Q4 2018
preliminary results

Telefónica Deutschland Investor Relations

20 February 2019

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Full year 2018 – Summary

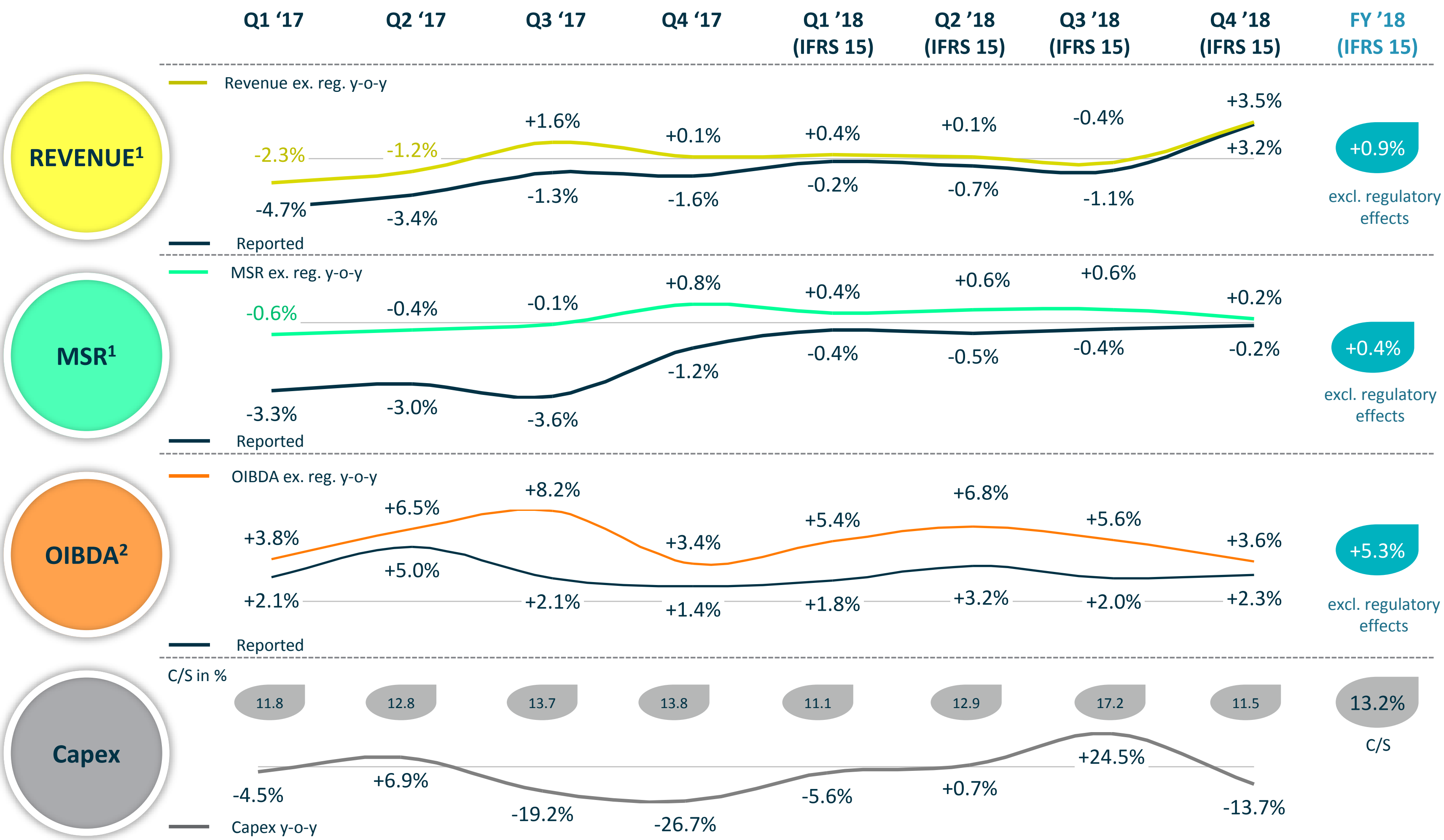
Full-year outlook met on operational momentum and synergy capture

DATA	REVENUE[1]	OIBDA[2]	C/S
+47% y-o-y	+0.9% y-o-y	+5.3% y-o-y	13.2% FY'18

- Continued demand for LTE (18.4 million LTE customers, +17% y-o-y) drives sustained mobile data traffic growth
- Revenue trends supported by strong demand for handsets
- Underlying MSR[1] trends solid, +0.4% y-o-y (+0.0% IAS 18); O_2 Free portfolio APRU-accretive, while visitor roaming & legacy base rotation with a retention focus were headwinds in the second half
- OIBDA growth supported by operational momentum and successful synergy capture with focus on fair market share
- C/S ratio in line with guidance, slightly higher CapEx vs the prior year (+1.7% y-o-y) as a result of LTE roll-out push
- Maintaining a high pay-out-ratio of FCF; dividend proposal of EURc 27 per share for FY 2018 to AGM in May 2019

[1] Excluding the negative impact from regulatory changes and y-o-y comparison based on IAS18 accounting standards for 2017 and IFRS15 for 2018
[2] Adjusted for exceptional effects, excl. the negative impact from regulatory changes and y-o-y comparison based on IAS18 accounting standards for 2017 and IFRS15 for 2018. For details please refer to additional materials of the Q4 2018 results release

Operational and financial trends solid



[1] Excluding the negative impact from regulatory changes and y-o-y comparison based on IAS18 accounting standards for 2017 and IFRS15 for 2018. Including 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

[2] Adjusted for exceptional effects, excl. the negative impact from regulatory changes and y-o-y comparison based on IAS18 accounting standards for 2017 and IFRS15 for 2018. For details please refer to additional materials of the Q4 2018 results release

2018 results – Guidance achieved on all metrics

	Outlook 2018[1]	FY'18	Outlook 2019
Revenue	**Broadly stable y-o-y** (excl. negative regulatory effects of EUR 30-50 million)	FY'17[3]: 7,296; FY'18[3]: 7,334; +0.5% ✓	Broadly stable **(excl. reg. impacts of ~EUR 60-70m)**
OIBDA[2]	**Slightly positive y-o-y** (excl. negative regulatory effects of EUR 40-60 million	FY'17[3]: 1,840; FY'18[3]: 1,903; +3.4% ✓	Broadly stable to slightly positive **(excl. reg. impacts of ~EUR 40-50m)** Transformation benefits of approx. EUR 40m gross
C/S	**Approx. 12-13%**	FY'17: 13.0%; FY'18: 13.2% ✓	Approx. 13-14%
Dividend EUR/share	Annual dividend growth for 3 consecutive years (2016-2018)	FY'16: 0.25; FY'17: 0.26; FY'18 (Proposal to AGM): 0.27; 4% ✓	Dividend proposal of EUR 0.27 per share to AGM in May '19

[1] The effects from the implementation of IFRS15 as of 1 January are not reflected in the financial outlook
[2] Exceptional effects such as restructuring costs or the sale of assets are excluded
[3] FY'17 based on IAS 18 accounting standards / FY'18 based on IFRS 15 accounting standards

We have completed our network consolidation successfully and are ensuring 5G readiness for the future

MAY 15

3G national roaming for all customers

JUL 16

Consolidation and roll-out of 4G network

MAY 17

Implementation of SON, SOC and CEM

AUG 17

1 MNC nation-wide

JUN 18

75% consolidation competed

H2 18

MBH cooperations

DEC 18

Network consolidation completed

Ongoing **Network optimisation** & **LTE** and **fibre in the backhaul** roll-out

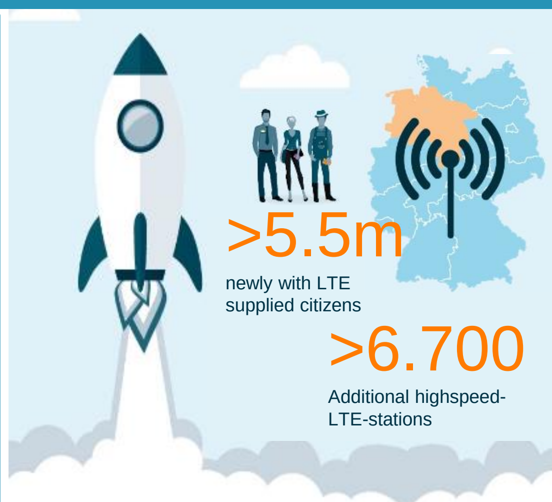
2022

Massive network quality improvement throughout Germany

Network consolidation completed

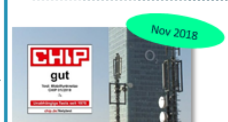
✓

a major milestone of becoming the “Mobile Customer & Digital Champion”



Major step up in the network tests in the 2nd half of 2018

No other German network operator
- has achieved such a **substantial improvement in its score** (+127 point y-o-y) since 2012
- has shown an improvement **despite more stringent measurement criteria**



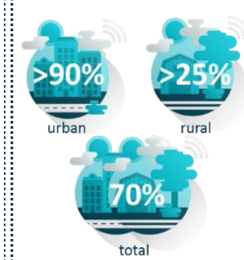
- Overall grade **"good"**; in Hamburg and Munich even "very good"
- CHIP described the O_2 network as having made a **"quantum leap"**

Computer Bild

Nov 2018

- **Improved network quality thanks to "strong LTE expansion"**
- Successfully shortened the gap to our competitors

Fibre in the backhaul (targets 2022)



Digital4Growth – Key Transformation drivers in 2019

D4G | 2019 | 2020 | 2021 | 2022

Gross OIBDA-relevant gains

EUR 40m

Transformation workstreams

EUR ~600m

SIMPLER

FASTER

BETTER

Revenue-related gains

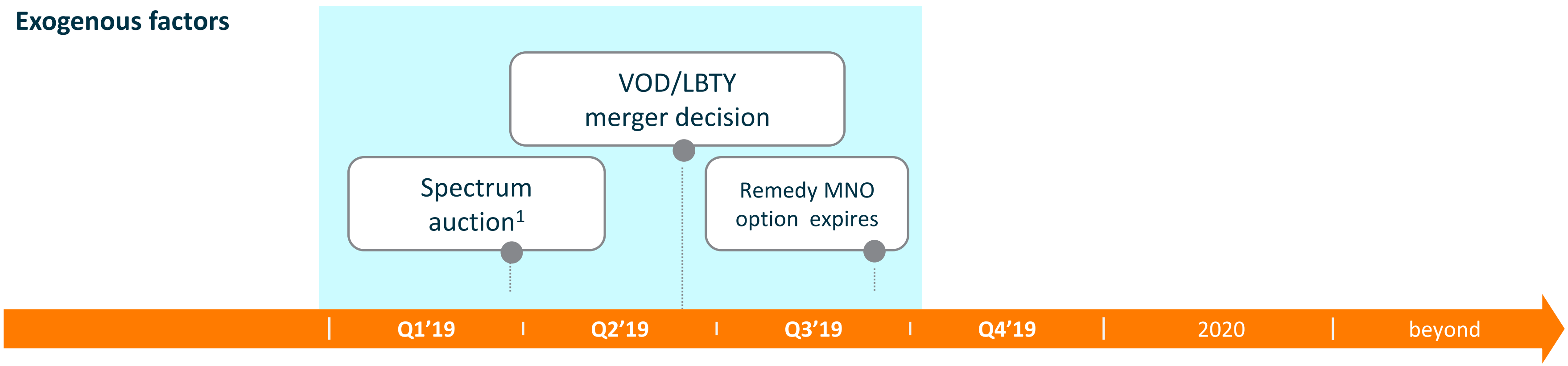
- **Portfolio adjustments & ARPU-up**
- **Digital/online sales and omnichannel initiatives**
- **Churn analytics**
- **eSIM**
- **ADA/IoT**

Cost-related gains

- **Customer Service efficiency initiatives**
- **Channel mix & shop optimisation**
- **Integration fixed bb customer service system**
- **Robotics: Process optimisation**

Underlying business solid; key drivers for 2019 with challenges and opportunities

Exogenous factors



Org. business development

- **Consumer / Own brands**: Churn-down, ARPU-up → Growth in line with market
- **Long-term partnerships**: Solid revenue streams, growing smartphone penetration → Profitable growth
- **Transformation**: Revenue opportunities & efficiencies → ~EUR 600 million cumulated gross OIBDA benefits by 2022
- **Network development**: LTE rollout, fibre in the backhaul, co-invest models → Quality improvement → Upside to commercial pricing

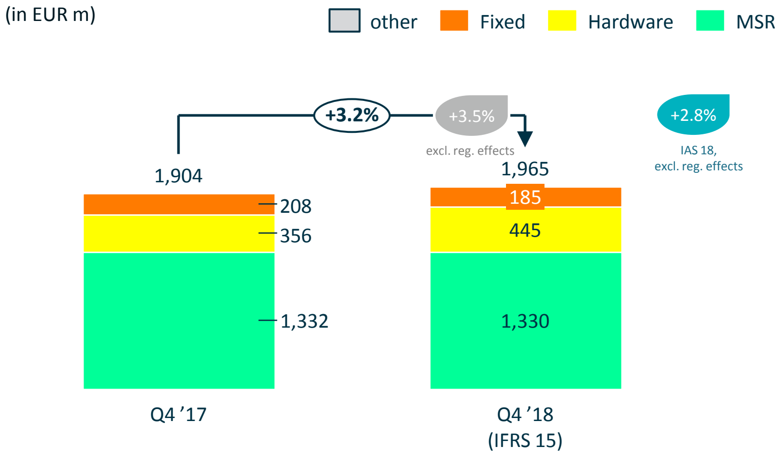
Q4 2018: Summary
Outlook 2018 achieved with strong quarterly results

Net adds **+279k PO** **+25k fixed BB**	• O_2 Free portfolio with O_2 Boost & O_2 Connect with good traction in the quarter • Partner trading remains strong with focus on 4G offers in a continued dynamic, but rational market environment • Continued strong demand for VDSL reflects customer migration trends of planned legacy platform shutdown in 2019
Revenue[1] **+3.5% y-o-y** **(+2.8% y-o-y IAS18)**	• MSR[1] trends broadly stable (ex reg effects of EUR 5 million): +0.2% y-o-y (-0.4% y-o-y based on IAS18) • Smartphones benefitting from strong seasonal trends with handset revenues[1] +25.2% y-o-y (+24.2% y-o-y based on IAS18) • Fixed revenue[1] reflects finalisation of wholesale migration; promos and higher share of bundle benefits in the retail base
OIBDA[2] **+3.6% y-o-y** **(+1.9% y-o-y IAS18)**	• OIBDA[2] benefitting from further synergy capture • Incremental synergies of approx. EUR 10 million (EUR 100 million YTD) from leaver programme, network & shops • Stable OIBDA margin of 26.3% in the fourth quarter
Leverage **0.6x**	• OpCF supported by additional Capex synergies of approx. EUR 15 million in Q4 (approx. EUR 50 million in 2018) while slightly higher Capex (+1.7% y-o-y in 2018) weighs as a result of LTE roll-out push • Maintaining a high pay-out-ratio of FCF; dividend proposal of EURc 27 per share for FY 2018 to AGM in May 2019

[1] Excluding the negative impact from regulatory changes and y-o-y comparison based on IAS18 accounting standards for 2017 and IFRS15 for 2018
[2] Adjusted for exceptional effects, excl. the negative impact from regulatory changes and y-o-y comparison based on IAS18 accounting standards for 2017 and IFRS15 for 2018. For details please refer to additional materials of the Q4 2018 results release

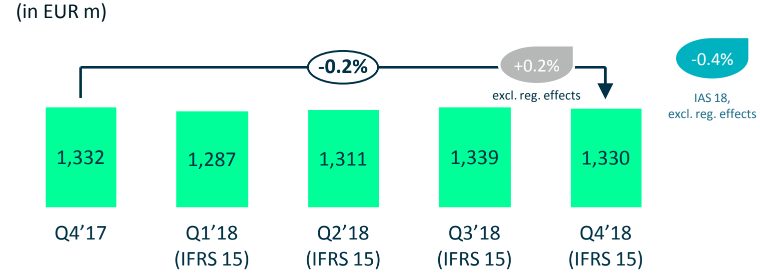
Sustained revenue trends benefit from good commercial momentum

Q4 revenue benefitting from strong demand for handsets

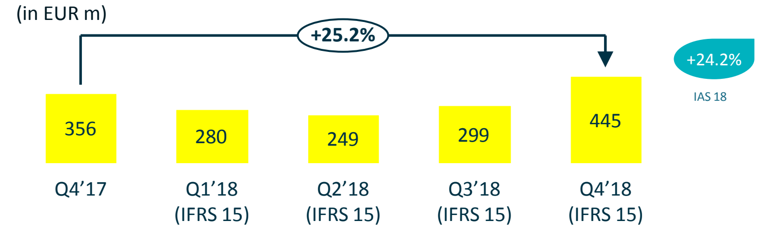


- Underlying MSR trends intact with ARPU accretive effects from O_2 Free in a competitive quarter with tough comps and unchanged headwinds; EUR 5m reg. effects
- Handset revenue benefitting from strong seasonal demand
- Fixed revenue reflects finalisation of wholesale migration; promos and higher share of bundle benefits in the retail base

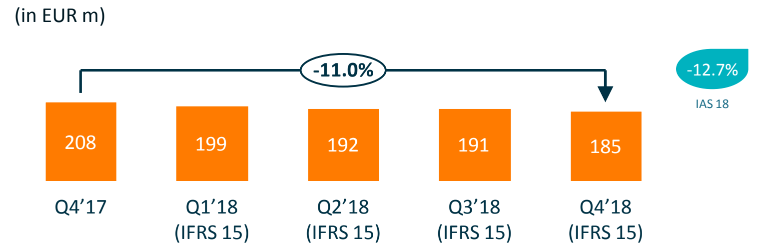
Underlying MSR trends intact



Strong seasonal demand for handsets



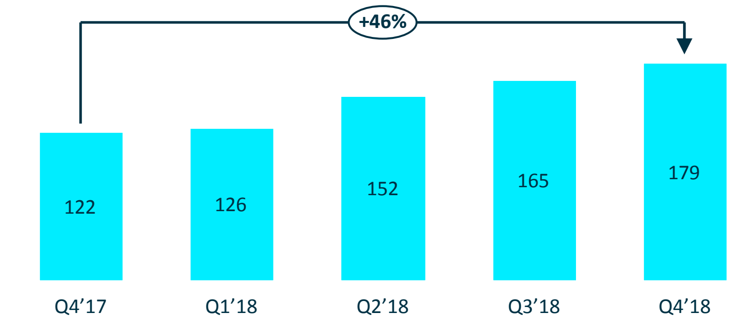
Wholesale migration major driver of fixed revenue



Data usage driven by large data buckets in the updated O_2 Free portfolio

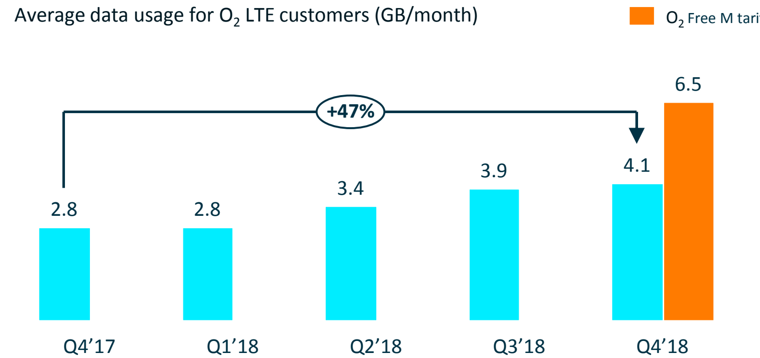
Mobile data with sustainable growth rates

Traffic (TB/Q)



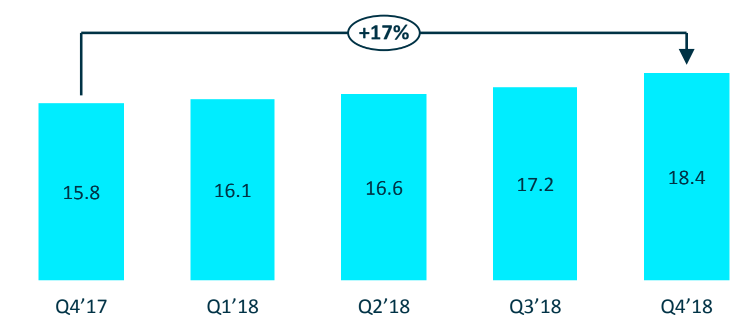
O_2 Free tariffs driving data growth

Average data usage for O_2 LTE customers (GB/month)



LTE customer base further increasing

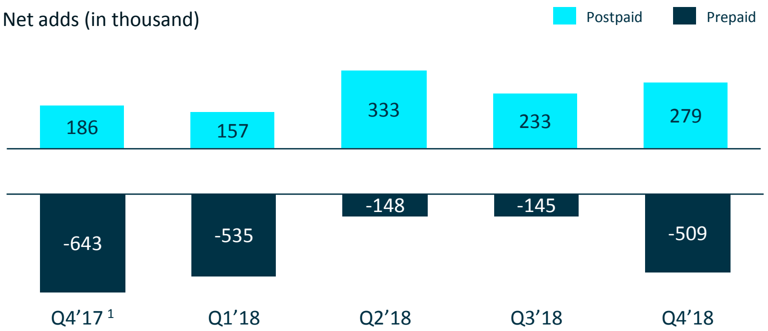
LTE customers (in million)



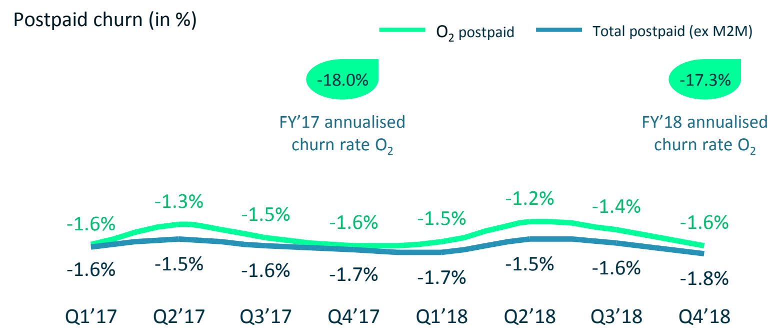
- Steady data growth supported by music & video streaming; data traffic up +46% y-o-y
- LTE adoption drives LTE customer base up +17% y-o-y to 18.4 million
- Average data usage of O_2 LTE customers climbs to >4GB per month
- O_2 Free customers with even higher usage of more ~6.5GB of data in the most popular tariff

Portfolio updates reflected in strong retail trading; churn low with seasonal effects

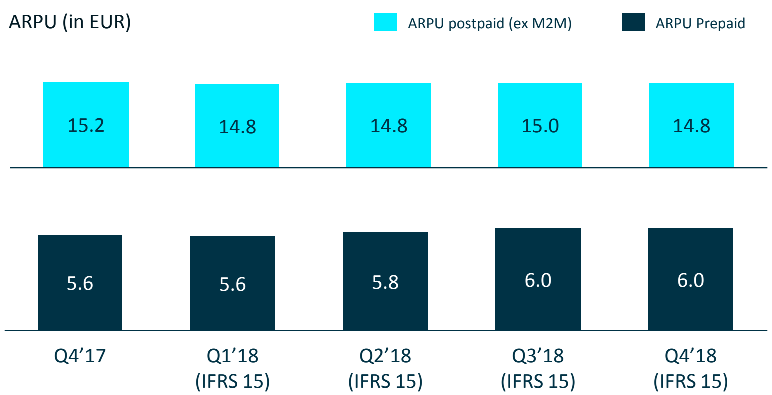
Focus on profitable growth across segments



Customer retention remains a key focus



Regulatory headwinds main driver of ARPU



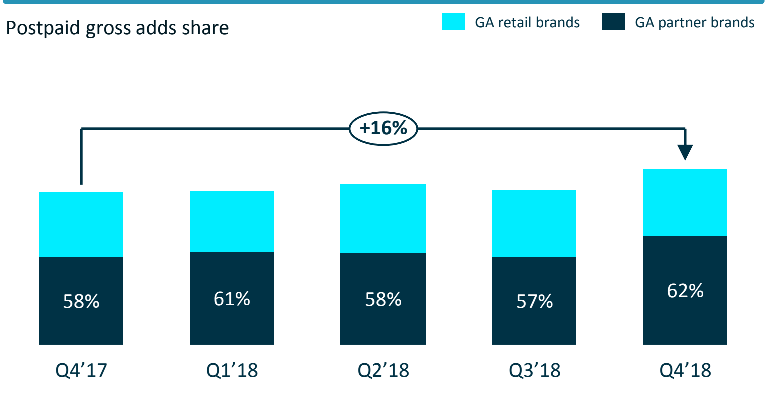
- O_2 Free portfolio remains well received; portfolio initiatives and fair share approach across segments continue to drive strong postpaid net additions
- Prepaid trends continue to reflect the regulatory changes; mainly the legitimation check
- Churn trends in O_2 consumer improving by 0.7 percentage points year-on-year
- Postpaid ARPU trends further stabilising despite regulatory headwinds & higher share of partner MSR

[1] Excluding the impact from the final prepaid customer base adjustment.

Rational market environment across segments; strong partner trading

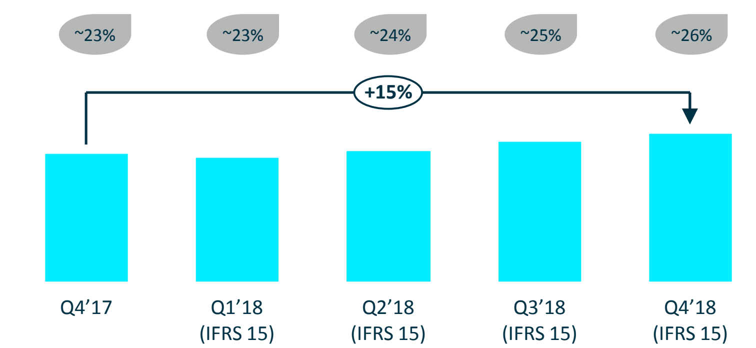
Partner trading reflecting seasonality

Postpaid gross adds share



Partner revenue growth in line with expectations

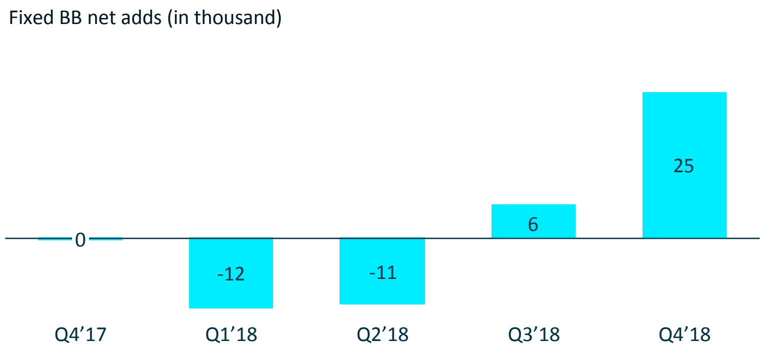
Postpaid partner MSR / Share over postpaid revenue (in %)



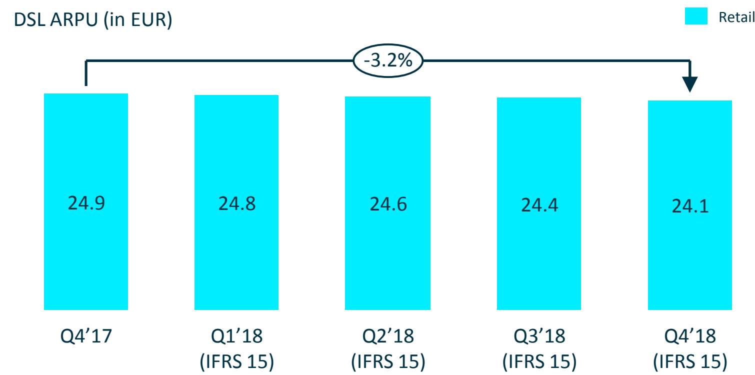
- Rational, yet dynamic market environment; maintaining our focus on fair market share
- Partner trading with strong gross adds; reflecting seasonality and migration trends
- Partner revenue continues to grow in line with expectations q-o-q and y-o-y on the back of data growth & the dynamics of the MBA MVNO contract

Fixed retail dynamics reflect effects of increasing bundle share; wholesale migration finished

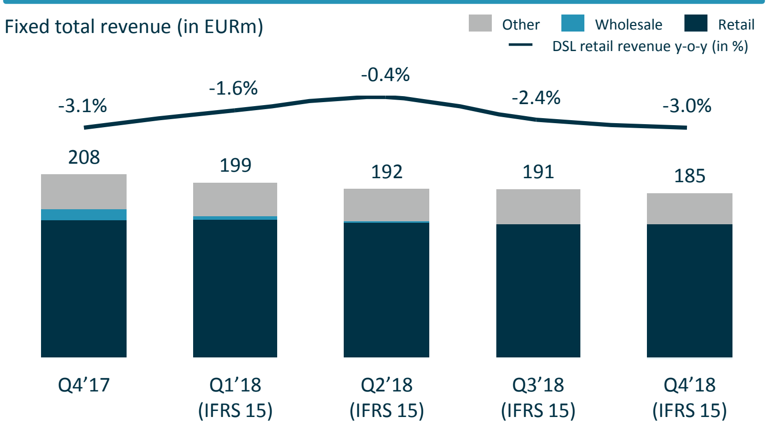
Fixed retail trading further improving



ARPU reflects higher bundle share

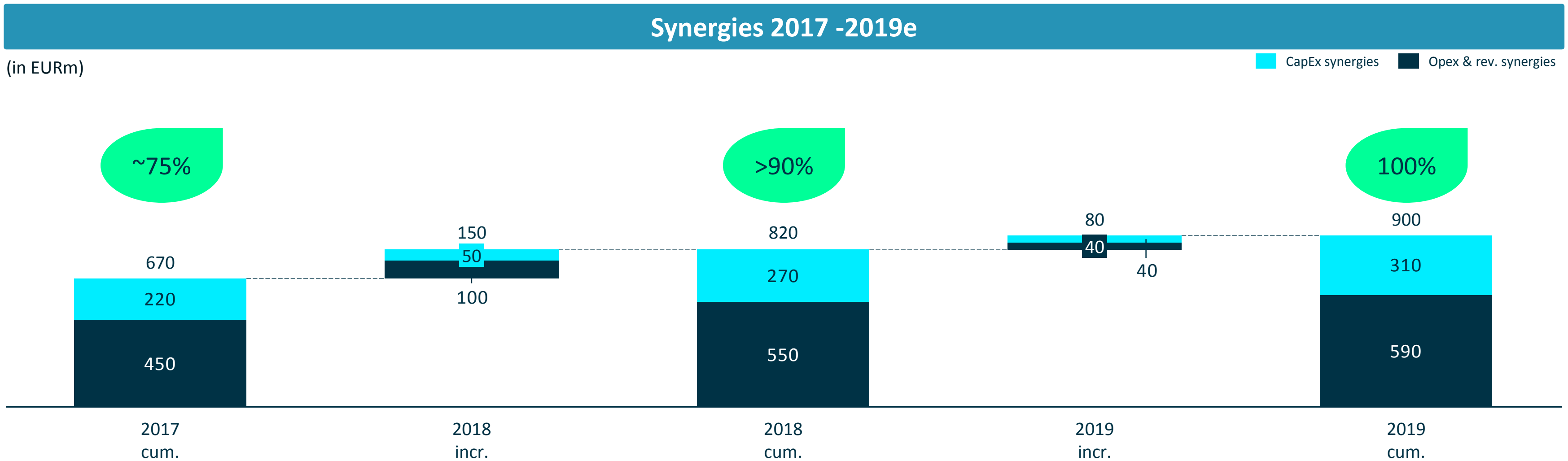


Fixed wholesale phasing out



- Fixed retail trading improving on the back of continued demand for VDSL, while ADSL trend reflects the close to final migration in light of legacy base shutdown
- ~70% of retail fixed customer base already on VDSL; up +25% y-oy-y to 1.4 million
- Retail DSL ARPUs & revenue trends reflect contribution of VDSL and higher bundle share
- Fixed wholesale customer migration completed; effects will be fading out in 2019

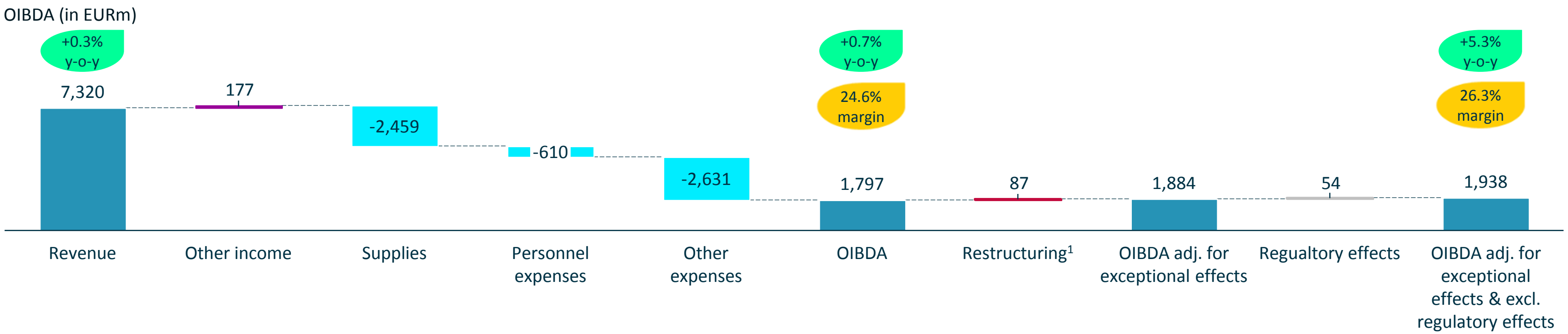
Synergy case: >90% of total target already delivered by 2018



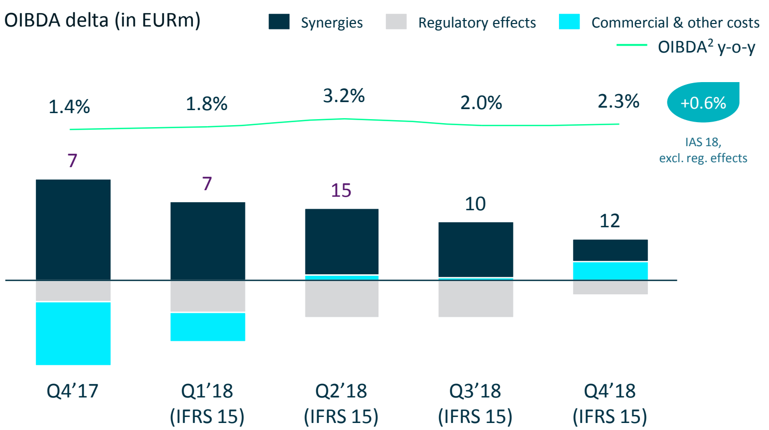
- Q4: Delivery of ~EUR 10 million incremental OIBDA and ~EUR 15 million Capex synergies
- Updated 2018 total synergy target of ~EUR 820 million achieved, reaching >90% of total synergy target; total target unchanged
  - YTD ~EUR 100 million of saving at OIBDA level; brought forward ~EUR 20m savings from 2019 into 2018 due to good progress with network consolidation project which is now finalised
  - YTD ~EUR 50 million of incremental Capex synergies mainly stemming from the rollout of a single LTE network
- EUR 80 million OIBDA & Capex-relevant (EUR 40m OIBDA & EUR 40m Capex) synergies expected for 2019; mainly roll-over effects

OIBDA reflects successful synergy capture, with solid operational momentum and RLH-regulation impacts

Structure of OIBDA for January to December 2018 (IFRS 15)



OIBDA[1] growth on the back of synergy delivery

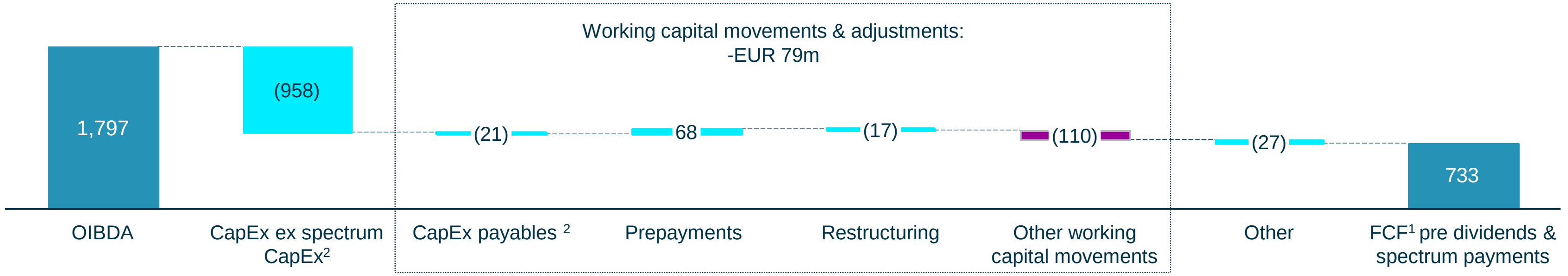


- Sustained OIBDA growth driven by incremental synergies of ~EUR 100 million in 2018, mainly roll-over effects and incremental NT synergies
- OIBDA margin expands by 1.1 percentage points to 26.3%
- Regulatory effects of EUR 54 million YTD; mainly usage elasticity effects from RLH
- Restructuring costs of EUR 84 million

[1] Exceptional effects were EUR 84 million of restructuring expenses (mostly in other expenses) and EUR 2 million of consultancy fees in the context of corporate transactions in the period January to December 2018
[2] Adjusted for exceptional effects

Strong y-o-y growth of FCF; leverage remains in line with target

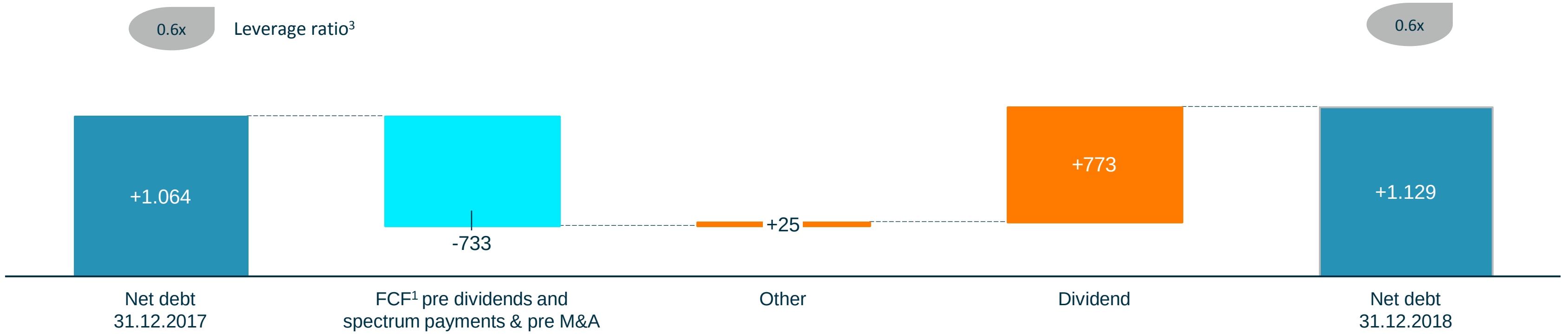
Evolution of Free Cash Flow (FCF)[1] YTD December 2018



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

Evolution of Net Debt[3] – Leverage[3] in line with target

Net Debt (in EURm)



[3] For definition of net debt & leverage ratio please refer to Q4 2018 earnings release.

Outlook 2019: Building on 2018 achievements as we move from integration to transformation

	Actuals FY'18 (IFRS15)	Outlook[2] FY'19 (IFRS15)	Midterm expectations
Revenue	7,320 FY '18	**Broadly stable** (excl. regulatory impacts of ~EUR 60-70 million)	**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) Synergies: ~EUR 40 million Transformation benefits: ~EUR 40m	**Ongoing margin improvement** supported by growth centric transformation case (~EUR 600 million gross OIBDA 2019/22)
C/S	13.2%	Approx. 13-14%	**Keeping Capex level stable** at around EUR 1 bn

- Underlying revenue reflect tailwinds from ARPU-up strategy supported by new O_2 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 programme
- 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
- Review of leverage target in light of IFRS 16, whilst maintaining investment grade rating

[1] Exceptional effects such as restructuring costs or the sale of assets are excluded
[2] The effects from the implementation of IFRS 16 as of 1 January 2016 are not reflected in the financial outlook.

Digital4Growth – Key Transformation areas

Gross margin & revenue gains

- Portfolio adjustments & ARPU-up
- Digital/online sales channel and omni-channel initiatives
- Churn analytics
- eSIM
- ADA/IoT

Key performance indicators

- O_2 app penetration: **>80%** (vs. 20% 2017)
- Gross adds market share in SME: **~30%**
- Tariff detox: **~40%**
- Postpaid churn: **-2%** pts
- Connected devices/ customer: **#4** (vs. #1.5 2017)
- IoT revenue upside: ~EUR **200-300m** cumulative

Cost savings

- Customer Service efficiency initiatives
- Channel mix & Shop optimisation
- Integration fixed BB customer service system
- Robotics: process optimisation

Key performance indicators

- Share of eCare events: **~80%** (vs. 65% 2017)
- Sales in self-assisted channels: **>25%** (vs. 15% 2017)
- Shop reduction: **>10%**
- Manual back-office interventions: **-80%**
- Total IT spend/ subscriber: **-15%**
- Lead time product changes: **Within hours**

Summary

FY 2018 guidance met on all KPIs with sustained focus on profitable growth
Finalised network integration

Revenue supported by successful ARPU-up portfolio,
retention focus and strong demand for handsets

Operational momentum and synergy delivery drives strong OIBDA[1] growth

FCF growth and low leverage support dividend proposal of EUR 0.27 per share for FY 2018

Solid outlook FY 2019 with focus on transformation; re-iterating mid-term expectations
Maintain high dividend in relation to FCF

[1] Excluding regulatory effects in the amount of EUR 60-70 million

Q4 2018 preliminary results - Q&A session

Reach out to us for any follow-up questions

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