Telefónica Deutschland

MUNICH, 27 July 2016

Preliminary results for January to June 2016

In an increasingly dynamic market, Telefónica Deutschland maintains operating momentum, moves from integration to transformation and provides mid-term dividend outlook

- **Reiterating full-year MSR outlook but narrowing range to 'slightly negative': MSR impacted by price competition in non-premium segment as well as regulatory and legacy base effects**
- **OIBDA[1] growth of +3.5% year-on-year (second quarter +1.2%) driven by successful synergy capture and transformation Opex effects; reiterating full-year OIBDA outlook**
- **Operating cash flow synergies of approximately EUR 95 million (second quarter approximately EUR 40 million) primarily from 2015 roll-over effects; postpaid customer migration to be completed soon**
- **Network focus shifts to 4G with start of integration on 1 July 2016**
- **Updating Capex outlook to 'mid to high single-digit % growth' on the back of more efficient Capex spend and network roll-out phasing; improving Operating Cash Flow**
- **Announcing annual dividend growth over next 3 years, starting with a dividend proposal of EUR 0.25/share for the financial year 2016**

Second quarter 2016 operational & financial highlights

- **Mobile postpaid** registered 339 thousand net additions on the back of an increasingly strong performance of partners. The company maintained its focus on retention and customer base management; as a result contract churn[2] improved by 0.1 percentage points year-on-year to 1.6% in the quarter.
- **Mobile prepaid** posted 71 thousand net additions on the back of strong partner trading.
- The **LTE customer base** saw a strong quarter-on-quarter increase again of 8.2% to a total 9.4 million accesses as of the end of June, reflecting the continued high demand from customers for high speed mobile access. **Data usage** for LTE customers in O_2 consumer postpaid continued to benefit from the demand for music and video streaming services and grew 16% quarter-on-quarter to 1.4 GB per month, up 42% year-on-year.

[1] Excluding exceptional and special effects. As of 30 June 2016 exceptional effects include restructuring expenses amounting to EUR 37 million and the net 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 impact which the Telxius deal had on OIBDA (EUR -6 million in the first six months of 2016) resulting primarily from higher operating lease expenses starting in May 2016.
[2] Starting 1 January 2014 M2M SIM-cards are excluded from calculation for postpaid churn and ARPU.

- The **retail DSL** business sustained its trading momentum from the prior quarter with 2 thousand net additions as VDSL broadband demand continues to be solid.
- **Revenues** came to EUR 1,834 million (-5.9% year-on-year), primarily reflecting lower year-on-year mobile services and handset revenues, with the latter driven by a marked slowdown in the demand for handsets.
- **Mobile service revenues** amounted to EUR 1,358 million (-1.7% year-on-year, and -1.5% excluding regulatory effects). Results continue to be affected by the increasingly strong performance of the partner business plus legacy base and regulatory effects. We maintain our focus on retention and the development of the customer base.
- **OIBDA** excluding exceptional and special effects[3] grew 1.2% year-on-year to EUR 459 million as a result of approximately EUR 40 million of savings from synergies as well as the higher year-on-year Opex effects relating to transformation activities.
- **CapEx**[4] totalled EUR 212 million (-12.6% year-on-year), as Capex phasing throughout the year is back-end loaded due to the intensification of network integration efforts in the second half of 2016.
- **Consolidated net financial debt**[5] was EUR 1,356 million at the end of June 2016 and with a leverage of 0.8x, in line with the stated target of at or below 1.0x.

[3] As of 30 June 2016 exceptional effects include restructuring expenses amounting to EUR 37 million and the net 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 impact which the Telxius deal had on OIBDA (EUR -6 million in the first six months of 2016) resulting primarily from higher operating lease expenses starting in May 2016.

[4] Excluding capitalised costs on borrowed capital in the first three months of 2016 for investments in spectrum in June 2015.

[5] 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 the payables for the spectrum auction.

Progress of integration and transformation activities

Telefónica Deutschland progressed further with the integration of E-Plus and is executing according to plan, now moving the focus from integration to transformation. Important milestones reached in 2016 include the second wave of the leaver programme, building the future multi-brand portfolio and optimising the IT and customer service landscape. From 1 July 2016 onwards the network focus has shifted towards the integration of the 4G networks.

- We have now finalised the future target organisation of the company. After constructive negotiations with the workers' council another 500 FTE have been given clarity about their employment situation. Thus, Telefónica Deutschland has already executed more than 80% of the total company target (a reduction of 1,600 FTEs) by 2018
- To further simplify and optimise IT operations, we extended our partnership with Atos Deutschland. Atos has taken over the responsibility of operating our IT systems and our employees from the Service Operations department from 1 July 2016
- We created a new common customer service & sales structure to simplify and combine previously independent customer service entities. As of 1 April 2016, customer service agents in the customer service entities in Hamburg, Bremen and Nuremberg are being transferred to independent subsidiaries within the company
- We have also started to unify our brand and tariff portfolio while maintaining our successful multi-brand strategy to maximise customer reach
    - The company will henceforth focus on the O_2 brand in the premium sector and is making good progress with the transfer of BASE and E-Plus postpaid customers to O_2 which is expected to be completed in the third quarter
    - Over the coming months we will also execute the migration of simyo customers to Blau, our primary value brand in the non-premium market
    - BASE was relaunched as an online only proposition aimed at value-conscious contract customers
- We also pushed ahead with the preparations for the physical integration of the O_2 and E-Plus 4G networks in the second quarter of 2016. With this focus shift from 3G to 4G, we are preparing for the future

- We have also sold our passive tower infrastructure of approximately 2,350 towers to Telxius, Telefónica S.A.'s infrastructure company for a purchase price of EUR 587 million, taking advantage of favourable market conditions for infrastructure assets. The transaction will have no impact on the targeted synergies related to the merger with E-Plus

Commercial update

Teléfonica Deutschland maintained market momentum in an increasingly dynamic market environment while at the same time maintaining a clear focus on retention and the development of the customer base. We continue to improve in customer and network surveys.

- Telefónica Deutschland has reinforced campaigns for existing customers, rewarding them for their loyalty with benefits in mobile and fixed-line
- We also continue to restructure our brand portfolio:
    - Relaunch of BASE in July: The new online proposition targets value-conscious customers
    - Transfer of customers from simyo to Blau as the new core non-premium brand
- O_2 Mobile Banking is Germany's first mobile-only bank, created in cooperation with Munich-based Fidor Bank, and was launched commercially in July. The product offers added-value services to O_2 postpaid customers and supports customer retention
- Moreover, we also signed a cooperation with Sky Deutschland in July 2016, enabling us to offer our customers exclusive, unbundled access to content such as the Bundesliga or Champions League football
- In June Telefónica Deutschland launched the O_2 TV & Video App in cooperation with German TV magazine TV Spielfilm. The app enables O_2 customers to watch over 50 TV stations free in live stream and to receive over 70 stations plus HD options for a monthly fee
- Moreover, Telefónica Deutschland and Huawei are currently running a 4.5G network trial near Munich
- In terms of network tests, we also continue to perform well. In the annual 'connect' fixed-line test Telefónica Deutschland maintained its third rank and significantly narrowed the gap to the number one compared to last year

Updated financial outlook 2016

We reiterate our full-year MSR outlook, but are narrowing the range from 'slightly negative to broadly stable' year-on-year to **'slightly negative'** year-on-year on the back of increased dynamics, especially in the non-premium end of the market. As expected, we also continue to see MSR headwinds from legacy customer base effects and regulatory effects. In contrast, data usage and our LTE customer base continue to grow, and we still expect this data growth to drive an inflection point in our MSR trajectory in the future.

At the same time we are reiterating our OIBDA outlook of 'low to mid single-digit' year-on-year OIBDA percentage growth (post Group fees, before exceptional and special effects[6]). The narrowing of the MSR outlook range has no impact on our OIBDA outlook, as we continue to benefit from the roll-over effects of the successful integration initiatives in 2015, as well as pushing ahead with employee restructuring, customer migration and network integration efforts in 2016. We thus continue to expect incremental Opex and revenue-related in-year savings from synergies of approximately EUR 150 million, as well as a cumulated savings level of approximately EUR 430 million (>50% of total OpCF target of EUR 800 million) by year-end 2016.

We are also adjusting our Capex outlook (excluding spectrum) from 'percentage growth in the low tens to mid' to **'high single-digit growth'** in year-on-year terms in 2016. This is largely the result of more efficient Capex spend as well as phasing topics related to the network integration.

We reiterate our general dividend policy. We view ourselves as a dividend-paying company with the intention to support a high payout ratio in relation to FCF. More specifically, over the next 3 years we intend to grow our dividend annually, starting with a **dividend proposal of EUR 0.25/share in 2016**. The company leverage[7] target of 'at or below 1.0x net debt/OIBDA over the medium term' remains unchanged and will be continually reviewed.

[6] Exceptional and special effects are excluded from our guidance. Exceptional effects include the net capital gain from the sale of Telefónica Deutschland's passive tower infrastructure in Q2 2016. The OIBDA impact resulting primarily from higher operating lease expenses between May and December 2016 will also be treated as a special effect for 2016 and thus excluded from our guidance.

[7] Leverage is defined as net financial debt divided by the OIBDA of the last twelve months before exceptional effects.

Updated financial outlook 2016:

	Base line 2015 (EUR million)	**Updated outlook 2016** (year-on-year)
MSR	5,532	Slightly negative
OIBDA Before special exceptional effects	1,760	Low to mid single-digit % growth
CapEx[8]	1,032	Mid to high single-digit % growth
Dividend[9]	EUR 0.24/share	Proposal: EUR 0.25/share

[8] Excluding investments in spectrum in June 2015 amounting to EUR 1,198m (including capitalised costs on borrowed capital).
[9] Proposal to the Annual General Meeting 2017.

Telefónica Deutschland's operating performance in the first half of 2016

At the end of June 2016 Telefónica Deutschland's **access base** grew by 1.2% year-on-year to **48.6 million** driven by a 1.9% year-on-year increase in the mobile customer base, which stood at 43.4 million.

Mobile postpaid continued to show good momentum in the market with the customer base growing 2.5% year-on-year to 19.6 million accesses at the end of June. The share of total mobile customers was up 0.3 percentage points to 45.2%. The company registered 520 thousand net additions in the first six months of 2016 and 339 thousand in the second quarter, compared to 342 thousand and 201 thousand in the same periods of 2015 respectively. Partner brands showed an increasingly good performance, delivering 49% of postpaid gross additions in the first half of the year (Q2: 53%).

The **mobile prepaid** customer base was up 1.3% year-on-year (23.8 million accesses) while 165 thousand net disconnection were registered for the period January to June 2016 (71 thousand net additions for April to June); this was mainly driven by the seasonal disconnection in the first three months of the year.

Postpaid churn[10] was stable year-on-year at 1.7% in the six months period and even improved slightly by 0.1 percentage points year-on-year to 1.6% in the second quarter. Supported by our continued retention focus, the O_2 consumer brand reported an even lower churn of 1.3% and 1.2% respectively (both down by 0.1 percentage points year-on-year) again.

Smartphone penetration[11] rose 5.0 percentage points year-on-year to 56.2% as of 30 June 2016 and continued to rise across all brands driven by the steady increase of demand for data both in the postpaid and the prepaid customer base; within the O_2 consumer brand smartphone penetration stood at 74.3% as of 30 June 2016.

The **LTE customer base** was up 8.2% quarter-on-quarter to 9.4 million as of 30 June2016, reflecting the continued high demand for high speed mobile access from customers.

The **mobile ARPU** came in at EUR 10.4 in the second quarter (-3.8% year-on-year after -3.3% in Q1) and EUR 10.3 for the first half of 2016. The postpaid ARPU[10] came to EUR 16.6 in the second quarter with the year-on-year decline improving to -3.3% (compared to -3.8% and -4.3% in the previous quarters), reflecting the success of upselling mechanisms in the legacy customer base mix. Prepaid ARPU was EUR 5.7 both for the six months period (-0.8% year-on-year) and the second quarter (-2.7% year-on-year) with a continued high demand for data amongst prepaid customers.

VDSL momentum was strong with 152 thousand net addition until June (76 thousand in both the first and second quarter of 2016), which more than offset DSL disconnection and resulted in 2 thousand positive net additions (6 thousand in the six month period). Consequently, the **total retail DSL customer base** is now stabilising at 2.1 million.

Fixed wholesale accesses continued with their expected decline (122 thousand net disconnections until June thereof 60 thousand in the second quarter), a reflection of the progressive decommissioning of the ULL (unbundled local loop) broadband access infrastructure.

[10] Starting 1 January 2014 M2M SIM-cards are excluded from calculation for postpaid churn and ARPU.
[11] Defined as the number of active mobile data tariffs over total mobile customer base, excluding M2M and data-only accesses.

Telefónica Deutschland

Telefónica Deutschland's financial performance in the first half of 2016

Revenues totalled EUR 3,691 million, lower 4.1% year-on-year (-5.9% year-on-year in the second quarter to EUR 1,834 million) mainly as a result of the performance of mobile service revenues and the handset business.

Mobile service revenues (MSR) declined 1.5% year-on-year for January to June to EUR 2,694 million and -1.7% in the second quarter to EUR 1,358 million (-1.5% excluding regulatory effects). This is a reflection of the increasingly competitive dynamics across segments in German mobile and the associated strength of the partner business, which resulted in a higher share of wholesale revenues. In addition, the company continues to see regulatory headwinds in the form of an MTR cut from EUR 1.72 to 1.66 in December. Customer base and OTT effects also continue to have a decreasing effect, as we focus on the development of our customer base through retention and upselling mechanisms.

Mobile data revenues rose 5.6% year-on-year to EUR 1,478 million for the six months period (+5.8% year-on-year to EUR 749 million in the second quarter) with the share over MSR increasing to 55.1% in the second quarter (up 3.9 percentage points year-on-year). Sustained revenue growth in non-SMS data outweighs the continuous decline in SMS revenues. **Non-SMS data** revenues amounted to EUR 1,124 million (+13.1% year-on-year) for the first half year and EUR 574 million in the second quarter, up +13.6% year-on-year. As a result, share of non-SMS data revenues over total data revenues was up 5.2% year-on-year to 76.7% for April to June.

Handset revenues fell 15.9% year-on-year to EUR 493 million in the first six months (EUR 226 million, -25.5% year-on-year in the second quarter), reflecting longer replacement cycles and handset saturation in the German market in line with broader European markets.

Fixed revenue fell by 4.5% year-on-year in the six months period (EUR 498 million) and by 5.9% year-on-year in the second quarter (EUR 245 million) with continued good traction for VDSL in the retail business. We continued to benefit from spot trading opportunities in the carrier voice business, while wholesale DSL declined in line with expectations. DSL retail revenue contributed -7.5% to the overall quarterly decline on the back of a customer base reduction of 0.5% year-on-year and the phasing of promotional effects.

Other income was EUR 436 million until June with the year-on-year growth mainly driven by the capital gain from the sale of the passive tower infrastructure in the second quarter of 2016.

Operating expenses including restructuring costs of EUR 37 million (14 million in the second quarter) amounted to EUR 2,958 million in the first half year 2016, down 4.2% year-on-year mainly driven by savings from integration projects (EUR 1,448 million for April to June; -5.6% year-on-year). Restructuring costs were mainly related to the leaver programme.

- **Supplies** came to EUR 1,206 million, 7.6% lower year-on-year (578 million, -10.6% year-on-year in the second quarter) mainly on the back of lower hardware costs of sales (42% of supplies vs 45% in the first six months of 2015) and lower connectivity-related cost of sales (49% of supplies).
- **Personnel expenses** totalled EUR 333 million (including restructuring costs of EUR 28 million) for the six months period (EUR 160 million in the second quarter) with a stable year-on-year decline of 3.2% mostly resulting from the successful execution of the first wave of the employee restructuring programme in 2015.
- **Other operating expenses** were down 1.3% year-on-year to EUR 1,418 million in the six months period, including restructuring expenses of EUR 8 million and EUR 6 million from higher operating lease expenses related with the sale of tower assets. In the second quarter other operating expenses amounted to EUR 710 million (down 1.7% year-on-year) with commercial and non-commercial costs making up 60% and 34% respectively. Savings resulted from the 2015 synergy initiatives, but were partly offset by commercial and other investments related to customer and brand migration activities in the first half of 2016.

Operating Income before Depreciation and Amortisation (OIBDA) in the period up to June 2016 benefitted from the net capital gain related to the sale of the Company's passive tower infrastructure in the second quarter of 2016 of EUR 352 million as well as the before-mentioned cost reductions. OIBDA in reported terms amounted to EUR 1,170 million (EUR 791 million for April to June).

Excluding exceptional and special effects[12] OIBDA in the first six month of 2016 grew 3.5% year-on-year to EUR 860 million (EUR 459 million, +1.2% year-on-year in the second quarter). In-year savings from integration activities (OPEX & revenue) amounted to approximately EUR 95 million (approximately EUR 40 million in the second quarter). The OIBDA margin increased by 1.7 percentage points year-on-year to 23.3% in the half year and +1.8% year-on-year to 25.0% for April to June.

Group fees amounted to EUR 26 million in the first six months of 2016 and EUR 13 million in the second quarter of the year.

Depreciation & Amortisation amounted to EUR 1,069 million in the first six month of 2016, a 3.5% year-on-year increase compared to the same period of 2015 (EUR 1,033 million), mainly resulting from higher software investments due to IT integration measures.

[12] As of 30 June 2016 exceptional effects include restructuring expenses amounting to EUR 37 million and the net 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 impact which the Telxius deal had on OIBDA (EUR -6 million in the first six months of 2016) resulting primarily from higher operating lease expenses starting in May 2016.

Operating income for January to June 2016 was positive in the amount of EUR 100 million on the back of the net capital gain from the sale of tower assets. However, depreciation & amortisation charges still exceed OIBDA excluding exceptional and special effects.

The net financial result for the six months period was negative in the amount of EUR 18 million mainly resulting from various financing activities including the bonds issued in November 2013 and February 2014, a promissory note executed in March 2015 as well as interest expenses from finance lease obligations.

The Company did not report **income tax expense** for January to June.

The result for the first half of 2016 came to EUR 83 million.

CapEx was EUR 430 million (-7.1% year-on-year) in the first half of 2016 and EUR 212 million in the second quarter of 2016 (-12.6% year-on-year) on the back of back-end loaded Capex phasing through the year.

Operating cash flow (OIBDA minus CapEx)[13] for the first six months of 2016 was EUR 740 million. Excluding exceptional and special effects[14], operating cash flow was EUR 430 million, up 16.9% year-on-year.

Free Cash Flow (FCF)[15] for the first six months of 2016 reached EUR 599 million and includes the proceeds from the sale of passive tower infrastructure to Telxius of EUR 587 million.

Working capital movements of EUR 360 million were mainly driven by prepayments for rental contracts of EUR 111 million, restructuring expenses amounting to EUR 43 million as well as other working capital movements which include silent factoring transactions for O2 myHandy receivables.

Consolidated net financial debt[16] stood at EUR 1,356 million at the end of June 2016, maintaining a leverage ratio of 0.8x.The slight increase compared to year end 2015 mainly results from the EUR 714 million dividend payment for the financial year 2015 paid in May 2016, partially offset by the proceeds from the sale of passive tower infrastructure to Telxius amounting to EUR 587 million.

[13] Excluding capitalised costs on borrowed capital in the first three months of 2016 for investments in spectrum in June 2015

[14] As of 30 June 2016 exceptional effects include restructuring expenses amounting to EUR 37 million and the net 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 impact which the Telxius deal had on OIBDA (EUR -6 million in the first six months of 2016) resulting primarily from higher operating lease expenses starting in May 2016.

[15] Free cash flow pre dividends and payments for spectrum as well as pre-acquisition of E-Plus (FCF) is defined as the sum of cash flow from operating activities and cash flow from investing activities.

[16] 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 the spectrum auction.

APPENDIX – DATA TABLES

TELEFÓNICA DEUTSCHLAND GROUP

SELECTED CONSOLIDATED FINANCIAL DATA

Unaudited

	April 1 to June 30			January 1 to June 30		
(Euros in millions)	2016	2015	% Chg	2016	2015	% Chg
Revenues	1,834	1,949	(5.9)	3,691	3,849	(4.1)
Operating income before depreciation and amortisation (OIBDA), before exceptional effects (1) and before special effects (2)	459	453	1.2	860	831	3.5
OIBDA before exceptional effects and special effects-margin	*25.0%*	*23.3%*	*1.8%-p.*	*23.3%*	*21.6%*	*1.7%-p.*
Special effects (2)	(6)	–	–	(6)	–	–
Operating income before depreciation and amortisation (OIBDA) and before exceptional effects (1)	453	453	(0.1)	854	831	2.8
OIBDA before exceptional effects-margin	*24.7%*	*23.3%*	*1.4%-p.*	*23.1%*	*21.6%*	*1.6%-p.*
Exceptional effects (1)	338	(3)	(>100,0)	316	15	>100,0
Operating income before depreciation and amortisation (OIBDA)	791	450	75.7	1,170	845	38.3
OIBDA margin	*43.1%*	*23.1%*	*20.0%-p.*	*31.7%*	*22.0%*	*9.7%-p.*
Group fees	13	11	20.0	26	23	12.7
Operating income before depreciation and amortisation (OIBDA) and before group fees	804	461	74.4	1,196	869	37.7
OIBDA before group fees margin	*43.8%*	*23.6%*	*20.2%-p.*	*32.4%*	*22.6%*	*9.8%-p.*
Operating income	262	(54)	(>100,0)	100	(188)	(>100,0)
Total profit (loss) for the period	252	(68)	(>100,0)	83	(213)	(>100,0)
Basic earnings per share (in euros) (3)	0.08	(0.02)	(>100,0)	0.03	(0.07)	(>100,0)
CapEx (4)	(212)	(242)	(12.6)	(430)	(463)	(7.1)
Operating cash flow (OIBDA-CapEx) (4)	579	208	>100,0	740	383	93.3
Free cash flow pre dividends and payments for spectrum (5) and pre-acquisition of E-Plus net of cash acquired	619	(2)	(>100,0)	599	102	>100,0
Free cash flow pre dividends and payments for spectrum (5)	619	20	>100,0	599	125	>100,0

(1) Exceptional effects as of 30 June 2016 include restructuring expenses amounting to EUR 37m and the net capital gain from the sale of passive tower infrastructure to Telxius amounting to EUR 352m.

(2) Special effects as of 30 June 2016 consist of the Telxius deal's OIBDA impact resulting primarily from higher operating lease expenses starting in May 2016.

(3) Basic earnings per share are calculated by dividing profit (loss) after taxes for the period by the weighted average number of ordinary shares of 2,975m for the years 2016 and 2015.

(4) Excluding investments in spectrum in June 2015 and excluding capitalised costs on borrowed capital.

(5) Free cash flow pre dividends and payments for spectrum is defined as the sum of the cash flows from operating activities and the cash flows from investing activities and does not contain payments for investments in spectrum.

Note:
OIBDA margin, OIBDA before group fees margin and OIBDA before exceptional effects-margin are calculated as percentage of total revenues, respectively.

Telefónica Deutschland

ACCESSES

Unaudited

(in thousands)	2016 Q1	2016 Q2	2015 Q1	2015 Q2	2015 Q3	2015 Q4
Final clients accesses	47,342	47,754	46,573	46,981	47,627	47,391
Fixed telephony accesses	2,003	2,007	2,022	2,010	2,000	1,998
Internet and data accesses	2,331	2,330	2,372	2,355	2,339	2,331
Narrowband	229	226	243	240	236	233
Broadband	2,101	2,104	2,128	2,115	2,103	2,098
thereof VDSL	593	669	*322*	*380*	*444*	*517*
Mobile accesses	43,008	43,417	42,179	42,617	43,289	43,063
Prepaid	23,744	23,814	23,264	23,501	24,004	23,979
Postpaid	19,264	19,603	18,915	19,116	19,285	19,083
thereof M2M	*682*	*704*	*443*	*506*	*571*	*632*
Postpaid (%)	44.8%	45.2%	44.8%	44.9%	44.5%	44.3%
Smartphone penetration (%) (1)	55.4%	56.2%	49.8%	51.3%	52.9%	54.2%
LTE customers (2)	8,691	9,400	5,146	6,093	7,002	7,883
Wholesale accesses (3)	911	850	1,085	1,059	1,018	972
Total accesses	**48,252**	**48,605**	**47,658**	**48,041**	**48,645**	**48,363**

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

(2) LTE customer defined customer with LTE enabled handset & LTE tariff

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

TELEFÓNICA DEUTSCHLAND GROUP

SELECTED OPERATIONAL DATA

Unaudited

	2016 Q1	2016 Q2	2015 Q1	2015 Q2	2015 Q3	2015 Q4
ARPU (in euros) (1)	10.3	10.4	10.6	10.8	10.9	10.5
Prepaid	5.7	5.7	5.6	5.9	6.0	5.8
Postpaid excl. M2M	16.6	16.6	17.2	17.2	17.4	16.9
Data ARPU (in euros)	5.6	5.8	5.5	5.6	5.6	5.5
% non-SMS over data revenues (2)	75.4%	76.7%	70.5%	71.5%	71.9%	72.5%
Voice Traffic (m min) (3)	15,490	16,207	15,837	15,492	15,487	15,879
Data Traffic (TB) (4)	51,599	61,726	40,172	42,255	45,898	50,501
Churn (%)	2.5%	2.1%	2.4%	2.1%	2.1%	2.8%
Postpaid churn (%) excl. M2M	1.8%	1.6%	1.7%	1.7%	1.7%	2.4%

Notes:

(1) ARPU (average revenue per user) is calculated as monthly average of the quarter.

(2) % non-SMS over data revenues in relation to the total data revenues.

(3) Voice Traffic is defined as minutes used by the company's customers for both outbound and inbound calls. Only outbound on-net traffic is included, inclusive of any promotional traffic. Traffic not associated with the company's mobile customers (roaming-in, MVNOs, interconnection of third parties and other business lines) is excluded. Traffic volume has not been rounded.

(4) Data traffic is defined as Terabytes used by the company's customers for uploads and downloads (1TByte = 10^12 bytes). Promotional traffic is included. Traffic not associated with the company's mobile customers (roaming-in, MVNOs, interconnection of third parties and other business lines) is also included. Traffic volume has not been rounded.

TELEFÓNICA DEUTSCHLAND GROUP

CONSOLIDATED INCOME STATEMENT

Unaudited

(Euros in millions)	April 1 to June 30 2016	April 1 to June 30 2015	April 1 to June 30 Change	April 1 to June 30 % Chg	January 1 to June 30 2016	January 1 to June 30 2015	January 1 to June 30 Change	January 1 to June 30 % Chg
Revenues	1,834	1,949	(115)	(5.9)	3,691	3,849	(158)	(4.1)
Other income	405	36	369	>100,0	436	83	353	>100,0
Operating expenses	(1,448)	(1,535)	87	(5.6)	(2,958)	(3,087)	129	(4.2)
Supplies	(578)	(646)	69	(10.6)	(1,206)	(1,306)	99	(7.6)
Personnel expenses	(160)	(166)	6	(3.4)	(333)	(345)	11	(3.2)
Other expenses	(710)	(723)	12	(1.7)	(1,418)	(1,436)	19	(1.3)
Operating income before depreciation and amortization (OIBDA)	**791**	**450**	**341**	**75.7**	**1,170**	**845**	**324**	**38.3**
OIBDA margin	43.1%	23.1%		*20.0%-p.*	31.7%	22.0%		*9.7%-p.*
Depreciation and amortisation	(529)	(505)	(25)	4.9	(1,069)	(1,033)	(36)	3.5
Operating income	**262**	**(54)**	**316**	**(>100,0)**	**100**	**(188)**	**288**	**(>100,0)**
Net financial income (expense)	**(9)**	**(14)**	**5**	**(33.9)**	**(18)**	**(25)**	**8**	**(30.5)**
Profit (loss) before tax for the period	**252**	**(68)**	**321**	**(>100,0)**	**83**	**(213)**	**296**	**(>100,0)**
Income tax	(0)	0	(0)	(>100,0)	0	0	(0)	(80.8)
Total profit for the period	**252**	**(68)**	**321**	**(>100,0)**	**83**	**(213)**	**296**	**(>100,0)**
Number of shares in millions as of end of period date	**2,975**	**2,975**	**–**	**–**	**2,975**	**2,975**	**–**	**–**
Basic earnings per share (in euros) (1)	**0.08**	**(0.02)**	**0.11**	**(>100,0)**	**0.03**	**(0.07)**	**0.10**	**(>100,0)**

(1) Basic earnings per share are calculated by dividing profit (loss) after taxes for the period by the weighted average number of ordinary shares of 2,975m for the years 2016 and 2015.

TELEFÓNICA DEUTSCHLAND GROUP

REVENUE BREAKDOWN

Unaudited

(Euros in millions)	April 1 to June 30 2016	April 1 to June 30 2015	April 1 to June 30 Change	April 1 to June 30 % Change	January 1 to June 30 2016	January 1 to June 30 2015	January 1 to June 30 Change	January 1 to June 30 % Change
Revenues	**1,834**	**1,949**	**(115)**	**(5.9)**	**3,691**	**3,849**	**(158)**	**(4.1)**
Mobile business	**1,584**	**1,685**	**(101)**	**(6.0)**	**3,187**	**3,321**	**(134)**	**(4.0)**
Mobile service revenues	1,358	1,382	(24)	(1.7)	2,694	2,735	(41)	(1.5)
Handset revenues	226	303	(77)	(25.5)	493	586	(93)	(15.9)
Fixed business	**245**	**260**	**(15)**	**(5.9)**	**498**	**521**	**(24)**	**(4.5)**
Other revenues	**5**	**3**	**1**	**39.5**	**6**	**7**	**(0)**	**(5.5)**

TELEFÓNICA DEUTSCHLAND GROUP

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

Unaudited

(Euros in millions)	As of 30 June 2016	As of 31 December 2015	Change	% Change
NON-CURRENT ASSETS	**13,567**	**14,406**	**(839)**	**(5.8)**
Goodwill	1,932	1,955	(23)	(1.2)
Other intangible assets	6,614	7,059	(444)	(6.3)
Property, plant and equipment	4,193	4,507	(314)	(7.0)
Trade and other receivables	132	157	(25)	(15.7)
Other financial assets	63	63	0	0.7
Other non-financial assets	127	160	(33)	(20.7)
Deferred tax assets	505	505	–	–
CURRENT ASSETS	**2,145**	**2,248**	**(103)**	**(4.6)**
Inventories	76	123	(47)	(38.5)
Trade and other receivables	1,593	1,520	73	4.8
Other financial assets	13	10	3	29.2
Other non-financial assets	187	61	126	>100,0
Cash and cash equivalents	276	533	(257)	(48.2)
Total assets = Total equity and liabilities	**15,712**	**16,654**	**(942)**	**(5.7)**
EQUITY	**9,633**	**10,321**	**(688)**	**(6.7)**
Common Stock	2,975	2,975	–	–
Additional paid-in capital & retained earnings	6,658	7,346	(688)	(9.4)
Equity attributable to owners of the company	9,633	10,321	(688)	(6.7)
NON-CURRENT LIABILITIES	**3,212**	**2,779**	**433**	**15.6**
Interest-bearing debt	2,023	1,686	337	20.0
Trade and other payables	153	154	(1)	(0.6)
Provisions	641	516	125	24.2
Deferred income	396	424	(28)	(6.6)
CURRENT LIABILITIES	**2,867**	**3,554**	**(687)**	**(19.3)**
Interest-bearing debt	90	568	(478)	(84.1)
Trade and other payables	2,050	2,272	(222)	(9.8)
Provisions	156	196	(40)	(20.3)
Other non-financial liabilities	96	48	49	>100,0
Deferred income	475	471	4	0.9

Financial Data				
Net financial debt (1)	1,356	1,225	132	10.8
Leverage (2)	0.8x	0.7x	0.1	9.3

(1) Net financial debt includes current and non-current interest-bearing financial assets and interest-bearing financial liabilities as well as cash and cash equivalents.
* Current and non-current financial assets include handset - receivables (current: EUR 327m in 2016 and EUR 321m in 2015; non-current: EUR 132m in 2016 and EUR 157m in 2015), positive Fair value Hedge for fixed interest financial liabilities (current: EUR 2m in 2016 and EUR 2m in 2015; non-current: EUR 15m in 2016 and EUR 12m in 2015) as well as loans to third parties (current: EUR 1m in 2016 and EUR 1m in 2015; non-current: EUR 0m in 2016 and EUR 1m in 2015)
* Current and non-current net financial debt include bonds, promissory notes and registered bonds issued (EUR 1,421m in 2016 and EUR 1,420m in 2015), other loans (EUR 598m in 2016 and EUR 501m in 2015), finance lease payables (current: EUR 73m in 2016 and EUR 180m in 2015; non-current: EUR 17m in 2016 and EUR 32m in 2015) as well as current interest bearing trade payables (EUR 0 in 2016 and EUR 119m in 2015).

Note:
Handset - receivables are shown under trade and other receivables in the Consolidated Statement of Financial Position.
Pending payments for spectrum amounting to EUR 221m (including capitalised costs of borrowed capital) are shown under trade payables against third parties in the Consolidated Statement of Financial Position and are therefore not included in the net financial debt calculation.

(2) Leverage is defined as net financial debt divided by the OIBDA for the last twelve months before extraordinary effects.

TELEFÓNICA DEUTSCHLAND GROUP

RECONCILIATION OF FREE CASH FLOW AND RECONCILIATION TO NET DEBT

Unaudited

	2016		2015			
(Euros in million)	Jan - Mar	Jan - June	Jan - Mar	Jan - June	Jan - Sept	Jan - Dec
OIBDA	**379**	**1,170**	**395**	**845**	**1,234**	**1,804**
- Other income and expenses resulting from finalization of purchase price [1]	–	–	–	–	–	(102)
- CapEX [2]	(218)	(430)	(221)	(463)	(704)	(1,032)
= Operating Cash Flow (OpCF)	**161**	**740**	**175**	**383**	**530**	**670**
+ Silent Factoring [3]	135	194	314	367	301	544
-/+ Other working capital movements	(294)	(554)	(421)	(672)	(503)	(515)
Change in working capital	**(159)**	**(360)**	**(107)**	**(306)**	**(201)**	**29**
+/- (Gains) losses from sale of assets	–	(353)	(17)	(17)	(15)	(15)
+/- Proceeds from sale of companies	–	–	68	61	58	57
+/- Proceeds from sale of fixed assets and other effects	–	591	0	–	0	1
+ Net interest payments	(18)	(19)	(14)	(18)	(22)	(33)
+ Taxes paid	–	–	–	0	0	0
+ /- Proceeds / Payments on financial assets	(4)	(1)	0	(0)	(0)	(10)
= Free cash flow pre dividends and payments for spectrum [4] as well as pre-acquisition of E-Plus net of cash acquired	**(20)**	**599**	**105**	**102**	**350**	**700**
+ Acquisition of E-Plus net of cash acquired [1]	–	–	–	22	22	132
= Free cash flow pre dividends and payments for spectrum [4]	**(20)**	**599**	**105**	**125**	**372**	**832**
- Payments for spectrum	(1)	(2)	–	(976)	(977)	(978)
- Dividends [5]	–	(714)	–	(714)	(714)	(714)
= Free cash flow post dividends and payments for spectrum	**(21)**	**(117)**	**105**	**(1,565)**	**(1,319)**	**(860)**
= Net financial debt at the beginning of the period	1,225	1,225	18	18	18	18
+ Other change in net financial debt	20	15	212	195	72	340
+ capital increase (less transaction costs of the period)	–	–	5	6	6	6
= Net financial debt at the end of the period (incl. Restricted cash)	**1,266**	**1,356**	**130**	**1,784**	**1,415**	**1,225**

(1) In the fourth quarter 2015, an agreement on the final purchase price was reached with KPN. The original purchase price was reduced overall by EUR 134m. The differences between the preliminary purchase price and the final purchase price was recognized in an amount of EUR 30m directly to goodwill within the twelve-month period. EUR 104m less expenses to reach the agreement in the amount of EUR 3m (of which EUR 2m have been paid) have been recognized at the end of the 12-month period in December 2015 in the income statement.

(2) Excluding investments in spectrum in June 2015 amounting to EUR 1,198m and excluding capitalised costs on borrowed capital.

(3) Full impact (YTD) of silent factoring in the first half year of 2016 of EUR 194m and of EUR 367m in the first half year of 2015 (transactions have been executed in March and June 2016 respectively in January, March and June of the year 2015).

(4) 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.

(5) Dividend payments of EUR 714m in May 2016 and EUR 714m in May 2015 respectively.

	2016		2015			
	Jan - Mar	Jan - June	Jan - Mar	Jan - June	Jan - Sept	Jan - Dec
= Free cash flow pre dividends and payments for spectrum (millions)	(20)	599	105	125	372	832
Number of shares (millions)	2,975	2,975	2,975	2,975	2,975	2,975
= Free cash flow per share (in euros)	(0.01)	0.20	0.04	0.04	0.13	0.28

TELEFÓNICA DEUTSCHLAND GROUP

CONSOLIDATED NET FINANCIAL DEBT EVOLUTION

Unaudited

(Euros in millions)	As of 30 June 2016	As of 31 December 2015	Change %
A Liquidity	**276**	**533**	**(48.2)**
B Current financial assets	**330**	**324**	**2.1**
C Current financial debt	**87**	**564**	**(84.6)**
D=C-A-B Current net financial debt	**(520)**	**(292)**	**77.9**
E Non-current financial assets	**147**	**169**	**(13.2)**
F Non-current financial debt	**2,023**	**1,686**	**20.0**
G=F-E Non-current net financial debt	**1,876**	**1,517**	**23.7**
H=D+G Net financial debt (1)	**1,356**	**1,225**	**10.8**

(1) Net financial debt includes current and non-current interest-bearing financial assets and interest-bearing financial liabilities as well as cash and cash equivalents.
B + E Current and non-current financial assets include handset - receivables (current: EUR 327m in 2016 and EUR 321m in 2015; non-current: EUR 132m in 2016 and EUR 157m in 2015), positive Fair value Hedge for fixed interest financial liabilities (current: EUR 2m in 2016 and EUR 2m in 2015; non-current: EUR 15m in 2016 and EUR 12m in 2015) as well as loans to third parties (current: EUR 1m in 2016 and EUR 1m in 2015; non-current: EUR 0m in 2016 and EUR 1m in 2015)
C + F Current and non-current net financial debt include bonds, promissory notes and registered bonds issued (EUR 1,421m in 2016 and EUR 1,420m in 2015), other loans (EUR 598m in 2016 and EUR 501m in 2015), finance lease payables (current: EUR 73m in 2016 and EUR 180m in 2015; non-current: EUR 17m in 2016 and EUR 32m in 2015) as well as current interest bearing trade payables (EUR 0 in 2016 and EUR 119m in 2015).

Note:
Handset - receivables are shown in trade and other receivables on the Consolidated Statement of Financial Position.
Pending payments for spectrum amounting to EUR 221m (including capitalised costs of borrowed capital) are shown in trade payables against third parties on the Consolidated Statement of Financial Position and are therefore not included in the net financial debt calculation.

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