



Telefónica January-September 2015 Results Conference Call Transcript

6th November, 2015

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Introduction

Pablo Eguirón - *Telefónica S.A. - Head of IR*

Good afternoon and welcome to Telefónica's conference call to discuss January-September 2015 results. I am Pablo Eguirón, Head of Investor Relations.

Before proceeding, let me mention that financial information contained in this document related to the first nine months of 2015 has been prepared under International Financial Reporting Standards as adopted by the European Union. This financial information is unaudited.

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Now let me turn the call over to our Chief Financial and Corporate Development Officer, Mr. Ángel Vilá, who will be leading this conference call.

Presentation

Highlights; Q3 fueling our organic growth profile

Ángel Vilá - *Telefónica S.A. - Chief Financial and Corporate Development Officer*

Thank you Pablo. Good afternoon and welcome to Telefónica's third quarter 2015 results conference call. Today with me is José María Álvarez-Pallete, Chief Operating Officer, and during the Q&A session you will have the opportunity to address us with any questions you may have.

Telefónica has achieved its third consecutive quarter of improving organic growth in 2015, firmly placing the Company in the new cycle of profitable growth initiated at the start of the year. We would like to highlight, in particular, that Spain returned to positive revenue growth this quarter, for the first time since 2008.

Both revenues and OIBDA accelerated in Q3 their organic growth to close to 5%, with the latter proving that we are successfully delivering on synergies in Germany and on cost efficiencies. Margin was stable throughout the year at 31% and was flat year-on-year organically. Operating Cash Flow returned to positive growth.

Our consistent investments in UBB led to a differential infrastructure, translating into innovative and quality commercial propositions and allowing to increase customer value, by improving year-on-year growth in average revenue per access and reducing churn.

Despite adverse currency impacts in Q3, which we will cover in further detail later on, we have achieved sequential improvement in FCF ex-spectrum to €2.5 billion up to

September, combined with a strong EPS increase of 63.5% year-on-year and a reduction in our post-UK sale leverage ratio to 2.32x.

Finally, we are pleased to reaffirm that we are fully on course to meet our guidance, which we upgraded in the previous quarter and dividend per share for both 2015 and 2016 are confirmed.

Key financials

Moving to slide 3, let me sum up our key financials, which have been very sound despite the currency turmoil in Q3. The negative impacts of FX at OIBDA level did not leak through into free cash flow as they were offset by lower CapEx, tax, interest and minorities payments both in the cumulative period to September and in the last three months.

Overall, the third quarter saw steady top line and OIBDA year-on-year growth, both in reported and in organic terms.

Net debt declined €1.5 billion in the quarter to €49.7 billion, principally due to cash flow generation and the lower value in euros of net debt in foreign currencies.

Full year guidance confirmed; on track to meet targets

As I said before, we are reiterating our outlook for 2015 and we are fully aligned in the nine months to fulfil this.

Under guidance criteria, revenue growth was 13.8%, comfortably exceeding the guidance of higher than 9.5%. OIBDA margin erosion stood at 1.3 percentage points, in line with target of around 1.2 p.p. and CapEx to Sales of 15.6% is also in line with around 17% at year end.

Leverage considering O2 UK sale is within guidance.

In terms of shareholder remuneration, we will pay in the coming weeks 35 euro cents per share in voluntary scrip dividend as the first tranche of the 75 cents corresponding to 2015. The second tranche will be paid in cash in the second quarter of 2016.

Strong FCF in Q3, to accelerate further in Q4

Turning to slide 5, FCF generation was robust in the first nine months to September, reaching €1.2 billion, or €2.5 billion before spectrum payments, and absorbing the already mentioned FX impact.

I would like to highlight the sequential FCF improvement in the quarter of €2 billion to €1.4 billion, leading to a solid year-on-year growth of 3.6% based on improvement in most of FCF metrics.

Let me remind you that YTD FCF is impacted by seasonal effects, and thus FCF should record a better performance in the fourth quarter.

Finally, EPS stood at €0.91 in January-September, up 63.5% year-on-year.

Organic growth and perimeter outweighing Q3 FX impact

Moving to slide 6, we can see how organic performance and perimeter changes have outweighed the FX fluctuation in Q3, leading to very solid revenue and OIBDA year-on-year reported growth of 10.8% and 2.9%, respectively.

The consolidation of E+, GVT and DTS had a positive impact in the quarter, jointly contributing 13.5 and 7.2 percentage points respectively to revenue and OIBDA reported year-on-year changes.

In addition, organic trends accelerated again in the quarter to explain the 5.4 percentage points of reported revenue growth and 5.1 percentage points of OIBDA's.

On the other hand, the depreciation of LatAm currencies in general, and in particular BRL and COP, dragged in Q3 around 8 percentage points in year-on-year revenue and OIBDA variation.

Revenue & OIBDA continue to accelerate

On slide 7, we highlight how organic revenue growth continues to perform attractively, ramping-up 40 basis points vs. the second quarter and with Spain demonstrating a strong progress of 130 basis points, reaching a positive year-on-year variation. In addition, T. Hispanoamérica posted a sequential acceleration of 220 basis points and reached 12.6% year-on-year growth.

Let me also highlight the impressive evolution of data revenues, up 19.3% vs. Q3 14 organically, and the increasing contribution of Digital services.

In addition, organic OIBDA growth ramped-up 140 basis points sequentially to 4.8%, boosted by the stellar performance of Germany and, in spite of adverse macro, by Brazil. Margin has remained flat throughout the year at 31% level, driven by stronger efficiency, synergies and simplification efforts reflected in the stable organic variation..

Attracting more customers and with higher value

Let me now turn to slide 8 to explain how our drive to increase quality rather than quantity in our customer base is paying off.

Overall organic accesses are slightly up, but in higher value services our performance has rocketed. As such, we added over 5 million LTE customers, more than quadrupling our base year-on-year, driving further adoption of smartphones, which were up 28% year-on-year.

Fibre connected and Pay TV net adds also continued to grow robustly on a sequential basis, putting us in a strong position to capture further growth opportunities and increasing their base vs. last year 36% and 18% respectively, in organic terms.

As a reflection of this, the growth in average revenue per access accelerated in the quarter to 2.8% year-on-year organic which, coupled with the decline of 0.7 p.p. in churn levels, demonstrate the increased value and sustainability of the model.

Data monetisation contributing to revenue acceleration

Data monetisation continued to contribute to revenue acceleration as you can see in slide number 9.

Booming smartphone penetration and data volume growth are the key levers for data monetisation. We are constantly developing initiatives to further monetise usage, launching data offers centred around integrated packages and new roaming commercial propositions.

In parallel, data traffic is boosted by increasing average smartphone usage, 21% higher year-on-year in Q3, and LTE usage, 63% more than 3G. Also, there is a unique opportunity to further incentivise data traffic as prepay smartphone penetration in Hispanoamérica is at just 27% vs. Brazil at 47%.

The benefits of smartphone penetration expansion and LTE adoption are clear and are delivering significant ARPU accretion:

- We are seeing double digit LTE ARPU uplift
- Data adoption is having a very positive impact on ARPU in Hispanoamérica and Brazil, with a significant prepay ARPU uplift of each new data customer
- And SMS drag is easing rapidly as can be seen in the acceleration of total data revenues, which already represent 44% of MSR.

Lastly, I would like to note that almost 30% of customers are using up their data allowance, of which 44% buy an extra data product.

Digital services: developing a platform for growth

To review our progress in Digital Services, please turn to slide 10.

Q3 has been a milestone quarter for digital services as we surpassed the 1 billion euro mark in quarterly revenues, largely due to the solid organic performance of our video segment with e652 million (25.6% higher than Q3 14). This positive evolution is built on our increasing content portfolio and improved technology, most notably in Brazil and Spain.

In other areas we continue to foster key partnerships to deliver enhanced solutions to our customers. In Cloud we have reached agreements with China Unicom and Equinix to expand our global data centre footprint, offering a truly international solution for multinational companies. We have also partnered with Microsoft to bring cloud migration to our SME customers.

In Security, we recently acquired Gesdatos, the leading platform in Spain for the management of data, now integrated into our international commercial offer. We also launched FiLIP in Spain, the first smartwatch for children which allows parents to monitor their children's safety.

Lastly, we are proud to once again be named global "Leaders" in M2M in Gartner's Magic Quadrant.

TGR: Towards all-IP network; Further IT simplification

TGR is the enabler of our progress by strengthening the networks and simplifying operations. In the third quarter TGR continued with the rapid rollout of fibre and LTE, key tools to capture value growth. As of September, 13.4 million premises were passed with

fibre in Spain and 16.6 million in Brazil, we had more than 30k LTE sites while 96% of 3G and/or 4G mobile sites are connected with UBB technology.

Additionally, we continued to progress on the deployment of All-IP, Network innovation and Best in class operations.

A key step towards IT transformation in the quarter includes the expansion of Full Stack, now in 15 countries. Lastly, we continued advancing on decommissioning applications, reducing physical servers, consolidating data centre services and virtualisation of IT.

Spain: Strong trading and increasing value

On slide 12 we summarise Telefónica España's trading performance.

Launched in July, our new convergent offer "Fusion+", enhanced with Digital+ content, drove an outstanding commercial turnaround in quarterly net adds across services on the back of strong gross adds and curtailed churn levels. All this was achieved despite summer seasonality and the removal of lock-in clauses since August.

"Fusion+" continues to fuel the growth in high-value services, such as fibre and pay TV, improving customer mix and driving Fusion ARPU up to €75.5, an 8.4% increase year-on-year and 5.1% increase quarter-on-quarter.

In addition, we launched a campaign for the high-end TV product in mid-August, with access to all premium content at a promotional price until the end of the year. By the end of September, almost half a million customers had subscribed to it, which increased the weight of customers with TV add-ons over the total Pay TV base to 36%, 8 p.p. more than in June.

Let me remark that commercial strength has been achieved despite not having the Champions League rights, which reflects a rational policy in content costs acquisition.

Our differential assets, namely UBB networks, continue their roll out to secure our leadership in value.

Spain: Return to revenue growth

Continuing with Spain on slide 13, revenues returned to growth (+0.2% year-on-year), for the first time since Q3 2008. Amid a more favourable environment, top line reflects a new revenue cycle underpinned by consistent customers base growth, higher value in the base, price repositioning and wholesale revenue.

Quarterly margin remained robust at 44.5%, although higher OIBDA year-on-year erosion than in Q2 in organic terms was mostly impacted by increased content costs as well as by higher equipment and network expenses.

Importantly, let me comment on the effort we are making to increase the reach of pay TV in Spain, a service that up to now has not been a mass product. With this purpose in mind we have launched an aggressive promotion while absorbing all the costs and this is obviously increasing margin pressure. However, once the discounted prices' impact dissipates we expect higher revenue flow-through to OIBDA.

And moreover, we will continue working on efficiency measures in the following quarters.

Germany: Maintaining market momentum

To review Telefónica Deutschland, please turn to slide 14.

We posted very solid momentum in the third quarter, with strong contract net adds leveraged on strong dynamism of partners. The Company enhanced its value offering, strengthening its O2 premium brand and revamping the value brand Blau.

Additionally, LTE continued to make progress, reaching a penetration of 16% and demonstrating that there is strong demand for data in the market. Within our O2 Blue All-in customer base, 37% of new clients took a tariff above 1 Gb and 54% of opted-in customers had at least 1 automatic data extension.

As a result, mobile data monetisation continued to flow through to mobile service revenue, but decelerated in the quarter mainly due to the increased contribution from partners. In addition, year-on-year growth of handset sales was lower sequentially affecting quarter-on-quarter revenue trends.

Germany: Early synergy capture boosting profitability

Telefónica Deutschland has posted very strong profitability and an improved outlook.

Early realisation of synergies after achieving important milestones, along with sustained commercial savings translated into further OIBDA acceleration to 28.5% in the third quarter, with integration savings explaining more than 45% of this improvement.

This, together with CapEx efficiencies, as network synergies outweighed the cost of LTE deployment, resulted in outstanding organic OpCF growth of 45% year-on-year, in the first nine months of this year.

On the back of this strong performance the Company updated yesterday its 2015 outlook, announcing more ambitious targets and proposed a 2015 dividend of €0.24 per share, stable vs. last year.

Brazil: Outperforming in high-value services

For a review of the performance of Telefónica Brazil, turn to slide 16.

As shown by our commercial and economic performance, we are outperforming the market once again this quarter, leveraging on our differential position in value services.

In the mobile business, contract gross adds reached highest-ever quarterly volumes, while smartphones and LTE adoption continued to accelerate, driving data ARPU to ramp-up year-on-year to 33%. This is reflected in the fact that Vivo is capturing all the market growth in service revenues year-to-date.

Regarding value services in the fixed business, T. Brasil attracted 100% of new Pay TV customers in the market and more than half of all high-speed broadband net adds up to August. As such, the Company's transformation towards a video and fibre company is improving ARPU and churn trends.

Brazil: Robust revenue & OIBDA growth

Telefónica Brasil's financial performance on slide 17 shows how growth in higher value customers is flowing into the P&L.

Thus, revenues sustained a robust year-on-year growth of 5.2%, based on booming mobile data and fixed business improvement. The latter is leveraged on the business in Sao Paulo that returned to positive year-on-year growth in Q3.

In addition, costs remained controlled, driving OIBDA growth acceleration to 2% year-on-year, maintaining profitability roughly stable year-on-year despite a tougher macro environment.

Hispam: Commercial momentum driving revenue acceleration

On slide 18, we review our performance in Hispanoamerica, where commercial momentum is driving a solid organic revenue acceleration.

The strong trading in mobile contract resulted in almost half a million net adds in the quarter, quadrupling year-on-year, while, at the same time, the growing adoption of bundled services in the fixed business led to solid fixed broadband and Pay TV net adds.

Strong commercial activity resulted, on the one hand, in top line growth, with year-on-year rates ramping-up to more than 12%, or 9% excluding Venezuela, while on the other hand, it was the main driver behind the 2 percentage points decline in profitability this quarter.

Mexico: Increasing scale & profitability

In Mexico, as shown on slide 19, we are gradually increasing both our scale and profitability.

Thus, the continued strong commercial activity is reflected in outstanding contract performance and is driving year-on-year accesses growth to 14% and smartphones to 87%. It is also the main driver behind the sustained double digit top line year-on-year growth, which in the third quarter reached 17.9% year-on-year.

At the same time, the ongoing profitability expansion is also remarkable this quarter, almost reaching the 30% mark, 4 percentage points more than one year ago.

Rest of Hispam: Capturing market value

In the rest of Hispanoamerica, as we show on slide number 20, we are also capturing market value with better commercial traction, with especially remarkable performances in Argentina, Colombia, Chile and Peru.

This has translated into consistent regional market outperformance in revenue growth and it is also the main driver behind the deceleration in OIBDA year-on-year growth.

UK: Continue outperforming the market

Turning now to slide 21, Telefónica UK posted strong customer growth for the sixth quarter in a row, outperforming the market, with total mobile customer base reaching 25 million at the end of September. Quarterly net adds were consistent and strong vs. prior quarters, with record market-leading contract churn at 0.9%.

LTE continued to gain traction, reaching a penetration of 30%, with increasing demand for higher subscription bundles as now more than 65% of new adds and upgrades are opting for tariffs of 1GB or more.

As a result, mobile service revenues performance continued to improve for the twelfth consecutive quarter and grew 4.2% year-on-year, excluding the impact of "O2 Refresh".

OIBDA margin surpassed 26% and expanded 1.7 p.p. year-on-year, excluding a non-recurrent impact of €34 million in the third quarter last year, thanks to the optimisation of commercial costs at 2.38x and would stand at 2.35x in the absence of the M&A deals closed in Q2.

€1.5bn net debt reduction in Q3 15

Let me now move to the financial slides starting on slide 22.

In Q3 debt has been reduced by €1.5 billion to €49.7 billion, mainly driven by:

- €1.4 billion FCF
- €1.2 billion savings in Latam debt when translated into euros due to FX depreciation

Leverage has been brought down to 2.84 times OIBDA, while it would be at 2.32 times post UK sale.

We expect to continue progressing on leverage improvement on:

- First, positive free cash-flow generation in Q4 15
- Second, growing OIBDA on an organic basis and also benefitting from the acquisition of E-Plus and GVT
- And third, closing O2 UK divestment in 2016

Progressive improvement in financial costs

Moving to slide 23, I would like to highlight that our effective interest cost is 54 basis points lower than in the same period of 2014. We have continued to benefit from the euribor rate reduction. This improvement was enabled by an intentionally decreased fixed rate debt in euros and lower refinancing costs, leading to 61 basis points savings, partially mitigated by higher debt in Latin American currencies, allowing for a reduction in the financial cost to 4.91%.

We have improved our robust liquidity position to exceed €16 billion, covering our maturities beyond 2016. We have continued with our proactive financing activity, and thus we have already raised over €13 billion of long term funding by tapping diversified sources of financing.

Summary

To recap,

We have presented today a very solid set of results that reinforce our profitable growth profile and strengthen our position to capture future growth.

We continue to demonstrate an improving organic performance across all metrics, driven by market momentum on value services.

We are obtaining encouraging results from integration activities in Germany, with Brazil to follow in the coming quarters.

We are delivering network quality upgrades based on our superior infrastructure, which allows us to respond to data traffic growth when demand is rocketing.

We are leaders in major markets with a superior competitive position backed by strong investments.

And we are fully delivering on commitments for this year and also confirming the shareholder remuneration policy in place for 2015 and 2016.

Thank you very much for your attention. We are now ready to take your questions.

Q&A session**Nick Brown - Goldman Sachs**

Thanks. Firstly EBITDA margins in Spain have been flat at about 44.5% for last three quarters. Should we expect that to fall in Q4 with the full quarter of La Liga costs and should we then expect EBITDA to grow from the first quarter of 2016 once the Fusión Premium TV commercials you mentioned roll off in January? And secondly, can you remind me, are all the revenues in EBITDA from Digital+ TV customers being reported in other eliminations or are you now reporting the content cost in the Spanish business without all of the revenues? Thank you.

José María Álvarez-Pallete - Telefónica S.A. - Chief Operating Officer

First on the OIBDA of Spain a few messages, the first message is that content cost is here to stay and therefore you have now an idea of a full quarter of the costs of having the most complete TV offering in Spain which has been the reason behind a very, very strong commercial momentum namely on the pay TV market. We have proven that we are rational because we have been able to do so with limited inflation on some of the existing costs like La Liga but not having others like the European Champions because of too high costs. And that's why the impact on margins in Telefónica España this quarter has been reflected by having the full amount of the content cost and just probably a month and a half of activity I would say.

On the upside, buffers that we have for the future, namely promotions, remember that we are having that impact of content, we have a promoted price of €9.90 on the package, promotion will be progressively expiring during the first quarter of 2016. We have roughly 600,000 customers on that promotion that would move upwards on that along that period and that will have any impact on OIBDA. Also pay TV penetration in Spain is one of the lowest in Europe, we are now in 29%. It used to be 22% just two years ago, so we have been gaining seven percentage points of pay TV penetration in just two years and that's why we are investing on the market.

And then also remind you that we keep doing extra efforts on the other part of the cost function of Telefónica España (distribution and others), so you should expect us to keep going into the direction of preserving efficiency in Spain. We don't guide on specific margins going on. You have an idea of what's the impact of content but also remember that this quarter's OIBDA is impacted by the promotion that would be expiring on the next year and that the extra customer base that we are capturing should also start to pay back during that period. So that's what I can tell you in terms of the margin in Spain.

In terms of how the integration of Telefónica España and DTS has worked this quarter, first of all, in terms of the internal wholesale revenues, they are part of the wholesale revenues that are reflected on DTS accounts, and that's basically applied for the football rights, the football La Liga rights based on Digital+, on the former DTS; while other sports like the MotoGP or the Formula 1 are accounted into the wholesale revenues of Telefónica España. Those revenues or those trends will be consolidated and we will try to give you full colour of both units being consolidated probably starting next quarter in order to avoid confusion on where each of the cost components is relying.

So as a result they are part of the internal wholesale revenues namely on the La Liga rights that are accounted on the DTS accounts, and a minor part of the sports rights, namely Formula 1 and MotoGP that are on the wholesale revenue of Telefónica España.

Georgios Ierodiconou - Citi

Good afternoon, I have two questions please, the first one on Spain. You mentioned earlier the 600,000 subscribers that could move out from the current promotion in January. Could you give us an indication of what kind of ARPU uplift you would expect given that profile?

Basically, what I'm trying to understand, if I'm not mistaken, last January you raised prices in mobile. Later in May you raised prices in Fusion. Do you think there will be enough inflation on TV and other areas this year to make up for annualizing some of these benefits in 2016?

My second question is on two of your Hispanoamerican assets, Colombia and Mexico. The first one, Colombia, you seem to be underperforming Tigo quite materially and I know there is an impact. Even if I adjust for that, there is quite a big gap. Is that because you responded late to the América Móvil price cut? Is this something that lasts for a while or would it be fixed relatively quickly?

And similarly, in Mexico you have a big tailwind right now. You seem to be benefiting a lot on the margin, but will you balance it a bit more in the future since you will be more commercially active? Any indications around your strategy in Mexico? Thank you.

José María Álvarez-Pallete - Telefónica S.A. - Chief Operating Officer

Thanks for your questions. On the customers that are currently under the promotion of €9.9 in Spain and the potential uplift, yes, we have an idea of what could be the movement upwards, but as you might imagine, we do not share that because it's commercially very sensitive.

They are enjoying our product of nominally €65 for €9.9. Most of them, or parts of them, were coming from the basic product, so we are analysing the customer base and we are preparing the offer that we will put to them in the different add-ons (series, sports, and others) in order to make sure that they move upwards on the value chain once this promotion is expiring. So, yes, we are anticipating uplift, significant uplift, but we are not sharing how much because we are specifically analysing those layers of customers and preparing that offer from whenever the promotion will be expiring.

On the price movements in Spain, we like to talk about upselling. We have upselling our customers. We have been giving more value for a little bit more money. The average price per megabyte or per gigabyte has been decreasing and, therefore, we are giving more value for a little bit more money.

We have been executing that consistently during this year. We started in January for the 1P product and we did the deep move in April on the Fusion product. And that's why Fusion ARPU year-on-year has been moving upwards 8%, which proves that we are able to make a value proposition for our customers that allow them to enjoy more value for a better ARPU.

And you need to score that into a situation in which we have been suffering an installation strike on the subcontractors, and we have been able to move back on the commercial side and to post a quarter of very, very solid commercial momentum. So, that proves that we can move upwards ARPU, by proposing more value for a little bit more price, and I think that that's a trend that we would like to continue going forward.

Remember, finally, that if you benchmark the commercial performance of this quarter, even considering that we have August and therefore seasonality, in the meantime, and you benchmark the absolute amount of net adds that we have been gaining all across the board with the first quarter of this year you will see that we have not only been regaining momentum, but we have been beating our first quarter performance. So, commercially speaking, very strong performance and we think that we can keep having both things at the same time: expanding our customer base and moving upwards the value proposition for our customers.

In terms of Colombia, this is probably a quarter in which we are regaining market momentum. We thought that the market would be more rational, but subsidies have been back into the market, namely because of the third player. And, therefore, we have been waiting for two quarters to see if the market was becoming more rational. It didn't, so we went back to commercial aggressiveness and we have been regaining market momentum. Of course, that has been affecting OIBDA, but our commercial effort, jointly with the fact that we keep investing significantly in our networks, allow us to think that going forward we have better trends, namely in terms of revenues.

Finally, on Mexico, it is true that for the first time in 10 years we have regulation, namely on interconnection asymmetry, supporting our efforts, but it is also true that the asymmetry of interconnection is lower this quarter than in the previous quarter because interconnection rate has been decreasing from MXN0.31 to something between MXN0.23 and MXN0.24. And, therefore, this impact is being slightly or progressively diluted.

The reason behind our strong momentum in Mexico is commercial. We have been successful on the prepaid for a sustainable time, but this quarter for the first time we have been successful, or more successful I would say, on the postpaid part of the market. And that's very encouraging.

It has a lot to do with the expansion of LTE that we are doing and the 3G improving coverage that we are also doing on the market. Therefore, the fact that we are reinvesting in terms of CapEx a significant part of the cash flow that we are generating commercially and thanks to the asymmetry.

So pretty enthusiastic, pretty positive about the future of our Mexican asset, much better trends. And not just relying on prepaid, this quarter is one of the first quarters in which we are more satisfied about our postpaid trends in Mexico.

David Wright - *BofAML*

Thank you for taking the call. Jose María, if I could just ask for a little more clarity on the cost allocation in Spain. You have taken wholesale revenues in DTS, but you've taken all of the cost in Telefónica España; is that correct? So when you do then consolidate DTS, we should assume some EBITDA growth recovery just on the natural sort of revenue uplift? That's question one.

And then my question two. When you say a full quarter of costs in Q3, but only marginal sort of revenue uplift from the football promotions? Is that correct? So we have taken effectively the La Liga cost, divided by four; for full quarter we'd put that in, but then we've only got revenues for sort of 1.5 months. I'm just trying to understand the exact cost allocation, thanks.

José María Álvarez-Pallete - *Telefónica S.A. - Chief Operating Officer*

Thanks for your question. Let me try to be a little bit more specific on the wholesale revenues.

The La Liga cost that is in the neighbourhood of close to €600 million, the owner of those rights is DTS and, therefore, this is not consolidated into Telefónica España. And, therefore, DTS is billing Telefónica España for the proportional part of the billing rights for their customer base and for their market share.

The other revenues coming from La Liga rights, wholesale revenues that are going to the third parties depending on the market share, those are also billed by DTS to Telefónica España.

Therefore, summarizing in terms of La Liga, using La Liga as an example: you have in Telefónica España the cost of their proportional part of the La Liga cost and the revenues coming from customers and third parties.

You will have, when we will be consolidating DTS revenues into Telefónica España revenues, its retail revenues accreting into Telefónica España revenues.

And then in terms of the cost, the La Liga rights are divided into the different quarters and therefore allocated. Remember that a significant part of the gross amount of the La Liga rights is passed through to the other players that want to have access to this premium content, namely Vodafone, Orange, and others. Therefore, you need to consider when running your numbers that close to 30% of that amount is flowing into the wholesale market to third parties and, therefore, not into the Telefónica's account.

David Wright - *BofAML*

Okay, that's much clearer. Obviously there is an assumption that the ARPU can uplift beyond the promotional period at the beginning of next year, but you are also seeing quite strong promotions from your competitors right now. So are you confident that you will see a sort of a wider market reaction, or is there a risk that your competitors also with some Champions League football might continue to push?

José María Álvarez-Pallete - *Telefónica S.A. - Chief Operating Officer*

The market is very competitive, but it has been very, very competitive, not just on the content part, but also on the pure 3P before TV for the last two years. And we have been able to move upwards our customers because we have significant, I would say, differential assets, namely our coverage, our fibre coverage.

Now, with the DTS incorporation, we have a satellite platform that is covering 100% of the Spanish territory and, therefore, we are also able to sell a bundled product to the regions of Spain in which we don't have coverage of fibre or VDSL. Then on top of that I think that you also need to score that we are doing cross-selling on the different customer base of the former DTS base with Telefónica's products.

And then I would also like to mention one specific issue, which is that 56% of our pay TV base is now with some kind of add-ons, which basically means that the value proposition that we are doing and the segmentation that we are doing at the market with the different layers of products on the TV side is gaining traction.

Therefore, and finally, let me add, in terms of the advantages that we think we have, is that on top of the network, in terms of the contents we also have, in terms of the technological features that we have been able to embed in our platform: TV on demand,

cloud storage, and more than 74 high-definition channels. So, I think that we have enough strength in our value proposition in our product, to allow us to think that we can uplift our customer base going forward.

A final point that I would like to mention. The over-the-top platform that we have been incorporating from Digital+ allow us to have, in just one quarter, more than 500,000 customers in Telefónica España that have now downloaded . And more than 70% of those are recurrently using the app. So I think that overall, when you put everything into consideration and you can see that also the strength of our fibre and the strength of our network, I think that we should be able to uplift our customers going forward.

David Wright - *BofAML*

And DTS is fully consolidate Q4, is that correct?

José María Álvarez-Pallete - *Telefónica S.A. - Chief Operating Officer*

We will do our best; we will be consolidating into Telefónica España so we avoid confusion going forward.

Jonathan Dann - *RBC*

Two questions please. One is looking at some of the listed subsidiaries, of some various I'm thinking Brazil and Germany, with tax changes in Brazil and I guess the pace of improvement in Germany, is there a moment to improve the capital structure, either less equity or more debt?

And then completely separately, are you looking at unbundling in Mexico?

Ángel Vilá - *Telefónica S.A. - Chief Financial and Corporate Development Officer*

Hi Jonathan, this is Ángel. Regarding the first question, we have a group-wide approach to the capital structure, which allows us to comply with our overall leverage commitments group-wide and also with some other criteria, like what amount of debt push-down we can have to subsidiaries, regarding to debt subordination issues and some other considerations that, for instance, rating agencies would be looking at. Also, we are managing taking into account the different commitments taken to the market. In the case of Telefónica Deutschland, at the time of the IPO in the prospectus there was some commitment to leverage that we have been complying with. And also, regarding our other major listed subsidiary, which is Brazil, we're continuously monitoring market conditions, cost of debt, the macroeconomic situation of the country, to optimise from a group perspective what the financial costs would be. This is a dynamic, obviously, exercise that we are continuously assessing and there could be variations over time. But, we feel that we are in a good position now.

José María Álvarez-Pallete - *Telefónica S.A. - Chief Operating Officer*

Taking your question about Mexico, we are analysing access to Telcel's infrastructure on the mobile side, because the current regulatory framework has forced the incumbent to prepare a wholesale offer by having indirect access to their passive network infrastructure, and therefore on towers, on the Telesites and others, yes we're analysing, not on the wireline side. We need to make sure that we have fixed our situation on the mobile side, namely that our prepay traction is in good shape, that our postpay traction keeps improving, which was a pending issue until this quarter. So, before considering any other movement, we're totally focused on our mobile business in Mexico in order to try to

accelerate our CapEx deployment and to make them as efficient as possible by having access, if possible and at reasonable prices, to indirect infrastructure of the incumbent in Mexico. So, not on the wireline side. Yes, we are analysing options on the wireless side.

Mathieu Robilliard - *Barclays*

Two questions, please. First, with regards to the process of the sale of Telefónica UK: if you can maybe give us a bit of colour in terms of how your conversations are progressing and what is the timetable. Should we still expect something to be closed by Q2 next year?

And then coming back to Mexico actually, obviously one of the new entrants there is planning to spend quite a bit of CapEx over the next few years; much more than what your current run rate suggests. Do you think that at some point you will have to ramp up CapEx there to catch up with that or you think you already have a head start in Mexico compared to the new entrant? Thank you.

Ángel Vilá - *Telefónica S.A. - Chief Financial and Corporate Development Officer*

Regarding the O2 UK approval process, as you know this process is being led by Hutchison and we are supporting them and participating in the meetings with the European Union. What they call the Form C was filed on September 11th, as expected. On October 30th, the Commission moved the file to Phase 2 - this was, I want to insist expected - and did not refer the file to the UK CMA.

There was an initial deadline set by the Commission on March 16th. This can be extended at the request of the Commission or voluntarily by a request from Hutchison. I want to stress that there is an ongoing constructive and continuous dialogue with the competition authorities. Our base case scenario continues to be that the deal gets approved with remedies. Regarding timing, we expect the deal to close in the second quarter of 2016, provided that the European Union does not significantly stop the clock. So, we remain optimistic and confident in the success of the deal.

Mathieu Robilliard - *Barclays*

Can you just confirm if there is a break-up fee in this deal?

Ángel Vilá - *Telefónica S.A. - Chief Financial and Corporate Development Officer*

The documentation is confidential, but I would assume that if there was a significant break-up fee we would have had to disclose it.

José María Álvarez-Pallete - *Telefónica S.A. - Chief Operating Officer*

Taking your question on Mexico; yes, as you might imagine, we have been monitoring very closely announcements from the brand-new competitor in the Mexican market about their future CapEx intentions and we have scored that in our model. Let me remind you that we have invested more than €10 billion of CapEx in Mexico in the last years.

Thanks to that, we have the second-best network after Telcel. And that's precisely why the other previous two contenders, namely Iusacell and Nextel, had national roaming agreements in our network and they were relying mostly on our network for a significant part. So, we can easily understand that AT&T would like to have their own network. And therefore they will need to catch up significantly in the next quarters, because they will need to basically build a significant part of the network which we have already done.

Having said that, we are accelerating CapEx in Mexico, because we think that the growth opportunity that lies ahead of us, we need to take advantage and therefore we cannot miss the opportunity. But, we are not in the need of precisely matching what AT&T is going to do. At the same time, we are analysing, as I was saying previously, any option that would help us or would facilitate the way to do that in a more efficient manner by having access to sites, if those were to be at reasonable pricing compared to deploying our own network. So, to make a long story short, we feel that we have a good base on our network. We also feel that we need to accelerate, because there is a huge opportunity ahead of us and the time is now because of the asymmetry of the regulation. We don't feel at such a disadvantage like AT&T might be feeling, but yes, we are accelerating. And we have not changed our CapEx because of the announcement done by AT&T.

Mathieu Robilliard - *Barclays*

If I may ask, is the project of the government around the 700 MHz spectrum part of the options you're considering, or that's a no-go for you?

José María Álvarez-Pallete - *Telefónica S.A. - Chief Operating Officer*

It's not one of the most attractive projects that we are analysing, but we are keeping everything on top of the table. We are analysing other projects with a better return.

Keval Khuroya - *Deutsche Bank*

Thank you, I've got two questions please. Firstly on Spain, at the start of the year you laid out an ambition to grow revenues in Spain on a cumulative basis in 2015. In the first nine months the Spanish revenues are down 1.5%. Do you think in Q4 we will see growth to allow you to reach flat or growing revenues for the full year; and if not what's gone worse than what you expected at the start of the year?

Then secondly on Brazil you have been doing a great job at outperforming the market, but do you think the current wireless growth rate is sustainable as we look to 2016? Do you expect any further impact from the weak macro environment and how do you feel about the recent competitive moves from TIM Brazil in particular? Thank you.

José María Álvarez-Pallete - *Telefónica S.A. - Chief Operating Officer*

Taking your question on Spain, we already discussed in previous calls that it was not a guidance. Having said that, we have been already having five months of growth in Spain and we think that the performance that we see in this quarter is going also into that direction, whether that's going to be enough to match or to surpass the previous year revenues is still to be seen, but again that's not a guidance and therefore we will keep working into that direction. Allow me to remind you that again we have already had five months in a row of growth in Spain.

Things that were unexpected that you were mentioning, first, the approval process of Digital+ took two months longer than we expected initially; second the subcontractor strike was not scored into the model at the beginning of the year and that had an impact on the second quarter and adds that is also affecting the performance, so we'll keep you posted, but allow me just to highlight that we have already had five months in a row of revenue growth in Spain.

In terms of Brazil, macro, it's affecting the business in terms of bad debt namely and therefore it is true that we have had a significant impact in terms of bad debt that is starting to be controlled and that's why we have been significantly upgrading our credit

scores for new adds. In spite of that we have been able to maintain the growth rate almost stable compared with the second quarter in terms of revenue growth and we have been able to accelerate in terms of OIBDA performance.

Thanks to the fact that we have been basically grabbing more than 50% of the contract net adds of the market, that we have been able to capture mostly 100% of the mobile service revenue growth of the market; and also because of the fact that we have been able to grab 100% of the pay TV net adds on the quarter which means that the products that we have in Brazil are very strong in these circumstances and that we are replacing the growth that is not coming from the macro environment, with market share we are grabbing from our competitors.

So, a very strong quarter commercially speaking in Brazil and even without the bulk of the synergies yet flowing through our accounts, remember that we are starting to see significant traction in terms of synergies in Germany, four quarters after the approval process, we are just one quarter after the approval process in Brazil, so pretty confident on the future of our Brazilian subsidiary.

Very satisfied by the commercial results especially if you take into consideration the fact that we were just in the middle of the integration process of both teams and therefore rather than losing focus on the market we have been able to accelerate our market aggressiveness and therefore capturing a significant part of the value of the market in the quarter.

So yes, the macro is affecting us in bad debt, in the cost of energy and in other supplies.

In spite of that we have been able to accelerate the OIBDA growth because of the first signs of the synergies. We have been able to preserve revenue generation, revenue growth compared with the previous quarter because we have been grabbing most of the value of the market in this quarter, so very satisfied with the performance of the Brazilian unit during this quarter.

Justin Funnell - *Credit Suisse*

Thank you, two quick questions. On Spain and fibre, the competitive dynamics, I think Orange announced couple of days ago they were going to extend their footprint; it's obviously going to take them time to do that. So I was just wondering what's going on, when you're competing against Orange and I guess what Vodafone built in fibre, when you are going head to head with them what sort of market share you get? I presume it's pretty high, but any visibility on that would be useful?

Then just generally, obviously going into this LatAm down cycle, you're relatively exposed as a group. Has it led to any new thinking about how you want to be exposed long term? Is there an argument to pivot back to Europe at some point? Thank you.

José María Álvarez-Pallete - *Telefónica S.A.* - *Chief Operating Officer*

Taking your question on our competitors' expansion in terms of coverage on fibre in Spain, yes, Orange announced this week that it looks like they have announced that they will be expanding their coverage from 10 million to 14 million from here until 2020.

We have already almost 14 million premises passed in Spain, and if the regulatory environment stays stable to go significantly above that level in the next year. So coverage is one of the factors that we are using in order to accelerate our value proposition in Spain, we take into account what they are doing but we are significantly ahead of them.

So allow me to say also that coverage is one of the elements but not the only one, the content is essential and we think we have the best overall content in the Spanish market. In spite of not having the European Champions League, we have a very good and very competitive product in terms of series, a very outstanding product in terms of movies, an outstanding product in terms of other sports and in terms of football rights; and we have also platform that is providing features that are hard to match by the others like video on demand, VDR, cloud storage, last seven days of programming, high definition channels.

So, it is hard for them to compete with us because we have a very good product and a very good bundle. So we acknowledge we were already accelerating and I think it is the right approach, competition based infrastructure is the right approach for fibre and I think that's precisely why Spain in the middle of the crisis has passed on being the sixth country Europe in terms of fibre customers, I'm not talking about relative or a percentage; I'm talking of absolute number of fibre connected homes from being the sixth in 2011 to being the leader in 2015. So I think this is the way to go, the more competition, infrastructure based competition, the better for the country, so we deeply encourage that.

Ángel Vilá - *Telefónica S.A. - Chief Financial and Corporate Development Officer*

Regarding the second question on geographical diversification, what I would like to point out is that if you look at metrics like free cash flow or SOTP value, we remain a European-centric company and given the high expected growth in OIBDA and operating cash flow that we will achieve in Germany, this will probably continue to be so.

So in our cash and value metrics, we continue to be a European centric company.

Giovanni Montalti - *UBS*

Two quick questions. The first one on your expectation in terms of inflation of the content for football. There should be an auction in a short term. We haven't seen much inflation last time around, so wondering what are your thoughts about this.

Second, if you can give us any colour about the current trading in terms of net additions, especially for pay-TV in Spain. Thanks so much.

José María Álvarez-Pallete - *Telefónica S.A. - Chief Operating Officer*

In terms of content, it's hard to say. But so far we have been able to send signals to the market that we want to be rational in terms of building the market and that's why it was a very limited inflation on the La Liga rights this year. And we have decided, for the time being, that we were not ready to pay the amount that was required to have the Champions in Europe. So we will try to do our best to make sure that content cost keeps under rationale terms.

Also, taking into consideration that we are at a part that, again, let me stress that Spain just have a 29% Pay-TV penetration, compared with an average of 61% in Europe, and there is way to go on the upside. So I think that if the pricing scheme is rational, we could try to create a stable environment here in Spain. So hard to see. We will see there is La Liga auction coming shortly, so we will keep you posted on that, but for the time being we are trying to send rational signals to the market.

Also take into consideration the fact that the remedies that were imposed to us because of the acquisition of DTS in terms of premium content that we need to have available for our competitors and the way those are being shared in terms of fixed versus variable

components, means that part of the fixed component of those premium rights is shared among the different players. So I think that nobody of the infrastructure-based players is really incentivized to pay crazy pricing because all of us will need to bear a significant part of the fixed cost.

And in terms of net additions in fibre, what we are seeing so far and now we are just with October recently closed is that the good trends that we were seeing keeps going. So we think that it should be another quarter of good net adds overall in the Spanish market.

Will Milner - *Arete*

Thanks very much. I had a couple. I just want to take I think it was Mathieu's question on the UK disposal a step further.

If you are unable to sell the UK business, if the European Commission doesn't approve or if Hutchison sees the remedies as too severe, could you maybe just discuss that scenario; what you believe your options are given the sort of leverage that the group would have after that decision? And obviously the LatAm devaluation that we've seen so far. That would be quite helpful to talk through your options in that scenario.

And then secondly, obviously a big part of the debate today has been about content costs and the promotion that you are running in Spain. From what I can see, the basic Fusión offer that people are taking is €59 and the promotion they will get stuff that costs €65 for basically €10. So in January the price for people on that promotion is going to jump from €59 to €124, which is obviously a huge jump.

I just want to understand how exactly you are going to manage that promotional roll off. Presumably you'll try and encourage consumers to take one of the add-on bundles, but just how is that going to work and how are you going to manage that when you hit that point in January? Thanks.

Ángel Vilá - *Telefónica S.A. - Chief Financial and Corporate Development Officer*

Regarding the first question, I would like to insist that we remain confident in the deal being approved with remedies and closing in the first half of 2016. In the unlikely situation that this was not the case, there would be several alternatives regarding our UK asset, which should be reasonably easy to execute either through M&A, capital markets, strategic or financial investors, doing a complete or a partial deal. There are several alternatives that one could think of.

And in addition, and irrespective of the UK deal outcome, we have several alternatives regarding other assets. For instance, we are strategically reviewing in-depth our portfolio of infrastructure assets to seek opportunities to free capital, realize value while maintaining operational control and this would include things like towers, submarine cables, backhaul, data centres, etc.

José María Álvarez-Pallete - *Telefónica S.A. - Chief Operating Officer*

Taking your question on the customers that are right now under this €9.90 promotion, and assuming (which is an assumption that is not totally correct) that they are all on the basic "Fusión contigo" offer of €59, if they were to move, and they have right now the premium extra TV offer (nominally €65 and is now being promoted to €9.90), we will not need to assume that all those customers are going to try to move to this nominal price of 65. And allow me to remind you that we have several add-on package that they could decide to move on some of those.

For example, right now you have the football package, the football add-on, which is a pure football package for €25 on top of the 59. You have the other sports which is €20. You have the movies which is just €9 and you have the series which is just €5. So we have tried to create flexibility for them to accommodate in the content that they would like to have and they would like to choose. Once they have tasted the full blended product of everything, they can decide if they move into that, if that is affordable for them. Or if not, they can decide to stay with at least one of the contents or two of the contents. So we have tried to create scalability on our product range to make sure that after the promotion they would be attracted to share part of their disposable income with us once they have tasted the product.

So that's our assumption. And again, allow me to remind that one of the basic assumptions is that not all of them are on the €59 Fusión package.

Jerry Dellis - Jefferies

The first question is around DTS, please. Last year DTS disclosed an EBITDA margin of around about 4.5%. There are now La Liga rights within the DTS perimeter, but has the DTS margin changed significantly since 2014?

And then secondly, in Brazil now you have TIM taking advantage of falling MTRs to bring off-net calls into the bundle. Do you expect a short-term impact from that? And would you be able to give us any guidance as to how much of your Brazilian revenue is derived from call-by-call off-net calls please? Thank you.

José María Álvarez-Pallete - Telefónica S.A. - Chief Operating Officer

Taking your question on DTS, we have issued the numbers of DTS for the five months that are wholly being consolidated. Basically in terms of OIBDA we are close to breakeven, if you put into consideration the wholesale cost that is being transferred from Telefónica de España on the other sports. So this 4.5% OIBDA margin right now is flat, is breakeven in terms of OIBDA for taking out positive extraordinary adjustments because of the mergers. So, I think that close to 0% OIBDA margin when we put everything into consideration and when we scored the wholesale cost being transferred to DTS from Telefónica de España.

In terms of Brazil, we do not disclose the OIBDA exposure because of interconnection. It has significantly decreased over the last five years because we knew that this was coming. So it used to be a very high exposure; now it's a pretty limited one because we have been bundling significantly our tariffs in Brazil during the last quarters.

Yes, it's a new feature on the market. We knew it was coming sooner or later. We have tried to prepare ourselves for that. And as Amos was stating on the call yesterday, everything in the quarter Vivo has been facing because we are the leaders of the market brand new product and much more aggressive promotions from our competitors.

And so far we have been able to overcome them, because we have, as I was stressing before in Spain, significant differential attributes in Brazil as well. We have the best brand; we have the best quality, the best coverage. We have the best distribution channels, the best distribution network, and integration is providing us with amazingly high cross-selling opportunities among the customer base of the former GVT and among the customer base of the former Vivo.

So, yes, brand-new feature on the market, something that was anticipated and therefore confident that we will be able to preserve our commercial traction.

Mandeep Singh - *Redburn*

Hi, thank you for taking the question. I just wanted to dig a bit more into a Spanish revenue growth. I appreciate this year was never official guidance, it was really an ambition, but do you think that next year 2016 as a cumulative, your revenue growth is actually positive and sustainable for the whole year?

Second question I have is really digging into the Spanish revenues in a bit more detail, there's a category of revenues called other which grew very significantly year-over-year. Excluding that, your revenues in Spain are declining by 2%, so if you could just sort of try and explain what that other category is? Is it accretive or dilutive to margins and just a bit of a revenue picture in Spain beyond just Fusión where you do give us a lot of disclosure? Thank you.

José María Álvarez-Pallete - *Telefónica S.A. - Chief Operating Officer*

Well, I tried to stress that it was not guidance and therefore we have tried to stress that it's not guidance for 2016 in order to avoid confusion going forward, but for sure, if we have been already having five months in a row of revenue growth, we think we can continue into that direction.

It took us almost seven years to turn Spain back into growth. It took us seven years to build the attributes to make sure that was sustainable with significant CapEx efforts, with significant price cuts, with significant bundling and therefore with significant discounts, significant efforts in terms of quality.

Allow me to stress the fact that one of the most important features of this quarter that has been almost unnoticed is churn reduction. We are back to historical levels of low levels of churn in Spain. So if you put on top of the table also the technological improvements or upgrades that we have been doing to our platforms and the expansion that we are doing in LTE and in fibre, definitely we are doing that because we think we can be a growing Company, but again we are not guiding and we will just keep you posted on a quarter-by-quarter basis.

In terms of the others line, it's a very low margin line. It's basically carriers and others. For further detail please keep in touch with Pablo and the IR team and remember also the fact that the split of revenues in the traditional way of Spain between fixed or mobile is having less and less sense because of the Fusión and the bundles. So I deeply encourage you to the overall numbers of revenues in Spain and for further details on the others, please contact Pablo and the IR team, they will give you more colour on that.

James Ratzert - *New Street Research*

Two questions please. First one is actually almost a direct follow-up from Mandeep's one just now regarding you have made a number of previous statements about aspiration for revenue growth in Spain. Now that has been achieved do you have an aspiration for EBITDA growth in Spain? And if so, when might that be able to be achieved?

Secondly, please, just wondering if you could give us an update on the situation around cash repatriation from Argentina. Is that something you have been able to do? And if not, how much cash is in Argentina at the moment? Thank you.

José María Álvarez-Pallete - *Telefónica S.A. - Chief Operating Officer*

Thanks for your questions. Now that we have been able to cross the lines of revenue growth in Spain, for sure we want as soon as possible to cross the line of OIBDA as well. We will try to give you more color on that during the fourth-quarter conference call in terms of the efforts that we are doing; not just because of the end of the promotion, but also the other efforts that we are doing by attacking the cost function in Spain, distribution and others. So, I hope that during the fourth quarter we will be able to give you more color on the cost structure of Telefónica de España going forward.

But yes, as you might imagine, after revenue growth for five months in a row and the platform that we have been able to build, now we are targeting to get back to OIBDA growth as soon as possible. So, allow me to postpone this for the fourth-quarter conference call, because I think that during that we probably will be able to give you more color on the extra cost effort that we will be running in Telefónica España.

Ángel Vilá - *Telefónica S.A. - Chief Financial and Corporate Development Officer*

Regarding Argentina, we have not repatriated any amount this year. The cash position is the equivalent of €203 million, which is decomposed in the equivalent of €105 million in pesos and €98 equivalent million in foreign currencies.

Fabián Lares - *JB Capital Markets*

Hi, good afternoon. Thanks for taking my questions. First of all, could you give additional information, now that the European Union has finally decided on the outlook for roaming; can you give us some information on how much that weighs on your consolidated basis in Spain and Germany and how much of this would be affected with the change in regulation in April 2016 and June 2017?

And second, with regards to the ruling, the statement by Standard & Poor's on hybrids I'm not sure if this was asked, but if it was I'm sorry; because I joined late. Could you give us more information as to what your strategy might be with hybrids given now that they account 100% of debt, whether you would retire these earlier, replace them with more senior, cheaper senior debt, etc.? Thanks.

José María Álvarez-Pallete - *Telefónica S.A. - Chief Operating Officer*

Thanks for your question. In terms of the roaming exposure, in terms of net exposure at the third quarter of this year is 1.5% of revenues so this is what we have right now. Allow me to remind you that we are already preparing our company for that.

We have all the players, but namely Telefónica has been putting together on our own network a significantly attractive tariff for roamers that are coming from the UK into Spain or from Germany to Spain or the other way around. So we already, as we were discussing before on the Brazilian interconnection question, we are also trying to anticipate that and to accommodate the impact on our accounts as we move over the end of roaming at the end of 2017. But right now, to be precise on the answer, 1.5% of net revenues, this is the net exposure to it.

And finally, allow me also to say that we have been growing 4.8% in revenues organic at the group level in Q3. Regulation is dragging 1 percentage point of that growth. If the regulatory situation would have been exactly the same than in the previous years, we would have been growing 5.8%.

So we are used to those regulatory effects. They are getting less and less relevant because regulation still weights in the previous century, but the impacts are getting less and less relevant.

Ángel Vilá - *Telefónica S.A. - Chief Financial and Corporate Development Officer*

Regarding the hybrids, S&P has revised the equity content assigned to several hybrid capital instruments to minimal from intermediate. In our case, all our hybrids have been impacted by this change.

This revision of the equity content has been triggered by a review of the rating event provisions in certain hybrid documentations, which allow the issuer to call the hybrids upon a reclassification linked to a change in the rating previously assigned to the issuer. Confronted with this situation, which was unexpected, our main target is to regain the equity content, to keep the financial flexibility we aimed at the times of the several issuances and also to maintain a good market access.

We are currently reviewing the documentation with legal counsel. We are reviewing our options and we are in dialogue with S&P about courses of action in order to regain expeditiously the equity content. And we will update the market in due course.

Pablo Eguirón - *Telefónica S.A. - Head of IR*

This was the final question. I'll pass now to Ángel for closing the call.

Ángel Vilá - *Telefónica S.A. - Chief Financial and Corporate Development Officer*

Well, thank you very much for your participation and we certainly hope that we have provided some useful insights for you. Should you still have further questions, please contact our investor relations department. Good afternoon.