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CREDIT OPINION
6 November 2016

Update

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RATINGS

Telekom Austria AG

Domicile	Vienna, Austria
Long Term Rating	Baa2
Type	LT Issuer Rating
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Telekom Austria AG

Update To Discussion Of Key Credit Factors

Summary Rating Rationale

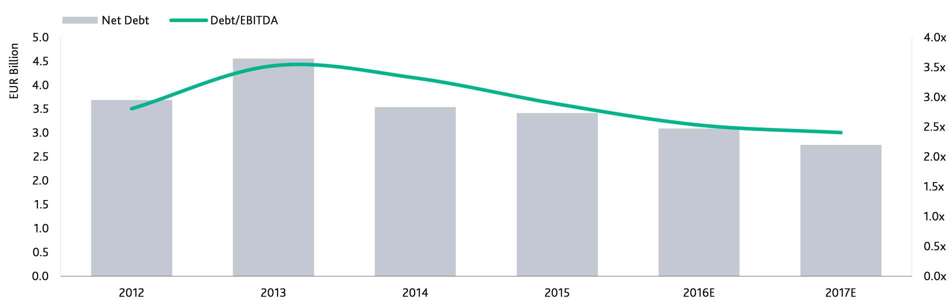
Telekom Austria's Baa2 rating is supported by the group's (1) medium scale; (2) position as a strong integrated player in the Austrian market; (3) geographical diversification in a number of CEE countries; (3) strategic advantage owing to its spectrum portfolio, which enhances its 4G network coverage; and (4) the quality of its network, despite the fact that more capex is needed for the acceleration in the fibre roll out.

Although the rating takes into consideration Telekom Austria's improving operating performance, it also reflects the exposure to macroeconomic conditions, regulatory headwinds and FX risks in CEE countries. Moreover, the rating still factors in some M&A risk as Telekom Austria may explore growth opportunities within its current CEE footprint.

The rating also factors in management's willingness to preserve the group's financial strength and public commitment to an investment grade rating. In addition, we also consider the benefits resulting from America Movil, S.A.B. de C.V.'s (America Movil: A2 negative) shareholding in Telekom Austria.

Telekom Austria is 28.42% owned by the Austrian government. As a government-related issuer (GRI), its Baa2 rating currently benefits from a one notch uplift owing to government support. Telekom Austria's baseline credit assessment (BCA), a measure of its standalone credit quality, is baa3.

Exhibit 1
Gross Leverage Is Expected To Stabilize Over 2016-2017
Net Debt & Debt/EBITDA Ratio Evolution



[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations
Source: Moody's Financial Metrics™ & Moody's Estimates

Credit Strengths

- Leading market positioning albeit in challenging operating environments
- Ongoing stabilization in operating performance
- Adequate liquidity profile
- Continued commitment to an investment-grade rating
- Strong implicit support from America Movil

Credit Challenges

- Regulatory & FX headwinds in Eastern European countries
- Very competitive domestic market
- High capital intensity as a result of acceleration in fibre roll-out
- Event risks

Rating Outlook

The stable rating outlook reflects our expectation that Telekom Austria will gradually continue to improve its operating performance in spite of macroeconomic, regulatory and competitive challenges in a number of markets. The outlook also factors in our expectation that management will preserve the company's financial strength within the publicly stated ratio guidance.

Factors that Could Lead to an Upgrade

We could consider upgrading Telekom Austria's rating if the group's debt protection ratios were to strengthen as a result of improvements in its operational cash flows, assuming no change in the sovereign rating or the levels of government support and default dependence. This would be reflected by, for example, an adjusted retained cash flow (RCF)/gross adjusted debt ratio trending towards 30% and a gross adjusted debt/EBITDA ratio that is lower than 2.8x on a sustainable basis.

Factors that Could Lead to a Downgrade

The ratings would come under downward pressure if (1) Telekom Austria's underlying operating performance were to weaken beyond our expectations as a result of more adverse macroeconomic, regulatory or competitive developments; or (2) the group were to make additional material debt-financed acquisitions and/or increase shareholder remuneration, such that its credit metrics were to deteriorate (reflected in adjusted RCF/adjusted gross debt sustainably below 20% and adjusted gross debt/EBITDA sustainably above 3.3x). Downward pressure could also be exerted on the rating if the group's liquidity profile were to weaken.

In addition, we would most likely no longer apply our GRI methodology to Telekom Austria or incorporate uplift in its final rating if (1) the government were to reduce its stake in the group to below 20%; or (2) we were to lower our government support assumptions for the group. While either one of these factors would likely result in a one-notch downgrade, there is currently no indication that either will occur.

Key Indicators

Exhibit 2
Telekom Austria AG [1]

	12/31/2015	12/31/2014	12/31/2013	12/31/2012	12/31/2011
Scale (USD Billion)	$4.5	$5.3	$5.6	$5.6	$6.2
EBITDA Margin	37.3%	34.2%	32.3%	35.8%	36.9%
Debt / EBITDA	2.9x	3.3x	3.5x	2.8x	2.6x
FCF / Debt	6.4%	1.9%	-15.8%	3.5%	3.3%
RCF / Debt	28.6%	26.0%	24.3%	27.4%	26.1%
(FFO + Interest Expense) / Interest Expense	7.1x	6.7x	6.6x	7.4x	7.7x
(EBITDA - Capex) / Interest Expense	3.3x	2.6x	-2.3x	3.6x	3.6x

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations
Source: Moody's Financial Metrics™

Detailed Rating Considerations

Continued Commitment To An Investment-Grade Rating And Stronger Financial Profile Following America Movil's Take Over

Telekom Austria has publicly stated that maintaining an investment grade rating remains a key priority for the group. Management has implemented a number of actions to enhance its financial flexibility, including (1) accelerated cost-cutting initiatives; (2) a moderate shareholder remuneration policy, recently updated as a consequence of an improvement in operating performance (from EUR0.5 to EUR0.20 per share); and (3) capital structure strengthening through the issuance of hybrid bonds.

America Movil, as major shareholder of Telekom Austria with a 59.7% share, was instrumental in this process. As part of the shareholder agreement, Telekom Austria successfully completed a capital increase back in November 2014 which amounted to EUR1 billion. This improved Telekom Austria's capital structure and financial position, and provided additional financial flexibility for investments. In July 2016, America Movil agreed to reduce its stake in the company to 51% in order to increase the free float.

Leverage (measured by gross adjusted debt/EBITDA) declined from 3.3x in 2014 to 2.9x in 2015. We expect leverage to continue to reduce in 2016, reaching around 2.5x by the end of the year. The publicly announced intention to grow via M&A in the existing footprint may slow Telekom Austria's deleveraging profile. Nevertheless, we anticipate that any potential transaction would be funded within the tolerance levels for the current Baa2 rating category.

Leading Market Positions, Albeit In A Challenging Competitive Environment

Telekom Austria holds a stable leading position in the domestic mobile market with a reported market share of 39.7%. In the fixed broadband segment it reported a 57.6% market share as of September 2016.

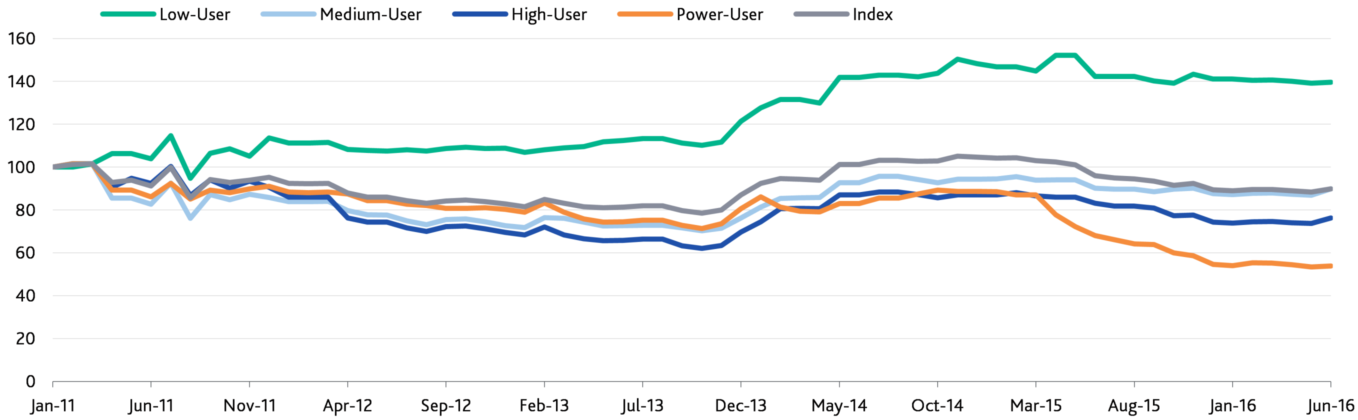
Nevertheless, the Austrian mobile market is mature, with a mobile penetration rate of 154.8% as of December 2015. After some early signs of market repair following the merger between Hutchison 3G (a subsidiary of CK Hutchison Holdings Limited (A3 stable)) and Orange Austria (unrated) in January 2013, renewed pressures have appeared. This has been mainly driven by mobile virtual network operators (MVNOs) such as HoT (unrated), UPC Austria (a subsidiary of UPC Holding B.V. (Ba3 stable)) and Mass Response (unrated), which have launched aggressive offers. Telekom Austria has mitigated price and revenue pressures by introducing cost efficiency measures and protecting existing tariff structures.

As per Exhibit 2, mobile prices in Austria appear to have bottomed out, although competition remains strong in the budget segment of the market. We anticipate this development to continue into 2017 with price pressures from MVNOs in the pre-paid customer segment. In the premium segment, operators are likely to focus on customer upselling strategies rather than on promotions to gain market share.

Exhibit 3

Mobile Prices In Austria Appear To Have Bottomed Out

Austria: Mobile Price Index (January 2011=100)



Source: Rundfunk Und Telekom Regulierungs

Telekom Austria is also one of the leading mobile operators in Bulgaria, with a reported 38.3% market share, in Croatia with a reported 36.4% market share, and in Belarus with a reported 43% market share as of September 2016. Nonetheless, the group has shown a weaker performance in international markets owing to macroeconomic headwinds in CEE, currency depreciation in Belarus and fierce competition in Bulgaria, Slovenia, Macedonia and Serbia.

High Capital Intensity As A Result Of Investments In Fibre And 4G Leads To Strategic Advantage Over Competitors

The company's key areas of investment include the expansion of its LTE mobile network across its markets and the acceleration of the fibre rollout in Austria.

Since November 2014, the company is developing LTE carrier aggregation (which can double the speeds up to 300Mbps from 150Mbps) in selected urban areas.

Telekom Austria is also adapting its fixed network infrastructure to meet the growing demand for high-bandwidth broadband solutions. The current standard product offers data speeds of 8Mbps to 16 Mbps. However, Telekom Austria is increasing its investments by EUR400 million over the period 2015-2018 with the target to provide bandwidths of 30Mbps for over 70% of Austrian households (2015: 40%). Notably, through the introduction of the hybrid modem – a technology which combines fixed line and mobile network to increase bandwidth - current household coverage for a 30Mbps speed is already available in 78% of Austrian households. 50Mbps: 60%). We note that this technology development will be key (1) to meet increasing demand for high-bandwidth speeds through the current fixed and mobile network; (2) to maintain a competitive edge with cable operators, and (3) to upsell current ADSL products.

We expect Telekom Austria's capex will remain high at around 18%-19% over sales (EUR750 million-800 million per year) over the next 2 years.

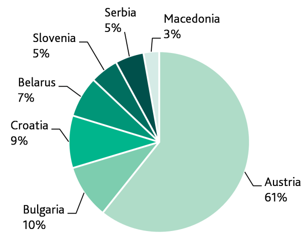
Early Signs Of Stabilisation In Operating Performance

In the nine months ended September 2016, revenues decreased by 0.3% on a pro-forma basis, with higher equipment sales offsetting the negative impact of roaming. EBITDA was up 2.1% over the period thanks to cost reductions and one-off items. FX headwinds in Belarus continued to represent a drag on revenues and EBITDA, which were negatively impacted by EUR71.7 million and EUR34.5 million, respectively.

Exhibit 4

Approximately 39% and 34% of Telekom Austria's Revenues and EBITDA, Respectively, Are Generated Outside Of Austria

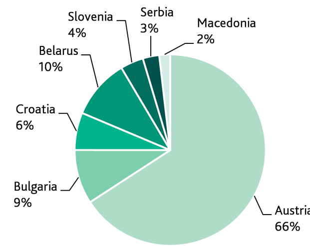
Revenue Breakdown By Segment (First 9 Months 2016)



Source: Company Data

Exhibit 5

EBITDA Breakdown By Segment (First 9 Months 2016)



Source: Company Data

The domestic operations experienced positive revenue growth in the first nine months of 2016 (+0.6%) as higher levels of subsidies compared to the previous year drove a stronger level of gross adds. We expect this positive trend to continue into 2017 as Average Revenue per Fixed Line (ARPL) is likely to grow.

Bulgaria's market continues to be challenging: higher equipment sales together with improving performance in fixed-line did not offset the continued macroeconomic and competitive pressures (especially in the business segment where pricing continues to be aggressive).

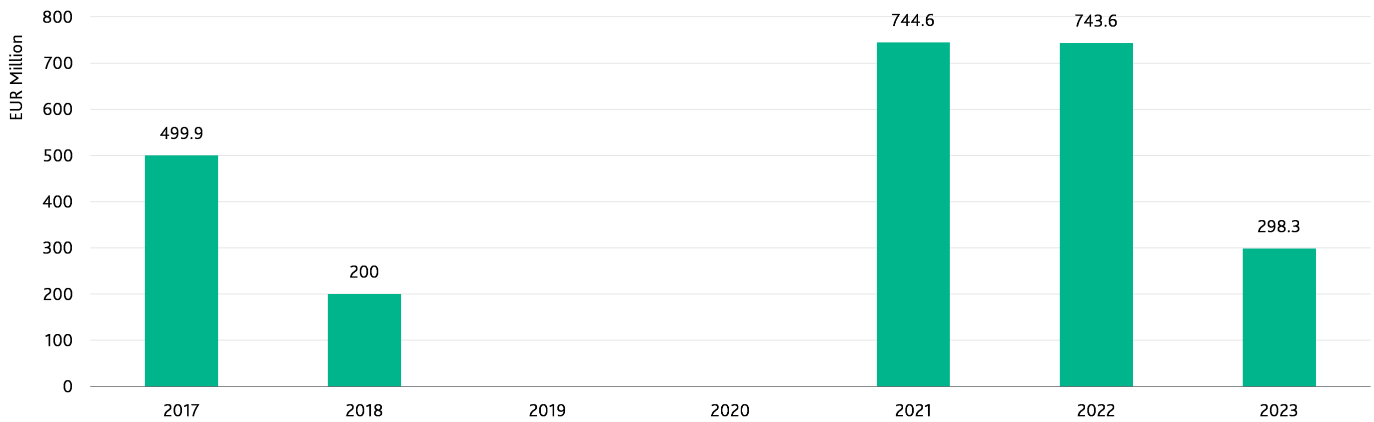
Liquidity Analysis

As of September 2016, Telekom Austria had approximately EUR67.5 million of cash and cash equivalents. In addition, it had EUR1 billion of committed credit lines. These facilities are currently unused and can be drawn at any time. They are not subject to material adverse change clauses or financial covenants.

Telekom Austria's liquidity profile is sufficient to cover its upcoming debt maturities as well as other cash demands. In this regard, we currently expect Free Cash Flow generation (after capex and dividends) over the next 12/24 months to be around EUR200 million - 250 million. The company's fixed average weighted bond coupon is 3.7% with an average maturity of 4.35 years at end of October 2016.

Over the first nine months of 2016, the company repaid a EUR750 million bond and EUR155.3 million worth of long-term bank debt. Upcoming debt maturities include a EUR500 million bond maturing in January 2017 and a EUR200 million bank loan maturing in November 2018.

Exhibit 6
Next Bond Maturity Will Take Place in January 2017
Telekom Austria's Debt Maturity Profile



Source: Company Data

Structural Considerations

Junior Subordinated Instrument Rating

The Ba1 rating of Telekom Austria's hybrid debt is two notches below the company's senior unsecured rating of Baa2. This rating differential reflects the fact that it (1) is a perpetual instrument; (2) is very deeply subordinated; (3) provides Telekom Austria with the option to defer coupons on a cumulative basis; (4) has no step-up prior to year 10 and none beyond 100 basis points (bps) thereafter; and (5) has a 500 bps step-up upon a change of control, in which event all senior creditors will be repaid first.

Profile

Telekom Austria AG (Baa2 stable) is the leading integrated telecommunications provider in Austria, providing 2.2 million fixed-line voice connections, over 1.5 million fixed-line broadband connections and serving 5.9 million mobile customers. The group has a nationwide presence, delivering a full range of services and products, including telephony, data exchange, interactive content, TV and information and communications technology (ICT) solutions. The group has also expanded its mobile operations into Central and Eastern Europe (CEE), where its customer base accounts for more than 14.8 million subscribers. Telekom Austria is one of the leading mobile operators in Bulgaria (through its subsidiary Mobiltel), Belarus (Velcom) and Croatia (Vipnet), and is also present in Slovenia (Si.mobil), Macedonia (Vip operator), Serbia (Vip mobile) and Liechtenstein (Telecom Liechtenstein).

Telekom Austria's main shareholders are América Móvil (A2 negative), with a 51% holding (fully consolidating Telekom Austria) and the Austrian government, with a 28.42% holding.

Rating Methodology and Scorecard Factors

Rating Methodology Grid

The Baa2 grid outcome is in line with the final rating assigned, and one notch higher than the underlying baseline credit assessment (baa3). The difference reflects the competitive operating environment in which the company operates, as well as headwinds in CEE countries and event risk. The final rating benefits from one notch uplift owing to government support.

We expect that Telekom Austria's credit metrics will remain broadly stable over the next 12 to 18 months. Over the same period, we expect a low single digit increase in revenues, in light of signs of stabilization in the Austrian market and growth coming from CEE countries. The group's EBITDA margin is expected to remain broadly stable in the 35-37% range. We expect adjusted RCF/debt in the 29%-31% region and free cash flow/debt between 4% and 6%, owing to the higher dividend policy and sustained capex levels. We also anticipate funds from operations coverage around 7.5x/8x and (EBITDA - capex)/gross interest expense in the 3x-3.5x range. In terms of leverage, adjusted net debt to EBITDA is likely to stabilize around 2.4x-2.6x.

Government-Related Issuer (GRI) Considerations

Given Telekom Austria's 28.42% owned by the Austrian government, the company is considered a government-related issuer (GRI) under our methodology.

As such, we consider the following inputs:

1) A BCA of baa3, reflecting Telekom Austria's underlying credit strength

2) The local currency rating of Austria (Aa1 stable)

3) The moderate default dependence, reflecting the financial and operational links between the group and the Austrian economy.

4) We have factored into Telekom Austria's rating a moderate level of government support based on the following considerations: (1) There is no explicit expression of support by the government, i.e., the government does not guarantee the debt of the GRI, (2) The government's 28.42% ownership of Telekom Austria and its willingness to behave as a rational shareholder might suggest that the government would be unlikely to be the sole provider of support. Instead, it would only consider providing support jointly with other shareholders in the form of a capital increase; (3) There are EU policy barriers to the provision of direct financial support and the government is likely to obey these rules; (4) We consider the Austrian government's historical approach to be moderately interventionist. The government reviews and supervises Telekom Austria's business and funding plans, which we consider positive relative to support assumptions, and appoints a number of board members; (5) In our view, it is unlikely that the Austrian government's good reputation would be damaged in the event of a default by Telekom Austria; and (6) Given its large workforce, the group's level of economic and social importance to Austria appears to be high, despite its strategic importance having diminished over recent years owing to the increasing presence of viable, privately owned competitors with significant market share.

Exhibit 7

Methodology Grid

Global Telecommunications Industry Grid [1][2]	Current FY 12/31/2015		Moody's 12-18 Month Forward View As of 11/4/2016 [3]	
Factor 1: Scale And Business Model, Competitive Environment And Technical Positioning (27%)	**Measure**	**Score**	**Measure**	**Score**
a) Scale (USD Billion)	$4.5	Ba	$4.6 - $4.7	Ba
b) Business Model, Competitive Environment and Technical Positioning	A	A	A	A
Factor 2: Operation Environment (16%)				
a) Regulatory and Political	Baa	Baa	Baa	Baa
b) Market Share	A	A	A	A
Factor 3: Financial Policy (5%)				
a) Financial Policy	Baa	Baa	Baa	Baa
Factor 4:Operating Performance (5%)				
a) EBITDA Margin	37.3%	Baa	35% - 37%	Baa
Factor 5: Financial Strength (47%)				
a) Debt / EBITDA	2.9x	Ba	2.4x - 2.6x	Baa
b) FCF / Debt	6.4%	Ba	4% - 6%	B
c) RCF / Debt	28.6%	Baa	29% - 31%	Baa
d) (FFO + Interest Expense) / Interest Expense	7.1x	A	7.5x - 8x	A
e) (EBITDA - Capex) / Interest Expense	3.3x	Ba	3x - 3.5x	Ba
Rating:				
a) Indicated Rating from Grid		Baa2		Baa2
b) Actual Rating Assigned				Baa2
Government-Related Issuer	**Factor**			
a) Baseline Credit Assessment	baa3			
b) Government Local Currency Rating	Aa1			
c) Default Dependence	Moderate			
d) Support	Moderate			
e) Final Rating Outcome	Baa2			

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations
[2] As of 12/31/2015
[3] This represents Moody's forward view; not the view of the issuer; and unless noted in the text, does not incorporate significant acquisitions and divestitures

Source: Moody's Financial Metrics™

Ratings

Exhibit 10

Category	Moody's Rating
TELEKOM AUSTRIA AG	
Outlook	Stable
Issuer Rating	Baa2
Senior Unsecured MTN -Dom Curr	(P)Baa2
Jr Subordinate -Dom Curr	Ba1
Other Short Term -Dom Curr	(P)P-2
TELEKOM FINANZMANAGEMENT GMBH	
Outlook	Stable
Bkd Senior Unsecured -Dom Curr	Baa2
Bkd Other Short Term -Dom Curr	(P)P-2

Source: Moody's Investors Service

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