Economies of The Baltic States

EESTI TELEKOM

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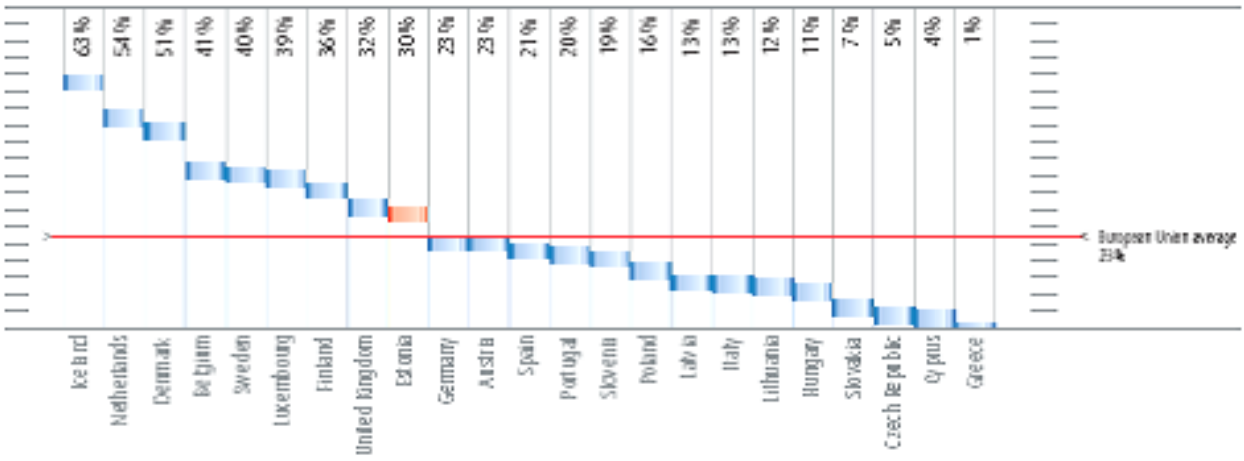
1. Introduction

The subject of this report is Estonian company called Eesti Telekom. Nowadays, it is one of the most recognizable and well-known brand on Estonian market. In this report we will focus on analysis of company's situation and perspectives. We will also deal with comprehensive view of telecoms market and various communication sectors supported by statistics, forecasts, estimations. Also, financial and employment statements of Eesti Telekom will be covered in further part.

2. Situation on the Estonian telecommunication market

It's not surprising, that Estonian telecoms market is one of the most and well developed in Eastern Europe. The fact is, that all the aspects of information society in Estonia are actively participating in common life. Estonia successfully implemented e-government, majority of schools are connected to fast, reliable broadband internet connection, e-government is extensively developed (paperless web-based facilities, online work, virtual offices and so on). It was Estonia that in October 2005 became first country, that introduced general political elections available through the internet via electronic ID cards (introduced some years before). Electronic online banking is nothing unusual, as it is used by well over 70 percent of Estonians, from many of them using even mobile phones instead of PC connection (fact concluded from 2005 survey). Unsurprisingly Estonians have the highest average spending on telecoms services in the CEES.



Households with broadband Internet in Europe in 2005

What's more, over thirty percent of households in Estonia is connected to a broadband connections. This puts Estonia on 9th place in Europe (see chart below). The average of EU is nearly 7% lower.

The competition on Estonian electronic communication market is quite satisfactory, with one exception – broadband market is dominated by Elion – Eesti brand. For other companies it is very hard to successfully enter and succeed in this segment of market. Shortcoming of competition are mentioned in different EU reports.

Telecommunication market is unsurprisingly dominated by mobile technology market. This is very good observable when considering level of penetration. According to surveys, before 2006 the penetration was a little bit more than 90%, but in 2 years it increased almost 20%. On the other hand, penetration of fixed-line telephony marker is over three times smaller, and exceeds 33%. Fixed telephony customer churn is between 4 – 5%.

Mobile telephony dominates the telecommunications market and there has been a rapid increase in the number of mobile subscribers associated with a decrease in the subscribers to fixed telephony services within the last years. In mid-2005, mobile penetration was 92%, reaching 107% at the end of 2005, and fixed line penetration some 33%. Fixed telephony customer churn is about 4-5%.

Mobile penetration growth in Estonia

Telephony market is dominated by three main players: Elion (brand of Eesti), Tele2 and Elisa. There are also some smaller, insignificant operators. It is critical to say, that before 2001 telecommunication market in Estonia was closed, and there was only Eesti Telekom that was operating there. Others entered the fixed telephony

market after the opening of the telecommunications market in 2001. The problem is, that the recessive trend of subscribers and movements to mobile technologies are making difficulties to alternative players, for instance in 2005 Tele2 announced stopping product development and marketing of fixed telephony in Estonia, Latvia and Lithuania. The company would have continued to serve existing customers and to offer mobile telephony services.

Economic growth in Estonia, which reached approximately 11,5% in 2006 is a good base for investments and development of the IT and new telecommunication sectors. The volume is rapidly growing, reaching almost 10%. The nominal growth of over 9 billion EEK was in one half comprised of Eesti Telekom turnover. It makes Eesti Estonian's largest and one of the most profitable group of telecommunication and IT companies.

3. Eesti Telekom

3.1 TeliaSonera

TeliaSonera is the leading communication company on the market in Nordic and Baltic countries. Moreover it provides services on other markets, like Eurussia, Russia and Turkey. TeliaSonera is a result of joint venture between two leading companies from Sweden (Telia) and Finland (Sonera). The majority of shares (over 50%) of Eesti Telekom is owned by TeliaSonera.
There are several main business in which TeliaSonera is operating in, that is integrate fixed and mobile communications, voice, data and telecom-related IT-services.

Business strategy

The global business strategy of TeliaSonera is

- ✓ Grow with new mobile and IP-based services.
- ✓ Simplify services.
- ✓ Consider selected acquisitions.
- ✓ Competitive costs
- ✓ Service portfolio

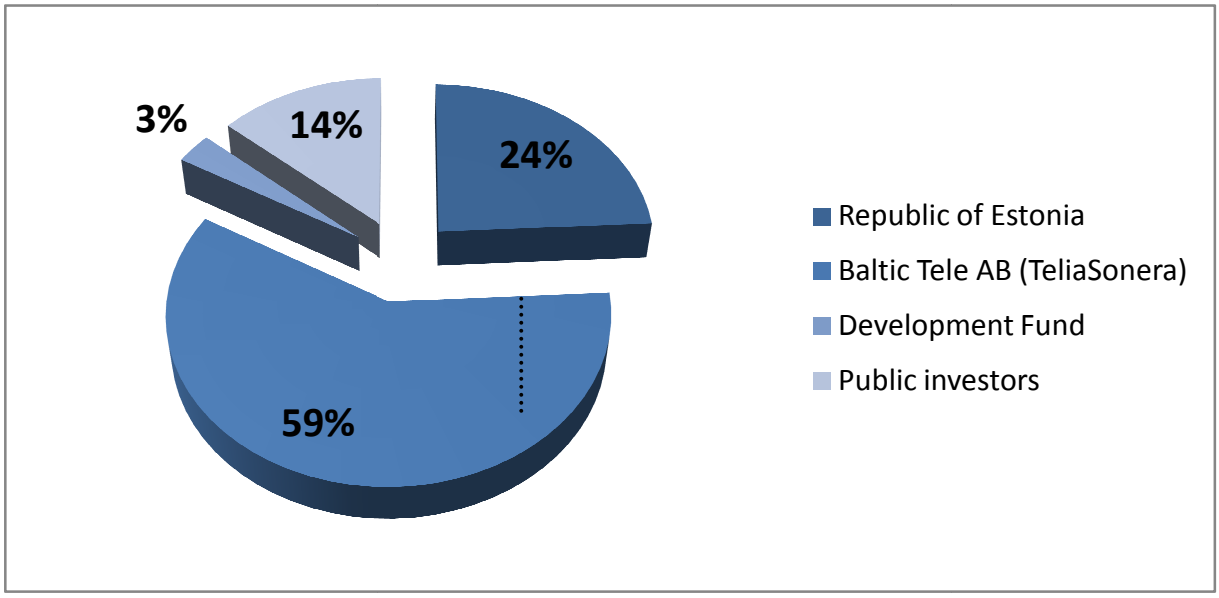
Shareholders

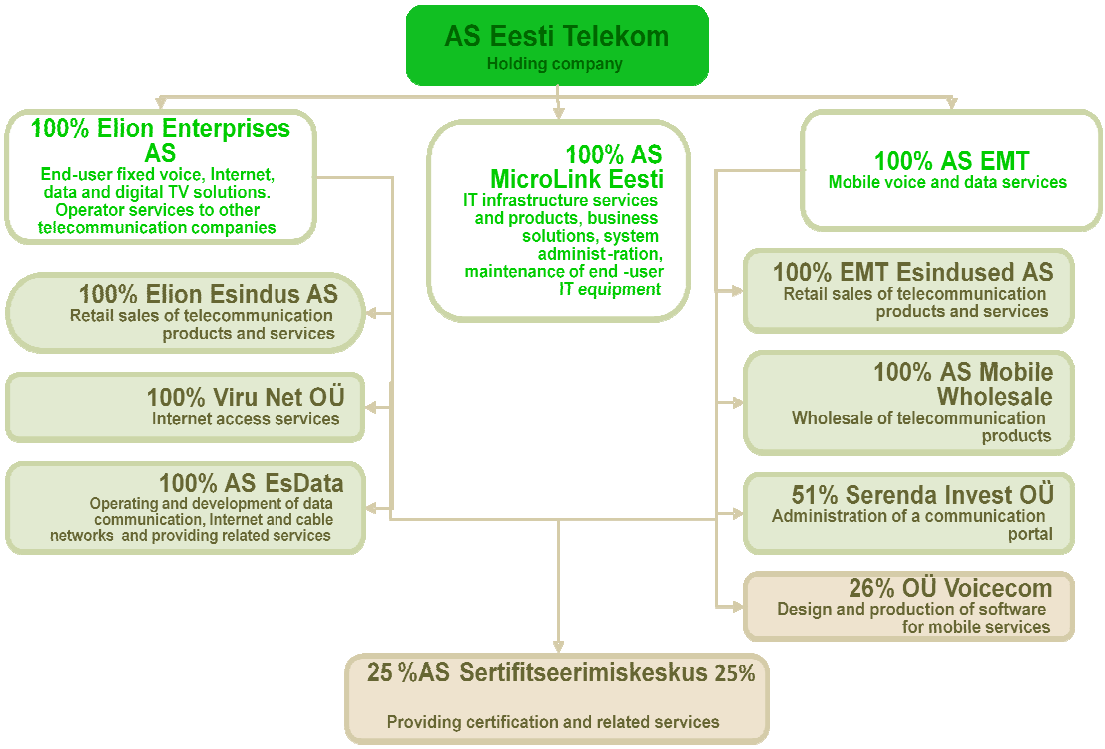
TeliaSonera consist of only one type of shares, and every share represents one vote on the General Meeting of shareholders. In 206, the number of shareholders went down to 691,106.
The Swedish and Finnish kept during 2006 respectively 64,4% and 19% of holdings. Ownership outside Sweden and Finland increased from 12,8% to 16,7%.
Summarizing the year we can say that Swedish private investors owned 3,2% of shares and institutional investors owned 19,7% of shares. Moreover Finnish private investors owned 2,2% and institutional investors owned 3,2% of shares.

TeliaSonera in figures in 2006

- Net sales increased 3,9% to SEK 91,060 million because of mobile and broadband growth.
- Number of customers growth:
  - 2.7 million new customers most of them owned Nordic, Baltic and Eurasian operations.
  - 14.8 million new customers in the associated companies MegaFon and Turkcell.
- Operating income, excluding non-recurring items, increased by 33% to SEK 26,8 billion
- EBITDA margin, excluding non-recurring items, decreased to 35,4 % because of the improvement was especially due to higher margins in Sweden, Finland and Denmark.
- Free cash flow increased to SEK 16,596 million.
- Net income totaled SEK 13,694 million (14,264) and earnings per share were SEK 2.56 (2.77).

Organization structure





3.2 History of Eesti Telekom

1991:

Reconstruction of whole telecommunication sector in Estonia due to achieving independence by this country. In the same year arose the Ministry of Transport and

Communication instead of the Ministry of Communication which was closed. Eesti Telekom, as it was a state-owned enterprise, became the main operator in Estonia telecommunication.

1991-1993:

During this two years, Eesti Telekom became a holding company comprising of two joint ventures – Eesti Telekom & EMT. Minority shares of this companies has been sold to Telecom Finland (Sonera) and Swedish Telia.

1992:

State granted Eesti Telekom rights for monopoly for the next ten years.

1994:

Eesti enters ISP market by acquiring 15% of the shares of EsData, one of the main ISPs.

1997:

The state enterprise was restructured as into the joint venture Eesti Telekom, thus the Estonian state decided to sell up to 49% of company's shares through public offering.

1999:

Due to the initial public offering (IPO), institutional and private investors purchased 49% of the shares of the Estonian state. Hence, a company's shares has been listed on London's and Tallin's stock exchange.

2003:

Widespread of Internet, data communication and IT as a new business areas led to change name of the company from AS Eesti Telefon to Elion Enterprise AS. Likewise, its subsidiary AS Telefonipood changed name to AS Elon Esindus

2005:

EMT was the first company in Estonia that implemented a 3G mobile communications network with such facilities as :

- mobile TV
- video calls
- faster mobile Internet

2006:

Serende Invest OÜ , a company that owns "Rate" trademark, and what goes with it – Rate.ee, sold 51% of shares to EMT

The same year in April Elion launched DigiTV to the market.

3.3 Eesti Telekom

Eesti Telekom is the largest group of telecommunication and IT companies in Estonia. It shares are listed on both Tallin and London Stock Exchange since 1999. The majority of shares belongs to Baltic Tele AB (part of TeliaSonera holding). Telia Sonera is joint-venture, created by two operators from Sweden (Telia) and from Finland (Sonera) to operate on Estonian market. Rest of shares are mostly held by state (24%) and private investors.

Eesti Telekom's wholly owns its subsidiaries:

- Elion Enterprises AS
- AS EMT
- Microlink (from July 2007, previously part of Elion)

It makes Eesti has leading position in the Estonian telecommunication market. What's obvious, AS Eesti Telekom is not directly involved in commercial operations. Its profit accumulates mainly from the profits of other companies in the group. In 2005 the operating income totaled 5 168 million kroons, and the group's net profit was 1 088 million kroons. The share capital of AS Eesti Telekom consists of 137 954 528 ordinary shares with a nominal value of 10 kroons each. Starting from 2005, the company's share price have been increasing on the stock exchange by over 5%.

Vision

As declaration says, Eesti Telekom group companies are about to be recognized as "trustworthy partners" and as "providers of the innovative solutions needed by customers". The aim is to provide different value added services from home and business communication possibilities for all the consumers, including different market range – from telephone calls, integrated communications and information technology solutions, through sales of telephones and computers to high-speed internet connections as well as the installation and maintenance of large information technology systems.

Strategy

The primary objectives that lie in framework of Eesti Telekom's strategy are:

- to be successfully customer focused company, with a deep understanding of their needs and desires, being able to offer them easy-to-use, easy-to-understand and useful solutions, which can support daily business activities and everyday life,
- to be constantly improving in customer service and services quality,
- to be provider of quality, modern and up-to-date sophisticated solutions,
- to offer solutions satisfying IT and communication needs for private and corporate users,
- in addition, to offer households different forms of entertainment – including high-quality digital television, providing video on demand, modern mobile TV and online games with necessary equipment, installation, service and maintenance,
- to develop new business areas from the wide range of IT services for private and corporate users, digital TV, 3G mobile services, leasing and rental services etc. ,
- to ensure revenue growth,
- to be effective using synergies inside the group, coordination and unification of most important functions.

3.3.1 Elion Enterprises AS

Elion is considered as the largest telecommunication and IT provider in Estonia, it was founded on 1 January 1993. A that time all international calls were routed through Moscow and people used rotary-dial phones. The company was established by the Estonian government to put an end to this, by establishing new comprehensive telecommunications network and opening up international connections.

In the first years of company's existence, it's main goal was to shorten the waiting list of people waiting for their own telephone at home, laying new telephone networks, and improving the quality of communication. All these principles were based on the agreement between the government and Eesti on 6 December 1992. Since then the company has laid hundreds of thousands of new phone lines with connections to Finland, Sweden, Russia and Latvia.

As a very successful company also in internet communication, in 1996 it has launched its own internet search engine called NETI that soon became the most popular webpage in Estonia. Moreover in 1999, it has become the leading company in providing dial-up and broadband internet connections. This gave Elion the possibility to lunch e-mail services at HOT, which in a short time became a unique communication centre and one of Estonian's most high-ranked web pages.

Since 1 January 2001 the company realized that is has to prepare itself, as the government monopoly guarantee ended in 2002. Threat of new companies entering the Estonian market was very close. That is why the company decided to invest 100 million kroons in the telecommunications network. Today Elion is the market leader in fixed network calls, internet connections and data communication solutions. Moreover is has made a powerful entry into the IT market.

From 29 December 2002 state-granted monopoly ended and so Elion is no longer a monopolist on the market, neither it is a technology company. It's main competitive advantage is: understanding the communication and business needs of its customers as they are longest on the market. What is more it has to create simple solutions, and it has the aim of becoming the best provider focusing its efforts in the needs of its customers.

From 2003 the company is known under a different brand name, Elion. This change was due to different kind of services provided by the company. It was no longer only telephone services provider, but its main source of income became services like internet, data communication and IT.

Elion in 2005:

In Elion's offer we can find things like telephone, data communication, internet, IT services and digital television services. In addition it offers integrate business solutions. Moreover they sell personal computers and install IT systems.

The company is a very promising one as internet connections grows more than 40% during this year and Elion with EMT sold 2,5 times more computers.

The breakout of offering new services was in 2005 when Elion started to provide digital television reception and in 2006 they presented television reception via ADSL network as part of a triple play solution. As a result Elion is able to provide communication and entertainment at the same time which resulted of course in higher profit. In April 2005, Elion became Europe's first digital television main head end working on an internet protocol in Tallin, which started to transmit domestic and sky channels of unprecedented quality to homes.

Elion also owns HOT and NETI:

As was mentioned HOT is the Estonian's most successful e-mail and web hosting environment, in addition the users can call each other for free and call other people through fixed and mobile lines. In 2005 HOT achieved an average of 126.000 visits per day and a total number of 915.000 users. There are sent 1,6 million e-mails per day, the mail box has virus and junk mail protection.

NETI on the other hand is Estonian's most popular Internet environment. In 2005 it achieved an average of 281.000 visits per day, 25.000 links to Estonian websites in the classified information catalogue and a total of 12.000 links to Estonian websites in the search database.

The market of Elion is growing rapidly as the number of telephone lines used by business clients has increased rapidly since the previous years and in addition to this ISP market for this company is also growing fast.

Elion subsidiaries:

- *AS ELION ESINDUS*: manage the company retail outlets.
- *AS EsDATA(100%):* EsData is an affiliate company which offer contemporary solutions for television program.
- In cooperation with Elion, Esdata provides cable TV services in new dwelling house regions, private houses, accommodation and office buildings.
- *VIRU NET OU (100%):* Leader internet service provider.
- *SK (Certification Centre, legal name AS Sertifitseerimiskeskus) (25% :* is Estonia's primary and currently the only certification authority (CA), providing certificates for authentication and digital signing to Estonian ID Cards.

3.3.2 AS MicroLink Eesti

"MicroLink Eesti is the largest Estonian IT company whose business interests include:

- system integration and infrastructure solutions
- software development
- ERP and business solutions
- IT consulting and training
- central systems and data centre solutions

- end-user PC services and support”

MicroLink Eesti is today considered as the company, which offer of IT products and services is the widest. Actually, MicroLink offers wide set of products and services across many fields – with leading business areas and technology solutions of MicroLink Eesti cover more than 90% of IT needs of modern private and public organisations.

Goals of MicroLink include giving its customers the possibility to “outsource all of their IT operations and development projects to MicroLink, in which case the customer itself can focus mainly on its business related IT strategy development”.

3.3.3 AS EMT

On April 28 EMT started its operation as an Estonian-Swedish-Finnish joint company. In the same year in June the first NMT 450 client was able to call with a mobile phone in Estonia. EMT is a high technology service company operating in the field of telecommunications and information technology. It is the only one Estonian – origin operator that owns and operates telecommunications networks in the domestic Estonian market. This enterprise develops and markets telecommunication and information technology related services, solutions and environments in Estonia and increasingly for export.

EMT was the pioneer in 3G mobile communication network, they were first to offer GPRS, mobile TV, mobile internet services and video calls as well. As a results of a study conducted in year 2006, their market share has increased approximately to 48%, which is very high share ratio.

EMT subsidiaries:

- *EMT Esindused* AS – 100% of shares
- *AS Mobile Wholesale – 100% of shares*

- Serenada Invest OÜ – 51% of shares
- *OÜ Voicecom – 26% of shares*

Things which happened in year 2006 and are worth mentioning:

- The number of customers reached 759000
- The total market share of the company is 48%
- launched new generation 3.5G (HSDPA) fast (3.6Mbps) data transmission service
- acquired 51% of Serenda Invest OÜ, owner of the brand Rate administering Estonia's most popular internet community portal
- launched new service MyTone, a service in which when users' number is dialled the caller will hear music or other sound of user's choice
- 3G network was opened in Tartu and Pärnu
- EMT SurfPort brings e-school to mobile phones; both the student and the parent can view class schedules, homework, grades, reprimands, attendance and messages from homeroom teacher via mobile phone.

The revenue of AS EMT increased by 11% compared to the third quarter of 2006 reaching 54.8 million EUR. The increase of revenues in the principal activities was caused primarily by an increase in the number of call minutes initiated from and completed in the EMT network and the growth of mobile data communications. Compared to the end of the third quarter 2006, the client base of AS EMT was 5% larger at the end of September this year, reaching 759 thousand active SIM cards. EMT assesses its market share of active SIM cards as 48%. The penetration of active cards in Estonia is 116%.

Very rapid growth continued to be shown by AS EMT mobile Internet revenues. In the third quarter of this year, the revenues for mobile data communications exceeded the revenues for the same period in 2006 by more than 50%. At the same time, the volume of data transmitted increased six fold. The number of AS EMT mobile data communications users in September 2007 was 119 thousand, 20 thousand more regular users than a year ago. The increase in popularity of mobile data communications is caused, on the one hand, by the introduction in June of new data

communication packages based on monthly fees, which provided clients with quality and high-speed data communications at conveniently controllable prices. Clients can choose between packages costing 6.33 EUR, 12.72 EUR and 25.5 EUR, which provide 30MB, 500MB or 3GB of data per month respectively. The monthly fees earned in the third quarter of this year exceeded the results in the same period of 2006 by 23%.

4 Financial and employment statements

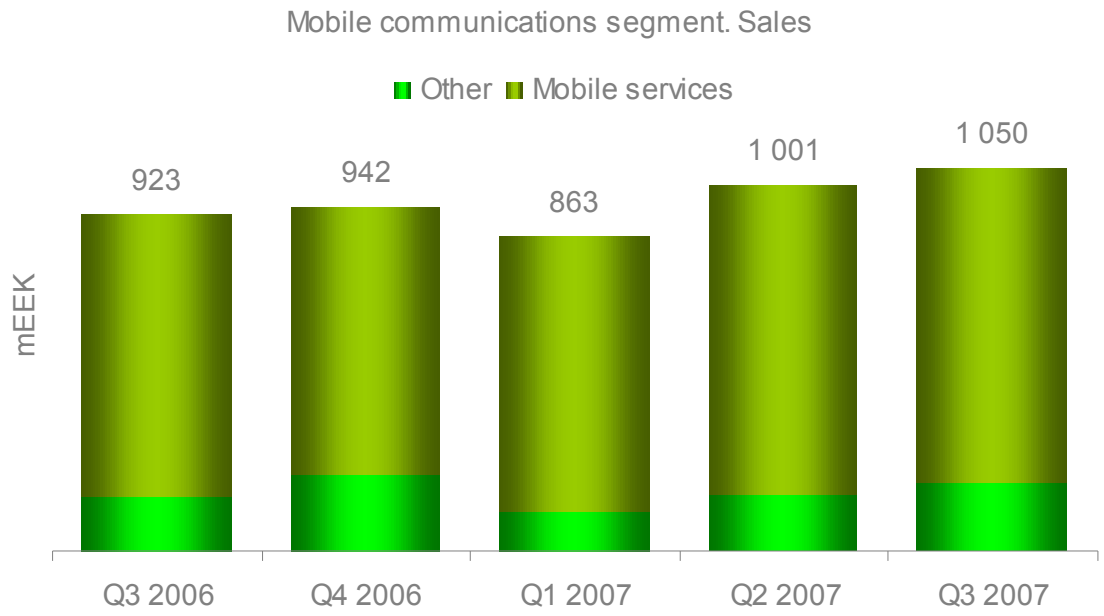
Last year was very fruitful if it comes about stock exchange, share prices increased about 5,6%, what is really high indeed, thus they were able to repay shareholders dividends. Not only stock exchange was crucial and helped in last year's development, but because of no loan debts, very positive result on the balance sheet and cash flows.

While in 2005 Eesti's revenues were on the level of 5.138 million EEK in 2006 this number jumped to 5.168 million EEK. Most of this revenue came from the mobile phone communication sector, almost 70%. The other part of growth was due to acquisition of new Elion's subsidiary, AS MicroLink Eesti. This acquisition which came in 2005, gave Eesti the leading role in Estonians IT market, which is capable to offer customer the widest range of communication and IT services. In both Eesti's communication sectors in 2006 growth was noted.

Most of revenues of Eesti comes from its subsidiaries. Strong sales of the Elion Group are mostly due to consolidation of the MicroLink Group. Growth of net income (year to year) is about 5% in last year, with over 13% of sales growth.

Operational cash flow balance in 2005 was 1 958 million EEK compared to 1 645 million EEK in previous year. This dynamic growth was caused mostly by acquisition of MikroLink, supported by larger investments into fixed asset.

The Eesti's cash flow balance from operations activities in 2005 was 1 958 million EEK compared to 1 645 million EEK in 2004. The main factor of increasing the cash flow was connected with the acquisition of MikroLink and larger investments into fixed assets.



Dynamic growth of ROA and ROE still remains on high level. In third quater ROA increased to 31.1% from 27.6% in previous quarter due to cash with small productivity and the high ratio of bank accounts among the assets. On the other hand, in third quarter of 2007, ROE was 46.3%, while three months before it was 42%.

Employment

From year to year the number of employees is rapidly increasing. For example at the end of year 2005 it was approximately 2190 while now it is reaching 2400. Mainly it is caused because of a merger with AS MicroLink, which rose the number of Eesti Group employees. All in all, it also have an influence on salaries, which rose from 396 million EEK to over 400 right now.

5 Vision and perspectives

Estonia is a very promising country as it comes to IT and communication markets as these markets are very profitable and they seem to keep developing. In order to sill be competitive in this environment Eesti Telekom Group has to focus on investing in services, quality and innovation, understand the business and communication needs of customers as to create the best solutions that are ordered by the customers. The main goal of companies strategy is to strengthen and improve the position on the home market creating new opportunities in the field of Internet and mobility.

As to strengthen its position among yung customers AS EMT bought 51% of Serenda Invest OÜon April 5 2006, which is the owner of the Rate brand, and administers Estonia's most popular Internet communications environment—Rate.ee.- and the largest social network in Estonia, which unites about 360,000 registered users. The average of users visiting Rate.ee is 15-25 year-old young people. They visit the webpage on the average of 130,000 visits per day. During 2006, Rate Solution OÜ earned revenues of 6.2 million kroons and a profit of 4.9 million kroons from services and advertisements on Rate.ee.

In addition, Elion introduced Digi TV to increase the opportunities for communication. Apart from delivering Internet and telephone connections, at the beginning of 2006 they started to offer a triple service including also "Home Solution" and "Multi-Story building Solution". They are one of the first to use passive optical network technology in Europe, and would like to reach half of the homes in Estonia by the year 2010 with DigiTV.

Eesti Telekom plans to continuous improvement of service quality. Some high priorities will include integrating communication solutions and improving market position. Furthermore, Eesti wishes to offer complex, idiosyncratic solutions, that could satisfy customers and serve for both private and business purpose.

EMT strongly believes, that further development of mobile communications service market will lead into higher degree of new services, offered to customers. It will involve investments into innovative technologies, allowing to spread into inexpensive, qualitative communication markets.

Continuous development of 3G network and expand of Edge network are primary plans for future of AS EMT. So far, Edge network covers popular places in Estonia nad all larger towns. It is predicted, that share of 3G mobile phones is about to increase significantly. It is believed, that "music telephone" will become popular, allowing to listen to the radio, music and record, becoming alternative to widely used MP3 players.

Elion is about to expand its position on DSL network market, and develop networks based on radio solutions. Fast development of IT services is planned, including both private and business sector.

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