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Q1 2012 Earnings Call
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MANAGEMENT DISCUSSION SECTION

Operator: Welcome to Deutsche Telekom's Conference Call.

Unverified Participant

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In addition to figures prepared in accordance with IFRS, Deutsche Telekom also presents non-GAAP financial performance measures, including, among others, EBITDA, EBITDA margin, adjusted EBITDA, adjusted EBITDA margin, adjusted EBIT, adjusted net income, free cash flow, gross debt, and net debt. These non-GAAP measures should be considered in addition to, but not as a substitute for, the information prepared in accordance with IFRS. Non-GAAP financial performance measures are not subject to IFRS or any other Generally Accepted Accounting Principles. Other companies may define these terms in different [audio gap] (3:40).

Operator: On our customer’s request, this conference will be recorded. Now, please listen to the statement of Timotheus Höttges. Afterwards, you are welcome to ask your questions. May I now you over to Mr. Stephan Eger.

Stephan Eger
Head-Investor Relations, Deutsche Telekom AG

Good afternoon and good morning to our listeners in the U.S. and welcome to the first quarter conference calls of Deutsche Telekom. I’m here with Tim Höttges, our group CFO, and I’ll send you the warmest regards of our group
CEO, René Obermann. He is not in the States. He's not in Mexico City. He's participating in a political event in Berlin. So sorry to disappoint you on that.

We have around about an hour's time, so we have to cut off sharply at 3:00. So without any further ado, I hand over to Tim, our group CFO.

Timotheus Höttges  
Chief Financial Officer, Deutsche Telekom AG

Yeah. Hello, everybody. This is only Tim here. So good afternoon and good morning to the U.S. First of all, we have delivered a solid quarter at DT and reiterate our full-year guidance. Our revenue trends have improved versus 2011 in Germany and in Europe resulting in a decline of only 1.1% this quarter.

Our adjusted EBITDA driven by a strong performance in the U.S. and Europe is almost stable year-over-year as is our free cash flow at €1.1 billion. And unlike many of our peers, we executed on our shareholder remuneration and our dividend policy by proposing to our AGM on May 24 an unchanged dividend $0.70 per share.

Now, our strong home Germany, we continue to perform better than most European peers while maintaining a strong market position and financial profile. The revenue trend in Germany is better than in any quarter in 2011. At the same time, we continue to show a high and even year-over-year slightly increased margin of close to 41%.

In the fixed line business, we showed very positive operational KPIs, with again drastically reduced line losses at 259,000. The improved broadband net adds of 102,000 supported by a broadband churn on a historic low, or the very strong IPTV sales of 173,000. In mobile data, revenue growth remains strong at 20% year-over-year driven by a further increase in smartphone sales with almost 300,000 iPhones sold alone.

In our European segment, we see a continuous improvement in revenue and EBITDA trends. The organic revenue decline was only 0.7% in the first quarter. Here, we did see some encouraging trends, particularly in Greece, Romania, and Bulgaria. The organic EBITDA decline was reduced to 2.2%. At the same time, we again, saw satisfying operational KPIs like smartphone, broadband or mobile contract subscriber growth figures.

In the U.S. we delivered an improvement in our overall customer and contract customer trends versus the difficult fourth quarter and delivered a strong financial quarter, which will give us the necessary headroom to invest as planned into the execution of our Challenger strategy throughout the rest of this year.

Let me briefly comment on the Q1 key financials for the group. As just mentioned, we are pleased with the revenue and EBITDA development in the first quarter. As you see in the table on chart six, due to an almost unchanged cash CapEx number, in the first quarter, also our group free cash flow is stable year-over-year. The net income number in the first quarter was mainly negatively influenced by two effects: a provision for the early retirement program in Germany, which we took in Q1 this year versus in Q2 last year. So this is just a seasonization during the quarter this year.

€18 million of additional depreciation predominantly from the U.S. versus Q1 last year is due to the deal announcement in March 2011. The business had been classified as held for sale and depreciations were stopped by then.

On slide seven, you see the revenue and EBITDA development in Q1 for the group and on a segmental level. The reported revenue decline for the group was helped by €86 million positive currency impact, mainly coming from the U.S. dollar. The organic EBITDA decline on the group level was 1.7%.
In Germany, the 2.3% revenue decline was driven by an improved minus 2.6% decline in our core fixed network business and a 1.8% decline in service revenues in mobile. In the U.S., the 2% revenue growth in euro was driven by the favorable foreign exchange development. The organic revenue decline was 2.3%, driven by mobile service revenue declining 5.4% year-over-year.

The increase in adjusted EBITDA at TM U.S. of 8% in U.S. dollar terms was driven by a great job on cost cutting, lower network costs and lower SACs and CRCs as a result of the success of our value plans.

In our European segment, the 2.6% decline in reported revenues was mainly driven by negative foreign exchange effects of €72 million and the mobile regulation impact of €51 million for the quarter. The organic revenue decrease was 0.7%, showing a continuous improvement versus the previous quarters. The EBITDA decline was 4.3%, also impacted by negative impact from foreign exchange of €26 million, and the mobile regulation of €17 million, resulting in an organic EBITDA decline of 2.2%.

At Systems Solutions, we saw a modest decline in revenues of 0.7% mainly driven by almost 4% lower internal revenues mainly coming from our Save for Service initiatives within the group. On the EBITDA side, there’s a slight improvement versus last year.

Let's turn to the first quarter detail in Germany. On slide eight you will find a new and more granular split on the development of our revenues in Germany. The revenue trend in Germany improved to minus 2.3% after minus 6.1% in Q4, partially driven by the discontinuation of the MTR impact and some of the one-timers we had last year, but also by an improvement in our core fixed network revenues and wholesale revenues.

Our core fixed network revenues have improved from minus 5.4% last quarter to minus 2.6% this quarter, with the main drivers being lower line losses and the healthy growth in our TV revenues. Wholesale revenues improved from minus 11.6% in Q4 to minus 3.9% in Q1 mainly driven by an improvement in voice and network services. The adjusted EBITDA for Germany declined by 2% in the quarter helped by a 1.6% OpEx reduction and resulting in a healthy and slightly year-to-year increased margin of almost 41%.

Mobile revenues declined by 1.2% driven by deterioration in service revenues. On a positive note, within mobile service revenues, the strong mobile data growth continues in Q1 with a 20% growth rate year-over-year.

We saw strong smartphone and iPhone sales in the quarter. Total customer and contract customer intake, however, was negative primarily driven by the customer migration of one reseller which heavily impacted our net adds and contract churn figures. However, our underlying branded contract customer churn remained stable at a rock solid 1%.

We’re speeding up our LTE rollout towards capacity limits and already covered a quarter of the German population by the end of the first quarter, up 11 percentage points in one quarter alone.

Let me give you some details on the development of our mobile service revenues in Germany in Q1 and our measures to address this in the coming months. Service revenues in the first quarter declined by 1.8%, mainly driven by the decline in voice revenues, minus €87 million; SMS revenues minus €12 million; and visitor revenues minus €9 million, which only partially was compensated by the healthy 20% growth in mobile data.

Business customer mobile services declined by 1.5%, driven by price declines as the result of tough competition which could not be entirely compensated by customer growth. Retail customer service revenues declined by 2% with the main drivers being ongoing migration of customers into our new tariff profile, and lower service provider
revenues, lower contribution from prepaid due to a less voice usage, and deterioration of our prepaid customer mix.

So what will now be our key initiatives to address this weakness? First, within our branded contract customer base, we will push very hard on mobile broadband, focusing on LTE, tablets, sticks, and data tariffs. On the business customer side, we will try to tap the large [ph] contingent (15:18) of our fixed-only customers better, particularly also with mobile data offers.

On the service provider side, we continue our efforts within ethnic and discount brands, and will also adjust our wholesale product portfolio. And in prepaid, we will come up with a new tariff proposition for our customers very soon.

In the German fixed broadband market, we stabilized our market share in excess of 45% with the strong number of broadband net adds of 102,000 in the quarter, resulting in an improved market share of net adds of beyond 30% on our calculations. At the same time, we showed another very strong quarter in IPTV sales, with 173,000 new Entertain customers won, bringing the total number of Entertain customers now to over 1.7 million.

This upselling strategy helped to increase our average revenue per access line by €0.40 to €25.60. Line losses were more than 24% lower than last year at only 259,000, one of the lowest quarter ever. Furthermore, we increased our broadband coverage in Germany, pushing our VDSL coverage to 36%, our DSL 16-megabit coverage to 53% and our Entertain via SAT coverage up to 82% of the population here in Germany.

Turning to the U.S., overall, we are pleased with the U.S. performance especially compared to the expectations although clearly, there are several areas of concerns remaining. Please note that we changed, by the way, on your request, our customer reporting to branded customer reporting, in line with our U.S. peers and to increase transparency of reporting. Branded contract is the old contract without machine-to-machine customers. Branded prepaid, the old prepaid without MVNOs. We provide a reconciliation with the previous metrics in the IR backup.

Service revenues decreased by 5.4%, resulting from our system losses. Please note that once again, service revenues in the U.S. have decreased to a lesser extent. [indiscernible] (18:18) 4% due to the [ph] inclusion (18:19) of one-time fees, which are not included in the service revenues under IFRS.

EBITDA also benefited from the success of the value plans, which were introduced last July. Both SAC to gross adds and SRC to retained customers were down more than 30% year-on-year. In addition, network cost also decreased by 4.5% despite a large increase in data volume due to the transition to fiber backhaul.

In terms of customers, T-Mobile U.S. returned to customer growth in the first quarter due to strong prepaid growth and the return to positive growth in machine-to-machine. You may recall that these were negative in Q4 due to the loss of one large customer.

On the other hand, branded contract customer losses though improved remained high due to lower gross adds and still a high churn. Looking just at branded contracts, that is contract without machine-to-machine customers, we saw a positive ARPU development with branded contract ARPU up $2 year-on-year due to a very strong growth in data.

T-Mobile made good progress with regards to the implementation of the Challenger strategy. Following SEC approval in late April, the AT&T breakup spectrum was transferred in early May. We recently signed the contracts
with Ericsson and Nokia Siemens Networks for the network modernization. So we remain firmly on track with regard to network modernization which includes refarming of 1900 MHz spectrum from GSM to HSPA+. This would allow existing iPhones to work on our HSPA+ network.

In terms of brand relaunch, we just started Phase 1 of the rebranding with our Test Drive campaign, which you may have seen already. We continued our distribution push with 115 new branded dealers. In addition, we expect to add more than 7,000 new doors among our national retail partners this year. The B2B ramp has been initiated and we signed four new MVNOs.

Finally, we have launched multiple initiatives as part of Reinvent, aiming for $900 million of gross cost savings in 2012 alone. This includes the recent rationalization of our call centers in the U.S. resulting in 1900 net job reductions.

We are also making progress with our churn reduction initiative. For the quarter, branded contract churn was reduced to 2.5% and the latest monthly numbers were even lower.

Turning to the European segment, we saw the continuation of the improvement in trends from recent quarters. As a result, organic revenue and EBITDA were close to a stabilization in the third quarter. This was helped by a Europe-wide performance improvement program, a simplification of the steering of our net cost and the rigid focus on activities like smartphone and mobile broadband push.

The growth in key market KPIs like TV, broadband and mobile contract customers remained strong in the first quarter, in all [ph] navcos (22:22). And this despite economic trends in some of the markets like Hungary, Croatia and Greece which are remaining very difficult.

Turning to our operations in integrated markets, the revenue trend in Greece improved further in Q1, particularly driven by good performance in mobile as a result of a higher subscriber base and revenue initiatives in the consumer segment. In fixed line, revenues continue to remain under pressure from an unfair, totally unfair and not consumer-oriented ex-ante regulation, keeping our offers at uncompetitive levels. The margin in Greece remained broadly stable year-over-year at 37.7%

In Croatia, the economy deteriorated in Q1 and austerity measures like the reinstatement of a 6% mobile tax, the introduction of a dividend withdrawing tax, or the increase of the VAT up to 25%, are not really supportive. Operationally, the business held up quite well, with revenues being helped by our ICT business and a higher year-over-year margin driven by strong cost discipline. Further cost savings and staff reductions are planned and announced for the year.

Looking at Hungary, the situation remains difficult as you all know. Negative foreign exchange effects impacted again the figures in euro terms. The potential new usage-based telco tax replacing the old one might create a burden on private and business customers and thus jeopardize the country’s competitiveness.

With respect to the competitive environment, all three mobile operators have appealed against the decision to distribute frequencies to the new entrant, so far unsuccessfully. In this difficult environment, our management team does a fantastic job fighting revenue declines by innovative approaches like reselling electricity and gas as well as insurance contracts via their distribution channels, and advanced integrated fixed and mobile offers. The EBITDA year-over-year comparison is negatively impacted by a positive one-timer in Q1 of last year.

In Slovakia, we returned to revenue growth in the first quarter, driven by fixed line and ICT revenue growth, whereas the margin dropped year-over-year versus a very strong Q1 last year. Positively, the growth in TV satellite
customers of 31% and in IPTV customers of 10.5% was very strong this quarter. In our mobile-centric businesses, revenues in euro were impacted by competitive pressures as well, tough regulation and the weak Polish zloty and Czech koruna in the quarter.

In Poland, revenues in Q1 were heavily impacted by foreign exchange and the MTR cut. Underlying revenues, ex those effects, were up by 3%, mainly driven by device revenues and due to more smartphone sales. The underlying EBITDA was almost on the previous year’s level in spite of heavy competition. We outperformed our main competitor, Orange, with regard to total revenues and contract net adds in this quarter.

In the Netherlands, revenues were positively impacted by a higher subscriber base, higher device revenues due to more smartphones being sold, the rest-effects from the unlimited-offer cancellation already seen in Q4 and other revenue initiatives. The EBITDA surge can be explained by a very weak Q1 2011, a more rational market invest and further cost savings. Furthermore, the outperformance versus our main competitor, KPN, in terms of service revenues and contract net adds is very positive.

In the Czech Republic, we are facing tough competition. Underlying revenues, ex foreign exchange and regulation however turned positive to 1.9%, whereas underlying EBITDA dropped slightly by 2.9%, mainly driven by a strong smartphone push in the quarter resulting in an increase in the share of dispatched smartphones from 30% last year to now 49% in Q1 and the healthy 24% mobile data revenue growth.

In Austria, we saw a continuation of the contract subscriber growth in Q1 and the strong smartphone push; 74% of all dispatched devices in Q1 were smartphones. Revenues declined by 1%, but without the regulatory impact, underlying revenues grew by 3.5%.

In this context, let me say a few words about our U.K. joint venture, Everything Everywhere, which already reported results last week. We continue to see good progress in terms of customer and underlying service revenue growth as well as synergy execution at Everything Everywhere and has launched a massive media campaign in order to push our planned LTE rollout in the U.K., and of course, DT remains fully committed to make Everything Everywhere a long-term success in the U.K. mobile market.

In Systems Solutions, we saw a slight revenue decline of 0.7% mainly driven by our Save for Service initiatives internally, whereas external revenues showed a slight increase, basically a similar picture as in Q4 last year. On the EBITIDA and EBIT, we made some good progress versus last year which was particular weak mainly driven by €166 million gross cost savings in that quarter.

Turning to the group financials, free cash flow was solid with an increase of 5.7% to €1.1 billion. The improvement in underlying net cash generated from operations was predominantly due to less tax and interest payments. The underlying CapEx development was essentially stable at a high level at €2.1 billion. The decrease in others resulted from less asset sales.

Let's turn to the development of reported net income, slide 19. Looking at the year-on-year comparison and starting off at our net profit of €418 million in Q1 last year, we saw an improved financial result due to the sales of our stake in Telekom Serbia, which at the same time increased the minorities.

Profit and loss taxes decreased partially resulting from a U.S.-related one-off tax charge in Q1. Including various other smaller effects, this would have increased net income to €639 million. However, as already mentioned, we took the €464 million provision for an early retirement program in Germany in Q1 partially offset by €143 million tax benefit from this provision. This represents a different timing of special factors compared to 2011. In 2011, we took the provisions for the early retirement in the second quarter.
In addition, we saw €80 million of additional depreciation predominantly from the U.S. due to the U.S. being fully consolidated again. As of the announcement of the AT&T deal last year, the U.S. was categorized as held for sale with no further depreciation. This was reversed in Q4 when the deal was cancelled. Therefore, the trend of higher depreciation will continue in Q2 and Q3 but then reversing in the fourth quarter. As a result of these factors, reported net income decreased to €238 million which is not a concern for me at all.

Finally, our balance sheet ratios improved further with an improved net debt over EBITDA ratio and gearing in Q1. Net debt dropped below the €40 billion mark to €38.6 billion, while shareholders’ equity remained stable around €40 billion.

We continued to maintain solid ratings with stable outlooks from all major rating agencies. Important to note is that we currently enjoy very favorable refinancing terms, particularly versus some of our peers. We took advantage of this earlier this year for some bond issuance, leaving us now refinanced for almost 36 months, way ahead of our normal liquidity reserve policy.

Before turning to the Q&A session, let me say something about our Q1 performance and how this fits in our full-year guidance. Q1 was a solid quarter for revenues and even more for EBITDA. Nonetheless, we confirm today our full-year 2012 guidance which includes the year-over-year EBITDA decline of €700 million due to the following reasons:

In the U.S. we will start to see more investments into our Challenger strategy from Q2 onwards, especially into the Phase 1 of our brand re-launch and thus, higher media spend and into B2B platform.

In Europe, we cannot exclude further negative development be it on the macro or the regulatory or austerity side, impacting our results negatively. Furthermore, we will invest more into marketing in some of our markets in Q2 and Q3 in order to push mobile broadband even further and gain market shares.

So overall, let me say this was a solid quarter. It was appreciated from the capital market so far. And we have quite solid numbers from the balance sheet ratios.

With this, I’d like to finish my presentation and I’m ready for your questions.
QUESTION AND ANSWER SECTION

Stephan Eger  
Head-Investor Relations, Deutsche Telekom AG

Thank you very much, Tim. We'll start right away with the Q&A session. [Operator Instructions] And please, as we want to be finished by 2:00 p.m. U.K. time, keep it simple and quick and please refrain to – only two questions per person. And we'll start off with Nick Delfas from Morgan Stanley. Nick?

Nick Delfas  
Analyst, Morgan Stanley & Co. International Plc

Yeah. Thanks very much, indeed. Just a couple of questions. Could you just tell us how you are doing on LTE in Germany? You said you covered 25% of the population of your total subscriber number. And also a question on Entertain, how is the split going between your satellite service and your overall DSL service? Thanks.

Timotheus Höttges  
Chief Financial Officer, Deutsche Telekom AG

So the first thing – Nick, the first thing is that today, we are building our LTE network at maximum speed. As you might recall, we have increased our CapEx over the last two years for mobile build-out by more than 50%, so something in the vicinity of €600 million is only going into the LTE push.

This is a head-to-head race with Vodafone here in Germany. The others are not present at all in this circumstance. Now, we have covered 25% of our pops in Germany. We have increased our footprint by 11% point only this quarter. And we are not only in the countryside, but as well in the cities; we are frontrunners in that one. And this huge investment which we took into the German mobile network shows already success.

There was not a single test, and there was a couple, more than six or seven tests which were done recently which wasn't won by the group, and by the way, with big differences to all the competitors. So, therefore, I think we cannot do more at that point in time. The amount of sites which we have built so far are in the vicinity of 1,500 sites in Germany furthermore on 4G. That is 4G alone.

Nick Delfas  
Analyst, Morgan Stanley & Co. International Plc

So, do you have the subscribers?

Timotheus Höttges  
Chief Financial Officer, Deutsche Telekom AG

On the subscriber side, we are something in the vicinity of 70,000 subscribers.

On Entertain front, your second questions, we had 80,000 net adds in the first quarter, more than 200,000 after seven months. We have launched a new proposition, an action-oriented tariff product here in the market recently. The only limitation we have were the media receivers because we were sold out and so we could have sold even more on the satellite product, but we hope that we are able to deliver on the demand very soon. That is I think the message we got from our delivery here.
Okay. Thanks very much.

We continue with Simon Weeden from Citigroup. Simon, please.

Yes. Thank you very much. I wondered if you could share with us how you saw the trends in the U.S. as you exited the quarter and through into April? And also update us on roughly what proportion of contract gross additions were taken out and equipment installment this quarter. Thank you.

The trends in the U.S. are pretty much unchanged to the first quarter. As I said, the trend on our branded contract is improving. We see a slight slowdown on gross adds in the overall markets – on contract gross adds in the overall market in the U.S. and our churn is improving quarter – month-over-month.

And Simon on your question with respect to how much of the gross additions coming from the equipment, installment planning, so the value plans account for about 45% in the first quarter.

Let’s continue with Fred Boulan. Fred?

Hi. Good afternoon. Two questions from my side, firstly, on your domestic broadband strategy, if you can share your thoughts on the – on how your high speed broadband rollout is doing? Cable operation reached about two-thirds of the country, and we’ve got this 3.0 by the end of this year. Are you comfortable with your VDSL progress?

And secondly on domestic mobile, you mentioned an action plan to regain momentum via mobile, broadband, and prepaid. But what do you make of increasing pricing pressure in the market? Are we not seeing a broader re-pricing, which will make your recovery in revenues a bit more difficult to achieve? Thank you very much.

So Fred, thank you for your question. I think with regards to the broadband rollout, we will definitely further improve the broadband coverage in Germany. You have seen that we increased our VDSL coverage up to 36% of the population. We are very closely working with the housing association to get even more access to customers in the apartments.

On top of that, DSL coverage improving as well, so we had a record CapEx in Germany last year of €3.7 billion total in Germany, something in the vicinity of [ph] €607 million (40:37) from mobile. So you could imagine how
much is going into the fixed line business here. This is by the way something in the vicinity 14% of total sales or let's say every €0.50 of €1 we earn in EBITDA terms, we are investing in Germany into the improvement of our broadband connectivity.

So the big question mark which always gets discussed is the question about our fiber-to-the-home. And whether we pursue here, yes, we are even working to improve our rollout in this area. But the big rollout is always a questioned from – or depending on the regulatory environment in Germany, which is still unclear for us. So, this is a political discussion which is heating up here in Germany, hopefully, and then we will give you details if something is changing here.

Your second question was, with regards to the pricing and the current launches we have seen. E-Plus has launched a very aggressive tariff, which is called Europhone and Drillisch followed that offer immediately and I think there was even another MVNO following. The offer is an on-net and surf-let 500 megabytes for €24.90, a SIM-only offer. And by the way, on Internet services. It's a small company I think with 10 employees.

Until now, we have not planned to cut our prices. We are a premium operator. We are market-leader and we are behaving rational in this regard. We’re watching it carefully and we have to find appropriate answers on how to react. So far – so nothing to worry, but I do not see that this is something we could compare with Free in France, for instance, because the market for this specific segment is already well-covered and the price gets to the existing average prices. It’s not that big as in France.

Frederic E. Boulan
Analyst, Nomura International Plc

Okay, but do you think the trends you are speaking can allow you to re-grow at one point this year in mobile or is the idea just to contain the pressure that we’re starting to see in Q1.

Timotheus Höttges
Chief Financial Officer, Deutsche Telekom AG

You might understand that we are not giving a guidance on specific revenue in a segment. But our clear ambition and that was the reason that we highlighted our mobile initiatives in this presentation today is that we want to improve our position here. It is not our intention to decline that business. It’s clear our intention with the tailwind on the MTRs and others to grow the business here in Germany, mainly with the data proposition we are pursuing. So therefore, we have measures, we have plans behind that and hopefully, we could get them executed.

Frederic E. Boulan
Analyst, Nomura International Plc

Okay. Thank you very much.

Stephan Eger
Head-Investor Relations, Deutsche Telekom AG

Thank you, Tim. Thank you, Fred. Let's move over to Emmet Kelly from Merrill Lynch.

Emmet B. Kelly
Analyst, Merrill Lynch International Ltd.

Yes, good afternoon. Just two questions, please. The first question is on German fixed line. So we've seen a nice improvement in your revenue growth trends there at the beginning of 2012. I think we've gone from negative 4.5%
growth in Q4 last year to negative 2.5% in Q1 this year. Can you just give us an insight into what the main drivers are here and whether we might see further improvements going forward into the rest of 2012?

My second question is on Sky Deutschland. Sky has now won exclusive rights for the Bundesliga on all platforms in Germany. Just wondering how do you see your relationship with Sky evolving in the future especially given your push of the Entertain product at the moment. Thank you.

So, yes, we are quite happy with the development in fixed line business. And mainly, by the way, that with the net add sales, we are again with the market share higher than 30%. So we participate even in the growth of this market with the relevant share. And our churn rate in this business is developing like DSL. So where are – where is the sales coming from? What are the lead products? TV; I mentioned that already 170,000 net adds; VDSL, 66,000 customers appreciating bandwidth. That is what we are facing here and therefore, we believe that with the double and with the triple-play offers, which we currently announce or offer in the market, we are attractive for the German customers.

With regards to the Bundesliga rights, it was always our [ph] clear statement (46:22) that we are not doing that deal. And we had a clear understanding on how much we are willing to invest for the total package on Bundesliga. In this calculation, we anticipated a further growth on the data mark which was already quite ambitious. And it was our clear message that we said the net present value is the maximum – if the net present value is turning zero, it’s the maximum we are willing to pay. So we were outbid in this regard, by the way, big time so therefore, I feel comfortable that we took the right decision here.

I cannot comment on Sky’s business model, but for us, so everyone’s clear, our cost structure, our distribution model and even the synergies which we would have with our media spend would have been significantly bigger, the synergies than the one Sky has. But anyway, I’m not talking about their business model.

Now we are trying to collaborate with Sky, so that we are able to continue our Bundesliga offering. The live coverage on our platform is something which is attractive, definitely. 10% of our Entertain customers are using Bundesliga today. Today it’s too early to say. We cannot see, let’s say the final outcome of the discussion. But from a commercial perspective, I would guess that we would find a positive commercial solution with Sky here in Germany.

Great. Thank you.

Now we are trying to collaborate with Sky, so that we are able to continue our Bundesliga offering. The live coverage on our platform is something which is attractive, definitely. 10% of our Entertain customers are using Bundesliga today. Today it’s too early to say. We cannot see, let’s say the final outcome of the discussion. But from a commercial perspective, I would guess that we would find a positive commercial solution with Sky here in Germany.

Yeah, just a couple of quick questions about cost reduction plans. I’ve seen the last year’s Save for Service, and I know you’ve just recently agreed some staff wage increases in Germany. How we should think about the kind of shape and your communication of any kind of plans beyond the current formal program? Thanks.
Look, we have in our presentations, our focus is made on turning the revenue trend, improving let’s say, the over performance of our portfolio stabilizing. Save for Service is an incremental piece of this turnaround story of this improvement which we are also pursuing across the markets. There is not a single country, there is not a single segment where we are not working on Save for Service initiatives. On the U.S., we have committed a €900 million saving plan for this year. On Germany, we have saved €300 million of OpEx in the first quarter which is I think is a recent – sorry, €300 million for the group, which is a reasonable run-rate.

It might be that we will make a more detailed description of Save for Service throughout the year for our investors here. But Save for Service is clearly, let’s say, a main initiative within the group. We know that we still have a gap on a productivity, on a margins level to our peers of something around 2% to 3% points. And we are working towards these benchmarks on the way how we organize our processes.

With regards to the wage agreement in Germany, let me maybe give you some further details how this wage agreement is constructed. The nominal increase is 2.3% in 2012, 2.1% and 2.1%, so two steps in the 12 months thereafter. Overall, this would add up to 6.5%, The underlying increase is only 3.7% over two years. Why is that? Because it includes a three-month delay where we do not have an increase for our German operation.

If you would now compare OpEx with OpEx, so take the current OpEx level for wages, including, let’s say, the increase for the civil servants as well for our – for the rest of the employees, the total increase of OpEx after three years would be €200 million. There are no other commitments made in this agreement. So all the other ways of improving our cost base, our total workforce cost within the group are opened and we will work within our Save for Service initiatives to further improve the productivity.
Hi, Hannes. So maybe everybody’s – maybe waiting that we make a statement with regards to the rumors around the U.S. And you know that I will not and I cannot and I don’t want to make any kinds of speculations or statements towards the rumors in the U.S. Therefore, what was right in the past is right today.

The first and almost most important thing, what we always have said is we want to improve our operative position in the U.S. business. And I think the first quarter is quite encouraging. We are well on track with our Challenger program. We are well on track on, let’s say, the refarming of our network and the program around that and we know that we will have an LTE offer which is competitive enough with all the players in U.S. market will be launched in 2013. So therefore, the first task is on its execution and well on track.

Now, towards the possible transactions, we always have said that we will want to have a de-risking of our U.S. business and a self-funding platform of, let’s say, for investments. This is right and it keeps – it stays right. So therefore, we are talking in the U.S. We are trying to find opportunities to improve the economies of scale in the U.S. But I cannot give you any more details what’s going on. And I’m even not commenting on whether a deal is coming or not coming or whether we do an IPO. That would be then too explicit.

With regard to the civil servants and the [Foreign Language], so far, nothing has been decided from a government perspective. But only to – for your information, this program would get extended, this is the cheapest way for Deutsche Telekom to reduce its OpEx basis from the instruments we have.

Stephan Eger
Head-Investor Relations, Deutsche Telekom AG

Thank you, Tim. Let's move on to Robin Bienenstock of Sanford Bernstein, please.

Robin A. Bienenstock
Analyst, Sanford C. Bernstein Ltd.

Yes, thanks very much. Two questions, I guess in historically the union members on your board had voted for the dividends so I was wondering when you had conversations with them about salaries. Is the dividend and is future investments in the network something that is discussed? And separately, a number of your peers are looking at trying to reduce subsidy or indeed separate handset financing from service plans and we're seeing a bit more of that in Germany recently. I was wondering what you think about that and whether you think that's something that could be appealing to you in Germany? Thanks.

Timotheus Höttges
Chief Financial Officer, Deutsche Telekom AG

So, Robin, first, we have had no board decisions or discussion on whether we trade dividend against further network build-out whatsoever. I think it was – we feel a very comfortable in what we have laid out with our financial strategy and our dividend commitments two years ago. We have now – we are now executing the second tranche of the three-year program. We have said that we are committed towards the third year on that one as well. We recognize that a lot of peers in the European environment are not able to fill their dividend commitments. I think that is different to Deutsche Telekom; unlike our peers, our payout ratio is only around 50%. And unlike our peers, we did not underspend in infrastructure. I want to be very clear on that one.

As mentioned already, the build-out of our LTE networks, not only in Germany, but as well in Europe. In Germany, we are spending 50% more than over the last average run rates in normal years. We have a physical limitation today on the speed on the LTE build-out. And therefore, there's no – nothing we are sacrificing today for our dividend. The opposite is the case with – even to take some of the cash flow to pay down our debts.
So, therefore, I think nothing to say. Nevertheless, internally, we are thinking about what would be our answer in 2013 toward the next phase of our financial strategy. This is an internal discussion. We haven't had the discussion with the board so far and we will come to the investors the moment we have a clear focus on that.

Stephan Eger  
*Head-Investor Relations, Deutsche Telekom AG*

Robin, did that cover your questions?

Robin A. Bienenstock  
*Analyst, Sanford C. Bernstein Ltd.*

Yup. That's – and on the subsidy.

Timotheus Höttges  
*Chief Financial Officer, Deutsche Telekom AG*

The subsidy? [Foreign Language]

Stephan Eger  
*Head-Investor Relations, Deutsche Telekom AG*

Robin, can you repeat your question on the subsidies again?

Robin A. Bienenstock  
*Analyst, Sanford C. Bernstein Ltd.*

Yeah, sure. The question was just simply a comment on the fact that some of your peers have been moving to try to reduce subsidy in Europe and we're seeing more in the way of separation of handset financing from service plans in various markets in Europe and I was wondering whether you thought that was something that would be interesting for you and whether you could see that happening more in Germany as well.

Timotheus Höttges  
*Chief Financial Officer, Deutsche Telekom AG*

Sorry. Now, I've got your question. I think with regard to Germany, we are market leader here in Germany. And therefore, we are offering both. We have a clear SIM-only product which we have in the marketplace and the customer is paying then the handset full price. There might be even some promotions on certain stocks. But this is the one offer, so then the tariff is, at least, more attractive from a price point. But as a premium provider, it is very important for our customer base – and we looked at that one – to either offer subsidized handsets.

And I'll give you one example. We have a promotion including subsidies on iPads. We have a tariff points €39.99 on the monthly recurring charge. And if you commit to 24 months, you get the iPad for €99. And this is very well appreciated from our customer base and from an economic perspective, it is something which is attractive for us. So we are normally not looking on whether we do it with or without promotion. We are always looking on the payback of the cost or the amortization rate which we have with customers along their 24 months duration.

Stephan Eger  
*Head-Investor Relations, Deutsche Telekom AG*

Let's continue with Mathieu Robilliard from Exane. Mathieu?
Mathieu Robilliard
Analyst, Exane BNP Paribas SA

Yes, just one quick question, please. Within the U.S., it seems that cost base has declined by around $200 million year-on-year if I get my math right, $200 million. Could you quantify maybe how much of that is due to the fact that you now have a roaming agreement with AT&T that supposedly means lower roaming costs, and how much is due to lower commercial expenses linked to the value plans. Thank you.

Stephan Eger
Head-Investor Relations, Deutsche Telekom AG

No, as we said in the presentation, Mathieu, I think a good chunk comes from the value plans, a good chunk comes from the reduced network costs as we always said, due to the fiber link and there's also some indirect cost savings coming from the closure of call centers, staff reductions, et cetera. That's the level of details we want to give on that one.

Let's move on with Justin Funnell from Credit Suisse. Justin?

Justin B. Funnell
Analyst, Credit Suisse Securities (Europe) Ltd.

Thank you. Just – these are my questions, Level 4 in Germany, you're pursuing pretty well in broadband, TV, just looking at level 4 still, is there sort of strategic priority when you're looking at the opportunities that require level 4 operators? And should we expect you to be doing a deal in that area in the next 12 months?

And then secondly, your comment about the debate, fiscal debate about fiber in Germany was heating up. Could you give us a bit more color on that? Is it heating up in a good direction or a more worrying direction, please?

Timotheus Höttges
Chief Financial Officer, Deutsche Telekom AG

I think the first thing is we should not discuss fiber rollout separately. What we all should discuss is a tech cable, because we are not building the cable – sorry fiber, for its fiber purpose only. We're building it, keep our market share at a high level to be competitive in the environment, not only short term but even long term. So in this circumstance, we are not discussing fiber only. We are discussing the entire infrastructure and even the access to the level 4 as a kind of consistent program.

If you would now question whether in this approach to a tech cable, Tele Columbus would be a target for acquisition for Deutsche Telekom or a re-entry into cable as one of the answers. I will not comment on any kind of speculations which you might have seen in the news here. We are working on – in every areas on accessing the cable and not letting them grow significantly.

With regards to the fiber discussion, maybe, let me state something on the regulatory side, what it would take for us to grow our investments here. I think the biggest problem we have is that the German market is overregulated. And we are very vocal on that one, in the news, in the political situation, these times. If the market is asking for more fiber investments, the overall commercial environment has to change. And how could that be enabled? I think one of the arguments could be that we regulate cable and Deutsche Telekom symmetrically. Either we get out of the regulation in the market where we are facing infrastructure competition or that cable gets regulated the same way as we do.
Second I think we need risk sharing agreements. We are very much fighting on the so-called [Foreign Language] in Germany that if people want to use our infrastructure that they not only have to pay a monthly fee or a minute fee or a kilobit fee, but they even have to make a fixed investment commitment if they are buying certain bundles.

And what we need as well to reduce the overall costs is that infrastructure wholesale obligation should be get imposed for competitors so that everybody could use the other’s existing infrastructure being stacked or everything. This would significantly reduce the overall investment and to help us to realize the return on capital employed, that is the role we’re steering the fiber rollout today.

Justin B. Funnell
Analyst, Credit Suisse Securities (Europe) Ltd.
Thank you.

Stephan Eger
Head-Investor Relations, Deutsche Telekom AG
Thank you very much, Tim. Moving on to Ulrich Rathe from Jefferies. Ulrich, please?

Ulrich W. Rathe
Analyst, Jefferies International Ltd.
Thanks very much. My first question would be on the book-to-bill in T-systems and the order intake, any one-offs? It was one of the lowest in memory. Is this a weak quarter and are there any reasons to anticipate this to increase again or what inference might it have on the future of revenue performance of T-Systems?

My second question is, obviously the whole sector has saw that valuations have come down including DT’s. Has this in anyway increased your appetite for M&A? Are you now increasingly look at opportunities that probably do cross your desk every day or do you have potentially an unchanged view on that? I think you have ruled out sort of major M&A some time ago. Is that still true in the current environment? Thank you.

Timotheus Höttges
Chief Financial Officer, Deutsche Telekom AG
Okay. I think the Systems Solutions answers are very straightforward. The order entry always compares with the last year, and last year in the first quarter, we had a few big deals. I want to mention one big deal. This was the entire data center outsourcing of Everything Everywhere which we booked in that quarter. This quarter we haven't seen big deals compared like this one. We saw some deals like BRT in the first quarter. But one of the reasons is that we haven't had these huge deals. By the way, there is trend or the tendency in this industry that there are less big deals as the ones we have seen in the quarters before.

On top of that, I think we are focusing very much on improving the productivity on the existing big deals. You saw already the positive impact on that one in the first quarter. We had huge transition and transformation costs of that deals at the beginning. Now, we're on the phase on capitalizing on that one. So therefore, very much we're focused on quality and on profitability of the existing deals than rather now fighting for new ones. But nevertheless, I talked to Reinhard Clemens yesterday the order entry situation and he said he's not worried about his pipes towards the remainder of the year. They have some interesting things coming so, don't take quarter as a trend.

With regards to the M&A policy, our M&A policy stays completely unchanged and we are not planning any big acquisitions. What we are doing today and you see that we are very disciplined following our financial strategy which is, by the way, highly-appreciated on the bond market. We have recently accessed the U.S. bond market
with €2 billion. We had a five-year coupon at 2.9% and we had a 30-year coupon at 4.9%, only to give you an indication how cheap we could refinancing ourselves and including the break-up fee, this will help us just on the EBITDA – on the cash flow side to reduce our interest payment by more than €200 million already this year.

All of this is – we are very disciplined in focusing at further reducing our debt burden for the full-year 2012, so excess cash is used for that one. By the way, same is true for [ph] OTE (1:08:51) where we make great progress on reducing their debt position as well.

That doesn't exclude smaller deals. I think it makes a lot of sense to accelerate the growth in our digital business unit with some brownfield investments or some smaller acquisitions. This is always possible to accelerate the growth profile of our group and you will maybe follow that in our sub-segment documentation, which we have in our doc for the first time this quarter.

Ulrich W. Rathe
Analyst, Jefferies International Ltd.

Thank you.

Stephan Eger
Head-Investor Relations, Deutsche Telekom AG

Moving on to Peter-Kurt Nielsen from Cheuvreux. Peter-Kurt?

Peter K. Nielsen
Analyst, Crédit Agricole Cheuvreux International Ltd.

Thank you. Just one quick question, it seems you replied to the previous question on German broadband. Tim, are you seeing anything externally or internally in your base, any indications that would make you doubt that you can believe – maintain, let's say, net adds of about 30% plus and the current low churn rate on domestic DSL for the remainder of the year? Thank you.

Timotheus Höttges
Chief Financial Officer, Deutsche Telekom AG

Look, first, I think, the churn rate is definitely something which we precisely understand. We understand the customer base. We have a huge CRM system. We have a lot of innovative products, so it is not just a price competition. It has a lot to do with the service proposition but as well what the person is future in build when customer decides upon a German product or Deutsche Telekom product. And with Entertain, there was a lot of other innovative things. I think we are very confident that we could keep the churn rate at a level where we are today.

Now, the net add number is always depending on how fast a market is growing. If you have a very slow increase of new customers gross adds coming to the market, at the same churn rate, your net add number is always depending on this circumstance. I cannot guarantee the 30% net adds for the remainder of the year. We definitely fight for that one. It has to do with the overall growth of the market, and I think that the new price points and with the new offerings we have in the market, we are doing pretty well over the first four months in this year.

Peter K. Nielsen
Analyst, Crédit Agricole Cheuvreux International Ltd.

Thank you.
Let's continue with Paul Marsch from Berenberg. Paul, please?

Two questions, I wonder if you could remind me, the 36% VDSL coverage that you've talked about, what would that be as a percentage of the installed cable customer base? I wondered if you know that statistic? And what's scope do you have to drive VDSL speeds even higher? You're obviously investing and expanding VDSL coverage. Are you investing in driving VDSL speeds higher as well?

So a very quick answer on the VDSL question. The overlapping area with VDSL is 90% to 95% overlapping with the cable footprint. So, if you have in mind, do we have a competitive answer in this area with VDSL? Yes, definitely our VDSL coverage is in these areas and that is one of the reasons that we are increasing our VDSL coverage in Germany.

Are we investing more in VDSL speeds? Definitely, yes. You know and we laid that out in one of the last presentations, we are following a hybrid approach. So you see that already in the presentation of today, but even the last ones that from DSL we have improved to ADSL into 16-megabit. From 2-megabit, we went to 6-megabit at our, let's say, normal proposition. From ADSL we go to VDSL and in our laps, we are working these days on vector DSL as one of the opportunities to further extend the speed on our copper lines. And on top of that, we are even improving some fiber-to-the-home where it makes sense and where we have to build an entirely new network.

And on top of that, that is quite encouraging and we have to look into that one, we are working very intensely on partnerships. We have announced Chemnitz as one example, where the fiber link and the fiber access is built by a municipality or a local company and we are the exclusive distributor on this infrastructure. So then, we are not building but we are using high bandwidth. So in all this together, and in some areas even LTE as an answer, we have now a hybrid approach with bandwidth to attack cable in Germany.

That's great. Thank you.

So there's three more people waiting in the chain. Maybe let's get started with Andrew Parnis of UBS. Andy?

Yeah, hi guys. I've got two questions, both on the U.S. The first one which is on the branded contract net add losses fell quite significantly in Q4 into Q1, is this a number now you expect it to keep on falling or do you think sort of around, sort of 500 level instead of a reasonable run rate for the rest of the year?
And then the second question was just on the Verizon spectrum. They basically said that they're interested in selling off some of their 700 megahertz A and B licenses in the U.S. Is this something you would interested with even though maybe it’s not necessarily as an exact fit with the current spectrum you hold? Thank you.

Timotheus Höttges  
Chief Financial Officer, Deutsche Telekom AG

Okay, Andrew, I think a very clear statement. Our most important task in the U.S. is to improve our contract branded churn. There is no question. We’re seeing a big churn, I think it was 710,000 customers in the fourth quarter. We have seen 500,000 losses in the first quarter. And whatever we do, whatever number is, the first discussion is around improving the churn in the U.S.

And by the way, we have some encouraging developments. It's not that we see it accelerating. We see improving trends. But as I said earlier, we have to even consider that the total market, the gross adds market, the new contract gross adds is slowing down in the U.S. So even if we are reducing our net adds – sorry, our churn, if we are reducing our churn, if we are not seeing more gross adds in the market, then we are facing further churn in the U.S. environment.

So what does that mean? We cannot give you now a precise number on how many net adds losses we will see over the next quarters. But definitely, we are working on improvements. We are planning improvements internally, and we hope to deliver them over the next quarters.

With regards to your question on Verizon Wireless; they have announced that they may sell 700 megahertz spectrum in the A and the B block conditional on the spectrum core purchasing being approved. Whether this spectrum is interesting for us, first of all, we are not interested in the 700 megahertz spectrum at this time. This is an incomplete footprint and there is even interference with the channel 51 TV stations. So, honestly, this spectrum is nothing which would be attractive for us.

We need – we would like to see AWS spectrum coming to the market which would be adjacent to our footprint and this is definitely something that we would be interested in but on the 700 megahertz side, we are a little more reluctant.

Andy W. Parnis  
Analyst, UBS Ltd. (Broker)

Okay, thank you.

Stephan Eger  
Head-Investor Relations, Deutsche Telekom AG

Thanks, Andy. Let's continue with Jonathan Dann of Barclays. Jon?

Jonathan R. Dann  
Analyst, Barclays Capital Securities Ltd.

Hi there. A question on your LTE strategies; are you pursuing LTE – or why are you rolling out LTE at different spectrum bands in say the U.S., Germany, the U.K.? I mean it would seem that the new iPhones will presumably have LTE on the same bands. And then the second question, I was just going through T-Mobile press release in the U.S. It seems that bad debts have nearly doubled. What’s happening there?
Look, the first thing is I think on the LTE, that this is always something to do with the allocation of spectrum in the respective countries. And we have to deploy the spectrum we were able to acquire and therefore, it differs from market to market but there is a tendency and you would see that across our footprint that 1800 MHz and the adjacent spectrum band is the one which we are deploying.

With regards to the [ph] – yes (1:18:41), interesting while we are working on LTE on the latest – so we do not need a second chipset for this product. We could only deploy one chipset with the LTE band which we have which would be at ranges to the AT&T and the Verizon version. And we could use with this spectrum the standard products of Apple and which will be delivered into the market from 2000-whatever onwards on the 4G proposition.

Your second question was with regards to the G&A cost and whether they increased despite our cost cutting efforts. Year-on-year, there is an increase. We had higher bad debt expense associated with new products and changes in custom and mixed towers sub-prime. I'm only talking about U.S. here and sequentially with some higher personnel incentive expenses just remember, we had to retention as well and some renewal and upgrade commissions to be paid in the first quarter. So that is the reason that we have this contradiction or this difficulty to explain development on the cost side.

The last one is Hugh McCaffrey from Goldman Sachs. Hugh, please go ahead.

Thanks, guys, and two questions, please. Firstly, just in the U.S., can you give us any color on whether the iPhone switcher and I guess plans for this are still on target? Do you expect to launch that in Q3, Q4? And I guess, have you started driving spectrum refarming ahead of that?

And secondly, just on Congstar and T-Mobile in Germany, how do you think about managing the price gap between Congstar and T-Mobile? And what do you think is a sustainable price difference between the two brands. Thanks.

[indiscernible] (01:21:05)

Maybe I'll start off with the price gap between Congstar and the Deutsche Telekom brand or the T-Mobile brand. Yes, we think it is sustainable. You know that Congstar is our low frills brand. We see ourselves well positioned against the competition in the low frills segments so far; no need to change anything from this – from today's perspective.
Hugh, with regards to the question or the color on the U.S. strategy, T-Mobile in the U.S. we're planning to launch 4G HSPA service in the 1900 megahertz band in a very large number of markets by the end of the year in fourth quarter. With this launch, we will automatically have access for the iPhone switchers. So therefore, yes, definitely, this is in our strategy included and whatever we could do here to accelerate and whatever we could do to foster that, we will do. So a positive message in this regard, and was there a second reference ahead of the fourth quarter. No, I think that was answering your question, hope so.

Hugh I. McCaffrey  
**Analyst, Goldman Sachs International Ltd.**

Yes.

Stephan Eger  
**Head-Investor Relations, Deutsche Telekom AG**

Hugh, did it answer your question, sorry?

Hugh I. McCaffrey  
**Analyst, Goldman Sachs International Ltd.**

Sorry, yes. It was just on the spectrum refarming in the 1900 band. Have you started trialing that yet today? I understand there may be some risk of disrupting your customers as you do that? So just...

Timotheus Höttges  
**Chief Financial Officer, Deutsche Telekom AG**

No, no, I have just as a spontaneous all of my mind and from the business reviews with Philipp Humm and his team, they have started the trials and they were very encouraging. So they were network modernization trials in both east and west facilities have shown up to 33% increase in data feeds as well as improved signal quality and in-building coverage and we have seen even happy iPhone users that have blogged about it. So that is I say the official answer which I get from the U.S. team on that subject. So therefore, I think nothing to worry in this regard. The team is quite optimistic.

Hugh I. McCaffrey  
**Analyst, Goldman Sachs International Ltd.**

That's great. Thank you very much.

Stephan Eger  
**Head-Investor Relations, Deutsche Telekom AG**

Thank you, Hugh. Thank you, Tim. I think we are now coming to an end. Sorry for over-running. If there are still some questions out there, I think my team will note that and we'll call you right away. As always you know that there is a replay for this conference call and if you want to, we can also send you the script. Thank you very much, Tim. Thank you all in the room and thanks to our investors out there and see you either in London, Milan, Frankfurt, Oslo or New York in the next four days. Cheers. Bye-bye.

**Operator:** We'd like to thank you for participating in this conference. The recording of this conference will be available for the seven days by dialing Germany 49-1-805-2043-089 wire reference number 428685 and the pound sign. I repeat Germany 49-1-805-2043-089 wire reference number 428685 and the pound sign. We are looking forward to hear from you again. Goodbye.