



Deutschland

Q2 2016 preliminary results

Telefónica Deutschland
Investor Relations
27 July 2016

Public – Nicht vertraulich



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H1-2016: Maintaining momentum in dynamic market; providing mid-term dividend outlook

MSR
-1.5%
y-o-y

- Market environment increasingly dynamic across segments
- Reiterating MSR outlook but narrowing range to 'slightly negative'
- Traffic statistics strong: Focus on 4G upselling to existing customer base

OIBDA¹
+3.5%
y-o-y

- Solid OIBDA growth on back of successful synergy capture; reiterating full-year outlook
- Almost EUR 100m in Opex & revenue synergies in H1; incremental savings in H2
- On track to achieve >50% of total targeted OpCF synergies of EUR 800m for 2016

Dividend proposal 2016
EUR 0.25/share

- Adjusting Capex outlook to 'mid to high single digit % growth'
- Improving OpCF; strong FCF generation potential
- Annual dividend growth over 3 years, starting with EUR 0.25 / share for financial year 2016



**Keep the
Momentum**



**Integrate
quickly**

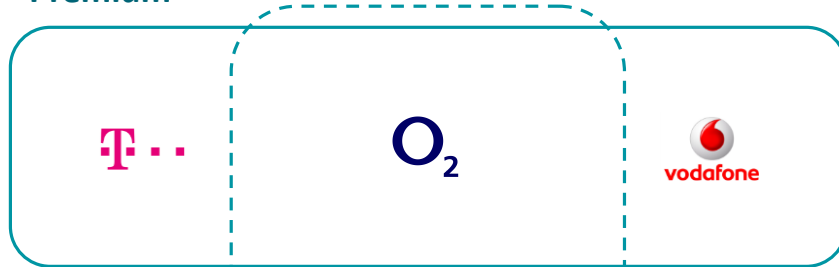


**Transform
the company**

¹ Excluding exceptional and special effects. As of 30 June 2016 exceptional effects include restructuring expenses amounting to EUR 37 million and the capital gain from the sale of passive tower infrastructure to Telxius amounting to EUR 352 million, while in the same period of 2015 a one-off gain from the sale of yourfone GmbH was registered. As of 30 June 2016 special effects consist of the Telxius deal's OIBDA impact (EUR -6 million) resulting primarily from higher operating lease expenses starting in May 2016

Market environment increasingly dynamic across all segments

Premium



Non-premium: Own secondary brands



Non-premium: Partner brands



Environment



Premium: 'More4more' constructive

- Refocus on premium postpaid
- Investment post migration
- Stimulate data growth
- 4G in focus



Non-premium: Strong competition

- Finalising future brand portfolio
 - Rebranding Blau
 - Relaunch of BASE as online-only value proposition
 - Migration of simyo to Blau
 - Maintaining ethnic brands
- Multi-channel strategy with extensive partnerships

Developing our core business: Brand building, retention and added-value services in focus

Building a premium brand through added-value services



connect



sky

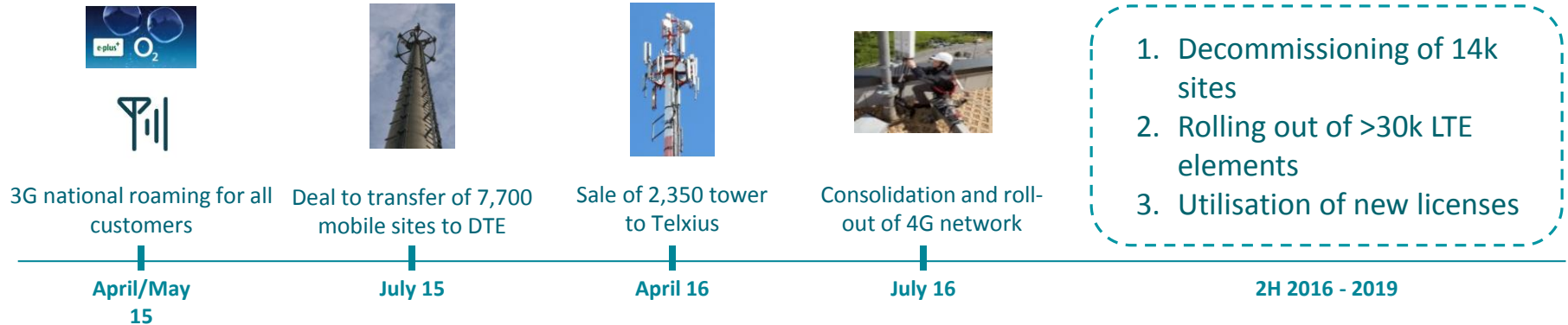


- **O₂ campaigns:** Focus on churn-reduction and 4G upselling
- **O₂ store relaunches:** Flagship store opening in Frankfurt
- **Continued success with customer service awards**
- **Strong result in connect fixed-line test**
- **Stepping up investment in value-added services**
 - **O₂ Banking update:** Launching Germany's first mobile-only bank account
 - Fully enabled bank account incl. credit via free app
 - Data benefits in place of interest
 - **Cooperation with Sky:** Movies & more
 - Unbundled exclusive access to content
 - Discounted sport offering, e.g. Bundesliga & Champions League
 - **O₂ TV & Video App:** Driving data usage
 - Free TV & Pay TV options
 - Increased data usage and driver for LTE and VDSL

Building the future: The roadmap to 4G integration

Network integration timeline

Next steps: Workstreams



TELXIUS Update tower sale

- Cash purchase price of EUR 587 million
- Net capital gain of EUR 352 million
- Proceeds support financial flexibility and reinvestment into business



4.5G trial

- 4.5 G carrier aggregation trial in Munich
 - Partnering with Huawei
 - Up to 1.2 Gbps in testlab
 - Up to 400 Mbps real life

Successful integration milestones reached – Shift to transformation



Integration

- **Leaver programme** ✓
 - Execution of wave 2 of the leaver programme
 - Clarity for 500 employees
- **IT Outsourcing to Atos** ✓
 - Service operations moved on 1 July
 - Outsourcing only service operations
- **Unified call centre model** ✓
 - Insourcing of customer service
 - Consolidation of business support systems
- **Postpaid customer migration** ✓
 - Consolidation of IT stacks
 - 90% of own premium postpaid base migrated



Transformation

- **Network development**
 - Moving focus from 3G to 4G
 - Start of 4G network integration on 1 July 2016
- **Brand optimisation**
 - Finalising future brand portfolio
 - O₂ as clear premium brand
- **New business areas: ADA and IoT**
 - Finalising internal structures
 - Advanced data analytics (ADA):
Developing business concepts
 - Mobility Insights: Using data analytics to help fight climate change in Nuremberg

Successfully executing overall synergy case

Q2-2016: Solid performance in a more dynamic environment

OIBDA¹
+1.2%
y-o-y

- MSR -1.7% (-1.5% excluding regulatory effects)
- Headwinds from strong partner trading as well as legacy base & regulatory effects
- OIBDA driven by ~EUR 40m Opex & rev-related synergies and transformation Opex

+339k postpaid
+71k prepaid
+2k DSL

- Strong postpaid momentum from partner business
- Prepaid reflecting seasonality
- Positive retail DSL net additions on strong VDSL demand

Outlook
update

- Reiterating MSR outlook but narrowing outlook range to 'slightly negative'
- Reiterating OIBDA outlook
- Adjusting Capex outlook to 'mid to high single-digit % growth' driven by more efficient Capex spend & network roll-out phasing

Dividend
guidance

- Improving OpCF on back of stable OIBDA and lower Capex outlook
- Annual dividend growth over 3 years, starting with of EUR 0.25 per share 2016
- Financial flexibility enhanced by tower transaction with capital gain of EUR 352 million

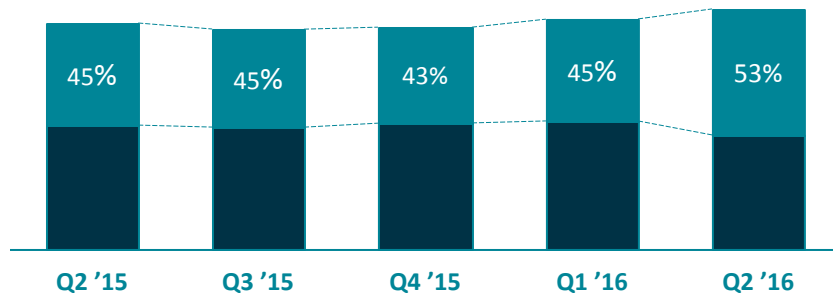
¹ Excluding exceptional and special effects. As of 30 June 2016 exceptional effects include restructuring expenses amounting to EUR 37 million and the capital gain from the sale of passive tower infrastructure to Telxius amounting to EUR 352 million, while in the same period of 2015 a one-off gain from the sale of yourfone GmbH was registered. As of 30 June 2016 special effects consist of the Telxius deal's OIBDA impact (EUR -6 million) resulting primarily from higher operating lease expenses starting in May 2016

Partner trading accelerates on back of more aggressive pricing in non-premium

Partner trading accelerating

PO gross adds (abs)

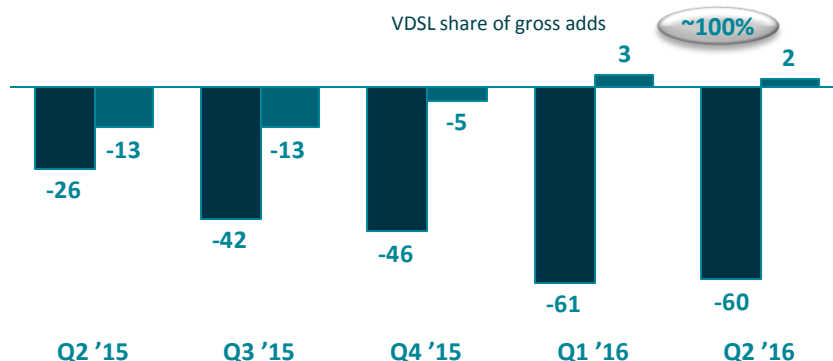
GA partner brands GA retail brands



VDSL drives fixed trading

Net adds (in thousand)

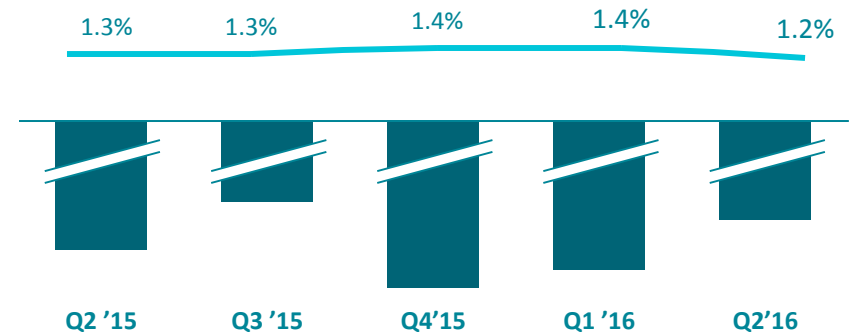
DSL wholesale DSL retail



Successful retention focus

PO churn

Churn retail brands O₂ PO churn (%)

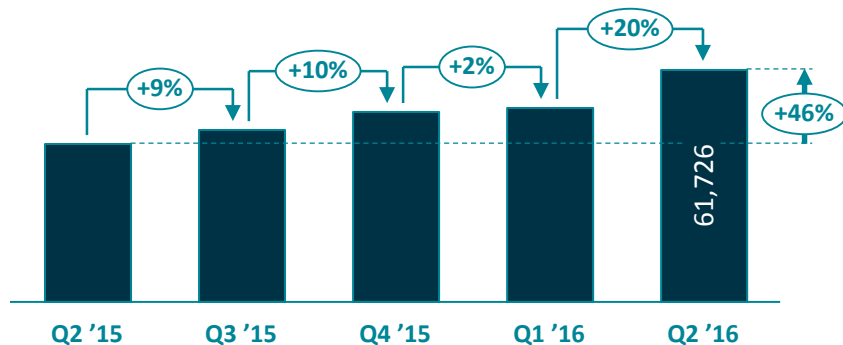


- Partner trading accelerating to 53% of gross adds as a result of more aggressive pricing in non-premium
- Premium retail churn continues to fall due to successful retention efforts
- 2k retail net adds show good traction in broadband driven by VDSL

Strong increase in data traffic drives LTE customer base development

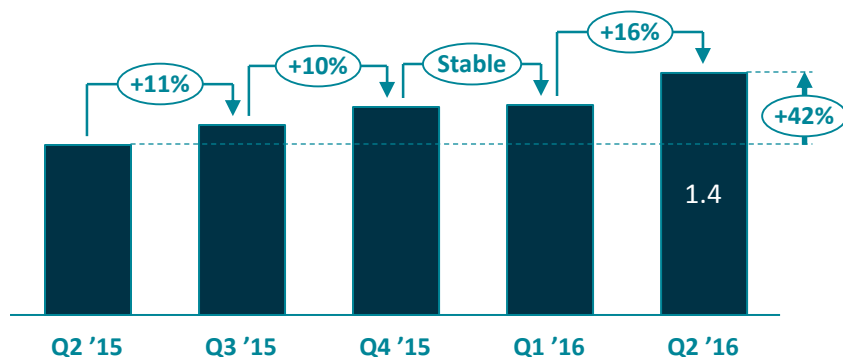
Data traffic picking up again

Traffic (TB/quarter)



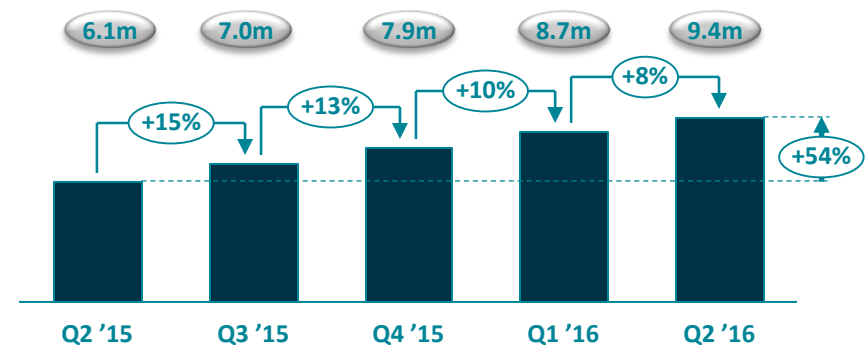
Strong usage among LTE customers

Average data usage for O₂ consumer LTE customers¹ (GB)



Significant growth in LTE customer base

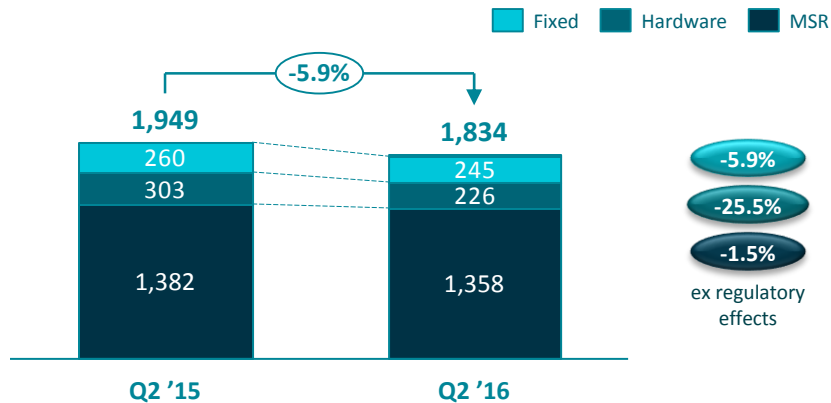
LTE customers (million)



- Data traffic up 20% q-o-q driven by music and video streaming
- Average data usage for LTE customers up 16% q-o-q to 1.4 GB
- LTE customer base grows to 9.4m, up 8% q-o-q and >50% y-o-y

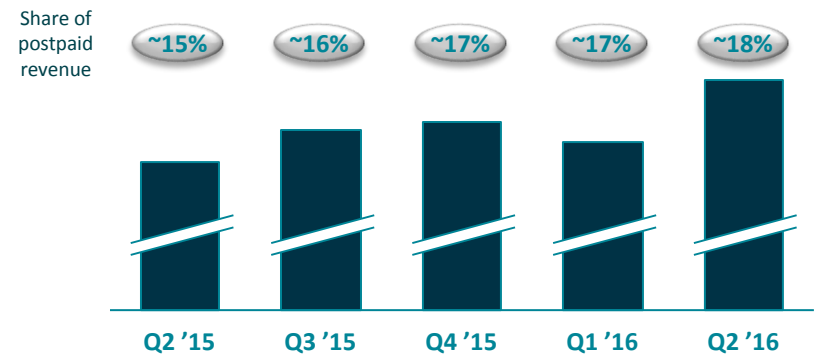
Competitive dynamics impact MSR; hardware replacement cycles lengthening

Revenue structure (in EUR m)

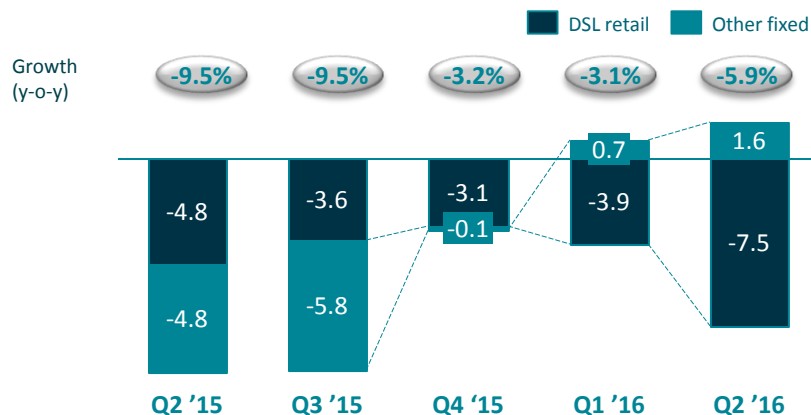


Partner share of postpaid MSR growing

MSR from partner business (in EUR m)



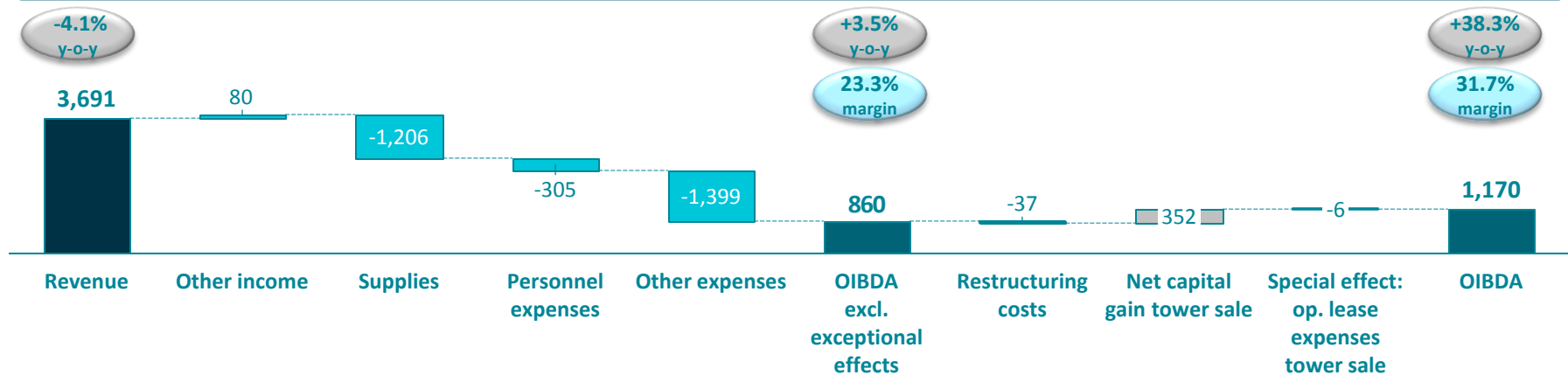
Fixed revenue y-o-y (in %)



- Hardware revenues continue to fall as a result of lengthening handset replacement cycles
- Partner share of postpaid MSR gradually increasing to ~18%
- DSL retail revenue driven by phasing of promotional effects

OIBDA driven by synergy capture and transformation OPEX effects

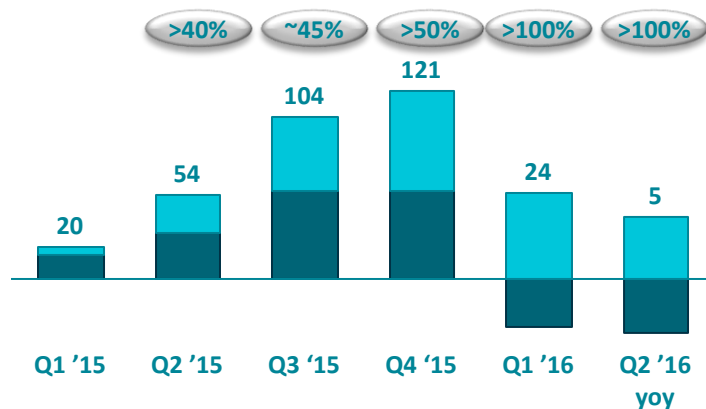
Structure of OIBDA for January to June 2016 (in EUR m)



Synergies driving OIBDA growth

OIBDA growth (y-o-y in EUR m)

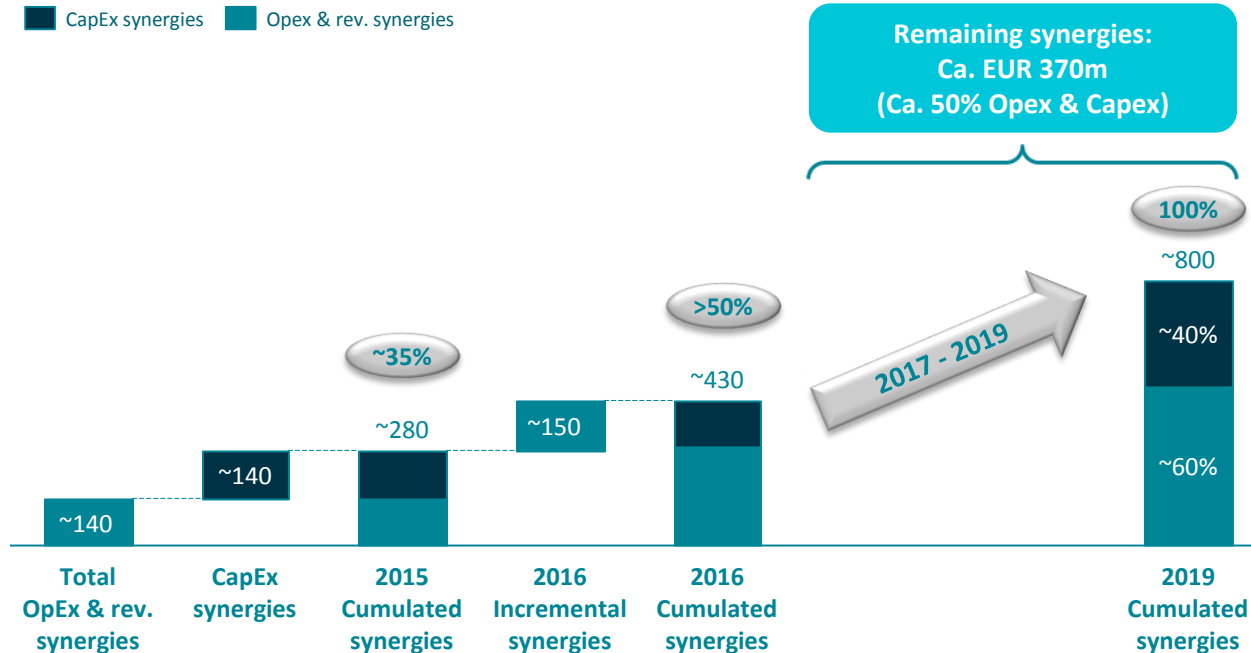
Share of synergies



- OIBDA driven by roll-over synergy effects; incremental savings expected in H2
- Transformation OPEX effects peaking in Q2
- Tower effects: EUR 352m net capital gain and EUR 6m Opex (May / June)

Continued successful execution on synergies: Postpaid customer migration almost completed

Synergy case 2015 - 2019 (EUR m)



- Successfully executing on all initiatives: PO customer migration almost completed
- Total target of EUR 800m OpCF synergies by 2019 unchanged
- Expecting to reach >50% of total target or ~EUR 430m by year-end 2016

Larger initiatives in 2016

Network integration

Brand & customer migration
IT transformation

Ongoing workstreams from 2015

Leaver programme
Total target ~1,600 FTEs

Shop footprint
Total target ~600 shops (-30%)

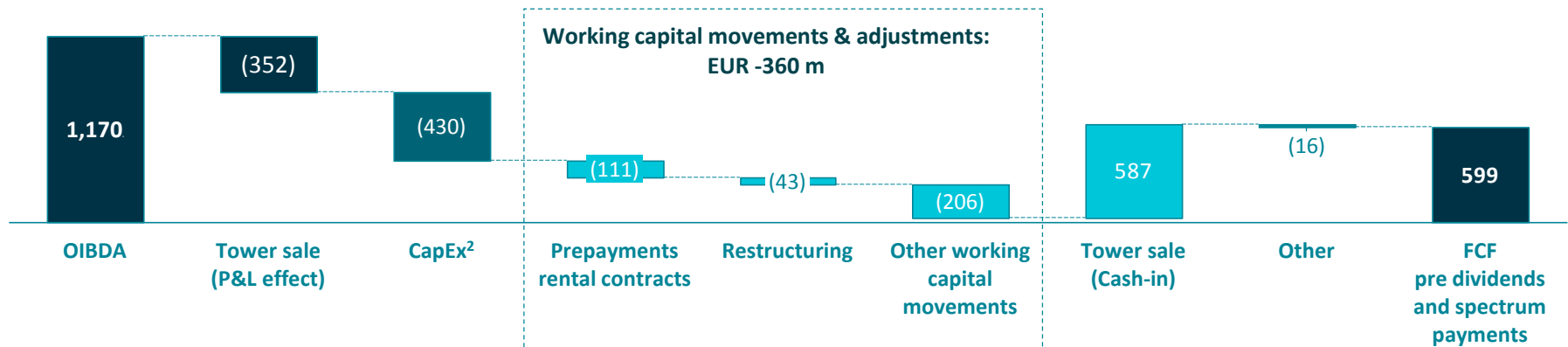
Facilities consolidation
Total target ~100k sqm (-50%)

Customer Service reorganisation & digitalisation

Simplification

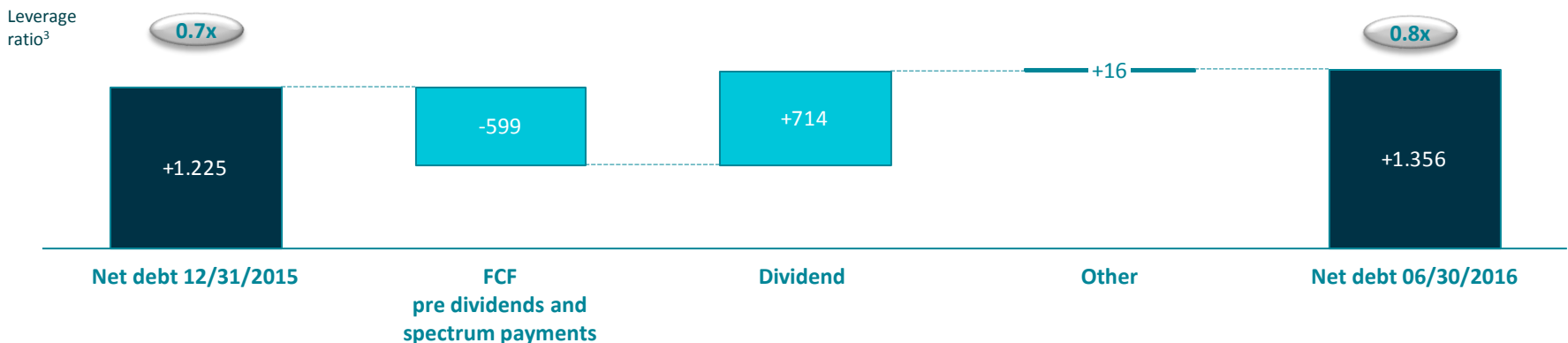
FCF driven by tower sale cash

Evolution of Free Cash Flow (FCF)¹ YTD June 2016 (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

Evolution of Net Debt² (y-o-y in EUR m) – Leverage ratio³ remains stable



² Excluding capitalised costs on borrowed capital in the first six months of 2016 for investments in spectrum in June 2015

³ For definition of net debt & leverage ratio please refer to Q2 2016 earnings release

Reiterating MSR and OIBDA, but lowering Capex outlook

	Baseline 2014 ¹ (EUR m)	Actual 2015 ² (EUR m / y-o-y pct. growth)	Outlook 2016 NEW ² (y-o-y pct. growth)	
MSR	5,528	5,532 / +0.1%	Slightly negative	Reiterating outlook
OIBDA	1,461	1,760 / +20.5%	Low to mid single-digit % growth	Reiterating outlook
CapEx	1,161	1,032 / -11.1%	Mid to high single-digit % growth	Updating outlook

- Reiterating MSR outlook but narrowing range from 'slightly negative to broadly stable' to 'slightly negative'
- Reiterating OIBDA outlook
- Adjusting Capex from '% growth in the low tens' to 'mid to high single-digit % growth' on more efficient Capex spend and LTE roll-out phasing
- Improving OpCF; strong FCF growth potential

>50%
of total target of
EUR 800m to be achieved
in 2016:
~EUR 430m²

Annual dividend growth over next 3 years, starting with proposal of EUR 0.25 in 2016

¹ Baseline figures for 2014 are approximate and the result of the aggregation and then consolidation of Telefónica Deutschland and E-Plus Group financials according to Telefónica Deutschland Group accounting policies. Figures are further adjusted by exceptional effects, such as capital gains or restructuring costs based on estimates made by Telefónica management and resulting in combined figures we believe are more meaningful as a comparable basis. For details refer to additional materials published on our website <https://www.telefonica.de/investor-relations-en.html>

² Expected regulatory effects (e.g. MTR cuts) are included in the outlook. Restructuring costs from the integration of E-Plus Group are excluded from OIBDA and CapEx excludes investments in spectrum.

Main takeaways

- Increased market dynamics; 2016 MSR expected to be slightly negative year-on-year
- Refocusing on the premium segment after customer migration, investing in 4G and stimulating data usage
- Continued OIBDA growth driven by synergy execution
- Lower Capex outlook results in improved operating cashflow
- Committing to mid-term dividend growth over 3 years, starting with EUR 0.25/share in 2016

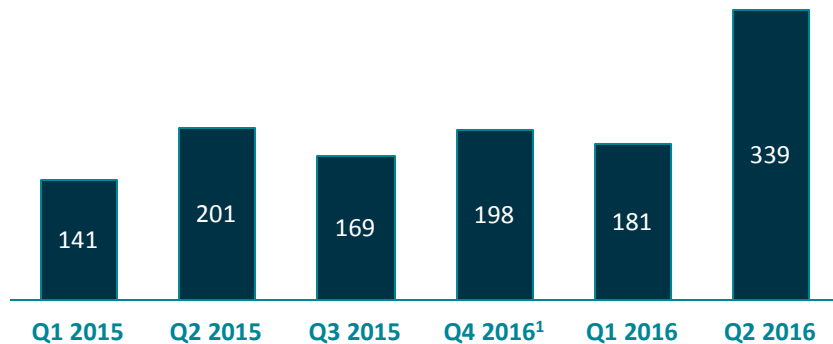
Telefónica Deutschland Q2 2016 preliminary results – Q&A session



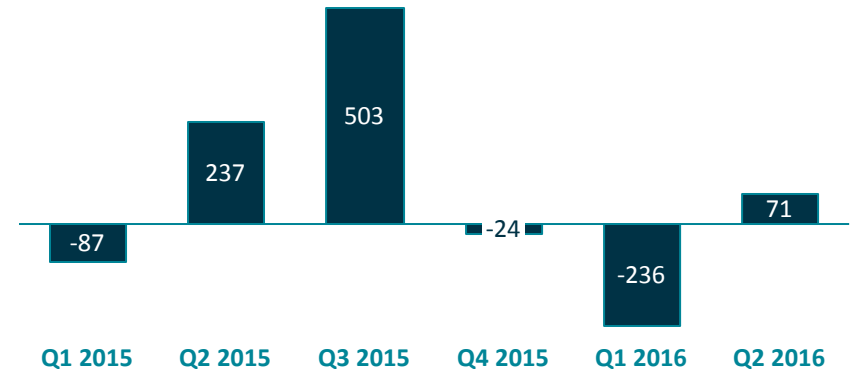
Appendix – KPIs

Mobile KPIs

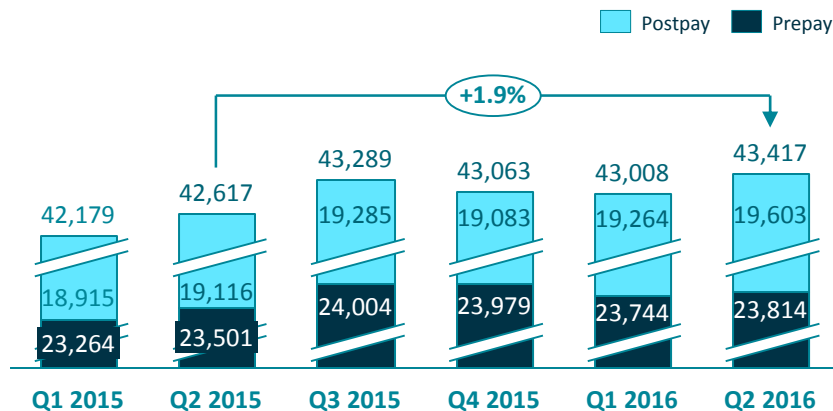
Postpay net adds ('000)



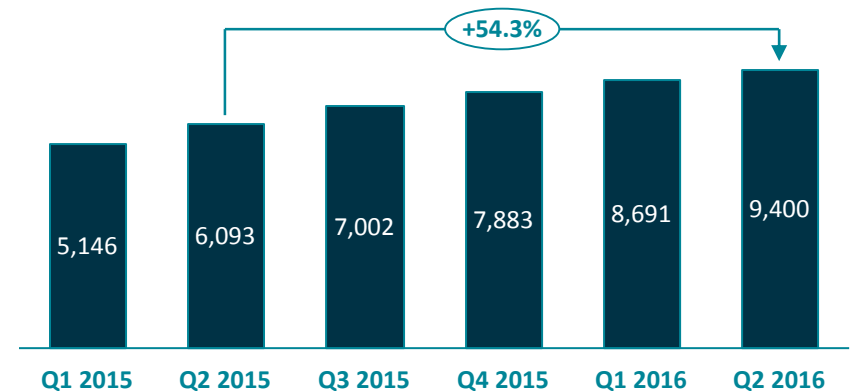
Prepay net adds ('000)



Mobile customer base ('000)



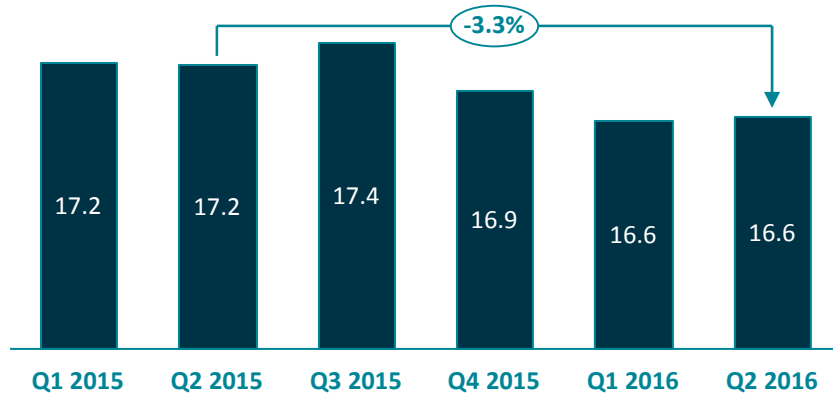
LTE customer base ('000)



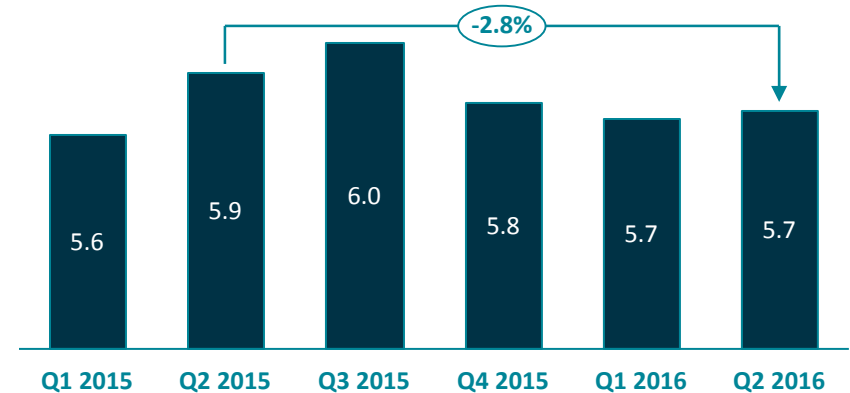
¹ Excluding an impact from a business customer base harmonisation at the E-Plus Group respective negative 202 thousand in reported terms

Mobile KPIs

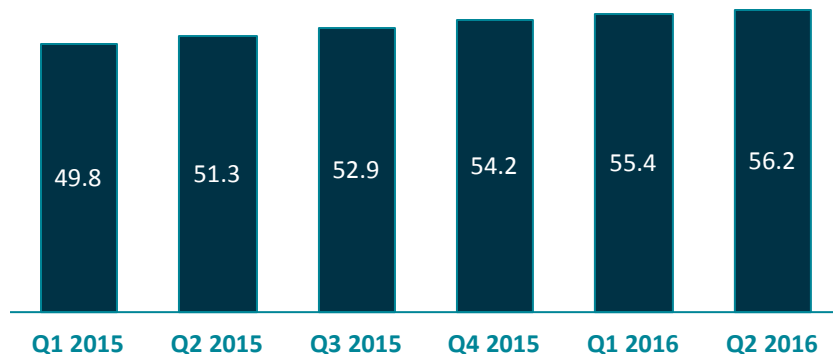
Postpay ARPU (EUR)



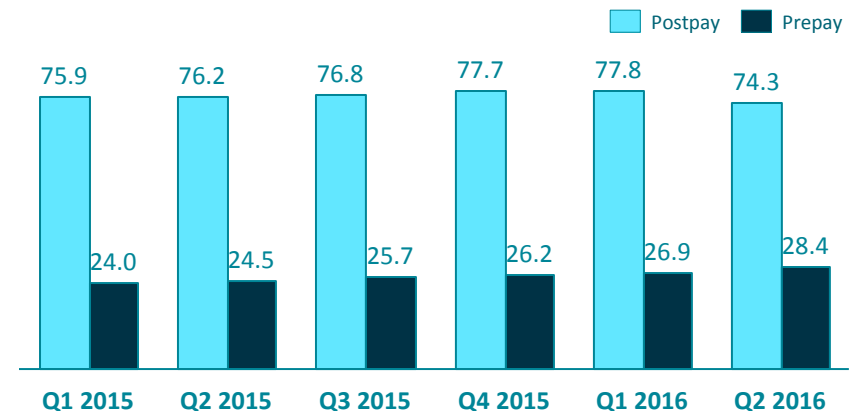
Prepay ARPU (EUR)



Smartphone penetration (%)¹



Smartphone penetration O₂ consumer (%)

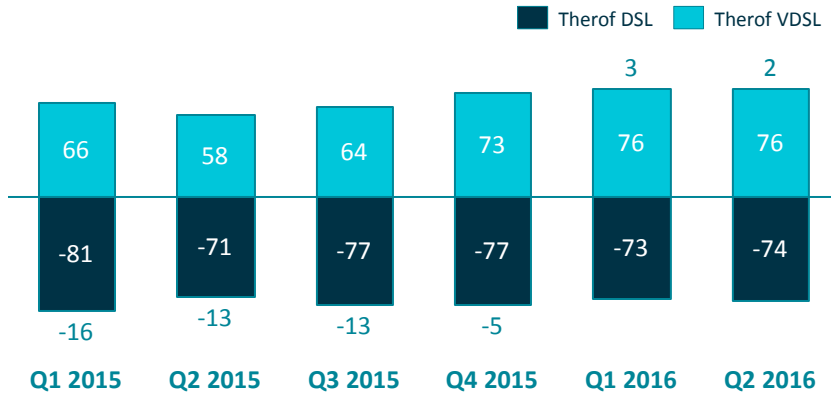


¹ Smartphone penetration is based on the number of customers with a smallscreen tariff (e.g., for smartphones) divided by the total mobile customer base less M2M, less customers with a bigscreen tariff

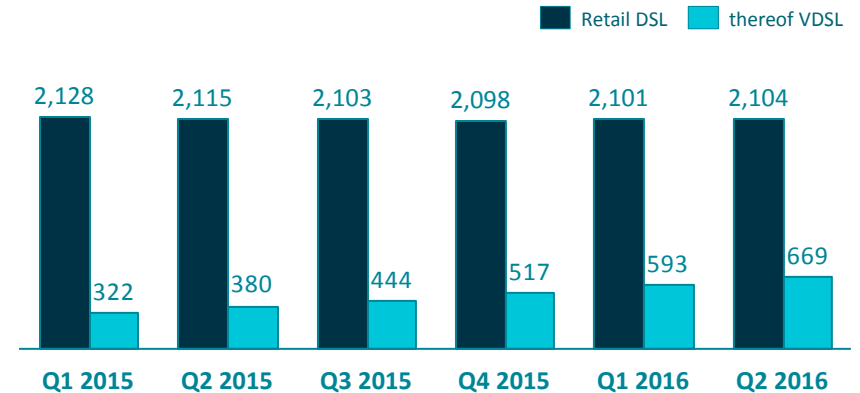
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Fixed-line KPIs

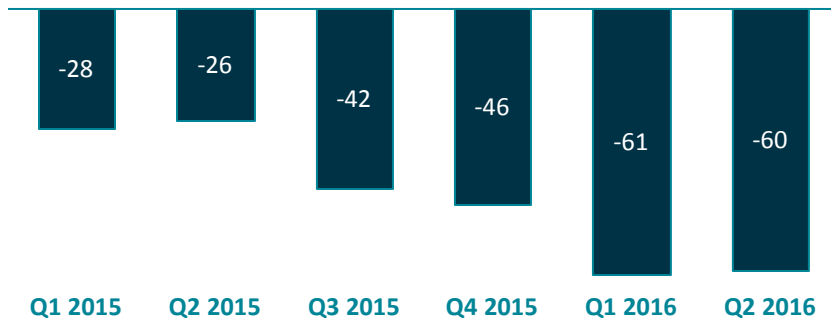
Retail broadband net adds ('000)



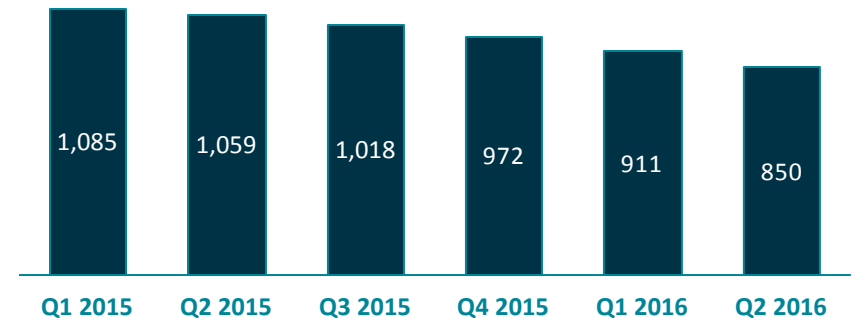
Fixed accesses ('000)



Wholesale net adds ('000)

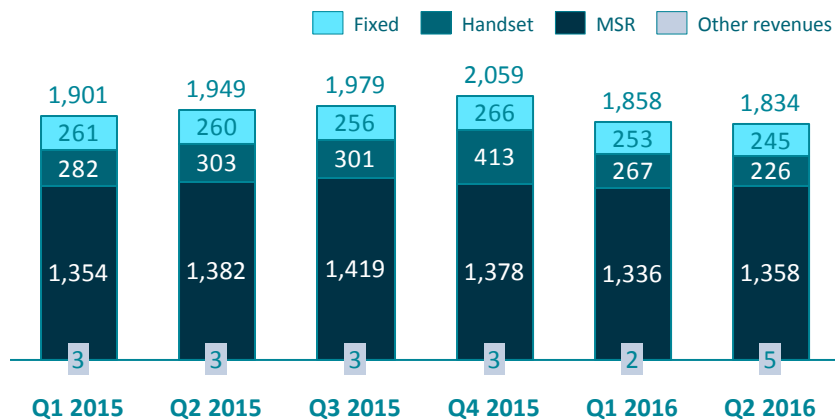


Wholesale accesses ('000)¹

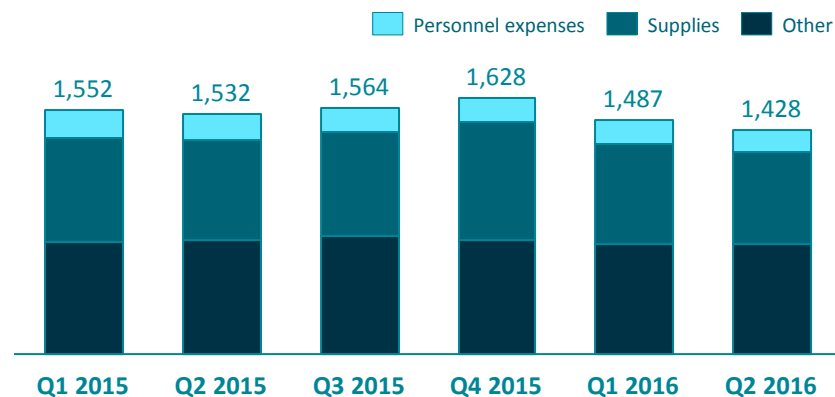


¹ Wholesale accesses incorporate unbundled lines offered to 3rd party operators, including wirelines telephony and high-speed Internet access

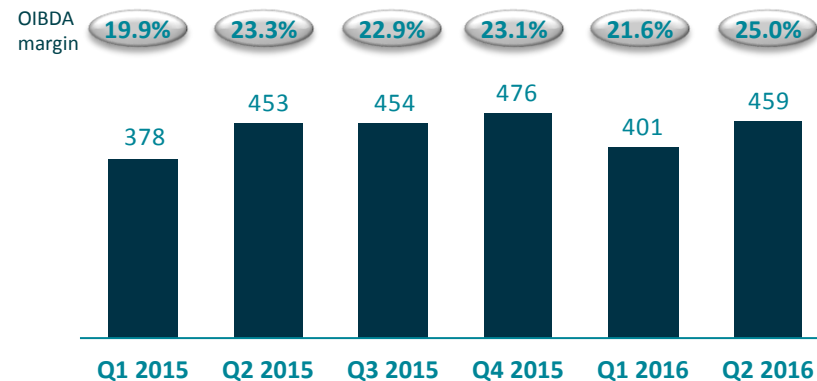
Revenue structure (EUR m)



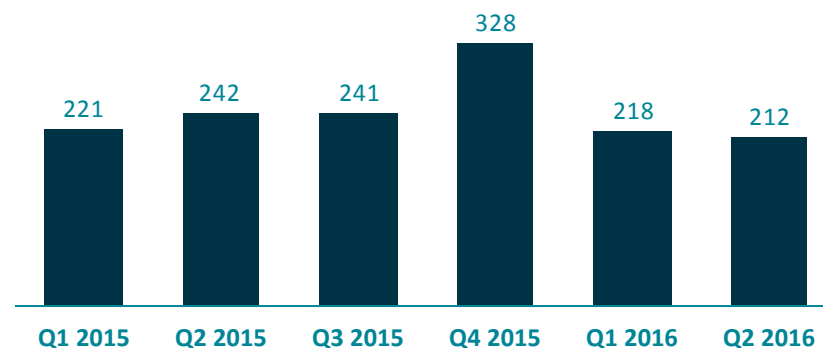
OpEx-Split² (EUR m)



OIBDA (post GF, pre except / EUR m)¹



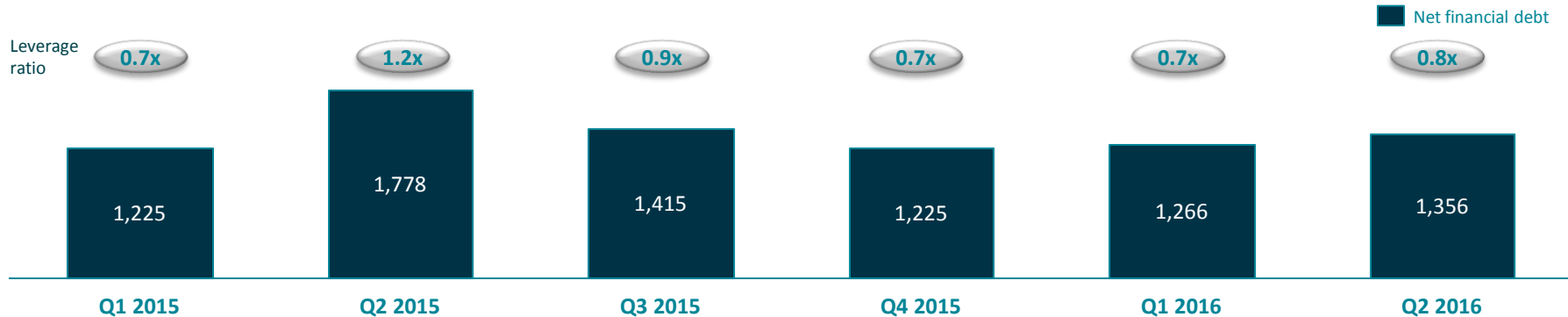
CapEx (EUR m)



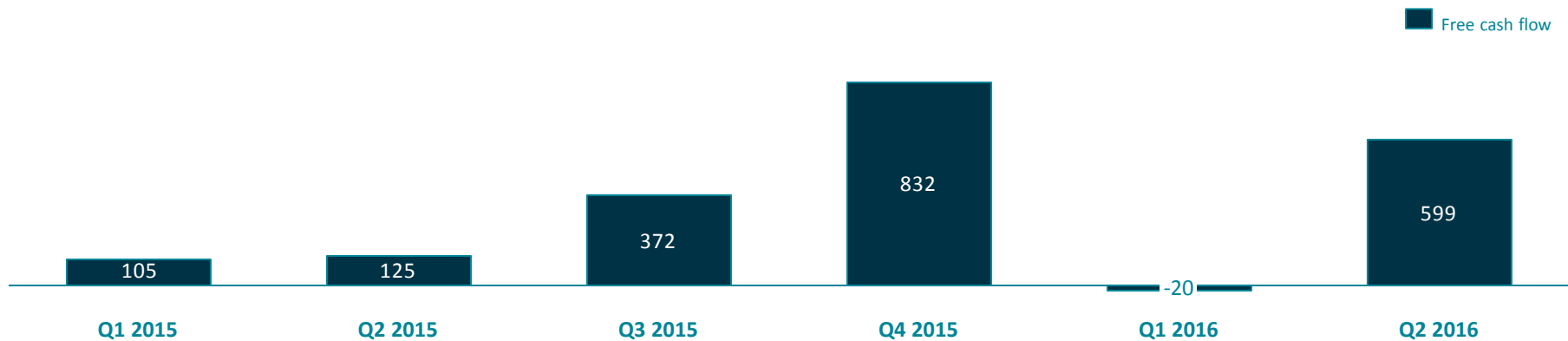
¹ Excluding exceptional & special effects. As of 31 June 2016 these include restructuring expenses of EUR 37 million, a net capital gain from the sale of tower assets to Telxius of EUR 352 million and EUR 6 million of higher operating lease expenses related with the sales of towers while in the same period of 2015 a one-off gain from the sale of yourfone GmbH as well restructuring costs of EUR 3 million were registered

Financials

Net debt and leverage



Free cash flow¹ (cumulative)



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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