Sixth Investor Conference
Telefónica O2 Europe: A winning mindset

Peter Erskine
London, October 11th 2007
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Overview

- Telefónica O2 Europe growth has exceeded that of our combined local markets

- We see continued growth ahead, despite challenging markets, building on our strong position

- Partnerships will be critical in the future, and we have a track record of good execution

- We see a clear path back to growth in Germany

- We are making real improvements on efficiency and leveraging the scale of the Telefónica Group

A winning mindset
A strong starting position

Opportunities for growth

Our strategy for continued outperformance
01 2006 results

- **Revenues**
  - FY 2005
  - FY 2006
  - 9% vs. mobile market growth of ~0.5% and fixed market decline

- **Mobile customer base**
  - FY 2005
  - FY 2006
  - 10% vs. market growth ~ 6%

- **OIBDA**
  - FY 2005
  - FY 2006
  - 3% vs. market decline of at least 5%

Source: Company data
O2 UK the outstanding performer

### OIBDA change 2004 – 2006 (£ in millions)

- £414m
- £320m
- £77m
£171m

### Service Revenue growth

- FY 2004: 15%
- FY 2005: ~11%
- FY 2006: 15%

#### #1 OIBDA growth

#### #1 Service Revenue growth

#### #1 Customer Satisfaction

#### #1 Active Customer Base

#### #1 Brand
01 O2 Germany has delivered a market beating performance in the past

O2 Germany EBITDA (€ in millions)

- vs. market CAGR ~3%
- #1 for EBITDA growth
- #1 Customer Satisfaction
- #1 Post pay ARPU

O2 Germany Service Revenue (€ in millions)

- vs. market CAGR ~4%
- #1 for Service Revenue growth
- #1 Customer growth 2003 - 2006
- #1 MoU
**Telefónica O2 Czech Republic turnaround**

**Year-on-year growth in fixed business revenues**

- Q2 06: -5.1%
- Q3 06: -3.5%
- Q4 06: -6.1%
- Q1 07: -0.1%
- Q2 07: 0.7%

**Year-on-year growth in mobile service revenue**

- Q2 06: 4.6%
- Q3 06: 6.5%
- Q4 06: 8.0%
- Q1 07: 5.5%
- Q2 07: 5.8%

**Turnaround in revenue trend**

- #1 Integrated Operator
- DSL growth 40%

**Increasing Service Revenue growth**

- Grown Post pay base 20%
- #1 Market Entry for 3rd player (Slovakia)
Telefónica O2 Europe

1. A strong starting position

2. **Opportunities for growth**

3. Our strategy for continued outperformance
There are significant growth opportunities in our “core” business...

**Mobile Market MoU**

CAGR 06-10E

<table>
<thead>
<tr>
<th>Country</th>
<th>2006</th>
<th>2010E</th>
</tr>
</thead>
<tbody>
<tr>
<td>UK</td>
<td>~10%</td>
<td>~15%</td>
</tr>
<tr>
<td>Germany</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Mobile as % of Total Outbound Minutes**

<table>
<thead>
<tr>
<th>Country</th>
<th>2006</th>
<th>2010E</th>
</tr>
</thead>
<tbody>
<tr>
<td>UK</td>
<td>32%</td>
<td>19%</td>
</tr>
<tr>
<td>Germany</td>
<td>69%</td>
<td>42%</td>
</tr>
<tr>
<td>Czech Republic</td>
<td>47%</td>
<td>37%</td>
</tr>
<tr>
<td>Ireland</td>
<td>80%</td>
<td>63%</td>
</tr>
</tbody>
</table>

**SMS Messages (TEF O2 Europe)**

<table>
<thead>
<tr>
<th>Year</th>
<th>2006</th>
<th>2010E</th>
</tr>
</thead>
<tbody>
<tr>
<td>(m)</td>
<td>25,000</td>
<td>50,000</td>
</tr>
</tbody>
</table>

CAGR 06-10E

~15%

**Mobile Market Penetration**

<table>
<thead>
<tr>
<th>Country</th>
<th>2006</th>
<th>2010E</th>
</tr>
</thead>
<tbody>
<tr>
<td>UK</td>
<td>107%</td>
<td>~115%</td>
</tr>
<tr>
<td>Germany</td>
<td>108%</td>
<td>~120%</td>
</tr>
<tr>
<td>Czech Republic</td>
<td>104%</td>
<td>~120%</td>
</tr>
<tr>
<td>Ireland (Including M2M)</td>
<td>108%</td>
<td>~117%</td>
</tr>
</tbody>
</table>

Sources: Strategy Analytics and company forecasts/analysis
... as well as opportunities beyond voice and text

**Bundles and converged services**
- Multi-play bundles (Duos & Trios)
- Homezone services
- Content / information access (fixed and mobile)

**Mobile Internet**
- Music
- Internet search and advertising
- Enhanced messaging
- Moving pictures

**Retail / Wholesale Broadband**

*O₂ Broadband*

*Telefónica*
02 Why is the timing right for growth in non-SMS data...?

- Internet Partnerships
- Business data

New business models – mobile advertising, transactions

Flat rate data pricing – per month, per day

Fit for purpose internet devices

Faster data networks – HSDPA, 3G

Laptop & datacards
Mobile Office

Internet Partnerships:
- Yahoo!
- Nokia
- Google
- Flickr
- Facebook
- YouTube

Business data:
- Laptop & datacards
- Mobile Office
Successful partnerships will be critical

- **Mobile Search**
  - Enable customers to explore the Internet on their mobiles
  - Develop new revenues streams from search advertising
    - 5% of total UK advertising spend in 2010E (WPP)

- **Reach new segments**
  - Strong brands, good distribution, limited overlap with O2 base
    - 1.4m Tesco mobile subs, 1m Tchibo subs

- **User Generated Content**
  - Bring popular internet services and brands to mobile
  - Increased adoption and usage of mobile internet

- **iPhone**
  - Apple innovation coupled with O2 brand & customer experience
  - A market-changing proposition
  - Exclusive to O2 in UK

- **TheO2 & O2 World in Berlin**
  - Partnering with AEG
  - A range of benefits exclusive to O2 customers
  - Deliver a unique customer experience, differentiate our brand & drive loyalty
Broadband gives us a platform for integrated services ...

**Today:**
- Basic propositions
  - Mobile and discount broadband bundles
- Limited integration of fixed & mobile environments

**Tomorrow:**
- Country & segment specific propositions
  - Duo and Trio offers
  - VoIP, IPTV
  - Content management (Bluebook); music, pictures, messages

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**DSL Penetration of households**

- UK: ~30 p.p.

- 2006
- 2010E

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<table>
<thead>
<tr>
<th>UK</th>
<th>Germany</th>
</tr>
</thead>
<tbody>
<tr>
<td>2010E</td>
<td>2006</td>
</tr>
<tr>
<td>30%</td>
<td>30%</td>
</tr>
<tr>
<td>40%</td>
<td>40%</td>
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<td>70%</td>
<td>70%</td>
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<tr>
<td>80%</td>
<td>80%</td>
</tr>
</tbody>
</table>
02 ...cost control is critical to growing profitability

- **More Direct Sales**
  - Aim to increase proportion of direct sales from 40% to 80%
  
- **Re-engineer Distribution Channels**
  - Change the distribution model to achieve greater leverage over indirect channels & control SAC/SRC
  - Increased use of SIM only

- **Reduce Acquisitions & Retention Costs**
  - More immediate response to customers & lower cost to serve

- **Self Service**
  - Developing options for reducing network costs

- **Network Options**
  - Assessing potential for reducing number of data centres and common sourcing/development of infrastructure
  - Common IT architecture

- **Data Centre Consolidation**

- **Regional IS Sourcing**

- **Regional Software Factory**
Telefónica O2 Europe

1. A strong starting position

2. Opportunities for growth

3. Our strategy for continued outperformance
While keeping customers at the heart of everything we do
...with specific priorities for each of our businesses

1. Maintain growth / margin balance, increase market share
   - Potential for margin improvement

2. Continue to differentiate through Customer Experience

3. Re-engineer cost-base
   - Customer investment, Customer service

4. Invest in & exploit mobile Internet and DSL opportunity

5. Broaden product and service range
We are seeing increasing use of non-SMS...

**Consumer**
- O2 has ~ 36% of total non-SMS data users in the UK market*
- O2 Active users numbers growing 25% year on year
- Total data volumes up 1/3 year on year

**Business**
- Growth in BlackBerry
  - O2 to grow Blackberry Base by ~45% in 2007E
  - 1st to market with the Blackberry Pearl and Curve devices
  - UK Market leader for Blackberry Internet Service (~45% share)

**iPhone**
- 3 products in 1
  - A Revolutionary Mobile Phone
  - The best iPod – *Music on the Move*
  - The real internet – *the best mobile user interface*
- 3 postpay tariffs, with unlimited data
- Attracts high value customers in key target segments
- A market leading mobile data proposition

* Mobile Data Association
...our broadband proposition offers further growth opportunities

Targeting:
- > 1 million customers by 2010E
- CapEx < £100m 2007E – 2010E

Further opportunities:
- Wholesale
- Network sharing
- Traffic management, QoS
- Femtocells

Households with DSL

Source: Internal forecasts

Superfast up to 20 Mbps
Straightforward value for money (no catches)
Mobile email
Unlimited usage
Plug and play set-up experience
Single on-line user interface Offering a consistent 'look & feel' for all O2 services:
Broadband bluebook blueroom

O2 Broadband
UK based Care

Dec-06 Dec-10E

+8 m

Source: Internal forecasts
...O2 UK will continue to grow above the market...

- Market share gains driven by segment focus & base growth
- Focus on execution and customer experience
- Grow share of market revenue by focus on high value customers
  - Strong relative ARPU performance
- Bigger bundles drive increased MoU
- Maintain data ARPU above market average through growth of non-sms data
03 ...building on success to date

“Great value, no catch” propositions

Simplicity
- Offering a simple VFM alternative for customers not requiring a handset upgrade
- 30 day contract
- Reduces handset subsidy costs

Favourite Place
- Over 650,000 customers enrolled
- 25% increase in Top ups

Business customers
- Penetration of mobile email +30% so far this year
- New customer ARPU +9% year to date driven primarily by growth in mobile email
Cost control will also be a focus...

**Customer Investment Costs**

- Maximising Direct Infrastructure
- Efficiency in Indirect Channels
- Extending handset replacement Cycles
- Postpay SIM Only

Cost to connect

Three digit £ million saving by 2010E

Cost to serve

Three digit £ million saving by 2010E

Further opportunities for savings in IT / Network
...as well as growing new revenue streams...
...and continuing to put our customers and people first

Customer satisfaction Index

Source: TNS Customer Satisfaction Tracker
Specific priorities for...

1. Return to growth in mobile
2. Accelerate growth in O2 DSL and converged products
3. Continue growth in wholesale business (mobile and broadband)
4. Build future proof infrastructure
5. Deliver on re-structuring programme
Being part of Telefónica helps us capture the opportunities...

- **CapEx investment of ~€3,500 m 2007E-2010E to:**
  - Build out of high quality 2G network and reduce reliance on national roaming
  - Build out of high quality 3G/HSPA network to support mobile Internet and our proposition for businesses
  - Rollout of ULL network to support converged service

- **Why? Germany offers a significant opportunity:**
  - Population of 82m and GDP of €2,300bn
  - Lower penetration, lower mobile minutes of use, lower % of total minutes on mobile
  - Low DSL penetration

- **We will continue to grow our revenue and market share**

- **As part of Telefónica we benefit from**
  - Savings from procurement, devices, networks, etc.
  - Leveraging products and expertise across the group
  - Best practice
The mobile market will return to growth...

The market in Q2

- Mobile customer growth accelerating:
  - Total market gross adds +23%*
  - Penetration +9p.p.*
  - MoU +16%

- However, growth in the subscriber base has not offset price declines
  - Total Market Service Revenue: -3%

- DSL market continues to grow strongly
  - +4m lines year-on-year

The way forward

- We see the market returning to growth, as:
  - Price declines will slow down
  - Fixed/Mobile substitution will increase
  - Mobile data will start to gain traction

Note: *Company data, Q2 07 vs. Q2 06
Source: Pyramid Research, IDC, internal forecasts
03 O2 Germany will return to growth in mobile through...

**Introduction of S/M/L product portfolio**
- Introduction of S/M/L logic for entire product portfolio
- Genion XL flatrate
- Fair & transparent pricing scheme

**Genion S/M/L Customer Base development**

**Launch of FONIC – 2nd brand**
- Own discount brand launched
- Distribution via online and Lidl (+2,700 stores)
- One very simple voice & sms offer
- Lowest price offer in the German market with 9.9 cent/min.&SMS in all networks

**Growth of mobile Internet**
- Launch of S/M/L Data Packs
- Data ARPU growth driven mainly by non-sms data (mobile Internet)
  - New pricing introduced
  - +60% CAGR in mobile internet users by 2010E

**DATA ARPU**
- 2006: €5.70
- 2010E: ~50%
- 24% Non-SMS

CAGR 06-10E

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**Customer Base development** (000)

- Dec-06: 200
- Mar-07: 600
- Jul-07: 1,200
- Aug-07: 1,800

x5
...with improving metrics in Q2...

- Stronger L-mix within new Genion contracts
- Improved net adds Q2 07 vs. Q1 07
- Strong HanseNet performance

**Genion (S/M/L) minutes of use development**

**Genion (S/M/L) ARPU development**

- Genion S/M/L
- +40%
- Genion
- +10%
- Genion
The Broadband market offers significant growth.

**German DSL market growth** – approx. 8.5 m net additions expected 2007E-2010E with around 70% from ULL.

*Partly and fully unbundled not including T-Com Wholesale lines
Source: Internal forecasts

- Five players make up ~90% of the retail market: T-com, UI, HanseNet, Arcor & freenet.
**03 O2 broadband and FMC**

**Consumer Broadband**
- Competitive pricing of O₂ DSL with triple flat rate
- Easy installation
- One bill for broadband and mobile

**FMC Services**
- Launch of Communication Center with synchronisation of address book, emails and calendar
- Bundled offerings, e.g. family pack for O₂ DSL customers

**Business DSL**
- One stop: Broadband DSL, inter / intra company networking and mobile solutions
- ADSL2+ and SDSL broadband
Strong wholesale partnerships will support Germany’s growth story

- Primary ULL provider of all major alternative ISPs
- AOL/Alice launched
- First products with freenet launched
- United Internet ULL

- Tchibo gross adds growth accelerated
- 1 million customers

- Own discount brand launched
- Distribution via online and Lidl (+2,700 stores)
Building future proof network infrastructure is vital to deliver our growth ambitions

- **Continue roll-out of GSM network** to reduce dependency on National Roaming
- **Significantly improved network quality through reduction of handovers**

- **Continue roll-out of 3G network** – coverage, density and HSPA
- **Supporting mobile internet and data propositions and future converged propositions**
- **Ongoing evaluation of sharing / partnership opportunities**

- **Telefónica Deutschland** already the leading ULL wholesaler
- **Strong basis for O2’s DSL offer for consumer and business customers**
- **Key supplier of all large ISPs in Germany**
- **40% - 50% CAGR 2006 to 2010E in DSL lines**
Cost control will again be a focus...

- **Short term**
  - Achieve a 20% reduction in indirect costs
  - Manage cost in line with average for European benchmark

- **Mid term**
  - Manage cost in line with 1st quartile of European benchmark

**Phase 1**

- ~€70m reduction in indirect costs in 2007E

**Phase 2**

- >€100m reduction in indirect costs in 2008E
  - Additional €40m in 2007E through early implementation of 2008E measures

**Phase 3**

- Structural and process changes in IT, network, back office, admin
  - Drive further reduction of indirect costs

Reach 1st quartile of European Cost Benchmark
03 Specific priorities for...

1. Accelerate DSL uptake & slow down line loss
2. Develop IPTV and ICT businesses
3. Launch additional converged services
4. Build on success in Slovakia
5. Exploit mobile data opportunity
6. Continue to drive MoU through migration strategy
DSL will continue to drive growth in the fixed business...

- Negative revenue trend reversed in Q2 07 (+0.7%)
- Internet, IPTV and IT & Business Solutions the key drivers of growth
- Continue ADSL growth
  - Bundles support growth of DSL
  - Develop a strong position in IPTV
- Fixed line disconnections to improve significantly from 2006 peak of -519,000 net adds
- Develop a trusted, network centric ICT integrator position
  - DELTAX purchase
...and data driving the mobile business in Czech Republic

- **Mobile customers (in thousands)**
  - Dec-06: 4,864
  - Dec-10E: 50%
  - % Postpay: 39%

- **Data ARPU (in CZK)**
  - 2006: 108
  - 2010E: 55%
  - % Non SMS: 40%

- **MoU (minutes)**
  - 2006: 102
  - 2010E: 50%
  - +8%/+10%

- Revenues continue growing strongly
- Driven by customer base growth and ARPU
- Voice ARPU growth driven by migrations to contract (~50% of base in 2010E) and MoU increases
- Non-voice ARPU growth driven by non-SMS data
Highly successful launch
- 455,000 customers at end Q2 07

Market share of 8% after 5 months of operations
- Initial target of 5%
- Now targeting 14% - 17% by end 2010E

Continuing to build own network
- 500 base stations
- 34% population coverage
- Postpaid launch

Cumulative CapEx investment over 4 years expected to be CZK 4.5-7.2bn
### Investor Guidance...

<table>
<thead>
<tr>
<th></th>
<th>FY2006 (1)</th>
<th>FY2006 (Adj.) (2)</th>
<th>CAGR 06-10E (3)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>REVENUES</strong></td>
<td>2,148</td>
<td>2,148</td>
<td>+1%/+4%</td>
</tr>
<tr>
<td><strong>OIBDA</strong></td>
<td>985</td>
<td>994</td>
<td>+1%/+3%</td>
</tr>
<tr>
<td><strong>CAPEX</strong></td>
<td>229</td>
<td>229</td>
<td>1.0 - 1.4 bn Cum (07E-10E)</td>
</tr>
</tbody>
</table>

1. Base 2006 reported numbers include three months of start-up losses in Slovakia.
2. OIBDA excludes other exceptional revenues/expenses not foreseeable in 2007E-2010E. For comparison purposes the equivalent other exceptional revenues/expenses registered in 2006 are also deducted from reported figures.
3. CAGR 06-10E guidance assumes constant exchange rates as of 2006 and excludes changes in consolidation, other than Deltax.
03 O2 Ireland has delivered in a competitive market ...

**SUBSCRIBER BASE (in thousands)**

- 13.5% growth in PostPay base vs. 2006
- Broadband sales significantly exceeding target since launch in July – 14,000 to date

<table>
<thead>
<tr>
<th>Quarter</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Q2 06</td>
<td>1,599</td>
<td></td>
</tr>
<tr>
<td>Q2 07</td>
<td>1,631</td>
<td></td>
</tr>
</tbody>
</table>

**SERVICE REVENUE**

- Blended ARPU €46.7 (+2% y-o-y)
  - 10% premium over Vodafone on prepaid ARPU
- MoU 249 mins, up from 237 minutes last year (+5%)

<table>
<thead>
<tr>
<th>Quarter</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Q2 06</td>
<td>€227 m</td>
<td></td>
</tr>
<tr>
<td>Q2 07</td>
<td>€237 m</td>
<td></td>
</tr>
</tbody>
</table>
...with a focus on growth & cost control for the future

**Opportunities for growth**
- Growth in postpaid base and ARPU
- Leverage growth in SME/Corporate segment to capture fixed minutes
- Differentiate O2 brand through focus on customer loyalty & service
- Build on the successful launch of HSDPA Mobile Broadband and introduce additional Broadband value added services
  - fixed/mobile convergent services
- Moving pictures
  - successful DVB-H trials
- Maximise Mobile Search and Advertising opportunities

**Cost control**
- Technology & Network options
  - 15% - 30% targeted savings
- Maximise the use of Online and Direct Channels
## Investor Guidance...

<table>
<thead>
<tr>
<th>(€ in millions)</th>
<th>TELEFONICA O2 EUROPE</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>FY2006 (1)</td>
</tr>
<tr>
<td>REVENUES</td>
<td>13,159</td>
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<tr>
<td>OIBDA</td>
<td>3,708</td>
</tr>
<tr>
<td>CAPEX</td>
<td>2,553</td>
</tr>
</tbody>
</table>

1. Base 2006 reported numbers include eleven months of O2 Group (consolidated since February 2006) and three months of start-up losses in Slovakia.
2. In terms of guidance calculation, Airwave results are excluded from base 2006. OIBDA excludes other exceptional revenues/expenses not foreseeable in 2007E-2010E. For comparison purposes the equivalent other exceptional revenues/expenses registered in 2006 are also deducted from reported figures.
3. CAGR 06-10E guidance assumes constant exchange rates as of 2006 and excludes changes in consolidation, other than Deltax in the Czech Republic.
Our vision for 2010...

- Guidance achieved
- Increased our share of total communications spend across our combined markets
- An integrated business with major new revenue streams

Highly Efficient Business
- Best in class cost benchmarks
- Delivering full synergy and learning benefits from Telefónica

Fully Engaged Customers and Employees
- Highest customer satisfaction
- Top 5 employer
- Top 5 brand
Telefonica