MOODY'S INVESTORS SERVICE

Credit Opinion: TDC A/S

Global Credit Research - 09 Feb 2016

Copenhagen, Denmark

Ratings

Category	Moody's Rating
Outlook	Stable
Issuer Rating	Baa3
Senior Unsecured	Baa3
Jr Subordinate	Ba2

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Key Indicators

[1]**TDC A/S**

	9/30/2015(L)	12/31/2014	12/31/2013	12/31/2012	12/31/2011
Scale (USD Billion)	**$3.8**	**$4.2**	**$4.3**	**$4.5**	**$4.9**
EBITDA Margin	**39.3%**	**41.4%**	**42.7%**	**41.8%**	**44.9%**
Debt / EBITDA	**3.8x**	**4.5x**	**2.8x**	**2.7x**	**2.3x**
FCF / Debt	**3.4%**	**0.8%**	**1.5%**	**2.5%**	**7.1%**
RCF / Debt	**17.3%**	**11.5%**	**16.6%**	**17.4%**	**22.1%**
(FFO + Interest Expense) / Interest Expense	**7.1x**	**7.2x**	**7.0x**	**6.8x**	**4.8x**
(EBITDA - Capex) / Interest Expense	**3.5x**	**4.0x**	**4.5x**	**4.2x**	**3.6x**

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. Source: Moody's Financial Metrics

Note: For definitions of Moody's most common ratio terms please see the accompanying User's Guide.

Opinion

Rating Drivers

- Small, integrated telecommunications company with limited international diversification

- Leading position in the highly competitive Danish market, with the CATV business regarded as a strategic asset

- High-quality landline infrastructure supported by heavy investment

- Operating performance in 2016 is expected to deteriorate, with stability in 2017 and growth in 2018

- Management´s commitment to an investment-grade rating implies a prudent financial strategy which is reflected in the cut in dividends recently announced

-Adequate liquidity risk management

Corporate Profile

TDC A/S (Baa3 stable) is the principal provider of fixed-line, mobile, broadband data services and cable television (CATV) offerings in Denmark. The company also provides telecoms services to business customers throughout the Scandinavian region. As of year-end 2015, TDC's reported EBITDA of DKK9.8 billion. The company's main market is Denmark, although it also has operations in Norway and Sweden.

Rating Rationale

TDC's ratings reflect our expectation that although operating pressures persist and reported EBITDA will fall in 2016 by DKK1.0 billion, management has designed a strategy to return to growth. As a result, we expect improving operating performance from 2017 onwards, based on cost reductions and better pricing environment. Dividend cut will help to preserve liquidity and financial metrics until this improvement can be realized, but ultimately we need to see the fundamental improvement materialize.

We recently affirmed the ratings because we believe that management will deliver on its recently announced new strategy, as well as: (1) the strength of the company's operations in Denmark, with strong market shares including 41% in the mobile segment; (2) the strategic fit and importance of all of TDC's subsidiaries, particularly its CATV business, youSee, which differentiates the company from its European peers and is an important part of the new strategy; (3) the company's relatively small size and low but increasing international diversification in Norway and Sweden; (4) its highly advanced network infrastructure; and (5) its appropriate liquidity risk management. However, the rating also reflects (1) the pressure on TDC's domestic operations, as a result of price declines caused by heightened competition in the Danish mobile market and regulation; (2) the company's strong cost control in order to maintain its EBITDA margin at above 40%; (3) TDC's rebranding strategy to have youSee as the prevalent consumer brand; and (4) its aim to combine its CATV and fixed telephony broadband offers in its various regions of operations.

DETAILED RATING CONSIDERATIONS

SMALL, INTEGRATED TELECOMMUNICATIONS COMPANY WITH LIMITED INTERNATIONAL DIVERSIFICATION

During 2015, TDC generated revenues of DKK24.4 billion solely from Denmark and the Nordic regions. The company's business remains heavily concentrated in Denmark, with its business there generating 77% of revenues and approximately 84% of reported EBITDA in 2015.

In October 2014, TDC acquired GET, the Norwegian cable-TV operator. The acquisition has enhanced TDC's existing operations in Norway, which were only focused on the business-to-business (B2B) segment. It has also enabled the company to leverage its current business and to diversify TDC's business model, thus creating potential growth opportunities outside Denmark. Notably, in order to lift profitability, GET aims to diversify from the current operational segment and to enter the mobile market through a mobile virtual network operator (MVNO) agreement.

LEADING POSITION IN THE HIGHLY COMPETITIVE DANISH MOBILE MARKET, WITH THE CATV BUSINESS REGARDED AS A STRATEGIC ASSET

TDC's multi-brand strategy enables it to retain strong market shares as a leading telecom operator in Denmark that provides traditional fixed-line, internet and mobile services. It is the largest provider of cable services in Denmark under its brand youSee.

TDC differentiates itself from its European peers as one of the few European telecom operators with a CATV business, because European regulators (within the EU) have generally required telecom companies to dispose of their cable businesses. This provides TDC with a strong competitive position, given that other cable operators represent a growing threat for European broadband/fibre operators. TDC has the ability to bundle high-quality services with growing demand for wireless internet (tablets and smartphones).

However, intense competition in the Danish mobile market has resulted in ongoing pressure on revenue and profitability, with continued falls in prices and investments. Meanwhile, average revenue per user (ARPU) has decreased steadily since 2011. Now that the Danish mobile merger between Telenor and TeliaSonera has been called off, there is a potential window of opportunity to raise prices in the mobile market, as all Danish players now contemplate how to improve currently insufficient returns on capital in a very competitive four-player mobile market setting. In this context, TDC started to increase entry-level prices in October 2015 and its competitors TeliaSonera (A3 stable) and Telenor (A3 stable) followed shortly afterwards. TDC brands, for instance, increased its cheapest All You Can Eat Packages pricing in two steps from DKK99 to DKK119.

Outside of the potential price increase opportunity, the outlook for mobile remains negative, especially on the B2B side where we expect significant ARPU pressure for the next 12 months. In consumer mobile, although some pressure remains, TDC benefits from success with its household-focus strategy and family offers. We do not expect stabilisation or market repair in the mobile sector until H1 2017.

Until now, TDC has been able to broadly sustain market shares through its low-cost and premium brands. As of December 2015, the company reported that it had a 64% market share in landline telephony (retail and wholesale), a 56% broadband market share, a 54% market share in TV (combining CATV, PayTV and internet protocol TV), and a 41% market share in mobile voice services. TDC is the market leader in all four segments in Denmark and we expected limited market share erosion supported by the new strategy management has shared with the market and is underpinned by a transformation of the company into a more agile, simpler and more efficient entity.

HIGH-QUALITY LANDLINE INFRASTRUCTURE SUPPORTED BY HEAVY INVESTMENT

Its highly advanced infrastructure, including cable ownership, provides TDC with strong network platforms both in fixed-line and mobile services. TDC's network strategy is to provide the best mobile and landline network in Denmark in terms of speed, coverage and quality. To achieve this, TDC plans to invest DKK25 billion through 2020, primarily in network infrastructure and customer installations. Over the past three years, TDC's capital expenditure (capex)/revenues has stood at 15%-18%, and we expect this metric to stabilize around 18%-19% as a proportion of sales, at approximately DKK4.2-4.5 billion. The step-up in capex will primarily be applied to TDC's high-speed broadband strategy. The fact that TDC runs simultaneously both a CATV and a telecom network differentiates it from its peers in the industry, enabling the company to segment and select the market, offering different technologies depending on demand and competition.

TDC has the largest and most extensive fibre network in Denmark and continues to bring fibre closer to its customers. Consequently, in 2014 and 2015 fibre was the largest type of investment in landline network technology as the build out of fibre network in Denmark continued. As an additional extension of TDC's fibre focus, in October 2014, TDC entered into a strategic partnership with Trefor, a Danish utility company and fibre network operator. The partnership will provide TDC Group with access to a comprehensive fibre network in the Danish B2B and business-to-customer markets (including 100,000 homes passed). TDC Group will take over operation of the network and implement a standard solution integrated with TDC Group's own operations and products.

Another strong boost to TDC's connectivity will come from the recently announced agreement with Huawei, which will enable the company to introduce DOCSIS 3.1 technology and its 1Gbps speed in Denmark. TDC also continued to expand its coax network in 2014, thereby increasing capacity and broadband speeds while accommodating increased demand for OTT services. The coax network now covers more than 50% of the Danish households.

With the acquisition of Get, TDC now has a state-of-the-art hybrid fibre coaxial-cable network in Norway, covering more than 700,000 homes. We foresee continued improvement of the 4G network in the mobile segment; TDC reached 99% 4G population coverage in Q1 2015. This will support increasing smartphone penetration and higher network usage, which will contribute to revenue stability in TDC's mobile segment.

CONTINUED FOCUS ON CUSTOMERS TO BECOME A TRUE PREMIUM PLAYER IN THE MARKET

TDC's new operational strategic focus mainly relies on connectivity, offerings and customer service in order to achieve a higher level of customer satisfaction and cash flow generation. The company's underlying objective is to reiterate and strengthen its premium positioning, which customers did not previously consider as such owing to TDC's infrastructure prior to upgrades over the past three years.

One of the main and most relevant actions undertaken by the company is the withdrawal of the TDC brand from the Danish consumer market. TDC integated the brand into youSee in mid-2016, due to its strong entertainment and broadband product offering. The integration of the two brands will lead to cost savings over three years of DKK200 million, supported by the combination of IT systems/processes, rationalisation of future capex and integration of offerings and related marketing expenditure.

Another strong factor will be the implementation of the "trim to save" plan, which the company expects to reduce operating expenses by DKK250 million in 2016. DKK150 million of these savings will be reinvested in new initiatives, leading to net savings of DKK100 million. Notably, the saving target over the three-year horizon amounts to DKK600-700 million. We note that the rebranding process could entail a degree of customer churn risk as (1) competitors could exploit the transition period to be aggressive and gain market share from youSee; and (2) the need to enhance the youSee brand to make it more attractive to customers. Moreover, the anticipated reengineering process could overshoot the company's expectation of completion by 2017. With the strong cost control focus helping to mitigate the continued pressure in operating performance, we expect TDC to maintain an EBITDA margin over 40% in the next 12-18 months.

TDC will focus strongly on its SMB and Enterprise segments after they represented the highest drag on 2015 EBITDA levels. Considering that SMB customers currently select operators according to price, the perception of TDC as a premium player will be the key to returning to growth in the segment; TDC will be advantaged if it can differentiate from its competitors through a superior infrastructure in both mobile and broadband. In this regard, we expect the churn of corporate customers to continue in 2016 and stabilise in 2017, as the pricing repositions towards the high-end of the market.

New targets have also been set for connectivity. TDC expects to expand Danish household coverage to 100%, 70% and 50% by 2018 for =10 Mbps, =100 Mbps and gigabit connections respectively. We consider the 1Gbps implementation as a strong competitive advantage in the future, as we expect the data usage to grow steadily, in both the consumer and business segment.

OPERATING PERFORMANCE IN 2016 TO DETERIORATE, WITH STABILISATION AND GROWTH IN 2017 AND 2018 RESPECTIVELY

TDC's 2016 operating performance is expected to deteriorate as a result of a number of factors including (1) high regulatory pressure evidenced by the unbundling of the cable network and abolition of roaming rates; (2) the aforementioned low prices driven by aggressive competition in both the mobile residential and business segments; (3) the termination/renegotiation at lower price of high margin public contracts; and (4) the recalibration of the product portfolio with high-priced products for the small and medium business segment.

In this regard, management guided for an 2016 EBITDA of DKK8.8 billion, with a reduction of some DKK1 billion compared to fiscal year 2015. Such a change will increase the company's Moody's-adjusted debt/EBITDA ratio to around 3.5x by end-2016. Under our expectations, TDC should also reach EBITDA stability in 2017 and growth in 2018, as operational performance improves supported declining pressure on prices.

We also continue to expect a further negative impact on revenue this year from the price adjustments and regulator-imposed roaming rates. We see limited downside regulatory risk in mobile as Mobile Termination Rates (MTRs) are now depressed, but further risk is possible on the fixed side. For example, there will be (1) further reductions in data roaming charges; (2) a review of the content and scope of the price control obligation; and (3) the possibility of a reintroduction of a price cap on some of TDC's services.

MANAGEMENT'S COMMITMENT TO AN INVESTMENT-GRADE RATING IMPLIES A CONSERVATIVE FINANCIAL STRATEGY

Notwithstanding the partially debt financed acquisition of GET in 2014, TDC remains committed to an investment grade rating. This was reiterated by the management decision to offset weaker cash flow generation through a revision of its shareholder remuneration policy in January 2016; shareholders returns will be based not only on financial performance and investment needs but even on the commitment to the rating. In this regard, cash dividend payments in 2016 were totally cancelled and will help to keep retained cash flow/debt above 20% in 2016. Retained cash flow (RCF) coverage ratios will worsen in 2017 as the company expects to pay the dividend (DPS guidance of DKK1).

Liquidity

We expect TDC's liquidity profile to remain robust over the next 12-24 months. In this regard, internal liquidity sources and available credit facilities will enable the company to more than cover its debt maturities and other expected cash demands over this period. As of December 2015, TDC had around DKK363 million in cash and cash equivalents. The company has committed credit facilities totalling EUR500 million (approximately DKK3.9 billion and maturing in September 2020) and EUR200 million (approximately DKK1.5 billion and maturing in December 2018), all largely undrawn. The maturity of the EUR 274m (approximately DKK2.0 billion) bond in December 2015 was repaid with cash and the drawing of a EUR100 million (approximately DKK760 million) bank credit facility, maturing in December 2015. The company converted the facility into a bank loan with a new maturity of December 2020. The following maturity will be in February 2018 when a EUR800 (approximately DKK6.0 billion) million bond will mature.

Rating Outlook

The stable outlook reflects our expectation that TDC will regain strong cash flow generation after capex through a combination of an improving pricing environment, more focused and agile marketing strategy, efficiency gains and capex optimisation. We have also taken into consideration the dividend reduction, which should help to preserve liquidity and credit metrics until a recovery in operating trends emerges. The outlook also reflects our expectation that TDC will execute the revised strategy, which will enable the company to stabilise its operating performance in 2017 and deliver growth from 2018 onwards.

What Could Change the Rating - Up

Although not currently expected, the rating could come under positive pressure on evidence that the company would achieve sustained improvements in its debt protection ratios, such as adjusted RCF/gross debt above 20% and gross adjusted debt/EBITDA trending to 2.5x, based on an improved business environment.

What Could Change the Rating - Down

We would consider downgrading TDC's rating if (1) the company were to deviate from the execution of its new strategy, as evidenced by deviation from a reported EBITDA of DKK8.8 billion for 2016; (2) the company were to embark on an aggressive expansion/acquisition programme, most likely outside of its existing footprint, leading to higher financial, business and execution risk; or (3) its credit metrics were to deteriorate, including adjusted RCF/gross debt falling to below 15% or adjusted gross debt/EBITDA trending towards 3.5x on an ongoing basis.

Other Considerations

Methodology grid: The Baa3 grid outcome reflects the combination of TDC's strong competitive position and high EBITDA margin, which compensate for its weaker cash flow metrics. As a result of persistent pressure in the domestic market, we expect mid-single digit revenue erosion in 2016. Lower cash flow generation will be compensated by the cut of dividend payment in 2016. Over the same period, we expect the company's EBITDA margin to exceed 40% as a result of its cost-cutting efforts. With regard to leverage, adjusted gross debt to EBITDA level is expected to be in the 3.4-3.5x region in 2016 and over 3.1x in 2017. We project adjusted RCF/debt at 21-22% in 2016 and 20-21% in 2017, as the dividend is expected to be distributed again, and adjusted free cash flow/debt at 5-7% over the same period. We also anticipate funds from operations coverage in the 6.5-7x range and (EBITDA minus capex)/gross interest expense at 3.5-4.0x.

Rating Factors

TDC A/S

Global Telecommunications Industry Grid [1][2]	**Current LTM 9/30/2015**		[3]**Moody's 12-18 Month Forward ViewAs of 2/4/2016**	
Factor 1: Scale And Business Model, Competitive Environment And Technical Positioning (27%)	**Measure**	**Score**	**Measure**	**Score**
a) Scale (USD Billion)	$3.8	Ba	$3.6	Ba
b) Business Model, Competitive Environment and Technical Positioning	A	A	A	A
Factor 2: Operation Environment (16%)				
a) Regulatory and Political	Baa	Baa	Baa	Baa
b) Market Share	A	A	A	A
Factor 3: Financial Policy (5%)				
a) Financial Policy	Baa	Baa	Baa	Baa
Factor 4:Operating Performance (5%)				
a) EBITDA Margin	39.3%	Baa	41.9%	A
Factor 5: Financial Strength (47%)				
a) Debt / EBITDA	3.8x	B	3.4x - 3.5x	Ba

b) FCF / Debt	3.4%	Caa	6.5% - 7%	Ba
c) RCF / Debt	17.3%	B	21% - 22%	Ba
d) (FFO + Interest Expense) / Interest Expense	7.1x	A	6.5x - 7x	Baa
e) (EBITDA - Capex) / Interest Expense	3.5x	Baa	3.5x - 3.7x	Baa
Rating:				
a) Indicated Rating from Grid		Baa3		Baa2
b) Actual Rating Assigned				Baa3

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. [2] As of 9/30/2015(L); Source: Moody's Financial Metrics [3] This represents Moody's forward view; not the view of the issuer; and unless noted in the text, does not incorporate significant acquisitions and divestitures.

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