

A stack of several blue and white notebooks is visible on the right side of the image, slightly out of focus. The notebooks are stacked on top of each other, with the pages of some visible. The background is a soft, warm-toned gradient.

“On a transformation journey”

Eva Castillo
CEO Telefonica Europe

Madrid, 19th June 2013

Telefonica

**XX Santander Global Banking & Markets
TMT Conference**

The world has changed ...

1990s



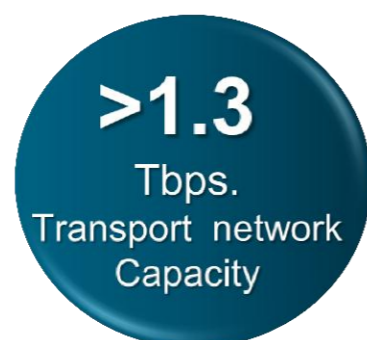
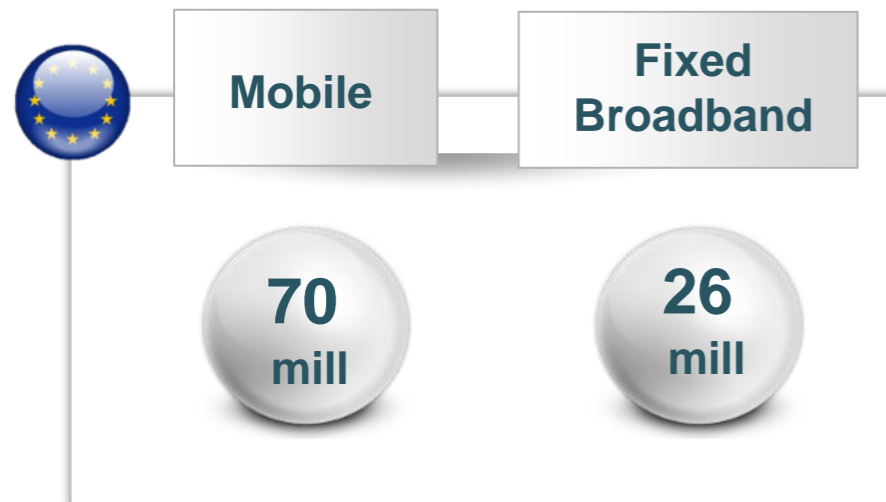
2012s



Long ago people danced at concerts,

....now they video, click, share, chat, tweet

Telefonica enjoys a remarkable scale and positioning in Europe to lead this change...



Transformation: the key lever to build a more sustainable model



Transformation of our commercial model

- Renewed commercial offer across footprint
- Bold commercial decisions: no subsidies
- Data monetisation
- Simplicity, transparency

Transformation of the operational model

- Efficiency and cost discipline
- Insourcing
- Simplification
- Market rationalization

Disrupt with **new Capabilities** and Approaches

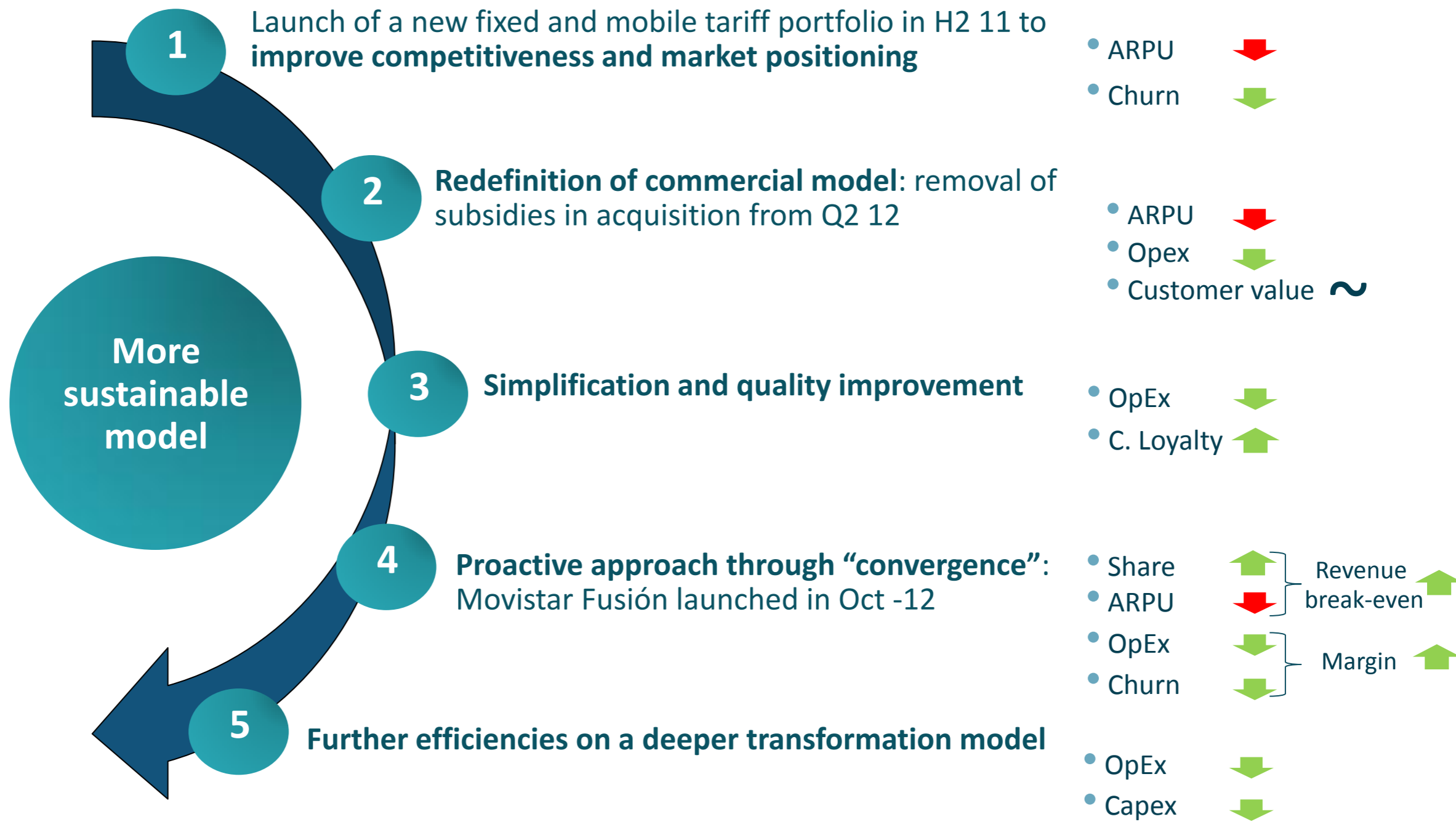
- Digital services for a new Era
- Network sharing
- Convergence

Re-inventing our business model to lead the sector

Spain: a leading example of this transformation



Our transformation journey started in 2011...



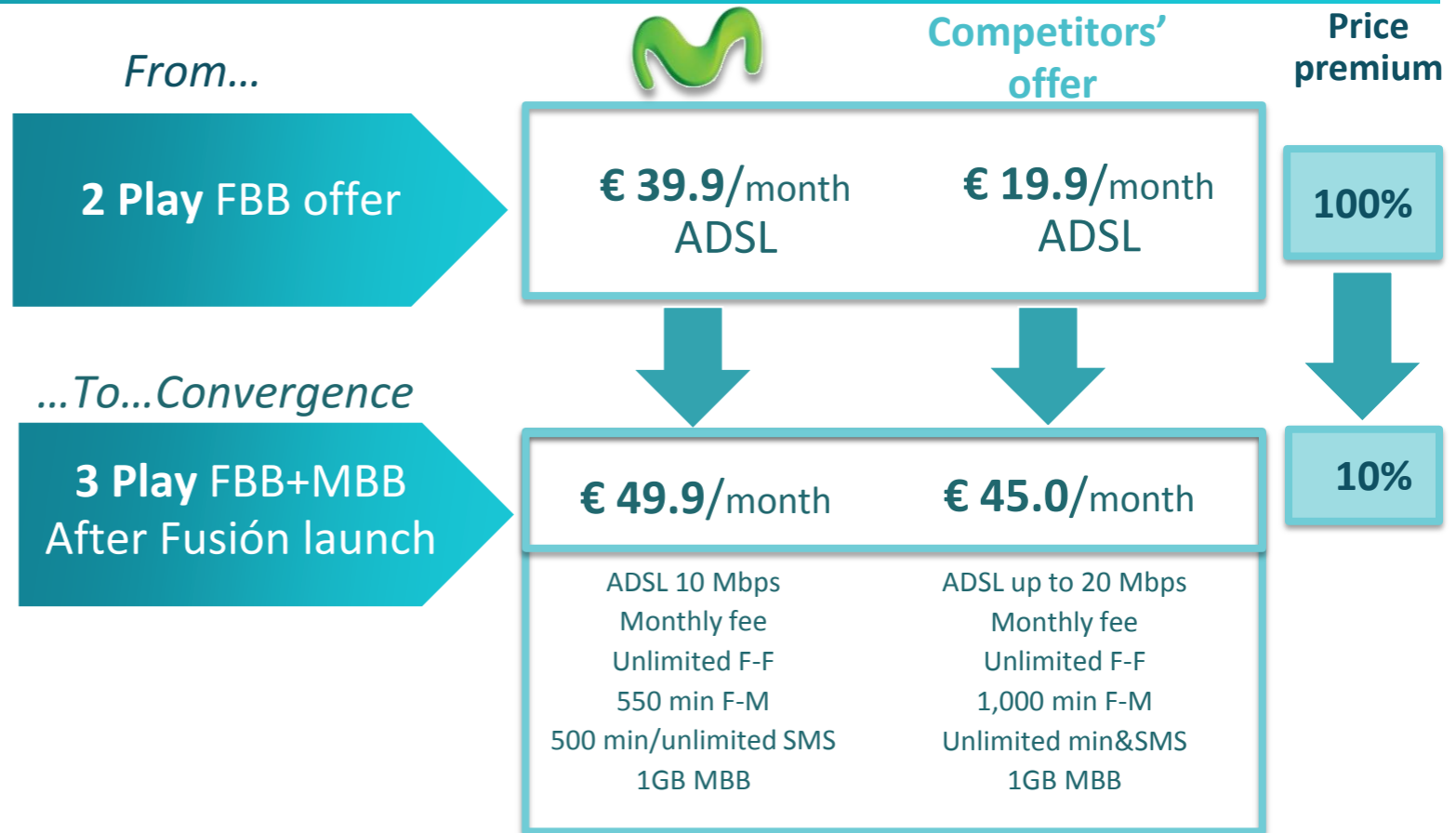
...allowing us to change market dynamics, and turning around our financial and commercial performance



Competitiveness recovered to capture market share

Reshaped market trends

- **Price premium significantly reduced** to a competitive level
 - ▶ Premium based on quality of service
- Value for money
- **Telefonica leading a market that is moving toward convergence**
- **Market more rational**
 - ▶ Towards lower handset subsidies



Large upside leveraged on fiber and Pay TV capability

- High upselling opportunity within Fusión
 - ▶ Fusión fiber 100 MB
- Pay TV offer adding differential value
 - ▶ "TV Familiar": +10€ promotional price until Aug,31st
 - ▶ "TV Sports": +20€
 - ▶ "TV Leisure": +12€



Movistar Fusión, the key lever behind our commercial turnaround



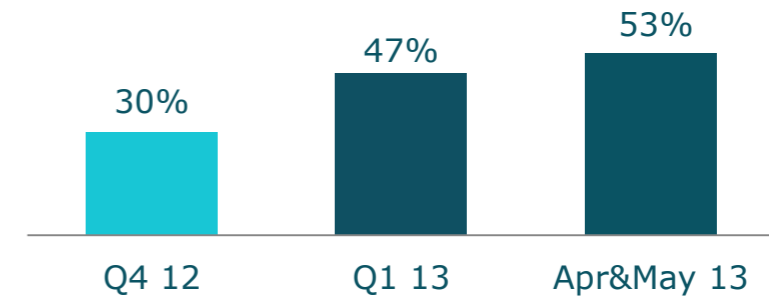
Fusión maintains strong market momentum

- **2 million Fusión customers** (May 13)
- **Customer mix improving:** higher percentage of new and upselling customers
- **Better customer satisfaction**
- **Revenue break-even from Jan 13**

Increased fiber uptake based on Fusión traction

- **2.3 M households passed** as of March 13
 - ▶ 372 K fiber customers connected (16% take)
- **Good results of Fiber vs ADSL**
 - ▶ Lower churn levels
 - ▶ ARPU uplift
 - ▶ Better customer satisfaction index
- **Flexible investment approach**
- **Co-investment agreement signed with Jazztel**
 - ▶ Targeting 3 M premises (1.5 M each)

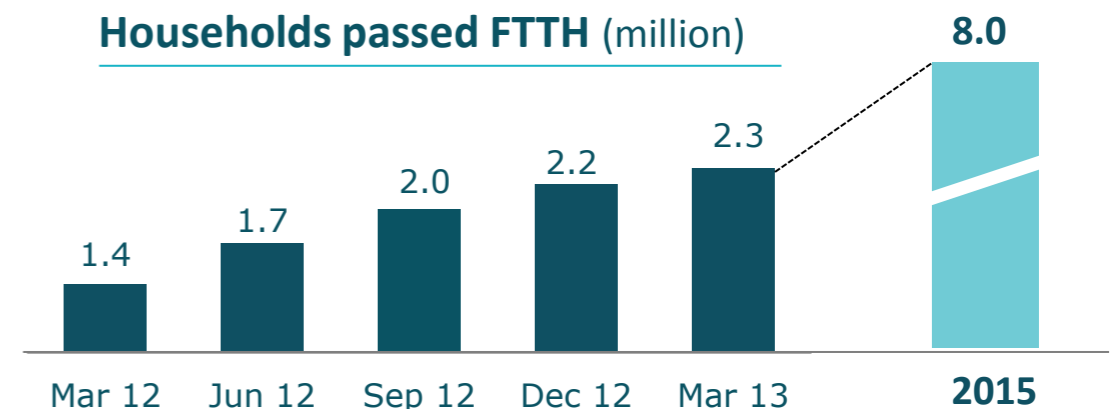
Movistar Fusión % New customers/Gross adds



Fiber vs FBB net adds ('000)



Households passed FTTH (million)





Renewed commercial offer in April to reinforce mobile competitive position

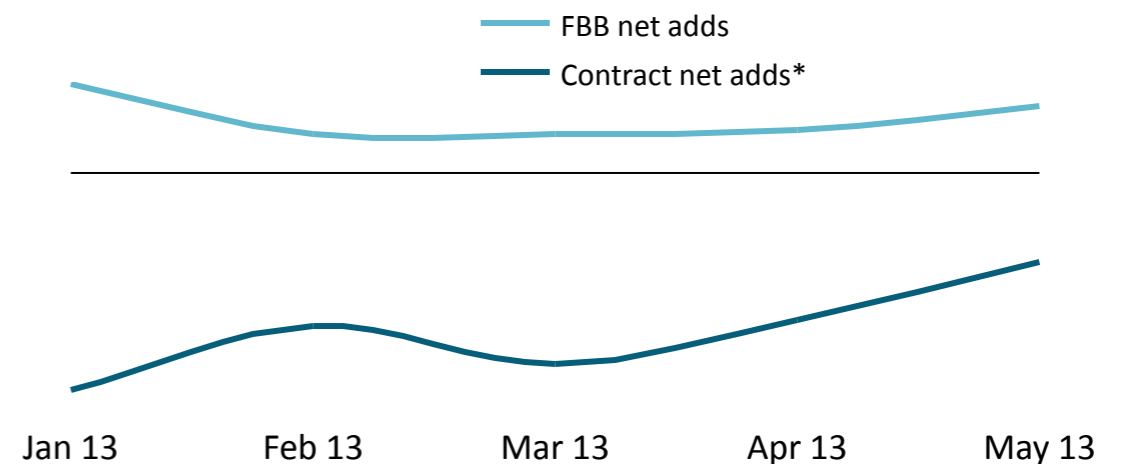
A complete offer in the convergent and only mobile space



Renewed tariffs starting to deliver results from May

- Ramp up in FBB net adds
 - ▶ Further churn improvement
- Ongoing strong fiber take-up
- Improving performance in contract mobile

FBB net adds and mobile contract net adds* ('000)



* Excluding M2M and dongles

Continued efforts to deeper transform our operating model



Transformation allowing us to better manage tough macro and competitive environment

• Ongoing benefits from 2012 cost cutting initiatives:

- ▶ Commercial savings from no-subsidies model
- ▶ Redundancy program: 6,500 net reduction in headcount
- ▶ Saving from simplification (portfolio and processes)
- ▶ Increased customer satisfaction

• Further efficiencies to come in 2013 on deeper transformation

- ▶ Personnel: bargaining agreement
- ▶ Insourcing: commercial, technical and support areas
- ▶ Deepening on simplification (IT, services, distribution...)



Call centers simplification

- Simplification of customer service model in number of centers and suppliers
- Transfer the execution to the regions

Results

- 43% of traffic already inshore
- 85% of positions transferred to regions by the end 2013
- Reduction of external cost: improving own resources productivity
- Increased customer satisfaction



Optimisation of distribution model

- Reduction of point of sales
- Foster online service

Results

- Simplification program in exclusive channels already in place (90% fulfillment)
- Increased profitability of exclusive stores
- Improved customer experience

... building a more efficient company for the future



This transformation journey is driving to business stabilisation

Revenue ex-handset sales stabilises its y-o-y trend in Q1 13

- Focus on fixed + mobile revenues due to Fusión impact
- Mobile handset sales -67% y-o-y (subsidies removal in Mar-12)

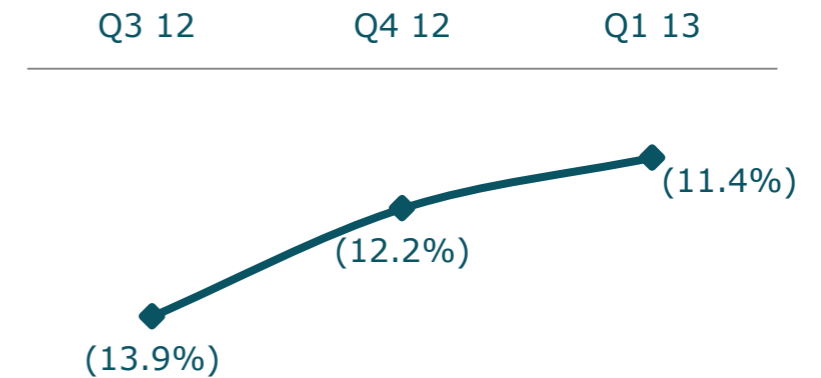
Sustained profitability

- OIBDA margin maintained at high level
- OIBDA margin sustainable on the back of further efficiency measures
- Leading profitability in Europe despite a challenging competitive and economic backdrop

Stable OpCF

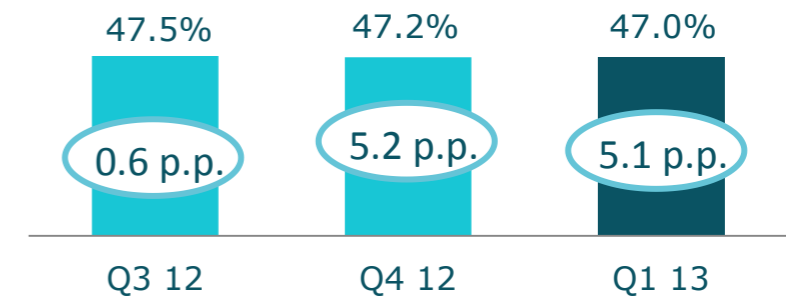
- Despite revenue pressure, efficiencies in Opex and Capex allowing us to maintain Operating Cash Flow
- Capex focused on growth areas as fiber

Revenues ex-handset sales (y-o-y)

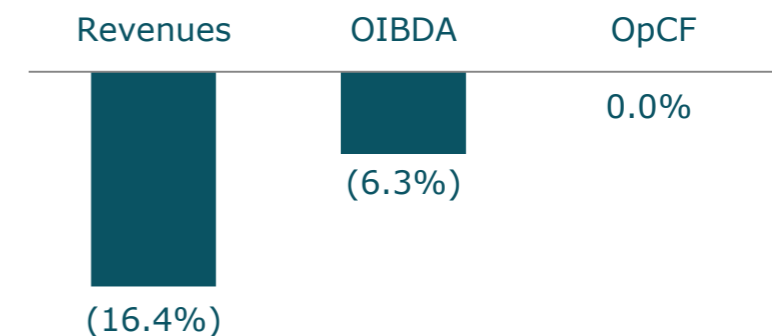


OIBDA Margin

Organic y-o-y change



Q1 13 (y-o-y organic)





T. UK: started 2013 with a strong set of results

Sustained commercial momentum

- Mobile base up 3%, with **contract mix at 53%** despite aggressive competition
 - ▶ **Strong traction in the contract segment**
 - ▶ Record low contract churn at 0.95%
- Smartphone penetration at 47% (+6 p.p. y-o-y)
- **“O2 Refresh”** launched in April to reinforce position

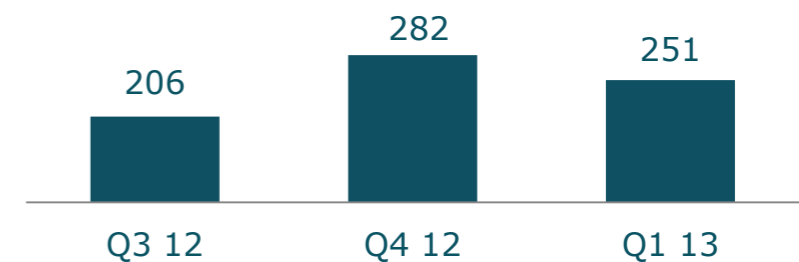
Revenue improvement

- **MSR trend improved for the second consecutive quarter**
 - ▶ Non-SMS revenues: main growth driver (+16.4% y-o-y)
- RPI increase and disposal of fixed business to impact from Q2 13

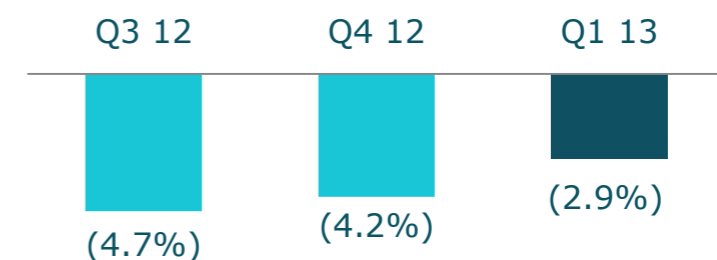
OIBDA back to growth

- **OIBDA margin expansion:** contained commercial expenses, network sharing and scale benefits
- **OpCF up 25% y-o-y** (excluding 800 Mhz spectrum investment of € 671 m)

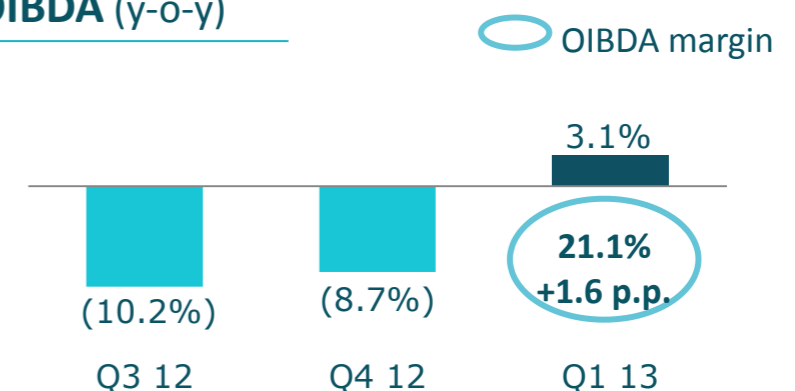
Sustained performance in contract net adds ('000)



MSR trend improvement (ex-regulation)



OIBDA (y-o-y)





Involved in business' transformation

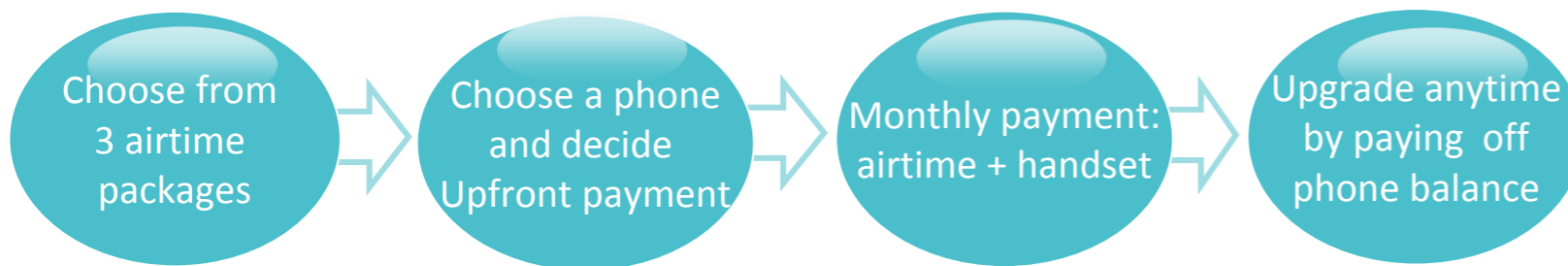
Launch of O2 Refresh to reinforce commercial momentum

- Customer-innovative offer based on a **simple, transparent and flexible all-in proposition**
- **The first to decouple handset and airtime costs**
- Maintained data centric strategy with no handset subsidy

O2 Refresh



Standard contract



Transformation of the operating model

- Focusing on our core business
- Working to become a more **on-line company**
- Looking for **efficiencies in the distribution channels**
 - ▶ Changing relationships with third parties channel
 - ▶ Optimisation of direct channel
- **Optimising customer service centers:** outsourcing of 2,360 employees
- Deploying our **network sharing agreement with Vodafone**



T. Germany: solid progress in mobile data in a competitive but rational market



Delivering on clear strategic priorities

- **Focus on high value customers**
 - ▶ Contract growth with mix improvement (53%, +2 p.p)
 - ▶ Accelerating smartphone penetration 28% (+7 p.p. y-o-y)
- **Loyalty**
 - ▶ Contract Churn at 1.5% (-0,2 p.p. y-o-y)
- **LTE**
 - ▶ Launching new LTE high speed areas
 - ▶ Commercial push from LTE still to come

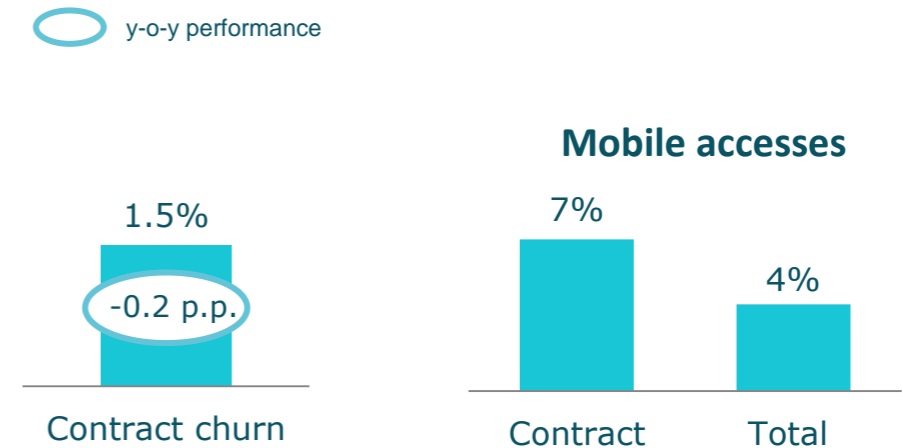
Reinforcing commercial proposition

- **New “O2 Blue all in” portfolio**
 - ▶ Innovative market tariffs
 - ▶ Encouraging trends in terms of mix
 - ▶ Best value for money proposition in the market to compete with affordable LTE allnet

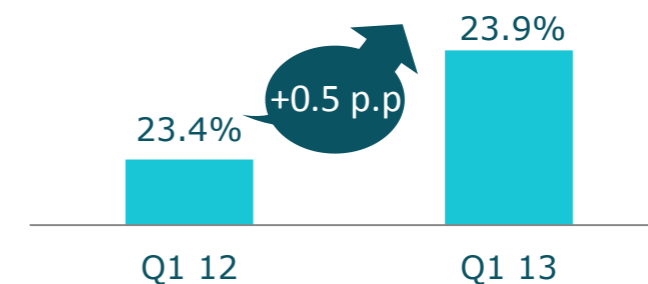
Focus on quality and capital allocation

- **Convergent strategy reinforced**
 - ▶ Unbinding MoU with DT for a long-term cooperation for the development of fixed NGA
- **LTE deployment**

Mobile business in Q1 13



OIBDA Margin



Main take-aways

- The world is changing and T.Europe has the assets to lead this technological change
- We have changed our mind-set across countries to think in Europe-global level, with an open-mind and flexible attitude
- We have strengthen our position in the market by changing the rules of the game with disruptive commercial initiatives, innovative tariffs and refreshed customer approach
- T. Europe is undertaking a deep transformation process towards increased profitability
 - Managing cost base and optimising the allocation of resources
 - Investing in future growth: LTE and Fiber
- We are moving on the right direction to lead the sector and become a benchmark operator



Telefonica
