Focus on profitable leadership
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02 Our strategy ‘Focus on profitable leadership’

03 Closing remarks
Resilience and flexibility in a difficult environment
Difficult macro conditions

Increased competitive pressure

Since our last Investor Day, we have faced a tough market environment

- Mobile ARPM decline accelerating
- Aggressive promotions and cross-subsidies in fixed broadband

Real GDP\(^1\) var. y-o-y

- FY 2008: 0.9%
- FY 2009: -3.7%
- FY 2010: -0.1%

Retail service communication market revenue variation\(^2\)

- FY 2008: -4.4%
- FY 2009: -4.0%
- FY 2010: -4.0%

\(^1\) Source: INE
\(^2\) Source: CMT and internal estimates
Our performance has been affected...

Revenues have fallen...

Comparable revenues evolution¹
T. España

-5.9%
-4.4%
FY 2008
FY 2009
FY 2010

Highly affected by price based competition

Comparable access & voice revenues evolution²
T. España, Fixed & Mobile

-9.2%
-8.2%
FY 2008
FY 2009
FY 2010

¹ Comparable terms for y-o-y change include Tuenti in the period Aug/Dec-09 and exclude the following effects:
USO, Telyco Morocco (since Jan-10) and sale of application rights

² Voice and Access Revenue: Include fixed/mobile access & voice (SMS included), narrowband and mobile & fixed equipment revenues and exclude USO and sale of application rights
... though we have been resilient in core value parameters

Sustaining market leadership...

Revenue market share\(^1\)
- T. España

 comparable OIBDA margin\(^2\)
- T. España

OpCF after WC change\(^3\)
- T. España

<table>
<thead>
<tr>
<th></th>
<th>FY 2008</th>
<th>FY 2009</th>
<th>FY 2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>T. España</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Revenue market share (^1)</td>
<td>~55%</td>
<td>~54%</td>
<td>~53%</td>
</tr>
<tr>
<td>Comparable OIBDA margin (^2)</td>
<td>~49%</td>
<td>~48%</td>
<td>~47%</td>
</tr>
<tr>
<td>OpCF after WC change (^3)</td>
<td>-4.3%</td>
<td>-5.5%</td>
<td>-4.3%</td>
</tr>
</tbody>
</table>

\(^1\) Retail communication (fixed & mobile) revenue market share. \(\text{Source: CMT and internal estimates}\)

\(^2\) Comparable terms include Tuenti in the period Aug/Dec-09 and exclude the following effects: USO, real estate capital gains, Medi Telecom disposal capital gain, Telyco Morocco (since Jan-10), TV Tax, revision of the estimates for the personnel commitments provided for prior periods to 2009, 2010 non-recurrent restructurings costs, bad debt recovery and sale of application rights

\(^3\) Operating Cash Flow after Working Capital change: Operating collections less OpEx and CapEx payments. Adjusted for intragroup fees

y-o-y variation
Going forward, we maintain our confidence in macro recovery

- The worst is over and the Spanish economy is expected to grow
- Reforms are firmly on track
- There are some uncertainties on the timing of the recovery

Spain vs. Euro Zone: GDP growth rate differential¹

<table>
<thead>
<tr>
<th>Period</th>
<th>GDP Growth Rate Difference</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pre crisis years 2005-08</td>
<td>+1.0</td>
</tr>
<tr>
<td>Crisis years 2009-10</td>
<td>-0.7</td>
</tr>
<tr>
<td>Reform years 2011-12</td>
<td>-0.4</td>
</tr>
<tr>
<td>Medium &amp; long term Beyond 2013</td>
<td>+0.5</td>
</tr>
</tbody>
</table>

¹ Source: IMF and OECD
Competitive pressure is not expected to increase much further

<table>
<thead>
<tr>
<th>Competitive situation</th>
<th>Competitors likely to focus on service as macro improves</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Revenue market share</strong>&lt;sup&gt;1&lt;/sup&gt;</td>
<td><strong>Large international players</strong>&lt;sup&gt;1&lt;/sup&gt;</td>
</tr>
<tr>
<td>Fixed &amp; Mobile</td>
<td>Financial discipline</td>
</tr>
<tr>
<td><strong>Telefónica España</strong></td>
<td>Need to ensure revenue and margins</td>
</tr>
<tr>
<td>Large international players</td>
<td>High leverage ratios</td>
</tr>
<tr>
<td>Cable operators</td>
<td>Savings banks major shareholders</td>
</tr>
<tr>
<td>Yoigo &amp; MVNOs</td>
<td>Small market shares</td>
</tr>
<tr>
<td>Other wireline players</td>
<td>Diverse</td>
</tr>
</tbody>
</table>

FY 2010

---

<sup>1</sup> Retail communication (fixed & mobile) revenue market share. Source: CMT and internal estimates
The regulatory framework is more predictable

**Strict traditional business regulation**

- **ULL prices:**
  - CMT has recently raised prices to €8.32 (~+7%), below European Union average (~€9)
  - CMT decision represents a new regulatory path for ULL prices going forward

- **Geographic segmentation** expected

- **TV tax** under EU review

- **MTR price cuts** following the glide path (€4 c/min by Apr-12)

**Critical future issues mostly defined**

- **NGN Regulation**
  - Framework already defined
  - Infrastructure competition is encouraged (bitstream services up to 30 Mbps)

- **Spectrum auctions**
  - New bands for LTE: 800 MHz & 2.6 GHz
  - Contests and auctions for existing bands: 900 MHz & 1,800 MHz
  - **Refarming:** Technological neutrality across current 2G bands

CMT has recently raised prices to €8.32 (~+7%), below European Union average (~€9). CMT decision represents a new regulatory path for ULL prices going forward.

Geographic segmentation is expected. TV tax is under EU review. MTR price cuts are following the glide path (€4 c/min by Apr-12).

NGN Regulation includes a framework already defined and infrastructure competition is encouraged (bitstream services up to 30 Mbps).

Spectrum auctions cover new bands for LTE: 800 MHz & 2.6 GHz, contests and auctions for existing bands: 900 MHz & 1,800 MHz, and refarming for technological neutrality across current 2G bands.
New opportunities are arising in the market

**Strong FBB penetration increase**

Fixed broadband market accesses\(^1\)

<table>
<thead>
<tr>
<th>Year</th>
<th>Accesses (Million)</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dec-09</td>
<td>9.9</td>
<td>+8%</td>
</tr>
<tr>
<td>Dec-10</td>
<td>10.7</td>
<td>~20%</td>
</tr>
<tr>
<td>Dec-13E</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Growing IT importance**

IT market revenues\(^2\)

<table>
<thead>
<tr>
<th>Year</th>
<th>Revenues (€ bn)</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY 09</td>
<td>3.6</td>
<td>+3%</td>
</tr>
<tr>
<td>FY 10</td>
<td>3.7</td>
<td>~15%</td>
</tr>
<tr>
<td>FY 13E</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Heavy MBB adoption**

IP Data Mobile market traffic\(^3\)

<table>
<thead>
<tr>
<th>Year</th>
<th>Traffic (Petabytes/ Year)</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY 09</td>
<td>11.8</td>
<td>+90%</td>
</tr>
<tr>
<td>FY 10</td>
<td>22.5</td>
<td>~x7</td>
</tr>
<tr>
<td>FY 13E</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Market smartphone shipments\(^4\)

<table>
<thead>
<tr>
<th>Year</th>
<th>Shipments (Million)</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY 09</td>
<td>4.2</td>
<td>+60%</td>
</tr>
<tr>
<td>FY 10</td>
<td>6.9</td>
<td>~x2</td>
</tr>
<tr>
<td>FY 13E</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

---

\(^1\) Source: Internal estimates. Retail FBB: Include FO (Fiber Optic), DSL, cable modem and satellite.

\(^2\) Source: Internal estimates. Includes Corporate market for desktops, hosting, security and other applications.

\(^3\) Source: Internal estimates

\(^4\) Source: IDC
We are focused on profitable leadership to successfully manage this scenario.

Core principles:
- Defense of our OIBDA and our value leadership
- Flexibility to adapt to market conditions
- Capture market growth opportunities in a profitable way

Strategic priorities:
- Smart focus on value vs. pure volume
- Reshaping of our cost base
- Optimized use of capital

Focus on profitable leadership balancing short term results, long term sustainability and growth.
Our strategy ‘Focus on profitable leadership’
Our strategy ‘Focus on profitable leadership’

- Smart focus on value
- Reshaping of our cost base
- Optimized use of capital
We are handling our diverse customer base through a customized strategy

Service revenue split¹
T. España %

<table>
<thead>
<tr>
<th>Wholesale &amp; others²</th>
<th>Corporate &amp; businesses</th>
<th>Consumer</th>
</tr>
</thead>
<tbody>
<tr>
<td>10</td>
<td>42</td>
<td>48</td>
</tr>
</tbody>
</table>

Solid wholesale platform

- **Offsetting** flows (Yoigo agreement, wholesale data revenues...)

High level of service:
- In the field specialized sales force and technical support

Leading quality provider:
- Corporate: fibre premises (up to 10 Gbps)

Integrated value offer:
- Corporate: BB & Services beyond Connectivity³/ Total revenues

Strong position within experienced decision makers

Value leadership in an adverse and very competitive segment

- Stronger position in **higher value segments**: FBB, Mobile Contract, Smartphones, 3P
- The highest customer **satisfaction**:
  -CSI GAP⁴
- Best Fixed & Mobile platform:
  -Best in class **fixed broadband coverage**⁵
  -Best 3G coverage and quality⁶

---

¹ Excludes fixed & mobile handset sales, subsidiaries and others
² Others include USO
³ BB (retail and wholesale FBB connectivity, MBB, fixed and mobile devices (PCMCIA and Dongle) and fixed data services) and Services beyond Connectivity (Content, digital services, ICT solutions and vertical units revenues)
⁴ GAP vs. best competitor
⁵ Local loop ≥ 1 Mbps over total loops
⁶ Source: Spanish “Asociación de Internautas” Dec. 2010

**FY 2010**
A smart focus on value is key to capture recovery and ensure competitiveness

- A differentiated customer experience
- A product portfolio adapted to the needs and value of the client
- A leading approach to growth opportunities
- Churn reduction
- Differentiated value proposition
- Revenue growth in key opportunities > €1.2 bn

Moving from “volume” to “value”...

... and sustaining revenue market share ~48%-50%\(^1\) in FY 2013E

---

1. Retail communication (fixed & mobile) revenue market share. Source: CMT and internal estimates
2. Revenue increase from FY 2010-2013 E. Includes Services beyond Connectivity revenues: Content, digital services, ICT solutions and vertical units revenues and MBB revenues from smartphones, smart devices and connectivity MBB, mobile mail, MBB equipment (PCMCIAAs, Dongles), roaming, and WAP browsing. SMS and M2M excluded
Customer experience remains a crucial differentiating factor

- Attack root causes for dissatisfaction (e.g. claims)
- Differentiate service levels based on customer value (e.g. platinum customer care)
- Ensure an integrated full-customer experience (e.g. multichannel, multi-business)
- Reinforce our emotional bond

Blended churn evolution
T. España Base 100

<table>
<thead>
<tr>
<th></th>
<th>FY 2010</th>
<th>FY 2013E</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>100</td>
<td>95-90</td>
</tr>
</tbody>
</table>

Maintaining a gap vs. main competitor
We are adapting our product portfolio to the needs and value of each segment

Developing best practices in the corporate space…

- Leading the corporate space…
  - Seamless Fixed & Mobile proposition
  - Global MNC’s platform
- … by leveraging our differentiated IT proposal

...and a flexible value proposition for mass markets

- Acceleration of RGUs growth through F&M BB and Services beyond Connectivity
- On-line self-managed bundles and services configuration
- Differentiated product strategies for value clusters

FY 2013E

Corporate: BB & Services beyond Connectivity / total revenues

~68%

(+8 p.p. vs. FY 2010)

2P & 3P / Fixed lines

T. España


43%

FY 2010

FY 2013E

---

1 BB (retail and wholesale FBB connectivity, MBB, fixed and mobile devices (PCMCIAs and Dongle) and fixed data services) and Services beyond Connectivity (Content, digital services, ICT solutions and vertical units revenues)

2 % of fixed lines with broadband and/or Pay TV
In MBB our priority is to actively develop the market in a profitable way

- Pushing Smartphone adoption
  - ~65% Smartphone sales/ Total contract handset sales

- Offering pricing schemes adapted to different levels of use
  - 100% Customers with tiered pricing
  - Evolution towards more speed, flexibility and value

- Fostering complementary BB proposal
  - >70% T. España complementarity of MBB and FBB
  - 2% T. España substitution of MBB and FBB

---

1. Figure as of Q410
2. Complementarity rate defined as the share of Mobile Connectivity users that have an additional Fixed Broadband connection
3. Substitution defined as current customers moving from FBB to MBB over total new MBB
4. MBB accesses with data attached rate/Total mobile customer base

MBB accesses / Total mobile accesses T. España

- FY 2010: 20%
- FY 2013E: ~x2

Total variation FY 2010-2013E: 20%
Services beyond Connectivity will continue to be developed enriching our portfolio

**TV**
- **Pay TV evolution:**
  - **OTT model**¹ (Video Club Movistar)
  - >90% coverage over FBB lines
  - Improved quality and content

**IT**
- Further expansion of our solutions:
  - private cloud, virtual data center, clean pipes...

**New services**
- Leverage of global product development: e-Health, Security, M2M, Financial Services...

---

¹ OTT: Over the top.
² Services beyond Connectivity revenues: Content, digital services, ICT solutions and vertical units revenues
Our smart focus on value will enhance and diversify our revenue profile

- **Churn reduction**
- **Differentiated value proposition**
- **Revenue growth in key opportunities > € 1.2 bn**

**Revenue mix evolution**

T. España %

<table>
<thead>
<tr>
<th></th>
<th>FY 2010</th>
<th>FY 2013E</th>
</tr>
</thead>
<tbody>
<tr>
<td>BB &amp; SbC²</td>
<td>29</td>
<td></td>
</tr>
<tr>
<td>Access &amp; Voice³</td>
<td>&gt;35</td>
<td></td>
</tr>
</tbody>
</table>

1 Revenue increase from FY 2010-2013E. Includes Services beyond Connectivity and MBB revenues
2 Includes BB (retail and wholesale FBB connectivity, MBB, fixed and mobile devices (PCMCIA and Dongle) and fixed data services) and Services beyond Connectivity (Content, digital services, ICT solutions and vertical units revenues)
3 Access and Voice revenue include fixed/mobile access & voice (SMS included), narrowband and mobile & fixed equipment revenues
Our strategy ‘Focus on profitable leadership’

- Smart focus on value
- Reshaping of our cost base
- Optimized use of capital
There is further room to improve our efficiency and continue delivering a benchmark OIBDA margin

Benefit from our commercial focus on value (vs. volume) and manage direct costs …

- Gradually balancing SAC to SRC, acquisition vs. retention
- Increasing share and effectiveness of commercial costs
- Maintaining direct margin\(^1\) over revenues

More resources dedicated to customers and maintenance of direct margin

… while reshaping our non-commercial expenses

- Leveraging global scale (purchases and product development)
- Increasing the level of automation and remote management
- Fostering simplicity in IT applications, offer and legacy networks
- Fully online traceable commercial processes in 2013

Focus on reduction of non-commercial expenses

Continuing to deliver a benchmark OIBDA margin

---

\(^1\) Revenues less supply costs (interconnection, content and other direct supplies)
Additional measures to gain more flexibility and compensate for potential recovery delays

Current initiatives ...

- 6% reduction in manager positions
- More flexible collective bargaining agreements
  - TME pay revisions not linked to CPI in 2011
  - More flexible structure policies

... and moving towards more flexibility and higher productivity

- Pay and benefit revisions more linked to productivity rather than CPI
- ~ 85% employees under collective bargaining agreements
- Each p.p. of CPI increase represents ~ €15 m cost increase per annum
- Potential outsourcing of operations to service providers and/or...
- ...further workforce restructuring processes

\[ \checkmark \sim 20\% \text{ employees in 3 years} \]

1 T. España perimeter
Our strategy ‘Focus on profitable leadership’

- Smart focus on value
- Reshaping of our cost base
- Optimized use of capital
We will optimize the use of capital by adjusting our asset base...

Ongoing processes...
- Sale of IT applications
- Real estate
- ... and other programs

Sale of non-core assets

- Mobile Network sharing
- Co-investment approach for fibre infrastructure inside buildings

Cash proceeds of €600 m in the period FY 11-13E
...and follow a “smart” investment policy to capture growth

**Premium speed and quality**
- Selective fibre deployment

**Best mobility**
- HSPA+ & LTE deployment

### Household coverage

<table>
<thead>
<tr>
<th>Speed</th>
<th>Dec-10</th>
<th>Dec-13E</th>
</tr>
</thead>
<tbody>
<tr>
<td>&gt;10Mbps</td>
<td>~75%</td>
<td>~80%</td>
</tr>
<tr>
<td>&gt;25Mbps</td>
<td>~30%</td>
<td>~45%</td>
</tr>
</tbody>
</table>

### Mobile coverage by peak speed

<table>
<thead>
<tr>
<th>Speed</th>
<th>Dec-10</th>
<th>Dec-13E</th>
</tr>
</thead>
<tbody>
<tr>
<td>&gt;14Mbps</td>
<td>~50%</td>
<td>~100%</td>
</tr>
<tr>
<td>&gt;42Mbps</td>
<td>~0%</td>
<td>~25%</td>
</tr>
</tbody>
</table>

New access networks represent up to 1/3 of cumulative CapEx FY 2011 - 2013E

We will remain flexible and adapt to market conditions

---

1 Peak theoretical speed supported
03

Closing remarks
Focus on profitable leadership will balance short term results and long term sustainability and growth

**Core principles**

- Defense of our OIBDA and our value leadership
- Flexibility to adapt to market conditions
- Capture market growth opportunities in a profitable way

**Strategic priorities**

- Smart focus on value vs. pure volume
- Reshaping of our cost base
- Optimized use of capital

**Targets summary**

- Revenue market share ~48%-50%\(^1\) in FY 2013E
- > € 1.2 bn\(^2\) growth in key opportunities
- A benchmark OIBDA margin
- CapEx adapted to market conditions
- Cash proceeds of € 600 m in FY 11-13E

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\(^1\) Retail communication (fixed & mobile) revenue market share. Source: CMT and internal estimates

\(^2\) Revenue increase from FY 2010-2013E. Includes Services beyond Connectivity and MBB revenues