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ELECTRONIC LODGEMENT

Dear Sir Madam

Telstra acquires Pacnet – transcript of analyst briefing

In accordance with the Listing Rules, I attach a copy of the transcript of the analyst briefing held on Tuesday 23 December 2014, for release to the market.

Yours faithfully



Damien Coleman
Company Secretary

**ACQUISITION OF PACNET
ANALYST AND MEDIA CONFERENCE CALL
23 DECEMBER 2014**

MR KOPANIDIS: Good afternoon, and welcome to today's teleconference on the Pacnet acquisition. My name is Peter Kopanidis, and I'm responsible for investor relations at Telstra. Also on the line today is Nicole McKechnie, who's responsible for media. The presenters today will be Telstra's Chief Financial Officer and Group Executive, International, Andy Penn, and Brendon Riley, Group Executive, Global Enterprise and Services. Today's presentation will be followed by a Q and A session with Andy and Brendon both for analysts and for media. In terms of the format for today, we won't step through the pack which has been lodged on the ASX. Both Andy and Brendon will go through respective presentations. And with that, I will hand over to Andy.

MR PENN: Thanks very much, Peter, and thank you, everybody, for hooking in today. And let me just acknowledge it's probably closer to Christmas than we all would like, but we were keen to get this transaction completed before the end of the year, and we're very pleased that we've been able to achieve that. I think, as you will know, we have three very clear pillars to our strategy at Telstra. The first is improving customer advocacy; the second is driving value from our core business; and the third is investing for longer-term growth. And I think in relation to the investing for longer-term growth, the Pacnet acquisition really ticks two important boxes there. One is our commitment to expand into Asia and then, secondly, our commitment to expand our Global Enterprise Services business.

We already have a substantial presence in Asia. We have more than 1400 people in the region, and that doesn't include our very significant and successful investment in Autohome, where we have another couple of thousand. We've got a considerable infrastructure network to support our expanding services business, and this acquisition will substantially increase that. We also have significant sales and corporate development resources internationally, and we're going to continue to look for opportunities to invest in the region.

What I will do is I will hand over to Brendon Riley, who will take you through the strategic rationale for the deal and, in particular, how it fits with our Global Enterprise Services strategy, and then Brendon will hand back to me, and I will comment on some of the financial aspects of the transaction before we open up for questions where, I think, we will do first with the analysts and investors on the phone, and then we will hand over and cover some media questions as well. So, again, thanks, everybody, for hooking in today. Sorry it's a little bit closer to Christmas than I think we would probably all like, but we're very pleased to get this deal done and announced. So with that said, I will hand over to Brendon.

MR RILEY: Great. Thanks, Andy, and good afternoon, everybody. As you know, we already offer integrated connectivity and services solutions across the region. This deal with Pacnet significantly enhances our presence in the region and accelerates our growth, and I think this is very, very important for what we're looking to do with global enterprise and services. The combined entity places Telstra in a leading position in terms of assets, people and capabilities, and it will effectively double the size of our GES business in Asia.

Our strategy is centred on serving enterprise and wholesale customers who connect with Asia. We believe the acquisition of Pacnet creates greater scale, presence and specialisation across Asia – all essential elements for our ambitions to grow and thrive in the region. In terms of network and geography, it increases the density and diversity of our reach across the Asian region and into the US. It provides strategically located assets, such as PoPS and data centres, and this also includes China. In terms of capabilities, it enhances our ability to offer new services, such as software-defined network-based services, known as SDN, across a network of interconnected data centres. It also doubles our talent pool, and it adds thousands of new customers, opening up a lot of incremental new opportunities for our business.

A little bit more colour on Pacnet themselves. As some of you know, Pacnet is headquartered in Singapore, and they have over 800 staff across 24 cities and 11 countries and regions from Australia into South-East Asia, north Asia, as well as the US and the UK. The acquisition includes Pacnet's interests into China as well through its joint venture, PBS, which stands for Pacnet Business Systems, which is licensed to operate domestic internet protocol virtual private network, which is IP VPN, and provide data centre and hosting services in China.

Pacnet's assets comprise 109 points of presence, 29 data centres and also submarine cables. Pacnet owns Asia's largest privately owned submarine cable network, which lands at 19 cable landing stations across Asia, and, all together, has 46,420 kilometres of cable. And it also controls two of the five fibre pairs on the Unity Trans-Pacific submarine cable connecting the United States to Asia. Their customer base includes more than 2400 enterprise customers, with a strength in financial services, the internet, social networking, e-commerce and professional services, and it does have a strong franchise in the growing OTT segment. They also have approximately 220 carrier customers comprising retail and wholesale telcos.

In terms of their products and services and the breakdown of their business – and the percentages I'm giving you will be of the fiscal year '13 financial results on a revenue basis – connectivity accounts for 32 per cent of the business. That's international private line, international ethernet and private wavelength circuits. Bandwidth comprises 26 per cent, which is fibre-optic submarine cable networks and associated operations and services. IT solutions is 26 per cent: IP VPN, IP transit, internet access, content delivery networks and SDN. What we would define as NAS solutions is nine per cent of the revenue: managed router, managed application acceleration services, managed firewall services. And then data centre, which comprises seven per cent, which is mostly collocation and some hosting.

I just wanted to sort of close my remarks before I hand back to Andy and just touch on what I think all of this means for our customers. For Australian businesses, businesses across Asia and, importantly, companies looking to expand and grow in Asia, the combined entity will provide powerful new options for networks and services, including China. From a submarine cable perspective, the combined entity and planned upgrades will provide one of the most sophisticated cable networks into most critical landing points across Asia, especially from the US, and we believe, you know, this is and will continue to be highly attractive for OTT companies and large enterprises expanding into Asia.

Demand for data centres with optimised networking is growing across Asia, and Pacnet will add another 29 interconnected data centres with the latest SDN services. Combining the cables and the interconnected data centres across the region, we believe this provides one of the most comprehensive connected backbones available across Asia. This core platform will enable Telstra to more rapidly scale and expand our unified cloud, unified communications, managed network services and security services offerings into selected markets, and this has always been our strategy. And in the second half of this financial year, we will launch new unified cloud and UCaaS, Unified Communications as a Service, offerings based on the very latest technologies from Telstra and our partners into selected networks.

For Pacnet's existing customers, we believe Telstra's history in the region, our financial strength and strategy for growth across Asia will provide strong incentives to continue their relationship with us and capitalise on our global capabilities, advanced services and also strength in the Australian market. And as we look to accelerate our growth in Asia, Pacnet also brings a wealth of talent, and we will look to integrate and also restructure our business to ensure we have the very best talent in the industry aligned to the goal that Andy mentioned, of providing the best customer service in the market.

Finally, we will undertake an extensive integration program, which is expected to take up to two years following transaction completion. This program will focus on sustaining an enhancing customer service as well as looking for synergies to drive simplicity and main competitiveness in all markets. So with that, let me pass back to Andy.

MR PENN: Thanks very much, Brendon. Well, as you would have seen from the release that we made this morning, the acquisition price for Pacnet is US\$697 million, and this includes gross debt of approximately US\$400 million. The acquisition we financed by cash reserves and existing committed bank debt facilities. As you know, we ended 2014 in a strong free cash flow position, notwithstanding the buyback and the spectrum acquisitions that we made in the first half of this financial year, and as you also would have seen from the materials that we released to the market, Pacnet's revenue for its financial year '13 was US\$472 million, and it's EBITDA was US\$ 111 million. As Brendon said, we see this as a very important strategically for our aspirations for our enterprise services business, and also our aspirations for expansion in Asia.

We, as Brendon said, plan to fully integrate the business, and we're targeting run rate synergies of approximately AUD\$65 million, which covers both opex and capex, and we feel that's a pretty conservative estimate which, sort of, arises from some of the overlapping infrastructure, albeit there's a high degree of complementarity between the two business, which is why we think this is very strategically attractive for us, and that doesn't include revenue synergies where we think that, you know, the additional scale in the region will make this more attractive to wholesale customers and enterprise customers as well. So we think financially it's a very attractive transaction. It meets all of our investment guidelines. It will be EPS accretive by year two. The return on invested capital will exceed our weighted average cost of capital at least by year three, and it's more accretive than a share buyback of the same size.

So that's the, sort of, high level financial summary. I'm sure we will take some more questions on that in a moment, but before I go across to questions, just a couple of points in relation to next steps. As you would expect, the transaction is subject to customary closing conditions, including regulatory and other approvals. We expect it to complete in the fourth quarter of this financial year, so obviously some time between April and June of 2015. I've mentioned that we expect to fully integrate all aspects of Pacnet, other than the China joint venture holdings, in order to capture the relevant synergies, and, more importantly, it will be integrated into the international business of Global Enterprises Services, which Brendon is running, and we expect to hit fully all of the synergies within two years of completion, and I've mentioned we also see some further upside in revenue synergies as we integrate the two businesses. With that I will hand back to Peter, who will then facilitate some Q&A, but thanks again, everybody, for hooking in. Peter.

MR KOPANIDIS: Thank you, Andy. We will now open up to questions from analysts. Ange, are there any questions on the line?

OPERATOR: Yes, there are. First question I have for you is from James Wang of Deutsche Bank. Please go ahead, James.

MR WANG: Hi guys. Just a question around the strategic rationale again of only the assets, versus renting these infrastructure assets. If I just look at the submarine cables industry, you mentioned before that Telstra does have a pretty sizeable network of submarine cables in the region, and that does appear from what we've read – it does appear to be quite a bit of capacity that's coming on, and my understanding is it's quite easy to increase capacity by upgrading equipment, rather than owning these additional cables, and if I look at Pacnet's revenue, it has been declining and it has been making operating losses if you account for D&A charges over the last two years. So I'm just wondering whether you might be better of strategically renting rather than owning these assets, and if you could also perhaps step through, you know, owning versus renting for both data data centres, submarine cables, and PoPs individually, please.

MR RILEY: I think I might take that one. So firstly, when we looked at the total, you know, economic equation, we felt it was very, very attractive with the Pacnet and also the Australian Telstra-owned cable assets. If you look at traffic that comes out of the United States into Asia there is a significant amount that will travel across these cable networks, and we think being able to, you know, consolidate those assets as much as possible not only provides us with a strategic in any of the over-the-tops coming into Asia, but also provides us with an opportunity to continue to drive synergies across all those cable assets. As I mentioned in my comments, we've got, through the work that Pacnet have done, software to find networking connectivity across the major data centres.

We've got data centre capability in China. So we also think that provides a highly diverse and very, very attractive set of not only cable landing points, but assets for, you know, people coming into Asia doing business in Asia to leverage from. Strategically, we also want to be able to go up the stack more probably than Pacnet has done. We've done that very, very successfully in the Australian market, and now what we've moved up the stack is, you know, worth over 2 billion a year, and we definitely want to leverage that and take that in. I think there will be some rationalisation of PoPs and some of the assets. I think if we look at perhaps some of

the data centre expansion plans that Pacnet had, we probably won't be going, you know, quite as far as they were originally intended. But, overall, you know, we're comfortable with the deal, and the opportunity that it presents.

MR WANG: Great. Thanks.

OPERATOR: The next question comes from Ian Martin of CIMB. Please go ahead, Ian.

MR MARTIN: Thank you. Two questions, if you wouldn't mind. First, Brendon gave a little bit of a profile of the customers, 2400 enterprise customers, in terms of the kind of market segments they're in – finance, e-commerce, and so on. But I just wonder how they compare with the current set of GES customers, at least the international customers in GES, and whether, you know, we're looking at a kind of expansion of the – a geographic expansion, if you like, of the customers that you might have found it hard to, you know, develop relationship and business services with through this acquisition, is the first question; and secondly, you provided the revenues and EBITDA for FY13, and I'm assuming that it's a little bit lower in FY14. I just wondered if you could confirm that, and what the kind of run rate is for FY14 on those two metrics.

MR RILEY: Let me take the first one. I might ask Andy to answer the second one. But, look, on the first one, I think what you've said is – would be a good summary. It's very, very – the customer set is very accretive to our existing customers, and that's both the industries they're in, the locations they're in, and also the type of deals that they have. So from that perspective, you know, we're very excited about it. They do have one, you know, probably significant Australian customer which is not a Telstra customer, so when you look at the Australian customer base it's also one that we haven't highly penetrated. So, for those reasons, it's also a very positive story.

MR PENN: And just picking up, Ian, on the, sort of, financial question, and maybe I will, sort of, comment a little bit on – to the point that James was raising as well. So, firstly and specifically to your question, the performance in FY14 is certainly consistent with FY13 and is showing improvement, and there's no doubt that the Pacnet business has been going through quite a bit of transformation and improvement under the current management team, which is demonstrating itself through the improving EBITDA. So that's a journey that we will continue with them, and it's basically a, sort of, a business mix, and just operating efficiency set of initiatives that have improved that. But it makes it ultimately a more attractive business. But, in summary, FY14 performance is in line, if not a little better than FY13, which is a continuation of the trend over the last couple of years.

MR MARTIN: Thank you.

OPERATOR: Thank you. The next question for you is from Raymond Tong of Goldman Sachs. Please go ahead, Raymond.

MR TONG: Good afternoon, guys. Just a couple of questions from me. Can you maybe provide a bit of colour on the China joint venture PBS and, I suppose, what opportunity is in that market. And, secondly, can you give a sense of what the

drivers are for the 65 million of synergies – the split between capex and opex. And maybe just finally, just what do you expect the DNA and capex to be for Pacnet?

MR RILEY: So maybe why don't I start out and take on the first question. So Pacnet and the joint venture that it has set up with his partners, PBS is one of the first, you know, foreign, you know, entities to be provided with licences – domestic licences in China. So they have got an IP VPN licence for 23 provinces and that has been given by the Chinese Ministry of Industry and Information Technology. There's 26 cell phone PoPs across 19 major key cities in China and then there's two major data centres; Chongqing and Tianjin – so one in the east and one in the west – and they're both, you know, large data centres and, you know, the joint venture – and they have been established, you know, in collaboration with the – you know, with the government in China and the joint venture has the right to buy those, you know, in a few years time.

So, overall, it gives us, you know, I think, a very, very good backbone in China to support, you know, our customers going into China and also potentially to grow and shape the industry in China itself. I will pass back to – maybe pass back to Andy on those last two points.

MR PENN: Sure. No. Look, thanks, Raymond, and thanks for hooking in. Look, on the synergies, we haven't sort of broken it down between capex and opex, as you would appreciate the majority is obviously opex. However, there are definitely some capex synergies which really arise as a consequence of reduced investment for cable investments and some technology investments which will be overlapping, so we will save some there. If you look at Pacnet's long-term capex to sales ratio, it has been around 10 or 11 per cent and there's nothing sort of, in a sense, unusual in terms of how that accounting works. So from a depreciation and amortisation perspective, it sort of – it flows through at roughly that sort of level as well, so you're looking at a business which has got gross revenues of 450 to 500 million dollars capex to sales of 10 or 11 per cent, you know. That sort of throws of then a – in the sort of 40 to 50 million dollar range.

MR TONG: Great. Thanks, Andy. Thanks, Brendon.

OPERATOR: Thank you. The next question is from Harsh Agarwal from Deutsche Bank. Please go ahead with your question.

MR AGARWAL: Hi. I had a couple of questions. One was on the regulatory approvals. Can you give us some more details on what sort of approvals you will need for the deal to go through and do you see any kind of issues with the approvals? And the second question, I guess, Pacnet has a very high cost of funds; nine per cent bond outstanding. I guess it might be too early in the game to give an answer, but just curious to see what's your view on the bonds. I mean, the bonds are, I guess, callable at some point. So curious to see if you guys have any thoughts on the bonds that Pacnet has outstanding. Thank you.

MR RILEY: Yes. Just on the first one, on the regulatory approvals, we will be working that very collaboratively with Carl Grivner, the CEO of Pacnet, and his team. And, you know, with today's announcement out of the way, we will commence that. Look, I wouldn't want to pre-empt, you know, any of the regulatory approvals, but I think we've got – you know, both Telstra and Pacnet have got very

good working relationships with the regulators across all the countries that we're dealing with and we will work this collaboratively and move it as quickly as we can. So that's probably about all I can say on the regulatory approvals, but let me pass to Andy on the second part of the question.

MR PENN: Yes. Look, thanks, Harsh, and, look, on the bonds, that's really something that we will tackle once we get into the integration process and you will probably appreciate why I wouldn't want to be drawn to sort of comment more on that at this stage, but it is something that we will tackle in terms of thinking about how we sort of move forward once we get into integration.

MR AGARWAL: Okay. All right. Thank you.

OPERATOR: Thank you. The last question currently is from Sameer Chopra from Merrill Lynch. Please go ahead with your question.

MR CHOPRA: Good afternoon. Looks like a pretty good deal, particularly post-synergies. I have two questions. One, you will now have a bigger footprint to offer your – some of your joint venture partners; people like PT Telkom and StarHub, etcetera. Now, I was just wondering, you know, how does that change the relationship with some of these new JVs that you've formed and, secondly, Brendon, could you give us a sense around how customers are starting to react to this? I presume you've had a few emails from customers. I was just wondering how they're reacting to this new offer.

MR RILEY: On the first item, it would be fair to say that with Pacnet – one of the countries that it really doesn't have – it has a PoP, but it doesn't have much – is Indonesia and we will definitely be, you know, working very, very closely with PT Telkom and with our joint venture there and we think this will be a wonderful set of additional capabilities that we can not only bring into the joint venture and collaborate with PT Telkom on, but also it provides a whole range of new options for us to work with Telin which is the international arm of PT Telkom.

We do have, I think, a very, very good relationship with StarHub and, you know, some of the other, you know, major carriers across Asia and I have no doubt that this will also help in our working relationship with them. Reaction from customers; I have to be really honest with you and say that unfortunately I've been on a flight most of today. I just sort of landed in time to take the calls, so I haven't had a chance yet to, you know – to personally speak with some of our customers. I know Carl, you know, has been keeping, you know, his customers set up-to-date with the discussions with Telstra and from everything he has told me, it's – you know, they have certainly been so.

MR KOPANIDIS: Thank you. And if there's no more questions over to Nicole and her audience.