Telefónica

RESULTS

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Conference call transcript

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Introduction

Adrián Zunzunegui – *Global Director of Investor Relations*

Good morning, and welcome to Telefónica's conference call to discuss January-March 2022 results. I am Adrián Zunzunegui from Investor Relations.

Before proceeding, let me mention that the financial information contained in this document has been prepared under international financial reporting standards, as adopted by the European Union. This financial information is unaudited.

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We encourage you to review our publicly available disclosure documents filed with the relevant securities market regulators. If you don't have a copy of the relevant press release and the slides, please contact Telefónica's Investor Relations team in Madrid or London. Now let me turn the call over to our Chief Operating Officer, Mr. Ángel Vilá.

Ángel Vilá – *Chief Operating Officer*

Presentation

Q1 22 Results

1. **Strategy execution whilst delivering growth**

Thank you Adrián.

Good morning and welcome to Telefónica’s first quarter results conference call. With me today are Laura Abasolo, Eduardo Navarro and Lutz Schüler. As usual, we will first walk you through the slides and will then be happy to take any questions.

I would like to start highlighting our clear strategic execution whilst delivering growth in Q1 22.

First, we reported another quarter of sustainable revenue growth which accelerated sequentially and for the first time in many quarters supported by local currency appreciation. Our new operating model is also adding digital capabilities and efficiency levers. All this allowed us to manage inflationary pressures extremely well this quarter.

Second, we reinforced our position in our core markets. In Spain, we launched last week miMovistar, the new portfolio through which B2C customers will be able to choose the products and services they need in a simple, customisable and flexible way; we also signed a 5-year agreement with DAZN to secure the highly valuable La Liga content with a 15% net cost deflation. In Brazil we gained further scale after closing the acquisition of the Oi mobile assets and expect to capture synergies of 5.4bn reais. This game-changer deal happens at a time when service revenue growth accelerates, and legacy exposure is reducing. In the UK, synergies are starting to kick in while remaining the gigabit leader in the market. Germany further enhanced its network quality, supporting its growth and profitability momentum.

Third, we continue to build optionality in many areas. In T. Infra, we are having very constructive conversations with many investors for the creation of Spain and UK fibre vehicles, while T. Tech is completing the build-up of a fast-growing business, with the acquisition of BE-terna to reinforce capabilities in the DACH region. In Hispam we continue modulating our exposure whilst increasing profitability, with optionality increasing.

And of course, the prospective in-market consolidation in Spain will bring benefits for customers and operators alike.

2. **Sustained growth momentum delivers strong start to the year**

Turning to slide 3, you will see we have had a strong start to the year with sustained growth momentum. We are delivering another quarter of sustainable revenue growth, together with cost efficiencies which allows to manage inflationary pressures. All this was supported by currency appreciation.

In the first quarter revenue grew by 3.2% y-o-y organically with robust growth across all business lines. Despite rising inflation, OIBDA growth accelerated to 2.1% y-o-y on an organic basis with a broadly stable margin.

We continued to prioritise investments in growth, managing to achieve a benchmark 12% of organic CapEx to sales in Q1. FCF was strong at €513m, an increase of €480m vs Q1 21.

Net debt stood at €27.5bn, increasing vs December-21 primarily due to FX appreciation, which in contrast has been extremely supportive in growth terms.

3. **Key financial metrics**

On slide 4, we have set out the key financial metrics for the quarter.

In organic terms, and once aggregating 50% of VMO2, revenues grew 3.2% y-o-y, OIBDA by 2.1% and OIBDA-CapEx by 6.4%. A clear improvement from previous quarters.

Reported revenues and OIBDA declined y-o-y mainly due to changes in the perimeter of consolidation, that deduct some 15p.p. to reported growth.

This more than offsets positive FX impact of €242m on revenues, €95m on OIBDA and €53m on free cash flow in Q1 22, mainly due to the appreciation of the Brazilian real. At the net debt level, FX had a negative impact of €1.3bn.

As stated in the previous slide, FCF surpassed the €500m mark in Q1 22 and net debt declined 23.3% year-on-year to €27.5bn.

4. **A stronger Telefonica for uncertain times, beating rising inflation**

On slide 5, you will see that Telefónica stands stronger under current uncertain times. Despite increased inflationary pressure in all our regions, Group revenues and OIBDA growth improve sequentially in all countries of operation.

Furthermore, in reported terms top-line is growing double-digit in Brazil and Hispam, mid single-digit in Germany and the UK, whilst improving growth in Spain. Furthermore, we achieved double-digit OIBDA growth in reported terms in Brazil, and mid to high single-digit OIBDA growth in Hispam, Germany and the UK.

As much as 80% of our revenue base has tariff mechanisms that protect us against inflation, including inflation-linked tariffs in most of our LatAm exposure. On top, we are adding revenue growth from T. Tech and the new digital ecosystems in our core units.

We believe that first quarter results have proven that we have a more efficient cost base than most of our peers. Our personnel cost base represents 14% of revenues driven by a consistent efficiency gains.

Through our focus on digitalisation and fibre we reduced expenses and have already a significantly lower exposure to legacy networks than our peers.

Finally, a benchmark setting CapEx of up to 15% of revenues provides an additional protection under current uncertain times.

5. **Well on track for 2022 guidance**

Moving to slide 6, we are well on track to achieve our 2022 outlook.

As you might remember we provided our guidance the day the Ukraine war started, and since then the macroeconomic outlook has significantly worsened. Despite this higher uncertainty and increasing inflationary pressure we delivered Q1 results within our guidance, which we reconfirm. We even delivered revenue growth at the high end of our guidance range.

In addition to Q1 OIBDA growth in line with our guidance we see tailwinds in the second half of the year. While inflationary pressure should be more evident in H1 such as energy costs in Spain, we will continue to accelerate efficiencies in the business to offset these pressures as best we can. We will benefit from the workforce reduction and lower content costs in Spain later in the year, and synergy realisation in the UK and Brazil will add to OIBDA growth as they ramp through the year.

On shareholder remuneration, we cancelled 139m shares and we will be paying 0.15 euros per share, the second tranche of the 2021 dividend, through a voluntary scrip dividend next June. As for the 2022 dividend, 0.15 euros per share will be paid in December 2022 and another 0.15 euros per share in June 2023, both in cash.

6. **Progress towards ambitious sustainability goals**

On slide 7 Telefónica demonstrates its commitment to sustainability by setting ambitious goals across the three main pillars of ESG.

Our key Environmental objectives include becoming net-zero by 2040 across the business and our value chain - with an interim target of scopes 1 & 2 in Brazil, Germany and Spain by 2025 - and zero-waste by 2030. We are working towards these goals with initiatives such as:

- The Telefónica Forest, which helps us reduce our carbon footprint; and,
- The Eco Rating scheme - now available in all our markets – which is enabling our customers to make environmentally informed decisions.

On the Social side we have set tangible targets to bridge the digital divide and to progress in our human capital management. We are:

- Continuing to rollout fibre and mobile connectivity to underserved areas. This includes the target to reach 90-97% rural mobile broadband coverage by 2024 in Brazil, Germany and Spain.
- We are also ensuring equal opportunities in the workplace through collective agreements like the Equality Plans just signed in Spain.

Finally, we wish to lead by example with solid objectives in Governance. In the first quarter we have:

- Remained on-track with our sustainable financing commitments; and,
- Continued to lead in transparency, as verified by Transparency International's latest report on IBEX 35 companies.

These are just some examples of how Telefónica is moving forward – working to build a greener, more inclusive and fairer world.

7. Spain

Moving to slide 8, where we show the results of our domestic market in Spain.

In Q1, T. Spain improved its commercial performance following a tariff upgrade in February. We successfully reduced convergent churn to its lowest level in 5 years, while simultaneously increasing convergent ARPU by 1.5% y-o-y to €91.1. Furthermore, our NPS reached record levels at 43%, the highest ever, delivering proof points of our customer centric strategy.

Throughout the quarter, we continued to enhance our services. Movistar customers will now have access to all "La Liga" matches for the next 5 seasons thanks to our new agreement with DAZN. Importantly the net cost for Telefónica to access all Liga games is 15% lower than in the previous cycle. Furthermore, last week we announced that our customers will be able to enjoy a new convergent portfolio, miMovistar, that's more flexible and complete with new added services beyond connectivity.

In Q1 2022, y-o-y revenue growth accelerated due to handset and services revenue, with double-digit growth in IT sales. The decline in OIBDA was mainly due to the significant increase in the cost of energy and the higher growth in lower margin handset revenue, partially offset by the generation of efficiencies. We nevertheless expect the peak energy cost impact to be behind us.

We continue to prioritise investments in growth and maintain a sound organic OIBDA-CapEx margin of 27%, the benchmark in the sector.

8. Germany

Moving to Germany on slide 9, which had a strong start to the year delivering sustained operational and financial momentum in the quarter on the back of core business strength and high customer demand for the O_2 Free portfolio.

Telefónica Deutschland reconfirmed its 'good'-rating in the connect network test, and 5G now covers ~40% of the population and is on track to achieve ~50% population coverage by the end of this year.

Looking at financials, revenue grew by 5.2% y-o-y organically in the first quarter, reflecting sustained mobile revenue growth on the back of continued good commercial traction of the O_2 brand and some support from the recovery of international roaming.

OIBDA posted strong organic growth of +7.0% y-o-y in Q1 22, with improved operational leverage in both, fixed and mobile, reflecting own brand momentum, further efficiency gains as well as some international roaming tailwinds.

CapEx was up +16.1% y-o-y organically in Q1 22, as Telefónica Deutschland continued to execute its 'investment for growth' programme according to plan in its final year.

9. Virgin Media O2

Moving to the UK, and our Joint Venture, Virgin Media O2, which has started ramping up network investments while improving products and services with big challenger decisions including not reintroducing EU roaming fees.

FTTP upgrade pilots were completed in February, paving the way for the planned deployment of full fibre across the entire fixed network commencing later this year, with completion in 2028. The VMO2 network already delivers gigabit speeds to over half of all UK premises, making it the biggest contributor to reaching the Government's broadband target.

VMO2 delivered resilient trading at the same time as implementing fixed and mobile price rises, which will support revenue growth in future quarters.

Looking at the financials, revenue was broadly stable in the first quarter, whilst OIBDA grew by 2.6% on an organic basis due to cost savings following the migration of the Virgin Mobile MVNO base, lower sales and commissions costs and the start of the flow through of cost synergies, which will ramp through the year.

10. Brazil

Moving to Brazil on slide 11.

Vivo started the year reinforcing growth trends seen in recent quarters.

Consistent growth in high value accesses reaffirmed Vivo as the telco with the best quality and value proposition.

In mobile, contract accesses increased by 7% y-o-y whilst maintaining churn at a low level of 1.2%.

In fixed, FTTH connections almost reached 5m, thanks to the implementation of alternative FTTH expansion models.

This translated into stronger financials:

- Vivo accelerated its organic year-on-year top line growth to 4.6%, with strong results in both mobile and fixed services. Legacy exposure continues to decline at a time service revenue growth expands.
- OIBDA grew 1.6% in organic terms despite inflationary pressures and lower margins from new digital services.

In euros, top line growth stood at 18% year-on-year and OIBDA +15%.

And finally, on ESG, Vivo continued to advance its commitment to sustainable growth by adding 23 power generation plants, with the aim of having 80 plants in operation by the end of 2022.

11. Oi mobile assets acquisition completed

Moving on to the next slide we review the acquisition of Oi's mobile assets in more detail.

On 20th April we successfully closed the acquisition of our portion of Oi's mobile assets which will allow us to further improve the profitability of our business, and at the same time, consolidate Vivo's leadership in the market.

With this acquisition, we will add 43MHz to Vivo's spectrum portfolio, 12.5m mobile accesses, of which 37% are in postpaid and 63% in prepaid, and 2.7k mobile sites.

This acquisition will benefit VIVO by generating synergies with an NPV of approximately €1bn, virtually matching the investment. Our synergy estimate conservatively excludes all revenue synergies at this stage.

12. Tech build-up

Turning now to slide 13, I would like to take the opportunity to recap on the successful build-up of our fastest growing business unit, Telefonica Tech.

T. Tech is progressing rapidly towards becoming a Next Generation IT Services Provider with cutting edge solutions in cyber security, cloud, IoT, big data, artificial intelligence and blockchain.

At the end of Q1, T. Tech acquired Incremental, a large Microsoft Dynamics partners, complementing the acquisition of T. Tech UK&I. And this week, T. Tech acquired BE-Terna, reinforcing its position in the German and DACH market.

These acquisitions, coupled with our in-house capabilities, allows Telefonica Tech to be a global company with around 5,400 highly skilled employees, reaching more than 5.5m B2B Group customers. Revenue is significantly outperforming the markets where we operate, with a well-balanced and difficult to replicate revenue mix.

13. Tech, outperforming its market

What I just shared with you is further proven on slide 14, where we show Q1 performance for T. Tech.

Revenue growth accelerated to 80.6% y-o-y, significantly outperforming the market. This was driven by a strong performance across the businesses and the integration of operations in 2021. Cyber is performing above expectations, with all services revenue in IoT growing double-digit in Q1.

Recent acquisitions have reinforced T. Tech's growth potential as shown by Q1 numbers.

Ultimately, a larger and stronger T. Tech is critical, in a market where digitalisation is a must, something we expect to remain a key growth lever for Telefónica.

14. Infra, driving value creation

Moving to slide 15, we review the latest developments at our infrastructure portfolio manager, Telefonica Infra.

In Q1, we continued to drive value creation across our portfolio and to execute the initial phases of work on our new fibre JVs, having started discussions with potential investors in the UK and Spain.

In Germany, UGG has approximately a quarter of a million premises under MoUs signed with municipalities. While in Brazil, FiBrasil continues to be on track to meet its deployment target, reaching 2.2m premises passed in Q1.

ONNET Fibra, in Chile, continued with its accelerated rate of deployment with 200k additional premises passed, maintaining its FBB leadership in the market. Meanwhile, in Colombia, the transaction with KKR was closed in January 2022 after receiving all necessary regulatory approvals and expects to pass 4.3m premises in 3 years.

During Q1 22, Telxius' Subsea Cable maintained strong commercial momentum, evidenced by the 65% growth in full contract value, which contributed to high single digit y-o-y OIBDA growth in reported terms.

I will now hand over to Laura, who will review our Hispam's operations and the Group's financial performance.

Laura Abasolo - *Chief Financial and Control Officer & Head of T. Hispam*

Hispam

Thank you Ángel.

Slide 16, shows the solid performance across the Hispam region.

Firstly, we continued our fibre transformation across our operations, with almost 3m new premises passed in last twelve months, showing a clear acceleration vs. the previous period's deployment.

Secondly, our revenues and OIBDA remained robust with revenues growing in all countries and new operational model offsetting inflationary pressures. It is worth noting the appreciation of Latam currencies, which had a strong positive effect on euro denominated growth.

And lastly, capital employed was reduced 14% on a y-o-y basis thanks to new asset light models with an efficient use of our resources.

Strong Balance Sheet, prudent management

Turning to slide 17, we highlight our strong balance sheet derived from a prudent debt management that has allowed us to benefit from a long average debt life, close to 13 years. We have over 80% of our debt at fixed rates and still report Group interest cost below 4%. So, we are very well positioned to face new market dynamics.

Our robust liquidity position that exceeds maturities beyond 2024 helps us to comfortably face any market environment.

We have made a lot of progress to increase local debt and align it more closely with our FX exposure.

I will now hand back to Ángel who will wrap up.

Ángel Vilá – *Chief Operating Officer*

Strong start to the year

To wrap-up, in slide 18, the first quarter showed a strong start to the year, with sequential improvement in organic and reported growth across whole Group, beating inflationary pressure, on which we expect the worst to be behind us.

FX provided support in this first quarter, allowing for strong double-digit reported growth in Brazil and Hispam.

From a commercial point of view, we maintained strong momentum, boosting FTTH, enabling us to increase relevance and engagement with our customers.

Looking ahead, synergies are starting to materialise in VM02, and will soon start to flow through from Oi and we continue to position Telefonica to sustainably grow in all business units.

Finally, we reiterate our guidance for 2022 and confirm 2022 dividend.

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

Q&A Session

Mathieu Robilliard – *Barclays*

First I had a question around net neutrality. I think you've been very clear over the past few years about wanting Big Tech to contribute towards network costs, as they are streaming probably 70% of European telco network traffic. I note from recent public comments that the EC, Mrs Vestager and Mr Breton, seem supportive, and they promised to come back by the end of the year with a framework that could enable European telcos to get a contribution from Big Tech.

So, my question really is, how confident are you that this could come through? What is the timeline? The reason I'm asking is that investors, at least some of them seem quite sceptical about a positive outcome there, notably in terms of how to implement this.

And then the second question is around Spain. I note that the convergent ARPU is up y-o-y, for the first time in a while. And I was wondering what was behind that? Is there less spin down, is competition less impactful, although we are seeing still a lot of aggressive promotions? So, I guess the underlying question is, is that ARPU trajectory sustainable in your view?

Ángel Vilá – *Chief Operating Officer*

Thank you, Mathieu, for asking about the topic of net neutrality and Fair Share regulation because this topic, as you say in your latest 2 reports, we think it brings a positive optionality for the whole sector.

As José María, our chairman, together with heads of DT, Vodafone and Orange commented in a letter to the Financial Times, the exponential growth of traffic in our networks is associated or linked to a limited number of content platforms, and is requiring all of us to do continued investments to meet the demand, and this is an increasing challenge in a context of declining profitability in retail markets.

And, traditionally, the large digital content platforms are not compensating the telco sector for the use of networks. The traffic they inject into the networks and therefore, the costs and investments that they induce in the networks. They have invested, of course, in international transport and CDNs, providing some relief for our costs. But most of this traffic still has to be delivered through our national networks and access networks where most of the cost and investment is located. So, this is why we are calling for a fair contribution to our costs to make this sustainable.

There were 2 recent reports delivered by, I think, Frontier Economics and Axon that delve into the cost of Big Tech traffic on European networks, the asymmetry of negotiating powers, the potential impact in Europe on socioeconomic terms that it would bring if Big Tech would cover part of this cost. So, we think that this should be the turning point where European policy makers are determined to take steps towards solving this problem, and we welcome the initial positive remarks by commissioners Vestager and Breton regarding this. We have hopes that Fair Share regulation should mark the end of the free ride for OTTs.

Then moving to your second question on the Spanish ARPU, we have been able to grow our ARPU 1.5% y-o-y in this quarter to €91.1 for the first time since the end of 2019. This growth in convergent ARPU is driven by the strategy that we have been deploying. And if I cover the moving parts, on the positive side of the evolution of this ARPU, the more for more move that we did in February (which still has not impacted the full quarter, of course) in legacy portfolio and also in the packages that include Netflix; we also had a positive that comes from the lower effect of promotions; another positive is higher consumption of out of bundle; and the fourth positive would come from new digital services.

On the other hand, this has been mitigated by higher weight of no-frill packs. And there was a ruling against betting entities advertising on TV that reduced part of our income.

So more for more, less promotions, higher out of bundle and new digital services were the positives driving our ARPU up.

David Wright – *BofA*

It´s only Q1, but your growth run-rate against guidance already looks quite conservative. And I know that within your proportionate OIBDA, Spain and UK represent about, give or take, 50%, and we can clearly see easing Spanish comps with energy costs, content and employee costs. We can clearly expect an acceleration in UK EBITDA as you get the full effect of price increases.

So, against that, you've had a strong start in Germany, but Germany also looks like a potential guidance upgrade. So, I just wonder what headwinds we could imagine in the other business units? I mean Brazil is talking about another postpaid ARPU rise too. So, what headwinds are out there that means you can't continue to beat this guidance? That's part one.

And then part two, LatAm, noncore Hispam, I guess, what is the potential still to maybe monetise any of those assets? Is that something you're stepping away from a little now? You've decapitalised the businesses that performed well? Or is it quite the opposite now as we come out of COVID it's back to the negotiating table?

Ángel Vilá – *Chief Operating Officer*

Thank you, David. On the first question on guidance. As I was saying in my speech before, we provided guidance when we presented full year results, which happened to be the day that this terrible war started and the macro context has worsened significantly since then, increasing uncertainty and inflationary pressures. But still, we are managing to bring Q1 results, for instance, in revenues, at the high end of our guidance range, and we have been beating consensus expectations at revenue, OIBDA, operating cash flow and free cash flow levels. These results demonstrate our ability to cope with inflation, and we showed sequential improvement in revenues, in OIBDA and OIBDA minus CapEx in organic terms. And thanks to FX tailwinds, even larger improvements in reported terms.

So, this gives us confidence, in spite of the adverse macroeconomic scenario, to reiterate our 2022 guidance of low single-digit growth in revenues and OIBDA and up to 15% CapEx to sales, despite these pressures. We will, of course, monitor the evolution across the year and make, if needed, any upside adjustments to this, but we think it's not the moment to make any upward adjustment now.

Laura Abasolo - *Chief Financial and Control Officer & Head of T. Hispam*

Thank you, David, for the question. First, our strategy remains intact regarding Hispam. As we said a couple of years ago, we remain committed to modulate exposure to the region, while creating the conditions to maximise its value via growth, consolidation and potential corporate transactions. I think that in the last 2 years, since the decision to spin off from an operational point of view, the region has been critical. We have transformed the operations and executed a turnaround.

We have approached the region, as you have been able to follow, with a very disruptive model both from an organisation perspective and from an infrastructure perspective. And I think we have achieved very solid results with that new management model, and it's being based, as I said in the past, with very thorough execution and pulling many levers.

As you say, now we have definitely a more favourable framework not only because we have built the pillars for a better outlook for Hispam, but also because it seems we could have a more stable macro and sector trends and also FX tailwinds. So, we think we have created value in Hispam. It has a lot of optionality, and we could consider things, as we will do for any asset within our portfolio, if it creates additional value. We will definitely look at everything.

But what I can say is that Hispam is no longer dragging financial or management resources, and I think it has a good optionality also from running the operations as we have been doing. And, in fact, I humbly say that we've been beating consensus almost every quarter since we came with this new model.

David Wright – *BofA*

And Laura, just quickly, is deleverage the absolute priority if you were to monetise any of those assets? Or could you now be persuaded even into share buyback territory?

Laura Abasolo - *Chief Financial and Control Officer & Head of T. Hispam*

Deleverage is definitely a priority. It's not an absolute priority in the sense that we have to de-lever while creating value and becoming a more sustainable company going forward but, deleverage is definitely a priority for us. We are strongly committed to an investment-grade credit rating.

Regarding shareholder remuneration, we came back to a full cash dividend of €0.30 per share, which is attractive and sustainable. And obviously, if there's excess free cash flow, we have to look at all potential uses of that free cash flow and deleverage could be one. And we will take the proper decision as we manage our balance sheet and our credit rating.

Fernando Cordero Barreira - *Santander*

The first one is on Spain and particularly on the new B2C offering, the miMovistar new platform. In that sense, I would like to understand which are the key strategic targets from your side with this new platform? And particularly to what extent are you prioritising to increase the value per customer to increase the number of successes customer versus to increase the absolute volume of customers given also what is the structure of the offer?

My second question is related to Telefónica Tech. You have already explained quite well the recent developments there. But I would like to understand which is still the pending M&A or inorganic growth roadmap in Telefónica Tech? And at which extent are you still open to incorporate, let's say, financial partners in order to keep funding the inorganic growth in Telefónica Tech, as you highlighted back in the past?

Ángel Vilá – *Chief Operating Officer*

Thank you, Fernando, for your questions. On May 15th we launched, the new portfolio of miMovistar. After having had the Fusion portfolio for 10 years, we revamped the convergent portfolio to make it more flexible. It is a portfolio which is modular. It starts with connectivity to which modules can be added to include television offer, devices, and then value-added services such as health, gaming, security to build a more complete and adapted formula for the customers. Existing Fusion customers can choose to continue with their current tariff or switch to miMovistar.

Prices are similar to those of Fusion. So, for comparable packages, there would not be a relevant impact on customers. However, we're aiming this portfolio to be service revenue accretive. We are aiming to have more traction commercially, especially in the mid ARPU segment of the market.

We continue to punch above the rest of the players in the high ARPU segments of the market. We have competitive offers now in the no-frills segment, but, what we have been seeing is that especially in the mid ARPU segment, we were not offering the flexibility that our customers wanted. Customers that wanted to upgrade from mid packages to include additional content, but didn't want to take many more features, couldn't do so easily, and we are now providing that opportunity.

So, we are aiming for additional commercial traction. Of course, there can be also some repositioning by some customers, but we're aiming to provide easier options for upgrading for medium-ARPU customers and reducing the churn in that segment, and therefore, increase the B2C service revenue with miMovistar.

Regarding Telefónica Tech, you can see on Slide 13 how we are building up the company. First, we did the carve-out of the units. We have then been executing M&A transactions either to strengthen the geographic presence (in particular in the U.K. and the German market) or capabilities. Now we move to the next stage, which is a focus on integrating these acquisitions and of course, continuing the growth momentum of Telefónica Tech. So, no significant further M&A pending.

And we will aim to communicate and explain Telefónica Tech as well as we can to the market to start seeing it in the sum of the parts of our group.

Our focus is to integrate these acquisitions, continue to deliver momentum, continuing to build q-o-q track record of Telefónica Tech which, because of these acquisitions is going to have a run rate of revenues by the end of this year, exceeding €1.5bn.

And we have seen interest from potential investors, but we will choose the right time to bring anybody in, and we think that there is still potential of growth for this unit. So, we'll pick the right time, which probably is not now, now it is time to integrate and continue to deliver growth momentum, and not continue doing M&A, and trying to convince you to show this in the sum of the parts of Telefónica.

Keval Khiroya – *Deutsche Bank*

Two questions, please. So firstly, we saw a step-up in the Q1 lease liabilities to €8.7bn. Are you able to discuss how we should think about that number going forward, and also the evolution of the lease payments in the cash flow? And then secondly, you had a strong OIBDA performance in group "other" reflecting Tech and also lower group costs. It's a line which perhaps is a bit more difficult for us to model, but can you provide some colour on how we should think about the OIBDA evolution for this group "other" line?

Laura Abasolo - *Chief Financial and Control Officer & Head of T. Hispam*

Thank you, Keval. On leases, the increase is a natural consequence of the Telxius deal we closed in 2021. So, you should see a step change in that, and then we will be more on a recurrent level. Having said that increase in leases, as you know, the net debt plus leases reduction was very significant with this transaction. We actually reduced the net debt-to-OIBDAL pro forma by 0.3x in our ratio on top of all the benefits: financial optimisation, redeploy these resources of the towers into other core operations, the value creation with a very high multiple, increasing vendor diversity in the tower space in Europe and so on. But that had an impact in leases as we explained when we announced the transaction.

We also have some impact from FX revaluation of Brazil and also Hispam, but mainly Brazil. And that could continue if FX remains strong, which could be good for revenue and OIBDA. But I think that increase has much to do with the Telxius deal.

And from the free cash flow perspective, the explanation could be similar, as we have the lease payments increase from the tower deal and also some FX revaluation.

On the other, unfortunately, Keval, this is a very difficult line to give you any colour on because it does have the impact of consolidation perimeter, and that's negative because we are excluding this year what we had included last year on towers, Costa Rica and El Salvador, so that's going to have a negative impact in the variation. It also includes restructuring expenses that this year should be definitely lower. So that would be a positive.

And apart from that, we have the holding and global units’ cost, and that's already impacting the others. We have been going through a lot of efficiencies, and we are a much leaner company in the corporation and global units in general. So that's good news.

And we also have the other subsidiaries not included in the core OBs or Hispam. So there we also have good news because we have the growth of some of the Tech services. We also have a very strong start of the year of our purchasing unit. We also have a very strong subsea cable, which I don't think you are taking into account in the consensus, and we have low-single-digit growth in the subsea cable unit.

So, in general, that would be good news together with the efficiencies. But unfortunately, if the perimeter changes and we have any restructuring or capital gains, which are not part of the core OBs, should also be there.

So, difficult to predict, but it is definitely going in the right direction.

Georgios Ierodiaconou - *Citi*

If I could start with a question around the fibre JV processes in the UK and Spain. I just wanted to clarify a couple of things. Firstly, whether the perimeter you are considering is just what you show in Slide 15 or whether there is any scope either in the UK or Spain to potentially go beyond the rural areas in Spain and beyond the 7m greenfield in the UK? And also, specifically in the UK, if you don't mind just updating us on the progress you had in finding some wholesale partners. And Angel whether I'm right in thinking that given wholesale adds value to the asset, is it fair to assume in the event that you do find a financial partner before you announce a wholesale deal that then it becomes less likely, or whether that's too simplistic? I'd be interested to get your feedback on that.

Ángel Vilá – *Chief Operating Officer*

Thank you, Georgios. I will take the first question, and I will ask Lutz to respond the second one on the wholesale partners.

On the first one on the fibre joint ventures. On the Spanish one, we decided to launch a fibre company covering a subset of our network, carving out part, as brownfield, of our fibre in areas where there are less than 20k inhabitants in towns. So, it's designed for rural areas which are not served partially yet, where there is still a greenfield opportunity to build, and also where there is an opportunity for potential consolidation of other players that have been building in some of these geographies.

We did this because it's an industrial project, not just pure financial engineering. It has a growth perspective, and it is eligible for fibre subsidies. And from the brownfield contribution, it has cash flow generation from day 1. And this would be an animal that then (because we will continue to consolidate it accounting-wise in our accounts) would not put any pressure on our financial position. We have already initiated talks with investors. We are seeing a very healthy level of interest. We're expecting first round non-indicative offers later this month. And this would be the project that we are aiming for fibre in Spain, not a different perimeter.

With respect to the U.K., we have on one hand, a project that we're doing 100% at VMO2, which is the upgrade of the current cable network to fibre that we will deploy between now and 2028. The pilots are confirming our estimates of cost for the upgrade. So that's going to be done by VMO2 completely.

And the fibre joint venture that we are already also in talks with investors, is up to 7m greenfield homes passed outside the current footprint of Virgin Media O2. It will be 50% an investor and the other 50% held by Telefónica Infra and Liberty Global. The process has been launched. We already got the first-round indicative bids. We're actively engaging with investors, and we see a strong interest in that process as well.

For the second question, I'll pass it to Lutz, please.

Lutz Schüler - *CEO of Virgin Media O2*

First of all you've seen our guidance for this year, that we will be growing OIBDA mid-single digit. I'm saying that because, yes, we are in wholesale negotiation, but we are doing this out of a position of strength. What do we have to offer if we have the ambition to cover 23m homes out of the U.K., that means we are 1 out of 2 national fibre networks. And of course, we want to have a certain share of the wholesale business. But we have to act in a balanced way because on one hand, we offer higher speed to a possible wholesale partner and maybe also some discounts. On the other hand, we don't want to disrupt the wholesale market that will devalue the entire fibre infrastructure we are all spending our money.

And maybe to your last question, are we in a hurry to close the wholesale deal before we are going to sign a deal with an investor on the fibre joint venture? The answer is clearly no. Two reasons for that. One, as you might know, we have currently a penetration of our network expansion program (we call it Lightning) of 30% and this delivers a very decent IRR. And obviously, we would commit something similar in this fibre joint venture. And number 2, a financial investor can make up its own mind if they think that we are getting a wholesale deal done over time or not, sitting on 23m fibre homes. I hope that helps.

Nawar Cristini– *Morgan Stanley*

I have two questions, please. The first one is really a quick follow-up on a previous question on the guidance. Could you discuss how the mix has been? It wasn't since the guidance was provided because, of course, it was then Ukraine and a lot has changed since then, so it'd to be interesting to have your assessment about how the different assets have been performing versus your initial expectations, in particular, the areas where probably you are doing better, and areas where perhaps it's less so. So, any comments on the mix will be particularly helpful.

And then I have a question about an area which was at least ahead of consensus expectations, is Hispam. Could you discuss a little bit how do you think about prospects here, in particular, given the deteriorating macro backdrop globally? Are you concerned about any impact here? That will be particularly helpful.

Ángel Vilá – *Chief Operating Officer*

Nawar, I'll take the question on guidance. As you know we do not disclose guidance by regions or segments, but I will try to give you some colour. On the revenue side, as you are seeing, we are growing revenues across the whole footprint, and we aim for revenue growth in all our units. In the UK, which was a bit more muted, we expect items like the price increases to start kicking-in in the coming quarters.

As for the OIBDA performance, there are factors which make us confident as the year progresses. So, for instance, in Spain, the impact of energy is going to be lapping in the second and especially from the third quarter, also the personnel reduction plan that didn't fully benefit the first quarter is now going to kick-in in every quarter. Also, the La Liga renewal with 15% deflation from the third quarter will be coming in. Synergies from the U.K. and Brazil consolidation are also ramping up during the year. Our German unit has had a very strong start to the year, and they have the tradition to beat guidance in the last few years, and we are confident that they will continue with their tradition also this year.

So yes, there are headwinds. There is inflation and economic effects from the war, cost of living crisis, but items like the ones I just described give us confidence to maintain and reiterate the guidance, and we think we are well on track to achieve it this year.

Laura Abasolo - *Chief Financial and Control Officer & Head of T. Hispam*

Thank you for the question. If we start with the political situation, there's still some uncertainty with the constitutional reform in Chile and others, but we expect events to evolve with no major distress for the institutional framework. Definitely, we have inflation that has become an additional source of tension, but we have been dealing with inflation for years in Hispam, and I will explain in a bit what we are doing in that front.

And then, as globally, there's been an increase in interest rates. But fortunately, we did a lot of work in financing last year and the year before, and we have secured very attractive financing. So, for that, we should be protected, which applies to the whole of the group, not only Hispam.

On the other hand, we have the positive impact of commodity prices, and that's also helping FX tailwinds, which in the case of Hispam is also important operationally because part of our OpEx and part of our CapEx is U.S. related.

On the hottest topic, which is inflation, let me tell you that we've been upgrading prices across the board and in most of our business units. Argentina, we've been talking for long, but we had 63% upgrade in tariffs for the last 12 months. Chile, we are updating tariffs 7%, in line with inflation in postpaid, fixed services and B2B is also the case. Colombia, we are updating mid low-end contracts by 4%, Peru 4% in fixed services, 7% in contract, Mexico as well, more in postpaid, 6%, prepaid 3%. So overall, inflation is being factored into revenue.

In OpEx, with this management model and also through labour reductions from last year, we are seeing that some of the OpEx lines with high incidence of labour impact us less. And it's worth mentioning that Hispam was really ahead of the curve on digitisation. So, we have reduced a lot call-centre' costs, shops' costs. You already saw the impact in Argentina, but that's something that would apply across the board.

And then as I said at the beginning, let me remind you on the important FX LatAm appreciation, which will result in improvements in external and fiscal accounts in the region. So, we have a positive outlook rather than negative. And on the negatives, I think we will keep on managing and we are better prepared with a leaner operational model as the one we have now.

Ángel Vilá – *Chief Operating Officer*

Thank you very much for attending this call in which we are presenting this very strong start of the year and the confident outlook that we have for the rest of the year. If you have any further questions, please do not hesitate to contact our IR department. Thank you