

Letter from the Chairman

Dear Shareholder:

The opening lines of the Annual Report should endeavour to briefly bring to life what those cold facts and figures illustrate in detail in the essential pages of the Company's records - the balance sheet and results. Furthermore, at **Telefónica** we are steadily reshaping our business strategies and corporate organisation to meet the challenges of a fast-moving marketplace. Hence, I shall devote these lines to sharing with you what I think we have already achieved and, above all, what we aim to achieve.

Since 1986 the external framework, within which **Telefónica** operates, has changed course more radically than ever before in our Company's lifetime.

The Telecommunications Bill (LOT) will bring sweeping changes in the regulations which govern the industry. In addition, a new tax law is soon to be applied to our Company, and a Private Television Act will be passed in the near future. All this implies that, from now on, nothing will ever be quite the same again.

What do these new circumstances mean? There will be more opportunities for greater profits and of course more risks may arise. We will have more freedom to succeed and less protection against mistakes. In other words, more responsibility for our own performance.

Are we ready for this new era? I have the fullest confidence that at **Telefónica** we are not only set to face these foreseeable changes but also, more importantly, to seize the opportunities which they provide.

I have two facts to back up this claim: the 1986 Financial Statements and our extensive decentralisation program.



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Our strong 1986 results are good news; I would even say that they are better than expected. This also reflects the steady upward trend of the Spanish economy. Having said this, I must add that this successful performance would have been impossible without the vigorous commitment to increasing efficiency of our workers and managerial staff. We are fully aware that **Telefónica's** accomplishments are the fruits of the joint efforts of 65,000 workers and over 700,000 shareholders.

Management and workers have set in motion an extensive market-driven reorganisation and decentralisation program. Provincial Managers will fulfill the essential role of running day-to-day operations and services, thus enhancing **Telefónica's** ability to identify and serve customers' needs efficiently.

Although we have not quite reached the point when **Telefónica** is seen to be a free competitor in the open market, the time will soon come.

I would add that, together with the pursuit of greater profitability, **Telefónica** should also undertake an overall transformation in its corporate culture. Shareholders may rest assured that we will meet this challenge.

On another note, I would like to take this opportunity to send my greetings to the many thousands of shareholders throughout Europe, America and Japan who participate in **Telefónica** and are an integral part of our success. For a company requiring huge financial resources in order to achieve its corporate goals, your support is of vital importance.

Today **Telefónica** is and intends to remain a worldwide corporation as far as shareholders and activities are concerned. To guarantee this, we are keeping to our «revolving holding company» policy, selling our stake in some industrial concerns while setting up promising new ventures in Spain and abroad. I am fully confident that this strategy will enhance the value of your investment in **Telefónica**.

You may rest assured that you are participants in a stronger and more efficient company, with greater prospects and a firm will to strive for ever better results.

It is not often that I can give you such firm assurance that the future has still greater rewards and corporate achievements in store, serving the public needs for the benefit of the customers, workers and shareholders of **Telefónica**.

Luis Solana
Chairman of the Board



