



FIFTH **INVESTOR** CONFERENCE

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

Telefonica

Leading a world of broadband solutions

Luis Lada

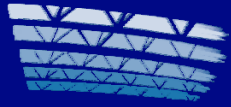
Executive Chairman, Telefónica de España



THE BEST COMBINATION OF
GROWTH AND RETURNS

Telefonica

Valencia - May 25, 2006



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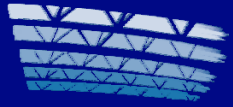
Content

01 During 2005 we continued to deliver top results while strengthening capabilities for future sustainability

02 Going forward we will leverage our competitive advantages to grow even further

- Positive socioeconomic landscape
- Sustainable growth based on a distinctive offering
- Higher efficiency levels
- Thoughtful investments to support future growth

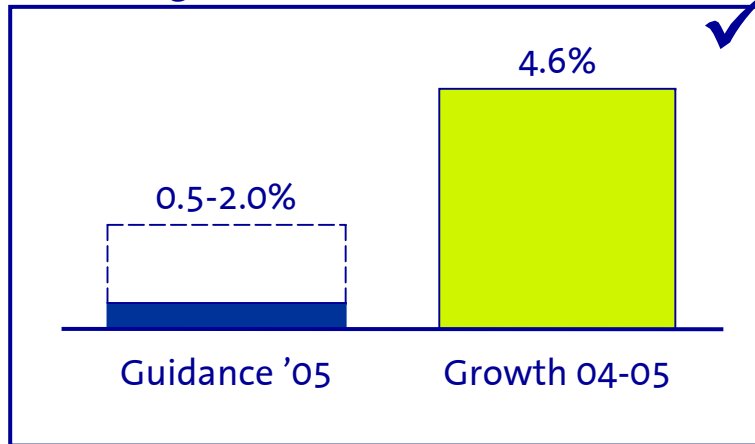
03 As a result, we commit to ambitious financial and operational targets



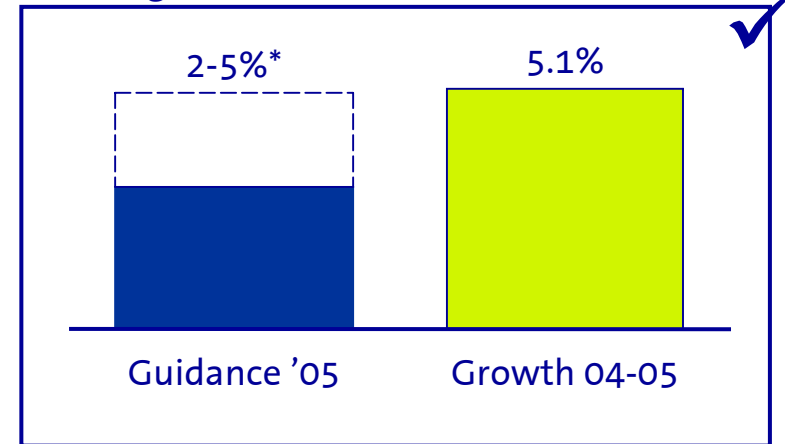
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01 Once again, we have delivered strong financial results and met or even exceeded our targets

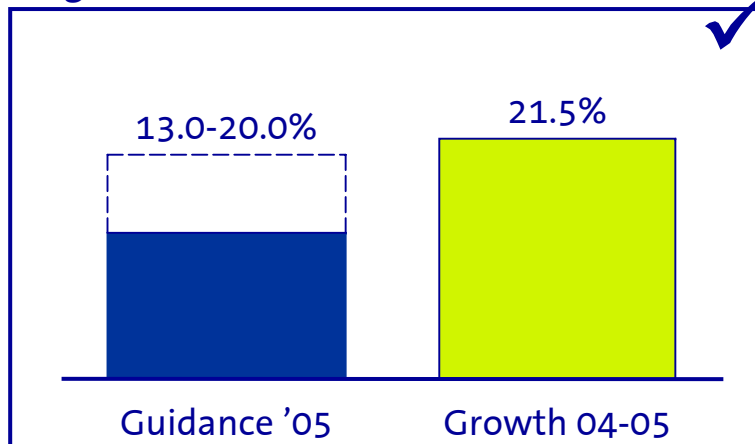
Revenue* growth



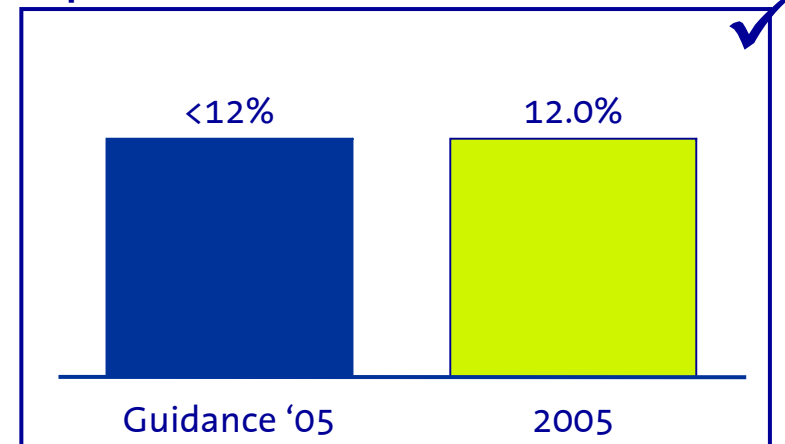
OIBDA* growth



OI* growth



Capex/revenues**



Note: Financial Data for TdE Group (including associates and excluding Terra)

* Foreseeable Revenue, OIBDA and OI. Figures reported for 2005 are: +4,8% Revenues growth, +4,5% OIBDA growth and +19,9% OI growth.

** CAPEX/Revenues ratio for TdE (not including associates) was 12,4%

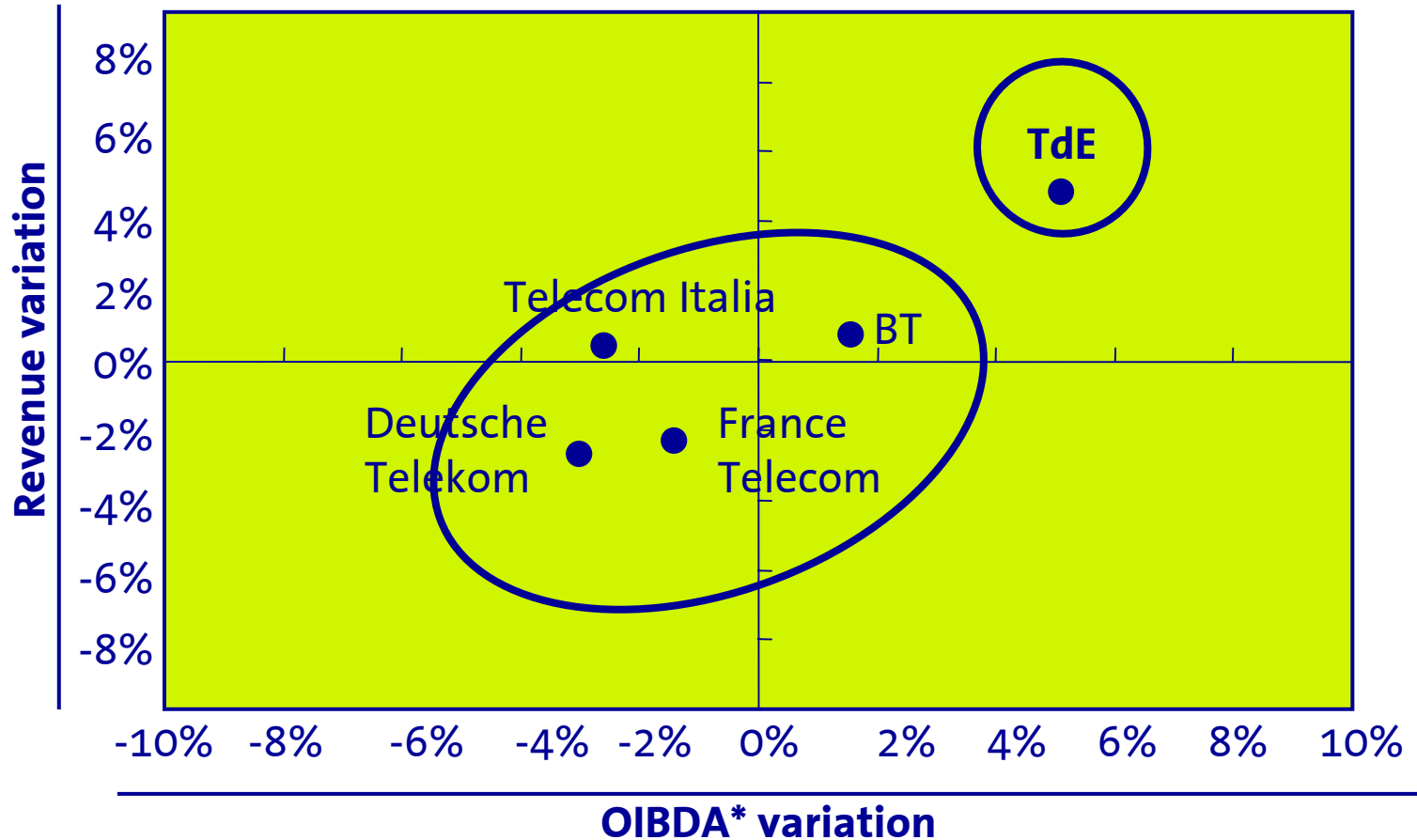
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01 We are one of the top incumbents in terms of revenue and profitability growth

Fixed business, 2005



* OIBDA for TdE, EBITDA for the other companies

Source: Companies reports (FT: revenues and GOM for HCS+ECS; TI: revenues and EBITDA for domestic wireline; DT: revenues and adjusted EBITDA for Broadband/Fixedline + Business Customers; BT: revenues and EBITDA for BT Retail + BT Wholesale April05/March 06)

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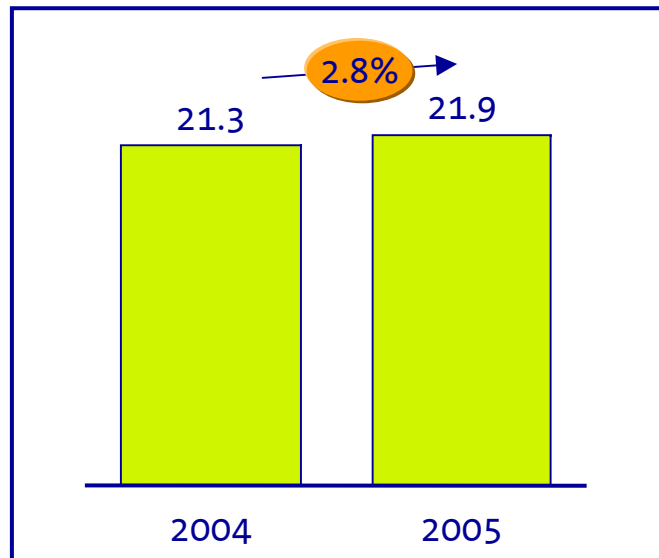
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01 These results were possible due to excellent operational performance (1/2)

Access growth

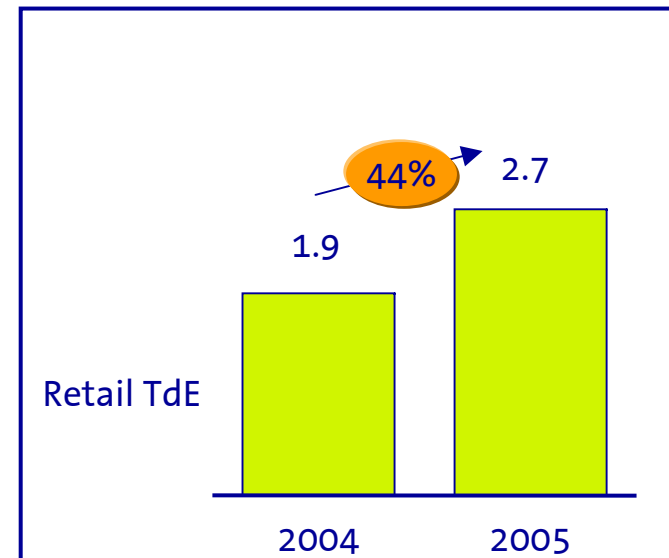
Total access growth*

Million



Internet broadband access growth**

Million



Broadband is the key contributor to access growth boosted mainly by the growth in bundles

* Includes basic accesses, narrowband Internet, broadband Internet, ULL and IPTV

** Excluding fully unbundled local loop, Wholesale and cable modem. Retail includes Terra and ISP friendly

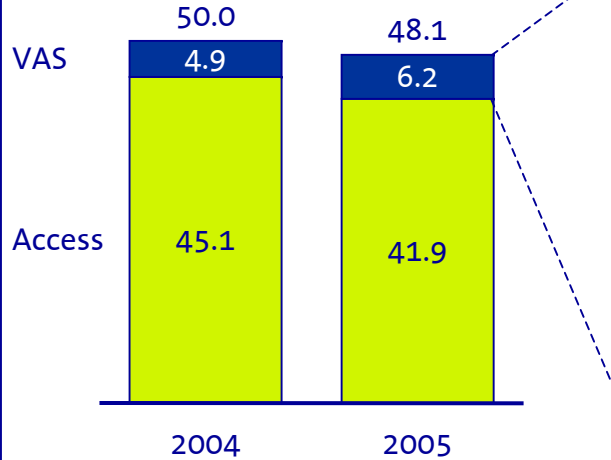


01 These results were possible due to excellent operational performance (2/2)

Broadband ARPU, bundles and “flat-fees”

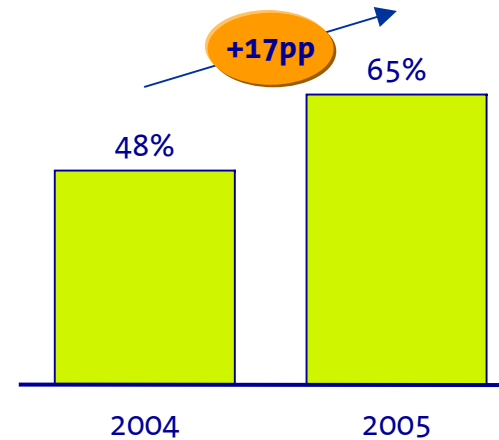
Broadband ARPU

EUR/month



VAS penetration over DSL

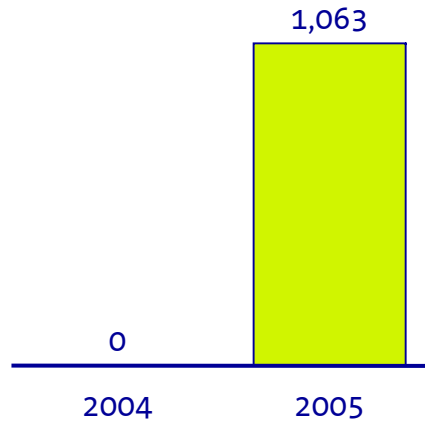
(%)



VAS ARPU increase has been critical to minimize overall ARPU reduction for broadband services

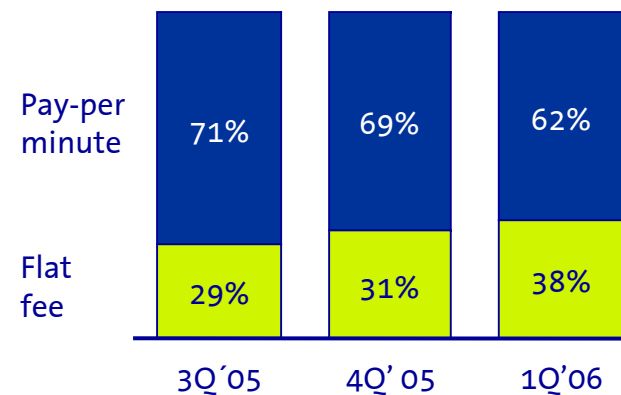
Duo and Trio subscribers

Thousand

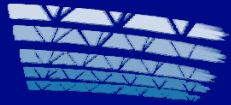


Voice traffic

Minute split, %



The increasing importance of bundling and “flat-fees” reduces the relevance of voice traffic as a key issue as it has been proven after the launch of Duos and Trios (sep05)



01 We are confident about our future revenue and return growth prospects

Customer perception improvement

- Telefonica has been valued by the Spanish Consumers Association as the fixed telco operator with the best quality/price ratio*

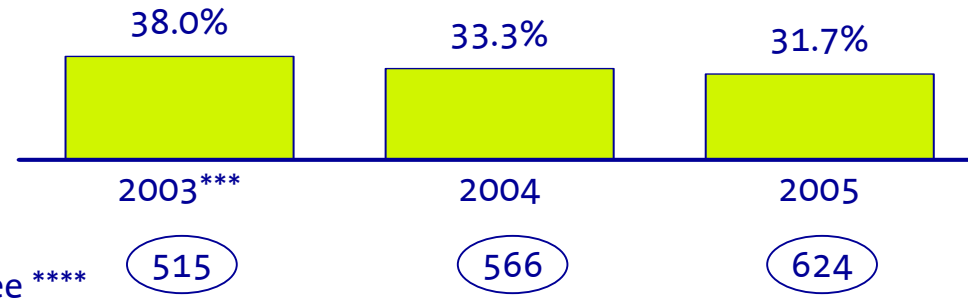
Strong P/S innovation

- Our positioning in broadband stresses service value, not only speed
- In households:
 - We are spearhead in video on-demand and many other interactive TV services
 - Flat-fee high-quality services embedded in bundles (Duo, Trio and fixed-mobile) have deactivated VoIP threat
- In businesses we have designed a broad new range of business solutions (e.g. design of new national ID)

Efficient and flexible cost base

Personnel costs/Operating costs**

Percentage



* According to a study released in January 2006 by Unión de Consumidores Españoles
 ** Excluding ERE provisions
 *** Prior to IFRS adoption
 **** Parent Company.



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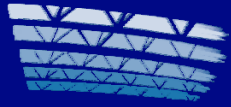
01 During 2005 we continued to deliver top results while strengthening capabilities for future sustainability

02 **Going forward we will leverage our competitive advantages to grow even further**

■ **Positive socioeconomic landscape**

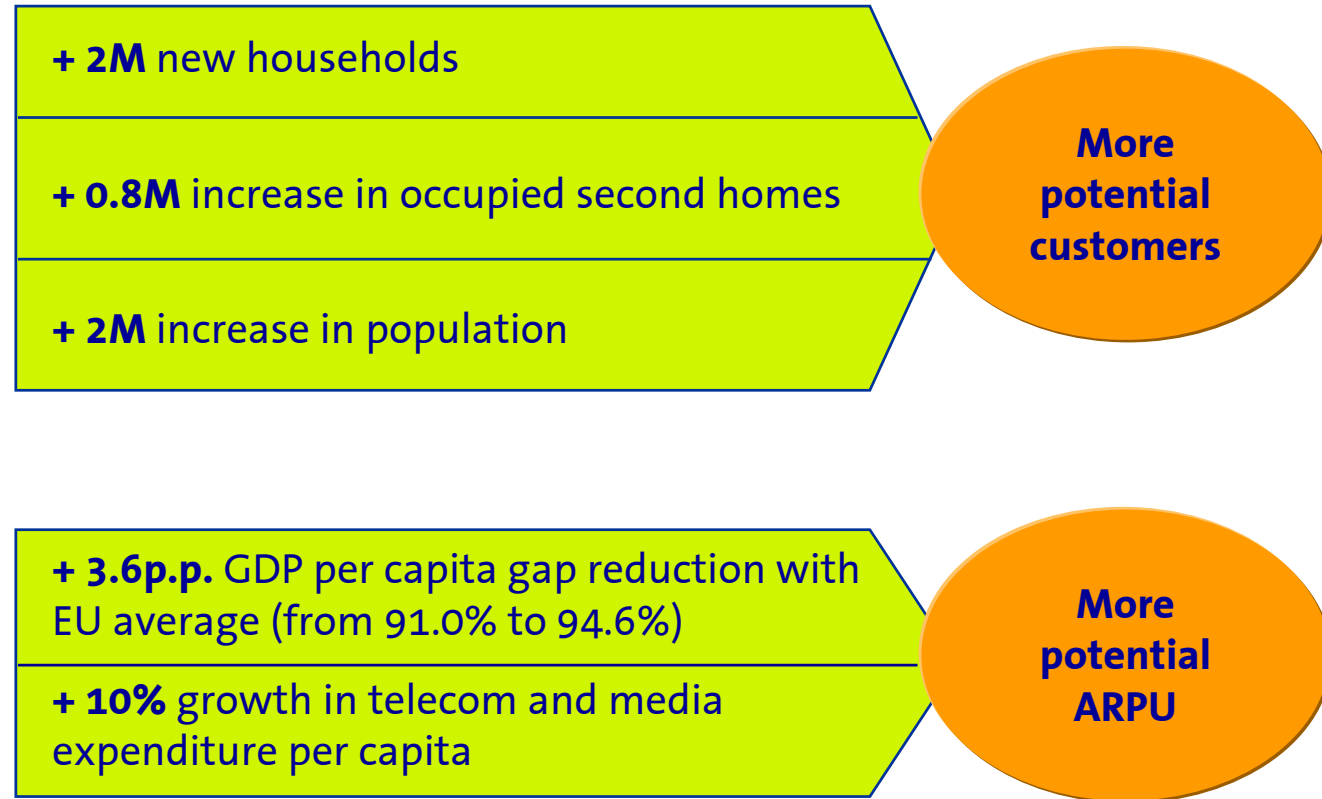
- Sustainable growth based on a distinctive offering
- Higher efficiency levels
- Thoughtful investments to support future growth

03 As a result, we commit to ambitious financial and operational targets



02 The Spanish positive socioeconomic outlook will support telecom sector growth

Spain figures, 2005-2009

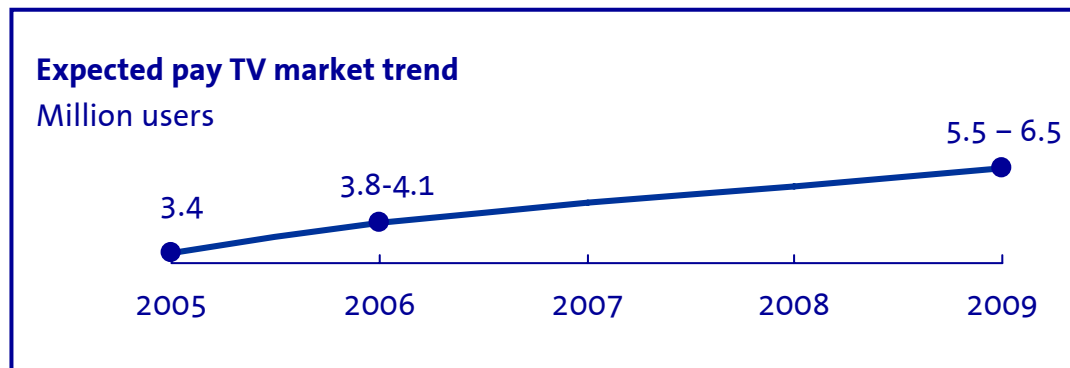
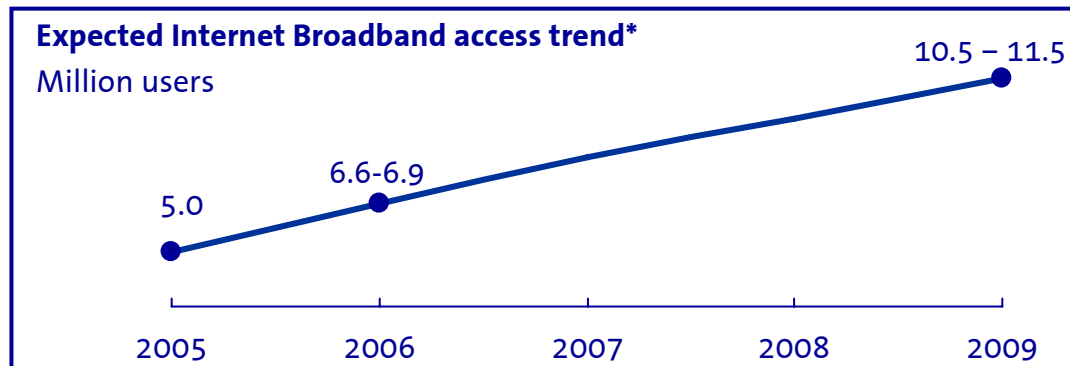
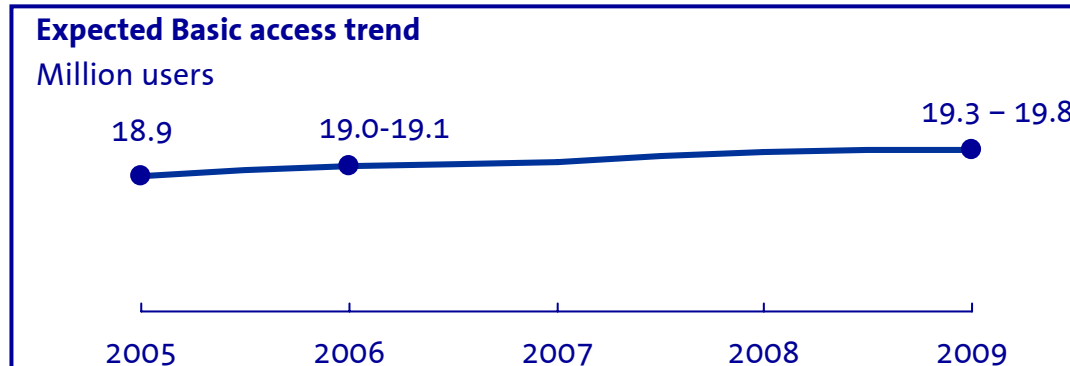


Source: Global Insight World Market Monitor, Yankee Group, Pyramid Research, IDC, PwC



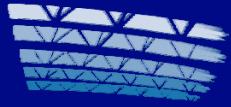
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02 And a solid, upward evolution of our key market indicators can be forecasted



Broadband adoption and services offered over a broadband connection will still be the key growth driver for the future

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02 Regulatory framework will be in line with EU guidelines

Retail regulations

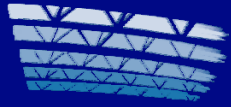
- End of price regulation except for accesses (CPI-x, +2% in 2007)
- Bundle authorisation will be based on replicability and the existence of related wholesale services in all cases

Wholesale regulations

- Need to offer wholesale services (bitstream, ATM, IP) that allow replication of all broadband and voice offers
- Voice traffic interconnection price asymmetry

Universal service

- New universal service regulation starting January 2008
- New services will not be affected by universal service rules (eg. Broadband)



Content

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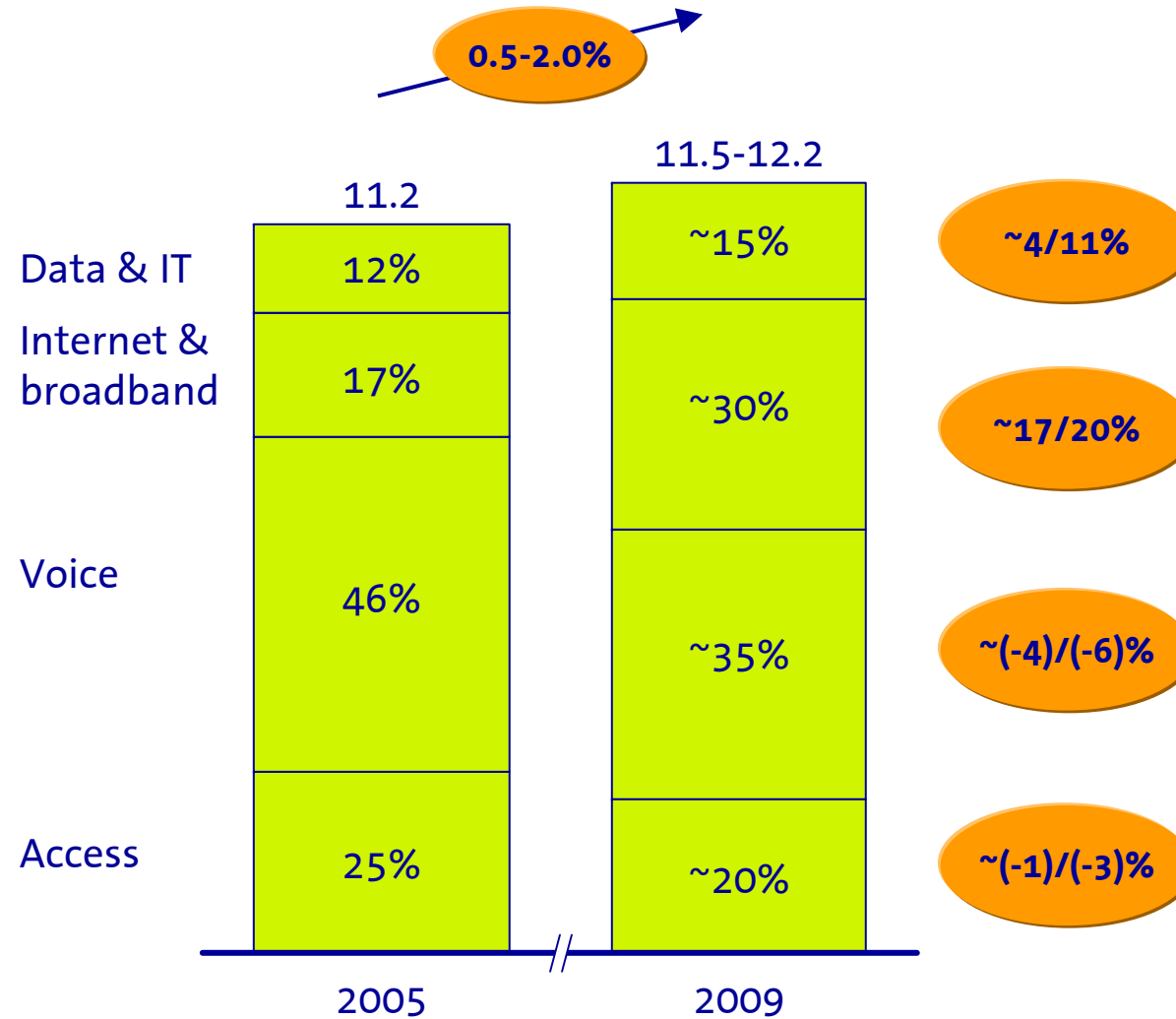
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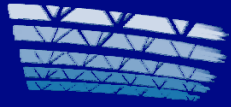
02 We will maintain solid revenue growth for the following years

Revenues. EUR billion

CAGR

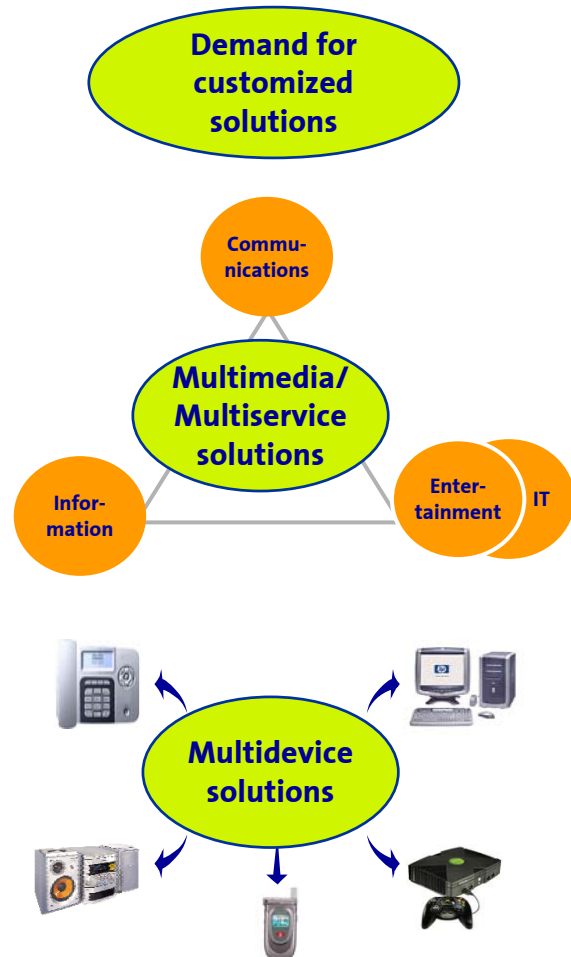


Note: TdE Parent Company (excluding Terra, Telyco, TTP and other affiliates)

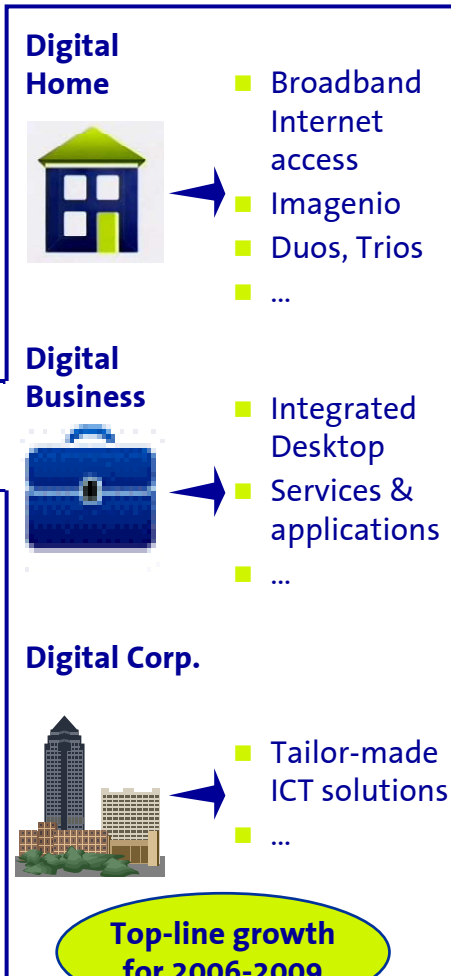


02 We will achieve this solid revenue through bundling and integrated solutions

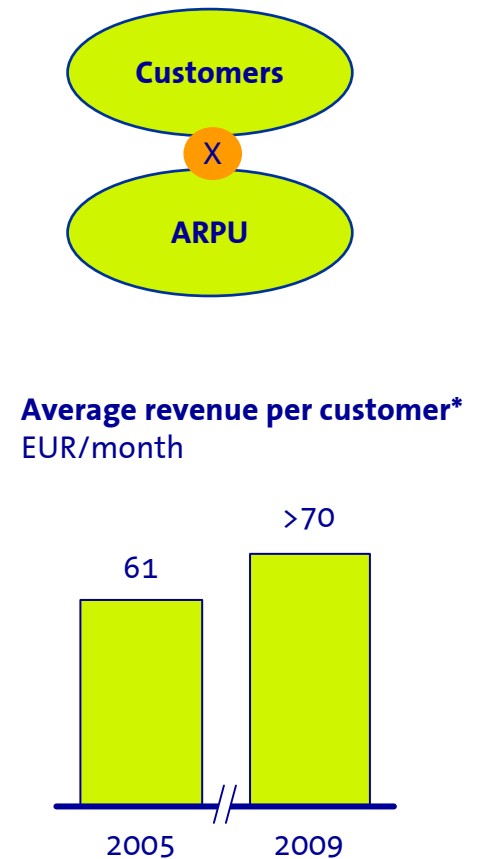
Three main trends



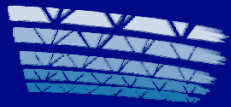
Three focused visions to deliver value to customers



Our growth strategy



* Retail revenues / number of customers

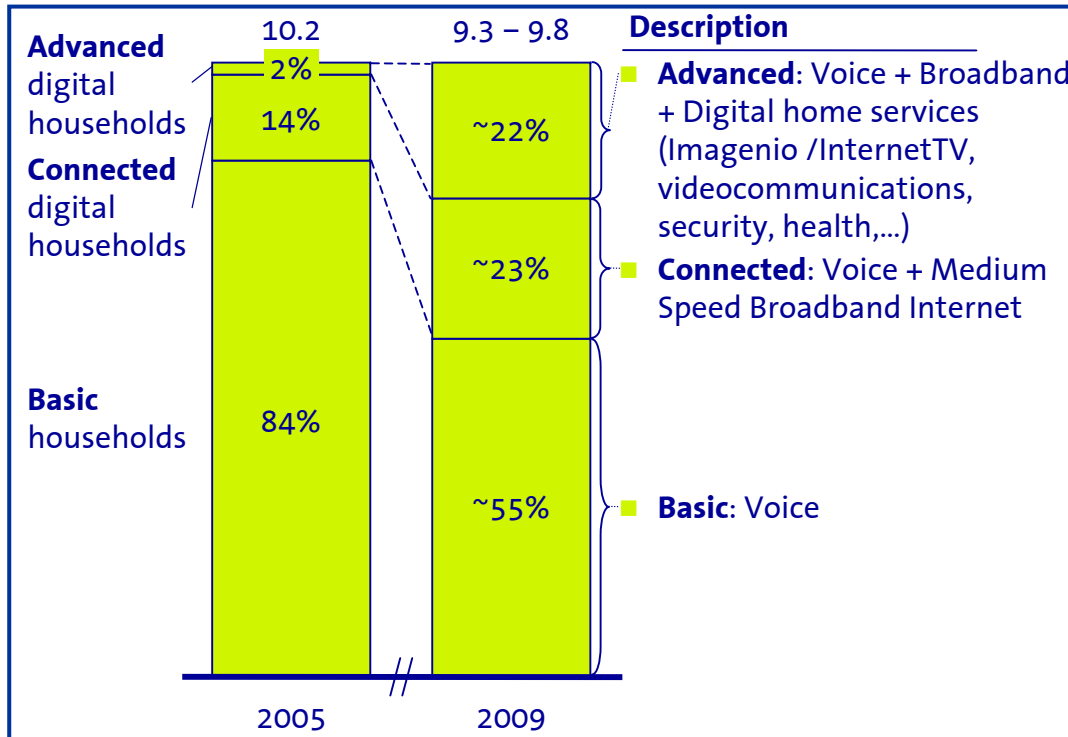


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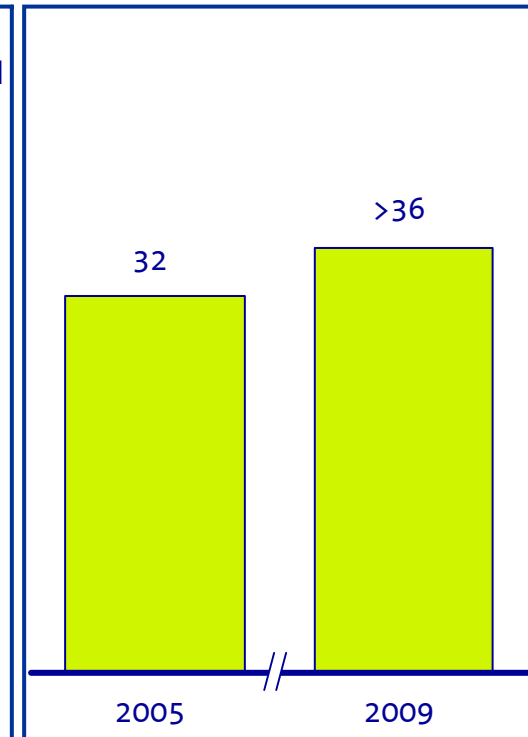
02 In households, we are offering bundles and solutions for all our customer segments, increasing overall ARPU



Household customers
Million of subs



Average revenue per household customer*
EUR/month



The increase in ARPU will be achieved , despite foreseeable price reduction, with the migration of customers to higher value segments

* Residential retail revenues / number of residential customers



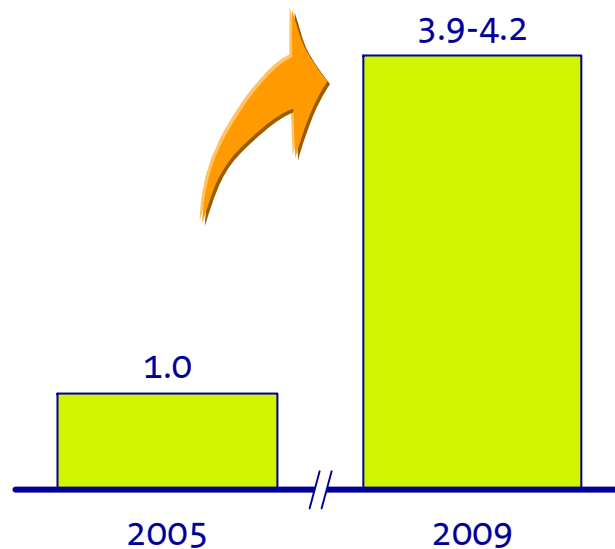
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02 Our digital household customers are already enjoying new solutions: Duo, Trio and Imagenio are the first steps to the Digital Home Concept



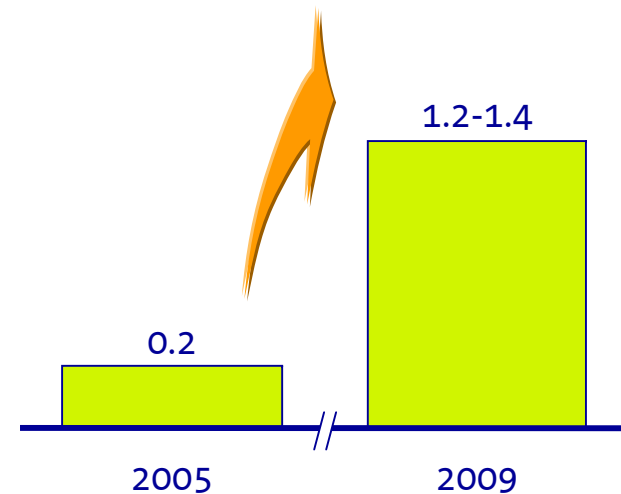
Our customers will keep on adopting bundles in the future

DÚO » TRÍO »
Million of subscribers*



Our Imagenio-based entertainment offering is the first step of our digital household offering

imagenio
Million of pay TV subscribers**



* Only households

** Includes SOHO and SME subscribers

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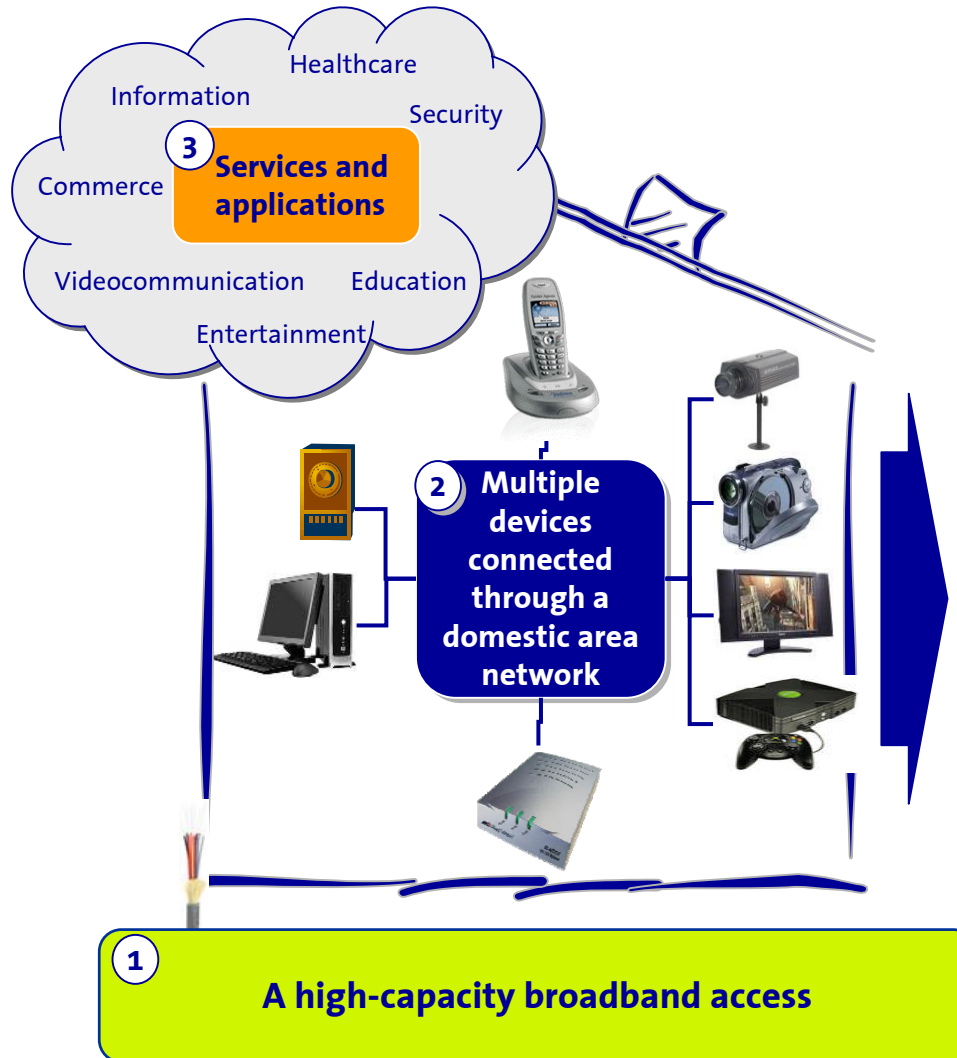
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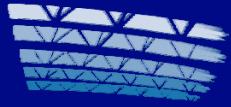
**We are already
working in Digital
Home market
development
*Trio TV spot***



02 We are working on offering our Digital Home customers an increasing array of services and solutions



- The Digital Home strategy is the result of the integration of three building blocks:
 - Broadband access
 - Multiple devices connected through a domestic area network
 - Services and applications
- In this context we can further segment in:
 - Connected Digital Homes (medium speed Internet connection)
 - Advanced Digital Homes. Multiple application and services on top of multiple devices/electronic equipment: TV, security content management, domotics.



02 In the short term we have an ambitious P/S roadmap for digital households



Household roadmap 2006-2007

Broadband Access

High-speed connectivity as a basis for Advanced and Connected Digital Homes

Domestic Area Network with multiple devices

TV videoconference with 3G interworking

Domotics: Integrated home devices and remote management

Seamless Fixed and mobile services

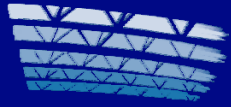
Services and Applications

Personal TV: HDTV, Shift TV, DVR, flexible content selection.

Internet multimedia (Pixbox)

Connectivity Bundled with VAS: Home content management

Family management (education, security and health)

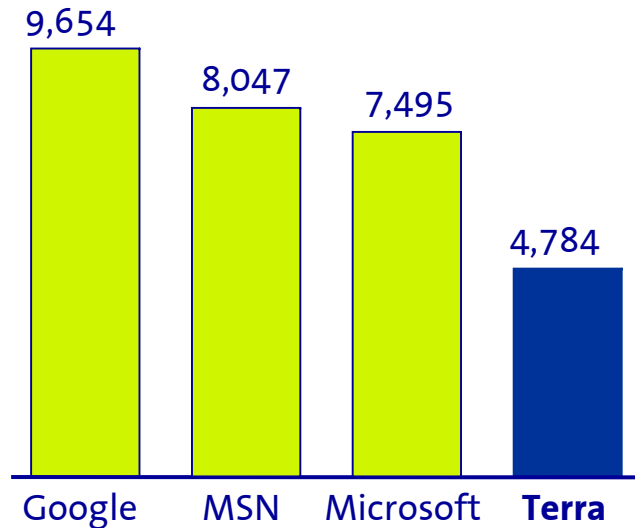


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02 The integration of Terra will allow us to strengthen our leadership in the digital household market



Most visited Internet brands
(thousands of unique residential visitors, march2006)



According to Nielsen/Netratings, Terra is the fourth most visited Internet brand in Spain

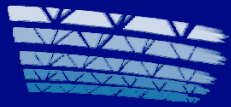
Source: Nielsen/Netratings Netview, March 2006

- We are adding value to our digital offer with the **integration** of a key player in the Spanish Internet market:
 - Leveraging Terra’s **online technology**
 - Enhancing the **content** offering
 - Increasing monetization through **advertising**
- As an example, our first product launch after the integration is **PixBox**



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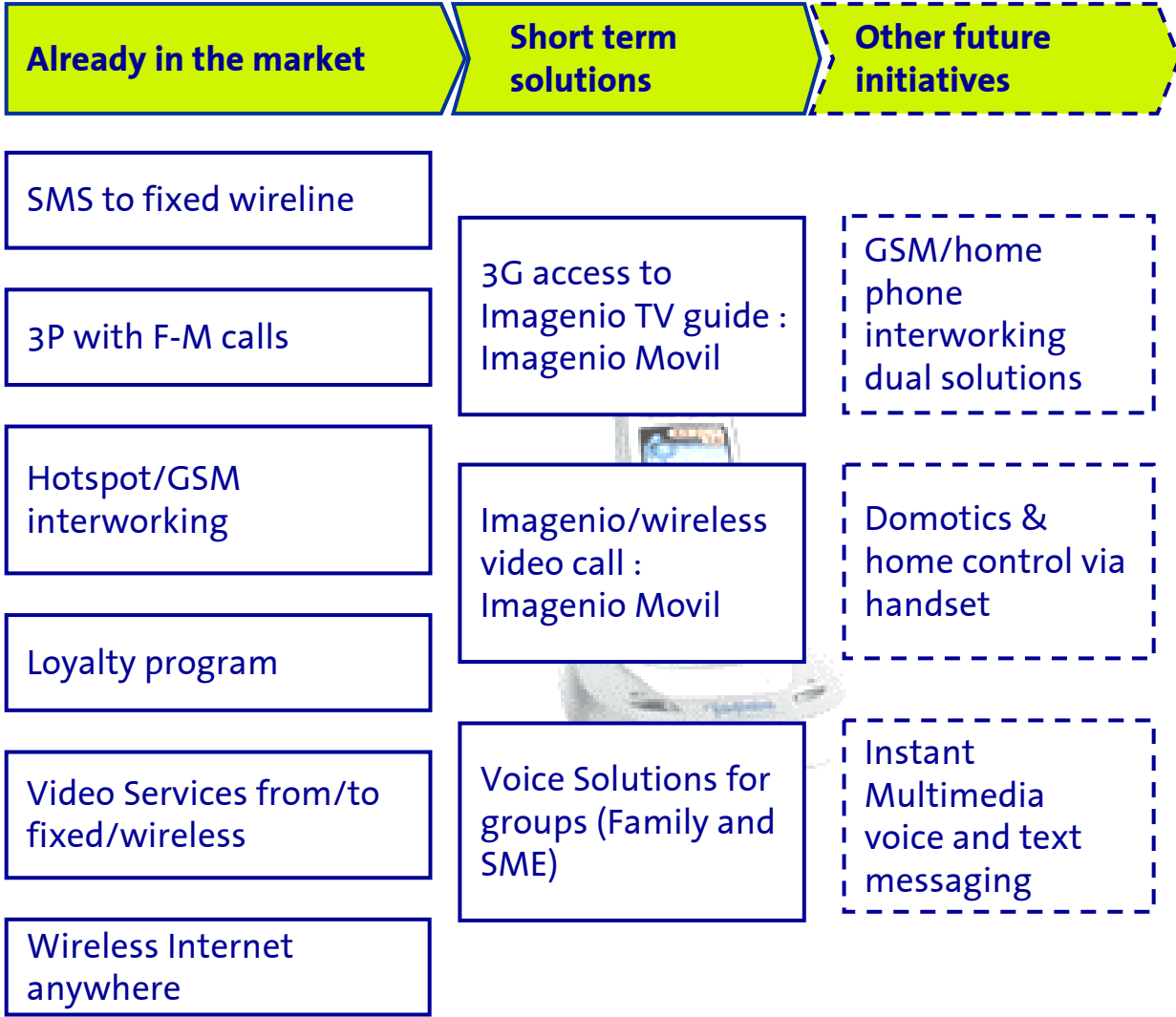
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02 We are also developing innovative fixed-mobile solutions

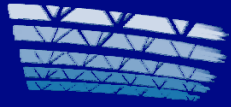


Our aspirations are:

- To be leaders in the development of fixed-mobile broadband services
- To evolve from a separated product offering towards fixed-mobile solutions



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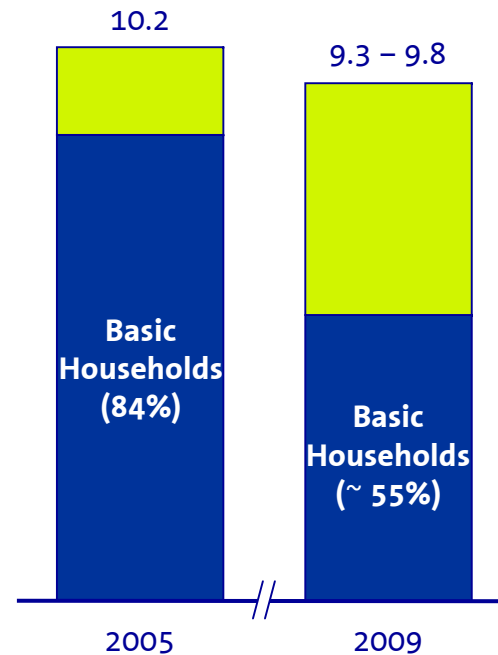
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02 And we also have a bundle & solutions strategy for our Basic Households

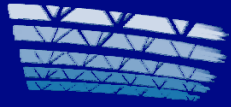


Households subscribers
Million subs



■ We are also creating value for our basic customers:

- ① Innovative product offering (e.g. **bundling access and voice**) and pricing schemes (e.g. flat voice rates)
- ② **Customized solutions developed for segments with special needs:**
 - Immigrants
 - Euroresidents
 - 2nd residences
 - Young families



02 Specifically, the revenue threat of VoIP in Spain is limited

	Voice customers	Broadband customers
Households	Due mainly to the existence of capacity interconnection fees in Spain, there is no substantial improvement on economics that would allow more aggressive pricing to ULL competitors	The double play offers outperform VoIP value proposition
SoHos & SMEs		Our integrated desktop offer provides a better value to our customers, bundling voice and other VAS
Large companies	We are offering tailor-made ICT solutions which are including VoIP according to our customers needs	

VoIP will base its development in Spain on a **'more service'** basis instead on a **'lower price for voice service'** basis

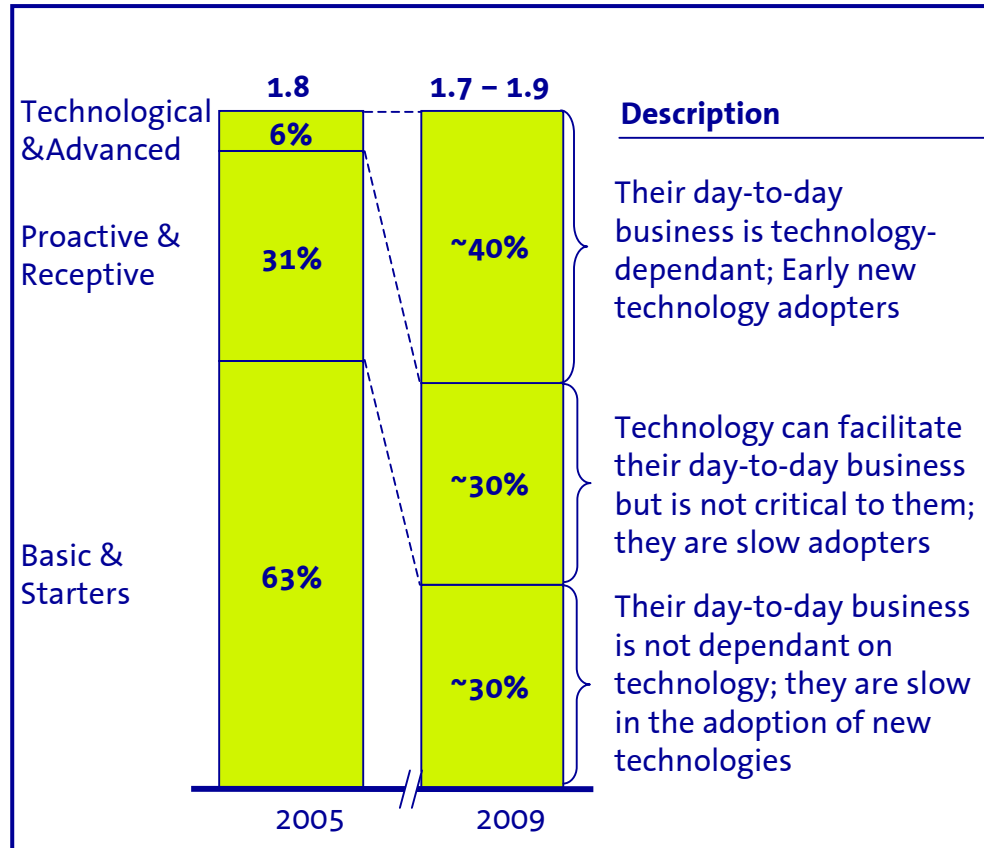


02 For SoHos and SMEs we are also targeting our specific customer needs



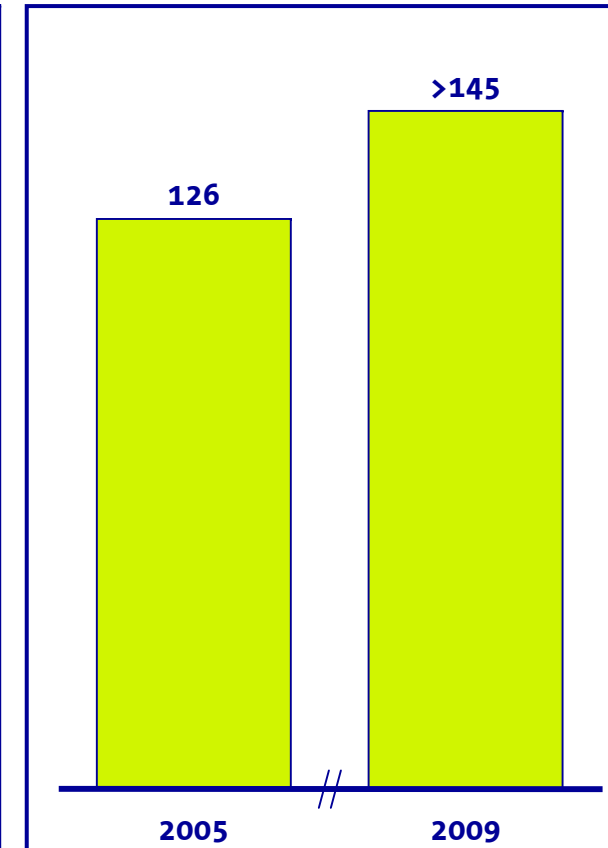
SoHos & SMEs customers

Million subs

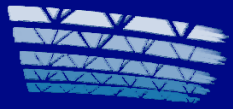


Average revenue per SoHo & SME customer*

EUR/month



We are planning to increase the ARPU by shifting our customer base from basic customers to more advanced customers with higher ARPU

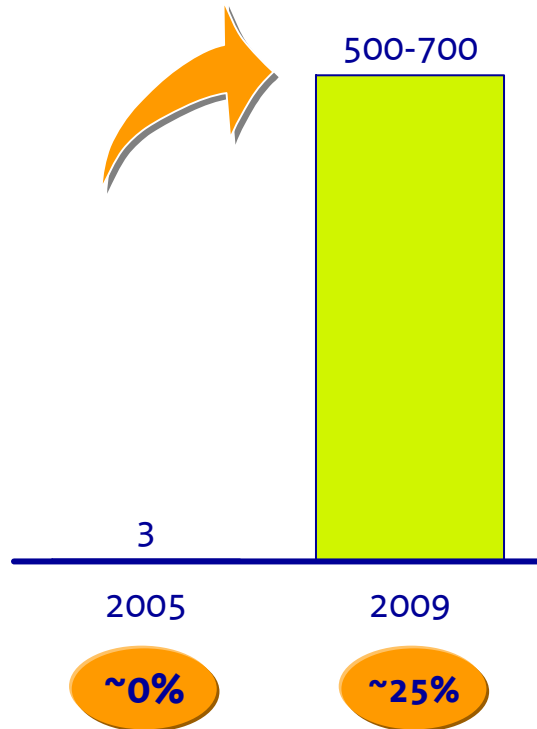


02 SMEs and SoHos also increasingly demand integrated solutions



% of integrated desktops over potential market

Number of integrated desktops*
Thousand



* IT and integrated desktops



- 1 Integrated Desktop**
Integrated access to all Communication and IT needs
- Voice
 - Switchboard
 - Phone equipment
 - LAN
 - Desktops and/or laptops

- 2 Services**
- Installation
 - Maintenance
 - Management
 - VPN
 - Guaranteed capacity access

- 3 Applications**
- **Horizontal applications:** web, intranet, antivirus, firewall, e-mail and content filter, PC back-up...
 - **Vertical applications:** video-surveillance, background music with DSL, legal content, CRM and ERP applications...



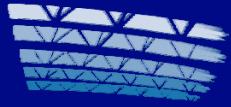
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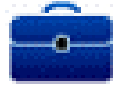
02



**We are already
working in Digital
Business market
development**
*Respuesta empresarios
TV spot*



02 In the short term we have an ambitious P/S roadmap for small businesses



Business roadmap 2006-2007

Integrated Desktops (service + maintenance)

Voice: Click2Call

Data: Remote desktop
control

LAN/Switchboard



Network Services

VPN

VoIP (centrex IP)



VAS

Network managed
services

Horizontal ASP (web
presence, firewall, PC
back-up)

Vertical ASP (CRM
applications, video
security systems)

**Customers build for themselves personalised services and pay a monthly
fee for it: All included**



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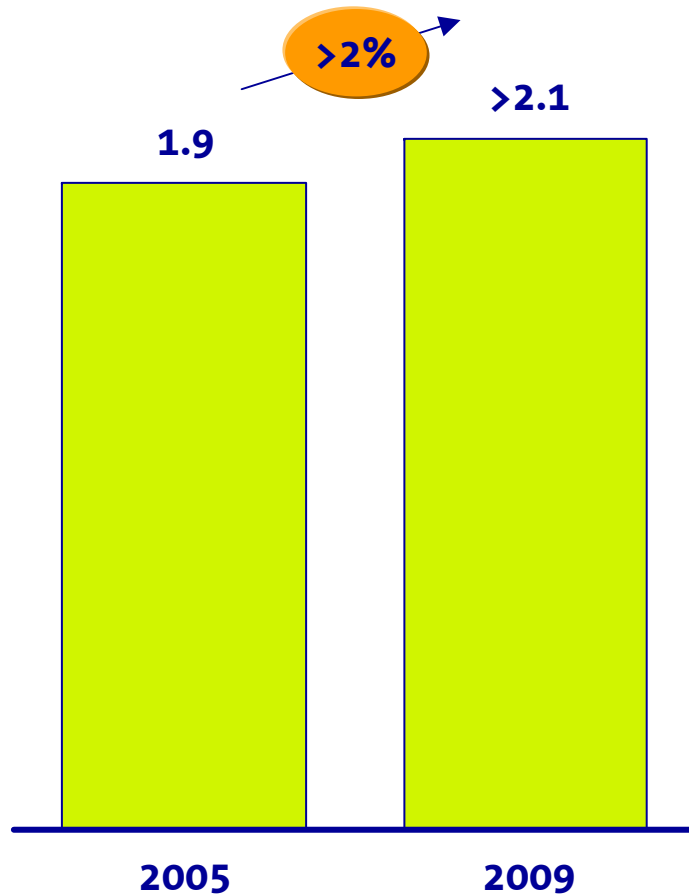
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02 We expect substantial revenue growth from contracts with large corporations

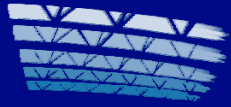


Revenue growth from large corporate contracts
(EUR billion)

 CAGR



We intend to achieve this revenue growth providing our current customers with additional, tailor-made ITC solutions



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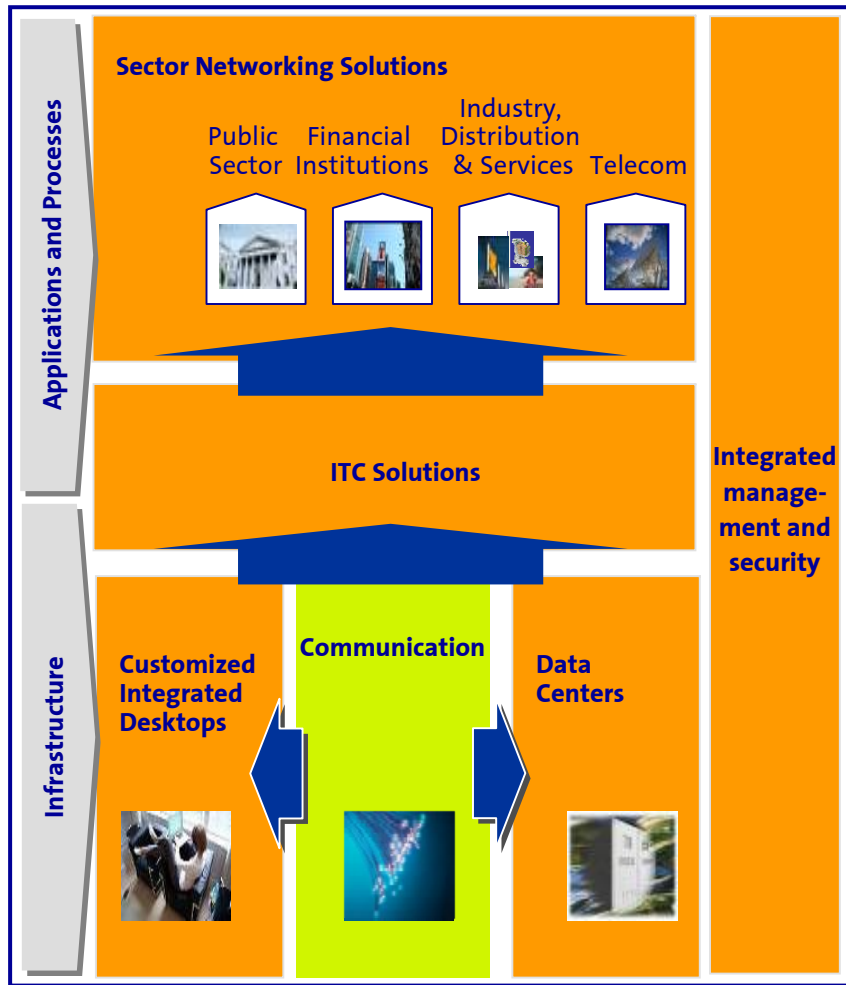
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02 We will leverage our strong foothold in Communications to respond to the arising demand of integrated ITC solutions by large corporations

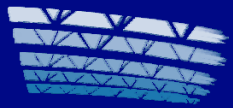


Information Technology
Communication

A new approach: ITC Solutions Provider for the Digital Corp.



- Telefonica is in the best position to provide ITC tailor-made solutions ...
 - IT competitors cannot easily replicate Telefonica’s **assets and know-how** in Communications
 - We have the largest **sales force** in Spain, accounting for 400 account managers trained for consultative sales and 650 pre sales engineers
- ... while it additionally develops **strategic partnerships** with relevant specialist players in adjacent industries...
- ... creating a new world of **Sector Networking Solutions** that, while customizable, can be **replicated** for different companies in the same sector, allowing for interworking between them



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02 Our new approach is already delivering real solutions

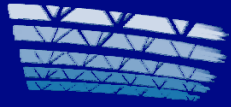


Information Technology
Communication

A new approach: ITC Solutions Provider for the Digital Corp. ... delivering specific solutions



Telefonica



02 In the short term we have an ambitious P/S roadmap to advance in the ITC world



ITC roadmap 2006-2007

Next generation corporate voice communications

Upgrade of Ibercom Service (VoIP, pay-per-post/application pricing scheme, etc ...)

Corporate broadband

New symmetric DSL accesses
Customized, corporate quality SLAs

Customized ITC management services

Client-premises fully customized Service Management Centers (CSP)

End-to-end desktop outsourcing solution

Customized solutions (collaborative tools, security, ID , equipment, support, ...)
Pay per worker/profile on a flat-rate basis

Industry-focused solutions network

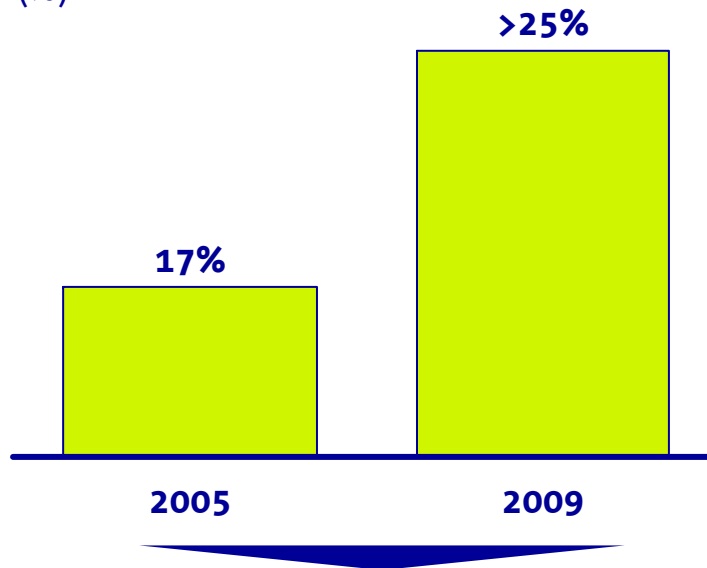
Industry ITC solutions on a pay-per-use basis (Medical Prescriptions Management ,
Online Insurance Claim Valuation, e-Government, Clearing House Processes...)



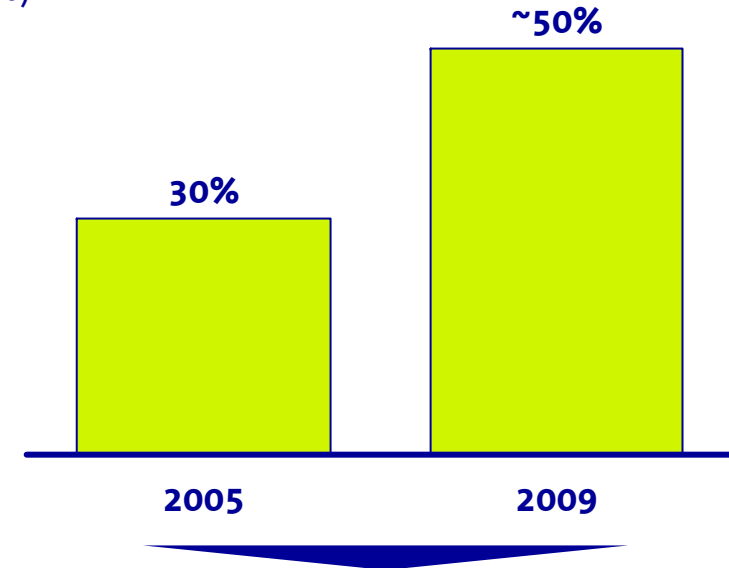
02 We enter a transformational period to become the ITC solutions provider leader



IT solutions revenues as % of our revenues from large corporations (%)

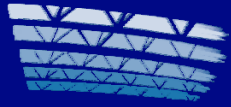


Revenues from multi-year contracts as % of our revenues from large corporations (%)



- Differential offering, wrapping together Communications & IT wherever ...:
 - ... our communications business gives us a cost edge over competitors
 - ... communications leverage the value of the solution
 - ... the solution is a natural extension of our traditional business

- Building long-term, confidence driven relationships to ensure sustainable revenue
- Helping clients grow, focusing in their core business while ensuring technological evolution



Content

01 During 2005 we continued to deliver top results while strengthening capabilities for future sustainability

02 **Going forward we will leverage our competitive advantages to grow even further**

- Positive socioeconomic landscape
- Sustainable growth based on a distinctive offering
- **Higher efficiency levels**
- Thoughtful investments to support future growth

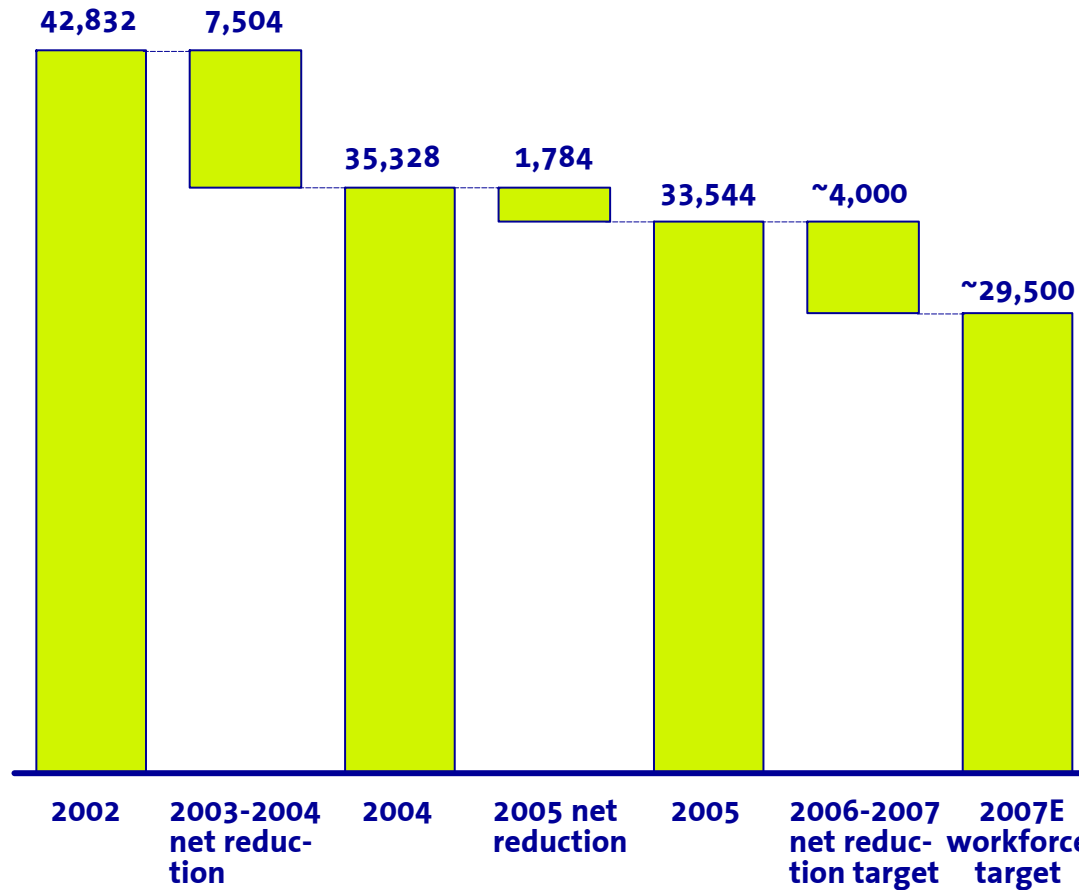
03 As a result, we commit to ambitious financial and operational targets



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02 We are completing the execution of our current workforce reduction program

Number of employees, TdE Group*



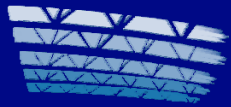
- The program will affect ~15,200 employees
- ~75% of the redundancy program already achieved
- ~1,250 people joined the program ytd
- ~4,000 people left to complete the program

Former perimeter



* Includes all TdE companies (TData España, Terra España, T Soluciones, TSS and TdE). Does not include TdE Group subsidiaries: TTP, Telyco and T-Cable



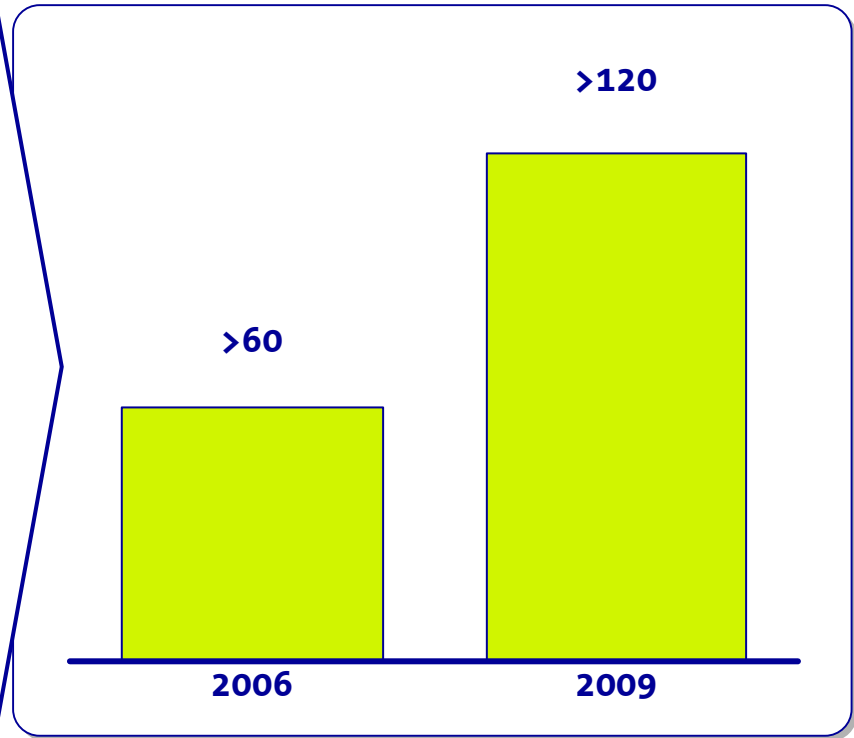


02 We are designing a more efficient operating model to maintain our solid cost base in the future

Levers

- Intra TdE (former perimeter)**
 - Integration of Infrastructure & Operations field activities
 - Back-Office and support areas process optimization
 - Outsourcing optimization (especially IT)
- TData + Terra**
 - TData + Terra Redundancy Programs
 - Network synergies (TData + TdE)
 - Commercial access costs synergies (Terra + TdE)
 - Infrastructure costs: Provisioning, maintenance...

Estimated operating cash flow yearly impact
€ Million



Additional Levers

Distrito C

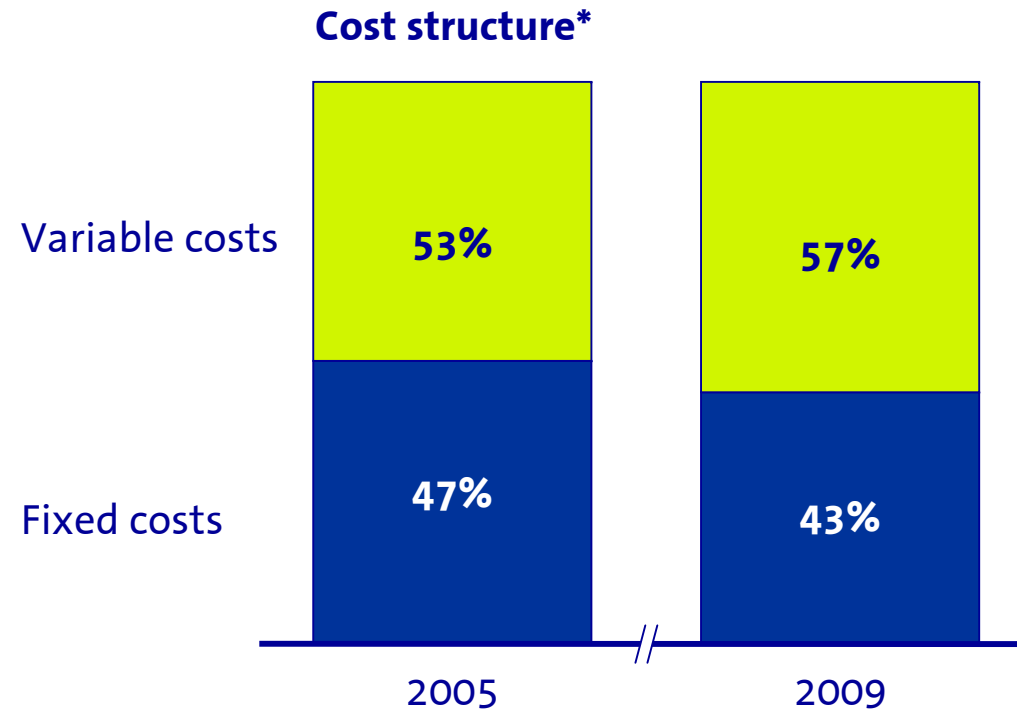
- Organizational efficiency
- Advanced workplace conception

Moviles España

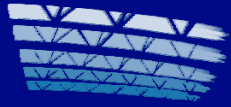
- Sales channels
- Network, IT and operation synergies



02 These efforts will help us move towards a more flexible and competitive cost structure



- Total operating costs evolution fully aligned with revenue growth
- More intense and variable third party collaboration model



Content

01 During 2005 we continued to deliver top results while strengthening capabilities for future sustainability

02 **Going forward we will leverage our competitive advantages to grow even further**

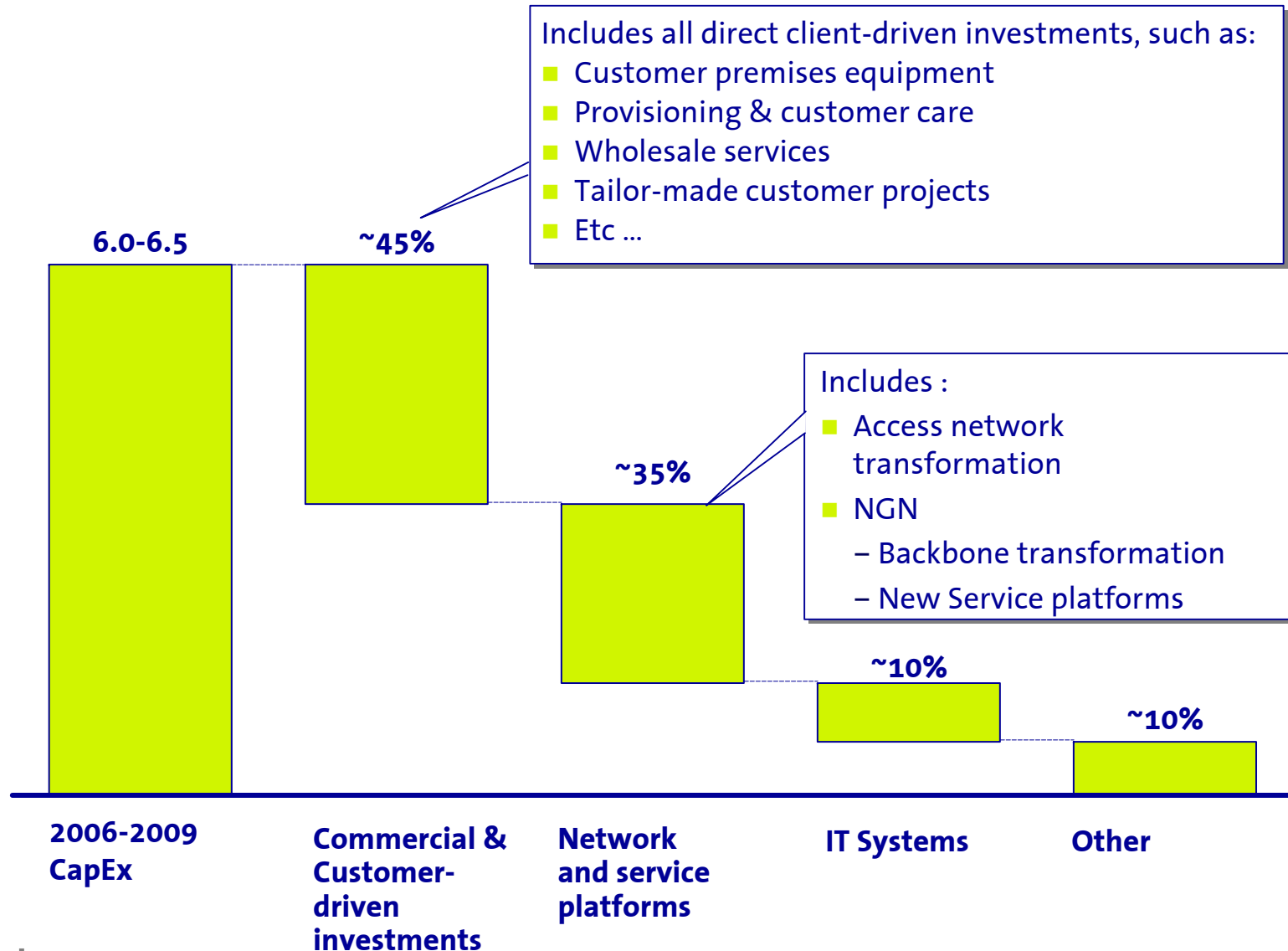
- Positive socioeconomic landscape
- Sustainable growth based on a distinctive offering
- Higher efficiency levels
- **Thoughtful investments to support future growth**

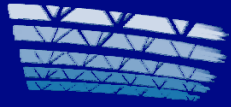
03 As a result, we commit to ambitious financial and operational targets



02 Our total investment will amount to € 6.0-6.5 billion for the 2006-2009 period

EUR Billion





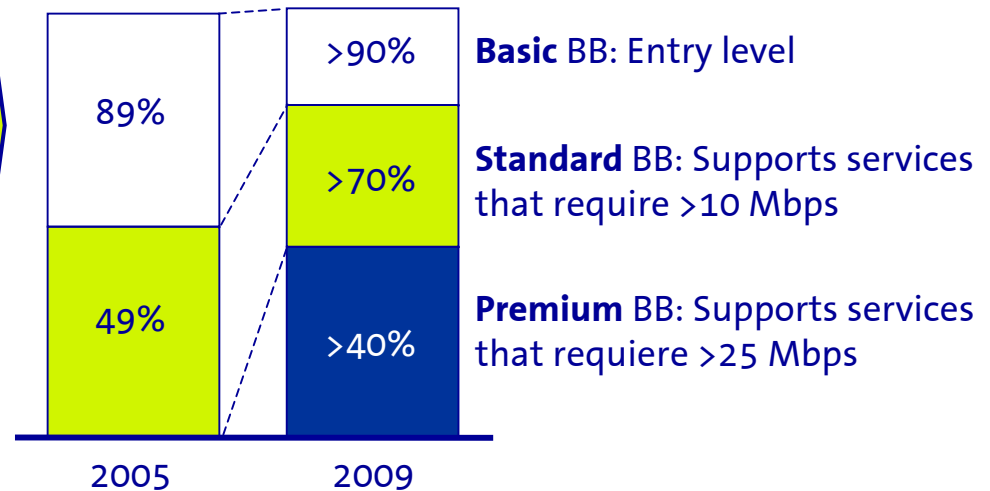
02 Access network transformation will be achieved with a thoughtful investment approach

Deployment criteria

- We are making local loops shorter in order to provide higher speeds.
- Deployment will take into account:
 - The best technical solution is chosen on a case by case basis (ADSL2+/VDSL2, Copper/FTTx)
 - The solution can easily scale in the future
 - Deployment is prioritized according to micro-area value
- Total investment will amount to ~800* million EUR for the 2006-2009 period

Our goal is to create a more flexible and higher capacity network

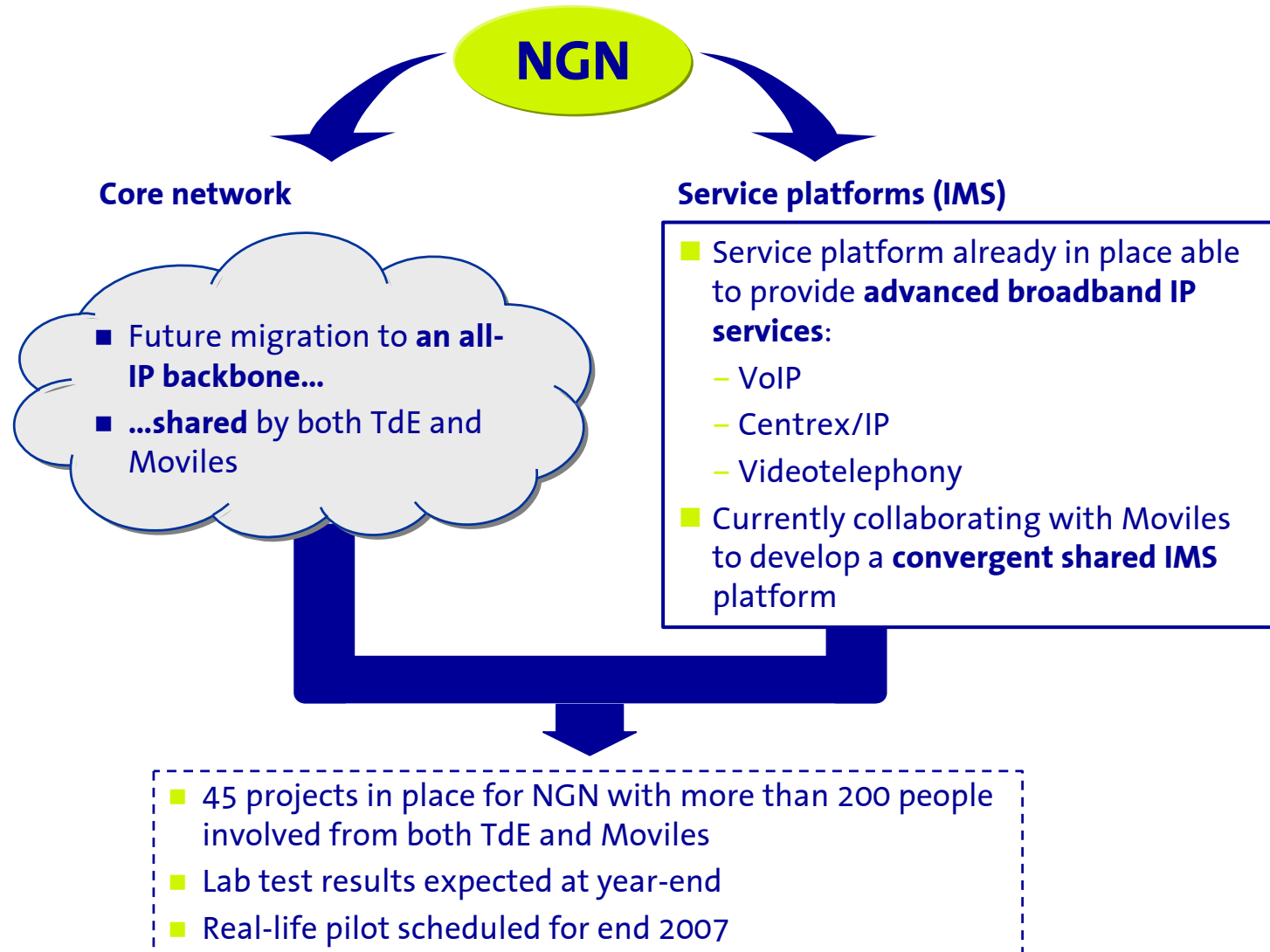
Coverage of hi-capacity local loops
% of TdE local loops

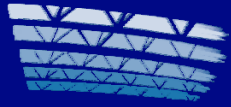


* Includes street cabinets, fiber, transmission equipment, full equipped nodes except cards, ... Does not include VDSL deployment



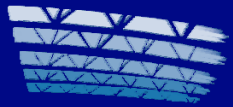
02 We are sharing with Moviles España the development of a next generation network





Content

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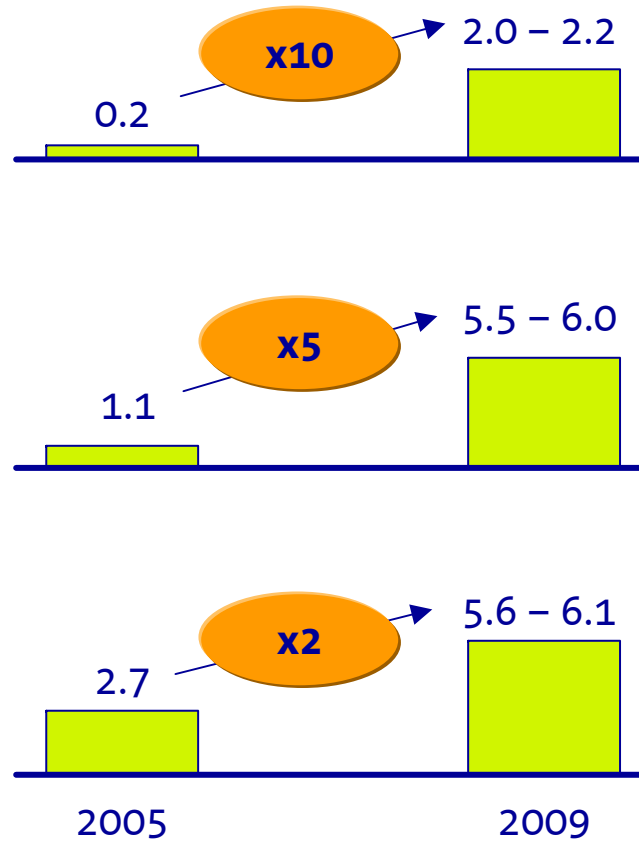
03 This strategy will allow us to achieve our main 2009 access goals

Advanced Digital Homes*
(million)

Duo and Trio customers**
(million)

Retail broadband Internet accesses
(million)

Basic accesses

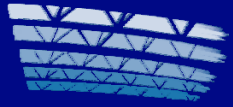


>95%
broadband
customers with
Duos and Trios

<2% reduction on a yearly basis,
reaching ~40% of accesses with
bundled voice or broadband in 2009

* More than 50% will be pay TV subscribers

** Includes Residential, SOHO and SME subscribers

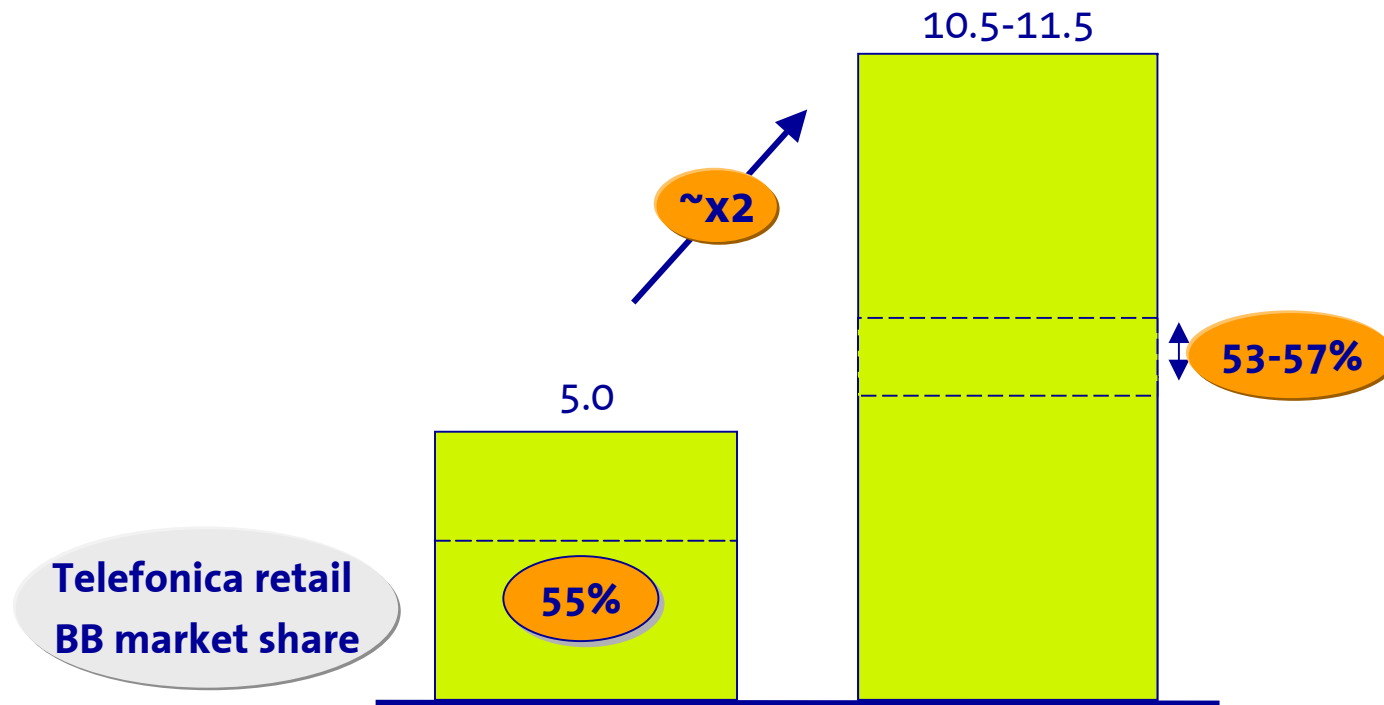


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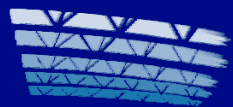
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03 Our priority is to increase broadband penetration and defend our broadband market share

Broadband Accesses, millions



Achieve 5.6-6.1 million broadband retail accesses by 2009



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03 Telefonica de España financial commitments

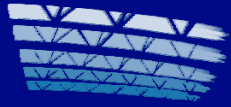
€ in Millions	FY 2005 *	CAGR 2005-09E **
Revenues	11,755	0.5 - 2%
Operating Income before D&A ***	4,765	3 - 6%
Operating Income ***	2,627	9-14%
CAPEX	1,401	6,000 – 6,500 (Cumulative CAPEX 2006-2009)

* TdE numbers are pro-forma, including Terra's Spanish unit since January 2005

** CAGR 2005-2009E guidance excludes changes in consolidation

*** In terms of guidance calculation, Operating Income before D&A and Operating Income exclude other exceptional revenues/expenses not foreseeable in 2006-2009. Personnel Restructuring and Real Estate Programs are included as operating revenues/expenses. For comparison purpose, the equivalent other exceptional revenues/expenses registered in 2005 are also deducted from reported figures

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Summary

- Strong financial results and solid position and strength to keep on competing in the future taking advantage of a positive socioeconomic environment
- Three-pillar strategy equally focused on growth and cash returns:
 1. **Top-line growth.** Based on **Integrated solutions** for each of our customer segments:
 - Our **Digital Home** offer will cover all communication, entertainment and information needs for Households
 - The **Digital Business** concept will provide increasingly customized IT and communication solutions on a per-user monthly fee
 - For large companies we will strengthen our position as an **ITC solutions** provider, offering fully customized ITC solutions for each individual customer
 2. End of our current workforce reduction plan and continue working towards reducing costs while **increasing** both our **efficiency** and **effectiveness** as well as our overall **quality** levels.
 3. Thoughtful investments to **upgrade our network** for the kind of advanced services that we are developing
- As a result, we expect to keep delivering solid top-line growth (0.5-2%) and Operating Income (9-14%)

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