

Telefónica

Telefónica Deutschland

Company profile


3Investor Relations, 02 September 2019

 **RECONNECT**

Executive Summary: Telefónica Deutschland

VISION

We want to become the **Germany Mobile Customer and Digital Champion** by leveraging growth opportunities with the biggest mobile customer base and by entering the next level of digitalisation

STRATEGIC PRIORITIES

- **Strong foundations** (integration success, customer base, technology, lean organization)
- Focus on **customer experience & digitalization**
- Generate **superior shareholder return** with high dividend pay-out ratio to FCF

OPERATIONAL AND FINANCIAL PERFORMANCE

- Telefónica Deutschland showing **sustained commercial performance and financial momentum** in a dynamic competitive, yet rational environment
- Underlying¹ revenue +1.8% year-on-year in HY1 with **focus on data monetisation** and continued strong demand for handsets
- Underlying² OIBDA (as per IAS 17) +0.7% year-on-year in HY1 reflecting **ongoing transformation & market invest**
- Solid B/S, liquidity position and FCF generation ability **support dividend commitment**

CAPEX AND EFFICIENCY

- Telefónica Deutschland acquired a **total of 90 MHz spectrum in the German 5G auction** for a total of EUR 1.425 billion, maintaining a highly competitive frequency position
- Capex invest remains **focused in network pushing LTE rollout**, with focus on network densification and roll-out into suburban areas to improve customer experience

¹ Excluding the negative impact from regulatory changes; mainly driven by the MTR regulation (mobile termination rate cut to EURc 0.95 per minute as of 1 Dec 2018) and the international call regulation within the EU that kicked-in as of 15 May 2019

² Adjusted for exceptional effects and excluding the negative impact from regulatory changes; mainly usage elasticity effects from the European roaming regulation and the international call regulation within the EU

Telefónica Deutschland at a glance

1 company - 4 years

- Largest and fastest mobile merger in the West
- One of the largest players in German mobile market by customers
- Synergy case upgraded to EUR 900 million will be delivered



>30% OIBDA growth
over 4 years



>30% Headcount
harmonised in 3 years



>30% Shop reduction
in 3 years



>25m Customers
migrated to one IT stack in 2016



>30% Network sites
to be consolidated by 2019

O₂ Free[®]

3G Unlimited
4G Big bucket portfolio

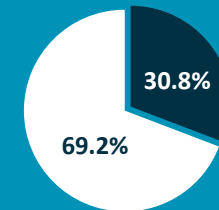
Revenue¹ **EUR 7,320m**
MSR¹ **EUR 5,267m**
OIBDA¹ **EUR 1,884m**
Capex² **EUR 958m**
Accesses **47m**

All figures FY 2018

Market Cap¹ **EUR 7,308m**
Fitch Rating: **BBB**
Listed: **MDAX**
TecDAX
Employees **>9,000**

All figures 30.06.2019

Shareholder structure



■ Telefónica Germany Holdings Ltd.
■ Freefloat

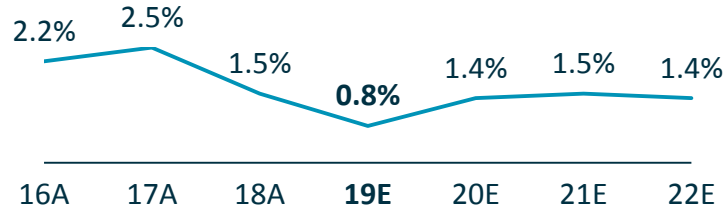
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² Excluding additions from capitalised right-of-use assets (as of 1 January 2019) respective excluding additions from capitalised finance leases (till 31 December 2018)

Macro outlook shows German economy will remain mostly stable with strong consumer spending to be expected

Summary of macro outlook¹

GDP growth real, %



CPI, annual change



Population % change 2018-'22

-0.05%

Key drivers and outlook

- Germany's **economy is in full swing**, no major changes expected
- **Low inflation rate (1.3%)**; no major risk expected
- Stable **low unemployment** rate at 4.9%²
- **Price regulations** like *Mobile Termination Rate, Roam Like Home* and *Intra EU Calls* **decrease revenues**, which need to be compensated

Political situation

- *Christian Democratic Union (CDU and CSU)* and *Social Democrats (SPD)* **continue to govern nationally as part of a longstanding Grand Coalition** led by chancellor Angela Merkel
- Merkel's potential **successor still uncertain**; upcoming government elections in 2021

Read across for Telefónica Deutschland

- **Strong purchasing power** and low inflation rate positively impacting overall business
- Latest **focus of German government** with regards to mobile infrastructure gives **window of opportunity to create a regulatory framework** which enables us to build the necessary infrastructure at a lesser cost (e.g. through participation in state aid program and/or other less cost-intensive co-operations)
- **Risk of 4th entrant** in regulatory framework

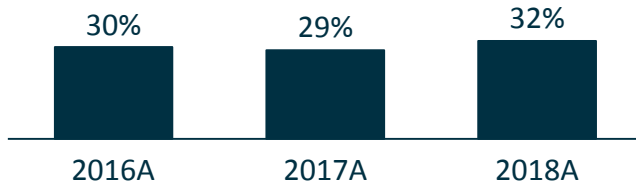
German telco market is expected to continue to deliver service revenues

Market share

TEF GER – mobile service revenue market share¹

#2

MSR market share



Market mobile service revenue m€

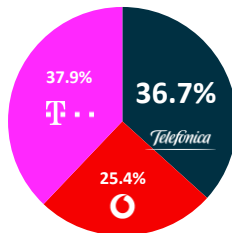
18,183

18,085

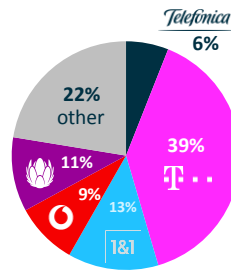
16,642

TEF GER –market share 2018²

Mobile accesses



Fixed BB accesses



Total market m accesses

116,7

34,4

Key market trends

MOBILE MARKET DEVELOPMENT

- German **mobile market outlook** (ex. reg. effects) **slightly growing**, backed by strong macro environment with attractive growth opportunities (mobile data, ADA³, IoT)
- **Significant regulation impact** resulting from MTR cuts and to a limited extent intra-EU call price caps
- **Willingness to spend is increasing with ARPU-up opportunities** from increasing penetration of data tariffs and LTE and increasing migration of customer to high-value tariffs (improved tariff mix)
- Telefónica Deutschland ranks **#2 in MSR market share**

FIXED MARKET DEVELOPMENT

- German fixed market shows a **moderate positive development** driven by continued infrastructure roll-outs in rural regions and increasing number of households
- Vodafone / Liberty merger expected to have **no major impact on growth trajectory**

Sources:

¹ Internal estimates based on public information, 2018 figures impacted by IFRS change;

² Internal estimates based on public information, network view

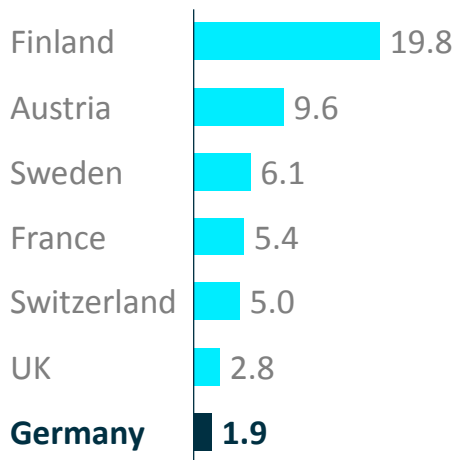
³ Advanced Data Analytics | ⁴ Market Intelligence & Research; Marketmodel 29.04.2019

Telefónica Deutschland is well positioned to lead one of the most attractive telco markets

MARKET TRENDS

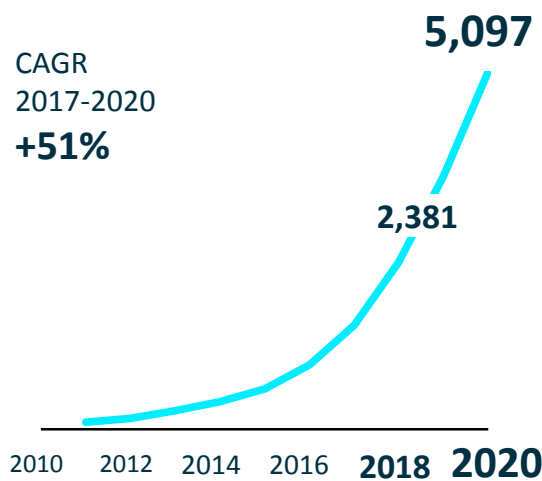
German market with significant further growth potential

Mobile data usage in Europe¹ in GB/month per connection



- Germany still a European laggard in terms of customer data usage
- Further opportunities from growing LTE adoption

Mobile data traffic in Germany¹ Annual volume of mobile data traffic in m GB



- Music & video streaming as usage drivers
- Avg. usage of 3 GB/month for LTE customers

Preparation for 5G opportunities



Risk of 4th entrant in the German market



Soft convergence trend



TV



Pre- to Postpaid migration



Advanced Data Analytics & IoT



Source: ¹Analysys Mason "Western Europe telecoms market trends and forecasts 2018–2023", 29.10.2018

Competitive advantages allow us to leverage growth opportunities on our way to become the **Germany Mobile Customer & Digital Champion**

LARGEST AND MOST MODERN NETWORK¹



We have completed our **network consolidation successfully** and are ready to deploy 5G fast and efficiently

FUTURE-PROOF PRODUCTS & SERVICES



Across all segments with largest owned **customer base of ~35 million**

TRANSFORMATION & DIGITALISATION



Transformation program **Digital4Growth (D4G)** places the customer at the centre of our actions

1) We want to become Germany's largest and most modern mobile network and build the best network for customer experience until 2020.

Becoming the Mobile Customer & Digital Champion: All-round infrastructure player confirmed

MOBILE INFRASTRUCTURE



4G



5G



> 4,400 new LTE sites in 2019
on track for FY 2019 target of 10,000

Driving innovation in 5G

Establishing the world's first 5G network for automobile production in Mercedes-Benz Cars "Factory 56"



FIXED NET INFRASTRUCTURE



VDSL



FttH



Cable



Long-term FttH and VDSL access through Deutsche Telekom

Exclusive cable wholesale access

to Vodafone's cable network in Germany; enhancing infrastructure footprint to give customers choice: Triple play offers via fixed & cable

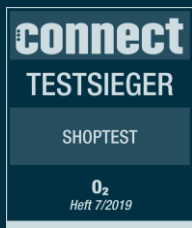


We have been successfully driving the 3 fundamental pillars of our business in HY1 2019: Quality, trading and financials

QUALITY

WINNER

Stores
National store operators



WINNER

Partner-Stores
Franchise operators



VERY GOOD

Fixed Net
Fixed Net big players



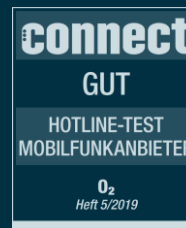
VERY GOOD

Fixed Net
Fixed Net offers



GOOD

Service Hotline
Telcos



4,5/5

O2 TV
Computer Bild User Test

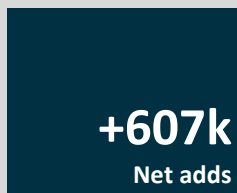


All awards from HY1 2019

TRADING

Postpaid

22.8m customers



All figures from HY1 2019

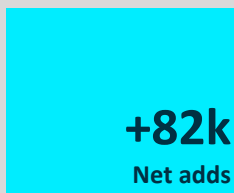
Churn

vs. -18.0% (FY'17)



Fixed

2.2m customers



FINANCIALS

Capex invest
ongoing

Revenue & MSR
growth

OIBDA
on track

All references to the results HY1 2019

Focus on customer experience to generate growth with a portfolio of future-proof products, services and solutions for all customer groups

B2C

TARGET
Leverage customer base, grow in mass market

LEVERS
Data monetisation
Willingness to pay
Extended Services / VAS

AMBITION
ARPU Up
Churn Down



B2B

TARGET
Grow customer base

LEVERS
O₂ Free Business
Focus on SME
Lean processes
Sales productivity

AMBITION
Fair market share



B2P

TARGET
Maintain leadership

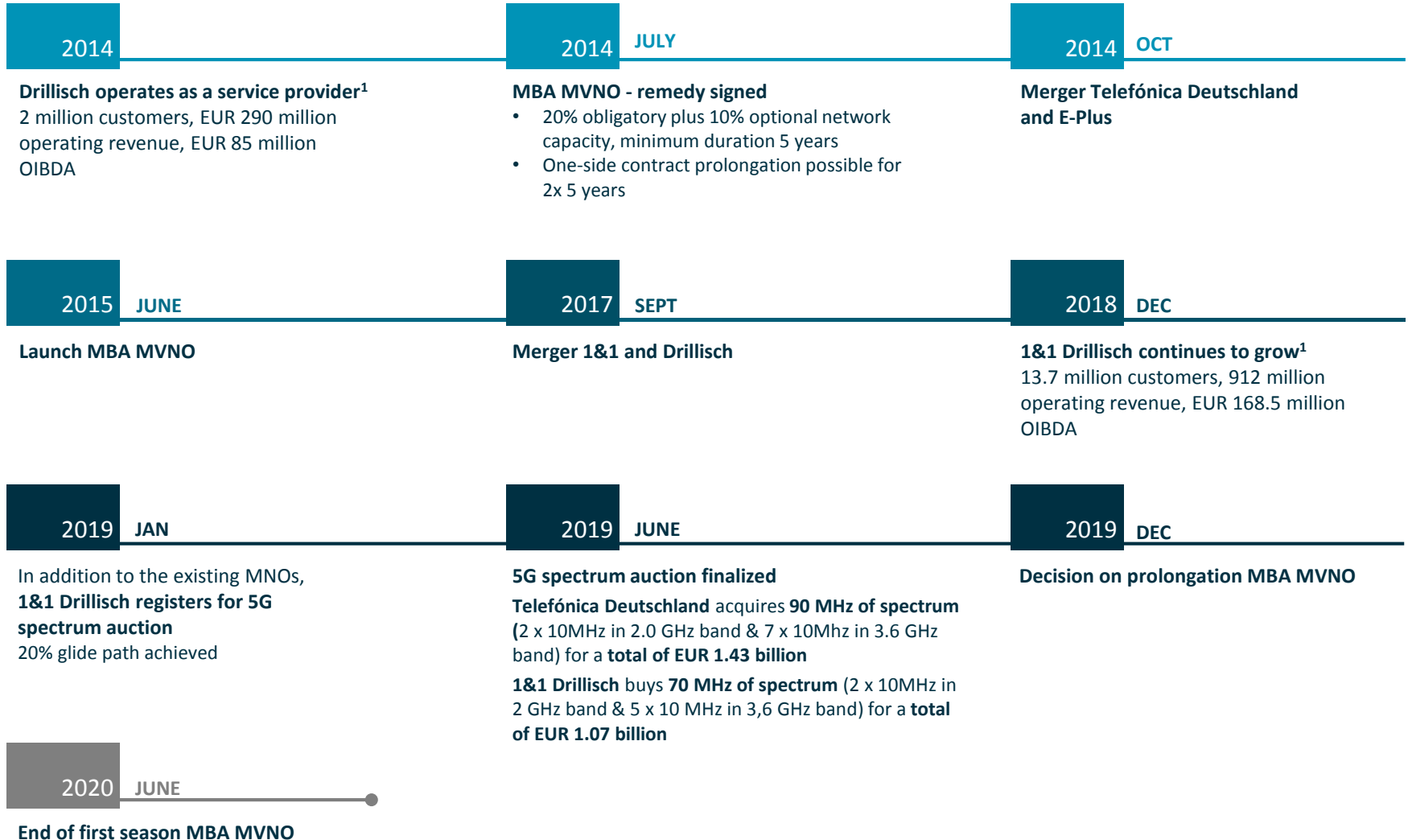
LEVERS
Data Monetisation
ALDI Talk brand

AMBITION
ARPU Up
Churn Down



B2P: Not all brands shown, only selection

Deep-dive: Overview of Telefónica Deutschland's relationship with 1&1 Drillisch

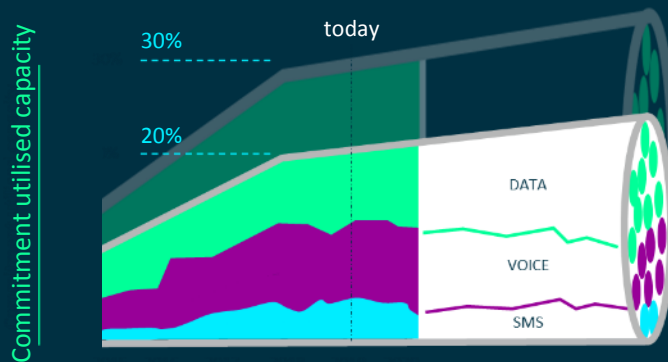


Post German spectrum auction no short- to mid-term impact expected; long-term mitigation by own & other partner business

SCENARIO 1:

Continuation of MBA MVNO

EU-approved capacity glide path

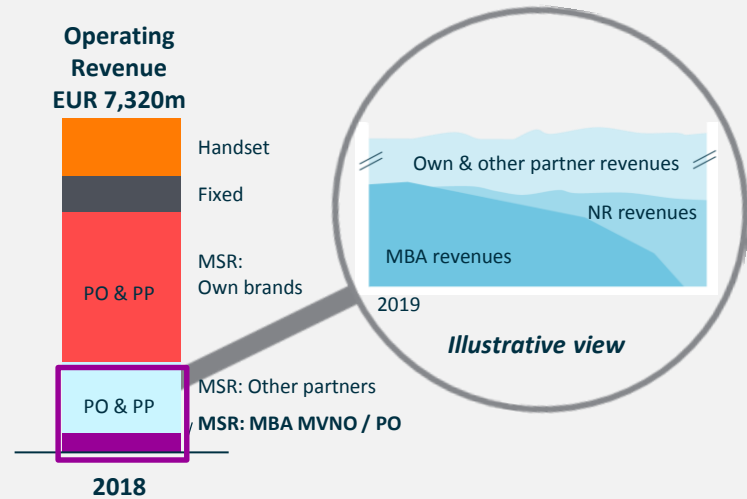


Four levers for revenue growth

- Exponential **data** growth
- **Capacity** of 20% and potential upgrade to 30%
- Price-tiering based on **speed**
- Price-tiering based on **technology**

SCENARIO 2:

MNO remedy – gradual transition



Gradual transition of revenue streams

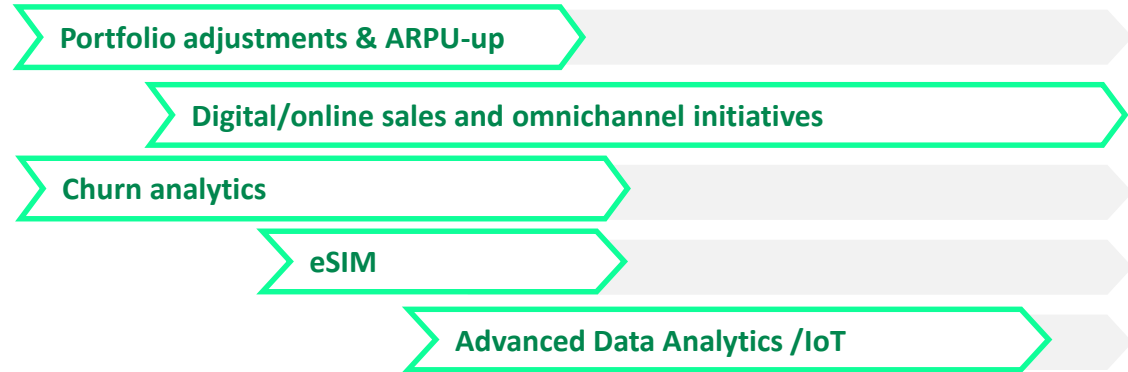
- **Commercial terms** derived from MBA MVNO
- **Sublease spectrum** for 2G/3G/4G national roaming
- MVNO and MNO only for a **transition period**
- Gradual ramp-up of **other partner & own business** to mitigate

Our transformation program 'Digital4Growth' is designed to transform our company holistically placing the customer at the centre of our actions

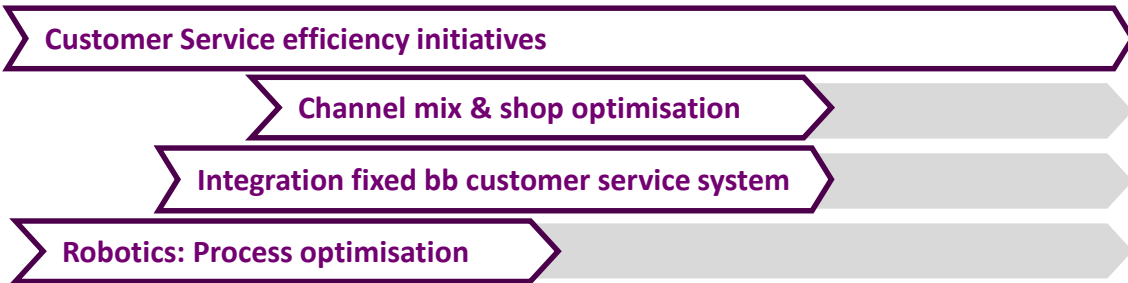


Transformation workstreams

Revenue-related gains



Cost-related gains



SIMPLER

FASTER

BETTER

Financial Performance: Strong trading & financial momentum in HY1 2019 with revenue further improving

TEF_TOTAL	2016	2017	2018 (IFRS15)	2019 (IAS 17)
mEUR	FY	FY	FY	HY 1
Operating Revenue	7,503	7,296	7,320	3,564
Operating Revenue excl. regulatory effects yoy		(0.5%)	0.9%	1.8%
Mobile Service Revenue	5,437	5,287	5,267	2,599
Mobile Service Revenue excl. regulatory effects yoy		(0.1%)	0.4%	0.9%
OIBDA adjusted for exceptional effects	1,793	1,840	1,884	887
OIBDA adjusted for exceptional effects & excl. regulatory effects yoy ¹		2.6%	5.3%	0.7%
CAPEX	1,102	950	966	496
C/S ratio	14.7%	13.0%	13.2%	13.9%
Operating Cash Flow²	967	835	831	352
Mobile Postpaid Net Adds	1,453	738	1,002	607
DSL Retail Net Adds	6	(32)	8	82

¹y-o-y comparison based on IAS17 accounting standards for 2018 and 2019; or details please refer to materials of the Q2 2019 results release

²OIBDA – Capex

HISTORICAL DEVELOPMENT

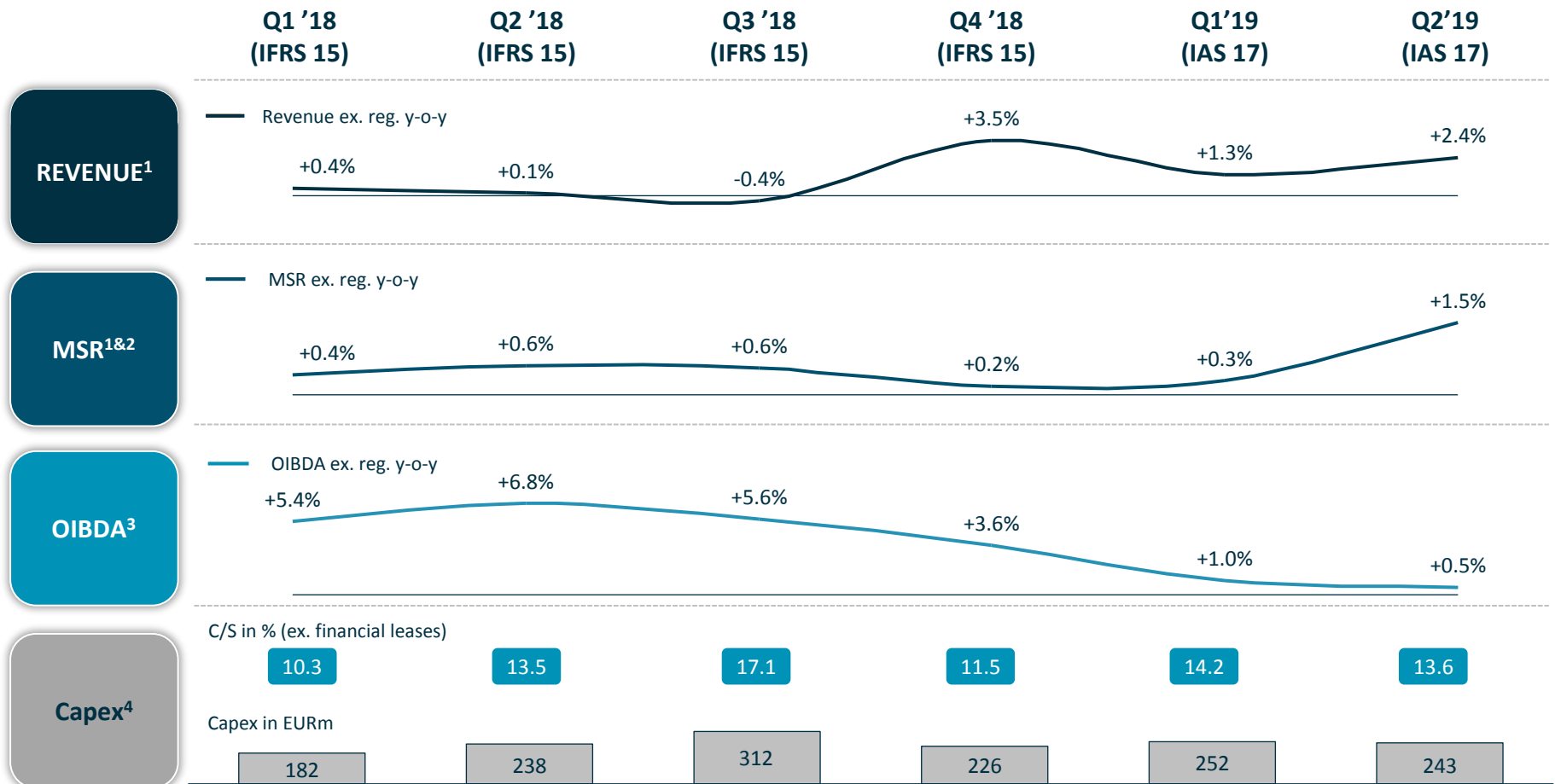
- OIBDA growth driven by synergies capture and new transformation activities (Digital 4 Growth)
- Network consolidation activities and market dynamics affected revenue development. Positive revenue growth in 2019

HY1 2019 PERFORMANCE

- Strong trading momentum in O₂ and partner brands; LTE customer base up +21.6% y-o-y to 20.2 million
- Demand for O₂ Free continues to drive data usage growth with a CAGR of 50%
- Underlying¹ revenue trends supported by sustained demand for handsets & strong traction of O₂ Free portfolio
- Reported MSR up +0.6% in Q2'19, crossing the zero line for the first time in 15 quarters; underlying¹ MSR trends improve to +1.5% y-o-y in Q2
- OIBDA reflects ongoing market and transformation invest; ~EUR 45 million benefit from roll-over synergies and transformation
- Capex phasing supports pace of LTE roll-out; mid-term expectations unchanged at approx. EUR 1 billion

**

Operational and financial trends remain strong



¹ Excluding the negative impact from regulatory changes (mainly driven by the mobile termination rate cut to EURc 0.95 per minute as of 1 Dec 2018)

² Mobile service revenue include base fees and fees paid by our customers for the usage of voice, sms and mobile data services. Also, access and interconnection fees as well as other charges levied on our partners for the use of our network are included

³ Exceptional effects were EUR xx million of restructuring expenses in the period June to September 2019 (EUR xx million based on IAS 17). The difference between restructuring charges under IAS 17 and IFRS 16 is due to the fact that certain IAS 17 operating lease commitments require the recognition of provisions, whereas those are recognised as lease liabilities under IFRS 16. Regulatory effects amounted to EUR xx million in the period June to September 2019

⁴ Excluding additions from capitalised right-of-use assets (as of 1 January 2019) and excluding additions from capitalised finance leases (till 31 December 2018)

Outlook 2019: Building on our 2018 achievements and a solid HY1 performance as we move from integration to transformation

	Actuals FY'18 (IFRS15)	Outlook ² FY'19 (IFRS15)	HY1 2019	Midterm expectations
Revenue	7,320 FY '18	Broadly stable (excl. regulatory impacts of ~EUR 60-70 million)	+1.8% yoy ✓	Revenue growth in line with German market; capturing market share in IoT
OIBDA ¹	1,884 FY '18	Broadly stable to slightly positive (excl. regulatory impacts of ~EUR 40-50 million)	0.7% yoy As per IAS 17 reporting ✓	Ongoing margin improvement supported by growth centric transformation case (~EUR 600 million gross OIBDA 2019/22)
C/S ²	13.2%	Approx. 13-14%	13.9% yoy ✓	Keeping Capex level stable at around EUR 1 billion

- Underlying revenue reflect tailwinds from ARPU-up strategy supported by new O₂ Free tariffs which help to counteract ongoing legacy base management topics, while we continue to leverage our many long-term partnership contracts
- OIBDA benefits from integration and transformation savings, partly offset by commercial and transformation invest; transformation savings to gradually ramp-up throughout 2019 and over the course of our four year D4G program
- Re-iterating midterm expectations: Expecting to growth with the market, strong confidence in our ability to grow FCF and continue to support a high dividend pay-out ratio to FCF

Strategic initiatives: Telefónica Deutschland's strategy provides superior growth & profitability

GROWTH



- Exploration of new **5G business opportunities** (e.g. 'Factory 56' with Mercedes-Benz)
- Continued **data monetization in B2C** from evolving O₂ and Blau portfolios, focusing on customer experience
- **All-round infrastructure player** (mobile, VDSL, cable), FWA optionality
- **Leverage partner business** to maximize value add
- Transformation of **B2B business** to exploit market opportunities in SME segment

EFFICIENCY



- Becoming Germany's '**Mobile Customer & Digital Champion**' with our transformation program '*Digital4Growth*', focusing on customer experience and digitalization
- Ongoing **invest into future-proof network & IT platforms** to increase efficiency
- Opportunity of **mobile network sharing**
- **Ambition to switch off 3G** by 2022
- **Lean & agile organization** to execute in a fast and efficient manner

RETURNS



- Leverage Germany's **largest owned customer base** (35m customers)
- **ARPU-up and churn-down**, through multi-brand and multi-channel service landscape
- **Transformation case** presented at CMD in Feb 2018 with upfront invest and gradual ramp-up of savings to **600 m€ gross OIBDA contribution** between 2019-22
- Open for **network sharing** especially in 5G environment
- Sustained OIBDA growth and efficient CAPEX spend supports **solid FCF trajectory** and **dividend**

Telefónica
