

## Announcement

### Moody's affirms Telekom Austria's ratings; changes outlook to negative from stable (Austria)

Moody's Investors Service has today affirmed Telekom Austria's (TA) A3 senior unsecured and issuer ratings and Prime-2 short-term issuer ratings and changed the outlook on the ratings to negative from stable. The change in outlook is a result of expected further regulatory and competitive pressure on TA's operating margin. This, together with the publicly stated free cash flow distribution policy through 2013, which assumes a full use of free cash flow either for shareholder remuneration or strategic investments whilst maintaining gross reported debt levels just under EUR 4 billion over the next few years, will exert pressure on TA's leverage and RCF/Debt metrics so that any further deterioration in operating performance with no prospects for recovery could result in a ratings downgrade.

#### RATINGS RATIONALE

"TA's rating reflects the government's 28.42% ownership of the group in addition to the following factors: (i) TA's integrated telecoms business model, which allows it to adapt to the developments in the telecoms industry; (ii) management's strategy and tolerance for financial risk, which directly influence debt levels and credit quality; and (iii) its operating margins and liquidity," says Carlos Winzer, a Moody's Senior Vice President and lead analyst for TA. "In Moody's view, TA's future cash flow generation may be limited by: (i) the current economic environment; (ii) sustained price pressure; and (iii) the effect from regulatory induced lower roaming tariffs and mobile termination charges in Austria, Bulgaria, Croatia and Slovenia," adds Mr. Winzer.

TA's ratings are now weakly positioned within the A3 rating category. The rating agency will monitor whether or not during the next few quarters the expected increase in certain mobile and fixed tariffs coupled with the overall economic recovery in Austria mitigates the expected pressure on the company's revenues. A rating downgrade could result from: (i) any deterioration in the group's operating performance; (ii) debt-financed acquisitions beyond free cash flow generation limits; and/or (iii) an increase in shareholder remuneration.

In Moody's view, TA's adjusted debt/EBITDA ratio could deteriorate this year and next year exceeding the 2.5x limit for the current rating and a retained cash flow (RCF)/adjusted gross debt ratio to slightly below 25%. However, an improvement should occur in the medium term.

TA's A3 rating continues to be supported by: (i) the group's scale; and (ii) its position as a strong integrated player in its highly competitive domestic market and a geographically diversified leading mobile operator in Austria and the countries it operates in Eastern Europe. The rating also factors in: (i) TA's continued strong cash flow generation; (ii) its capital structure objective including a reported net Debt to EBITDA between 2.0 and 2.5x; (iii) the group's dividend payout of 55% of free cash flow, and the intention to return excess capital to shareholders if appropriate investment opportunities are not found; (iv) a strong liquidity profile, with a EUR 1 billion committed backup bank facility and no material refinancing needs in 2011; and (v) the understanding that management does not intend to reduce debt in the foreseeable future. The A3 rating currently benefits from a one-notch uplift as a result of the group being government-owned, low dependence and moderate support factors.

A one-notch rating downgrade could occur over the next 12-18 months if further erosion of TA's financial flexibility were to be reflected in weaker debt protection ratios than currently expected (including an RCF/adjusted gross debt ratio sustainably below 25%, and an adjusted debt/EBITDA ratio sustainably above 2.5x), with no prospects for recovery, whether as a result of operational underperformance, a large debt-financed acquisition, or extraordinary shareholder distributions.

In addition, in case of lower levels of support or if the government were to reduce its stake below 20%, although this is very unlikely at this point, Moody's would most likely no longer apply the government-related issuer methodology to TA. This would likely result in a one-notch downgrade.

Conversely, although not currently expected, an upgrade could occur if TA's debt protection ratios were to strengthen as a result of improvements in its operational cash flows and prudent financial policies. Assuming no change in levels of government support and dependence, the rating could come under positive pressure if it was clear that the group would achieve improvements in its debt protection ratios, such as an RCF/debt ratio exceeding 35% and a debt/EBITDA ratio that is lower than 1.5x on a sustainable basis.

Moody's would stabilize the rating if TA experienced some improvement in its operating performance during 2011, which would strengthen the EBITDA in the short term.

Moody's most recent rating action on Telekom Austria was implemented on 14 May 2007, when Moody's affirmed the group's A3 senior unsecured rating and Prime-2 short-term ratings and changed the rating outlook to stable from positive.

The principal methodologies used in rating TA were Moody's "Global Telecommunications Industry Rating Methodology", published in December 2010, and "Government-Related Issuers: Methodology Update", published in July 2010. Both reports are available on [www.moodys.com](http://www.moodys.com). Other methodologies and factors that may have been considered in the process of rating this issuer can also be found on Moody's website.

Headquartered in Vienna, Austria, Telekom Austria is a leading provider of telecommunication services in Austria with 2.3 million fixed voice lines, almost 1.1 million fixed-line broadband connections and serving 5 million mobile customers as of December 2010. TA has a nationwide presence, delivering a full range of services and products, including telephony, data exchange, interactive contents, TV and ICT solutions. The group has also expanded its mobile operations outside Austria, where its customer base accounts for more than 14.2 million subscribers. TA 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. TA reported EUR4.8 billion revenues and EUR 1.8 billion EBITDA as of December 2009.