Telefónica Deutschland

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Telefónica Deutschland – Interim statement for January to September 2023

Telefónica Deutschland extended growth path – fully on track for FY23 outlook

- **Maintained robust commercial traction both in mobile and fixed; +396k mobile postpaid and +31k fixed BB net adds, 'value-over-volume' focus**
- **Achieved +2.2% y-o-y revenue growth mainly on good MSR momentum**
- **Improved OIBDA[1] growth to +3.6% y-o-y on enhanced operating leverage and successful cost management**
- **Made excellent progress with 5G network roll-out within normalised C/S envelope – '5G Plus' now on air in the entire 5G network**
- **Strong ESG commitment – well on track to deliver a sustainable digital future**
- **Fully on track for in Jul-23 upgraded FY23 outlook and to meet FCFaL consensus[2] for FY23**

Operating performance

Telefónica Deutschland delivered another quarter of robust growth in Q3 23 underpinned by its 'value-over-volume' strategy. The company's sustained commercial momentum is building on the well-received 'more-for-more' tariff portfolios and normalised churn rates as well as enhanced quality of service. The renowned connect magazine awarded a 'very good' rating to the O_2 shops as well as the O_2 fixed BB hotline, the 'myO_2' App achieved even an 'outstanding' rating.

In parallel, Telefónica Deutschland continued to make strong progress with the densification and further roll-out of its green 5G network. Since 10 Oct-23, O_2 customers can experience '5G Plus' (i.e. 5G stand-alone) in the O_2 network. This marks the beginning of a new technology era with '5G Plus' being available to >90% of the German population. The company is well on track for nationwide 5G coverage latest by YE25.

As part of its ESG-agenda, Telefónica Deutschland assumes responsibility also for its employees and the wider society. The company's attractiveness as an employer rose to all-time highs in the recent employee survey. Telefónica Deutschland's employees are highly engaged for society, i.e. by participating in the company's 'Volunteering Days' or the annual 'O_2 Telefónica Run' where the joint sporting activities are translated into charity donations.

Moreover, Telefónica Deutschland remains committed to its climate protection goals and has been nominated as a finalist for the '16th German Sustainability Award'. The Company strives to reduce its Scope 1 & 2 emissions by 95% and ultimately neutralising them no later than 2025. Also, the company is taking concrete actions to be net CO_2 neutral along its entire value chain (Scope 3) by 2040.

[1] Adjusted for exceptional effects. In Q3 23 exceptional effects amounted to EUR -0m of restructuring costs (EUR -4m in Q3 22)
[2] Company compiled consensus, for details please refer to financial results section for Q3 23 on Telefónica Deutschland's website.

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Mobile business

Mobile postpaid posted +396k net adds in Q3 23 vs. +304k in Q3 22 (+1,066k in 9M 23, up +10.5% y-o-y). Commercial success in the market is driven by the continued O_2 brand momentum and a solid contribution of partner brands. **O_2 postpaid churn** stood at a low rate of 1.0% in Q3 23 (1.2% in Q3 22) reflecting the O_2 brand appeal in combination with enhanced network and service quality.

M2M recorded +55k net additions in Q3 23 vs. +32k in Q3 22 (+154k in 9M 23, up +49.1% y-o-y).

Mobile prepaid net disconnections slowed to -22k in Q3 23 vs. -58k in Q3 22 (-506k in 9M 23 vs. +213k in 9M 22 including some revenue neutral reactivations), mainly reflecting the ongoing German market trend of prepaid to postpaid migration.

As a result, Telefónica Deutschland's **mobile customer accesses** grew +1.0% q-o-q[3] to 45.0m as of 30 Sep-23. The own-brand momentum combined with low churn rates are the main drivers of the strong increase of the **mobile postpaid base** (ex M2M), +5.1% y-o-y to 27.4m accesses (60.9% of total mobile access base, up +5.4 p.p. y-o-y). **M2M accesses** grew even +7.8% yoy to 1.8m whereas the **mobile prepaid base** accounted for 15.8m, down -17.8% y-o-y mainly due to some revenue neutral technical[4] base adjustments in the prior year.

O_2 postpaid ARPU growth accelerated to +2.0% y-o-y growth in Q3 23 (+1.2% y-o-y in 9M 23), reflecting customer demand for high value tariffs while partly offset by the reduction of MTRs as of 1 Jan-23; underlying[5] ARPU growth was even stronger at +2.6% y-o-y (+1.8% y-o-y in 9M 23).

Fixed business

Fixed broadband posted +31k net additions in Q3 23 vs. +19k in Q3 22 (+77k net additions in 9M 23 vs. +14k in 9M 22) reflecting the success of Telefonica Deutschland's technology agnostic 'O_2 myHome' tariff portfolio and low churn rates. **Fixed churn** improved 0.3 p.p. y-o-y to 0.8% in Q3 23.

Fixed broadband customer base was up +4.2% y-o-y to 2.4m accesses as of 30 Sep-23, thereof 78.4% VDSL accesses, -1.9 p.p. y-o-y as cable and fibre are gaining further trading momentum.

Fixed broadband ARPU[6] maintained its growth path mainly driven by the increasing share of higher value customers in the base, +2.2% y-o-y to EUR 25.6 in Q3 23 (+1.9% to EUR 25.5 in 9M 23).

[3] -4.2% y-o-y mainly on a revenue-neutral technical base adjustment in prepaid in Q4 22.

[4] Introduction of a stricter active SIM-card definition in Q4 22 post some revenue neutral reactivations of SIM-cards over the course of FY22.

[5] Excluding MTR-cut from EURc 0.55 to EURc 0.40 as of 1 Jan-23.

[6] Definition adjustment of fixed BB (FBB) ARPU calculation as of 1 January 2023 to fully reflect all fixed revenue streams; for comparability reasons including adjustment of previous year's values.

Financial performance

Revenues posted solid growth of **+2.2% y-o-y to EUR 2,131m** in Q3 23 (+4.8% y-o-y to EUR 6,323m in 9M 23) driven by ongoing mobile service revenue momentum.

Mobile service revenues[7] recorded strong growth of **+3.4% y-o-y to EUR 1,523m** in Q3 23 (+4.0% y-o-y to EUR 4,394m in 9M 23) with the negative impact from the MTR glidepath[8] more than offset by continued own-brand MSR-momentum and a solid contribution from partners.

Handset sales slowed to **-2.1% y-o-y to EUR 395m** in Q3 23 (+9.1% y-o-y to EUR 1,298m in 9M 23). High value smartphones remained popular while, as expected following record quarters, the overall customer demand for 'O_2 myHandy' contracts was somewhat softer in line with German market trends.

Fixed revenues grew **+1.8% y-o-y to EUR 208m** in Q3 23 (+2.3% y-o-y to EUR 616m in 9M 23) with **fixed retail BB revenues** recording even stronger growth of **+6.1% y-o-y** in Q3 23 (+5.0% in 9M 23).

Other income was EUR 45m in Q3 23 (EUR 115m in 9M 23, +1.9% y-o-y).

Operating expenses[9] were slightly higher **+1.6% y-o-y to EUR 1,512m** in Q3 23 (+5.5% y-o-y to EUR 4,517m in 9M 23) mainly reflecting the anticipated inflationary impacts.

- **Supplies** were slightly lower (-2.6% y-o-y) to EUR 631m in Q3 23 (up +3.3% y-o-y to EUR 1,931m in 9M 23) reflecting the positive effects from the MTR-cuts[7] and volume related hardware cost of sales. In Q3 23, connectivity-related cost of sales and hardware cost of sales accounted for 39% and 58% of supplies, respectively.
- **Personnel expenses** were up +12.7% y-o-y to EUR 168m in Q3 23 (+9.4% y-o-y to EUR 494m in 9M 23) mainly reflecting the increase of base salaries as a result of the y-o-y general pay rises in FY22/23 in combination with a slightly higher FTE-base y-o-y driven by insourcing of key capabilities to support transformation and growth ambitions.
- **Other operating expenses** (other Opex) were slightly up +2.6% y-o-y to EUR 688m in Q3 23 (+6.6% y-o-y to EUR 2,020m in 9M 23) mainly reflecting commercial activity in the quarter (e.g. 'O_2 Mobile' portfolio) as well as continued technology transformation while energy costs as expected presented a small tailwind to Q3 23. Commercial and non-commercial costs accounted for 66% and 31% of other Opex in Q3 23, respectively. Group fees were EUR 9m in Q3 23 (9M 23 EUR 28m vs EUR 26m in 9M 22).

OIBDA[10] growth improved to **+3.6% y-o-y at EUR 665m** in Q3 23 (+2.7% y-o-y to EUR 1,922m in 9M 23). Improved MSR quality on continued own brand momentum was partly offset by the anticipated and above mentioned Opex increase. **OIBDA**[9] **margin** expanded +0.4 p.p. y-o-y to 31.2% in Q3 23 while contracting -0.6 p.p. y-o-y to 30.4% in 9M 23 with the latter mainly due to the strong growth of broadly margin-neutral hardware revenues in the 9M period.

Depreciation & Amortisation was slightly higher y-o-y (+2.2%) at EUR 1,736m in 9M 23 mainly driven by useful life reduction of PPE due to IT-transformation.

Operating income was EUR +185m (+10.4% y-o-y) in 9M 23.

[7] Mobile service revenue includes base fees and fees paid by the company's customers for the usage of voice, SMS and mobile data services; it also includes access and interconnection fees as well as other charges levied on partners for the use of the company's network.

[8] MTR-cut from EURc 0.55 to EURc 0.40 as of 1 Jan-23.

[9] Operating expenses include impairment losses in accordance with IFRS 9 in the amount of EUR 25m in Q3 23 and EUR 73m in 9M 23 (EUR 22m in Q3 22 and EUR 66m in 9M 22).

[10] Adjusted for exceptional effects. In Q3 23 exceptional effects amounted to EUR -0m of restructuring costs (EUR -1m in 9M 23). In FY22, exceptional effects were restructuring costs of EUR -4m in Q3 22 and EUR -5m in 9M 22 respectively.

Net financial expenses accounted for EUR -59m in 9M 23 compared to EUR -20m in 9M 22.

Income tax was at EUR +5m in 9M 23. As a result, **total profit for the period** improved to EUR +125m in 9M 23, up +17.4% y-o-y.

CapEx[11] was lower -9.7% y-o-y at EUR 312m in Q3 23 (-9.5% y-o-y to EUR 816m in 9M 23) with a **CapEx/Sales ratio** of **14.7%** (12.9% in 9M 23)**.** Telefónica Deutschland continued to make excellent progress with densification and further 5G network roll-out within its normalised C/S envelope. The company is well on track for nationwide 5G coverage latest by YE25.

Operating cash flow (OIBDA minus CapEx[10]) rose by +14.5% y-o-y to EUR 1,105m in 9M 23 as a result of both, strong operating and financial performance as well as Capex normalisation post the successful completion of the Company's 'Investment-for-Growth' programme.

Free cash flow (FCF)[12] amounted to EUR 761m in 9M 23 (EUR 710m in 9M 22). Lease payments for antenna sites and leased lines were EUR 553m in 9M 23 (EUR 520m in 9M 22). This reflects a combination of network densification including new BTS sites to cover white spots and some anticipated y-o-y increases. As a result, **FCFaL** shows the usual back-end loaded profile while improving +9.5% y-o-y to EUR +208m in 9M 23 (EUR 190m in 9M 22). FCFaL adjusted for payments for investments in associated companies[13] amounted to EUR 223m, up +12.6% y-o-y.

Working capital movements were on broadly similar levels as in the prior year, EUR -264m in 9M 23 vs. EUR -239m in 9M 22. The development in 9M 23 was mainly driven by a decrease in capex payables (EUR -148m) as well as other working capital movements of EUR -117m, especially driven by higher pre-payments (EUR -50m) and increase in inventories (EUR -10m).

Consolidated net financial debt[14] as of 30 Sep-23 was EUR 3,535m with the increase vs YE22 mainly reflecting the company's dividend payment of EUR 535m in May-23. Still, leverage ratio of 1.4x[15] remained well below the company's self-defined upper limit of 2.5x; leaving comfortable leverage headroom with regards to the company's BBB-rating with stable outlook by Fitch which has been confirmed on 19 Oct-23.

Financial Outlook FY23

Telefónica Deutschland continued its robust growth path in 9M 23 with its 'value-over-volume' focus underpinning its growth ambitions. Consequently, the company is well on track to achieve its in Jul-23 upgraded FY23 outlook and to meet FCFaL consensus[16] for FY23.

[11] CapEx includes additions to property, plant and equipment and other intangible assets while investments for spectrum licenses and additions from capitalised right-of-use assets are not included.

[12] Free cash flow pre dividends and payments for spectrum (FCF) 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 as well as related interest payments.

[13] +/- Proceeds/payments for investments in associated companies amounted to EUR -15m in 9M 23 and EUR -8m in 9M 22.

[14] Net financial debt includes current and non-current interest-bearing financial assets and interest-bearing liabilities as well as cash and cash equivalents and excludes payables for spectrum.

[15] Leverage ratio is defined as net financial debt divided by OIBDA of the last twelve months adjusted for exceptional effects.

[16] Company compiled consensus, for details please refer to financial results section for Q3 23 of Telefónica Deutschland's website.

	ACTUAL 2022 (1)	OUTLOOK 2023 (2)	ACTUAL 9M 23
Revenues	EUR 8,224m	Upper-range of low single-digit percentage y-o-y growth	EUR 6,323m, +4.8% y-o-y
OIBDA Adj. for except. effects	EUR 2,539m	Upper-range of low single-digit percentage y-o-y growth	EUR 1,922m, +2.7% y-o-y
CapEx to Sales Ratio	14.7%	Around 14 %	12.9%

(1) Revenues and OIBDA include non-recurrent special factors in the amount of EUR +26m million in Q4 22.
(2) As updated in Jul-23 and unchanged incl. regulatory headwinds of ca. EUR -50m to -60m at revenue level and ca. EUR -10m to -15m at OIBDA level in FY23.

Link to detailed Data Tables

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