

Half-year Report



This version of the Half-Year Report is a translation from the original which was prepared in the Czech language. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the Czech version of the Half-Year Report takes precedence over this translation.

Note:

O2 Czech Republic a.s. hereinafter "O2 CZ" or "O2" or the "Company".

O2 Slovakia, s.r.o. hereinafter "O2 Slovakia".

O2 IT Services s.r.o. hereinafter "O2 IT Services".

Belonging in the Group O2 Czech Republic are the company O2 Czech Republic a.s., subsidiary companies involved in the concern, and other companies in which O2 Czech Republic a.s. has an ownership interest, hereinafter "O2 Group".

Financial data and information listed in this Half-year Report are not verified by an auditor.

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Foreword by the Chairman of the Board of Directors

Dear Shareholders,

First let me follow up on what I already stated in the 2015 Annual Report. After the successful spin off of our fixed and mobile infrastructures, we dedicated ourselves fully to improving the efficiency of all our operations and commercial activities. We openly declared we did not want to be just a telecommunications operator but what is called 'digital economy enabler'. We want to help people realize their potential, be agent of inspiration, motivation and information. For this reason, we tasked ourselves with accelerating the development and planning of new products and services and improving the existing ones, among other things.

I am pleased that our performance and results in the first half of 2016 demonstrate that we are on the right track. We brought out a number of innovations for our customers. Their reaction and behaviour show that they are positively curious about our new proposition to them, and they buy our new services. The loyalty of our customers has, in some areas, hit record high. The growing demand from our customers has reflected positively also on our financial performance. As a result, we could invest in areas that, in the future, will become the source of new experiences for our customers and new revenue streams for us.

In the area of fixed voice, which has, for a long time, been showing a negative trend due to the high fixed-mobile substitution, in January we introduced a revolutionary tariff with unlimited on-net and off-net calling within the Czech Republic. Already six months after it launched, it became apparent that was very popular with our customers: they call 40% more and the volume of outgoing minutes to mobile networks grew 210%. As a result, the trend of declining fixed voice revenues slowed down to a half of the original rate.

O₂ TV, our digital television product, is also enjoying a surge in popularity. After we introduced a streamlined proposition and launched our sports channel O₂ Sport last year in summer, in January we started offering an OTT version to all homes in the Czech Republic, regardless of the provider of their internet connection. Already more than 30 thousand customers got a second set-top box for their home. In the second quarter of the year, we promoted our offer through the campaign O₂ TV Try & Keep, which granted a free two-month trial to all new customers. Watching television via a web-based interface and on the small screen is increasingly popular with customers, with their numbers growing two and a half times year on year, to close to 300 thousand. We also acquired additional exclusive rights to sports events and, at the beginning of August, we are launching a new channel, O₂ TV Football. Actions like these contributed to a 70% year-on-year increase of O₂ TV revenues in the first half of the year.

In the mobile segment, we focused on increasing the coverage of the population with our 4G LTE network; the service is presently available to more than 90% of people in the Czech Republic. This ranks us in the top five countries in the European Union. We want to roll-out broadband internet to 99% of the population by the end of the year and focus also on network densification, to improve signal quality also inside buildings. In the auction of the remaining spectrum, which ended in the middle of June, we secured four out of seven 1.800 and 2.600 MHz spectrum blocks for our customers, for the total price of close to 1.5 billion Czech crowns, so that we can accommodate the growing demand for data. This strengthened our position on the vanguard mobile broadband internet.

Thanks to the increasing penetration of our fast mobile network, tariffs with generous data plans and simpler ordering of additional data after the allowance is used up, the volume of data traffic increased 80% year on year. More than 50% of devices in our network are smartphones, and one in four already supports 4G LTE. All these factors reflect positively on mobile revenues, which grew 12% year on year and continue to compensate for the loss of revenues from traditional voice and SMS which are under sustained competitive pressure in the business segment. From May, our mobile revenues have to face additional pressure from lower roaming rates introduced by the new regulation. We were the first operator to start offering travel insurance to our roaming customers; the service can be easily activated every time the customer signs on in a network abroad.

Our corporate and government clients continued to enjoy the benefits of our communication concept Elastic Business Solutions. On this platform, we focus on the promotion and description of specific application of our ICT, IT, voice and data products and services, which boost the capacity of businesses to flexibly respond to the changing business environment.

Despite the fact that, in the first half of 2016 we recorded a growth in our customer base and financial performance in Slovakia, the dynamics has been slowing down. We decided to enter the fixed access market, to ensure that we keep growing also in the future. Through our subsidiary O2 Business Services, we successfully completed the design of our product portfolio and went commercial with our proposition for corporate and government customers. In collaboration with O2 Slovakia, we prepared a commercial proposition of mobile

services which we started marketing in the second quarter of the year. We signed contracts with major government and corporate customers.

As concerns financial performance, the total consolidated revenues reached CZK 18.2 billion, which is roughly equivalent to the first half of the last year. In the second quarter, the year-on-year dynamics improved, mainly as a result of an upturn in the market trends in the Czech Republic. Our commercial and sales initiatives in fixed voice and pay TV, as described above, are making a positive contribution. After a 25% leap increase in 2015, in the first half of 2016 we managed to sustain a further slight EBITDA growth. Despite an increase in the payroll costs due to insourcing of our call centre personnel, assigning core employees to boost customer care capacity at new brand stores and recruiting additional IT personnel, and due to the incorporation of O2 Business Services in Slovakia, the total costs (sales and operating costs) fell 2% year on year. The net profit increased 10%.

The first half of the year also confirmed that, after the spin-off of our infrastructure into a separate company, we are a business with a low investment requirement. The ratio of investments to revenues was 6.2%. We carried on with our investments related to IT transformation, with the aim to streamline systems and processes and shorten the time-to-market for new product and services. We also invested in core networks, acquired additional broadcasting rights for sports events and bought a live truck with state-of-the-art equipment which we use not only for our own live broadcasts for our sports channel, but we also rent it out to other partners in the Czech Republic and beyond. In Slovakia, we invested mainly in improvement of the quality of our 3G network and the roll-out of our 4G network; we plan to accelerate the project, especially in the second half of the year. In connection with our venture into the fixed access market in Slovakia, we completed the roll-out of the 3.7 GHz wireless access FWA network with a blanket coverage of all regional and district towns.

I expect that the market environment will remain highly competitive also in the second half of the year. Yet I am confident that we can rise to this challenge and capitalize on our strengths in order to improve our market position. We will take advantage of the fact that the rate of development of new technologies and services is very dynamic in our industry. We will continue to bring products, services and solutions to the market which add to customer experience and help us cement our leadership of the Czech telecommunications market.



Tomáš Budník

Chief Executive Officer and Chairman of the Board, O2 Czech Republic a.s



Calendar of key events

January

The Professional Services Division was spun off into the subsidiary O2 IT Services s.r.o.

The Company considerably reduced its portfolio of fixed voice products and started offering unlimited calling to all fixed and mobile networks in the Czech Republic.

The Company increased its international internet connectivity in the Czech Republic, with TeliaSonera chosen as the principal provider.

The Company released its operating and financial results for the year 2015, confirming that the premise of benefits of separating the fixed and mobile access infrastructure, as posited in earlier analyses, was correct.

Wood & Company Financial Services, a.s. commenced the process of acquisition of Company shares on the regulated market as part of the share buy-back programme.

February

The Company expanded its O₂ TV distribution network. The new type of set-top box can be bought at electronics retailers and also online.

A part of Corpus Solutions a.s., a software development company, was integrated into the subsidiary O2 IT Services s.r.o.

The Company started pilot testing of the hybrid modem. The new device combines fixed and mobile access technology.

March

Acting in capacity of sole member exercising the rights of the General Meeting of O2 Slovakia, s.r.o., O2 Czech Republic a.s., approved the payment of a share from the profit of O2 Slovakia, s.r.o. for the year 2015, in the total amount of EUR 41.1 million (approximately CZK 1.1 billion), to the sole member O2 Czech Republic a.s.

The Company launched 3CC technology in Nové Butovice, Prague, which allows to use three frequency bands concurrently and increases the speed of mobile data as well as the network capacity.

O₂ TV expanded its content proposition to include DTV and the most popular videos from Aktuálně.tv owned by the publishing house Economia.

The Company increased the Playback function interval in O₂ TV to 50 hours from the original broadcast.

April

The Company announced that it would start, as the first in the Czech market, to offer insurance in a mobile, and that, starting from 30 April, two additional roaming tariffs *Volání bez hranic* and *Svět Basic* would be added to its portfolio.

The Company acquired a new mobile unit (OB van) for live television broadcasts of not only its own O₂ Sport channel but the van is rented to other local and international partners.

The Company started offering NAISÍTI prepaid card which offers, in addition to low rates on calls and SMS to all networks, also an economy data package.

O2 IT Services s.r.o. opened Security Expert Center (SEC), a new cybersecurity centre in Prague.

An Ordinary General Meeting was held. The supreme governing body approved the regular (unconsolidated) financial statements and the consolidated financial statements for the year 2015 prepared under the International Financial Reporting Standards (IFRS). The General Meeting also approved the distribution of unconsolidated 2015 profit and a part of unconsolidated retained earnings, in the total amount of CZK 4,964 million, as dividends.

O2 Czech Republic a.s. and China Telecom (Europe) Limited signed a Memorandum of Cooperation.

The Memorandum covers several strategic areas: data roaming, international connectivity, data centre services, as well as development projects in the field of e-government and smart solutions.

The Company released its operating and financial results for the first quarter of 2016. Despite the increased pressure, especially in roaming and corporate services, the Company maintained its operating profit level of the previous year. The Company strengthened its position in the digital television segment (O₂ TV), mobile data and in Slovakia.

May

The start-up accelerator BOLT forged strategic partnership with two businesses: Taxify taxi service and Dateio, a precision marketing consultancy.

Kateřina Pospíšilová was appointed director in charge of strategy, innovation, regulation and competition law.

The Company announced its partnership with Oliver consultancy, to start from July. Oliver will coordinate the in-house creative team.

June

The Company partnered with Spotify, the world's number one music streaming service.

The Company launched Datomat – a place where customers can do various challenges to earn extra data on top of their tariff data allowance.

The spectrum auction for the 1,800 MHz and 2,600 MHz frequencies ended. The Company secured four out of seven auctioned blocks for the total price of close to CZK 1.5 billion.

The Company introduced O₂ eKasa, a comprehensive electronic record of sales solution.

Independent multinational certification agency TÜV NORD Czech, s.r.o. audited the Company's Integrated Management System (IMS) in its entirety, as a precondition for recertification. The Company retained all its certificates.



Business overview

Factors significant for the business and the results of the first half of 2016

THE CZECH TELECOMMUNICATIONS MARKET

Also in the first six months of 2016, the Czech telecommunications market was driven mainly by innovation in the area of mobile data and television broadcasting. The market saw further acceleration and increasing of availability of mobile and fixed internet.

Sharing of 3G and 4G mobile networks also continued, as did the consolidation of 2G networks; the joint project with T-Mobile has been pursued by Česká telekomunikační infrastruktura a.s. (CETIN) from 1 June 2015, after the demerger of the Company. In the area of fixed internet access, CETIN continued with the construction of remote DSLAMs, which, together with the implementation of vectoring, resulted in a growth of the customer base and broadband internet availability, and increased the connection speed for existing customers.

Operators also responded to the enactment of the electronic record of sales legislation and brought out business solutions to address the need.

An overview of the main additions to the O2 CZ proposition can be found in section Residential segment.

In January, T-Mobile increased the data allowance for its premium tariff, and, in April, also for its prepaid weekly bundles. At the beginning of the year, the company revamped its home internet proposition; presently it offers three home internet tariffs. In April, T-Mobile launched a TV product with three tariffs and a 48-hour playback function.

In March, Vodafone innovated its family tariff *Red+* and *Red+ Business* and started offering *Připojení bez kabelu* (Connection without cable) for free with the shared tariffs. In May, Vodafone rebranded its premium tariff to *Red LTE Premium*.

In March, UPC Business launched the campaign *Neplaťme víc* (Why Pay More), as part of which it unveiled two new VoIP tariffs; data customers of other providers are also eligible.

On 14 June 2016, the Czech Telecommunication Office (CTO) announced the completion of the auction of available spectrum in 1,800 MHz and 2,600 MHz band. Out of the seven blocks auctioned, the O2 CZ claimed four (three 1,800 MHz and one 2,600 MHz blocks), while T-Mobile bought two blocks (both 2,600 MHz) and Vodafone one 1,800 MHz block. The total price paid for the spectrum reached CZK 2.6 bn, with O2 CZ due to pay close to CZK 1.5 bn.

REGULATION

Legislation

In terms of legislation regulating the area of electronic telecommunications or with material implications for the business of O2 CZ, no fundamental changes occurred. Regulation (EU) 2015/2120 of the European Parliament and of the Council of 25 November 2015 on roaming regulation and network neutrality came into effect on 30 April 2016.

Relevant markets analysis and product regulation

O2 CZ continued to meet its obligations based on the relevant markets analysis which the CTO completed in previous periods.

The CTO published an analysis of relevant market no. 1S (formerly market no. 1) – Access to a public telephone network provided at a fixed location, and of relevant market no. 2S (formerly market no. 2) – Call origination in a public telephone network provided at a fixed location. Both analyses concluded that the markets had failed the so-called three-criteria test. As a result, they cannot be considered as relevant, and remedies can no longer be imposed.

The CTO published an analysis of relevant market no. 2 (formerly market no. 7) – Wholesale call termination in individual mobile networks. As in the past, the CTO proposed to make all network operators players with significant market power and to impose duties in the existing scope. The call termination rate remains subject to regulation at CZK 0.27 per minute exclusive of VAT.

International roaming regulation

Roaming services and prices in the European Union are regulated until 2022 by Regulation of the European Parliament and of the Council (EU) No. 531/2012. According to European regulation, regulated retail prices published on 1 July 2014 applied until 30 April 2016. From May 2016, the rates were adjusted by Regulation of the European Parliament and Council (EU) No. 2015/2120, amending, among others, also Regulation No. 531/2012.

Frequency spectrum management

A tender procedure for the frequencies of 1,800 MHz and 2,600 MHz was held in the first half of 2016. The auction part was concluded on 14 June 2016, with O2 CZ securing 2 x 10.8 MHz frequencies in the 1,800 MHz band and 25 MHz in the 2,600 MHz band, for the total of CZK 1.5 bn. On 19 July 2016, the CTO announced that the second phase of the auction part in which the spectrum was divided has been completed. On 26 July 2016, the CTO called O2 CZ for payment of the total price for awarding the right to use the radio frequencies in the amount of CZK 1,472,050,000. The Company made the payment on 5 August 2016. On 22 August 2016, the CTO returned to the Company a guarantee of CZK 450,000,000, which was a condition for participation in the tender. O2 CZ paid the guarantee in March 2016. Based on the tender conditions, the Chairman of the CTO Council shall decide on the awarding of an allocation of radio frequencies within 30 days of the total price payment. To the date of approval of this Half-year Report (24 August 2016) the allocation of radio frequencies award did not happen.

The CTO is working on a tender procedure for the 3.7 GHz frequencies, to start only after the full procedure for the 1,800 MHz and 2,600 MHz frequencies is concluded.

Products and services

RESIDENTIAL SEGMENT

In the first half of 2016, the Company debuted a number of new products and services. In addition to traditional voice, messaging and data, customers benefited from many offers, e.g. discounts at partner stores in the loyalty programme Extra výhody, up to 40% off O2 services with Extra karta or regular credit for digital content purchases in O₂ Active.

Mobile services

The roll out mobile 4G LTE internet continued in the first half of 2016. At the end of June, the service was available to close to 90% of the population; the Company plans to reach 99% population coverage by the end of the year. In Nové Butovice district of Prague, the Company launched 3CC technology which allows for concurrent use of three frequencies, which theoretically increases the speed of mobile internet to around 300 Mbps, and boosts the overall network capacity. The Company plans to launch 3CC also in other districts of Prague by the end of the year.

In connection with the roll-out of 4G LTE, the Company also focused on marketing devices which support this technology. During the course of April and May, the Company invited customers to exchange their old handset for a new, 4G LTE-enabled one, with a recycling bonus of CZK 700. At the end of the half-year period, one in four handsets were 4G LTE capable, and the volume of data traffic saw an 80% year-on-year increase as a result of the fast mobile network penetration and the proliferation of tariffs with more generous data plans.

In connection with new European regulation, starting from 30 April the Company has been offering two roaming tariffs: *Volání bez hranic* with a discount on travel insurance, and *Svět Basic*, where calls, SMS and data in EU member states are billed at the same rates as in the Czech Republic, with a per-unit surcharge.

In June, the Company partnered with Spotify, global leader among music streaming services. The partnership now offers 30 million music tracks to all consumers, and listening to favourite songs does not use up their data allowance. The offer comes with a free three-month trial of Spotify Premium.

In the first half of the year, the Company also launched Datomat – a website where customers can complete various challenges in exchange for extra data allowance on top of their tariff plan. During summer holidays, contract and prepaid customers of O2 services will find a code for 50 MB of free data in each half-litre Coca-Cola bottle bearing the campaign sticker.

In the summer, the Company started offering travel insurance via the small screen, as the first in the Czech market. Like roaming, the insurance is activated automatically, when the device is picked up by the roaming network. The product offers insurance cover against all usual travel-related risks in all countries of the world where O2 has a roaming partner. As a bonus, new and existing customers who travel this summer and subscribe to the roaming tariff *Volání bez hranic* are insured for free.

In the prepaid segment, the Company NAISÍTI, a prepaid card which offers low call and SMS rates to all networks and an economy mobile data plan.

Fixed services

In the middle of January, the Company unveiled a streamlined fixed voice proposition. About a hundred of legacy consumer tariffs was consolidated to only two: *Volání ČR* with unlimited calls to all fixed and mobile networks in the Czech Republic, and *Volání SVĚT*, which, in addition to unlimited calls within the Czech Republic, offers also 1,000 free call minutes to mobile and fixed numbers in the most popular foreign destinations. The majority of homes already migrated to the new tariffs, which proved very popular as they eliminate the need to keep tracks of minutes used and does not charge a rental fee. As a result, people call 40% more with the new tariffs.

Already 60% of homes use broadband VDSL internet which was made possible by to the installation of remote DSLAMs. During the first half of 2016, the Company increased the connection speed for almost 80 thousand homes.

The Company was the first in the Czech Republic to start pilot testing of a hybrid modem. The new device combines the technologies of fixed and mobile internet. Hybrid internet will allow the Company to significantly boost internet speed to two thirds of homes in the future.

The number of active customers of O₂ TV, a service which is available over the O2 landline or an online connection from any provider, reached 217 thousand (IPVT and OTT version combined) at the end of June. The add-on O₂ TV Multi, which lets customers watch O₂ TV on several home television sets concurrently, proved very popular. The service was activated by more than 30 thousand homes. The Company presently manages a base of 250 thousand active set-top boxes.

Digital television owes its present popularity mainly to its unique functions (playback, record, etc.) and the proprietary channel O₂ Sport which offers multidimensional content. Customers also like to watch O₂ TV online on the small screen or in the chain of Staropramen pubs. The number of people who actively watch O₂ TV in the mobile application or online on the internet increased two and half times year on year; in June 2016, close to 300 thousand viewers have already opted for this type of television content distribution.

In February, the Company significantly expanded its O₂ TV distribution network. The new set-top box which, from last year, accommodates internet connections of various providers, is now sold in electronics stores and selected e-shops.

In the first half of the year, the Company innovated its unique Playback function and increased the playback limit to 50 hours after the original broadcast. The function is available via set-top boxes and mobile phones, tablets and the online interface.

In April, the Company launched a campaign offering a free two-month trial of O₂ TV; after the trial period, customers could switch to one of the paid tariffs or deactivate the service.

The sports channel O₂ Sport continued to achieve its long-term strategic goals and expanded its content proposition. From 2017, customers can look forward to up to two thousand matches of the Women's Tennis Association (WTA) tour. O₂ Sport secured the WTA broadcasting rights until 2019, and it is the largest tennis programming package to be aired in the Czech Republic. From the 2018/2019 season, the channel will exclusively broadcast HC Sparta Praha and Bílí Tygři Liberec ice-hockey matches under a five-year contract signed with both clubs.

The Company is developing a concept of three separate channels devoted to the most popular sports: football, ice-hockey and tennis. O₂ TV Fotbal is set to launch already on 8 August.

CORPORATIONS AND PUBLIC SECTOR

In the first half of 2016, the Company further promoted its communication concept Elastic Business Solutions. In April, it hosted Elasticom 2016, an international innovation and new technology conference. The conference set out to increase the awareness of the Elastic Business Solutions concept, and establish the Company as a leader in technology and innovation. In the follow-up phases, the Company will focus in greater detail on specific application of products and services which help businesses adapt quickly to the ever-changing market environment.

The Company significantly streamlined its fixed voice portfolio. New flat-rate tariffs with calls to all fixed and mobile networks in the Czech Republic were offered to more than 170 thousand Czech businesses. There is also a tariff with special rates on international calls for customers who have a need of frequent international communication. The Company is also working to build up its VoIP tariff proposition. In the area of mobile access, the portfolio of actively marketed products has been streamlined, and the Company is presently marketing simple *Vario* tariffs and individual offers. More and more customers take advantage of the self-service portal www.mojeo2.cz.

As regards data and internet, in the first half of the year the Company continued to sign up new infrastructure and national internet connectivity providers through direct partnership. Internet connectivity was boosted for the duration of prime sports events, and the Company also pursued further improvements of its internet and data network. O2 CZ added a number of new products such as O₂ TV or comprehensive Wi-Fi connectivity to its portfolio for corporate customers.

In the area of IT infrastructure, the Company extended its traditional ICT service proposition. The service O₂ Datová centra remains the backbone, around which there are additional services, e.g. dedicated servers and data storage. The Company is also one of the leaders in the Czech market of cloud solutions, not least due to its partnership with global technology leaders such as Microsoft, IBM, HP, EMC and Cisco.

As the rate of cyber-attacks grows, the Company is also focused on providing security services, e.g. O₂ AntiDDoS and O₂ Next Generation Firewall, which grant the necessary level of protection to businesses.

In all its IT service delivery, the Company pays due heed to the concept of Elastic Business Solutions, as evident in the new O₂ Elastická kancelář (Elastic Office), among others. The service combines the conventional (O₂ Desktop) and new components, e.g. O₂ Managed Print Services.

O2 Czech Republic Group

OVERVIEW OF THE O2 GROUP AND KEY DEVELOPMENTS IN THE FIRST HALF OF 2016

O2 Group comprises the company O2 CZ, subsidiaries and some other companies in which O2 CZ holds a controlling interest. In the first half of 2016, the majority of the business of O2 Group was within the territory of the Czech Republic. Through its wholly-owned subsidiary, O2 Slovakia, O2 Group provides mobile communication services to customers in Slovakia. From the beginning of 2016, O2 Group offers, through O2 Business Services, a.s. (wholly-owned subsidiary of O2 Slovakia), a comprehensive portfolio of fixed and mobile access and ICT services to corporate customers in Slovakia.

Several changes occurred in the O2 Group during the first half of 2016. A new company was incorporated, eKasa s.r.o., which provides solutions for electronic record of sales. As part of the reorganisation of sales and marketing activities in the area of providing services over optical fibre, the Company decided to wind down the business of Internethome, s.r.o. and transfer some of its activities to O2 CZ. For a full overview of changes in the O2 Group please refer to section Events in O2 Group governance in this Half-year Report.

The following table shows a regional breakdown of consolidated revenues (excluding revenues from non-telecommunications services):

in CZK mil.	Half year ended 30 June	
	2016	2015
Czech Republic	15,209	15,351
Slovakia	3,208	3,226
Consolidation adjustments	-194	-184
Consolidated revenues total¹⁾	18,223	18,393

¹⁾ Excluding revenues from other non-telecommunication services

In the first half of the year, O2 Group continued, through its subsidiary Bolt Start Up Development a.s. and its BOLT start-up accelerator, with the identification of viable investment opportunities. In line with its strategy, BOLT focuses on partnering with start-ups which aim to bring innovative ideas, solutions and unique technologies to the market. By investing in them – and not only in financial terms, BOLT fosters the growth of each such company, with the overarching goal to exploit mutual synergies through innovative thinking and ideas and the latest technologies on the one hand, and a contribution to the O2 ecosystem in the form of a strong customer base, large distribution network and big data on the other.

The first such investment project was TapMedia, the developer of Tapito mobile app. Tapito sends a feed of the best of online articles from the Czech internet to the locked small screen of the mobile phone. Another was an investment in Taxify OÜ of Estonia, a player on the European taxi market, including the Czech Republic. Thanks to its partnership with the BOLT accelerator, Taxify benefits from a number of synergies with O2 CZ, especially in big data. The latest to date is the investment in Dateio which is active in precision marketing to clients of banks.

The total number of O2 Group customers was as follows:

in thousands	as at 30 June	
	2016	2015
Fixed voice	760	883
xDSL	782	799
ADSL	314	395
VDSL	468	404
O2 TV (pay TV) ¹⁾	217	190
FIXED ACCESS SEGMENT – CZECH REPUBLIC	1,760	1,872
Contract customers	3,298	3,252
Prepaid customers	1,600	1,693
MOBILE ACCESS SEGMENT – CZECH REPUBLIC	4,898	4,945
Contract customers	1,021	884
Prepaid customers	817	826
MOBILE SEGMENT - SLOVAKIA	1,838	1,711
GROUP CUSTOMERS TOTAL	8,496	8,528

¹⁾ IPTV and OTT

Transformation programme

As stated in the 2015 Annual Report, in 2015 the O2 Group embarked on a comprehensive transformation programme, Simple Online Company. In the first half of 2016, intensive effort was expended on the programme implementation. The next phase of the programme started at the end of April, which focuses on the insourcing of services which had previously been provided to business customers through an external partner company. As a result of this change, O2 CZ controls the whole process – from ordering to delivery to the customer, and thus guarantees a high standard of service.

Insourcing and recruitment of new employees

In order to increase the effectiveness of sales channels, reduce employee turnover and its dependence on external suppliers, O2 CZ decided to insource the staff teams and recruit new employees in selected activity areas. At the same time, by taking this step, O2 CZ responds to the growing demand for specific professions, from the less qualified to highly specialized ones.

Insourcing concerns approximately 600 call centre and back office workers who had been working for O2 through by external agencies as temporary workforce, and now will be made core employees of the Company. This will lead to lower staff turnover and, as a result, to lower recruitment and training costs. Sales production and customer experience will also improve. In the experience of O2 CZ, the motivation of core employees is double that of temporary workers through an agency.

The franchise and brand stores are also undergoing changes. By the end of 2016 O2 CZ plans to convert all franchise-operated stores into its own brand stores. The Company will offer an employment contract to all employees of franchise-operated stores, of whom there are approximately 350. The transformation aims to improve customer experience and the sales at individual stores, improve employee loyalty and reduce their turnover by 50%.

In the IT centre in Pardubice, which O2 CZ inaugurated in November 2015, the Company has plans to employ up to 60 IT specialists, developers and software specialists in the centre, in order to stabilize key development capacity in the Company and reduce its dependence on external suppliers.

As a result of insourcing and recruitment, O2 CZ's headcount increased by 478 employees as at the end of June 2016.

O2 Group total headcount in geographical breakdown was as follows:

	as at 30 June	
	2016	2015
O2 Czech Republic	3,473	2,946
O2 Family	74	86
O2 TV	10	4
O2 IT Services	362	262
Employees in the Czech Republic	3,919	3,298
O2 Slovakia	613	515
O2 Business Services	35	21
Employees in Slovakia	648	536
Group employees total	4,567	3,834

SLOVAKIA

O2 Slovakia

In the first half of 2016, O2 Slovakia recorded a growth in all financial and operating indicators. Detailed information can be found in section Commented financial and operating results of the O2 Czech Republic Group in this Half-year Report.

At the end of last year, O2 Slovakia's proprietary 2G network covered 96.1% of the population in Slovakia, and its 3G network close to 70% of the population. At the end of June 2016, its own 4G network reached 25% of the country's population. In the second half of the year, O2 Slovakia plans to forge ahead with its roll-out of the 4G network in Slovakia and boosting the capacity of its existing 3G network.

At the start of 2016, O2 Slovakia bolstered its leadership in customer care and service quality with its already seventh consecutive victory in the independent "TECHBOX of the year" competition, where readers vote, among other things, for the best Slovak mobile provider in the previous year. In the first half of the year, O2 Slovakia conquered another milestone after it reached the one-million contract customers mark at the beginning of May.

At the beginning of February, O2 Slovakia revamped its bonus scheme for buyers of new handsets by introducing Poukázka na zařízení, a new service which lets customers combine and port any mobile number.

In April, O2 Slovakia unveiled a new data traffic management service Datahit, which allows the customer to roll over their unused data allowance to the next month and automatically buy additional data allowance if the original is used up. The roll-over method is fair in that it ensures that the rolled-over data is used first, and only after the data allowance for the month in question is triggered.

Starting from May 2016, O2 Slovakia started a commercial pilot of national television under the O₂ TV brand, with up to 25 television channels available at this point. The company also introduced its version of home television with a set-top box, which, in the pilot phase, is available in three municipalities in the western part of Slovakia.

O2 Business Services

On 22 December 2015, O2 CZ and O2 Business Services, a.s. (O2 Business Services), which is a wholly-owned subsidiary of O2 Slovakia, signed an agreement on the sale of a part of business of O2 Business Services Slovakia, organizačná zložka O2 Czech Republic, by O2 CZ to O2 Business Services, with effect from 1 January 2016. As of that date, all business of the branch company, including all and any assets and liabilities, employees, etc., has been transferred to O2 Business Services. As of that date, the branch company had no active business, and on 18 May 2016, the Board of Directors of O2 CZ decided to wind it down.

During the first half of the year, O2 Business Services forged ahead with the roll-out of its FWA 3.7 GHz network, to fully cover all regional and district towns. Furthermore, the consolidation of the legacy networks of Business Services and O2 Slovakia continued, with both companies building joint POP aggregation sites. The network was also undergoing redesign (backbone and backhaul).

The product portfolio design was successfully completed, and a new service proposition in all product areas for corporate and government customers started selling. The basic telecommunications services (internet, MPLS and fixed voice) for the corporate segment were completed in terms of their technical, process and commercial development, and duly launched in the market. In collaboration with O2 CZ whose platform it uses, O2 Business Services launched its ICT service proposition. O2 Business Services and O2 Slovakia also unveiled its project to adapt their information systems to support the marketing of mobile voice services to large customers. In collaboration with O2 Slovakia, O2 Business Services prepared a commercial offer of mobile services which it has been actively marketing from the second quarter.

The recruitment of all key operating and sales employees was concluded. The sales team for the corporate segment has been transferred from O2 Slovakia to O2 Business Services, and trained to sell the full O2 Business Services portfolio.

O2 Business Services successfully installed and handed over to customers the first data and voice solutions. A contract was signed with a major government customer, the Slovak Statistical Office, for the delivery of end-to-end voice and data service for the country's elections in the next four years. In the area of ICT, O2 Business Services entered into a contract with the municipal district Staré město Bratislava, for WiFi service covering the whole of Bratislava. In the corporate segment, the company secured a contract for voice and data services from the largest food retail chain.

O2 IT SERVICES

The Professional Services Division which, until the end of 2015, as part of the Company independently designed and developed customer solutions in the field of information and communication technology, was transferred to a subsidiary O2 IT Services s.r.o., with effect from 1 January 2016. As of this date, all activities of the Professional Services Division have been taken over by O2 IT Services s.r.o.

The strategic portfolio of O2 IT Services comprises mainly IT and business consulting, system integration, application development and the development of Managed Services, IT operation and optimisation and IT security. The company provides IT services to the external market and also to other members of the O2 Group. In February, O2 IT Services acquired a part of Corpus Solutions, a software development company. As a result, it boosted its application development and coding capacity and gained new competences.

In the first half of 2016, key areas of dynamic growth were, in particular, the Company's new cybersecurity facility Security Expert Center, technologies collectively labelled as the Internet of things, orchestrated cloud infrastructures and integrated application solutions.

In the first half of 2016, the Company also forged ahead with the implementation of its other major IT projects, for example ISDS (Databox Information System) for the Czech Post, TCTV 112 for the Ministry of Interior, development and maintenance of ISKN (Land Registry Information System) for the State Administration of Land Surveying and Cadastre, various projects at the Ministry of Agriculture, private cloud solution for RWE or IT operation for O2 CZ.

Major new projects or development tasks for existing projects were implemented for clients such as CENIA, Czech Post, State Administration of Land Surveying and Cadastre, Komerční banka, Lesy ČR, Ministry of Transport, Ministry of Defence, Ministry of Interior, Ministry of Agriculture, O2 CZ, Criminal Registry, RWE or the State Agriculture Intervention Fund.

Commented financial and operating results of O2 Czech Republic Group

In this section we present and comment in detail on the unaudited consolidated financial results of O2 Czech Republic a. s. for the first half of 2016 prepared in accordance with International Financial Reporting Standards (IFRS).

Consolidated financial results

Consolidated revenue reached CZK 18,223 m in the first half 2016, down 0.9%. In the second quarter, the rate of the year-on-year decline slowed down as a result of an improvement in the revenue trends in the Czech Republic. The Company's performance has been driven by the slightly higher mobile customers' spend achieved by the Company's focus on customer value, growing volume of mobile data, O₂ TV revenue growth, slower rate of the fixed voice revenue decline and the stability of revenues in Slovakia. The upsides partially compensated for the lower revenue from mobile voice and fixed data services which have been driven down by sustained pressure on the in the corporate segment.

Revenues in the Czech Republic reached CZK 15,209 m, which translates into a 0.9% year-on-year decline (-0.2% in the second quarter). Fixed revenues fell 1.2% year on year down to CZK 5,652 m in the first half of the year (-0.9% in the second quarter alone); 70% growth in O₂ TV revenues and a slower rate of fixed voice revenue decline did not fully compensate for the erosion of data revenues. Mobile revenues were CZK 9,557 m in the first half, which is down 0.6% year on year, while in the second quarter they improved 0.2%. The performance has been impacted mainly by the lower revenues from traditional voice and messaging in the corporate segment, while revenues from residential contracts, and in particular data revenues, continued growing. The rising revenues from the sales of hardware also contributed to the overall improvement in the second quarter.

Revenues in Slovakia reached CZK 3,208 m in the first half 2016, down 0.6% year on year.

Total consolidated expenses were down 2.3% year on year to CZK 13,465 m in the first half 2016; operating expenses declined 3.5% year on year to CZK 4,072 m. In the Czech Republic, operating expenses saw a drop of 5.5% year on year, also due to the positive impact of employee insourcing in call centres, recruitment in IT and reorganisation of the franchise and brand store network, as described in section Overview of the O2 Group and key developments in the first half of 2016. On the other hand, operating expenses in Slovakia increased 4.2% year on year, largely due to investments in the new fixed business. Personnel expenses (including restructuring costs) were up 6% year on year, also in connection with the insourcing and recruitment programme. This growth was more than compensated for by the lower IT & network maintenance expenses (-26.9%) and lower cost of external call centres capacity. As at the same date, the cost of sales was down 1.8% year on year following a trend of lower cost of services, which delivered better revenue quality and lower commercial costs.

Earnings before interest, depreciation and amortization (EBITDA) increased 4.7% year on year to CZK 5,053 m in the first half 2016. The performance has been helped also by a one-off income of CZK 92 m in the first quarter, after the administrative court ruled to terminate the competition law authority's penalty proceedings against the Company. As a result, EBITDA margin reached a solid level of 27.7% in the first half of the year, up 1.5 percentage point year on year.

In connection with the ongoing transformation of IT and systems, O2 CZ identified some of its systems as obsolete and booked a one-off impairment charge of CZK 125 m in relation to these assets. Depreciation and amortization charges went down 6.6% year on year to CZK 1,657 m. Consolidated net income increased by 9.8% year-on-year to CZK 2,552 m in the first half 2016, largely due to growing EBITDA, but also helped by lower depreciation and amortisation.

Consolidated additions to fixed assets (capital expenditures) reached CZK 1,129 m in the first half 2016, up 10.2% year on year. The higher capex was driven largely by investments related to IT transformation (upgrade, consolidation and implementation of IT and systems) to streamline systems and processes. The Company also continued investing in its core network and the acquisition of a modern live broadcasting truck, to boost its capacity to produce television and media content also for partners in the Czech Republic and beyond. In Slovakia, investments were directed into building 3G network capacity, expanding 4G coverage enhancement and upgrading of the billing and CRM systems. As a result, the O2 Group capex to revenue ratio reached 6.2% in the first half 2016.

Consolidated free cash flow¹ reached CZK 2,027 m in the first half 2016. In a year-on-year comparison, the higher cash payments in the first half 2016 for capex which was booked in the second half 2015, and the payment of a guarantee related to participation of the Company in the auction of the 1,800 MHz and 2,600 MHz spectrum, need to be taken into account. The free cash flow in the first half 2015 was, on the other hand, positively impacted by one-off higher working capital with CETIN (CZK ~ 1 bn).

Consolidated financial gross debt amounted to CZK 7,975 m at the end of June 2016. During the first half 2016, the Company drew the second and third tranches, CZK 5 bn in total, of a credit line of up to CZK 12 bn, and cash and cash equivalents reached CZK 3,095 m. As a result, net debt² to EBITDA reached 0.47 as at the end of June 2016.

Results of the mobile segment in the Czech Republic

Through its *FREE* tariffs, the Company continues to focus on its consumer value proposition, aiming to maintain high quality and loyalty of its customer base. In the corporate segment, the Company wants to maintain its leadership through a product and service proposition which addresses the needs of corporate clients, with a commitment to be the innovation leader in the Czech mobile market. At the end of June 2016, the Company's 4G LTE network reached 90% of the population. The LTE service is available in 5,500 Czech villages and in all highways. The Company intends to increase the coverage of broadband internet to 99% by the end of the year, and focus on network densification to improve indoor coverage. In the recent spectrum auction,

¹ Net cash flow from operating activities plus net cash used in investing activities

² Gross debt less cash

the Company secured for its customers four of seven available 1,800 MHz and 2,600 MHz spectrum blocks, for which it paid close to CZK 1.5 bn. The spectrum acquisition will be reflected on the financial results (capex and cash flow) only after the new spectrum is assigned, which is expected to happen in the third quarter 2016. The spectrum investment strengthened the Company's position on the vanguard of mobile broadband internet. The new frequencies will also boost the transmission capacity and, as a result, improve customer experience.

While the revenues from the residential contract base continued growing, corporate segment revenues followed a downward trend due to competitive pressures. The Company's strategy to focus on data revenue growth delivered, however, a positive average revenue per user (ARPU) trend and a 0.9% year-on-year improvement in the first half 2016 combined with a lower churn (down 0.5 percentage point to 1.5%).

The demand for mobile data continued to grow mainly as a result of the Company's improved tariff proposition with more generous data plans and a simple ordering of extra data after the original allowance is used up. The volume of mobile data traffic increased 80% year on year in the first half 2016. In addition to the broader 4G LTE network coverage, the growth has been also driven by the Company's ongoing focus on marketing LTE smartphone. As a result, data revenues³ in the first half 2016 went up 2.5% year on year. Small-screen internet base grew 15.1% year on year to 1,672 thousand customers at the end of June 2016. Smartphone penetration⁴ also grew and reached 51.8% at the end of June 2016, up 8.1 percentage points year on year. LTE smartphones accounted for 24.9% of all handsets in the O2 CZ network (double on the previous year), and for 48% of all smartphones. The number of LTE customers⁵ reached 661 thousand as at 30 June 2016.

The total mobile customer base reached 4,898 thousand at the end of June 2016. The number of contract customers increased 1.4% year on year to 3,298 thousand. In the first half of the year their number went up by 50 thousand. The number of prepaid customers reached 1,600 thousand as at the same date. The ratio of contract customers to total mobile customers was 67.3% at the end of June 2016, up 1.6 p.p. year on year.

The blended monthly average churn rate fell 0.5 percentage point year on year to 1.5% in the first half of 2016. In the same period, the contract churn was only 0.7%, down 0.7 percentage point year on year. The monthly average churn rate in the prepaid segment was 3.2% (3.0% in the second quarter), which is a 0.4 percentage point decline year on year (down 0.8 percentage point in the second quarter).

The total mobile ARPU was CZK 286 in the first half 2016, up 0.9% year on year, as the lower voice and SMS revenues due to competitive pressure have been compensated by improved quality of the customer base and higher data spend. The contract ARPU declined 0.6% year on year to CZK 370, while the prepaid ARPU fell 1.2% year on year to CZK 117 in the first half 2016 overall, but improved by 0.6% to CZK 121 in the second quarter alone.

Revenues from mobile operations in the Czech Republic were CZK 9,557 m for the first half 2016, which is a drop of 0.6% year on year. In the second quarter alone, operating revenues improved by 0.2%. Revenues from mobile services eroded by 1.1% to CZK 8,748 m. Competitive pressures in the corporate segment caused voice and messaging revenues to go down, which was the main factor in the trend. The higher residential spend, on the other hand, has given a boost to data revenues. Mobile-originated voice revenues fell 7.2% year on year to CZK 4,366 m in the first half 2016, while messaging (SMS & MMS) revenues were 14.9% lower due to the lower effective per-unit price and the lower number of SMS sent. Data revenues increased 12.5% year on year to CZK 2,352 m. Revenues from termination (interconnection) went up 2.3% year on year to CZK 1,132 m, mainly as a result of higher incoming voice and SMS traffic. Revenues from hardware sales were up 7.6% to CZK 705 m.

Results of the fixed segment in the Czech Republic

In the fixed business, the Company recorded a solid operating and financial performance as a result of new service proposition in the O₂ TV and fixed voice segments. Migration of all customers to the new O₂ TV tariffs introduced in July 2015 is having a positive effect on the customer base and revenues.

The Company continues investing in the acquisition of exclusive sports content. A brand new O₂ TV Football channel will go live in August, to be followed by O₂ TV Tennis and O₂ TV Hockey in 2017. The OTT version (O₂ TV Air M) of the service was enjoying a surge in popularity. The service is available to all households in the Czech Republic regardless of their internet provider and it is sold in retail and e-tail channels. In the second quarter, the Company promoted the service with a free two-month Try and Keep trial.

In fixed voice, the Company has been marketing a new tariff with unlimited calls to all networks in the Czech Republic. At the end of June, a vast majority of households enjoy the tariff. The popularity of this proposition is manifested in the fact that customers on new tariff call 40% more.

³ Excluding SMS and MMSS

⁴ Smartphones as % of total handsets base

⁵ Customer with LTE smartphone and LTE USIM

The total number of fixed voice accesses saw a 14 % year-on-year decline, down to 760 thousand as at the end of March 2016. The migration of customers to the new unlimited tariff has led to a year-on-year average revenue per line improvement of 35%.

The number of xDSL accesses reached 782 thousand at the end of June 2016. The share of fast VDSL accesses kept growing to 60%, with already 468 thousand customers using the technology (up 16.1 % year on year). In the first half 2016, the Company boosted the speed of fixed internet in over 70 thousand homes.

The number of active O₂ TV customers reached 217 thousand (IPTV and OTT), up 14.4% year on year. The figure includes also customers who signed up for the free trial and chose not to opt-out. Those, who at the end of June enjoyed the free two-months Try and Keep trial, could return the set-top box (opt-out) or subscribe to one of the paid tariffs by the end of August. As a result, the full effect of this promotion on the customer base of O₂ TV will be seen in the third-quarter financial results. The add-on service MULTI which lets viewers watch television on more than one TV set at a time also proved very popular, with more than 30 thousand customers signing up for it. O₂ CZ now records close to 250 thousand active set-top boxes. Unique features (playback, record, etc.), and also the proprietary O₂ Sport channel with multidimension are proving to be the demand drivers in the area of digital television.

Customers also like to watch O₂ TV on the web and in the mobile application, or in pubs of the Staropramen chain. The number of people who actively watch O₂ TV online and on the small screen increased two and half times year on year, with close to 300 thousand mobile and online viewers in June.

Total fixed operating revenue reached CZK 5,652 m in the first half 2016, down 1.5% year on year, while in the second quarter alone, the rate of decline slowed down to 0.9% and CZK 2,823 m. The higher revenues from O₂ TV and ICT could not fully offset the fall in voice and data revenues. The rate of decline in voice revenues slowed down further as a result of the vast majority of customers migrated to the new higher-value unlimited tariffs. In the first half 2016, voice revenues fell 6.9% year on year to CZK 1,393 m, while in second quarter alone, the negative trend slowed down considerably and the revenues were 704 m, which is only a drop of 4% year on year. Internet & broadband revenues (including O₂ TV) were up 3.2% year on year to CZK 2,543 m in the first half 2016. The 70.3% upside in O₂ TV revenues was the key driver of this growth. ICT revenues were up 2.3% year on year to CZK 832 m in the first half 2016.

Results in Slovakia

In the first half of 2016, the O2 Slovakia group⁶ reported a growth in its customer base and improvement in its overall financial performance, despite fierce competition in the Slovak market. The group has made a positive contribution to the O2 Group's financial results, with 18% to the consolidated revenues and 22% to the consolidated EBITDA. In addition to its mobile business, the group is also developing and implementing a fixed access proposition with a focus on the corporate segment.

The total number of mobile customers reached 1,838 thousand as at the end of June 2016, which is a 7.4% year-on-year growth. The customer base increased by 29 thousand in the first half, of which 17 thousand were second-quarter additions. The trend has been driven largely by contract additions. The number of contract customers grew 15.5% year on year to 1,021 thousand as at the end of June 2016, while the number of prepaid customers dropped slightly by 1.2% year on year to 817 thousand. Overall, the customer blend quality keeps improving and the ratio of contract customers to total base in Slovakia was 55.6% as at the end of June 2016, up 3.9 percentage points year on year. O2 Slovakia saw a steady demand for its smartphone proposition, which in turn drove the growth in smartphone penetration, which reached 53.0% as at the end of June 2016, up 6.1 percentage points year on year. The number of mobile internet customers went up 13.0% year on year to almost 800 thousand. As a result, mobile data revenues grew 19% year on year.

During the first half of 2016, O2 Business Services completed the rollout of its wireless 3.7 GHz (FWA) access network, which presently covers all regional and district towns in Slovakia. The company successfully completed the development of its product portfolio and service proposition for the corporate and government segment. Standard telecommunication services (internet, MPLS and fixed voice) and ICT solutions for the corporate segment services were launched in the market.

In terms of financial performance, the total operating revenues in Slovakia stayed relatively flat year on year at CZK 3,208 m, with a contribution from the growing customer based, improved customer mix, revamped handset portfolio and the related stronger revenues from hardware sales, and improved data revenues. EBITDA in Slovakia was flat year on year at CZK 1,058 m, which translates into a 34.7% EBITDA margin in the first half 2016.

The total mobile ARPU in Slovakia in the first half 2016 reached CZK 249.2 (EUR 9.2), with the contract ARPU at CZK 336.5 (EUR 12.5) and the prepaid ARPU at CZK 152.2 (EUR 5.6).

⁶ Including O2 Business Services and Tesco Mobile Slovakia

Outlook for the second half of 2016

In the second half of 2016, the Company's management expects that the revenue performance will be similar to the one seen in the first half of the year. In the fixed segment, the customers will migrate to the unlimited tariff, which will help to further slow the revenue decline down. The growth focus will stay on O₂ TV. The negative impact of roaming regulation will be reflected in the mobile segment revenues (mainly in the third quarter); this could, however, be compensated with higher volumes of voice and data roaming traffic. The competition is likely to remain fierce, mainly in the corporate segment. The positive dynamics spurred by greater LTE penetration in the customer base, upsell to higher tariffs and higher revenues from the sale of hardware and accessories could eliminate the market downside. In Slovakia, the O2 Group will focus mainly on bringing out the fast 4G LTE network to more population, in order to accelerate data revenue growth and offset the negative impact of roaming regulation.

In terms of capex, the O2 Group will, in addition to the abovementioned 4G LTE network rollout in Slovakia, pursue further acquisitions of exclusive sports content for its customers. Capex related to the acquisition of the 1,800 MHz and 2,600 MHz spectrum will be booked in the full amount (CZK 1,472,050,000) in the third quarter following the settlement of the total price, return of the guarantee (CZK 450 m) and spectrum assignment by the CTO. The ongoing IT transformation, mainly in the postpaid billing and CRM areas, will also reflect on the capex in the second half of the year.



Events in corporate governance of the Group

All changes in the corporate governance of the Company in the first half of the year were connected with the declaration of the O2 Czech Republic concern and the spin-off of parts of enterprise on the part of O2 CZ and some of its subsidiaries.

From 1 April 2016, the Company has been managing its controlled entities as a concern pursuant to the provisions of Section 79(3) of the Act No. 90/2012 Coll., the Business Corporations Act¹. The O2 Czech Republic concern comprises most of its subsidiaries². The concern is led by O2 Czech Republic a.s. in the capacity of the managing entity. The main reason is the single management to ensure a long-term promotion of the concern's interests under the concern's single policy. The control is exercised through coordination and conceptual management of the concern's business activities.

As of 1 January 2016, the Professional Services Division was transferred as a part of an enterprise from O2 CZ into the subsidiary O2 IT Services s.r.o. As of the same date and based on a sale and purchase agreement, a part of an enterprise, which comprised the branch office O2 Business Services Slovakia, to O2 Business Services, a.s., which is a subsidiary of O2 Slovakia, a.s. (see also section Business overview of this Half-year Report). On 18 May 2016, the Board of Directors of O2 CZ decided to wind down the division (see also section Business overview of this Half-year Report). With effect of 3 February 2016, O2 IT Services s.r.o. acquired a part of the enterprise of Corpus Solutions a.s., a software development company. On 16 March 2016, the statutory executives of Internethome, s.r.o. decided to wind down the business, and, with effect from 1 June 2016, a part of the enterprise which provides public telecommunications over optical network technology, was sold to the parent company O2 Czech Republic a.s. On 17 May 2016, eKasa s.r.o. was incorporated as a subsidiary to provide services in the area of electronic record of sales. The subsidiary Bolt Start Up Development a.s., which operates BOLT, a start-up accelerator, acquired an equity interest in Dateio s.r.o. (21.4%) and in Taxify OÜ (1.96%) of Estonia.

General Meeting of O2 CZ – 19 April 2016

- Approved the regular financial statements and consolidated financial statements for the year 2015 as prepared under the International Financial Reporting Standards. The statutory auditor KPMG Česká republika Audit, s.r.o. gave an unqualified opinion.
- Approved the distribution of unconsolidated profit for the year 2015 and a part of unconsolidated retained earnings, in the total amount of CZK 4,964 m, as dividends. A dividend of CZK 16 or CZK 160 before tax was paid per each share in the nominal value of CZK 10 and CZK 100, respectively. The record day for the payment of dividends was 19 April 2016. The disbursement day was 19 May 2016.
- Approved an amendment to the Articles of Association. The changes included namely the extension of the scope of O2 CZ's business, to prepare the Company for future entry on the insurance brokerage market, and to let it continue as provider or broker of consumer credit finance. Other changes had been necessitated by amendments to some accounting and audit laws.
- Appointed KPMG Česká republika Audit, s.r.o. as its statutory auditor for the year 2016.

The full list of all resolutions of the General Meeting can be found on the Company website (<http://www.o2.cz/spolecnost/en/general-meetings>).

Board of Directors of O2 CZ

In the first half of the year, the Board of Directors had 17 meetings. No changes were made in the personnel composition of the Board of Directors in the first half of 2016.

Supervisory Board of O2 CZ

In the first half of the year, the Supervisory Board had two meetings. No changes were made in the personnel composition of the Supervisory Board in the first half of 2016.

¹ With respect to O2 IT Services, concern management has been applied since 22 December 2015.

² The full list of companies in the O2 Czech Republic concern can be found on the Company website (http://www.o2.cz/spolecnost/en/376775-skupina_o2_cr_a_ostatni_ucasti/)

Audit Committee of O2 CZ

In the first half of the year, the Audit Committee had two meetings. No changes were made in the personnel composition of the Audit Committee in the first half of 2016. Internal Audit and Risk Management, as the Company's internal unit, was organisationally subordinated to the Audit Committee, as required by the amendment to the Act No. 93/2009 Coll., on auditors.

Other persons with controlling power

With effect from May 2016, Kateřina Pospíšilová was appointed Director for Strategy and Innovation. She is responsible for strategy, innovation, regulation and competition law.



Financial part

O2 Czech Republic a.s.

**INTERIM CONSOLIDATED FINANCIAL STATEMENTS
FOR THE SIX MONTHS ENDED 30 JUNE 2016**

**PREPARED IN ACCORDANCE WITH INTERNATIONAL
FINANCIAL REPORTING STANDARD IAS 34 INTERIM FINANCIAL
REPORTING**

Translation note

This version of the interim consolidated financial statements is a translation from the original, which was prepared in the Czech language. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the Czech version of the interim consolidated financial statements takes precedence over this translation.

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GENERAL INFORMATION

O2 Czech Republic Group (the "Group") consists of O2 Czech Republic a.s. (the "Company") and its subsidiaries: O2 Slovakia, s.r.o., O2 Family, s.r.o., Internethome, s.r.o., O2 TV s.r.o., O2 IT Services s.r.o., Bolt Start Up Development a.s., eKasa s.r.o. and O2 Business Services, a.s. (subsidiary of O2 Slovakia, s.r.o.). The Group operates a joint venture Tesco Mobile ČR s.r.o. with Tesco Stores ČR a.s. and has a branch O2 Business Services Slovakia, organizačná zložka O2 Czech Republic a.s., in the Slovak Republic.

The Company has a form of a joint stock company and is incorporated and domiciled in the Czech Republic. The address of its registered office is Za Brumlovkou 266/2, Prague 4, 140 22, Czech Republic.

The majority shareholder of the Company as at 30 June 2016 is PPF Telco B.V. („PPF“).

These interim consolidated financial statements are not audited.

Main events in the first half of 2016

Share buyback

In accordance with the decision of General Meeting from 8 December 2015 concerning acquisition of treasury shares (up to 10% for 5 following years), the Company implemented the share buyback programme in the first half of 2016. As at 30 June 2016 the Company held 2,199,220 treasury shares with the total purchase price of CZK 527 million.

Changes in subsidiaries and other financial investments

During the six months ended 30 June 2016 the Company established a new subsidiary eKasa s.r.o., which provides solutions for electronic records of sales. eKasa is incorporated in the Czech Republic and had no commercial activity in the period ended 30 June 2016.

Startup accelerator Bolt, subsidiary Bolt Start Up Development a.s., that promotes unique technology projects continued to be active in the first half of 2016. It has newly established a cooperation with Estonian company Taxify OÜ operating on European (including Czech) taxi market as well as with Dateio, s.r.o., a Czech company specializing in targeted marketing. Bolt acquired an equity stake in both companies.

A non-monetary contribution of Professional Services Division into O2 IT Services s.r.o., approved by Company's General Meeting on 8 December 2015, entered into effect on 1 January 2016. This transaction has no impact on consolidated financial statements of the Group.

Demerger of parent company PPF Arena 2 B.V.

The demerger of parent company PPF Arena 2 B.V. came into effect on 23 January 2016. As a result of the demerger, PPF Arena 2 B.V. ceased to exist and new successors PPF Telco B.V. and PPF Infrastructure B.V. emerged. All shares of the Company were transferred to PPF Telco B.V. PPF Group owns 100% of PPF Telco B.V.

Insourcing and recruitment of new employees

In order to increase effectiveness of sales channels, to diminish labor turnover and mitigate dependence on external suppliers the Company decided to insource and hire new employees in selected operational areas during the year. The decision was also the Company's response to increasing demand for some professions ranging from less qualified to specialized workforce.

Insourcing mainly targets approximately 600 employees in call centers and back office formerly staffed on temporary basis by external agencies, which will now join the Company's in-house staff. The insourcing will reduce labour turnover and decrease recruitment and training costs. Insourcing will also stimulate higher sales performance and provide better customer experience. Based on the Company's experience, in-house staff tends to be twice as much motivated as temporary agency staff.

Further changes are planned for franchise and own brand stores. By the end of the year, the Company plans to operate only its own brand stores. New brands stores will be staffed with approx. 350 employees with a standard work contract with the Company. Main goal is to augment customer experience, increase stores performance, employees' loyalty and decrease labour turnover by up to 50%.

The Company also plans to employ up to 60 IT specialists, developers and software specialists in its IT center in town of Pardubice, which opened in November 2015. This will enable the Company to obtain and retain key development competencies within the organization and reduce dependance on external suppliers.

By the end of June 2016 the Company employed total of 478 new employees as a result of these efforts.

O2 Czech Republic concern

With effect from 1 April 2016 the Company established in accordance with the Art. 79 Sec. 3 of the Business Corporations Act the O2 Czech Republic concern, in which the Company is a controlling enterprise.

Auction of frequencies 1 800 and 2 600 MHz

The Company has bought at auction four strategically important blocks of radio frequencies in the 1 800 and 2 600 MHz bands in June 2016. The Company has reached the most favourable conditions for future development of mobile internet 4G LTE to its current capacities. In addition the Company wants to utilise acquired blocks for the preparation of next generation network 5G and for the strengthening of capacity. Overall financial volume from closed auction has reached the amount of almost CZK 1,500 million.

INTERIM CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

For the six months ended 30 June 2016

In CZK million

	Notes	For the six months ended 30 June 2016	For the six months ended 30 June 2015
Revenues	1	18,223	18,393
Other income from non-telecommunication services and activation of fixed assets		295	213
Expenses		(13,465)	(13,781)
Earnings before interest, taxes, depreciation and amortization (EBITDA)	1	5,053	4,825
Depreciation and amortisation		(1,657)	(1,775)
Impairment loss		(116)	(2)
Operating profit	1	3,280	3,048
Finance income		18	7
Finance costs		(58)	(108)
Results attributed to joint venture		(5)	(4)
Profit before tax	1	3,235	2,943
Corporate income tax	1, 3	(683)	(618)
Profit for the period from continuing operations	1	2,552	2,325
Profit from discontinued operations	2	-	1,722
Profit for the period		2,552	4,047
Other comprehensive income			
Items that may be reclassified subsequently to profit or loss			
Translation differences		14	(68)
Other comprehensive income, net of tax		14	(68)
Total comprehensive income, net of tax		2,566	3,979
Profit attributable to:			
Equity holders of the Company		2,552	2,325
Equity holders of CETIN (from discontinued operations)		-	1,722
Total comprehensive income attributable to:			
Equity holders of the Company		2,566	2,257
Equity holders of CETIN (from discontinued operations)		-	1,722
Earnings per share for continuing operations (CZK) - basic*	4	8	8

* There is no dilution of earnings as no convertible instruments have been issued by the Company.

INTERIM CONSOLIDATED BALANCE SHEET

As at 30 June 2016

In CZK million	Notes	30 June 2016	31 December 2015
ASSETS			
Property, plant and equipment		4,582	4,638
Intangible assets		15,568	16,147
Investments in equity accounted investees	14	67	42
Other non-current assets		189	270
Deferred tax asset		267	323
Non-current assets		20,673	21,420
Inventories		552	722
Receivables		6,616	6,156
Current tax receivable		29	-
Cash and cash equivalents	7	3,095	1,970
Current assets		10,292	8,848
Total assets		30,965	30,268
EQUITY AND LIABILITIES			
Ordinary shares		3,102	3,102
Treasury shares		(527)	-
Share premium		11,894	11,894
Retained earnings, funds and reserves		968	3,348
Total equity		15,437	18,344
Long-term borrowings	9	7,975	2,970
Deferred tax liability		53	60
Non-current provisions for liabilities and charges		25	22
Non-current other liabilities		171	94
Non-current liabilities		8,224	3,146
Short-term borrowings		-	11
Trade and other payables		7,060	8,391
Income tax liability		37	245
Provisions for liabilities and charges		207	131
Current liabilities		7,304	8,778
Total liabilities		15,528	11,924
Total equity and liabilities		30,965	30,268

INTERIM CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the six months ended 30 June 2016

In CZK million	Notes	Share capital	Share premium	Treasury shares	Currency translation reserve	Funds	Retained Earnings	Total
At 1 January 2016		3,102	11,894	-	198	191	2,959	18,344
Currency translation differences – amount arising in period		-	-	-	14	-	-	14
Profit for the year	1	-	-	-	-	-	2,552	2,552
Total comprehensive income		-	-	-	14	-	2,552	2,566
Capital contribution and other reclassifications		-	-	-	-	59	(59)	-
Acquisition of treasury shares		-	-	(527)	-	-	-	(527)
Distribution declared in 2016	4	-	-	-	-	-	(4,964)	(4,964)
Dividend on treasury shares		-	-	-	-	-	18	18
At 30 June 2016		3,102	11,894	(527)	212	250	506	15,437

In CZK million	Note	Share capital	Share premium	Treasury shares	Currency translation reserve	Funds	Retained Earnings	Total
At 1 January 2015		27,461	19,349	(1,596)	296	6,587	2,056	54,153
Currency translation differences – amount arising in period		-	-	-	(68)	-	-	(68)
Profit for the period	1	-	-	-	-	-	2,325	2,325
Net profit attributable to shareholders of CETIN (from Discontinued Operations)		-	-	-	-	-	1,722	1,722
Total comprehensive income		-	-	-	(68)	-	4,047	3,979
Capital contribution and other reclassifications		-	-	-	-	45	(45)	-
Distribution declared in 2015	4	-	-	-	-	-	(4,103)	(4,103)
Treasury shares operations		-	-	-	-	-	71	71
Cancellation of treasury shares		(472)	(1,124)	1,596	-	-	-	-
Acquisition of O2 IT Services, s.r.o.		-	-	-	-	(79)	-	(79)
Distribution of profit and other distribution to CETIN shareholders relating to spin off project	2	(23,887)	(6,331)	-	-	(6,322)	(1,722)	(38,262)
At 30 June 2015		3,102	11,894	-	228	231	304	15,759

INTERIM CONSOLIDATED STATEMENT OF CASH FLOWS

For the six months ended 30 June 2016

Notes

For the six
months ended
30 June 2016

For the six
months ended
30 June 2015

In CZK million

Profit after tax		2,552	4,047
Non-cash adjustments for:			
Income tax		683	1,072
Results attributed to Joint Venture		5	4
Dividend income		(4)	(4)
Depreciation		488	1,521
Amortisation		1,169	1,299
Impairment loss		116	2
Profit (-)/ loss (+) on sale of property, plant and equipment		5	(14)
Net interest and other income (charges)		23	42
Foreign exchange losses (+)/gains (-) (net)		5	(1)
Fair value changes		3	-
Change in provisions and allowances		79	217
Other non-cash operations		-	67
Operating cash flow before working capital changes		5,124	8,252
Working capital adjustments:			
Increase (-)/decrease (+) in trade and other receivables		92	(657)
Increase (-)/decrease (+) in inventories		169	(80)
Increase (+)/decrease (-) in trade and other payables		(430)	602
Cash flows from operating activities		4,955	8,117
Interest paid		(32)	(45)
Interest received		-	4
Income tax paid		(870)	(831)
Net cash flow from operating activities		4,053	7,245
Cash flows from investing activities			
Purchase of property, plant and equipment		(635)	(978)
Purchase of intangible assets		(1,357)	(599)
Proceeds from sales of property, plant and equipment and intangible assets		6	1
Cash purchase of equity accounted investments		(10)	(65)
Cash purchase of other investments		(16)	-
Dividends received		4	4
Payment of security deposit to Czech Telecommunication Office		(450)	-
Release of restricted cash		432	-
Net cash used in investing activities		(2,026)	(1,637)
Cash flows from financing activities			
Proceeds (+) / repayments (-) of borrowings	9	5,000	630
Acquisition of treasury shares		(527)	-
Dividends paid		(4,946)	(3,927)
Distribution of CETIN's cash	2	-	(1,970)
Net cash used in financing activities		(473)	(5,267)
Net increase/(decrease) in cash and cash equivalents		1,554	341
Cash and cash equivalents at beginning of year	7	1,538	3,256
Effect of foreign exchange rate movements on cash and cash equivalents		3	(1)
Cash and cash equivalents at the year end	7	3,095	3,596

Accounting policies

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A Basis of preparation

The interim consolidated financial statements were prepared in accordance with International Accounting Standard IAS 34 Interim Financial Reporting (“IAS 34”).

The interim consolidated financial statements do not include all the information and disclosures required in the annual financial statements, and should be read in conjunction with the Group’s annual consolidated financial statements as at 31 December 2015.

The amounts shown in these consolidated financial statements are presented in millions of Czech crowns (“CZK”), if not stated otherwise.

B Significant accounting policies

The accounting policies adopted in the preparation of the interim consolidated financial statements are consistent with those followed in the preparation of the consolidated annual financial statements for the year ended 31 December 2015.

C Change in accounting policy

No significant changes in accounting policies were applied in the period ended 30 June 2016.

D Seasonality of operations

There is no seasonal nature either in fixed line segment or mobile telecommunication segment. Telecommunication business of the Group is not regarded as seasonal.

E Treasury shares

Treasury shares are presented in the balance sheet as a deduction from equity. The acquisition of treasury shares is presented in the statement of changes in equity as a reduction in equity. No gain or loss is recognized in the income statement on the sale, issuance, or cancellation of treasury shares. Consideration received from sale of treasury shares is presented in the financial statements as an addition to equity.

Condensed notes to the interim consolidated financial statements

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1 Segment information

Segments recognised by the Group are as follows:

- Czech Republic:
 - fixed segment – telecommunication and data services using fixed network and WiFi infrastructure, ICT services provided by the Company and other subsidiaries in the Group excluding O2 Family, s.r.o.
 - mobile segment – mobile telecommunication and data services provided by the Company and O2 Family, s.r.o.
- Discontinued operations – separately reported segment in 2015 relating to CETIN (spun off entity), which provides wholesale services using its own fixed and mobile infrastructure and wholesale services provided by CZECH TELECOM Germany GmbH and CZECH TELECOM Austria GmbH
- Slovak Republic - mobile telecommunication and data services provided by O2 Slovakia, s.r.o and O2 Business Services, a.s.

The operating results of all segments are regularly controlled and reviewed by the chief operating decision maker who holds the power to make decisions about resource allocation to the segment and to assess its performance.

Inter-segment pricing rates in 2016 and 2015 were determined on the same basis as rates used for other mobile operators.

For the six months ended 30 June 2016	Czech Republic	Slovak Republic	Elimination CR vs SR	Group
In CZK million				
	Fix	Mobile		
Revenues	5,652	9,557		
Cost of Sales (CoS)	(3,531)	(4,602)		
Gross margin	2,121	4,955		
Other income from non-telecommunication services and activation of fixed assets	264			
Other costs excluding (CoS)	(3,344)			
Earnings before interest, taxes, depreciation and amortization (EBITDA)	3,995			
Revenues	15,209	3,208	(194)	18,223
Other income from non-telecommunication services and activation of fixed assets	264	27	4	295
Total consolidated income	15,473	3,235	(190)	18,518
Total consolidated costs	(11,478)	(2,177)	190	(13,465)
Earnings before interest, taxes, depreciation and amortization (EBITDA)	3,995	1,058	-	5,053
Depreciation and amortization	(1,318)	(339)	-	(1,657)
Impairment loss	(116)	-	-	(116)
Operating profit	2,561	719	-	3,280
Interest expense	(36)	-	-	(36)
Interest income	13	-	-	13
Other financial income/(expense)	(14)	(3)	-	(17)
Net financial loss	(37)	(3)	-	(40)
Results attributed to joint venture	(5)	-	-	(5)
Profit before tax	2,519	716	-	3,235
Corporate income tax	(488)	(195)	-	(683)
Profit for the period	2,031	521	-	2,552
Assets (excl. Goodwill)	27,672	5,246	(6,409)	26,509
Goodwill	4,456	-	-	4,456
Total Assets	32,128	5,246	(6,409)	30,965
Trade and other payables	(5,703)	(1,636)	279	(7,060)
Other liabilities	(8,447)	(36)	15	(8,468)
Total liabilities	(14,150)	(1,672)	294	(15,528)
Fixed assets additions	892	247	(10)	1,129

For the six months ended 30 June 2015	Czech Republic	Slovak Republic	Elimination CR vs SR	Discontinued Operations	Elimination Continuing vs Discontinued operations *	Group
In CZK million						
	Fix	Mobile				
Revenues	5,738	9,613				
Cost of Sales (CoS)	(3,515)	(4,754)				
Gross margin	2,223	4,859				
Other income from non-telecommunication services and activation of fixed assets	198					
Other costs excluding (CoS)	(3,529)					
Earnings before interest, taxes, depreciation and amortization (EBITDA)	3,751					
Revenues	15,351	3,226	(184)	7,960	(4,558)	21,795
Other income from non-telecommunication services and activation of fixed assets	198	15	-	193	-	406
Total consolidated income	15,549	3,241	(184)	8,153	(4,558)	22,201
Total consolidated costs	(11,798)	(2,167)	184	(4,930)	4,558	(14,153)
Earnings before interest, taxes, depreciation and amortization (EBITDA)	3,751	1,074	-	3,223	-	8,048
Depreciation and amortization	(1,446)	(329)	-	(1,045)	-	(2,820)
Impairment loss	(2)	-	-	-	-	(2)
Operating profit	2,303	745	-	2,178	-	5,226
Interest expense	2	-	-	-	-	2
Interest income	(45)	-	-	-	-	(45)
Other financial income/(expense)	(52)	(6)	-	(2)	-	(60)
Net financial loss	(95)	(6)	-	(2)	-	(103)
Results attributed to joint venture	(4)	-	-	-	-	(4)
Profit before tax	2,204	739	-	2,176	-	5,119
Corporate income tax	(431)	(187)	-	(454)	-	(1,072)
Profit for the period	1,773	552	-	1,722	-	4,047
Assets (excl. Goodwill)	21,922	5,048	-	-	-	26,970
Goodwill	4,443	-	-	-	-	4,443
Total Assets	26,365	5,048	-	-	-	31,413
Trade and other payables	(6,040)	(1,404)	-	-	-	(7,444)
Other liabilities	(8,037)	(173)	-	-	-	(8,210)
Total liabilities	(14,077)	(1,577)	-	-	-	(15,654)
Fixed assets additions	835	193	-	807	-	1,835

* column Elimination Continuing vs Discontinued operations represents amount of purchases and sales of the Company from new business relations with the spun off part CETIN (Discontinued operations) from the period January to May 2015 (further comments in Note 2)

2 Discontinued operation

On 28 April 2015, the General Meeting of the Company approved a separation project of the Company through a spin off with a formation of a new company Česká telekomunikační infrastruktura a.s. (CETIN). The decisive date of the separation was 1 January 2015, in accordance with the national legislation. From the perspective of the International Financial Reporting Standards the date when the Company cease the control over the spun off part CETIN was 1 June 2015. Under IFRS 5, financial indicators relating to company CETIN for the period from January to May 2015, or as of 31 May 2015 respectively, are classified in the interim consolidated financial statements for the six months ended 30 June 2015 as Discontinued operations.

3 Income tax

In CZK million	For the six months ended 30 June 2016	For the six months ended 30 June 2015
Total income tax expense consists of:		
Current income tax charge	634	629
Deferred income tax charge (+)/credit (-)	49	(11)
Income tax	683	618

Deferred income taxes are calculated using currently enacted tax rates, 19% in the Czech Republic (2015: 19%) and 22% in Slovakia (2015: 22%).

4 Dividends, other distribution and earnings per share

In CZK million	For the six months ended 30 June 2016	For the six months ended 30 June 2015
Dividends declared (including withholding tax)	4,964	4,103

Dividends include a withholding tax on dividends paid by the Company to its shareholders. There has been no interim dividend paid in respect of 2016 and 2015. The approval of the 2015 profit and its distribution as a dividend for this financial year was agreed at the Annual General Meeting on 19 April 2016 (2014: 28 April 2015). Pursuant to the decision of the Annual General Meeting, the dividend in the amount of CZK 16 per share from the 2015 profit were payable on 19 May 2016 (2013: CZK 13).

Basic earnings per share are calculated by dividing the net profit attributable to shareholders by the weighted average number of ordinary shares in issue during the period. The weighted average number of shares takes into account the weighted average effect of changes in treasury shares during the year.

Continuing operations

	For the six months ended 30 June 2016	For the six months ended 30 June 2015
Weighted number of ordinary shares outstanding (thousands)	309,189	310,220
Net profit attributable to shareholders (in CZK million)	2,552	2,325
Basic earnings per share (CZK)	8	8

Discontinued operations

	For the six months ended 30 June 2016	For the six months ended 30 June 2015
Weighted number of ordinary shares outstanding (thousands)	309,189	310,220
Net profit attributable to shareholders (in CZK million)	-	1,722
Basic earnings per share (CZK)	-	6

5 Property plant and equipment

During the six months ended 30 June 2016, the Group acquired assets at a cost of CZK 433 million (as at 30 June 2015: CZK 401 million). Assets with a net book value of CZK 85 million were disposed of by the Group during the six months ended 30 June 2016 (as at 30 June 2015: CZK 29 million).

6 Intangible assets

During the six months ended 30 June 2016, the Group acquired intangible assets at a cost of CZK 696 million (as at 30 June 2015: CZK 627 million). Assets with a net book value of CZK 29 million were disposed of by the Group during the six months ended 30 June 2016 (as at 30 June 2015: CZK 0 million).

During the six months ended 30 June 2016 the Group recognized impairment loss of CZK 116 million (as at 30 June 2015: CZK 2 million). Impairment loss mostly represents value of intangible assets, which were made redundant due to ongoing IT system transformation.

7 Cash and cash equivalents

In CZK million	30 June 2016	31 December 2015
Cash at current bank accounts and other cash equivalents	1,643	1,185
Cash at current bank accounts and other cash equivalents with related parties (Note 13)	1,452	785
Total cash and cash equivalents	3,095	1,970
- of which restricted cash	-	(432)
Cash and cash equivalents included in cash flow statement	3,095	1,538

Cash deposited on an escrow account held on behalf of the Company (restricted cash) as at 31 December 2015 was released to Czech Telecommunication Office (CTO) on 1 February 2016 in accordance with the concluded agreement.

The committed and undrawn facilities available to the Group amounted to CZK 4,662 million as at 30 June 2016 (as at 31 December 2015: CZK 9,662 million).

As at 30 June 2016 and 31 December 2015 no cash and cash equivalents were pledged.

8 Inventories

As at 30 June 2016 the inventories are stated net of an allowance of CZK 92 million (as at 31 December 2015: CZK 95 million), reducing the value of the inventories to their net realisable value.

9 Borrowings

On 16 December 2015 the Company entered into a long-term facility agreement with maturity in 5 years and credit limit of CZK 12 billion. The interest rate is based on PRIBOR increased by 0.60% margin. The loan is used to refinance former debt and for general corporate purposes. The debt is not secured by any assets owned by the Group.

In line with the facility agreement, the Company made following drawings in the six months ended 30 June 2016: (i) amount of CZK 4 billion drawn on 20 January 2016 and (ii) amount of CZK 1 billion drawn on 18 April 2016. As at 30 June 2016 the Company used total of CZK 8 billion of the available credit (as at 31 December 2015: CZK 3 billion).

10 Restructuring costs

During the six months period ended 30 June 2016 the Group recognised restructuring costs of CZK 49 million (as at 30 June 2015: CZK 161 million).

11 Contingencies and litigations

The Company is involved in a number of legal disputes arising from standard business interactions. Developments which occurred throughout the first half of the year 2016 are described below.

I. The Office for the Protection of Economic Competition - proceedings on the fine CZK 91.9 million

The Supreme Administrative Court rejected the cassation complaint filed by the Office for Protection of Economic Competition, which definitively confirmed that the Company cannot be forced to return the penalty to the Office and the Office cannot even impose the penalty again. In accordance with the decision the Company recognised the returned penalty in Other

income from non/telecommunication services and activation of fixed assets in the period ended 30 June 2016.

II. Disputes with the company AUGUSTUS spol. s r.o.

The Constitutional Court rejected the constitutional complaint filed by the company AUGUSTUS spol. s r.o. (AUGUSTUS), which tried to reverse final decision in the dispute against the Company, which had been running since 1996 and which the Company finally succeeded. The proceeding is closed and will not be reported within the significant potential liabilities of the Company.

There are currently ongoing actions and proceedings against AUGUSTUS and its director in order to claim unjustified enrichment and recovery of damages. Decision on partial distribution of the yield from bankruptcy issued by the Municipal Court in Prague on 13 October 2015 was confirmed by the High Court in Prague. Following this, the claim of the Company was partially satisfied in the extent of CZK 32 million.

III. VOLNÝ, a.s. – legal action on CZK 4 billion

Another hearing in this case was held on 6 May 2016, during which the Court reviewed the possibility of appointing an expert to reassess expert opinions filed by both, the Company and Volný, a.s. The Company filed objections against the expert proposed by Volný, a.s. on the grounds that the expert is prejudiced in relation to the matter. The court has not yet appointed any other expert, nor it has clarified the set of questions.

IV. ČESKÉ RADIOKOMUNIKACE a.s. – legal action on CZK 3.1 billion

The decision which fully dismissed the legal action against the Company was issued on the oral hearing held on 22 April 2016. The main reason was that the plaintiff did not provide the court with relevant facts and evidence. The written counterpart of the decision with detail reasoning hasn't been delivered yet.

V. TELECONSULT-INTERNATIONAL, spol. s r.o. – legal action on CZK 54.4 million

The court dismissed the legal action in the amount of CZK 52.7 million and granted to the Company the recovery of 97% costs of the proceeding on the oral hearing held on 14 January 2016. The amount CZK 1.7 million was granted to TELECONSULT-INTERNATIONAL, spol. s r.o. The amount should allegedly represent the difference between measurements of minutes in May 1998. The rest of the proceeding was terminated due to the partial withdrawal of the legal action. The Company filed the appeal against the part of the decision, which partially granted the claim to the plaintiff. The same did TELECONSULT-INTERNATIONAL, spol. s r.o. regarding the dismissed part of the claim.

VI. The criminal proceeding lead according to the Act No. 418/2011 Coll.

The Company filed complaint against the initiation of criminal prosecution to the Supreme Public Prosecutor's Office on 7 September 2015. By decision of the Supreme Public

Prosecutor's Office dated 11 March 2016 the decision which initiated criminal prosecution against the Company was entirely canceled and the police authority was ordered to inquire the case again and issue a new decision. The Supreme Public Prosecutor's Office stressed out that in the initial decision wasn't proved and not even described how actually the Company could committed criminal offences. The Company has filed the proposal to terminate the investigation to the police authority.

VII. BELL TRADE s.r.o. – legal action on CZK 5.2 billion

Although the Constitutional Court of the Slovak Republic already once decided that the jurisdiction of Slovak courts is not given in the matter and proceeding was terminated, the Company discovered yet another attempt to start another lawsuit against the Company with different reasoning.

On 14 March 2016 the proposal of BELL TRADE s.r.o. (BELL TRADE) company was delivered to the County court in Malacky, where BELL TRADE proposed the re-entry of the Company as the defendant into the procedure, which has been led solely between Slovak subjects - BELL TRADE and PET PACK SK s.r.o. on CZK 31 million, after Constitution court's decision.

BELL TRADE, whose current sole director, shareholder and also the legal representative is attorney JUDr. Milan Fulec, try to base this new claim and new attempt to establish the jurisdiction of the County court in Malacky on the letter from 8 June 2015, in which he stated that "withdraws from all agreements concluded between the RVI, a.s. and O2" and reserves the right to claim recovery of damages caused by such withdrawal. New claim raised against the Company represents the amount CZK 5.2 billion with interest from 14 March 2016.

The entire claim is again completely artificial. No contracts were ever signed and the Company never receive any delivery for which shall anybody claim such payments. BELL TRADE never claimed that it became a contractual party of contracts (which were never concluded). So far BELL TRADE always acted only as a "creditor", thus the holder of (supposedly existing and payable) claims against the Company. Moreover BELL TRADE always maintained that contracts were allegedly concluded for 10 years period and would have therefore come to an end on 31 December 2013 at latest. But current claim of BELL TRADE is based on withdrawal which was sent year and a half after this date. By this, any damage could not ever occur to BELL TRADE. Such alleged damage could hardly be connected to contractual relations between PET-PACK SK s.r.o. and BELL TRADE and to Slovak courts in any way. By decision from 16 May 2016 the County court in Malacky rejected the proposal of BELL TRADE to re-entry of the Company as the defendant. BELL TRADE filed the appeal to the Regional court in Bratislava.

VIII. Other

The Company is also involved in other legal disputes. The aggregate value of these disputes, in which the claim is higher than CZK 5 million and which have not been closed in 2016, exceeds

CZK 53 million. Possible impact of these disputes is reflected in the financial statements, however, risks associated with individual disputes are not significant.

The Company considers disclosing other information regarding the said litigations not advisable, as it could endanger the strategy of the Company in these cases.

The Company is convinced that all litigation risk of the Group has been appropriately reflected in the financial statements.

12 Commitments

Capital expenditure contracted but not yet included in the financial statements as at 30 June 2016 amounted to CZK 1,869 million (as at 31 December 2015: CZK 455 million). The majority of contracted amounts relate to the telecommunications network and service contracts.

Amount of CZK 1,472 million arising from closed auction awarding the licences to use radio frequencies in the 1800MHz and 2600MHz bands is included in the Commitments as at 30 June 2016. CTO expects the decision on the allocation of the radio frequencies to be made in the second half of 2016.

13 Related party transactions

Companies PPF Telco B.V. and PPF A3 B.V., through which Mr. Petr Kellner controls the Company, are part of PPF Group.

The Group provides services to all related parties on common commercial terms. Sales and purchase transactions with related parties are based on contractual agreements negotiated on common commercial terms and conditions and at market prices. Outstanding balances of assets and liabilities are unsecured, interest free (excl. financial assets and liabilities used for financing) and the settlement occurs either in cash or by offsetting. The financial assets balances are tested for impairment at the balance sheet date. As at 30 June 2016 and as at 31 December 2015 no allowance or write-off was incurred.

The comparative information in this note is reported including discontinued operations.

The following transactions were carried out with related parties:

I. Parent company:

The dividend paid during the six months period ended 30 June 2016 to the shareholders from PPF Group amounted to CZK 4,172 million (for the six months ended 30 June 2015: CZK 3,417 million). The liability from dividend distribution to the parent company was duly paid as at 30 June 2016 and 31 December 2015.

II. Other related parties – PPF Group and associated and joint ventures:

Balance sheet	30 June 2016	31 December 2015
In CZK million		
a) Receivables	135	365
b) Payables	1,109	1,193
c) Financial derivative instruments	-	(1)
d) Cash equivalents (see Note 7)	1,452	785
Statement of total comprehensive income	For the six months	For the six months
In CZK million	ended 30 June	ended 30 June
	2016	2015
a) Sales of services and goods	279	64
b) Dividends income	4	4
b) Purchases of services and goods	5,377	1,139
c) Management fees	-	45
d) Interest income	-	3
e) Changes in fair value of derivatives (net)	2	-

For the period January – May 2015, the separated part of CETIN was under control of the Company from the perspective of IFRS. Sales and purchase with the related parties shown above therefore include only transactions for the period of June 2015.

During the six months ended 30 June 2016 there were no capital purchases with related parties. During the six months ended 30 June 2015 capital purchases were solely with CETIN; the Company sold assets to CETIN at carrying value CZK 99 million for the sale price of CZK 108 million and acquired assets from CETIN for CZK 91 million.

III. Other related parties

Members of the Board of Directors and of the Supervisory Board of the Company were granted the following benefits:

In CZK million	For the six months	For the six months
	ended 30 June 2016	ended 30 June 2015
Salaries and other short-term benefits	27	22
Personal indemnification insurance	-	-
Total	27	22

No loans were provided to members of Board of Directors and Supervisory Board in 2016 and 2015.

No loans were provided by the Group to related parties.

14 Subsidiaries, associates and joint ventures

As at 30 June 2016

	Subsidiaries	Group's interest	Cost of investment in CZK million	Country of incorporation	Activity	Method of consolidation
1.	O2 Slovakia, s.r.o.	100 %	6,116	Slovakia	Mobile telephony, internet and data transmission services	Consolidated (full consolidation)
2.	Internethome, s.r.o.	100 %	272*	Czech Republic	Provision of WiFi internet access	Consolidated (full consolidation)
3.	O2 Family, s.r.o.	100 %	200	Czech Republic	Mobile telephony, internet and data transmission services	Consolidated (full consolidation)
4.	O2 TV s.r.o.	100 %	1	Czech Republic	Digital television	Consolidated (full consolidation)
5.	O2 IT Services s.r.o.	100 %	242	Czech Republic	Information technology services	Consolidated (full consolidation)
6.	Bolt Start Up Development a.s.	100 %	2	Czech Republic	Startup fund	Consolidated (full consolidation)
7.	O2 Business Services, a.s.	100 %	82	Slovakia	Mobile telephony, internet and data transmission services	Consolidated (full consolidation)
8.	eKasa s.r.o.	100 %	-	Czech Republic	Provider of solution for electronic records of sales	Consolidated (full consolidation)
Associates						
9.	První certifikační autorita, a.s.	23 %	9	Czech Republic	Certification services	Not consolidated (not material)
10.	AUGUSTUS, spol. s r.o.	40 %	-	Czech Republic	Auction sales and advisory services	Not consolidated (in bankruptcy)
11.	TapMedia s.r.o.	20%	15	Czech Republic	Mobile applications development	Not consolidated (not material)
12.	Dateio s.r.o.	21 %	30	Czech Republic	Development of targeted marketing platform	Not consolidated (not material)
Joint ventures						
13.	Tesco Mobile ČR s.r.o.	50 %	6	Czech Republic	Mobile virtual network operator for prepaid services	Consolidated (Equity method)

14.	Tesco Mobile Slovakia, s.r.o.	50 %	-	Slovakia	Mobile virtual network operator for prepaid services	Not consolidated (not material)
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* The Company recognised impairment provision of CZK 261 million for its investment in Internethome, s.r.o.

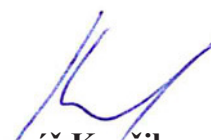
15 Post balance sheet events

There were no events which occurred subsequent to the balance sheet date and which would have a material impact on the condensed consolidated financial statements for the six months ended 30 June 2016.

24 August 2016



Tomáš Budník
Chief Executive Officer
Chairman of the Board of Directors



Tomáš Kouřil
Chief Financial Officer
Vice-chairman of the Board of Directors



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Other information for shareholders and investors

Shareholder structure

O2 CZ shareholder structure as at 30 June 2016:

	Name	Address	Percentage of share capital held	Percentage of voting rights held
1	PPF Telco B.V.	Strawinskylaan 933, Amsterdam, Kingdom of the Netherlands	73.79%	74.32%
2	PPF A3 B.V.	Strawinskylaan 933, Amsterdam, Kingdom of the Netherlands	10.27%	10.34%
PPF Group total			84.06%	84.66%
3	O2 Czech Republic a.s. (treasury shares)	Za Brumlovkou 266/2, Praha 4-Michle, 140 22, Czech Republic	0.71%	0.00%
4	Investment funds and individual owners	–	15.23%	15.34%

Share capital and shares

In the first half of 2016, no changes occurred in the share capital. The share capital of O2 CZ, which as at 30 June 2016 was CZK 3,102,200,670, has been fully paid up and was formed of the following shares:

- A.
- | | |
|--------------------------|-------------------|
| Type: | ordinary |
| Kind: | registered |
| Form: | booked |
| Number of shares issued: | 310,220,057 |
| Nominal value: | CZK 10 |
| Total volume of issue: | CZK 3,102,200,570 |
| ISIN: | CZ0009093209 |
- B.
- | | |
|--------------------------|--------------|
| Type: | ordinary |
| Kind: | registered |
| Form: | booked |
| Number of shares issued: | 1 |
| Nominal value: | CZK100 |
| Total volume of issue: | CZK 100 |
| ISIN: | CZ0008467115 |

Equity

The structure of unconsolidated equity of O2 CZ as at 30 June 2016 was as follows:

	(in CZK mil.)
Share capital	3,102
Issue premium	11,894
Treasury shares	(527)
Funds	7
Retained earnings	3,569
Total	18,045

Trading in O2 CZ shares

In the period from the start of the year until 30 June 2016, the price of O2 CZ shares fell 13.5% to CZK 217, while the Prague Stock Exchange (PSE) main index, PX Index, fell 14.6% down to 816.91 points. As at 30 June 2016, the market capitalisation of O2 CZ was CZK 67.3 bn. It represented 7.4% of the PSE's equities market capitalisation at the end of the first half of 2016, which ranked the Company fourth among those traded on the PSE stock market.

The total volume of O2 CZ shares traded on the PSE market in the first half of 2016 broke the CZK 3.5 bn mark, compared with CZK 7.7 bn in the first half of 2015. This indicator puts the Company's shares in the top five traded stocks, and accounted for close to 5% of the total volume of shares traded on the market. The average daily traded volume in the first half of 2016 was CZK 27.6 m. As of 24 August 2016, i.e. the date of approval of this Half-year Report, the price of O2 CZ shares reached CZK 227.6, representing 9.3% decrease year to date. In the same period PX index went down by 10.3% to 858.06 points.

O2 CZ share performance against PX index



General Meeting

The General Meeting was held on 19 April 2016. The conclusions of the General Meeting are given in an overview in section Events in Corporate Governance of the O2 Group in this Half-year Report.

Dividends

The General Meeting approved, among other things, the payment of dividends for the year 2015. Out of the profit posted in 2015 and a part of the retained earnings, a total of CZK 4,964 m was paid as dividends, which is a dividend of CZK 16 per share in the nominal value of CZK 10, and CZK 160 per share in the nominal value of CZK 100. The record day was 19 April 2016 and the disbursement started on 19 May 2016 through Česká spořitelna. For more information on the payment of dividends please visit the Company website: <http://www.o2.cz/spolecnost/en/dividends/>.

Own shares of the Company

As stated in the 2015 Annual Report, on 28 January 2016 O2 CZ launched a programme to buy back its own shares on the regulated market of the Prague Stock Exchange, under terms and conditions published in connection with the share buy-back programme on 23 December 2015. By 30 June 2016, O2 CZ acquired a total of 2,199,220 own shares (0.7% from the total of ordinary shares issued) for the price of CZK 527 m. No own shares have been alienated or cancelled during the first half of 2016. For details of the process of acquisition of own shares please visit the Company website: http://www.o2.cz/spolecnost/en/shares/453904-nabyti_vlastnich_akcii_v_roce_2016.html.

Institutional investors and shareholders please contact:

Investor Relations

O2 Czech Republic a.s.

Za Brumlovkou 266/2, 140 22 Praha 4-Michle

Tel.: +420 271 462 076, +420 271 462 169

E-mail: mailto:investor_relations@o2.cz, <http://www.o2.cz/spolecnost/en/investor-relations/>



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Declaration of persons responsible for the Half-year Report

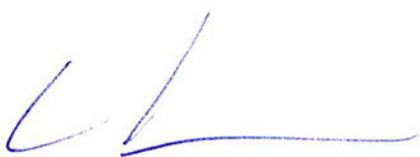
| 6 | Declaration of persons responsible for the Half-Year Report

Tomáš Budník, Chairman of the Board of Directors of O2 Czech Republic a.s.

and

Tomáš Kouřil, Vice-chairman of the Board of Directors of O2 Czech Republic a.s.

hereby declare that, to their best knowledge, the consolidated Half-Year Report gives a true and faithful reflection of the financial situation, business and the results of the Company and its consolidated whole for the past accounting period, and of the outlook on the future development of the financial situation, business and results.



Tomáš Budník

Chairman of the Board of Directors



Tomáš Kouřil

Vice-chairman of the Board of Directors

In Prague on 24 August 2016