Creating a Leading Digital Telco in Germany

23 July 2013

Telefónica Deutschland Holding AG, Investor Relations
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Creating a Leading Digital Telco in Germany

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Acquisition of E-Plus by Telefónica Deutschland
### Two step transaction structure

1. **Acquisition of E-Plus by Telefónica Deutschland for a combination of cash and a stake in the enlarged Telefónica Deutschland**
   - €3.70bn of cash
   - 24.9% stake in enlarged Telefónica Deutschland (after capital increase)

2. **Telefónica subsequently to acquire a 7.3% stake from KPN for €1.30bn in order to maintain a 65% ownership in the enlarged Telefónica Deutschland**
   - Transaction to unlock significant value, with synergies of €5.0–5.5bn NPV
   - Total consideration of €5bn in cash and a 17.6% stake in the enlarged Telefónica Deutschland

### Recommended transaction

- Recommended transaction approved by Telefónica’s Board of Directors and Telefónica Deutschland’s Supervisory Board
- Transaction has support from KPN’s Board of Management, and from KPN’s Supervisory Board
- KPN shareholders’ approval required at KPN’s General Meeting in H2 2013
- Telefónica Deutschland shareholders’ approval required at Telefónica Deutschland’s General Meeting in H2 2013
- Transaction expected to close in mid 2014, following clearance from relevant authorities

### Key dates

- KPN shareholders’ approval required at KPN’s General Meeting in H2 2013
- Telefónica Deutschland shareholders’ approval required at Telefónica Deutschland’s General Meeting in H2 2013
- Transaction expected to close in mid 2014, following clearance from relevant authorities
Transaction structure

Transaction summary

Two step structure

1. Acquisition of E-Plus by Telefónica Deutschland for a combination of cash and a stake in the enlarged Telefónica Deutschland
   - €3.70bn of cash, financed through a rights issue fully underwritten by Telefónica and a group of banks
   - 24.9% stake in enlarged Telefónica Deutschland (after capital increase)

2. Telefónica subsequently to acquire a 7.3% stake of the enlarged Telefónica Deutschland from KPN for €1.30bn, post-transaction, in order to maintain a 65% ownership in the enlarged Telefónica Deutschland
   - Total consideration of €5bn in cash and a 17.6% stake
Transaction rationale

1. Creation of a Leading Digital Telco
   - A leading player with a combined customer base of 43m, 42% in postpaid
   - Strong scale benefits with combined mobile revenue market share of 32%
   - Driving mobile market growth in Germany since 2010:
     - +2.2pp in postpaid customer share
     - +5.8pp in prepaid customer share
   - Strong capabilities for mobile data

2. Value crystallization through significant synergies
   - NPV of synergies of €5.0–5.5bn, net of integration costs
     - Net savings from year 2
     - Annual run-rate synergies of approx. €800m; 75% of run-rate synergies by year 4
   - Incremental value from additional revenues, financial and tax synergies
   - Highly experienced management team with a proven track record of integration

3. Enhanced Profitability & FCF in Germany
   - Improved profitability and enhanced cash flow generation
   - Stronger competitive position from increased scale

Source: Company data, broker research
Transaction rationale (cont'd)

4. Creating a superior customer experience
   - Customers to benefit from the best high speed mobile and fixed experience from a single LTE network and access to future-proof DT NGA network
   - Strong multi-brand portfolio across segments
   - Offering ICT / cloud solutions for business customers
   - Best distribution channel and outstanding customer service
   - Ready for convergence through cross-selling / up-selling opportunities
   - Leveraging Telefónica’s global capabilities: Digital innovation, scale,....

5. Value Creation for Telefónica Deutschland Shareholders
   - Unlocks significant value for Telefónica Deutschland shareholders
   - Increases financial flexibility (improving leverage) while maintaining an attractive shareholder remuneration
     - Conservative pro forma balance sheet
   - EPS and FCF accretive from first year of full operation\(^{(1)}\)

1. Based on run-rate synergies before integration costs
Creation of a Leading Digital Telco

**Q1 2013 mobile revenue market share (%)**

- Enlarged Telefónica Deutschland: 31.6%
- T-Mobile: 34.8%
- Vodafone: 33.6%
- Telefónica Deutschland: 17.6%
- E-Plus: 14.1%

**2010 – 2012 Postpaid mobile market share growth (pp)**

- Enlarged Telefónica Deutschland: 2.2%
- T-Mobile: 2.0%
- Vodafone: (4.2)
- Telefónica Deutschland: 2.0%
- E-Plus: 0.2%

**2010 – 2012 Prepaid mobile market share growth (pp)**

- Enlarged Telefónica Deutschland: 5.8%
- T-Mobile: (0.3)
- Vodafone: (5.5)
- Telefónica Deutschland: 0.9%
- E-Plus: 5.0%

- Combining Telefónica Deutschland’s and E-Plus’s track records of growth with Telefónica Deutschland’s capacity for MBB

Source: Company data, broker research
1 Highly attractive mobile market

- Relatively low churn
  - Monthly Churn, 2012 (%)
    - Germany: 2.0
    - EU Average: 2.6

- Strong subscriber base growth
  - 2013E YoY Growth (%)
    - Germany: 2.7
    - EU Average: 1.4

- Smartphone penetration upside
  - Smartphone connections as % of mobile connections, 2012 (%)
    - Germany: 27.4
    - EU Average: 34.4

- EBITDA growth
  - 2009 – 2013E CAGR (%)
    - Germany: 1.0
    - EU Average: (4.3)

Source: WCIS, broker research
Identified and realisable synergies of €5.0 – 5.5bn NPV

**Distribution and customer service**
- Rationalisation of distribution network
- Increased efficiency in customer service costs leveraging best practices and scale
- Channel management and overheads

**Network**
- Focused rollout on one common nationwide LTE network and improved quality from 3G network consolidation
- Backbone, backhaul and core network consolidation, with reduced OpEx from network integration (rentals, power, maintenance, transport costs, overheads)
- Site consolidation and rationalisation: reduction of around 14,000 sites
- Increased efficiency by leveraging scalable transmission agreement with Deutsche Telekom

**SG&A**
- Reduced SG&A expenses
- Processes rationalisation
- Continued focus on becoming a more lean and agile organization

**Revenue and other**
- Exploit SME opportunity from a broader and higher quality platform
- Improved customer satisfaction
- High speed fixed broadband cross-selling opportunity across an enlarged customer base

Operating synergies of €4.5bn NPV

Revenue and other synergies of €0.5-1.0bn NPV
Synergies value of €5.0 – 5.5bn NPV

NPV of €5.0-5.5bn
- Net savings from year 2
- Run-rate synergies approx. €800m from year 5; 75% of run-rate synergies by year 4
- Incremental value from additional revenues, financial and tax synergies
3 Stronger competitive position from increased scale in Germany
Based on consensus forecasts

**2013 Revenue**

<table>
<thead>
<tr>
<th></th>
<th>In EUR billion</th>
</tr>
</thead>
<tbody>
<tr>
<td>Telefónica Deutschland</td>
<td>5.1</td>
</tr>
<tr>
<td>E-Plus</td>
<td>3.2</td>
</tr>
<tr>
<td>Enlarged Telefónica Deutschland proforma</td>
<td>8.3</td>
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</table>

**2013 OIBDA**

<table>
<thead>
<tr>
<th></th>
<th>In EUR billion</th>
</tr>
</thead>
<tbody>
<tr>
<td>Telefónica Deutschland</td>
<td>1.3</td>
</tr>
<tr>
<td>E-Plus</td>
<td>0.9</td>
</tr>
<tr>
<td>Enlarged Telefónica Deutschland proforma</td>
<td>2.2</td>
</tr>
</tbody>
</table>

**2013 Capex**

<table>
<thead>
<tr>
<th></th>
<th>In EUR billion</th>
</tr>
</thead>
<tbody>
<tr>
<td>Telefónica Deutschland</td>
<td>0.7</td>
</tr>
<tr>
<td>E-Plus</td>
<td>0.6</td>
</tr>
<tr>
<td>Enlarged Telefónica Deutschland proforma</td>
<td>1.3</td>
</tr>
</tbody>
</table>

**2013 OpFCF**

<table>
<thead>
<tr>
<th></th>
<th>In EUR billion</th>
</tr>
</thead>
<tbody>
<tr>
<td>Telefónica Deutschland</td>
<td>0.6</td>
</tr>
<tr>
<td>E-Plus</td>
<td>0.3</td>
</tr>
<tr>
<td>Enlarged Telefónica Deutschland proforma</td>
<td>0.9</td>
</tr>
</tbody>
</table>

Source: Broker consensus. Not adjusted for accounting differences, pre-synergies

1 Defined as OIBDA-Capex
**Enhanced profitability and cash flow generation in Germany**

Pro forma financial impact on Telefónica Deutschland, based on consensus forecasts

<table>
<thead>
<tr>
<th>Revenues</th>
<th>OIBDA</th>
<th>OpFCF&lt;sup&gt;1&lt;/sup&gt;</th>
</tr>
</thead>
<tbody>
<tr>
<td>In EUR billion</td>
<td>In EUR billion</td>
<td>In EUR billion</td>
</tr>
<tr>
<td>2013</td>
<td>2013 proforma</td>
<td>2013</td>
</tr>
<tr>
<td>5.1</td>
<td>8.3</td>
<td>1.3</td>
</tr>
</tbody>
</table>

- **EPS and FCF accretive from first year of full operation<sup>(2)</sup>**

Source: Broker consensus, not adjusted for differences in accounting policies

<sup>1</sup> Defined as OIBDA-Capex

<sup>2</sup> Based on run-rate synergies before integration costs
Creating superior customer experience

- Strong commitment to invest in the German market
- Spectrum and network capacity to cope with growing data volumes
- Access to fibre backhaul
- Environmental benefits through reduction of sites
- Improved situation in the business sector
- Improved network quality for E-Plus subscribers through access to Telefónica Deutschland’s state-of-the-art network

- Over 1,800 points of sale to serve our customers directly
- Outstanding customer service to provide the best digital experience

- Combination of the most creative players in the market
- Tariff innovation, voice & mobile data bundling
- Multi-brand strategy to better serve different customer needs
- Innovative propositions to offer ICT / cloud solutions for business customers

- Increased up-selling and cross-selling potential extended to E-Plus customer base
- Significant tangible benefits such as churn reduction

- Benefits from leveraging Telefónica’s best practices
- Innovation through Telefónica Digital
- Global capacity: Data centers, scale benefits and shared services
Expected transaction timetable

Key milestones:
- 23 July 2013: Signing of Agreement
- July/Aug 2013: Submission for regulatory clearance
- September 2013: KPN convocation of EGM

Key approvals:
- H2 2013: KPN EGM
- H2 2013: Telefónica Deutschland EGM

Results announcements:
- 23 July 2013: Telefónica Deutschland H1 results
- 23 July 2013: KPN H1 results
- 25 July 2013: Telefónica H1 results

Mid 2014: Completion of merger

Regulatory approval of acquisition

Mid 2014: Regulatory approvals expected and other conditions cleared
Closing remarks

- A natural strategic move for Telefónica Deutschland to create a Leading Digital Telco with focus on mobile data and LTE enhancement
- Significant value creation through €5.0 – 5.5bn NPV synergies crystallization
- Germany is the largest mobile market in Europe and is the most advanced in data monetisation
- Substantial value creation for Telefónica and Telefónica Deutschland shareholders
  - Investing in future growth while improving financial flexibility
  - Enhancing cash flow generation profile
  - Accretive for Telefónica and Telefónica Deutschland EPS and FCF from year 1
January – June 2013
Operating & Financial performance
### Overview of key financials

Top line pressures compensated by more efficient usage of resources

<table>
<thead>
<tr>
<th></th>
<th>In EUR million</th>
<th>January - June</th>
<th>April - June</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2013</td>
<td>2012</td>
<td>% y-o-y</td>
</tr>
<tr>
<td>Revenues</td>
<td>2,445</td>
<td>2,554</td>
<td>(4.2)</td>
</tr>
<tr>
<td>OIBDA</td>
<td>572</td>
<td>597</td>
<td>(4.1)</td>
</tr>
<tr>
<td>OIBDA margin</td>
<td>23.4%</td>
<td>23.4%</td>
<td>0.0 p.p.</td>
</tr>
<tr>
<td>Group fees</td>
<td>(31)</td>
<td>(32)</td>
<td>(1.5)</td>
</tr>
<tr>
<td>OIBDA before group fees</td>
<td>603</td>
<td>629</td>
<td>(4.0)</td>
</tr>
<tr>
<td>OIBDA before group fees margin</td>
<td>24.7%</td>
<td>24.6%</td>
<td>0.1 p.p.</td>
</tr>
<tr>
<td>Capex</td>
<td>296</td>
<td>271</td>
<td>9.4</td>
</tr>
<tr>
<td>Free Cash Flow(^1) pre dividends from continuing operations</td>
<td>345</td>
<td>152</td>
<td>n.m.</td>
</tr>
</tbody>
</table>

\(^1\) Free Cash flow pre dividends defined as OpCF minus working capital minus interest payments and taxes minus other changes. In 2013 no discontinued operations did exist.
## Revenue performance

Ongoing trends from the transition to a data-centric environment

### Wireless service revenue
- Driven by postpaid dynamics
- Non-SMS data revenue acceleration
- Lower y-o-y trading performance
- Higher y-o-y tariff renewals in the base

### Handset sales
- Reflecting y-o-y phasing in device launches
- Encouraging trends from LTE-enabled devices

### Wireline revenues
- Sustaining recent trends
- Lower retail DSL customer base
- Declining voice transit business

### Total revenue

<table>
<thead>
<tr>
<th></th>
<th>Q2 '12</th>
<th>Q2 '13</th>
<th>Q2 '13 ex MTR</th>
</tr>
</thead>
<tbody>
<tr>
<td>Other</td>
<td>1,295</td>
<td>1,247</td>
<td>1,216</td>
</tr>
<tr>
<td>Wireline</td>
<td>344</td>
<td>311</td>
<td></td>
</tr>
<tr>
<td>Handset</td>
<td>161</td>
<td>155</td>
<td></td>
</tr>
<tr>
<td>Wireless</td>
<td>789</td>
<td>779</td>
<td>748</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>o/w Non-SMS data</th>
<th>Q2 '12</th>
<th>Q2 '13</th>
<th>Q2 '13 ex MTR</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wireless</td>
<td>189</td>
<td>235</td>
<td>235</td>
</tr>
</tbody>
</table>
Trading performance in Q2 2013
Consistent approach to a complex market, driving smartphone penetration

- **60k postpaid net additions**
  - Market focus on retention and customer base
  - Better customer mix from O₂ Blue All-in push
  - Successful management of tariff migrations

- **27k prepaid net additions**
  - Strong performance from secondary brands
  - Adoption of new prepaid smartphone tariffs

- **Improved smartphone penetration**
  - More affordable handsets & digital behaviour
  - Prepaid opportunity driven by new tariff offers

- **Stable retail DSL net disconnections (-40k)**
  - Continuous uptake of VDSL gross additions
  - (28% of gross adds in VDSL available regions take speed option)
Continuous improvement of mobile data monetisation
Focus on execution based on a clear set of priorities

1. Drive data & smartphone penetration for new & existing customers
2. Fit demand of customer base to volume & speed portfolio
3. Data upselling / foster LTE adoption

Traffic vs Revenues
- Non-SMS data revenue (y-o-y%)
- Data traffic (y-o-y%)
- +21%
- +25%

Revenue structure of WSR
- Incoming voice
- Incoming SMS
- Out-of-Bundle
- In-Bundle

Q2 '12 vs Q2 '13
- 9% vs 7%
- 7% vs 4%
- 34% vs 24%
- 51% vs 64%

1 Within O2 corebrand postpaid segment
Continued dynamics in O₂ massmarket postpaid
Tangible results from base management leveraging O₂ Blue All-in

Main drivers for wireless service revenues

Q-o-Q absolute performance ex MTRs

% vs Q4-Q1

Q1 '13

Trading

Tariff migrations

Base effects

Seasonal effects

Q2 '13

Customer base management

ARPU dilution (€)

-33%

Jan

Jun

Tariff renewals (#)

High Mid Low

Q2 '12

Q2 '13

Up-selling opportunities

Weighted ARPU from portfolio mix

+9%

O₂ Blue (2012)

O₂ Blue All-in (2013)
Stable y-o-y OIBDA performance
Revenues downside partly offset by cost savings

OIBDA

in EUR million
(changes y-o-y)

OIBDA H1 2012
+597

Revenues
-108
-29
-80

Other income
+8
+1

Supplies
+54
+5
+49

Personnel
0
-1

Other Expenses
+1
+22

OIBDA H1 2013
+572

OIBDA margin

in %

Group Fees as % of Revenue

H1 2012
23.4%
1.2%

H1 2013
23.4%
1.3%

Telefónica Deutschland Holding AG

Public – Nicht vertraulich
03
Q&A
Q&A

Telefónica Deutschland Q2 2013 results conference call
For further questions please contact IR department

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