

NOTA DE PRENSA

PRESS RELEASE

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TELEFÓNICA'S NET INCOME INCREASED BY 42.2%, REACHING 779 MILLION EUROS IN THE FIRST QUARTER OF THE YEAR

Financial Highlights

- Revenues amounted to €13,132M (+5% year on year; +1.5% in organic terms), driven by service revenues (+1.7% organic growth). Mobile data revenues services was particularly notable, maintaining its double-digit growth.
- OIBDA reached €4,021M (+4.8% year on year; +1.3% in organic terms) and the margin remained stable.
- Free cash flow totalled €599M in the quarter, and improved by €530M versus January-March of 2016.
- Net income reached €779M (+42.2% vs 1Q16) and earnings per share stood at €0.14 (+48.8%).
- Improved quality of the customer base reflects in LTE customers (1,7x year-on-year), in the number of smartphones (+18%) and in the growth in FTTx and cable (+21%). Total customer base stands at 347 million accesses.

José María Álvarez-Pallete, Executive Chairman of Telefónica:

"First quarter results reflected a further step forward in our business model, which is focused on the pursuit of sustainable growth. The differential quality of our asset portfolio enables us to offer differential services, which translated into improvements in our results; in particular: i) the growth in main financial metrics, including the positive impact of foreign exchange rates in the quarter; ii) the savings obtained from synergy capture and process simplification; and iii) the strengthening of our balance sheet and the strong free cash flow growth, 9x higher vs. January-March 2016. In addition, we have announced the launch of AURA, a new, more innate and simple customer relationship model, a pioneer in the area of cognitive intelligence. At the same time, the results are aligned with our expectations and allow us to reiterate the guidance set for 2017".

Financial Results – January-March 2017

Telefónica presented today its results for the first quarter of the year, which show growth in main financial and operational metrics and a positive impact of exchange rates. With regard to **revenues for the quarter, the figure stands at 13,132 million euros, a 5% increase year on year.**

	January-March 2017	% y-o-y reported	% y-o-y organic
Revenues	€ 13,132 M	+5%	+1.5%
OIBDA	€ 4,021 M	+4.8%	+1.3%
Net Income	€ 779 M	+42.2%	-

In organic terms, revenue has grown by 1.5%, driven by service revenues (+1.7%). Mobile data revenues maintained double-digit y-o-y growth (+13.5% in organic terms).

OIBDA amounted to 4,021 million euros between January and March 2017, which was 4.8% y-o-y (+1,3% in organic terms). This positive result reflects a positive revenue evolution, cost containment efforts, and synergy capture and efficiencies from the transformation process. The OIBDA margin stands at 30.6%, remaining stable versus previous year.

Net income reached 779 million euros in the first quarter, which represented a year-on-year increase of 42.2%, and earnings per share stood at €0.14 (+48.8%).

The company remains committed to the **Company's transformation** with major progress made in the quarter, both in infrastructure and LTE coverage. Regarding infrastructure, at the end of the first quarter, Telefónica achieved nearly 40 million premises passed with FTTX and cable (+14% vs 1Q16), of which 17.4 million are in Brazil (FTTH and cable) and 17.5 million in Spain (FTTH). Moreover, LTE coverage increased by 64%, of which 88% is in Europe. In addition, in February, Telefónica introduced a new customer relationship model based on cognitive intelligence, which was a pioneer in the industry.

In this context, the focus of **CapEX** for the first quarter of 2017 was once again on the deployment of ultra-fast networks and amounted to 1,621 million euros during the period, which was 4.4% less than in the same period of 2016, reflecting integration synergies, consolidation and network optimisation. **Operating cash flow (OIBDA-CAPEX), stood at 2,400 million euros (+12%).**

Free cash flow reached 599 million euros in the first three months of the year, which was a year-on-year increase of 530 million euros, despite working capital seasonality. The effective cost of interest payments in the past 12 months stood at 3.48% to March, which was 128 b.p. lower than the first quarter of 2016.

Net financial debt at the end of the quarter stood at 48,766 million euros, 171 million euros higher compared to December 2016, which is the smallest debt increase in a first quarter of the last three years, despite the seasonal peculiarities of the period. In this regard, Telefónica's **financing activity** amounted to approximately €6,106m equivalent and focused on strengthening the liquidity position, refinancing and extending debt maturities, in an environment of very low rates. Therefore, at the end of March, the company maintained a comfortable liquidity position, with gross debt maturities covered beyond the next 24 month. The average debt life, including the operations carried out since the end of the first quarter, is 8.29 years.

The **customer base** amounted to 347 million accesses, which remained stable year on year, and reflects its improved quality, boosting the average revenue per user (+2.1% organic year-on-year growth) and maintaining low levels of churn. The weight of higher-value services continued to increase, as shown by the better numbers of LTE customers (1,7 times), mobile contract accesses (+5%), smartphones (+18%) and FTTx and cable customers (+21%).

The Company reiterates its guidance and dividend announced for 2017.

TELEFÓNICA
CONSOLIDATED INCOME STATEMENT
Unaudited figures (Euros in millions)

	January - March		% Chg	
	2017	2016	Reported	Organic
Revenues	13,132	12,511	5.0	1.5
Internal exp. capitalized in fixed assets	208	213	(2.5)	(5.2)
Operating expenses	(9,348)	(8,943)	4.5	1.0
Supplies	(3,730)	(3,675)	1.5	(0.2)
Personnel expenses	(1,818)	(1,749)	4.0	(0.7)
Other operating expenses	(3,800)	(3,519)	8.0	3.1
Other net income (expense)	29	49	(42.2)	(43.5)
Gain (loss) on sale of fixed assets	8	6	33.9	23.7
Impairment of goodwill and other assets	(7)	1	c.s.	c.s.
<i>Underlying operating income before D&A (OIBDA)</i>	4,109	3,860	6.5	
Operating income before D&A (OIBDA)	4,021	3,838	4.8	1.3
<i>OIBDA Margin</i>	30.6%	30.7%	(0.1 p.p.)	(0.0 p.p.)
Depreciation and amortization	(2,451)	(2,322)	5.6	(1.3)
Operating income (OI)	1,570	1,516	3.6	5.2
Share of profit (loss) of investments accounted for by the equity method	2	(3)	c.s.	
Net financial income (expense)	(449)	(659)	(32.0)	
Profit before taxes	1,123	853	31.7	
Corporate income tax	(314)	(298)	5.4	
Profit for the period	809	555	45.8	
Attributable to equity holders of the Parent	779	548	42.2	
Attributable to non-controlling interests	30	7	n.m.	
Weighted average number of ordinary shares outstanding during the period (millions)	5,062	5,073	(0.2)	
Basic and diluted earnings per share attributable to equity holders of the Parent (euros)	0.14	0.09	48.8	
<i>Underlying basic and diluted earnings per share attributable to equity holders of the Parent (euros)</i>	0.18	0.12	46.1	

Notes:

- Since the second quarter of 2016 Telefonica's operations in the United Kingdom are no longer reported as discontinued operations and all its assets and liabilities have ceased to be reported as "held for sale", and have been reclassified back into full consolidation, in compliance with International Financial Reporting Standards (IFRS). For comparative purposes, the results of Telefonica Group of the first quarter of 2016 are reported following the same criteria.

- The weighted average number of ordinary shares outstanding during the period has been obtained applying the IAS rule 33 "Earnings per share". Thereby, the weighted average of shares held as treasury stock have not been taken into account as outstanding shares. On the other hand, the denominator is retrospectively adjusted for transactions that have changed the number of shares outstanding without a corresponding change in equity (as if such transactions had occurred at the beginning of the earliest period presented). For instance, the bonus share issue carried out to meet the scrip dividends paid in 2016, have been taken into account. Also, the ordinary shares that would be issued upon the conversion of the mandatorily convertible notes issued on 24 September 2014 are included in the calculation of earnings per share from that date.

- Basic earnings per share ratio is calculated dividing Profit for the period attributable to equity holders of the parent, adjusted for the net coupon corresponding to "Other equity instruments", by the weighted average number of ordinary shares outstanding during the period.

- 2016 and 2017 reported figures include hyperinflationary adjustments in Venezuela in both years.

Definitions:

Organic Growth: Assumes constant exchange rates from 2016, excludes the impact of hyperinflationary adjustments in Venezuela in both years and considers a constant perimeter of consolidation. In OIBDA and OI terms, excludes write-downs, capital gains/losses from the sale of companies, sale of towers, restructuring costs and material non-recurring impacts. CapEx also excludes investment in spectrum.

Results by geographies:
(y-o-y changes in organic terms)

Spain. Telefonica España's results continued to reflect the strategy focused on increasing customer value, which resulted in the growing penetration of high-value services. However, the y-o-y changes in the first quarter were affected by the different phasing of tariffs and promotion upgrades. Revenues in January-March came to €3,066m and decreased 2.6% both due to lower service revenues (-1.5%) and lower handset sales (-29.9%).

OIBDA, excluding an additional restructuring provision of €76M, totalled €1,219m in the quarter, decreasing 2.4% y-o-y; and OIBDA margin grew 0.1 p.p. y-o-y to 39.8%. CapEx in January-March stood at €333m, and operating cash flow grew solidly by 8.3% to €886m

Germany. Telefónica Deutschland maintained solid operational momentum in the first quarter of 2017, leveraging a continued strong performance of partners while the competitive environment showed further signs of improvement across segments. The Company also benefited from continued successful execution on the integration milestones. Results were in line with the full-year outlook, reflecting significant regulatory impacts (the reduction in mobile termination rates since December 2016 and the glidepath of the European roaming legislation) that weighed both on revenue and OIBDA performance.

In the first quarter, revenues reached €1,771m (-4.7% y-o-y, improving vs. -6.0% in the fourth quarter of 2016). OIBDA totaled €400m in the quarter and grew 1.4% y-o-y, despite the negative effect from the above mentioned regulatory changes, and reflected incremental synergies totaling €35m more (vs. €55m in the first quarter of 2016), as well as investments in “O2 Free” positioning. The OIBDA margin was 22.6%, up 1.4 p.p. y-o-y.

CapEx benefited from savings related with network consolidation and the rollout of a single LTE network and fell 4.2% y-o-y to €208m in the quarter. Operating cash flow (OIBDA-CapEx) totaled €192m; up 7.7% y-o-y.

United Kingdom. In the first quarter of 2017 Telefónica UK continued to reinforce its position as a leading mobile operator in the UK with increasing users on its network and y-o-y growth in both revenues and OIBDA, underpinned by increasing ARPU and leading levels of loyalty.

Revenues in the first quarter totalled €1,601m and grew 2.1% y-o-y (+2.4% in the fourth quarter 2016). OIBDA grew 0.6% y-o-y to €416m in the quarter, driven by continuing revenue growth, and OIBDA margin stood at 26.0%, slightly decreasing y-o-y (-0.4 p.p.).

CapEx amounted to €225m in January-March, an increase of 30.8% y-o-y, principally dedicated to furthering the LTE rollout. Thus, operating cash flow (OIBDA-CapEx) totalled €191m in the quarter (-21.0% y-o-y).

Brazil. In the first quarter of 2017, Telefónica Brasil recorded an acceleration in revenues mainly driven by the positive performance of mobile service revenues that, together with the reduction in operating expenses (synergies and efficiency measures), enabled it to maintain the solid y-o-y expansion of margins and the strong growth of operating cash flow. Revenues in the first quarter totalled €3,165m and increased by 1.6% y-o-y, underpinned by ARPU growth across the main services. OIBDA totalled €1,104m and increased by 7.5% y-o-y, while the OIBDA margin increased to 34.9% (+1.9 p.p. y-o-y). Over the three first months of the year, the company generated synergies of €107m, €46m of which had a positive impact on revenues from cross-selling and €61m in expenses from renegotiations with suppliers and lower commercial and personnel expenses.

CapEx in this quarter (€397m) was mainly dedicated to expansion of the 4G network, the IP backbone and expansion of the fibre network, reflecting optimisation thanks to the use of big data and synergies. As such, operating cash flow (OIBDA-CapEx) totalled €707m in the quarter and maintained solid growth (+21.6%).

Hispanoamérica. Telefónica Hispanoamérica recorded a solid set of financial results in the first quarter of the year, which was reflected in the positive y-o-y performance in revenues and OIBDA, thanks to the strategic focus on capturing value that translated into a strong increase in the average revenue per user (+9.3% y-o-y).

Revenues in the first quarter increased to €3,285m and grew by 9.2%. OIBDA in the first three months increased to €904m and increased 6.2% y-o-y, while the OIBDA margin stood at 27.5% (-0.8 p.p. y-o-y). The CapEx totalled €430m and decreased 9.0% y-o-y, and was mainly allocated to the rollout of 4G and fibre networks and to improve and increase the capacity of 2G and 3G mobile networks. Thus, the operating cash flow (OIBDA-CapEx) rose to €474m, with y-o-y growth of 23.6%.

TELEFÓNICA
SELECTED FINANCIAL DATA
Unaudited figures (Euros in millions)

	January - March	% Chg	
	2017	Reported	Organic
Revenues	13,132	5.0	1.5
Telefónica España	3,066	(2.6)	(2.6)
Telefónica Deutschland	1,771	(4.7)	(4.7)
Telefónica UK	1,601	(8.6)	2.1
Telefónica Brasil	3,165	30.2	1.6
Telefónica Hispanoamerica	3,285	7.6	9.2
Other companies & eliminations	244	(8.6)	(3.3)
Telxius	188	36.4	5.4
OIBDA	4,021	4.8	1.3
Telefónica España	1,143	(8.6)	(2.4)
Telefónica Deutschland	400	2.0	1.4
Telefónica UK	416	(9.8)	0.6
Telefónica Brasil	1,104	37.2	7.5
Telefónica Hispanoamerica	904	4.4	6.2
Other companies & eliminations	53	(15.8)	(44.7)
Telxius	92	n.m.	14.3