

freenet **GROUP**



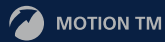
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GRAVIS

TLTALKLINE

freenet
digital



Interim report as of 30 June 2014

2nd quarter 2014

freenet AG • Hollerstraße 126 • 24782 Büdelsdorf

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Key financials: Group overview

Result

In EUR million/as indicated	1st half 2014	1st half 2013	Q2/2014	Q1/2014	Q2/2013
Revenue	1,444.7	1,584.9	727.2	717.5	809.6
Gross profit	373.0	349.8	190.5	182.5	177.0
EBITDA	173.1	170.4	87.6	85.4	85.2
EBIT	140.7	142.7	71.2	69.5	71.7
EBT	120.5	122.6	60.5	60.0	61.5
Group result from continued operations	114.5	115.6	57.1	57.4	55.4
Group result from discontinued operations	0.0	0.0	0.0	0.0	0.0
Group result	114.5	115.6	57.1	57.4	55.4
Earnings per share (€) (diluted and undiluted)	0.89	0.90	0.44	0.45	0.43

Balance sheet

In EUR million/as indicated	30. 6. 2014	30. 6. 2013	30. 6. 2014	31. 3. 2014	30. 6. 2013
Balance sheet total in € million	2,469.5	2,389.7	2,469.5	2,520.9	2,389.7
Shareholders' equity in € million	1,168.5	1,115.7	1,168.5	1,297.0	1,115.7
Equity ratio in %	47.3	46.7	47.3	51.5	46.7

Finances and investments

In EUR million	1st half 2014	1st half 2013	Q2/2014	Q1/2014	Q2/2013
Free cash flow ^{1,2}	131.3	126.8	74.2	57.1	70.4
Depreciation and amortisation	32.4	27.7	16.4	16.0	13.5
Net investments ² (CAPEX)	10.5	6.0	4.7	5.8	3.4
Net cash ^{2,3}	-545.3	-537.2	-545.3	-424.9	-537.2

Share

	30. 6. 2014	30. 6. 2013	30. 6. 2014	31. 3. 2014	30. 6. 2013
Closing price Xetra in €	23.23	16.78	23.23	25.39	16.78
Number of ordinary shares in '000s	128,061	128,061	128,061	128,061	128,061
Market capitalisation in EUR'000s ³	2,974,857	2,148,864	2,974,857	3,250,829	2,148,864

Employees

	30. 6. 2014	30. 6. 2013	30. 6. 2014	31. 3. 2014	30. 6. 2013
Employees ³	4,904	4,516	4,904	4,961	4,516

Key financials: overview Mobile Communications segment

Customer development

In million	1st half 2014	1st half 2013	Q2/2014	Q1/2014	Q2/2013
Mobile Communications customers ³	12.99	13.56	12.99	13.13	13.56
Thereof Customer Ownership	8.84	8.56	8.84	8.79	8.56
Thereof contract customers	5.90	5.81	5.90	5.87	5.81
Thereof no-frills customers	2.94	2.75	2.94	2.92	2.75
Thereof prepaid cards	4.14	5.00	4.14	4.34	5.00
Gross new customers	1.42	1.63	0.73	0.69	0.86
Net change	-0.31	-0.52	-0.15	-0.16	-0.15

Result

In EUR million	1st half 2014	1st half 2013	Q2/2014	Q1/2014	Q2/2013
Revenue	1,418.5	1,569.1	714.5	704.0	801.6
Gross profit	350.9	339.3	179.5	171.5	171.5
EBITDA	181.9	168.7	91.3	90.5	85.6
EBIT	154.4	142.9	77.5	76.9	73.1

Monthly average revenue per user (ARPU)

In EUR	1st half 2014	1st half 2013	Q2/2014	Q1/2014	Q2/2013
Contract customer	21.4	22.4	21.5	21.2	22.5
No-frills customer	2.9	3.5	3.0	2.9	3.6
Prepaid card	2.8	2.9	3.0	2.7	3.0

¹ Free cash flow (FCF) is defined as cash flow from operating activities minus investment in property, plant and equipment and intangible assets, plus proceeds from the disposal of property, plant and equipment and intangible assets.

² This information relates to the overall Group (including discontinued operations).

³ At the end of period.

To our shareholders

From left to right: Joachim Preisig, CFO; Christoph Vilanek, CEO; Stephan Esch, CTO



Letter to shareholders

Dear shareholders, business partners, customers and friends of freenet AG,

In 2014, Europe's biggest telecommunications magazine, connect, asked its readers and users—as it does every year—to vote on the best products, networks and services in the internet and mobile communications fields in a grand total of 26 categories. For the sixth consecutive time, our main brand mobilcom-debitel had the distinction of being named the “best mobile communications provider/retailer of the year”.

How does a company secure this position for itself in a market that is shaped like almost no other by unrelenting dynamism, fierce competition and great challenges? A market where the saturation level in the traditional mobile communications segment is now 1.4 mobile connections per citizen for mobile phones, smartphones and tablets. Where the ARPU—average revenue per user—have been falling continuously for years because customers, for reasons of transparency and cost security, have been inquiring more and more keenly about flat rates at affordable prices.

On the other hand, it is also a market that boasts the fascinating possibilities of digital lifestyle, which is increasingly shaping our day-to-day lives and making them easier: we now use mini mobile computers not only to surf, but also to shop, book and pay, to make our homes more comfortable and safe, and to perform tasks for our work and studies, for entertainment and when we travel. And where, as a result, the data volumes transmitted using mobile devices are currently increasing by around 20 per cent a year.

As the biggest network-independent telecommunications provider in Germany, freenet AG has been overcoming these challenges successfully for several years and has adopted the appropriate strategic orientation: in the traditional business segment of mobile communications, our main brand now devotes its attention particularly to high-calibre contract customers—for example by establishing the Allnet tariff structure, which covers individual usage profiles of all kinds with attractive, made-to-measure flat rates. Our lower-priced discount brands, on the other hand, are aimed predominantly at price-conscious smartphone users via online sales channels.

In addition to this, we are operating with increasing success in the digital lifestyle segment with innovative products and user-oriented services. Across all of our segments, moreover, we have continuously improved our services, product and service diversity and proximity to customers over the preceding quarters and years. We have achieved this not least by making prudent acquisitions such as the GRAVIS retail chain and Motion TM in 2013 and freenet digital Group at the beginning of this year.

The fact that we are doing very well in the competitive environment with this strategic positioning and are successfully executing our goal of sustainable profitability year in, year out is demonstrated once again by our figures for the second quarter of 2014:

- gross profit increased significantly compared to Q2 2013 and amounted to 190.5 million euros, equivalent to a gross margin of 26.2 per cent;
- EBITDA rose to 87.6 million euros, and
- the free cash flow continued with its positive development, totalling 74.2 million euros.
- We achieved this positive development despite the fact that at its current level of 21.5 euros, postpaid ARPU was again down compared to the previous year in line with the general market trend.

As a result of this ARPU trend and especially due to the waiving of revenue in the low-margin hardware segment, our revenue is below that posted in the same quarter of 2013 at 727.2 million euros.

Based on the cumulative figures for the first six months of 2014 with an EBITDA of 173.1 million euros and a free cash flow of 131.3 million euros—we confirm the figures of our guidance for 2014 financial year, with an EBITDA of around 365 million euros and a free cash flow of some 265 million euros. Hereby, we once again lay the foundation for our shareholder-value-oriented dividend policy that further provides for a distribution of between 50 and 75 per cent of the free cash flow. Accordingly, freenet AG's Annual General Meeting 13 May 2014 resolved to make dividend payouts amounting to 185.6 million euros; this corresponds to 1.45 euros per dividend-entitled share or 72.5 per cent of the free cash flow of 2013.

We are particularly pleased with how customer ownership is developing. The number of customers in the postpaid and no-frills segment rose further in the second quarter of 2014 by around 50,000, taking the figure to 8.84 million. The number of contract customers contained therein could be increased in the same period by 32,000 to 5.90 million. It is the eighth quarter in which growth could be realized. We see this as an affirmation of our strongly user-oriented charges and tariffs, which we regularly enhance even further as part of special promotions—and with which we frequently achieve top rankings in the trade journals' independent comparative tests.

At the same time, this development confirms that we are right to keep working consistently on the improvement of our products, services and internal processes.

In the second quarter, for example, we broadened our portfolio to include a complex security package in the home automation field in response to the rapidly increasing number of home burglaries in Germany. With "SmartHome Sicherheit"—as our new digital lifestyle product is called—the smartphone is advancing to become the control centre for monitoring and security within people's homes. In line with the modular principle, customers can assemble a wide range of components according to their needs.

The product's basic components comprise:

- an alarm siren,
- a WiFi-enabled camera with motion detector and night vision,
- two further motion detectors and
- an opening detector for doors and windows,
- two remote control units for activating and deactivating the system,
- an alarm button for assaults and
- a cloud solution for the secure storage of the recorded material.

Further essential services, such as checking and monitoring by a security company and an insurance for emergency repairs after a burglary has taken place, complete the package.

We have also enhanced our product range in the entertainment area by adding a further games option: Game Pack Basic is now available to beginners as an inexpensive variant costing around 2 euros per month so that they can try out online games on their smartphones. In addition, they can download two games per month from the extensive range offered by the games supplier Gameloft.

For a service provider such as freenet, being as close as possible to customers is an essential part of our business model. That is why we work continuously on the optimisation of our presence and our selling interface at heavily-frequented, sought-after locations. Against this backdrop, our subsidiary GRAVIS signed an agreement in the second quarter to acquire up to twelve retail units of the former Apple premium reseller reStore. This increases the number of GRAVIS stores in Germany from 34 to up to 46. Including the mobilcom-debitel shops, the number of directly controllable stores in the Group will increase to around 610. We are going to gradually revamp the shops that have now been acquired—and broaden their product and service range to include digital lifestyle products, from other premium manufacturers, mobile offers and service solutions. The tenor of these changes is exemplified by the new GRAVIS store in Rostock that opened in May; there, on 165 square metres of floor space, customers can find Apple, Samsung and Sony products complete with the right accessories.

The range on offer there includes services such as repairing damaged hardware and providing individual training measures. On Mother's Day, for example, GRAVIS staged a promotion with gift vouchers for individual training in the use of smartphones and programs such as Pages, iMessages, Photoshop, Aperture and the Android operating programs. The training activities are provided entirely in accordance with the needs, wishes and time preferences of the prospective participants—either in the stores or in telephone-supported online courses at home. The beginners' service starts at 60 euros for one hour and participants are only charged for the time actually used, on a minute by minute basis.

Needless to say, extensive advice free of charge is available in our shops—for example on the roaming charges that have been reduced in price, on properly telephone use during trips abroad, and on “spring cleaning” for smartphones, which involves the decluttering of apps and memories, the elimination of waste data, battery care and other precautionary measures. In June, GRAVIS also gave away another 100,000 digital subscriptions to the magazines iPad Life and iPhone Life on its website.

In the months ahead, we are going to enhance the service in our shops even further with another project: Click & Collect. This is designed to combine the comforts of online shopping with the advisory and shopping experience of an actual retail outlet by having customers pick up the goods that they ordered online in a mobilcom-debitel shop of their choice, while also being able to take advantage of the in-store employees’ advisory expertise. Click & Collect is embedded in our long-term multichannel model “N@xt”: the purpose of this is to help us develop more quickly into a multichannel retailer that will henceforth guide our customers reliably through all the further points of contact, irrespective of where and when they first came into contact with us—internet, hotline or shop.

Telefónica Deutschland has received the conditional approval for the takeover of E-Plus Group from the European Commission in early July. freenet will utilize this step of market consolidation to improve its own competitive position. The terms of the transaction guarantee freenet an extension of the existing business relation with Telefónica Deutschland until 2025, including the availability of the most current technical standards.

This brings us back to the initial question—about the reasons for the recurring awards: it is the variety of small activities and large steps, the tireless work on improvements large and small in the interests of customers, that ultimately come together in a coherent overall picture—comparable to a mosaic.

Furthermore, we—the management and every single employee—continuously devote all of our strength, expertise and experience to making our common undertaking a little bit better. Day by day, month by month, year by year! Today and in the future, too!



Christoph Vilanek



Joachim Preisig

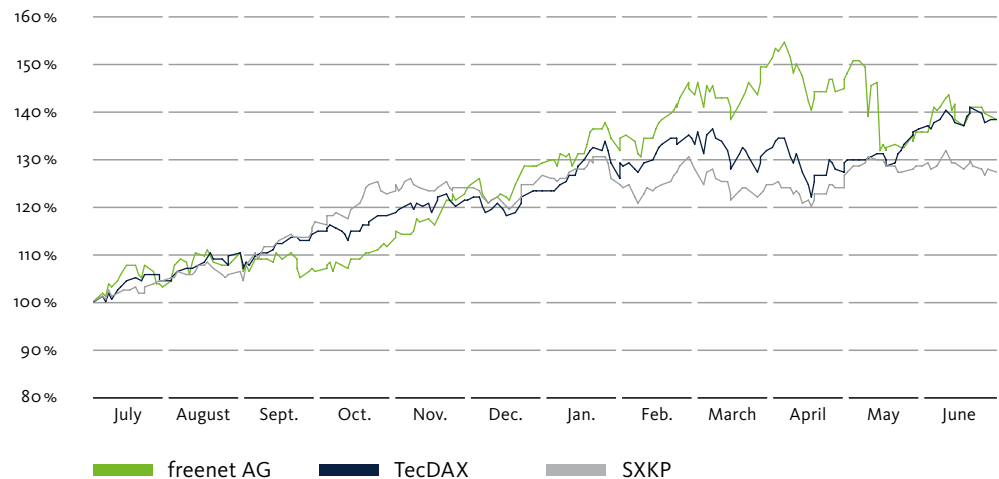


Stephan Esch

freenet AG on the capital market

Performance of the freenet share

Figure 1: Performance of the freenet share over the past 12 months
(indexed; 100 = Xetra closing price on 30 June 2013)



German stock market

In the second quarter, the basic economic trend in Germany was positive. However, this prevailing mood, which was sustained, among other things, by the findings of the business survey conducted by the Association of German Chambers of Industry and Commerce (DIHK), could not be maintained throughout the quarter under review. As a result, the expectations for real gross domestic product are now at around the level of the first quarter.

Accordingly, investors on the German stock market were increasingly unable to discern any encouraging optimism during the quarter. After the DAX, the leading German index, had briefly passed the 10,000 points mark, the mood latterly showed a marked downturn among both institutional and private investors. Against the background of the high dividend payouts in the second quarter, domestic institutional investors in particular showed themselves to be notably active in that quarter.

As well as the existing structural economic policy risks affecting the eurozone, dealing with the geopolitical risks in Eastern Europe, too, is likely to influence future developments on the capital market.

Against this backdrop, the German stock market continued to trend sideways in the second quarter of 2014. While the DAX closed at 9,833 points on 30 June 2014 and thereby remained virtually unchanged in the second quarter, the TecDAX recorded a sharp increase of 5 per cent to 1,309 points in the reporting period.

The freenet share

The freenet share price fell by 8 per cent in the last quarter. The share started the second quarter with a Xetra daily closing price of 25.70 euros, and continued to trend throughout the quarter—following the dividend payout of 1.45 euros for each share entitled to participate in the profits—closing at 23.23 euros. The average Xetra daily closing price in the reporting period was 23.81 euros.

Over the past quarter, around 38.1 million freenet shares were traded on the electronic trading platform Xetra compared with 32.8 million in the first quarter of 2014 and 31.8 million in Q4 2013. The proportion of shares traded on alternative exchanges (dark pools) fell to 39 per cent of the total volume traded in the second quarter, down from 40 per cent in the preceding quarter and 42 per cent in the fourth quarter of 2013. The average daily volume traded on Xetra amounted to around 605,000 shares in the reporting period. An average of 512,000 freenet shares were traded per day on Xetra in the previous quarter, and 517,000 in the fourth quarter of 2013.

In the second quarter of 2014, the freenet share lost around 8 per cent of its value and lagged behind its benchmark index—the TecDAX—which rose by around 5 per cent in the same period. The SXKP index, in which the European telecom companies are compiled, posted only an increase of 2 per cent in the second quarter of 2014.

In a twelve-month comparison, the freenet AG share saw a rise of 23 per cent and trended similarly to the European telecom companies compiled in the SXKP, while the TecDAX improved by 40 per cent.

Shareholder structure

freenet AG's share capital totals 128,061,016 euros and is divided into 128,061,016 no-par-value bearer shares. Each share represents 1.00 euro of the share capital.

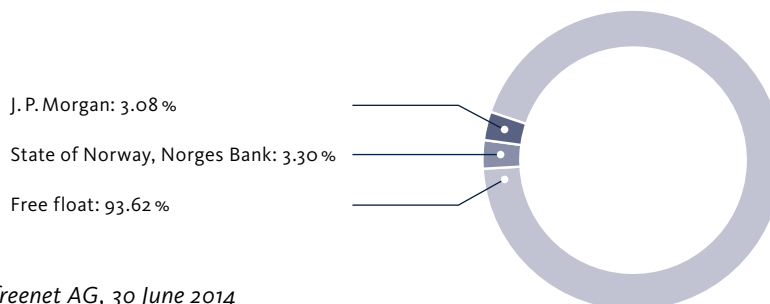
According to the voting rights disclosures received pursuant to Section 21 of the German Securities Trading Act (WpHG), freenet's shareholder structure changed as follows during the reporting period:

- On 7 May 2014, BlackRock (USA) informed us that it had fallen below the 5 per cent reporting threshold on 5 May 2014. Its share of the voting rights in freenet AG on this day amounted to 4.99 per cent (6,399,211 voting rights).
- On 8 May 2014, BlackRock (USA) informed us that it had exceeded the 5 per cent reporting threshold on 6 May 2014. Its share of the voting rights in freenet AG on this day amounted to 5.001 per cent (6,404,161 voting rights).
- On 12 May 2014, Norges Bank (Norway) informed us that it had fallen below the 3 per cent reporting threshold on 9 May 2014. Its share of the voting rights in freenet AG on this day amounted to 1.74 per cent (2,230,926 voting rights).
- On 13 May 2014, Norges Bank (Norway) informed us that it had exceeded the 3 per cent reporting threshold on 12 May 2014. Its share of the voting rights in freenet AG on this day amounted to 3.30 per cent (4,230,926 voting rights).

- On 6 June 2014, BlackRock (USA) informed us that it had fallen below the 5 per cent reporting threshold on 4 June 2014. Its share of the voting rights in freenet AG on this day amounted to 4.96 per cent (6,346,438 voting rights).
- On 17 June 2014, BlackRock (USA) informed us that it had fallen below the 3 per cent reporting threshold on 13 June 2014. Its share of the voting rights in freenet AG on this day amounted to 2.92 per cent (3,739,948 voting rights).

As a result, the shareholder structure of freenet AG on 30 June 2014 was as follows:

Figure 2: Shareholder structure of freenet AG on 30 June 2014



Source: freenet AG, 30 June 2014

Based on the voting rights disclosures received during the quarter under review, free float has increased from 88.85 per cent to 93.62 per cent compared with the end of the first quarter 2014. According to the definition of Deutsche Börse AG, the free float continues to be 100 per cent.

Interim group management report

Economic report

Business performance

As an independent service provider, freenet AG serves the growing digital lifestyle market with integrated product worlds, customer-oriented services and affordable mobile tariffs in all of Germany's mobile telecommunications networks. The portfolio encompasses the company's own tariffs and services and corresponding services from network operators in Germany in the traditional business segment of mobile communications/mobile internet. In addition to this, the company offers innovative digital applications relating to home automation and security, data security, entertainment and infotainment—including the latest smartphones, tablets and notebooks as end devices, plus attractive accessories.

The primary target group for all of the above comprises private customers: as part of a multi-brand strategy, the main brand mobilcom-debitel—in view of the fierce competition within the sector—concentrates primarily on high-quality contractual relationships when acquiring customers and managing existing ones, while freenet's discount brands cover the no-frills segment.

In the second quarter of 2014, the company further expanded its range of products, tariffs and services in the digital lifestyle, mobile communications and mobile internet segments and launched new activities in the fields of sales, marketing and customer service.

New digital lifestyle applications, ...

mobilcom-debitel has been offering products in the field of home automation for around two years now. These activities began with the SmartHome sets for mobile control of domestic heating systems by means of an app. This was followed last summer by different versions of the SmartHome camera as a security solution that enables users to monitor their homes using a mobile device when they are not there.

The company is continuing to expand these activities. Since May 2014, mobilcom-debitel customers have been able to acquire a complete security package offered in cooperation with SFR—one of the leading telecommunications providers in France—and the well-known service provider Europe Assistance at a fixed monthly price of 19.99 euros. In addition to the required control centre for the system as a whole, it includes an alarm siren, a WiFi-enabled camera with a motion detector and night vision, plus two further motion detectors and an opening detector for doors and windows, as well as two remote control devices for activating and deactivating the system. The package also contains an alarm button for assaults at home and a cloud solution whose securely hosted storage space holds recordings for 30 days for subsequent analysis purposes. Additionally, users can enhance their systems by adding further devices such as smoke and water alarms, power points and cameras.

In the event of a break-in, moreover, users are provided with valuable services: when the alarm is sounded, a security service provider first monitors the location, then remains in the location for up to 24 hours if there was a genuine break-in, and arranges for emergency repairs which are included in the package up to an amount of 200 euros. The components described above can be operated simply by using apps on the user's iPhone or Android smartphone, or alternatively on a web browser.

In the entertainment area, mobilcom-debitel enhanced the extra service GameFlat, which has been available since May 2013, with additional options for all new and existing customers as and from the beginning of 2014: GamePack Plus offers the game enthusiasts among Android smartphone and tablet users access to a variety of attractive “Freemium Games” for 3.99 euros per month. The pack consists of games that customers can play free of charge at first. In the course of the game, however, they are then offered the option of paying to acquire additional levels, tools, and so on.

Since mid-May, Game Pack Basic, a lower-priced variant for beginners, has also been available to users who would like to try out online games on their smartphones: starting at 1.99 euros monthly, they can download two games per month from the extensive range offered by the games supplier Gameloft; these include current blockbusters such as Iron Man 3, Thor 2 and Shark Dash.

... first-rate hardware offers and ...

In the second quarter of the current year, freenet continued to promote its offers for the inexpensive acquisition of suitable smartphones and other digital lifestyle products from a variety of premium manufacturers—with the smartphones usually being combined with attractive voice and data tariffs. The offers included:

- the Samsung GALAXY S5 for a one-off price of 29.99 euros—in a package with the real Allnet tariff in the Vodafone network for 46.98 euros per month; the services included comprise flat rates to all German networks (landline/mobile/SMS), flat-rate surfing with up to 1 GB and the security solution Norton Mobile Security with a total value of 48 euros;
- the Nokia Lumia 520 from 1 euro with the Bluetooth mini-loudspeaker MD-12 from Nokia and 50 euros starting credit, in combination with the Blue Basic tariff from o2 for 8.99 euros per month—with internal network flat rate, 50 free minutes and 200 free SMS messages per month to all networks nationwide, and flat-rate surfing with 200 MB;
- the Nokia Lumia 625 at the special discount price of 4.95 euros per month, combined with the Flat M Internet tariff; as well as the internet flat rate with 300 MB, it contains a telephone flat rate to the German landline and o2 mobile communications networks.

In the run-up to the World Cup in Brazil, mobilcom-debitel launched a number of special promotions for football fans. For example, the mobile DVBT receiver Elgato Eye TV W converts the user’s iPhone, iPad, Android smartphone or tablet into a TV by means of a free app—and not only during World Cups. Cables and an internet connection are not required—good mobile communications reception is enough. The Soundball from Sony with a Brazilian look and feel provided the right sound effects. Or—as the quieter option for the people around us—the Scullcandy Uprock headphones in the version licensed by the German Football Association (DFB) that has stadium-like sound effects.

The subsidiary GRAVIS, too, had some very attractive offers in its online shop—also without any World Cup link. These included the Philips SoundCurve DS8800W as AirPlay loudspeakers—for the kitchen and office, for example—or, unrelated to the World Cup, the universal remote control Logitech Harmony Smart Control. Together with the suitable app, it can be used to control TVs, Blu-ray players or digital receivers via the user’s iPhone or iPad.

... low special-offer prices

As digital lifestyle applications become more and more successful, low-priced, transparent flat rates are gaining in importance for customers. Since last July, mobilcom-debitel has had a clear and comprehensive range on offer in the form of the Allnet tariff spectrum: it is geared to the individual needs of users, who can choose low-cost packages with different features for all of the German mobile communications networks—and have consequently turned the Allnet tariffs into an established option in the intense competition that prevails in the sector.

With its targeted discount and tariff options, moreover, freenet is confronting the market with challenges time and again: these generally take the form of temporary campaigns by the Group's discount brands, which can be obtained from their own or neutral online platforms. Some examples:

- In April, klarmobil offered an Allnet flat rate in the o2 network, including SMS and 500 MB of mobile internet usage without the monthly basic charge in the first two months of the contract; with the Allnet-Spar (economy) flat rate in the D1 network at the beginning of June, too, the first two months were free. The end of the quarter then brought two particularly attractive offers: firstly, Talk Allnet Comfort in the Telekom network, with a 300 MB volume included and a telephone flat rate to all networks nationwide for 4.99 euros per month; and secondly, a package from Allnet-Starter in the D network, with a 200 MB volume included, 100 free minutes and SMS messages, a Nokia Lumia 630 and the free Bluetooth loudspeaker MD-12 from Nokia for 9.95 euros per month.
- At freenet Mobile, customers received a D1 voice flat rate to all German networks, including mobile surfing up to 250 MB, in April for 16.95 euros. In June, freeSmart followed with 50 free SMS messages and free minutes to all German networks, plus a data volume of 100 MB in the o2 network, without any basic charge in the four-month minimum term of the contract; after that the charge is 6.95 euros.
- Talkline, in turn, reduced its Allnet flat-rate tariff with a data volume of 1.2 GB, plus SMS and voice flat rate to all German networks, to a notional 19.90 euros per month by making a one-off special payment to its customers.

Finally, the main brand mobilcom-debitel offered the o2 Flat M Internet for 4.95 euros per month at the end of May—with savings of 480 euros over the two-year term compared with the regular charge. The tariff contains a telephone flat rate for calls to the German landline network, a mobile flat rate for the o2 network and a data volume of 300 MB. Additionally, the company granted starting credit of 50 euros for Android smartphones and tablets in various device and tariff combinations.

Marketing campaigns for the World Cup

The bus tour through German cities has been an integral part of the mobilcom-debitel marketing mix since 2010. To mark the World Cup in Brazil, the mobilcom-debitel trucks again embarked on their tour of Germany and in which they went on to visit a total of 41 towns and cities between 26 May and the World Cup final on 13 July. At the same time, a mobilcom-debitel promotion team went on its own tour of German pedestrian zones during the four weeks of the World Cup, right up to the final, ensuring increased footfall in the surrounding shops and specialist dealerships by carrying out 160 promotions in all. Passers-by were given the chance to try their luck as either a virtual striker or goalkeeper, in return for which they received vouchers that they could exchange for a prize in the shops.

Also at the beginning of May, the “Weltmeister-Wette” (World Cup wager) was launched by mobilcom-debitel. It was promoted with a broad-based campaign on television and radio, via online channels and social media as well as at the point of sale in mobilcom-debitel shops: anyone who made a purchase through one of these sales channels—in the shop or specialist dealership, online or via telesales—or signed or extended a contract between 1 May and 13 July received a participation code to predict the upcoming World Cup winners online. The prizes had a total value of over 180,000 euros and included three Mini Coopers and ten digital lifestyle packages worth 10,000 euros each. Accordingly, all of the shops were designed and fitted out with the appropriate World Cup accoutrements.

Expansion of shop sales

In the last financial year, freenet integrated GRAVIS, the leading German retail chain for Apple products, which had been acquired at the turn of 2012/2013, into the Group and gradually developed the company into a supplier of digital lifestyle products, including those of other premium manufacturers.

In the second quarter of 2014, this wholly-owned freenet subsidiary, in turn, signed a contract to acquire up to twelve shops belonging to the Apple premium reseller reStore. This will allow GRAVIS to increase its presence and its sales strength in sought-after prime locations in German cities—and its number of shops will rise from 34 to up to 46. With the appropriate redesign and restructuring having been carried out, the focus is now on marketing Apple products and digital lifestyle accessories, as well as services such as individual training measures and repairs.

Key drivers of the business development

Customer development

In million	30. 6. 2014	31. 3. 2014	31. 12. 2013	30. 9. 2013	30. 6. 2013
Mobile Communications customers	12.99	13.13	13.29	13.37	13.56
Thereof Customer Ownership	8.84	8.79	8.76	8.67	8.56
Thereof contract customers	5.90	5.87	5.86	5.82	5.81
Thereof no-frills customers	2.94	2.92	2.90	2.85	2.75
Thereof prepaid cards	4.14	4.34	4.53	4.70	5.00
Gross new customers	0.73	0.69	0.91	0.79	0.86
Net change	-0.15	-0.16	-0.08	-0.19	-0.15

Despite persistently tough competition on the market, the number of contract customers again rose slightly in the second quarter of 2014. The increase over the previous quarter amounts to around 30,000 customers, with a postpaid customer base of 5.90 million as at 30 June 2014. This means we were able to continuously grow this customer group, which is a key focus for our strategic business approach, from the second quarter of 2012 onwards following a period of stabilisation. In a year-on-year comparison, the increase translates into some 95,000 customers. In our view, this positive development is attributable to the constantly updated range of products we offer with attractive contract tariffs in conjunction with rising customer demand for data usage with modern smartphones.

We also increased our customer base again in the second strategically important customer group, the no-frills segment. The quarterly rise of 20,000 to 2.94 million customers as at 30 June 2014 is evidence of the ongoing growth in our discount market segment, in which we primarily use online sales channels to serve particularly price-sensitive customers who need less individual advice. A year-on-year comparison illustrates the persistently dynamic trend in this market segment, revealing growth of around 190,000 customers.

Accordingly, our customer ownership—which includes the postpaid and no-frills customer groups and serves as a key performance indicator for our company—rose by 50,000 customers (0.6 per cent) in the reporting period. This represents a 280,000 increase in our customer base, taking it to 8.84 million and corresponding to a rise of approximately 3.3 per cent compared with the second quarter of 2013.

The number of prepaid SIM cards in circulation continued to fall as expected in comparison with the previous quarter, amounting to 4.14 million cards on 30 June 2014. As at 31 March 2014, the number of active prepaid SIM cards in circulation totalled 4.34 million. The number was down by 0.9 million cards year-on-year (30 June 2013: 5.00 million cards). This further fall is the result of more inactive SIM cards being deactivated by network operators.

This means the total number of mobile communications customers declined by around 145,000 to 12.99 million (31 March 2014: 13.13 million) in the quarter under review. Consequently, the mobile communications customer base has shrunk by around 570,000 compared with the same period of the previous year (13.56 million).

Monthly average revenue per user (ARPU) in the Mobile Communications segment

In EUR	Q2/2014	Q1/2014	Q4/2013	Q3/2013	Q2/2013
Contract customer	21.5	21.2	21.6	22.6	22.5
No-frills customer	3.0	2.9	3.0	3.5	3.6
Prepaid cards	3.0	2.7	3.0	3.2	3.0

The monthly average revenue per contract customer (postpaid ARPU) increased to 21.50 euros in Q2 2014, 0.30 euros higher than the level of the previous quarter. However, the ARPU has shrunk by 1.00 euro compared with the same period of the previous year (22.50 euros). This can still be attributed primarily to unrelenting price competition on the German market. This means that some freenet customers with older contracts, which in some cases still have relatively high basic monthly fees, are also switching to the current smartphone tariffs on offer. Compared to that, the ARPU generated by new customers is showing a relatively stable trend.

At 3.00 euros, the monthly average revenue per no-frills customer in the quarter under review (no-frills ARPU) remained virtually unchanged compared with the previous quarters (Q1 2014: 2.90 euros; Q4 2013: 3.00 euros). However, the no-frills ARPU was 0.60 euros lower than in the second quarter of 2013 (3.60 euros). This trend also reflects competitive pressure—e.g. from sales promotions—in this price-sensitive market. The no-frills segment primarily caters for particularly price-conscious mobile communications customers who take out contracts online.

Compared with the previous quarter, prepaid ARPU increased by 0.30 euros to 3.00 euros in the second quarter of 2014, thereby remaining stable in a year-on-year comparison.

Assets, earnings and financial position

Revenue and results

In EUR'000s	Q2/2014	Q2/2013	Change
Revenue	727,222	809,636	-82,414
Gross profit	190,533	177,019	13,514
Overhead costs	-102,899	-91,857	-11,042
EBITDA	87,634	85,162	2,472
EBIT	71,192	71,667	-475
EBT	60,501	61,481	-980
Group result	57,074	55,395	1,679

GROUP REVENUE fell by 10.2 per cent in the second quarter of 2014 compared with the same period of the previous year. Among other factors, lower revenue from low-margin business (primarily hardware sales to sales partners and distributors and from the prepaid segment) and the decline in postpaid ARPU by an average of 1.00 euro per customer had a negative impact on revenue. Contrasting effects which, however, did not compensate for the aforementioned reduction resulted from the inclusion of freenet digital Group in the Group's scope of consolidation.

The **GROSS MARGIN** widened by 4.3 percentage points to 26.2 per cent compared with Q2 2013, which was primarily attributable to the significant decline in low-margin business mentioned above. **GROSS PROFIT** was 13.5 million euros up on the same quarter last year at 190.5 million euros—mainly as a result of the addition of freenet digital Group to the group of consolidated companies.

OVERHEAD COSTS—which form the difference between gross profit and EBITDA and include the items **OTHER OPERATING INCOME, OTHER OWN WORK CAPITALISED, PERSONNEL EXPENSES, OTHER OPERATING EXPENSES** and the **RESULT OF COMPANIES CONSOLIDATED USING THE EQUITY METHOD**—rose by 11.0 million euros compared with Q2 2013, also mainly as a result of the larger group of consolidated companies.

The Group result from continued operations before interest, tax, depreciation and amortisation (**EBITDA**) in Q2 2014 came to 87.6 million euros, 2.9 per cent above the level of Q2 2013.

DEPRECIATION AND AMORTISATION was up 2.9 million euros compared with Q2 2013 at 16.4 million euros. This was primarily due to the amortisation of intangible assets recognised in the course of the purchase price allocations for the acquisition of freenet digital Group and due to increased amortisation of proprietary software.

NET INTEREST INCOME, i.e. the balance of interest income and expenses, was reported at -10.7 million euros in Q2 2014, reflecting a slight improvement of 0.5 million euros over the same quarter of the previous year—attributable largely to the acquisition of freenet digital Group.

As a result of the effects outlined above, the **GROUP'S PRE-TAX EARNINGS (EBT)** fell slightly by 1.0 million euros year on year to 60.5 million euros.

INCOME TAX expenses totalling 3.4 million euros were reported for the quarter under review (Q2 2013: 6.1 million euros). This figure resulted from offsetting current income tax expenses in the amount of 7.2 million euros (previous year: 7.3 million euros) against deferred tax income, due primarily to the addition to deferred tax assets from tax loss-carryforwards totalling 3.8 million euros (previous year: 1.2 million euros).

As in the second quarter of the previous year, the **GROUP PROFIT** reported for Q2 2014 resulted solely from continuing operations and amounted to 57.1 million euros. This represents a slight increase of 1.7 million euros compared with the 55.4 million euros earned during the same quarter of the previous year.

Assets and financial position

Assets

In EUR million	30. 6. 2014
Non-current assets	1,868.4
Current assets	601.1
Total assets	2,469.5

In EUR million	31. 3. 2014
Non-current assets	1,880.4
Current assets	640.4
Total assets	2,520.9

Liabilities

In EUR million	30. 6. 2014
Shareholders' equity	1,168.5
Non-current and current liabilities	1,301.0
Total equity and liabilities	2,469.5

In EUR million	31. 3. 2014
Shareholders' equity	1,297.0
Non-current and current liabilities	1,223.9
Total equity and liabilities	2,520.9

As at 30 June 2014, the **BALANCE SHEET TOTAL** amounted to 2,469.5 million euros, having decreased by 51.3 million euros (2.0 per cent) since 31 March 2014 (2,520.9 million euros).

On the **ASSETS SIDE**, non-current assets decreased by 12.0 million euros. This was largely due to a fall in intangible assets of 10.4 million euros to 403.8 million euros, which in turn resulted from a combination of ongoing amortisation and a low level of new investment. The increase in goodwill of 1.6 million euros is connected with the now finalised purchase price allocation for the acquisition of freenet digital Group (+1.2 million euros) and the provisional purchase price allocation for the takeover of shops belonging to reStore GmbH (+0.4 million euros).

Within current assets, there was a notable 18.4 million euro decline in trade receivables to 376.9 million euros. This downward trend can be attributed firstly to the increase of 7.1 million euros in the second quarter 2014 in the volume of receivables sold for mobile phone upgrade options. Please refer to note 5 of the selected explanatory notes pursuant to IAS 34 for more information. Secondly, the receivables from hardware distributors fell as a result of the reduced volume of business in this area. Cash and cash equivalents decreased by 12.4 million euros to 108.9 million euros. The decrease in cash and cash equivalents resulted primarily from the dividend distribution and the annual payment of interest on the corporate bond, while the cash flow from operating activities and the revolving line of credit, which was utilised to the extent of 129.0 million euros, served to increase the level of cash and cash equivalents.

On the **EQUITY AND LIABILITIES SIDE**, gross borrowing increased, in comparison with 31 March 2014, by 108.0 million euros to 654.2 million euros, mainly as a result of the revolving line of credit—in connection with the dividend distribution—that was utilised to the extent of 129.0 million euros as at 30 June 2014. On the other hand, borrowing arising from the corporate bond decreased as a result of the interest payment which is due on this corporate bond each April.

Trade payables decreased by 9.9 million euros to 359.7 million euros as a result of the downward trend in hardware business. The decline in other liabilities and accruals of 18.3 million euros to 157.9 million euros was primarily a consequence of the payment of a nominal sum of 12.5 million euros towards the exclusive distribution right vis-à-vis Media-Saturn Deutschland GmbH.

The **EQUITY RATIO** decreased from 51.5 per cent at the end of March 2014 to 47.3 per cent at the end of June 2014, mainly as a result of the dividend distribution that took place in the second quarter of 2014. The dividend distribution also provides the backdrop to the increase in net borrowing, which amounted to 545.3 million euros as at 30 June 2014; this represents a rise of 120.4 million euros compared with the total reported at the end of the previous quarter.

Cashflow

In EUR million	Q2/2014	Q2/2013	Change
Cash flow from operating activities	78.8	73.8	5.1
Cash flow from investing activities	-4.3	-2.8	-1.5
Cash flow from financing activities	-215.9	-207.7	-8.2
Change in cash and cash equivalents	-141.4	-136.7	-4.7
Free cash flow ¹	74.2	70.4	3.8

¹ Free cash flow (FCF) is defined as cash flow from operating activities minus investment in property, plant and equipment and intangible assets, plus proceeds from the disposal of property, plant and equipment and intangible assets.

In the second quarter of 2014, **CASH FLOW FROM OPERATING ACTIVITIES CAME** to 78.8 million euros, which equates to a year-on-year increase of 5.0 million euros. In addition to the 2.5 million euro rise in EBITDA, the increase in net working capital, although 3.3 million euros lower at 2.7 million euros, had a positive effect on cash flow from operating activities. It should be noted here that receivables from mobile phone upgrade options with a nominal value of 30.3 million

euros were sold to a bank as at 30 June 2014 (please refer to note 5 of the selected explanatory notes for more details), resulting in an increase of 7.1 million euros compared with 31 March 2014. On the other hand, it should be stated that payments relating to a network operator bonus both in the second quarter of 2014 and in Q2 2013 (approx. 21.0 million euros in 2014 versus approx. 19.0 million euros in 2013) were each only received in April, after they were due, thereby providing the explanation for the respective increases in cash flow from operating activities in the second quarter compared with the first. Taxes on income amounting to 6.0 million euros were paid in the second quarter of 2014 (previous year: 5.3 million euros).

CASH FLOW FROM INVESTING ACTIVITIES amounted to -4.3 million euros in Q2 2014, compared with -2.8 million euros in the second quarter of 2013; in each case it consisted mainly of investments in property, plant and equipment and intangible assets. The most significant investments in the quarter under review were in the areas of proprietary software in connection with a range of strategic projects, and IT developments.

In the quarter under review, **CASH FLOW FROM FINANCING ACTIVITIES** increased to -215.9 million euros compared with -207.7 million euros in the same period last year. The dividend distribution increased by 12.8 million euros, from 172.8 million euros in the second quarter of 2013 to 185.6 million euros in the second quarter of 2014, thereby accounting for most of the change. In the second quarter of 2014, moreover, interest totalling 30.2 million euros (second quarter of previous year: 29.9 million euros) was paid, primarily in connection with the corporate bond.

As a result of the factors described above, **FREE CASH FLOW** in the second quarter of 2014 increased by 3.8 million euros year-on-year to 74.2 million euros.

Financial Management and Control System

The corporate strategy of freenet AG is underpinned by focused financial management, which uses the capital structure and liquidity development as key performance indicators (KPIs). The strategy is implemented by means of a comprehensive treasury management system based on established controlling structures.

The capital structure is primarily managed via financial KPIs comprising gearing, the interest coverage ratio and the equity ratio. Gearing indicates how much of the current operating result (EBITDA) would be needed to pay off the company's net debt (borrowing less cash and cash equivalents). Interest coverage is the ratio of EBITDA to the interest balance.

Key figures of financial management

	Target 2013	Q2/2013	Q1/2014	Q2/2014	Target 2014/15
Debt ratio	1.0–2.5	1.5	1.2	1.5	1.0–2.5
Interest Cover	> 5	8.6	8.4	8.4	> 5
Equity ratio	> 50 %	46.7 %	51.5 %	47.3 %	> 50 %

Gearing is currently 1.5, as it was on 30 June 2013, and therefore remains in the lower portion of the strategic range of 1.0 to 2.5. The increase over the previous quarter was caused by the dividend distribution. Borrowing is dominated by the corporate bullet bond in the amount of 400 million euros due in April 2016 and due to the 2017/2019 promissory note of 120 million euros.

At 8.4, interest coverage is virtually unchanged compared with Q2 of the previous year and Q1 of the current year and is still well above the target level.

The equity ratio as at 30 June 2014 is just below the target level of 50 per cent. There has been no significant change compared with the previous year's reporting date. It should be noted that the equity ratio usually falls to its lowest level on a quarterly comparison after the dividend distribution, which takes place in the second quarter. As a result, we assume that in the subsequent quarters this key financial indicator will improve until the next dividend payout.

Employees

At the end of Q2 2014, the number of employees had fallen to 4,904 compared with 4,961 at the end of the first quarter of 2014. The decrease in the number of employees compared with the previous quarter results mainly from the structural shift from mobilcom-debitel branches to mobilcom-debitel franchise partners.

Opportunities and risk report

To control and monitor its ordinary business activities, the company management has established a comprehensive monthly reporting system which encompasses both the financial and the non-financial performance indicators within the Group. The Executive Board is kept up to date about results via regular formal discussions with all of the relevant segments. During these discussions, the participants also discuss current topics as well as future internal and external developments, measures and potential opportunities. The identification, analysis and communication of the opportunities, as well as their exploitation, constitutes an entrepreneurial (management) task which is performed by the Executive Board, those responsible for the individual segments, and the respective decision-makers in a process of continuous communication.

freenet AG continued to focus consistently on mobile voice and data services in the first six months of 2014. The main focal points in the marketing of smartphones and flat-rate tariffs were customer quality and the stabilisation of the contract customer base. In addition, a great deal of importance was again attached to digital lifestyle activities. As well as the integration of freenet digital into the freenet Group, the marketing of SmartHome products and digital lifestyle options—such as md Cloud or Norton Mobile Security—was intensified.

The company sees external opportunities in the following market developments in particular:

- the increasing readiness of customers to pay for mobile communications devices,
- the trend towards mobile internet use via smartphones and tablet PCs,
- the trend towards more expensive devices (smartphones) and an associated higher level of use and/or the associated sale of flat-rate products,
- the trend towards the interconnectedness of products in the home (“the internet of things”).

The trend towards paying for mobile communications devices and to the spread of mobile internet use due to the increasing prevalence of smartphones, as well as the interconnectedness of products in people’s homes, could have a positive impact on the development of revenue and cash flows.

Internal opportunities for the company could arise from the following circumstances in particular:

- examination and implementation of strategic options in the fields of mobile communications and digital lifestyle,
- continuous intensification of commercial relationships with suppliers in the interests of stabilising existing conditions models and developing new ones,
- fortification and further development of IT systems to achieve a further improvement in customer satisfaction,
- enhancement of our selling strength via the expansion of existing sales channels and the use of new sales partnerships,
- further improvement of shop performance, also through the marketing of additional products,
- implementation and marketing of new products in the digital lifestyle area,
- intensified establishment of the brands klarmobil, freenetmobile, callmobile and debitel light in the steadily-growing discount market with a view to participating even more strongly in this growth market,
- continuous process and quality improvement that leads to a lasting reduction in the cost structures.

The operating activities of freenet AG as a network-independent mobile communications service provider, and its strategic commercial orientation towards becoming a genuine digital lifestyle provider, are leading in particular to the internal opportunities referred to above. Effects generated by these opportunities could have a positive impact on the level of revenue, (overhead) costs and cash flow.

Overall evaluation of the opportunities situation

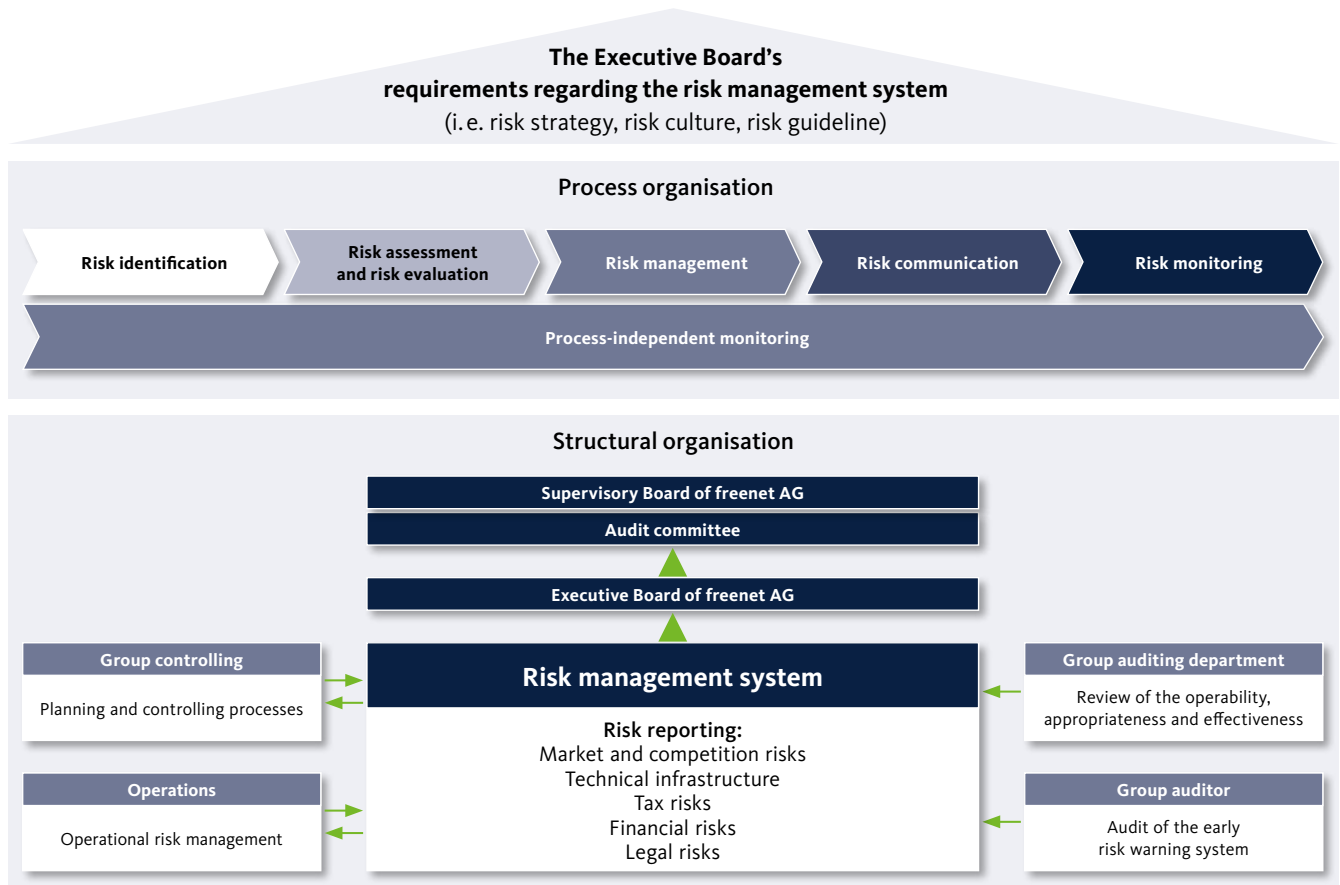
Thanks to the regular monitoring of internal and external opportunities by means of the monthly reporting system and communication during the formal meetings, the management is in a position to fulfil the entrepreneurial (management) task incumbent upon it and therefore, by taking advantage of opportunities, to make a positive contribution to both the operational and the strategic safeguarding of the company's success.

Risk management system

If the continued existence of freenet AG is to be guaranteed in the long term, an efficient risk management system will be of the utmost importance. The risk management system at freenet AG is applied solely to risks, and not to opportunities. Its purpose is to ensure that risks for the company's future development are identified at an early stage by all of our managers and are communicated to the responsible decision-makers within the company in a systematic and comprehensible manner. The purpose of the timely communication of risks to the responsible decision-makers is to guarantee that appropriate steps are taken to deal with the risks identified and that damage to our company, our employees and our customers is thereby averted.

To achieve this, the Executive Board of freenet AG has set up an efficient early risk identification, monitoring and control system within the Group that complies with the statutory requirements of a risk management system. The systems and methods of the risk management system are an integrative component of freenet AG's general organisational structure and workflow management.

Figure 8: Process and structural organisation of the risk management system of freenet AG



In formalised risk reports compiled at least every six months, the individual specialist departments at freenet AG and at the freenet subsidiaries record and/or update existing and any new risks which exceed a defined materiality threshold. The risk reports describe the specific risks and examine them for the likelihood of their occurrence and for their effects on the company on the basis of standardised criteria (risk analysis and assessment). Based on the risk reports' findings, various alternatives for action are carried out within the scope of general company management so that there is an appropriate response to the risks identified (risk control and risk monitoring). The individual risk reports are combined into an overall Group risk report and communicated to the Executive Board. Even between the standard reporting times, risks are recorded, analysed, assessed and controlled as soon as they have been identified and, depending on their order of magnitude, reported immediately to the Executive Board and the Supervisory Board (risk communication).

In guidelines which are continually supplemented and improved, the Executive Board has defined the major risk categories for the Group, developed a strategy for dealing with these risk

categories and documented the allocation of tasks and areas of responsibility within the Group's risk management system. Employees are familiar with these guidelines, which serve to specifically enhance their risk awareness (as part of risk communication).

The methods and systems of risk management are constantly examined, enhanced and adjusted. freenet AG's internal auditing department plays a supporting role in this process, whereby regularly checking risk reports forms the focal point here. The Supervisory Board, and in particular freenet AG's audit committee, monitors the effectiveness of the risk management system in the light of requirements under company law. The Supervisory Board is involved in the process through regular reporting and, if required, topical reporting by the Executive Board (process-independent risk monitoring).

To control and monitor its ordinary business activities, the company management has established—in addition to its risk management system—a comprehensive monthly reporting system which encompasses both the financial and the non-financial performance indicators within the Group. The Executive Board is kept up to date about results via regular formal discussions with all of the relevant segments. Topical themes are also discussed and future measures debated at these formal discussions (as part of risk communication).

Major risks

Out of all the risks for the freenet Group that were identified, those risk areas or individual risks which, from a current viewpoint, might have a major influence on freenet AG's net assets, financial position and results of operations are explained below. Since 31 December 2013 there have been no major changes regarding the likelihood of the individual risks or risk areas occurring or regarding their effects.

Market and competition risks

In terms of both revenue and earnings, the mobile communications area is by far the most significant segment in the freenet Group. Accordingly, this area also generates the most significant market and competition risks.

The telecommunications markets continue to be shaped by fierce competition and a pronounced readiness of customers to switch products. This can lead, on the one hand, to a loss of revenue and market shares and to pressure on margins in the respective segments, and/or make it more difficult to gain market shares.

On the other hand, the intense competition might necessitate higher expenditure on acquiring new customers accompanied by declining income and a pronounced readiness of customers to switch products. freenet AG tries to counter its customers' readiness to switch with customer retention schemes. If these are not successful enough, or only at inappropriate cost, this will have a negative impact on freenet AG's revenue and income position.

The margins in the mobile communications service provider business are largely determined by the network operators and how they structure their tariff models. The mobile communications network operators are increasingly deciding to sell their own products and drive the mobile communications service providers out of the market. Added to this is the fact that the business structure of mobile communications network operators enables them to some extent to offer better conditions than the mobile communications service providers. This, in turn, can lead to the loss of sales channels and customers.

A further reduction in the “termination rates” by the German Federal Network Agency will reduce revenue per customer on the market. Due to the reductions that have already taken place in the past, the anticipated risk, just for a service provider such as freenet, is low despite a medium likelihood of occurrence.

Despite the opportunities described above, the merger of the two mobile communications network operators O2 and E-Plus could lead to restrictions in competition between the remaining network operators. This could result in a weakening of the service-provider model and have a negative impact on freenet AG's revenue and earnings position.

Since 2008, mobile communications revenue with “non-voice” services has risen substantially due to the rapidly increasing use of data services. freenet AG wants to use the growth opportunities offered by mobile internet to absorb price-related revenue losses in the area of call charges. If freenet AG does not succeed in generating an appropriate level of mobile coverage, or if no attractive purchasing models are provided by the network operators, this might result in lasting negative earnings prospects for the company.

The expansion of business with mobile communications devices involves price risks. A reduction in the network operators' premiums in that area, too, could lead to a higher capital commitment risk and a greater marketing risk.

The discontinuation of sales channels and/or cooperation partners could result in a situation where the gross activations at other existing, or new, partners must be realised subject to tougher conditions or cannot be replaced.

Changes in the law, interventions by regulators or landmark court decisions can have an impact on the tariff structure and the possibility of customers asserting claims. This can have an impact on both revenue and cash flow levels. The effects of individual decisions or of changes in the law may not in themselves be substantial. freenet AG counters the risk by regularly monitoring developments on the regulators' side and/or by following the outcomes of court decisions. The likelihood of such risks occurring can be assessed as medium, with the result that the risk of negative effects on the company's earnings position is classified as moderate in overall terms.

In order to bolster its digital lifestyle strategy, freenet AG has recently made some corporate acquisitions. There is a general risk that the operating activities at these new equity interests will not develop as expected, and consequently that the digital lifestyle segment's growth will remain below the anticipated level. This would have a negative impact on both the earnings and the cash flow position at freenet AG.

Technical infrastructure

The serviceability and efficiency of the technical infrastructure, including the company's computing centres and billing systems, are of considerable significance for its operational success and its continued existence. Network failures or service problems caused by system malfunctions or breakdowns can result in a loss of customers. While the loss of customers leads to a decrease in revenue, a malfunction of the systems means that freenet AG cannot provide its services and is therefore unable to generate revenue. This risk has a negative influence on revenue and cash flow.

Tax risks

Assessment periods that have not yet been audited fully can be subject to changes that result in payments of tax arrears or changes in the loss-carryforwards if the tax authorities, when conducting their external tax audits, come to divergent interpretations of tax regulations or divergent assessments of the respective underlying circumstances. The same applies for tax types which have not yet been fully assessed, especially if the types in question are not generally subject to an external tax audit.

The risk of divergent interpretations and assessments of circumstances applies particularly to reorganisations under company law. It therefore cannot entirely be ruled out that as a result of asset contributions, other conversion procedures, new capital injections and changes of shareholders, the corporation tax and trade tax loss-carryforwards declared by the corporations in the freenet Group and hitherto assessed accordingly and separately by the tax authorities, could be reduced or eliminated altogether.

If 25 per cent or more of the shares or voting rights in the company are concentrated directly or indirectly in one hand or in the hands of a number of shareholders with aligned interests (harmful acquisition of shares) within five years, any negative income (corporation tax and trade tax loss-carryforwards) of the company that was not settled or withdrawn by the time of the harmful acquisition of shares could be lost either partially or in its entirety in accordance with Section 8c of the German Corporation Tax Act (KStG). Shares are deemed to be concentrated in one hand if they are transferred to an acquirer, to persons associated with that acquirer or to a group of acquirers with aligned interests.

The company has no influence on the occurrence of this risk because the (possibly partial) elimination of the negative income (corporation tax and trade tax loss-carryforwards) that was not settled or withdrawn by the time of the harmful acquisition of shares is brought about by implementing measures and transactions at shareholder level. Against this backdrop, it cannot be ruled out that a disposal or additional purchase of shares by the company's shareholders might lead to a concentration of 25 per cent or more of the shares in one hand. The same risk applies if 25 per cent or more of the shares or voting rights become concentrated in the hand of one shareholder or a group of shareholders with aligned interests for the first time as a result of other measures. The legal consequences described above apply accordingly.

In the mobile communications sector there is a situation to the effect that external sales partners act as brokers for mobile communications contracts between the mobile communications service providers (such as freenet AG) and end customers, while simultaneously issuing mobile phones to the end customers for free or at a discount in their own name and for their own account. With regard to this practice of issuing phones, there are problems relating to value added tax that have not yet been resolved. Case law in financial proceedings so far has come to different conclusions on the issue of sales partners issuing mobile phones. In connection with this, the finance courts in Saarland and Baden-Württemberg have, in two judgements, taken the view that issuing the mobile phones free of charge constitutes a service in return for payment from the sales partner to the end customer, as components of the commission that the mobile communications service provider pays to the sales partner are third-party payments rendered for the delivery by the sales partner to the end customer as defined by Section 10 (1) sentence 3 of the German Value Added Tax Act (UStG). An appeal against the judgement by Baden-Württemberg Fiscal Court was lodged with Germany's Federal Finance Court (BFH). The BFH pronounced judgement on this appeal procedure on 16 October 2013, reasoning that Baden-Württemberg Fiscal Court's assessment in the pending individual case is not objectionable under appeals law. The company expects that the German Federal Ministry of Finance will make a statement in the near future about the time-related and content-related aspects of a general applicability of the aforementioned BFH judgement for the mobile communications sector. From the company's point of view, there is an overwhelming likelihood that the aforementioned BFH judgement will have no significant negative effects for freenet AG under VAT law. There remains a risk, however, that in the event of such effects freenet AG would have to repay some of its input tax to the tax office, which would have a substantial negative effect on the company's net assets, financial position and results of operations.

Financial risks

To reduce the liquidity risk, we make use of a variety of financial instruments. The liabilities due to banks shown under borrowing result from a fixed-interest corporate bond (recognised in the accounts as at 30 June 2014: 403.5 million euros) that was issued as part of the refinancing in April 2011 and from the bonded loan that was finalised in December 2012 (shown as at 30 June 2014 with a balance totalling of 121.0 million euros—of which 56.1 million euros is accounted for by a tranche with a variable interest rate and 64.9 million euros by two tranches each with a fixed interest rate). In addition, the Group has a revolving line of credit totalling 300 million euros which had been drawn on in the amount of 129.0 million euros as at the mid-year point. The company's financial leeway is restricted by the regulations in the credit agreements.

freenet AG is the borrower in each case and mobilcom-debitel GmbH is the guarantor; in respect of the revolving credit line, mobilcom-debitel GmbH can also call up sums directly from the credit agreement. The company is allowed to obtain external funds outside of the credit agreements only to a strictly limited extent, for example with the aim of financing future strategic investments.

In addition to this, the Group's financial and operational leeway is restricted by particular contractual constraints (known as undertakings and covenants) to which freenet AG has subjected itself in view of the credit agreements it has signed. These impose restrictions on the company,

for example in the areas of changing the Group's business operations, carrying out internal structural measures in the Group in accordance with company law, furnishing collateral, and any purchases and/or disposals of assets, particularly the ownership of shares.

The restrictions referred to above can—in themselves or in combination with other factors, such as a deterioration in the general economic situation—have a negative impact on freenet AG's net assets, financial position and results of operations.

With regard to the borrowing with variable interest rates, our company is subject to interest rate risks largely in relation to the EURIBOR. The company counters these risks with a mixture of fixed and variable-rate borrowing. The interest rate risks are not explicitly hedged, although the cash at hand, which is largely invested on the basis of EONIA and/or EURIBOR at variable interest rates, functions as natural hedging and reduces the interest rate risk from the variable-rate borrowing accordingly.

Financial investments are generally made in the form of call money and term deposits at commercial banks with a high credit standing.

In freenet AG's consolidated balance sheet, on-balance-sheet goodwill as well as intangible assets such as customer relationships and trademark rights are disclosed in substantial amounts. There is a risk of substantial impairments in the event of impairment tests being carried out in the subsequent periods.

Default risks are present in connection with the trade receivables and other assets reported in the balance sheet. The default risk in these cases is the unexpected loss of cash and cash equivalents or income as a result of the partial or total default on the receivable in question. Value adjustment allowances were recognised in the reporting date balance sheet in preparation for the expected default. If these value adjustment allowances proved to be insufficient, this would have negative consequences for the net assets, financial position and results of operations.

The risks with relevance for the assessment of risk in respect of the receivables sold are the credit risk and the liquidity risk. The credit-risk-related loss to be borne by the freenet Group is linked from the outset to the fixed purchase price reduction that is retained by the bank at the time of the sale and, in view of this, any unutilised parts are not reimbursed to the freenet Group. Compared to a situation without the receivables sale explained above, the freenet Group's credit-risk situation is improved by this fixed purchase price reduction. Similarly, the liquidity risk situation improves as a result of the receivables sale because the sale of the receivables immediately improves the level of liquidity and, accordingly, the credit lines can be preserved.

If the macroeconomic conditions deteriorate, this might lead to a situation where the freenet Group can no longer uphold its agreements with the creditor banks. This could result in the creditor banks being given the right to make the loans due immediately.

Foreign currency risks arise from freenet Digital Group's operating activities but their order of magnitude for the freenet Group is immaterial. Other financial risks, such as changes in interest rates, are regarded by the company as immaterial and therefore do not need to be disclosed separately in the group management report.

Legal risks

Former shareholders of mobilcom AG and freenet.de AG have applied for the judicial review of the conversion relation from the merger of mobilcom AG and freenet.de AG to form the current freenet AG in 2007 in accordance with Section 15 of the German Conversion Act (UmwG). If the court finds the conversion relation to have been inappropriate in these appraisal proceedings, a settlement will be made by means of additional cash payment. The additional payment must be made to all of the shareholders who were affected, even if they were not claimants in the appraisal proceedings.

The company is assuming, however, that the conversion relation was appropriate and that there will be no need for additional cash payments, as the conversion relation was calculated diligently and was audited and confirmed by the merger auditors appointed by the court.

It regards this assessment of matters as having been confirmed by Kiel District Court (Landgericht), which has rejected the applications by both groups of shareholders. A number of applicants have lodged an appeal against this ruling at Schleswig-Holstein Higher Regional Court (OLG).

mobilcom AG, as the company's legal predecessor, as well as a number of other companies from the former mobilcom Group, came to a settlement with France Telecom and affiliated companies in 2002. The effectiveness of this settlement is being called into question by some individual shareholders.

The company regards this settlement as effective and has no grounds for suspecting that France Telecom does not feel bound by it. If the opinions of these shareholders are nevertheless upheld in court, it could then be expected that France Telecom would assert a claim for the sum of 7.1 billion euros, which it waived as part of the settlement, against the company and that it would contest any counter-claims by the company in respect of their merits and their amounts.

Some individual shareholders are of the opinion that the capital increase through contributions in kind carried out in November 2000 by mobilcom AG as legal predecessor of the company was erroneous, or rather, the contribution in kind had no intrinsic value, with the result that, on the one hand, the company would still be entitled to settlement claims running into billions against France Telecom, while on the other, the shares issued to France Telecom had no voting rights. The company is assuming that the capital increase through contributions in kind was carried out in a legally effective manner. The company is therefore also assuming that this will have no impact on the appraisal proceedings.

Overall evaluation of the risk position

Thanks to the risk management process which has been implemented, as well as the monthly reporting system, the Executive Board has an overview of the risk situation in its entirety. In comparison with the previous year, individual risks have changed little in respect of their likelihood of occurrence or their impact. All in all, it can be assumed that the risks will have no impact on the continued existence of the freenet Group. The Executive Board will continue to observe the existing risks in the future.

Key features of the internal control and risk management system in relation to the Group accounting process (Section 289 (5) and Section 315 (2) no. 5 of the German Commercial Code [HGB])

Definitions and elements of the freenet Group's internal control system

The freenet Group's internal control system is based on the internationally recognised framework drawn up by COSO (Committee of Sponsoring Organizations of the Treadway Commission). This encompasses all processes and measures for safeguarding the effectiveness, efficiency and correctness of accounting methods, especially in the area of ensuring compliance with legal requirements.

freenet AG's Executive Board has instructed all areas within the Group to manage their control processes in accordance with standardised principles.

The individual areas analyse their processes continuously, also in relation to new statutory requirements and other standards to be complied with, develop internal regulations on the basis of those and train the responsible employees.

The key elements of the freenet Group's internal monitoring system are based, on the one hand, on automated IT control processes with alarm thresholds, and on the other hand, on manual process controls for validating the plausibility of the automatically aggregated findings. The risk management system is linked to the internal control system and encompasses not only operational risk management throughout the Group, but also the systematic early identification of risks as well as their control and monitoring. More explanatory notes about the risk management system can be found in the "Risk management system" section of the risk report.

Structure of the Group accounting process

Accounting procedures are reported in the separate financial statements of freenet AG's subsidiaries, largely by way of local accounting systems from the manufacturer SAP. freenet AG uses the module "EC-CS" from SAP as its consolidation system at the highest level in the Group. When the consolidated balance sheet, the consolidated income statement, the consolidated statement of cash flows, and the consolidation of capital, liabilities, expenses and income, etc., are being prepared, the subsidiaries' reporting data are fed into the consolidation system in different ways—mostly automatically via the SAP module "FI", but in individual cases also manually by entering the reporting data. The individual disclosures in the management report and the explanatory notes are gathered from standardised report packages and institutionalised coordination processes within the scope of the internal control system which are maintained in MS Excel and other programs. The consolidation of these explanatory notes, too, is carried out in MS Excel.

The Group auditors at freenet AG check the correctness and the authorisations in the consolidation system SAP EC-CS at regular intervals. freenet AG's Group auditor regularly checks the interface between SAP-FI and the consolidation system SAP EC-CS and the reconciliations of the subsidiaries' standardised reporting packages all the way up to freenet AG's consolidated financial statements.

Major regulatory and control activities for ensuring proper and reliable Group accounting

The internal control system's measures designed to safeguard proper and reliable Group accounting ensure that business transactions are recorded fully, promptly and in accordance with the law and the company's articles of association.

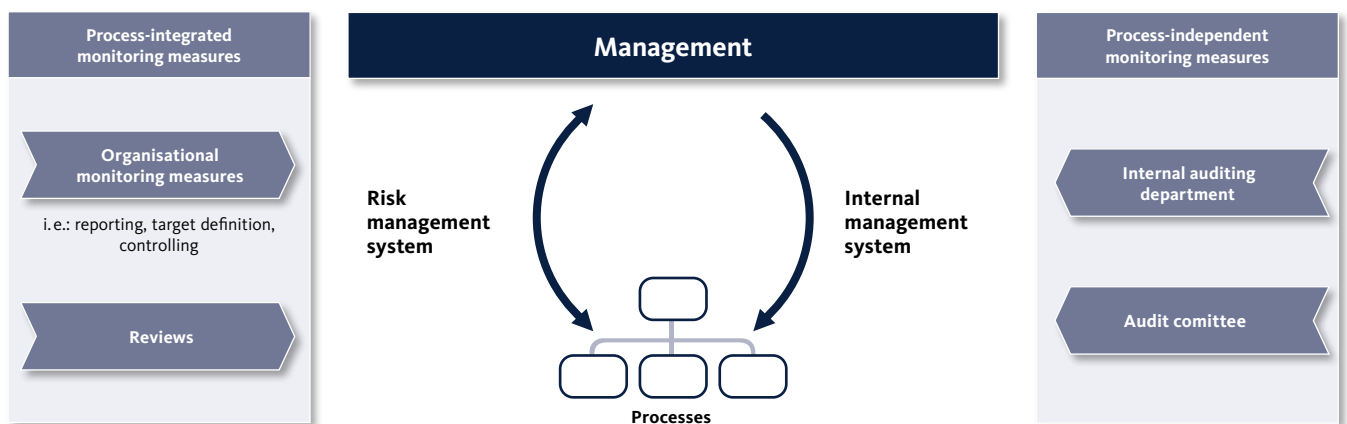
The regular control elements within the internal control system are aimed at extensive automation of the processes to generate and counter-check all significant data, starting with the accounting-relevant raw data and also including accounting vis-à-vis customers and ultimately valuation allowances, accruals and deferrals, and depreciation and amortisation. The automated controls are supplemented by manual validation of the plausibility of all relevant interim results and random checks of the underlying detailed data. This ensures that assets are carried out properly and that assets and liabilities are stated, evaluated and reported accurately in the consolidated financial statements. In addition, the process-independent audits by freenet AG's Group auditing department function as extraordinary control elements on behalf of the Supervisory Board, in particular under the supervision of the audit committee of freenet AG's Supervisory Board.

The annual audit of the internal control system by the Group auditing department showed in 2013 that the areas audited had implemented ideas for improvement which had been identified in the previous years. On the one hand, they have continuously intensified their proven controlling activities and increased the frequency of their checks, and on the other, they have increased the degree of automation within their controlling activities. They systematically derive measures from their control findings and monitor the success of these.

The Group auditor and other auditing entities are likewise included in the freenet Group's control environment with process-independent auditing activities.

In particular, the auditing of consolidated financial statements by the Group auditor and/or the auditing of the form-based financial statements from Group companies included in the consolidated financial statements constitute the final process-independent monitoring measure with regard to the Group accounting process.

Figure 4: freenet AG's internal control system



Forecast

The Executive Board confirms its guidance for the current financial year as included in the Group management report 2013 for the 2014 and 2015 financial years. There were no significant changes in the second quarter of 2014.

Accordingly, for the 2014 and 2015 financial years the company continues to expect a slight increase in Customer Ownership (postpaid and no-frills) — an important indicator — with the postpaid ARPU expected to fall slightly in the current financial year and stabilise in 2015.

A decrease in Group revenue is expected for the 2014 financial year, as the company has waived certain very low margin retail business activities with Hardware effective from the first quarter of 2014. A stabilisation of Group revenue is expected for the 2015 financial year.

In line with the developments described above, the company aims to achieve a Group EBIDTA of around 365 million euros for the 2014 financial year and around 370 million euros for the 2015 financial year.

The company also aims to achieve a free cash flow for the freenet Group in the amount of approx. 265 million euros in the 2014 financial year and approx. 280 million euros in the 2015 financial year. Free cash flow is defined as cash flow from operating activities, less investments in property, plant, equipment and intangible assets, plus cash inflows from the disposal of intangible assets and property, plant and equipment.

Due to long-term contractual commitments in the forecast period, the planned merger of the two network operators, O² and E-Plus, will have no measurable, negative effect on the business activities or the target indicators EBITDA and cash flow.

Significant events after the reporting date

There were no events after the balance sheet date which was of significance to the freenet Group.

Transactions with related parties

The following major transactions took place between the Group and related parties:

In EUR'000s	1. 1. 2014 –30. 6. 2014	1. 1. 2013 –30. 6. 2013
Sales and income attributable to services		
Joint ventures		
FunDorado GmbH, Hamburg	172	102
Companies with a major influence on freenet AG¹		
b2c.de GmbH, Munich (Drillisch AG Group)	n. a.	286
	172	388
Purchased services and onward charging		
Companies with a major influence on freenet AG¹		
eteleon e-solutions AG, Munich (Drillisch AG Group)	n. a.	24
b2c.de GmbH, Munich (Drillisch AG Group)	n. a.	3,029
	0	3,053

The following major receivables due from and liabilities due to related parties existed as at 30. June 2014:

In EUR'000s	30. 6. 2014	30. 6. 2013
Liabilities from regular transactions		
Joint ventures		
FunDorado GmbH, Hamburg	76	29
	76	29

All transactions were at market rates.

If the parties were not classified as related parties under IAS 24, no details were provided (n.a.).

¹ According to a voting rights notification dated 25 March 2013, the voting rights of Drillisch AG, including the shares held by MSP Holding GmbH, totalled 10.43 percent at 20 March 2013. So, because Drillisch AG has not been able to exercise any controlling influence on the freenet Group since 20 March 2013, Drillisch AG and its affiliated companies have not been classified as related parties. Transactions with companies in the Drillisch group during the first quarter of 2013 were therefore only reported as transactions with related parties if they occurred before 20 March 2013.

Condensed interim consolidated
financial statements

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Consolidated income statement

for the period from 1 January to 30 June 2014

In EUR '000s	1st half 2014 1. 1. 2014 – 30. 6. 2014	1st half 2013 1. 1. 2013 – 30. 6. 2013	Q2/2014 1. 4. 2014 – 30. 6. 2014	Q2/2013 1. 4. 2013 – 30. 6. 2013
Revenue	1,444,746	1,584,885	727,222	809,636
Other operating income	31,896	32,540	16,663	14,995
Other own work capitalised	5,164	2,863	2,766	1,385
Cost of materials	-1,071,707	-1,235,042	-536,689	-632,617
Personnel expenses	-94,802	-81,592	-48,507	-40,614
Depreciation and impairment write-downs	-32,399	-27,708	-16,442	-13,495
Other operating expenses	-142,362	-133,340	-73,899	-67,699
Operating result	140,536	142,606	71,114	71,591
Share of results of associates	148	125	78	76
Interest receivable and similar income	681	787	389	314
Interest payable and similar expenses	-20,840	-20,913	-11,080	-10,500
Result before taxes on income	120,525	122,605	60,501	61,481
Taxes on income	-6,023	-7,015	-3,427	-6,086
Group result from continued operations	114,502	115,590	57,074	55,395
Group result from discontinued operations	0	0	0	0
Group result	114,502	115,590	57,074	55,395
Group result attributable to shareholders of freenet AG	113,978	115,354	56,647	55,139
Group result attributable to non-controlling interest	524	236	427	256
Earnings per share in EUR (undiluted)	0.89	0.90	0.44	0.43
Earnings per share in EUR (diluted)	0.89	0.90	0.44	0.43
Earnings per share from continued operations in EUR (undiluted)	0.89	0.90	0.44	0.43
Earnings per share from continued operations in EUR (diluted)	0.89	0.90	0.44	0.43
Earnings per share from discontinued operations in EUR (undiluted)	0.00	0.00	0.00	0.00
Earnings per share from discontinued operations in EUR (diluted)	0.00	0.00	0.00	0.00
Weighted average of shares outstanding in thousand (undiluted)	128,011	128,011	128,011	128,011
Weighted average of shares outstanding in thousand (diluted)	128,011	128,011	128,011	128,011

Consolidated statement of comprehensive income

for the period from 1 January to 30 June 2014

In EUR '000s	1st half 2014 1. 1. 2014 – 30. 6. 2014	1st half 2013 1. 1. 2013 – 30. 6. 2013	Q2/2014 1. 4. 2014 – 30. 6. 2014	Q2/2013 1. 4. 2013 – 30. 6. 2013
Group result	114,502	115,590	57,074	55,395
Change in fair value of held-for-sale financial instruments	-31	-65	1	-16
Foreign currency translation adjustments	56	0	55	0
Taxes on income recognised directly in equity	-7	19	-16	5
Other comprehensive income (not recognised in profit or loss)/ to be reclassified to the income statement in the following periods	18	-46	40	-11
Other comprehensive income (not recognised in profit or loss)	18	-46	40	-11
Consolidated comprehensive income	114,520	115,544	57,114	55,384
Consolidated comprehensive income attributable to shareholders of freenet AG	113,996	115,308	56,687	55,128
Consolidated comprehensive income attributable to non-controlling interest	524	236	427	256

Consolidated balance sheet

as of 30 June 2014

Assets

In EUR '000s	30.6.2014	31.3.2014	31.12.2013
Non-current assets			
Intangible assets	403,838	414,256	397,331
Goodwill	1,151,758	1,150,118	1,122,112
Property, plant and equipment	33,284	34,363	33,752
Investments in associates	1,394	1,465	1,395
Other investments	1,542	1,540	1,540
Deferred income tax assets	188,709	184,916	186,947
Trade accounts receivable	75,578	77,343	78,508
Other receivables and other assets	12,329	16,416	14,549
	1,868,432	1,880,417	1,836,134
Current assets			
Inventories	70,640	74,643	69,802
Current income tax assets	4,648	4,609	2,326
Trade accounts receivable	376,867	395,255	423,121
Other receivables and other assets	40,064	44,669	35,049
Cash and cash equivalents	108,866	121,261	110,766
	601,085	640,437	641,064
	2,469,517	2,520,854	2,477,198

Shareholders' equity and liabilities

In EUR '000s	30.6.2014	31.3.2014	31.12.2013
Shareholders' equity			
Share capital	128,061	128,061	128,061
Capital reserve	737,536	737,536	737,536
Cumulative other comprehensive income	-12,768	-12,808	-12,786
Retained earnings	312,138	441,107	383,776
Capital and reserves attributable to shareholders of freenet AG	1,164,967	1,293,896	1,236,587
Capital and reserves attributable to non-controlling interest	3,519	3,092	2,995
	1,168,486	1,296,988	1,239,582
Non-current liabilities			
Trade accounts payable	23	0	0
Other payables	52,310	66,596	65,894
Borrowings	517,980	517,766	517,599
Deferred income tax liabilities	151	154	157
Pension provisions	44,965	44,646	44,369
Other provisions	6,609	9,352	9,512
	622,038	638,514	637,531
Current liabilities			
Trade accounts payable	359,697	369,605	401,970
Other payables	105,543	109,540	113,520
Current income tax liabilities	55,632	53,706	43,276
Borrowings	136,227	28,399	20,413
Other provisions	21,894	24,102	20,906
	678,993	585,352	600,085
	2,469,517	2,520,854	2,477,198

Schedule of changes in equity

from the period from 1 January to 30 June 2014

In EUR '000s	Cumulative other comprehensive income							Shareholders' equity
	Share capital	Capital reserve	Revaluation reserve	Actuarial valuation reserve in accordance with IAS 19	Retained earnings	Capital and reserves attributable to shareholders of freenet AG	Capital and reserves attributable to non-controlling interest	
As of 01.01.2013	128,061	737,536	-13	-13,284	324,883	1,177,183	370	1,177,553
Initial consolidation of subsidiaries	0	0	0	0	0	0	2,994	2,994
Dividend Payment	0	0	0	0	-172,815	-172,815	0	-172,815
Acquisition of additional shares in subsidiaries	0	0	0	0	366	366	-366	0
Recognition of stock option liabilities connected to company acquisitions	0	0	0	0	-7,601	-7,601	0	-7,601
Group result	0	0	0	0	115,354	115,354	236	115,590
Change in fair value of held-for-sale financial instruments	0	0	-46	0	0	-46	0	-46
Sub-total : Consolidated comprehensive income	0	0	-46	0	115,354	115,308	236	115,544
As of 30.6.2013	128,061	737,536	-59	-13,284	260,187	1,112,441	3,234	1,115,675

In EUR '000s	Cumulative other comprehensive income							Shareholders' equity	
	Share capital	Capital reserve	Revaluation reserve	Foreign currency translation adjustments	Actuarial valuation reserve in accordance with IAS 19	Retained earnings	Capital and reserves attributable to shareholders of freenet AG		Capital and reserves attributable to non-controlling interest
As of 1.1.2014	128,061	737,536	-69	0	-12,717	383,776	1,236,587	2,995	1,239,582
Dividend Payment	0	0	0	0	0	-185,616	-185,616	0	-185,616
Group result	0	0	0	0	0	113,978	113,978	524	114,502
Change in fair value of held-for sale financial instruments	0	0	-22	0	0	0	-22	0	-22
Foreign currency translation	0	0	0	40	0	0	40	0	40
Sub-total: Consolidated comprehensive income	0	0	-22	40	0	113,978	113,996	524	114,520
As of 30.6.2014	128,061	737,536	-91	40	-12,717	312,138	1,164,967	3,519	1,168,486

Consolidated statement of cash flows

for the period from 1 January to 30 June 2014

In EUR '000s	1. 1. 2014 – 30. 6. 2014	1. 1. 2013 – 30. 6. 2013
Result from continued and discontinued operations before interest and taxes (EBIT)	140,684	142,731
Adjustments		
Depreciation and impairment on items of fixed assets	32,399	27,708
Result of companies using the equity method	-148	-125
Income from the sale of subsidiaries	0	-4,009
Profits/Loss on disposals of fixed assets	-197	28
Increase in net working capital not attributed to investing or financing activities	-18,186	-24,396
Other non-cash components	0	-151
Income taxes paid	-12,815	-8,993
Cash flow from operating activities	141,737	132,793
Investments in property, plant and equipment and intangible assets	-10,886	-6,090
Proceeds from the disposal of property, plant and equipment and intangible assets	417	48
Purchase of subsidiaries	-46,929	-12,111
Proceeds from sale of subsidiaries	540	500
Outflow of funds from deconsolidation	0	-2,734
Return of contributions from companies consolidated using the equity method	150	0
Interest received	487	530
Cash flow from investing activities	-56,221	-19,857
Payments to company owners and minority shareholders	-185,616	-172,815
Payments for the acquisition of minority interests	0	-5,000
Cash repayments of borrowings	-158	-44,865
Interest paid	-30,642	-30,533
Cash flow from financing activities	-216,416	-253,213
Cash-effective change in cash and cash equivalents	-130,900	-140,277
Cash and cash equivalents 1.1.	110,766	207,353
Cash and cash equivalents 31.3.	-20,134	67,076
Composition of cash and cash equivalents		
In EUR '000s	30. 6. 2014	30. 6. 2013
Cash and cash equivalents of continued operations	108,866	127,076
Liabilities for short-term financial planning to banks	-129,000	-60,000
	-20,134	67,076
Composition of free cash flow		
In EUR '000s	30. 6. 2014	30. 6. 2013
Cash flow from operating activities	141,737	132,793
Investments in property, plant and equipment and intangible assets	-10,886	-6,090
Proceeds from the disposal of property, plant and equipment and intangible assets	417	48
Free cash flow (FCF)	131,268	126,751

Selected explanatory notes in accordance with IAS 34

Major accounting, valuation and consolidation principles

1. These condensed consolidated interim financial statements have been prepared in accordance with Regulation (EC) No. 1606/2002 of the European Parliament and of the Council, based on the international accounting standards endorsed by the European Union, the International Financial Reporting Standards (IFRS), in accordance with IAS 34. The Group took into account all IFRSs adopted and mandated by the EU. No review of these condensed consolidated interim financial statements has been carried out.

The Group applied all of the accounting standards which have been mandatory since 1 January 2014. Of the accounting standards which were applied for the first time, the following had no material impact on the presentation of the Group's net assets, financial position and results of operations: the amendments to IAS 32 (Financial Instruments: Presentation—Offsetting Financial Assets and Financial Liabilities), IAS 39 (Financial Instruments: Recognition and Measurement—Novation of Derivatives and Continuation of Hedge Accounting), IFRIC 21 (Levies: Identification of a present obligation to pay a levy) and the amendments to IFRS 10, IFRS 12 and IAS 27 with regard to the exemption of investment companies from the consolidation obligation. The revised IAS 36, whose application has been mandatory for the first time as of 1 January, requires more detailed disclosures if there is evidence of impairment. If, as was the case in the first half of 2014, there is no evidence of impairment, the disclosures are less detailed.

The accounting and valuation methods used to prepare the interim report for the period ending 30 June 2014 and to establish the benchmark figures for the previous year are the same as those which were applied in the consolidated financial statements for the period to 31 December 2013. A detailed description of the Group's accounting and valuation methods is included in the notes to the consolidated financial statements of freenet AG as at 31 December 2013.

Significant events and transactions

2. On 16 December 2013, the Group concluded a purchase agreement to acquire all of the shares and voting rights in the companies Jesta Digital GmbH, now renamed as freenet digital GmbH, based in Berlin; Jesta Digital Holdings, Inc., now renamed as freenet digital Holdings, Inc., based in the USA; and Jesta Digital Group U.S. Holdings, Inc., based in the USA (these companies and their subsidiaries are hereinafter referred to as “freenet digital Group”). Following approval from the anti-trust authorities and after having met other conditions, the takeover was completed effective 15 January 2014, which gave the Group control over this subsidiary. With offices in Berlin and Los Angeles, as well as around 300 employees, freenet digital Group is one of the world’s leading providers of modern digital entertainment formats and services for users of digital applications.

A cash purchase price of USD 72.18 million was agreed. The cash purchase price was subject to adjustments depending on the net working capital, cash and cash equivalents, and financial liabilities of the purchased group of companies. The authoritative binding determination of these purchase price adjustments took place in July 2014. The final cash purchase price is the equivalent of 45,984 thousand euros. In the first six months of 2014, the Group recorded a cash outflow of 50,125 thousand euros as the provisional cash purchase price. The proceeds amounting to 4,141 thousand euros resulting from the final adjustment of the cash purchase price were received by the Group in July 2014 after the reporting date of these condensed consolidated interim financial statements.

In addition, there may be a first earn-out ranging between USD 0 and USD 10 million; the exact amount of this earn-out is based on the gross profit of freenet digital Group for the 2014 calendar year. As of the first-time consolidation on 15 January 2014, the Group recognised a purchase price liability of 3,655 thousand euros for the first earn-out. For this purpose, various scenarios throughout the full range were evaluated with their probabilities of occurrence. As at 30 June 2014, this purchase price liability is recognised at 3,757 thousand euros, following the addition of any accrued interest.

There may also be a second earn-out. This depends on whether freenet digital Group or significant parts thereof is/are sold within the first 60 months of being acquired or within the first 96 months if a certain EBITDA level is achieved. Under certain conditions, a defined share of the proceeds from the sale would fall due as an additional purchase price, for which no upper limit has been set.

The purchase price allocation carried out in accordance with IFRS 3 for the acquisition of freenet digital Group is final and conclusive.

The following overview provides details of the assets and liabilities of freenet digital Group acquired at fair value at the time of the initial consolidation:

Assets and liabilities of Jesta Digital Group measured at fair value as at 15 January 2014

Assets		Liabilities	
In EUR'000s	15.1.2014	In EUR'000s	15.1.2014
Non-current assets		Non-current liabilities	
Intangible assets	26,873	Deferred tax liabilities	7,523
Goodwill	29,249		7,523
Property, plant and equipment	660		
Other receivables and other assets	202		
	56,984		
Current assets		Current liabilities	
Current income tax assets	1,415	Trade account payable	10,249
Trade accounts receivable	18,141	Other liabilities and deferrals	3,982
Other receivables and other assets	2,710	Current tax liabilities	8,307
Liquid assets	3,833	Other provisions	3,383
	26,099		25,921
	83,083		33,444

The difference of 49,639 thousand between the assets and liabilities represents the expected total purchase price at the time of the initial consolidation (final cash purchase price of 45,984 thousand euros plus the expected first earn-out at the time of acquisition of 3,655 thousand euros). The purchase price allocation results in goodwill of 29,249 thousand euros, which is attributable mainly to freenet digital Group's ability to continue acquiring new customers in the future, as well as to the company's workforce which cannot be recognised separately on the balance sheet. The goodwill was allocated to the cash-generating unit "freenet digital Group". The acquired intangible assets mainly comprise customer relationships worth 12,189 thousand euros, technology (in excess of the sum already reported in freenet Digital Group's financial statements in the purchase price allocation) in the amount of 9,132 thousand euros and trademark rights totalling 3,879 thousand euros, which were recognised as a result of the purchase price allocation. Due to the subsequent amortisation of the intangible assets recognised in the course of the purchase price allocation over a useful life of 48 to 60 months, amortisation amounting to 1,309 thousand euros per quarter will be recognised in the first four years following the acquisition date and 1,066 thousand euros per quarter in the fifth year following the acquisition date. No contingent liabilities were recognised in the purchase price allocation. The fair value of the acquired receivables is 21,053 thousand euros. Value adjustment allowances amounting to 2,122 thousand euros were set aside for gross trade receivables of 20,263 thousand euros as at the acquisition date. We

have not identified any transactions which have to be shown separately from the acquisition of the assets and liabilities. A budgeting plan based on the DCF procedure and with valuation relevance was made available for the purchase price allocation. This covered a detailed period of three years and a rough planning period of a further three years. The royalty relief method was used to determine the fair values of the technology and the trademark rights. The fair value of the customer relationships was determined using a capital-value-oriented procedure based on the residual value method.

The ongoing spread of smartphones and tablet PCs together with data-friendly mobile phone tariffs is fuelling increasing demand for mobile digital lifestyle applications. With the acquisition of freenet digital Group, freenet plans to press ahead with its growth course in the digital lifestyle segment.

For the purpose of the freenet AG Group's segment reporting, freenet digital Group was allocated to the "Other/Holding" segment.

During the first six months of 2014, freenet digital Group contributed a total of 12.7 million euros to Group revenue with third parties following its first-time consolidation. If this transaction had taken place on 1 January 2014, its contribution to Group revenue would have been 14.1 million euros in the first six months of 2014. Its contribution to the Group's earnings was of minor significance. This would still have been the case had the transaction taken place on 1 January 2014.

3. By means of an asset deal in the second quarter of 2014, the Group acquired from reStore GmbH, Düsseldorf, by way of the subsidiary GRAVIS which is reported in the "Mobile Communications" segment, the right to be specified in the rental agreements as the new shop tenant for particular shop locations previously operated by reStore GmbH, or to conclude these rental agreements anew with the landlord. This right applies to up to twelve locations. Three locations, for which payments amounting to 637 thousand euros were made, had been taken over by 30 June 2014.

The simplified purchase price allocation carried out in connection with this acquisition is of a provisional nature because it was only possible to establish a provisional figure for the fair values of the identifiable assets and liabilities. The provisional purchase price allocation dealt with the acquired assets as follows: 165 thousand euros was allocated to the right to take over the rental agreements or conclude them anew and 75 thousand euros was allocated to factory and office equipment taken over. The remaining 397 thousand euros was recognised provisionally as goodwill and can essentially be attributed to the workforce that was taken over.

The reStore locations were taken over as part of our strategy of further increasing the number of our directly controllable shops, and therefore our proximity to customers.

4. The statement of cash flows for the first six months of 2014 shows an outflow of 46,929 thousand euros for the acquisition of subsidiaries under the cash flow from investing activities. In addition to the cash price of 50,125 thousand euros paid for the acquisition of freenet digital Group, the Group also received cash and cash equivalents amounting to 3,833 thousand euros for the purposes of the statement of cash flows (holdings of liquid assets less liabilities due to banks in connection with the short-term management of financial investments) as a result of the first-time consolidation of freenet digital Group. The Group's cash outflow for the reStore shops it has taken over so far has been 637 thousand euros.
5. For some time now, the freenet Group has been offering its end customers the opportunity to choose higher-value devices for an additional monthly fee with its mobile phone upgrade option. Contracts with this mobile phone upgrade option continue to be recognised as follows: freenet has an unconditional right to payment from the customer receiving the mobile phone as part of the mobile phone upgrade option. freenet records a receivable in the amount of the present value of the additional monthly amounts to be paid by the customer for the higher-value mobile phone over the term of the contract when the contract is signed and the mobile phone is handed over. As customers' willingness to pay more for higher-value smartphones has increased, the number of postpaid customers selecting this mobile phone upgrade option has risen steadily over the past few financial years. This also means that the figure for deferred receivables relating to the mobile phone upgrade option recognised under non-current and current trade receivables has climbed continuously. For the freenet Group, this means that tied-up capital has been rising for years: today's higher-value smartphones are more expensive to purchase than the mobile phones of the past, and while cash outflows to acquire these devices occur before or when a contract is signed with the end customer, cash inflows from the mobile phone upgrade option are spread over the 24 months of the contract with the end customer.

With this in mind, the Group has concluded a factoring agreement with a bank, which was first utilised in Q1 2014. As at 30 June 2014, receivables from the mobile phone upgrade option with a nominal value of 30.3 million euros (31 March 2014: 23.2 million euros) were sold. Consequently, deferred receivables from the mobile phone upgrade option within non-current and current trade receivables fell to 184.3 million euros as at 30 June 2014 compared to 31 March 2014.

The contract with the bank is a master agreement with an indefinite term. It is possible to sell mobile phone upgrade option receivables on a quarterly basis up to a certain limit. Within this limit, freenet is at liberty to decide whether and to what extent receivables are to be sold. This sale of receivables without recourse represents genuine factoring. The relevant risks (such as the risk of default) and opportunities are transferred to the bank. The bank purchases the receivables with a defined del credere discount and it also bills freenet for interest and fees.

6. The underlying figure for the statement of cash flows is the earnings generated by ongoing and discontinued operations before interest and income taxes (EBIT). The following table shows the way in which this EBIT figure is derived from the consolidated income statement:

Calculation of the starting point for determining the consolidated cash flow statement

In EUR'000s	1. 1. 2014 - 30. 6. 2014	1. 1. 2013 - 30. 6. 2013
Earnings before taxes of continued operations	120,525	122,605
Interest payable and similar expenses of continued operations	20,840	20,913
Interest payable and similar income of continued operations	-681	-787
Earnings before interest and taxes (EBIT) of continued and discontinued operations	140,684	142,731

Other disclosures

7. Our disclosures on the subject of fair values are as follows (see next page):

The following overview 'Fair value hierarchy as at 30 June 2014', shows the key parameters upon which the valuation of both financial instruments measured at fair value as well as some of the financial instruments measured at amortised cost and for which a fair value has been determined, are based. For definitions of the individual levels as per IFRS 13, we refer to the Notes to the Consolidated Financial Statements of freenet AG as at 31 December 2013.

Financial instruments according to classes as of 30 June 2014

In EUR'000s	Valuation category according to IAS 39	Carrying amount 30.6.2014	Approach				Fair Value 30.6.2014
			Amortised cost of purchase	Cost of purchase	Fair value in income statement	Fair value in equity	
Assets							
Cash and cash equivalents	KF	108,866	108,866				108,866
Total cash and cash equivalents		108,866	108,866				108,866
Other financial assets (measured at cost of purchase)	ZVF	503		503			-
Other financial assets (measured at fair value)		1,039				1,039	1,039
Total other financial assets		1,542					
Trade accounts receivable	KF	452,445	452,445				452,665
Other non-derivative financial assets	KF	33,382	33,382				33,382
Held-for-sale other assets	ZVF	2,864				2,864	2,864
Derivative financial assets	EFVM	0			0		0
Non-financial assets		16,147					
Sum of receivables and other assets		52,393					
Liabilities							
Trade accounts payable	FV	359,720	359,720				359,720
Financial debt (liabilities due to banks and shareholders)	FV	653,909	653,909				696,764
Derivative financial liabilities	EFVM	0			0		0
Sum of financial liabilities within the scope of IFRS 7		653,909					696,764
Other non-derivative financial liabilities measured at cost of purchase	FV	95,473	95,473				95,473
Non-financial liabilities		62,381					
Sum of liabilities and deferrals		157,854					
Financial instruments not covered by the scope of IFRS 7							
Present values of liabilities from finance lease according to IAS 17		298					298
Pension provisions according to IAS 19		44,965					44,965
Provisions for employee participation programmes according to IFRS 2		1,988					1,988
Sum of financial instruments not covered by the scope of IFRS 7		47,251					
Thereof aggregated by valuation categories according to IAS 39							
Held-for-sale financial instruments (HFS)	ZVF	4,406		503		3,903	3,903
Loans and receivables (LR)	KF	594,693	594,693				594,913
Financial instruments measured at fair value through profit or loss (FIPL)	EFVM	0			0		0
Financial liabilities measured at amortised cost of purchase (FLAC)	FV	-1,109,102	-1,109,102				-1,157,957

Fair value hierarchy as of 30 June 2014

In EUR'000s	Total	Level 1	Level 2	Level 3
Held-for-sale other assets	2,864	2,864	0	0
Other financial assets	1,039	1,039	0	0
Trade accounts receivable	74,728	0	0	74,728
Borrowings	560,556	437,332	0	123,224
Total	-481,925	-433,429	0	-48,496

There were no shifts regarding the levels.

Other financial assets are measured at fair value. Wherever a reliable estimate of fair value is not possible, the asset is valued at its cost of acquisition. The shares that are valued at acquisition cost are not publicly traded and there is no active market for them. Furthermore, a sale is not currently planned. If there are indications that fair values are lower, these are used.

8. With the exception of the acquisitions described above, the scope of consolidation remained unchanged compared with the consolidated financial statements for the period ending 31 December 2013.
9. As was the case in the 2013 consolidated financial statements, an average rate of 29.85 per cent (same period in the previous year: 29.3 per cent) was used to calculate the current and deferred income taxes.
10. During the first six months of 2014, net borrowing increased by 118.1 million euros from 427.2 million euros to 545.3 million euros. The cash flow from operating activities was the most important factor reducing net borrowing, while the dividend distribution and the purchase of freenet Digital Group were the main reasons for cash outflows which had the opposite effect.
11. There were no events of significance after the balance sheet date.
12. Segment reporting (see following double-page spread)
The "Other/Holding" segment includes other business activities in addition to operating activities. These primarily include freenet AG's activities as a holding company (with the provision of intra-Group services in central divisions such as Legal, HR and Finance), as well as other accounting entries that cannot be clearly allocated. The segment revenue of 37.6 million euros (previous year: 24.3 million euros) reported for the "Other/Holding" segment in the first half of 2014 relates to operating activities (34.4 million euros; previous year: 21.5 million euros) and other business activities (3.2 million euros; previous year: 2.8 million euros). The gross profit of 25.1 million euros (previous year: 13.1 million euros) reported for the "Other/Holding" segment in the first half of 2014 relates to operating activities (25.3 million euros; previous year: 13.1 million euros) and other business activities (-0.2 million euros; previous year: 0.0 million euros). The EBITDA of -8.8 million euros (previous year: 1.8 million euros) reported for the "Other/Holding" segment in the first half of 2014 relates to operating

activities (0.2 million euros; previous year: 10.3 million euros) and other business activities (-9.0 million euros; previous year: -8.5 million euros). The EBIT of -13.7 million euros (previous year: -0.2 million euros) reported for the “Other/Holding” segment in the first half of 2014 relates to operating activities (-2.0 million euros; previous year: 5.5 million euros) and other business activities (-11.7 million euros; previous year: -7.5 million euros).

The decline in EBITDA and EBIT generated by the operating activities of the “Other/Holding” segment compared with the same period last year is primarily attributable to the fact that the figure for the first half of 2013 included gains of 4.0 million euros from the disposal of freeXmedia GmbH.

Segment report 1 January to 30 June 2014

In EUR'000s	Mobile Communications	Other/Holding	Elimination of intersegment revenue and costs	Total
Third-party revenue	1,413,938	30,808	0	1,444,746
Intersegment revenue	4,527	6,790	-11,317	0
Revenue, total	1,418,465	37,598	-11,317	1,444,746
Cost of materials, third party	-1,063,244	-8,463	0	-1,071,707
Intersegment cost of materials	-4,277	-4,080	8,357	0
Cost of materials, total	-1,067,521	-12,543	8,357	-1,071,707
Segment gross profit	350,944	25,055	-2,960	373,039
Other operating income	30,723	5,548	-4,375	31,896
Other own work capitalised	4,210	954	0	5,164
Personnel expenses	-72,942	-21,860	0	-94,802
Other operating expenses	-131,072	-18,625	7,335	-142,362
Share of result in associates	0	148	0	148
Segment EBITDA	181,863	-8,780	0	173,083
Depreciation and impairment write-downs	-27,456	-4,943	0	-32,399
Segment EBIT	154,407	-13,723	0	140,684
Group financial result				-20,159
Taxes on income				-6,023
Group result from continued operations				114,502
Group result from discontinued operations				0
Group result				114,502
Group result attributable to shareholders of freenet AG				113,978
Group result attributable to non-controlling interest				524
Investments in continued operations	9,117	1,769		10,886

Segment report 1 January to 30 June 2013

In EUR'000s	Mobile Communications	Other/Holding	Elimination of intersegment revenue and costs	Total
Third-party revenue	1,565,752	19,133	0	1,584,885
Intersegment revenue	3,360	5,176	-8,536	0
Revenue, total	1,569,112	24,309	-8,536	1,584,885
Cost of materials, third party	-1,227,120	-7,922	0	-1,235,042
Intersegment cost of materials	-2,726	-3,302	6,028	0
Cost of materials, total	-1,229,846	-11,224	6,028	1,235,042
Segment gross profit	339,266	13,085	-2,508	349,843
Other operating income	27,074	7,339	-1,873	32,540
Other own work capitalised	2,594	269	0	2,863
Personnel expenses	-70,103	-11,489	0	-81,592
Other operating expenses	-130,139	-7,582	4,381	-133,340
Share of result in associates	0	125	0	125
Segment EBITDA	168,692	1,747	0	170,439
Depreciation and impairment write-downs	-25,756	-1,952	0	-27,708
Segment EBIT	142,936	-205	0	142,731
Group financial result				-20,126
Taxes on income				-7,015
Group result from continued operations				115,590
Group result from discontinued operations				0
Group result				115,590
Group result attributable to shareholders of freenet AG				115,354
Group result attributable to non-controlling interest				236
Investments in continued operations	5,260	830		6,090

Further information

Financial calendar

6 August 2014

Interim Report as of 30.06.2014—Second Quarter 2014

9 September 2014

TMT Conference, Commerzbank, Frankfurt, Deutschland

23 September 2014¹

3rd German Corporate Conference, Berenberg/GS, München, Deutschland

7. November 2014¹

Interim Report for the period January to September 2014—Third Quarter 2014

¹ Probable dates.

Imprint, contact, publications

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The annual report and our interim reports are also available at:
www.freenet-group.de/investor/publications/quarterly-annual-reports

The English version of the Interim Report is a translation of the German version of the Interim Report. The German version of this Interim Report is legally binding.

Current information concerning freenet AG and the freenet share is available on our website at:
www.freenet-group.de/en



If your mobile phone has QR-Code recognition software, you will be directed to the freenet Group website by scanning this code.

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