

Telefonica Deutschland Holding AG

Germany / Technology
 Hamburg Stock Exchange
 Bloomberg: O2D GR
 ISIN: DE000A1J5RX9

Q3/24 results

RATING
BUY

PRICE TARGET
€ 3.00

Return Potential 42.9%
 Risk Rating Medium

ROBUST Q3 RESULTS

Telefónica SA, the parent of Telefonica Deutschland Holding AG, published Q3/24 results last week. Headline numbers for the Germany business continued to show robust operating performance with a solid 33% AEBITDA margin. Driven by solid own brand performance, German revenue of €2.10bn (-1.6% Y/Y) was in-line with FBe (€2.13bn; -1.5%). However, the topline figure was offset by headwinds, due to the halving of mobile termination rates (MTR) from January 2024 to €0.20 and the changes to the 1&1 contract. In our view, the O2 brand remains strong in Germany in what continues to be a rational telecommunications market. We maintain our Buy rating and €3 target price.

Mobile Service Revenues (MSR) of €1.5bn down 1.8% (-0.4% excluding MTR) with post-paid ARPU of €12.9 down -5.2% Y/Y but +3% Q/Q Contract net adds, excluding 3rd party Mobile Network Operators accesses, amounted to 226k equal to a sequential quarterly improvement of +11k (+5%). Contract churn remains low at 1.1% driven by the core brand. Population coverage of 5G has grown to 97% vs the 96% announced in July 2024. The company also announced the reduction and simplification of its tariff plans focussed on the €30 ARPU (average revenue per user) per month category with a value-for-money offering. Regarding the mitigation of the 1&1 contract loss, Telefónica referenced the progress made so far this year with the signing of new contracts with Lebara, Lyca and the extension of the freenet contract. The mass migration of 1&1 customers is expected to occur in 2025 with the full financial effects being visible in the 2026 financial year.

Targets unchanged on in-line results Q3 results were close to FBe. We have thus left our full-year 2024 estimates unchanged and reiterate our Buy recommendation. Our €3 price target is based on a blended peer group and DCF approach and corresponds to a ~10% discount of the latter method.

(p.t.o.)

FINANCIAL HISTORY & PROJECTIONS

	2021	2022	2023	2024E	2025E	2026E
Revenue (€m)	7,766.0	8,223.0	8,615.0	8,609.7	8,284.7	8,191.4
Y/Y growth	n.a.	5.9%	4.8%	-0.1%	-3.8%	-1.1%
AEBITDA (€m)	2,410.0	2,538.0	2,617.0	2,667.6	2,488.2	2,359.0
AEBITDA margin	31.0%	30.9%	30.4%	31.0%	30.0%	28.8%
Net income (€m)	211.0	230.0	273.0	300.3	230.6	141.7
EPS (diluted) (€)	0.07	0.08	0.09	0.10	0.08	0.05
DPS (€)	0.18	0.18	0.18	0.00	0.00	0.00
FCF (€m)	964.0	495.0	652.0	767.4	591.6	748.5
Net gearing	65.6%	70.3%	73.0%	73.3%	60.7%	46.9%
Liquid assets (€m)	1,017.8	778.4	584.0	456.2	986.0	1,679.0

RISKS

Risks are typically regulatory surprises surrounding spectrum auctions.

COMPANY PROFILE

Telefónica Deutschland is one of the leading integrated telecommunications providers in Germany, with 45.1m mobile telephone lines and 2.4m broadband lines. The company offers mobile and fixed network services for private and business customers as well as innovative digital solutions based on its infrastructure and mobile data analysis.

MARKET DATA

As of 08 Nov 2024

Closing Price € 2.10
 Shares outstanding 2,974.55m
 Market Capitalisation € 6246.56m
 52-week Range € 1.55 / 3.12
 Avg. Volume (12 Months) 3,524,846

Multiples	2023	2024E	2025E
P/E	22.8	20.7	27.0
EV/Sales	1.2	1.2	1.2
EV/AEBITDA	3.9	3.8	4.1
Div. Yield	8.6%	0.0%	0.0%

STOCK OVERVIEW



COMPANY DATA

As of 31 Dec 2023

Liquid Assets € 584.00m
 Current Assets € 2,733.00m
 Intangible Assets € 4,518.00m
 Total Assets € 15,447.00m
 Current Liabilities € 4,467.00m
 Shareholders' Equity € 5,535.00m

SHAREHOLDERS

Telefónica Germany Holdings Ltd 69.2%
 Telefónica Local Services GmbH 27.6%
 Free Float 3.2%

**Table 1: Third quarter results vs prior year and FBE**

All figures in EURm	Q3/24	Q3/24E	variance	Q3/23	variance	9M/24	9M/23	variance
Revenue	2,098	2,130	-2%	2,131	-2%	6,286	6,323	-1%
AEBITDA	694	643	8%	674	3%	2,027	1,950	4%
Margin	33.1%	30.2%	-	31.6%	-	32.2%	30.8%	-
CapEx*	332	280	19%	312	6%	798	816	-2%
% of sales	15.8%	13.1%	-	14.6%	-	12.7%	12.9%	-

*excluding Spectrum

Source: First Berlin Equity Research; Telefónica SA

German Fixed Line Fixed line revenues totalled €216m (+3.8% Y/Y) with price rises helping ARPU grow 5.2% to €26.9. Subscriber losses were primarily traced to lower value DSL customers with churn stable at 1%. Despite challenging economic conditions, growth of the fixed line ARPU was resilient and may signal the continuation of a relatively benign competitive environment in the mobile space for Telefónica in Germany.

Financials EBITDA (pre-leases) adjusted for exceptionals grew to €694m taking margins to 32.6%—up 140bps on Q3/23—and beat our forecasts thanks to solid cost control and an improved mix of higher margin business on a lower handset sales contribution. These sales were down -3.6% to €380m owing to volatility in new model launch dates.

Capital expenditure in the quarter was higher than expected at €332m (+6.3% Y/Y) following the typical pattern of second-half weighting on capital spend. At the Q3 juncture, CapEx spend was roughly 71% of our full-year estimate. We look for the KPI to total €321m in Q4/24 and thus leave our full-year 2024 targets intact.

INVESTMENT CASE

Stable backdrop Telefónica Deutschland has benefited from a more stable industry backdrop. As Deutsche Telekom's (DT) share of industry revenues has stabilised in recent years, counterintuitively this has benefited both incumbent and competitor revenue growth. Industry revenue growth ex-DT has accelerated from 0.6% over the 2015-2020 period to 1.7% during 2020-2023. Despite its heavy weighting in the competitor group, Telefónica Deutschland has continued to outgrow peers delivering a 4.6% CAGR over the 2020-23 time frame, and recent performance remains robust especially in the post-paid segment.

1&1 a temporary adjustment We view the loss of 1&1 revenues simply as an interruption in this longer-term trend. The erosion in revenues will be gradual at least until mid-2025, and Telefónica Deutschland has already made progress in: (1) filling the MVNO traffic gap; (2) dramatically expanding the scope of its freenet MVNO agreement; (3) winning the Lyca Mobile MVNO contract; and (4) announcing the Simyo MVNO relaunch.

Industry capex is falling Overall, European Telecoms industry CapEx fell by 5.5% in 2023 as expenditure on fibre to the home and 5G peaked. Based on operator industry data, this should be the beginning of a marked trend of improvement in capital efficiency with a further one third decline anticipated in the CapEx to sales ratio by the end of the decade.



Network virtualisation Due to moderating 5G spend and the benefits of the trend to network virtualisation, we expect mobile operators to be prime beneficiaries of capital productivity improvements. Telefónica Deutschland is at the forefront of the existing infrastructure operators' move towards network virtualisation, and we expect the benefits to ultimately be visible in both CapEx and OpEx raising the probability of a positive mid-term CapEx surprise.

Reducing cash burden; additional positive developments The BNetzA's (Bundesnetzagentur) inclination to extend spectrum licenses in multiple bands for 5 years potentially removes the cash burden of additional spectrum auctions for Telefónica Deutschland. As one of the big 3 industry players, strict coverage obligations will already fit, to a significant degree, with 02's network roll-out. **Cash accumulation will be an increasing feature of the business as the suspension of the dividend means Telefónica Deutschland will accumulate an additional €535m (€0.18 per share; ~8%) cash/value annually.**

VALUATION

Third quarter results were close to our forecasts. We leave our 2024 targets unchanged and maintain our Buy rating. Our price target remains at €3 and factors in a conservative c.10% discount to our DCF model.

Table 2: DCF model

In EURm	2024E	2025E	2026E	2027E	2028E	2029E	2030E	2031E
Sales	8,610	8,285	8,191	8,281	8,372	8,463	8,556	8,647
NOPLAT	328	254	170	275	330	474	555	637
(+) depreciation & amortisation	2,247	2,162	2,138	2,099	2,114	2,010	1,946	1,881
Net operating cash flow	2,575	2,417	2,308	2,374	2,444	2,484	2,501	2,518
(-) Total investments (CapEx, RoU & WC)	-1,856	-1,863	-1,587	-1,806	-1,750	-1,762	-1,726	-1,769
(-) Capital expenditures	1,119	1,277	1,065	1,093	1,097	1,109	1,121	1,133
(-) Lease obligations	637	613	606	613	611	609	616	623
(-) Working capital	-99	27	84	-100	-42	-43	10	-14
Free cash flows (FCF)	719	554	722	568	694	723	775	749
PV of FCF's	713	516	633	468	538	527	531	482

In EUR '000	
PV of FCFs in explicit period	6,563
(+) PV of FCFs in terminal period	7,427
Enterprise value (EV)	13,990
(+) Net cash / (-) net debt	-4,041
(+) Investments / minority interests	0
Shareholder value	9,949
Fair value per share (€)	3.34

		Terminal EBITDA margin						
		30.0%	30.5%	31.0%	31.5%	32.0%	32.5%	33.0%
WACC	3.4%	7.91	8.35	8.78	9.22	9.65	10.09	10.52
	4.4%	5.27	5.55	5.82	6.09	6.36	6.64	6.91
	5.4%	3.84	4.02	4.21	4.40	4.58	4.77	4.96
	6.4%	2.93	3.06	3.20	3.34	3.47	3.61	3.74
	7.4%	2.30	2.40	2.51	2.61	2.71	2.81	2.92
	8.4%	1.84	1.92	2.00	2.08	2.16	2.24	2.32
	9.4%	1.49	1.55	1.62	1.68	1.74	1.80	1.87

Terminal growth rate	1.0%
Terminal EBITDA margin	31.5%
Cost of equity	8.1%
Pre-tax cost of debt	5.0%
Tax rate	20.0%
After-tax cost of debt	4.0%
Share of equity capital	57.4%
Share of debt capital	42.6%
WACC	6.4%

		CapEx / sales ratio						
		11.6%	12.1%	12.6%	13.1%	13.6%	14.1%	14.6%
WACC	3.4%	10.52	10.09	9.65	9.22	8.78	8.35	7.91
	4.4%	6.91	6.64	6.36	6.09	5.82	5.55	5.27
	5.4%	4.96	4.77	4.58	4.40	4.21	4.02	3.84
	6.4%	3.74	3.61	3.47	3.34	3.20	3.06	2.93
	7.4%	2.92	2.81	2.71	2.61	2.51	2.40	2.30
	8.4%	2.32	2.24	2.16	2.08	2.00	1.92	1.84
	9.4%	1.87	1.80	1.74	1.68	1.62	1.55	1.49

*Please note our model runs through 2036 and we have only shown the abbreviated version for formatting purposes



INCOME STATEMENT

All figures in EURm	2020	2021	2022	2023	2024E	2025E	2026E
Revenues	7,532	7,766	8,223	8,615	8,610	8,285	8,191
Cost of goods sold	-2,434	-2,404	-2,524	-2,676	-2,648	-2,625	-2,679
Gross profit	5,098	5,362	5,699	5,939	5,962	5,660	5,512
Personnel expenses	-611	-585	-622	-670	-669	-644	-637
Other OpEx	-2,346	-2,526	-2,709	-2,826	-2,777	-2,672	-2,647
Other income	542	402	153	159	142	136	123
EBITDA	2,683	2,653	2,521	2,602	2,657	2,480	2,351
Depreciation & amortisation	-2,369	-2,381	-2,283	-2,310	-2,247	-2,162	-2,138
Operating income (EBIT)	314	272	238	292	410	318	213
Net financial result	-66	-62	-36	-90	-76	-62	-56
Other financial result	0	-3	-15	-10	0	0	0
Pre-tax income (EBT)	248	207	187	192	334	256	157
Income taxes	80	4	43	81	-33	-26	-16
Minority interests	0	0	0	0	0	0	0
Net income / loss	328	211	230	273	300	231	142
Diluted EPS (in €)	0.11	0.07	0.08	0.09	0.10	0.08	0.05
AEBITDA	2,319	2,410	2,538	2,617	2,668	2,488	2,359
AEBITDA (-) CapEx	1,225	1,125	1,329	1,484	1,548	1,211	1,294
Ratios							
Gross margin	67.7%	69.0%	69.3%	68.9%	69.2%	68.3%	67.3%
AEBITDA margin on revenues	30.8%	31.0%	30.9%	30.4%	31.0%	30.0%	28.8%
EBIT margin on revenues	4.2%	3.5%	2.9%	3.4%	4.8%	3.8%	2.6%
Net margin on revenues	4.4%	2.7%	2.8%	3.2%	3.5%	2.8%	1.7%
AEBITDA (-) CapEx margin on revenues	16.3%	14.5%	16.2%	17.2%	18.0%	14.6%	15.8%
Tax rate	-32.3%	-1.9%	-23.0%	-42.2%	10.0%	10.0%	10.0%
Expenses as % of revenues							
Personnel expenses	8.1%	7.5%	7.6%	7.8%	7.8%	7.8%	7.8%
Other OpEx	31.1%	32.5%	32.9%	32.8%	32.3%	32.3%	32.3%
Depreciation & amortisation	31.5%	30.7%	27.8%	26.8%	26.1%	26.1%	26.1%
Y-Y Growth							
Revenues	n.a.	3.1%	5.9%	4.8%	-0.1%	-3.8%	-1.1%
EBITDA	n.a.	-1.1%	-5.0%	3.2%	2.1%	-6.6%	-5.2%
Operating income	n.a.	-13.4%	-12.5%	22.7%	40.2%	-22.4%	-33.0%
Net income/ loss	n.a.	-35.7%	9.0%	n.m.	10.0%	-23.2%	-38.5%



BALANCE SHEET

All figures in EURm	2020	2021	2022	2023	2024E	2025E	2026E
Assets							
Current assets, total	3,277	3,160	2,810	2,733	2,624	3,108	3,800
Cash and equivalents	1,333	1,018	778	584	456	986	1,679
Trade receivables	1,297	1,498	1,359	1,452	1,462	1,407	1,391
Other ST assets	451	436	499	539	550	561	572
Inventories	129	138	140	148	145	144	147
ST financial assets	67	70	34	10	10	10	11
Non-current assets, total	13,915	13,658	13,220	12,715	12,256	11,980	11,517
Intangible assets	4,617	4,137	3,605	3,158	2,745	2,347	1,954
Property, plant and equipment	3,706	3,491	3,512	3,484	3,441	3,600	3,559
Goodwill	1,616	1,360	1,360	1,360	1,360	1,360	1,360
Rights-of-use	2,852	3,348	3,277	3,203	3,167	3,133	3,101
Trade & other receivables	157	269	292	280	307	295	292
Other financial assets	301	396	448	414	416	418	420
Deferred tax assets	476	433	463	538	543	549	554
Other LT assets	190	224	263	278	278	278	278
Total assets	17,192	16,818	16,030	15,448	14,880	15,088	15,317
Shareholders' equity & debt							
Current liabilities, total	4,490	4,287	4,292	4,467	4,139	4,118	4,183
Trade payables (incl. Spectrum)	2,582	2,886	2,768	2,964	2,917	2,891	2,950
Deferred income	548	552	594	522	527	532	538
Lease liabilities	514	548	597	555	555	555	555
ST debt	715	89	128	286	0	0	0
Other ST liabilities	50	53	70	77	77	77	77
Provisions	66	66	67	55	55	55	55
Deferred tax liabilities	15	93	68	8	8	8	8
Long-term liabilities, total	6,372	6,495	5,929	5,446	5,443	5,443	5,467
Lease liabilities	2,326	2,781	2,663	2,559	2,559	2,559	2,559
LT debt	1,577	1,627	1,510	1,235	1,235	1,235	1,235
Trade payables (incl. Spectrum)	1,101	998	901	808	798	791	807
LT provisions	784	647	472	523	523	523	523
Deferred tax	365	255	247	229	236	243	250
Other non-current liabilities	219	187	136	92	92	92	92
Shareholders' equity	6,330	6,036	5,809	5,535	5,298	5,527	5,667
Total consolidated equity and debt	17,192	16,818	16,030	15,448	14,880	15,088	15,317
Ratios							
Current ratio (x)	0.7	0.7	0.7	0.6	0.6	0.8	0.9
Quick ratio (x)	0.7	0.7	0.6	0.6	0.6	0.7	0.9
Net debt	3,732	3,957	4,086	4,041	3,883	3,353	2,659
Net debt / EBITDA (x)	1.4	1.5	1.6	1.6	1.5	1.4	1.1
Net gearing	59%	66%	70%	73%	73%	61%	47%
Equity ratio	37%	36%	36%	36%	36%	37%	37%
Return on equity (ROE)	5.2%	3.5%	4.0%	4.9%	5.7%	4.2%	2.5%
Capital employed (CE)	6,223	5,649	5,239	5,300	4,943	4,677	4,159
Return on capital employed (ROCE)	5%	5%	5%	6%	8%	7%	5%



CASH FLOW STATEMENT

All figures in EUR '000	2020	2021	2022	2023	2024E	2025E	2026E
Net income	328	211	230	273	300	231	142
Depreciation & amortisation	2,369	2,381	2,283	2,310	2,247	2,162	2,138
Other non-cash items	0	2	14	11	0	0	0
Asset disposals	-408	-245	12	7	0	0	0
Income tax result	-80	-5	-42	-82	33	26	16
Financial result	66	62	36	90	76	62	56
Operating cash flow	2,275	2,406	2,533	2,609	2,657	2,480	2,351
Change in working capital	-83	-213	29	-12	-99	27	84
Tax paid	0	0	-56	-89	-33	-26	-16
Net operating cash flow	2,192	2,193	2,506	2,508	2,524	2,482	2,420
CapEx	-1,000	-1,167	-1,379	-1,176	-1,119	-1,277	-1,065
Disposal proceeds	17	4	6	4	0	0	0
Company investments / disposals, net	765	533	6	-15	0	0	0
Income from investments, net	-20	-1	-11	65	0	0	0
Interest income	5	4	7	13	0	0	0
Cash flow from investing	-233	-627	-1,371	-1,109	-1,119	-1,277	-1,065
Free cash flow (FCF)	1,959	1,566	1,135	1,399	1,405	1,205	1,355
Equity inflow, net	0	0	0	0	0	0	0
Repayment of lease liabilities	-547	-602	-640	-747	-637	-613	-606
Debt inflow, net	-199	-565	-79	-117	-286	0	0
Interest paid	-63	-64	-43	-95	-76	-62	-56
Dividend paid to shareholders	-506	-535	-535	-535	-535	0	0
Other adjustments	-92	-115	-77	-99	2	0	0
Cash flow from financing	-1,407	-1,881	-1,374	-1,593	-1,532	-675	-662
Net cash flows	552	-315	-239	-194	-128	530	693
Cash, start of the year	781	1,333	1,018	778	584	456	986
Cash, end of the year	1,333	1,018	778	584	456	986	1,679
AEBITDA/share (in €)	0.78	0.81	0.85	0.88	0.90	0.84	0.79
Y-Y Growth							
Operating cash flow	n.a.	0.0%	14.3%	0.1%	0.6%	-1.7%	-2.5%
Free cash flow	n.a.	-20.1%	-27.5%	23.3%	0.4%	-14.2%	12.5%
AEBITDA/share	n.a.	3.9%	5.3%	3.1%	1.9%	-6.7%	-5.2%

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PRICE TARGET DATES

Unless otherwise indicated, current prices refer to the closing prices of the previous trading day.

AGREEMENT WITH THE ANALYSED COMPANY AND MAINTENANCE OF OBJECTIVITY

The present financial analysis is based on the author's own knowledge and research. The author prepared this study without any direct or indirect influence exerted on the part of the analysed company. Parts of the financial analysis were possibly provided to the analysed company prior to publication in order to avoid inaccuracies in the representation of facts. However, no substantial changes were made at the request of the analysed company following any such provision.

ASSET VALUATION SYSTEM

First Berlin's system for asset valuation is divided into an asset recommendation and a risk assessment.

ASSET RECOMMENDATION

The recommendations determined in accordance with the share price trend anticipated by First Berlin in the respectively indicated investment period are as follows:

Category		1	2
Current market capitalisation (in €)		0 - 2 billion	> 2 billion
Strong Buy ¹	An expected favourable price trend of:	> 50%	> 30%
Buy	An expected favourable price trend of:	> 25%	> 15%
Add	An expected favourable price trend of:	0% to 25%	0% to 15%
Reduce	An expected negative price trend of:	0% to -15%	0% to -10%
Sell	An expected negative price trend of:	< -15%	< -10%

¹ The expected price trend is in combination with sizable confidence in the quality and forecast security of management.

Our recommendation system places each company into one of two market capitalisation categories. Category 1 companies have a market capitalisation of €0 – €2 billion, and Category 2 companies have a market capitalisation of > €2 billion. The expected return thresholds underlying our recommendation system are lower for Category 2 companies than for Category 1 companies. This reflects the generally lower level of risk associated with higher market capitalisation companies.

RISK ASSESSMENT

The First Berlin categories for risk assessment are low, average, high and speculative. They are determined by ten factors: Corporate governance, quality of earnings, management strength, balance sheet and financial risk, competitive position, standard of financial disclosure, regulatory and political uncertainty, strength of brandname, market capitalisation and free float. These risk factors are incorporated into the First Berlin valuation models and are thus included in the target prices. First Berlin customers may request the models.

RECOMMENDATION & PRICE TARGET HISTORY

Report No.:	Date of publication	Previous day closing price	Recommendation	Price target
Initial Report	23 October 2024	€2.10	Buy	€3.00
2	Today	€2.10	Buy	€3.00

INVESTMENT HORIZON

Unless otherwise stated in the financial analysis, the ratings refer to an investment period of twelve months.

UPDATES

At the time of publication of this financial analysis it is not certain whether, when and on what occasion an update will be provided. In general First Berlin strives to review the financial analysis for its topicality and, if required, to update it in a very timely manner in connection with the reporting obligations of the analysed company or on the occasion of ad hoc notifications.

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Legally required information regarding

- key sources of information in the preparation of this research report

- valuation methods and principles
- sensitivity of valuation parameters

can be accessed through the following internet link: <https://firstberlin.com/disclaimer-english-link/>

SUPERVISORY AUTHORITY: Bundesanstalt für Finanzdienstleistungsaufsicht (German Federal Financial Supervisory Authority) [BaFin], Graurheindorferstraße 108, 53117 Bonn and Marie-Curie-Straße 24-28, 60439 Frankfurt am Main

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