Swisscom “investing for sustainable returns”

Presentation for Vontobel Conference

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1. Big Picture – investing for sustainable returns

A. Telecoms is a <u>fixed cost</u> business

- Capital intensive (Capex)
- Low COGS, high fixed Opex

B. Making money in fixed cost business is about <u>scale and share</u>

- Scale: # customers
- Share: position within market

C. To achieve scale and share requires best <u>network</u> & <u>pricing</u> (differentiation)

- Transparent offers reflecting changing customer demand
- Superb network availability

D. To sustain is about

- Willingness and financial ability to (continue to) invest
- Selecting the right investments from both technology and competition perspective at the right time

E.
FCF generation supported by Capex, Marketshare & Pricing power

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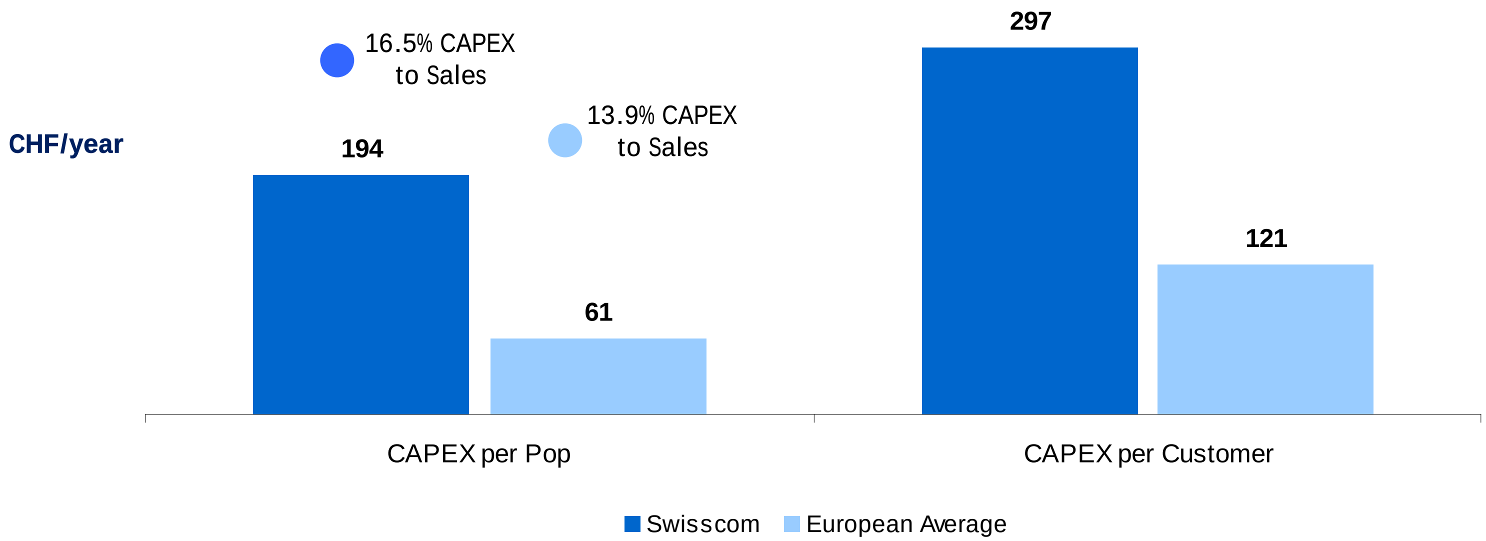
A. Telco, a fixed cost business - Capital intensive (Capex)

Networks by definition constructed to cover an entire country and all inhabitants (pop)



Based on 2011 figures

Domestic

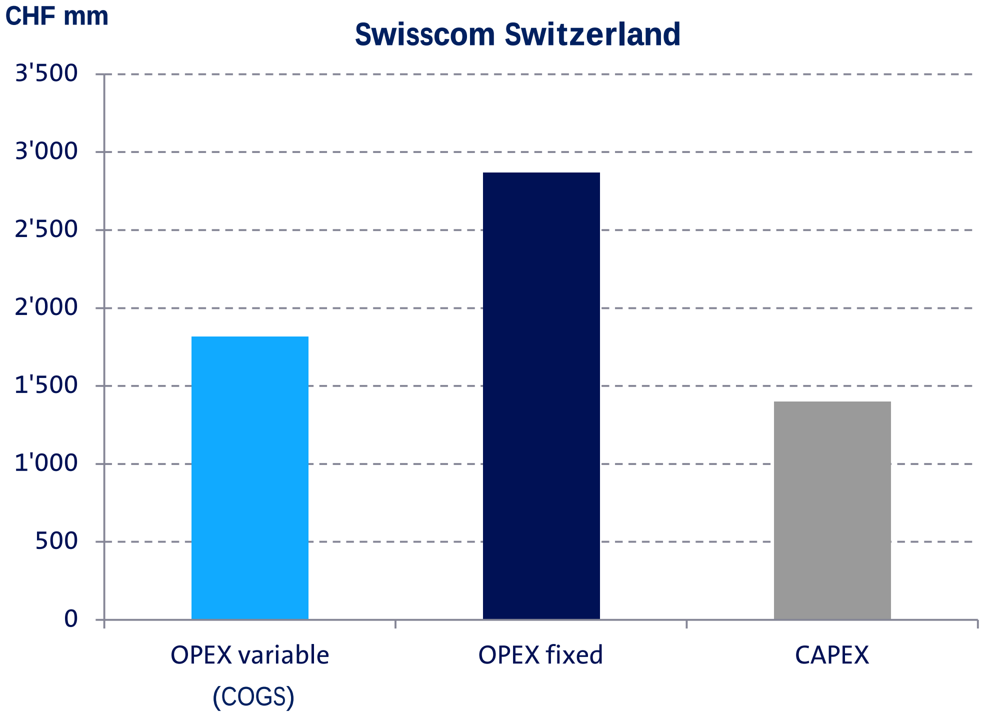
(incumbents only, domestic business)

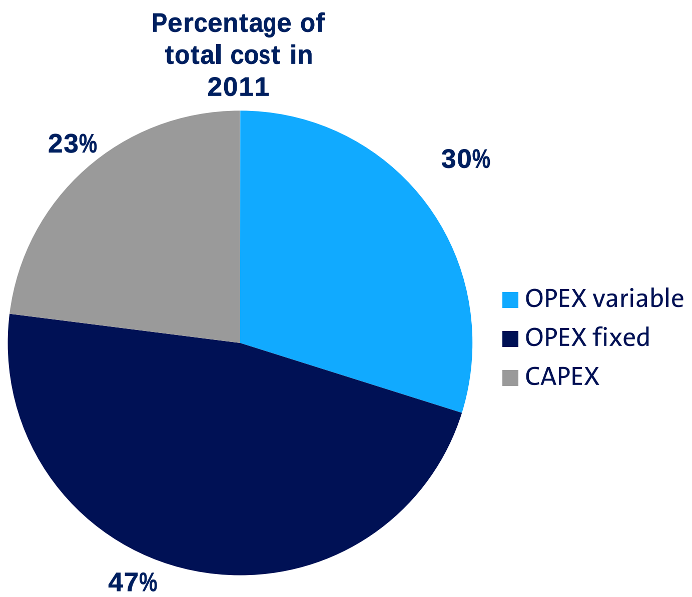
source: Swisscom and broker research

Swisscom invested around 3x more than peers on a Pop basis and over 2x more on a per customer basis. The Capex / Sales is 20% higher than peers, pointing towards the benefits of high market share and premium which can be charged on the back of best network quality

A. Telco, a fixed cost business - Capex & Opex at Swisscom

Operating a network involves mainly fixed, and only limited variable, cash out

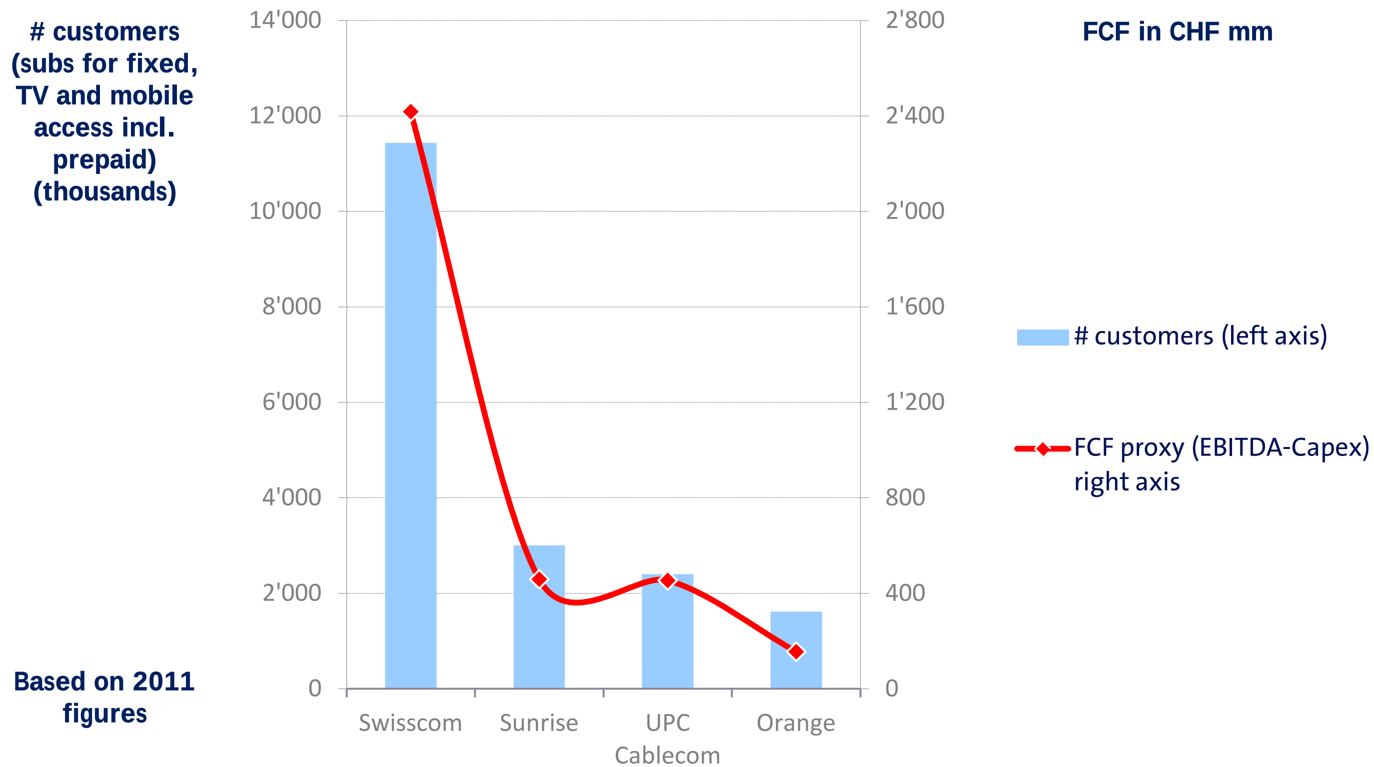




70% of cash out is fixed by nature

B. Making money in a fixed cost business is about scale

Critical mass is crucial with minimum amount of customers to breakeven (on basis EBITDA – Capex) in Switzerland probably at around 1 million



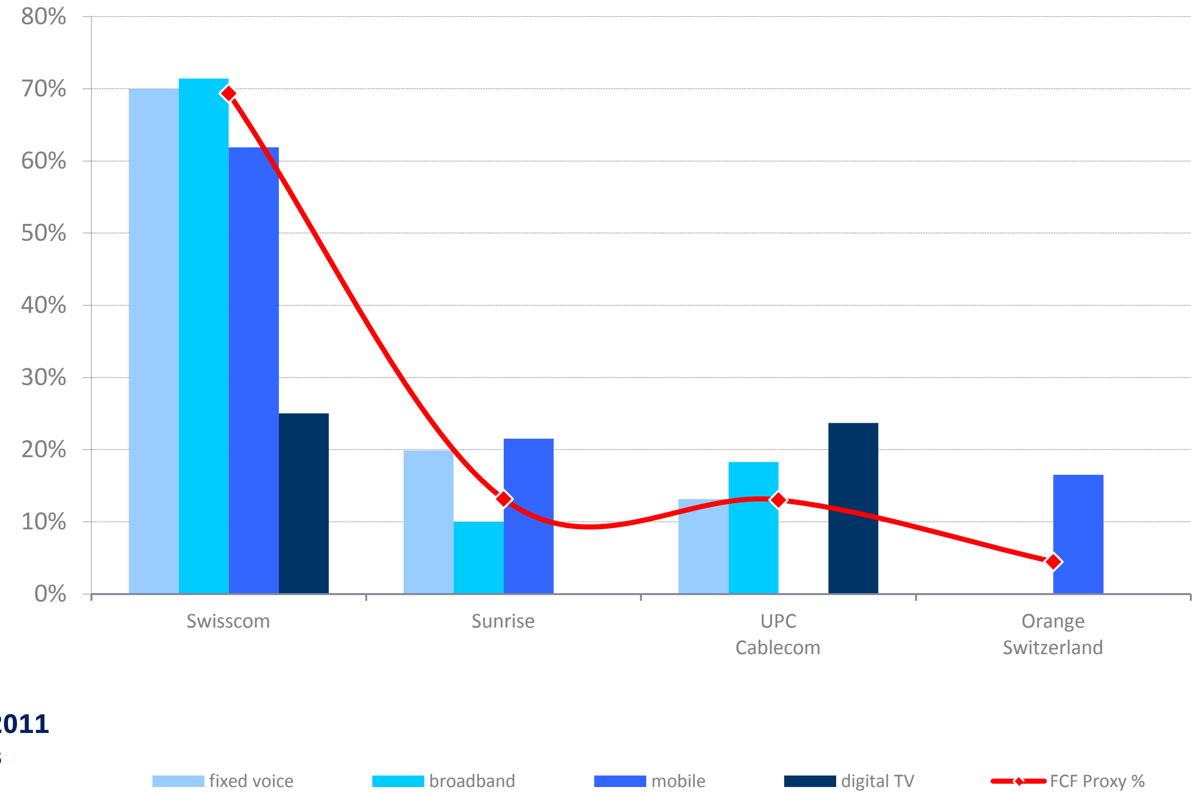
source: Swisscom research

Scale matters, with relative share of FCF higher than customer share

B. Market share is crucial to generate significant FCF

Correlation FCF and Market share in the Swiss market

% market share



Based on 2011 figures

source: Swisscom research

Scale matters, with share of FCF higher than (blended) share of market

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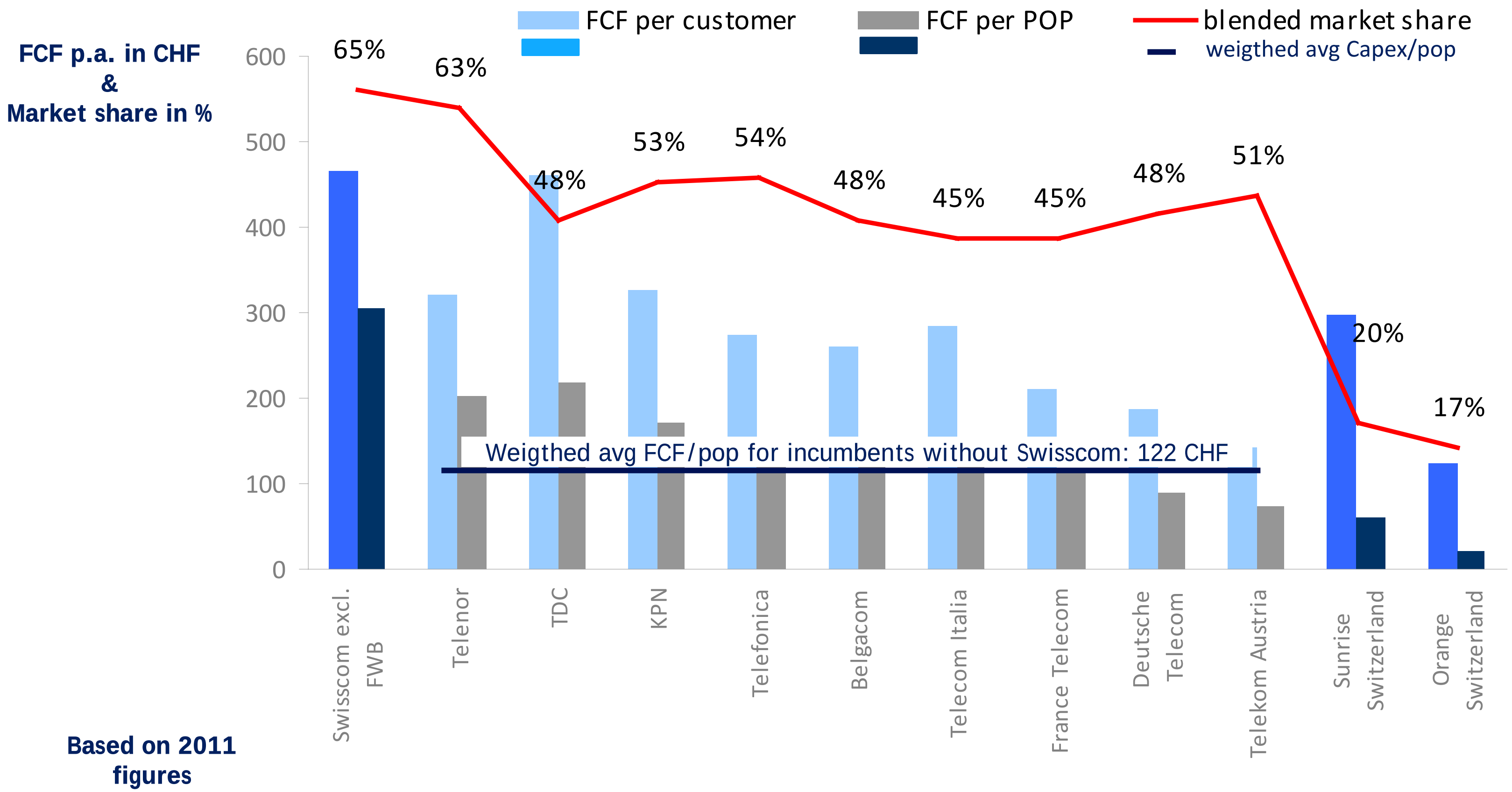
B. Market share and FCF are correlated, also internationally

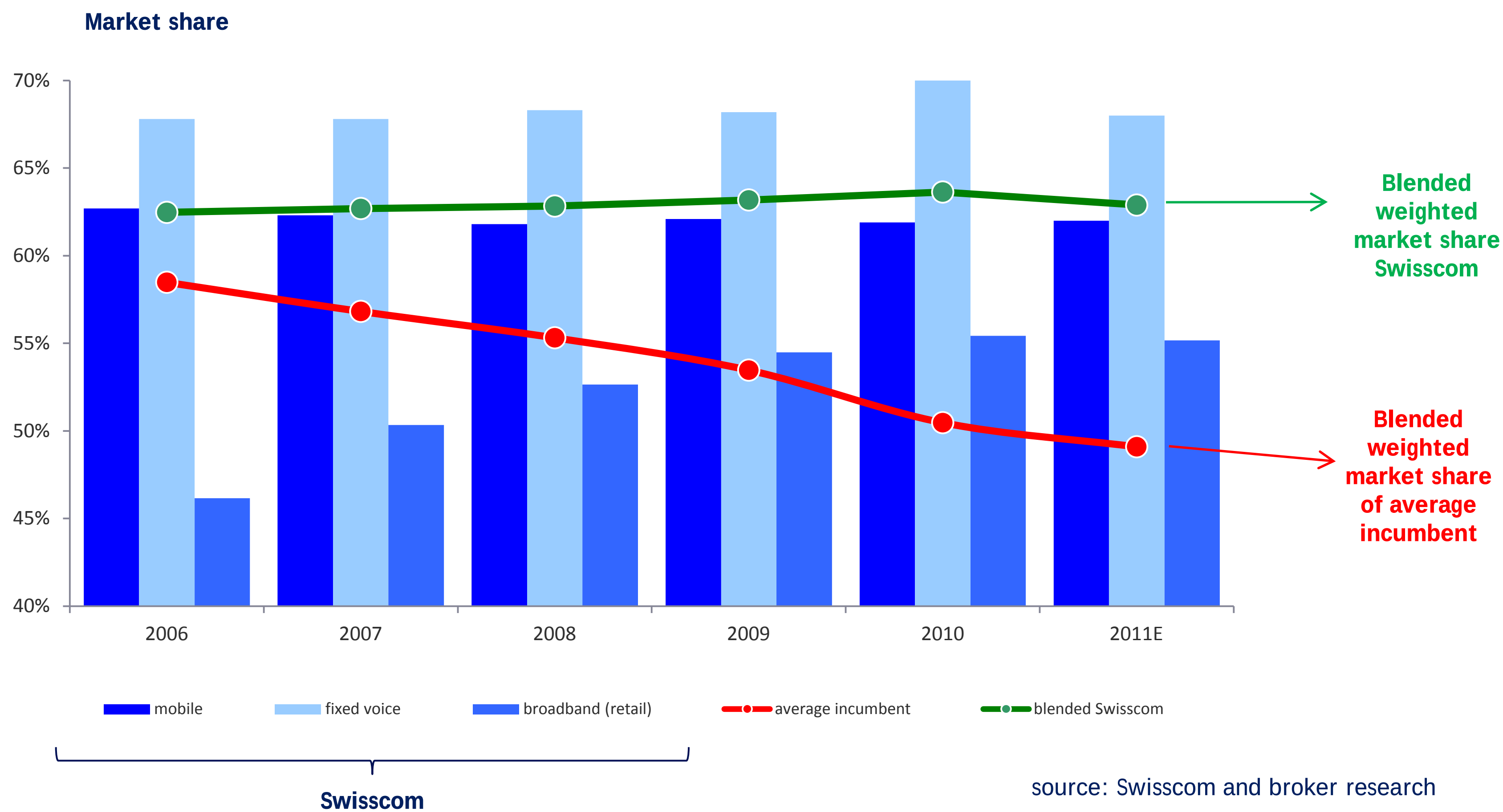
Blended market share in domestic operations versus FCF per pop and per customer



source: Swisscom and broker research

In quite some other countries, the minimum required market share for breakeven will be higher than in Switzerland, considering also large players create less FCF/pop

Swisscom market shares "more than" stable, with gap towards avg. incumbent increasing



source: Swisscom and broker research

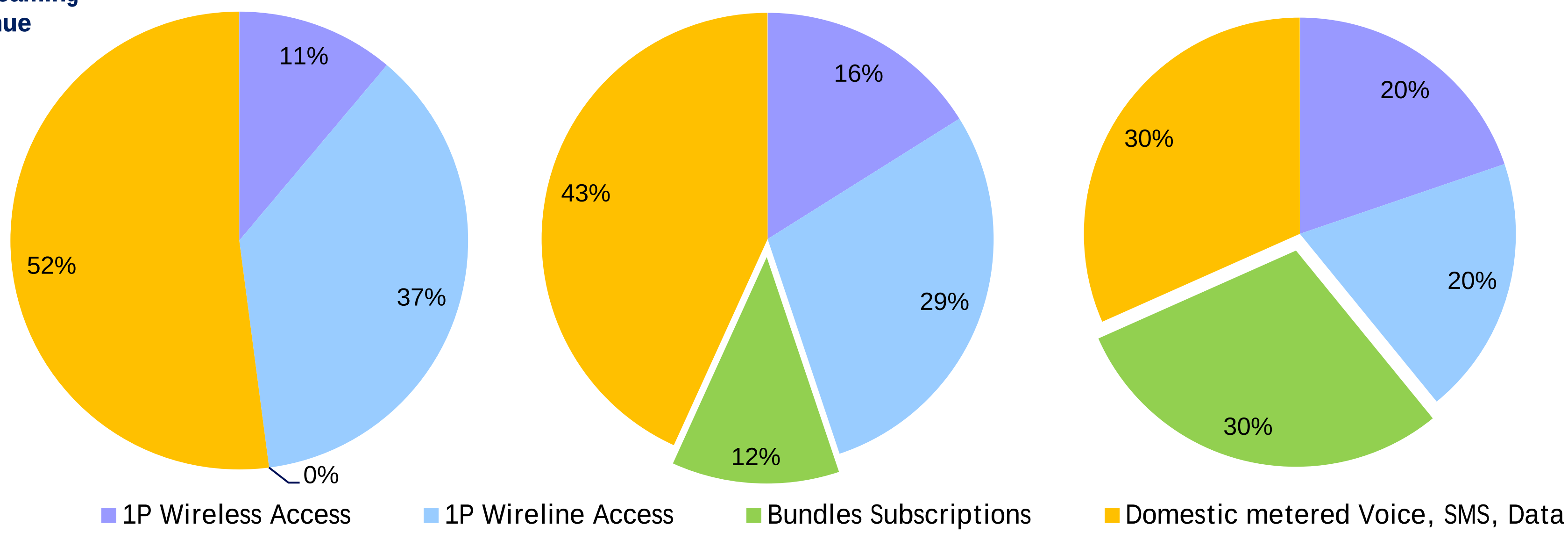
Strategy to invest pays off in terms of market share. Ability to offer bundles (incl. 4P as of lately) helps to cement market share and drive future FCF generation. Part of which again can be used to invest and sustain returns.

C. Customers desire more predictable pricing (less variable)

Do not fight customers' desire to move away from metered revenues, but create bundles which compensate this

Swisscom Switzerland without wholesale and roaming revenue

2008 CHF 5.5 bln | **2011** CHF 5.6 bln | **In around 3 years** ~ CHF 5.6 bln



Revenues from bundles to go from 0 in 2008 to well over CHF 1.5 bln (30% of total) in a few years

Variable metered revenues from >50% in 2008 to around 30% in a few years. Trend to continue. Challenge: to create bundles generating a compensating amount of new revenues. Sofar it worked.

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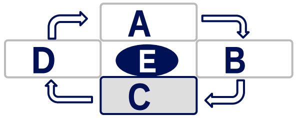


C. Scale and share require best pricing strategy & best network

Pricing differentiation can only be maintained through transparency and superior quality

- **Intuitive pricing should be on "speed" as experienced by customers, not on "data consumed": the average customer has no idea how much data was used, and customers value what they can experience: speed of connection**
- **Differentiating on speed is more sustainable: preempts inroads by OTT providers (e.g. Apps such as "iVoice") and is difficult to replicate by competitors as network quality ensuring the factual delivery of speed must be top-notch**

New mobile price plans from 25 June 2012: offering 5 plans with all-inclusive voice/SMS/data, which differentiate on speed only

	Natel infinity XS	Natel infinity S	Natel infinity M	Natel infinity L	Natel infinity XL
					
Bandwidth (max)	0,2 Mbit/s	1 Mbit/s	7,2 Mbit/s	21 Mbit/s	100 Mbit/s
Price (CHF/month	59	75	99	129	169
Roaming in W-Europe (min. voice,nr SMS, Mb Data)	-	-	30/30/30	100/100/100	200/200/200

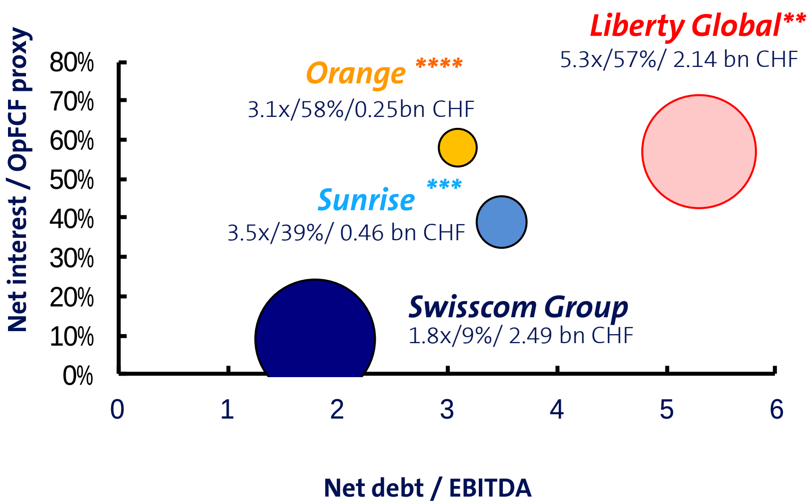
**Swisscom plans to continue investment into best networks, services and availability.
This will ensure market share, which in turn is the precondition for generating surplus FCF**

D. To sustain is about … capacity to invest

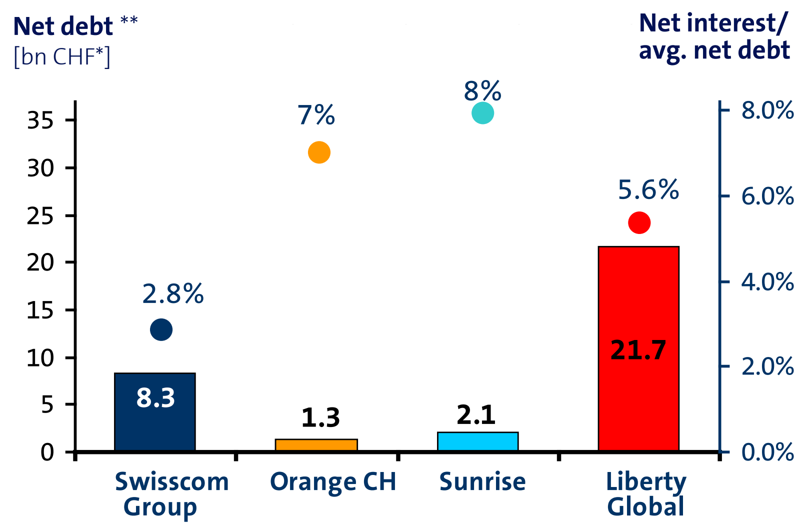
Financial strength compared

Debt/interest ratios in 2011

*Bubble size = OpFCF proxy in bn CHF**



Net debt and avg. cost of debt in 2011



Sources: all figures based on latest publicly available data in reports of Sunrise and Liberty Global (mother company of UPC Cablecom)
**1 USD = 0.94 CHF*
*** Liberty Global assumption: Operating cash flow = EBITDA*
**** Sunrise based on figures as published*
***** Orange CH: estimate derived from publicly available data*

Not just the will, but esp. the ability plays a role in who can stay at the forefront of offering best quality networks & services. With recent changes in ownership in Swiss market, competitors will face more budget constraints than Swisscom – both relatively and absolute – which is a clear window of opportunity. Where Swisscom pays 9% of its FCF in interest, the others pay 39 to 58%….

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D. To sustain is about … Finding the right mix of technologies to invest into – at the right time

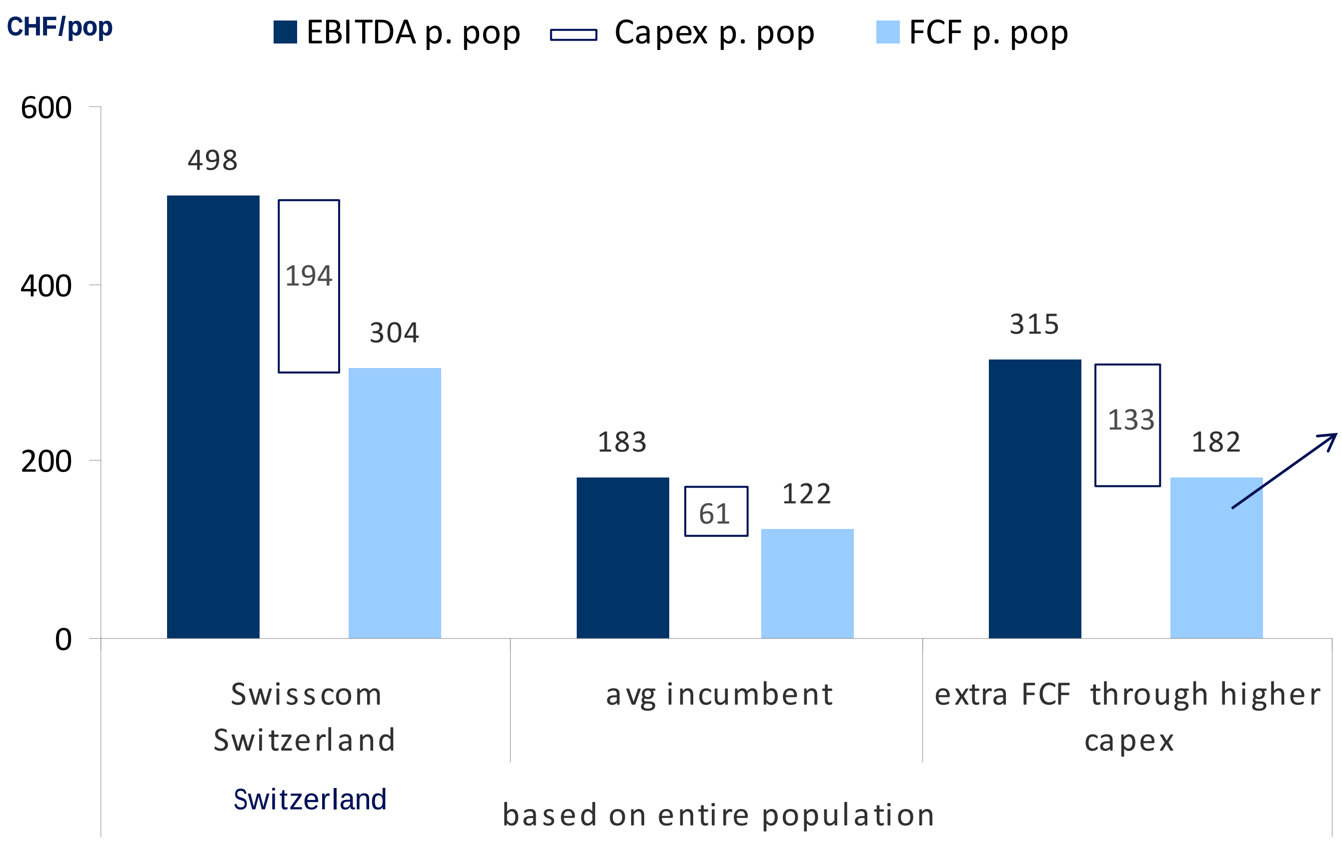
Share	Area	Competition	Current deployment	Potential technologies
0%–30%	Top 20 cities	Utilities as partner	VDSL 8-30 Mbps; FTTC/VDSL 20-50 Mbps; FTTH 100-1000 Mbps	
30%–60%	Smaller cities Agglos	Large CATVs	VDSL 8-30 Mbps; FTTC/VDSL 20-50 Mbps	Vectoring 50-100 Mbps; FTTDP up to 500 Mbps; FTTH 100-1000 Mbps
60%–100%	Rural areas and remote municipalities	Small or no cable operators	xDSL up to 8 Mbps; VDSL 8-30 Mbps; FTTC/VDSL 20-50 Mbps	HSPA+/LTE up to 100 Mbps (shared); Vectoring 50-100 Mbps; FTTDP/(H) up to 500/(1000) Mbps

0% 30% 60% 80% 100%

Finding the right technology mix is a constantly evolving process of optimization. It needs to take account also of competitors' ability and speed of rollout. Swisscom will invest up to CHF 100 mm extra p.a. over the next few years (from 2012) in an extended technology mix and footprint, in order to be ahead of competition, cement future market share, and generate best excess returns.

E. Superior FCF generation from higher Capex and market share

Investments (Capex) done by definition to cover entire country, therefore should be compared with other incumbents on a per pop basis



CHF 182 extra FCF/pop esp. from higher capex (better network justifying better pricing) and higher market share (as a result)

source: Swisscom and broker research

Spending 133 CHF / pop p.a. more than peers leads to higher market share, better pricing and CHF 182 more FCF p.a. per pop : "Capex is a good investment" leading to sustainable returns.

Conclusion - investing for sustainable returns

A. Telecoms is a <u>fixed cost</u> business

B. Making money in fixed cost business is about <u>scale and share</u>

C. To achieve scale and share requires best <u>network</u> & <u>pricing</u> (differentiation)

D. To sustain is about investing in right technology mix at the right time - <u>to drive future FCF generation</u>

E.
FCF generation supported by Capex,
Market share &
Pricing power

In a fixed cost business, size & scale drive incremental FCF. To make this sustainable, offering intuitive pricing differentiation and best networks is key, as this also drives market share. Therefore, continued investment is the most important driver for future cash flow generation.

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