Event transcript KPN Q4 & FY 2022 Results

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DISCLAIMER

Operator: Good day, ladies and gentlemen and welcome to KPN's 4th Quarter and Full Year 2022 Earnings webcast and conference call. Please note that this event is being recorded. At this time, all participants are in a 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 star one 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: Thank you operator and good afternoon, ladies and gentlemen, thank you for joining us. Welcome to KPN's 4th quarter and Full Year 2022 Results Webcast. With me here 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 harbour on page two 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 are also included in the press release published this morning. Also, statements are subject to the safe harbour.

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

Joost Farwerck: Thank you, Reinout, and welcome everyone. Let me start with some highlights from the 4th quarter and the full year results. We are pleased to have delivered on our 2022 outlook. Throughout the year, we have consistently grown our group service revenues, very important and clear proof point of the success of our strategy.

Within the mix, our business service revenues grew for the third quarter in a row and has now reached the point of inflection. Consumer fibre and mobile service revenues showed continued growth, partially offsetting the comparative dynamics in the broadband market. And in wholesale, we see the ongoing success of our open network policy, leading to continued growth. Whilst our cost base was affected by higher energy prices and one-off allowances to our staff, we were able to protect our margins. And, as a result of careful cost and cash management, we delivered solid EBITDA and free cash flow growth.

Together with the joint venture Glaspoort, we added a record number of households to our fibre footprint during 2022. We were again awarded the best mobile network, both in the Netherlands and in the world, and we were also recognised as the best All-in-1 broadband provider in the Netherlands, both on fibre and on copper.

Our return on capital employed continues to move in the right direction. The confidence in our strategy and the successful execution enables us to pay a progressive dividend and to return additional capital to our shareholders. Last year, we completed the €300 million share buyback, and this year, in 2023, we will again execute the share buyback programme of €300 million, effectively distributing all of our free cash flow to our shareholders.

As usual, Chris will give you more details on our financials and walk you through our outlook for this year. First, I'll take you through a couple of business details. Like I said, we've delivered on our 2022 outlook. EBITDA AL came in above €2.4 billion, CAPEX was stable around €1.2 billion, free cash flow was strong at €862 million, slightly ahead of the upgraded outlook we gave with the half-year results. We reiterate our dividend commitment, and we will pay a regular dividend per share of €0.143 over 2022.

Now, we've made good progress with our accelerate to grow strategy over the last two years, and we are now entering the third year of this plan. In the years after, we will, of course, further focus on the key pillars of our strategy. The first one, leverage and expand our superior networks. Second, grow and strengthen our customer base. And, thirdly, continue to simplify and streamline our operating model. And we intend to update the market before year end with our 2024-2026 strategy and ambitions.

Let's now look at the first pillar of this strategy, our best-in-class networks. Last year, KPN's own fibre rollout reached 348,000 homes passed, and if you add Glaspoort to this, it was over 0.5 million homes in the Netherlands. Together, we now cover almost half of the Netherlands, and we aim to reach roughly 80% of Dutch households by the end of 2026. And after reaching that point, CAPEX will come down to a much lower, sustainable level.

So far, we delivered a solid set of new fibre connections, and we are further optimising the way we roll out and connect households. On top of the traditional report of house passed numbers, we have additional household capacity, households covered with fibre through street presence, which we can also use in our commercial approach. And according to this definition, the number of fibre homes passed is 3.7 million at the end of 2022.

As you will know by now, our fibre business case is centred around the market share gains, ARPU uplift and lower maintenance cost of fibre. And as we continue to roll out fibre, our growing fibre footprint will result in an improved penetration rate for retail and wholesale. In fact, today our retail fibre base surpassed our copper base; that happened in Q2 last year. So nowadays, we have more broadband customers on fibre than on copper; important.

And this effort is visible in the financials. Looking at our Q4 results, we currently generate almost €1 billion of annualised fibre service revenues and that number is growing rapidly. In Q4, our consumer fibre revenues increased by 14% year-on-year, driven by a growing base and an attractive ARPU. All in all, fibre, as you know, is at the heart of our strategy to create long-term value for all our stakeholders.

And the investments we make in our mobile network and services are paying off as well. The Ookla and Umlaut benchmark recently recognised KPN as the best mobile network in the Netherlands and the world. And, alongside this, we were also rewarded as best All-in-1 broadband provider by the Dutch Consumer Association, and we were awarded as best fixed internet provider by Tweakers. So, these are all good signs of appreciation for our products and services.

Let's now move to the consumer segment. Adjusted consumer service revenues decreased by 0.3% year-on-year in the fourth quarter. On the one hand, we see consistent mobile service revenue growth, driven by solid base developments in growing ARPU. And, on the other hand, in a challenging competitive environment, our fixed services revenues are impacted by declines, mainly from KPN's legacy portfolio. Broadband service revenues grew slightly as fibre broadband revenues continue to grow strongly, offsetting the decline in copper.

Looking at customer satisfaction, NPS remains one of our top priorities and KPN continues to lead in the Dutch markets despite rising costs of living impacting general customer sentiment.

So, if we take a deeper look at our fourth quarter KPIs, our operational performance on fibre remains strong. We activated 50,000 fibre households last quarter. Despite the solid commercial momentum, our total broadband net adds showed a small decline on the back of increased competition in the broadband markets. Our fixed ARPU remained broadly stable at €53. And combined, our fixed service revenues decreased 2.3% year-on-year, impacted by structural decline in legacy, a shift in accounts for content packages and lower traditional voice traffic.

We continue to see solid trends in mobile: our post-paid base increased by 19,000 and our post-paid ARPU grew 2%. And combined, this led to a strong 4.7% growth in mobile service revenues.

Let's now move to the B2B segments. In 2022, we delivered an important milestone for our company. We realised our ambition to turn around our business segment, as we saw service revenue grow for three quarters in a row. Business NPS remains positive, although slightly down sequentially, and this was also partly due to the volatile economic environment.

The operational transformation and progress of our business segment continues to advance as we have migrated a significant part of our customers to our future-proof propositions, such as KPN EEN in SME and KPN smart combinations in LCE. This helps our customers make their business truly digital and drive cross and up-sell opportunities as reflected in the improved trends we saw across the board.

SME remains the main engine of B2B growth, driven by solid commercial momentum in both broadband and mobile. Also, LCE continues to move in the right direction. The migration of our customers to the smart combinations' portfolio is close to completion and we expect to deliver this sustainable inflexion this year. And the business we call tailored solutions continued to perform in line with expectations. This segment caters to large customers, often with an individualised approach. Customers here are generally partners for life, not least that we have taken important steps to improve profitability through a strong focus on standardisation, value and sustainable customer relationships.

In our wholesale, service revenues were again solid and increased 2.5% in the fourth quarter. In 2022, we added 84,000 post-paid SIMs and 27,000 broadband lines.

Now turning to sustainability, we are already, for a couple of years, fully committed to creating sustainable long-term value for all our stakeholders. Therefore, we are proud that KPN was once again recognised as a global climate leader according to the Carbon Disclosure Project, CDP. In December we signed an agreement with Eneco for the purchase of wind energy from 2027 from a new to be built wind farm at sea near the Dutch coast. As from 2027, more than half of our electricity will come from this farm at lower costs. And this is aligned with KPN's ambitious sustainability targets and helps to de-risk our long-term energy price exposure.

So, details in short. Now let me hand over to Chris to give you more details on our financials.

Chris Figee: Thank you, Joost. As Joost mentioned earlier in the presentation, we delivered on our guidance for the year. We will put forward guidance for 2023 that we also solidly underwrite. So, let me start by summarising some key figures.

First, the adjusted revenues increased 0.5% in Q4, supported by sustainable group service revenue growth. Second, adjusted EBITDA AL after leases increased by 2.4% in Q4, driven by service revenue growth and lower costs. Our EBITDA margin came out above 45%. Third, free cash flow increased almost 10% compared to 2021 and exceeded our target due to higher EBITDA and less taxes paid.

Our free cash flow margin of revenues improved by 130 basis points. Finally, our continued focus on sales for value creation is paying off, as evidenced by another solid improvement in return on capital employed, to 13.1%, up over 200 basis points year-on-year.

Adjusted group revenues were up 1.4% year-on-year. In the mix, consumer revenues were flat as growth in mobile service revenues and fibre revenues was offset by declining legacy and copper business. Business revenues increased more than 2%, largely driven by SME, with further improvement in the other business revenues towards sustainable service revenue growth as well. And wholesale revenues grew by almost 4%.

Other revenues were mostly supported by lower intercompany charges and revenues related to our fibre rollout. Group service revenues increased by 1.5% compared to last year, underpinned by strong growth in our business segments. Business service revenues grew by 3%, driven again by continued strong performance in SME, while the trend in LCE is gradually improving and behaves according to our long-term plan towards inflexion next year – sustainable inflexion next year.

Wholesale service revenues grew 2.5% year-on-year and in consumer, our service revenues were broadly flat, but the trend improved a bit compared to the previous quarter. Mobile service revenues continued to grow. In fixed, it reported a decline as the growth in fibre was offset by declining legacy services, less voice traffic and the accounting effects of content services. Importantly, broadband-only service revenues in consumer – that is a fixed service without legacies, fibre and copper together – were effectively displaying a small but positive growth as fibre growth outstripped the copper service revenue decline.

For 2023, we continue to expect some headwinds, but the trend is expected to improve, supported by implementing price adjustments and commercial improvements. Moreover, from Q2 onwards, we will see the lapping of the accounting effect that held back the reported broadband service revenue growth in 2022.

Adjusted EBITDA grew 2.4% compared to last year, driven by service revenue growth and lower indirect costs, partially offset by €54 million higher direct costs. Factors for this increase was the impact of higher non-service revenues, such as handsets and hardware sales; third-party access costs, at Glaspoort; and a change in service revenue mix in B2B. Service revenue and direct cost developments, our contribution margin grew by over €50 million. Add to that, our lower indirect OPEX and we get to the substantial increase in EBITDA of over €50 million.

Our personnel expenses decreased by €35 million. This reflects efficiency and productivity improvements from digitisation as well as natural attrition. Digitisation also helped to lower ITTI expenses, partly offset by other OPEX which rose, mostly on higher energy costs. In total, our indirect cost savings for the year were €38 million, as ongoing efficiencies were partly offset by industry-wide inflationary pressures from energy and labour costs, but both aligned, a cost reduction remained.

With respect to 2023, our cost base will be impacted by wage indexation and higher energy costs. The estimated gross impact on personnel costs of the new CLA is about €45 million.

Regarding our total energy spending and considering the 20% of energy we have still to consume on the spot market, we expect our total energy bill to be €50-55 million higher in 2023. And, obviously, also things can be moving towards this number, depending on how prices on the spot markets develop during the year. But the up and downside relative to our estimate is relatively limited.

At €862 million, our free cash flow was around 10% higher than last year and the cash margin of revenues moved to 16.2%. This improvement is mainly the result of EBITDA growth and less the cash taxes paid as we were able to realise and use some of our liquidation losses related to E-Plus.

Next to this, note the change in provisions includes a voluntary pension contribution of €23 million related to a DB plan of Getronics US. As a result of the tax tailwind in 2022, and using the opportunity provided by the increase in US interest rates, we decided to make an additional contribution to this pension plan. And this will again lead to lower contributions going forward and brings the plan a whole lot closer to full funding and eventual buyout. This investment will support free cash flow developments in the coming years, and we believe our free cash flow margins should be able to hover around 16% of revenues in the coming years.

KPN remains focussed on creating long-term value, which is evidenced by the strong return on capital employed. Our ROCE improved 210 basis points year-on-year to 13.1%, mainly due to increased operational efficiency on a stable capital base.

We ended the year with a strong and resilient balance sheet. The average cost of senior debt increased by 83 basis points, mainly due to higher interest rates on floating debt. At the year end, with a leverage ratio of 2.3 times, comfortably below our ceiling of 2.5 times. Also, our interest coverage remains strong.

Year-on-year, net debt increased by €130 million, driven by various non free cash flow items, since our dividend and share buyback were mostly covered by free cash flow. Total liquidity remained very robust at the end of the year, consisting of €1.5 billion in cash and short-term investments and our fully undrawn revolving credit facility.

Let’s now turn to our outlook and ambitions for 2023. For this year 2023, there are well-documented headwinds, particularly around inflation, with wage indexation and rising energy costs likely to affect our cost savings run rate. We are implementing measures to mitigate this impact as much as possible and remain on track strategically and operationally and still deliver slight growth this year.

We expect adjusted EBITDA after leases to come in around €2.41 billion, slight growth compared to 2022, despite the significant step-up in personnel and energy costs. EBITDA growth we expect to be skewed towards the second half of 2023. CAPEX will remain stable at a peak level of €1.2 billion, and we expect free cash flow of around €870 million, which represent a slight increase compared to 2022, but importantly, it means that despite the tougher economic climate and inflation, we will be able to meet the 2023 targets that were set during the 2020 Capital Market Day. In 2023, there's some large movements in free cash flow items, such as €100 million higher cash taxes and further improvement of working capital, but all in all, the effective improvement in free cash flow is likely to be very close to the effective increase in EBITDA.

In line with our progressive dividend policy, we expect to pay a regular dividend of €0.15 per share over 2023. This is up almost 5% compared to the €0.143 for 2022, and again at the upper end of the 3-5% target range. Our financial framework is aimed at long-term value creation for our stakeholders. In this respect, we are committed to return excess cash to our shareholders.

Our improved cash margins and strong financial position enable us to grow shareholder returns for 2023 through a growing dividend and new share buyback programme. Over the last two years, we've bought back €500 million worth of shares in total. For 2023, we intend to execute a share buyback programme of another €300 million. This means that we again will effectively distribute the free cash flow we generate to our shareholders; or alternatively stated, that all distributions are fully covered by the generated cash.

To summarise, I am proud to deliver our upgraded 2022 guidance, showing improving top-line trends, growing EBITDA and rising free cash flow. Going forward, we expect to see sustainable growth in group service revenues. And, although we face volatile market conditions, the measures we have implemented provide us with confidence in our ability to maintain a growing EBITDA and growing free cash flow. To me, KPN continues to demonstrate healthy margins, earnings and cash flow resilience and we feel confident about the cash generating ability of our group.

Our fibre roll-out programme has maintained a solid pace and has a proven attractive return profile. And we remain committed to returning excess cash to our shareholders and are confident that our progressive dividend policy can be complemented by structured, incremental capital returns going forward.

Thank you for listening to our story, now let's turn to your questions.

Questions and Answers

Reinout van Ierschot: Thank you, Joost and Chris. As usual I would like to ask you to limit your questions to two. Operator, over to you please.

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 star one on your telephone. This question is from Andrew Lee at Goldman Sachs, please go ahead.

Andrew Lee (Goldman Sachs): Good afternoon, guys, I had a question on LCE and then a cost-based question. So, just on the LCE inflection, you effected the growth in Q4, but you continuously referred to your inflection to sustainable growth being a 2023 thing during your presentation today. Can you just clarify really what you mean by that? Does that mean LCE declines again in early 2023? And maybe if you could lay out your visibility here and why LCE would not kick on to mid-single-digit growth like SME has?

And then just one question on cost, the lease inflation headwinds, could you give us some detail on the scale of each of that headwinds and what the relationship really is between local market inflation and lease cost inflation, just so we can understand it a bit better going forward? Thank you.

Joost Farwerck: Okay, I think I will take the LCE question and Chris will take over on cost base. Yes, I fully agree with you, by the way. So, we plan for the real inflection point in LCE in the second quarter of this year. In Q4, we already went up to, I believe, 0.4%, so that's very good. So, the original planned inflection point is mid-2023, but I agree, I don't see any reason to really go down again. So, of course, the challenges are a bit out there – it's a bit – business goes in batches every now and then, so the real confirmation we got from the company is Q2, but of course we are pushing really hard to make the 0.4% higher instead of lower. So, I recognise what you're saying.

And on the costs?

Chris Figee: Yes, on the costs, on the headwinds from the lease inflation, I think about €10-20 million of headwinds. We have of course got different lease contracts, we've got different owners of our towers and even, in fact, there's not just one but an amalgamation of contracts. Most of them have a link towards domestic inflation. There's not a one-size-fits-all answer but often they are linked to Dutch CPI, which for us means we expect to be €10-20 million cost headwinds next year. But that is already embedded and included in the EBITDA guidance.

Andrew Lee: Thank you.

Operator: The next question comes from Polo Tang from UBS, please go ahead.

Polo Tang (UBS): Yeah, hi, thanks for taking the questions, I have two. The first one is just about the pricing in competitive environments. So, T-Mobile Netherlands raised prices by 8.6% in January but what is your impression as to how these price rises have landed? Has there been any sign of increased churn to your mobile and have you detected any changes in terms of competitive dynamics in the market?

The second question is really just around your fibre build, because you've added about 94,000 homes passed, fibre homes passed, in Q4. How should we think about the pace of this build for 2023 and 2024? So, is 90,000-100,000 homes per quarter a normal run rate or is there scope to accelerate this? And what are you seeing in terms of competitive fibre build? Thanks.

Joost Farwerck: Yes, Polo, on pricing, yes, we are in a competitive environment. Having said that, we saw some price increases all over and indeed T-Mobile, 8.6% on mobile. We, in October, did 5.8% so that is, I believe, also why NPS in Q4 all over our operators is a bit under pressure. So, that's a balancing act. But all in all, the market understands, especially how we explain price increases, because we relate it also to the way we increased the CLA to our own people.

So, I think we handled that well. But still, we see discounts out in the market every now and then. The broadband market is a bit moving. Last quarter Vodafone Ziggo was somewhat under pressure, then we see discounts on their side. Sometimes we react. I strongly believe that we are running here a longer-term strategy. It is very important to create value on the longer term, roll out fibre, differentiate ourselves by delivering quality, higher speeds, more content.

We recently introduced a new TV interface, mixing linear TV with over-the-top for end-users and also allowing us to introduce over-the-top overnight. So, having said that, I think it's important for KPN to run our own plan and not follow all these discounts in the market.

Fibre roll-out, yes, so we also are responsible for allocating the build capacity to Glaspoort, at least the majority of that. So, we look at things combined. But of course, the KPN roll-out is fairly important for us as well. So, last year, 550,000; I think this year we should at least do 600,000, but the jury is out. There's a lot of capacity shortage in the market. We really, like I just said, run this for the longer term, so we committed ourselves to our partners for 2023, but also for 2024 and 2025. We are already planning 2024 and 2025 now. That's our way to move.

There is competition from Delta, ODF and other small players. The difference between us and them is that when we roll out house passed, we may currently connect 70% of the households as well, while the others are mainly rolling out homes passed. So, there is also a big difference in the quality of the fibre networks we are building. So, it is super important for KPN to just push the fibre machinery as hard as we can.

Polo Tang: Thanks.

Operator: Your next question comes from the line of Joshua Mills from BNP Paribas Exane, please go ahead.

Joshua Mills (BNP Paribas Exane): Thanks guys. Just another one from me on pricing. So, I think you've explained well the 3.5% fixed price rise in July, then you had the 6% price rise back in October. Can you just give some colour on what your thought process around each of those price rises was? And whether anything has changed in terms of customer perception, your ability to offer extra things in the bundles, which meant you were more comfortable doing a bigger price rise in mobile and fixed? And the reason I'm asking is just to try and get a sense of your thought process as we approach the next round of fixed client price rises, which I guess will be in June, the middle of this year. Thanks very much.

Joost Farwerck: Well, Chris, maybe you want to add something, but on pricing, of course we look at increases. 75% of our business is in subscriptions so it is important all over the segments to see how the price increase will work out in the year to come. Like I just said, we look at inflation but also at other drivers. Yes, if we do 6% in the CLA, there is a big chance that we will do more on price increase on the internet broadband than we did last year, but we will decide on that at the beginning of Q2. So, that's a balancing act.

It is also our ambition to move customers to higher value subscriptions. So, by moving them from 500MB to 1GB for instance. So, we just introduced a new line-up on the internet. We took out the 50MB proposition, that no longer exists. So, the minimum you buy with KPN is 100MB, but we really are moving our customers to 500MB and then 1GB. And on the mobile side, we move them to unlimited. So, the combination of price increases, but also driving up the value of the subscription proposition is the important game to play. And that, combined with the growing base, works out quite well, especially in mobile, and we want to do the same trick in broadband.

Chris Figee: Yes, I mean, in mobiles, we've got contractual arrangements to be able to push through CPI in the price change, so this would justify CPI increase in mobile. And the mechanics for that increase of 5.8, that's the calculation at the time, so some time lag. Although in mobile, we said it's going to be 5.8 with a cap of two. So, it's never going to be more than €2 per month, managing our reputation impact on customers somewhat. But in mobile, it is a pretty mechanical exercise, and we can decide on our own discretion to provide some cap on it.

And on broadband, with more art than science, we've got our own policy to follow. As Joost said, we managed the front book to back book distance. Given its reputation, you make sure that it is value for money and you, of course, take an important clue on – the inflation you have to deal with in that sense. Our CLA increase offers a good indicator of how we think what's fair and explainable to our customers when it comes to broadband.

Joshua Mills: Thanks, and maybe just one quick follow-up. A number of operators in different markets are trying to now include CPI increases of contractual obligations in both fixed and mobile bundles. Is there any reason why you wouldn't try in the future include CPI linkage in your fixed line as well as mobile? Thanks.

Joost Farwerck: In renewal contracts, we introduce this rise, but like Chris said, we run a big back book and a front book so it takes some time before you really can consider 80% of the base in that contract environment. But you're right, we introduced it.

Joshua Mills: Thank you.

Operator: Next question comes from the line of Luigi Minerva from HSBC, please go ahead.

Luigi Minerva (HSBC): Yes, good morning and thanks for taking my questions. I have two. The first one is on your energy bill indication, so that's very helpful. You mentioned €50-65 million more in 2023 and I was wondering if you can give us more details and what are the assumptions behind these expectations? Particularly what proportion is hedged, at what terms? What proportion is still exposed to the spot price?

And the second question is on competition dynamics. There is often contamination between dynamics in consumer and SMEs. Obviously, you are doing very strongly with SMEs, but as you said, the broadband has seen intense competition this year. So, I am wondering if you see any risk of contamination that may affect your SME performance in the coming quarters. Thank you.

Chris Figee: Okay, Luigi, on energy, let me start the story in 2022, then 2023 and also have a first sneak peak, or at least some crystal ball gazing for 2024. I mean, in 2022, our energy consumption was about 480 GWh and we lowered it to 455 GWh last year at an average price of about €77 per MWh. So, that is relatively cheap.

For 2023, we are 80% bought forward, and we start buying these contracts forward since long – we started those two years ago. 80% has been bought forward, 20% we buy on the spot market. We always do that. We can't do more because we think we can reduce our energy consumption even further, so the 455 GWh will go down to 435 GWh or even 425 GWh in terms of the actual consumption during the year.

We bought so far at around €150-160 on average per GWh through forward contracts. The €50-65 million total price bill increase assumes around 435 GWh of usage at an average price of around €180. So that means, if we continue to buy at the current spot market, there is a bit of upside there. So, that's good news. There's a bit of upside with 2023. It's not massive, but 20% to be still bought with guidance using €180 per MWh, current price around €164, is a bit of a tailwind for 2023.

For 2024, we've bought I think 38% forward and we were planning to, like, let's plan for the same amount of 2023. If you look at the forward price for 2024, they are also around €165-ish at this point in time. So, the good news, if this all continues, that means that we will not have another energy bill increase in 2024, at least with today's market position. That means 2023, €50-65 million more, some upside, let's see what that does to our guidance or business. For 2024, if current markets persist, and the market doesn't go berserk again, that means we will no longer have another energy uplift. We will probably stay at this higher spend level going forward, which should help our EBITDA in 2024, given the fact that there will be some price amendment in mid-year.

So, on energy, a bit of a tailwind for this year. As we previously said, lease costs are also a bit higher, so the energy tailwind is a bit used to offset higher lease costs and it all feeds into the current EBITDA guidance. But from energy, there's a bit of upside.

Joost Farwerck: Yes, on the SME performance, now we really have a separate platform to serve our SME customers. It's the KPN EEN platform. It works quite well. It is a different environment than broadband for consumers because it's a combination of workspace, mobile business proposals and security solutions. And until now, I do not see real risks of SME customers moving to consumer propositions. Of course, there is an overlap in what we call SOHO and consumer. But that's based on more or less the same portfolio. So, if you look at our SOHO customers, we also did a price increase on mobile of 5.8% and 3.5% from the internet, and it's a look alike of what we do in the consumer segment. So, on SME, I expect that one to be separated from that segment.

Luigi Minerva: And just to clarify, the SOHOs are reported as part of SMEs or are they part of the residential segment?

Chris Figee: Well, SOHO, it depends on what we sell. Mainly consumer products and then we report the consumer lines in consumer segments. So, like I say, there's an overlap. So, you referred to the SME and the risk of the SME customers making use of consumer propositions, well, that's more the segment we call SOHO, and that we already consider for the main part retail propositions.

Luigi Minerva: Okay, thank you so much.

Operator: The next question comes from the line of Stephen Malcolm from Redburn, please go ahead.

Stephen Malcolm (Redburn): Yes, good afternoon, guys, and thanks very much for taking the questions. A couple, first on the mix of consumer and business service revenues in 2023, and secondly, just on the free cash, so the bridge from 2022 to 2023, if that's okay? Firstly, just when I look at consensus for 2023, I mean, consensus as consumer revenue is growing at 1.8% and business at 1.2%. That's kind of flipped on what we've seen in the second half of 2022. So, the question is, do you think that mix makes sense? Do you think you can take consumer revenue growth back up to nearly 2%, or should we expect that the onus to fall more heavily on business, which is clearly doing very well at the moment, to get the numbers that you expect on the service revenue side in 2023?

And then just on free cash flow, can you help us bridge the €870 million? I mean, EBITDA broadly flat, CAPEX broadly flat. It looks like a lot of the strain will probably fall on working capital. And maybe just reassure us that you're not taking short-term measures, whether it be through vendor financing, handset financing that may – that you may need to unwind and may cost more money going forward as interest rates rise and the costs of those sorts of measures begin to weigh on cash flow and earnings? Thanks a lot.

Chris Figee: Yes, on service revenues, you are right, so indeed, if you look at the last quarter momentum really was on business markets more than consumer markets. It's a bit crystal ball gazing, I do see – because I think your point, the risk – or the risk is, I think, the outlook is that relative to consensus, business markets will be better and compensate for possible risk to consumer, due to the competitive environment, which will help us meet the underlying growth. If you look at our own contingency and risk planning, that's exactly what's in there. So, I think your observation is pretty valid. But that means that the service revenues as such are well protected.

When it comes to free cash flow guidance, the first reassurance point is trust us, we will not going to do funny financing out there. We have a small vendor financing programme but massive unused capacity and also handset financing. We've got a – I've got it in there to use as a safety valve but don't intend to really upscale it.

In order to understand 2023 cash flows, we have to look at 2022, right? We delivered €862 million cash flows, but in that we spent about €25 million in a one-off contribution to a US pension fund. I thought it was a pretty good idea because rates went up in the US, we were able to terminate that fund at peak rates, which will save us €7 million structurally in our pension contributions in the coming year. So, an one-off investment of €25 million to save €7 million will already give you €30 million on the year-on-year comps.

Secondly, in 2022, we already implemented a shortening of the timelines of SME. So, from a legal perspective, it was supposed to be SME companies earlier; that the law goes into place in 2023, was in the original plan. We brought forward into 2022. So, those are two negative headwinds that are all in the 2022 numbers. That means the underlying cash generating of business is actually quite strong.

And then, on working capital, you can see working capital was flat in the year. And that was also because we built up some inventory due to questions on supply chains, also as a preparation of a new TV product, we built up quite a stock of TV set-up boxes that we're using now. So, you'll see a bit of running down of inventories that we've built up during 2022. We see opportunities to improve working capital on what we call our product plus cycle. So, we've a product plus strategy that we sometimes have some giveaways to broadband.

That purchase outcome is shortened and everywhere I look in working capital, I see opportunities. For example, to invoice some of our large corporate customers earlier. We focus a lot on shortening payment terms, we've done that, but I think there is also work to be done on invoicing them earlier.

We are insourcing our activities; we see an opportunity there. So, a big chunk of 2023 is also smarter ways of working around working capital. In that, we should be able to pay the higher taxes that are ahead and, of course, let's be all fair, we are allowed to call the hybrid bond in March, which we'll officially announce, refinance it with Euro Perpetual and those cash flows will no longer be in our free cash flow reported. So, that's a reporting tailwind that we have to be clear about.

But it’s a combination of, I think, solid cash flow in 2022, which actually was held back by one-offs that we deliberately invested. That will come back in 2023. We will have a number of working capital optimisations that are really around the business area and not around financing. And those two should help us pay the higher tax bill.

Stephen Malcolm: Sorry, Chris, I should know this, but can you just remind me of the hybrid tailwind for 2023?

Chris Figee: Yes, it’s about – it’s about €20 million or so, plus. And I think it’s all fair to say that – actually, that supports the growth in our free cash flow also somewhat.

Stephen Malcolm: Okay, that’s brilliant. Thank you very much.

Operator: The next question comes from the line of Alexandre Roncier from BofA, please go ahead.

Alexandre Roncier (Bank of America): Hi guys, thank you very much for taking the question. I would just like to come back to CAPEX please. Obviously, we’ve talked about the ramp-up of the fibre roll-out in 2023 and even in the later years but I was just having a question regarding your total envelope. And obviously if we do some quick maths and get costs per homes passed over the year, there’s some saving there. But could you maybe highlight the cost of the fibre spend and what have you this year? I know you talked about 70% of your homes passed are now connected. But equally, why the small moderated freeze in non-FTTH CAPEX this year as I think a while back, you were more targeting to actually reduce the rest of that investment envelope? Thank you.

Chris Figee: Well, on the non-FTTH CAPEX, please note that non-FTTH CAPEX is still below 14% of revenues and has been there for the past and still is there. The small increase actually is in customer CAPEX, it’s more actually business customer CAPEX is going up. So, non-fibre CAPEX, non-fibre, non-customer CAPEX was flat, and it was the customer CAPEX that was up and it was really in the business segment where we had some CAPEX related to the growth in our business areas.

So, if you look at fibre, fibre was down a bit in euro terms, but also last year we had an acquisition that was qualified as CAPEX, so €20 million – €30 million less fibre investment included last year, about €70 million or so M&A. So, the net real decrease in fibre spend was about €12 million. And then on the non-fibre CAPEX, B2B customers up, customer CAPEX, and the real network CAPEX was flat in the year and still well below 14% of revenues.

Alexandre Roncier: Okay, great, thank you.

Operator: The next question comes from the line of David Vagman from ING, please go ahead.

David Vagman (ING): So, good afternoon, everyone, and thanks for taking my question. And sorry to come back on the fibre roll-out, I’m curious to the standalone fibre roll-out. Could you explain us how we should basically model the standalone fibre roll-out until 2025? I think in the past you were referring to 500,000. And then, given the technical change in the definition, should we be somewhat prudent on the take-up phase? So, that’s on fibre.

And then on, secondly, on the Glaspoort JV, so the JV, it’s made some nice progress in 2022. What are the wholesale costs that you have budgeted for, for this year, so 2023? Thank you.

Chris Figee: Yes, so on the fibre roll-out, we've planned for this year, 2024, 2025 and 2026. Like I said, we want to reach the level of 600,000 roughly. We'll see how that works. We are also changing the way we roll out. We go a bit faster, we have improved the customer process to connect households, so we don't need all these steps in between often. And we are also going to do something new and that is to touch high builds, high buildings, to connect. That's also a complete different ballgame compared to the lower build households that, yeah, the SDU steering compared to the MDU steering. And therefore, it's very good not to try to connect 80% of all the households before we start the commercial process.

On Glaspoort, your question is how we distribute roll-out capacity. Now, we have a plan with Glaspoort, which is up to a million households roughly to build for us. And so that's under construction, but that's more ring-fenced. So, that's ring-fenced when it comes to areas, capacity and numbers of households. And the rest of the Netherlands is KPN's own target. So we run it in parallel and especially this year, I would like to upscale KPN's roll-out a bit more.

David Vagman: Okay, thank you. And when you are referring to the 600,000, that's KPN's standalone, excluding Glaspoort's?

Chris Figee: No, no, no, no, that's consolidated. The standalone would be a major trick. So, that is – that's consolidated. It's important for us to look at the plan consolidated because we take the commercial approach consolidated as well.

David Vagman: Okay, thank you. And on the wholesale costs that KPN has to pay Glaspoort?

Chris Figee: Yes, so we pay wholesale broadband access to Glaspoort, like T-Mobile is doing to KPN, for a while and – until we come to the moment of consolidation.

Joost Farwerck: And whatever KPN pays wholesale will be fully in line with the new ACM regulatory framework that's in place. So, KPN is, I would say, almost an ordinary customer in this regards, and we pay according to the ACM framework that Glaspoort has made public.

David Vagman: And I guess it's a bit of a headwind in 2023, given the home passed?

Chris Figee: Yeah, I agree. It's a bit of a funny thing, right? Because we are actually paying those costs out of EBITDA, and we are reconsolidating, as a minority interest, the results below EBITDA. So, it's almost like, until consolidation, Glaspoort is a bit of an EBITDA drag in this regard. I'm not sure whether, in my personal view, the market fully comprehends the value of Glaspoort, but at this point, you're right, up to consolidation, it is a drag on EBITDA and the plus is seen below the line, below EBITDA, which very few people see. That will turn around post-consolidation, but in the mid-term, it is an EBITDA drag. So, that also gives some colour towards what I think is a fair achievement to deliver some growth in EBITDA next year because it actually is some increasing costs.

David Vagman: Okay, thank you. Thank you very much.

Operator: The next question comes from the line of Giorgios Ierodiaconou from Citi, please go ahead.

Georgios Ierodiaconou (Citi): Yes, good afternoon and thank you for taking my questions. The first one is another question on fibre, and I think you mentioned the fact that you are already making the planning for 2024 and 2025. I was curious if you could share with us any indications around costs involved in the roll-out when you engage with some of the subcontractors? Whether there has been any changes because of inflation. I understand there may be a change of mix, but curious if like for like you are seeing any significant changes in terms of the cost of deployment.

And then, another question, it's just a couple of quick clarifications for 2024 to some of the answers that Chris gave earlier. Firstly, around energy, you mentioned that 40% is purchased for 2024 hours. I am curious if you could give us roughly the price at which it was purchased? Maybe you mentioned it, but I missed it.

And then, secondly, when you are discussing earlier the working capital moves and some of the benefits, I was curious to understand which ones may also continue to give incremental benefit in 2024? So, you have the €7 million, which is sustainable for a few year on working capital. Some of the actions you are doing, is it going to be not just sustainable but also enhanced in 2024 versus 2023, the influence that you may see? Thank you.

Joost Farwerck: Yes, so on the fibre planning, I mean, we have a plan until the end of 2026. It is about planning in areas and construction capacity. Of course, with our partners we also negotiate the labour cost and, as you can understand, these go up. With most of the partners, we increase about 5% when it comes to labour.

On the other hand, we also do a lot of innovation on the fibre side by rolling out in a more efficient way, connecting households from the outside instead of the inside. So, listening to all your questions, by the way, I think later in the year, we should do a fibre update for you guys because there's a lot to say about fibre. But we innovate a lot on moving from homes passed to homes connected to homes activated.

We innovate in our commercial approach, so all in all, I am confident that the capacity envelope of €1.2 billion is enough for the coming years and that we can step down after 2026 completing the roll-out for the main part and covering 75-80% of the Netherlands.

Chris Figee: Yes, Georgios, you sneaked in two questions into one, but they are follow-ups, so you are allowed to do it. No, look, on the €7 million on pension, that's probably sustainable for the next, yeah, compared to plan, that's three to four years. At some point, the plan was actually supposed to end because of annual contributions, but we brought it forward. So about €7-8 million free cash flow tailwinds for the coming say three to four years, compared to the plan that I have.

When it comes to energy 2024, we've, as you said, hedged about 38%, on average price of €160 to €170. Obviously, we started buying it also quite early last year and even a bit before that. So, that means at this point in time it feels that, with today's prices and 2023 and 2024, that the energy bill for 2024 will not rise materially towards 2023. The average price we're paying for 2024 is about the average price of 2023, is equal to the average price in the spot market today and is equal to the average price in the forward market for 2024. So, in a situation, they are all aligned, which actually means that for 2024, if prices stay where they are, you will see energy prices being flat or being slightly less even than 2023.

Now, what does that mean for 2024 and cash generation? Coming back to your first question, the third part actually, the third question you sneaked in on working capital, the measures we took this year are one-off, you can change – or you can invoice earlier, that's often a one-off measure. There could be some spill over into next year, but I always find two things; one is the more you look at, the more new ideas you find. So, of course, increasingly, it becomes marginal, but I think the measures we take this year will predominantly, in 2023, small spill over in 2024 and then we have to come up with new ideas. But those expected 2024 that the increase in EBITDA will be the leading factor increase in our free cash flow again.

Of course, it depends on how the world develops. If energy prices stay where they are, I think we should be able to resume the increase, the delta in EBITDA that was paused with €5-10 million or so in 2023, but it will be larger next year.

Georgios Ierodiaconou: Excellent, thank you.

Operator: The last question comes from the line of Keval Khiroya from Deutsche Bank, please go ahead.

Keval Khiroya (Deutsche Bank): Thank you. I've got two questions. So, firstly, the price increases that you've talked about, but do you think the Dutch market can also sustain front book price increases on important tariffs like mobile unlimited and fixed broadband? I note some of the lower mobile tiered tariffs have nudged up slightly.

And then secondly, can you comment at all on how we should think about personnel expenses in 2023? Is there any room for declines given you have a new CLA agreement too? And I guess there may be some workforce reductions beyond that. Thank you.

Joost Farwerck: Could you please repeat the first question, Keval, we missed the gist of the first one?

Keval Khiroya: Yes, yes, sure. So, you've obviously seen back book price increases in the Dutch markets, but do you think we'll also see front book price increases as well on tariffs like mobile unlimited and fixed broadband? I think some of the lower mobile tier tariffs have nudged up but those haven't as yet.

Joost Farwerck: Well, Keval, when it comes to price increases, we are not increasing back book only, we look at more or less every proposition on its own and then we decide on how to increase. So, for instance, all the legacy is increased much higher than the newest version of what we introduced. And then we show you the blend of 3.5% in internet and 5.8% in mobile. So, it's not that we only focus on back book, we really try to lift up the whole base when we do an increase. Yeah, and your second question?

Chris Figee: Yeah, Keval, on your personnel expenses, it's a very good question because it brings me to a point I'd like to make at the end on our quarterly distribution of EBITDA next year. Personnel expenses, can we bring it down in 2023? Obviously, we've got a CLA increase, which is on average 6%, which is a reasonable – which will cost us €45 million more in terms of total labour spend in 2023. We obviously counter this by reducing our headcount, increasing productivity and using attrition. So, our total personnel spend will not go down. That's – the 6% is too much for that, but we will try to nibble as much away from that increase as we can by increasing efficiency, by using attrition, by looking at smart restructuring certain units of KPN and we continue the path of FTE decline. Last year we declined by about 350 FTEs. I think we should certainly do the same next year to even more, to make sure we continue to increase productivity and counter that.

And, I know that you're asking – you're not asking but I'm now going to use the opportunity to tell it, we want – we've set a 2024 €10 million EBITDA for next year, say €5 million growth,

€10 million growth, that order of magnitude. We feel pretty confident with that number. It could be seen as a bit of a floor, but then again, the distribution will be skewed to the end of the year, it will be back end loaded. Remember in Q1, so this – last year was very good. Q1 2022 was a fantastic Q1, so year-on-year comps will be tough. The energy price will kick in, of course, in Q1 and be earned back during the year. And our CLA will have a first batch starting in February, so the 6% distributed over two rounds and the first batch starting in February.

So, that means that in Q1, expect the headline EBITDA to be declining versus last year. It will be growing ex-energy, but of course, the number that counts is EBITDA where we will see a small decline and that will bring it back up to our growth during the year as, of course, during the year last year, we had these one-offs paid out to the staff that we won't do again. It's all embedded in the CLA. During the year you can see the benefits of our base growth, you can see the benefits of our price increases. So, it's important to note that, while we fully underwrite the EBITDA commitment to the year, it's a floor for 2023, it will be somewhat back-end loaded. It's good to flag that Q1 will probably be a negative EBTIDA number but then will recover during the year. So, I want to make sure that we're all on the same page before we get to that reporting part of the season.

Keval Khiroya: Thank you.

Reinout van Ierschot: Okay. Thank you everyone. If there is any further questions, please contact the KPN Investor Relations team. Have a nice afternoon, bye-bye.

Joost Farwerck: Thank you.

Chris Figee: Thank you.

Operator: Ladies and gentlemen, this concludes today's presentation.

[END OF TRANSCRIPT]