Telefónica

RESULTS
January - December 2021

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-December 2021 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 Chairman and Chief Executive Officer, Mr. José María Álvarez-Pallete.

José María Álvarez-Pallete– *Chairman & CEO*

Presentation

Q4 21 Results

1. 2021: strategic execution delivering positive results

Thank you Adrián. Good morning and welcome to Telefónica's fourth quarter results conference call. With me today are Ángel Vilá, Laura Abasolo and Eduardo Navarro. As usual, we will first take you through the slides and then we will be happy to take any questions you may have.

I would like to start by highlighting the strategic execution during 2021 which is delivering positive results.

We remain focused on our core markets. We completed the biggest transaction in Telefónica's history, the JV with Virgin Media in the UK, whilst the acquisition of Oi's mobile assets in Brazil got final regulatory approval and is expected to close in the coming months. We secured key 5G spectrum in Spain, Brazil and the UK, accelerated fibre deployment, and brought our German network quality to the highest market standards. We also continued building a digital consumer ecosystem in Spain and Brazil in areas such as connectivity, entertainment, home, wellness and finance.

We further reduced our exposure to Hispam through portfolio simplification and debt allocation. We are implementing a new operational model which, together with CapEx optimisation, allows us to reduce capital employed. At the same time, we now have a higher share of debt in local currencies, accounting for 28% of the Group's total.

T. Tech again outperformed the market increasing revenues in 2021 by over 30% y-o-y to almost €1bn. This was achieved whilst strengthening capabilities through acquisitions and best-in-class partnerships.

In T. Infra, ongoing value creation and crystallisation continues, along with the creation of growth opportunities through fibre vehicles. This strategy was proven by the towers sales to ATC at a record multiple.

Finally, our streamlined and digital operating model is delivering enhanced efficiencies, with 80% of processes already digitised and implementing technology solutions such as Open RAN, green energy, fibre, and 5G. We are focused on attracting and retaining the best talent, offering agile and flexible working and striving to be at the forefront of innovation.

2. 2021 Key metrics

Slide 2 shows the solid performance across our key metrics in 2021.

First, our connectivity leadership was reinforced, with Group accesses growing by +3% to 369m and with strong traction in strategic areas that are key to economic growth, such as UBB, fibre and mobile contract. We remain Western world leaders in UBB, with total UBB premises passed reaching 159m as of 31st December.

Second, in 2021 sustainable growth was restored with revenues growing organically 2% y-o-y and OIBDA growing 1.4% y-o-y.

Third, free cash flow generation remained robust, with free cash flow excluding spectrum reaching almost €3.8bn, or €0.66 per share, well above the dividend per share of €0.30. Our focus on smart capital allocation is reflected in the 14.2% CapEx to Sales ratio, comfortably below our guidance.

Fourth, net financial debt has decreased by a remarkable €26.2bn since the peak in June 2016 to €26bn at year-end, driven by the completion of M&A deals, and solid and steady free cash flow generation over the past years.

Finally, it is worth highlighting that Group's shareholders' equity doubled vs. 2020 to €22bn mainly due to capitals gains booked along the year.

3. Enabling sustainable growth

Moving to slide 3, our focus on delivering sustainable growth is evident in our Q4 performance.

Starting with the financials, we posted simultaneous organic revenue and OIBDA growth for the third quarter in a row. At the top line, all business units are growing and OIBDA has proved resilient, with an improving y-o-y trend in Spain. FX had a declining and minor impact in the quarter, and spot rates imply further tailwinds to come.

The significant reduction in net debt in 2021 was achieved mainly through capital gains from M&A transactions, totalling €11bn. In addition, free cash flow ex spectrum costs improved sequentially in the last quarter to almost €3.8bn in 2021.

We remain a customer-centric group. Commercial momentum improved in the quarter, driven by products and services with superior connectivity, outstanding digital experiences and highly efficient networks.

We also remain efficient in capital allocation, with CapEx allocated to next generation networks being approximately 45%, and committed to promoting inclusive connectivity.

And we continue to deliver on ESG, which is a core part of our strategy, including how we contribute to the economy in terms of GDP, employment and fiscal contribution.

4. Financial summary

Moving to slide 4 for our financial summary.

Our full year reported figures were impacted by capital gains, changes in the perimeter of consolidation and, in the last quarter, by restructuring provisions of €1.5bn in OIBDA, mainly in Spain, and an impairment in Peru.

Revenues reached €9.7bn in the fourth quarter, growing +3.1% organically, while OIBDA increased by +0.4%. Underlying OIBDA totalled €3.2bn, while net income for the full year was over €8.1bn despite restructuring charges and the impairment mentioned earlier.

Net financial debt for the year was €26bn, -26% lower than the previous year and FCF reached almost €2.7bn.

5. 2021 upgraded guidance met

Slide 5 highlights that we successfully achieved our recently upgraded 2021 guidance across revenues, OIBDA and CapEx to sales ratio.

We are also confirming today the payment of the second tranche of the 2021 dividend of €0.15 per share, which will be paid in June through a voluntary scrip dividend. The first tranche, €0.15 per share, was paid last December, with 65% of shareholders opting to receive shares.

In addition, we will propose to the AGM the adoption of the corresponding corporate resolutions for the cancellation of 2.41% of shares held as treasury stock as of 31st December 2021.

6. ESG initiatives aligned with UN SDGs

At Telefonica, we are committed to sustainability, and we align and measure our progress across our ESG pillars against the United Nations Sustainable Development Goals.

- We are reducing our environmental impact by using cleaner energy and shifting to more efficient technologies. We are taking our customers on a journey towards decarbonisation by providing them with products and services, such as Eco Rating and Eco Smart, that enable them to monitor and reduce their environmental impact.
- On the social side, we are committed to connecting the unconnected and bringing high-speed internet to as many people as possible, for example, we have now connected 2.4m people in remote communities with mobile broadband in Peru. We also continue to innovate, internally through our new Innovation and Talent Hub and externally through new programmes to scale up startups. Furthermore, we are ensuring that our workplaces are more inclusive.
- We continue to make progress on governance. Our Board of Directors has been restructured and we now have a leaner and more diverse Board of Directors with 15 board members, 9 of which are independent and with female representation of 33%.

Finally, I would like to highlight that our progress has been recognised externally. We have been included on the prestigious CDP A-List for the 8th consecutive year for our leadership in climate action and we have been ranked 1st worldwide in the World Benchmarking Alliance's Digital Inclusion Benchmark.

7. ESG leaders with well well-defined targets

Telefónica has set robust targets to underpin our ESG commitments, and we have summarised the main ones on this slide.

- We will reduce our carbon footprint by becoming net zero in Scope 1 & 2 emissions in our main markets by 2025 and across our whole footprint and our value chain by 2040. By 2030, we will be using 100% renewable energy in every market we operate.
- We have made tangible commitments to become a zero-waste company by 2030. We plan to reuse 90% of customer premise equipment by 2024; recycle 98% of waste; and introduce ecodesign criteria in all our branded equipment by 2025.
- We have also set objectives to monitor how we are contributing to the decarbonisation of other sectors by enabling our customers to avoid emissions via digital services and choose sustainable products and services.
- We will bridge the digital divide by promoting digital inclusion, with 90% to 97% connectivity in rural areas in our main markets by 2024 and we have committed to train at least 100,000 people every year in new digital skills.
- We will promote gender equality by eliminating the pay gap by 2050 and achieving parity at the highest levels of the business by 2030.

Finally, we align our remuneration to ESG metrics, accounting for 20% of all employees' annual variable pay and an additional 10% of senior executives' long-term incentives.

I will now hand over to Ángel to go through a detailed review of the business performance.

Ángel Vilá – *Chief Operating Officer*

8. Spain | Customer Customer-centric model leads to high cash conversion

Thank you José María. Moving to Spain on slide 8.

Commercial activity improved in Q4, supported by a y-o-y improvement in churn to its lowest level since the second quarter of 2017, and record levesl of customer satisfaction. Convergent ARPU improved sequentially to €90.4, leading to an ARPU in the second half of the year €1.4 higher than that of the first half.

We further strengthened our market positioning during the quarter; we acquired "La Liga" content for the coming seasons at a lower cost, and launched "Fusión Digital Pymes", a digitalisation solution that enable capitalising on the European Recovery Funds in the SME segment of the B2B sector.

On financials, Q4 revenue growth improved y-o-y to +0.5%, and OIBDA annual decline was reduced to -3.4%, on captured efficiencies mitigating higher energy costs and higher costs from strong sales in IT and handsets.

Worth to note is the voluntary redundancy plan implying a provision of €1.4bn in Q4 personnel expenses, with a positive impact on cash flow from 2022 and an annual run-rate of savings of around €200m from 2023 onwards.

Once again, cash conversion stands out, with an organic OIBDA-CapEx margin of 27% in 2021.

Finally, we are announcing today that T. España is ready to launch in conjunction with T. Infra the process to create a FibreCo focused on lower density areas targeting more than 5m premisses passed and open a substantial minority stake to potential investors.

9. Germany | Strong FY 21 growth momentum

Moving to Germany, we continue to have strong commercial momentum, underpinned by the O_2 free portfolio and network parity resulting in over half a million contract net additions and ARPU growth in the quarter.

The 3G switch-off was completed in 2021 and the energy efficiency ratio of the network improved by 78% compared to 2015. The 5G network covered 30% of the German population by the end of the year.

Looking at the financials, this commercial momentum has driven continued top line growth of +3.1% y-o-y, with OIBDA expanding by +4.0% y-o-y in 2021.

The company's 3-year investment for growth programme passed its Capex peak in FY 21, resulting in an OIBDA-CapEx margin of 14.7% in 2021.

10. UK | Extending network leadership and commercial strength

Moving to Virgin Media O2, which completed its gigabit rollout on time across its 15.6m premises passed during Q4 and is now the biggest contributor to the Government's broadband target. 5G is also now available in more than 300 towns and cities and remains on-track for 50% population coverage in 2023.

As part of VMO2's ambition to roll out full fibre further and faster across the UK, Liberty Global and ourselves have initiated discussions with a number of potential financial partners regarding the creation of a network build joint venture. The focus of the entity will be on building a full fibre network of up to 7m premises in new greenfield areas by the end of 2027.

Commercial momentum remained strong with the total base growing+ 5% y-o-y to reach 56m at the end of 2021, driven by FBB accesses growing by +3% y-o-y to 5.6m and the mobile contract base growing by +2% y-o-y to 15.9m.

Looking at the financials, revenue was broadly stable in the fourth quarter, whilst OIBDA growth has slowed due to the return of some sales and marketing costs, as well as increased investment in growth drivers.

In 2022, VMO2 expects to deliver mid-single-digit growth in pro forma transaction adjusted EBITDA, (before cost to capture), supported by improved top-line growth and the delivery of synergies, so that the cash distribution to shareholders is anticipated to be £1.6bn.

11. Brazil | OIBDA growth offsets cost inflation

Moving to Brazil on slide 11.

Vivo finished the year with outstanding commercial and financial results.

In mobile, contract accesses grew +8% y-o-y, improving the customer mix and lifetime value.

In fixed, FTTH reached 4.6m connections, an increase of +36% y-o-y as we expanded our fibre coverage in the most valuable areas across the country through organic deployment and via FiBrasil.

Looking at the financials, we posted simultaneous y-o-y growth in revenues and OIBDA, with fixed revenues growing for the second consecutive quarter and efficiencies offsetting high levels of inflation.

On ESG, we continued to make good progress this quarter, demonstrated by the inauguration of our first biogas facility and being ranked as the top telco in the Latam DJ Sustainability Index.

Finally, after receiving final approvals, the acquisition of Oi´s mobile asset is almost complete and will allow us to further improve the quality of our mobile network and reinforce Vivo's market leading position.

12. Tech | Accelerating our sustainable fastest fastest-growing business

Moving to slide 12.

Telefónica Tech, our sustainable focused fast-growing technology company, delivered superior revenue growth throughout 2021.

Revenue almost reached €1bn in 2021 as growth accelerated to +50% y-o-y in Q4, driven by improving organic trends and further enhanced by M&A operations executed along 2021.

T. Tech, as a leading integrator of technology with strong operational capabilities, is already benefiting from the recovery of the economic activity and the digitisation projects post COVID-19, proven on the better revenue performance in the second half of 2021.

T. Tech has delivered on its priorities, outperformed the market, enhanced its capabilities and scale and improved its growth profile towards higher value services.

Looking forward, a solid increase in sales well above revenue growth makes us predict a strong performance for 2022.

13. Infra | Growth and optionality ahead

Moving to slide 13.

Throughout 2021, Telefónica continued to focus on pursuing value creation opportunities and enlarging its infra portfolio.

In Germany, UGG launched operations in six federal states and in Q4 accelerated the MoUs signed with municipalities, representing more than 170k premisses passed.

FiBrasil is on track to reach its deployment target, with 2m premises passed in 2021.

ON*NET Fibra Chile continued its accelerated rate of deployment, reaching 1m additional premises passed in 2021.

In Colombia, InfraCo received all necessary regulatory approvals and the transaction closed in January 2022.

We continue to explore alternatives to crystallise the value of our infra assets and look for growth opportunities, while assessing our optionality across all asset classes. This was demonstrated by the acquisition, together with

Pontegadea, of KKR's stake in Telxius cable at the beginning of the month, reinforcing our ownership in an extremely relevant asset.

And, as I previously stated, we have initiated processes for the establishment of fibreCo vehicles in UK and Spain.

I will now hand over to Laura to take you through our Hispam operations and financial position.

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

Hispam | Growing profitably in value

Thank you Ángel.

Moving to Hispam on slide 14.

Our strategy continues to bear fruit:

- Firstly, we accelerated value growth throughout the year, with outstanding performance in contract, UBB and pay TV.
- Secondly, we are implementing incremental and progressive operational synergies, thanks to digitalisation and simplification of our new operational model, creating a leaner and more efficient company.
- Thirdly, we continue to modulate our exposure to the region, reducing capital employed by -22% y-o-y.
- Finally, despite the tough macro and competitive environment, revenues, OIBDA and OIBDA-CapEx increased in both reported and organic terms.

Significant debt reduction on strong FCF and inorganic measures

Turning to slide 15, our net debt has been reduced by €9.2bn y-o-y to €26bn at the end of December 2021, or €26.3bn including post-closing events. Thanks to resilient free cash flow generation of €2.6bn, coupled with the completion of strategic and inorganic initiatives, namely the sale of Telxius towers and the VMED O2 UK JV.

The Net debt/OIBDA ratio is now 2.59x, -0.2x below the 2020 ratio.

Looking ahead, we are well covered. Our liquidity cushion amounts to €24.6bn and the average debt life is up to 13.63 years, placing us in a comfortable position given maturities are covered beyond 2024.

We have remained active as well in managing our debt, with financing activity of €12.8bn in 2021 and 2022 year-to-date, including the financing of JVs such as German fibre, VMO2, FiBrasil and Cornerstone operations. We remain committed to ESG financing, which we plan to increase to over €10bn the coming years. We have recently completed the refinancing of our main syndicated facility of €5.5bn which is now linked to sustainability objectives.

I will now hand back to José María who will wrap up.

José María Álvarez-Pallete– *Chairman & CEO*

2022 outlook |Driving returns through growth

Moving to slide 16, we are ready to commit for 2022.

Our guidance includes 50% of VMO2 in the UK, as it better reflects the reality of the Group and provides a more comprehensive evolution of Telefonica's managed businesses. UK is a core market for us, and as such, we devote resources to this core unit.

We guide for "low single digit growth" in both revenues and OIBDA, a step forward from the 2021 upgraded guidance, in spite of added inflationary pressures. In terms of investment, and even including the JV in the UK, we stick to our guidance of up to 15% CapEx to Sales. Investment peak remains behind.

We will push for revenue growth in all our geographies, with main growth drivers in Spain and Brazil stemming from lower margin activities such as IT, new digital services and equipment. OIBDA performance will on top be more back-end loaded. In some regions inflationary pressures will be more evident in the first half of the year (such as energy costs in Spain), though we will continue to accelerate efficiency generation to offset those. Additionally, synergy realisation in UK and Brazil would add to OIBDA growth as they ramp through the year.

We will continue to closely monitor the macro situation and to manage our resources according to the evolution of the pandemic and potential new restrictions, but we think we have left behind the worst economic impact.

On dividends, we are announcing €0.3 per share for 2022, payable in cash, in two tranches, December 2022 and June 2023. We believe reasons that justified the voluntary scrip dividend implemented in 2020 have been mostly left behind, whilst we are very confident in our FCF sustainability. As I said before, we are proposing to cancel 2.41% of treasury stock held as of December 2021. And we may as well consider using excess FCF to tactically buy own stock.

Return to value accretive growth

To recap, please turn to slide 17.

First, in 2021, we delivered successfully against our strategic priorities, reinforcing our position in our core markets, reducing exposure to T. Hispam, creating value and capturing growth opportunities through T. Infra and T. Tech and significantly reducing debt by streamlining our operations and delivering robust FCF.

Second, we successfully met our full year targets, which were upgraded at our Q2 results.

Third, investments during the last year have allowed us to deliver best in class CapEx to Sales ratio, with enhanced UBB experience, whilst promoting inclusive connectivity.

Fourth, positive momentum continued in Q4, with growth in revenues and OIBDA and sequential improvement in free cash flow.

Looking forward, we are confident in the outlook for 2022 and we are pleased to announce a dividend of €0.3 per share in cash.

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

Q&A Session

Georgios Ierodiaconou - *Citi*

In terms of the OpEx phasing in Spain for 2022, you gave some indications of the negative impact in the third quarter. You seem to have managed it better in the fourth. I think it would be great if you can give us an indication of how we should think about it in 2022 in light of the movements we're seeing in the energy markets as well?

And the second question linked to that is more on the top line in Spain. You mentioned during the presentation that Telefónica Tech is getting some of the benefit from what I understood in the European Recovery Fund. But I'm just curious if you can give us an update on what to expect on that front during 2022 with regards to Spain, and Telefónica Tech? I know one of your competitors are optimistic about the impact they expect to see. So I'm curious to hear from you

Ángel Vilá – *Chief Operating Officer*

Let me take you on how we see 2022 in the OpEx phasing that you were talking about, but also a little bit on the outlook. As always, this should not constitute a guidance because we do not guide on specific geographies but, yes, we can give you some colour on the trends we see.

First of all, in terms of how we see the market, we think it will continue to remain competitive in the low end, but rational in the high end. We expect our commercial traction to continue sequentially improving, as you have seen in this fourth quarter. A little bit less so in the first quarter because we just increased or did a "more for more" movement that always comes with more muted commercial activity. But later in the year, the commercial trend, we expect to continue moving forward. And accordingly, we aim for slightly growing revenues in Spain.

The main growth drivers, and this partially is linked to your second question, one would be B2B where we see continued momentum in IT growth. And as I was saying in my speech, we are launching specific products for digitalisation of SMEs, which is a substantial part of what we expect to be European Recovery Funds disbursed in 2022 in Spain. Also handset sales or equipment in general, we see that they should have traction in 2022 based on our new offer of mobile Fusión with handset.

ARPU erosion should be lower in 2022 y-o-y and continuing the trend that we see in q-o-q, clear growth in digital services. This revenue growth, when you look at equipment and you look at some of the digital and IT services, comes with a lower margin. So, we estimate margins in Spain to be in the high 30s for the year 2022.

And, this links clearly with your question on OpEx phasing, we expect performance to be a better in the second half than the first half. Several things are underpinning this expectation:

- from a commercial standpoint, as I was saying, a tariff repositioning in the first quarter will imply that we could have a muted quarter, but then this will improve the second half.
- The margin will be under pressure from energy prices. We are factoring in the first half significant or relevant impact on this, which will annualise from the second half, geopolitical situation allowing.
- Efficiencies in personnel will start from February onwards,
- And in the final part of the year we'll have also the benefit from the new La Liga deflation in content costs.

  So, we expect the second half to have better traction in the first half. And with respect to CapEx, you should expect a similar weighting to 2021.

I hope I've covered the moving parts that you were interested in, in the OpEx and also a little bit on the top line in B2B.

Georgios Ierodiaconou - *Citi*

If I could ask one quick follow-up. I know you don't give guidance, but assuming no major shift in the market, and I appreciate there's uncertainty around energy prices, is it realistic to expect OIBDA to be flattish before the end of this year? Is that not achievable under some type of circumstances?

Ángel Vilá – *Chief Operating Officer*

I commented that we expect slightly growing revenues and margins in the high 30s, so one can do the multiplications.

David Wright – *BofA*

Thanks for the very comprehensive presentation on ESG. Just on your comments José María, on excess free cash flow to buy back or to potentially consider buybacks. You've obviously got the VMO2 recapitalisation due earlier than expected, I think. That was announced a few days ago, and obviously, that would benefit your free cash flow this year. Is that the kind of excess free cash flow that you're defining here? Or could we be talking about excess free cash flow from asset sales, for instance? When you talk about excess free cash flow, could you just elaborate a little on what that comprises?

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

I consider this more from a conceptual point of view. We are comfortable with our balance sheet, we have reinforced equity significantly, we have reduced net financial debt, we are fully committed to maintain our solid investment grade rating. And within all of that, if there is excess free cash flow, which could be from dividends from our JVs, it could be from potential tax impact upside, it could be from inorganic deals (although, as you know, inorganic deals have not been driven by net debt reduction, but more for strategic value creation), we could devote that excess free cash flow as a complement to our shareholder remuneration. So that would be the point.

So far in previous years, and mainly in 2020 and 2021, with a scrip dividend payment, free cash flow has been devoted to deleveraging.

David Wright – *BofA*

Thank you for that Laura. And if I could ask to just my second question.

José María, in your concluding remarks, you talked about some synergy impact from Brazil and the U.K. to support growth through the year. So just to clarify, there's no sort of synergy from Brazilian consolidation in the guidance. I'm pretty sure there is not. And then when could you expect that deal to be complete? And should we expect you to come out and amend guidance on the back of that?

Thank you.

José María Álvarez-Pallete– *Chairman & CEO*

I will frame out the question and I will hand it over to Ángel for more detail. But the answer is, yes, we are including synergies coming from the Oi acquisition in Brazil, as well as the synergy realisation in the U.K. For more detail in Brazil, I hand it over to Ángel

Ángel Vilá – *Chief Operating Officer*

Yes, we finally managed to align all those stars that had to be aligned, and we got all the approvals necessary for the Brazilian deal. We expect to close the deal in the first half of the year, we expect it to be as soon as possible within what is left of the first half of the year.

As our colleagues in Brazil stated in the conference call yesterday, we will provide the full detail on the synergies' estimations once we have closed the deal. Now the process of the split of the Oi mobile asset into three sub-assets, one to be acquired by each one of the players, is taking place. So, we prefer to have the final full detailed picture of the assets to be bought. Also, there are customary price adjustments to what we pay. So, when we have the full detailed picture, which, again, we'll do as fast as possible within what is left of the first half of the year, we'll provide.

In the past we have had substantial cases in Brazil where we have announced, delivered and overdelivered the synergies that we announced. It was in the GVT transaction, also when we combined Vivo with Telesp after acquiring the 50% of Portugal Telecom. So, a track-record of delivering synergies and in the previous cases that I mentioned, overdelivering the synergies are already on our track record.

David Wright – *BofA*

Could I just clarify. I'm maybe misunderstanding and I apologise, but your guidance sets constant perimeter of consolidation. What you're telling us that there are synergies from Brazilian deal in the guidance?

José María Álvarez-Pallete– *Chairman & CEO*

Yes, because we are not changing the perimeter, it is still Vivo. I mean, we are acquiring customers, and we are acquiring spectrum. We are not acquiring a company.

Luigi Minerva – *HSBC*

The first one is on your announcement about the FibreCo in Spain. And I just wanted to just understand, in principle, whether you think that there is value in setting up these frameworks with minority investors only when the new footprint to deploy? So essentially, what is the rationale in focusing it on the rural areas? Is that because you want to deploy more there, and that's why you are welcoming minority investors?

And more broadly, I was wondering what is the end game with these fibre structures that you are putting in place? Do you expect eventually to be completely out of these fibre vehicles? Or perhaps medium-term, you would like to buy out your co-investors? I presume the answer is different depending on the markets, but I leave it to you.

Ángel Vilá – *Chief Operating Officer*

We are setting up the FibreCo in Spain in the format of a regional FibreCo in low-density areas and not proceeding with other fibre projects in Spain. We are doing this because we think it would create the most attractive project for Telefónica and for potential investors.

It's an industrial project, not a financial engineering one. It's a project that aims for growth. So, this would be a growing FibreCo, which is targeting still unbuilt areas. In these areas, there is a lower (or even absolutely low) risk of overbuild, and as a result, the FibreCo should have higher percentages of take-up of premises.

It's also a project that would be eligible for fibre subsidies from the European funds and others. Of course, it will benefit from Telefónica Spain´s know-how in building and operating fibre networks, also Telefónica Spain being the anchor customer of this company.

We are building it with a partial brownfield contribution and then a greenfield build to reach in excess of 5m premises passed. With this initial brownfield contribution, the company has a cash flow profile that will allow potential investors to leverage their upstream Bidcos while keeping a controlled level of debt at the FibreCo itself because we plan to continue to consolidate accounting-wise that FibreCo, and we do not want to contaminate the parent's balance sheet nor the ratings.

And very importantly, this FibreCo will be born with the ambition to trigger consolidation and rationalisation of the altnet FibreCo space in Spain.

So, we think that this, alongside with the FibreCo we're launching with Liberty and VMO2 in the U.K., these are the two most attractive projects for infrastructure investors nowadays in Europe.

As you were asking, our FibreCos that we have in Germany, in Brazil, in Chile, in Colombia, now in the U.K. and Spain, are aiming for growth and investing in areas that are still uninvested because we think that it's the way to continue progressing in our infrastructure. We are the absolute leaders in fibre in Europe, and José María was explaining our position of leadership in fibre globally, but we also are mindful of the return on capital employed.

Regarding the end game, you saw in the slide in the presentation, the portfolio we are building of different FibreCos, and for us, fibre is the technology of the future. All options will be open, but these are very attractive valuable FibreCo assets, whereby third-party investors will have put an objective level of valuation for each one of them. So, we are creating value, we are creating growth and at the same time, we are doing it very mindful of the return on capital employed.

Pilar Vico de Haro – *Credit Suisse*

I have two on my side, please. So first, I had a question on the customer mix in Spain. You have previously given a number of mix of low mid high-end customers in your retail base. Can you please provide an update on that? And could you tell us how much is O2 out of this mix and the impact of the 16 Fusión product? So what would be the percentage of convergent customers now on O2?

And second, you announced the creation of the FibreCo in Spain for low density areas. So what is your thinking regarding the creation of a FibreCo for your entire Spanish business? Is this now off the table with today's announcement? Or is still something that you would consider?

Ángel Vilá – *Chief Operating Officer*

On the mix of the convergent portfolio, we stopped disclosing this mix because we realised that what we were qualifying as high, medium and low value would not correspond to what would be the corresponding ARPUs with respect to our competitors. So, what we would be calling medium or low value would be the average ARPU of our following competitors. So, we were kind of giving some commercially sensitive information to the market and creating a categorisation, which was not consistent with the rest of the players.

What I can say is that the convergent value mix is being supported by our strategy of combining more products in the bundle, including, for instance, the handset offering, the fibre speed, the data, the content, also with new B2C digital services that we are including as an ecosystem. There is, yes, some polarisation in the market. So you should assume that in the higher end we continue to have higher traction compared to the rest of players and the low, which is very competitive, are polarising more compared to the medium.

But in the end, you can see the blended result in the sequential increase in ARPU. In the reduction in churn: we have 1.4%, it's the lowest since 2017. We have the highest Net Promoter Score, and we have widened the gap with our competitors.

Regarding O2 it has been contributing to the base positively, both in fixed broadband and in mobile postpay. So this is increasing our weight in what we used to call the lower end of the spectrum.

With respect to the FibreCo, José María, if you want to comment on that one?

José María Álvarez-Pallete– *Chairman & CEO*

The FibreCo that we are announcing today, the FibreCo we are executing in Spain, all other projects are finalised or postponed; so this is the fibre project in Spain.

Fernando Cordero Barreira - *Santander*

Thank you for taking my two questions. The first one is more on the, let's say, in the short term. And I would like to understand how do you see the wholesale revenue flow evolving in the Spanish market, and you have already given some guidance on the whole Spanish operations? But just to understand how the wholesale has and could be evolving considering there's some deceleration that we have seen in the fourth quarter?

And also the second question with a more longer-term view and coming back to the discussion on the end game on the different FibreCos. You're already having right now, let's say, different JVs or different potential dividend sources in the future. And I would like to understand, although it is not going to be a fact in the short term, given the capacity effort. But what is your outlook or what is your expectation regarding the potential dividend flow to come from the different FibreCos that you are having right now in Chile and Colombia, in Brazil, in Germany? So in that sense, trying to understand what could be the potential contribution to the free cash flow, also considering the increasing relevance of dividends from JVs.

Ángel Vilá – *Chief Operating Officer*

With respect to wholesale revenues, we expect them to remain rather stable in 2022. We have growing MVNO. We continue to see traction in the fibre wholesale. Important with pandemic becoming an endemic, there should be further roaming activation. And on the contrary, we will have, in the same way that we have lower content cost from La Liga, lower resale of TV revenues compared to the season where we had the full La Liga content to be resold.

And with respect to the cash flow profile of the different FibreCos, now they are in the investment phase, and second, as you can see in the slide where we have described the FibreCos, slide number 13, we have different levels of ownership of this FibreCos.

- UGG, which is 50% owned by Allianz and 50% owned by Telefónica, split between Telefónica Infra and Telefónica Deutschland. This is fully ringfenced from the parent, financially, rating-wise and so on, and it's in the investment phase. So, it's a company in which we are still for some time in the investment phase.
- FiBrasil, which is 50% CDPQ and the other 50% split equally between Telefónica Brasil and Telefonica Infra, is a company that was created with the contribution of brownfield, partially did an acquisition and the rest is being financed mostly from the funds contributed by CDPQ and leverage, and Telefónica Group contribution was the brownfield we did initially. So again, it's ringfenced. It's not cash consuming. For us, we should not have additional contribution.
- On the Chilean and Colombian FibreCos, KKR is leading those companies. We are a minority shareholder.
- With respect to the Spanish FibreCo we are announcing today, as I said, it will start with significant brownfield contribution that will be cash generating from the beginning. And it will be able to access fibre development subsidies. So, this is not going to be cash consuming for the Group in any significant way.
- And in the greenfield JV 50-50 in the U.K., it's early days, we need to see in the discussion with potential investors, what will be. But in the scenarios that we are designing the equity ticket is quite limited for the promoters: Liberty Global and ourselves.

These will be assets that will need to develop over the coming years. Here, we are looking at this stage to capture growth and to improve even further the leadership positions that we have in UBB in several of these markets. So, it´s still early to say and to project cash flow distributions from these companies.

Stan Noel - *Bernstein*

I've got two questions. The first one is about your portfolio strategy in the presentation. You showed quite a long menu of infra optionalities. You had a slide on the different CapEx. I assume you're still working on reducing exposure in Hispam. Maybe can you remind us what is your portfolio strategy? And what are your top priorities?

And the second question is about the open letter that you published in the Financial Times last week, along with the other European telcos, along with other CEOs. In this letter, you're asking for the network investment burden to be shared in a more proportionate way with the few digital content platforms who account for the majority of traffic on your network. I was wondering what kind of, what specific business model do you have in mind to implement? And what's the likelihood that regulators will allow you to go ahead?

José María Álvarez-Pallete– *Chairman & CEO*

On the strategy, we remain very focused on the 5 pillars of action that we announced back in November '19. The first one, focus on our four core markets being Spain, Brazil, the U.K. and Germany. Reducing capital or optimising our capital exposure to Latin America. The third one being Telefónica Infra. The fourth being Telefónica Tech. And the fifth being a leaner, more digitised operational model. So, we stick to what we announced back in November '19. And everything we do you should frame that on those 5 pillars of action.

And therefore, we have been accelerating the execution over the last 2 years in spite of COVID, and we are really, really focused on that.

And in terms of the overall regulatory situation, of the overall regulatory view, COVID has accelerated digitalisation everywhere. And in fact, data volumes have been growing 50% recurrently y-o-y. Out of that growth, more than 70% is coming from video streaming and is coming from social networks. And therefore, what we are saying is that in Europe, mainly, the pressure on investment, the pressure on returns and the pressure on cost of capital needs an urgent decision. Europe needs an industrial policy.

And therefore, I think the way to measure relevant markets is wrong. I think that now we are no longer competing with a traditional ecosystem. We are competing with an enhanced and amplified ecosystem.

I'm going to give you an example. In the case of Spain, we are supposed to be a dominant player in the pay TV market because according to the local regulator, there are roughly 6m pay TV customers in Spain, and we have more than 50% of the market share. The reality of the Spanish market is that there are more than 8m additional pay-TV customers coming from streaming platforms. And therefore, the total market size is not 6m. It's more than 15m and therefore, we are no longer the dominant player. And we have some restrictions, several restrictions on our commercial offer.

So, our position is that time has come for a change, that we need to be aware that the European sector needs a revamp. And that revamp means that this famous consolidation of 4 to 3 is no longer 4 to 3. It might be 100 to 99. So that's our position. And I think that COVID and the pandemic has accelerated this controversy, has accelerated this anomaly in the market.

So that's our position, and that's where we see regulators' mindset evolving.

José María Álvarez-Pallete– *Chairman & CEO*

I hope we have been able to provide you enough information through the slides and through the Q&A session.

In any case, should you have further questions, please contact our IR department. Thank you very much for your interest in our company. Thank you.