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**BUSINESS DESCRIPTION**

Hellenic Telecommunications Organization S.A., usually known by its Greek initials OTE, is the dominant telecommunications provider in Greece with a strong presence in south-eastern Europe. It was founded in 1930, originally as AETE and in 1949 OTE was created in order to unify the telecommunications services of Greece. Until 1998 it was exclusively state owned and the telecommunications market was a monopoly. Although, OTE was gradually privatized and since July 2009 Deutsche Telecom became the largest shareholder of the Group. In 2019, DT owned 46% of the company leaving only a remaining 5.7% to the Greek state.

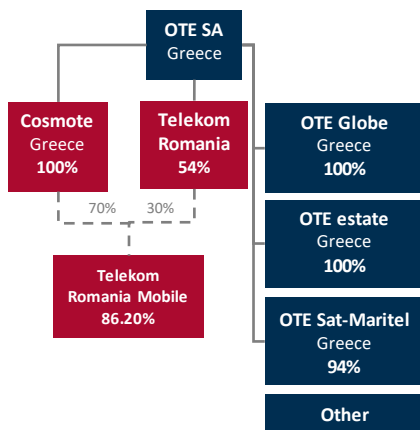
**Geographic and business segments:** The business structure of OTE Group is mainly composed of two segments. Most of the revenues are generated in the fixed segment (56.50%), in which TV services and the wholesale sector (17% of revenues) are included, while the rest is derived from the mobile segment (40.50%) and various other revenues (3%). OTE group, apart from its activity in the Greek market, also has operations in Romania. More specifically, it owns 54.01% of the share capital of Telekom Romania, which was the incumbent telecommunications provider. Also, the group possesses 86.20% of the mobile telephony division of Telekom Romania and until 2018 it had in its portfolio 97.20% of Telekom Albania as well, which was sold for € 50 million. The main revenues are derived from the Greek market, with a proportion of 76% of its total revenues (38.57% in fixed, 24.30% in mobile and 12.87% others). Besides its activity in Greece, in 2018 OTE gained 24% of its revenues from its business exposure in Romania (9.36% fixed and 8.38% mobile and 6.57% others). In terms of profitability, OTE group had a consolidated adjusted EBITDA margin of 34.70% in 2018. Specifically, in Greece the adj. EBITDA margin is 40.9%, +1% from 2017, while in Romania reached 14.6%, after decreasing by -2% from the previous year.

**Products and services offered:** OTE offers a wide variety of telecommunications products and services for homes and businesses. It is a provider of fixed-line and mobile telephony, broadband services, satellite television services and Internet Protocol Television (IPTV). Except for selling these products, it additionally offers bundles (2-play, 3-play), which combine all the above services at a lower price than the sum of the individual parts. An important revenue channel for OTE is the wholesale segment. The wholesale sector consists of two main operations, the first one is the rental of OTE’s network to its competitors and the second regards the ICT projects, in which it provides a large spectrum of telecommunications services adjusted to the needs of businesses. Additionally, OTE participates in the retail distribution services through one of its subsidiaries, GERMANOS. The other subsidiaries of OTE in Greece differentiate from the traditional services, offering a wide range of telecommunications products and services, for the maritime world (OTESAT Maritel) and for professional training (OTE Academy). Moreover, the group has recently established an insurance contract platform called “Cosmote insurance” and a payment service platform, “Cosmote payments”, while the group is also planning to expand in the market of online betting.

Key figures	
Bloomberg Code	HTO:GA
Reuters RIC	OTEr.AT
Share price (18/4/2019)	€ 12.32
Outstanding shares (in millions)	479.94
Market Capitalisation (in billions)	5.95
52w High	€ 12.68
52w Low	€ 9.39

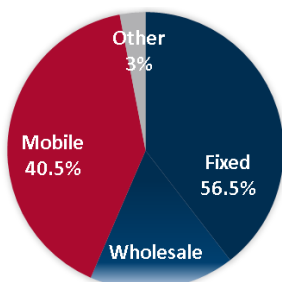
Source: Thomson Reuters Eikon

Figure 1: Group structure



Source: OTE Group reports

Figure 2: Revenues by segment

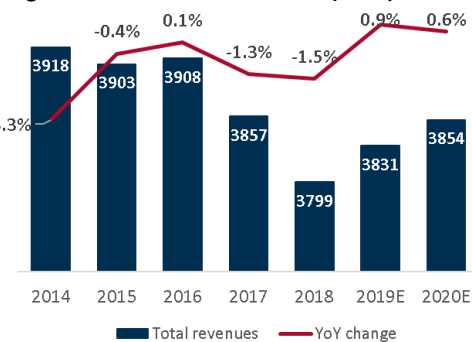


Source: OTE Group reports

**INDUSTRY OVERVIEW & COMPETITIVE POSITIONING**

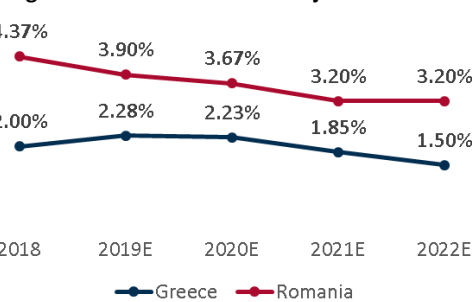
The telecommunications industry in Greece has been relatively steady over the past 3 years in terms of growth. In 2018, the total turnover of the industry reported a marginal increase resulting in a total market size above €5 billion. On the other hand, the Romanian market is characterized by fierce competition and is marked by the recent entrance of an aggressive 4th operator, Digi. Apart from stagnation, an intense delay regarding the penetration of new technologies can be noticed in the Greek telecommunication market creating a large growth margin for all telecommunication companies. Based on our analysis, OTE will manage to grow thanks to four main drivers: 1) the recovering economic environment, 2) increased mobile data consumption 3) higher VDSL and Fiber take up and 4) expansion to other business through its customer base.

**Figure 3: Total Revenues of OTE (€ mn)**



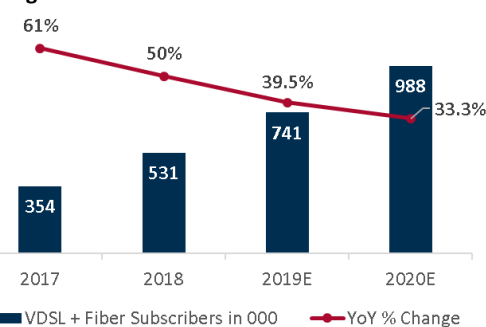
Source: Company Reports

**Figure 4: Real GDP Growth Projections**



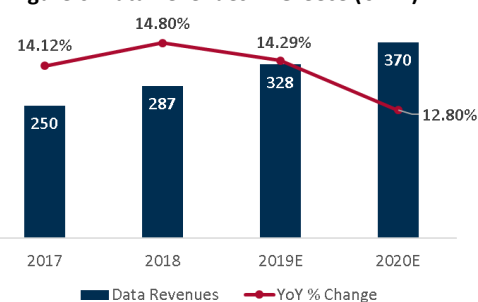
Source: IMF, OECD, World Bank

**Figure 5: VDSL + Fiber subscribers in Greece**



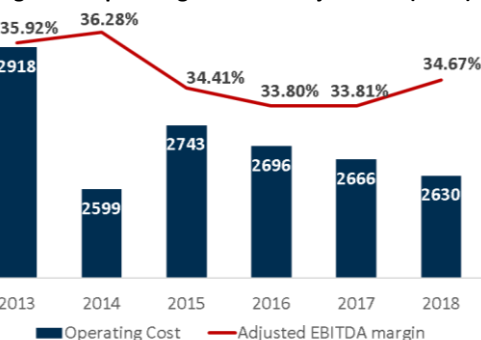
Source: Company Reports, Team Assessment

**Figure 6: Data Revenues in Greece (€ mn)**



Source: Company Reports, Team Assessment

**Figure 7: Operating costs and adj EBITDA (€ mn)**



Source: Company Reports

**Economic recovery in Greece:** Income per capita is an essential driver for telecommunication companies since a higher disposable income allows customers to consume more expensive services like VDSL, Fiber and mobile data. According to estimations of economic organizations (IMF, OECD, EU Commission, ESM, World Bank), Greece, where OTE has its main activity and source of revenues, is expected to slowly return to normality and grow with an average rate of +1.97% over the next five years.

**VDSL and Fiber penetration:** The Greek market lags behind its European peers in terms of adoption of these new technologies. Currently, only 7% of Greeks use these networks while the respective EU average is 33%. OTE will manage to capitalize from this market dynamic since it has managed to offer the best product in terms of quality and reach the majority of the potential customer base. In order to provide the VDSL and Fiber service telecommunication companies must own and invest in upgrading telephony cabinets. OTE has strategically chosen the cabinets it will upgrade, by obtaining 73% of all cabinets in Greece and leaving only 27% to its competitors. In the areas where these cabinets are developed, only OTE will have the privilege to offer high-speed broadband services, like VDSL. Based on our analysis, OTE has not only upgraded the majority of the cabinets in Greece but has also invested in the wealthier areas of Athens and Thessaloniki. This is very important since disposable income is an essential factor for someone to upgrade its connection to a faster one, as Fiber technology is more expensive. Consequently, OTE will benefit from this investment and increase its revenues.

**Higher Data Consumption:** Data revenues are very important for OTE since they compose 26% of the mobile service revenues and present great growth prospects for OTE. Since the emergence of high-speed 4G networks, which enables the end users to enjoy high quality of services for cheaper calls, instant messaging and social media, the percentage of data revenue to total revenue has grown from 11% in 2012 to 33% in 2018. Considering the fact that the Greeks consume only 0.46GB per month while the average European consumes 2.4GB, it becomes clear that there is room for increased GB consumption.

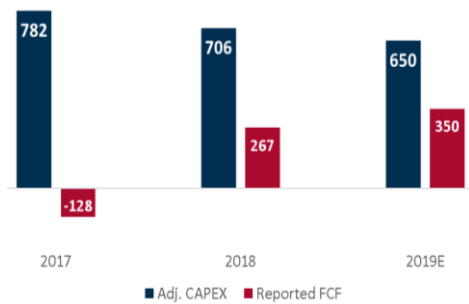
**Expansion to other business through its customer base:** In 2017 OTE announced its plan to enter the market of insurance, e-payments and online betting. Regarding the first, OTE has launched "Cosmote Insurance", a web application which functions as an intermediary between insurance offices and customers and receive a commission. This is very important since the group is entering a market of €4 billion with high growth prospects since Greeks mainly use public insurance. However, as public sector's reforms continue the revenues of the sector are about to increase. Online betting is also an emerging sector in Greece since it is in the process of substituting the traditional gaming agencies with total revenues of €5.2 billion in 2017, representing 46% of the total (traditional + online) betting revenues in Greece. Finally, in 2019 OTE will also launch "Cosmote Payments" entering the business of e-payments, an emerging sector in Greece serving individuals and companies in their daily transactions. This strategic movement depicts the will of the group to diversify its revenue sources and monetize on its vast customer base. This process will be conducted through marketing strategies of the company to promote its new services and exploit current customer networks.

## FINANCIAL ANALYSIS

**Thanks to cost reduction, OTE will boost adjusted EBITDA margin:** Generally, a high EBITDA margin demonstrates an effective company. Over the past years, this metric had a decreasing trend from 35.90% in 2013 it fell to 33.80% in 2017. However, it seems that OTE has managed to reverse this achieving an adj. EBITDA margin of 34.67% in 2018, while it is expected to maintain this trend in the future. This is the case since has managed to combine a revenue growth with a decrease in its operating costs. This process is carried out through digitalization of the work process and Voluntary Leave Schemes (VSL) which will decrease its personnel costs.

**Cash Flows and Capital Expenditure (CAPEX) return to normality in 2018:** OTE mainly uses CAPEX for maintenance or purchase of equipment and intangibles. Due to the huge line and cabinets infrastructure, CAPEX affects OTE's financial results intensively through the Free Cash Flow. In 2017 OTE's CAPEX peaked at €782 million and the company announced that from 2018 CAPEX would be significantly decreased to €700 million. The main reason for

**Figure 8: Adj Capex and Reported FCF (€ mn)**



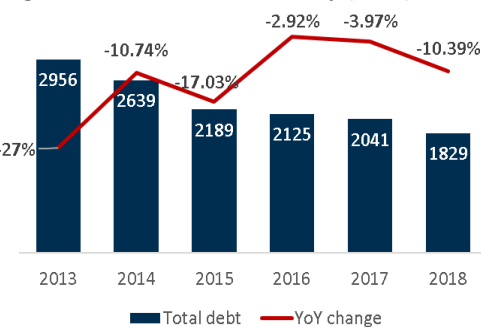
Source: Company Reports

CAPEX being so high is the investments made in order to secure the best cabinets and to install a fiber network of 13,000 cabinets. In fact, the company recently announced that CAPEX for 2018 was €706 million leading to higher FCFs of €267 million.

Starting from 2018, OTE implements its new remuneration policy towards its shareholders: This policy, which started in 2018 and will last until 2019, states that OTE will remunerate its shareholders with 100% of its Free Cash Flows (FCF) that reached €267 million in 2018. This amount will be divided in a split of dividend payout (65%) and share buy-back program (35%) resulting in a dividend of €0.46, marking a 31% increase from the 2017 dividend (€0.35). The Share Buy Back program of 2018 was launched in early April 2018. On 13th November 2018 the Share Buy Back program was completed and until then 8,890,960 shares have been bought at an average price of €10.5266. According to the company's estimates the total payout for the 2019 will be €350 million. Similarly with the remuneration policy of last year, the expected dividends (65%) are €221 million and Share Buy Back (35%) €129 million.

OTE is following a conservative policy regarding debt accumulation: Total debt has decreased from almost €3 billion in 2013 to €1.8 billion in 2018. In particular, the leverage of the group (Total Debt/Total Equity) has decreased from 128.30% in 2013 to 71.02% in 2018. What is more, the Cash and Cash Equivalents/Current Liabilities ratio equals to 0.46 showing that the group is highly capable of repaying its short-term debt. Moreover, OTE has drastically decreased its cost of debt, from 7% in 2013 to 3.9% in 2018, signaling that lenders have a positive outlook for the Group.

**Figure 9: Total Debt of OTE Group (€ mn)**



Source: Company Reports

## VALUATION

We conducted a multiple peer group analysis using the commonly applied ratio EV/EBITDA. The EV/EBITDA ratio helps to allay some of the P/E's downfalls and is a financial metric that measures the return a company makes on its capital investments. EBITDA stands for Earnings Before Interest, Taxes, Depreciation, and Amortization. In other words, EBITDA provides a clearer picture of the operating performance of a company, since it strips out debt costs, taxes, and accounting measures like depreciation, which spreads the costs of fixed assets out for many years. It is also more appropriate in analyzing the value of an infrastructure-intensive business, like the telecommunications sector. To understand the usefulness of EBITDA as a valuation metric, an investor must understand the nature of the telecommunications sector. The sector is, overall, characterized by being high-growth and capital intensive, with high fixed costs and relatively high levels of debt financing. Many companies have a large base of fixed assets, leading to correspondingly high levels of depreciation expenses. For example, OTE's depreciation, amortization and impairment costs for 2018 FY account to €755 million when its EBITDA accounts to €1,250 billion. An additional factor to consider is that telecom firms sometimes receive tax incentives from the government. These tax incentives can result in rather volatile swings in free cash flow, which means cash flow metrics may not be the best-suited evaluation points for telecom firms. By excluding capital expenditures, depreciation and financing costs, EBITDA provides a cleaner evaluation of a company's earnings.

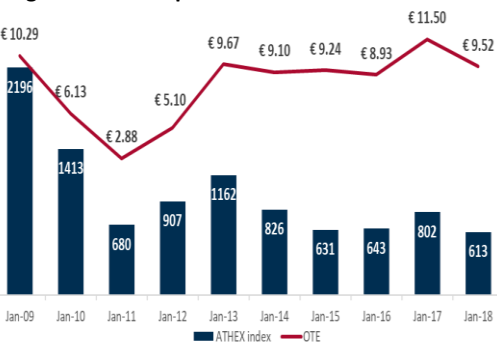
**Figure 10: Comparison with peers**

Peer Group	FY 2018	
Company Name	EV/EBITDA	Capitalization
OTE	4.4x	5.6b
DEUTSCHE TELEKOM	6.30x	74b
KPN	8.09x	12b
PROXIMUS	5.52x	8.4b
VODAFONE	5.89x	38.6b
TELEFONICA	6.44x	39.1b
SWISSCOM	7.56x	24.9b
ELISA	10.67x	6.8b
75th Percentile	8.09x	
Median	6.44x	
25th Percentile	5.89x	

Source: Thomson Reuters Eikon, Bloomberg

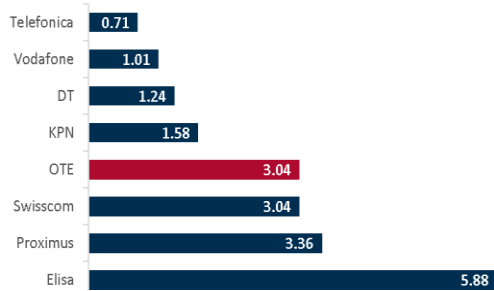
OTE currently trades at a capitalization of €5.56 billion and an EV/EBITDA ratio of 4.4x. The peer group is constructed of important telecommunications companies, like Deutsche Telekom (OTE's largest shareholder), and others smaller closer to the size of OTE, like KPN, Proximus and Elisa. We chose the 25% percentile and not the median to compute the EV/EBITDA multiple for this valuation, as OTE has a competitive disadvantage due to the macroeconomic outlook of Greece that delayed its expansion. Greece's country risk can actually be immediately observed at the EV/EBITDA ratio of OTE, as it has the lowest ratio among its peers. One significant driving effect that constitutes to this is OTE's low capitalization, a component that is greatly correlated with the country that each company mainly does business in. Moreover, another major component that keeps OTE's EV/EBITDA in lower levels is its relevant low debt, OTE's capitalization/debt ratio equals to 3.04x, rendering OTE as the company with the 4th lowest debt proportionally to its capitalization.

**Figure 11: Share price vs index**



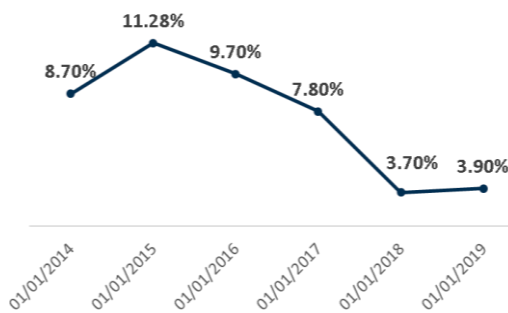
Source: Thomson Reuters Eikon, Bloomberg

**Figure 12: Capitalization/Debt ratio**



Source: FACTSET, Thomson Reuters Eikon

**Figure 11: 10-Year Greek Gov. Bond**



Source: Bloomberg

Moreover, by taking into account OTE's low capitalization due to Greece's country risk the capitalization/debt ratio would be even higher signaling the low level of OTE's leverage which drags its EV/EBITDA ratio down. Finally, after conducting the multiples valuation method we came up to a fair price of €13.30 per share for FY 2018. Should Greece have lower country risk and OTE higher leverage, the method would conclude to an even higher valuation.

## RISKS

Generally, OTE is a stable company with a low risk profile. However, our positive outlook on the Group may not hold if the Greek economy unexpectedly deteriorates and returns back to depression or if OTE experiences a drop in its sales due to increased competition.

**Macropolitical Environment (Impact: High/ Probability: Medium):** The danger posing the major threat to OTE is that of macropolitical uncertainty. Even though Greece has exited the third bailout program and both main parties agree on a pro-Euro policy, the country is not ready yet to access affordable financing from the markets showing that instability continues to exist, since structural reforms are still pending and the problem of the non-performing loans is not addressed yet. Furthermore, the political situation should also be taken into consideration, as the forthcoming elections (2019) reinforce uncertainty environment. In conclusion, a deterioration of the economic or political situation could jeopardize the company's domestic sales and increase the country's risk premium.

**Risk of increasing competition (Impact: Medium/ Probability: Low):** Existing competitors in Greece are constantly trying to improve their networks and products. A potential increase in investments along with the new arrival of TV content for Vodafone and Wind could affect OTE's market share and profitability. Moreover, if Digi continues the price war in Romania, it will create more issues for OTE in terms of revenues and market share

**Risk of new technologies (Impact: High/ Probability: Low):** OTE invested a significant amount in fiber technologies. If a new technology could emerge sooner than OTE expects, it would significantly affect OTE's long-term growth. However, this risk is low as there is a trend towards fiber technology. Also, telecommunication companies have managed to monetize on web messenger applications (What's App, Viber etc.) through increased data consumption. So, we do not anticipate that a new technology will substitute OTE's services.

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