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Telefónica Deutschland – Preliminary results for January to June 2022

Expanding FY22 OIBDA outlook on sustained commercial traction & financial performance

- Continued commercial traction on core business strength, celebrating O₂ brand's 20th anniversary in Germany and winning 374k postpaid net additions in Q2 22
- Revenues maintained growth path in Q2 22, +5.8% y-o-y, driven by sustained mobile service revenue (MSR) momentum
- OIBDA¹ grew +2.7% y-o-y in Q2 22 on improved MSR quality & continued efficiency gains - underlying² +4.7% y-o-y
- C/S of 14.5% – on the back of strong progress with 5G rollout, ambition raised to ~60% pop coverage by YE22 within unchanged Capex envelope
- Driving ESG strategy – promoting a sustainable digital future
- Expanding FY22 OIBDA outlook upwards to 'low to low mid-single digit percentage growth'

Operating performance

Telefónica Deutschland delivered another quarter of strong operational and financial momentum in Q2 22. The company continued to expand its mobile market share in a dynamic yet rational environment on the back of core business strength building on network parity and ESG leadership.

Telefónica Deutschland remains focussed on its ESG roadmap delivery and is well on track to reduce its emissions by 90% and neutralising residual emissions latest by 2025. At the same time, social responsibility and digital inclusion are part of the company's identity. Initiatives such as the 'Digitaltag' held in the company's BASECAMP in Berlin promote digital literacy by teaching the relevant skills. Telefónica Deutschland's employees are also highly committed to social engagement. At this year's 'Volunteering Day', they supported Ukraine refugees with hands-on support, i.e. providing language support for children and online job application coaching. The Ukraine Relief Fund of the 'Aktionsbündnis Deutschland hilft' acknowledged the willingness of Telefónica Deutschland's employees to donate, with the company topping up these donations.

Telefónica Deutschland has celebrated the 20th anniversary of the O₂ brand in Germany. The launch of the promotional tariff, O₂ Grow, once again underpinned that the company continues to lead innovation in German mobile. Commercial momentum has continued on the back of strong customer demand for the O₂ portfolio and a solid contribution from partner brands, resulting in sustained growth of the contract mobile base. The anticipated temporarily higher churn on the back of the European Electronic Communications Code (EECC) introduction started to normalise in Q2 22.

Telefónica Deutschland continued to execute its 'investment for growth' programme according to plan in its final year. The 5G network roll-out is making strong progress and the company already has achieved the targeted ~50% pop coverage well ahead of target. Consequently, Telefónica Deutschland raised its 5G ambition to ~60% pop coverage by YE 2022 within an unchanged Capex envelope due to roll-out efficiencies.

¹ Adjusted for exceptional effects. In Q2 22, exceptional effects amounted to EUR -1m of restructuring costs (EUR -2m in Q2 21).

² Excluding non-recurrent special factors of EUR 12m in Q2 21.

Mobile business

Mobile postpaid maintained its commercial momentum on the back of strong customer demand for the O₂ portfolio and a solid contribution from partner brands. As a result, net additions totalled +374k in Q2 22, stable y-o-y (+374k in Q2 21; +661k in H1 22 vs. +594k in H1 21).

M2M reported +37k net additions in Q2 22 vs. +82k in Q2 21 (+71k in H1 22 vs. +124k in H1 21).

Mobile prepaid posted +370k net additions in Q2 22 (+91k net additions in Q2 21; +271k in H1 22 vs. -18k in H1 21) supported by revenue neutral SIM card reactivations, the company's support programme for refugees from Ukraine as well as some seasonality.

The anticipated temporarily higher churn on the back of the European Electronic Communications Code (EECC) introduction started to normalise in Q2 22. **Postpaid churn in the O₂ brand** was flat y-o-y at 0.8% in Q2 22 (1.0% in H1 22, +0.1 p.p. y-o-y) leveraging network parity.

Telefónica Deutschland's **mobile customer accesses** grew to 46.7m (+3.8% y-o-y) as of 30 Jun-22, driven by strong growth (+6.6% y-o-y) of the **mobile postpaid base**, climbing to 25.8m accesses (55.2% of the company's total mobile access base, up +1.4 p.p. y-o-y). **M2M accesses** were 1.7m as of 30 Jun-22, a strong increase of +9.8% y-o-y while the **mobile prepaid base** was flattish (-0.1% y-o-y) at 19.2m.

O₂ postpaid ARPU was -0.7% y-o-y in Q2 22 (-0.6% y-o-y in H1 22) reflecting customer demand for high value tariffs offset by a combination of the accelerated MTR glidepath and some enhanced focus on customer loyalty including retention and bundle benefits. Underlying³ O₂ postpaid ARPU was +0.4% y-o-y both in Q2 22 and in H1 22. **Prepaid ARPU** was EUR 6.6 in Q2 22, up +5.2% y-o-y (+5.4% to EUR 6.5 in H1 22).

Fixed business

Fixed broadband customer base was marginally up at 2.3m accesses (+0.2% y-o-y) as of 30 Jun-22. **VDSL base** stood at 1.8m accesses, up +0.7% y-o-y to 81.1% of fixed BB customer base. In Q2 22, fixed BB registered +5k net additions (-6k net disconnections in H1 22) leveraging Telefónica Deutschland's technology agnostic O₂ my Home products that was enriched by a new 1 Gbit/s offer on the cable network during Q2 22. Fixed-mobile substitution (FMS) also remained popular.

Fixed churn reached 1.1% in Q2 22 and was marginally up (+0.2 p.p. y-o-y) mainly as a result of the EECC implementation.

Fixed broadband ARPU continued to grow as a result of the increasing share of high value customers in the base and stood at EUR 24.7 in Q2 22, +2.1% y-o-y (+2.5% to EUR 24.6 in H1 22).

³ Excluding MTR effects. MTR glidepath: EURc 0.78/min effective 1 Dec-20 / EURc 0.70/min effective 1 Jul-21 / EURc 0.55 effective 1 Jan-22.

Financial performance

Revenues maintained their growth path, increasing +5.8% y-o-y to EUR 2,003m in Q2 22 (+5.5% y-o-y to EUR 3,949m in H1 22) on sustained mobile service revenue growth momentum despite tough comps⁴ in the quarter and on strong demand for handsets.

Mobile service revenues⁵ grew +2.3% y-o-y in Q2 22 to EUR 1,402m (EUR 2,753m in H1 22, +2.8% y-o-y) despite the negative impact from the accelerated MTR glidepath⁶ combined with tough comps⁴ in the second quarter. Underlying⁷ growth was of +3.4% y-o-y, both in Q2 22 and H1 22. Mobile service revenues benefitted from the ongoing strong commercial traction of the O₂ brand as well as some support from the recovery of international roaming.

Continued strong demand for high value devices and good availability of devices at Telefónica Deutschland drove **handset revenues** in Q2 22, posting **+24.1% y-o-y growth to EUR 395m** (+18.4% y-o-y to EUR 787m in H1 22).

Fixed revenues grew +0.9% y-o-y to EUR 201m in Q2 22 (EUR 399m in H1 22, -0.4% y-o-y). **Fixed retail BB** growth trends were in-tact and posted a **+2.5% y-o-y increase** in Q2 22 (+2.1% in H1 22) reflecting the increasing share of high value customers in the base. The low margin international carrier business continues to reflect the anticipated drag from European mobile termination rates.

Other income reached EUR 40m in Q2 22 and EUR 72m in H1 22 (EUR 28m in Q2 21 and EUR 57m in H1 21).

Operating expenses⁸ included restructuring expenses in the amount of EUR -1m and increased **+7.9% y-o-y to EUR 1,415m** in Q2 22 (+5.6% y-o-y to EUR 2,792m in H1 22).

- **Supplies** increased +12.9% y-o-y to EUR 629m in Q2 22 (+6.5% y-o-y to EUR 1,221m in H1 22) as the positive effects from the MTR-cut⁶ were more than off-set by volume driven higher hardware cost of sales. Connectivity-related cost of sales and hardware cost of sales accounted for 37% and 60% of H1 22 supplies, respectively.
- Underlying, **personnel expenses** were lower -0.6% y-o-y at EUR 149m (including EUR -1m of restructuring expenses) in Q2 22 and flattish (+0.2% y-o-y) at EUR 302m in H1 22. The y-o-y lower FTE base is partly compensating for the general pay-rise of 1.75% as of 1 Dec-21. In reported terms, personnel expenses in H1 22 were up +6.0% y-o-y mainly due to received social security payments in H1 21 for employees of temporary closed O₂ shops during the government enforced lockdown.
- **Other operating expenses** (other Opex) were up by +2.7% y-o-y to EUR 613m in Q2 22 (+3.8% y-o-y to EUR 1,224m in H1 22) reflecting technology transformation, commercial activity including an enhanced retention focus and more normalised marketing spend vs. a partial lockdown quarter in the prior year. Commercial and non-commercial costs accounted for 67% and 30% of other Opex in Q2 22, respectively. Group fees accounted to EUR 9m in Q2 22 and EUR 17m in H1 22 (EUR 6m in Q2 21 and EUR 15m in H1 21).

OIBDA⁹ grew +2.7% y-o-y to EUR 629m in Q2 22 (+4.9% y-o-y to EUR 1,231m in H1 22) despite tough comps⁴ in the quarter. OIBDA growth reflects improved operational leverage mainly in mobile on the back of continued own brand momentum, further efficiency gains as well as some international roaming tailwinds (underlying⁷ growth of +4.7% y-o-y in Q2 22 and +5.9% y-o-y in H1 22). **OIBDA⁹ margin stood at 31.4%** in Q2

⁴ Q2 21 and H1 21 respectively, included non-recurrent special factors in the amount of EUR +14m at revenues/MSR and EUR +12m at OIBDA level.

⁵ Mobile service revenue includes base fees and fees paid by the company's customers for the usage of voice, SMS and mobile data services; it also includes access and interconnection fees as well as other charges levied on partners for the use of the company's network.

⁶ MTR-cut from EURc 0.78 to EURc 0.70 per minute as of 1 Jul-21 and from EURc 0.70 to EURc 0.55 per minute as of 1 Jan-22.

⁷ Excluding non-recurrent special factors.

⁸ Operating expenses include impairment losses in accordance with IFRS 9 in the amount of EUR 24m in Q2 22 and EUR 44m in H1 22 (EUR 12m in Q2 21 and EUR 33m in H1 21).

⁹ Adjusted for exceptional effects. In Q2 22 as well as H1 22, exceptional effects amounted to EUR -1m of restructuring costs (EUR -2m in Q2 21 and EUR -17m in H1 21).

22, down -1.0 p.p. y-o-y (31.2% in H1 22, -0.2 p.p. y-o-y) mainly reflecting the strong growth of broadly margin neutral hardware revenues.

Depreciation & Amortisation was lower -5.2% y-o-y reaching EUR 1,124m in H1 22 mainly as a result of the 3G sunset at YE21 which was partly offset by higher RoU asset amortisation and licenses added in the context of network modernisation.

Operating income stood at EUR +105m in the first 6M of 2022 compared to EUR -29m in the prior year.

Net financial expenses accounted for EUR -11m in H1 22 vs. EUR -33m in the prior year.

Income tax was at EUR -22m in the first half-year of 2022 compared to EUR -21m in H1 21.

As a result, **total profit for the period** reached EUR +67m in H1 22 vs. EUR -84m in the prior year.

CapEx¹⁰ increased by +4.2% y-o-y in Q2 22 reaching EUR 291m (+9.5% y-o-y to EUR 556m in H1 22) with a CapEx/Sales ratio of 14.5% (14.1% in H1 22) as Telefónica Deutschland continued executing its 'investment for growth' programme in line with plan in its final year. The 5G network roll-out is making strong progress achieving the targeted ~50% pop coverage well ahead of target. Consequently, the company raised its ambition for 5G pop coverage to ~60% by YE22 with an unchanged Capex envelope due to roll-out efficiencies.

Operating cash flow (OIBDA minus CapEx¹⁰) increased +3.7% y-o-y and reached EUR 673m after the first 6 months of 2022. Excluding exceptional effects, operating cash flow amounted to EUR 675m in H1 22, up +1.3% y-o-y.

Free cash flow (FCF)¹¹ amounted to EUR 373m in the first 6M of 2022 compared to EUR 382m in 6M of 2021. Lease payments, primarily for antenna sites and leased lines, amounted to EUR -395m in H1 22 (EUR -368m in H1 21). As a result, FCFaL stood at EUR -22m for the reporting period compared to EUR +14m in H1 21.

Working capital movements were EUR -281m in H1 22 vs. EUR -253m in H2 21. The development in H1 22 was mainly driven by a strong decrease in capex payables (EUR -239m) following the capex peak in Q4 21, increased pre-payments (EUR -57m), net restructuring impacts (EUR -6m) as well as other working capital movements of EUR 21m. The latter include the development of trade and other payables (EUR -141m), which was outweighed especially by trade and other receivables (EUR 184m).

Consolidated net financial debt¹² amounted to EUR 3,739m as of 30 June 2022 with the q-o-q increase mainly driven by the EUR 535m dividend payment for FY21 in May 2022. The leverage ratio of 1.5x¹³ remained well below the company's self-defined upper limit of 2.5x and leaves comfortable leverage headroom with regards to the company's BBB-rating with stable outlook by Fitch.

¹⁰ CapEx includes additions to property, plant and equipment and other intangible assets while investments for spectrum licenses and additions from capitalised right-of-use assets are not included.

¹¹ Free cash flow pre dividends and payments for spectrum (FCF) 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 as well as related interest payments.

¹² 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 spectrum.

¹³ Leverage ratio is defined as net financial debt divided by OIBDA of the last twelve months adjusted for exceptional effects.

Financial Outlook FY22

In a dynamic yet rational market environment, Telefónica Deutschland delivered sustained profitable growth in the first half of 2022, supported by network parity and its ESG leadership. The company thus built on previous financial years' momentum in the final year of its three-year 'Investment for Growth' programme.

Telefónica Deutschland posted good business momentum in the first half of the year. This was driven by the ongoing strength of the core business and high customer demand for the O₂ Free portfolio and was supported in the second quarter by the offers in context of the O₂ brand's 20th anniversary in Germany. Overall, this compensated for the anticipated, temporarily slightly higher churn due to the implementation of the European Electronic Communication Code (EECC) into the German Telecommunications Act (TKG), which already showed the anticipated signs of normalisation in the second quarter of 2022.

The further recovery of international roaming revenues compared to previous year, which especially in the first half was characterised by COVID-19-related restrictions, compensated for the expected drag from the regulatory reduction of mobile termination rates for voice minutes to EURc 0.55 as of 1 January 2022.

Telefónica Deutschland continued to see improved operational leverage mainly in mobile on the back of continued own brand momentum, with further efficiency gains from transformation as well as regaining market share. As expected, the more volatile handset business was largely OIBDA-neutral.

At the same time, Telefónica Deutschland assumes social responsibility and supports people who have fled the war in Ukraine through personal commitment of its employees as well as with special tariff offers and immediate aid measures to stay in contact with their friends and relatives in Ukraine. The company's business model is proving resilient, despite a further significant inflation increase due to the war.

In this context, Telefónica Deutschland expands its outlook for OIBDA adjusted for special effects upwards to 'low to low mid-single digit percentage growth' in financial year 2022 and re-iterates its outlook for revenues of 'low single digit percentage growth'. The assumptions for regulatory headwinds remain unchanged at EUR 70 to 80 million at revenue level and EUR 15 to 20 million at OIBDA level. Capex/Sales (C/S) is also expected to remain unchanged at 14-15%.

Telefónica Deutschland's assumptions are based on broadly unchanged overall economic conditions, current competitive dynamics and existing wholesale relationships. At the same time, management is continuously monitoring and analysing the impact on the company from the further developments of the COVID-19 environment as well as macro-economic and geopolitical changes related with the war in Ukraine.

	Actual 2021	Previous Outlook 2022	H1 / 2022 (y-o-y)	Updated Outlook 2022
Revenues	EUR 7,765 million	Low single digit percentage year-on-year growth	EUR 3,949 million (+5.5 %)	Low single digit percentage year-on-year growth
OIBDA adjusted for exceptional effects	EUR 2.411 million	Low single digit percentage year-on-year growth, further margin expansion	EUR 1,231 million (+4.9 %)	Low to low mid-single digit percentage year-on-year growth, further margin expansion
Capex/Sales	16.5 %	14 – 15%	14.1 %	14 – 15%

[Link to detailed Data Tables](#)

Further information

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