
Local Conference Call

TIM Participações

2Q19 Results

July 31th, 2019

Operator: Good morning, ladies and gentlemen. Welcome to TIM Participações 2019 Second Quarter Results Conference Call. We would like to inform you that this event is being recorded (Operator Instructions). There will be a replay for this call on the company's website. After TIM Participações remarks are completed, there will be a question-and-answer session for participants. At that time, further instructions will be given. We highlight that statements that may be made regarding the projections and goals of TIM Participações constitutes the beliefs and assumptions of the company's Board of executive officers. Future considerations are not performance warranties, they involve risks, uncertainties and assumptions as they refer to events that may or may not occur. Investors should understand that internal and external factors to TIM Participações may affect their performance and lead to different results than those planned.

[Operator Instructions]

Operator - Now I'll turn the conference over to the CEO, Mr. Pietro Labriola, so he can present the main message for the second quarter of 2019. Please, Mr. Pietro, you may proceed.

Pietro Labriola - TIM Participações S.A. - CEO, Member of Board of Statutory Officers & Director

Good morning, everyone, and thanks for attending our results conference call. As I stated last quarter, we will put a lot of focus on execution and make some short-term adjustments to gain result momentum. We will also return to our DNA of innovation and agility. I believe that we are achieving this step by step. And during the second quarter, we reported results and achievements, which denote we are back on track. I will walk you through the main highlights of second quarter, and then the team will help to answer your questions.

In the second quarter, we were able to post solid results despite the external challenges of the low economic activity and aggressive competition. Service revenues showed a slight acceleration in growth, reaching 2.4% year-over-year versus 1% of the last quarter. We still need to improve to reach our annual guidance, but we are on the right track.

We continue to perform very well on the cost side, which combined with better revenues, led to an acceleration in EBITDA as well. Our growth reached 6.2% compared to last year, allowing margins to expand to 37.9%. These solid results were supported by a renewed market approach, always taking advantage of what was already working and changing what needed adjustment.

In this context, TIM Black Família was our major launch during the quarter. This deck completes our portfolio of mobile offering, increasing our presence in the IN segment and providing a clearer path for offer upgrades. As we were the last ones to launch a family proposition, we didn't want to just replicate the other players. That is why we brought the concept of an entertainment hub, which looks away from price competition and that the upselling process, well, actually even more, we are creating for clients a reason why to upgrade.

TIM Black Família is the first offering in Brazil to include the Netflix subscription, and we look forward to enriching our proposal with other content providers in the future. The plan offers all the features that common family plan would offer as well as music content, magazine, newspaper, social network, international roaming package with Voice and WhatsApp and extra service. So far, the market response is very interesting. Close to 1/3 of our gross addition in top speed are coming from this family plan.

After a long period out of the media, we launched a new campaign for our Control plans, focusing on the key features and making sure that we remain relevant in the minds of clients. While in Prepaid, we started a selective and reserved response to our competitor with the goal of improving our acquisition rate and top-up levels. In this segment, we are more expensive than the other players, but we are adding features to what they already have. For example, when we sell a period of services and sponsored data, for the latter, we implemented the TIM Ads platform, our first move in this field where the most is yet to come. On top of that we are improving our customer support channels, adding WhatsApp ChatBot to Prepaid users.

The combination of this action without our execution adjustment in the B2B segment is helping us to sustain solid mobile ARPU growth of 5.8% year-over-year, with Postpaid, excluding machine-to-machine, declining 1.9% and Prepaid growing 2.9%. Customer base dynamics remained healthy with Postpaid,

excluding machine-to-machine, up by 4.8%, and Prepaid data user at nearly 22%. This last number denotes an interesting change in the profile of our customer base as really the position of champions of the second SIM and become the face or unique theme in more and more customers.

Mobile has been a game of resilience. But as I've described, we are adjusting our go-to-market to help accelerate growth in the second half. And we look forward to a more rational competitive environment and the better economy as they reform our advancing.

One of the main highlights of our business is TIM Live, which continued to show strong momentum. In the second quarter, growth was once again driven by a combination of high-single-digit ARPU expansion and a solid double-digit customer base expansion. This represented an important milestone with TIM Live surpassing 500,000 customers. As a result, TIM Live revenues grew more than 30% compared to the last year.

Since the first quarter, our FTTH rollout has been below our expected expansion rate as we had to focus on adjusting some issue with contractors in certain regions and treating feedstock processes. We understand that the major adjustments were completed during the second quarter, that is why we were able to close the quarter with 5 additional cities with FTTH, reaching 17 in total. We are now covering 1.6 million households, and we should accelerate in the third quarter to offset the delays between January and May.

Since the last quarter, I started pointing out that we will look into other source of revenue. So, I want to update you on some of the key initiatives we are working on outside the B2C work. We're exploring more and more Internet of Things solution (IoT). I commented last quarter about the Conectar Agro initiative in which TIM is promoting 4G technology on 700 MHz in the countryside of Brazil, and partnering with major names in the country's Agro business segment. This quarter, we completed the migration of the machine-to-machine base of Porto Conecta, an MVNO that used to run over our network. Along with lines, we also bring expertise and system from the operation.

And the last but not least, we are developing partnerships for connected car application. We hope to have news pretty soon on this topic. Importantly, these verticals also offer opportunities for cross and up-selling consumer and VAS products. So, while being financially small today, the combined effect can be relevant in the next 2 or 3 years.

To support all of that, we need to evolve our infrastructure, and we are working on several fronts. In mobile network, for example, our 4G coverage continues to

expand driven by 700 MHz rollout. We are covering more than 1.5 thousand cities with this band. At same time as our 4.5G coverage reached more than 57% of urban population. We continue to gain additional capacity with our spectrum refarming project at 1.8 and 2.1 GHz. As a result, our 4G network is the largest, most available and at the lowest latency in the country, bringing a high-level experience to our customers.

Still on the mobile network front, we are starting to implement techniques on our 4G network that were originally designed for 5G, and we are having a lot of success. Our test showed that massive MIMO can boost capacity by 2x to 3x under real conditions.

On the fiber side, we are expanding our transport network to support both the mobile business and FTTH rollout. In the past 12 months, we have increased high capacity backhaul penetration by 5 percentage points, reaching almost 70% of our side. FTTH coverage also expanded significantly. We are now covering 4x more households.

As you probably saw last week, we signed a memorandum of understanding with Vivo to explore different initiative to share infrastructure. The goals of such discussions are to find opportunities for both companies to work together to improve customer experience, while having more efficient spending of CapEx and OpEx, shifting resources to where the customers are most benefited. We will focus our discussion in the 2G single grid LTE at 700 MHz in most cities, which may be expanded later. But we will also discuss other technology, bandwidth and other operation and maintenance initiatives. We think this is the right path for smart telcos. The fourth element of this operation is information technology. The fifth part was a period of major development for our system. We know this may create some instability at first, but there is certainly a fundamental basis for the evolution of the company.

We implemented a new Internet of Things platform connecting to our network. We finished the migration of the machine-to-machine management system of Porto Conecta. On the network digitalization front, we signed a new contract, implement 37 data centers through 2021. And we've completed the delivery of new charging and billing features to support new products and customer care activities.

The progress of our infrastructure is key for pursuing elevated customer experience and satisfaction. That is why we need to solve the issue of today, while preparing for the future. Having this in mind, this quarter, TIM was the first operator in Brazil to initiate 5G tests on realized network in 3.5 GHz band. We are testing in 3 different locations with 3 different vendors. We are conducting

trials with technology institutes to evaluate different products, solution and new business model and to develop reference center on this new technology.

The development of our infrastructure has been a key element to transform the company in many areas. The digitalization process, for instance, is helping to change significantly client experience and improve satisfaction, at the same time as it positively impacts our OpEx. Our digital transformation program attacks 4 major fronts: caring, billing and payment, acquisition of clients and Prepaid recharges. In all of them, we are delivering strong evolution, which helps to capture the savings forecasted in our efficiency plan of BRL 1.2 billion between 2019 and 2021.

Our efficiency plan is a combination of digital and traditional initiative and the right implementation of both is generating robust savings. In the first half, they reached around BRL 330 million. This led normalized OpEx to remain stable in the quarter and during the first 6 months of 2019. Despite the overall positive dynamics in cost and regardless of staying at 3% of gross revenue, bad debt still represents a challenge. To put it into perspective, excluding bad debt, our normalized OpEx only decreased by 2.1% year-over-year. Our expectation is that we reach an inflection point in this line during the second half of 2019.

Moving on the other financial highlights. As I pointed out earlier, despite a tough macroeconomic environment and competitive landscape, the company was able to accelerate revenue growth when compared to the previous quarter.

In the second quarter, top line grew 2.4% year-over-year. The acceleration compared to the first quarter was mainly driven by mobile revenues, which grew 1.9% combined with low double-digit fixed revenue expansion mostly reflecting TIM Live growth.

Mobile service revenue performance was driven by ARPU dynamics, as I mentioned before, showing a solid mid-single-digit growth. And this resilience is a consequence of the expansion of a high-value customer base. Postpaid lines now represent close to 40% of the customer base, while Postpaid revenues represent 66%. Despite this, it's important to realize that we do not expect Prepaid to reach zero. We believe that Brazil will always have a significant portion of revenue and base in this segment. Thus, both segments are helping to produce a slightly better performance. Postpaid revenues grew 5% year-over-year, while Prepaid low this double-digit decline in the first quarter, twice single digits in the second quarter.

As described until now, our solid execution led to resilient revenues and controlled costs that combined resulted in an EBITDA expansion of more than

6% and once again, the record number for the second quarter EBITDA margin increased by 140 basis points to another record of 37.9%.

In the second quarter, we reported a normalized net income of BRL 423 million, 27% higher year-over-year.

EBITDA minus CapEx increased by 24.1%, reaching 16% of total revenues, while net financial position decreased about BRL 640 million in the last 12 months, leading to a leverage of 0.40x net debt-to-EBITDA. In conclusion, we delivered a consistent first half that put us in a position to reach our annual targets. On top of that, our tax disputes related to PIS and Cofins received favorable court decisions, unlocking BRL 3.4 billion in tax credit, of which BRL 2.9 billion was booked this quarter. Our Board also approved the distribution of BRL 370 million in interest on equity. And we are expecting to reach nearly BRL 1 billion in distribution.

We will continue to focus in execution, while we look for opportunities to accelerate value creation in the second half of the year that we expect to present a more positive external environment.

Thank you. We will now open the floor for questions. Please, operator.

Questions and Answers

[Operator Instructions]

Operator - The first question comes from Ms. Susana Salaru, Itaú.

Susana Salaru (Itaú) – We have two. The first one is related to bad debt. What are the initiatives that have been taken to improve collections or to reduce the bad debt? That would be our first question. And second, I know that you mentioned, but I couldn't actually fully understand, the Mobile Service Revenue trend for the second half of the year, if I understood correctly, you will expect it to accelerate? Just if you could elaborate on that, if that's the case and this is correctly? And what would be the drivers for this acceleration?

Pietro Labriola (CEO) - As we stated also in the previous call, we expect in the second -- related to the first question, that is bad debt. As we already mentioned in the call of the first quarter, we expect to improve our bad debt level in the second half. For sure, we are not satisfied about the level that we have today. And due to the fact that we are optimistic, usually, we see the area where we are not performing at the top as the area where we can have a better level of performance in the future opportunity. So, what we expect with the action that we

put in place that we described also in the previous quarter, we expect an improvement on this area.

For sure, we are trying also to work better on the marketing side. Keep in mind that this is a country where we reached penetration of Postpaid as overall market of 108 million Postpaid customers. So, what is happening today that is important also to start to manage. Let me say, the customer that had the boundaries between Control and Prepaid in a different way.

What we did is that we have launched at the beginning of July, also a new offer that is a kind of Control with payment advance that allows us to control better the risk on the credit, when we are already reaching the market and a penetration of Postpaid. I think also the opportunity to explain better also, what can happen on the revenue because I'm quite sure that when you tell that market has reached 108 million Postpaid customers, some wanting that there is no more growth in the market. This is not the truth. We have to work in the meantime on all the areas.

First of all, the growth of mobile revenues, and so I can answer to you also related to the second question, is coming, first of all, from the up-selling intra-plan. What we mean? We can upgrade Control customers to Postpaid and we're upgrading Postpaid customers to higher ARPU offers. This is one of the reasons why the TIM Black Família offer that allows to increase the ARPU of our customer. We have to continue to work on the Control as we are doing today in a rational way without push too much price because it should be irrational, and we'll never drive a huge increase in terms of elasticity in the volume. And then we have to work on other 2 elements.

The first one, as I was mentioning to you that is the boundary between Control and Prepaid, where there are customers that are willing -- that have willingness to pay BRL 40, but that can have some risk. And so, in this area, a Control offer with a payment in advance could help. While on the Prepaid, and this is the good news, the charges of July are flat compared to the recharges of May. So, we are starting to rebound our Prepaid base. All in all, all these elements will help us to continue to grow mobile revenues. And in the July number, we already see an improvement also in the revenues of the Postpaid.

Operator - Our next question comes from Diego Aragão, Goldman Sachs.

Diego M. Aragão (Goldman Sachs) - Regarding the MOU signed up with Vivo, what can you share with us regarding the potential savings in OpEx and CapEx in both 2G and 4G technologies?

Pietro Labriola (CEO) - Diego, it's too early to give numbers. We got a commitment to work for the next 90 days. On our side, Leo Capdeville that you know very well, that is our CTIO, will lead the project. And we hope to come back in the result of next quarter with some numbers, some more details. But what is important to think -- to say is that we think that this is the right path. Network sharing at this level could allow improving the level of efficiency of our network and further development of our investment in area that will improve the customer experience of our customer base.

Diego M. Aragão (Goldman Sachs) - Okay. And my second question, if I may, is regarding your cash flow profile. I mean, we are clearly seeing some great improvements on your cash flow, as you mentioned, EBITDA less CapEx is growing more than 20% year-on-year. And now you are guiding to distribute BRL 1 billion in IOC this year. So, this marks a great improvement compared to 3 years ago. But my question is, how prepared are you to pursue it further in market consolidation, if some opportunities presented? For instance, we recently stated that they can explore all strategic options to maximize their shareholder value in the mobile business. So, in a hypothetical scenario, where this asset is available, how prepared are you to pursue your further consolidation?

Pietro Labriola (CEO) - Diego, if I can joke, the sentence "we are exploring all the possible option to increase shareholder value", it seems a slogan, because since I am not wrong, it was the same sentence that was used by Vivo in the conference call. But again, come back to the reality. What is happening that we are entering in a period in which we have good opportunity because several things are happening at the same time. The MOU with Vivo is giving us an opportunity to further improve our capacity to continue to increase our network quality in an efficient way. The fact that we are going to have a bid for new frequency, allow us to do evaluation of what can be and can make sense for us. And in the meantime, the market consolidation that it seems will happen, is giving us the opportunity to have, not just one choice, but with the possibility to choose. We are preparing the financial of our company to be able, exactly as you mentioned, to explore all the opportunity that can increase for our shareholder, the value of our company. It will be an interesting period of time. The second half, I think that will give us a lot of surprise.

Operator - Our next question comes from **Frederico Mendes, Bradesco**.

Frederico Mendes (Bradesco) - I have two questions as well. I mean the first question is on the revenue front, I just wanted to get a better understanding about the line other revenues, especially I'm not sure if you give this, but if you could

give any color about the cancellations, the revenue from cancellations of all these lines, this would be great. That's my first question.

And then on the second question, I think it is broader. But what is the strategy of TIM today? In the past it was really clear that the company was focusing on improving its network in up-selling. Today, it looks like you're much more restricted of this up-selling, also because of the impact on our bad debt. So just trying to understand, TIM today will be focusing more on the Prepaid clients? Especially as TIM Pré Top is getting relevance, so you continue to focus on increasing your Postpaid bases? Where are you, turning today, let's say, TIM in the next one or two years?

Pietro Labriola (CEO) - About the revenues in the other revenue line, we have something that is, for us, also really important because it's that fast in terms of cash flow. It's an important accelerator in terms of our network development. And so, it is very helpful on both sides. Let's remember, in any case that we continue to post a real very good profitability number. On the EBITDA, we reached 37.9%. On the other point, that is more ready to strategy that has also, again, to explain better what we can expect in the future. What we are doing, if I can tell, let me say, slogan, we are discontinuing in continuity. What I mean? For sure, the strategy of continue to up-sell Prepaid customer base to Postpaid is no more the only mantra of our company. So, what we are going to do?

On the traditional services, what we have to do is that we have to work very well on the quality to increase our level of service on the Postpaid. Trying to create a better continuity of the offer to continue to convince our Control customer to move to the Postpaid. The creation of Plano Família was made to put something more on the Postpaid to convince our customer base to migrate from Control to Postpaid. Just to give you some idea, on the Postpaid Plano Família offer that will be also put on the other TIM Black Postpaid offer, where functionality has rollover or the possibility to have direct access to a human attendant. Why that? Because you have to justify for the customer why they should move from BRL 50 or BRL 60 of Control to Postpaid. And this is the part that we are mentioning related to Intra-plan migration.

Under Control, we have to continue to migrate our customer base from Prepaid to Control. But it's clear that I can tell you that the volume that we reached in the past cannot be maintained. So, we have to work in a different way, trying to reduce the level of risk on bad debt, working also with new kind of offer, as I mentioned before, where the payment is upfront.

Last, but not least, on the Prepaid segment, we have to continue to work with because we have a huge opportunity of ARPU uplift with the consolidation of the

second SIM to our customer. On top of that, we have to consider that there are areas that we are going to develop, and then we will discuss more in the end of the year for the next 3-year plan, we are working to understand the opportunity that arise from mobile advertising and financial services. I don't have to mention to you about other players, our competitors, that are adding to this area revenues between BRL 100-120 million. So, I'm not telling that they can reach this amount of money in 1 month, but it shows you that there is opportunity also in this area.

So, all in all, we have to continue to execute very well on the traditional services on something that is no more just one action, but is 3 or 4 actions in the meantime. We have to improve all the quality and the performance in our customer base, because the name of the game would be chain reduction and we have to start to explore also adjacencies as we mentioned, financial services, mobile advertising, IoTs. Then in the mid to long run, we have to evaluate also the opportunity that can arise from fixed wireless access, because I think that we are the operator that is positioning the best condition to exploit this kind of opportunity, being the operator with the lowest level of legacy on fixed network.

Adrian Calaza - TIM Participações S.A. - CFO and Member of Board of Statutory Officers

Adrian Calaza - This is Adrian. On your first question related to others. As Pietro was mentioning, the main portion of these other revenues are related to network sharing. And mostly in this case of the second quarter to swaps. As we already discussed, this is about swap for us. It's also very important. It's not only a source of revenue. It's most of all, it's source of efficiency in terms of both CapEx and OpEx. And also, in terms of timing, where these swaps bring us additional, for example, fiber coverage that we need to construct it, it will take a long period of time. So just to give you an idea of what the importance of these sources of revenues for us. So probably, you will see also in the future in different quarters, some jumps in terms of the other revenues mostly related to the swaps. On the other hand, then you have the rent sharing agreements that we have, those are most stable revenues. So again, just know the underlying importance of this line.

Frederico Mendes (Bradesco) - Perfect, perfect. Adrian, Pietro, it's very clear. Just wanted to follow-up here on the same front. So, basically here is, you are investing mostly on infrastructure the major part of your CapEx is going on that way. So, when you are more of a near unique sense to believe that also that infrastructure relative to you the more of your network. And then, of course, this line should continue to go up. I'm assuming, the margin of the line is relatively similar to sell plan on the B2C. You should not have a major change in this line increase in the future, should not have a major change in margins. Is it correct?

Adrian Calaza - I'm not sure if I heard correctly your questions. Relative in terms of margin as you know, clearly, this revenue would have very low margins. What brings us additional efficiencies mainly on CapEx and on future OpEx. Then clearly, we are improving our infrastructure. These are additional fiber coverage that we have and those that we sell to other operators. Just remember that each operator uses a slow portion of a fiber deployment. So, it's always important to have this network sharing. You saw that there are a lot of movements in the last years related to network sharing. It's imperative for the operators to be much more efficient in the use of infrastructure. So, everything is related in the sense.

Operator - Our next question comes from Valder Nogueira, Santander.

Valder Nogueira (Santander) - One first quick question. How much of the pace of Postpaid has been hurt by what's happening in the bad debt side? Are you more cautious? You mentioned, Pietro, that you were working on the customers that were on the boundaries of the 2 plans. But how much has bad debt hurt you? That's the first question.

Pietro Labriola (CEO) - Part of the bad debt is rated exactly from what you mentioned. We are more cautious. Just to give you an idea about what happened usually, we have the acquisition then the customer that can generate bad debt appears in terms of cancellation mainly after 6 months and the bad debt continues to generate that effect in 9 months. So, this is the reason for which we are forecasting an inflection rate in the second half. What we are doing is that we are doing some fine-tuning in our strategy. We are not doing it breakthrough. But it's something that makes a lot of sense to further improve our financials overall. This is the reason of which we expect also weak bad debt in the third quarter that will not impact our achievement in terms of revenues and margin because again, differently from what's happening in the past, we are able to manage the transition without generating impact in our numbers.

Valder Nogueira (Santander) - Okay. And second question is that a lot have been said that some M&As are happening on the spectrum side. And we have an upcoming 5G auction. And we also have some frequencies can due, some already beginning next year and some in 2023. How do you play out your spectrum capacity vis-à-vis the spectrums that are coming due, not only of competitors, but yours? The possibilities that you have to do M&A involving spectrum from other players? And how concerned are you with the renewal of the existing mobile licenses? And at which cost?

Pietro Labriola (CEO) - Okay. Valder, I leave the stage to Mario, but in this case, just as a strategic view. As we mentioned before, we want to say that we are entering in a period of time where acting in a clever and rational way, we have more opportunity to improve our position compared to what was happening in the past. But I leave Mario to better answer.

Mario Girasole - Yes. Thank you for the question. Probably you can imagine this issue with 3 dimensions. First of all, of course, you will have in some point of time, next year probably, new spectrum available, this is not only 5G spectrum because there would be also the 700 MHz spectrum that is typically the 4G. So, the 700 megahertz, 2.3, 3.5 and millimetric spectrum. On the other side, today you have a lot of agreements among players in specific areas to share spectrum that increases also the capacity of the system to manage these scarce results. And then what was the third point you had? I don't remember.

Valder Nogueira (Santander) - The license.

Mario Girasole - License. Yes, the license. The license is, of course, one of the key pillars of the PLC79. The PLC79 that, of course, is fundamental for the sector as the fixed concession side and as the mobile successive renewable side that we expect will be approved this year because this is something, of course, that from a regulatory point of view is, of course, needed by the sector as a whole. So, the PLC79 for the renewal, spectrum sharing for efficiency and the new spectrum for the next year.

Valder Nogueira (Santander) - Okay. But it's still on that question, Mario. Do you have an expectation, assuming that the PLC79 may be approved, okay? Assuming that is approved, and it comes with, say, the ability to renew the license. Has there been any consideration of at which cost this renewal will take place?

Mario Girasole - The reference we have today, the cost that we have today for the renewal, that is 1% per year of the net revenues related to that spectrum. I think that the good news could be the fact that today, this is a cash out. In the new scheme, we could have, for example, a pay or play, a possibility, not to cash out this value, but to invest this value in those coverages, so the last favorable areas. And so, we think that the value reference we think is more or less the reference that we have today. The idea is to consider it as additional CapEx possibility.

Valder Nogueira (Santander) - Okay. This is an area that I believe is not properly exploit, to revert that learning into coverage?

Mario Girasole - Yes.

Valder Nogueira (Santander) - Are you confident that this possibility could fly?

Mario Girasole - No. This is what we are discussing at legislative level. This is clear. The basis of the PLC79 is that all the resources created by the PLC79, all will be available for the coverage that the country needs. So, we think that is also for the spectrum, we will have this new arrangement.

Leonardo De Carvalho Capdeville - TIM Participações S.A. - CTIO & Member of Board of Statutory Officers

Leonardo De Carvalho Capdeville (CTIO) - Well, just complementing some part of this spectrum strategy... As Mario said that we are focusing, let's say, 3 main pillars. The focus is about the new spectrum, you are right. We have an auction ahead. But as important as that with the PLC79, we have the spectrum trade. So, maybe some opportunity can come from this line. The second is the opportunity that we are facing from the sharing agreement. Remember that in the past, we had agreement for RAN sharing with Oi and we, let's say, make an upside of the RAN sharing from MORAN to MOCN is used as the spectrum sharing in a more advanced way.

The third, and so important is that, is that the technology is suffering a very, very, let's say, optimistic, incremental for efficient users of this spectrum. On that I'd like to highlight that we were the third company, let's say, in the world, to test the new technology for MIMO in 4G in our network. And the result was very, very interesting. Just to your point, another, we have a 2, 3x more capacity on the same spectrum using this kind of MIMO. This is a technology that I used lately from our 5G round and what some vendors are doing is anticipate this technology, MIMO on 4G. So, we are seeing that on this front, we have a very interesting opportunity to increase our capacity using the existing spectrum. Okay?

Valder Nogueira (Santander) - Thank you, Leo, always refreshing hearing you.

Operator - Our next question comes from Marcelo Santos from JP Morgan.

Marcelo Santos (JP Morgan) - I have two. The first one is, if you could comment a little bit more on how much space more do you see to gain margins on digitalization initiatives? So, you have several indicators that you prepare that show space to grow. And the second question would be regarding TIM fiber. What has been the main hurdles to grow? I mean, is the sales team, competition? Are there personnel to install the equipment? So, I know you're

growing fast, but what prevents you from growing even faster? These are the two questions.

Pietro Labriola (CEO) - Okay. About digitalization initiatives, we think that we still have good room for improvement. Just to give you an idea, with close, I think, yesterday, or the day before yesterday, they did internal to move part of our customer care functionalities to artificial intelligence functionalities. I think that we will put that in place by September, October, and it will allow us to have a further acceleration on the digitalization and the cost of our customer care.

In the meantime, starting from, just to give you an idea, we changed also our IVR system. I don't want to go too much in detail, just to give you an idea that is not a slogan, but it's the truth. We are changing our IVR system for the Prepaid and in the DDD, where we were able already to do that our capability to add automatized interaction with our customer base moved from 69% to 75%. This gives you an idea of what we are doing. And we expect to move all our segments with this automatized IVR, again, by the end of the year.

The automatization is going strongly on the customer care, but we are working also to better understand all the activities today that are still human intensive, because for the next year we are imagining a specific project to work with artificial intelligence in the area where we have seen a lot of activities that are human intensive. We still have good possibility of improvement also on the recharge, where we have already reached a good level. But we think that we can move forward. And I think that in next quarter, we will present also a new concept of a project I think internally is so-called Next TIM that could further accelerate our capacity to be efficient using digitalization.

Related to TIM fiber, what's happened was that among some of the different players that we are using as for maintenance and delivery, was a company that was unable to perform. So, what's happened that you have to change and change this kind of company takes time. In fact, the issue today was mainly related, not to our commercial performance, because we have reached the highest level of gross adds, but was more related to the level of service that we were guaranteeing due to this problem.

In the meantime, another factor that caused us to decelerate was that in some cities, exactly that is up and also for the mobile to put new antenna, we are probably to use the poles to put our fiber. The last on our side was that we have increased, we have doubled the number of projects that we have to manage. Because in this way, if there is a rejection of 50%, we're able to, in any case, deliver what we have in the plan. We are quite sure about that because in the third quarter, we are recovering the part of the gap that was generated in the first

half and we're sure about that because we already started installation. And the main part, the main bottleneck that was the bureaucratic authorization was already passed.

Operator - Our next question comes from Maria Azevedo from UBS.

Maria Tereza Azevedo (UBS) - I still have two questions on my side. Following up on the previous CapEx questions. If you could please comment how disruptive do you think 5G is going to be to your strategy, if you're expecting more gradual rollout? If you see any disruptive CapEx cycle out of it? If it's going to be more focused on B2B initially? And in the past, we're very vocal about WTTx and fixed wireless broadband. How important do you think that's going to be for your 5G and residential strategy going forward? So that would be my first question.

Pietro Labriola (CEO) - Okay. Maria, I'm trying in some way to answer both the questions. The second question was related to the WTTx and how much is important in our future strategy? And this also confirms what I told before. We see in this market, a huge opportunity coming from fixed wireless access. The activity that we put in place with WTTx was very useful for us because is allowing us to better understand how to manage this kind of business, that is not complex as this fixed line business in terms of delivery and all this kind of stuff. But in any case, it's not exactly the same to sell a SIM in a shopping. And this is very useful. And I think that also, the position of some of the other player related to the 5G is also related to the fact that they see 5G as fixed wireless access as a threat to their business model.

Related to the CapEx in the 5G, we do not imagine a disruptive approach, but it's more a gradual approach in the development. It's clear that it's too early to try to understand better the level of CapEx and all this kind of stuff, because it's important to understand better from what will be published by Anatel with the public hearing that will allow us to have a better understanding about what can be done. But what they told you is exactly the position of SindiTelebrasil, the position of all the operators that don't want an approach that could drive a huge amount of CapEx upfront, and with a gradual development of that. I don't know if I was able to answer to your questions.

Maria Tereza Azevedo (UBS) - Perfect. No, that's very good. And my second question would be on competition. You have talked here in the past that the entire industry should take a step back in terms of aggressive zero rating offers. How rational do you see your competitors on that front? I mean do you expect

pressure now to improve both in terms of pricing, but also in terms of bundles and zero rating apps?

Pietro Labriola (CEO) - I can tell you that what we are experiencing is that with some small exceptions, I see clarity for more rational and some more on the same line for us than the 2 players that must be controlled in terms of rationality, are Nextel and Oi. While Nextel is very aggressive below the line offer. And you will understand that also looking at the balance of the mobile number portability. We are very aggressive also in the acquisition that is something always risky in terms of bad debt. But again, we think that is a momentum, because it's very difficult to take that place that amount of giga, with that kind of network. So, makes no sense to react in an irrational way. And we're starting to see some irrationality on the Oi side, but I think that is quite understandable. I don't think that is a strategy that can be sustainable in mid-long run. Yesterday, on TV, I saw an offer BRL 99 for 50 gigas, now I don't have to tell you always about the network of some players to understand that this is something that is sustainable in the short run for a small number of customers. All in all, I continue to see rationality and perhaps market consolidation will have to continue with this rationality that will help everybody to improve. The quality of service for our customers has to increase the quality of the network throughout the country.

Operator - Our next question comes from Alejandro Lavin from Citigroup.

Alejandro Lavin (Citigroup) - Just a couple of quick questions from your guidance for this year. So, the first one would be, just to confirm, you are still confident on reaching all your targets for this year? And the second is, would this be possible with the current pace of GDP growth? Or would you expect, or would you need an acceleration in GDP in the second half to get there?

Pietro Labriola (CEO) - Okay. I think that is important to realize exactly what you mentioned in the beginning. Our guidance was built with the GDP expectation that was stood at 2.5%. And so, we continue to restate that we are confident to reach our guidance in a tough environment. We hope also that the improvement will be more, let me say, psychological, because the impact of the pension reform will not generate the flow of money in Brazil in the second half, but we generate psychological impact that could restart the willingness to spend by customer. But again, we are confident to reach our guidance also in this kind of environment that was changed compared to the beginning of the year.

Operator - Without any more questions from analysts, we will now start the Q&A session with the press.

Vicente Ferreira - This is Vincent Ferreira. The first question comes from Ana from Convergência Digital. And the question is, like, could you detail the new contract to implement the 37 new data centers until 2021, in a moment where your rivals are scaling down from those activities?

Leonardo De Carvalho Capdeville (CTIO) - In fact, we need to highlight that we are talking about a different data centers here. The data centers that our competitors are scaling down is about the old ones, this is kind of a biggest data center and more focused on IT. The new data center that we are talking here in TIM is about the evolution for the virtualization of the core on the network. This is smallest and is more applied for our future topology that will be very, very necessary for the 5G. Because in the 5G, we will need to have more, let's say, power computing and more content delivery on the edge to use at maximum, the low latency the technology came.

One important point that you highlight is that now we are testing in a 3 different regions, the 5G in Brazil. One is in a city in the South, other in Southeast and other in Northeast. And the way that we are doing that is exactly to use this kind of new concept of topology in a virtualization core and our content cache. So, with that we can deliver a very important quality over the 5G. So, the idea here is to increase this presence. Remember that in Brazil, you are talking about a country with some kind of continental territory. So, it's very important for the customer experience that we have more on the edge this power capacity and the content.

Vicente Ferreira - The second question comes from Miriam from Telesíntese. And she'd like to know about the MOU with Vivo, if in this MOU will have as well a sharing of frequencies?

Leonardo De Carvalho Capdeville (CTIO) - Hi, Miriam, it's Leonardo, again. In fact, the MOU with Vivo is focused to have the most efficient, let's say, investment and the use of data for the best customer credit quality and experience. So, I guess the details, we will be in the end of this work, we have 90 days to conclude that. But it's possible that we use this kind of spectrum sharing. Again, this is not new. We already did this with Oi in 2.5 GHz. So, it is the kind of discussion that our technical group will have to present the best way to use this spectrum.

Vicente Ferreira - The last question coming from the press is from Mr. Alexandre Melo, Valor Econômico. And he would like to know if understanding on the sharing of infrastructure as a more advanced way, means that in the coming auctions, TIM and the other operators will proceed in forming a consortium to make bid together on those lots that are going to be sold by the government?

Mario Girasole - Thank you, Alexander. Mario Girasole speaking. The participation options in a bid are written in the rules of the bid. So, we don't know what will be these rules. In general, from the experience of the past bids is the consortium option was not an option from a regulatory point of view. At the same time, in particular, the 4G bid 2.5 and 700 megahertz, that creates some incentives in network sharing to implement the network, that is what we did since 2013. And we are trying to put as a business practice in the last several weeks.

[Operator Instructions]

Operator - Ladies and gentlemen, without any more questions, I am returning to Mr. Pietro Labriola for his final remarks. Please, Mr. Pietro, you may proceed.

Pietro Labriola (CEO) - Thank you. I want to reiterate what I said during our last conference call. TIM Brasil has strong fundamentals and we're in a position to take full advantage of the economic recovery that should accelerate in the second half into 2020. With the go-to-market adjustments we are implementing as we return to our DNA, we're already regaining momentum. The road will be bumpy, but we are back to the right track.

Before we conclude this call, I'd like to say we have 2 great additions to our team that I'm sure will contribute significantly to our business: Mr. Alberto Griselli has joined us on the executive team as Chief Revenue Officer, with over 15 years in consulting teams; and Mrs. Flávia Bittencourt as independent Board member with many years of experience in telecom, banking, private equity and consumer goods.

Thank you, once again, for participating in our conference call. Have a great day. And I hope we can meet soon.

Operator - Here we conclude the second quarter of 2019 conference call of TIM Participações. Your lines can be disconnected. From now on, for further information and details of the company, please access our website, www.ri.tim.com.br. Thank you.
