

# PRESS RELEASE

**Madrid, 23 February 2017**

The organic growth of the business translates into healthy cash generation, with an annual free cash flow totalling 4,370 million euros (+24.4%).

## **Telefónica increases its growth rates in 2016 and achieves a net income of 4,038 million euros (+4.8%), excluding non-recurrent factors**

**Jose María Álvarez-Pallete, Executive Chairman: "2016 results strengthened our sustainable growth, following the fourth quarter acceleration of growth rates in main operational metrics. At the same time, the strong acceleration of free cash flow generation in the year and the long-term financing raised, accelerated deleverage and bolstered our financial structure. For 2017 we expect similar operating trends: revenue stability despite higher regulatory impacts mainly in European markets, OIBDA margin expansion and lower CapEx intensity".**

- Telefonica announces guidance<sup>1</sup> for 2017 and confirms shareholders remuneration:

- Revenues: stable vs. 2016, despite the negative impact from regulation (approximately 1.2 p.p.)
- OIBDA Margin: year-on-year expansion up to 1 p.p.
- CapEx/Sales excluding spectrum: around 16%.

- Revenues and OIBDA The organic growth rates of the business continued to increase, as shown by the quarterly increase in revenues (+2.7%) and OIBDA (+9.4%). In annual terms, revenues totalled 52,036 million euros (+1.3%) while OIBDA stood at 15,118 million euros (+4.7%).
- Non-recurrent factors. The figures reported at the end of the year are affected by several non-recurrent factors, mainly an impact of 1,290 million euros in the fourth quarter related to restructuring costs, which will generate additional savings and will improve efficiency. Without these effects, in underlying terms, OIBDA totalled 16,519 million euros for the year.
- Net income. Telefónica made a profit of 4,038 million euros in 2016, 4.8% more than in 2015, excluding the non-recurrent factors for the year. Taking these effects into account, the net income at 2,369 million euros.
- Investment. The company continued to maintain historically high figures in terms of investment. Thus, the annual CapEx stood at 8,928 million euros, including the acquisition of spectrum, and was mainly assigned to the deployment of ultra-fast networks, in such a way that, by the end of 2016, there were already more than 39 million premises passed with FTTx and cable.

### <sup>1</sup> Guidance 2017:

#### **Guidance 2017:**

- ✓ Assumes constant exchange rates of 2016 (average of 2016), excluding the impact of hyperinflationary adjustments in Venezuela in both years, and constant perimeter of consolidation.
- ✓ Excludes:
  - OIBDA excludes additionally write-downs, capital gains/losses from the sale of companies, tower sales, material non-recurrent impacts and restructuring costs.
  - CapEx excludes additionally spectrum acquisition.

#### **2016 adjusted base: Revenues (51,734 million euros), OIBDA margin (31.8%) and CapEx (ex-spectrum) to sales ratio**

- ✓ Excludes:
  - The results of the companies sold in 2016 (Telefó, T. Personalizadas and Vocem) from January 1st, 2016 to the date of exiting the perimeter of consolidation.
  - OIBDA excludes additionally write-downs, capital gains/losses from the sale of companies, tower sales, material non-recurrent impacts and restructuring costs.
  - CapEx excludes additionally spectrum acquisition.

- Debt and cash generation. Net financial debt fell by 998 million euros in the quarter and stood at 48,595 million euros in December 2016. Meanwhile, the annual free cash flow rose by 24.4% in the year and totalled 4,370 million euros, as a result of the improving business in the different countries and despite the commitment to investment.
- Customers. The quality of the customer base continued to improve, due both to the increase in average revenue and the improvement in churn rates (-0.5 percentage points year-on-year). The total number of accesses stood at 350 million and reflected the growth of greater-value services, including LTE (1.8 times more than in 2015, up to 66.3 million), smartphones (17%), fibre and cable (+24%) and mobile contracts (+6%).
- Financing. Telefónica's financing activity in 2016, together with the bond issues in January and February 2017, exceeded 13,100 million euros and continued to focus on strengthening the liquidity position, refinancing the debt maturities (within an environment with very low interest rates) and extending maturities. Thus, the liquidity position stands at 23,842 million euros, almost covering debt maturities for the next two years and extending average net debt to 6.77 years.
- Diversification and scale. Telefonica is well diversified across markets in terms of revenues: Telefónica Spain accounts for 24.4%, Telefónica Latin America 24.2%, T. Brazil 21.3%, T. Germany 14.4% and T. United Kingdom 13.2%.
  - Telefónica Spain returns to profitable growth profile in 2016 and recorded organic increases of 1.1% and 1.4% in service revenues and the OIBDA, respectively.
  - Telefónica Brazil's consolidates its mobile market leadership and closes 2016 with an operating cash flow increase of 17.8% in the year.
  - Telefónica Germany's OIBDA growth rate accelerated in the last quarter of the year (by an +3.8% organic year-on-year), supported by the capture of synergies.
  - The business in the United Kingdom enhanced its position as the leading mobile operator in the market in 2016 and grew in terms of revenues (+0.6%) and OIBDA (+1.7%).
  - Telefónica Latin America closed the year with an annual rise of 8.6% in revenues and 3.9% in the OIBDA and also displayed a very solid fourth quarter, with both items recording double-digit year-on-year growth within a context of intense commercial activity.

**Madrid, 23 February 2017.-** Telefónica today presented an underlying net income of 4,038 million euros (+4.8% year-on-year). Bearing in mind the non-recurrent impacts recorded in the year -mainly restructuring costs, capital gains and goodwill losses- the reported annual net income stands at 2.369 million euros.

With organic growth rates consolidating the current positive trend, the figures published today reflect a strengthened competitive position, due to the company's differential infrastructure and the investment undertaken. The company has once again reported extremely high investment figures, up 8,928 million euros on 2016, chiefly assigned to the deployment of ultra-fast networks. At the end of the year, Telefónica had 39.2 premises passed with FTTx and cable, and 62% LTE coverage (87% of the total in Europe).

The quality of the customer base also continued to improve in 2016, in such a way that revenues rose by an organic 1.3% (by 2.7% in the quarter) to 52,036 million euros. We should highlight service revenues, whose year-on-year growth rose by 3.7%. The increase in OIBDA, although affected by the above-mentioned extraordinary factors, accelerated during the quarter, by up to 4 times in reported terms compared with the figure obtained in the last quarter of 2015 and by 9.4% more in organic terms. The organic growth for the year as a whole stood at 4.7%, with a total of 15,118 million euros. In underlying terms, the figure reached 16,519 million euros.

The free cash flow was also considerable, with a total of 2,055 million euros in the quarter and 4,370 million euros throughout the year (+24.4% year-on-year). Net debt, on the other hand, fell by 998 million euros in the quarter and stood at 48,595 million euros in December, as a result of which both items, solid cash generation and the resulting organic deleverage, remain strategic pillars of the company.

TELEFÓNICA  
CONSOLIDATED INCOME STATEMENT  
Unaudited figures (Euros in millions)

	January - December		% Chg		October - December		% Chg	
	2016	2015	Reported	Organic	2016	2015	Reported	Organic
Revenues	52,036	54,916	(5.2)	1.3	13,721	13,862	(1.0)	2.7
Internal exp. capitalized in fixed assets	867	946	(8.3)	(5.9)	231	277	(16.8)	(14.4)
Operating expenses	(38,043)	(43,075)	(11.7)	(0.7)	(10,852)	(13,697)	(20.8)	(2.3)
Supplies	(15,242)	(16,547)	(7.9)	(3.1)	(4,134)	(4,334)	(4.6)	(0.7)
Personnel expenses	(8,098)	(10,349)	(21.8)	1.9	(2,958)	(4,955)	(40.3)	(0.8)
Other operating expenses	(14,703)	(16,179)	(9.1)	0.5	(3,760)	(4,408)	(14.7)	(4.8)
Other net income (expense)	186	270	(31.0)	(8.8)	39	225	(82.5)	(48.2)
Gain (loss) on sale of fixed assets	296	279	6.1	(57.3)	266	159	67.7	(68.0)
Impairment of goodwill and other assets	(224)	(106)	112.2	n.m.	(219)	(105)	108.8	n.m.
Operating income before D&A (OIBDA) Underlying	16,519	16,851	(2.0)		4,464	4,210	6.0	
Operating income before D&A (OIBDA)	15,118	13,229	14.3	4.7	3,187	721	n.m.	9.4
OIBDA Margin	29.1%	24.1%	5.0 p.p.	1.0 p.p.	23.2%	5.2%	18.0 p.p.	2.0 p.p.
Depreciation and amortization	(9,649)	(9,704)	(0.6)	2.0	(2,518)	(2,472)	1.8	(2.0)
Operating income (OI)	5,469	3,525	55.2	8.3	669	(1,751)	c.s.	25.3
Share of profit (loss) of investments accounted for by the equity method	(5)	(10)	(54.3)		(2)	(1)	n.m.	
Net financial income (expense)	(2,219)	(2,609)	(14.9)		(369)	(687)	(46.3)	
Profit before taxes	3,245	906	n.m.		298	(2,438)	c.s.	
Corporate income tax	(846)	(155)	n.m.		(105)	297	c.s.	
Profit for the period	2,399	751	n.m.		193	(2,142)	c.s.	
Non-controlling interests	(30)	(135)	(77.9)		(49)	(95)	(48.6)	
Net Income	2,369	616	n.m.		145	(2,236)	c.s.	
Weighted average number of ordinary shares outstanding during the period (millions)	5,061	5,071	(0.2)		5,053	5,118	(1.3)	
Basic earnings per share (euros)	0.42	0.07	n.m.		0.01	(0.45)	c.s.	
Basic earnings per share (euros) Underlying	0.75	0.71	5.1		0.23	0.09	165.7	

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 Grupo Telefonica of 2015 and 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 2015 and 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 Net Income, adjusted for the net coupon corresponding to "Other equity instruments", by the weighted average number of ordinary shares outstanding during the period.
- 2015 and 2016 reported figures include hyperinflationary adjustments in Venezuela in both years.
- Group consolidated results consolidate GVT and DTS' results since 1 May 2015.
- Telef3 has been deconsolidated from the Group consolidated results since 1 November 2016.

Telefonica announced today the guidance for 2017 and confirmed shareholders remuneration, so the second tranche of 2016 dividend (0.20 euros per share in cash) will be paid in the second quarter of 2017, and dividend for 2017 of 0.40 euros per share in cash, will be paid in the fourth quarter of 2017 (0.20 euros per share) and in the second quarter of 2018 (0.20 euros per share).

- Revenues: stable vs. 2016, despite the negative impact from regulation (approximately 1.2 p.p.)
- OIBDA Margin: year-on-year expansion up to 1 p.p.
- CapEx/Sales excluding spectrum: around 16%.

On the other hand, as of December 2016, Telefonica Group total accesses increased by 1% year-on-year to 350.0 million, with continued customer quality improvement. Thus, unitary customer value improved in the fourth quarter: both due to average revenue per customer growth, accelerating year-on-year to 4.4%, and

churn improvement (-0.5 percentage points year-on-year). Growing demand for data, speed and content was reflected in the strong growth of high value services: LTE customers stood at 66.3 million (1.8 times vs. the previous year), with net additions in the quarter +25% year-on-year; mobile contract accesses and smartphones grow +6% and 17% year-on-year, respectively; FTTx and cable customers grew by 24% vs. 2015 and pay TV accesses reached 8.3 million with a penetration of 48%.

### Income statement analysis

Before analysing the results, the negative impact arising from the evolution of exchange rates continued to diminish; in the fourth quarter, it deducted 3.2 percentage points from year-on-year revenue change, -8.0 percentage points in 2016. At OIBDA level, the impact in the year was -8.8 percentage points and its negative impact was also reduced significantly in the fourth quarter (-94 million euros; -187 million in the previous quarter; -885 million in the first six months). Nevertheless, it is important to highlight that currency depreciations had a limited impact in terms of cash generation, since depreciations also decreased payments in euros related to investments, taxes, interest and minorities, almost entirely offsetting the negative impact at OIBDA level in 2016.

In the fourth quarter of 2016, the changes in the perimeter of consolidation (mainly the sale of Telef ) reduced revenue and OIBDA year-on-year growth 0.5 percentage points and 2.1 percentage points respectively (+1.4 percentage points in revenues and +1.3 percentage points in OIBDA in January-December 2016 affected by the incorporation of GVT and DTS in May 2015).

### Revenues and expenses

**Revenues** increased to 13,721 million euros in October-December and grew by 2.7% organic (-1.0% in reported terms), posting an acceleration of 3.0 percentage points, driven by the solid performance of service revenues (+3.7% in the fourth quarter; +2.6% in the year). In the January-December period, revenues amounted to 52,036 million euros, +1.3% organic year-on-year (-5.2% reported). Excluding the negative impact of regulation, revenues would have grown 3.6% organic year-on-year in the quarter (+2.2% in 2016).

The revenue structure reflected the high degree of diversification and scale of the Company; thus T. Espa a accounted for 24.4% of consolidated revenues from January-December, followed by T. Hispanoam rica (24.2%), T. Brasil (21.3%), T. Deutschland (14.4%) and T. UK (13.2%).

By services, in January-December 2016, broadband revenues accelerated their year-on-year organic growth to 16.1%, services over connectivity grew by 7.7% and voice and access decreased by 7.9%. Thus, broadband revenues and services over connectivity accounted for 46.8% of total revenues in 2016 (+6.1 percentage points year-on-year). Mobile data revenues continued to post double digit growth this quarter (+12.3% organic year-on-year in the quarter and in the year) and represented 52% of mobile service revenues from January-December (+4.9 percentage points) due to the increased penetration of smartphones and LTE.

**Operating expenses** totalled 10,852 million euros in the fourth quarter and improved their organic evolution by 0.8 percentage points vs. the previous quarter to -2.3% year-on-year (-20.8% reported) due to better commercial spend evolution, a change in the trend of personnel expenses and the capture of synergies and efficiencies from the transformation and simplification process. In January-December 2016 operating expenses amounted to 38,043 million euros and decreased 0.7% organic year-on-year (-11.7% reported).

Reported operating expenses and other net income/expense for the fourth quarter were affected by restructuring cost provisions amounting to 1,290 million euros (1,250 million euros in operating expenses and 40 million euros in other net income/expense). These provisions did not impact cash flow generation in the

quarter and were carried out within the Company's transformation and simplification process, which shall enable the generation of incremental savings and efficiencies with a positive impact on cash generation.

Operating income before depreciation and amortisation (OIBDA) amounted to 3,187 million euros in the quarter and its reported year-on-year change (4 times) was affected by the factors mentioned above. Quarterly underlying OIBDA reached 4,464 million euros (4,210 in the same period of 2015) and excluded the following impacts: i) Restructuring costs (-1,290 million euros in the quarter; -1,399 million euros in January-December); ii) Capital gains/losses from the sale of companies (+228 million euros in the quarter; +212 million euros in the year); iii) Goodwill impairments (-215 million euros in the fourth quarter).

In 2016, OIBDA totalled 15,118 million euros and increased by 4.7% in organic terms (+14.3% year-on-year in reported terms). In underlying terms, OIBDA increased to 16,519 million euros.

Organic OIBDA growth accelerated to 9.4% year-on-year in the fourth quarter, with highlights including double digit growth of T. Hispanoamérica, return to growth in T. España, growth acceleration in T. UK and sustained growth rate in T. Deutschland. Thus, OIBDA accelerated its organic growth for the second consecutive quarter (+6.3 percentage points vs. the third quarter). Excluding regulation, OIBDA would have increased 10.4% organic year-on-year in the quarter (+5.7% in January-December).

OIBDA margin for the quarter stood at 32.5% in organic terms and continued to expand by increasing 2.0 percentage points year-on-year, reflecting positive revenue evolution, cost containment efforts and synergies generation. In 2016, OIBDA margin totalled 31.5% organic and expanded 1.0 percentage points vs. the previous year.

**Operating income (OI)** stood at 669 million euros in the fourth quarter of 2016 (-1,751 million euros in the same period of 2015) and increased by 25.3% year-on-year in organic terms. In 2016, operating income amounted to 5,469 million euros (+8.3% year-on-year organic; +55.2% reported).

Net financial expenses totalled 2,219 million euros in January-December, 14.9% lower than the previous year mainly due to the savings from debt management (hedging in pounds linked to T. UK and lower cost of debt in European currencies) and higher revenues associated with inflation in Venezuela, partially offset by the capital loss from the sale of 1.5% stake in China Unicom (-155 million euros) and the result of the divestment in Telecom Italia, S.p.A in 2015 (+380 million euros). In the fourth quarter, net financial expenses reached 369 million euros and decreased vs. the same period of 2015 (687 million euros), mainly due to the reduction in the cost of debt and the impact of inflation in Venezuela

#### **Net income and Capex**

Consolidated **net income** in the quarter reached 1,233 million euros in underlying terms (145 million reported), 2.5 times vs. the same period of the previous year, while in January-December net income amounted to 4,038 million euros (2,369 million reported) and increased by 4.8% year-on-year. Underlying basic earnings per share stood at 0.23 euros in the fourth quarter, 2.7 times vs. the same period of the previous year, and 0.75 euros in January-December (+5.1% vs. 2015).

In 2016, **CapEx** from January-December totalled 8,928 million euros, including 345 million euros for spectrum acquisition, and increased by 3.9% organic vs. 2015 (-14.7% reported). In the fourth quarter, CapEx increased by 11.6% organic year-on-year (+7.5% reported) and stood at 2,912 million euros. The investment effort was mainly focused on the deployment of ultrafast networks, with investment in growth and transformation representing 78.8% of the total (+0.2 percentage points year-on-year).

**Underlying operating cash flow** (OIBDA-CapEx) excluding spectrum for October-December reached 1,556 million euros (279 million euros reported) and grew by 3.8% year-on-year. In 2016, operating cash flow increased by 0.3% vs. 2015 to 7,937 million euros in underlying terms excluding spectrum (6,535 million euros reported).

Thus, in January-December 2016, **free cash flow** totalled 4,370 million euros and increased by 24.4% year-on-year.

**Net financial debt** stood at 48,595 million euros at December 2016 and decreased by 998 million euros in the fourth quarter, thanks to: i) free cash flow generation of 2,055 million euros; ii) net financial divestments of 287 million euros, mainly associated with the sale of Telef . On the contrary: i) shareholder remuneration (534 million euros, including dividend payment and coupons from capital instruments), ii) payment of labour-related commitments (140 million euros), iii) other factors affecting the valuation of liabilities (432 million euros, including the refinancing of commercial liabilities), and iv) the higher value in euros of net debt in foreign currencies, mainly due to the appreciation of Latin American currencies vs. the euro (238 million euros).

Compared to December 2015, net financial debt decreased by 566 million euros in 2016, due to: i) free cash flow generation of 4,370 million euros; ii) net financial divestments of 500 million euros, mainly associated with the sale of the stake in China Unicom and Telef  and iii) lower value in euros of net debt in foreign currencies (91 million euros). On the other hand, factors causing the debt to increase: i) shareholder remuneration (dividends, treasury stock, issuance of capital instruments net of coupon payments) in the sum of 2,389 million euros; ii) payment of labour-related commitments (738 million euros) and iii) other factors affecting the valuation of liabilities amounting to 1,268 million euros (including the refinancing of commercial liabilities).

In 2016, **Telef nica's financing activity** amounted to approximately 10,542 million equivalent euros, without considering the re-financing of commercial paper and short-term bank loans. The activity mainly focused on strengthening the liquidity position, refinancing debt maturities in an environment of very low interest rates and extending maturities. Including January and February bond issuances, financing activity exceeded 13,100 million euros, almost covering debt maturities for the next two years and extending average net debt to 6.77 years.

## Digital Services and Global Resources

**Digital services** revenues continued to present double-digit year-on-year growth and reached 1,281 million euros in the fourth quarter (+11.1%) and 4,792 million in 2016 (+14.1%). Video revenues, 726 million euros in the quarter (2,802 million in January-December), maintained a solid year-on-year growth rate (+9.7%; +12.4% in the year) driven mainly by the consistent increase in the TV base in Hispanoamerica (+4%) and by the improvement in ARPU in Brazil and Spain associated with the wider adoption of premium content. Pay TV accesses stood at 8.3 million as of December (including 4.3 million satellite TV accesses), stable versus 2015.

In 2016, **Telefonica Global Resources** has modernised the Company's networks and systems capacities, improving service quality and customer experience and, at the same time, has accelerated the strategy of simplification and generation of efficiencies. Global Network and Operations focused on the expansion of the capacity and coverage of the ultra-broadband access network (FTTx and cable) and the network core.

The growing demand for data continued to drive strong data traffic growth throughout the year (+49% year-on-year), both in fixed broadband (+48% year-on-year). To meet this demand, at the end of 2016, the number of premises passed with ultra-broadband networks (FTTx and cable) increased to 39 million, of which 17 million were in Brazil (FTTx), 17 million in Spain (FTTH) and 5 million in Hispanoamerica (FTTx and cable).



Meanwhile, 4G population coverage stood at 62%, 10 percentage points more in the year (91% Spain; 79% Germany; 95% UK; 60% Brazil; 49% Hispanoamerica), with a total of 55,417 locations.

Additionally, the transformation of the All-IP network has progressed with the deployment of VoIP, VoLTE and VoWiFi. VoIP is offered in 7 countries (Spain, Brazil, Germany, Colombia, Argentina, Chile and Peru) and has reached 6.3 million accesses; VoLTE is now available in 6 countries (Germany, Colombia, Peru, Brazil, Argentina and UK) and native VoWiFi is now offered in Germany and Argentina.

#### Notes:

**Organic Growth:** Assumes constant exchange rates from 2015, 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-recurrent impacts. CapEx also excludes investment in spectrum.

**Underlying Growth:** Reported figures excluding the impact of write-downs, capital gains/losses from the sale of companies, tower sales, restructuring costs and material non-recurrent impacts as well as depreciation and amortisation charges from purchase price allocation processes.

#### Guidance 2017:

- ✓ Assumes constant exchange rates of 2016 (average of 2016), excluding the impact of hyperinflationary adjustments in Venezuela in both years, and constant perimeter of consolidation.
- ✓ Excludes:
  - OIBDA excludes additionally write-downs, capital gains/losses from the sale of companies, tower sales, material non-recurrent impacts and restructuring costs.
  - CapEx excludes additionally spectrum acquisition.

2016 adjusted base: Revenues (51,734 million euros), OIBDA margin (31.8%) and CapEx (ex-spectrum) to sales ratio

- ✓ Excludes:
  - The results of the companies sold in 2016 (Telef , T. Personalizadas and Vocem) from January 1st, 2016 to the date of exiting the perimeter of consolidation.
  - OIBDA excludes additionally write-downs, capital gains/losses from the sale of companies, tower sales, material non-recurrent impacts and restructuring costs.
  - CapEx excludes additionally spectrum acquisition.

TELEFÓNICA ESPAÑA

Telefónica España results showed a significant improvement in 2016 and reflected the recovery of a profitable and sustainable growth profile, underpinned by a leading differential infrastructure in Europe, enabling it to increase the penetration of high value services tailored to increasing customer needs.

In 2016, service revenues returned to growth (+1.1% year-on-year) and at the same time, cost management and savings obtained from simplification have translated into year-on-year growth of OIBDA (+2.2%) and cash flow generation (+1.8%), excluding impacts.

Furthermore, in the last quarter of 2016, there was a sequential improvement in the year-on-year growth of service revenues (+1.9%; +1.2 percentage points vs. the previous quarter) and OIBDA (+2.6%; +0.8 percentage points vs. the third quarter).

It is important to note that the results of the fourth quarter of 2016 are impacted by the extraordinary provision of 856 million euros, booked in the quarter and associated mainly with the extension of the voluntary employment suspension plan to 2018, which will generate a positive impact on cash flow generation from 2018 and an annual run-rate of savings in direct expenses of approximately 100 million euros from 2019. These savings are in addition to those derived from the 2016-2017 plans.

TELEFÓNICA ESPAÑA  
CONSOLIDATED INCOME STATEMENT  
Unaudited figures (Euros in millions)

	January - December		% Chg		October - December		% Chg	
	2016	2015	Reported	Organic	2016	2015	Reported	Organic
Revenues	12,713	12,402	2.5	(0.1)	3,216	3,220	(0.1)	(0.1)
Mobile handset revenues	497	648	(23.4)	(23.4)	142	202	(29.7)	(29.7)
Revenues ex-mobile handset revenues	12,216	11,754	3.9	1.1	3,074	3,018	1.9	1.9
Consumer (1)	6,536	6,129	6.6	1.8	1,631	1,576	3.5	3.5
Fusión	4,095	3,368	21.6	21.6	1,053	895	17.7	17.7
Non-Fusión	2,441	2,761	(11.6)	(20.0)	578	681	(15.2)	(15.2)
Business	3,423	3,473	(1.4)	(1.4)	881	869	1.4	1.4
Communications	2,708	2,799	(3.3)	(3.3)	675	681	(0.9)	(0.9)
IT	716	674	6.2	6.2	206	187	9.7	9.7
Other (2)	2,257	2,152	4.8	3.2	563	573	(1.8)	(1.8)
Internal expenditure capitalized in fixed assets	327	350	(6.5)	(6.5)	83	100	(17.5)	(17.5)
Operating expenses	(8,652)	(10,526)	(17.8)	(1.8)	(2,821)	(4,952)	(43.0)	(3.5)
Supplies	(3,375)	(2,996)	12.7	4.4	(899)	(867)	3.7	3.7
Personnel expenses	(2,997)	(5,173)	(42.1)	(6.2)	(1,357)	(3,477)	(61.0)	(10.7)
Other operating expenses	(2,280)	(2,356)	(3.2)	(5.9)	(566)	(608)	(7.0)	(7.0)
Other net income (expense)	(29)	(29)	0.5	c.s.	(28)	(29)	(4.2)	c.s.
Gain (loss) on sale of fixed assets	111	136	(18.0)	(15.3)	64	27	136.7	31.5
Impairment of goodwill and other assets	(4)	2	c.s.	c.s.	(2)	4	c.s.	c.s.
Operating income before D&A (OIBDA)	4,467	2,336	91.2	1.4	512	(1,631)	c.s.	3.4
OIBDA Margin	35.1%	18.8%	16.3 p.p.	0.6 p.p.	15.9%	n.m.	n.m.	1.4 p.p.
CapEx	1,847	1,827	1.1	3.0	564	505	11.6	11.6
Spectrum	7	49	(85.0)	(85.0)	-	-	-	-
OpCF (OIBDA-CapEx)	2,621	509	n.m.	0.6	(52)	(2,136)	(97.6)	(1.8)

Notes:

- The reported figures include DTS in Telefónica España's consolidation perimeter from 1 May 2015.

- OIBDA before management and brand fees.

- Mobile handset revenues have been restated from 1 January 2015 including all the business of Telefónica España (previously only Telefónica Móviles España).

(1) Consumer revenues include residential and SOHO revenues.

(2) Other revenues include wholesale, subsidiaries and other revenues.

Movistar Fusión" consumer reached 4.3 million customers (+5% year-on-year) and 2.5 million additional mobile lines (+26% year-on-year), and recorded quarterly net additions of 47 thousand, which continue to drive the penetration of convergent "Fusión" customers over total consumer customers: 83% in



broadband (+3 percentage points year-on-year), 80% in TV (+10 percentage points year-on-year) and 73% in mobile contract (+6 percentage points year-on-year). The quarterly ARPU of "Fusión" stood at 81.6 euros, 12% higher year-on-year, driven by the portfolio renewal and tariffs update, and by the continued improvement of the value mix of customers.

**Operating revenues in the quarter** (3,216 million euros) and in the year (12,713 million euros) remained stable year-on-year (-0.1% in both periods).

**OIBDA** in the fourth quarter after excluding factors stood at 1,306 million euros and increased 2.6% year-on-year, while the margin stood at 40.6% and expanded 1.1 percentage points year-on-year. The abovementioned factors in the fourth quarter included: i) provisions for the employment suspension plan and optimising the distribution channel (837 million in personnel expenses and 18 million in "other net income/expenses" respectively in the fourth quarter of 2016 vs. 2,896 and 30 million in the fourth quarter of 2015); ii) capital gains from the sale of Telecomunicaciones Personalizadas, a public telephony service in penitentiary centres, (29 million in the fourth quarter of 2016) and iii) capital gains from the sale of real estate assets (33 million euros in the fourth quarter of 2016 and 22 million euros in the fourth quarter of 2015).

In 2016, OIBDA increased to 5,223 million euros excluding factors and increased 2.2% year-on-year, while the margin expanded 0.9 percentage points year-on-year to 41.1%.

**CapEx** stood at 1,847 million euros in January-December, including 7 million euros for the purchase of spectrum in the second quarter of 2016 (+3.0% year-on-year; +11.6% in the quarter) due to the intense deployment of LTE and continued investment in fibre.

Thus, **operating cash flow** returned to growth in 2016 to 3,384 million euros, +1.8% excluding factors.

#### TELEFÓNICA DEUTSCHLAND *(year-on-year changes in organic terms)*

Telefónica Deutschland maintained operational momentum in a dynamic fourth quarter of 2016, leveraging the successful launch and encouraging customer response to its new premium portfolio "O2 Free". Competitive pressure in non-premium segment is showing some signs of improvement, that continues in the first months of 2017. At the same time, the Company delivered its integration milestones, generating additional savings in line with the synergy targets. In addition, Telefónica Deutschland also met its outlook for the full-year financial results. Furthermore, the results are affected by the reduction in mobile termination rates since last 1 December (-34%; from €1.66 cents to €1.1 cents).

**Revenues** in the fourth quarter of 2016 reached 1,936 million euros (-6.0% year-on-year) and 7,503 million euros for the twelve month period (-4.9% year-on-year).

**OIBDA** came to 481 million euros in the fourth quarter and accelerated its year-on-year growth to +3.9% excluding impacts (+3.6% in the third quarter) leveraging on incremental synergies of approximately 25 million euros in the quarter (approximately 150 million euros in 2016). In the period January-December 2016, OIBDA amounted to 1,794 million euros and increased 3.8% year-on-year excluding the above-mentioned restructuring costs and the positive settlement of 102 million euros and the "yourfone" effect of 15 million euros in the first quarter of 2015.

The **OIBDA margin** was 24.8% in the fourth quarter, up 2.5 percentage points year-on-year and 23.9% for the twelve months period, up 2.1 percentage points year-on-year organic and ex-yourfone in the first quarter of 2015.

TELEFÓNICA DEUTSCHLAND  
CONSOLIDATED INCOME STATEMENT  
Unaudited figures (Euros in millions)

	January - December		% Chg		October - December		% Chg	
	2016	2015	Reported	Organic	2016	2015	Reported	Organic
Revenues	7,503	7,888	(4.9)	(4.9)	1,936	2,059	(6.0)	(6.0)
Mobile Business	6,498	6,832	(4.9)	(4.9)	1,690	1,791	(5.7)	(5.7)
Mobile service revenues	5,437	5,532	(1.7)	(1.7)	1,349	1,378	(2.1)	(2.1)
Data revenues	2,992	2,840	5.3	5.3	746	712	4.8	4.8
Handset revenues	1,061	1,300	(18.4)	(18.4)	341	413	(17.6)	(17.6)
Fixed Business	981	1,043	(5.9)	(5.9)	238	266	(10.3)	(10.3)
FBB and new services (1)	748	803	(6.8)	(6.8)	182	199	(8.6)	(8.6)
Voice & access revenues	233	240	(2.9)	(2.9)	56	66	(15.5)	(15.5)
Internal expenditure capitalized in fixed assets	104	113	(7.4)	(7.4)	25	30	(17.8)	(17.8)
Operating expenses	(5,844)	(6,226)	(6.1)	(6.8)	(1,492)	(1,631)	(8.5)	(8.7)
Supplies	(2,452)	(2,712)	(9.6)	(9.6)	(674)	(747)	(9.8)	(9.8)
Personnel expenses	(646)	(655)	(1.4)	(7.9)	(157)	(155)	1.5	(1.7)
Other operating expenses	(2,747)	(2,859)	(3.9)	(3.9)	(661)	(729)	(9.4)	(9.0)
Other net income (expense)	32	70	(54.8)	113.9	12	128	(90.7)	20.6
Gain (loss) on sale of fixed assets	(0)	14	c.s.	c.s.	(0)	(1)	(80.9)	(80.9)
Impairment of goodwill and other assets	-	-	-	-	-	-	-	-
Operating income before D&A (OIBDA)	1,794	1,858	(3.4)	2.9	481	586	(18.0)	3.8
OIBDA Margin	23.9%	23.6%	0.4 p.p.	1.9 p.p.	24.8%	28.5%	(3.6 p.p.)	2.5 p.p.
CapEx	1,108	2,230	(50.3)	6.8	360	330	9.0	9.2
Spectrum	6	1,198	(99.5)	(99.5)	1	2	(11.5)	(11.5)
OpCF (OIBDA-CapEx)	686	(372)	c.s.	(2.1)	121	256	(52.9)	(6.9)

Notes:

- OIBDA before management and brand fees.

(1) Includes broadband connectivity services (retail and wholesale), including value added services, data and ICT revenues, other services over connectivity and FBB equipment.

**CapEx** was up 9.2% year-on-year to 360 million euros in the fourth quarter (+6.8% year-on-year to 1,108 million euros in 2016) as investments were back-end loaded in 2016 due to the intensification of the network integration efforts in the second half of the year.

**Operating cash flow** (OIBDA-CapEx) totalled 686 million euros and remained almost flat in 2016 (-0.2% year-on-year).

TELEFÓNICA UK (year-on-year changes in organic terms)

In 2016 Telefónica UK continued to reinforce its position as a leading mobile operator, consistently outperforming the market, with a growing customer base, increasing spend by customers as well as market-leading loyalty, leading to a strong financial performance with sustained revenue growth. Total mobile accesses (25.5 million) grew 2% year-on-year driven by a 9% year-on-year increase of the contract mobile customer base.

**Revenues** in the fourth quarter reached 1,721 million euros and grew 2.5% year-on-year excluding the impact of "O2 Refresh", once again improving the growth trend from the previous quarter (+0.1% year-on-year) on both mobile service revenue and handset sales and others. For the full year, revenues totalled 6,861 million euros, +0.6% year-on-year (ex-"O2 Refresh").

**OIBDA** growth in the quarter reached 4.1% year-on-year to 334 million euros and improved vs. the third quarter (+1.6%) on revenue growth acceleration and strong cost control. Full year OIBDA reached 1,709 million euros (+1.7% year-on-year). Thus, OIBDA margin expanded in both the fourth quarter (19.4%; +0.4 percentage points year-on-year) and the full year 2016 (24.9%; +0.8 percentage points year-on-year).

TELEFÓNICA UK  
CONSOLIDATED INCOME STATEMENT  
Unaudited figures (Euros in millions)

	January - December		% Var		October - December		% Var	
	2016	2015	Reported	Organic	2016	2015	Reported	Organic
Revenues	6,861	7,837	(12.5)	(1.5)	1,721	2,011	(14.4)	2.4
Mobile service revenues	5,121	5,778	(11.4)	(0.3)	1,220	1,447	(15.7)	1.3
Data revenues	3,094	3,369	(8.1)	3.4	738	848	(12.9)	4.5
Handset revenues and other	1,739	2,059	(15.5)	(4.9)	500	564	(11.2)	5.2
Internal expenditure capitalized in fixed assets	141	162	(13.1)	(2.2)	34	43	(21.1)	(5.4)
Operating expenses	(5,276)	(6,074)	(13.1)	(2.9)	(1,421)	(1,636)	(13.2)	1.1
Supplies	(3,226)	(3,769)	(14.4)	(3.7)	(858)	(992)	(13.6)	2.9
Personnel expenses	(528)	(549)	(3.9)	1.2	(145)	(144)	0.3	(6.3)
Other operating expenses	(1,522)	(1,756)	(13.3)	(2.4)	(418)	(499)	(16.2)	(0.5)
Other net income (expense)	(16)	(14)	11.9	25.9	(2)	(7)	(74.8)	(67.3)
Gain (loss) on sale of fixed assets	(1)	3	c.s.	c.s.	1	1	84.9	102.2
Impairment of goodwill and other assets	-	15	-	-	-	15	-	-
Operating income before D&A (OIBDA)	1,709	1,929	(11.4)	1.7	334	426	(21.7)	4.1
OIBDA Margin	24.9%	24.6%	0.3 p.p.	0.8 p.p.	19.4%	21.2%	(1.8 p.p.)	0.4 p.p.
CapEx	931	883	5.5	18.7	278	231	20.2	42.1
Spectrum	-	-	-	-	-	-	-	-
OpCF (OIBDA-CapEx)	778	1,046	(25.6)	(12.7)	56	196	(71.3)	(39.9)

Notes:  
- OIBDA before management and brand fees.

**CapEx** amounted to 931 million euros in the January-December period, an increase of 18.7% year-on-year, mainly invested in further LTE rollout as the Company continues to expand its indoor coverage to reach 98% by the end of 2017.

**Operating Cash Flow** (OIBDA-CapEx) totalled 778 million euros in the full year to December (-12.7% year-on-year).

TELEFÓNICA BRASIL (year-on-year changes in organic terms)

In the fourth quarter of the year Telefonica Brasil consolidated the trend of solid year-on-year growth both in revenues and in OIBDA, which, together with the year-on-year reduction of CapEx in the year, translated into a strong increase in operating cash flow.

These results reflected the selective commercial activity focused on high value customers, the continued generation of synergies after the acquisition of GVT and the strict cost control, which offset inflationary pressure and regulatory impacts.

The company managed **97.2 million accesses**, stable year-on-year. Mobile accesses increased by 1% year-on-year, with focus on higher value customers which resulted in a clear increase in the quality of mobile accesses: contract accesses +7%, smartphones +25% (75% penetration, +15 percentage points year-on-year) and LTE accesses +118%.

**Revenues** in the fourth quarter totalled 3,058 million euros (11,097 million in 2016) increasing by 1.1% year-on-year (+0.9% in 2016) driven by ARPU growth across all services, which was partially offset by

regulatory impacts and lower handset sales (-2.3 percentage points and -0.7 percentage points respectively in year-on-year change for the quarter).

**OIBDA** in the fourth quarter reached 1,085 million euros (3,714 million in the year) and decreased by 0.9% year-on-year due to the positive impact of the expiration of a payable account for 98 million euros in the fourth quarter of 2015; excluding this impact, OIBDA would have grown by 8.9% (+8.1% in the year).

Thus, **OIBDA margin** expanded to 35.5% in the quarter (-0.7 percentage points year-on-year, +2.6 percentage points excluding the aforementioned impact) and 33.5% in the year (+1.4 percentage points year-on-year, +2.2 percentage points excluding the impact mentioned above).

TELEFÓNICA BRASIL  
CONSOLIDATED INCOME STATEMENT  
Unaudited figures (Euros in millions)

	January - December		% Chg		October - December		% Chg	
	2016	2015	Reported	Organic	2016	2015	Reported	Organic
Revenues	11,097	11,060	0.3	0.9	3,058	2,587	18.2	1.1
Mobile Business	6,669	6,905	(3.4)	1.7	1,853	1,526	21.4	2.7
Mobile service revenues	6,357	6,495	(2.1)	3.1	1,774	1,444	22.8	4.0
Data revenues	3,381	2,853	18.5	24.7	1,016	705	44.2	25.5
Handset revenues	312	410	(23.9)	(20.0)	79	82	(3.7)	(20.7)
Fixed Business	4,428	4,154	6.6	(0.2)	1,205	1,060	13.6	(1.2)
FBB and new services (1)	1,695	1,502	12.9	6.5	473	386	22.5	6.5
Pay TV	504	391	29.1	11.8	137	116	18.3	4.6
Voice & access revenues	2,229	2,262	(1.5)	(6.9)	595	559	6.4	(7.7)
Internal exp. capitalized in fixed assets	114	91	25.0	4.8	32	23	43.1	7.1
Operating expenses	(7,498)	(7,655)	(2.0)	(1.9)	(2,029)	(1,741)	16.5	(1.6)
Supplies	(2,249)	(2,568)	(12.4)	(10.9)	(600)	(593)	1.1	(14.0)
Personnel expenses	(1,167)	(1,042)	11.9	3.1	(326)	(262)	24.2	3.8
Other operating expenses	(4,082)	(4,044)	0.9	2.5	(1,103)	(885)	24.6	5.0
Other net income (expense)	1	75	(98.2)	(97.0)	23	108	(78.4)	(75.6)
Gain (loss) on sale of fixed assets	(1)	5	c.s.	(84.8)	(2)	10	c.s.	c.s.
Impairment of goodwill and other assets	1	(3)	c.s.	c.s.	3	(3)	c.s.	c.s.
Operating income before D&A (OIBDA)	3,714	3,573	3.9	5.3	1,085	983	10.3	(0.9)
OIBDA Margin	33.5%	32.3%	1.2 p.p.	1.4 p.p.	35.5%	38.0%	(2.5 p.p.)	(0.7 p.p.)
CapEx	2,138	2,105	1.6	(2.9)	769	604	27.2	14.6
Spectrum	48	-	-	-	1	-	-	-
OpCF (OIBDA-CapEx)	1,576	1,468	7.3	17.8	316	379	(16.6)	(25.6)

Notes:

- The Consolidated Income Statement of Telefonica Brasil includes GVT since 1 May 2015.

- OIBDA before management and brand fees.

(1) Includes broadband connectivity services (retail and wholesale), including value added services, ICT revenues, other services over connectivity and FBB equipment.

The company closed 2016 having generated **synergies** of 247 million euros, 95 million euros of which positively impacted revenues from cross-selling and 152 million euros in expenses from renegotiations with suppliers and from lower commercial and personnel expenses.

**CapEx** totalled 2,138 million in 2016 (representing 19% of revenues, excluding 48 million euros for the acquisition of spectrum in the third quarter), mainly devoted to the expansion of the 4G network and the IP backbone, to the increase in the capacity of the 3G network and to the development and improvement of fixed networks (more selective expansion of pay TV).

Thus, **operating cash flow** (OIBDA-CapEx) totalled 1,576 million euros in 2016, +17.8% year-on-year (+26.2% excluding the non-recurrent impact of the fourth quarter of 2015).

TELEFÓNICA HISPANOAMÉRICA (year-on-year changes in organic terms)

In the fourth quarter of 2016, Telefónica Hispanoamérica posted solid operating and financial results, with double-digit year-on-year growth both in revenues and OIBDA. These results reflected the focus on value customers, services bundling and continued network improvement.

**Total accesses** increased to 135.9 million at December 2016 (+1% year on year).

TELEFÓNICA HISPANOAMÉRICA  
CONSOLIDATED INCOME STATEMENT  
Unaudited figures (Euros in millions)

	January - December		% Chg		October - December		% Chg	
	2016	2015	Reported	Organic	2016	2015	Reported	Organic
Revenues	12,579	14,387	(12.6)	7.5	3,435	3,622	(5.2)	10.9
Mobile Business	8,882	10,347	(14.2)	6.3	2,462	2,614	(5.8)	13.4
Mobile service revenues	7,918	9,161	(13.6)	7.0	2,156	2,309	(6.6)	12.0
Data revenues (1)	3,511	3,688	(4.8)	19.6	952	955	(0.2)	21.3
Handset revenues	953	1,188	(19.8)	(0.7)	304	306	(0.6)	22.7
Fixed Business	3,732	4,070	(8.3)	12.2	983	1,015	(3.2)	10.9
FBB and new services revenues (2)	2,003	2,064	(2.9)	21.6	535	521	2.7	20.4
Pay TV revenues	598	569	5.0	10.9	157	147	6.5	4.5
Voice & access revenues	1,131	1,436	(21.3)	(0.7)	290	346	(16.2)	(0.7)
Internal exp. capitalized in fixed assets	126	125	1.1	18.2	42	39	6.2	24.2
Operating expenses	(9,134)	(10,329)	(11.6)	8.8	(2,504)	(2,652)	(5.6)	7.9
Supplies	(3,704)	(4,176)	(11.3)	4.4	(991)	(1,060)	(6.5)	3.5
Personnel expenses	(1,584)	(1,686)	(6.1)	22.8	(482)	(445)	8.2	21.7
Other operating expenses	(3,847)	(4,466)	(13.9)	7.7	(1,032)	(1,147)	(10.0)	6.9
Other net income (expense)	103	72	43.8	63.8	28	23	22.7	45.6
Gain (loss) on sale of fixed assets	18	101	(82.3)	(93.5)	20	93	(78.3)	(90.3)
Impairment of goodwill and other assets (3)	(215)	-	-	-	(215)	-	-	-
Operating income before D&A (OIBDA)	3,477	4,356	(20.2)	3.9	805	1,124	(28.4)	11.5
OIBDA Margin	27.6%	30.3%	(2.6 p.p.)	(1.0 p.p.)	23.4%	31.0%	(7.6 p.p.)	0.2 p.p.
CapEx	2,613	3,060	(14.6)	6.5	815	857	(4.9)	8.1
Spectrum	284	338	(16.0)	(11.2)	2	(4)	c.s.	(23.3)
OpCF (OIBDA-CapEx)	864	1,296	(33.3)	(0.3)	(10)	267	c.s.	22.0

Notes:

- After considering Venezuela as an hyperinflationary country, P&L and CapEx from the operations in the country are to be accounted at the closing exchange rate Bolivar Fuerte/Euro. The January-December 2016 consolidated financial statements use the exchange rate of the Venezuelan bolivar set at the denominated DICOM (674 Venezuelan bolivars fuertes per dollar).

- OIBDA before management and brand fees.

- 2015 and 2016 reported figures include the hyperinflationary adjustments in Venezuela in both years.

(1) Since the first quarter 2015, data and voice revenues have been reassigned to homogenise the year-on-year comparison.

(2) Includes broadband connectivity services (retail and wholesale), including value added services, data and ICT revenues, other services over connectivity and FBB equipment.

(3) Includes goodwill impairments of 91 million euros in Mexico and 124 million euros in Venezuela in October-December 2016.

**Revenues** in the fourth quarter amounted to 3,435 million euros (12,579 million euros in the year) and accelerated year-on-year growth to 10.9% (+7.5% in the year) due to the improvement in both the fixed and the mobile business. Stripping out the impact of regulation, revenues would have increased by 11.8% year-on-year (+8.6% in the year).

Thus, **OIBDA** growth once again accelerated in the quarter to 11.5% (+3.9% in the year) and reached 805 million euros (3,477 million euros in the year). **OIBDA margin** stood at 23.4% in the quarter, impacted by restructuring costs (+0.2 percentage points year-on-year) and at 27.6% in the year (-1.0 percentage points year-on-year). Excluding the abovementioned factors (restructuring expenses, impairments of goodwill and capital gain), OIBDA would have reached 1,089 million euros in the quarter (3,761 million in the year).

In the year, **CapEx** totalled 2,613 million euros and grew 6.5% year-on-year and was devoted to the deployment and improvement both of mobile and fixed networks. The year-on-year growth excluded 284 million euros of spectrum acquisition in Peru in the third quarter of 2016 and 338 million euros in 2015

due to the acquisition spectrum in Argentina, Chile, Mexico and Ecuador. Thus, **operating cash flow** (OIBDA-CapEx) remained practically stable year-on-year (-0.3%).