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# Deutsche Telekom AG (DTE.DE)

Q2 2018 Earnings Call

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## MANAGEMENT DISCUSSION SECTION

**Operator:** Good afternoon and welcome to Deutsche Telekom's Conference Call. At our customers' request, this conference will be recorded and uploaded to the Internet.

May I now hand you over to Mr. Hannes Wittig.

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Hannes C. Wittig

*Head-Investor Relations, Deutsche Telekom AG*

Yeah. Thank you. Good afternoon, everyone, and welcome to our second quarter 2018 conference call. With me today is our CFO, Thomas Dannenfeldt. Thomas will first go through a few highlights followed by quarter's financials.

After this, we have time for Q&A.

Before I hand over to Thomas, please pay attention to our usual disclaimer, which you'll find in the presentation.

And now, it's my great pleasure to hand over to Thomas.

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Thomas Dannenfeldt

*Chief Financial Officer, Deutsche Telekom AG*

Yeah, thank, Hannes, and a very warm welcome also from my side here on the call. Yeah, as always, we start with the year-to-date view before we go into greater detail regarding the quarter's trends, and – our strong growth continued in the second quarter on both sides of the Atlantic. The half year stage organic sales were up 2.2% and organic EBITDA is up 5.2%, our ex-U.S. EBITDA is up 2.4%, and our free cash flow and adjusted earnings are up double-digits. All of this is nicely consistent and no surprise with our new four years growth guidance we gave you at this year's Capital Market Day's in end of May. And I'm pleased to say that our operational momentum remains

strong across the board. You saw the strong the numbers and the guidance – upgrade in the U.S. which we're passing on in the group guidance today. Germany and Europe are growing as promised and we are encouraged by an improved T-Systems order book as we're working to turnaround this business as well.

So, let's start with our usual update on customer experience. We're excited about the launch of our super vectoring product last week. As of 1st of August 6 million, 15% of Germany will get speeds up to 250 megabits per second

250 megabits per second, and as we told you earlier, this great product will be available to more than a third of German homes around year end.

A large majority of the customers will have guaranteed minimum speeds of 175 megabit per second, this is something obviously you cannot guarantee in any shared infrastructure, I mean cable. Confirming the quality of our infrastructure, a month ago we want to connect fixed network test well ahead of the country's cable operators. And at the beginning of July, we signed a groundbreaking FTTH agreement with Stuttgart Region, a 1.3 million homes, a 90% of the total will be passed with the direct fiber by 2030. Our business parts will connected in the next few years too. The region will assume around one-third of the rollout cost, and our all costs per home passed will be below €1,000 an average. I think this is a great building block for the fiber strategy that we outlined at our Capital Market Day, and of course, this is baked into our guidance.

In Europe, we launched our revamped digital app and we are seeing an immediate boost to our app penetration. We're rolling out our successful creation B2B portal to the other network as well. In the last two weeks, we also gained permission from the European Commission to acquire UPC Austria, and we finalized our fiber wholesale agreement with Orange Polska, as we continue to strengthen our converged footprint. We're working to gain the necessary approvals for planned transactions in the U.S., and in the Netherlands. Sorry. In both cases we aim to create much a stronger competitors to the market leaders especially as we move towards 5G. As we can see on slide 6

our momentum with customers remain very strong. 11 million German homes subscribed to our high-speed broadband products. In our German and European operations we added 1 million converged customers and 1.7 million mobile contract customers. And you saw T-Mobile's relentless momentum when they reported results last week. T-Mobile also again raised their net add guidance last week by 350,000 at the midpoint and is now targeting 3 million to 3.6 million branded postpaid net adds in 2018.

Let me also highlight some recent customer service awards. In the U.S. T-Mobile achieved the highest score in J.D. Power customer care survey for any wireless service provider ever. And in Germany we won the connect test for the best broadband provider hotline. As mentioned earlier, our U.S. colleagues have raised the EBITDA guidance for the year by a \$100 million. We have to raise our group EBITDA guidance by the same amount, actually it's not exactly the same amount, it's in euros, so it's a bit higher.

Our outlook for our ex-U.S. EBITDA remains unchanged. Also our group free cash flow guidance remains unchanged. This reflects T-Mobile's decision to spend CapEx at the high end of the previously expected range of \$4.9 billion to \$5.3 billion. Sorry. Our guidance for CapEx outside of the U.S. remains unchanged.

Let me now dive a bit deeper into this quarter's performance starting with key financials on slide 9. Our reported revenues this quarter declined by 2.8% year-over-year. But these numbers were impacted by an almost 10% weaker U.S. dollar. On an organic basis revenues would have grown by 1.3%. Our reported adjusted EBITDA was flat but that would have been up 3.9% organically.

Our ex-U.S. EBITDA grew 2.7% organically this quarter, up from 2.2% last quarter in line with our full year guidance. Adjusted earnings were flat year-on-year this quarter and unadjusted earnings were impacted by the €550 million Toll Collect settlement. Free cash flow is up 16.4% again well on-track for our full year guidance.

Now let's dig a bit deeper into the segment starting with Germany, headline sales were down 0.9%, driven by IFRS 15 effect, which we estimate at around 1% to 1.5% of sales for the year as a whole. While our like-for-like service revenues were strong. Our EBITDA was up 1.9% year-on-year on-track for a full year guidance to grow German EBITDA from €8.4 billion to €8.6 billion this year.

On the next page you can see that our reported mobile service revenues, again adjusted for IFRS 15, remain strong at 2.9% year-over-year driving continuous growth in overall service revenues. Similar to the last quarter Q1, this is after around one percentage point impact from mobile regulation, and some offsetting benefit from higher visitor revenues. The main driver for this strong momentum is successful upselling both in B2C and B2B based on our more for more approach and as you can see on slide 12, our commercial performs remains steady with 122,000 own branded contract notice.

We continue to see a favorable gross mix driven by upselling to a more rich rate plans for example Livestream on, and our own branded ARPU remained stable.

remain stable. For those of you who are potentially concerned about the increased competitive noise at the lower end of the German market, let me reassure you, we remain guided by a consistent more-for-more logic.

As you now can see on slide 13, mobile data growth accelerated by 71% year-over-year with the average customer data usage at 2.3 gigabytes this quarter. This was driven by our new unlimited plans and from greater data allowances for our converged customers. 45% of our Magenta branded mobile contracts are now part of a converged relationship and 20% of our broadband wholesales.

Now moving onto the fixed line side on slide 14. We were able to sustain our improved broadband customer momentum. If you adjust for losses from our All IP migration which were broadly unchanged this quarter, we estimate a netted share north of 40%. The strong performance was achieved even though competition unfortunately did not follow our move at the beginning of February to cut the promotion period from 12 months to 6 months. At the beginning of August, we took a further step towards better broadband monetization by reducing promotional incentives. Demand for our fiber products remains strong. We achieved more than 600,000 additions this quarter. By the way, this is the 11th consecutive quarter of more than 0.5 million fiber net additions.

Line losses grew sequentially this quarter and are down slightly year-on-year. This mainly reflect seasonality, as well as our IP migration, which drives accelerated cannibalization of legacy B2B lines.

Last but not least, this quarter, we added 47,000 TV customers. Here our run rate remains below target. But at least we were able to improve the mix, which has become richer. Continuing with fixed on slide 15, our retail revenues fell 0.5% year-on-year, which is a bit better than last quarter's minus 0.9%.

As you know, since the beginning of this year we include certain B2B broadband products in our broadband revenues, which largely explains the very strong headlines rose of 6.2%. More important our like-for-like broadband revenues grew 2.5% up from 1.8% last quarter. Some of you may wonder why this growth doesn't translate into better overall revenue growth.

One reason on top of legacy revenue attrition is that our broadband revenue definition excludes certain sales incentives, which are instead accounted for in other revenues. From next quarter on we will adjust this reporting. We currently expect that this will result in a like-for-like third quarter broadband revenue growth of close to 2%. I think that's helpful because it gives a more complete perspective on what's really going on the broadband side. To be clear this has no impact on our overall financials and our Capital Market Day's guidance for broadband revenue CAGR of 3% to 4% through 2021 also remains unchanged.

We now cover 34% of German households with our street fiber network. Our LTE coverage has reached 95% and 77% of our lines have been migrated to IP up 16 percentage points in the last 12 months.

Moving on now to our usual two slides on T-Mobile as we've already -- we presented very good results last week. In the U.S. we won 1.6 million new customers. This was the 21st quarter with more than 1 million net adds with more than \$1 million net ads.

On the next slide, as usual we show some selected performance metrics for our U.S. subsidiary. Our branded postpaid phone showed and improved further and reached a new record low of 0.95%. Their debt expense remained at a record low of 1% reflecting the improved customer quality. Our commercial results are underpinned by a strong network and recent tests again confirm T-Mobile's clear leadership. Cost of service are down year-on-year despite the accelerated build out of our new low band spectrum.

Now moving on to the European segments. This was another quarter of strong commercial momentum. We added 334,000 new contract customers, 73,000 broadband customers, 22,000 new TV customers and 229,000 new converged customers. Some of our TV markets are increasingly penetrated and we shift our focus here increasing towards better monetization. On page 20 our European segment has continued on its new growth trajectory both at revenue and the EBITDA level. Reported revenues were up 1.3%. EBITDA by 0.6%. Organic EBITDA was up 0.7%. The half year stage we see ourselves well on track for a full year and our Capital Markets Day's guidance -- our Capital Markets Day's guidance. The next chart shows that we have now migrated 74% of our homes in Europe to IP. Our LTE coverage now stands at 96%. We are passing almost 7 million homes with fiber, it's 1.4 million -- 1.5 million more than one year ago.

This mainly reflects our Greek fiber build out. Moving onto System Solutions on Slide 22 revenues and EBITDA declined, but our momentum

improved sequentially, at the half year stage, we feel good about our full-year guidance, we're encouraged by the momentum we are seeing in our growth portfolios. And as we said at the Capital Market Days, our earnings this year are impacted by significant investments and transformation and growth such as all IP, IoT, cloud and health. We're confident these will bear fruit, as well our significant restructuring effort which we have announced six weeks ago.

The next slide shows the segment group development where our Dutch numbers continue to be heavily impacted by accounting and regulation with another decent commercial quarter in the Netherlands with 87,000 contract net adds, mainly from B2B by the way, as the consumer market is heavily impacted by high levels of convergence. Adjusted for regulation in IFRS 15, our Dutch service revenues would have been almost stable and our EBITDA would have been up by €8 million.

On page 24, we provide some more detail on our German tower business. Recurring rental revenues and EBITDA grew by 4% similar to last quarter driven mainly by efficiencies. In the last 12-month, we added 1,000

sites to our German footprint, in the second half of 2018, we intend to further accelerate this run rate as we cover white spots along the [indiscernible] (00:15:20) in rural areas, proactively addressing one of the key pinpoints in German politics. Mainly driven by lower interest costs our first quarter free cash flow grew by 16.4% to €1.5 billion, well on track for our full-year guidance. Our net debt benefited from the additional free cash flow, however, this quarter also saw significant outflows including from dividend payments

share buybacks at T-Mobile U.S. and at the end of toll collect settlement. Almost all of the remaining net debt increases due to the stronger dollar.

With this we remain in our balance sheet comfort zone, as you can see on the page 26. Also during the quarter we made good progress towards the financing agreements for planned U.S. merger, essentially completing the preparations and necessary content at the DT level.

So then my next two slides summarize our strategy and the commitments we presented to you at the Capital Market Day this year in May and I think Q2 is another very good step towards these commitments.

And with that I think Hannes and myself are ready to take your questions.

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## QUESTION AND ANSWER SECTION

Hannes C. Wittig

*Head-Investor Relations, Deutsche Telekom AG*

A

Excellent. Thank you very much, Thomas. Now we can start with the Q&A part. [Operator Instructions] And with that we start and the first question is from Christian at HSBC.

Q

Yeah, thanks for taking my question. I have a couple of ones. One, which is I guess obvious on the current noise around the – the fourth mobile player in the German markets. So how do you assess the risk of a fourth network operator from your perspective, I mean you met with the German government recently at the mobile [indiscernible] and I would be interested in your view on the current situation there?

And then secondly on mobile performance, are you seeing any impact from the recent noise on the low end? I mean, your net add overall was strong but just would be interested in your view what you're seeing there?

I mean despite the fact that you have a more for more strategy, but will be good to know how you're impacted by the noise there? And then lastly on fixed, it looks like you had a very strong Q2 also a much better momentum against cable it seems, are the customers really coming in on higher speeds, do you see strong demand for these higher speeds. I mean you're now launching this super vectoring as well. Any early let's say early indication of interest in those speeds would be interesting as well? Thanks.

A

So first question was on the noise on, regarding I think the 5G auction and the discussion around the fourth player – potential fourth player. I think there was an interview and you might refer to that as the head of the council

authority and he was basically saying two things. He was saying lot of things, but two bigger relevant elements like I guess here for us. One is it would be good to have a fourth player in the market there was one statement he made and the other statement he made that whatever happens there needs to be the right balance of consumer price and competitive friendly moves and investment friendly moves.

Whatever that means, but there was at least that generic statement. So just to make everyone aware here again on the call what happens right now is the consultation prior to an auction where you hear all the voices, all the perspectives and I think it's not a surprise that the head of the council authority is taking that perspective in rule. I think what is more important to us is if you look in the coalition contract there is clear messaging and statement that there should be messaging and statement that there should be incentives to foster investments. That's number one. I think what's also very important to understand is and feels that – in that interview at least that someone hasn't thought too much about, as you can spend every year once. And for the key question, we need to focus here right now on the German market and that's clearly a political agenda it is to foster further investments in 4G quality, 5G rollout and FTT B or H rollout. It is important to make sure that we spend the money for those investments and that there are enough incentives to spend the money for those investments. So I think there was a – an analyst giving and it wasn't non-German analyst but I found giving a very good let's say perspective on that. I'm just quoting because I printed it out.

There is one part saying, aggressive regulatory intervention in the past has led to resellers such as Freenet and 1&1 Drillisch obtaining a combined EV of 13 – more than €13 billion despite not investing in infrastructure compared to mobile network owner, as for instance, Telefónica Deutschland of €10 billion EV, with 5G and FTTH coverage yet to come Germany can't afford to have a forward mobile entrant.

So I think that is – that perspective is very much in line, what I believe, what the key question here is how to foster investments for the future infrastructures. And I think that's what should be said about that. Secondly, mobile performance, on the low end, I think, yes, competition at the low end of the German market has been more intense. In general the discounters as well as some of the second brands improved their value for money position, simply by increasing data volumes. On the other hand

for us increased data volumes is good to be very clear, and it's part of our strategy and you see also the growth we reflected in our numbers here, because the more people consume, and let's be clear the additional consumption mainly comes from consumption of mobile music and mobile video.

The more a good network experience becomes relevant. So, yes there is that noise, yes it's driven by more data volume, but we don't consider that as a – necessarily as a bad thing, especially as we have a clear and well aligned multi-brand approach, you know that, where we have telecom on the upper end of the consumer part and with constable second brand. I think we remain committed to our innovation and more for more amorphous strategy, and we don't see too much of spill overall impact there. So we're not concerned.

On the fixed side, yeah basically your question was where is that good momentum coming from? And I mentioned that in my speech, what we've seen now is more than 11 quarters of more than 500,000 600,000 customers moving from old broadband areas and infrastructure to new one, I have to say, we'd love to see even more people choosing a 100 megabit versus 50 megabit, but in principle the move from [indiscernible] (00:23:16) into the new infrastructure demanding higher speeds that dynamic is very much intact and it's obviously also fueled by the role out we're doing constantly. We're now having roughly a third of the people taking a 100 megabits that's why I'm saying it could be more, but clearly that demand is driving



fueling the growth in that area. And as we're still rolling out and we don't see a high level of penetration on the 100-megabits, we are confident on what we said in the Capital Markets Day is to foster even the development on the broadband revenues.

A

Yeah. And I think Tom also said it in his speech that we have one advantage, DSL line is essentially a dedicated line and it's not a shared line. So with super-vectoring of course this may become even more – come even more in focus, when we can guarantee the first 6 million homes more than the 100.75 of these homes, even a 175 megabits. And so that's the minimum speed you will enjoy at all times. And that's pretty good. And so we are actually competing well in the network tests and where we are head-to-head against cable, we are doing well.

Q

Yeah.

A

So that goes back to your question. Next question is from Mathieu at Barclays, please.

**Mathieu Robilliard**

*Analyst, Barclays Capital Securities Ltd.*

Q

Yes. Good afternoon. Thank you. I had two questions please. First in terms of FTTH and the fact that you got the approval from the regulator with regards to your training center EWE. Is it now the plan to go around and talk with different players to maybe setup a similar arrangement? And if that's the case can you maybe give us a little bit of color on how this co-investment model is setup from your end and how that fits into the ongoing FTTH review by the regulator? And another question I'm afraid is around regulation government. I think the [ph] DFT was saying the other day that the German government had approved €2.4 billion of subsidies for rural broadband. I had in mind that in the coalition contract

or something like €10 billion to €12 billion for that maybe Mathieu is referring to is for one-year and what the coalition is referring to is four years, five years, so you can maybe clarify that that would be helpful? Thank you.

A

Yeah, Mathieu, I'll start with the second question. Yeah, in the coalition contract, there is that vicinity of €10 billion to €12 billion for the four years mentioned. And I think what the government did is so to say as a starting point to, right what you mentioned to approve the €2.4 billion of which I guess roughly half is the – is for the first year. Obviously there is a thought that also the proceeds on the spectrum auction kicking in next year will be added to that. So it's a starting point, it's fine ultimately for sure not the end and the vicinity isn't been or there's no correction in the vicinity of €10 billion to €12 billion but as I said it's a four years perspective and more to come. That is on the second question on the subsidies.

On the first question, approve from regulator for the GV correct. What's still missing now and that's the next step is to get the support of the antitrust authorities, 00:27:01 authorities in the same interview by the way I quoted a



minute ago Mr. Mund [ph] was in principle supported for that logic and ideas but now let's see we need to see that from a process we are keen to get it done as fast as possible because we're ready to go. And want to start doing it as well as our partners EWE. And obviously, our intention is to copy that model. The issue is a bit if you want to copy them all you need to find people who are willing to invest

and EWE – and from what we have seen last two years is the second largest fixed line investor in Germany, who has been the second largest fixed line investor in Germany. So what we're doing right now we're looking down the line of third, number four, number five and so on obviously trying to see whether we can copy the model because we believe that model is helpful and would be good. But obviously it takes two to tango, so we need to approach and that's what we're going to do, the partners will find out whether there is a joint way looking forward.

A

Okay. Thanks Thomas. So next is Akhil at J.P. Morgan. Akhil, please

Q

Hi. Thank you for taking the question. Just a few believes, firstly sticking on the subject of fiber, you mentioned earlier the agreement that you've signed instagaurd, which has obviously raised a lot of interest given the co-investment or even a subsidy I guess it's a to the government's offering. I just wonder if you could give us a few comments on firstly what the participation would like from other parties whether you did see other bidders. And if not what so call is to why not.

And then I guess more broadly is this starting to raise interest more broadly in Germany, i.e., could we start to see other municipalities in Germany moving down the similar path. The second question is on the U.S. Thomas there's some headlines on Bloomberg just highlighting that you're expecting some feedback on the T-Mobile U.S. Sprint merger situation later this month, just keen to understand what exactly you're referring to and how significant that could be.

And then the third thing is that we've seen a number of headlines on Holland where the European Commission stopped the clock in terms of wanting more data from you, I just wanted if you're able to make this year any color on exactly what they are off to and just more broadly if you still expect to complete this by the end of year?  
Thanks.

A

Yeah, Akhil. Thanks for the question. First of all, on the U.S. let me clarify first, I think in terms of timing what I said is we filed our public interest statement on 18th of June, the SEC has issued the public notice on 28th of July and there is so-called merge opponents petitions to deny 00:30:08 to end of August so that's the first – the next step of so to say of the process. And then later on, mid of September, our supporters of positions are due and then you have a reply to that later on October so that's the normal process and that was what I had this morning on the call with the journalists mentioned.

So just to clarify that, it's just the simple, normal process the FCC is pursuing here. Then on fiber in Stuttgart, yeah, I think basically, the whole deal is about covering with a 5G infrastructure especially on IoT Infosmart cities, the 90% of that region, 90% of was FTTP or FTTH and then earlier also the businesses in that area and we are

investing €1.1 billion and there's €500 million is support by the region. Participation from other bidders, yeah, was my personal expectation was that more parties were serious

willingness to put a stake into the ground, meaning put own money into the ground would show up. That was very limited. I was a bit surprised about, I'm hearing since years about all the money being available in the market, that's so little commitment of own money brought to the table was existing as far as we know at least.

Anyway for us it's a model which we like and we like to copy, we like for sure, we have the intention to motivate other cities/areas. It's not only the city, let's not forget, it's the broader area to encourage them to talk and think about the same model, and go for the same as we are willing to put a stake in the ground and put our money as you know.

So that is obviously a hope we have. And as far as I've seen so far, the dynamics in Germany once someone has something the other doesn't have. There's always some good dynamics around that. So then you have the third question was I think on Netherlands. That was on the – I think that it was that – that stopping the clock thing in the EU, that was restarted by the way, retroactively to a 6th of August. We don't consider that as a big topic. It happens from time-to-time in those processes and so from our point of view no big – no big topic here.

A

So the next question is from Usman at Berenberg, please.

Q

Hello. Thank you for taking the question. I've just got two questions please. Firstly on German mobile, I can see in the report you've disclosed that B2B mobile was up around 3.6%, which implies that consumer is kind of slightly lagging even though the overall growth is quite strong. So, I mean how – I guess the question is what is differentiating being able to grow more strongly in B2B mobile versus consumer mobile for you in Germany and is there a potential way to accelerate the consumer mobile growth as well.

The second question was just on German broadband. There seems to be a slight blame game going on here with one of your largest operators that indicating that you didn't follow them in raising prices. So, while you're saying that someone else didn't follow you in reducing promotions. So I mean could you just give a bit more color on is it the smaller operators that didn't follow you or what's going on? Thank you.

A

Yeah. Thanks for the question. I'm going to start with the German mobile. Actually, we don't disclose the split of the mobile service revenues in B2B and B2C, so I'm not sure where you get the numbers from but what's correct is that B2B over in excess a bit in the contribution to that growth. So directionally that's right. By the way that's a trend we've seen since a lot of quarters. And I think it's actually because the logic of more for more is you offer more, you spend more and the willingness to pay in the B2B sector is obviously a bit higher because it helps and supports the business better than it is partially on the consumer side.

Potential to accelerate in B2C, you've seen our guidance was given in the Capital Market Day is for the mobile service revenue

Revenue longer term growth, we are over indexing a bit – have been a bit above that also if you strip out B2C – B2B so I'm really happy with the numbers I'm seeing currently. That is on the mobile side.

And then on the B2B – on the broadband side, in terms of revenue prices, what happens actually is we had – we offered that promotional activity of you pay €20 for the first 12 months whatever kind of speed you take to encourage the people to use the highest speed and then after 12 months that was the idea you can decide whether you want to have the highest speed 150 or 160, the intention was obviously to drive the share of 100 megabit of – customers choosing a 100 bit upwards. So on the other hand, it was obviously you had a strong promotional negative impact also on the revenues and so we decided to [ph] halven that period and February from 12 to 6 and no one followed. And in April, that was more intense competition again and some promos were put into the sales activities again, which we again took down in August. I don't think it's helpful to talk about the one or the other hasn't followed. Everybody should make up his mind what he believes is right for his own company and the marketplace. We believe there is again more for more, there is enough more we offering that promotional activities can be reduced a bit. That's why we did it again in August and we feel good about the runway that we've seen so far, so that that's where we are.

A

Okay. Great. Next question is from Josh at Redburn. Josh?

at Redburn. Josh?

Mandeep Singh

*Partner, Redburn (Europe) Ltd.*

Q

Actually, hi, Hannes ,it's Mandeep on Josh's behalf. He's actually on the Free-Net call so thanks for taking the question. It's regarding the sort of commentary we've seen coming out of the U.S. that the DOJ is reportedly in favor of maybe three network players in a 5G world.

But clearly conversation that you had in private with the DOJ, you can't necessarily disclose but can you just tell us just generally your tone, how constructive you think the support is in the broader sort of political arena, lobbyists just from all the various stakeholders that you think are contributing to the debate.

Where do you think the debate currently is in the U.S., broadly.

A

I think the -- what's setting the scene I think is important and what's obviously setting the scene this time very differently to back to some years back when we had the AT&T, T-Mobile merger discussions is that John and the team has shown the market and all players in the markets. I mean customers as well as the administration that T-Mobile is shaking up the market and driving the market to the favor and advantage of the customer and that the DNA of that company is super clear along that line of thinking and acting.

So I think that there's obviously setting the scene a bit. That's number one and I think number two was also setting the scene is the case per se. I mean the case offers for everyone, upsides. I mean every stakeholder it is – I mean you will see a 5G infrastructure, you won't see in the U.S. in that kind of depth and quality without that merger. They we will create jobs from day one on. So for -- I think for the economy I think fro economy and for the

administration as well as upside and creating jobs from day one is also upside for the employees, for the shareholders. So, I think it's a no brainer that we are extremely bullish about that case and obviously those two things are influencing the process, but other than this, I think there's nothing I can add to.

**Operator:** Great. Thanks, Thomas. And next we have George at Citi. Please.

Q

Hi, Thanks for taking the questions. I have two. The first one is around old IP migration and even though the KPIs on the fixed line in other metrics are relatively strong, the line losses remains slightly on the weaker side onward, you would have expected a few months ago. So I'm just trying to understand as we go towards the last 10% of customers you need to switch off, is it more business customers which means the churn driven when you're going to annual IP migration could be higher? Is it something we should expect to carry on for the next six quarters, seven quarters until you continue? And if you give us any indication of whether you have any idea of what is kind of the revenue headwind you're facing because of this process?

And my second question is more – just to get an idea with all the moving parts you have in mind of how the net debt and the leverage metrics could progress over the next 6 months to 12 months and I don't know there are few deals, which are not insignificant as that may move the numbers around, but on the other things like smaller drivers here and there, that are one off day chart that we may be missing? Thank you.

A

Yeah. Thanks for the question. I'm going to start with the all IP.

I think there is – there are two areas where you see impact by the IP migration we're doing right now. One thing is obviously on the broadband side and it is the larger extent of that one. Nowadays is B2C driven that's roughly 25,000 per quarter, impacting the net adds, just by customers we actively canceled – where we actively canceled the contract. And it's always hard to – to say that, it's a shame. Okay. So that's one part, and then you have the – what also takes place is once you transform business customers obviously, what you see is that they switch off some legacy lines very often not broadband lines, but simply voice lines they find in their inventory and they switch off. So the larger extent of the impact on the line losses is B2B and the larger one on the – on the broadband lines is B2C and as I said, B2C is roughly that 25K per quarter which is relatively constant along the last four quarters. As our current status on IP migration is 77 last 12 months have been 16% you can imagine that there is another round island for four quarters six quarters ago, mostly it's been four quarters to go to get that done and have a number which is very close to a 100%, but in that timeline we'll – still see that – that impact.

On the net debt side, I think, we've been crystal clear. We need to first of all distinguish two ways forward, the one way is no U.S. deal for whatever reason let's assume, we can't get the deal or we don't get the

allowance to go for that deal then my leverage, my upper end of the leverage – which my upper end of the leverage is 2.5 that's my the level I want to keep with where we are today as well. I think we share that with the rating agencies and we'll feel good about keeping that knowing that the growth profile is very sustainable we have right now in the company based on the U.S. on Europe, on Germany so that's where we are and where we will be in case of no deal looking forward and I was also clear that in case of a deal we will leave that comfort zone for at least two years to simplify the impact of integration taking place in the first two years.

A

Yeah. Okay. So with that the next question is from Ulrich at Jefferies.

Ulrich Rathe

*Analyst, Jefferies International Ltd.*

Q

Yeah. Thank you. I have a two questions. The first one is on the Stuttgart deal, could you describe what part of the commitment that you've made as part of this agreement actually ahead of activities that you would have done anyway. So is there really a give of [indiscernible] (00:44:41) comment and sort of almost slightly a different way of asking the same question. If it's a very large number of major urban centers in Germany where to now ask for a similar deal with Deutsche Telekom would that affect your CapEx plans or could you fit in such deals in large volumes into the current planning that would be my first question, the second question is on mobile I mean there are some initial sort of signs that Telefónica's mobile network is getting a bit better at least regionally,

And obviously they do pricing on the premium brand below Deutsche Telekom and that's because of the network quality expose, and I'm wondering do you see the price points on Magenta mobile defensible if really Telefonica networks become smaller, more credible also for premium customers in 4G? Thank you.

A

Yeah, thanks Ulrich for the question. First of all, Stuttgart deal, I think the simple answer on the question what is extra, what we given is obviously if you think about Stuttgart above the depth and of the coverage of FTTB or FTTH and also 5G I know, we're talking about 90%. That is something you – without having like Stuttgart region someone willing to contribute to it, contribute with money to ensure that there is that level of density of coverage. Obviously, without that element, we wouldn't have done that. So part of that, yeah, and the long-term plan always, but for sure that level of quality and consistency along 5G and FTTH and FTTB, no.

And the second element is the timing is 20-30, so that doesn't mean we're talking about €100 million per year for the Stuttgart region so our CapEx envelope is a bit larger, so we can digest another Stuttgart, Munchen, Hamburg, Berlin, Dusseldorf, what – a go, go, go, go, and so it's not like we're desperately sitting here and thinking, oh my goodness, what if the other way around that's true. We would love to see more of that. And we are as I said already, we are also hoping that dynamics

also hoping that that dynamics will kick in. On the mobile side, and your question on the mobile infrastructure, I think, and my position, what I do like is a marketplace where the customer has the choice. And where you have high visibility off – for instance today, if you go with a €10 price point you can easily get 3 gigs, 4 gigs, potentially 5 gigs in the marketplace, and you know if you go with our premium brand, you pay €35 upwards to get it, and everyone knows. So, that the transparency of for customers and that customer choice is important because without that you will see disruption or regulation kicking in and that's what we don't need.

And that also implies that we continuously find new reasons for the customer to spend more money with us than with others. And you know what I do like is, if others start to compete with us on the quality level, that's the game we can play. We know how to play it. And on the mobile infrastructure, you know that, it's about the back hauling of the infrastructure, it's how fast you transform from 4G into 5G. It's about your spectrum opportunities you have et cetera, et cetera. And we feel very good about that game because that's our game.

And obviously also fixed mobile convergence plays a game in here, and I mean not only the tariff plan, very often people shortcut the whole convergence story to a tariff plan. I'm talking about the convenience. Ultimately what we want to achieve is, sell a subscription to the Internet, you use wherever you are you have the perfect quality. That's the perspective we want to go. And you don't care about fixed or mobile or you are in the plane or you're somewhere on the ground you don't care about that anymore. So all those components obviously play a role to continuously gives a new reason for the customer to buy our products and that's our game. So we are pleased to see that quality game is the name of the game nowadays in the market. And we believe we have enough elements in our [indiscernible] (00:49:27) in our toolbox to differentiate for their own.

A

Just to add the number Thomas assumes you're familiar with, but just to reiterate it that we want to spend €2 billion on FTTH related CapEx run rate in the 2021 and thereafter and that's also connected with our message at the Capital Markets Day that our CapEx outside of the U.S. will not exceed €7.9 billion go it back to €7.6 billion. So within that €2 billion framework of course there is room for a number of projects like Stuttgart, which will cost us about €100 million a year.

So the next question is for Ottavio at, [indiscernible] (00:50:21), please.

Q

Hi, good afternoon. A couple of follow-up questions from my side. The first one is actually and following on the questions are related to the TV and partnership you doing on the FTTH and my question is relates the ownership of the infrastructure. The one with EWE, you got the JV, so I assume that the infrastructure would be 50%, 50% owned by you and EWE, do you have any plans at some stage to buy out EWE or there is anything on the framework agreements on that particular topic? The partnership, I believe that you just get subsidies, so there's not any sort of impact on the ownership on the infrastructure but you can clarify on that.

The second follow-up question is on the  
  
can clarify on in that.

The second follow-up question is on the 5G spectrum auction, the very first question on the call was referring to the comments made by the 00:51:24 in the – it's ability to introduce roaming, compatible roaming on the – all the three operators to enable a full entrance. My question is a bit different, I heard that there has been a lot of discussion in terms of the build-up requirements for the 5G and I would just double check if there's been any agreements about what sort of build-up requirements will be – or would you aim to do on 5G over the next three to five years. And would you believe that it's acceptable that the post makes this point in time. Thank you.

A

Yeah. First of all, on the joint venture, the joint venture is not an off-balance vehicle, it's a joint venture and you're right, it's 50:50, we own the infrastructure about 50% and there is no intention to buyout EWE. The intention is to start and get the infrastructure rollout done and that's our focus and the rest is simply I think two parties joining forces on delivering a better infrastructure.



On the Stuttgart, situation is quite simple we get support to create that dense consistent infrastructure. But the ownership is a 100% for those. So there is no impact on the ownership to correct. On 5G, I think what you're mentioning the build-up requirements for 5G is something which took already – is taking place right now as part of the consultation and whenever you have consultations, you have various thoughts in the room and one thought is obviously

the thought which was already in the room with the 2015 auction, which was in principle, the question, shall we reduce expectations on the proceeds. And put more, I mean, we meaning the regulator and put higher requirements in terms of the quality of built out into the – into the license agreements.

So basically as a regulator, you can, from one extreme to the other tune that, you can give the in conceptual, you can give spectrum for free and have super high requirements in the quality later on, because you always can spend the money once, so you spend it there or – on the other extreme, you will maximize the proceeds like what has been done back in 2000 or so with the UMTS license.

But then you have to deal with the consequences on a delayed rollout and quality of infrastructure and obviously, the discussion about what's the right balance to that is something which is taking place right now.

And potentially that will have then an inflow into the license agreements or requirements. But there is no agreement so far, obviously that will be potentially part of the license agreement. By the way, our position is quite simple, we lobby for lower proceeds for the – for the spectrum and more focus towards the quality of the infrastructure being required to roll out later on. As on principle, we like the second more than the first one obviously, also here it's about the right balance obviously but as I said, there are no agreements existing so far on the 5G side.

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A

So obviously, quite

disappointed that Thomas, we thought you can spend the same dollar twice, but I found you that magic is not in place, but let me also like add something just conceptually in the context of this national roaming idea. And it's true also for other countries. If you have access to other people's infrastructure then you don't build your own and so if you want to have better levels of coverage then you don't impose national roaming. It's very simple. It creates a clear obvious investments and incentive and we think enough people understand that in Germany. So we have actually had a meeting with the minister as you probably read and there was a conditional agreement to increase the mobile coverage, depending on the terms of the auction. So just to add that maybe on top of what Thomas has just said.

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**Operator:** And then the next question is from Jon Dan at RBC. Please.

Q

Hi, there. It's two questions on monetizing broadband, if I look at the tariffs you only charge €5 more for a 100 megabits versus 50 megabits. So I guess it seems like if people won't pay €5 more for more, I guess it seems like it'd be a tough environment to raise, to monetize broadband? And then secondly on the topic of monetizing assets, what's the latest on the Dutch towers and also the German towers? I sensed at the Capital Markets Day that you might be wavering back toward keeping them?



A

On the towers there's nothing new. On the monetization of broadband, I think let's just remind ourselves a bit before we started the rollout of the infrastructure last three and half years, four years we've done three and a half years you know retail and

four years we've done three-and-a-half years, retail and wholesale broadband revenues have been significantly declining, retail was minus 2% and also was minus 5%. They're both growing now 2% to 3% on the wholesale side and as I said around to on the retail side. So obviously that monetization works. It is fair to say what does it take to get the share of the people taking 100 megabit again up. I guess that's a bit around also the culture in Germany. I think people often tend to start with the first step instead of going to the maximum in the first instance maybe in countries like the U.S. people would go for the maximum speed immediately. Germans or more slower in adapting that, but as I said we've seen 11th consecutive quarter of more than 500,000, 600,000 of customers moving from ADSR to the new infrastructure. And we believe we will see continuous upselling and upgrading of the people themselves and not only to 100 million but later on also you see and we start not offering them super vectoring on a 175 to 50. So that is kind of natural process we believe will take place, and that's why we've laid out our 3% to 4% CAGR for the broadband revenues for the next four years till 2021.

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## Unverified Participant

Okay. It actually looks like there are no more questions, which is good on a hot summer afternoon and so if you have any more questions, please contact the Investor Relations department and we hope to help you then and so with that, I give back to the operator. Thank you very much.

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**Operator:** We'd like to thank you for participating at this conference. The recording of this conference will be available for the next seven days by dialing +49-1805-204-7088 via reference number 521842£. We are looking forward to hear from you again. Goodbye.

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