



**MAKEDONSKI TELEKOM AD SKOPJE**  
KEJ 13 NOEMVRI NO. 6, 1000 SKOPJE, R. MACEDONIA

**ANNUAL REPORT**  
**on the operations of the Group of Makedonski Telekom AD - Skopje in 2013**

*On 13 February 2006, Magyar Telekom Plc., the controlling owner of Makedonski Telekom AD – Skopje (the Company), (via Stonebridge Communications AD - Skopje, majority shareholder of the Company), announced that it was investigating certain contracts entered into by another subsidiary of Magyar Telekom Plc. to determine whether the contracts were entered into in violation of Magyar Telekom Plc. policy or applicable law or regulation. Magyar Telekom's Audit Committee retained White & Case, as its independent legal counsel to conduct the internal investigation. Subsequent to this, on 19 February 2007, the Board of Directors of the Company, based on the recommendation of the Audit Committee of the Company and the Audit Committee of Magyar Telekom Plc., adopted a resolution to conduct an independent internal investigation regarding certain contracts in Macedonia.*

*Based on publicly available information, as well as information obtained from Magyar Telekom and as previously disclosed, Magyar Telekom's Audit Committee conducted an internal investigation regarding certain contracts relating to the activities of Magyar Telekom and/or its affiliates in Montenegro and Macedonia that totaled more than EUR 31 million. In particular, the internal investigation examined whether Magyar Telekom and/or its Montenegrin and Macedonian affiliates had made payments prohibited by U.S. laws or regulations, including the U.S. Foreign Corrupt Practices Act (the "FCPA"). The Company has previously disclosed the results of the internal investigation.*

*Magyar Telekom's Audit Committee informed the U.S. Department of Justice (the "DOJ") and the U.S. Securities and Exchange Commission (the "SEC") of the internal investigation. The DOJ and the SEC commenced investigations into the activities that were the subject of the internal investigation. On 29 December 2011, Magyar Telekom announced that it had entered into final settlements with the DOJ and the SEC to resolve the DOJ's and the SEC's investigations relating to Magyar Telekom. The settlements concluded the DOJ's and the SEC's investigations. Magyar Telekom disclosed the key terms of the settlements with the DOJ and the SEC on 29 December 2011. In particular, Magyar Telekom disclosed that it had entered into a two-year deferred prosecution agreement (the "DPA") with the DOJ. The DPA expired on 5 January 2014, and further to the DOJ's request filed in accordance with the DPA, the U.S. District Court for the Eastern District of Virginia dismissed the charges against Magyar Telekom on 5 February 2014.*

*According to the information provided to the Company by Magyar Telekom Plc., on 2 December 2009, the Audit Committee of Magyar Telekom Plc., provided the Magyar Telekom's Board of Directors with a "Report of Investigation to the Audit Committee of Magyar Telekom Plc." dated 30 November 2009 (the "Final Report"). In relation to the issuance of the Final Report and the information provided to the Company by Magyar Telekom, in January 2010 the Chairman of the Company's Board of Directors requested third party legal and tax expertise for assessment of the potential accounting and tax implications arising from the transactions conducted by the Company and its subsidiary (T-Mobile Macedonia) subject to the Final Report.*

*The external experts prepared reports (the "Reports") on their assessment and submitted the Reports to the Chairman of the Company's BoD and the Management of the Company and its subsidiary accordingly. As a result, based on the analysis of the Tax and Legal experts and information available to the Management related to the transactions subject of the Final Report, amount of MKD 248,379 thousand has been identified as potential tax impact, together with related penalty interest, as of 31 December 2009 arising from the transactions conducted by the Company and its subsidiary subject to the Final Report. In 2010 the amount related to the identified potential tax impact, together with related penalty interest, amounted to MKD 261,834 thousand out of which MKD 227,972 thousand related to the Company were paid in 2010 upon an executive decision issued by*

the Public Revenue Office. In 2012 the amount of MKD 36,724 thousand related to the identified potential tax impact, together with related penalty interest, in the subsidiary was paid upon an executive decision issued by the Public Revenue Office. In addition, the value of one contract of MKD 105,147 thousand capitalized within treasury shares was reclassified and derecognized against the Retained earnings. The other contracts that were identified by the Final Report and the reports of the tax and legal experts related to transactions undertaken by the Company and its subsidiary were expensed in the related periods (2001-2007).

In May 2008, the Ministry of Interior ("MOI") of the Republic of Macedonia ("RoM") submitted to the Company an official written request for information and documentation regarding certain payments for consultancy services and advance dividend, as well as certain procurements and contracts. In June 2008 the Company submitted copies from the requested documents.

In October 2008, the Investigation Judge from the Primary Court Skopje 1 – Skopje (the criminal court), has issued an official written order to the Company to handover certain original documentation. Later in October 2008, the Company officially and personally handed over the requested documentation. Additional MOI requests in written were submitted and the Company provided the requested documentation.

The Primary Court Skopje 1 in Skopje, Investigative Department for Organized Crime delivered a summon to the Company in connection with the criminal charges against the former CEO of Makedonski Telekom AD- Skopje, Mr. Szendrei, the former CFO of the company, Mr. Plath, the former member of the BoD in Stonebridge and former member of the BoD in Makedonski Telekom AD – Skopje, Mr. Kefaloyannis and the former CEO of the Stonebridge, Mr. Kisjuhász and asked for a statement whether the Company has suffered any damages on the basis of the said consultancy contracts.

On the hearing held on 13 April 2009, the representatives of Makedonski Telekom AD Skopje declared the position of the Company that taking into consideration the ongoing independent internal investigation conducted by White & Case, approved by the Company's BoD, it was premature to preannounce any damage which may be caused by means of the implementation of the mentioned contracts or with reference to them. An expertise was performed on 11 May 2010 and the experts from Ministry of Justice of the Republic of Macedonia – Court Expertise Office – Skopje, asked for some additional documents from Company's side in order to prepare the expertise. The Company has collected and submitted the requested information/documentation to the Court Expertise Office.

On 14 March 2011, the Company received from the Primary Court Skopje 1 a copy of the "Finding and Opinion", dated November 2010, issued by the Bureau of Judicial Expertise to the Primary Court Skopje 1 as a result of the expertise procedure. The "Finding and Opinion" addresses and contains conclusions regarding five contracts entered into with Chaptex and Cosmotelco in 2005 and 2006 and formerly reviewed by the Audit Committee of Magyar Telekom. The "Finding and Opinion" concludes that, based on these contracts, expenditures in the amount of EUR 3.975 million were made by the Company and Stonebridge to Chaptex "without evidence for performed services"; accordingly, shareholders of the Company and Stonebridge in the proportion of their shareholding, suffered damages in the aforementioned aggregate amount as result of decreased proceeds for payment of dividend in 2005 and 2006.

Based on publically available information, we understand that the Public Prosecutor has filed an indictment in 2011 against Mr. Szendrei, Mr. Kisjuhász and Mr. Plath, but not against Mr. Kefaloyannis. The Company, as a damaged party in this case, has not received an official court invitation for the hearing.

Pursuant to the questions posed by the investigative judge, it could be concluded that the public prosecutor has addressed the Company as a party damaged by the actions of the defendants. However, based on the content of the order for expertise issued by the investigative judge, and on the basis of the expert opinion, it can be concluded that now damaged parties are shareholders of the Company (Stonebridge AD Skopje, the Republic of Macedonia and minority shareholders) and therefore the state budget, as the Republic of Macedonia is a shareholder in the Company. Therefore, the public prosecutor should clear out who is considered as damaged party in this particular case, which is of significant importance for the position of the Company in this proceeding and its further actions. At the moment there aren't any indications that the Company could be found liable and made to pay any penalties or fines for the criminal procedure which is initiated against the individuals and accordingly the Group did not record any provision.

On 23 February 2012 the Company received a request for documentation from the Financial Police Office of the Ministry of Finance of the RoM related to certain consultancy contract and underlying documentation, which were also provided to White & Case during the internal investigation. The Company responded to the request accordingly.

*We have not become aware of any information as a result of a request from any regulators or other external parties, other than as described above, from which we have concluded that the financial statements may be misstated, including from the effects of a possible illegal act.*

This Annual Report on the Operation refers to the Group of Makedonski Telekom AD - Skopje, which includes Makedonski Telekom AD – Skopje (hereinafter referred to as: “MKT”), T-Mobile Macedonia AD Skopje (hereinafter referred to as: “TMMK”) and the e-Macedonia Foundation – Skopje (hereinafter jointly referred as the: “the Group”). MKT is a joint stock company incorporated and domiciled in the Republic of Macedonia for the provision of telecommunication services. The MKT’s immediate parent company is AD Stonebridge Communications – Skopje, solely owned by Magyar Telekom Plc., registered in Hungary. AD Stonebridge Communications – Skopje was under voluntary liquidation by the end of 2013 and from January 2014 its status has changed and is no longer under liquidation procedure. The ultimate parent company is Deutsche Telekom AG registered in the Federal Republic of Germany.

MKT is the primary fixed line service provider in Macedonia. MKT’s objectives for the forthcoming years comprise being a leading provider of technology in Macedonia and providing quality services with attractive prices in order to be prepared for the increasing competition.

MKT provides traditional fixed line telecommunication services and content services within the scope of the fixed line network, broadband services and integrated solutions, including TV over Internet Protocol (“IPTV”).

In January 2014, MKT successfully completed the All IP Transformation Project and the last customer on the public switched telephone network (“PSTN”) was migrated to IP Multimedia Subsystem (“IMS”) platform. The IMS platform enables the use of different advanced and innovative services in the fixed telephony.

TMMK is the leading mobile service provider in Macedonia, dedicated to provide up-to-date technologies and advanced service offerings, commensurate to the highest technological and service standards.

In 2013, mobile voice revenues contributed with 43.3% to the total revenues, while 21.7% of the total revenues of the Group were generated from fixed line voice services. The fixed line internet and data services revenues contributed with 12.5%, while mobile internet and data services revenues contributed with 8.6% of the total revenues.

The fixed line voice revenues still mark a downward movement, mainly due to the decreased number of fixed-line customers and a decrease of the outgoing traffic. IPTV revenues have grown mainly due to the growing IPTV subscriber base. Mobile voice revenues decrease is driven by the lower voice retail revenues as higher outgoing minutes could not offset the lower subscription fees as a result of new promotions and offers reflecting the strong competition, and the decline in the post-paid customer base.

At the end of 2013, MKT had 266,620 voice access fixed lines compared to 291,328 at the end of 2012. The fixed line penetration was marked with a similar movement, stabilizing at 13.4% at the end of 2013. The number of total DSL access increased to 185,514 at the end of 2013, compared to 172,166 at the end of 2012. The number of IPTV customers at the end of 2013 reached 87,686 customers (including 3 Play, IPTV only and 2 MAX) marking more than 30% increase from the end of 2012. The number of Fiber to the Home (“FTTH”) customers reached 23,594 at the end of 2013.

TMMK had a customer base of 1,195,250 at the end of 2013, compared to 1,181,437 at the end of 2012. The mobile market penetration in Macedonia is 108.4%, which shows the trend of individuals owning multiple SIM cards. As a result of the market saturation, TMMK especially focuses on retaining the customers in order to protect the market share.

The Macedonian mobile market was characterized by highly competitive campaigns and offers in 2013. Due to the increased competitiveness and in order to prevent the churn and encourage the usage, TMMK launched various campaigns, price plans and additional services specially designed to meet the subscribers’ needs, with a focus on value instead of price. These offers are targeting different customer segments.

In 2013, TMMK introduced several products that differentiate TMMK on the mobile market and provide additional

value for the customers.

TMMK is continuously working on creating a market demand for mobile Internet and stimulating mobile data usage via device/data price plans.

## **Regulation and Pricing**

The Macedonian law concerning the electronic communications (Law on Electronic Communications - "LEC") was enacted on 5 March 2005. Thus, by means of certain transitional provisions, the country's telecommunication regulations were harmonized with the European Union ("EU") regulatory framework. Furthermore, a number of strict obligations for the existing operators were stipulated. In December 2013, a public debate was opened for a new draft LEC in order for the LEC to be aligned with the EU Framework Directives 2009. The new law is expected to be enacted in the first quarter of 2014.

On 29 June 2011 MKT was designated as a Universal Service ("US") provider for fixed telephony services, public payphones and equivalent access for disabled end-users for a five year period starting from 1 January 2012. In 2013 a USO fund was established, in which all telecommunications operators with annual turnover above 100 thousand EUR in Macedonia are participating.

On 13 December 2013, MKT received a Resolution of the Agency for Electronic Communications (the "Agency") for determination of net cost for provision of universal service for 2012 in the total amount of 41million MKD (669 thousand EUR).

The services encompassed by the universal service for which MKT has received reimbursement from the universal service fund are:

- Access to public telephone services at a defined fixed geographic location: 14,246,771 MKD (231,654 EUR).
- Reasonable number of public pay phones: 14,311,910 MKD (232,714 EUR).
- Ensuring conditions for equivalent access to and use of publicly available telephone services for disabled end-users: 12,596,969 MKD (204,829 EUR).

The request for reimbursement from the USO fund for investment for improvement of the quality of service for 2012 in the total amount of 124 million MKD (2 million EUR) is refused as unfounded.

## **Regulation of Fixed Line Business**

In line with the data for the development of the telecommunications market published in the third quarter of 2013 by the Agency, the Agency had registered 61 providers of public fixed telephony services until 31 December 2013, but not all of them are active. The Agency proposed the deletion of the inactive providers during 2014.

Under the LEC, MKT has been designated as an SMP operator on the market of fixed line voice telephony networks and services, including the market of access to the networks for data transmission and leased lines. MKT, as an SMP operator, has the obligation to enable its subscribers to access publicly available telephone services of any interconnected operator with an officially signed interconnection contract.

According to the current bylaws, MKT has an obligation to publish reference offers for the wholesale products for interconnection, Unbundling Local Loop ("ULL"), local Bit-stream Access ("BSA"), Wholesale Line Rental ("WLR"), Reference Access Offer for access to ducts and dark fiber ("RAO") and wholesale leased lines. Initial Fiber to the "x" ("FTTx") regulation was introduced in the second quarter of 2011 with the obligation for Reference Access Offer ("RAO") for ducts and dark fiber imposed on MKT by the Agency. The approved reference offer was published on 5 December 2011 and is fully in line with the introduced Rulebook for specific network access and elements and applicable as of 1 January 2012. Retail regulation of fiber products was announced by the Agency on the first public meeting in May 2013 and it was included in the draft document for the Agency annual working plan for 2014, published on 18 October 2013 as a proposal for market analyses of Market 2 – Retail market for publicly available telephone services on fixed location. Market analyses for terminating and trunk segments (markets 9 and 10), broadcasting transmission services (Market 13), physical access to network infrastructure (Market 7), wholesale

broadband services (Market 8), wholesale access, origination and termination in mobile networks (Market 11 and Market 12) are also announced and expected in 2014/2015.

In August 2012 the Agency published the draft results from its own-developed LRIC Bottom-up costing model for Local Bit-stream (cost based) and for retail and wholesale Leased Lines, ducts and dark fiber and minimal set of leased lines (cost based). As a result, on 15 January 2013, the Agency brought a decision for decrease of the fees and approved the changed Reference offer for provision of physical access and usage of electronic communication infrastructure and associated facilities (ducts and dark fiber). The new fees are applicable from 1 February 2013. VIP Operator and ONE signed RAO contracts with MKT in 2013 for access to MKT's ducts.

The Reference offers for Wholesale digital leased lines ("WS DLL"), Local Bit-stream access and Minimal set of leased lines were also approved by the Agency and new changed methodologies of calculation of prices (length-dependent) were implemented. The WS DLL and Local Bit-stream access fees have been decreased as of 1 December 2012 and the fees for minimal set of leased lines as of 1 January 2013.

The Number Portability ("NP") procedures are an obligation that arises from the LEC and the Number Portability Rulebook for all operators in Macedonia. The deadlines for porting are two days in a fixed network and one day in a mobile network. A beep signal is also introduced in the networks of MKT and TMMK, which informs the customers that their call is made towards a ported number. The signal is unified for all operators.

In December 2013, the Agency opened a public debate upon the Numbering Plan of the RM, wherein Number portability rulebook and assignment of numbers and series of numbers from the numbering plan were enacted. The implemented changes for terminating the use of geographical numbers are in line with the forthcoming implementation of IP technology in operators' networks. The changes are applicable from 1 January 2014.

### **Regulated retail prices**

Under an obligations arising from Article 49 of the LEC (retail price regulation), followed with the amendments in July 2012 of the Rulebook for retail regulation, the Agency specified the manner and procedure for regulation of the retail prices for fixed voice telephony networks and services of the operator with significant market power on the relevant retail markets. MKT is an operator with SMP status on the relevant retail market 1 (access to the public telephone network at a fixed location) and market 2 (publically available telephone services at a fixed location). The prices for retail products offered on these two markets are subject of regulation by the Agency. The regulation of the retail prices is ex-ante, meaning that the Agency has to approve each price introduction, price change on every product or promotion prior to its being launched in retail. The ex-ante regulation is based on price squeeze methodology.

Regarding the individual pricing offers, especially tenders for mobile telephony, MKT and TMMK are faced with a constant pressure from the competitors which are in a position to offer lower prices, usually below costs, in order to increase their customer base as a result of the under-regulation.

### **Regulated Wholesale Prices**

MKT has a cost based price obligation for the Regulated wholesale services, using LRIC. The results from the Bottom - up LRIC costing model are implemented as of 1 April 2011.

As of 1 November 2011, MKT stopped offering PSTN and ISDN services for its customers as well as for its wholesale partners and all newly committed services are based on Internet Protocol ("IP") technology. In line with the PSTN migration of the MKT network, the Agency approved the proposed modifications of the WLR Reference Offer and BSA Offer of MKT applicable as of 1 January 2012. MATERIO was changed on MKT's initiative from 1 May 2012, and lower fixed termination rates (for origination, termination and transit) for 25% were approved by the Agency. The IP MATERIO (Internet Protocol Reference Interconnection Offer of MKT) was submitted for approval to the Agency in October 2013 on MKT's initiative, in line with the conclusions of the market analyses for submission of MATERIO changes with description and conditions for IP interconnection. The Agency approved the IP MATERIO on 27 December 2013. The changes are effective from 1 January 2014. Other fixed operators are ready for IP Interconnection, whereas the mobile operators cause certain delay in the introduction of IP Interconnection with

mobile network.

On 3 September 2013 MKT published its amended BSA offer and introduced wholesale ADSL packages for testing of internet services in line with MKT's retail offers. In addition, amended wholesale ADSL packages were introduced in October 2013 with a broadband on demand service enabled for use in a period of 3 days or 7 days, in line with the retail portfolio of MKT.

The Agency approved new prices for duct rental services on 18 January 2013, decreasing the prices previously set by MKT by more than 50%. The prices were determined by the Agency according to the LRIC methodology.

The new measures in line with MKT's SMP obligation on wholesale markets for fixed call origination (market 4), termination (market 5) and transit (market 6) from the final document include: implementation of IP interconnection by 2016 at the latest for fixed and mobile operators, transitional period for IP interconnection for alternative fixed and mobile operators up to three years, submission of updated MATERIO with IP IC description (service and fees) and conditions by 31 October 2013 at the latest. The other measures for Market 4, 5 and 6 are the same as before (interconnection and access, access to specific network facilities, carrier selection ("CS") and carrier pre-selection ("CPS") transparency, non discrimination, accounting separation, price control and cost accounting).

In June 2013, the Agency announced starting of the first analysis on the wholesale market number 13 (Transmission of broadcasting content to end users) and on 14 June 2013 announced starting of second analysis of market 9 and 10 (Transmission and termination segments of LL) and also on market 7 (Physical access to network infrastructure). The analysis is expected to be finished by the end of the first quarter in 2014 and published for public hearing.

## **Regulation of Mobile Business**

TMMK has frequency usage rights for the following radiofrequencies for public mobile communication systems:

- 2 x 12.5 MHz in the 900 MHz (GSM) band, validity period: 8 September 2008 – 8 September 2018 (10 years)
- 2 x 10 MHz in the 1800 MHz band, validity period: June 9, 2009 – 9 June 2019 (10 years)
- 2 x 15 MHz + 5 MHz in the 2100 MHz band, validity period: 17 December 2008 – 17 December 2018 (10 years)
- 2 x 10 MHz in the 800 MHz band, validity period: 1 December 2013 – 30 November 2033 (20 years)
- 2 x 15 MHz in the 1800 MHz band, validity period: 1 December 2013 – 30 November 2033 (20 years)

The competitor One has frequency usage rights for the following radiofrequencies for public mobile communication systems:

- 2 x 12.5 MHz in the 900 MHz (GSM) band
- 2 x 10 MHz in the 2100 MHz band
- 2 x 10 MHz in the 800 MHz band
- 2 x 15 MHz in the 1800 MHz band

The competitor VIP has frequency usage rights for the following radiofrequencies for public mobile communication systems:

- 2 x 10 MHz in the 900 MHz (E-GSM) band
- 2 x 10 MHz in the 1800 MHz band
- 2 x 10 MHz in the 800 MHz band
- 2 x 15 MHz in the 1800 MHz band

Thus, the spectrum for public mobile communications in the 800 MHz, 900 MHz and 1800 MHz bands is fully assigned to the 3 mobile operators. There is a remaining available spectrum in the 2100 MHz band, and the 2600 MHz band is not assigned for public mobile services at all.

The retail services provided by the mobile network operators in Macedonia are currently not subject to price regulation.

Since 2007, TMMK and ONE have been designated with an SMP status on the wholesale market for voice call

termination services in mobile communication networks, whereby several obligations were imposed on them, such as: interconnection and access, non-discrimination in interconnection and access, accounting separation and price control and cost accounting.

TMMK's first Referent Interconnection Offer was approved by the Agency in July 2008. Based on the second round analysis of wholesale call termination services in public mobile communication networks on 30 July 2010, TMMK received a Decision for changing the RIO by which the Mobile Termination Rate ("MTR") was defined with a glide path decrease in a timeframe of four years (until 2013). In September 2011, the price for the national MTR was decreased to 3.1 MKD/min. and was planned to continue decreasing by 0.1 MKD/min. each year, down to 2.9 MKD/min. by September 2013. At the same time, the Agency regulated the MTRs for ONE and VIP (VIP was designated with SMP on this market in the second round analysis) with a four year glide path. In May 2012, the Agency made a revision of the calculation of MTR of all three mobile operators and imposed new glide path. As from 1 June 2012 until 31 August 2013, TMMK's MTRs were set at 3.0 MKD/min., while ONE and VIP Operator's MTRs were set at 4.0 MKD/min. MTR symmetry to 1.2 MKD/min. calculated using Bottom-up LRIC+ were applied from 1 November 2013 (based on a new Agency Decision brought in August 2013), and a further decrease to 0.9 MKD/min. calculated using Bottom-up pure LRIC will be applied from 1 September 2014.

On 11 October 2013, Albatone, the first MVNO on the Macedonian telecommunication market hosted by ONE, started with its operations.

After the first analysis of the wholesale SMS termination market in 2011, all 3 mobile operators were designated with SMP status. In 2013 the Agency conducted a second round analysis on this market and imposed new regulated prices – symmetrical for all 3 operators and 75% lower than the previous ones. The prices became effective on 1 January 2014.

An auction procedure concluded in August 2013 awarded the whole 790 – 862 MHz band together with the unassigned spectrum in the 1740 – 1880 MHz band for LTE technology in a public tender. Each of the 3 Macedonian mobile operators acquired an LTE radiofrequency license of 2x10 MHz (in the 790 – 862 MHz band) and 2x15 MHz (in the 1740 – 1880 MHz band). Each license was acquired for a one-off fee of EUR 10.3 million (MKD 634,011 thousand). TMMK will retain the license for 20 years, until 1 December 2033, with an extension option for 20 years in accordance with the LEC.

In 2013, after the analysis of the wholesale market for call termination in public telephone network at fixed location, TMMK was designated with an SMP status on this market by an Agency decision and ordained to modify its reference offer. The regulation relates to the fixed services of TMMK realized by using the Wholesale Line Rental of MKT. In accordance with the Wholesale Line Rental Reference Offer of MKT, TMMK is using MKT's network and the interconnection (termination) of a call is done and charged by MKT. TMMK submitted a modification of its reference offer for approval to the Agency, and initiated an appeal to the Agency's decision before the Administrative Court. The modifications were approved by the Agency on 26 December 2013, and the new regulated service was implemented in TMMK's RIO as from 27 December 2013.

### **Audiovisual and Media Regulation**

In May 2013, the Macedonian Parliament adopted a Law on film production, amended in January 2014, imposing obligations for payment of annual fee by all cable operators (retransmission) and operators that provide Internet services. The fees are defined as follows:

- 1% from the revenue of cable operators which are operating with TV broadcasting program services
- 1% from the revenue of the entities that provide Internet services
- 2% from the revenue of the legal entities which are operating in the distribution, rental and sale of movies

The above-mentioned fees are applicable as of 2014, calculated on the level of the related revenues from 2013.

The Law on Audio and Audiovisual Media Services entered into force on 3 January 2014. The Agency for Audio and Audiovisual Media Services, the legal successor of the Broadcasting Council, has the right and obligation to conduct program supervision of the program packages that are retransmitted by the operators of public electronic communications networks.

MKT, as a provider of audio or audiovisual media service on demand, has editorial responsibility regarding the selection or the content of the service. It is obliged to keep the audiovisual media service on demand unchanged at least 30 days after its being made available to the users.

Additional obligations imposed by the law and affecting MKT are:

- If a program is subtitled in a language different from the language used originally when the program was produced, it has to be subtitled in Macedonian or in the language of the community that is not a majority, but is spoken by at least 20% of the population in the Republic of Macedonia, except for teleshopping and advertising programs.
- Annual fee for the surveillance carried out by the Agency, in the amount of 0.5% of the total revenues earned by the retransmission and 0.5% of the total revenues earned for on demand activity, has to be paid to the Agency.
- Local program services can be transmitted within their service area and public broadcasting services funded by the broadcasting fee have to be transmitted and free of charge.
- In its subscription agreements, MKT has to specify the list of program services which are currently retransmitting in its program package.
- The internal television channel output, i.e. the signal of that channel has to be recorded fully and without interruption and the recording has to be available at least 30 days after broadcasting.
- MKT is obliged to keep the catalogue and the content of the audiovisual media service on demand for at least 30 days after its being made available to the users.
- Obligation for promotion of European audiovisual works.
- MKT is obliged to deliver the output signal continuously to the location for collecting signals for monitoring purposes.

MKT, along with all other providers, has a period of nine months starting from the date of the entry into force of the Law, to submit an application for registration to the Agency for Audio and Audiovisual Media and to align its activities with all the obligations stipulated in the Law.

## **Macedonia and the European Union**

The Republic of Macedonia signed the Stabilization and Association Agreement with the EU and its Member States on 9 April 2001. The Macedonian Parliament ratified the Agreement on 12 April 2001, reaffirming the strategic interest and the political commitment to the integration with the EU. The Stabilization and Association Agreement was ratified and it has been in force since 1 April 2004.

On 17 December 2005, the EU decided to grant the Republic of Macedonia an EU candidate status.

Following the candidate status, the EU must set a date for the start of the negotiations regarding the full accession, encompassing all aspects of the EU membership, including trade, environment, competition and health. Macedonia, as a candidate country, should harmonize its legislation with the EU.

On 14 October 2009, the European Commission issued the 2009 Progress Report. Macedonia received a recommendation from the European Commission for the opening of the accession negotiations. The country made significant progress and substantially addressed the key reform priorities, known as eight plus one benchmarks.

Based on the Progress Report issued in October 2013, a progress was made in this area with the implementation of a national legislation in the fields of electronic communications and audiovisual policy and the preparation of new legislation aimed at the alignment with the EU acquis. The alignment with the acquis on electronic communications remains a priority.

## **Competition**

The competition in the telecommunications business is well-developed in almost all segments. Several main players shape the telecommunications market in Macedonia.

Telekom Slovenia is offering various services under the brand name ONE: mobile and fixed voice, mobile and fixed broadband internet and TV. The main mobile offer of ONE for 2013 is the new Select Business portfolio that allows the customers to create their own service package. The entry fees of these offers are set at a pretty low level and they also include a free low-end handset. In 2013 ONE maintained a stable mobile customer base, as well as a market share of 23.33% (source: Report for electronic communications development Q2 2013, the Agency). In the fixed segment, ONE offers low price triple play bundles (fix voice/internet/TV). ONE was selected to implement the digitalization of the free-to-air TV signal, which ended by 1 June 2013. The digitalization resulted in an increase of their TV customer base to 55,042 in Q2 2013 compared to 37,886 in Q1 2013 (source: Report for electronic communications development Q2 2013, the Agency).

Other major competitor is the mobile operator VIP which has limited its services to mobile based services only. VIP was focused on the launching of a SIM-only offer without obligations. With an aggressive pricing policy, which continued in 2013 as well, they have increased their market share to 28.14% in Q2 2013 (source: Report for electronic communications development Q2 2013, the Agency).

The main characteristic of the mobile offers of ONE and VIP are the low price and the doubling or tripling of the inherent values of the bundles.

All three mobile operators acquired 4G/LTE (Long Term Evolution) licenses in August 2013. The first mobile virtual network operator (MVNO) Alfabone started with its operations in October 2013.

The cable operators also have a significant role in the telecommunications market and, as providers of cable television as their main service they are well-established on the Macedonian market. Most of them offer internet broadband services and fixed voice services. Telekabel and Blizoo are the biggest cable providers among over 70 active cable operators. Blizoo offers Hybrid Fiber Coaxial ("HFC") services – optic near your home with very high data rate for internet services and digital television. However, all cable operators have shown a decline after the TV signal digitalization.

The product portfolio of all operators is driven by bundle products. The cable operators are bundling their TV offer with internet and fixed voice services. The fixed voice service of the cable operators is usually perceived as a value added service as the cable operators are charging very low access fee or presenting the fixed voice service as free of charge and including also free traffic in their own network bundled in the offer. As the overall market is price sensitive, the price perception plays a major role in the customers' choice and thus the cable operators' offers are seen as more competitive than MKT's in terms of prices.

MKT and TMMK are focused on increasing the market share in the ICT segment, thereby stepping into the already highly developed ICT market with innovative services.

The trend of NP continued to increase in 2013, for both mobile and fixed numbers. By the end of Q2 2013 there were 103,465 mobile and 114,849 fixed ported numbers in total (source: Report for electronic communications development Q2 2013, the Agency).

With all the main telecommunications services of MKT and TMMK, such as providing different bundled offers – a combination of different services, MKT and TMMK still have the biggest market share. As at 31 December 2013 MKT has a fixed voice market share (including wholesale) of 69%, fixed broadband internet market share (including wholesale) of 52% and TV market share of 21% (source: internal best expert estimates). In the second quarter of 2013 the market share of TMMK was 48.53% (source: Report for electronic communications development Q2 2013, the Agency). The Agency uses the market share calculation method based on the total number of active SIM cards which were used in the previous three months.

## **Marketing and Sales**

Operating in a highly competitive environment in all telecommunication segments, MKT and TMMK are focused on new services and on retention of the existing, as well as acquisition of new customers. Marketing activities based on customer needs and habits are performed in order to build strong customer relations. High quality service, loyalty offers and handset upgrade programs are also intensively used in order to increase the customer satisfaction and to

prevent and decrease the customer churn rate both in the residential and the business segment. The main focus in 2013 on the fixed and mobile market (both residential and business segment) was put on the retention of the existing customers and the up-sell to bundled services, as well as on the acquiring of new customers.

The process of digitalization of the TV signal in June 2013 continued the positive TV growing trend that started with the fixed portfolio repositioning in 2012. The TV customers base has grown in line with the expectations for 2013 and MaxTV continues to be the main retention tool for Voice and Internet users.

Besides the enrichment of the bundled double and triple play services, a low entry TV product for single voice customers was also introduced. Several major campaigns were launched for achieving the planned sales results and for increasing the awareness of the benefits provided with the services. The BB internet services were enriched with the introduction of high speed internet products (1Gbps) on FTTH technology, and Internet on demand – service suitable for non regular users of internet.

The increased FTTH coverage and the benefits of the fiber-based product offers improved the customer base over fiber for 95% at the end of 2013 compared to 2012.

As a response to the aggressive price movements of the competition, new offers for the post-paid and prepaid mobile segment were created (introduction of COOL – new interactive tariff model designed for the youngsters community; creation of package at their choice, using free bonuses, etc).

Mobile data services remained in focus in 2013, where the voice data bundles were enriched providing additional value for the customers: offering more minutes, increased internet traffic volume and Mobile MaxTV.

The attractive handsets offers contribute to the gross additions and the retention in both prepaid and post-paid segment. The increased sales of smart phones led to migration from voice tariff models to voice data bundles.

TMMK introduced a new Smart Business portfolio and upgraded the mobile Team Business portfolio, making it even more attractive to the customers and retaining the unique value proposition that cannot be matched by competitors.

During 2013, in the fixed Business segment, MKT upgraded the bundled offers and further enhanced the inherent values of the packages with speed, traffic and quality of service as main elements.

MKT was also focused on providing our Business customers with the new cutting edge ALL IP network that will provide our customers with new innovative services to be run over a highly reliable and fast IP network and activated via one click of a button.

MKT and TMMK are focused on further development of the Cloud market and offered a wide variety of cloud services to our customers like Virtual Disc, Virtual Private Server, e–Accounting and many more. A special New Year campaign was tailored to the specific business needs, offering a bundle of Tablet + Mobile Internet + Cloud services for great satisfaction of our business customers.

The Loyalty Program was extended with an enlarged partnership network and is available for both the prepaid and the post-paid segment. In addition, M-payment (MobiPay) was launched in 2013 as a new payment method using the handset as a payment tool.

MKT and TMMK have developed different sales channels in order to serve the customers from different segments. MKT and TMMK use direct sales channel such as: own retail network, telesales, on-line sales channel, technicians, direct sales agents, account managers (for Institutional, Key Accounts and Large Accounts) and introduced a multichannel logic in the sales and service of the SOHO (Small-Office-Home-Office) segment. The indirect sales channel is based on indirect master dealers with their own network of shops, partner shops and kiosks. Telesales activities for proactive retention and loyalty activities were also introduced.

The main sales channels are the MKT and TMMK shops. There are 39 joint shops as at 31 December 2013. In 2013, the own shop network was rationalized by closing 6 shops and opening two new ones at more attractive

locations. All shops are offering the complete TMMK and MKT product portfolio under the same conditions and with the same customer service level. As part of the implementation of the Sales Boost program, own shops operations were improved in spite of the transaction (sales vs. service) ratio and the up-sale execution in 2013.

Partners' presentation in own shops was extended by the introduction of m-Wall since July 2013. TMMK introduced the iPhone 5S and iPhone 5C on the market on 1 November 2013.

Sales activities that include home delivery via telesales were used in 2013 for retention of fixed and mobile subscribers. From November 2013, on-line sales started with sales via the WEB Shop.

In 2013, the direct agents put a strong emphasis on the sale of FTTH products for the residential and Small-Office-Home-Office ("SOHO") customers.

Another channel of the distribution network of MKT and TMMK is the dealers' cooperation. As at 31 December 2013, the network consisted of 7 master dealers with 60 shops as TMMK partners and 7 master dealers with 35 shops as MKT partners. The majority of the TMMK master dealers' shops are joint shops offering the full MKT and TMMK portfolio, except for cash collection. TMMK's prepaid and post-paid packages (with or without handsets) are available in all dealers' shops. In addition, prepaid vouchers are also available in 4,015 kiosks.

Technicians took active role as salesmen for the fixed portfolio throughout 2013, contributing to the IPTV sales.

The IP Multimedia Subsystem ("IMS") migration and the activity related to it were performed by the Inbound Call centre.

A part of the MKT product portfolio (e.g. telephone sets, TV sets, computers, printers, network equipment and home appliances) is available to the customers using payment by instalments through their telephone bill.

## **Research and Development**

MKT and TMMK will continue to build and maintain technologically advanced, flexible, and cost-efficient telecommunication infrastructure in order to reach the customers' demands and expectations. In 2013, we proceeded with the development of all network segments: Access, Core and Transport Platforms, as well as Service Platforms.

In 2013 we continued expanding FTTH as a powerful network for sustainable future. FTTH Network enables greater efficiency, and stands as a foundation for profitable growth in growth areas such as cloud computing, entertainment, business services, etc. At the end of 2013 we installed capacities to cover 101,000 Homes passed all over the country.

ADSL capacities were also extended during 2013, covering 54% of the households with the installed ports at the end of 2013.

The increasing demand for video and data services requires extension of the transport network capacity. During 2013, the capacities of the IP/ Multi-protocol label switching ("MPLS") network were extended according to the traffic increase.

In terms of Service Platforms, the main focus in MKT was the upgrade of the IPTV platform to a new SW version and the extension aimed at supporting the new IPTV customers. The IMS Platform was commercially launched in 2011 and it is used for provisioning of VoIP as part of the 2Play and 3Play services and as a base for PSTN network migration towards the all-IP network. During 2013 MKT extended the IMS platform for Voice users and started the implementation of IMS Geo-Redundancy.

In 2013, MKT continued with the extension of Ethernet over the copper and optic cable capacities for provisioning of data services for business customers. This extension enabled support of new business customers, modernization of Time Division Multiplex ("TDM") network with migration of the existing business users towards all-IP network.

For improvement of the Fulfilment and Common Data Management domain, during 2012 we started the implementation of Resource/Service Inventory, Activation and Workforce Management Systems. These are very complex systems that touch almost each part of the operational activities for residential customers.

The implementation continued during 2013 and the commercial start is planned in first half of 2014.

As at end of year 2013, TMMK's radio access network consisted of 639 physical sites on which there are 639 2G base stations sites providing 99.9% population coverage, 337 3G base stations providing 87% population coverage and 30 4G base stations, providing 15% population coverage, allowing the subscribers to use high speed mobile Internet.

The Radio Access Network ("RAN") was extended in 2013 in order to support increased mobile traffic. During 2013 TMMK introduced LTE technology and started the modernization of the Mobile Core Network. In terms of Mobile Service Platforms, in 2011 the implementation of M-Wallet started as a base for mobile payment services. The implementation of the project continued in 2012 and the commercial launch was in June 2013.

In line with the determination to be a technology leader in the country and even broader in the region, MKT and TMMK will continue with the development of the network in order to provide high quality services, increased customer satisfaction, increased network availability, increased operational efficiency and secure long-term evolution.

In order to stimulate corporate R&D and innovation, MKT and TMMK organized an Innovation Partner Contest in 2013. The Innovation Contest was officially announced at a Telecom Innovation Conference organized by the MKT Group and the Macedonian ICT Chamber of Commerce in December 2012. More than 70 proposals were submitted within the contest by various entities such as universities, start-up companies, and individual innovators. The following five projects were selected by the MKT Group for joint product development and implementation with the selected partners:

- "T-Care" (Multi-user platform for online customer care, based on artificial intelligence)
- "Smart Wine" (Integrated end-to-end M2M cloud solution for intelligent monitoring of agriculture parameters using wireless sensor network)
- "Cloud Message" (Distributed web-based social network for sharing messages, private or public, and advertisement coupons, depending on the user's preference, with a mobile augmented reality based client)
- DoxBee (Cross-platform system for collaboration with MS word documents)
- MarketKonekt (B2B/B2C online trading platform in Macedonia)

MKT will continue with activities in the area of new development and innovation. In that regard, the cooperation with the universities is also seen as a good opportunity to support these activities.

## **Information technology**

Reducing the complexity of the IT architecture by consolidation and modernization of the IT systems and infrastructure was the main focus in 2013. The improvement of the support and the automation of the corporate processes was the main goal, as well as the improvement of the One Company customer experience.

Integration of the IT infrastructure and architecture is a prerequisite for the implementation of common processes on MKT Group level and increasing the process efficiency.

The main achievements in 2013 were:

- Implementation of Enterprise Marketing Management system: a DT-wide solution for campaign management aimed at providing tools to create, update and monitor multi-channel marketing campaigns that drive sales leads and closure rates.
- Started project for Retail Billing system consolidation for fix and mobile customers. The scope is to have all lines of business consolidated in a single billing system. This will reduce the costs, but also allow the business to grow in new directions in the future, gain synergies in the operations of the business and expand the possibilities for new products and services such as full quad-play for all business areas. Deployment is planned for quarter two of 2015.
- HW replacement and DB upgrade for Data Warehouse & Business Intelligence system - replacement of the obsolete hardware and upgrade of the databases and software versions, at the same time consolidate them on one hardware platform, ideally virtualized by expanding our current virtual infrastructure.

- Midrange Storage System Upgrade - replacement of obsolete midrange storage systems in MKT&TMMK with one midrange storage system in order to integrate and host all current application data separated in between.

IT continued its significant role in the implementation of the new Fixed/Mobile Converged products/services and development of ICT concept. Following the ICT strategy, IT has several successful implementations of Custom Cloud solutions, mainly for the Public Sector, it has identified a potential for additional customers in the Large Enterprise Sector, as well as implementation of cloud products for the general SME and residential market segments, like VPS, cloud ERP solution and Online security product. IT has enlarged the resource pools with implementation of virtualization technologies and we are continuing with the implementation of the automation and self-service layers in the upcoming period.

The IT security standards have been improved by implementing several security relevant systems that decrease the operational risks and improve customer and personal data protection.

In the course of 2013, MKT and TMMK continued with the local activities of the project for implementation of a new consolidated CRM system. This system should enable a comprehensive view of customers and further sharpen the customer focus of MKT and TMMK.

Andreas Maierhofer

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