



LETTER TO SHAREHOLDERS

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ear Shareholder,

On previous occasions when I have had the opportunity to address you in this Annual Report, I have emphasized the irreversible nature of the arrival of competition and our constant preparation for this event. During 1995 the liberalization process of the telecommunications sector has followed its course and highly significant legislation has been passed, such as the Cable Telecommunications Law or the Decree governing Closed Users Groups. Last year a second mobile telephony operator also commenced its activity and this spurred us on in our efforts, at an even greater rate.

With great satisfaction I believe I can ensure you that Telefónica is ready to operate successfully in the competitive environment which already surrounds us. A large number of the new services provided by our Company are already competing in the marketplace. Perhaps for this reason and as evidence of my assurance to you, the 1995 financial results show a notable improvement both in turnover and quality, with no increase in service charges, in fact quite the opposite. The consolidated net income of the Telefónica Group, excluding the results attributed to external partners, reached the figure of 133,000 million pesetas, representing an increase of 18.2% over 1994. There was no cutting back on our constant efforts to restructure and we maintained

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our characteristic prudent and rigorous financial and economic management policy.

Given the further privatization of Telefónica, it could not be otherwise. The Public Sales Bid of 12% of the Spanish State holding in the Company, which took place last October, gave us the opportunity to make clear certain corporate policy commitments aimed at obtaining greater value for our shareholders. These commitments refer to the increase in revenue per line (thanks to the more intensive use of installation capacity and the extension of our services), the growth in productivity (including the adaptation of human resources to the real needs), the self-financing of the Group (one of whose essential ingredients is a rigorous policy of investment selection) and, finally, the dividend growth in accordance with the profits of the Group. In all these aspects 1995 has witnessed significant steps forward.

There is no doubt whatsoever that Telefónica has ceased for ever to look back to the past and has embarked on an ambitious project aimed at building firm foundations for the future. Thus, along with the major advances in mobile telephony, 1995 saw us finally join the Unisource alliance, which effectively integrates us into one of the major consortiums concerned with providing Paneuropean and global services.

One fact that I would particularly like to highlight is our increasing activity in the development and implementation of our services. In 1995 we managed to create a service every week, among them INFOVIA, our strategic bid for access to the information highways. However, we aim to intensify even more the growth rate of new services. It is here, through our steady efforts, trusting only in ourselves, increasing day-by-day our competitive strength, that we place the greatest hopes for our Company's prosperous future.

With kind regards,

Cándido Velázquez-Gaztelu Ruiz

Chairman of the Board of Telefónica de España, S.A.