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Purchasing: An efficiency lever for the Telefónica Group
Key messages

Purchasing is one of the key levers for the Telefónica Group to increase efficiency

- Telefónica has implemented a Group integrated management model: the Advanced Purchasing System (APS)
- APS was launched in 1998. Today it’s consolidated almost in the whole Telefónica Group
- In addition to the significant savings derived, there is still room for improvement in APS implementation
**Purchasing is at the heart of Telefónica’s efficiency effort**

*Year 2001. Million euros*

High potential impact: 1% in purchasing costs reduction translates into a 6% improvement in net cash flow

* Basically interconnection fees, audiovisual contents, legal and financial products and services

<table>
<thead>
<tr>
<th>Revenues</th>
<th>Personnel</th>
<th>Purchases</th>
<th>Others*</th>
<th>Operating Cash Flow</th>
</tr>
</thead>
<tbody>
<tr>
<td>31,052</td>
<td>5,390</td>
<td>14,850</td>
<td>6,331</td>
<td>4,481</td>
</tr>
</tbody>
</table>

Net Cash Flow 2,292
We have developed a Group integrated management model...

Key principles

- Aggregate all group purchases by category
- Professionalize and develop specialized “purchasers”
- Balance centralization synergies & execution flexibility

To radically change the buying concept:

From multiple buyers in all areas and companies

- Individual price & conditions negotiation
- Provisioning, centralized in each company

To a single global purchaser

- Global price & conditions negotiation
- Assignment
- Provisioning, decentralized in each area

Supplier evaluation
**The Advanced Purchasing System (APS)**

- **Strategy**
  - A single and global purchasing strategy
  - High integration level with suppliers and internal customers

- **Processes**
  - Standard processes
  - Internal & external transparency
  - Planning & coordination

- **People**
  - People development through:
    - Products & purchasing techniques training
    - Clear and exciting career path

- **Organization**
  - Coordinating three layers: global, country & company
  - Specialized by product/category

- **Systems**
  - Integration with other internal systems and ERP
  - Using leading technology platforms
... which supports purchasing for a wide range of products and services*

Total APS purchases, year 2001. Million euros

~70% of Group Capex
~42% of Group Opex

Total purchases APS: 13,150
Network infrastructure: 3,475
Services and construction work: 4,350
Commodities: 2,725
IT: 1,750
Marketing & Advertising: 850

APS is supporting more than 85% of Telefónica’s total purchasing
... and has been built over an integrated system to optimize capabilities

- **E-Procurement** will support up to 20% of products and services purchases which are able to be included in a catalog
- **E-Marketplace** will support up to 40% of common purchases managing offers and allowing an on-line bidding system

* SSC, Shared Services Center
Launched in 1998, APS has been extended to most of the Group companies...

- Gradual introduction of Group companies
  - Gain credibility
  - Manage complexity
- Quick incorporation of new companies
... and has shown a significant impact since then

Consolidating the system...

- A solid internal platform of capabilities
- A competitive suppliers base:
  - Helping them to identify and reduce inefficiencies
  - Achieving medium and long term agreements
  - Implementing a quality standardization system
- An exhaustive control system
  - Linking budget and purchases
  - Identifying and pursuing saving opportunities
- Aligned technologies through standard specifications

... to achieve strong savings:

- 15%-25% in 1st year of integration for each Company
- More than 5% in following years
But there is still room for improvement in APS implementation

**Width, increasing APS coverage**

- Roll-out APS to consolidate the remaining 10-15% of volume
- Agreements with new partners to increase purchasing volume and take advantage of synergies

**Depth, developing APS key elements**

- Intensify the use of e-technologies
- Develop APS tools and processes
- Reduce inventories and fixed assets via standardization
In 2002 we will focus APS development on three axes: first, intensify the use of e-technologies...

- Information flow and purchasing agility improvement
- The objective is to include 40% of total purchases
- Leverage Adquira* to develop the marketplace

Objective: get yearly savings about 90 million euros

- The objective is to include 20% of purchases in 2003 (all products and services which are able to be included in a Catalog)
- From this catalog, SBUs will be able to make orders, selecting items previously negotiated by APS
- Allows internal workload reduction

* Adquira is a BBVA, Iberia, Repsol-YPF and Telefónica marketplace partnership.
... second, develop APS tools and processes ... 

- Knowledge management systems
- Strengthening of advanced purchasing tools usage
- Efficiency improvement

Objective: get yearly savings about 170 million euros

- Supplier development plan:
  - Implement continuous improvement processes
  - "Telefónica’s Suppliers Club"
- Process reengineering for Companies and outsourcing
  - Suppliers relation in the fixed telephone network

- Supplier management by SLA’s
  - Responsibility is on the supplier’s side. Motivation for improvement
  - Setting terms using benchmarking
... and third, work with suppliers and logistic areas to reduce inventories and fixed assets

<table>
<thead>
<tr>
<th>Warehouses (Number)</th>
<th>Inventories (Million euros)</th>
<th>Number of references (Thousands)</th>
</tr>
</thead>
<tbody>
<tr>
<td>201</td>
<td>962</td>
<td>61</td>
</tr>
<tr>
<td>2003</td>
<td>646</td>
<td>46</td>
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The objective is to achieve with this lever a global savings of NPV 210 million euros
In summary:

- Telefónica has already implemented a single purchasing process which is
  - one of the key structuring drivers for the Group
  - A solid contributor to efficiency improvement

- We have a commitment to continuously improving purchasing by the introduction of new technologies and the development of new tools and processes in APS