

# Answers to Frequently Asked Questions

## Question 1

### What makes Rostelecom attractive for investors?

The following points underpin Rostelecom's investment attractiveness:

- Leading positions in markets with significant growth potential (broadband Internet access, Pay TV, services of data processing centres, and other digital services), as well as participating in the growth of the mobile data segment through its 45% share in the joint venture with Tele2 Russia;
- A unique network infrastructure (in terms of coverage and capacity) with fibre optic access serving more than 30 mln households;
- A potential to further improve operating efficiency (real estate, personnel, etc.), which will provide substantial cost savings;
- Incentivized management (professional management team committed to achieving strategic goals through their participation in a share option plan);
- A progressive dividend policy (at least 75% of the free cash flow, and at least RUB 45 bln in aggregate for three years).

## Question 2

### The 2020 Strategy states that you expect further growth in revenues, notwithstanding the gradual saturation of the markets of your presence. What will be the basis of such growth?

Revenue Growth is going to be driven by:

- A growing market share in the broadband internet access and Pay TV segments and growing ARPU per household;
- Expanding presence in new markets with higher growth potential. In addition to its substantial expertise, the Company has the necessary infrastructure and client base to realise the growth potential of these market segments. The key growth points in the segment of new services are:
  - Data centres;
  - Cloud services;
  - OTT video;
  - Industrial Internet of Things;
  - Geodata.

## Question 3

### How is the management team being incentivised to implement the adopted strategy?

In March 2014, Rostelecom's Board of Directors approved the Company's long-term incentive plan for management.

The programme provides for the launch of a share option plan for ordinary shares, which can be purchased by the programme's participants through an annual bonus payments system. Annual bonuses are paid in accordance with performance.

The programme will last for three years (starting from 2014) and approximately 200 senior and mid-ranking managers will participate in the programme, including the heads of regional branches.

The long-term key performance indicators (KPIs) used to determine awards within this programme are as follows: free cash flow (FCF), net profit and return on invested capital (ROIC). The long-term incentive scheme adopted by the Board of Directors is aimed at attracting talented professional managers, it is also designed to make managers more interested in raising the Company's fundamental value and capitalisation and this brings the expectations of shareholders and potential investors in line with the interests of Rostelecom's key employees.

Moreover, Sergey Kalugin, Rostelecom's President, has additionally invested RUB 1 bln in shares in Rostelecom.

## Question 4

### What is your M&A strategy? Are you considering deals in the broadband internet and pay-TV segments?

Concerning M&A deals, the Company's strategy is as follows:

- Rostelecom may acquire or strengthen positions/expertise in promising and fast-growing market segments. The acquisitions of SafeData or IQMen are

an example of this.

- Rostelecom may strengthen its positions in certain regional markets, mainly in the broadband internet and TV segments. One example is the acquisition of telecommunications business of Morton Group.

## Question 5

### Why were the mobile assets in the joint venture with Tele2 Russia transferred? What are the Company's plans with respect to the share in the joint venture (JV)?

By establishing the joint venture with Tele2, the Company gained an opportunity to concentrate its resources, both management and financial, on the core business — the fixed line segment.

The viability of pooling Rostelecom's assets with Tele2 Russia was based on the following strategic considerations:

- The mobile assets of Rostelecom and Tele2 Russia ideally complement each other, both in terms of geographical coverage and the existing experience of Tele2 Russia, related to the introduction of innovative solutions, with the extensive range of licences and new-generation frequency bands of the Company.
- As a result of the deal, the joint venture expanded its geographical presence to the federal level, and gained sufficient coverage to successfully compete with the existing federal operators;
- Rostelecom also benefitted by significantly reducing its direct investments in the mobile communication segment, as well as by transferring the debt associated with mobile operations to the joint venture;
- The joint venture is managed by a separate and competent management team and possesses the best cost control system on the market;
- Upon the MVNO agreement, the joint venture will be able to offer convergent fixed and mobile communication services nationwide.

The decision to create the joint venture will ensure the Company's contribution to the growth of the mobile data market through a share in the standalone business, representing a strategic investment for Rostelecom.

## Question 6

### What about the future of the quasi-treasury block of shares held by your subsidiary Mobitel? Are you planning a SPO or cancellation?

There are several possible scenarios in respect of this block of shares, including the allocation of shares among investors or using them in M&A deals. Currently, no decision has been taken.

## Question 7

### What are your long-term objectives with regards to the key financial indicators?

It is expected that the implementation of initiatives under the Company's strategy for the period to 2020 will permit it to achieve:

- The average annual rate of growth in revenues of 1–2%;
- The average annual rate of growth in OIBDA of 3%;
- The share of the digital segment in revenues of 60% by 2020;
- The improvement of the CAPEX/revenues ratio by 3 to 4 percentage points by 2020

## Question 8

### What are the prospects for the fixed telephony segment?

The fixed telephony market has been shrinking for the last few years. This is a worldwide trend experienced by traditional operators in many countries. At the same time, a certain level of demand for fixed line telephony services still exists, particularly in rural areas and not easily accessible settlements where the development of alternative communication technology involves significant costs and is not economically attractive.

We strive to retain as much as possible the fixed telephony subscriber base by implementing the following initiatives:

- Promotion of packaged offerings;
- Improvements in the quality of client services and the modernisation of our network infrastructure;
- A special programme including measures for retention of clients using voice services.

## Question 9

### What influence does exchange rate fluctuation have on your business?

Our revenues and operating expenses are originated and incurred in Russia and are not hugely dependent on fluctuations in the exchange rate of the national currency. Our currency exposure on income and expense items are minimal. The presence of a foreign currency component both in income and in expense permits the Company to hedge fluctuations of the exchange rate, to balance out the positive and negative effects on the financial statement.

The income in the foreign currency items in particular, includes payments from international operators for interconnect and traffic transit services.

The Company's operating expenses also include costs in foreign currency, associated with the interaction between operators and acquisition of content from international producers.

As for the Company's capital costs, the foreign currency component is equal to about one third of total costs. The Company strives to reduce this component as much as possible by purchasing domestic replacements of imported equipment, as well as fixing the price of the contracts with vendors in roubles or linking it to a fixed exchange rate of the foreign currency.

## Question 10

### Mobile Internet versus fixed Internet? What are the prospects for fixed Internet access, given the growing speeds of mobile data transmission?

Despite the active development of data transmission in cellular networks, mobile access cannot match the quality, reliability and speed of a fixed line connection. Furthermore, mobile networks do still require the availability of a fixed component connecting the base stations with the transport infrastructure. The Company expects continuing development of fixed and mobile networks that will complement each other and ensure seamless connection for the client.

A competitive advantage of Rostelecom is that the Company is the only operator with the opportunity to provide nationwide quad-play services.



## Question 11

### Are any additional contributions to the authorised capital of the joint venture with Tele2 Russia planned for financing its current operations?

The joint venture finances its investment programme independently, and it possesses the necessary reserves of financial resources to do so. Currently, Rostelecom has no plans to spend its own funds to finance the current operations of the joint venture.

## Question 12

### What are the Company's plans for the development of the media business?

The Company maintains the following approach to the development of the media business:

Directions for the development	Example
The creation of partnerships with leading content producers.	In 2014, Digital TV, a joint venture with VGTRK, was created, which is currently a developing business. Digital TV is the largest Russian producer and distributor of thematic channels, and has a market share of 28%
Creation of partnerships to gain expertise for the purpose of additional monetisation of media opportunities.	One example of such partnerships is the creation, jointly with the Korean corporation GS Home Shopping Inc., of a large teleshopping channel. The creation of the joint venture will provide an opportunity to pool resources and expertise to offer a new level of quality of organisation of TV commerce.
Participation in producing content production projects.	In 2015, Rostelecom co-financed the production of its first motion picture called "The Route is Created" which was released in March 2016.

## Question 13

### What are the Company's plans for the further modernisation of its network? Are there any plans to switch to SDN/NFV?

Rostelecom possesses the largest fixed telecommunication infrastructure in Russia, based on which the Company provides services to hundreds of thousands of corporate and federal clients, as well as to mlns of Russian households. During the last few years, the has Company invested in increasing the capacity of its transport network to more than 12 Tb/s and modernised the last-mile infrastructure, covering up to 31 mln households with fibre optic technology.

The further development of the network infrastructure of the Company is connected with its virtualisation and transition to SDN (Software-Defined Network) / NFV (Network Functions Virtualization) technology. On such networks, the control level is separated from data transmission units and is realised by software means.

This approach has the following advantages:

- Simplified network architecture;
- Reduced dependence on solutions from foreign vendors;
- Faster and flexible introduction of new innovative services on the market.

Therefore, the Company has the opportunity to save both on capital costs and on network maintenance costs. As a result of transforming the network, the Company expects to reduce operating expenses related to the maintenance of the network infrastructure by 25% and reduce the level of capital costs by 3 to 4 percentage points by 2020.

The Company plans to complete the majority of work related to the transition to the network infrastructure based on the SDN/NFV technology in 2019.