear, so that's actually depressing the first half of 2013 numbers relative to the first half of 2014, and that will even itself out over a year, so that will have an impact, and the second, probably, key driver is also the Sensis, because we provide this on a pro forma basis excluding the impact of M&A; it has a sharper decline in the second half of the year in terms of earnings than in the first half, and so that would drag that down on a guidance basis as well. So when you take those two factors into account in conjunction with, you know, the business generally, then, you know, we're still comfortable with the current guidance that we're providing. On the – sorry, David

MR THODEY: No. No. No. You go.

MR PENN: I was then going to go to fixed margins, which was the other question.

MR THODEY: Great. I'll just make one comment. Ian – I think, you know, the underlying operating performance of the business remains, you know, solid. Good. So I – but there is just some anomalies in the half to half.

MR PENN: And then my – the other question was really in relation to fixed margin, which I think you have probably answered for us, which is that we saw a one percentage point decrease in fixed voice and a one percentage point increase in fixed broadband, and that is very much reflecting the changing scale of those two businesses. Fixed voice is – enjoys a EBITDA margin of about 60 per cent and declined 7.3 per cent in the first half, so we're pretty pleased that we continue to be able to get – scale across the rest of our business and productivity, that means the margin impact was only one percentage point. Fixed broadband benefited just from, again, the increasing scale there.

MR MARTIN Great. Thanks.

MR THODEY: Thanks Ian.

MR KEYS: Thanks Ian. Good morning, Raymond.

MR TONG: Good morning, David. Morning, Andy. Just three questions. Just, firstly, in mobile, is just the margin improvement you mentioned was driven partly by handset subsidies. Do you think you're at the right levels at the moment to balance, I suppose, growth and margin, and do you think that there's further scope for, sort of, handset subsidies to go down a bit more?

MR THODEY: Why don't you go first? No. You go.

MR PENN: No. No. Okay. So, well, I think – so you're right. That was part of the reason the margin improved two percentage points, but it also improved because we got ARPU growth and data monetisation and also continued productivity and scale growth as well, so activations were slightly lower in the first half of this year relative to last year, so that would have been one driver. Cost of mobile phones has gone up slightly, but the cost of customer contributions, as well, has gone up slightly more than that. So it has had an impact, but not a huge impact. I think the more important point is actually the value of the overall mobiles proposition. We continue to invest very heavily in the network. That's clearly demonstrating itself in the fact that we got very, very strong customer growth, and also the value of the overall product and the innovation we are doing of the products, some of the innovations that David mentioned as well. So I think the overall value proposition for a customer is pretty attractive, and I think that's demonstrated by the nearly three quarters of a million of extra SIOs that we had in the first half.

MR THODEY: So I was just going to make a very similar comment. I think the balance is about right. I think what we have – you know, we have got to be very attuned to what's going on in the market, but, you know, the – you know, when you have got a network of the size and scale and breadth that we have got, it's a great value proposition, and our job is to make sure people understand that, get a great experience, and continue to price for value.

MR TONG: And, I suppose, secondly, just in terms of the costs outlook. I think underlying costs is up 4 per cent, partly due to the, sort of, the big contracts and the investment in NAS. Can you talk about, I suppose, when the outlook for the second half – whether that investment is still going to continue or – and when do we, I suppose, expect to see the inflection point in the earnings for these big contracts?

MR PENN: Well, look, at a general level usually it's the first year to two years in a big, sort of, five to six year contract that you have a bigger cost bubble, but, look, my – our view is that, you know, going into next financial year, you should start to see, you know, some better clarity about how we're driving, you know, better methodologies, centres of competence to, you know, drive margins out of those contracts. Yes. Okay?

MR KEYS: Thanks, Raymond. Operator, could we please take some questions from analysts on the phone?

OPERATOR: Thank you. Our next question comes from Mark McDonnell, BBY. Go ahead, please, Mark.

MR McDONNELL: Thank you. Good morning, gentlemen. Three quick questions from me. Firstly, David, on the NBN, thank you for the very helpful clarification of your objectives. I'm wondering if you

could comment on the timeframe for the renegotiation; your expectations there – not absolute worst-case, but, shall we say, a mid-case outcome. Is it 6 months, 12 months? I'm just curious to know your thinking about that. Secondly, with regards to your comments about supporting SVOD via Foxtel, I'm wondering if you could shed some light on what the nature of the problem was with the aborted launch of the Presto service, and, again, how long is it likely to be before that service is up and running? And, thirdly, in relation to the capital management, I'm just wondering if – I know you – in past, you have stated that your preference is to pay fully franked dividends as the preferred method for capital return, but given that your franking credit balance is quite low – I can't actually find the number in the accounts, but based on the amount of tax you are paying, I suspect that it's – you're running very close to the wire. I'm just wondering to what extent you're looking at other options, including, for example, a share buyback. Thank you.

MR THODEY: Great. Look, thanks, Mark. I will let Andy take the third question, but let me take the first two. Timing is very hard to comment. We're really driven by the government on this one. I mean, obviously, Mark, we would like to get it done as soon as possible, as I'm sure the government would, and it's just a little bit too early to really give any indication of that, because it has just been the last few weeks that people got back from leave and have started the process. But what I will commit to you – as soon as we have got any sort of sense of milestones we will let you know, but it would be not appropriate – you know, it's just – we just don't know at the moment. So we will keep you posted on that one.

Your question on the Foxtel Presto and the platform – yes. Look, it is late. And it related to two things. One was just the integration of a number of different software products to really give the type of customer experience we wanted to give, and that took us a bit of work going up into Christmas, and then, hey presto, one of the interfaces that Google was providing us was pulled, and we had to go to option B, which is sometimes is just the way it is. But, look, it is imminent. Imminent. I won't announce a date, but it is very close, and we are very keen to get that product into market and to support it both through Foxtel and looking at how we can also add it into the Telstra bundle. So that's the first two. Andy, do you want to take the capital management and - - -

MR PENN: Sure. So, morning, Mark. On capital management, the – we don't actually include the franking balance in the half year accounts. It is in the full year accounts. That's why you can't see it. But in the full year you might recall it was slightly negative, and it's, sort of, still slightly negative, so that's the situation with the franking. Yes. You're right, and it's stated in our framework that the board's position is the preference is that shareholders like fully franked dividends, and as I have maintained in the past, I think, you know, to be able to do that over the longer term, firstly we have got to sustain – you know, we have got to get sustained earnings growth, and I'm pleased that we are continuing to achieve that, and secondly we need to take account to the extent that that comes from offshore and doesn't generate franking will need to have a payout ratio which is less than 100 per cent, which we have achieved last year as well.

You might recall the government's policy decision to change the instalment basis for corporates this year comes in. So effectively what that means in 2014 financial year we will pay, in cash flow terms, 14 months of tax, and given that we pay \$1.8 billion dollars a year in tax, that adds about another \$300 million worth of franking into our account in the second half of the year, so I don't have any particular concerns on franking. I think, more broadly, your question was in relation to capital management share buybacks, et cetera. I think, look, all I can say is – and I know, you know, there's obviously, you know, keen interest in what we think about when we think about capital management, but that's why we have provided the framework that we have. Obviously if we had something to announce, we would, but what I would say is that, you know, any decisions that we make will be firmly in line with that capital management framework, and certainly not before we receive proceeds from transactions because, you know, they still have to go through and meet regulatory approvals, et cetera. So I think they would be my comments, David.

MR THODEY: Yes. Yes. And, look, I can just reinforce Mark that the board as, you know, really active in their capital management, you know, considerations and will continue to be.

MR McDONNELL: Thanks very much.

MR KEYS: Okay. Operator, next caller please.

Telstra Half-Year Results Presentation, 13 February 2014 - Transcript

OPERATOR: Thank you. Your next question comes from Fraser McLeish from Credit Suisse. Go ahead please.

MR McLEISH: Thanks very much. Just a couple from me. Andy, just on the guidance, I just want to be dead clear. The growth of the – from the – of low single digit from the 10.6 billion base, that includes Sensis EBITDA, does it?

MR PENN: Yes, it does. It – because, effectively, the way in which we do guidance – and it obviously become more complicated in a period when we have M&A – is that we remove the impact of M&A from the current period. So it effectively means that TelstraClear impairment is still in the FY13 base but we need to adjust FY14 for any M&A that we do in FY14. So the answer is yes.

MR McLEISH: So yes – so we add in Sensis and then take it out again to get to the number on the reported basis.

MR PENN: So I apologies it is complicated but, as I said, that's the only way in which we can really do guidance.

MR McLEISH: Okay. No worries. And just – David, the other question I wanted to ask was just on the efficiency savings. It looks like they're sort of run rate a bit less in the half than what it had been tracking at for the last few periods and is that – does that sort of – is that slowing down the amount of savings you can get or are you still feeling pretty positive that there's plenty of savings you can continue to drive going forward?

MR THODEY: Look, it's primarily timing, Fraser. We – it is – it is less for the half. We've got a very active set of initiatives to drive out in the second half. I'm looking at Robert and he's nodding at me saying he can do it so we're still targeting at that gross level the billion. So yes, we're – we've got to do it. We've got to keep at it.

MR McLEISH: And is there a few – a few more years to go in that – on that sort of – that sort of level?

MR THODEY: Yes, they get harder, Fraser, but yes, we think we can do it. You know, we're currently planning for the next two to three years a billion a year at a gross level and it's not easy work but committed to it.

MR McLEISH: Perfect. Thank you very much.

MR KEYS: Thank you. Next caller please, operator.

OPERATOR: Thank you. We don't have any other questions registered at the moment.

MR THODEY: This could be a first. Could be the first time ever.

MR MARTIN: I've got plenty of questions for you, David.

MR THODEY: Yes

MR MARTIN: I will just ask two at this point. The Asia growth strategy - - -

MR THODEY: Yes.

MR MARTIN: - - - I think it looks quite promising. Can you just give us a broad indication of the level of resource that's going into that. I saw a media report recently, I think when the Singapore data centre was opened - - -

MR THODEY: Yes.

MR MARTIN: - - - that it was about 20 million. I guess that's excluding the infrastructure.

Telstra Half-Year Results Presentation, 13 February 2014 - Transcript

MR THODEY: Yes. Yes. Well, look, we're both doing two things. Both – we're investing capital as well as people. In terms of business development and new initiatives, probably close to 100 people, Andy, that we've put into that sort of area. In terms of capital, in terms of the cables, Cloud – have you got that number for

MR PENN: It's pretty modest, Ian, but I mean it would be less than \$100 million.

MR THODEY: Yes, less than a hundred. What we're trying to do is – is find areas where it doesn't take enormous risk. I mean, like, let's take the JV with Telkom Indonesia. That's a services business. There will be some capital required but it's not like going in and acquiring an enormous business that you – you know, you may or may not have great experience and so it's about setting foundations that we can grow over time in fast growth areas. And so we'll continue to look for those sort of opportunities going forward and we've got a good base to do that from.

MR MARTIN: Okay. You made a comment about leveraging mobile as well - - -

MR THODEY: Yes.

IAN: - - - which is kind of curious when you've just sold CSL. How do you leverage mobile into Asia, then, when - - -

MR THODEY: The words were carefully chosen. I didn't say go and buy mobile operations firstly, so just to make sure you know what I didn't say. But what we find is that, you know, Telstra mobile engineers are probably some of the most respected engineers in the world. We've built this great capability under a guy called Mike Wright and the team there that have really been at the forefront of the deployment of large mobile networks that really take advantage of new spectrum. And we're finding there's, you know, quite a lot of opportunities where we could partner with operators to help them in the deployment where we're really leveraging our capability. Now, we need to see how that plays out but we think that's a good opportunity.

MR PENN: And David, is it worth mentioning, I mean – the point on CSL – so I appreciate why, at one level, you know, at a higher level that could look contradictory. I mean, the bottom line is our view is that we have a very successful business in Hong Kong but the Hong Kong market is really in need of consolidation. There's five players in a market of only eight million people and, indeed, there's some spectrum changes which are up coming which are only going to sort of potentially encourage the market to open up more. So we've been strongly of the view the market will benefit from consolidation and, having looked for opportunities in that regard – I mean, you know, we're economic rationalists and the offer that was put in front of us was a very attractive one because it took advantage of that consolidation opportunity and that's why, as David said, we've chosen our words very carefully that it's about optimizing value and our view is this is the right time optimize value on that asset.

MR MARTIN: Okay. Can I just ask one on the regulatory front as well because I noted one of your NBN objectives is to try and provide some – or encourage some regulatory certainty and good luck with that.

MR THODEY: Thank you.

MR MARTIN: While that's going on, the ACCC is going to start its fixed services review.

MR THODEY: Yes.

MR MARTIN: Resetting the range of fixed line services, access price services from July, I think. Last time that happened it was terrible for investors, terrible for your share holders. The ACCC back-flipped several times. No one knew where they were going. You know, billions of dollars lost by your shareholders. I notice you put out a – in a debt prospectus last year, you warned debt investors that these pricing arrangements force you to price below cost. Most of the risk, obviously, is held by equity investors rather than debt investors. I just wonder what your advice is to shareholders about that upcoming review and what's your expectation given where we were last time?

MR THODEY: Well it's – I mean, a really good question, Ian, because as you know regulators have a mind of their own and we have to be very actively involved, in which we are, and I think there's a number of considerations as we go into this review. Remember, you've got the NBN on one side versus the copper network and I think that in terms of looking after the interests of the consumer that that factor is going to have to be considered. Also, in terms of the copper network and especially the fixed broadband network, there's some principles from the electricity industry about core capability of infrastructure to support the future. Kate McKenzie gave a very, I think, insightful presentation about the impacts of contention to consumer experience and if investment does not continue in some aspects of the copper network of – like fixed broadband – there could be serious consequences to consumers.

I think there's some other mitigating factors here that need to be considered as the ACCC deliberate and we will be very active in that process and already are. I think that's about all I can say for now.

MR MARTIN: Okay. Thank you.

MR KEYS: We will take a question from you, Raymond, and then we will go back to the phone.

MR TONG: Just two further questions. Just in regards to the NBN payments and the infrastructure payments, I think there's about \$139 million this half, up from about \$60 million in the second half. Just how should we be thinking about those payments and how they ramp up in the second half and into FY15 just given the transit network is due to be handed over by mid-year.

MR PENN: Yes, well I think maybe the way to think about it, Raymond, is that the Infrastructure Service Agreement payments obviously are largely to do with the transit at the moment because the level of rollout for NBN is obviously quite modest. So, you know, you can assume that that's going to continue sort of at the current level and then is going to be subject to the level of rollout of NBN. PSAA, similarly, is obviously going to be subject to the level of rollout of NBN. TUSMA is sort of more or less sort of at a full level so that's going to sort of trend in the same path that you can see there. And then the Information Campaign and Migration Deed will – the amortisation will conclude in the second half of the year.

MR TONG: So we should be expecting \$140 million for the second half. Is that sort of what you're trying

MR PENN: Well, I don't want to put the numbers out there but I think if you going to make grand assumptions about the rollout of NBN – but I tried to sort of tell you those numbers which, in a sense, effect and those that are subject to the rollout.

MR TONG: And just secondly, just in terms of I suppose the free cashflow targets and guidance that you've put out before of two to three billion. Can you maybe give an update to that? I think you're at about \$1.8 billion at the moment.

MR PENN: Yes, well also just to sort of back – sort of reflect back on that. So that was something that we communicated two years ago, in April of last year, so – and we said over three years so that's in a year's time. As you rightly point out, we're 1.8 billion at the moment. It was also subject to the rollout of NBN and, of course, there's been a number of very significant transactions since then. So basically if these transactions consummate, that's going to add approximately 2.5 billion of cumulative fresh free cashflow between now and the end of the second half of the year so on that basis we will be well beyond the two to three billion within the current – sorry, within the second half of this year.

MR KEYS: Okay, operator. Next caller please.

OPERATOR: Thank you. Your next question comes from Sameer Chopra, Merrill Lynch. Go ahead please.

MR CHOPRA: Good morning. I just had two questions on the NAS business, if I can. First of all, you know, you spoke about as the NAS contracts are digested that there will be changes in the opex structure and the margins from these. Can you just give us a sense for what we should expect on

labour and service contracts, like, what happens next year as the defense contract hits maturity? And the second one was Asia NAS pipeline, if you can give us a sense of what the pipeline in Asia looks like. Thanks.

MR THODEY: Okay, Sameer. Yes, look, the way these managed services businesses run is how – you bring on new contracts as you set up competencies across multiple customers. So let's take an area like managed WAN or managing large complex IP networks. You know, we've picked up the contracts from IBM, we've got Health and Defence, and the key capability is how you drive consistent processes across all three so you get the leverage of scale. I mean, in any one of these services businesses you would expect, you know, in the area of mid-20s type margins and that's where we are really focused on at the moment. We're – we're doing okay at the moment but we think there's more to be achieved. Also, you've got the big outsource contracts but then you've got the – what we call the disciplines, the disciplines around unified communications, video conferencing, areas like building out the emergency mobile networks in Queensland for G20, we're doing quite a bit in the health area.

And so they are specific individual, what we call, integration products and, again, they can range from 25 to 35 per cent margins. So two different types of business within the NAS portfolio and, I think, the challenge for the team and for me as well is how we really drive that scale productivity. But we think we've got, you know, good opportunity to do it and that's day-to-day blocking and tackling that we need to do. In terms of the pipeline across Asia, yes, look, it's pretty strong actually. We've seen a lot of activity, you know, as we build out our presence in South East Asia. We've got to do more work as we get into North Asia, I think. We've had a lot of interest in the core international carriages of coming in – companies coming from the US into Asia and signed a large number of contracts with the large IT vendors doing very well. What we call over the top vendors, but that's not managed services. That's more core carriage.

But we're very pleased with, you know, the sort of initiatives we're seeing quite a bit coming out of Korea. South Korea. Again, that's why we're having to increase our coverage in the market. And it's a sales effort now as we've got the capabilities. So early signs good. Over time, I think we will be able to give you more of an idea of pipeline and what contracts we sign in the quarter, and Brendon Riley, who is running that business, is very familiar with that from having run IBM Global Services throughout Europe and in Asia. So I couldn't think of a better guy to do it.

MR CHOPRA: Thanks, David.

MR KEYS: Operator, next caller please.

OPERATOR: Thank you. Your next question comes from Sachin Gupta from Nomura. Go ahead, please.

MR GUPTA: Yes. Thank you very much. I just have a few questions. Firstly, on the PSTN business, the decline seems to be improving. Is that something you think you can continue? Are we getting to the bottom of these declines? Secondly, you have fantastic mobile margins. But any thoughts on where you think the mobile margins could go from here on – on a 12 month or a 24 month view? And, lastly, just on this Asian strategy once again you talk both enterprise and mobiles. I imagine enterprise would be looking to form more alliances. I'm not sure I entirely understand what exactly is the mobile strategy in Asia. Thanks.

MR THODEY: Okay. I will make a few comments and then Andy can maybe pick up a few too. Look, PSTN decline, you know, look, it's a good six months of result. Remember, you've got NBN coming at us. So I think you've got to factor that in. I would be delighted if PSTN declined, say, about the same level. But it really depends on how quickly NBN ramps up to make a real estimate and until we have got through the negotiations we really don't know the answer there.

Mobile margins, we think they're about where they should be. I think that while we don't ever forecast on margins, we've always said high 30s. So that's about where we would like to be. I think, in any period, you might get, you know, ups and downs depending on, you know, a lot of factors go into that especially around our investment cycle in the network. You know, what's happening with the handset vendors and, of course, we like competition with handset vendors and long may that continue. So I think that's – but around the high 30s is where we should plan to be.

Look, maybe I can just help you on this Asian strategy because it isn't that difficult. It's pretty simple. In the enterprise government sector where enterprises and governments need large complex projects with large IP core networks, that's what we do, have done, always will do for many years in Australia and throughout Asia and that's a good business. That includes cloud computing. I mean, in Australia, the computing market is about a \$12 billion market. So if you want to extrapolate that through into Asia, you know, it's a very, very big market. We don't need to take very much share to get good growth. So that's a great opportunity but it's all around managing complex networks for large enterprise and government customers. Put that aside. You got that one? That makes sense, Sachin?

MR GUPTA: Yes. Thank you.

MR THODEY: Okay. Mobile is completely separate. You know, over the years, we've looked to buy mobile operators around the region. They are a very high multiple and very hard to create value for shareholders. So rather than doing that, we are working with other operators where it makes sense to basically export our talent and capability to help them build differentiated networks and that may take many different commercial constructs. But it has got far less capital investment. Now, it's not to say we won't put capital out there but it's just a very different model. More of a partnership model. So that's what we're doing in the mobile business and we will see how we go in the next couple of years. Does that make sense?

MR GUPTA: Yes. Yes, thank you. I think that's fine. Appreciate it.

MR THODEY: Okay. Right. Over time, we will be able to speak to you more about it. Okay.

MR KEYS: All right. Operator, next caller please.

OPERATOR: Thank you. Your next question comes from Richard Eary from UBS. Go ahead, please.

MR EARY: Good morning, guys. Just a couple of questions from myself. If you look at the revenue base now coming through – there's obviously an increase in contribution from NAS and international products. Can you just give us a sense of actually where the profitability is trending it within those products given the growth rates. That's the first question. The second question with regard to deployment of capital and talk around Asia. You know, how confident you are – are you of delivering a better return to shareholders in Asia than the ROIC that you're delivering domestically. Some sense in terms of guidance around that and how you're thinking about that would be great. And then just lastly, if you look into the market pricing. Obviously, we saw a little bit of increased competition in the market towards the back end of December. There's obviously new plans out – coming through the start of this year and I understand that you're trying to make some changes in terms of your plans as at this March. I just wondered if you can sort of talk around how you're actually viewing the market at the moment and how you see that trending over the next sort of six to 12 months.

MR THODEY: Okay. Why don't I get Andy to talk to the profitability of the business in Asia and NAS. But as a couple of sort of introductory comments, it's still in the early ages which – while continuing, you know, growth it is still in terms of the total. Not significant. But I remain incredibly positive about the opportunity and I will make some comments about what I think the ROIC and Asia in a moment. But let me get Andy to talk just about one and then I will pick up on competition.

MR PENN: Well, you can –

MR THODEY: Yes. No – if you've got any comments, we will hear them, you can - - -

MR PENN: No. No. Sure. Well, sorry, firstly, I think in relation to profitability, international, definitely, we're growing profitability there. If you look at the underlying businesses that we owned during the period – Autohome is growing very, very strongly as demonstrated by its success following the listing. The Telstra Global business continues to improve profitability and also CSL, albeit, obviously, we've entered into agreements to sell that nonetheless, in the period, grew profitability. So on the NAS side, profitability on NAS did not grow in the first half. But that's for the reasons we've

already canvassed in a very detailed way in relation to the contracts that we have taken on. But as David has mentioned, you know, our aspiration will be now to improve the profitability of that over time. Having said that, we wouldn't expect the NAS services business to enjoy the same sort of margins that we do on our carriage business and then, in relation to international, via a function of the nature of the businesses and, I think, realistically moving forward they are going to be more orientated towards Global Enterprise Services NAS than they are carriage businesses for the reasons we have discussed strategically.

So I think they're the points around the evolution and that. And I think the points on ROIC will follow that as well. So, obviously, in our core infrastructure base carriage businesses, so our mobiles businesses, our fixed line businesses, you know, they're large capital investments and relatively large EBITDA margins to reflect the level of capital we're investing. Whereas the services businesses tend to be more capital light and slightly lower margins. But nonetheless are going to require capital in the early days to – you know, to support the growth of those businesses. So I mean they're the contextual comments that I will make David. I think we interestingly for you we published the ROIC number for the first time in my presentation at a group level because I think its a really important number and one that you're sort of putting your finger on Richard that we're focussing on very hard in terms of making the internal capital decisions that we need to make.

MR THODEY: Look, Andy, I think that's exactly right. I mean, Richard, it's an area that we spent a lot of time on, because as you build up, sort of, the services side of business, it does have a different financial structure concerning the amount of capital you need to put in and how you drive returns. We need to be very careful about how we manage it and how we report it. But when you look at Asia, and you look at the incredible growth that is in all those markets, and as you know, it's a heterogeneous market, and as you build capability and the desire and opportunity right across those markets I think one of the things that we bring is, you know, great capability.

I personally think it's a great opportunity for Australia, not just for a company like Telstra, and I think – well, I'm hoping that there's a lot of support for it, because, as, you know, an Australian domicile company with such a great, you know, legacy, I think we have got a great opportunity to grow. Now, we need to be considered about that, because we are very conscious of shareholder returns and our large retail shareholder base as well. But it's – I think it's a land of opportunity. Now, just because you go there, doesn't mean you make money. You have got to be really disciplined. You have got to spend time understanding markets.

But we have got 75 years of history, and that's actually – if you ever travel overseas, it actually, you know, puts us in incredible stead whenever we turn up to these markets. Now, so I think we can get good returns. We will not do it unless we can. Now, it may take a couple of years to get to the returns that we need, but we will only do it if we can. When you turn to competition in the mobiles market, look, I remain an eternal optimist, Richard, about the mobiles market. The demand for our products and service remains, you know, at all time highs. The innovation going into that industry is second to none. Everything is becoming mobile-led. And I know that you have, you know, different views on it, but I think the returns from this business will continue to be strong for a number of years.

Now, there will be periods of high competition. There will be times when pricing moves around. But when, you know, consumers and businesses are dependent on a service, I think the opportunities are enormous. So, yes. You know, we will continue to have the normal skirmishes we have in the market, and long may competition, you know, be rich and vibrant. But we are well prepared and we will continue to, you know, run a balanced business and drive differentiation. We have never been a price player never will be. But we will, you know, look for differentiation at all levels. So, yes. A little bit more noise on the market, but we're ready and up for that.

MR EARY: David, can I just ask a follow up. Is – that – I mean, I think Andy or yourself mentioned that, obviously, the transit build for NBN, which is obviously in its last 2 to 3 year deployment will finish at the end of this year, which, obviously, I think, will, you know – will result in obviously capital intensity, you know, falling out in '15. But if we're looking at, obviously, the growth in NAS, and, obviously, you know, from the global services point of view in terms of a delayed return with obviously capital investment up front, should we not think about capital intensity dropping in the business in '15, but more being held at similar levels. I know that this is obviously not in the guidance, but I'm just trying to get an understanding that, obviously, if we're pushing more growth in NAS and global and

Telstra Half-Year Results Presentation, 13 February 2014 - Transcript

there's a delayed impact to the capital investment up front, are we not going to expect to step down as this sort ofcapex comes out in '15?

MR PENN: Richard, it's Andy. I mean, I think, as you probably recall, we – within our framework we have said that our medium term, sort of, target on capex to sales ratio at a group level is 14 per cent. We increased that to 15 per cent for last year and this year, which gave us another half a billion dollars to invest in accelerating the LTE rollout as well as supporting the NBN transit build, as you point out. You're right. I mean, looking at the capex to sales ratio at the group level is sort of a crude instrument. We don't look at it like that. That's just the way we report it for the market to be helpful, but, I mean, we obviously get it – look at it a more granular level business by business. But, look, notwithstanding all of that, I don't actually think that the points of change that we have discussed are material enough to change our view that, you know, around 14 per cent is the right sort of medium term number. So we will complete the – well, I say complete – we have completed the – obviously, the additional rollout of LTE, and we have got a lot more planned on mobiles, but we believe we can do that within our capex envelopes.

MR EARY: Okay. Thanks, guys. Much appreciated.

MR KEYS: We have about 10 minutes left in this briefing, so probably time for another couple of questions. Thank you, operator.

OPERATOR: Thank you. Your next question comes from Laurent Horrut from CLSA. Go ahead, please.

MR HORRUT: Thank you very much. Thanks, David and Andy. First off, let me just say I think you have done a great job at, sort of, recovering from a pretty tricky situation in 2009, and – but enough with the flattery. I think you have done a great job but I'm going to ask you some tough questions now.

MR THODEY: Okay, Laurent.

MR HORRUT: All right. First one is, Andy, I'm a bit intrigued by the difference in accounting treatment between Sensis and CSL, because if you say – if you're discontinuing Sensis, you still have the Trading Post, you still have True Local, so I don't understand how different the two transactions are. And while we're on that, what would be the best way to work out a true FY13 pro forma base? Is it just to take \$248 million from CSL out of the number – the restated number you published? And just – Andy, another subset on that is EBITDA consensus for FY15 is roughly \$10.8 billion. Even assuming a slightly better guidance going forward, I just can't get there, so I'm just wondering, you know, how comfortable are you with that sort of forecast in the market? That's my first question. Do you want me to ask all my questions, or I go one by one?

MR PENN: No. I'm happy to tackle that first one - - -

MR HORRUT: Okay.

MR PENN: - - - first. Look, just in terms of the different treatment in Sensis and CSL, it is a decision of the accountants, can I say, rather than necessarily me. But, I mean, basically, the premise is, as I outlined before, that Sensis is predominantly a print advertising business, and we have pretty much got out of the print advertising business as a consequence of the sale of that asset, notwithstanding your point about Trading Post. But, I mean, to all intents and purposes, we have exited the print advertising business. CSL is a mobiles business, which is very, very different. We have definitely not got out of the mobiles business. It's a core business of ours. And in the end and on balance, that is fundamentally what drives the advice from the auditors as to why we need to treat those businesses in the way in which we treat them. So I can't really add any more than that I am afraid. It's - - -

MR HORRUT: That's fine.

MR PENN: - - - the accountant's adjudication, and that's the way it is. I'm not quite sure I fully understood your question in terms of how you need to deal with the pro forma, but I think, when we are looking at guidance, we need to think that our guidance base is ignoring the impact of M&A in the

current period, so we need to sort of say, well, let's assume we didn't exit Sensis and, indeed, the transaction isn't consummated yet, or CSL for the rest of the year, and then let's look at what our result would be likely to be. So we have to make some judgments as to how those businesses were trading, relative to their plans in consolidation with the rest of our business performance, and we are very comfortable with our guidance of low single digit growth at that time. I can't comment on, obviously, what the market is saying other than to say that we also keep a very close eye on what the market thinks our result would be, and were we to see a significant difference with what we saw our result to be then we would have a disclosure obligation which we would obviously meet. So I think you can conclude from that that, you know, we don't see that difference. We're comfortable with our guidance and we are comfortable with how the market thinks we are performing.

MR HORRUT: No. That makes sense. Just for clarity: so you have restated at EBITDA FY13 \$10168. So do we take \$248 off CSL to get to the real number for FY13? That's off – because that was CSLs contribution in '13. So is that how we should approach it?

MR PENN: I don't think you need to take CSL out at all, but, I mean - - -

MR HORRUT: Why not?

MR PENN: What we did – we did publish the note on how we have restated the accounts, and I can point you to that. If that doesn't clarify your question, maybe if you could raise it with Andrew Keys in Investor Relations, and we will add to the transcript from this briefing any further clarification that is necessary.¹

MR HORRUT: That's great. Now, question for David. David, you know, historically you have always indicated that you think Telstra should stand between 14 and 15 per cent of capex every year. My question is obviously in the context of NBN. Is there any potential capex event over the next three years that would mean you have to spend much more than 14, 15 per cent and how would you, in the context of potential involvement in NBN, is there a scenario where Telstra does have to spend its on capex towards an NBN rollout?

MR THODEY: Under the current contracts, no. There is no significant capital requirement in anything that - - -

MR HORRUT: Okay.

MR THODEY: - - - is in place. But if that was to change through the negotiations and we believed it was in the best interests of shareholders, we would consider it but we would come back and talk to you about it.

MR HORRUT: Okay.

MR THODEY: But there is nothing that you should figure into your spreadsheets at the moment.

MR HORRUT: Okay. Fantastic. Just – is structural separation of – on the table today, ie, is there a scenario where in exchange for your involvement, a further involvement from Telstra in the NBN, there is a caveat particularly made for HFC whereby you could actually retain some of a fixed line asset or I should say access networks. And the first last one to Andy, if you had the choice between three options delivering the same NPV, one was reimbursement in the domestic business. The second one was an M&A opportunity and the third one being capital management and buyback all delivering the same NPV what would be your preference?

MR THODEY: I think I can answer your first question. We are not considering structural separation.

MR HORRUT: So it stays on the table.

¹ There was no 2013 restatement in relation to CSL. There was a restatement to treat Sensis as a discontinued business. A reconciliation was lodged with the ASX on 10 Feb 2014 and is available at www.telstra.com.au/aboutus/investors.

Telstra Half-Year Results Presentation, 13 February 2014 - Transcript

MR THODEY: That's the first one. And the second one, I'm not sure Andy is going to give you - - -

MR PENN: Well, no, no. It sounds like a multiple choice. Which I always used to love at school but – no, look, I think it's quite a simple answer and I think we've already articulated it in our capital management framework which is that where we would undertake an acquisition, it would need to show a benefit ahead of buyback at a similar level. So we're trying to make sure that we hold ourselves to that discipline. But, I think, also in our capital management framework we've said that, clearly, this is about looking to increase the dividend over the longer term. What I have said, consistently, is to do that we have to grow earnings. And to grow earnings we need to continue to reinvest in the business. We can do that organically. We've invested half a billion dollars over the last couple of years in addition to what we normally would to really continue to solidify our leadership in mobile networks and we will continue to do that. And then we've also announced \$226 million of acquisitions as well to support NAS, to support eHealth, Telstra Ventures. So the good news is that I think we're in a strong position to find those opportunities. But also in a very disciplined way.

MR HORRUT: And just, Andy, how is the M&A environment in Asia in terms of multiples and valuations. I imagine it would be quite tricky, no?

MR PENN: Well, I think so, Laurent. I think Andrew was going to try and make this the last question, which we must, because we do have a few other people. But what I would say, really, would just repeat what David said earlier. But I think in the core infrastructure businesses in mobiles businesses, which is why our strategy on mobiles is quite subtle is that, you know, the multiples are very difficult to see how you add shareholder value from. But nonetheless, we do see opportunities to leverage our capabilities to add value but unlikely to be through acquisitions of existing large incumbent mobile players unless something radically changed.

MR HORRUT: Thank you.

MR THODEY: Laurent, I just want to put a qualifier on my comment.

MR HORRUT: Yes.

MR THODEY: To the four principles I laid out, I also want to say that there's nothing off the table because if it was in the best interests of shareholders, then I would do it.

MR HORRUT: Yes.

MR THODEY: But today, we have never been able to see that structural separation generates real value for shareholders. But if, during the course of the negotiations, something was put to us that drove, you know, even more value, we would consider it. So – because I just want to be absolutely clear. Nothing is off the table. But, you know, we do what we know today or what I can comment on.

MR KEYS: Operator, we have time for one more caller. Thank you.

OPERATOR: Thank you. Your next question is from Paul Brunker. JP Morgan. Go ahead, please.

MR BRUNKER: Thank you. I will make it a quick one. So in terms of mobile business, do you see any change in momentum during the half or since the half ended? Thinking about what happened to Vodafone's numbers over the course of the half and whether you saw your gains at a fairly steady pace or did they tail off towards the end of the half. And just quickly on the Belong brand, obviously is it going well enough to be rolled out nationally? Any comments about where you see those subs coming from, what proportion of them are not non-Telstra subs. Thank you.

MR THODEY: Yes. Paul, could you just give me a little bit more – in your question about your reference to Vodafone. What were you referring to?

MR BRUNKER: I was just referring to the fact that their subs losses were very heavy in the September quarter and much less so in the December quarter. Although Optus' numbers this morning for December weren't very good. So I was wondering whether you had seen most of the

Telstra Half-Year Results Presentation, 13 February 2014 - Transcript

gains happening early in the half or – you know, and momentum tailed off, or was it a fairly steady pace over the half?

MR THODEY: Right. The – well, yes. I think you're right. Both other operators have reported negative quarters in the December quarter and, as we go into the – just getting some help here.

MR PENN: No. Sorry. I was just pointing out to David that we did announce at the first quarter, I think, in our analyst Investor Day, SIOs in the first quarter. Which, I think, from recollection were 235,000, in the first quarter and we - - -

MR THODEY: 739 - - -

MR PENN: 739 in the - - -

MR THODEY: half. Yes. I think where Paul is going is sort of early signs. Look, the market, you know, has got a little bit more heat in it but early days for the quarter, I would say. And – so, no. I'm confident we've got a great team in mobiles and well attuned to what they need to do and we believe in strong momentum in mobiles and we will do what is necessary going forward. But we are a value based player. In terms of the Belong brand, look, when we went through the Belong business case, obviously, what you've got to consider is that there is a lot of substitution going to take place, ie, you were just, you know, moving your own customers from your own brand of product to another brand and, of course, that wouldn't be a very sensible thing to do. We're very targeted around the Belong brand about where we want to be – that to be strong, just like we are in the Boost brand as well. And as we ramp that up in the next quarter and a half, hopefully we will see, you know the additions coming forward. Okay.

MR KEYS: All right. Thank you.

MR THODEY: Thanks.

MR KEYS: That is the last of the questions. David, would you like to make some closing remarks, please.

MR THODEY: Look, thanks, Andrew. Look, I think all I can really repeat is that it's been a – you know, a strong half. We're pleased where we're at. But as always in this industry, you never rest on your laurels and we've got a lot of work to do as we go ahead. But just, you know, deliver revenue, profit and customer growth. It's great to see increase in the dividend and, also, to confirm guidance. I think we're in the right place at the half but now we move on to the next half and the next year. So thanks very much.

MR KEYS: Thank you. We will be taking a short break and we will recommence for a media briefing in 10 minutes. Thank you.

TRANSCRIPT ENDS