

Letter to shareholders

Dear shareholder:

AS AN OWNER OF **TELEFÓNICA** SHARES, YOU ARE A PARTICIPANT IN ONE OF THE LEADING telecommunications companies of Spain and Latin America, one that has set itself the goal of advancing until it reaches the ranks of the five leading operating companies worldwide. A company that in 1998 went on to manage 49 million customers from a figure of 35 million in 1997, and which has experienced a 14.5% annual growth of net profit following an investment campaign unprecedented in the sector.

In 1998, the value of our company's shares has increased 52 per cent, sustaining a trend of continuously increasing value, which has seen them grow 104 per cent since the conclusion of the privatization process in 1997.

When I addressed you a year ago in these pages, I referred to the progressive liberalization of the telecommunications marketplace, and I expressed the confidence with which we in **Telefónica** were meeting the challenges posed by competition. With 1998 over, we can say that we did well not to fear the opening of the market. In **Telefónica**, we view this process not as a threat, but as a great



opportunity; it is a means to achieve additional growth and enter markets where we had not been present before.

The delay on the part of the Spanish Regulatory Authority in resolving such critical problems as the access deficit, tariff rebalancing and an interconnection pricing policy which sets prices below real costs, has spurred **Telefónica** to improve its efficiency, to diversify its sources of revenue, and to carry out strategic investments in businesses and markets with high growth potential.

The acquisitions made in Brazil have placed **Telefónica** in the position of leading operator in the largest telecoms market of the region. These investments are part of the company's strategy to maintain as its priority objective the creation of shareholder value. I would like to specifically endorse the company's commitment to leadership in the Spanish- and Portuguese-speaking market; a commitment which will guarantee growth for years to come.

Telefónica continues to place a high value on fostering direct links with its customers by offering an increasing number of solutions that bring together telecommunications, Internet and multimedia services.

The company has already become a multinational operator and it therefore needs a single brand for all its services in all geographical and service markets in which it operates. For this reason,

we have adopted the **Telefónica** name as our trademark, in a graphic expression which symbolizes the market changes that have taken place and associates them with the concept of close ties to our customers in all the countries where we operate. Today, one of **Telefónica's** greatest assets is its brand name.

Telefónica means growth, and in this context we must place our decision to substitute the distribution of a dividend by a policy of capital increases charged to reserves, a policy which will be continued if the shareholders' meeting approves it.

We started 1998 with a three-fold commitment to our shareholders, our customers and our employees. We now close the year with legitimate pride in having achieved our objectives in a particularly complex environment. We are also aware that success today is no guarantee for the future, and this conviction is enormously stimulating for us.

Ours is undoubtedly the most dynamic sector in the world and one of the most affected by two unstoppable factors of change: the globalization of the economy and the speed with which companies are evolving. We are prepared to operate successfully in this scenario and we have absolute confidence in the future of Telefónica.

I would like to close this letter by once again expressing my gratitude to our shareholders, customers and employees. They are the ones who have made it possible for **Telefónica** to become a leading company and a benchmark in the telecommunications market.

A handwritten signature in blue ink that reads "Juan Villalonga". The signature is written in a cursive style with a long vertical stroke on the left side.

Juan Villalonga
Chairman and CEO of Telefónica

