Vodafone Group Plc

Offer for Kabel Deutschland

Analyst & Investor Conference Call

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Introduction

Vittorio Colao

Chief Executive Officer, Vodafone Group

Hello everyone, and welcome to this conference call. I am joined by Andy Halford, Philipp Humm and Jens Schulte-Bockum, the COO of Vodafone Germany. We are going to talk you through the Kabel Deutschland transaction, our plans for the combined businesses and the financial effects and then take your questions. I will be using the slides which are available on our website.

So starting on page two, let me run you through the highlights of this transaction, where we see six key factors supporting the acquisition case. Firstly, Kabel Deutschland is an attractive business well-positioned for further growth in Europe's business economy. It's present in 13 of the 16 states and has 7.6 million direct customers and its network capacity is over 15 million homes. The combination of a large cable footprint, long-term contracts and a strong growth track record and low but increasing penetration of new services is a very powerful one. Second, putting our business in Germany together with theirs would create a leading integrated player, with 5 million broadband customers, 7.2 million TV customers and over €11 billion of revenue in our most important controlled operation, and it is entirely consistent with our convergence strategy. It is also fair to say that Vodafone today does not have the depth of expertise in broadband networks and TV to maximise the opportunity across Europe, so I'm also delighted that Kabel Deutschland's strong management team would significantly enhance our capabilities in this regard. They will lead our combined consumer fixed business in Germany on completion. Fourth, this transaction represents in-market consolidation with significant and highly visible cost and capex synergies. As Andy will cover later, we see a normal run-rate of over €300 million of savings in the fourth full year after completion being comfortably achievable, with a net present value of over €3 billion.

This deal is also about growth. By bringing Kabel Deutschland under the Vodafone brand, adding our powerful distribution network and cross-selling our respective services into both customer bases, and reducing churn in the process, we believe we can generate substantial synergies, including synergies from cross-selling and increased customer loyalty with an NPV of €1.5 billion. Finally, the financial metric of the deal absolutely meet our M&A criteria for IRR and ROIC given the significant cost and capex synergies and the positive outlook for growth.

Moving to page three, which most of you will recognise from our last few results presentation. You will see the right hand side is becoming increasingly populated with evidence of our progress. As we have said before, our strategy is a market-by-market one reflecting the different conditions and opportunities in each market. Wholesale access is possible where we have either an open incumbent or an effective regulator but ultimately, some kind of incumbent wholesale deal will be necessary in all markets to maximise our geographical reach for next generation access. Where incumbent or regulation is moving slowly and economics make sense, we are deploying our own fibre, focusing, of course, on the densely populated area. We will pursue M&A when there is a clear value case and when it can enhance other approaches. Cable & Wireless, where integration is progressing very well and we are already marketing unified services and winning new business, has proven to be a really good one. We are confident that Kabel Deutschland, with its significant scale, high quality infrastructure and management expertise, can and will be the same. I would like now to hand over to Philipp to talk about specifically the German cable market and the combination of our two businesses.

The German Cable Market

Philipp Humm

Chief Executive Officer, Northern and Central Europe

Good afternoon everyone. Slide four lays out the clear attractions of cable in Germany. It's a secure platform in the German TV and fixed broadband market, marketable to well over half of the homes in the country, compared to around 2% for fibre and around 25% for VDSL. In terms of price and capabilities, cable is currently the best in class proposition in the market. It also benefits from low churn and long-term contracts due to the relationships with housing associations, which, for example, account for around 60% of Kabel Deutschland's direct customers. It is also, importantly, a future proof technology. Today, it can deliver up to 400 megabits per second and going forward there is a clear demand-led upgrade path to gigabit speed. This allows cable to offer the most advanced TV services today with the capacity and flexibility to allow for future innovation in entertainment, both interactive and broadcast.

Moving to slide five, turning now to Kabel Deutschland itself, it is the largest cable operator in Germany with a presence in 13 out of 16 federal states and it has the largest cable network in the whole of Europe. Its cable passes over 50 million homes. The network has already been bi-directionally upgraded for 11.2 million homes to make marketing of triple-play services possible, with a further 1.2 million to be added as part of a new programme already announced by the company. The business offers a great combination of a large and very stable existing base with 7.6 million customers and highly attractive growth opportunities. Penetration of internet, home phone and pay TV services is relatively low and innovations such as DVR are only just beginning.

Moving to slide six, and what gives us confidence in the future growth opportunity from adding additional services? It is the very low penetration of marketable services compared to other cable operators around Europe. Kabel Deutschland currently has only 1.4 revenue generating units, known as RGUs, per customer and Liberty in Germany already has 1.6. Both are low compared to median figure in Europe of over 2 and a best in class figure of 2.9. The ARPU in comparison is more dramatic, with most highly penetrated cable operators achieving ARPU nearly four times that of Kabel Deutschland. To some extent the gap in penetration reflects the German operators' relatively late move to update the networks and we fully expect it to narrow over time, as we push high-speed broadband and pay TV services into the base.

Moving on to slide seven, now let's look at how Vodafone Germany and Kabel Deutschland will offer nationwide services when the businesses are combined and unified under the Vodafone brand. In the Kabel Deutschland area, to leverage their cable platform, expanding the marketable footprint and increasing product penetration. In the others areas, we will use our VDSL agreement with Deutsche Telekom, which is expected to reach 12 million households in these areas alone by 2018. There is no doubt that the expertise that Kabel Deutschland's people bring will significantly enhance our TV and high-speed broadband services outside the core KD footprint. In the areas not covered either by cable or VDSL, we will continue to use ULL and bit-stream for DSL and this will all be enhanced by our market leading LTE coverage. As a result, we will have a strong nationwide offering combining the strength of advanced fixed and mobile technology.

Moving on to slide eight, as Vittorio mentioned in his opening remarks, we see an excellent opportunity to accelerate Kabel Deutschland's growth by combining our assets and expertise with theirs. Firstly, the Vodafone brand has nationwide recognition, allowing us to market next generation services in a much more impactful and efficient way, as we increasingly move to a consistent suite of services delivered over two main advanced technology platforms – cable and VDSL. Secondly, we will bring a massive step change in distribution scale within KD's coverage areas delivering a seven-fold increase in branded stores. Thirdly, the combination achieves really meaningful scale across the three pillars of fixed, mobile and enterprise with the growth and cross-selling opportunity that inevitability come with it. The revenue upside opportunity is substantial with an NPV of more than €1.5 billion from cross-selling and improved customer loyalty. Finally, the expertise of Kabel Deutschland's management is highly complementary to our own, bringing cable, TV and internet knowhow alongside our deep knowledge in mobile and DSL.

And now, I'm going to hand over to Andy, who will take you through the cost opportunities, new terms and timetable.

Business Review

Andy Halford

Chief Financial Officer, Vodafone Group

Thanks, Philipp, and good afternoon everyone. So onto the next slide, we've laid out the three broad areas where we see opportunities for substantial costs and capex efficiencies. Firstly, reflecting Vittorio's comments that this really is an in-market consolidation, we've seen significant value from combining elements of KD's network with Vodafone's. In the key areas of mobile backhaul and national and regional backbones, we can eliminate significant third party costs by instead using KD's footprint. We will consolidate IT stacks and begin to close down our co-location exchange activities, as we move off our ULL infrastructure. The combined value of these benefits will be over €120 million per year with an NPV of over €1.1 billion. Secondly, we see some very straightforward savings from migrating customers off our ULL and bit-stream DSL services and onto cable. Approximately 1 million of our 3 million or so DSL customers sit within the Kabel Deutschland footprint, giving run-rate savings of a further €120 million per year, with an NPV of more than €1.2 billion. Finally, the combination of central functions, as well as improved efficiencies in property and procurement, should generate a further €60 million plus savings annually, equivalent to an NPV of over €700 million. This gives a total NPV of cost and capex synergies, after taking integration costs into account, of over €3 billion. To put these into context, the year four run-rate is equivalent to only about 3% of the combined operating and capital cost bases of the two businesses, which gives us real confidence in their achievability.

Going now onto slide 10, so what are we paying and how does it work from a process and regulatory perspective? The offer is €84.5 per share, plus the final dividend announced back in February, giving a total value to Kabel Deutschland shareholders of €87 per share. Both the management and supervisory boards of KD support the strategic merits of the transaction. Technically, they cannot recommend the offer until the offer document itself is published, which is timetabled for early July. But they have indicated that they intend to do so and the management board intends to accept it in respect of their own holdings. The transaction will, of course, be subject to regulatory approvals, including merger control and a 75% minimum acceptance condition. We have also drawn up a business combination agreement, which sets out certain principles on the conduct of the offer and subsequent integration. With regard to the offer, this includes a non-solicitation obligation on the part of Kabel Deutschland in respect of third party transaction and a matching right for Vodafone in respect of a competing offer. It also secures cooperation in obtaining merger control approvals. Amongst the guiding principles for integration is our intention to respects the rights of employees, work councils and unions.

And so onto slide 11. Finally, the transaction absolutely meets our two key M&A hurdles with respect to IRR and ROIC. We also expect it to be accretive to EPS from the first full year post-completion after costs and capex synergies but before integration costs, and for free cash flow per share, it would be accretive in the second full year on the same basis. We expect to fund the deal from our existing facilities, leaving us with pro-forma net debt to EBITDA of around 2.4 times. With respect to the timetable, we expect to publish the offer document in early July. The offer period itself will run from the publication of the offer document for up to 10 weeks. But ultimate closing is not expected until the end of the calendar year given the timing of the merger control process.

With that, I'll hand back to the operator. In fact, I'll hand back over to Vittorio for some comments or do you want to go to the operator? We'll go straight to the operator and take your questions first. Thank you.

Questions and Answers

Andrew Beale, Arete Research

Hi, it's Andrew Beale from Arete. I just wanted to focus on your leverage. You quote 2.4 times, which I suspect will be nearer 2.8 on an IFRS 11 basis, but that number obviously excludes a few liabilities. I'm thinking of India tax, spectrum and German spectrum as the bigger ones, and obviously Verizon Wireless has been a great source of dividends for you in the last 18 months but again Verizon is talking about a leaner period of dividends after this one that's just about to be paid and they're talking about calling in the Verizon Wireless debt and perhaps holding back some resources for spectrum, perhaps 600 megahertz. So I guess my question is how we should we get comfortable that your leverage, which could peak above three times EBITDA, will come down? Should we be thinking about asset disposals, whether Verizon or India IPOs? I mean, what is it that gets the leverage down on a consistent basis?

Andy Halford

Yes, Andrew, I'm pretty comfortable actually. I mean, the 2.4 times that we've put in here sort of reflects the debt levels at the end of March, and reflects the Verizon Wireless dividend that's coming in in the next few days. Over the balance of this year and into next year, clearly we've got the cash generation for the rest of the business. Verizon Wireless, we do not know the timing of future dividends and yes, they've referred to a lean period but equally we have had one dividend payment during that period and as we go forward, net-net, this will be a cash contributing transaction in its own right. So I feel pretty comfortable we've still got headroom even on the 2.4 times multiple and therefore, I think the balance sheet is quite comfortably able to absorb this.

Andrew Beale

So disposal's not on the agenda or we should think about those as very much being on the agenda?

Andy Halford

No, I – you know, completely open mind. It doesn't move us in the direction of disposals any more than previously.

Andrew Beale

Okay.

Nick Lyall, UBS

It's Nick at UBS – afternoon. Just a quick one first on quad-play please. Is quad-play something you plan relatively soon or do you view quad-play in the German market as a bit more, it's a move maybe for later and you'll see how Deutsche Tel reacts first to the acquisition? And the second point was just on the slides themselves. I mean, many of the reasons here for acquiring KDG, you could say the same of, say, the Netherlands or Spain, so how do you reassure investors that you're not possibly going to do the same in multiple markets in Europe, particularly Netherlands and Spain, please? Thanks.

Vittorio Colao

Why don't I let Philipp take the first half and I take the second?

Philipp Humm

Yes. Now Vittorio said on the outset we're looking at it market-by-market, so what we do in Germany does not mean that we won't do the same in other areas. If you look at the German market, the German market is less driven really by quad-play but simply more by being in the position to offer customers very attractive high-speed broadband both on mobile and in fixed line. For us, KDG is simply a very, very attractive asset, growth asset, with a very superior network and as such also product offering. So the opportunity is great but it is already great from being able to sell broadband and TV services. Quad-play is, if you want, only the second step.

Vittorio Colao

And then, Nick, on the second point, how do we manage the read across and how do we reassure investors? I think that the best way to reassure investors is in general that we follow three principles: we look at good assets, and that's the way we look at things; we put things in the context of the relevance for us of the market; and finally, we look at the alternative strategies and the value of alternative strategies. So while the ambition is clearly to serve our customers, consumer and enterprise, in all of their needs, the assets that are required to do so might vary from one situation to the other.

Nick Lyall

Okay, that's great. Thank you.

Tim Boddy, Goldman Sachs

I wanted just to ask a little bit about looking forward and the opportunity over time to potentially acquire the parts of Germany where you're not present now. Is that something that you think in principle would make sense? And then I guess I'd like to ask Nick's question in a slightly different way, which is that – is there a reason why the synergies you've outlined don't apply in a number of other markets on a proportionate sort of basis, but it strikes me the challenge there is that you actually have a business that is much smaller than some of the cable competitors, particularly, say, in Netherlands, so would you consider selling assets to cable competitors in some of these markets to get the benefit of some of these synergies that you so clearly identified? Thanks so much.

Vittorio Colao

Yes, Tim, very good question. The rest of Germany I don't think today is a strategic issue. We have a very good deal with Deutsche Telekom for covering, whatever, you know, the 14-15 million homes that we will not – likely will not reach with cable. We are focused on – we will be focused on the integration. We have at this moment, you know, done what we thought was the best possible deal to get synergies and integrate a cable platform into a broader platform. On the other markets, I think it's a little bit the same answer that Andy gave before. We are open. We look at all the assets on a regular basis, all the markets on a regular basis, and we have only to make a judgment on what is the best strategic future for those assets and if some assets will be better owned by others, of course, we will consider but it is not particular or special for this type of decision. It applies also to, you know, the general discipline of Vodafone.

Tim Boddy

Thanks very much.

Jens Schulte-Bockum, COO, Vodafone Germany

Vittorio, this is Jens here. If I can add one comment on the synergy, I think it's important to acknowledge that the synergies in Germany are particularly attractive because a lot of them are derived from the fact that we are already present with a significant fixed network presence in Germany, including more than 3 million customers with a considerable overlap on the KDG footprint and, of course, the associated backbone networks that we can leverage and combine with KDG. So, I think it would actually be somewhat misleading to assume the same level of synergies can be read across other markets.

Vittorio Colao

Very good point Jens, thank you.

Stephen Howard, HSBC

Hi, everybody, and thanks for the call this afternoon. I just have a couple of questions. Firstly, what do you think the primary issues are likely to be in your discussions with the merger control regulators? And secondly, obviously, over the years, you've done a number of fixed line acquisitions, most recently, Cable & Wireless and so on and before that, things like some of the Tele2 unbundled businesses, and I was wondering if you could just sort of fill us in as to what you think are the most important learning points you've derived from those various acquisitions. Thanks.

Vittorio Colao

On the merger control regulators, I mean, unless Jens has a specific comment there, I would say that we don't expect the discussions to be very complicated because this is a combination of two companies that operate in different sectors and gives actually birth to a stronger player in the market that will be more competitive. We don't see dominance or any kind of competition concern to be very likely. I don't know, Jens. Do you have anything to add to that?

Jens Schulte-Bockum

No, you're exactly right. You know, if you look at the individual segments in which we operate, it's largely complementary. You know, Vodafone Germany has next to no exposure in TV. KD has next to no exposure in mobility. There is some overlap in broadband but, you know, the combined broadband access is less than 15% of the German market. So based on those observations, we don't see any grounds for regulatory scrutiny.

Vittorio Colao

Yes, on the lessons learned from Cable & Wireless, Tele2 and Arcor itself, I mean, I run the risk of being a bit generic here but I would say the real lesson learnt is the need to manage a very tight integration plan but not be too quick in dismissing assets that are unique to these companies. The best – I think, again Cable & Wireless is a good example, we have a very tight integration plan. We have accelerated the integration plan but we have basically merged or recreated some of their units within Vodafone because there are competencies and assets that are unique to those companies that we, of course, want to keep. Same applies to Tele2. We integrated Tele2 in different ways in Italy and in Spain and again, where we have been able to preserve the uniqueness and migrated under the Vodafone brand, it has been very good. Arcor is, you know, a good case as well. In general, the strength of the Vodafone brand is higher and the extend-ability of the Vodafone brand is higher than what some people are saying. So it's a brand that works well in the broader communications sector and in general the cost synergies are hard and with good solid integration plans, they show up pretty quickly. These, I would say, are the main lessons learned.

Stephen Howard, HSBC

Thank you.

Jerry Dellis, Jefferies

Good afternoon. I've got two questions please. One of the revenue synergies you've highlighted is the potential to cross-sell cable into the legacy Vodafone base. I wondered if you could confirm that legacy Vodafone broadband customers would need to sign new contracts before you can migrate them to cable, and I'd also appreciate your view on the potential challenges of getting them to agree to that. It seems that one challenge could be the fact that while Vodafone scores very highly in the independent surveys, KDG has been scoring quite poorly. Another practical obstacle perhaps is that legacy Vodafone customers might need to accept their new router being in a different part of the house and I wonder why they would put up that upheaval when they would have the choice of switching to a high quality alternative from Deutsche Telekom or Telefonica or United Internet or so on.

My second question is in appendix one, you mention that there's a €300 million adjustment to KDG's reported March 2013 debt and that adjustment relates to, I guess, pension liabilities and the estimated value of the LTIP. I wondered if you could clarify how much you've assumed specifically for the value of the LTIP at €87. Thank you.

Vittorio Colao

If I can comment on the first one, we think that customers will see a big benefit in migrating with the right offer from an ADSL offering into a cable high-speed high quality offering. So I think we believe that this will be of major value add to the customer base and we will be aggressively marketing it into our own customer base, and we assumed a certain churn, obviously, as we will make it not a mandatory offer but an offer customer will have to accept, and we've also assumed the cost of changing CPEs or cost of adapting the cable in the households. So that has been taken care of in the model, and the assumed revenue synergies.

Andy Halford

Yes, and on your second question, Jerry, the adjustment there, you're right, is primarily to do with things like pensions and LTIPs but we have not given the breakdown split between the two.

Jerry Dellis

Would it be okay just to come back on the first question, please? I'd just be interested, given that the, sort of, the "connect" and so on survey data is reasonably sort of, you know, detailed, why you take the view that the KDG broadband offering is particularly so high quality and how you get comfortable that the churn associated with the migration process will be capable of being very tightly contained. Thank you.

Vittorio Colao

If you take one point of evidence today, if you look at the net adds being realised in the German broadband market, all the net positive net adds are being done right now by the cable companies mainly. So if you look at last year, 300,000 net adds in broadband, 300,000 of these adds were by KDG. So that shows you that there is quite a high acceptance from a customer point of view for these products. We also know from our customers that they are very interested in moving to the next speed bracket, which is why we're pushing in both directions – VDSL on one hand but KDG on the other hand – to be able to fulfil the demand of customers and we will definitely work intensively with KDG's management to make sure that the customers will have a good experience in the process.

Jerry Dellis, Jefferies

Okay, thank you.

Vittorio Colao

Thank you.

John Karidis, Oriel Securities

Good afternoon. Thanks for taking the question. It's actually two questions but I think they're related. Looking at the valuation of the deal, I work it out to be just over 11 times EBITDA and I just sort of wonder, granted the synergies are substantial but I find it seems like the value of those synergies is being given to the KDG shareholders rather than retained by Vodafone. Is there anything you can say on this, please, to help me? And then, secondly, given that you've decided to buy KDG that covers 40% of the market only and I guess less of GDP, what shall we sort of deduce about what you think the value of your wholesale agreement is with Deutsche Telekom? Thank you.

Vittorio Colao

Why doesn't Andy get the first one and then Philipp and I will answer the second one?

Andy Halford

Yes, so John just on the first one – yes, a multiple on sort of unadjusted published numbers about 11. Clearly, we are very much of the view that there are significant both cost and capital synergies but cost, in terms of the EBITDA, if you adjusted for those, you'd get a number more like eight times multiple. Exactly how much is being paid away depends, sort of, what you regard as being the base price of the business and how much is the premium but the collective of the €3 billion of the cost synergies and indeed the €1.5 billion of the revenue synergies, they are very, very big numbers on the upside there and it is only a proportion of those that are being paid away. So I think there is still a significant amount of value retention here for Vodafone.

Vittorio Colao

On the second point, I'll just ask Philipp to comment but let me say the agreement with DT remains very strategic, which is also why we are very keen to complete it, because, of the 40 million homes in Germany, KDG only covers a small fraction of it, a percentage of it. In the remaining part, in the KDG area and outside of the KDG area, clearly the vectoring agreement with Deutsche is very important and actually KDG upgrades our strategy after the DT deal. So I see them as complementary and actually mutually reinforcing.

Philipp Humm

I mean, approaching the customer going forward, we will basically use three networks. One is the KDG network, as Vittorio said, covering about 30 million plus households marketable. We'll have the DT VDSL deal, which should be 14-15 million addressable customers and, for the rest of the country, we'll continue to be able to rely on ADSL, which they have, for example, quite an attractive proposition in the market of ADSL/satellite. And last but not least, don't forget that we are already now covering 69% of the country with LTE. So we will have all four technologies in full play in the market to be able to offer customers a pretty ubiquitous proposition across all networks.

John Karidis

Thank you.

Ottavio Adorisio, Societe Generale

Hi, good afternoon, gentlemen. I have a couple of questions. First, I would like to follow up from a previous one. It's on the NPV of the cost synergy. Today, you say that you're targeting almost synergy that awards around €30 plus per share. Therefore, I would like it if possible if you can comment on the fact why you've not tried to acquire the asset before and ideally, when you look at it in 2010, consider the synergy you are targeting will be worth more than the IPO share price.

And the second one is on the backhaul. You say that Vodafone will benefit from cable network, which will provide transmission capacity for your base station at a considerably lower cost, tripling the market rate for least capacity. Therefore, could you just comment on the fact that in all the other markets, the integrate operators can access this backhaul at a much lower price? That means that Vodafone is at a cost disadvantage versus these particular operators.

The third one is pretty quick on the impact on EPS. You provide the impact without the application of purchase accounting. If you can just give us some colour about what would be the final impact when that particular accounting has been implemented. Thanks.

Vittorio Colao

Yes, certainly, on the first one, yes, we looked at KDG before and we also looked at basically everything that moves in every market where we are or which are relevant for our own strategy. As everything in life, there are priorities. There are times when things are mature and times when things can happen and times when things cannot happen or there are other priorities. So the good news is that this is a pretty solid deal on cost and capex grounds. Maybe the other questions are for Jens. The only thing I want to stress is don't forget the earlier comment that Jens made. Vodafone Germany is a company which is already in fixed line and has a huge amount of traffic already, much higher than any other Vodafone operating company, because of its fixed line 3 million customers and presence. So the relevance, the comment on the relevance of backhaul, you have to put it into the context of the specific market. Hence, we say it's always a market-by-market thing. India is different from Germany because the nature of the business in India is different and the data loads are different in India. So everything has to be balanced. Do you want to comment, Andy or Philipp, on the backhaul thing?

Philipp Humm

Yes. Why I don't start and then Jens can take over then? I think the important thing is that we are trying to put together two networks using each other's existing networks, so better utilisation and closing what we either rent or buy from other providers, right? So the advantage is really in merging the networks and using the own infrastructure, and it doesn't imply that we have a cost disadvantage in the market at this point of time. Jens, do you want to comment further?

Jens Schulte-Bockum

Yes. I think the subtlety here is that we basically can replace what is currently opex, that we pay for leasing lines to connect pay stations through capex or, you know, fibre plants that already exist. So, I mean, it's a straightforward make or buy type of consideration here, and of course we take the advantage here of fibre plants that already exist inside KDG, and I think on a forward-looking basis the economics of building our own fibre plant are obviously improved because that would serve both Vodafone mobile pay stations, as well as the capacity extension in the co-ex network.

Frank Knowles, New Street Research

Hello, yes, this is Frank Knowles from New Street Research. I actually had one specific question on regulatory approval, whether you would expect that the Federal Cartel Office in German would have a role in looking at this deal or if you think it would just be a European scrutiny. And then, secondly, I wonder if you could just clarify a couple of things that have been asked already. Did I understand that you would force migration onto some Vodafone customers currently served by DSL in order to make sure you can disconnect the central office equipment and, if so, how would that work in practice in terms of needing to maybe do rewiring inside homes and so on, in order to allow that to happen? And lastly, I didn't quite follow the reasoning on why you wouldn't look to buy Unitymedia as well. If the economics of the transaction for KDG are so compelling, I didn't quite follow that wouldn't also be the case in the Unity regions, because obviously the wholesale DT deal is not as good as buying KDG in KDG regions. Thank you.

Vittorio Colao

Jens, why don't you take the German question and then I will go on the Unity and the approval?

Jens Schulte-Bockum

Yes. I mean, from a regulatory process, we will have to file this with the European level first and it is possible that the Federal Cartel Office in Bonn ask for referrals, so that – we have not necessarily assumed that but it's possible. And in terms of the overall process duration, we take the view that the process should be finalised by the end of this calendar year, so that doesn't seem to impact our timetable in a significant way. On the question of forced migration, we aren't assuming a forced migration but, as Philipp explained earlier, we will go out of our way to incentivise customers to move from the current DSL plant onto cable and the way we can do this is by offering the customer a substantially better experience – higher speed experience, additional product characteristics – at the same or a better price. So, you know, we are quite confident that the vast majority of customers can be swayed over the time period that we've assumed here and, again, we've taken some level of churn into account for areas where, you know, that is not leading to the customer satisfaction or where it should not be possible. So that's the current assumption on customer migration.

Vittorio Colao

Yes. On Unity, I mean, it doesn't seem to me the priority today. We need to integrate, complete first this transaction, integrate and extend the services. Today, it doesn't seem a doable or appealing thing. In the future, I mean, never say never but we are talking about immediate priorities being different.

Frank Knowles, New Street Research

Thank you.

Lawrence Sugarman, Liberum Capital

Good afternoon. Two questions please. You set out clearly the management structure with KD taking the control on the fixed side and Vodafone management in Germany on the mobile side. Clearly, part of this deal is focused on achieving a convergence strategy. Ultimately, do you think that there is the management expertise within both of these business to focus on that or do you think that that skillset will actually have to come from outside? And secondly, just returning slightly to the question Ottavio asked around looking at what actually drove you to make this decision now. You've talked about different situations and the opportunities that exist for the group as a whole but is there anything that is actually specifically that you see as developments within the German markets that has meant that it is more attractive now to do this than even as much as, say, three or four months ago?

Vittorio Colao

Well, let me – well, Jens can prepare the answer or Philipp can prepare the answer to the first question. Let me get the second one. There's not a three month, four month window that we see. We just see Germany as our, you know, main country. We have a very strong team there. We have already a fixed line business. We have launched LTE; LTE is starting to get some traction. So it was now but when I say now it means, you know, months, not the last four or something like that. Now, it seems the right time to move with a transaction that will strengthen our best platform in one of Europe's more solid countries, but again, it's not 'now' this week, it's a strategic 'now'. Jens, any comment on the management structure or, Philipp, more in general our approach to fixed mobile convergence from an organisational point of view?

Philipp Humm

Let me start and then pass on to Jens. I think, overall, we have a pretty formidable team here with KDG being the market leader in the TV space, with Vodafone being market leader in mobile, with the two of us being a very strong number two in broadband. So I think from a knowhow point of view, from a skills point of view, we have all we need to compete very, very effectively in the German markets, and we will try to leverage the knowhow of that team as much as we can for other areas in other regions, in our portfolio. So, that being said, we'll probably have to adapt here and there as every market is different, every market is local, with the necessary local knowhow, as things are needed. Jens, something more specific?

Jens Schulte-Bockum

Yes, two comments. The first one just to clarify, we see KDG and the KDG management team as the future hub for the fixed consumer business. In enterprise, we are already operating on a fully converged space inside Vodafone. We have a significant fixed business in enterprise and the share there is much higher and a lot of the products that we offer in enterprise are already, you know, fully unified communication products. If I come back to, you know, the convergence or converging strategy longer term, you know, we do see significant multi-screen concept opportunities. We see opportunities around leveraging, you know, KDG's plans for wi-fi and for amending our, you know, data platforms, you know, across different bearers. So there are a number of opportunities on the table and we are quite confident that we can address those with the teams at hand.

Lawrence Sugarman, Liberum Capital

Thank you.

Mandeep Singh, Redburn Partners

I just want to come back to M&A and leverage overall. I mean, you've said you're very comfortable with your pro-forma leverage of 2.4 times. This is clearly quite a significant transaction, I think the fourth or fifth biggest deal that Vodafone has ever done. Is it just fair to say, and please do clarify, can you do more material acquisitions without selling Verizon Wireless? I just wanted to get clarity on that, please.

Andy Halford

Mandeep, I think the way we look at is the issue number one is whether there are transactions out there that are strategically needed by us and can create value. Secondly is the issue as to how we stop them but I think, absolutely, it should be in that order. Clearly, this puts the level of debt in the group up a reasonable amount. It does not put it up absolutely to any sort of limit, so there is still some flexibility there. So I'd say over the next few quarters that we are in a reasonable position with the debt level. It does not rule things out but equally, you know, we need I think to press on and close this transaction.

Mandeep Singh

Thank you.

Vivek Khanna, Deutsche Bank

Hi, good afternoon, everyone. Sorry, just a quick question on organisational structure if I may. You have indicated that you expect KDG to remain a legal entity, you know, post this transaction but when it comes down to synergies, also it does say that you need full legal integration in order for that to be achieved so just – I'm just trying to understand as to what is the future of the KDG holding, KDG AG, pardon me, and more importantly, the KDGVS GMBH entities going forward, if, as part of the realisation of the synergies, whether those would sort of, you know, disappear in due course?

Andy Halford

Yes, I think that, to some degree, it's just getting through it all over time. You know, first of all, we need to go through the process of getting the offer document out and getting the shareholders in KDG to vote on it. We have agreed the principles that will be applied during the integration process and that will then be the next step, and then finally we'll get on with the full operational side. So I think this is something that is just going to evolve over a period of time and we'll do things in a sensible, pragmatic way.

Vivek Khanna

Thank you very much.

James Britton, Nomura

Hello, thanks very much. Can you hear me okay?

Vittorio Colao

Yes.

James Britton

Excellent. My questions are, firstly, will you accelerate the use of tax losses in Germany with this transaction and can you just clarify the tax loss carry-forwards that you require? Secondly, on capex, why are you comfortable that there won't need to be a Project Alpha every couple of years? I mean, capex hikes do seem to be the rule of cable companies rather than the exception these days. And then thirdly, on regulation, how long do you think it will be before European regulators and competition authorities share your view on integrated communications and regulate on that basis? I understand that they are in the midst of revisiting market definitions this year. Thanks.

Vittorio Colao

Yes, so Andy, Philipp, and then myself.

Andy Halford

Yes, so James on the tax, we have not assumed any use of pre-existing tax losses that the KDG business may or may not have and we have just applied the normal tax rate as we go forwards.

Philipp Humm

Yes, and from a network point of view, we have today already a very modern network, which is largely upgraded to DOCSIS 3.0, at 87%, so we're just growing the percentage there. Second, we have a network, which is underlying on 862 megahertz of spectrum capacity, which can be made to use. So we've carefully looked at the necessary investments on the network side and feel quite confident that we will not see such a spike following the Alpha investment, which the KDG management has pulled forward now over the next three years, of 300 million. And to remind you, in cable, about two-thirds of the capex you're looking at is capex which is typically CPE or success-based, ex-CPE or commissions or other things. A third is something which highly depends on the success you have on gross adds and net adds, which then drive, or not, the capex variations.

Vittorio Colao

Yes, on the regulation view, I expect the European authorities to come with their views towards the end of the summer or beginning of the fall, but let's say September. I expect them, based on our contact with them, to be more understanding of the need to consolidate, to invest and to have better returns on capital. I also suspect them, and I think it's good, that they will not compromise the above with reduction in competition, which is why this transaction leaves me confident because this would in any way reduce competition. If anything, it's trying to be a possibility of the KDG and the Vodafone offers to be more appealing in the market or, if you want, our infrastructure to be more efficient once it's merged. So this should be consistent 100% with the new approach that Vice-President Kroes is proposing.

James Britain

Okay. Can I just ask one follow up on the tax situation? Can you just clarify the tax loss carried forward for KDG? Thanks.

Andy Halford

No, it's not relevant here. We are sure that they won't be carried forward.

James Britain

Okay, thanks.

Mandeep Singh

Hi, sorry, I just wanted to come back to the leverage and the M&A question again, because I'm a little bit confused. If my understanding is correct, you've previously said, you know, you would go – be willing to go from A- to BBB+, say, for the right transaction – clearly, this is the right transaction in your mind – but that you would target getting back to A- and that remains your target rating over some period of time. I just wanted to find out if you were willing to reconfirm that as a soft guidance target and maybe give us some sort of timetable over which you would prefer to get back to A-?

Andy Halford

So, directionally, yes, what we have said is we are prepared to go to BBB+ for a period of time with a view of going back to A- over time. We have not gone specifically into time and I think it's probably inappropriate to go specifically into time. Our mind would be, though, that we head back in that direction over a period.

Mandeep Singh

Thank you.

Justin Funnell, Credit Suisse

A couple of just clarifying questions. I missed the start of the call, so maybe it was covered. Do you have any idea at this stage, please, what percentage of the KDG customer base are Vodafone customers and what percentage of Vodafone Germany customers are on KDG? What's the size of the cross-sell opportunity please? Secondly, the synergies, obviously they are a mix of opex and synergies. Have you given a steer on the percentage of that as opex? Could we have seen the large majority is opex or not? Was it more 50/50? And thirdly, as you say during the conference call, it's only about 3% of the combined opex and capex; you're pretty confident about them. I'm just wondering if, you know, you could see more upside out of this, really; it seems to be quite a small amount of cost cutting. Are you being conservative to start with or actually are you a bit constrained by the commitments you're making to the works councils, please?

Vittorio Colao

I would say the first two questions are perfect for Jens and the third one for Philipp and myself. So Jens, why don't you start?

Jens Schulte-Bockum

On the respective cross-selling potential and customer overlap, we have no particular reason to assume that the distribution of the respective customer bases is different. That said, we enjoy, as Vodafone, higher market shares on average in the KDG footprint, particularly in the north and east of Germany, so that helps the case. We take these numbers, you know, carefully into consideration. I think for verification purposes, I think it's relatively safe to assume the average market shares and then do the maths based on those.

Vittorio Colao

To your other two questions, on the synergy, opex and capex, we do not give a breakdown between the two.

Andy Halford

It's majority opex, I'm pretty [sure]–

Vittorio Colao

Majority is opex but we don't give an exact breakdown and overall, the way we have calculated the synergies, also the cost and capex synergies, would consider them to be realistic, and we traditionally try to over-deliver on our promises and we would want to continue to do that as well here.

Justin Funnell

Thank you.

Vittorio Colao

Well, first of all, thank you all for your questions. Let me close by emphasising the rationale again for this transaction. First of all, Kabel Deutschland is a highly attractive business with significant growth prospects. Together, we will create a leading integrated player in Germany, which is our most important market. We're also bringing on board a strong and experienced management team who will lead our consumer fixed line business in Germany. This is an in-market consolidation case with significant cost and capex synergies but we also see opportunities to accelerate Vodafone's and Kabel Deutschland's growth in Germany. And finally, the transaction is value accretive for Vodafone shareholders and meets all of our M&A criteria. Thank you very much for your time, for your questions and I look forward to meeting you individually. Thank you.