Telefónica Deutschland

Q3 2017 preliminary results

Telefónica Deutschland
Investor Relations
25 October 2017

Public – Nicht vertraulich

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9m 2017: Solid operational momentum & synergies on track, regulation impact as expected

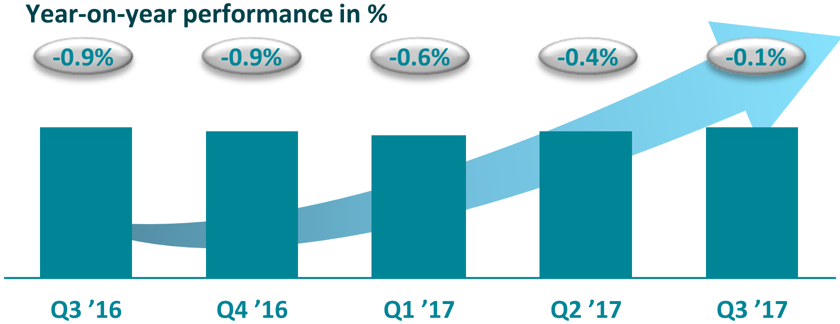
MSR[1] **-0.4% y-o-y** **(excl. regulatory effects)**	• Solid operational momentum in a dynamic competitive environment with focus on data monetisation • Continued improvement of MSR trends excl. regulatory effects; maintain investment focus to stimulate MSR momentum
2.4 GB **average data usage[2]**	• LTE adoption and O_2 Free portfolio as drivers of sustained data growth • 15.7 million LTE customers; +48% year-on-year • Traffic up 51% y-o-y; usage of 2.4 GB for O2 consumer postpaid LTE customers
OIBDA[3] **+3.1% y-o-y**	• OIBDA growth in line with outlook, reflecting synergy capture and investments in O_2 Free • Incremental OIBDA relevant savings of ca. EUR 115 million in the nine month period • Refining full year OIBDA outlook to “flat to low single digit % growth”
Operating Cash Flow	• OpCF generation remains strong on the back of operational momentum and synergies • Dividend proposal of EUR 0.26 per share (+4% year-on-year) to AGM in May 2018

[1] Excluding the impact from regulatory changes. For details please refer to additional materials of the Q3 2017 results release
[2] For O_2 consumer postpaid LTE customers
[3] Excluding exceptional effects. For details please refer to additional materials of the Q3 2017 results release

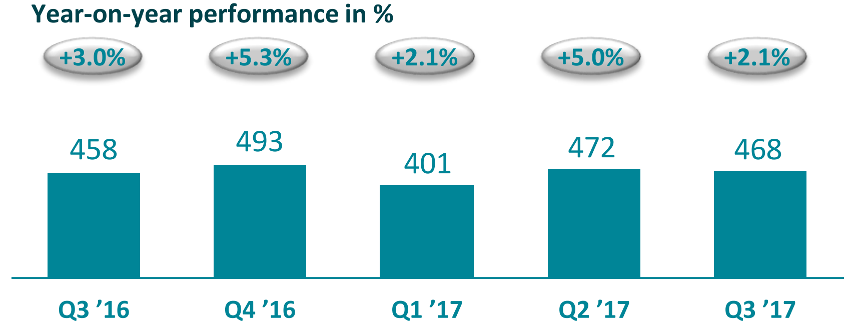
MOMENTUM + TRANSFORMATION

Confirming and refining full-year 2017 outlook

Underlying[1] MSR trends continue to improve



OIBDA[2] with sustained year-on-year growth



	Baseline 2016 (EUR m)	**Outlook 2017** (y-o-y pct. change)	**Actual 9 months 2017** (EUR m / y-o-y pct. change)	
MSR	5,437	**Slightly negative to flat[1]** Excluding the impact from regulatory effects	**4,072** / -0.4% (excl. regulatory effects of EUR 118 million)	✓
OIBDA	1,793[2]	**Flat to mid single-digit % growth[2]**	**1,341** / +3.1%	✓
CapEx	1,102	**Around EUR 1 billion**	**688** / -7.5%	✓
Dividend	EUR 0.25/share (Payout May 2017)	**Dividend growth over 3 years** (2016-2018)		

Refining OIBDA outlook to:

Flat to low single-digit % growth[2]

Dividend proposal to AGM 2018 of:

EUR 0.26/ share

[1] Excluding the impact from regulatory changes; for details please refer to further materials of Q3 2017

[2] Excluding exceptional effects; for details please refer to further materials of Q3 2017 results release. We have calculated a comparable for 2016; for details please refer to materials of the full year 2016 results release

Competitive environment remains dynamic with focus on profitable growth

Premium

Non-premium: Own secondary brands

Ethnic brands

Non-premium: Partner brands

MNVOs & Service Provider

Branded Reseller (selection)

Brands with access to Telefónica Deutschland network

Premium: Bigger data buckets fuel data growth

- O_2 Free 15 promo and new **O_2 Free** portfolio well received by new and existing customers
  - Usage of **> 5GB** per month
  - **ARPU accretive**
- **High-speed DSL portfolio** complements offer in a soft converged market environment

Non-premium: More benign pricing environment

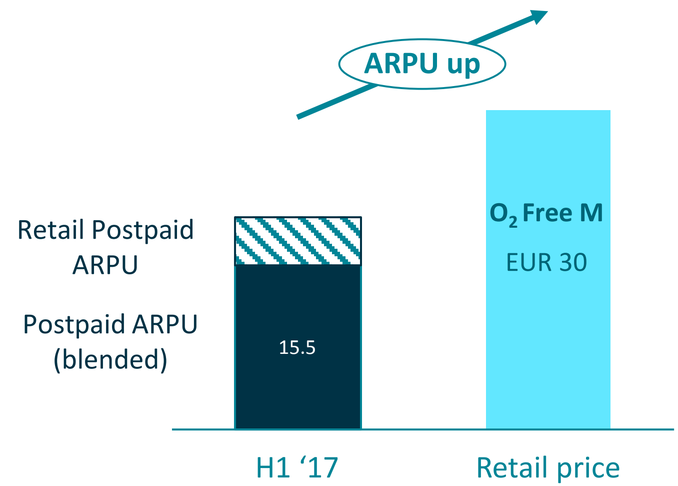
- **Multi-brand & multi-channel strategy** supports broad customer reach across segments, leveraging distribution power of partners
- **MNVOs** shifting to higher price points and larger data allowances

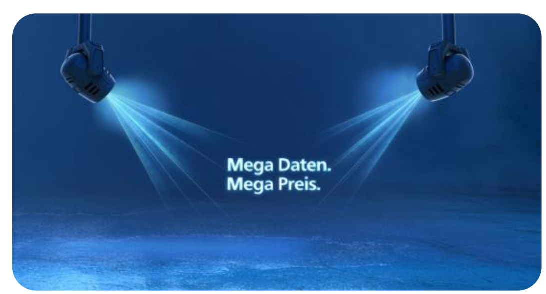
New O_2 Free portfolio sets new standard for mobile freedom with ARPU-up potential

O_2 Free (from 6 Sept 2017)

	S	M	L	XL
		Tipp		
Data	LTE Max 1 GB	LTE Max 10 GB	LTE Max 20 GB	LTE Max 25 GB
Price	€19.99	€29.99	€39.99	€49.99

3G flat – throttle to 1 Mbps
after consumption of high-speed volume





Network consolidation progressing according to plan

Network integration timeline 2016 - 2019

April/May 15

3G National Roaming for all customers

July 15

Deal to **transfer 7,700 sites** to DTE

April 16

Sale of towers to Telxius

July 16

Consolidation & roll-out **4G network**

April 17

Implementation of **SON** & **SOC**

May 17

Excellence Award 2017

Implementation of **CEM**

August 17

1 MNC nationwide

- Decommissioning of **14k sites**
- Roll-out of **30k LTE elements**
- Utilisation of **new licenses**
- Pilot network for **5G**

- Conversion to **one nationwide mobile network code (MNC)** – even in non-consolidated areas
- **HD Voice** now available for calls from the O_2 network into the Deutsche Telekom network and vice versa
- **Test drives** by a independent service provider **confirm** the **improvements in network quality** in consolidated regions

Transformation agenda to be presented at Capital Markets Day in early 2018

Integration | Today | Transformation

Concept

- **Growth** – e.g. ADA / IoT
- **Customer**
- **Efficiency** – e.g. E2E, real-time
- **Investment** – Capex / Opex / Restructuring

Customer at the heart of our transformation agenda

Capital Markets Day

TEF D will hold a **CMD in context of Q4 2017 results** to give an update on:

- **Integration process**
  - Integration milestones achieved, status of projects
  - Synergy capture and phasing
- **Transformation agenda**
  - Vision & strategy
  - Details on main workstreams
  - Investment needs and benefits

Q3 2017: Solid operating momentum & benefits from synergy execution

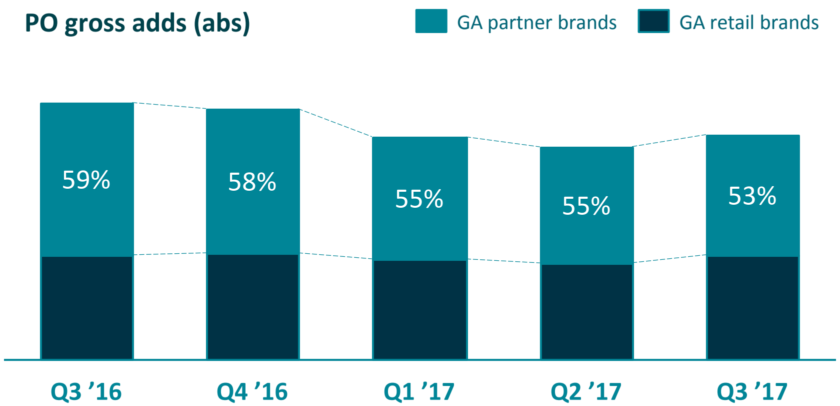
MSR -0.1% y-o-y (excl. regulatory effects)	• MSR incl. regulatory effects -3.6% year-on-year; trends improving sequentially • Tailwinds from O_2 Free, headwinds regulation & legacy base effect • Recovery in discount pricing supports stable postpaid churn
Net adds +183k postpaid +103k VDSL	• Solid operational momentum in the quarter driven by O_2 Free & birthday promotions • Share of postpaid wholesale trading stabilising on back of tariff adjustments • Continued strong demand for VDSL; wholesale migration effects visible
OIBDA[1] +2.1% y-o-y	• OIBDA benefitting from successful synergy capture; further margin improvement • Approx. EUR 40 million of synergies, stemming from roll-over effects & additional savings • Margin enhancement of +0.9 percentage points year-on-year to 25.3% in the third quarter
OpCF +58% y-o-y	• OpCF benefits from additional approx. EUR 30 million Capex synergies • Cash flow trajectory supports dividend commitment • Leverage at 0.8x, in line with target

[1] Excluding exceptional effects. For details please please refer to further materials of the 2017 results release

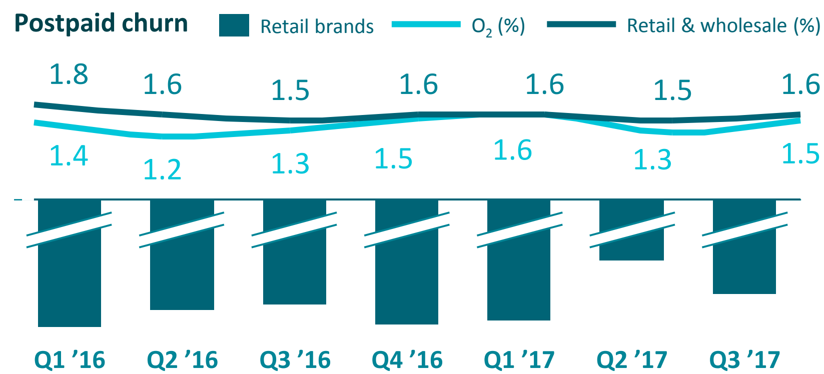
MOMENTUM TRANSFORMATION

Retail vs. wholesale trends further improving; churn trends remain solid

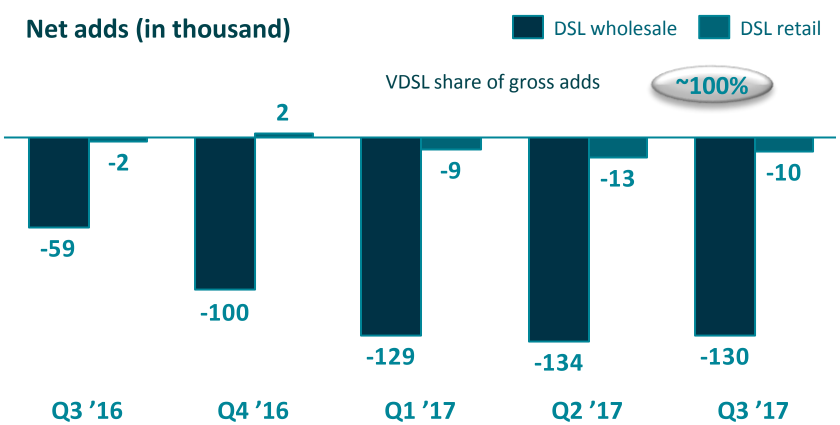
Visible effect from price increases



Maintaining retention focus



VDSL drives fixed trading

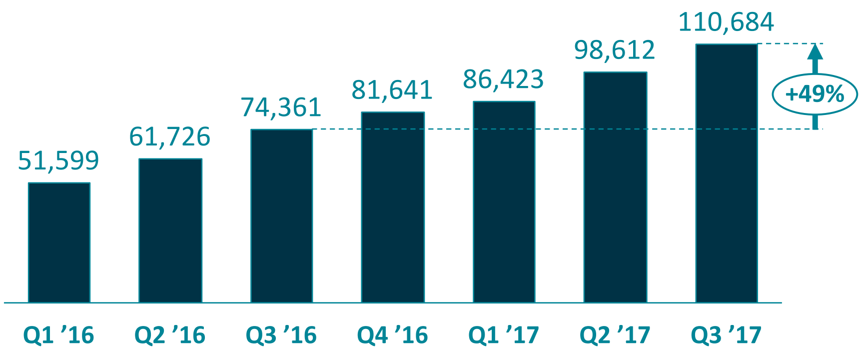


- Solid trading momentum in retail on the back of O_2 Free 15 and new O_2 Free portfolio
- Partner trading reflects changes in pricing
- Churn in O_2 consumer remains low, slight seasonal uptake in line with prior years
- VDSL with record net adds of 103 thousand; customer migration in wholesale continues in line with expectations

Adoption bigger data buckets & LTE drive sustained data growth

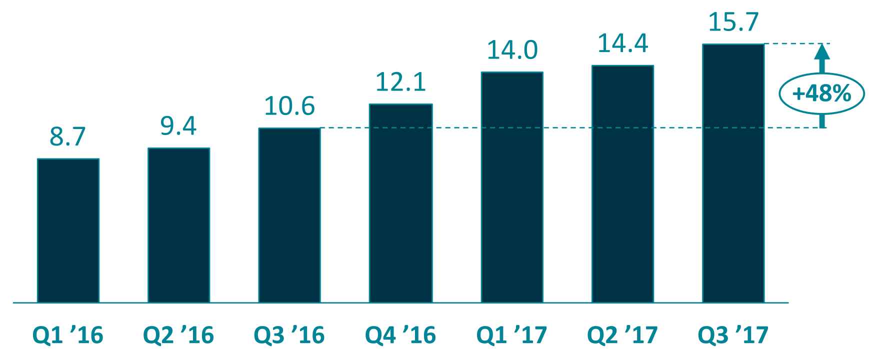
Sustained data traffic growth

Traffic (TB/quarter)



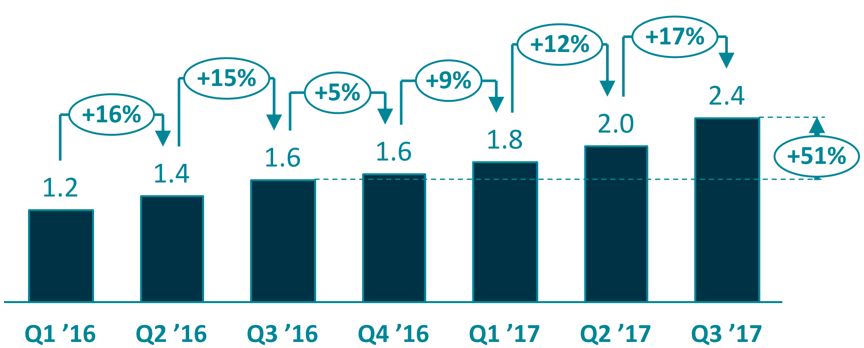
LTE adoption continues to grow

LTE customers (million)



Music & video streaming drivers of data growth

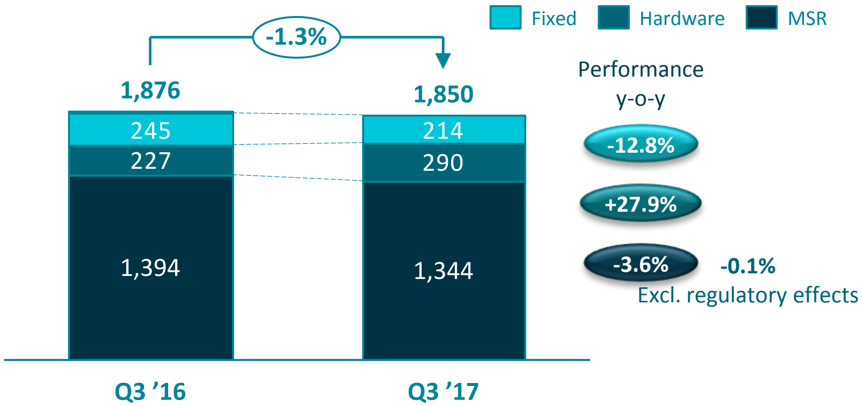
Average data usage for O_2 consumer LTE customers (GB)



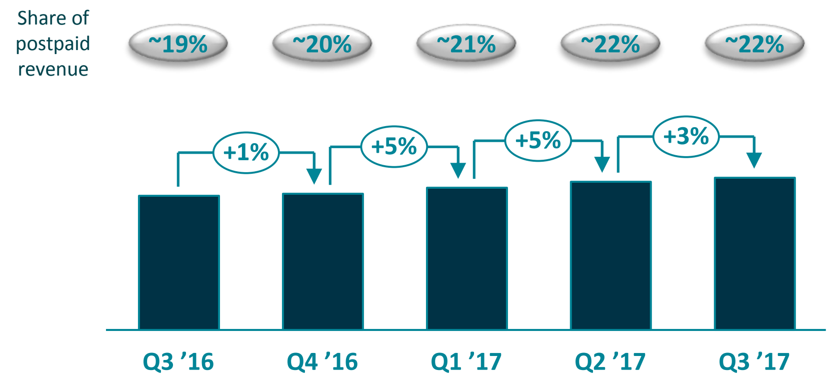
- LTE customer base up 48% y-o-y to 15.7 million; increasing LTE penetration in prepaid
- Music & video streaming key drivers of data traffic growth; up ~50% y-o-y
- Average monthly data usage for O_2 consumer LTE customers up ~51% y-o-y to 2.4 GB, bigger bundles drive data usage

Underlying MSR trends further improving; stable partner share of postpaid MSR

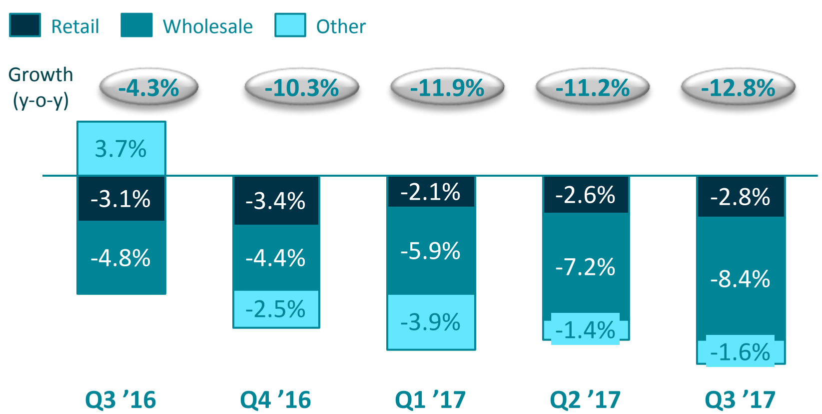
Revenue structure (in EUR m)



MSR from partner business (in EUR m)



Contribution to fixed revenue y-o-y[1] performance

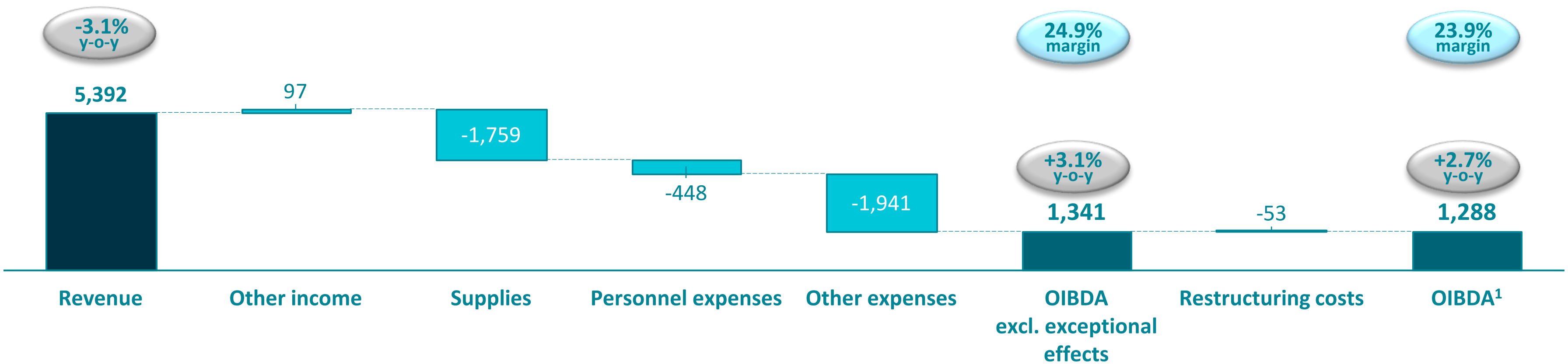


- Further sequential improvement of underlying MSR trends while regulatory effects weigh in reported terms
- Partner share of postpaid MSR remains stable
- Underlying trends for handsets slightly improving; Q3 benefited from stock clearance
- Lower y-o-y customer base both in retail and wholesale drives dynamics in fixed

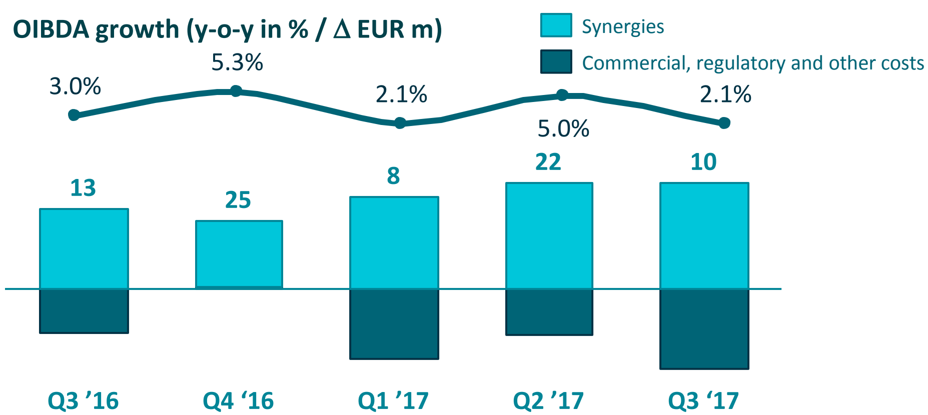
[1] Please note a change in the definition of the fixed retail/wholesale split, which better reflects revenue allocation across segments

OIBDA reflects successful synergy capture, RLH-regulation and investment activities

Structure of OIBDA for January to September 2017 (in EUR m)



Synergies driving OIBDA growth



- Successful synergy capture: Incremental savings of ~EUR 40 million in Q3 (~EUR 115 million YTD) mainly from FTE restructuring and network consolidation
- Continued investment focus to drive midterm MSR growth
- Data growth under the RLH-regime weighs on wholesale costs
- OIBDA margin at 24.9%, up 1.5 pp y-o-y

[1] Excluding the extraordinary gain related with the sales of tower assets to Telxius in Q2 2016

Confirming and refining full-year 2017 outlook

Outlook 2017

	Baseline 2016 (EUR m)	Outlook 2017 (y-o-y pct. change)	Actual 9 months 2017 (EUR m / y-o-y pct. change)	
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OIBDA	1,793[2]	**Flat to mid single-digit % growth**[2]	**1,341** / +3.1%	✓
CapEx	1,102	**Around EUR 1 billion**	**688** / -7.4%	✓
Dividend	EUR 0.25/share (Payout May 2017)	**Dividend growth over 3 years** (2016-2018)		

Refining OIBDA outlook to:
Flat to low single-digit % growth[2]

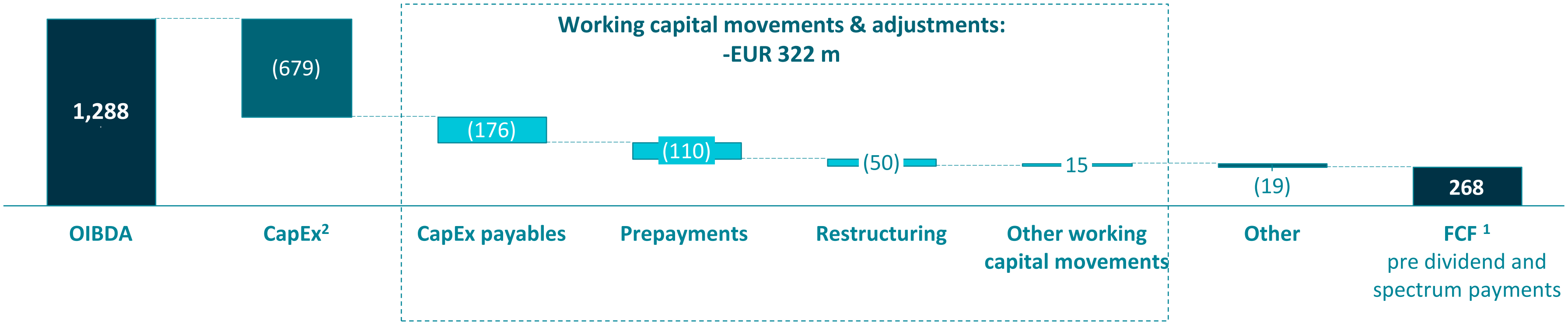
Dividend proposal to AGM 2018 of:
EUR 0.26/ share

- **Synergy execution in line with expectations**, fully on track to achieve EUR 670 million operating CF savings by year end 2017 (~75% of total target in 2019)
- OIBDA expectation reflects **effects from regulatory changes** as well as **our investment focus**
  - Significant uptick in data usage from customers under the new roam-like-home regime => elasticity effects weighing on connectivity-related wholesale costs with unchanged expectation of no less than 4-5% year-on-year
  - Ongoing market investment needs in a dynamic competitive environment to partake in the revenue opportunity from accelerating data usage

[1] Excluding the impact from regulatory changes; for details please refer to further materials of Q2 2017
[2] Excluding exceptional effects; for details please refer to further materials of Q2 2017 results release. We have calculated a comparable for 2016; for details please refer to materials of the full year 2016 results release

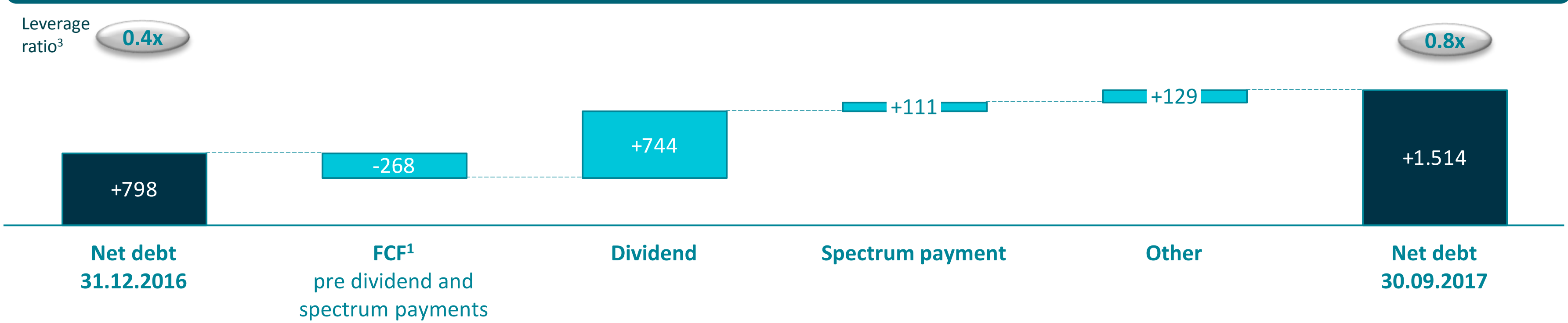
Financial leverage in line with target

Evolution of Free Cash Flow (FCF)[1] YTD September 2017 (in EUR m)



[1] Free cash flow pre dividend and spectrum payment is defined as the sum of cash flow from operating activities and cash flow from investing activities
[2] Excluding additions from captalised finance leases and capitalised costs on borrowed capital for investments in spectrum.

Evolution of Net Debt[3] (y-o-y in EUR m) – Leverage ratio[3] increases due to dividend payment



[3] For definition of net debt & leverage ratio please refer to Q3 2017 earnings release

Main takeaways

- Q3/9 months results in line with outlook; **confirming full year outlook for MSR and Capex**, **refining 2017 OBIDA guidance**

- **New O_2 Free portfolio** and 15-year anniversary activities helps stimulate data growth in German market; focus on the **data monetisation opportunity from bigger data buckets**

- Maintain **commercial investment focus** to stimulate **MSR momentum**

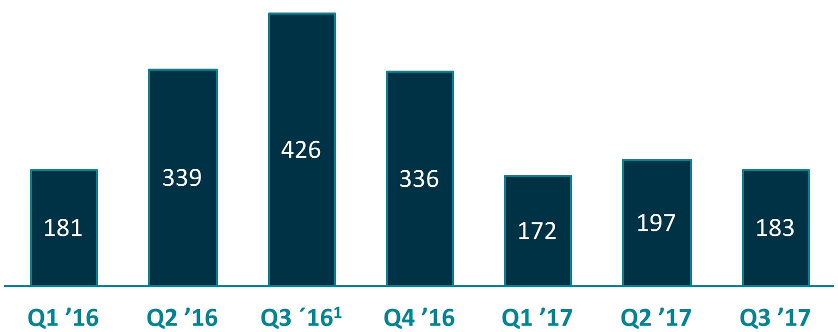
- OIBDA reflects **synergies and investments** in our premium positioning

- **Dividend proposal of EUR 0.26 per share** for the financial year 2017 supported by cash flow momentum; **reiterating commitment to grow dividend** for 2018

Appendix – KPIs

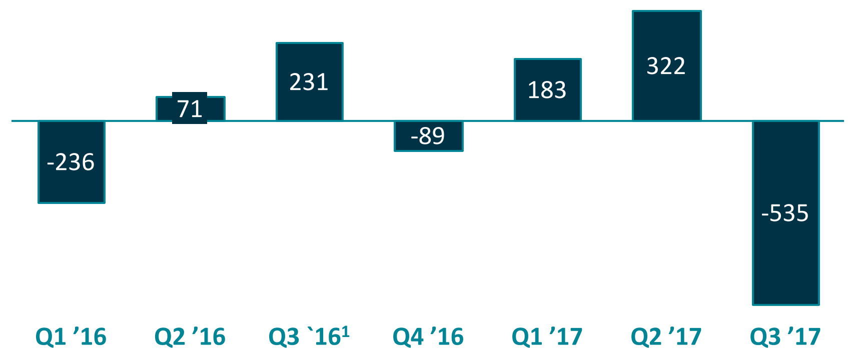
Mobile KPIs

Postpay net adds ('000)

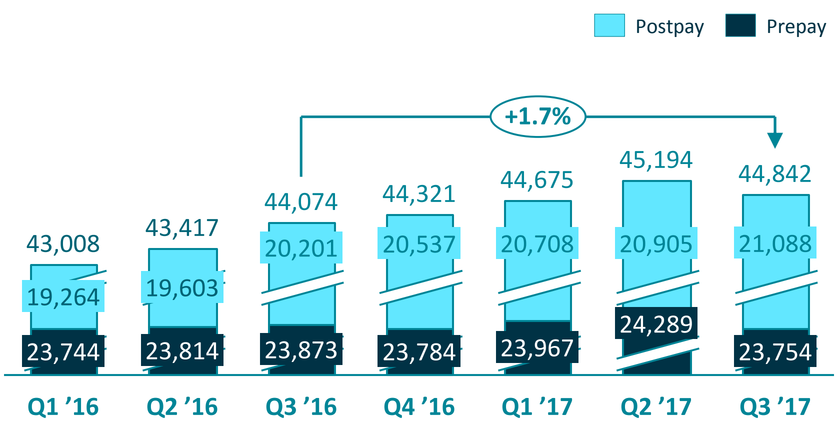


[1] Excluding reclassification of 172k customers from prepaid to postpaid as part of the customer migration activities

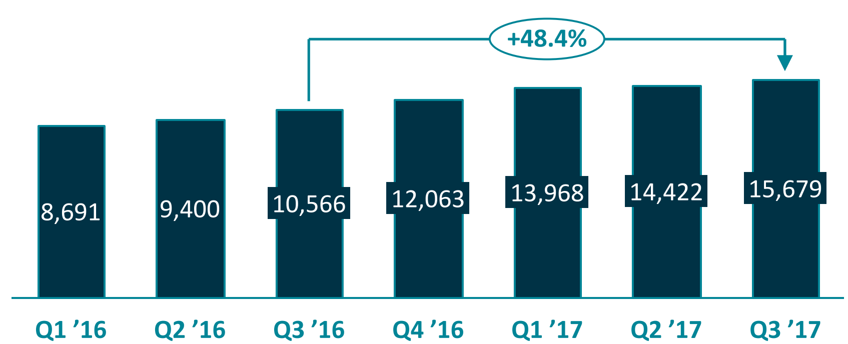
Prepay net adds ('000)



Mobile customer base ('000)

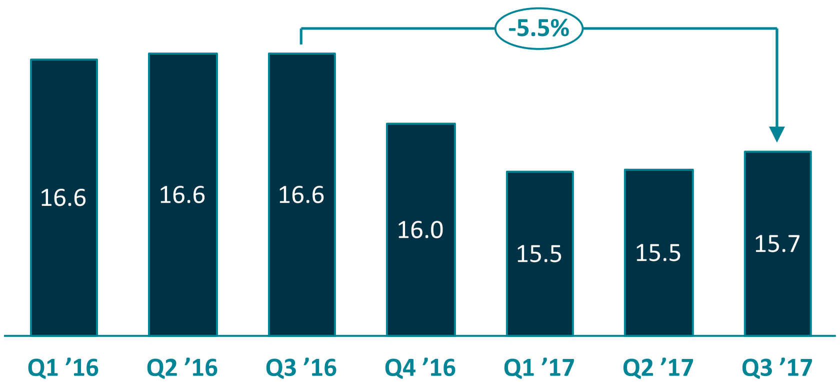


LTE customer base ('000)

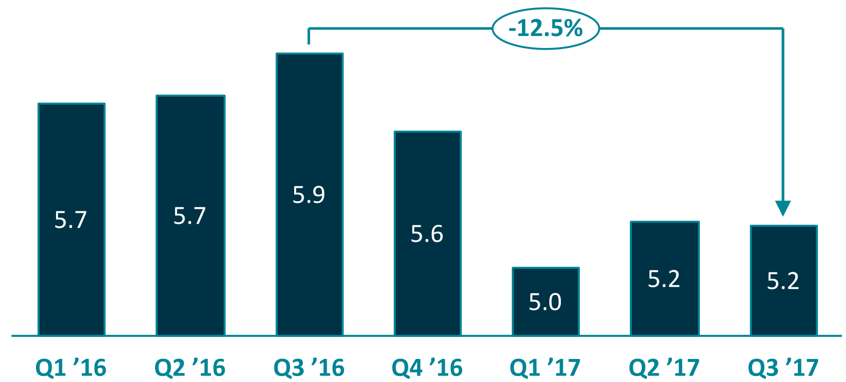


Mobile KPIs

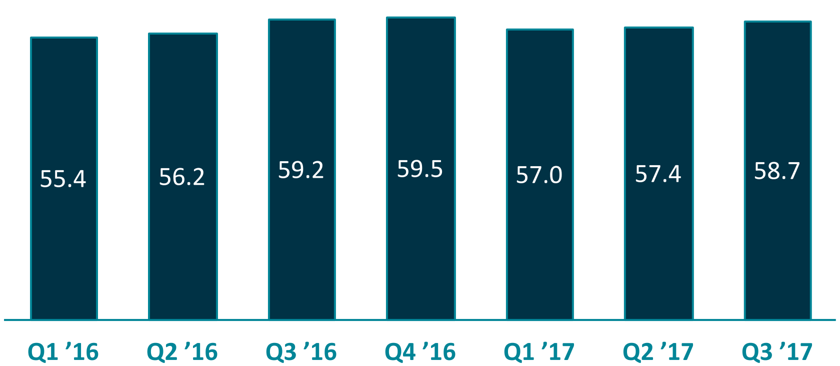
Postpay ARPU (EUR)



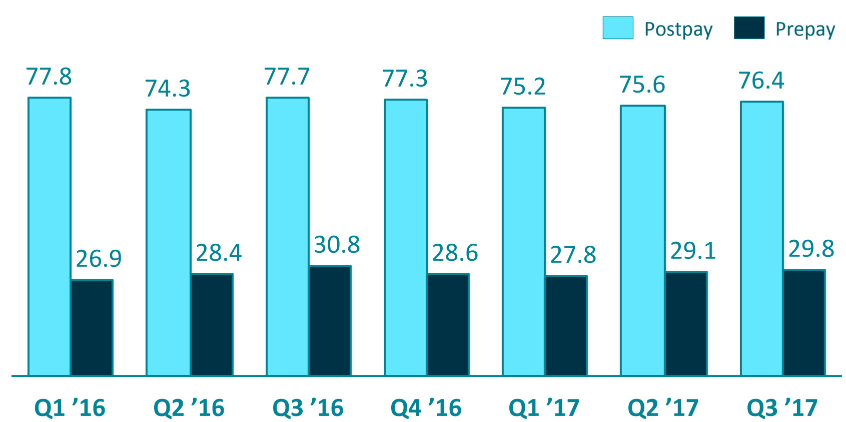
Prepay ARPU (EUR)



Smartphone penetration (%)[1]



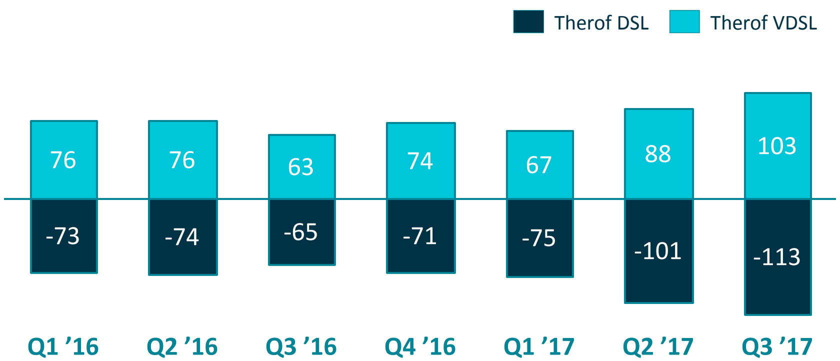
Smartphone penetration O_2 consumer (%)



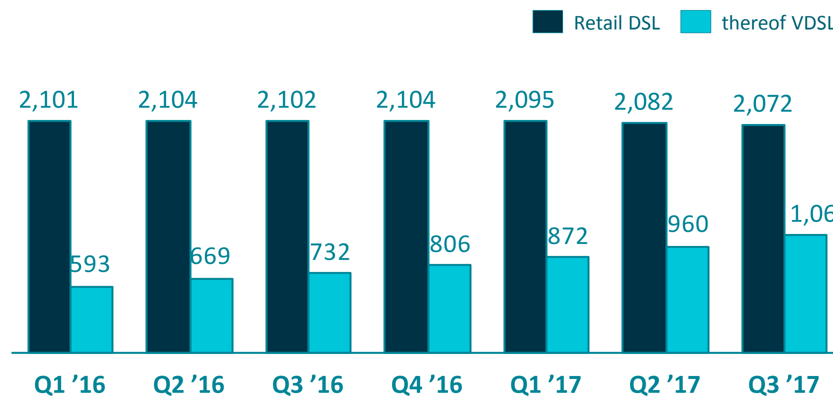
[1] Smartphone penetration is based on the number of customers with a smallscreen tariff (e.g., for smartphones) divided by the total mobile customer base less M2M, less customers with a big screen tariff

Fixed-line KPIs

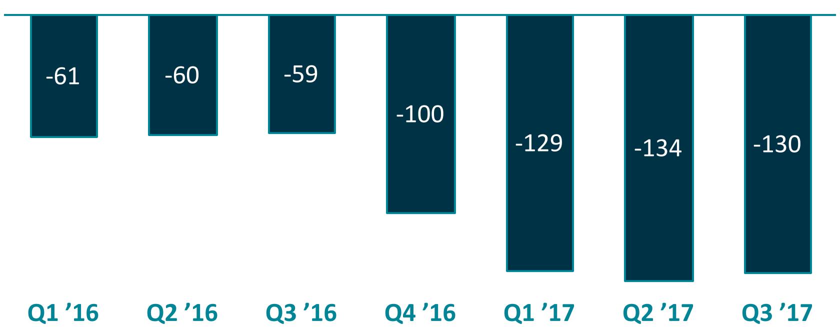
Retail broadband net adds ('000)



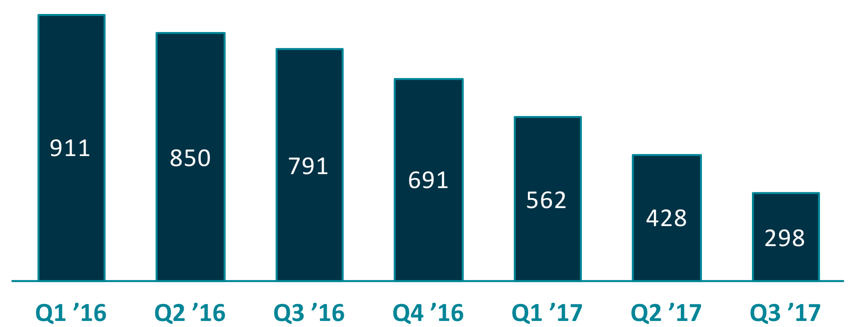
Fixed accesses ('000)



Wholesale net adds ('000)



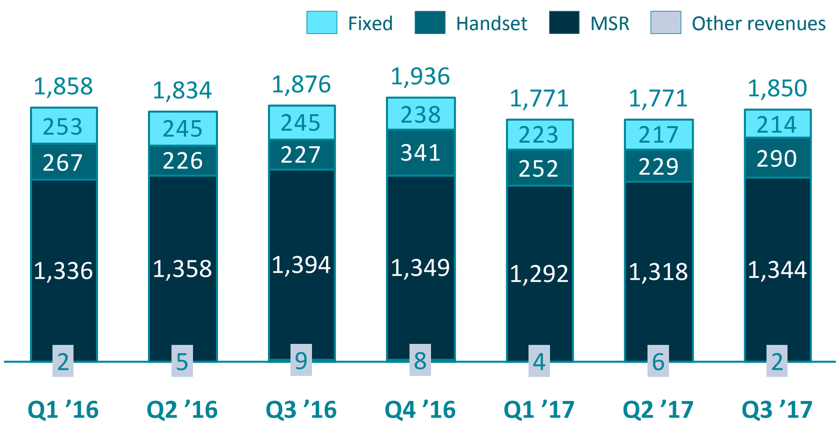
Wholesale accesses ('000)[1]



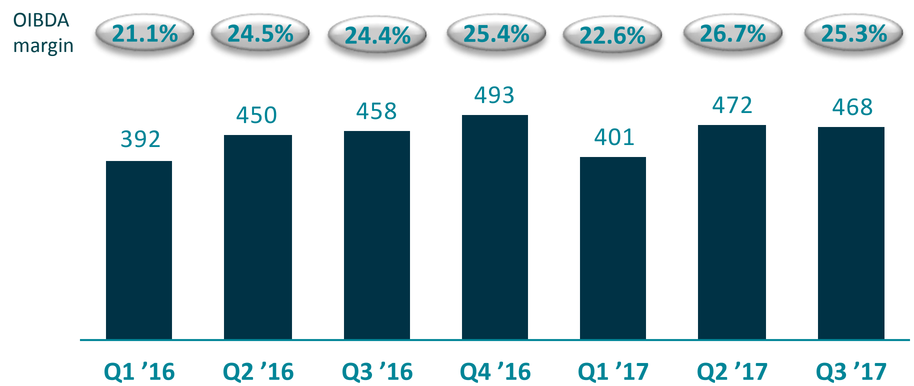
[1] Wholesale accesses incorporate unbundled lines offered to 3rd party operators, including wirelines telephony and high-speed Internet access

P&L

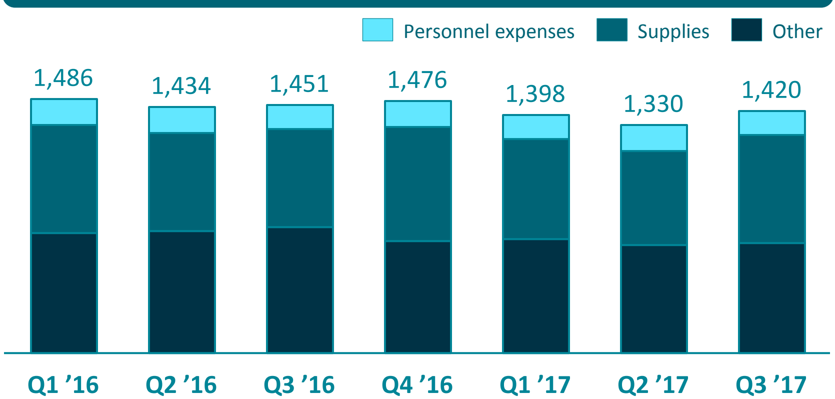
Revenue structure (EUR m)



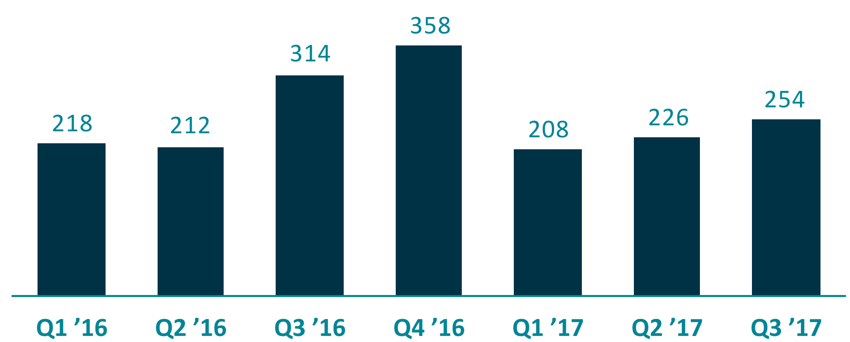
OIBDA (post GF, pre exceptional effects / EUR m)[1]



OpEx split[2] (EUR m)



CapEx (EUR m)

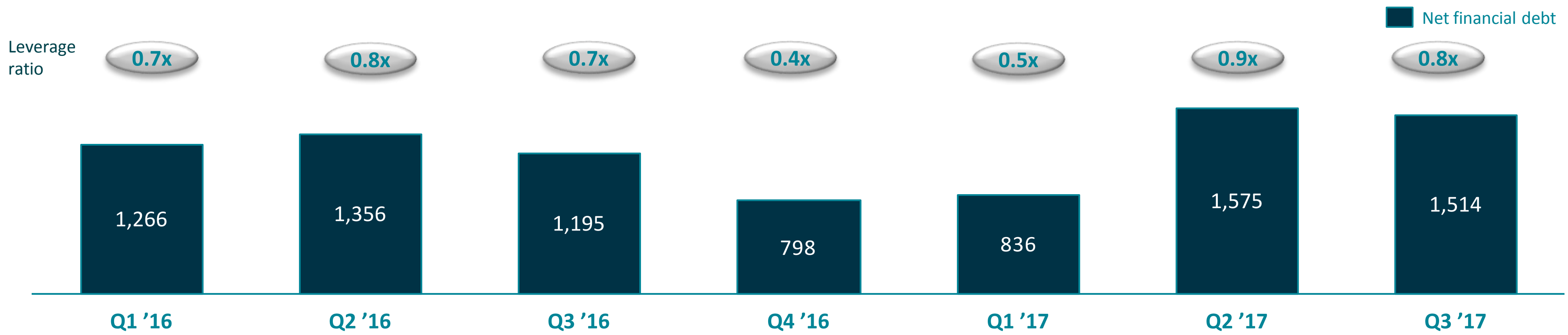


[1] Exceptional effects include restructuring costs as well as the net capital gain from the sale of Telefónica Deutschland's passive tower infrastructure in April 2016. We have calculated a pro-forma OIBDA of EUR 1,793m for 2016, which includes the operating lease-related effects from the sale of Telefónica Deutschland's passive tower infrastructure in April 2016, as if it had occurred on 1 January 2016

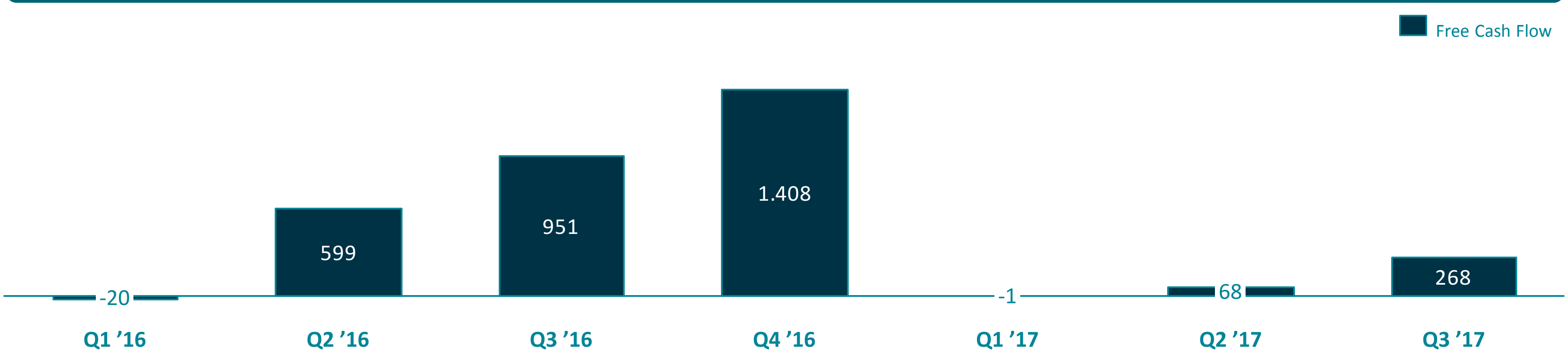
[2] Opex-split before exceptional effects

Financials

Net debt and leverage



Free cash flow[1] (YTD)



[1] Free cash flow pre dividends and payments for spectrum is defined as the sum of cash flow from operating activities and cash flow from investing activities and does not contain payments for investments in spectrum in June 2015 as well as related interest payments

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