MOODY'S INVESTORS SERVICE

Credit Opinion: TDC A/S

Global Credit Research - 13 Oct 2015

Copenhagen, Denmark

Ratings

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

Contacts

Analyst	Phone
Carlos Winzer/Madrid	34.91.768.8200
Ivan Palacios/Madrid	
Michael J. Mulvaney/London	44.20.7772.5454

Key Indicators

[1]**TDC A/S**

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

- Relatively small size telecom with low international diversification

- Strong competitive position in Denmark, with the CATV business regarded as a strategic asset

- High-quality landline infrastructure supported by heavy investment

- Expectations of sustained negative impact on revenues as a result of fierce price competition

- Restructuring processes and strong cost control partially mitigates challenging operating domestic environment

- Commitment to an investment-grade rating

- Solid liquidity profile

Corporate Profile

TDC A/S (Baa3 stable) is the principal provider of fixed-line and mobile voice communications, internet broadband data services and cable television (CATV) offerings in Denmark. The company also provides telecoms services to business customers throughout the Scandinavian region. TDC's revenues for the 12 months to 30 June 2015 amounted to DKK24.1billion (approximately EUR3.2 billion) and EBITDA of DKK9.9 billion (EUR1.3 billion). The company's main market is Denmark, although it also has operations in Norway and Sweden.

Rating Rationale

TDC's ratings reflect (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; (3) the company's highly advanced fixed-line infrastructure; and (4) its effective liquidity risk management.

However, the rating also reflects (1) TDC's relatively small size and low international diversification; (2) the increasing pressure on the company's domestic operations as a result of price declines caused by regulation and heightened price competition in the Danish mobile market; and (3) TDC's strong cost control in order to partly offset the recent deterioration in the company's EBITDA margin.

TDC's current rating also factors in the acquisition of GET AS in October 2014, which will temporarily weaken TDC's credit metrics beyond levels commensurate with the rating, although the company maintains its commitment to an investment grade rating.

DETAILED RATING CONSIDERATIONS

RELATIVELY SMALL SIZE AND LOW INTERNATIONAL DIVERSIFICATION

In the last-12-months to June 2015, TDC generated revenues of DKK24.1 billion (approximately EUR3.2 billion) solely from Denmark and the Nordic regions. Scale is important in this sector, as it (1) implies geographic and business diversity; (2) enhances a company's ability to absorb a temporary disruption, acquisition or a misjudged capital investment; (3) creates greater leverage with suppliers of network equipment or handsets; and (4) enhances access to capital markets.

The company's value remains heavily concentrated in Denmark, with its business there generating 75% of revenues and approximately 82% of total EBITDA.

As of October 2014, TDC acquired GET, the Norwegian cable-TV operator. The acquisition will enhance TDC's existing operations in Norway which were only focused on the B2B segment. It will also enable the company to leverage its current business and to also diversify TDC's business model, thus creating potential growth opportunities outside Denmark.

TDC could have a strategic interest to further diversify away from Denmark, while maintaining its current commitment to an investment grade rating.

LEADING POSITION IN A HIGHLY COMPETITIVE DOMESTIC 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 providing traditional fixed-line, internet and mobile services, and 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 price (ARPU (average revenue per user) down 20-30% since 2011) and investment, which is down more than 30% over the last 5 years. 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 returns on capital in a very competitive four-player mobile market setting. This context could result in new price increase attempts being more successful than past ones.

Outside of the potential price increase opportunity, the outlook for mobile remains negative, especially on the B2B side where significant ARPU pressure is expected for the next 18-24 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 as well as market repair in the mobile sector until H2 2016.

Until now, TDC has been able to broadly sustain market shares through its low-cost and premium brands. As of June 2015, the company reported that it had a 65% market share in landline telephony (retail and wholesale), a 57% broadband market share, a 53% 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.

HIGH-QUALITY LANDLINE INFRASTRUCTURE SUPPORTED BY HEAVY INVESTMENT

The combination of a 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 over the period 2011-20, primarily in network infrastructure and customer installations. Over the past three years, TDC's capital expenditure (capex)/revenues has been around 13% to 15%, and we expect this metric to slightly increase over the next few years to above 17% as a proportion of sales, above DKK4.1 billion. The step-up in capex will primarily be applied to TDC's high-speed broadband strategy and 4G rollout. 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 customers. Consequently, in 2014 fibre continued to be the largest type of investment in landline network technology, as 750km of fibre cables were added to TDC's network. 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 B2C markets (including 100,000 homes passed), while TDC Group will take over operation of the network and implement a standard solution integrated with TDC Group's own operations and products. 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 population. 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. In the mobile segment, we expect continued improvement of the 4G network (TDC reached a 99% 4G population coverage in Q1 2015) to support increasing smartphone penetration and higher network usage, which will contribute to revenue stability in TDC's mobile segment.

EXPECTATIONS OF SUSTAINED NEGATIVE IMPACT ON REVENUES AS A RESULT OF PRICE REGULATION

Denmark's telecommunications market is characterised by strong competition and is among the most strictly regulated markets in the EU, measured in terms of impact and development. We continue to expect negative impact on revenue (although less severe, around DKK200-300 million compared to the past, in excess of DKK600 million) from the pricing model and regulator-imposed roaming rates. We see limited downside regulatory risk in mobile with MTRs now depressed, but see further risk on the fixed side. For example, there will be further reductions in data roaming charges as well as a review of the content and scope of the price control obligation and the possibility of a reintroduction of a price cap on some of TDC's services.

RESTRUCTURING PROCESSES AND STRONG COST CONTROL MIGHT NOT BE SUFFICIENT TO MITIGATE CHALLENGING DOMESTIC OPERATING ENVIRONMENT

Although we estimate the company's EBITDA margin at around 40% for this year, there is continued pressure on gross profit as well as on revenues; we expect organic revenue erosion in the low-single-digit percentages in 2015 and an organic revenues decline of some 1.5% in H1 2015. This is as a result of price declines which derive from: (1) pressure on the consumer mobile segment owing to the aggressive campaign promoting the low costs/no frills segment becoming market standard, including competitors increasingly using handset subsidies in premium brands such as Telenor; and (2) regulation. An organic EBITDA decline of 7.5% in H1 2015 and an acknowledgement that pressures are likely to continue into H1 2016 is a reminder that TDC's ability to pull the cost lever to offset its revenue challenges has weakened.

We believe that the company will be able to continue to partly offset much of the impact of possible further price erosion though the continued focus on (1) differentiation through customer care, service quality and breadth of product offering, thereby strengthening the company's position in the domestic pay-TV markets; and (2) efficiency improvements, although at a reduced pace of cost cutting is expected as cost cutting becomes more difficult.

COMMITMENT TO AN INVESTMENT-GRADE RATING

Notwithstanding the partially debt finance acquisition of GET in 2014, TDC remains committed to an investment grade rating. With regard to TDC's financial policy, we expect a temporary deterioration following the acquisition of GET, especially as regards to the ratio of adjusted gross debt/EBITDA, which increased to approximately 4.5x in 2014 before decreasing to 3.2x this year. Although TDC's management has reduced the dividend pay out to approximately 60% from 90% in order to enhance free cash flow and offset the above negative effect on leverage, this credit-supportive action will not fully offset the higher financial risk related to the GET transaction.

Liquidity

We expect TDC's liquidity profile to remain solid over the next 12-24 months; internal liquidity sources should enable the company to cover its debt maturities and other expected cash demands over this period. As of June 2015, TDC had DKK593 million (approximately EUR70 million) in cash and cash equivalents. The company has recently renewed its credit facilities totalling EUR500 million (around DKK3.7 billion), now maturing in 2020 and EUR200 million (approximately DKK1.5 billion) now maturing in 2018. In February 2015, the bank bridge loan from the acquisition of GET (EUR1.6 billion, approximately DKK12 billion), was refinanced through a combination of senior unsecured EMTN (Euro Medium Term Notes) bonds (EUR800 million, approximately DKK5.9 billion, 12 years maturity) and hybrid capital (EUR750 million, approximately DKK5.6 billion). In addition, the EUR800 million (approximately DKK5.9 billion) bond that matured in February 2015 was refinanced with bank loans (EUR650 million) and cash. Except for the DKK2 billion (approximately EUR270 million) bond maturing in Q4 2015, TDC has no bond maturities before 2018, where the EUR800 million bond (approximately DKK5.9 billion) is coming due.

Rating Outlook

The stable outlook reflects our expectation that TDC will maintain strong cash flow generation after capex through a combination of operating stability, efficiency gains and capex optimisation. We have also taken into consideration the dividend reduction. The outlook also reflects our expectation that TDC will retain financial metrics that are commensurate with a Baa3 rating, including adjusted retained cash flow (RCF)/gross debt around 20% and a gross adjusted debt/EBITDA of below 3.3x.

What Could Change the Rating - Up

We do not currently expect to upgrade TDC's ratings. However, any significant strengthening of the company's debt protection ratios - as a result of improvements in its operational cash flows and a reduction in debt - could have upward rating implications. 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 could downgrade TDC's rating if (1) 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 (2) 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 organic revenue erosion in the mid-single-digit percentage points in 2015 and 2016, which will partially affect cash flow. 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 TDC's financial policy, we expect a temporarily deterioration following the acquisition of GET, especially as regards to the ratio adjusted debt to EBITDA which deteriorated to 4.5x in 2014 (2.8x in 2013) before decreasing to around 3.2x in 2015, where we expect to be maintained in 2016. We expect adjusted RCF/debt at around 18%-20% in 2015 and 2016, and adjusted free cash flow (FCF)/debt below 4% in those years. We also anticipate funds from operations (FFO) coverage in the 7.0x-8.0x range and (EBITDA minus capex)/gross interest expense around 4.0x/5.0x.

Rating Factors

TDC A/S

Global Telecommunications Industry Grid [1][2]	**12/31/2014**		[3]**Moody's 12-18 Month Forward ViewAs of 9/17/2014**	
Factor 1: Scale And Business Model, Competitive Environment And Technical Positioning (27%)	**Measure**	**Score**	**Measure**	**Score**
a) Scale (USD Billion)	$4.2	Ba	$3.5-$4.0	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	41.4%	A	41%-44%	A
Factor 5: Financial Strength (47%)				
a) Debt / EBITDA	4.5x	B	3.0x	Ba
b) FCF / Debt	0.8%	Caa	<4%	Caa
c) RCF / Debt	11.5%	B	18%-20%	B
d) (FFO + Interest Expense) / Interest Expense	7.2x	A	7.0x-8.0x	A
e) (EBITDA - Capex) / Interest Expense	4.0x	Baa	4.0x-5.0x	Baa
Rating:				
a) Indicated Rating from Grid		Baa3		Baa3
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 12/31/2014; Source: Moody's Financial Metrics [3] This represents Moody's forward view; not the view of the issuer

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