Building Value

César Alierta
Chairman & CEO
Telefónica S.A.
Objectives for these two days

- Review the progress since Río, during a difficult year
- Update Group’s strategy
- Understand why our strengths and strategic plan make us different
- Communicate a clear picture of divisional performance and outlook
- Have an opportunity to meet Telefónica’s senior management
- Provide you with an updated outlook for the medium term
Contents

• Progress since Río 2001
• Telefónica’s strengths
• Telefónica’s Strategic Vision
Progress since Río 2001 - Telefónica performance during a difficult year
Telefónica today

Scale & breadth

• 78 Million clients

• Operating in 17 countries

• Participating in all key businesses (Wireline, wireless, data, internet, media/ content)

Performance

• One of the most efficient Telcos in the world

• Best credit rating among European incumbent Telcos

• Outperforming European sector in ROCE during 2001

• Eur 67 bn (Equity Value) Company* with Eur 31 bn in revenues and Eur 13 bn in EBITDA

• 2nd European incumbent Telco by Market cap

* 67 bn Equity Value as of March 6th.
Our Challenge - Building Value

• Improve returns from core assets
  – Focus on customer innovation, service and quality to drive top line
  – Continue efficiency improvements to drive bottom line
• Strengthen Business Lines by leveraging all group assets across the customer base

Organic growth

Non organic growth

• Selectively invest in/acquire new assets as a source of additional profitable growth
• Unlock value from non core assets

Balance sheet strength and cash flow remains key differentiator
### Highlights 2001 (I):

#### SPAIN

- **TdE:** Return to EBITDA growth (+1.3%)
- Successfully defended market share and margins (EBITDA margin: 44%)
- Regulatory mgmt. progress: tariff rebalancing
- Operational excellence:
  - OPEX reduced by 3.1% yoy
  - Execution of Commercial Strategy
- Leading broadband offer in Spain (375,816 ADSL)
- Minimized growth in Capex (+4%) despite broadband expansion

<table>
<thead>
<tr>
<th>35% of consolidated EBITDA</th>
<th>20.6 MM LIS</th>
</tr>
</thead>
</table>

#### LATAM

- Largest EBITDA contributor even in difficult macroeconomic environment
- Top level EBITDA margin (51%)
- Significant cost cutting and conservative bad debt provisioning policies
- Capex peak in 2001
- **Telesp:** anticipate regulatory goals & significant revenue & EBITDA growth: 25% & 20% ($R)
- **CTC:** return to profitability thanks to cost control
- **TASA:** efficiency measures implemented to minimize crisis impact
- **TdP:** manage regulatory transition in a low growth environment

<table>
<thead>
<tr>
<th>40% of consolidated EBITDA</th>
<th>21.6 MM LIS*</th>
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</table>

* CANTV lines not included
Highlights 2001 (II): Wireless

26% of Consolidated EBITDA
29.8 MM Clients*

Becoming the European benchmark on business execution:
- Record EBITDA margin (49%; +12pp)
- Strong increase in customer base (+23%) coupled with reductions in SAC+SRC & churn rates
- Expanding market share gap with 2nd operator

Sound results, despite adverse economic environment:
- 32% increase customer base
- Healthy growth based on conservative customer accounting criteria
- TEM-PT JV on track to lead Brazilian mobile market

Strategy aligned with market conditions:
- Network sharing agreements already closed and CAPEX efforts minimized
- GPRS operations launched in Germany; reduced activity in Italy

Rationalize Capex & Opex with focus on FCF per customer

* Total managed customer base
### Highlights 2001 (III):

#### Terra Lycos (Internet)
- Delivering proforma revenue growth (+22% yoy) and improving profitability (24 pp improvement in EBITDA margin)
- Record 55% growth in pay subs (1.7 MM pay subs as of Dec’01)

#### T Data (Data)
- Incumbent data operations met Rio expectations
- Finalised repositioning of T-Data non incumbent operations

#### TPI (Directories)
- Strong increase in revenues and EBITDA (23.9% and 6.2% yoy)
- Progress on footprint expansion (Chile, Brazil, Peru)

#### Admira (Media)
- Mixed performance on top of a complex industry environment: still disappointing for Telefónica
- Endemol strong increase in Revenues and EBITDA (62.8% and 51.1% respectively)

#### Atento (Call Centers)
- Improved operating efficiency, with 22% growth in revenues and 113% in EBITDA
- Revenue diversification: 42% of revenue growth from external clients

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**On track Towards Profitability**
2001 - Financial Highlights

<table>
<thead>
<tr>
<th>CASH &amp; RETURNS</th>
<th>2001</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>FCF *</td>
<td>2,292</td>
<td>218%</td>
</tr>
<tr>
<td>CAPEX **</td>
<td>7,923</td>
<td>(12.9%)</td>
</tr>
<tr>
<td>ROCE ***</td>
<td>7.9%</td>
<td>0.6 pp</td>
</tr>
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<thead>
<tr>
<th>P&amp;L</th>
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</thead>
<tbody>
<tr>
<td>Revenues</td>
<td>31,053</td>
<td>9.0%</td>
</tr>
<tr>
<td>EBITDA</td>
<td>12,804</td>
<td>7.4%</td>
</tr>
<tr>
<td>Operating Income</td>
<td>5,430</td>
<td>9.5%</td>
</tr>
<tr>
<td>Net Income</td>
<td>2,107</td>
<td>(15.9%)</td>
</tr>
</tbody>
</table>

- Significant FCF growth
- Top ROCE among major European Incumbent Telcos
- Lowest Intangible assets to total asset ratio
- Growth rates on track with Rio targets
- 13% EBITDA growth excluding FX
- FX losses from AR$ devaluation included

* FCF = EBITDA - Financial Expenses – Capex (ex-UMTS) - Taxes
** Excluding UMTS licences
*** ROCE = Operating Income x (1-Taxes)/(YearEnd Stockholders’ Equity+Minority Interests+ Net Debt)
Telefónica Operations in Argentina

**Impact of crisis**

- Devaluation effects:
  - Total 2001 P&L effect (Eur 369 mn)
  - Additional Shareholder Equity impact in 2001 (Eur 1.4 bn)
  - No write off needed on Telefónica’s Balance Sheet as of Dec. 31st 2001
  - Potential additional impact in 2002

- Economic slowdown:
  - Reduction in demand
  - Increase in Bad-debt

**Action taken**

- Actively working towards renegotiation of the regulatory framework

- **Drastic Efficiency Measures**
  - Active negotiations with suppliers to reduce costs
  - Radical process redesign to lower structural costs
  - Strict bad debt control
  - Frozen CAPEX

- Monitor sector developments closely to improve competitive position in the recovery process
Telefónica’s strengths
A solid base for *Building Value*
A solid base for Building Value

Telefónica has all of the assets required to maintain “momentum” and will take advantage of its strong position to selectively seize available opportunities in the sector

• Good track record
• Powerful core skill set
• Solid financial position

Building Shareholder Value through Solid Growth
**Good Track Record**

- Consistently outperformed stock market and Telecom sector
- Increased and broadened sources of revenue and EBITDA
- Balance sheet strength maintained to reduce costs and keep flexibility
- Created credibility in capital markets

**Relative Share Price Performance**

**Sustainable Operating Growth**

**FCF & ROCE Evolution**

*FCF = EBITDA - Financial Expenses - Capex (ex-UMTS) - Taxes*
**Powerful Core Skill Set**

### Strong Skills to Manage Growth and Strengthen Leadership

<table>
<thead>
<tr>
<th>Managed Fixed Clients (Million)</th>
<th>1999</th>
<th>2001</th>
</tr>
</thead>
<tbody>
<tr>
<td>CAGR 9%</td>
<td>35.8</td>
<td>42.3</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Managed Wireless Clients (Million)</th>
<th>1999</th>
<th>2001</th>
</tr>
</thead>
<tbody>
<tr>
<td>X 1.9</td>
<td>15.6</td>
<td>29.8</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Internet Access Clients (Million)</th>
<th>1999</th>
<th>2001</th>
</tr>
</thead>
<tbody>
<tr>
<td>X 3.3</td>
<td>1.3</td>
<td>4.4</td>
</tr>
</tbody>
</table>

### Best Talent, Know-how and Assets

- Strong management team broadly recognised in the sector
- Successful track record in LatAm, gives us credibility to enter new markets
- Most efficient wireline operator in terms of LIS/employee (505 Spain, 804 LatAm)
- TME, setting a new performance benchmark in the European wireless market
- Strong brand equity
- Strong Sales and Distribution Network (>13,000 points of sale in Spain, >8,000 in LatAm)
- Extensive network providing access to our 78 million clients**

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* In the region of presence in each country
** Including CANTV
**Strong Financial Position (I)**

- Conservative investment strategy leading to the strongest balance sheet in the sector
- Diversified cash flow resulting in reduced volatility and superior credit rating
- Lower cost of debt: enhanced returns for equity investors
- Increased flexibility from strong cash generation & Balance sheet

*Telefónica is ready to capitalise on the sector’s weaknesses*

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**EBITDA by Geography**

- 1999:
  - SPAIN: 60.8%
  - BR: 10.5%
  - ARG: 13.0%
  - CH&PERU: 15.9%
- 2001:
  - SPAIN: 10.9%
  - BR: 10.9%
  - ARG: 11.3%
  - CH&PERU: 20.9%

**EBITDA by Business**

- 1999:
  - TEF: 14.4%
  - BT: 46.3%
  - TI*: 36.5%
- 2001:
  - TEF: 26.0%
  - BT: 35.2%
  - TI*: 40.3%

**Net Debt / EBITDA 2001**

- TEF: 2.3
- BT: 2.5
- TI*: 2.7
- DT: 4.1
- FT: 5.1

*Including Olivetti’s net debt; Source: Company’s Reports SSSB, ABN Amro*
**Strong Financial Position (II)**

*Cash Flow provides Flexibility*

**Cash Flow generation capacity would allow full debt repayment before maturity (6 years)**

**Capacity to invest in new opportunities**

### 2002-2007 Accumulated cash flow

- **EBITDA**
- **CAPEX**
- **Working Capital, net interest, taxes and other**
- **Cash available to shareholder**

### Improving Rio targets (Constant FX, 2ARS/US$)

- **Extra EBITDA-CAPEX from new Business Plan 02-05**

<table>
<thead>
<tr>
<th>Year</th>
<th>EBITDA</th>
<th>CAPEX</th>
<th>Working Capital</th>
<th>Cash available to shareholder</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>90.2</td>
<td>42.6</td>
<td>17.7</td>
<td>29.9</td>
</tr>
</tbody>
</table>

* Capex excluding UMTS licenses

** Source: Analysts estimates
Telefónica’s Strategic Vision: Current Focus
Corporate Strategy Drivers

Customers

- Individual Business Line aggressive capture of customer base
- Focus on profitable quality customers
- Build advanced commercial and marketing platforms for deeper segmentation and customer care

Financial

- Accelerated Growth Model
- Unlock value through disaggregation of Business Lines
- Profitable Growth Model
- Focus on ROCE and FCF

Services

- Fast build up of an Internet and Media/Content Franchise
- Lead the digital revolution through our Broadband Strategy leveraging on core Network and Content Assets

Geographic Footprint

- Lead Spanish and Portuguese speaking markets
- Build European presence
- Selective and results oriented multi-regional approach
  - Complete LatAm footprint
  - Opportunistic European participant
  - Selective expansion in Mediterranean Basin

Current Focus

- Selective and results oriented multi-regional approach
  - Complete LatAm footprint
  - Opportunistic European participant
  - Selective expansion in Mediterranean Basin
Customer satisfaction: our priority

**RECENT DRIVERS**

- Individual Business Lines encouraged to rapidly expand customer base

**CURRENT FOCUS**

- Focus on profitability and quality services for customers
- Build advanced commercial and marketing platforms for deeper segmentation and customer care

MILLION CUSTOMERS*

<table>
<thead>
<tr>
<th>Year</th>
<th>1999</th>
<th>2000</th>
<th>2001</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>56</td>
<td>68</td>
<td>78</td>
</tr>
</tbody>
</table>

CAGR 18%

* Including CANTV
Services: Embracing the Digital Revolution

The Digital Revolution

Traditional

Evolving from a connectivity to an application/solution provider

CONNECTIVITY

SERVICES

APPLICATIONS

CONTENTS & SOLUTIONS

Building market position for digital customer needs

- Wireline and Wireless Connectivity
- ... 
- Telephony
- Internet Access
- Videoconference
- VPNs
- ...

- Telephony
- Entertainment Applications
- Market Places
- VoD, PPV
- ...

- Networking Applications
- Corporate Applications
- ...

- ITC Integration
- Customised Solutions
- ...

Growth

Cash Flow Generation

- Infotainment & Entertainment
- Digital Home
- e-Company Transformation
- BroadBand Solutions for Corporations
- e-Administration
- ...

Evolving from a connectivity to an application/solution provider
Services: Leveraging on Internal and External Skills

New partnership model with external contractors to achieve closer alignment of objectives and reinforce Telefonica’s customer facing operations.

New Service development model through partnerships.

Set up a new Corporate Content Unit leveraged on Endemol and other assets.

**Contents** (Services and Applications)

**Access**

**Network**
Geographic Footprint: LatAm

Deepen Telefonica’s position in Latam and increase its contribution to the Group’s EBITDA

- Expand in new high growth potential markets where we are not incumbent (e.g., Brazil beyond Sao Paulo and Mexico):
  - Organic growth (e.g., Brazil 2002)
  - JVs (e.g., Mobile JV with PT in Brazil)
  - Acquisitions

- Constant improvements in efficiency through Active Regional Management

- Regional offering is a key competitive advantage
Geographic Footprint: Europe

• Spain: Maximising Cash Flow from existing businesses and defending competitive position by enriching the current portfolio with new Broadband Services

• The restructuring process of the European telecom sector will create new opportunities for Telefónica in the next few years

• Selective investments will allow Telefónica to capitalise on this restructuring process

• Leverage proven skills and current assets to enter new markets

• UMTS position outside Spain - minimise investment and open to options based on achieving attractive returns
Financial:

- INCREASE OPERATING EFFICIENCY
- EXCELLENCE IN CAPEX EXECUTION
- CLEAR INVESTMENT CRITERIA
- GROWTH IN CUSTOMER BASE
- GROWTH IN USAGE OF CURRENT SERVICES
- GROWTH IN NEW SERVICES
**Key business priorities to deliver profitable growth**

<table>
<thead>
<tr>
<th>2001 Results * (Eur mn)</th>
<th>EBITDA</th>
<th>Net Income</th>
</tr>
</thead>
<tbody>
<tr>
<td>T. LATAM</td>
<td>5,163</td>
<td>1,275</td>
</tr>
<tr>
<td>TdE</td>
<td>4,508</td>
<td>1,078</td>
</tr>
<tr>
<td>TEM</td>
<td>3,334</td>
<td>893</td>
</tr>
<tr>
<td>TPI</td>
<td>129</td>
<td>65</td>
</tr>
<tr>
<td>TERRA LYCOS</td>
<td>(232)</td>
<td>(566)</td>
</tr>
<tr>
<td>T.DATA</td>
<td>24</td>
<td>(486)</td>
</tr>
<tr>
<td>ADMIRA</td>
<td>153</td>
<td>(347)</td>
</tr>
<tr>
<td>ATENTO</td>
<td>54</td>
<td>(110)</td>
</tr>
</tbody>
</table>

- **Strengthen core business performance**
- **Capture growth opportunities profitably (particularly increasing penetration in LatAm and Broadband strategy)**
- **Crystallize the value of the positions Telefónica has developed**
- **Broadband as a contributor to continued improvement in results**

*Results from individual Business Lines
Increase Customer Revenues

Growth Customer Base
- Around 100MM Clients in 2004 Total
  - Over 13 MM BB Clients
    > 4.5 MM ADSL
    > 8.5 MM GPRS/UMTS

Growth in Usage of Current Services
- Proactive commercial initiatives to encourage growth in traditional services

Growth in new Services
- Rising ARPU mainly through our Broadband strategy

Total Switched Minutes
- CAGR 3-7%

ARPU
- BROADBAND
- TRADITIONAL

Financial:
Profitable • Growth

TdE, T-LatAm, and TME
**Financial:**

*Profitable Growth*

**Increase Operating Efficiency**

- Still room for improvement in LIS/Employee
- Improve OPEX to add efficiency gains

**2001 LIS/EMPLOYEE**

<table>
<thead>
<tr>
<th>LATAM</th>
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<th></th>
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</thead>
<tbody>
<tr>
<td>Telemar</td>
<td>1,287</td>
<td>1,287</td>
</tr>
<tr>
<td>TELESIP</td>
<td>1,198</td>
<td>1,198</td>
</tr>
<tr>
<td>Brasil Telecom</td>
<td>1,095</td>
<td>1,095</td>
</tr>
<tr>
<td>CTC</td>
<td>803</td>
<td>803</td>
</tr>
<tr>
<td>TASA</td>
<td>526</td>
<td>526</td>
</tr>
<tr>
<td>Tdp</td>
<td>471</td>
<td>471</td>
</tr>
<tr>
<td>Telecom Argentina</td>
<td>379</td>
<td>379</td>
</tr>
<tr>
<td><strong>TlatAm</strong></td>
<td><strong>804</strong></td>
<td><strong>804</strong></td>
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<table>
<thead>
<tr>
<th>EUROPE</th>
<th></th>
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<tbody>
<tr>
<td>TDE</td>
<td>505</td>
<td>505</td>
</tr>
<tr>
<td>TI*</td>
<td>448</td>
<td>448</td>
</tr>
<tr>
<td>DT*</td>
<td>428</td>
<td>428</td>
</tr>
<tr>
<td>BT*</td>
<td>354</td>
<td>354</td>
</tr>
<tr>
<td>FT*</td>
<td>253</td>
<td>253</td>
</tr>
</tbody>
</table>

* As of September'01
INVESTMENT PRINCIPLES

- Standalone risk adjusted returns required to be above the cost of Capital
- Seek control in acquired assets
- Clear opportunity to own the customer and sell expanding service portfolio
- Opportunity to leverage existing skills, assets and presence

Financial:

- Focus on extension of Latin American and European Markets with special attention to Brazil, Mexico, Western Europe and Mediterranean Basin
- Broadband connectivity key to expansion of service
- Improves competitive position, opens new growth markets, stimulates customer interest
- Own customers from day one - seek early cash generation
- Maximise return on capital through efficient operation
- Disposing assets with no strategic fit
In summary,

• Since we last met in Rio, we have delivered against an ambitious set of performance targets. The performance gap with our peers has widened

• We will continue building value by improving returns from our core assets and seeking and developing new sources of profitable growth

• Our track record, skills and financial strength give us confidence for the future

• You can expect a continued emphasis on superior management from us and a will to develop and grow our business

• Over the next two days we will have the opportunity to prove that our ambitions are based on solid fundamentals, a clear set of performance priorities and a talented management team
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