



# FIFTH **INVESTOR** CONFERENCE

Valencia. May 25 th - 26 th. Ciudad de las Artes y las Ciencias

*Telefonica*

# The best combination of growth and returns in the industry

**César Alierta**

Chairman and CEO, Telefónica



Valencia - May 25, 2006



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- 01 Telefónica: a new and better company in a growth market
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- 01 Telefónica: a new and better company in a growth market
- 02 Our unique profile
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# 01 Since we met one year ago, Telefónica has become a new Company



We have been **proactive to acquire the best available growth platforms to achieve the right balance** by businesses and geographies **and to benefit from the full potential for economies of scale...**

**... to continue offering the best combination of growth and returns now and in the future**



**The integration** of Bellsouth Latam assets and Cesky Tel. has finished, and the take over of O2 and Colombia Tel. is being executed **at a record speed with no business disruption at all**

- **2004 and 2005 guidance fully delivered and even upgraded in a context of profit warnings in Telecoms**
- **Q1 results well in guidance 06**



Our new profile shows that **we have already achieved the appropriate scale and diversification.** Now, successful execution is even more important...

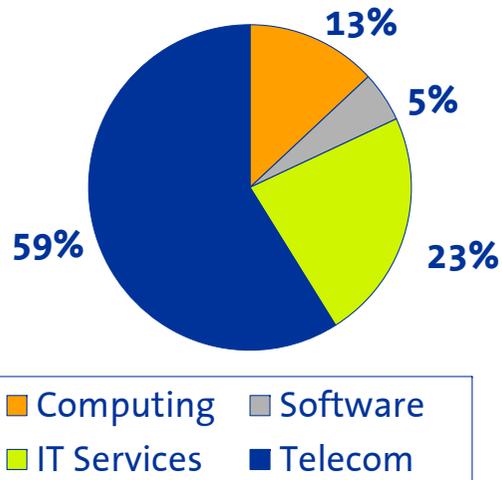
**... to extract value from scale and diversity through an integrated management of operations**



# 01 A new Company that will take the best from the very promising growth opportunities of the ICT industry

## 2005 Global ICT Market

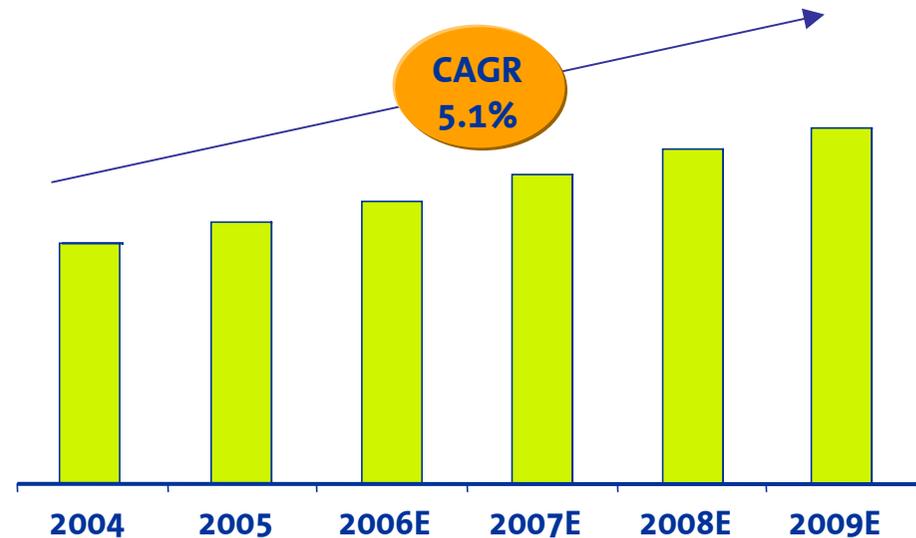
(US\$ Bn)



Source: Gartner, May 2006

## Total ICT Spending (2004-2009E)

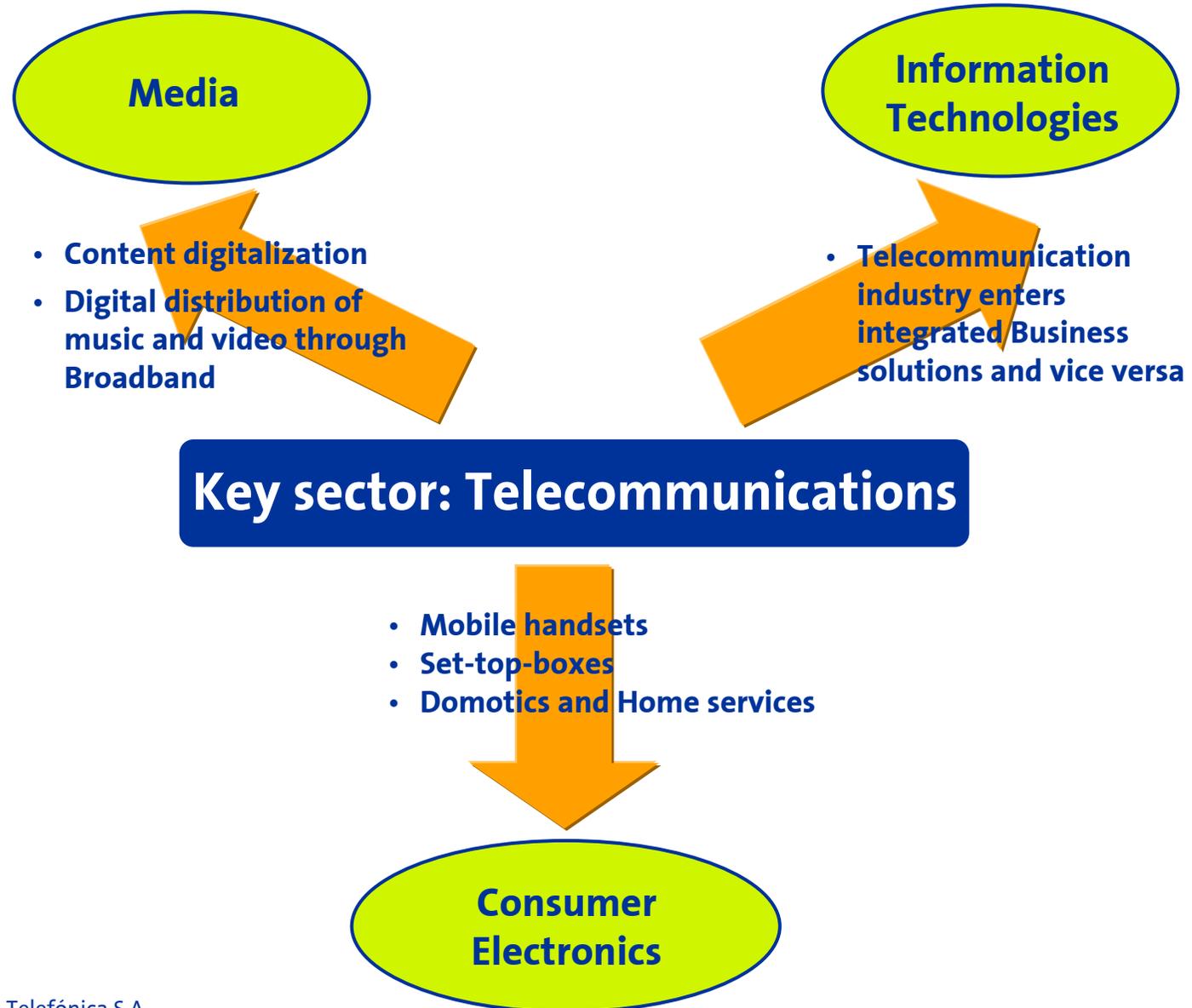
(US\$ Bn)



The sector is growing in size and economic impact, as ICT becomes an essential tool to enhance the competitiveness of the economy and to improve the standards of living



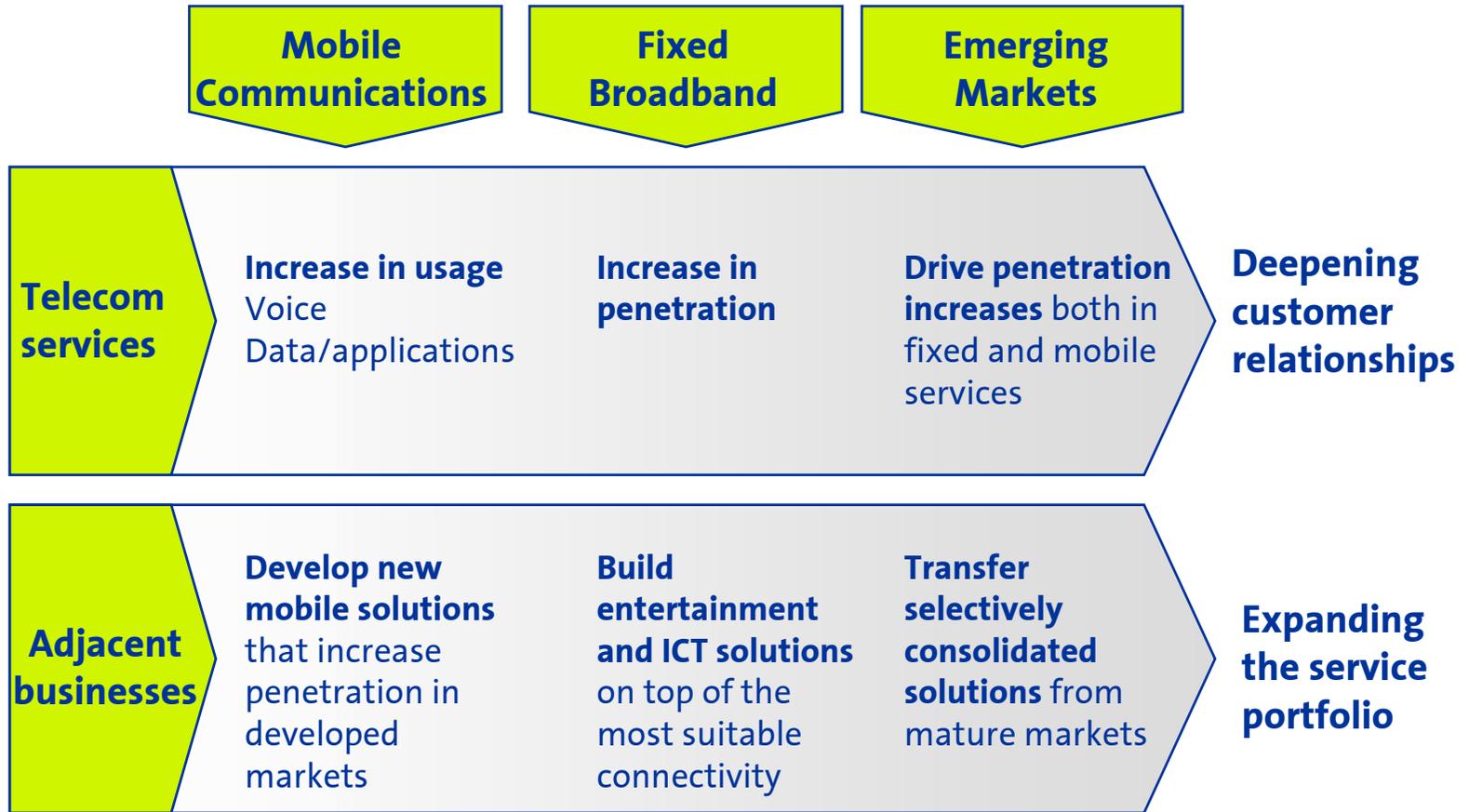
# 01 Telecoms, which are key to fuel the ICT expansion, will lead this growth to boost its revenues...





# 01

## ...leveraging on four key growth levers...



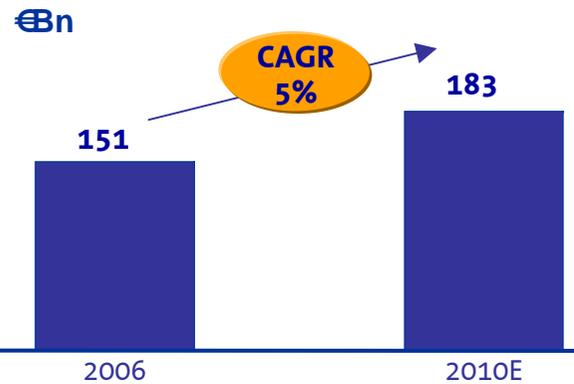
*These growth opportunities will be accelerated by a **growing demand for new “digital lifestyles” (at home and at work)**, and by the increasingly important role of telecommunications in society*



# 01 ... offering a large potential in the coming years

## Mobile communications

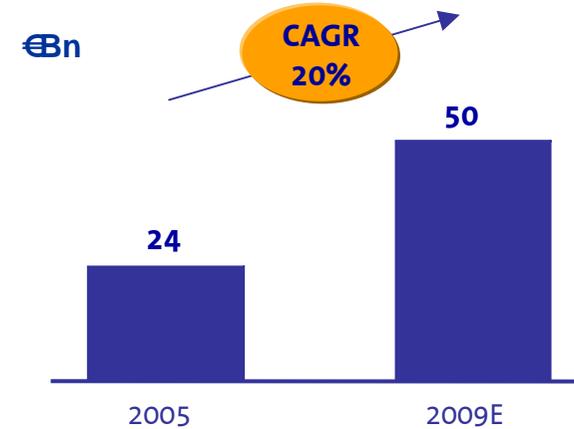
Estimated mobile revenues in Western Europe  
(2006-2010E)



Source: Gartner Datarequest, March 2006.

## Fixed Broadband communications

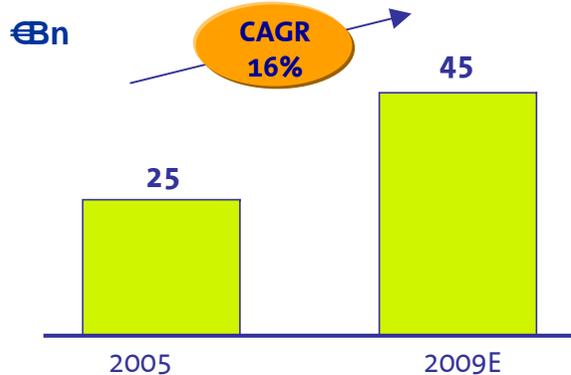
Estimated BB revenues in Europe  
(2005-2009E)



Source: Yankee Group, December 2005

## Opportunities in emerging markets

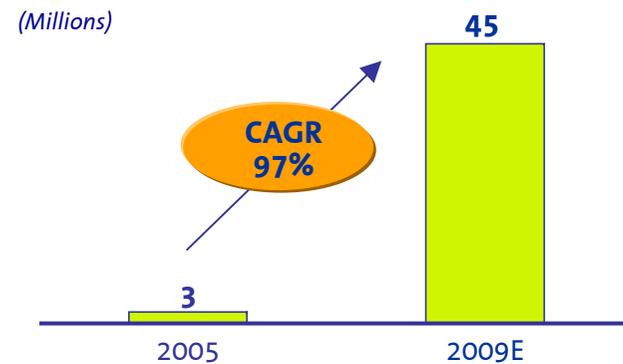
Estimated mobile revenues in LATAM  
(2005-2009E)



Source: Ovum, September 2005. Includes voice and data (Exchange rate: 1,2\$/€)

## Development of adjacent businesses

Estimated global IPTV users (2005-2009E)



Source: IDC, 2005



# 01 But only those companies adapted to sector trends will fully exploit these opportunities

## Major industry trends

**Globalization**

**Competition that fosters market dynamism**

**Convergence**

## Winners will be companies having...

### Regional scale

- Global communities of clients
- Regional leadership
- Global brands

### Local commercial strength

- Close to customers
- Differentiated positioning

### Operating efficiency

- Competitive margins

### Innovation

- Source of sustainable differentiation

### Adaptability

- Capacity to anticipate value migrations or extensions between sectors
- Ability to adapt to changes on technologies, business models and regulatory environments



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01 Telefónica: a new and better company in a growth market

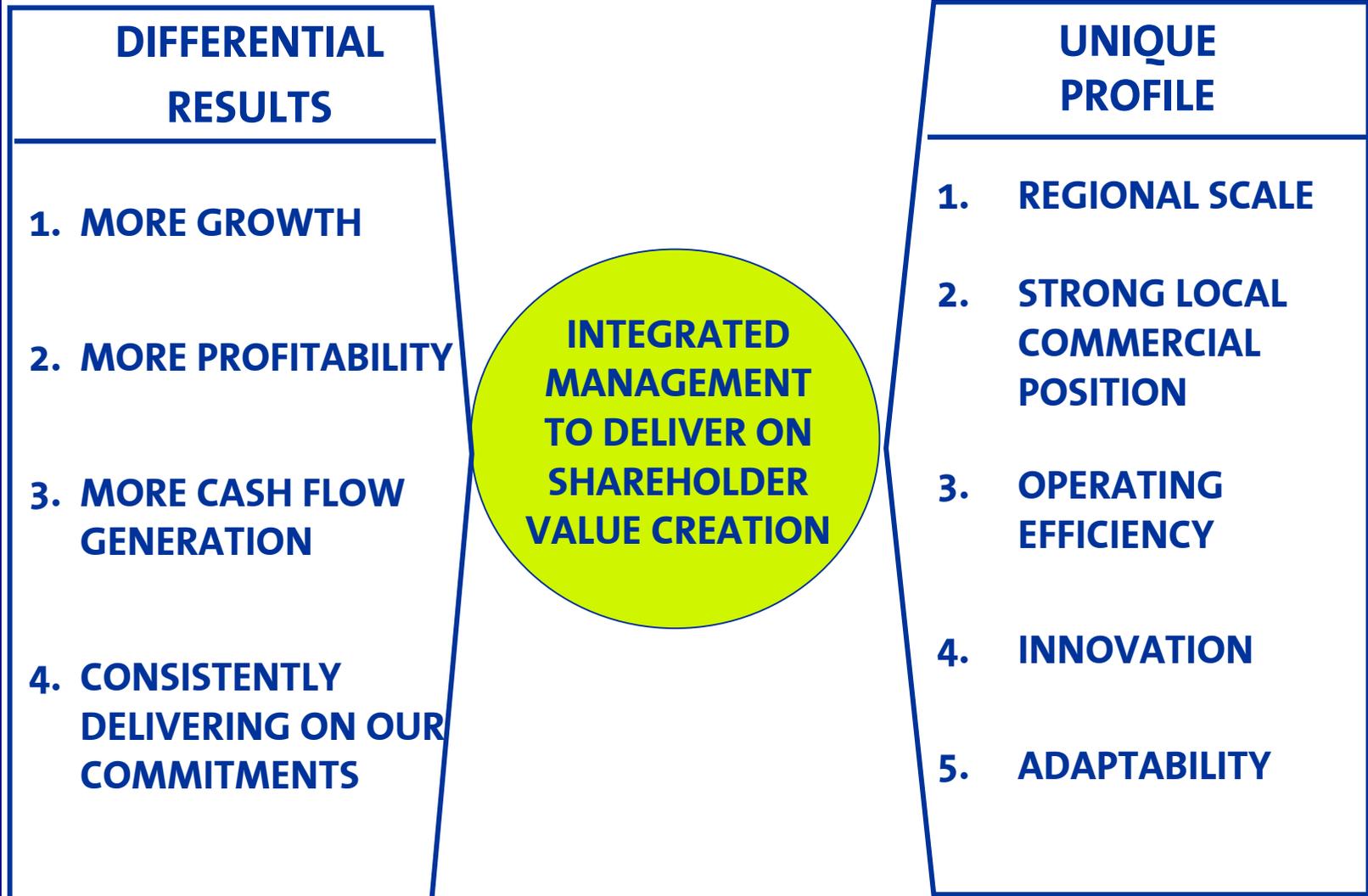
02 Our unique profile

03 Our strategic guidelines to lead the sector's evolution

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## 02 We have achieved differentiated results thanks to a unique profile in our industry





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## 02 Our results top the best performances in the sector in terms of growth at the operating level,

### ■ Revenuë growth<sup>(1)</sup>

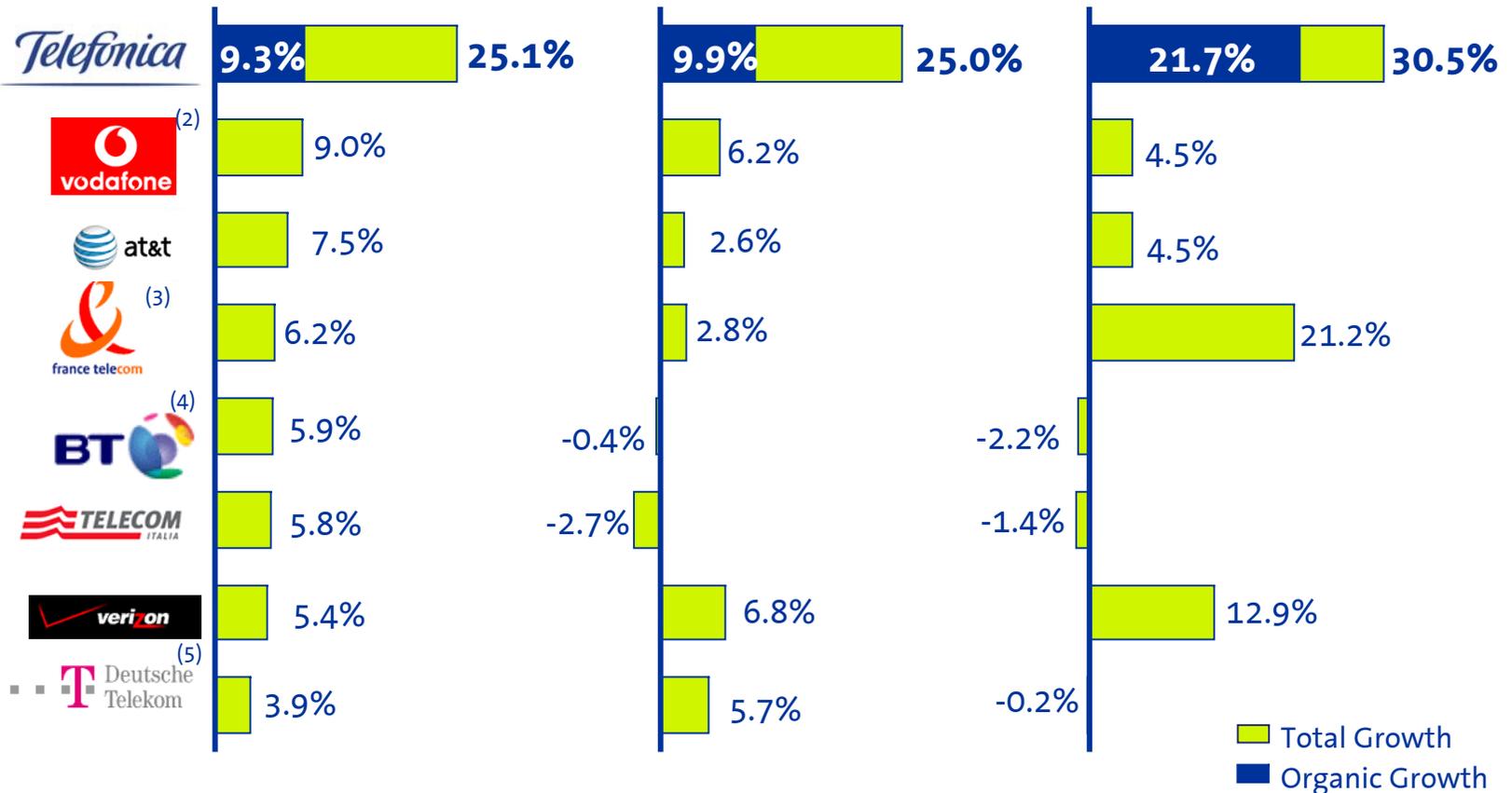
2005 vs. 2004

### ■ OIBDA growth<sup>(1)</sup>

2005 vs. 2004

### ■ OI growth<sup>(1)</sup>

2005 vs. 2004



(1) Based on information published by the companies

(2) Results for the six months to 30 September 2005. Adjusted EBIT.

(3) EBITDA = gross operating margin defined as revenues less supplies, operating expenses (net of operating results) and wages and salaries, excluding pension plans and stock options.

(4) Results for the twelve months to 31 March 2006. Adjusted EBITDA and EBIT.

(5) Adjusted EBITDA and EBIT.

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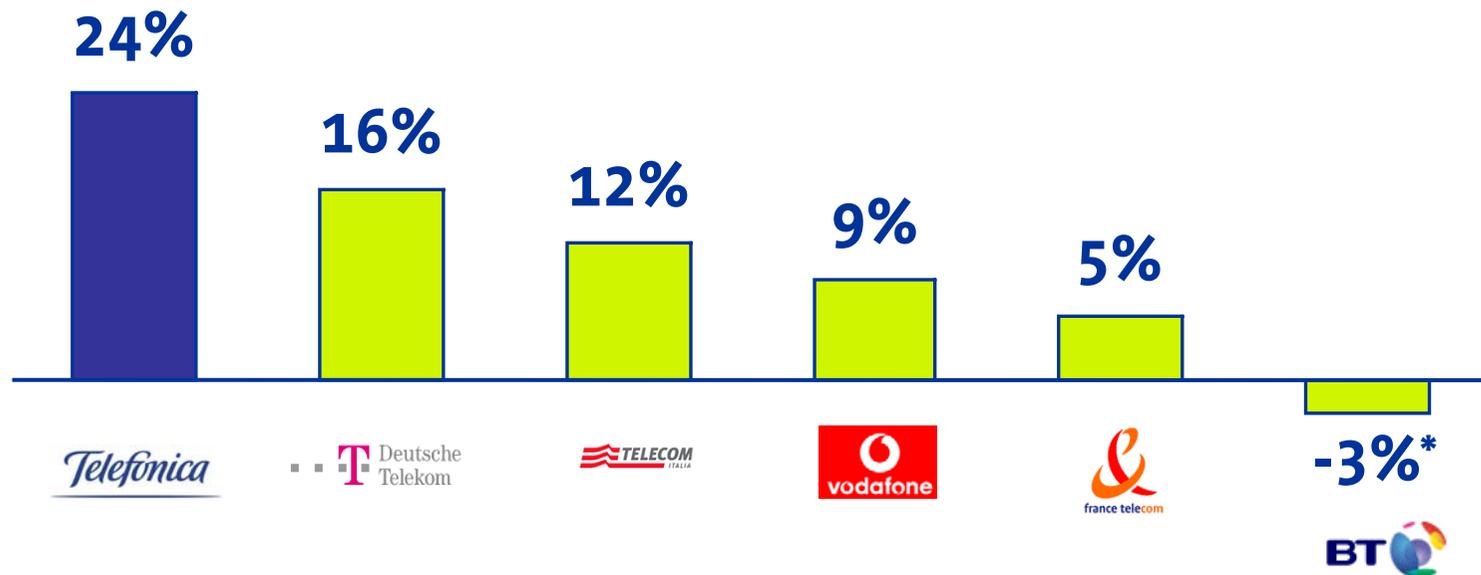
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## 02 ... in terms of earnings momentum ...



### Adjusted EPS Growth

2005/2004



Adjusted EPS: excluding extraordinary results before goodwill and adjusting deferred taxes. Fully diluted.  
Source: SG, Telecom Weekly, (4th of May).

\*Data as of 2006E



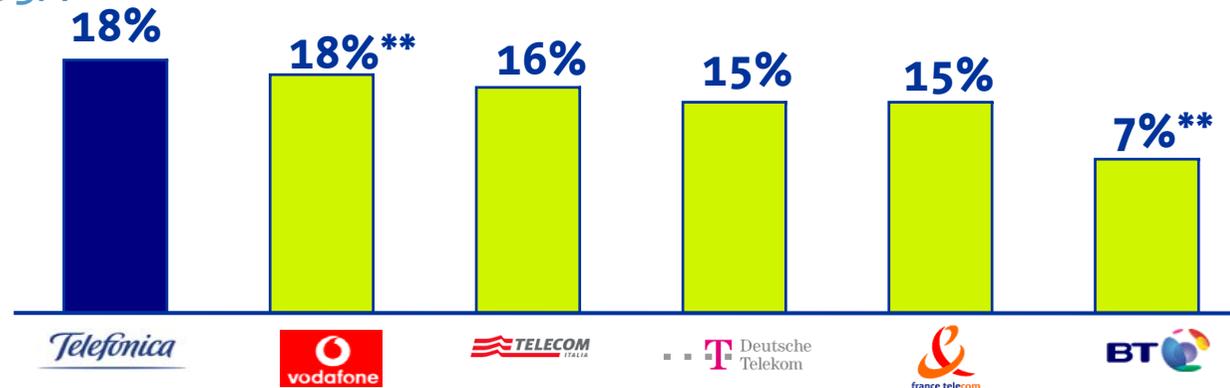
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# 02 ...and in terms of Cash Generation, as the basis of our shareholder remuneration policy



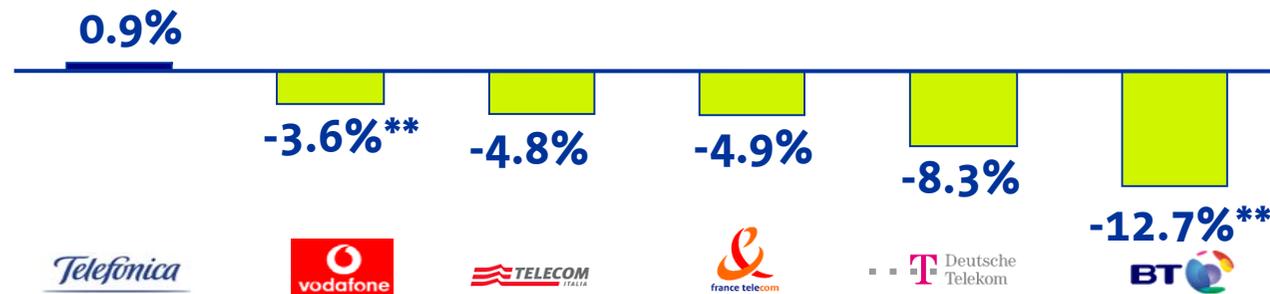
## Free Cash Flow\* as % of revenues

2005A



## FCF\* Growth

2005/2004



Source: Merrill Lynch "European Telecoms Valuation Monitor (Mar'06)

\*FCF: EBITDA-CapEx-Interest expenses- Taxes-Working Capital-Dividend to minorities-Others

\*\*Data as of 2006E

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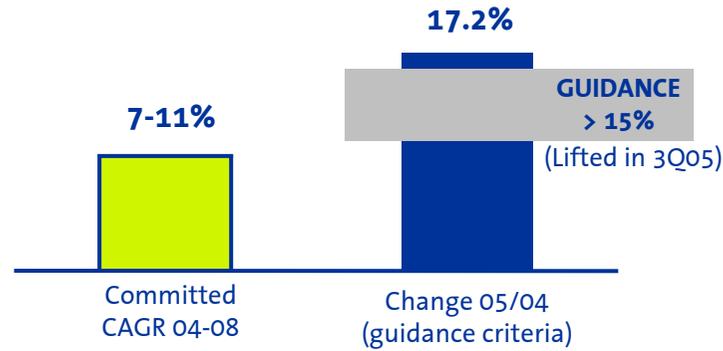
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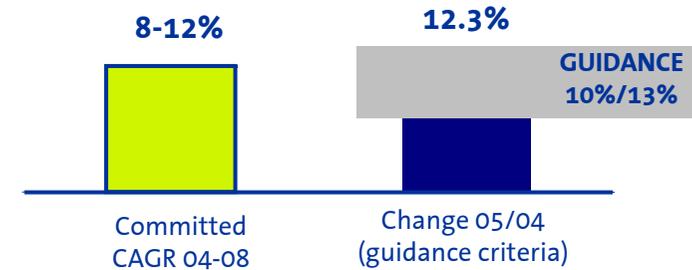
## 02 We consistently deliver on our commitments



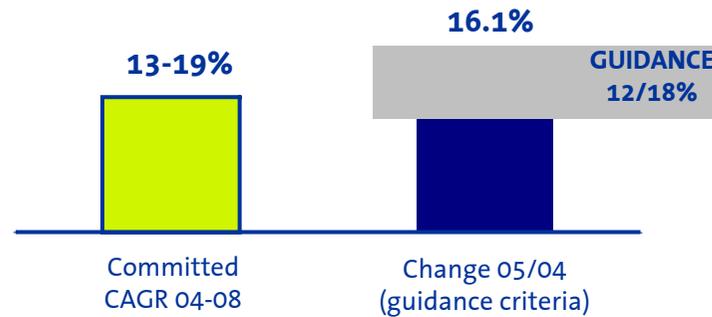
### Revenue growth\* ✓



### OIBDA growth\* ✓



### OI growth\* ✓



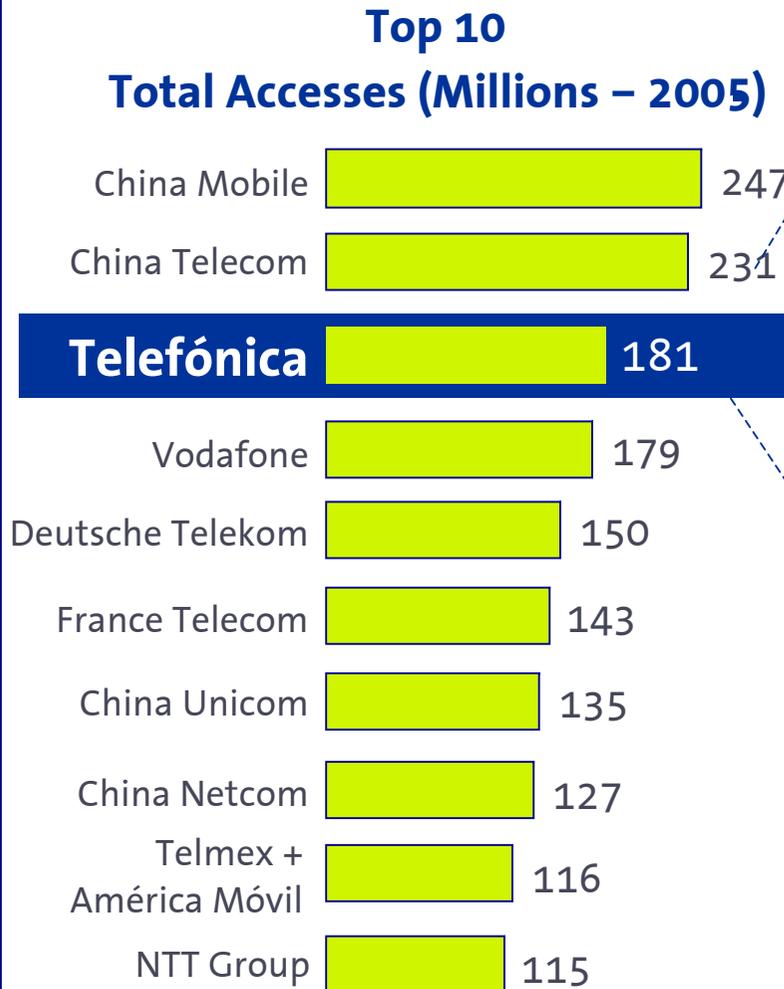
\*Constant exchange rates as of 2004.

Barcelona committed CAGR 04-08 calculated under Spanish GAAP.

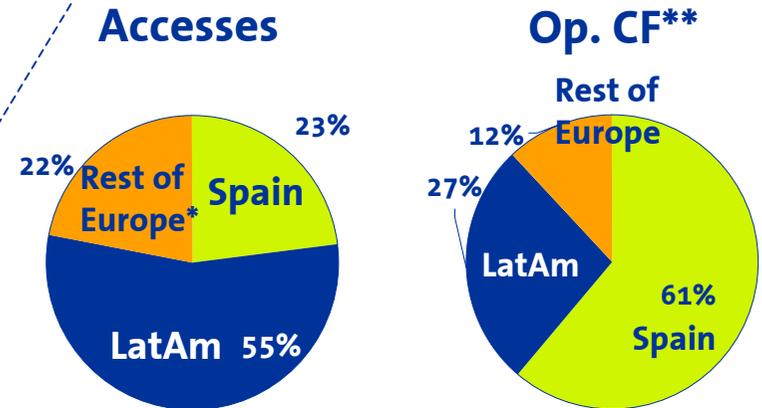


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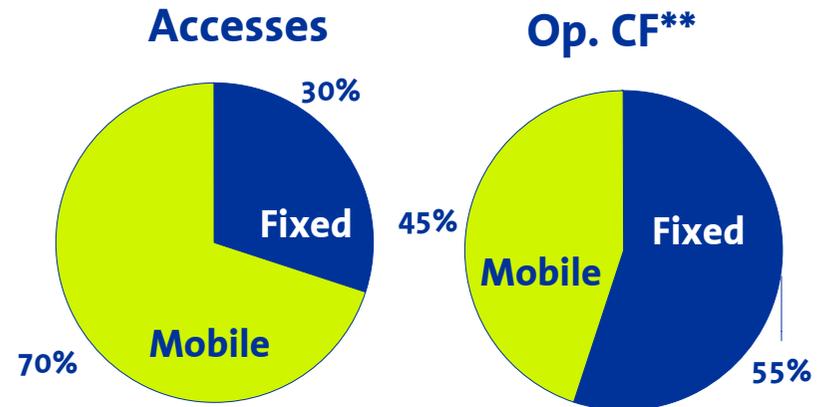
# 02 Our unique profile: Benefiting from regional scale...



## GEOGRAPHICALLY DIVERSIFIED



## BUSINESS DIVERSIFIED\*\*\*



Note: 2005PF: Full year Cesky and O2 included.

\* Includes Morocco

\*\* Op. CF = OIBDA – Capex Avg Exchg Rate.

\*\*\* Fixed includes Narrowband, BB and Pay-TV

Total Accesses based on information published by the companies. Fixed lines+Mobile subscribers+NarrowBand&BB+PayTV





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# 02 ... that we actively manage



## The value of being part of Telefónica

(Illustrative)

OIBDA growth(%)

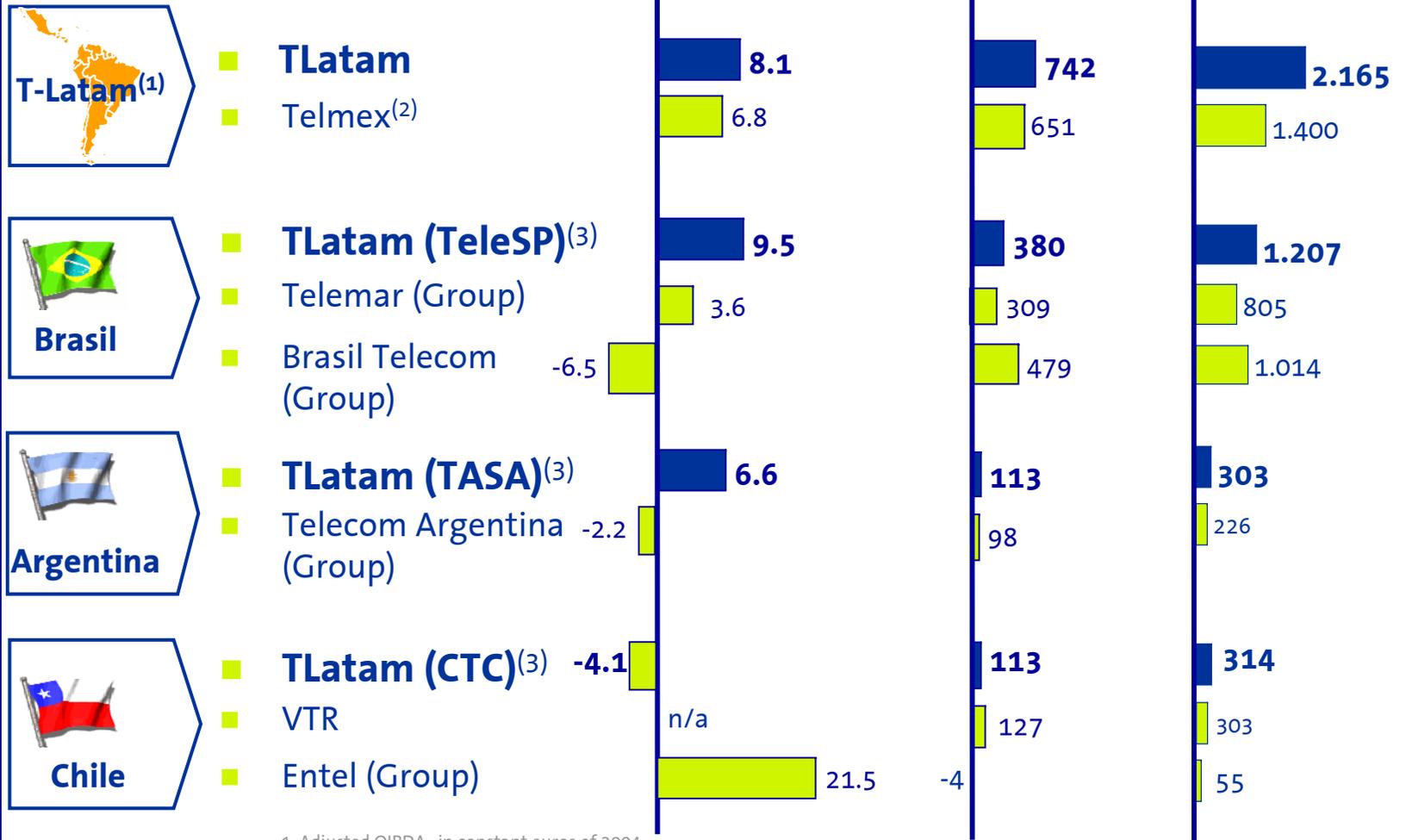
2005 vs. 2004

Net DSL  
accesses<sup>4</sup>

2005 A ('000)

Tot. DSL  
accesses<sup>4</sup>

2005 A ('000)



1. Adjusted OIBDA in constant euros of 2004.

2. Includes Net Brazil.

3. Reported OIBDA in local currency.

4. Wholesale and retail DSLs included. TRR not included.

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## 02 Our unique profile: Local commercial strength



### Leadership and control of customer interface:

#### ■ Connectivity

- High knowledge of our customers' profile

#### ■ Customer care and Billing

- 5 M daily contacts (globally)

#### ■ Commercial network and branding

- Strong brand recognition and consistent leadership in individual markets
- >65,000 points of sale worldwide

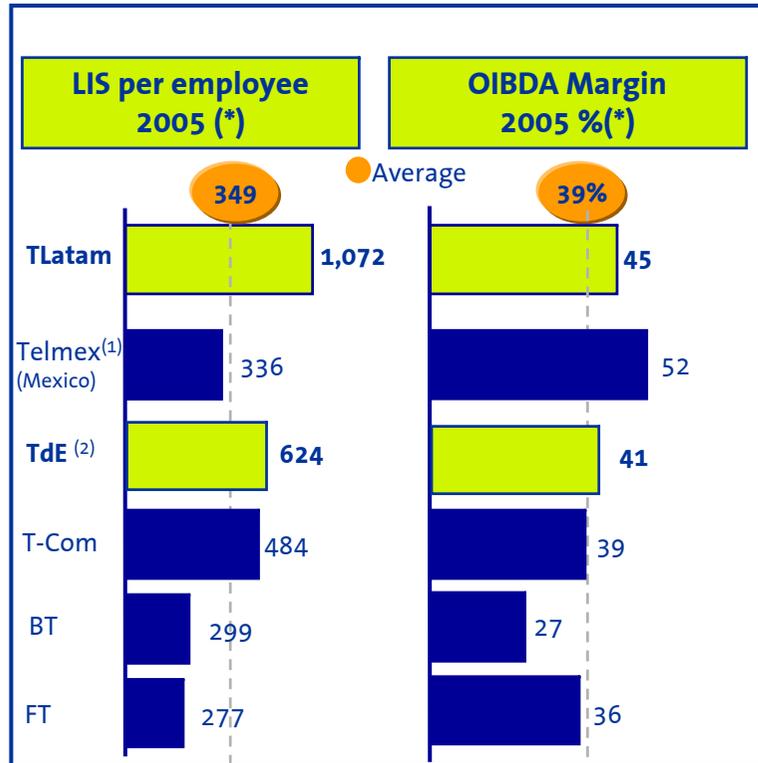


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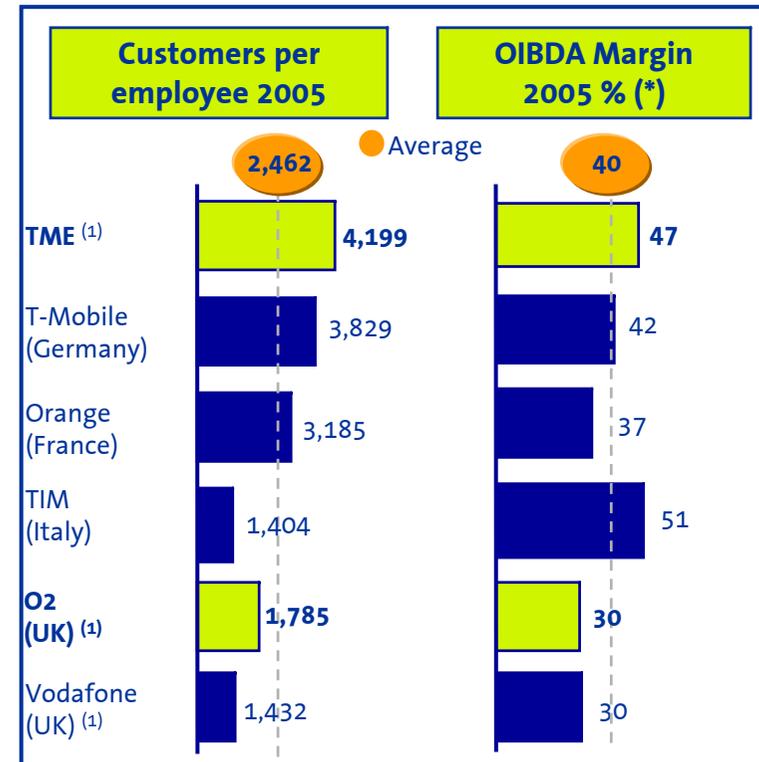
# 02 Our unique profile: Operating efficiency



## Best in class Fixed ...



## ...and Mobile Telecom



**We have begun the chase for efficiency before our competitors that still have to**

Source: Morgan Stanley, May'06.  
(\*) Including PSTN and ADSL 2005  
(1) Employees as of 2004, published by the company  
(2) TdE Group  
Note: Average excludes TdE and Tlatam

Information published by the companies as of 2005.  
Note: Average excludes TdE and Tlatam

Source: Morgan Stanley, May'06  
(1) Information published by the companies as of 2005.  
Note: Average excludes TME and O2

Information published by the companies as of 2005.  
Note: Average excludes TME and O2



## 02 Our unique profile: Innovation for a distinctive competitive position



**imagenio** »



- Launch in 2003 as a pioneering IPTV service in Europe
- First replicated in early 2006. Still unique VoD feature in ADSL market
- >200,000 customers in Dec'05

**O<sub>2</sub> Genion**



- First in Europe, launched in 1999
- First replicated in late 2005
- 3.5M customers in Germany in 2005



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# 02 Our unique profile: Adaptability



## We've done the major restructuring this industry needs

Transforming our asset base

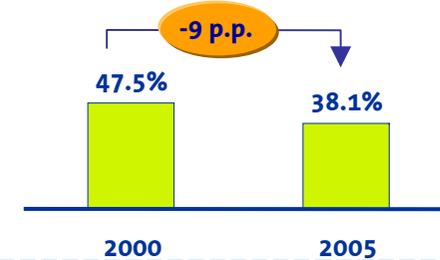
Fixed assets\* / Total accesses (€)

\* Net of amortization



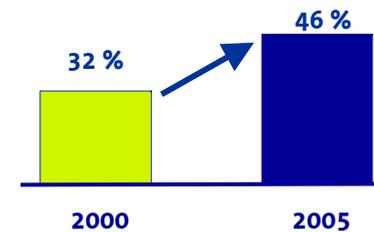
Transforming our cost structure

Fixed Costs vs. Total Costs



Strengthening our commercial focus

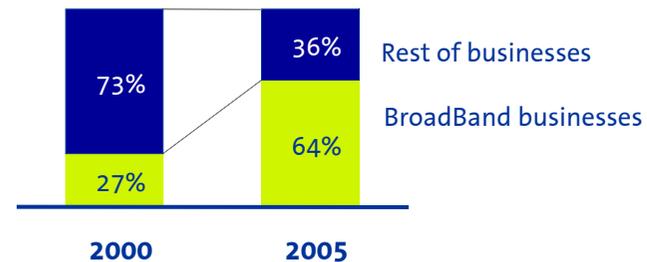
Commercial expenses as % of total Expenses\*\*



\*\*Total expenses excluding supplies, variation in allowances for bad debts and operating taxes. TdE, TLatam and TEM considered

Focusing on investments for growth

Capex mix



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## 02 In summary, we have achieved differential results thanks to a unique profile in our industry

### DIFFERENTIAL RESULTS

1. Highest organic growth in the European industry...
2. ...with earnings well above the market, growing by 24%...
3. ...supported by a strong cash flow generation of 18% over revenues with positive growth...
4. ...allowing us to consistently deliver on our commitments

### INTEGRATED MANAGEMENT TO DELIVER ON SHAREHOLDER VALUE CREATION

### UNIQUE PROFILE

1. A balanced portfolio of over 180 M accesses,...
2. ...with a #1/#2 position supported by strong capabilities and assets...
3. ...and high OIBDA margins based on the lowest rates of LIS/ customers per employee...
4. ...pioneering in the launching of new P&S like Imagenio or Genion...
5. ...while adapting ourselves through a more flexible and dynamic structure



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## 03 Our Vision

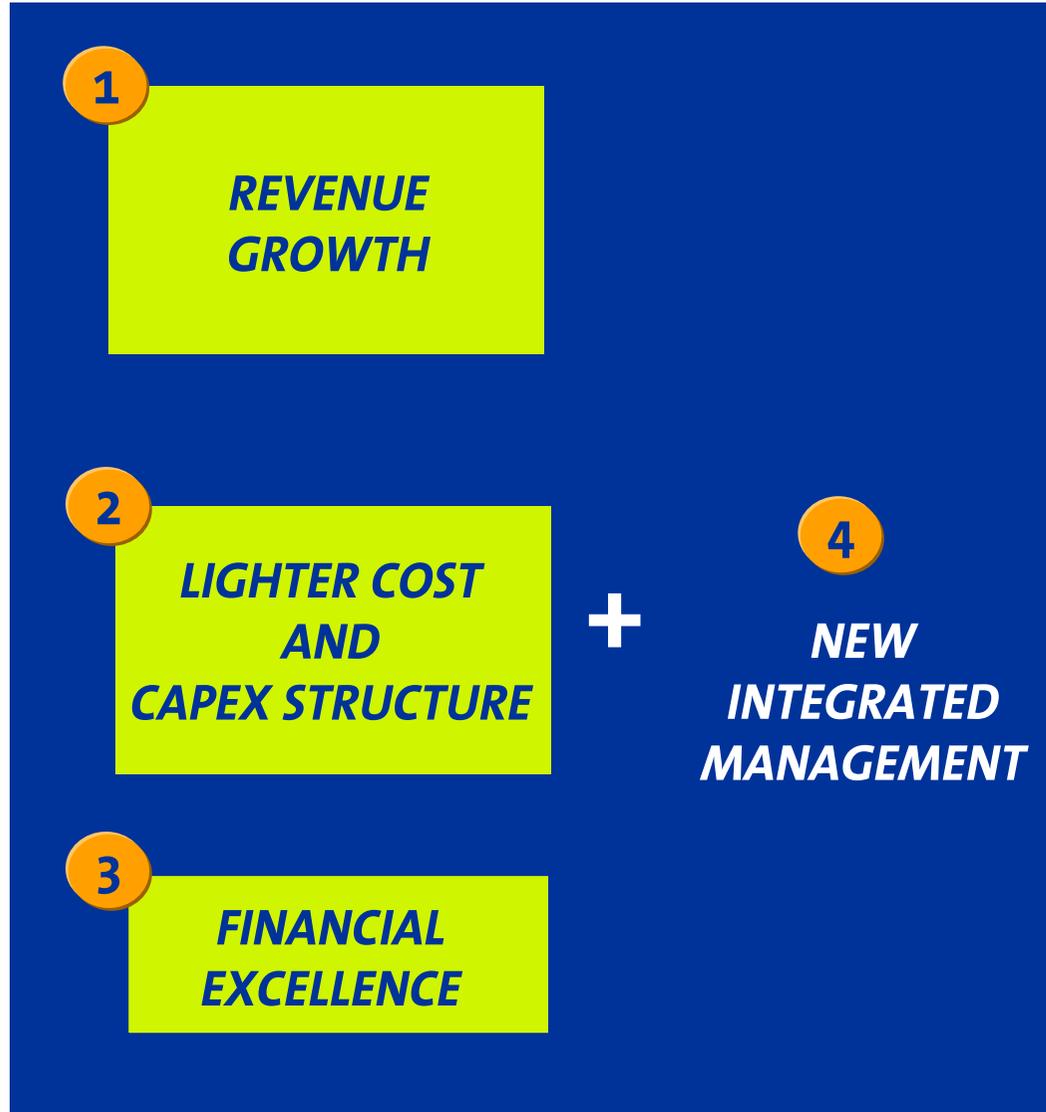
***Telefónica: the most competitive, customer oriented, solutions driven, integrated IP Company, with a clear goal...***

***... to deliver the best combination of growth and returns in the industry to our shareholders***

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# 03 Our strategic focus will be developed through four major objectives



- **Better Results**
- **Growing EPS**



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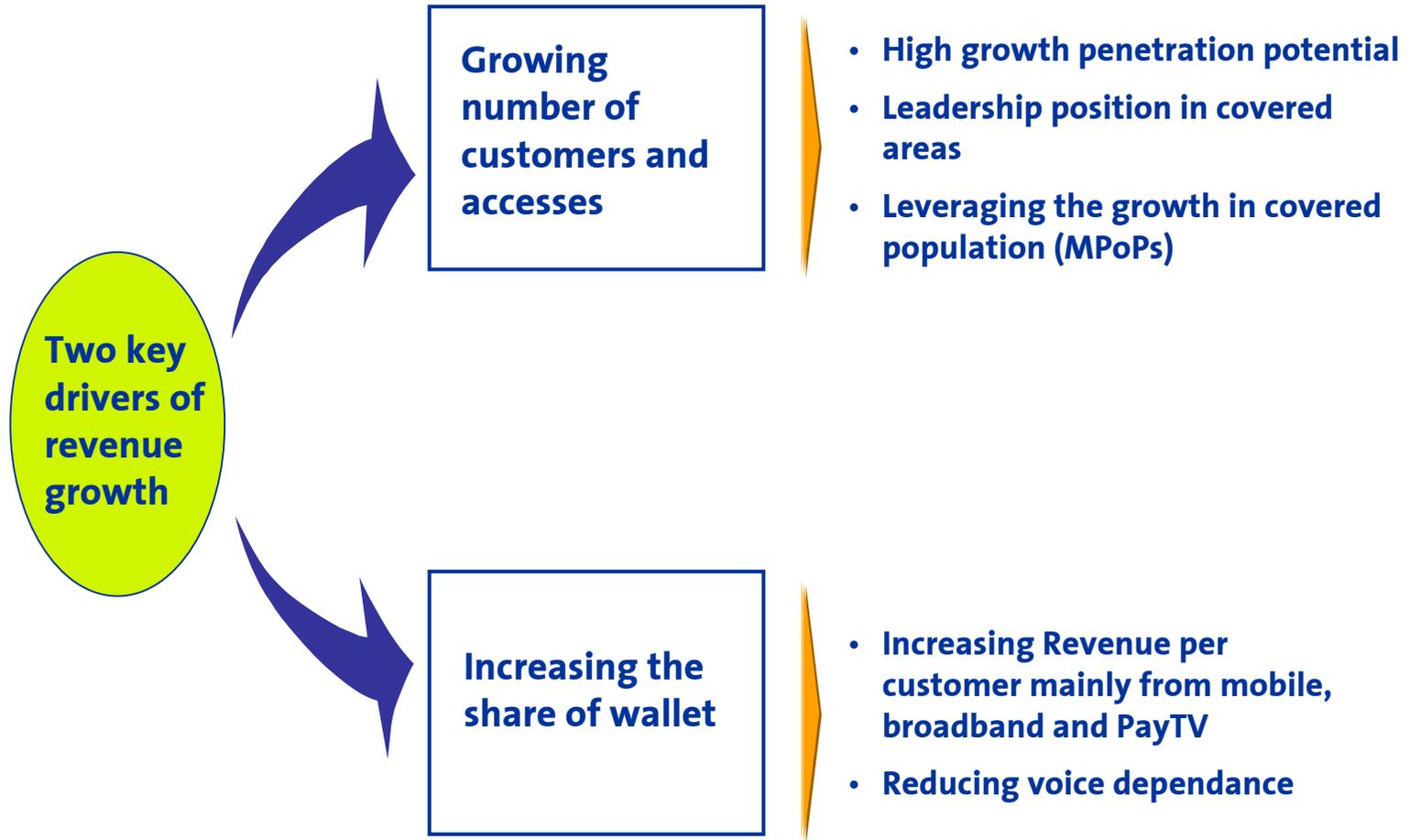
## 03 Our differentiated top line growth well ahead of peers is driven by

1

- Unique high growth Latam businesses
- O2 differential growth momentum in Europe
- Superior revenue growth of Spanish assets within the European market
- Český Telecom full integration as a new opportunity
- Ongoing revenue upside from new businesses
- Additional revenue enhancement from integrated mgmt.



# 03 Increasing our customer base and our revenues per customer will be the key drivers of revenue growth





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# 03 Leading us to manage a growing number of customers and services in a larger potential market...

1

## High Growth Penetration potential

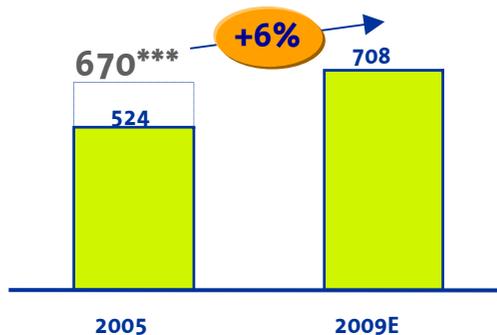
Penetration Inc. 05-09E*	Fixed BB	Mobile
Spain	<b>+22pp</b>	<b>+11pp</b>
Rest of Europe*	<b>+21pp</b>	<b>+12pp</b>
Latam (e.g. Brazil)	<b>+8pp</b>	<b>+33pp</b>

+

## Leadership in covered areas

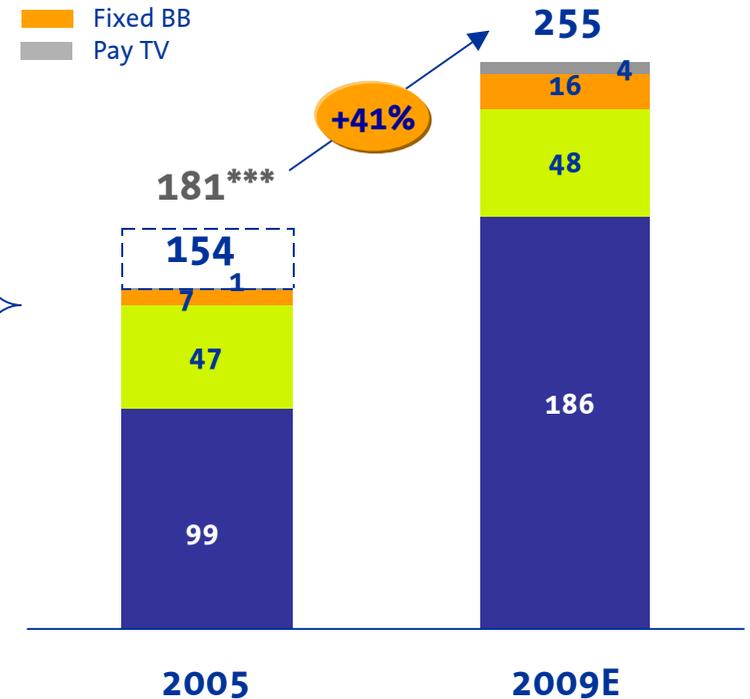
+

## Covered Population Growth (MPoPs)



## Number of Accesses (M)

- Mobile
- Fixed \*\*
- Fixed BB
- Pay TV



\* Sources: Yankee Group, Ovum and Pyramid. Rest of Europe: UK, Germany and Czech Republic

\*\* Includes narrowband, leased circuits and leased local loops

\*\*\* Including O2



## 03 ... and to increase total Revenues per customer...

1

- **Increasing revenue per customer** while strongly accelerating the growth of our access base

- **Delighting our customers with innovative proposals** of integrated solutions for communication, information and entertainment



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# 03 A clear set of management actions to continue growing our top line...

1

## Customers

Multi business customer insight

Integrated channel management

Refreshed and segmented brand strategy

## Innovation

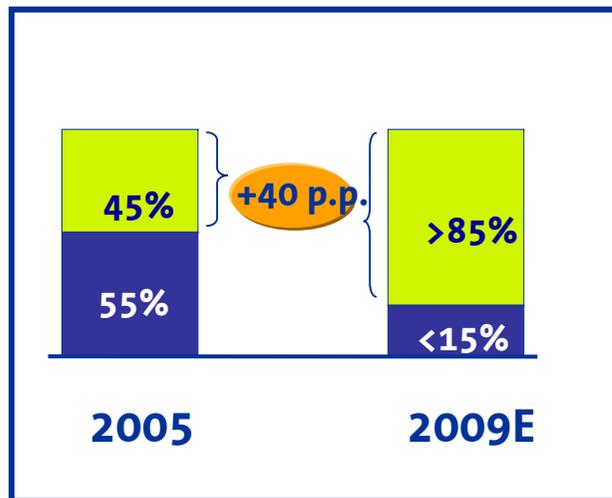
New portfolio of P&S:  
Convergent Services, New Internet-based business models,  
Personal TV services

Top-notch content offer



# 03 ... while evolving the revenue business model...

## REVENUE MIX EVOLUTION



- Data, Broadband and other Revenues, including bundled minutes
- Outgoing Traditional Voice traffic Revenues

- Our dependence of traditional voice will be reduced by 40 p.p. during the period 2005-2009E
- Voice will increasingly be sold in flat rates and bundles with other services, as a component of complete solutions for our customers' needs
- Data revenues will be our main growth source in the period



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# 03 ... and keep on transforming our cost and CapEx structure

2

A very Efficient Operating model

## PRODUCTIVITY INCREASE

Network operating cost per Access  
Total 05-09 Change



## CAPEX CONTROL

CapEx to revenues



Economic benefits from an **integrated broadband all-IP-based network and NGA...**

... reinforced by a **common vision and evolution of our IT systems...**

... and an **integrated procurement model** to maximize savings in the purchase area



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## 03 Financial discipline is a key element of our management strategy

3

**De-leveraging  
to re-build  
financial  
strength**

### COMMITMENTS

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- BBB+/Baa1 as rating floor
- Net debt + commitments below 2.5x OIBDA in the medium term, as of 1Q06 is 2.8x OIBDA

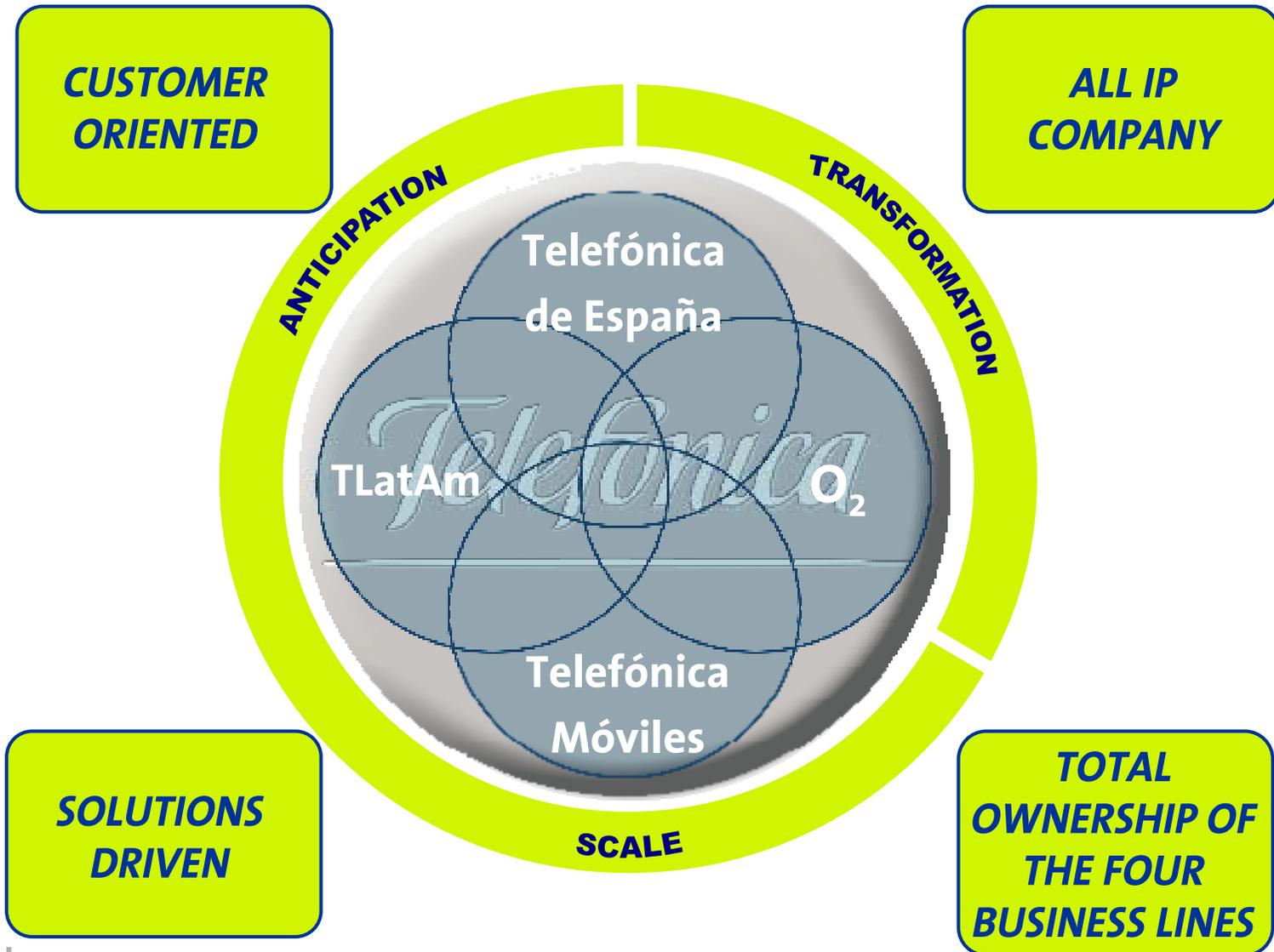


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# 03 New integrated management of our businesses will allow us to extract additional value

4





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# 03 Telefónica delivers results through focused individual businesses and integrated relationships 4

## MANAGEMENT PROGRAM



**INTEGRATION**

**Integrated relationships among businesses**  
Julio Linares  
“Extracting the value of a new integrated management”

Extract the maximum value from our scale and diversity

**Financial discipline well preserved**  
Santiago Fdez. Valbuena  
“Value addition by cost subtraction”

**EXECUTION**

Focus on delivering growth and results

**MAXIMIZE VALUE CREATION FOR OUR SHAREHOLDERS**





## 03 Telefonica as a new and better Company: a new and unique profile to capture the very promising growth opportunities

- Enhanced growth prospects, well ahead of peers
- Well-balanced by business and geographies
- Enormous potential to extract value from scale and diversity through a new integrated management
- Financial discipline well preserved
- Growth to fully flow to investors



**Superior proposition to  
Shareholders**

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