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Safe harbour
Driving business performance for continued earnings growth
Driving business performance for continued earnings growth

• Telefónica stands out in a challenging environment

• Three building blocks support our future earnings growth
  – Accelerating performance of core businesses
  – Capturing our natural growth potential
  – Strengthening our “one company” model

• These building blocks translate into a set of management priorities and commitments
The environment remains challenging ...

- Growth is taking longer than expected to materialize: uncertainty and cautiousness

- Loss of favour in the financial markets
  - Difficulty in capital raising
  - Short term uncertainty blurring long term sector outlook

- Increased focus on short term
  - From “growth” to “earnings” and “cash-flow”
... with an impact on our day-to-day business

**Wireline**
- Declining prices
- Increasingly difficult to improve efficiency

*Fixed communication effective price per minute*  
*Spain (€ cents)*

<table>
<thead>
<tr>
<th>Year</th>
<th>2000</th>
<th>2001</th>
</tr>
</thead>
<tbody>
<tr>
<td>Price</td>
<td>5.7</td>
<td>4.5</td>
</tr>
</tbody>
</table>

21%

**Wireless**
- Slowdown in subscriber growth
- Growth in wireless data not forthcoming  
  (slow uptake in WAP, delays in UMTS)

*Year-on-year subscriber growth. Spanish market*

<table>
<thead>
<tr>
<th>Year</th>
<th>99</th>
<th>00</th>
<th>01</th>
</tr>
</thead>
<tbody>
<tr>
<td>Growth</td>
<td>113%</td>
<td>63%</td>
<td>19%</td>
</tr>
</tbody>
</table>

**Internet/Portals**
- Fall in advertising market
- Unmet expectations on e-commerce demand and margins
- Financing difficulties

*Growth in advertising revenues*

<table>
<thead>
<tr>
<th>Year</th>
<th>1999</th>
<th>2000</th>
<th>2001</th>
</tr>
</thead>
<tbody>
<tr>
<td>Growth</td>
<td>171%</td>
<td>76%</td>
<td>-11%</td>
</tr>
</tbody>
</table>

**Data transmission**
- Over-investment and over capacity
- Collapse in transport prices and margins
- Altnets struggling and players exiting the business

*Costs of a 2Mbits circuit from NY to London*  
*Indexed to 1998 price*

<table>
<thead>
<tr>
<th>Year</th>
<th>1998</th>
<th>Feb 2002</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost</td>
<td>100</td>
<td>8</td>
</tr>
</tbody>
</table>

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*All in-coming and outgoing traffic in TdE network (voice, narrowband Internet, interconnection)*

Source: Telefónica; Band-X Indices; IAB; eMarketer
Strong fundamentals and solid growth platforms will become key differentiators

Challenging economic environment:
- Financing restrictions
- Impact on demand
- Slow recovery expected
- Increasing saturation in developed markets
- Slowdown in demand growth
- Unfinished regulatory framework
- Efficiency improvements increasingly difficult

Environment remains uncertain and highly demanding for telecom companies

Key differentiating factors among integrated telcos:
- Strong fundamentals
- Solid growth platform
Telefónica is in a unique position

✅ We have delivered on earnings
✅ We have met each of our objectives
✅ We have solid and diversified client base and revenue streams
✅ We are well positioned to capture profitable growth ahead

Important achievements to date …
… rather than restating our achievements, we would like to review how Telefónica will deliver earnings growth
Driving business performance for continued earnings growth

• Telefónica stands out in a challenging environment

• Three building blocks support our future earnings growth
  – Accelerating performance of core businesses
  – Capturing our natural growth potential
  – Strengthening our “one company” model

• These building blocks translate into a set of management priorities and commitments
Three building blocks drive our business

Make the most of our client base and expand it, creating and satisfying their needs

- Understanding the needs of highly differentiated customer segments
- Capturing latent demand in traditional and new communication services leveraging four growth dimensions
  - Internet
  - Mobility
  - Broadband
  - Content
- Increasing loyalty and expanding our client base
Three building blocks drive our business

- Accelerating performance of core business
  - Continuous improvement in core businesses

- Capture our natural growth potential

- Strengthen our “one company” model
Accelerating performance of core businesses, eliminating inefficiencies

• Enhance commercial focus
• Improve efficiency
• Optimize capital base
• Work towards a fair regulatory framework
Accelerating performance of core businesses
Enhance commercial focus

Actively managing our customer base
- Segment specific CRM campaigns and loyalty programs
- Strengthened focus in SMEs

Developing new products and services (innovation)
- Shift from network enabled to customer driven innovation
- Continuous flow of new products and services
- New value added services, multi-service offers and bundled services
- Integrated Broadband solutions for Corporations

Adapting our distribution model
- Shift from product to customer focus in I&M services
- Proactive channel management and value driven incentives
- Rapid development of new channels

Number of customers (millions)

<table>
<thead>
<tr>
<th>Service</th>
<th>2000</th>
<th>2001</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pay-TV</td>
<td>68,2</td>
<td>78,4</td>
</tr>
<tr>
<td>Wireless</td>
<td>24,9</td>
<td>32,3</td>
</tr>
<tr>
<td>Wireline</td>
<td>42,3</td>
<td>45,0</td>
</tr>
</tbody>
</table>

- Significant progress in 2001, but continued effort required
- Customer proximity is a never ending task
## Accelerating performance of core businesses

**Improve efficiency**

<table>
<thead>
<tr>
<th>Year</th>
<th>Manageable Cost Efficiency</th>
<th>Discretionary costs*</th>
<th>Net Revenues**</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>49.1%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2001</td>
<td>46.5%</td>
<td>-2.6pp</td>
<td></td>
</tr>
<tr>
<td>2002</td>
<td>≈-2/-3pp</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

* Includes personnel and external services

** Revenues less cost of sales (purchases, interconnection expenses, provisions and tributes)

Continuous effort in manageable costs efficiency in 2001 with ambitious objectives for 2002
Accelerating performance of core businesses
Selective CAPEX to optimize capital base

CAPEX*
€ billion

2000 2001 2002
9,1 7,9

-13,2% -17/-20%

• Significant effort to control CAPEX compatible with organic business growth...
  – 19% CAPEX reduction in TdE’s traditional business
  – 7.9% CAPEX reduction in Telefónica Latam
  – Significant CAPEX rationalization in Telefónica Móviles, especially in Spain

• ...and aggressive investments to develop growth businesses
  – ADSL expansion in Spain
  – Achievement of “metas” in Brazil

• In line with a multi-year effort to improve EBIT

* Excluding UMTS licences and capitalized costs
Accelerating performance of core businesses
Work towards a fair regulatory framework

• We are continuously demanding a fair regulatory framework that promotes competition and fosters growth

• To date, we have been able to overcome the impact of regulatory measures

• Looking forward, we expect a more stable regulatory outlook, but still significant uncertainty for the levels of planned investment
Three building blocks drive our business

Accelerating performance of core business
- Continuous improvement in core businesses

Capture our natural growth potential
- Extracting the full potential of our existing customer base
- Expanding our customer base

Strengthen our “one company” model
Two dimensions to capture our natural growth potential

Extracting the full potential of our existing customer base
• Unlock latent demand for new services, e.g.,
  – Broadband
  – Wireless data

Expanding our customer base
• Natural expansion of our footprint, e.g.
  – Brazil
Significant growth potential in our markets

Example: Internet access. Thousands

Telefónica will benefit from the gap in Internet and broadband penetration

### Spain
- **SMEs**
  - Current Internet access: 2.180
  - Potential Internet access*: 12.820
  - Current Internet penetration: 41%

- **Residential**
  - Households with Internet access: 2.180
  - Total Households: 12.820
  - Current Internet penetration: 17%

### Latin America
- **SMEs**
  - Current Internet access: 3.810
  - Potential Internet access*: 45.310
  - Current Internet penetration: 24%

- **Residential**
  - Households with Internet access: 3.810
  - Total Households: 45.310
  - Current Internet penetration: 8%

* One potential access for every 10 employees in each physical office

Source: Telefónica; Pyramid; Target; Receita Federal; Exame; Lehman Brothers
Translating the Broadband opportunity into revenues and earnings

1. Closing the penetration gap in Broadband access infrastructure
2. Developing a full and compelling service offering for the residential segment
3. Evolving towards end-to-end solutions for our business customers, to capture additional value
4. Refocusing our media assets to address the content opportunity and capture the value for Telefónica
Closing the penetration gap in Broadband access infrastructure

Spain + Latam
Thousands of DSL lines

- Objectives for 2001 largely surpassed
- Ambitious but realistic deployment objectives
- Close management of economic parameters for profitability
Developing a full and compelling offer for the residential segment

Example: Imagenio

Imagenio

- Telephony
- Videoconferencing
- High-speed Internet Multimedia messaging
- TV for PC
- Multi-player games
- Games on demand
- Digital TV
- Video and music on demand
- Internet access on TV
- Open and premium TV channels

- 1,000 homes (pilot phase)

TdE: project management
Terra: PC content/services
Admira: audio visual contents for PC/TV
Telefónica Cable: TV/Radio channel aggregator
Evolving towards end-to-end solutions for our business customers

Example: eBA* initiative

**Concept**
- New service strategy for Large Corporations through a joint effort from several Business Lines in the Group
  - Network Communications Services
  - Applications and content
  - Communication management
  - Solutions design

**Approach**
- Boost high-capillarity Broadband communications and usage of Data Centers
- Develop high value added services
- Reassure reliable solution and high quality management

Development of complete, customized, “end-to-end”, industry-specific solutions for corporations
- To help customer increase efficiency in their own businesses
- To capture larger part of corporate communication expenditures

*e-Business over Broadband
Refocusing our media assets to address the content opportunity and capture value for Telefónica
Example: Multiplatform content and services unit

- Reorganize and focus the management of the Group’s content assets
- Centralize content acquisition, maximizing Group’s bargaining power and acquisition know-how to obtain the best available content
- Identify opportunities for intragroup synergies, developing new multiplatform content suitable for different networks and platforms
Brazil: we have the best platform for growth

Brazil. Million Reais

- Full contribution of new adds
- Tariff rebalancing
- Increased fixed to mobile traffic

- New growth opportunities opened by anticipation of “metas”
- Offer long distance service to current clients, both in Sao Paulo (450-550 M R$ revenue increase during 2002) and outside of Sao Paulo (250-300 M R$)

- Current ADSL penetration in line with developed countries (1,6%)
- Priorities for 2002 include reduction of OPEX and increasing ARPU in SMEs
- New opportunities for increasing market share in corporates

- Present in highest growth regions
- Additionally, joint venture with PT opens up new markets and generates significant synergies

2001 revenues*

<table>
<thead>
<tr>
<th>Business</th>
<th>Revenues</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Traditional wireline business</td>
<td>12,816</td>
<td>34%</td>
</tr>
<tr>
<td>Long distance wireline</td>
<td></td>
<td>18%</td>
</tr>
<tr>
<td>Broadband + Data</td>
<td></td>
<td>20%</td>
</tr>
<tr>
<td>Mobile</td>
<td></td>
<td>16%</td>
</tr>
<tr>
<td>Other</td>
<td></td>
<td>11%</td>
</tr>
<tr>
<td>2005E revenues</td>
<td>&gt;20,000</td>
<td></td>
</tr>
</tbody>
</table>

* Proforma (including Teleleste)
These new opportunities add up to significant growth

2/3 of 2002 revenue growth arising from new opportunities

Growth in traditional businesses
- Broadband/Internet
- Data services
- Wireless data
- Content

Growth from new opportunities
- Extracting full potential of existing customer base
- Expanding our customer base

Total Revenue Growth 01-02

- Brazil*

* Excluding broadband and Internet
Three building blocks drive our business

**Accelerating performance of core business**
- Continuous improvement in core businesses

**Capture our natural growth potential**
- Extracting the full potential of our existing customer base
- Expanding our customer base

**Strengthen our “one company” model**
- Consolidate our “one company” model
Evolving our flexible one-company model anticipating industry developments

The trends we observe...

- Before: Multiple pure growth options
- Now: More integrated client approach has higher value
- Data and Internet businesses becoming closer to our core
- Need to optimise efficiency in the use of our resources as one of today’s main driver for value creation

...lead us to work on two organizational fronts...

Simplify our approach towards the client
- Fulfilling client needs
- Articulating interfaces

Excel in efficiency
- Capturing synergies
- Creating units to leverage scale in non-core activities
- Managing aggressively internal market transfer prices

...to optimise the performance of our model

More simplicity...

...while maintaining
- Focus
- Transparent business performance
- Management accountability
Strengthening our “one company” model

Multibusiness working sessions
- Group and country Committees
- Focused task forces
- Competence Centers

Structured horizontal processes
- Finance and treasury
- Planning/Control
- Procurement
- Brand management
- IT architecture

Centralization of non-core areas and growth initiatives
- Efficiency improvement in non-core areas
- Multi-business growth initiatives

Share best practices and align priorities
Optimize critical resources
Capture synergies

Values that strengthen our common culture
Driving business performance for continued earnings growth

- Telefónica stands out in a challenging environment

- Three building blocks support our future earnings growth
  - Accelerating performance of core businesses
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  - Strengthening our “one company” model

- These building blocks translate into a set of management priorities and commitments
We continue to manage the same key parameters we communicated last year in Rio

Guidance for 2002

Key management parameters

• Customer profitability and market share
• Marketing effectiveness to enhance usage
• Cross-selling
• Efficiency
• Operational leverage
• Quality
• Asset turnover
• CAPEX allocation and control
• Reduction of asset base

Deliver continued earnings growth
Operational imperatives that will make a difference in 2002

- Fulfil ADSL economic targets
- Intensify commercial coordination in broadband and Internet to accelerate revenue growth
- Implement Group initiatives for resource management to reduce future cost pressures
- TeleSp: be ready to fully capitalize on upside of the Brazilian economy
- Accelerate the development of the JV with PT to materialize the benefits as soon as possible
- Speed up operational take-over of our new assets in Mexico
- Closely monitor that new mobile service revenues reach targets
- Ensure that T-Data delivers in the countries where we are incumbent
- Refocus media assets to maximize value and minimize cash-out for Telefónica
Our commitment: deliver continued earnings growth

Guidance for 2002

Revenues (€ Billion)

<table>
<thead>
<tr>
<th>Year</th>
<th>Growth 2001-02</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>7.9%</td>
</tr>
<tr>
<td>2001</td>
<td>9.0%</td>
</tr>
<tr>
<td>2004</td>
<td>12-14%</td>
</tr>
<tr>
<td>2005</td>
<td>6-8%</td>
</tr>
</tbody>
</table>

Customers (millions)

<table>
<thead>
<tr>
<th>Year</th>
<th>Growth 2001-02</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>15%</td>
</tr>
<tr>
<td>2001</td>
<td>&gt;100</td>
</tr>
<tr>
<td>2004</td>
<td>1%</td>
</tr>
</tbody>
</table>

2001 customers by market

- Spain: 49%
- Brazil: 23%
- Argentina: 19%
- Other Latam*: 1%
- Other**: 1%
- Venezuela (7%), Chile (5%), Peru (4%), Mexico (2%), El Salvador (<1%), Guatemala (<1%)
- Morocco

Real Constant exchange rate. Current business perimeter
Our commitment: deliver continued earnings growth

Guidance for 2002

Cost efficiency
(Discretionary expenses / net revenues)

-2,6pp
-2/-3pp

Operational leverage
(Fixed costs/total costs)

-2,3pp
-2/-3pp

* Estimates
Our commitment: deliver continued earnings growth

Guidance for 2002

<table>
<thead>
<tr>
<th>Year</th>
<th>EBITDA (€ billions)</th>
<th>Growth 2001-02</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>11.9</td>
<td>7.4%</td>
</tr>
<tr>
<td>2001</td>
<td>12.8</td>
<td>9-12%</td>
</tr>
</tbody>
</table>

- Real
- Constant exchange rate. Current business perimeter
Our commitment: deliver continued earnings growth

Guidance for 2002

**Total CAPEX** (€ billion)

<table>
<thead>
<tr>
<th>Year</th>
<th>CAPEX</th>
<th>Growth 2001-02</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>9.1</td>
<td>-13.2%</td>
</tr>
<tr>
<td>2001</td>
<td>7.9</td>
<td>-17/-20%</td>
</tr>
</tbody>
</table>

**CAPEX** / revenues

<table>
<thead>
<tr>
<th>Year</th>
<th>CAPEX%</th>
<th>Growth 2001-02</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>32%</td>
<td>-6pp</td>
</tr>
<tr>
<td>2001</td>
<td>26%</td>
<td>-6/-8pp</td>
</tr>
</tbody>
</table>

* Real

- Constant exchange rate. Current business perimeter

* EX-UMTS licenses and capitalized costs
Our commitment: deliver continued earnings growth

Guidance for 2002

**EBIT (€ billion)**

<table>
<thead>
<tr>
<th>Year</th>
<th>2000</th>
<th>2001</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>5.0</td>
<td>5.4</td>
</tr>
</tbody>
</table>

**Growth 2001-02**

- 15.5%
- 9.5%
- 10-13%
- 3-6%

**Cash-flow***

<table>
<thead>
<tr>
<th>Year</th>
<th>2000</th>
<th>2001</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>0.7</td>
<td>2.3</td>
</tr>
</tbody>
</table>

**Growth 2001-02**

- x 3
- x 2

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* EBITDA – CAPEX (exc. UMTS licences and capitalized interests) – financial costs - taxes

Real

Constant exchange rate. Current business perimeter

In conclusion, ...

- We continued to improve our business performance in 2001
- We have strengthened our one company model
- Our growth aspirations are real
- We have a clear path for 2002-2005
- Our commitments will deliver tangible results in 2002

Driving business performance for continued earnings growth