

13-Aug-2020

Deutsche Telekom AG (DTE.DE)

Q2 2020 Earnings Call

CORPORATE PARTICIPANTS

Timotheus Höttges

Chief Executive Officer

Christian P. Illek

Chief Financial Officer

OTHER PARTICIPANTS

Ulrich Rathe

Jefferies International Ltd.

Christian Fangmann

HSBC Trinkaus & Burkhardt AG

Georgios Ierodionou

Citigroup Global Markets Ltd.

Joshua Mills

Exane

Polo Tang

UBS AG (London Branch)

Andrew Lee

Goldman Sachs

MANAGEMENT DISCUSSION SECTION

Timotheus Höttges

Chief Executive Officer

BUSINESS HIGHLIGHTS

Opening Remarks

- I think it's the big picture there, Hannes called it out in the prep call today showing that we are well on track both sides on the Atlantic, given the highlights of our very strong H1 results
- As usual, my overview will be followed by Christian and he is going then into the details
- I think this was a very special quarter
- We incorporated Sprint's operation and we created the new T-Mobile
- And with the new T-Mobile, we create the new Telekom
- We entered a win-win agreement in this quarter with Softbank, creating a big option value for Deutsche Telekom shareholders going forward, and we delivered operationally on a very strong basis despite COVID
- And I hope you have compared our numbers with the competitors' numbers
- I'm really proud about my organization and how we performed

EBITDA and Investments

- We delivered headline growth in – both inorganically anyhow and organically, commercial growth and strong earning growth

- And we're ahead of our large European peers on EBITDA
- In the US, we overtook AT&T in branded customers
- And outside of the US, our organic EBITDA grew by 4%
- We maintained our high investments and we took big steps towards 5G leadership on both sides of the Atlantic; I'd love to go into that one later on
- Despite COVID-19, we reiterate our full-year guidance for ex-US EBITDA, which we handed out to you before COVID and with regards to the FCF.
- And we are also able to provide strong full year guidance for the whole group, including the new T-Mobile

Employee and Customer Satisfaction

- I'm also really happy that we are seeing record employee and customer satisfaction [indiscernible] (0:02:57) double-digit growth
- And outside of the US, we had the highest employee satisfaction ever measured
- Customer satisfaction is also up through record levels in Germany and elsewhere across our footprint, and this is a good message, people really appreciate the work we have done so far in this COVID crisis providing good connectivity, very stable, resilient services

Sprint Merger

- Move on to page 4, and the Sprint merger, which is putting us into a total different league
- First, in the US we have now overtaken AT&T in terms of branded wireless customers
- Second, we have the best spectrum position
- You know that
- It is a spectrum deal and we will build the network on this basis to the best infrastructure in the US.
- And we have confirmed \$43B of synergies and obviously we are trying to beat this estimate
- I think it's even very good to see how this new team around Mike Sievert is coming together and the great spirit which this team has working remote but executing along every KPI which we had laid out pre-merger

New Deutsche Telekom Post-Merger

- Slide 4 shows a few key stats of the new Deutsche Telekom post-merger
- We are now a €100B turnover company
- We are providing an annualized EBITDA close to €40B.
- Our balance sheet is now €270B big and we employ 230,000 people across the globe
- And we look forward to huge benefits and future returns from this transaction for Deutsche Telekom's shareholders

H1 Year Financial Performance

- Let's look at quick summary of our H1 year financial performance on page 5
- Headline financials are up strongly, boosted by the first-time consolidation of Sprint
- That said, organic revenues were stable year-on-year and organic EBITDA was up 8.6% in H1
 - I think this is a unbelievable strong number comparing that most of our competitors are suffering big time due to the COVID crisis
- FCF was up by 19.6% year-on-year and all segments contributed to our strong EBITDA growth, with one small exception, our T-Systems unit, which was not able to mitigate corona-related headwinds completely

KEY INVESTMENTS.....

- On page 6, we show some of our key investments outside of the US.
- We call it the flying wheel, which is going on

Germany

- In Germany, we now cover 35.5mm lines of fiber of which 1.8mm was gigabit connectivity
- In the EU, we passed 6.3mm with gigabit-capable lines, bringing the total footprint including Germany to 8.1mm
- And we now have almost 0.5mm lines on super-vectoring, up 4 times in the last 12 months
- We entered a benchmark agreement with the city of Münster to our FTTH toolbox and that is the way our partnership's going on
- We further improved our service KPIs

FIRST CONTACT RESOLUTION RATE

- Our first contact resolution rate, which is our most important KPI for service, is up more than a quarter in the last 12 months
- Complaints are down by almost half
- T-Mobile won the J.D. Power customer care award again with the highest score ever seen

MOBILE NETWORK LEADERSHIP

- And we keep investing in mobile network leadership and we have geared up in 5G, I come to that on the next slide
- I always promise that we are taking over 5G leadership at all our markets
- And when we spoke last time I think we hide it a bit our plan for Germany
- Remember, I said, look, let's see what we are announcing for the year
- But now we can talk about it
- We are now covering half of the country with the full three carriers of 2.1 gigahertz spectrum

FREE SPECTRUM

- Very silently we have bought spectrum, free spectrum, from Telefónica, 2.1 gigahertz, deployed that on our infrastructure across the country and we are now able to provide this coverage all over the places without building new sites
- And on top of that we are building leading 3.6 gigahertz coverage
- So, we are just accelerating our build-out by using 2.1 gigahertz, the free spectrum, and in addition over time when we get the approval for all the new rooftops and towers we will increase our 3.6 gigahertz coverage on top of that
- And with this, we will more than double provided speeds for our German customers already by the end of next year
- And as you know, this is the way ahead for our German peers
- I'm very happy and very proud about the technical team of Germany who made this silent strategy live and that we have now an advance of four to five times more coverage than Vodafone and even in significant advantage when it comes to speed

T-Mobile US

- Last week, you heard T-Mobile US talk about the great progress we are making
- T-Mobile US achieved a world's first by launching standalone 5G nationwide last week, and TMUS already covers over 250mm POPs with 5G in 600-megahertz area. 5G in 2.5 gigahertz has been deployed in eight markets, and there we see average speeds of 300 megabits per second
- And as you also heard on their call, T-Mobile is upgrading sites to 2.5 gigahertz at a rate of 700 sites a week

Europe

- We also invested in 5G elsewhere in Europe
- In the Netherlands, we defended our spectrum lead in last month's auction and we already cover 80% of the Netherlands with 5G and aim for full coverage by year-end
- And we are also off to a strong start in other European markets, especially Austria and Poland

Customer Growth

- Looking to page 8, I'd like to draw your attention to our customer growth because this is the basis for what we are
- We are not only a yield company, we are even a growth company
- And we remain strong during the crisis
- Remotely, we were selling more by our service center than ever before
- In our European footprint, we added 1.3mm new converged customers
- And in Germany, more than 15mm homes are served by our fiber products now
- And we saw a solid mobile customer growth on both sides of the Atlantic despite corona, and Christian will give you all the numbers for each of the markets

GUIDANCE.....

- On slide 9, let me explain you our guidance for this year, and taking that in steps
- Our ex US guidance is very simple
- There is no change
 - This is despite the COVID-19 crisis
- We are able to mitigate the headwinds so far, and we believe we can do this for the remainder of the year
- Our group guidance is based on our ex US guidance

EBITDA

- For EBITDA, it was €13.9B
- At the contribution from T-Mobile YTD, for EBITDA based on IFRS, this was €9.5B
- At the midpoint of the guidance, you heard from T-Mobile last week, €11.2B including Sprint
- And finally, we deduct the US GAAP IFRS bridge that we expect for the remainder of the year, minus €0.4B
- For 2020 group EBITDA, this gives you around €34B

FCF and Cash CapEx

- For group FCF, this adds up to at least €5.5B
- And this is after an expected group cash CapEx, no cuts at all, with now €17B of volume, and this is without spectrum
- And again, this is based on the TMUS guidance last week plus an unchanged outlook for Europe
- So, very brave, very committed, and very strong half-year Deutsche Telekom in this difficult environment, beating our competition, and that's enough for me today

Christian P. Illek*Chief Financial Officer*

FINANCIAL HIGHLIGHTS

Revenues

- And let me start with the typical overview on page 11 and highlight some of the financial results
- So, reported revenues were up 35%, on an organic basis, we would have been at negative 0.6% after the 1.1% growth which we showed last quarter
 - And that is very much driven on the top line throughout the COVID-19 crisis

EBITDA

- If you take a look at the EBITDA after leases, this one growth including Sprint by 56% organically
- You see there is a strong 8.4% after the 9% which we showed last quarter
- Our performance also in the ex US is very stable and nice
- On a reported basis our EBITDA grew by 3.3%, organically by 4.1%
- And last quarter we basically reported out a 4.2% growth

FCF, Adjusted EPS and Organic Growth

- FCF has massively improved by almost 60% this quarter and the contribution is coming from both sides of the Atlantic
- The earnings, adjusted EPS were down by 4% this quarter
- And obviously we have a big increase in net debt but we will get into this one in more detail later on
- If we're moving to the next page, you see the organic growth momentum DT ex US and the US and you see that we're showing a very stable progress on both parts of the business

Impact on the Corona Crisis

- So, let me give you also a little bit of an update on what is the impact on the corona crisis which we gave you an overview throughout Q1 results
- And I would say by and large, we're pretty much seeing what we were anticipating
- So, we're seeing a significant impact especially in Q2 when it comes to retail roaming but also when it comes to less visitor revenues
 - And that is very much in line with the expectation which we had

- We're also seeing on the flipside, which is a tailwind effect, that the out-of-bundle revenues especially in Germany and to a lesser degree in other European operations are much higher than we anticipated it to be
 - And that obviously offsets some of the roaming effect
- We're seeing on B2B, I would say a bifocal result
- Obviously the enterprise business of T-Systems is impacted significantly whereas the SMB or SME business is still steady

EQUIPMENT REVENUES AND BAD DEBT DEVELOPMENT

- On the other two impacts, equipment revenues and bad debt development, we haven't seen a lot of deterioration in Q2
- Equipment revenues are down a bit
- On bad debt we don't see anything
- I think we are seeing basically a very much comparable performance to last year's results
- So the key question is now going to be what's going to happen in Q3 and what's going to happen in Q4
- Obviously we have only limited visibility but for the time being, what we're assuming is that we are basically staying in line with that impact which we have shown you in Q1
 - That is also one of the reasons why we're basically reiterating the guidance both on EBITDA and FCF for the business ex-US.

Germany

- Let me move over to the segment performance and start as usual with Germany
- And let's move over to page 13
- What you can see is basically overall revenues grew by 1.1% and the EBITDA growth sees or saw a slight acceleration to 3% but – and that's actually well above our full year target; so from this perspective, very, very nice
- The total service revenue growth accelerated to 1.6% y-over-y
 - This is very much driven by the fixed line performance which we have seen in Q2

Mobile Service Revenue

- Moving to the next page, 14, mobile service revenue declined by 1.1%
- That obviously includes all the roaming effects
- If we would exclude the roaming effect and the visitor effect, we would be close to 2% which would be in line with our mid-term guidance on the service revenue
- Also, if you compare the performance in the previous year with this year, obviously, we had to fight against a strong quarter in Q2 last year, and therefore, we expect that we're going to see a slight improvement in H2 when it comes to the mobile service revenue
- And again, as I said, the guidance which we gave at the Capital Markets Day of 2% remains intact

FIXED LINE REVENUES

- Fixed line revenues were up almost 3% y-over-y, very much driven by the strength of the broadband revenue growth, but also wholesale showed a very strong result
- We talked about the tailwind effects of the out-of-bundle calls
- If you basically carve those effects out, they would qualify for 1.3 percentage points of these 2.9%

- And you see that this is really significant what we're seeing here
- So, we expect this out-of-bundle revenue to stay there, but also what we're seeing is that the momentum is coming slightly down
- So, it's not like it's comparable for example with the March or the April numbers which we have seen

Commercial Performance

- We're moving to page 15
- You see that the commercial performance remains pretty intact
- So we continue to see significant growth in MagentaOne
- We have registered about 110,000 branded contract net adds
- I would say that's an almost normal intake, slightly below that
- The B2C churn remains on a low level at 0.8%
- And also, we're seeing a significant increase on mobile data usage with our contract customers
 - And that 50% obviously supports our more for more strategy
- We have now 3.5mm customers on StreamOn, that is an increase of 400,000 customers since the beginning of the year

Broadband Performance

- Moving on to the next chart on page 16, I think you may recall I was complaining about the broadband performance in Q2 last year and said, okay, we have to improve from here
- This year, I have to reverse that assessment and I have to applaud for the performance of that 87,000
- That is three times the numbers we have seen from [ph] the guys in Düsseldorf (0:18:36) and it's also the second consecutive quarter where we're really well above the 40% net adds share at least according to our analysis
 - And I think this is a very, very strong result
- Also, if you've taken a look at the line losses with negative 62,000, that is pretty much a third of the previous year's line losses
- And I think we looked back into those and we couldn't find a lower number since 2004, and we had to stop at 2004 because we didn't have any further documentation of the previous years

FIBER CONNECTION

- On the fiber connection, we added about 400,000 fiber connections this quarter
- So, that is comparable with last quarter
- The TV performance is okay-ish, but it's really also impacted by the shop closures and the limitations we have once you enter a shop
 - So, from this perspective, I would say it's an okay result
 - But relatively speaking, probably the weakest number on that chart

Retail Fixed Revenues

- If we go on to the next page, 17, you see that the retail fixed revenues have grown by 2%, and that is, as I said, driven by the broadband revenue growth of 5.5% but also wholesale grew of three reasons
- One, there is upselling into higher bandwidth
- The second one, we have seen stronger interconnection revenues

- And I think we have to also bear in mind that the unbundling fee has been increased last year, and that is obviously positively impacting the revenue growth of the wholesale business
- So, overall, I would say a very, very strong quarter from the German team
- We're really pleased also with the consistency how they're executing
- So, I'm confident that we see hopefully a similar result in the upcoming quarters

Mobile Service Revenue

- So, if we're moving to page 18, again, the US and you know that the US has given their Q2 results and also their guidance last week
- In this first combined quarter, T-Mobile reported a mobile service revenue of \$13.5B and an adjusted EBITDA of \$6.9B
- Unfortunately, we have certain pro forma perspective unavailable on IFRS basis, so therefore we have to basically take a look at the absolute figures

Customer Base

- We're moving to the next page, you see how we're executing on an operational basis and T-Mobile continues to grow their customer base also in that combined – with that combined company
- And bear in mind, the Sprint customer base was on a shrinking basis
 - So, I think this has to be also factored into that equation
- So, the team is now working full steam ahead in order to basically combine the company to bring the network to life which we promised, and I think what they already achieved is quite astonishing

SPRINT RETAIL OUTLETS

- So, the Sprint retail outlets have been rebranded by beginning of August. 85%, and we knew that beforehand, of the Sprint customers have a compatible handset on the T-Mobile network
- More than 10% of the Sprint post-paid traffic is already on the network
- We have that rollout of 2.5 gigahertz in eight major markets
- And we ramped up the 600 megahertz rollout to 700 sites a week
- So, from this perspective I think despite all the complications you have with the COVID crisis I think T-Mobile US, the new T-Mobile is really off for a good start

European Performance

- Moving to the next chart, which is the European performance; and the European performance was especially impacted on the revenue side by A, the roaming impact which actually kicked in as anticipated and that is a negative one
- We also had some – a negative revenue impact on the ICT business
- So, that one is also consistent with what we have seen at T-Systems
- And there were some currency headwinds which we had to face which basically qualify for almost – for more than half of that revenue decline
- However, the team was able to basically respond to that top line challenge by rigorous cost management and that helped the European segment on an organic basis to basically show a consecutive EBITDA growth now for the 10th consecutive quarter
- And by the way I forgot to mention this, Germany is now on quarter 15 with consecutive growth

CONTRACT NET ADDS

- If we're moving to the commercials of Europe, I think they are looking very good and solid
- We see a good intake on contract net adds, especially given the fact that the first and the second month of Q2 were really slow and we were really concerned
- But then we had a massive rebound in June, and that helped basically to slow the quarterly numbers
- You know that the European segment is very keen in order to drive customers into a converged contract relationship
 - This is where we have another 265,000 new converged customers, and they're covering now more than 50% of their broadband base with that converged offering
- Again, we had 69,000 net adds on the broadband side, very much in line with the previous year, and we had a slight increase of 20,000 on the TV side
- So, I think very solid performance
- And especially, I'm really confident given the rebound which we have seen in June that we will continue to see good results from Europe

T-Systems

- Now, to the weak part of Q2 performance
- That is T-Systems
- And I think, as you may recall, we said in Q1 call, so who is impacted relatively the most by COVID and we said we expect this to be T-Systems
- Unfortunately, we were right
- So – and you see that impact here now playing out in Q2
- On a 12-month running basis, the order entry is down by almost 4%

REVENUES

- Revenues are down by 3.4%
- The adjusted EBITDA is down on a reported basis by 23% or 21% on an organic basis
- It doesn't matter
- It doesn't move the needle
- I think we have to bear in mind this is on a reported basis €29mm
- However, I think that is – you see that there is a negative impact on their business and we expect that those headwinds will continue
- We're also hopeful that we see some positive signs in H2, but there is one thing for sure we have to accelerate the transformation on the T-Systems side in order to respond to that situation

Group Development

- Group development on page 23; so, what you see is a very strong revenue growth of 4.8%, by the way the strongest revenue growth which we have seen since we established this segment
- Adjusted EBITDA grew by 13.2%, driven by basically three effects
- One is the positive revenue momentum which we're seeing in both business segments, the merger synergies which are kicking in and the T-Mobile Netherlands operations and a lot of other efficiency measures which they have taken
- So, it's a very strong performance which we have seen on the group development segment performance

Dutch Business

- So if we move on to the next page and see – basically drill down on the Dutch business
- Again, the Netherlands are able to grow their customer base despite the COVID-19 crisis
- And I think this is a very good net contract intake
- Also what you see that in a shrinking market – in a shrinking Dutch market, T-Mobile Netherlands is able to grow by 2.3%, also solid broadband net adds and a very, very strong earnings momentum
 - So this is really a very strong result

Tower Business

RECURRING REVENUE GROWTH AND EBITDA

- So next page on towers very quickly, I think we're seeing that we have a continuous recurring revenue growth in the tower business and that also the EBITDA after leases has grown y-over-y
- There is no surprise in that tower business development also relative to the previous quarters
- But we're really happy with the performance of the GD Towers business
- So, that basically gets me to an end of the review of the operating segments and let's move on the group financials on page 26

FCF

- So, as I said, FCF is up by 57%
- That is very much driven also from the cash flow from operations
- And the contribution is actually coming from both sides of the Atlantic
- As you have seen also DT ex US has basically beaten the consensus on EBITDA and obviously it has a positive impact on the FCF

Net Debt and Dividend

- If I'm taking a look to the net debt, the net debt moved from €77B to €121B
- And there is obviously that €44B consolidation effect from Sprint
- I'm getting to that detail later on
- We had in H1 a solid FCF performance and a contribution of €3.9B
- Overall, dividend – of which the German one was the biggest one with 2.8 – it was €2.9B
- And we had spectrum auctions in the US and also in Hungary
 - That explains the €900mm
- And we had some favorable effects coming from the dollar when it comes to the net debt which basically worked in our favor of €1.7B
 - That gets you in that vicinity of €121mm

First Consolidation of Sprint

- If we're moving to the next chart, let me explain to you the first consolidation of Sprint
- So, what you see here, the €44.1B can be basically divided in three sections

NET FINANCIAL LIABILITIES

- One is, what are the net financial liabilities? That's €35B

- Also, we had to add leasing liabilities, which are basically tower leasing liabilities of €6.8B, and that is totally comparable to what you see in US GAAP

LEASE SPECTRUM AND NET DEBT

- And then, there is a different treatment of lease spectrum between the US GAAP and IFRS
- On IFRS basis, you have to basically activate this on the balance sheet, and, therefore, that increases your net debt by another €2.5B
 - And this is what's been shown here that is the 2.5 – the long-term contract of that 2.5 gigahertz spectrum, which we're having in – which we inherited from Sprint
- So – and if we now break down the net debt, you see that the – I would say the net debt prior to leasing liabilities is close to €100B now and that we have another leasing liability contribution of €24B
 - And that translates into leverage ratios, including the leasing liabilities, of 2.9
 - That shouldn't surprise anybody because we always said as soon as we're basically consolidating with Sprint, we're leaving the corridor, and if you take a look at the ex or pre-IFRS 16 basis that would be 2.73

QUESTION AND ANSWER SECTION

Ulrich Rathe

Jefferies International Ltd.



So, my first question would be the TV adds. You mentioned that they were slightly slower because of the shop closures. I'm just wondering why that doesn't affect the broadband intake, so, was the attachment rate lower in the quarter and what are the reasons for that?

And the second question is maybe on the GD Towers business. This is a fundamental question, are these revenues based on actual contracts that are sort of framed in commercial terms? I mean things, like MSAs or is this intercompany transfer pricing that's ultimately decided in the finance department that determines the reporting of these tower revenues and EBITDA. Thank you very much.

Timotheus Höttges

Chief Executive Officer



Okay. Ulrich, I will start with the first part of the question, then Christian is going to the second one. Look, we had this – I think you were referring on the TV adds mainly on the German situation. And it's right that the lockdown was something that people – they were building up their connectivity at home, their Internet services, their speed, but they haven't changed, let's say, as much TV service at the same time.

So, we had this international promotion which we had put out which is the Disney+ app and we were quite successful on the Disney+ with 700,000, around 700,000 additional net adds, and which we have created on this one. But nevertheless I think on the TV side this was not an added service which we were able to provide, it was more about adding speed to the customers here at the German locations.

So, why that was? I think in this situation, people were not willing, let's say, at least to change their entertainment service and even saving some money in this regard, but this is just a guess I have to make here for my – yeah, I do not have the details on why we were suffering here from my end.

Christian P. Illek
Chief Financial Officer

A

Tim, may I add something?

Timotheus Höttges
Chief Executive Officer

A

Please, go ahead.

Christian P. Illek
Chief Financial Officer

A

I think if you take a look to the distribution and how a service is being bought, the shop is absolutely the most important area for the TV business and it's a hard-to-explain product. So, you need to have time in order to persuade a customer. And even as we open up the shops again, you don't have that same footfall in the shops right now as you had it prior to the crisis. And I think that negatively affected the TV net adds; because the strongest channel for broadband is still the call center. Right? So, it's being bought on different channels. And I think I would add this to your explanation as well.

Timotheus Höttges
Chief Executive Officer

A

Excellent.

Christian P. Illek
Chief Financial Officer

A

So, on the tower revenues, very clear, it's based on an MSA. The MSA is being compared with external customers. You can be rest assured that the German segment wouldn't allow to pay more for the services than third-party customers buying for the same service. So, I think it's based on an MSA and it's based on, I would say, market-oriented pricing. And therefore, I think these commercial or the commercial performance, you would see a similar commercial performance if this would be a third-party company.

Christian Fangmann
HSBC Trinkaus & Burkhardt AG

Q

Because I only can ask two, I'll focus on Germany. You had a very strong fixed line performance in Q2, more than offsetting the weakness on mobile service revenue. What are you seeing in terms of trends? Also with respect to the low churn environment which definitely benefited you in Q2, if you looked into early Q3, do you see that low churn environment still benefiting you?

And then looking into H2 from a cost saving perspective, is there anything we need to bear in mind except for the last mile tailwind that is not going to sustain? Q2 was very strong on the EBITDA margin front. And then maybe for Tim, I know it's a two-and-a-half question, but Tim, your view on the TKG novelle, so the telco law amendments and what's your view on the current status, that will be helpful as well. Thanks.

Timotheus Höttges
Chief Executive Officer

A

Okay. Let me start with the broadband stuff here. And look, the first thing what we see here and definitely – and you're living in Germany is that our network is perceived being stable. We have built vectoring, super-vectoring almost now for Germany 90%. We have 80% on our let's say ownership, which we are serving. And customers

were really well-served through this COVID situation, all the home offices, especially in the rural areas, were based on our infrastructure. On top of that, most of the business customers were served via our networks and we had no outage at all in our infrastructure. What we see is a significant improvement, a significant improvement on the customer satisfaction. So, by the way, we haven't seen a jump like this in the history.

Now, on top of this good perception on customer service we are – on the consumer side, we had finished the IP migration. And we're almost close to finish up on the IP migration in the B2B area as well. So, we had no additional churn from this angle anymore which was hurting us. And on top of that one, people are sticking with the reliable brand in the crisis. That is what we see. So, new offers like the ones we have seen from 1&1 like six months for free promotion on the tariffs, they may have resonated with people at the base of the market but not with our – the customer base of Deutsche Telekom. So, they were not that price sensitive on this topic. And all of this were driving churn down. Customer satisfaction up and on top of that us speeding services at the same time.

So, I think this is the recipe which we had. And then on top of that I don't know was it 180% or whatever but our service people approaching customers with new service where we have built higher bandwidth were even quite successful in outbound calling which gave us another uptake on our broadband side.

So, we are now where – I always want to have the company in this 40% range. We achieved that without making services for free, like 6 months for free or 12 months for free or whatever for free. So, but with a reliable product and that's the way which we are planning going forward.

Christian, you can go in the second one and then I'll make the third one.

Christian P. Illek

Chief Financial Officer

A

Okay, just on the fixed line performance because there was a question from Christian whether we expect any changes in H2. So, I think what I said in my presentation already that the out-of-bundle revenue result is coming down a bit. So, we don't expect H2 being as strong as H1. And I think that is one which have to be taken into account.

And another one on a positive side is, we're having a very juicy win-back rate from cable customers right now, which also proves that the performance of the vectoring network and the performance of our overall setup is really attractive to consumers. So, on the – I think if we're taking a look on the cost side on H1, I think we're tracking along the indirect cost reduction targets for this year. You remember the €1.45B across all segments. And I think I would expect that we don't see a lot of changes in H2. But always bear in mind, there is a Christmas quarter. We don't know what's going to happen. So, there's always promotional activities and all this stuff.

So, I wouldn't expect any kind of massive changes on the cost side, on the promotion side. But not everything is being taken into account right now. And the tile rollover is not recurring after H1 because y-over-y, obviously, we had that increase in summer last year so, we don't see that positive effect tile effect replicating in H2. So, I think everything is captured in the reiterated guidance of €13.9B.

Timotheus Höttges

Chief Executive Officer

A

Let me address this regulatory topic and the TKG novelle which is out for discussion. And to frame it, at the beginning, our expectation is that the TKG – the amendment is creating an even – much more investment-friendly and current legal framework for facilitating and accelerating the FTTH rollout.

I think from a 5G perspective, look, more or less the strategic problems are solved. But from an FTTH acceleration build-out perspective, the TKG has a big chance to improve the environment.

I think Germany should use the opportunity for a general reduction of regulation and bureaucracy, especially against the background of the corona crisis and all the economic challenges which we had. I think the network operators who are willing to invest should be relieved from a lot of additional burdens in the TKG.

There are obstacles in the build-out obligations, and there is a law which is in discussion which is an acceleration, which is a little bit less federal system but more central approach to help us to accelerate the build-out. This is a very important piece.

Second, national roaming obligation. I think the EU code sets out very strict requirements on this one. And I think United Internet should invest into their own business. We are open for discussions with these guys, but the current draft version which we have on the table reflects the existing EU codex. So, therefore, I think this is on the right track in that there is no mandatory national roaming forcing us deflating our big investments which we have taken over the last years and finding a commercial agreement with our partners who want to use this structure.

The third part which is important for us [ph] and I think is the right approach (0:43:35). And the current draft reflects the EU codex and includes the removal of [indiscernible] (0:43:40). So, this should happen within the next five years. And I think this is a very important thing because if we want to build profitable FTTH and you cannot access up to 25% of the households in Germany, our profitability is limited by that one. And on top of that, even from an antitrust perspective and a competitive perspective, this is not helpful for consumers. We are challenging the status quo. And this is currently baked into the proposal.

The FTTH regulation itself is reflecting positive [ph] assent (0:44:24) as well. For instance, the switch from ex ante to ex post regulation is part of that or non-discriminatory access regulation is part of that. But I think beyond that we need a much more consequent step going forward with regards to the FTTH build-out when it comes for instance to reciprocity with regard to access fees. So, if we are using the infrastructure of somebody and they're using ours, reciprocity should conclude the same prices of retail price differentiation as an option or non-discriminatory wholesale access regulation. These are pieces where we have to work on details over the last years.

Not everything will be solved by the TKG [indiscernible] (0:45:13). But there is an institution called Bundesnetzagentur who as well can help us beyond that in the framework of the – and so, in principle, a lot of topics addressed but not solving all the issues on FTTH. Yes.

Georgios Ierodias

Citigroup Global Markets Ltd.



Also on Germany, my first question is more around strategy. There's a new head of Germany and I was curious if you could share any initial thoughts or priorities that's really harsh for the business in terms of maybe cost-cutting. And also, I believe some of your European operations have been a bit more active in content historically, I know it may not be the most popular thing nowadays but whether you do see perhaps some opportunity in looking at strengthening your content.

And then the second question is around the 87,000 net adds and outperformance vs. your main competitor. I think you've already given some explanations earlier to [ph] Dominik's (0:46:33) question, but I was wondering if there is any data you could share with us. I believe you don't track NPS, but any customer satisfaction surveys you are doing, whether you are starting to see a shift vs. the performance of your competitors. Thank you.

Timotheus Höttges

Chief Executive Officer

A

Let me start with the first part of the question, and maybe Christian, you might help me then on this one. The first one with regards to Srini, look, for me I'm very happy that our supervisory board came to the conclusion that Srini is the right guy for running the German role. Because it's his proven track record of combining a growth mindset with efficiency which he had shown in the past, not only from his Indian history at Bharti but as well from what he has shown in the European landscape. I think he is so in detail of technology, understanding the capabilities of our efficiency. He is always challenging the status quo and trying to find new ways. Look what he has done from – coming from a mobile carrier in the European environment to a pure TV and even fiber player there and how efficiently he has driven this business.

I think this is qualifying him for taking this bigger role in the German landscape. Now, with regard to his priorities, Germany is very successful. And so, the good things should not be questioned. That is that is for sure. We have made a huge step going forward on the 5G side and the mobile services side. We are leading here the pack significantly and even with the 5G attempt are beyond where we were in the past. We have done a lot of things on the customer service side which is impressive if you see our Net Promoter Scores, our TRI*M's results and the amount of complaints and the costs by the way which came down by less service issues.

We have seen that on the B2B side we are growing in a segment where nobody else in Europe is showing that performance. And we just included the TC part, the telecommunications service part of T-Systems in this one to become even more customer-oriented in this way. These are all questions where he has to deliver and execute on our inhibitions.

I think what he's about is very much about the fiber rollout because the way forward is now after finishing the IP - sorry, the VDSL and super-vectoring build-out we are now focusing on making FTTH as efficient as possible. And we are finding ways of deploying FTTH at larger scale beyond 2mm houses on an annual basis. And the way of doing that, the way bringing this to the customers, the way of growing the segment in this area beyond where we are today in a profitable manner is definitely something Srini's bringing to the party.

The digitization of Germany is another task, which he's driving, which will help us in the customer [indiscernible] (0:49:50) as well in the productivity, which the German organization is working on. And we have commitments with regards to cost-cuttings, which we want to deliver.

And the last thing is we have made so much efforts and so much progress in the internationalization of our group over the last five years that it's now as well – at one point to internationalize Germany and to get this international view on the German entities is another cultural element, which we are driving with this appointment. So, I think the best people for the most difficult and most complex jobs, this is always how you should play it. And this is why he's the best man at that position at that point in time.

Christian P. Illek

Chief Financial Officer

A

Why shouldn't I take the second one on the 87,000? So, first of all, Georgios, I wouldn't say there is anything special about Q2. And the 87,000 is very much comparable with the 83,000 in the previous quarter. We're always arguing that consumers are buying for a number of reasons and not only because of speed. And, obviously, we have over time massively increased our quality in the service, the quality of the proposition. We again won that big test on TV, and also, the performance of our network because we have now about 500,000 super-vectoring

customers. So, from this perspective, and I think the customer is always buying for a basket of reasons and I think that is the biggest supporter.

The second one is, as Tim said earlier on, we don't have any drag from the all-IP migration anymore because it's been finalized. And we're always arguing that there is a structural negative impact coming from the all-IP migration. Once this has been finalized, obviously the numbers have to become better. And we see this since Q1.

The third one is cable migration. We have quite a bit of surprising positive results on cable win-backs. So, it looks like we were discussing with you in the previous quarter that Vodafone is moving a customer from the wholesale relationship they're having with us onto their own network, but not everyone is agreeing to this.

And I think we're taking part of those customers who have been touched and that actually supports our growth as well. And I think there is then the COVID impact. I would sense, I can't prove it, but I think in a time of crisis, consumers tend to turn to the market leader who they trust the most. And I think that is also a positive effect which helps us throughout this crisis.

Joshua Mills

Exane

Q

The first is just related to some comments which Tim made at the AGM in June where you laid out the ambition to have a full optical fiber network by 2030 saying that fiber-to-home is the future for Germany. Has anything changed in your thought process or conversations with the regulator around the ultimate mix you'll have between fiber-to-home and vectoring? Or is this still consistent with the message you've given us before around the fiber factory?

And then the second question, just being more of a technical one, how do you account for the value of your call option for the 45mm T-Mobile shares at \$103 which is now in-the-money? Is that part of your net debt calculations? And second maybe just to check on this, what kind of leverage position would you feel comfortable at executing on that option if you have ambitions to increase your exposure to the US over time? Thanks.

Timotheus Höttges

Chief Executive Officer

A

Okay. Joshua, let me start with the FTTH question. And the first one is our vectoring and super-vectoring discussion which was heavily challenged from the outside world, sometimes even from politicians saying why haven't you started with FTTH alone or only. And looking hindsight, it was maybe the best and most clever decision we have ever taken in history because of the environment. COVID in 2020, we would have provided 80% of the customers with lower than 16 megabits per second or below, and 20% of the people would have had an FTTH service. So, this country would not have worked the way how it did without vectoring and super vectoring.

Now, this comes to an end. We have now – we are now on the vectoring rollout which is all this Amazon - replacements which is more – software change in the [ph] street (00:54:50) cabinet, where we are working on and we can do that, so there is another opportunity for that one. But I want to now bring this company to the next step, into the FTTH leader.

And we always have been the network leader, I think, impressively on mobile. In 5G, we have a clear path on what we want to do over the next years. On FTTH, we have to learn a lot of things.

In the past, we had – this year, we had about €1B investment to pass 500,000 lines. We are focusing on schools, on the subsidized build, on new builds, on business parks. So, these are the areas where we are working on this right now.

But in addition, we have launched new partnerships with Intel, with the city of Münster recently. And on top of that, we are now learning how to gear up the FTTH rollout in a much more productive and efficient way. And that is what I'm trying to do. I want to approach this business unit with a more kind of factory approach. That means get more for the same amount of money.

And we are not providing a new CapEx envelope today for next year; we have provided the CapEx envelope for this year which is consistent to what we have said in previous meetings. We have €8B ex US investments, which we can invest, of which €5.5B are being spent in Germany, a lot of them into the fiber build-out. And I hope that we are now scaling up from 500,000 beyond 1mm into 2mm on an annual basis and learning to deploy that faster and cheaper.

And at the same time, I'm trying to work with politicians to support our way going forward, to say, look guys, if we don't have a business case, we will not invest. And the others are waiting until we are investing. They are not investing on their own. I'm leaving the €7mm commitment from Deutsche Glasfaser at the moment out of sight. But when it comes to the huge landscape of Germany we need another environment of political direction. And this is – I have a lot of open ears on this one. People are considering what they can do and I'm getting more and more optimistic, at the same time we're doing our homework.

Christian P. Illek*Chief Financial Officer*

A

Okay. So, let me try to answer the value of the call option. So, the transaction price of the call option was zero. Therefore, the recognition on the on the balance sheet is also zero. So, there is no net debt increase. But there is a difference between the transaction value and the fair value. And that's roughly €1B and that will be amortized in the P&L under other financial income over the course of four years.

And if there is a massive, massive, massive increase of the T-Mobile share price and the intrinsic value of the 44mm share option is increasing significantly obviously that will have a positive impact on the EPS. So, that's my understanding on how we deal with this.

Polo Tang*UBS AG (London Branch)*

Q

Just two questions, bigger picture questions. The first one is really just on Huawei. We've obviously seen an increasing number of restrictions and bans on Huawei in a number of European markets. So, what's your view as to what will happen in Germany and how would Deutsche Telekom be impacted if there were restrictions or limitations in the use of Huawei equipment?

And the second question is really just a bigger picture question on consolidation, in M&A. So, we obviously had the EC decision to block the Three/O2 merger in the UK in 2016. That was recently overturned by the European General Court. But I'm just interested in terms of your perspective on the sector. Do you think this opens the door to further consolidation across Europe? And do you detect a change in attitude from politicians and regulators on the subject of consolidation? Thanks.

Timotheus Höttges

Chief Executive Officer

A

Okay. Polo, let me try to answer this big picture questions here. Look, yes, we see that let's say for instance the British National Security Council decided that the sourcing of new Huawei could have been – is no longer allowed at year-end of 2020 and that they have to take components out of the system. And so you have seen this week the German IT security institute, we call it BSI, they have published their security guidelines. And there was some bit of press speculation as well. And we have no privileged insight into when the final decision will be taken in Germany. But we don't think anyone is advocating a rip and replace scenario for Germany here as well.

And I anyhow think that it's a little bit over-accelerated, the topic that Deutsche Telekom is exposed, is strategically dependent on Huawei. This is not the case. We are not dependent on any kind of vendor. The question is about, let's say, the time to market of new technologies and innovation, and the question is as well about the economics around that. And I think that the German political situation is on a more neutral stand with regard to the Huawei. They are focusing very much on the security aspects of vendors, by the way, all vendors.

So the IT security, that's something which is on its way going forward. They are really forcing an open RAN in migration. I hope that they even put that into the legal environment because this is helping us big time not only to get more control about let's say all the boxes which we are buying but as well it will help us from an efficiency perspective to disaggregate our infrastructure and clarify a lot of the steering mechanisms here. And I hope you are aware about the open RAN engagement which we are showing here in this system.

We have informed that the German government about where we are using our Huawei equipment. We are not using any kind of Chinese equipment in our current network infrastructure or let's say few which we are rebuilding. We are now talking more about let's say the access nodes and in this case, we are providing both Ericsson and some Chinese equipment for 5G services these days and even the 4G. So that's where we are. And let's see the political position and how this evolves over time. And we are not dependent on any kind of vendor. We have a multi-vendor strategy and 35% by the way of our vendors are coming from the US, 25% coming from Europe, another 25% Asia including China and the rest of the world. So, this is where we stand and I think Germany is having a more neutral stance here.

Christian P. Illek

Chief Financial Officer

A

Okay. So let me basically take on that EU consolidation question. Look, we've...

[indiscernible] (1:03:05)

Christian P. Illek

Chief Financial Officer

A

...we've heard this as well. We have heard Madame Vestager or Breton commenting favorably around a stronger or a consolidation of the EU telecommunications sector. But I recall this very vividly as I returned back to this company in 2015, everyone was talking about this and in the meantime, not a lot of this has happened.

So, I think we're listening to this. Obviously, that was always our point of view that the market is way too fragmented in Europe and that we don't establish scale economics broad enough. But I think we have to be realistic what is talk and what is actually action. And the good point on this one is, I think we have so much growth opportunity besides that question that I think we have a very good future in front of us, whether we get a stronger consolidation, yes or no.

Andrew Lee

Goldman Sachs



I had two. One was on your – firstly on shareholder returns thoughts following your Q2 update. So, we've clearly seen better TMUS performance, you've raised guidance there, faster synergies, and sounds likely now to raise its total synergy guidance. And I just wondered has that changed the timing in which you can raise DT group shareholder returns. How do you think now about the mechanics or the route to upstreaming cash to shareholders? For instance, would you start raising dividends as soon as you hit that net debt to EBITDA ceiling of 2.75 times? Any help on how you think about that would be really appreciated.

And then the second question was just about how you think now about the strategic positioning of TMUS? Do you think it needs a great convergence exposure? Any comments on that would also be helpful. Thank you.

Timotheus Höttges

Chief Executive Officer



Look, very quickly, and Christian, maybe you go deeper into this dividend decision. Honestly, I cannot release any kind of shareholder return thoughts at that point in time. It's too early. We are managing, let's say, this crisis, the integration all at the same time. And we are very happy about the progress we are making, but there is no discussion in the group at that point in time which we can share at that point then with regard to the future remuneration. But we definitely have to understand that. Nevertheless there is one issue on the US. We have the de-leveraging effect which we are driving firsthand. But, Christian, you might add something on this one.

With regards to your – the other question, I think, exposure to convergence, no, the answer is no. And you see that the growth, the integration, the focus on mobile services, the 5G, the fixed mobile substitution opportunities, which we have on our mobile network, the huge capacity which we are providing now to the market, the entry into the B2B market which we are driving, this is, let's say, first priority and these are the low-hanging fruits which we are driving.

Looking to the market environment I do not see so much progress being made on the convergence side and from our competition there. And so that's – we have so much potential to grow in the environment that I would say it's no urgency at that point in time to focus on convergence or any kind of deal with regard to convergence.

Christian P. Illek

Chief Financial Officer



So, Andrew, a couple of perspectives from my side. So, first of all on the shareholder returns on the DT side there is no change at all. I think we continue with what we already communicated. Now, on the T-Mobile US performance, I think if you take a look at the merger case and I base my assumptions always on the merger case and then we'll see whether performing better or not. I think there is a massive, massive deleveraging kicking in after three years which is 2023. And obviously, that continues to be that case from 2023 onwards.

The second point is – because we haven't decided on any kind of shareholder return strategy with the T-Mobile US yet. The second thing is you have seen T-Mobile announcing a shareholder return policy back at the Capital Markets Day in 2008 (sic) [2018] (1:07:51). That was the 2, 3, 4 program. So, that wouldn't be something new. If they have excess cash that they basically return it back in terms of a share buyback program. But right now I think it is too premature to discuss about a shareholder return strategy in the US because I think that has to be discussed internally before we discuss this externally.

Timotheus Höttges

Chief Executive Officer

CLOSING REMARKS

- I think delivering what we have promised that is to say the biggest task which we have in mind. And you've seen that we have a very strong H1 the year on both sides of the Atlantic. So, the hedge which we always had in mind is working
- I think the next half year is our hands full on deck, a lot of things to be done. The delivering of the benefits of the T-Mobile US merger for our customers and as well for our shareholders is of utmost, highest importance
- We want to deliver more and faster on our growth, on build-out and on profitability, when it comes to the networks, the network is the basis of what we're doing. And the more we can do the better it is. But we have to do that in a very efficient way
- And for me, strategic-wise, I would not say everything is solved. But the biggest focus we should have is the FTTH for Germany and the factory approach, which we are driving. So, there is something to be discussed going forward with Srinu and the team
- We should improve the regulatory framework at the same time. So – and Germany is going into the phase of pre-elections. And in this time it's very important to understand the progress with regard to digitization, FTTH. So, everybody is open-minded these days and listening what we are doing
- The next one is digitize, digitize and digitize. And so, when something is unclear in the company we should digitize. This is on a good progress within the company but you cannot do enough of it, both internal processes but as well with regard to the customer interaction. And this is, let's say, another big change, which is helping us to save for fiber and save for profitability. So, the digitization is definitely something which is at our desk
- And the last thing is the de-risking of the T-Systems business and the improvement of the performance going forward. And this is, operationally and strategically, a big question for us we are discussing
- So, even here we have enough to do so. Knowing that some of you are on vacation, I'm trying to slow over
- I hope that more companies and people are coming back to the offices soon
- And with this I'd like to say thank you for your trust and for your support over the last time and let's move on

Disclaimer

The information herein is based on sources we believe to be reliable but is not guaranteed by us and does not purport to be a complete or error-free statement or summary of the available data. As such, we do not warrant, endorse or guarantee the completeness, accuracy, integrity, or timeliness of the information. You must evaluate, and bear all risks associated with, the use of any information provided hereunder, including any reliance on the accuracy, completeness, safety or usefulness of such information. This information is not intended to be used as the primary basis of investment decisions. It should not be construed as advice designed to meet the particular investment needs of any investor. This report is published solely for information purposes, and is not to be construed as financial or other advice or as an offer to sell or the solicitation of an offer to buy any security in any state where such an offer or solicitation would be illegal. Any information expressed herein on this date is subject to change without notice. Any opinions or assertions contained in this information do not represent the opinions or beliefs of FactSet CallStreet, LLC. FactSet CallStreet, LLC, or one or more of its employees, including the writer of this report, may have a position in any of the securities discussed herein.

THE INFORMATION PROVIDED TO YOU HEREUNDER IS PROVIDED "AS IS," AND TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, FactSet CallStreet, LLC AND ITS LICENSORS, BUSINESS ASSOCIATES AND SUPPLIERS DISCLAIM ALL WARRANTIES WITH RESPECT TO THE SAME, EXPRESS, IMPLIED AND STATUTORY, INCLUDING WITHOUT LIMITATION ANY IMPLIED WARRANTIES OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE, ACCURACY, COMPLETENESS, AND NON-INFRINGEMENT. TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, NEITHER FACTSET CALLSTREET, LLC NOR ITS OFFICERS, MEMBERS, DIRECTORS, PARTNERS, AFFILIATES, BUSINESS ASSOCIATES, LICENSORS OR SUPPLIERS WILL BE LIABLE FOR ANY INDIRECT, INCIDENTAL, SPECIAL, CONSEQUENTIAL OR PUNITIVE DAMAGES, INCLUDING WITHOUT LIMITATION DAMAGES FOR LOST PROFITS OR REVENUES, GOODWILL, WORK STOPPAGE, SECURITY BREACHES, VIRUSES, COMPUTER FAILURE OR MALFUNCTION, USE, DATA OR OTHER INTANGIBLE LOSSES OR COMMERCIAL DAMAGES, EVEN IF ANY OF SUCH PARTIES IS ADVISED OF THE POSSIBILITY OF SUCH LOSSES, ARISING UNDER OR IN CONNECTION WITH THE INFORMATION PROVIDED HEREIN OR ANY OTHER SUBJECT MATTER HEREOF.

The contents and appearance of this report are Copyrighted FactSet CallStreet, LLC 2020 CallStreet and FactSet CallStreet, LLC are trademarks and service marks of FactSet CallStreet, LLC. All other trademarks mentioned are trademarks of their respective companies. All rights reserved.