

Swisscom Group 2002 Annual Report:

## Swisscom reports stable operating income despite unfavorable climate

	2001	2002	Change
Net revenue (in CHF millions)	14,174	14,526	2.5%
EBITDA before exceptional items (in CHF millions)	4,409	4,413	0.1%
EBIT before exceptional items (in CHF millions)	2,235	2,408	7.7%
Net income (in CHF millions)	4,964	824	-83.4%
ADSL accesses (at 31.12.)	33,379	195,220	484.9%
Number of mobile customers (at 31.12 in millions)	3.37	3.60	6.9%
Number of full-time equivalent employees (FTEs) at 31.12	21,328	20,470	-4.0%

**The Swisscom Group continued to steer a successful course in 2002 despite an unfavorable economic climate. Expectations were fulfilled, with revenue rising 2.5% to CHF 14.5 billion, operating income before exceptional items, depreciation and amortization (EBITDA) remaining stable at CHF 4.4 billion, and EBIT (before exceptional items) up 7.7%.**

**In spite of the continuing difficult environment Switzerland's leading telecoms company expects operating income (EBITDA) for fiscal 2003 to remain unchanged.**

In 2002 Swisscom succeeded in growing revenue and EBIT (before exceptional items) in the face of a difficult environment. As in the previous year, net income was influenced by an impairment charge of CHF 702 million booked against the goodwill of debitel (2001: CHF 1,130 million). debitel was revalued on the basis of a value of EUR 10 per share. The impairment resulted from a further decline in future expected growth in the mobile communications market.

In 2001, operating income (EBIT) was significantly influenced by two further exceptional items: the disposal of a 25% stake in Swisscom Mobile AG to Vodafone and the sale of real estate, resulting in gains of CHF 3,837 million and CHF 568 million respectively. Excluding these exceptional items and the impairment charge booked against the goodwill of debitel, operating income (EBIT) rose on a like-for-like basis by 7.7% due to lower depreciation and amortization charges.

Financial expense of the Swisscom Group decreased by CHF 254 million in 2002 to CHF 517 million as a result of impairments on financial assets in 2001 of CHF 418 million. In 2002 the expense item includes CHF 111 million relating to the impairment of Swisscom's investment in Infonet Services Corp. and CHF 41 million relating to its shareholding in Swiss International Airlines.

Due to these special effects, net income in 2002 fell from CHF 4,964 million to CHF 824 million. For the 2002 financial year, net earnings per share stand at CHF 12.18, while net earnings per share adjusted for exceptional items is CHF 19.92. With net debt of CHF 642 million and a year-end equity ratio of 43%, Swisscom's financial position remains extremely sound.

### **Healthy balance sheet enables adjustment to return policy – high returns**

At the General Meeting of Shareholders on May 6, 2003, the Swisscom Board of Directors will propose a dividend of CHF 12 per share (2001: CHF 11) and a par value repayment of CHF 8 per share (2001: CHF 8). Subject to approval of this proposal, par value per share will be reduced from CHF 9 to CHF 1. This will result in a total distribution of over CHF 1.3 billion, corresponding to approximately 5% of Swisscom's market capitalization at the end of 2002.

The continued strength of the balance sheet has allowed Swisscom to adjust its return policy. Until now, Swisscom has distributed approximately half of its net income (after adjusting for exceptional items) as dividend payments to shareholders. The key element of the new policy, which is now in force, is the annual distribution of further freely available funds. The funds available for distribution consist of net cash from operating activities less capital expenditure (on fixed assets and acquisitions) and debt repayments. Distribution will take the form of a dividend amounting, as before, to approximately half of the adjusted net income, a possible share buy-back, or – as is the case this year for the last time – a reduction in par value. A share buy-back need not take place concurrently with the dividend distribution.

The new return policy is based on a continuing solid Swisscom balance sheet combined with high earning power. The pay-out can be made without significantly changing balance sheet relations in the next few years while at the same time retaining high flexibility with regard to capital expenditure and acquisitions.

**Proposal for the election of three new members to the Board of Directors**

Three members of the Swisscom Board of Directors will be standing down at the forthcoming Shareholder's Meeting: Franco Ambrosetti, Ernst Hofmann and Gerrit Huy. Swisscom extends its thanks to the three retiring members for the services they have rendered over the past five years. The following persons are proposed for election to the Board: Michel Gobet, from Villarsel-le-Gibloux (Switzerland), residing in Neuchâtel (Switzerland), Torsten Kreindl, from Austria, residing in Munich (Germany), and Richard Roy, from Germany, residing in Dreieich (Germany). Michel Gobet is currently Secretary of the Communications Union and has been proposed as successor to Ernst Hofmann as employee representative. Torsten G. Kreindl is a business engineer and partner of the American venture capital company Copan in Munich. Richard Roy, who has a degree in engineering, was until last year Vice President for Corporate Strategy at Microsoft and today works as an independent management consultant.

**Pension fund coverage approximately 94%**

Swisscom contributes to comPlan, a defined benefit plan, which provides retirement benefits for its employees in Switzerland. ComPlan covers the risks of old age, death and disability in accordance with Swiss pension legislation. At December 31, 2002, the pension plan was underfunded by approximately CHF 300 million, which corresponds to a funding ratio of 94% under Swiss law. Initial measures have been taken to improve the difficult financial situation of comPlan. For example, since the beginning of 2003 the interest on retirement savings capital (dual pension plan) has been reduced to 3.25% for employees leaving the plan. The interest rate for other insured members will be defined at the end of 2003. The situation at comPlan will be reviewed until the middle of 2003 and where necessary further measures will be initiated.

As an expression of thanks for their services and as an incentive for the future, Swisscom is offering employees up to 10 shares on preferential terms. The Board of Directors has also approved a share/option scheme for middle and senior management. As part of the employee performance share plan and the share/option scheme for middle and senior management, Swisscom will purchase up to 65,000 shares (less than 0.1% of the outstanding shares) on the open market.

**Outlook for 2003: Expansion of PWLAN activities in Europe and stable Group EBITDA**

Swisscom continues to focus on fixed network and mobile communications in Switzerland, where the company has a solid base and is the leader in both market segments. With annual investments of over CHF 1 billion, Swisscom is also ensuring its leading technological edge. In the ADSL area Swisscom is in intensive competition with cable network operators on the last mile. Increased

marketing activities and highly attractive prices led to a sustained ADSL boom in Switzerland with some 200,000 ADSL accesses installed by the end of 2002.

Outside Switzerland, Swisscom is mainly active in debitel and as a minority shareholder of Cesky Telecom a.s. and Infonet Services Corp. Since growth in Switzerland is strongly inhibited by regulation, Swisscom is continually examining ways of strengthening its position in Europe. The emphasis is on cross-border business models for submarkets with an international focus. For example, Swisscom has founded a new company named Swisscom Eurospot with the aim of building a leading position in Europe in the rapidly growing market for Public Wireless LANs (PWLAN): local networks that provide wireless, broadband access to Internet and office solutions.

In view of the current market situation, Swisscom expects pressure on revenue and margins to continue in 2003. Nevertheless, thanks to sustained and consistent cost management the company expects to maintain the same level of operating income (EBITDA) as the previous year.

## Segment reports

**Fixnet** reported slightly lower revenue from external customers of CHF 4,888 million in 2002. Revenue from access rose by 2.2% thanks to the growing number of ISDN accesses and an increase in the monthly charge for ISDN from August 1, 2001. ISDN growth slowed down as a result of the rollout of ADSL and more intense competition from cable network operators. Revenue from national telephony traffic fell 7.1% to CHF 848 million. Substitution by mobile services led to an overall lower volume for this market. This, coupled with the new numbering plan launched in the second quarter of 2002, are the main factors behind the drop in traffic volume. Introduction of a single national tariff for the fixed network on May 1, 2002, has had a slightly negative net effect on revenue.

With increased volumes and lower prices, revenue from international telephony traffic remained stable. Despite the migration of surfing traffic from the local area, revenue from ISP (Internet dial-up) dropped due to increasing substitution through broadband offerings (ADSL) from various carriers. By contrast, traffic volume for Bluewin narrowband services grew due to an increase in customer numbers. Wholesale national reported a rise in revenue due to higher traffic volume as a result of the new numbering plan as well as strong growth in the market for ADSL access. Despite higher volume, Wholesale international revenue grew by only 2.5% as a result of lower average prices. Revenue from International Carriers' Carrier Services dropped by 2.7% as volume declined.

Expenses in the Fixnet segment fell year-on-year by 1.3%. The 2002 figures include CHF 85 million (2001: CHF 35 million) in costs arising from measures to reduce the workforce. The shift from retail to lower-margin wholesale revenue and a decrease in total revenue drove EBITDA down by 4.3%.

**Mobile** increased revenue from third parties by 4.1% year-on-year to CHF 3,255 million. The customer base for voice traffic was further expanded, resulting in a 3.7% increase in revenue. Revenue from data communications rose 24.5% due to the ongoing success of SMS. While strong volume growth was recorded for the GPRS offerings (e.g. MMS (multimedia messaging services) and mobile solutions) launched in 2002, this will significantly impact revenue only in the course of 2003. Wholesale posted a 12.9% drop in revenue, primarily due to increased network coverage by rival carriers and the corresponding reduction in use of the Swisscom network. In 2002 the penetration rate for the Swiss mobile communications market rose to 77.6%. Swisscom Mobile contributed to this market growth in an intensely competitive environment. Market share declined slightly, while the number of subscribers rose by 6.9% to 3.6 million. Customer loyalty measures were deployed to minimize the loss of high-worth postpaid customers to the competition. Year-on-year, average revenue per user and month (ARPU) fell by 4.4%. New customers exhibit lower usage habits than existing customers.

At CHF 2,138 million, segment expenses for Mobile are 1.5% higher than the previous year. The reduction in customer acquisition costs is outweighed by spending on measures to intensify customer loyalty. Moreover, personnel and IT expenses rose as a result of the growth-related expansion of corporate structures. On the other hand, expenses for network operation and maintenance dropped. EBITDA increased by 5.2 % to CHF 1,974 million, with an EBITDA margin of 48.%. EBIT rose accordingly by 6.3% to CHF 1,685 million.

**Enterprise Solutions** reported a year-on-year decline in revenue of 8.1% to CHF 1,365 million. Revenue and volumes for national telephony traffic followed the same pattern as in Fixnet. The reduction in revenue is primarily attributable to the new numbering plan introduced in Switzerland and the single national tariff. The decline in revenue from value added services is mainly attributable to tariff reductions and a loss of certain large customers. Networking posted a 10.3% drop in revenue to CHF 568 million due to weak demand as a result of the economic slowdown. Managed network services suffered from price erosion which failed to be offset by the growing demand for broadband.

Enterprise Solutions succeeded in reducing segment expenses by 6.1% compared to the previous year. Purchases of network services dropped, as reflected by the decline in revenue. While additional savings were made on advertising costs, IT expenses rose. Overall, cost reductions were insufficient to compensate fully for the drop in revenue. EBITDA decreased by 40.4 % to CHF 68 million and EBIT by 55.6 % to CHF 36 million.

**debitel** is the largest network-independent telecommunications company in Europe and the third-largest mobile communications provider in Germany. Despite difficult market conditions, debitel succeeded in growing revenue in Swiss franc terms by 8% in 2002. In the first half-year, mobile

companies in Germany adjusted their customer base by eliminating inactive prepaid customers. For debitel this move resulted in 1.4 million fewer prepaid customers. Thanks to customer loyalty measures, subscriber numbers were significantly increased, particularly in the postpaid area, and exceeded the 10 million mark by year-end. Outside Germany debitel posted double-digit revenue growth, primarily due to acquisitions which strengthened national companies in the Netherlands and France.

The increased revenue for debitel was accompanied by a disproportionate increase in revenue costs. Operating expense increased further as a result of customer loyalty measures and losses in the French hardware business, as well as charges arising from integration of the former Talkline Nederland B.V. At the same time, cost reductions were achieved primarily in the distribution and marketing areas. The number of employees in Germany was reduced by 245 due to process optimization measures. Outside Germany the number of employees remained stable year-on-year despite the acquisition of Videlec S.A. in France. debitel posted a 15% fall in operating income before interest, tax, depreciation and amortization to CHF 159 million as the result of a disproportionate increase in costs.

The **Other** segment primarily consists of the two Group companies Swisscom Systems and Swisscom IT Services. Swisscom Systems is active in the distribution and maintenance of private branch exchanges (PBXs). In 2002 the company was affected by a decline in market volume and falling hardware prices. Revenue dropped by CHF 70 million, representing a year-on-year reduction of 14.7%. Comprehensive restructuring measures and a new business direction were introduced in the year under review. As previously announced, some 470 jobs will be shed in the course of 2003. The CHF 80 million expense associated with this reduction in the workforce was recorded in the 2002 financial statements and, together with the reduction in revenue, resulted in a CHF 143 million drop in EBITDA compared with the previous year. As of December 31, 2001, Swisscom IT Services merged with AGI IT Services and in 2002 posted an increase of CHF 188 million in revenue, primarily due to the business activities brought in by AGI IT Services.

The EBITDA of CHF 111 million is negatively affected on the one hand by costs arising from Swisscom Systems' move to reduce the workforce and by poor performance of its operating business, and positively affected on the other hand by the improved results of Swisscom IT Services. The net outcome is a year-on-year reduction in EBITDA of CHF 25 million.

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