

Telefonica

Deutschland

Creating
the
Leading
Digital
Telco



Investor Presentation

November, 2014

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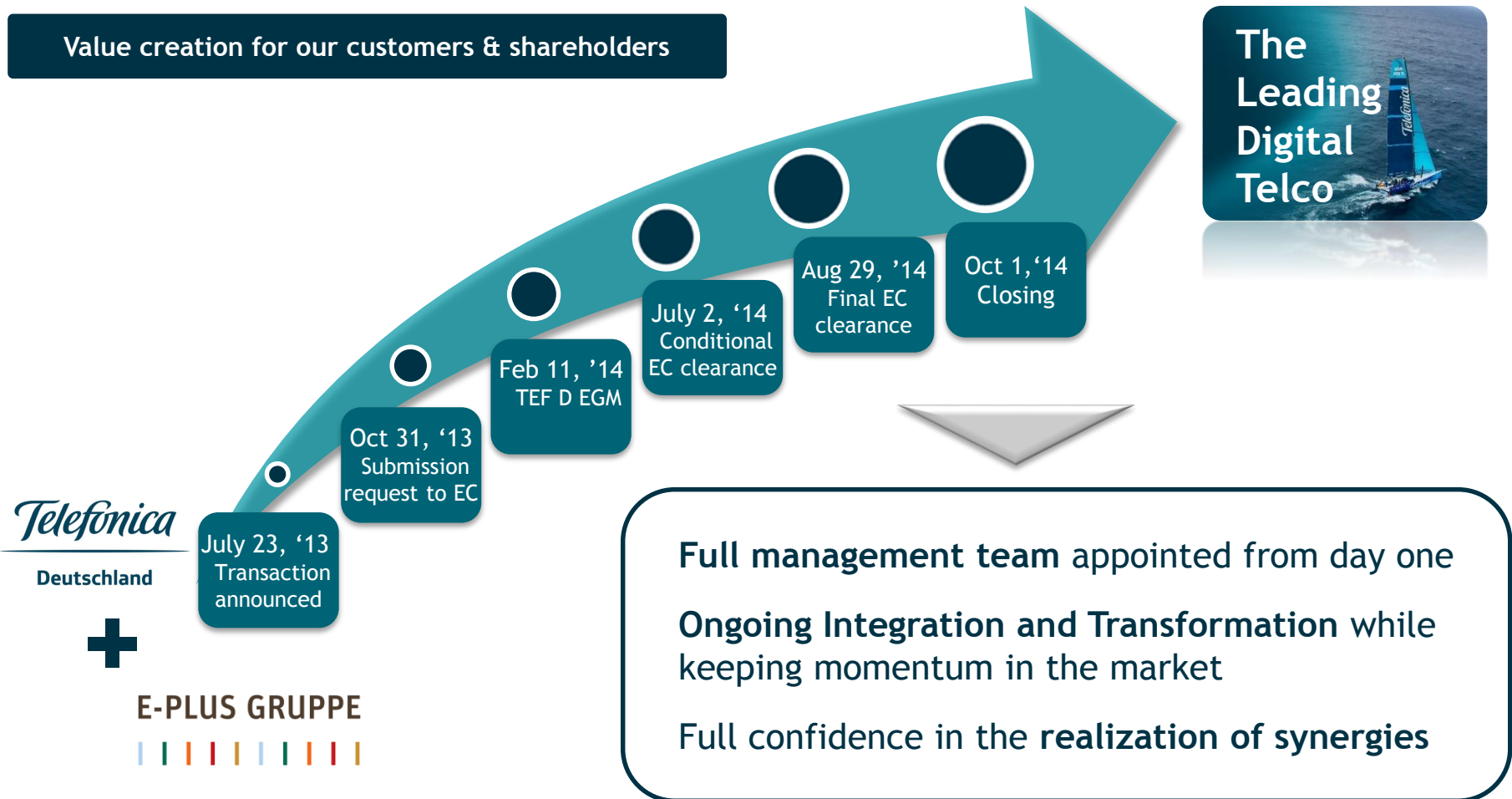
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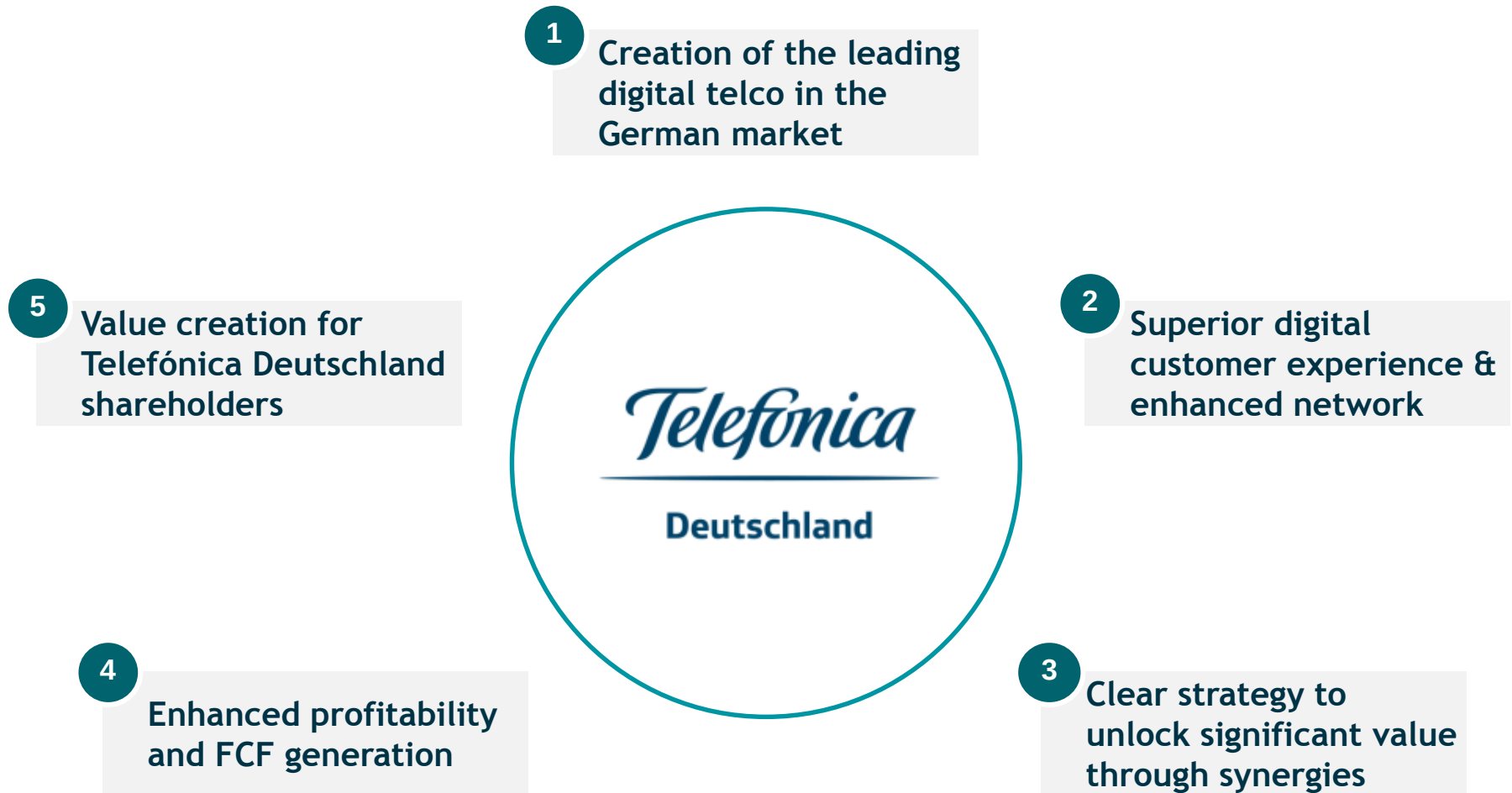
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Successful start for the new Telefonica Deutschland



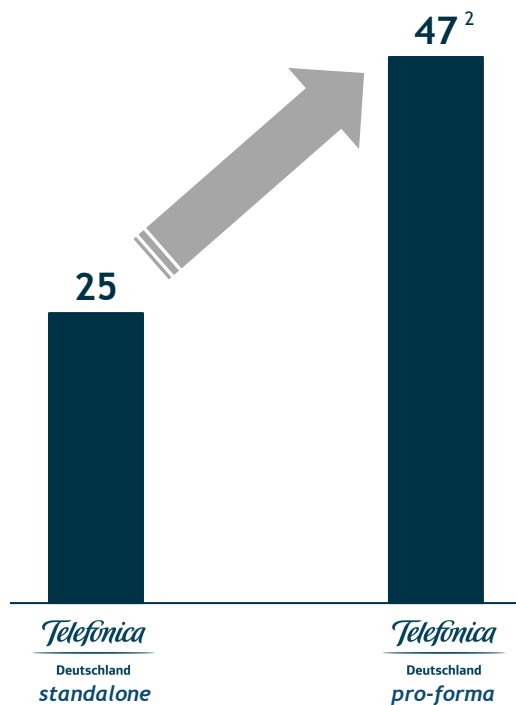
Key investment highlights



Enhanced competitive position from increased scale

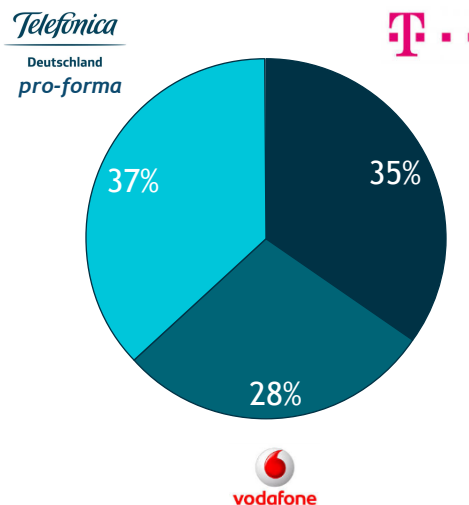
Total accesses (Jun-2014)

In million



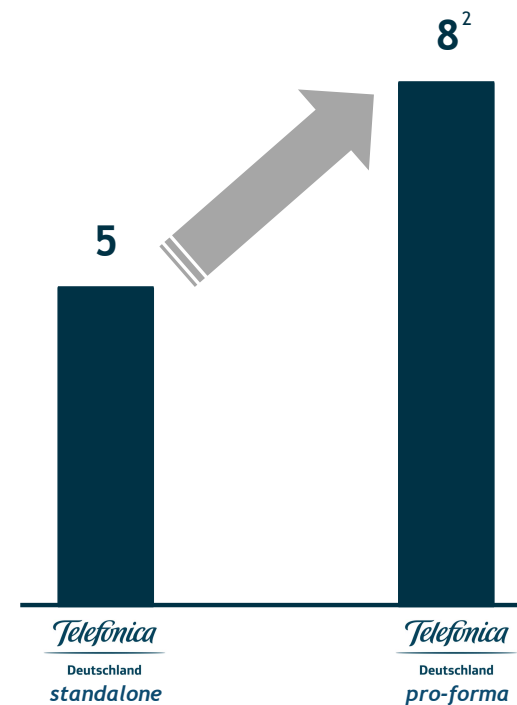
Mobile market shares (Jun-2014)¹

Market size c. 113 million mobile subscribers



Total revenue (FY 2013)

In EUR billion



Note:

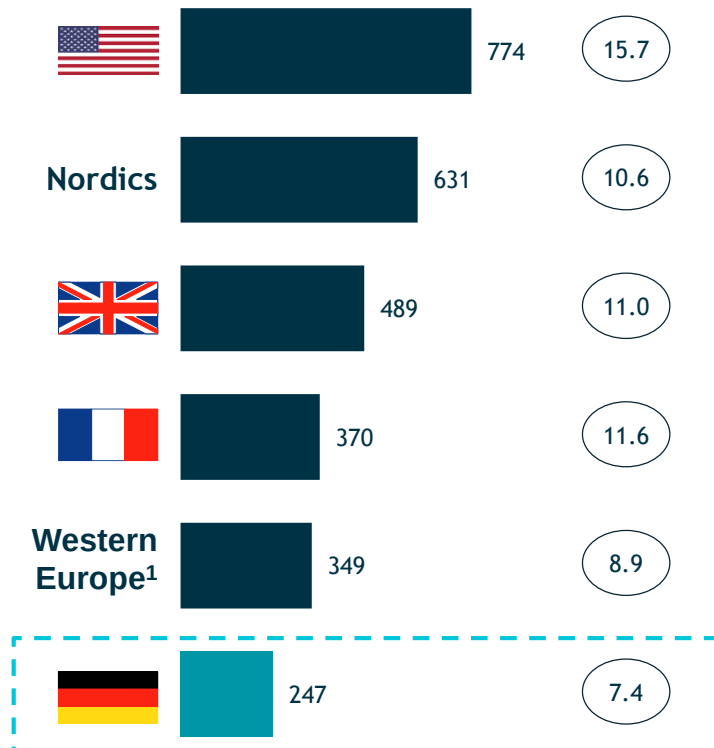
- 1 Based on reported results by Telekom & Vodafone, pro-forma calculation for TEF D
- 2 Combined total customer and revenue numbers based on pro-forma calculations

LTE unlocking a sizeable data monetization opportunity

Average small screen data usage

MB per user per month

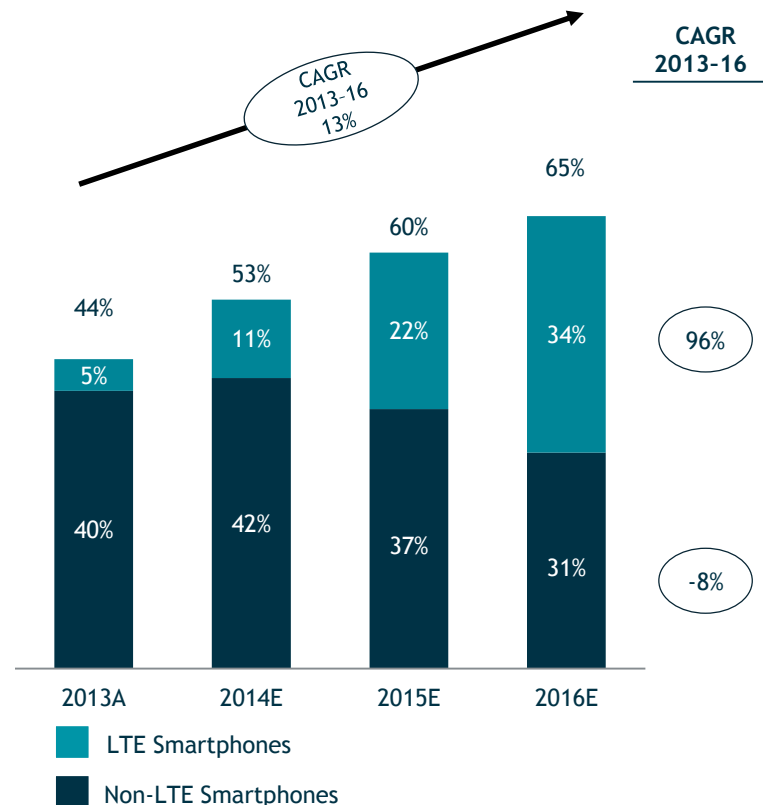
Data ARPU
per month (€)



Source: Analysis Mason Limited. Data relates to 2013
Data ARPU includes SMS and non-SMS

Smartphone handsets penetration in Germany

in (%)



Source: Companies, Analysis Mason Limited
Smartphone penetration: number of 3G / 4G smartphone customers divided by the number of all handsets

Building the Leading Digital Telco in Germany

Offer **Best network experience**



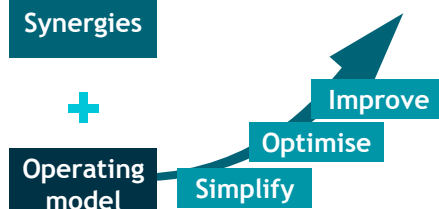
Golden Grid for 2G/3G + LTE roll-out

Offer **Superior customer experience**



Multi-channel & Digital first

Achieve **Cost Leadership**



Synergies & Lean operating model



Keep the Momentum



Integrate quickly



Transform the company

Our successful multi-brand strategy supports superior data monetization

Multi-brand approach¹

Core brands		 
Secondary/ partner brands	  	 
Wholesale	   	  

- Addressing full spectrum of customer segments while optimizing sales reach
- Tailored approach per segment/brand
- Attractive wholesale partnerships

Note:

¹ Selection of current brands. Non exhaustive list

Monetize mobile data and LTE opportunity

Customer insight-led portfolio design

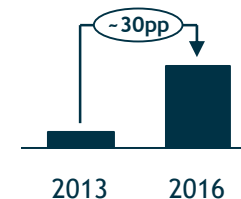
Drive data and smartphone penetration for new and existing customers

Leverage digital services

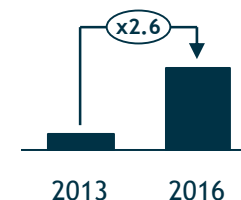
Data upselling / foster LTE deployment

German market trends

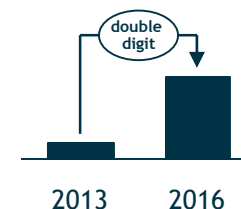
LTE smartphone penetration



Data traffic²



Data revenue CAGR³



Source: Analysys Mason Limited

Notes:

² Total cellular data traffic increase (petabytes)

³ Data revenue (non-SMS)

Best sales & service experience through extensive multi-channel retail and digital approach

Our multi-channel approach



Steer the customer across all channels and provide a seamless customer experience across all touch points

Digital approach

- “Online first” - use digital channels as a foundation for every customer interaction

Web/mobile portals



Apps



Chats/Forums



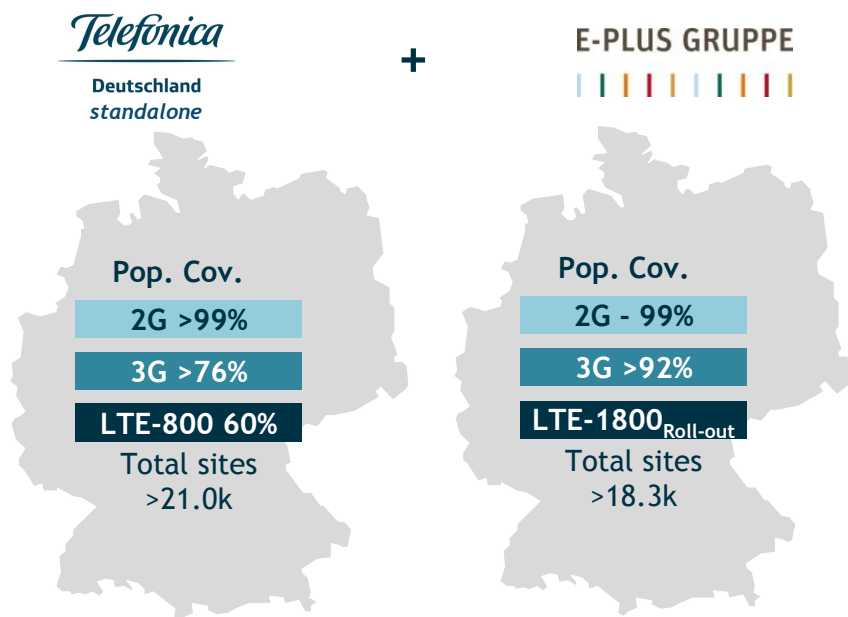
Social media



- Boost brand preference across all digital channels
- Provide better digital experience and increase customer satisfaction (maximize convenience)
- Generate the most value from every contact
- Differentiate ourselves from our competitors with our digital experience

The right infrastructure to compete and monetize the mobile data opportunity

The right network infrastructure assets...



...to improve perceived network quality while accelerating LTE deployment

“Golden grid” for legacy 2G/3G network

Accelerate LTE roll-out

Scale up fiber for backhaul



Strong spectrum holding for infrastructure-based competition

Seize additional value by leveraging scale and Telefónica's global capabilities

2

Fixed Broadband

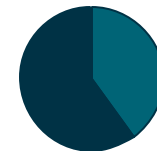
- Nationwide access to incumbent's future proof NGA infrastructure
 - Up to 15m VDSL households - vectoring to enhance high-speed proposition (100 Mbps)
- Allow seamless high-speed multi-access, multi-screen propositions
- Cross-selling opportunity to current E-Plus mobile customer base



Business segment

- Clear opportunity given market size and low Telefónica Deutschland market share today
- SME market approach to mobility-focused industries:
 - Innovative best value for money offerings
 - Improvements in network / service quality
 - Increased marketing effort for customer awareness

O2 Unite



Business revenue share of total telco revenues in Germany

Telefónica global

- Telefónica enables Telefónica Deutschland to benefit from
 - Global scale for sourcing (handsets, network elements etc.)
 - Global services (MNCs¹, roaming, digital, ICT etc.)



Note:

1 MNCs: Multi National Customers

We confirm expected synergies to exceed €5bn (NPV¹)

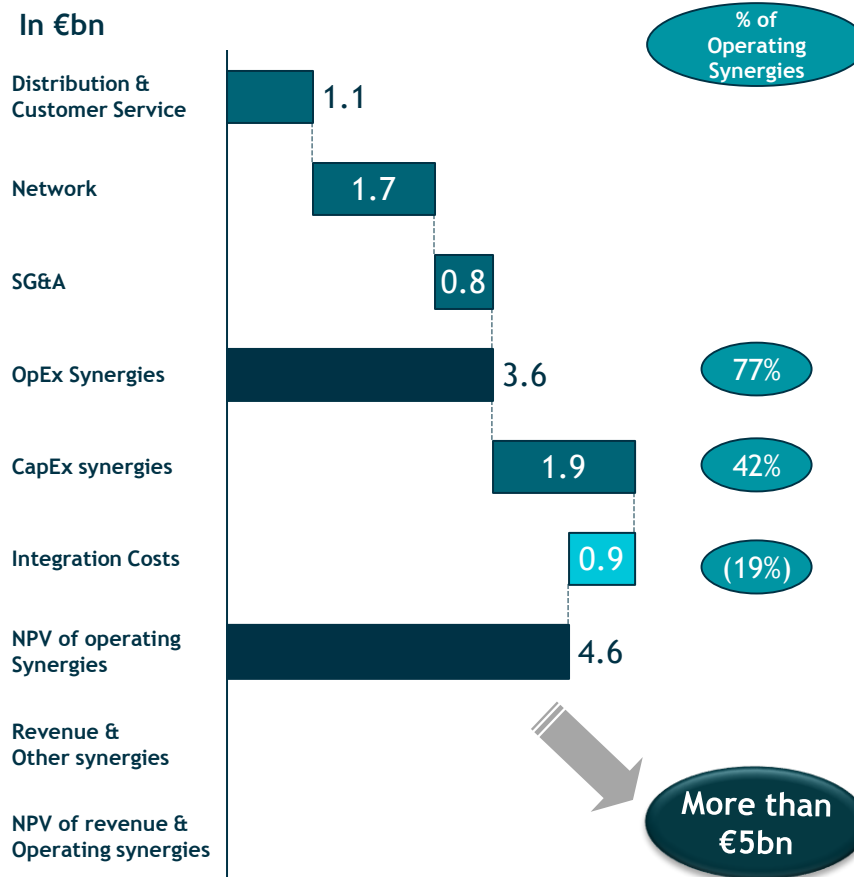
Rapid execution of integration activities

Network Golden Grid
defined (~14K redundant BTS)

Headcount restructuring
plan defined (-1.6K FTEs¹ by 2018)

Full alignment of **Procurement**
processes

Cross & upsell **O₂ Unite & O₂ DSL**
into enlarged customer base



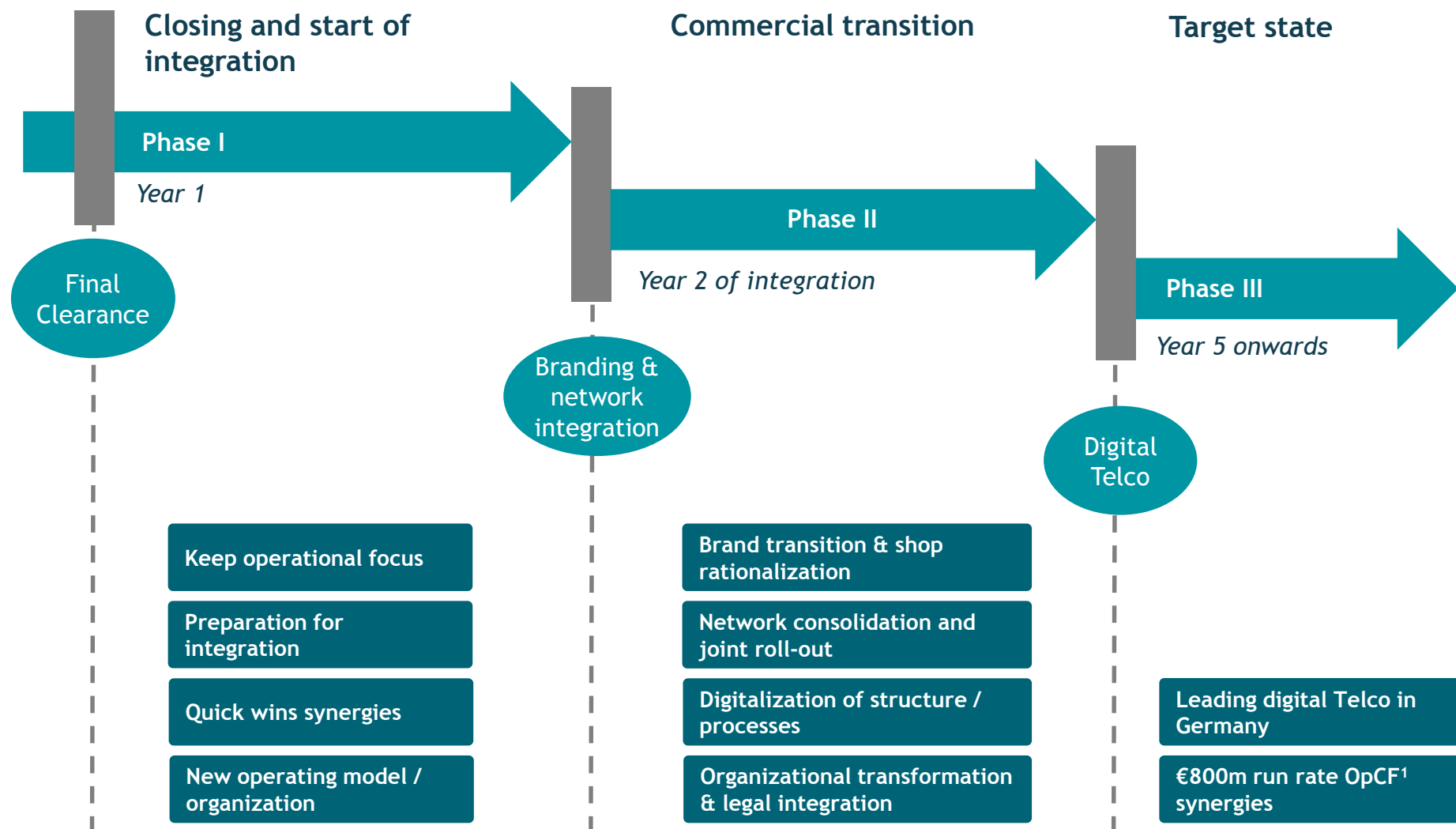
Approx. €800m² run-rate of operating cash flow synergies by year 5 of integration - 80% of which by year 4

Notes:

¹ Calculated as the sum of the present values of forecasted future cash flows including the so-called "terminal value" (NPV of expected future cash flows beyond the explicit forecast horizon) after tax.

² Run-rate of opCF synergies is pre-tax and does not include potential upside from wholesale revenues and others

Integration execution timeline



Significant drivers ahead for improved profitability and FCF generation

Synergies

- Approx. €800m run-rate¹ OpCF² synergies

Profitability

€800m run-rate
opCF synergies

Data monetization

- Drive mobile data ARPU by increasing the demand for data services through:
 - More convenient LTE driving data usage
 - Always offering the latest digital products and services
 - Value-added services (e.g. financial services, media and entertainment services, mobile security solutions, etc.)

LTE

Technology

Digital VAS

Improved
mix

Lean operating model

- Create a leaner organisation by simplifying the operating model and integrating marketing, sales and service units
- Optimize processes, increase network performance and improve IT systems, primarily through digitalization of processes

Operating
model

Simplify

Optimise

Improve

Increased scale

- Economies of scale of the combined company in relation to network, administration, IT, rent and procurement, etc.

Telefónica
Deutschland

Telefónica
Deutschland
+
E-PLUS GRUPPE
| | | | |

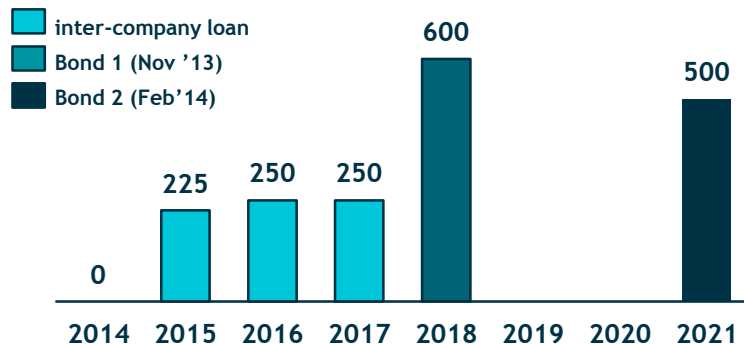
Notes:

- From year 5 of integration onwards
- OIBDA minus CapEx

Solid financial profile, successfully positioned in the debt capital markets

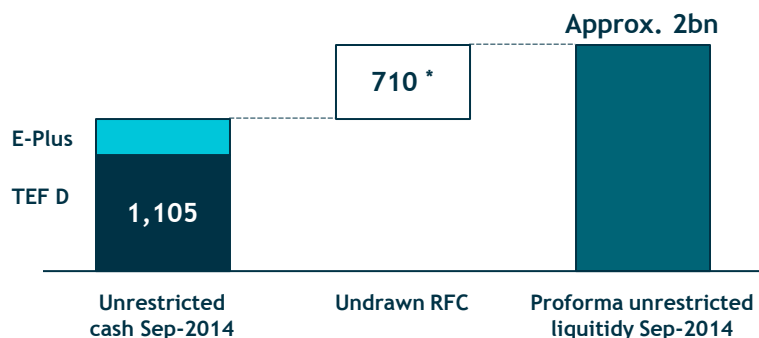
Extended maturity profile

In million Euro



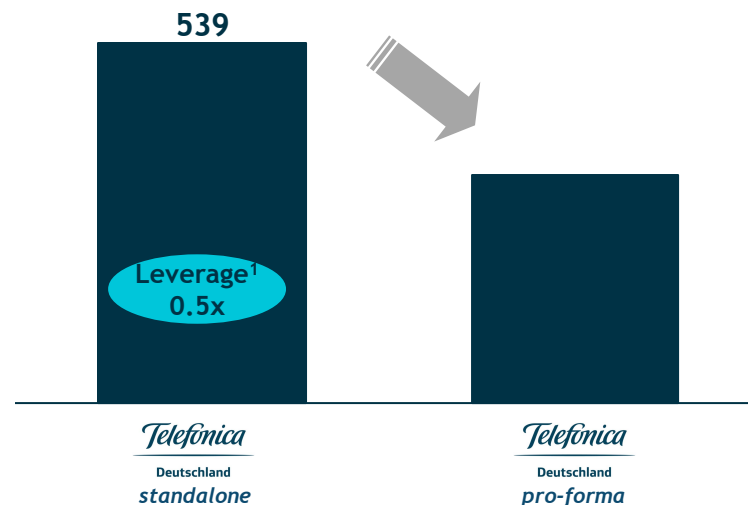
Strong liquidity position

In million Euro



Net Financial Debt² as of Sep-2014

In million Euro



- Target leverage¹ ratio below 1.0x over the medium term

Notes:

- 1 As measured by Net Financial Debt/OIBDA (Last 12 months)
- 2 For definition of Net financial debt please refer to the appropriate section of the Prospectus

* RCF maturing €50m in Q2 2016, €100m in Q3 2016, €200m in Q2 2017, €200m in Q3 2017 and €160m in Q4 2017; all RCF bilateral contracts amended and conditions improved in Q2 and Q3 2014

We aim to maintain an attractive shareholder remuneration policy

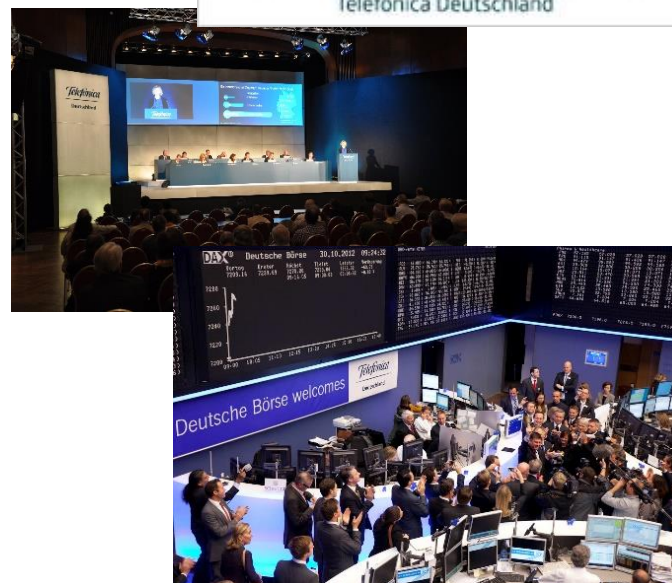
Shareholder remuneration policy - main guidelines¹

Maintain high payout in relation to FCF

Consider expected future synergy generation in dividend proposals

Keep leverage ratio below 1.0x

Current intention to suggest to the general shareholders' meeting a cash dividend of at least €700 million, payable in 2015



Notes:

¹ Refer to the appropriate section of the Prospectus for full policy

Main takeaways

1

Creation of the Leading Digital Telco in the German market

- Customer market leader (47m accesses)¹
- Enhanced competitive position from increased scale, continued innovation and challenger mindset
- Significant data monetization opportunity

2

Superior digital customer experience & enhanced network

- Network quality perception improvement on strong infrastructure assets
- Multi-channel retail and digital approach
- Multi-brand strategy supports data monetization

3

Clear strategy to unlock significant value through synergies

- More than €5bn NPV; €800m Op CF run-rate by year 5
- Main drivers: Network, Customer service and SG&A
- No significant impact from remedies on cost synergies; potential upside from stronger wholesale contribution

4

Enhanced profitability and FCF generation

- Significant upside from rapid realization of synergies
- LTE push further propelling data monetization
- Simplified and lean operational model

5

Value creation for Telefónica Deutschland shareholders

- Aiming to maintain a high FCF payout ratio
- Consider future upside from synergies in dividend proposals
- High financial flexibility with leverage ratio below 1.0x

¹ As of June 2014. Number of accesses of E-Plus determined under TEF D criteria

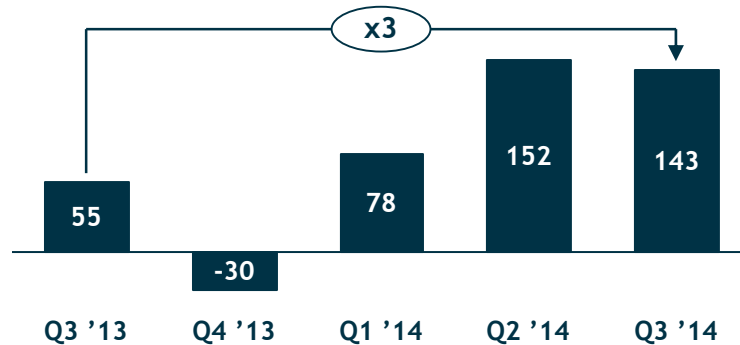
Appendix

Q3 2014 review for TEF D (standalone):

Commercial momentum driving mobile data monetization further

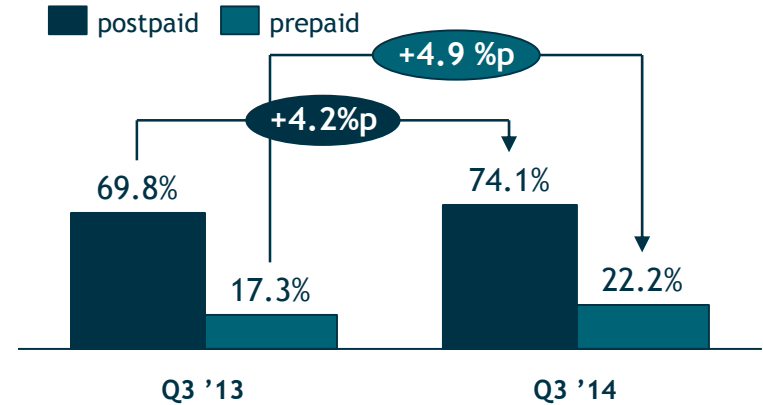
Mobile postpaid: Evolution of Net Additions

In k



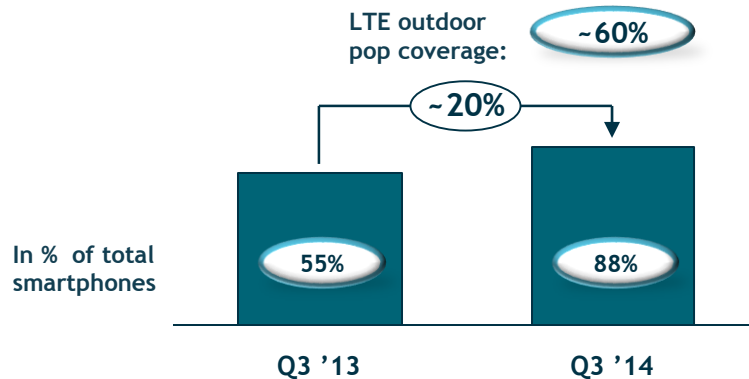
Smartphone penetration¹

In % of O₂ Consumer customer base



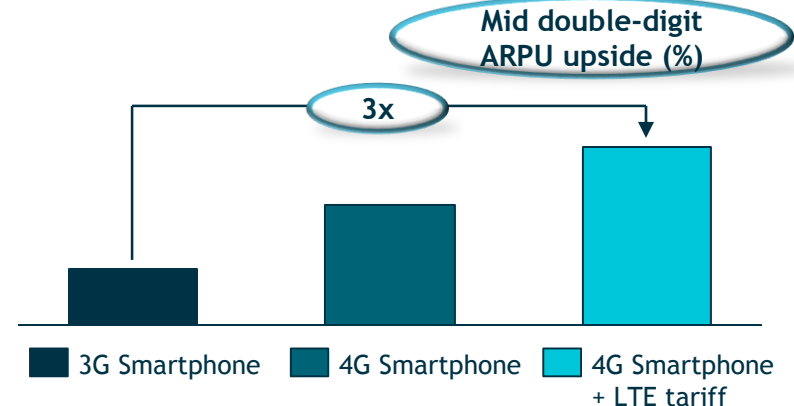
LTE handset adoption

Sale of LTE-enabled smartphones



LTE as a major driver for increase data usage

Average usage per month



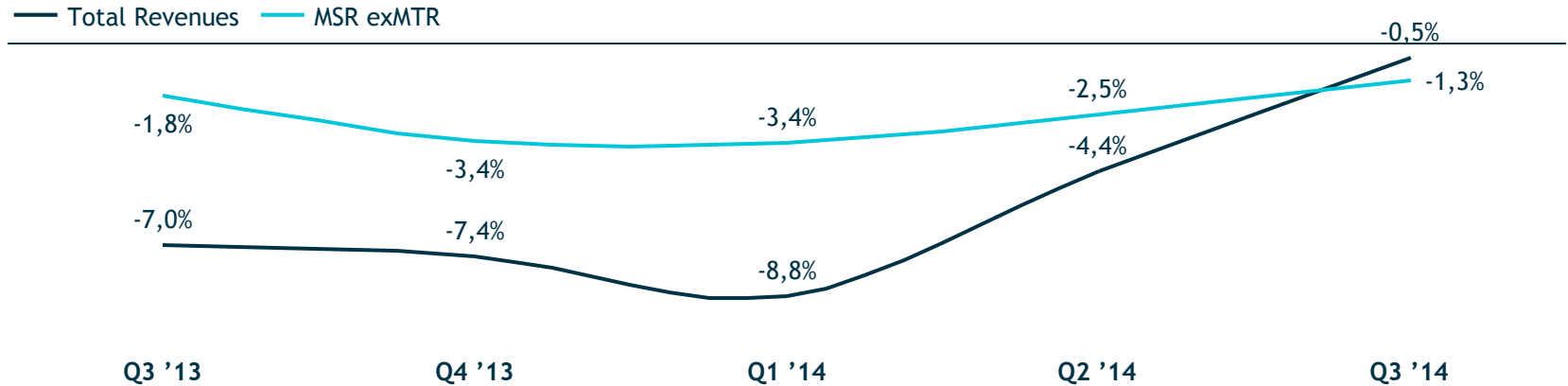
¹ Defined as the number of active mobile data tariffs over total mobile customer base, excluding M2M and data-only accesses.

Q3 2014 review for TEF D (standalone):

Continued improvement in revenue performance

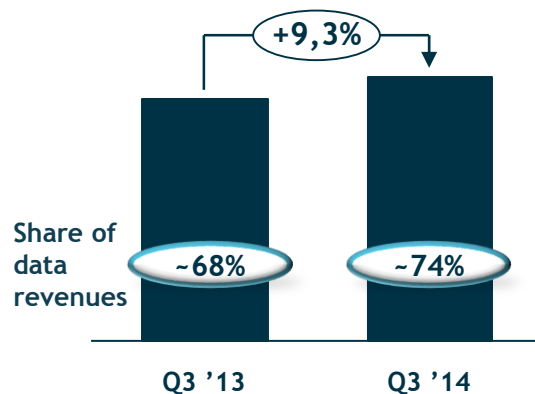
Evolution of Revenues

Year-on-year in %



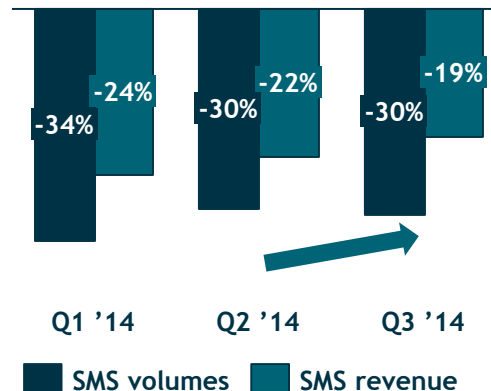
Non-SMS data revenues

Year-on-year



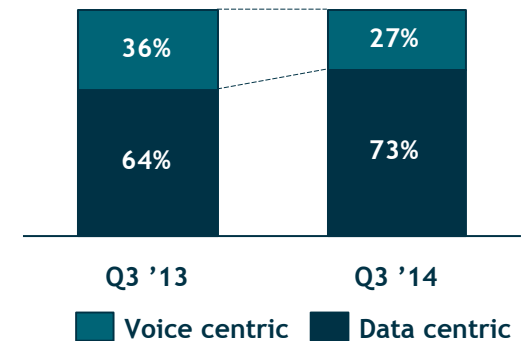
Evolution of SMS

Year-on-year in %



Base Management

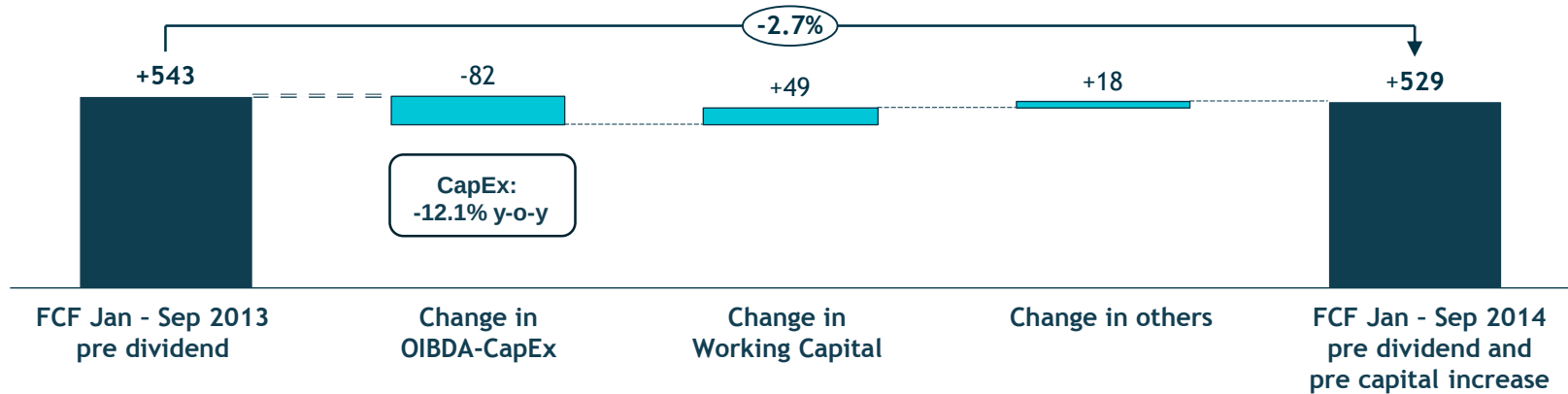
In % of o₂ Consumer Postpaid



Q3 2014 review for TEF D (standalone): Solid financial profile maintained

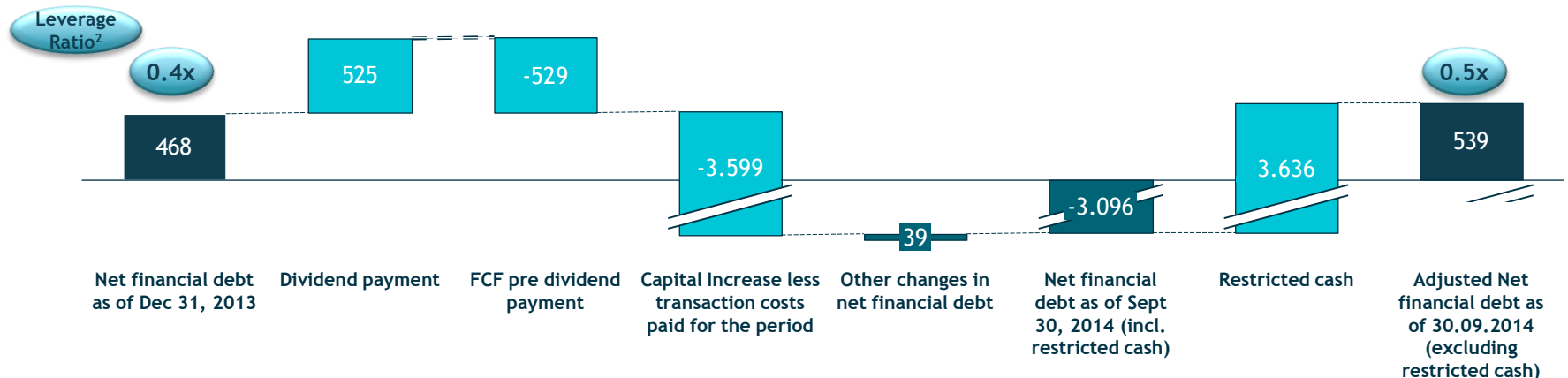
Evolution of Free Cash Flow ¹

Year-on-year in EUR million



Evolution of Net Debt ²

In EUR million



¹ Free cash flow pre dividends from continuing operations is defined as the sum of cash flow from operating activities from continuing operations and cash flow from investing activities from continuing operations.

² For definition of Net Debt and Leverage Ratio please refer to additional materials of Q3 14 results

Transaction structure

2 step transaction structure

1) Acquisition of E-Plus by Telefónica Deutschland for a combination of cash & a stake in the enlarged company

- €3.64bn cash to KPN raised by means of a cash capital increase
- 24.9% stake in the enlarged Telefónica Deutschland (after capital increase) to KPN
- E-Plus asset to Telefónica Deutschland

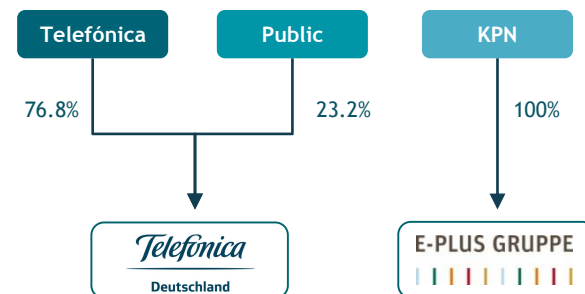
2) Telefónica S.A. subsequently paid €1.3bn to KPN for

- 4.4% stake in the enlarged Telefónica Deutschland

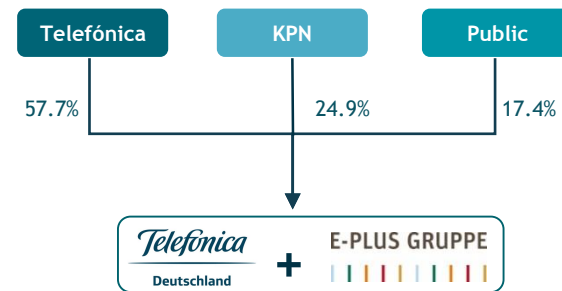
Call option, (exercisable in one year)

- For up to a further 2.9% stake from KPN. Telefónica may exercise its call option for up to €510m plus interest, or buy shares in the market

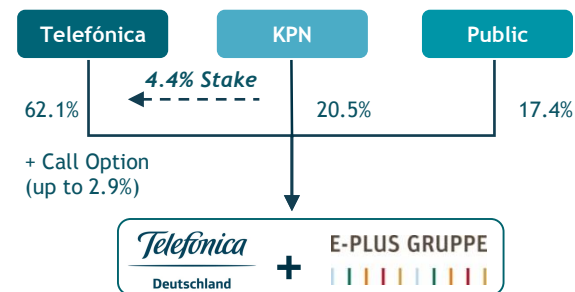
Pre-transaction ownership structure



Intermediate ownership structure



Final ownership structure



Synergy realization based on a thorough analysis and clearly defined integration plan

Network

- Improved quality and capacity in 4G with reduced CapEx requirement
- Consolidation of 2G/3G access networks, backbone and backhaul, with reduced rental, power, maintenance, transport and overhead costs
- Reduction of around 14,000 sites to reach “golden grid”
- Leverage scalable cooperation with Deutsche Telekom regarding fixed line services
- Overall improved network perception of digital services leading to higher customer satisfaction and lower churn



Distribution and customer service

- Leverage and scale effects of broad distribution network and customer service organizations
- Optimization of retail footprint resulting in reduction of rent and overhead
- Focus on digital customer touch points for sales and service initiatives



SG&A

- Accelerated execution of organizational transformation towards lean and digital structures enable reduced IT, admin and rent expenses
- Rationalization of focused advertising and marketing expenditure



Revenue and other

- Additional growth opportunities in consumer and SME segments due to a broader and higher quality network leading to increased satisfaction
- Increased cross selling opportunity for fixed broadband from enlarged combined customer base
- Remedy impact with overall upside potential from strong wholesale component



MNO consolidation is possible in Europe, while all data monetization opportunities remain open

1

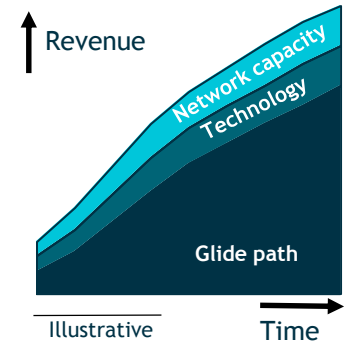
Upfront MBA¹ MVNO - capacity access (20% + opt.+10%)



- ✓ June 25, 2014: MBA MVNO contract
- ✓ August 14, 2014: Agreement for sales of up to 650 shops
- ✓ November 13, 2014: LOI acquisition of yourfone

■ MBA¹ MVNO reflects a continued focus on mobile data monetization

- Scale benefits
- Capacity glide path: throughput, data volume and voice/SMS
- Usage clauses to ensure network quality
- Allows for technological investments and price differential (4G vs. 3G and future)



2

1 potential new MNO entrant

■ No spectrum-related commitments under 2 GHz

- LTE-800 MHz spectrum holding unaffected
- Alignment with “spectrum 2016” project

3

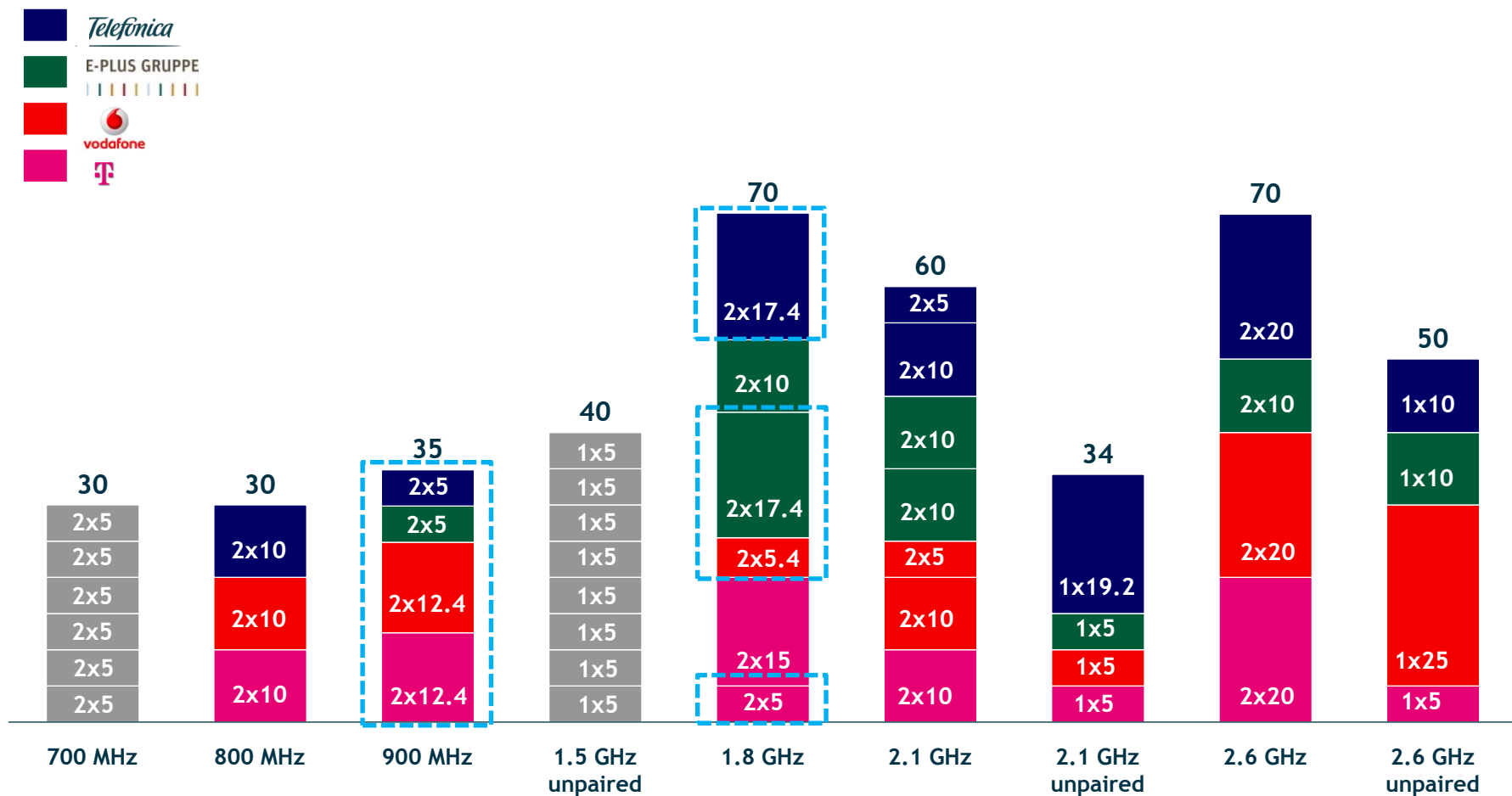
Non-MNO: extend existing contracts until 2025

■ Non-MNOs to continue their current business model

- 4G access with 1 year delay after launch of MBA MVNO

- Most representative 4:3 mobile network consolidation in Europe
- Wholesale price agreements negotiated on a pure commercial basis

Current spectrum landscape in Germany



Expiring in 2016

New spectrum expected to be made available

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