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Telefónica Deutschland – Interim statement for January to September 2022

FY22 outlook upgrade on continued strong commercial traction & financial performance

- **Innovative O₂ Grow tariff key driver of sustained core business momentum, resulting in >300k total postpaid net additions in Q3 22**
- **+6.0% y-o-y revenue growth in Q3 22 driven by sustained mobile service revenue momentum and record Q3 for handset sales**
- **OIBDA¹ grew +4.7% y-o-y in Q3 22 on improved MSR quality & continued efficiency gains**
- **Achieved 5G pop coverage of ~75%, well ahead of year-end target due to roll-out efficiencies within unchanged Capex envelope – C/S of 14.9% in 9M 22**
- **Continued focus on ESG strategy to deliver a sustainable digital future**
- **Upgrading FY22 outlook to ‘low mid-single digit percentage growth’ for revenues & OIBDA**

Operating performance

Telefónica Deutschland continued its growth path in Q3 22, delivering another quarter of strong commercial traction and sustained financial performance. The company is regaining mobile market share in a dynamic yet rational environment. Ongoing core business momentum is building on high O₂ brand appeal including strong customer demand for the innovative O₂ Grow tariff, network parity and ESG leadership.

The 2022 mobile network test of Smartphone Magazine has established the O₂ network as #2 in Germany. For the first time, Telefónica Deutschland achieved as one of only two German mobile networks the top-rating ‘outstanding’. Network quality enhancements also further increased NPS across Telefónica Deutschland’s brand portfolio.

The widely acknowledged network quality improvements and sustainability roadmap are the foundation for Telefónica Deutschland’s ‘more for more’ pricing strategy evidenced by first initiatives already launched in the market. Since early October, the O₂ Grow tariff is positioned at EUR 35 per month while the technology-agnostic O₂ myHome portfolio was not only expanded by a 500 Mbit/s-tariff but also the 1 Gbit/s promotion has been withdrawn.

Telefónica Deutschland continues to drive its ESG roadmap. The company is delivering on its climate protection targets, well on track to reduce its CO₂ emissions by 90% while neutralising residual emissions latest by 2025. Also, Telefónica Deutschland takes concrete measures to be net CO₂ neutral along its entire value chain by 2040.

At the same time, the company is helping society to thrive. Telefónica Deutschland has been one of the first European MNOs responding to a request for support from the Ukraine. The company donated a mix of new and refurbished hardware network components that can be used without restrictions for the expansion and repair of several thousand mobile sites in the Ukraine.

As a result of the focused execution of the ‘investment for growth’ programme, Telefónica Deutschland has made excellent progress with its network modernisation and 5G roll-out. 5G pop coverage reached ~75% at

¹ Adjusted for exceptional effects. In Q3 22, exceptional effects amounted to EUR -4m of restructuring costs. In Q3 21, exceptional effects mainly included a capital gain related to the spin-off and sale of the operations of the final tranche of ~4k mobile sites passive infrastructure to Telxius amounting to EUR +262m as well as restructuring costs and other exceptional items of EUR +2m.

the end of September and has already over-achieved the year-end target due to roll-out efficiencies within an unchanged Capex envelope.

Mobile business

Mobile postpaid continued its growth momentum in Q3 22 leveraging the high O₂ brand appeal in the market. The company's successful tariff innovation O₂ Grow was a major driver of strong core brand gross additions. Contribution of partner brands was again solid. As a result, net additions totalled +304k in Q3 22 (+415k in Q3 21) and +965k in 9M 22 vs. +1,009k in prior year period.

M2M recorded +32k net additions in Q3 22 vs. +40k in Q3 21 (+103k in 9M 22 vs. +164k in 9M 21).

Mobile prepaid posted -58k net disconnections in Q3 22 (-104k in Q3 21) and +213k in 9M 22 vs. -122k in 9M 21. These developments reflect the German market trend of prepaid to postpaid migration and some seasonality including the reverse effect from revenue neutral SIM card reactivations in the prior quarter.

Churn rates in Q3 22 are reflecting the anticipated temporarily slightly higher churn on the back of the European Electronic Communications Code (EECC). Still, **postpaid churn in the O₂ brand** stood at low rates of 1.2% in Q3 22 vs. 1.0% in Q3 21 (1.1% in 9M 22, +0.2 p.p. y-o-y) leveraging network parity.

Telefónica Deutschland's **mobile customer accesses** increased to 47.0m (+3.6% y-o-y) as of 30 Sep-22, driven by the ongoing strong growth of the **mobile postpaid base** (+6.0% y-o-y), reaching 26.1m accesses (up +1.3 p.p y-o-y to 55.5% of the company's total mobile access base). **M2M accesses** were 1.7m as of 30 Sep-22, a strong +9.0% y-o-y increase while the **mobile prepaid base** was flattish at 19.2m (+0.1% y-o-y).

O₂ postpaid ARPU was -1.3% y-o-y in Q3 22 (-0.8% y-o-y in 9M 22) reflecting a combination of the accelerated MTR glidepath and some enhanced focus on customer loyalty including retention and bundle benefits while high value tariffs remained popular. Underlying² O₂ postpaid ARPU was -0.7% y-o-y Q3 22 and -0.1% y-o-y in 9M 22 mainly reflecting y-o-y trends in international roaming. **Prepaid ARPU** was EUR 7.0 in Q3 22, up +5.4% y-o-y (+5.5% to EUR 6.6 in 9M 22).

Fixed business

Fixed broadband (BB) registered +19k net additions in Q3 22 (+14k net additions in 9M 22) driven by the popular cable tariffs within Telefónica Deutschland's technology agnostic O₂ my Home products. As a result, fixed BB customer base came to 2.3m accesses (+0.9% y-o-y) as of 30 Sep-22 with VDSL (1.8m accesses) as a major contributor (80.2% of fixed BB customer base, -0.7 p.p. y-o-y). Customer demand for the 4G/5G based fixed-mobile substitution (FMS) offer also remained strong.

Fixed churn was marginally up by +0.2 p.p. y-o-y to 1.1% in Q3 22 mainly driven by legacy DSL net disconnections in combination with the anticipated effects from the EECC implementation.

Fixed broadband ARPU continued to benefit from the increasing share of high value customers in the base and grew +3.3% y-o-y to EUR 25.1 in Q3 22 (+2.7% to EUR 24.8 in 9M 22).

² Excluding MTR effects. 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.

Financial performance

Revenues continued to show strong growth, **up +6.0% y-o-y to EUR 2,085m** in Q3 22 (+5.7% y-o-y to EUR 6,034m in 9M 22) driven by sustained mobile service revenue momentum and a record Q3 for handset sales.

Mobile service revenues³ maintained their growth path, posting **+3.7% y-o-y growth** in Q3 22 **to EUR 1,473m** (+3.1% y-o-y to EUR 4,226m in 9M 22). The ongoing strong commercial traction of the O₂ brand and a solid contribution from partners more than compensated for the negative impact from the accelerated MTR glidepath⁴.

Handset sales recorded a record Q3 as a result of the ongoing strong demand for high value devices and good device availability at Telefónica Deutschland. Handset revenues in Q3 22 **grew +18.9% y-o-y to EUR 403m** (+18.6% y-o-y to EUR 1,190m in 9M 22) with customers increasingly opting for longer-term handset financing.

Fixed revenues were **up +0.5% y-o-y to EUR 204m** in Q3 22 (EUR 603m in 9M 22, -0.1% y-o-y) driven by the growth of the fixed retail BB business while the low margin international carrier business continued to reflect the anticipated drag from lower European mobile termination rates. **Fixed retail BB revenues grew +1.6% y-o-y** in Q3 22 (+1.9% in 9M 22) reflecting the steadily growing share of high value customers in the base.

Other income reached EUR 41m in Q3 22 and EUR 113m in 9M 22 compared to EUR 294m in Q3 21 and EUR 352m in 9M 21 including an EUR +262m capital gain related to the spin-off and sale of the final tranche of ~4k mobile sites passive infrastructure in prior year.

Operating expenses⁵ were up **+7.5% y-o-y to EUR 1,489m** in Q3 22 and +6.2% y-o-y to EUR 4,280m in 9M 22 including restructuring expenses in the amount of EUR -4m in Q3 22 and EUR -5m in 9M 22.

- **Supplies** increased +4.7% y-o-y to EUR 648m in Q3 22 (+5.8% y-o-y to EUR 1,868m in 9M 22) with the positive effects mainly from the MTR-cut⁴ more than off-set by volume related higher hardware cost of sales. Connectivity-related cost of sales and hardware cost of sales accounted for 38% and 59% of 9M 22 supplies, respectively.
- **Personnel expenses** were slightly higher y-o-y at EUR 149m in Q3 22 (+2.5% y-o-y) reflecting the FY21/FY22 salary reviews⁶ partly compensated by a y-o-y lower FTE base. Underlying, personnel expenses in 9M 22 were +1.0% y-o-y while in reported terms they were up +4.8% y-o-y mainly due to received social security payments for employees of temporarily closed O₂ shops during the government enforced Covid-lockdown in 2021.
- **Other operating expenses** (other Opex) increased +11.2% y-o-y to EUR 671m in Q3 22 (+6.3% y-o-y to EUR 1,894m in 9M 22) reflecting higher energy costs, technology transformation and commercial activity. Commercial and non-commercial costs accounted for 64% and 32% of other Opex in Q3 22, respectively. Group fees accounted to EUR 9m in Q3 22 and EUR 26m in 9M 22 compared to EUR 9m in Q3 21 and EUR 24m in 9M 21.

³ 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.

⁴ 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.

⁵ Operating expenses include impairment losses in accordance with IFRS 9 in the amount of EUR 22m in Q3 22 (EUR 19m in Q3 21) and EUR 66m in 9M 22 (EUR 52m in 9M 21).

⁶ General pay-rise of +1.75% effective 1 Dec-21 and +3.4% effective 1 Sep-22 as well a one-time payment of EUR 500 per employee in Jul-22.

OIBDA⁷ expanded +4.7% y-o-y to EUR 642m in Q3 22 (+4.8% y-o-y to EUR 1,872m in 9M 22) with continued own brand momentum driving improved operational leverage mainly in mobile and due to further efficiency gains as well as some roaming support. **OIBDA⁷ margin was 30.8%** in Q3 22, down -0.4 p.p. y-o-y (31.0% in 9M 22, -0.3 p.p. y-o-y) mainly reflecting the strong growth of broadly margin neutral hardware revenues.

Depreciation & Amortisation was lower -4.4% y-o-y reaching EUR 1,699m in 9M 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 +168m in the first 9M of 2022 compared to EUR +256m in the prior year which included an EUR +262m capital gain related to the spin-off and sale of the final tranche of ~4k mobile sites passive infrastructure.

Net financial expenses accounted for EUR -20m in 9M 22 vs. EUR -48m in the prior year.

Income tax was at EUR -34m in the nine-months period of 2022 compared to EUR -62m in 9M 21.

As a result, **total profit for the period** reached EUR +106m in 9M 22 vs. EUR +143m in the prior year including the above-mentioned capital gain.

CapEx⁸ reached EUR 346m in Q3 22, up +14.3% y-o-y (+11.3% y-o-y to EUR 902m in 9M 22) with Q3 being the peak investment quarter this year. **CapEx/Sales ratio** was 16.6% in Q3 22 and **14.9% in 9M 22**. Telefónica Deutschland continued executing its 'investment for growth' programme in line with plan in its final year. Consequently, the company has made excellent progress in network modernisation and 5G roll-out. 5G pop coverage reached ~75% at the end of September and has already over-achieved the year-end target due to roll-out efficiencies within an unchanged Capex envelope. At the same time, Telefónica Deutschland is well on track to complete the swap of its core network to Ericsson technology.

Underlying operating cash flow (OIBDA minus CapEx⁸) was flattish y-o-y (-0.6% y-o-y) EUR 965m in 9M 22. Strong operating and financial performance largely compensated for the y-o-y higher Capex spend related with the focused execution of the 'investment for growth' programme. In reported terms, operating cash flow for the nine months period was down -21.1% y-o-y mainly due to the before mentioned EUR +262m capital gain in Q3 21.

Free cash flow (FCF)⁹ amounted to EUR 710m in 9M of 2022 compared to underlying EUR 644m in prior year (EUR 1,180m including EUR 536m proceeds mainly from the before mentioned sale of assets). Lease payments, primarily for antenna sites and leased lines, amounted to EUR -520m in 9M 22 (EUR -474m in 9M 21). As a result, FCFaL stood at EUR +190m for the reporting period compared to underlying EUR +170m in 9M 21 (EUR +706m including the proceeds from the sale of assets).

Working capital movements were EUR -239m in 9M 22 vs. EUR -258m in 9M 21. The development in nine-month 2022 was mainly driven by a strong decrease in capex payables (EUR -206m) due to FY21 spill-over effects from the company's 'investment for growth' programme and increased pre-payments (EUR -31m).

Consolidated net financial debt¹⁰ amounted to EUR 3,410m as of 30 Sep-22. Leverage ratio of 1.4x¹¹ remained well below the company's self-defined upper limit of 2.5x. This leaves comfortable leverage headroom with regards to the company's BBB-rating with stable outlook confirmed by Fitch on 25 Oct-22.

⁷ Adjusted for exceptional effects. In Q3 22, exceptional effects amounted to EUR -4m of restructuring costs. In Q3 21, exceptional effects mainly included a capital gain related to the spin-off and sale of the operations of the final tranche of ~4k mobile sites passive infrastructure to Telxius amounting to EUR +262m as well as restructuring costs and other exceptional items of EUR +2m.

⁸ 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.

⁹ 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.

¹⁰ 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.

¹¹ Leverage ratio is defined as net financial debt divided by OIBDA of the last twelve months adjusted for exceptional effects.

Financial Outlook FY22

Telefónica Deutschland built on previous financial years' momentum in the final year of its three-year 'Investment for Growth' programme, delivering strong commercial traction and sustained financial performance in 9M 22. The company thus is regaining its mobile market share in a dynamic yet rational environment.

Telefónica Deutschland's sustained core business momentum is building on high O₂ brand appeal including strong customer demand for the innovative O₂ Grow tariff launched in May 2022, network parity and ESG leadership. As a result, the gross additions momentum is largely compensating for the anticipated, temporarily slightly higher churn due to the implementation of the European Electronic Communication Code (EECC) into the German Telecommunications Act (TKG). The company expects this effect to normalise towards the end of this year.

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

Telefónica Deutschland further 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. The strong growth of the more volatile handset business was as expected largely OIBDA-neutral.

At the same time, Telefónica Deutschland continues to drive its ESG roadmap with digitalisation as a key enabler for addressing climate change and achieving CO₂ neutrality targets. The company's business model is proving resilient, despite a significant increase in inflation.

In this context, Telefónica Deutschland upgrades its financial year 2022 outlook for both, revenues and OIBDA¹², to 'low mid-single digit percentage growth' including anticipated energy costs of around EUR 210m. 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 current economic conditions and competitive dynamics as well as 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.

¹² Adjusted for exceptional effects.

	Actual 2021	Initial Outlook 2022	Previous Outlook 2022	9M 2022 (y-o-y)	Updated Outlook 2022
Revenues	EURm 7,765	Low single digit percentage y-o-y growth	Low single digit percentage y-o-y growth	EURm 6,034 (+5.7 %)	Low mid-single digit percentage y-o-y growth
OIBDA adjusted for exceptional effects	EURm 2,411	Low single digit percentage y-o-y growth, further margin expansion	Low to low mid-single digit percentage y-o-y growth, further margin expansion	EURm 1,872 (+4.8 %)	Low mid-single digit percentage y-o-y growth, further margin expansion
Capex/Sales	16.5 %	14 – 15%	14 – 15%	14.9%	14 – 15%

[Link to detailed Data Tables](#)

Further information

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