

Telecom Italia  
9M'08 Group Financial Results – Conference Call  
Milan - November 7, 2008  
Q&A session

1. Mr. Matthew Collett from Cazenove:

*Hi there. Two questions, if I may. Firstly, you mentioned that you're not seeing any signs of an impact from the economic slowdown. I just wondered what criteria you're using to monitor that. And secondly, I think you said on the Q2 conference call that you are going to give free mobile broadband to fixed broadband customers. Are those... is that deal still going on? And are those subscribers included in your mobile subs number for the quarter? Thanks.*

Let me answer on the crisis, on the macroeconomic crisis... on the macroeconomic environment that we see. We have signs, of course, that times are getting tougher... we see it on the international roaming, where we have a decline in revenues, and we see it on the small office... home office sector, but what we try to do is to compensate the impact of high income elasticity of the... the impact of income elasticity to our revenues with a concentration on low-price elasticity segments of the market, raising prices... So, in a sense... of course, we see that there is an impact; this impact is mostly on the lower revenue high elasticity customers, but we try to concentrate the actions, raising prices, on higher revenue lower elasticity customers. So, I think we have been able so far to compensate for the impact of the macroeconomic deterioration. We, of course, don't know what will happen next... in the next few months and how this macroeconomic situation will evolve. But I'm very confident that the way we are handling the segmentation of the market will allow us to come up with a consistency in the trends that Marco Patuano and Oscar Cicchetti have shown you. On the other question I will ask Luca Luciani to answer.

Well... I mean, back to mobile broadband growth. As you can see, this is a consistent growth quarter-over-quarter and this comes from both prepaid and postpaid markets. Now, what's the key reason behind this? It's the possibility to extend the current ADSL customer base into mobility so that it's not a pure substitution growth; in fact, one of the most attractive offers that we presented at the last Dealer's convention was the concept of: you take an internet key and you pay the bundle internet key and the mobile data into the fixed invoice bill. It means that the easiest way to take up this market is to bring the current Alice ADSL customer base... and bring it into mobility. So that, for sure, there is a pure mobile market but most of our growth comes from already existing internet customers that wish to go outside. This is even proved by the fact that these connections of fixed lines are in line with our forecasts and better than previous quarters. So that there is no speed-up of these connections of fixed broadband because of mobile broadband.

Thank you Luca. Next question, please.

Can we have the next question, please?

2. Mr. Carmelo Pappalardo from Dresdner Bank :

*Good afternoon. Three questions, please. The first question is the... on the revenue guidance. In order to reach the guidance for the full year, Q4 needs to be strong, showing a positive performance on a reported basis. Could you give us more color on that point? On that issue? Also, taking into account that the possible contribution of the exchange rate against the reals, that helped you in the first nine months in 2008, today seems reversed. The second question is on*

*Brazil, in particular just to have your first impressions on the increased competitive environment in Brazil after OE entered in Sao Paolo. The third question is the repricing on mobile: in particular just to better understand if the strong performance we have on the outgoing revenues is also confirmed in October without any strong sign of deterioration in usage or in char rate. Thank you.*

Okay. I think that just to give you a quick answer to the three questions you raised: on the revenue guidance... you mentioned a strong fourth quarter; I think that what... if you see in the trends that we quoted the number of figures that show the trend that we have in October and you see that the October figure is higher than the third quarter figure. So, we are very confident that thanks to... thanks to the repricing, thanks to the stabilization of... of char... and thanks to the... thanks to the strong slowdown in ULL, we will be able to meet the guidance. On the increased competition in Brazil: yes, the market is changing. It's much more complex than simply an increased competition, because of what is happening in Sao Paolo. We are reviewing the... we are making a strategic assessment of what is going on and, of course, we will be reacting. But I'm confident that we are gaining back our... the perception of a strong player that in the first two quarters we in a sense have lost a little bit and, therefore, the market reaction to our... to the steps we have taken is very positive. On the third question on repricing, on mobile: yes, we see a strong growth also in the next few months. But perhaps... perhaps Patuano would like to add something on the exchange rate of the reais.

Yes. On the exchange rate we are keeping in our forecasts a slight deterioration of the exchange rate, but we don't think that this exchange rate will affect dramatically the overall figures. So, yes we are considering a change in the macroeconomic scenario even if we are slightly positive on Brazil with respect to the rest of related American economies.

Okay. Next question, please?

*Thank you.*

Next question is from...

Sorry, Luca Luciani speaking. Back to the repricing question, I'll go a little bit deeper: for sure, yes, in October we have on the prepaid segment something like a +5% growth, so that the key evidence is benefits on revenues, low turn, if you confirm... if you compare the mobile number portability donor in August and September they are lower than the previous year... and similar trends in October. And third, I would say that much more than turnout... there is a lot of migration between internal firm profiles because let's consider that our repricing activity has been counterbalanced with many new tariff plans, like Chiara, like Easy TIM, like TIM Per Due and, lastly the big "all you can eat" concept within TIM Tribù, so that most of our customers had an alternative to the previous one that limited a lot the turnout of our customers.

Okay. Next question, please?

3. Mr. Nick Lyall from UBS:

*Yes, hallo there. Yes, Nick Lyall from UBS. Can I just ask two questions, please? On the... it looks as if the marketing and sales costs went up in the third quarter, and I just wondered: you made some comments about increasing commercial activity particularly in the fixed in the fourth quarter. Should we expect a similar rise in marketing activity in the fourth quarter as well? And, secondly, on the fixed line business again, you have 55,000 broadband adds in October; does that include*

*much naked ADSL... retail naked ADSL so far? Would you expect that number to improve given the introduction of the product? Thank you.*

Okay. Mr. Cicchetti will answer to the first question, Mr. Labriola will answer to the second question.

Yes. As far as the commercial costs are concerned, I gave... I have already given you a first cut breakup... the... let's say that the savings that we have been able to achieve in terms of commercial costs, in terms of acquisition costs, is mainly related to a deep sales channel reorganization where we selected some clusters of sales channels, we closed some categories of different channels, for instance what we call the Tele-sale, and we decreased the commissioning and so, to that extent, even with those measures taken, we have been able to maintain our commercial plans. I think that Pietro Labriola can answer the question about the broadband customer base.

Yes, sure. If we look at the number that we are seeing in September and in October, we are quite confident that we will overcome the guidance of the 6 million 700,000 broadband customer portfolio. And we are also quite optimistic in terms of line losses, because also the number of line losses in the market in the month of October is giving us good results.

*Okay. If you could just, maybe... is there much of an impact from naked ADSL within that 55,000 number? Is that also on the savings for Q4 or rather on the market of Q4 do you think you'll see a rise again or... is there anything you can say, maybe, about the direction of marketing and sales budgets?*

Mr. Cicchetti.

Yes. In the fourth Q I think that we will continue to get benefits from the (...) commissioning, but on the other hand we will have some increase in the advertising cost because we are launching some important campaigns for ADSL broadband wireline and the new wireless broadband swift.

*Okay. Thank you very much.*

Next question, please?

Next question, please?

4. Ms. Robin Bienenstock from Stanford Bernstein :

*Hi, thanks very much. Actually, I'm not a Mr., I'm a Ms... but, anyway... my first question is: really, can you tell me what percentage of capex is coming from SACs? Do you have a kind of a long-term strategy about that? And are you at risk, given your contract conversion, of essentially eroding the profitability of what's quite a nicely profitable market? And my second question is about your business: I'm kind of surprised that you're reporting fixed and mobile businesses separately: are they still organizationally separate or are they working more hand-in-hand these days? Thank you.*

On the... on the reorganization, according to the... to the... business line division in consumer and business, we will be making a special session... a session with the analysts in order to provide the figures. So, till the end of the year, we will be providing figures according to the traditional... the traditional division mobile and fixed. But I didn't get your first question, because there were problems with the line.

*I'm sorry. My first question was: can you tell me what percentage of capex this quarter is from SACs? From subscriber acquisition costs? And can you tell me how that's changed over time? And whether or not you're at risk of eroding the margins of your business but as you're increasing your convert contract and to a subsidy, a more subsidy model?*

Let me answer on the mobile... Luca.

On the mobile, the subscriber acquisition costs capitalized are 250 million euros year-to-date. So 250 million in nine months, and this includes, let me say, the handset subsidy commission, subsidy for the business and the postpaid. This is on the mobile side. Nothing on the fixed.

Perhaps, Oscar Cicchetti would like to add a comment.

I think that the... considering the fixed and the mobile the SAC capitalization costs are equal to 221 million, of which 75 million in the third quarter. This is, let's say, basically in line with that posted in the first months of 2007, that is around 218 million euros, of which 85% in the third quarter. And Luca Luciani has already given the numbers for the mobile.

*Thanks very much.*

Next question, please?

5. Ms. Michaela Ferruta from Intermonte:

*Good evening. I have three questions, if I may. The first one goes back to the weakening of the economy, where you gave us some details; can you tell us on the cost side what actions you could put in place for 2009? Clearly layoff, a possible increase in unbundling and monthly fee would help? Would a possible decrease in, for example, advertising, be a possibility? Can you give us an idea of the lever that you can use in order to face a possible, maybe not likely, but possible, deterioration in revenues? The second question regards dividend guidance: in August you actually confirmed that the guidance for dividends was possibly going to be in line with last year; you are now confirming 2008 targets: can you tell us something about dividends? And, finally, in September you told us that there was an interest to invest in Telecom Italia capital: can you give us an update also on this issue? Thank you.*

On the first question: the weakening of the economy and the impact that this has on the cost side; of course, that will be totally detailed when we'll be presenting the plan at the beginning of December. So, this question will be answered on that occasion. On dividends, as you have seen, TI generates healthy profits and has a robust liquidity margin and the trends are improving, but of course the Board of Directors will decide on dividends, as it always happens after the end of the year's results. So, again, we will update you on this at the appropriate time. And the third... the capital structure plan: there is nothing new on that side.

*Thank you.*

Next question, please?

6. Mr. Terence Sinclair from Citygroup:

Yes, thank you. Good afternoon. It's just one question on capex: we would have thought, given the capex levels that you're running with, that there may be an opportunity to cut capex quite aggressively over the next few months. I know that the capex is down, year-on-year in Italy, so obviously after Brazil even disregarding the (...) acquisition, it's really a question for Italy: what scope do we have currently to cut capex? Thank you.

I'll ask Mr. Patuano to answer this.

Sorry, can you repeat the final part of the question?

*I just wonder what color you can give us, perhaps, on the extent to which capex is currently committed? For next year? To what... what part of the capex might be postponed, if you wish to delay capex in Italy? Or rethink capex budgets? The question really relates to how far you can cut the overall capex profile doing this so much as in Italy?*

Yes, I understood. Well, as Mr. Bernabè told you before, answering a question before... anything related to 2009 will be disclosed on the next December 2 presentation of the new business plan; it's something that we will answer in the next conference call.

*All right. Thank you.*

I'll ask Mr. Pileri, perhaps, to provide some color on the commitment for next year.

Yes, good evening. First of all, I would like to tell you that from the technical platform point of view, we are in line with the guidance for this year, because we are targeting a deduction in capex of more... of approximately 400 million euros, according to the... to what we presented in March, following all the actions that we presented in optimizing the open access...access organization, mainly the information technology, as Mr. Bernabè presented to you in the first part of the conference call, and the... and also the other network departments in capex optimizing. Next year, we will continue to reduce our capex expenditure thanks to the improvement in the convergence network deployment that can... that will allow us to reduce our expenditure still giving the possibility to maintain broadband evolution both in the fixed and in the mobile and thanks, again, to the optimization of the information technology department with (...) optimization, the internationalization of many activities and the rationalization of the sourcing model. Then we will still continue next year to reduce our capex expenditure.

*Thank you very much.*

**7. Mr. Ottavio Adorisio from Société Générale:**

*Hi. Good afternoon gentlemen. I have a couple of questions, if I can. The first one is related to the economy, which is a main topic today: you basically limited the impact to roaming and some WAP services. Actually, when I look at the volumes you generate in voice, there has been a significant decline both on fixed and mobile: the fixed around 20 basis points if one compares the trends in the previous quarter. And when I look at your mobile trends, you went from +27 to +16 and now +5: so, almost, I would probably say, a huge fall here. I was just wondering why you don't (...) this to the economy? And the second point is on the capital structure: it's undeniable that in the market your share price's driven by rumors or whatever is going on in terms of a potential reserve capital increase; considering the management basically stands behind a strong balance sheet of the company, can you basically say why there's a need for a capital increase? And if there isn't any, can you just tell the market that there's never going to be any capital increase? Thanks very much.*

Thank you very much for this question. On the first part of the question, concerning why we don't think that what we see in terms of volumes is the consequence of the crisis, of course it might be; it's difficult to fine tune the components of this, but, basically, and I will ask Luca Luciani and perhaps Mr. Labriola to give a little bit more of color on this... but basically what we have done is that we drastically reduced the kinds of promotions that were driving volumes, because we had strong route impacting on our network at lower prices. We decided to keep up prices and to slow down both, because we didn't see much benefit from this. But I will ask Luca Luciani to elaborate a little bit and perhaps also Mr. Labriola.

Yes, I mean, on page 17 we have most of the answers, because the big, let me say, differences in volume growth are all in the prepaid market. Now, what we did a year ago and what we are doing now. We started in the first quarter 2007 with a very low usage in the prepaid market, and we implemented a strategy based on increasing the usage through promotion, and this resulted in a very important growth in terms of minutes. Now, starting from the second quarter of this year, we reduced the pusher motion in both massive and one-to-one promo in order to stabilize the trends of the usage and try to capture investments we did last year to, let me say, addict our customers with more and more usage of volume. Now, if you look at the slide, you see that the promoted parts of the volume dropped by 10 points; let's consider that the average price of this volume is one third of the average. On the other side, if you look at old plans and the new tariff plans, so that non-promoted volume, you can see that there is a growth year-over-year... clearly... and the average price of this part of traffic is significantly higher than the average, so that net-in-net we invested in more volume a year ago, consumers are now more addicted to the usage than they were in 2006 and early 2007, now we are more selective in terms of promo, and the net effect is that revenues are increasing.

Mr. Labriola.

Yes. On the fixed line what is happening is that this particular acknowledged situation allows us to push more on complete flat rate offers on the consumer side, because these kinds of offers seem to give to the customer, at a psychological level, the possibility to contain their level of expenditure. Instead, on the business side, perhaps there should be a big opportunity, let me use this kind of word, because, while in the past year companies preferred to buy equipment instead of renting it... while in this situation, with a lot of problems in terms of credit and cash, they could prefer to go back to solutions that are on a rental basis. This could allow us to launch a number of services based on manager service... way that could allow us to lock in some way the customers with Telecom Italia.

On capital structure, I would just like to say that unfortunately there are rumors on the market, we are not responsible for the rumors, the market is very nervous and it takes whatever is said around to drive up and down prices. So, I cannot comment on rumors, but what I can comment, and what we declared very explicitly several times, myself and also the Chairman, is that we don't need a capital increase.

*So, there isn't going to be... you will oppose any reserve capital increase to whatever funds... asked for? So you basically ask to buy on the market? To anybody...*

Sorry, I didn't... I didn't get it.

*So if for any funds that you would like to be (...) in Telecom Italia you would ask to buy on the market? You would never do any reserve capital increase?*

Everybody is free to buy on the market. So, they are welcome.

*No, I know that everybody is free, but from your side, you will never approve any reserve capital increase to any foreign fund ?*

**Well...**

*This is the question.*

**Well, it's not... it's not in the agenda now.**

*But... it's not in the agenda now, but could it be in the agenda later? Or, given the strong balance sheet that, basically, Telecom Italia has, you don't need it?*

**I think that... I mean, I think that I have answered very explicitly, so I think we have to move to the next question.**

*Thanks.*

**8. Mr. Justin Funnel from Credit Suisse:**

*Thanks. Could you, firstly, just elaborate a little bit on your comment during the call, that you are exploring some sort of financing with the bank, to 600 million euros; is that a bond, is that a loan? And is that in line with comments made at the half year results, that you don't want to fund or raise funding, I think above a 6% interest rate? Secondly, I think you also mentioned on the call, that the economy is affecting small business customers, as well as those segments you mentioned; was it correct doing that and could you outline it a little bit more? Is that in mobile and fixed? And does it explain, again, perhaps, some of the volume trends in fixed? Finally, a sort of big picture issue in Brazil is that the termination rates, which, I believe, some of your peers have up to 30% or more of their revenues coming from termination... the rates are there many outbound voice call, prices, the regulator is looking at termination rates and essentially bringing it down to cost at some point. I was wondering if at this stage, ahead of your review, you can outline a little bit what you plan and what you expect will happen to the termination rates in Brazil over the next 2 years, please?*

**I'll ask Marco Patuano to answer to your first question.**

**Yes, I confirm you that our debt structure is very healthy. We have a significant portion that is very long term, as I told you before, and I confirm that we have a very robust margin of liquidity that is increasing in the third quarter and we are now up to 5.8 billion, with a total liquidity margin of over 12 billion. So, confirm that we are not in the condition of getting financing at any cost. Of course, if some opportunity comes, for example, the European investment bank, which has a very attractive interest rate and, basically, not very much affected by the conditions of the market. Of course, we will attack it and we will do it, but we don't consider that, since the markets are very nervous and very volatile in the very short term we will touch base on different conditions we are in a condition, in a very lucky condition, that we can wait until the market climate is safer.**

**On the second question, I will ask Mr. Labriola to answer and on the third Mr. Cicchetti.**

**Okay, I'll better elaborate on the small business side. In the past year, one of the main difficulties that Telecom Italia was finding, trying to push services on a rent... on a rent monthly basis, was related to the fact that our customers prefer to buy equipment and to let them managed by other people, instead to rent and let it managed by Telecom Italia. In this situation, due to the difficulty to access credit facility by little companies, you in Italy we are in a particular situation where the main part of our business segment is made by little companies, what is happening is that it could be**

better preferred by this kind of company a solution that allows them to have the facility that they need to continue to work on their activity on a monthly... on a rent business. This is a good opportunity if we consider that we are going to launch, as Mr. Cicchetti mentioned during the presentation, a turn-key solution all-in-one for IP, for voice, data and management of all the internal facilities inside the company. So, we think that this could be an opportunity on our side. Related to the volume that you were asking more in detail about, on volume, on traffic, on the fixed line, what is happening is that... I shouldn't discuss about volume, I should discuss about pricing strategies. What we are describing in the past quarter is that Telecom Italia, already in the past, has pushed a lot in development of pricing strategy on a flat basis rate. This allows us to continue to keep customers on our network, except changes in volumes. The only number that you can show in terms of actual situation on volumes is that we continue to face a cannibalization of traffic volumes from mobile to fixed. But we don't see, at least today, any kind of cannibalization due to the economic crisis.

Third question Mr. Cicchetti.

The question, if I'm not wrong, is about the tariff adjustment in Brazil. I agree with you: there are a lot of discussions about the incoming traffic in Brazil, but as a matter of fact in July the so-called "boom" has been adjusted, with an increase of 2%, that means 0.42 reais. As you perhaps know very well, Brazil is a mobile market with a very high termination rate. This is structural in this market and there is also, let's say, the real explanation, the reason behind the very, very important growth of on-net traffic in all the operators' offers, and this is also, as I mentioned in my speech, one of the, let's say, most important moves that we did in our special plan, because we tried to increase the on-net traffic just to avoid this important outcome... outcome cash-out for the termination... for the termination traffic.

Thank you, Oscar. I will take one or more question.

9. Mr. James Britton from Nomura:

*Thank you very much. If you managed to get the full-line rental and the unbundling increase, can you just clarify for us the impact on your revenues on an annualized basis? And is there scope for increases half way, or is it likely to be all or nothing? And secondly, what is the interest rate available on the undrawn credit (...)? And then, finally, on the cash-flow statement: is there any share in the form of 50 million cash-in for the disposals in the quarter for just one way whether the rest is from the Alice sales and finally, cash taxes for Q4 ? Can you just give us an idea of what that might be?*

Well, on the first question. First of all, I cross fingers because we didn't get it yet, so we will enter into negotiations and therefore I cannot be very precise, neither I want to be very precise on this, but, perhaps, Mr. Talotta, our Chief Regulatory Officer, can give you a little bit of flavor on this.

Yes, good evening.

*Good evening.*

My only remark is quite simple. It's related to the number of unbundling customers, but has been developed in the last years in the competitive market. If it's like this, it's quite simple to know there are more or less 4 million unbundling lines. And the unbundling proposal made by Telecom Italia

has to consider also the margin squeeze related to the monthly rental fee residential, that has been proposed in the same period. So, what we expect is that the authority will consider and protect these very important regulatory underlines... but we are working on it. So, there are no final numbers to be delivered today.

Sorry, it's not because we cannot do the arithmetic, but we don't like to put up a figure now at the beginning of the negotiation process.

*Sure. Can you...*

The second question I'll have Marco Patuano answer.

Yes, you asked a forecast for liquidity for the end of the year. We are now 5.8 group, which is more than 5.3 Italy and the remainder in Brazil. We consider that at the end of the year, more than 5 billion will still be in our liquidity position.

And you also asked something on the cost of the facility. The cost of the facility is 27 basis points over the base rate.

Okay, thank you very much everybody. Sorry for keeping you late on Friday afternoon, but unfortunately we could do the Board meeting only today. We will try to avoid any other Board meeting next year on Friday and I wish you all a good weekend.

Thank you very much.

Ladies and gentlemen, the conference call is over. Thank you very much for your attention.