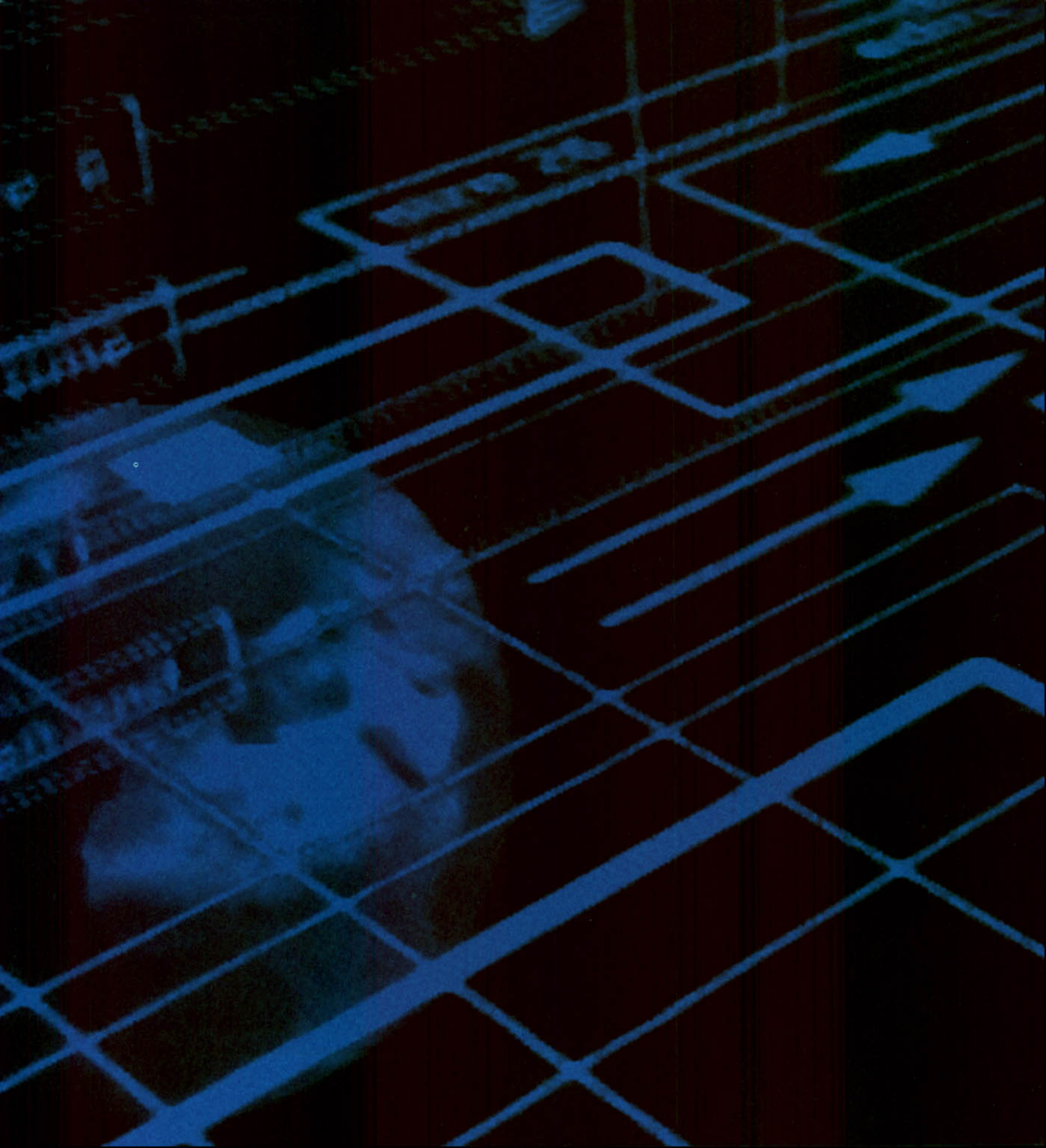


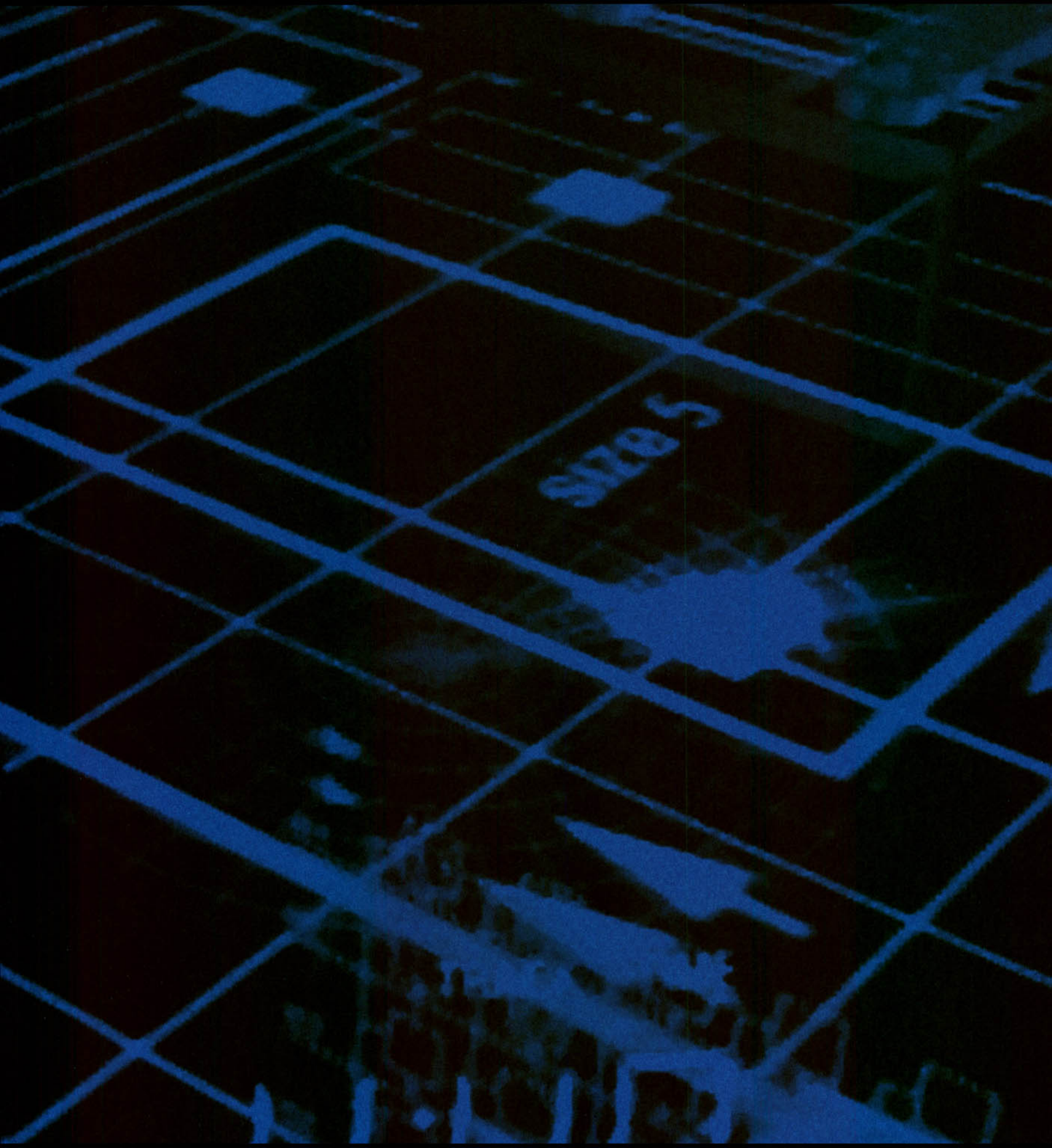
Telefónica

*Annual
Report
1997*



Telefónica





Annual Report
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Telefónica

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TELEFONICA GROUP: HIGHLIGHTS

	1993	1994	1995	1996	1997
Lines in service (thousands)	20,614.4	22,683.0	24,247.3	26,477.1	28,429.9
Basic telephony (1)	14,253.5	14,685.4	15,095.4	15,412.8	15,854.4
IBERCOM (1)	548.3	622.2	651.3	691.3	715.4
ISDN (1)	0.6	5.4	28.0	96.0	228.5
Abroad (2)	5,812.0	7,370.0	8,472.6	10,277.0	11,631.6
Cellular subscribers	419,543	726,242	1,375,519	3,329,398	5,053,404
MoviLine (analog) (1)	257,261	411,930	892,187	1,307,929	1,100,595
MoviStar (GSM) (1)	—	—	36,768	1,037,716	2,087,101
Abroad (3)	162,282	314,312	446,564	983,753	1,865,708
Cable TV subscribers	—	55,861	774,989	1,149,260	1,551,860
In Spain	—	—	—	—	—
Abroad (4)	—	55,861	774,989	1,149,260	1,551,860
Employees (5)	84,056	103,938	99,203	92,148	92,151
Revenue from operations (million pesetas)	1,297,437	1,578,850	1,740,557	2,006,058	2,363,102
Debt ratio (%)	53.1	49.8	47.9	44.7	47.3
Capital expenditure (million pesetas) (6)	445,274	810,655	663,851	867,197	1,231,326
Cash flow (million pesetas)	502,882	644,750	750,357	811,235	961,435
Net income (million pesetas.)	96,367	112,608	133,214	160,282	190,063

(1) Figures for Spain.

(2) Lines in service include those of TASA, CTC, Telefónica del Perú, CANTV and CRT.

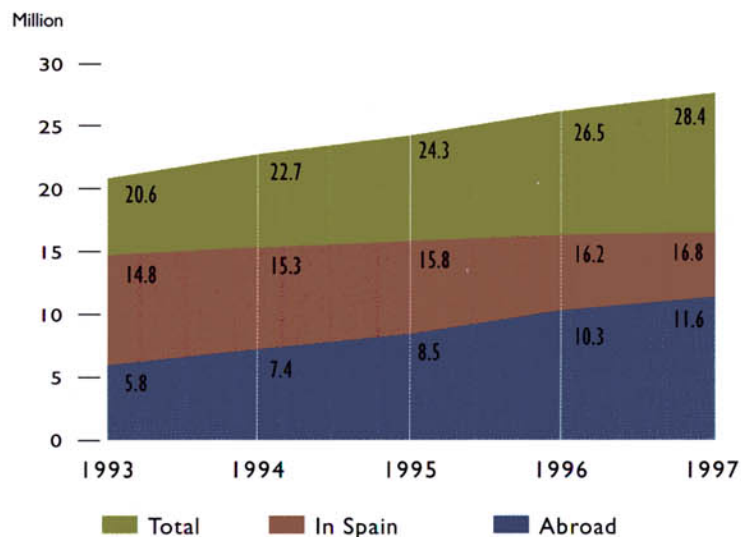
(3) Cellular subscribers included those of Cotelco and Telefonica Romania up to 1996. In 1997, these two companies are not included.

(4) Cable TV customers in 1997 correspond to CTC, Telefónica del Perú and Cablevisión Argentina. In previous years, Multicanal was included but not Cablevisión.

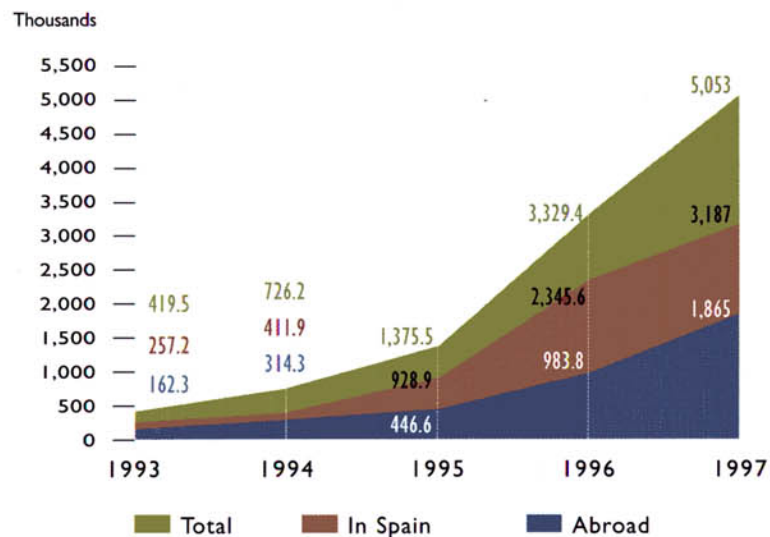
(5) Average number for the year. At year-end 1996 and 1997 the workforce totalled 91,389 and 92,022 employees, respectively.

(6) Tangible, intangible and financial.

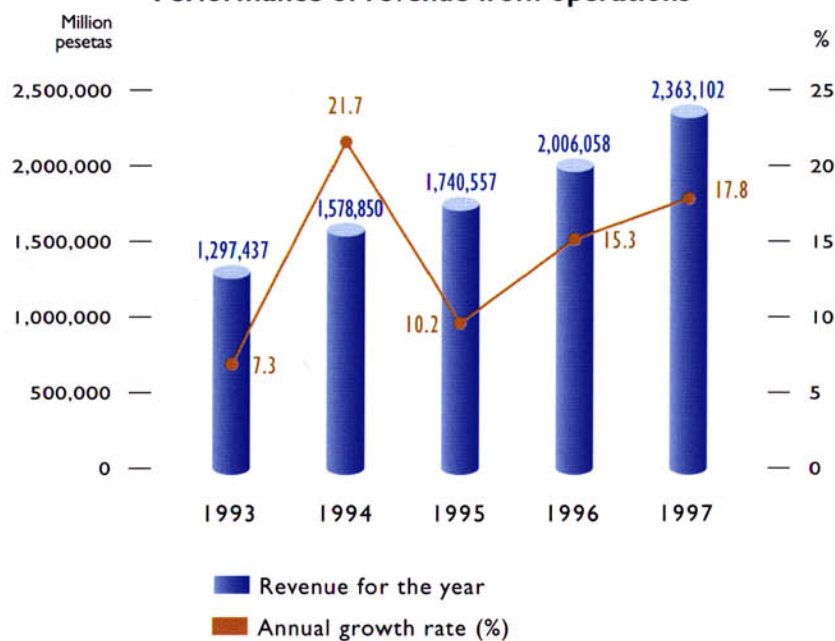
Performance of lines in service



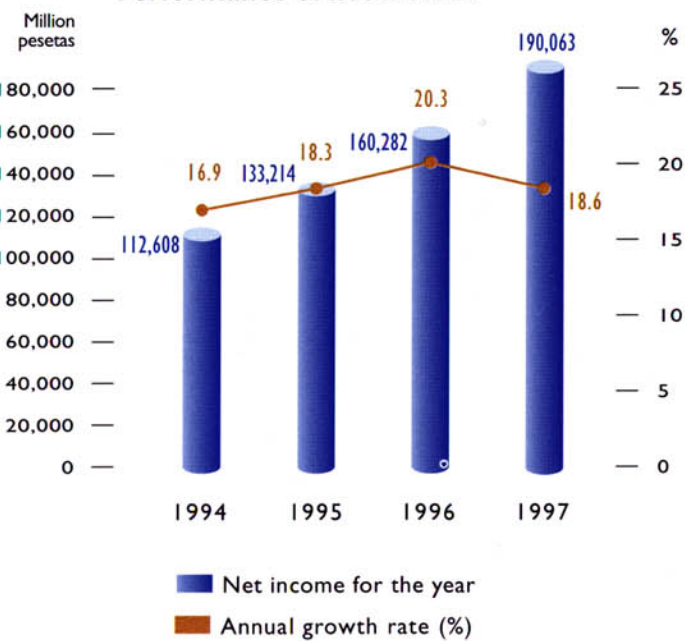
Performance of cellular subscribers



Performance of revenue from operations



Performance of net income





Telefónica

Letter to Shareholders

Dear Shareholder:

A YEAR AGO, WHEN WE TOOK OUR FIRST STEPS AS A totally privatized company, I spoke to you of my absolute faith in the **Company's** future and of our three-way commitment to our shareholders, our customers and to Spanish society in general.

A year has passed, and I take great satisfaction in telling you that we have every reason to be proud of being **Telefónica** shareholders. We form part of a **Company** whose share price has risen 44% over the year, and whose profits have grown 18.6% to reach Ptas 190,063 million. Throughout 1997, we have offered our customers an ever-increasing range of services and, at the same time, we have cut prices, and provided our society with a

telecommunications system that is modern, flexible and reliable.

We took on a three-way commitment and we have fulfilled our promises. We are Spain's leading enterprise in terms of revenue and market capitalization. We have 35.5 million customers in Spain and Latin America, making us the leading telecommunications operator throughout the Spanish-speaking world. We are moving into new geographical markets and, with the support of our international alliances, we are set to play an active role in the reshaping and expansion process that is under way in the communications sector throughout the world.



We want to establish ourselves as the world's fifth-ranked operator in the telecommunications field and therefore, by building on the solid foundations we have already laid, we have begun to move into new lines of business in the audiovisual sector, thus adding a totally new dimension to the relationship with our customers.

Our high levels of investment, coupled with our constant dedication to research and development, have enabled us to consistently offer improved services increasingly tailored to the needs of each of our customers.

We are contributing to the growth in competition and to the economic development of all the countries in which are present, by creating wellbeing for the general public and, through our policy of social support, by playing an active role in socially-oriented projects.

We therefore feel we have reason to be proud of the success and service capability of the company we own, but we must not be lulled by complacency. There are many important challenges ahead of us and our present achievements should spur us on to facing them with determination.

A time of great new opportunity and potential is opening up for the **Telefónica Group**, which will,

in turn, undoubtedly create additional value for our shareholders.

Spain is currently undergoing a transition period which will shortly culminate in the total liberalization of the telecommunications marketplace. **Telefónica** has no misgivings about the advent of competition, because we know how to act in a competitive environment, and we already work with a competitive spirit. We have shown this in Spain, in the field of mobile telecommunications, as well as in those countries where we operate in a totally liberalized market. This challenge brings out the best in us and spurs us on.

We therefore welcome competition with open arms, as we know that it pushes us on to bigger and better things. The only thing we insist on is that the rules of the game be clear, precise and fair for everyone, set by an independent and unbiased regulator.

Beyond Spain's frontiers, we intend to continue taking advantage of the excellent investment and growth opportunities offered by a region in constant expansion such as Latin America. This will enable us to sustain and increase the value created for our shareholders. In order to exploit these opportunities to the full, we will push

forward in the process of integrating the management of all the **Group's** operators.

We can be sure that throughout 1998, **Telefónica** will continue to progress in its aim to consolidate its leadership within and beyond Spain. We will not neglect the three-way commitment I mentioned at the beginning of this letter.

Our main objective is to create shareholder value, which can only be achieved through the expansion and nurturing of our businesses and the constant provision of a service that guarantees our customers the highest quality.

We would therefore like to express our gratitude to our customers, for the trust they have placed in **Telefónica**, and to the tens of thousands of people throughout the world who work for **Telefónica**. Thanks to them, we have become what we now are: a leading company in the telecommunications marketplace.



Juan Villalonga

CHAIRMAN OF TELEFÓNICA



ANNUAL REPORT

1997

1997 has been a year of particular importance in **Telefónica's** long history, with two events of outstanding significance marking the beginning of a new era: the total privatization of the Company's share capital and the progression towards the total liberalization of the Spanish telecommunications market with basic telephony opening up to competition in 1998.

The Public Offering of the remaining State-held shares was extremely successful, not only as a consequence of the performance reflected by the share-price, but also due to the broadening of the Company's share base, which witnessed the incorporation of more than a million new shareholders.

Telefónica now ranks as Spain's leading wholly-privatized operator, providing global telecommunications services and dedicated to leading a sector open to competition and whose presence on a worldwide scale is of ever-increasing importance as it is becoming one of the principal creators of economic activity, generating wealth and employment.

When considering deregulation, mention should be made of the appearance of a second operator in the arena of voice telephony, as well as the setting of December 1st 1998 as the date for the total liberalization and opening up of the Spanish telecommunications market, combined with the establishing of a calendar for the granting of new licences for mobile and basic telephony, in addition to those already in existence and those still to come in the cable TV sector.

Attention should be drawn to **Telefónica's** particularly strong support of the rapid progress towards a totally liberalized European community for two reasons: firstly, for **Telefónica** to be fairly compared with other leading European and worldwide operators and to avoid any regulatory bias during the transition period of the duopoly.

The situation that **Telefónica** faces is not new. The **Company** has faced competition in numerous countries and in the liberalized sectors in Spain itself, so with this



**Telefónica is unshakeably
in favour of rapid progress
towards a totally liberalized
European community**

knowledge and experience behind it, it is more than capable of facing this challenge with confidence and optimism and maintaining its longstanding commitment to its shareholders, customers and society in general.

Telefónica's role as a global operator is reflected in both its international expansion and in the provision of its transnational services, as well as the diverse range of services it offers, which can be grouped into three basic categories: traditional business lines, interactive and multimedia communications and audiovisual businesses.





TRADITIONAL BUSINESS LINES

The traditional line of business for a telecommunications operator such as **Telefónica** is that of basic telephony, which continues to be of vital importance in the profit and loss accounts. Due to the tariff rebalancing introduced, this business segment continues to more than hold its own in the face of the imminent opening up to competition. This is clearly reflected by those markets already open to competition (data transmission and mobile telephony, for instance), in which **Telefónica** holds a position of leadership. Throughout 1997 a great effort has been made to increase the Company's flexibility, through its market focusing, the reining in of costs, a greater degree of competitiveness, and an enhanced capacity to offer its customers global solutions at the right price and with a heightened degree of efficiency.



The Residential Market

The strategies applied in the Spanish and Latin American markets differ due to the difference in the maturity of these markets. The prime objective in Latin America is that of enhancing market penetration, as this is an area that still offers considerable development opportunities which will enable the expansion of its customer base. In Spain, where almost the whole population is provided service coverage, **Telefónica** focuses on increasing average usage per line, through the introduction of new services and the promoting of second lines.

Telefónica is answerable to an overall figure of more than 20 million residential customers, small businesses and business people. Of this figure, more than 12.5 million reside in Spain, where, in 1997, traffic volume grew by around 5.5% to reach 10.1 minutes per line per day. This increase was a result of the introduction of new supplementary services, the 72% growth in the number of calls made from the fixed network to mobile telephones, the significant 360% increase in incoming **InfoVia** traffic, and the tariff cuts introduced.

**The tariff rebalancing
in our basic telephony business
allows us to guarantee our success
in the liberalized marketplace**



The Telefónica Group addresses the needs of more than 20 million residential customers, small businesses and business people

The strategies for Spain

The strategies applied in the market aimed at the **Retail Customer** are founded on the constant study and awareness of the needs of our customers, in order to offer made-to-measure solutions to their requirements. Proof of this is the recently introduced complete customer-care service which further enhances the 24-hour technical assistance provided, at the same time as advising our customers on how to benefit from our services.

One particular feature of this strategy is the new basic service concept of a "new telephone line" which offers additional applications, most of them included in the monthly subscription charge, such as the **Network Answerphone** service which is now used by more than half our customers.

The introduction of these supplementary services, which also include **Call-Waiting** and **Call-Rerouting**, has resulted in 500% growth compared with 1996, with more than 6.5 million customers now taking advantage of some of these services. Throughout 1997, measures were taken to offer a complementary line of services based on the identification of the caller which has opened up a whole new range of possibilities.



Tariff cuts were also introduced in Spain with a view to promoting traffic. Interprovincial call prices went down twice over the year: the first price cut taking place in April which reduced the tariff by an average 5%, only to be followed by another 5% cut in July. International call prices went down an average 8.8% and several basic telephony charges were also reduced, such as change of residence, temporary suspension of service, etc. Regarding second lines, our marketing campaign based on a 43% cut in the subscription charge, resulted in the installation of 315,000 second lines.



Not only was the residential market given additional services and tariff cuts, it was also offered specific packages which further increase the appeal of the basic service. With the suggestions and needs of our customers once again in mind, September witnessed the launching of the **Personal Plans** (provincial, interprovincial and international) which enable greater usage of the telephone service under extremely competitive conditions. These made-to-measure products have been very well received by our customers.

At the beginning of 1998, **Telefónica** launched its “**Clear Plans**” package, which combines a number of products and services related with the new telephone line which includes all the digital services available, along with the new integral maintenance service, etc..., as well as **Discount Plans** for the elderly, young people, families, international calls and housing communities which is just a taste of the things to come throughout the year.

1997 has seen the implantation of the technical developments necessary to introduce the **New Numbering Plan**, which will be launched in Spain on April 4th of this year, and which will increase the number of digits in each telephone number to 9. This will offer the market important development possibilities as it will greatly increase the capacity to assign numbers and in turn heighten the diversity of the services on offer.

Work on the network has been completed by which all the lines can receive **Itemized Billing**, therefore achieving the much strived for objective of increasing the clarity of this information, which has also been improved by the introduction of new applications which permit such things as being able to find out the consumption registered in real time since the previous bill.

The new commercial policy

The area **Retail Clients** has launched a new customer-care programme aimed at offering our customers the highest degree of efficiency possible. Throughout 1997, contact with our customers grew considerably, resulting in a 30% increase in the number of commercial operations carried out.

This new programme is based on the following:

- ♦ The customer-care line 004, which offers direct attention, by telephone, using which the customer can purchase or subscribe to a diverse range of products and services, inquire about these same products and services, place complaints and register line faults, 24-hours a day, 365-days a year. 1997 doubled the number of calls received by this service in 1996.
- ♦ The **Tiendas Telefónica** (Telefonica Shops) are where our customers are made aware of and can try out the whole range of services and products **Telefónica** offers. In 1997, 94 shops were opened and this service will continue to expand in 1998. **Telefónica** services and products are also sold in many of Spain's principal department stores.

**Our made-to-measure solutions
to our customers' needs make
for the competitive usage
of the service**



- ♦ **Telefónica's Virtual Store**, which can be accessed through **InfoVía** and Internet to make inquiries or subscribe to the services and products offered by **Telefónica**.

- ♦ **Catalogue Sales**, using which the customer, who has previously received our catalogue, can acquire or subscribe to any of the products or services on offer by simply making a free-phone call to the customer-care service, and these will be delivered at no extra charge.

1997 witnessed not only the launching of the **Customer-Care Centres** and **Technical Assistance** service, but also the creation of a new line of specialized after-sale products and services which will appear in the market in the course of 1998 and will allow us to satisfy the specific demands of certain segments of our clientele.

The Corporate Market

The complete and personalized
attention offered to our customers
is the key to gaining
their loyalty

Regarding our corporate clients the commercial strategy is based on the following aspects: the optimizing of the price structure; made-to-measure solutions; single, global and itemized billing; the creation of offers aimed at specific segments; complete and personalized customer attention as a key element in the procuring of their loyalty; and, the defining and promoting of integral services based on the solutions offered by **Telefónica** and its technological partners.

Corporate Clients

1997 saw the **Ibercom Service** expand within the **Corporate Clients** market, through the launching of new services and marketing. **Telefónica** has greatly improved its range of applications through such new services as **Ibercom Leasing**, **Ibercom Master**, the development of **Ibercom ISDN** or the launching of its **Call Center** for queries. Regarding data communications, the **Data&Voz** service, integrating voice and data, has been further improved, and it is now possible to migrate from the **Ibertex** service to **InfoVía**.



In leased circuits the migration from analogue to digital circuits has been promoted, as has the possibility to migrate to higher speed circuits, improving quality and optimizing costs.

Thanks to the consolidation of our **Integral Customer-Care System (SGIC)**, customers have begun to use **Telefónica's** new information highways. Using **InfoVía** and Intranet, which guarantee confidentiality, our customer can place orders, make inquiries and access information about his business from his own home or workplace.

To inform our customers about all the information systems on offer, we have created a **Corporate Customer Care Centre** which, through the dialling of a single access number provides our customers with information on all the commercial and technical contact points.

Small and medium-sized companies (PYMES)

With the small and medium-sized company in mind, specific programmes have been developed to offer this vital segment of the Spanish economy made-to-measure solutions to their needs. The **PYMES Selection Programme**, which includes the principal members of the PYMES segment, offers personalized attention to our customers; its commercial channel, **Canal Indirecto**, has been strengthened, now offering a network of 150 distributors; the **Consultor** programme has been launched, providing advice free of charge to thousands of small and medium-sized Spanish companies in order to improve their competitiveness through telecommunications services; principal hard and software manufacturers also collaborate with **Telefónica** in order to promote and offer advice on the benefits of using information and communication technology.

Regarding the commercial relations with other network operators, Interconnection Services continued to be developed throughout 1997 as a result of the entrance of new mobile telephony operators and a interconnection agreement was also formed with the second fixed telephony operator.

International telephone traffic

The international traffic carried by **Telefónica** during 1997 reflected significant 20% growth compared with the previous year. This growth comes as a consequence of the economic recovery, which began at the close of 1996, combined with the favourable performance of tourism and the cuts in international tariffs.

Throughout the year, discount packages on international traffic continued to be offered, of which two are particularly outstanding; **Masterbono I and II**, in addition



Thousands of small and medium-sized companies receive advice and information free of charge to assist in the enhancing of their telecommunications service and increase their competitive edge

**In under a year international
communications tariffs have been
cut by 20%**

to the packages already on offer: **Masterbono Básico Internacional** and **Masterbono Megavip Internacional**.

Regarding the interprovincial discount packages, the trend has been similar to that of international discounts in line with the relevant regulatory framework, with several proposals having been made to the corresponding regulatory authorities.

Continuing the tariff strategy drawn up the previous year, an average 8.8% reduction was introduced on international tariffs on March 15th, 1997, reflecting a global reduction of 20% in less than a year.

Data transmission

Data transmission services are provided by **Telefónica Transmisión de Datos**, within a sector that has been open to competition since 1995. This company acts as its customers' technological partner offering made-to-measure solutions to their data communication needs. In 1997 **Telefónica Transmisión de Datos** withdrew from Unisource to become totally integrated in the **Telefónica Group**. From now onwards **Telefónica Servicios Avanzados de Información** and **Telefónica VSAT's** commercial strategies will form part of those of **Telefónica Transmisión de Datos**.

The quality of our customer care has improved considerably since the inauguration of the new **National Control Centre (CNC)**, which is responsible for monitoring the network 24-hours a day. The pace of development and launching of new services has been stepped up, and those services with greatest value-added, those that integrate voice and data (**CINCO, DataVoz**) or network interconnection services such as **LAN (InterLan)**, have now gained customer critical mass.

Telefónica VSAT has continued to hold its position of leadership in the corporate communications via satellite market. This type of communications was liberalized at the beginning of 1997. The presence of new operators with licences to transmit via satellite has served to spur **Telefónica VSAT** in its aim to achieve global connection capability and to improve its service quality, as this is the only road to success in this highly competitive market.

Infrastructures

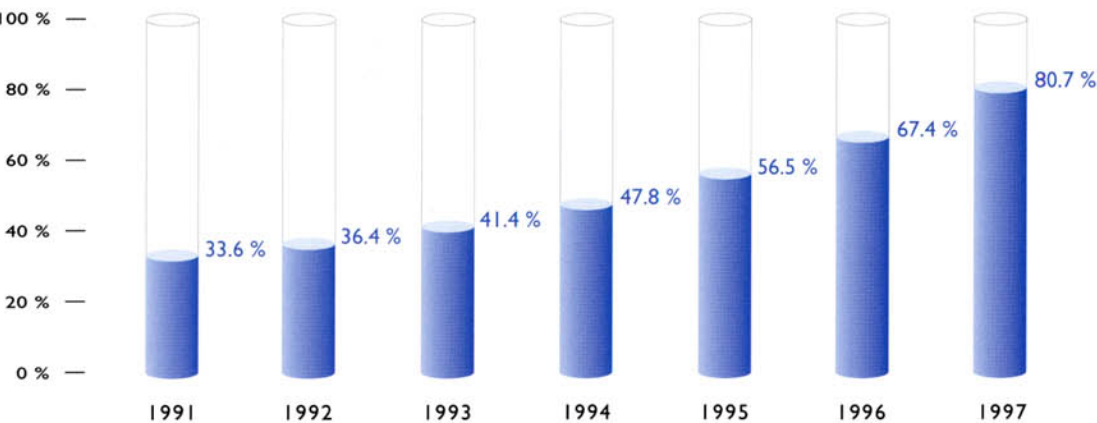
Our infrastructures are undergoing profound changes, on the one hand in order to adapt to the new competitive environment, and on the other, in order to introduce the technical advances necessary to be able to offer new services with the highest degree of quality.

Regarding switching technology, our digital exchanges have been brought up to date to comply with the regulations laid down by the regulatory authorities regarding the **New Numbering Plan** which will introduce 9-digit telephone numbers throughout the whole country and permit the choice of operator.

With regard to the transmission technologies, the first wavelength division multiplexing has been installed which quadruples the carrier capacity of optic fibres, therefore raising the number of telephone channels from 30,000 to 120,000. Proposals are also being considered that would raise this figure to one million telephone channels.

Latin America will have a fibre optic
underwater cable network
with state-of-the-art transmission
technology

Network digitalization



International communications with America have particularly benefited in 1997 from the signing of important international agreements to construct two underwater cable systems, which will begin to operate in the area of the Atlantic Ocean in 1999; these being the **ATLANTIS-2** that will connect Spain and Portugal with Argentina and Brazil, and the **COLUMBUS-3** that will link Spain, Italy and Portugal with the US. These two projects will result in the creation of a ring fibre optic underwater network around the South American continent, provided with state-of-the-art transmission technology and the most advanced maintenance systems, capable of adapting to both traditional and new future developments based on multimedia applications.

1997 witnessed the consolidation of the interconnection structures between **Telefónica de España's** basic telephony network and that of the mobile telephony operators, offering a maximum degree of efficiency and paving the way for the interconnection with Spain's second fixed telephony operator's network.

With an aim to taking maximum advantage of the carrier possibilities offered by such new technologies as ATM and Internet Protocol, at the same time as strengthening **Telefónica's** competitive position in terms of information access services, a new network development model has been designed by **Telefónica**, based on ATM and IP nodes, to provide integrated global and multiservice capabilities.

The multiservice access networks foresee the introduction of interactive multimedia services on different band widths

It should be underlined that a great effort has been made throughout the year regarding the multiservice access networks, both in terms of technological improvements, and in terms of the designing of network structures, as innumerable new opportunities are opening up as a result of the interactive multimedia services on different band widths. With this in mind, new solutions have been found for the distribution of analog cable TV, along with the necessary elements needed to create a platform for the distribution of digital cable TV and interactive services. Pilot schemes have also been launched to test the possibilities of offering telephony, high-speed data transmission and video-on-demand through the optic fibre networks, along with the testing of advanced solutions for the transmission of high-speed signals (above 2Mbit/s) using the customer's wire loops.

The tests carried out using radio systems should also be mentioned as these fulfill the needs of fixed access, at the same time as offering a greater selection of services and applications.

More than 1,147,000 kilometres of land optic fibre cable has been laid since this technology was first introduced, providing all types of services.

In November the new **National Monitoring and Operating Centre (CNSO)** was inaugurated. This Centre will be responsible for the monitoring, operating and maintenance of all **Telefónica's** networks and services. This same building will also house the main after-sales centres for corporate clients.

Within the systems that will come under the responsibility of the **CNSO**, that of the **Monitoring System for the Signalling Network (SSRS)** will also be included. This system gives information in real time regarding any malfunction in this network, which is commonly known as the **Telefónica** network's "nervous system".

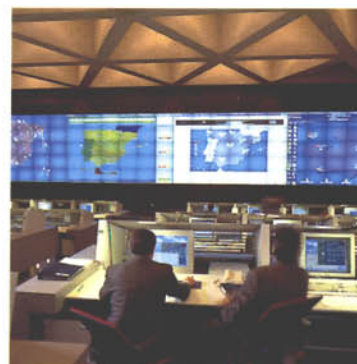
Regarding **Telefónica's** international service, there are four digital exchanges, five centres for satellite communications and 74 earth stations equipped with access to the different satellite systems (Intelsat, Eutelsat, Hispasat, Panamsat etc.); the Company also has 29 underwater cable stations of which 13 are exclusively dedicated to underwater cables, at the same time as participating in 53 underwater cables of which 23 are moored in Spain.

In December the installation of the **ATLAS System** was concluded throughout the whole of the Spanish territory. As a consequence, one single system is capable of providing all kinds of circuits, for both customers and trunks among exchanges, which operates using one central database.

This system centralizes applications and therefore shortens the time needed to provide the service, which naturally strengthens **Telefónica's** competitive edge in terms of leased circuits, which are, at the same time, a vital tool for the the optimizing of the investment in the plant.

Following the policy initiated a few years ago in preparation for the need to compete in new markets, **TEMASA (Telecomunicaciones Marinas)** has continued to invest in tools and equipment such as the submersible **NEREUS**, which is considered to be the most advanced tool of its kind. The acquisition of two more cable-laying ships is also currently underway in order to gain a foothold in the maintenance market covering the South American Pacific, and to increase our competitive edge in the installation marketplace where many possibilities are opening up.

The new National Monitoring and Operating Centre provides a global views, in real time, of all Telefónica's networks and services



The R&D strategy
is market-focused enabling
us to address the services
and solutions demanded by today's
telecommunications

Research and development

The **Telefónica Group's R&D** strategy is one totally oriented towards the market, so that the **Group** is unfailingly able to offer the necessary telecommunications services and solutions to cover the market's requirements. One example of these services is that of the new version of **InfoVia**, with another being the availability of reliable and sturdy infrastructures that amply cover the demands of both the residential and corporate customer for Internet and on-line services. Yet another example is that of the development of the **Advanced Personal Card** service and also the **One-Stop-Shopping** service for the retail customer.

In 1997 the development of the **Operation and Maintenance Structure** was finalized which was a major contributor to the creation of the **National Monitoring and Operating Centre (CNSO)** and the development of the **Operating System for the Signalling Network** previously mentioned, at the same time as contributing to a new version of the **Traffic Monitoring System**.

Other products have been developed for the **Telefónica Group's** companies, such as the **Customer-Care Centre**, the **Answerphone Service** and the **Centre for the Monitoring** of brief messages belonging to **Telefónica Móviles**, as well as other products for **Telefónica Transmisión de Datos** and **Telefónica Multimedia**.

Mobile services

1997 has once again been a year of significant growth in the mobile communications marketplace, where **Telefónica** now has over 5 million customers of which 3.2 million derive from the Spanish market and 1.8 from Latin America.

At year-end 1997, **Telefónica Móviles** had 3,187,696 active mobile customers in Spain, of which 2,087,101 subscribe to the **MoviStar** service and 1,100,595 to **MoviLine**. In total these two services have gained the net figure of 842,051 new customers, 36% up on the figure for the previous year, and placing us fourth in the European ranking. Although the most outstanding feature is that **MoviStar** has doubled its customer base, at the same time as doubling its nearest competitor's net customer increase.

The following information should give some idea as to the performance registered by the **Telefónica Móviles Group**:

In 1997 MoviStar doubled
its customers in Spain as well
as doubling its nearest competitor's net
customer increase

TELEFÓNICA MÓVILES GROUP HIGHLIGHTS

	1997	1996	Increase
Operating Revenues (mill. ptas.)	362,938	258,882	40.2 %
Pre-Tax Income (mill. ptas.)	38,982	21,109	84.7 %
Capital Expenditure (mill. ptas.)	100,203	140,997	-28.9 %
Total Assets (mill. ptas.)	400,459	352,744	13.5 %
Carried Calls (mill.)	2,954	1,684	75.4 %
Base Stations	4,968	3,504	41.8 %
Sales Outlets	9,200	6,600	39.4 %
Celular Customers	3,187,696	2,345,645	35.9 %
Mensatel Customers (Paging)	344,689	56,125	514.1 %
RadioRed Customers (Trunking)	17,612	8,906	97.8 %
Basic Telephony with Cellular access	238,626	222,260	7.4 %
Employees	2,377	1,831	29.8 %
Subcontractors	2,274	1,827	24.5 %

Operating revenue has grown by 40.2% to reach Ptas. 363,000 million. Pre-tax income has been even more spectacular having almost doubled the figure for 1996 to total almost Ptas. 39,000 million.

At year-end, the company was responsible for net fixed assets amounting to Ptas. 400,000 million, subsequent to the Ptas. 100,000 million investment made during the course of 1997, placing the accumulated figure invested by **Telefónica** in Spain's mobile service at Ptas. 464,000 million.

The traffic carried by our mobile networks has reached almost 3,000 million calls, reflecting 75% growth compared with 1996.

By and large, these achievements derive from the continuous effort made to satisfy our customers, applying three main principles: **Commitment to Quality, Innovation Capacity and Customer Care.**

Telefónica Móviles was the first mobile services operator in Spain to be awarded the AENOR ISO 9001 quality certificate. Since then quality has been a priority, with improvement processes being constantly introduced in all areas and throughout all the Group's companies, as is the case of **MensaTel**, which was awarded the ISO 9002 certificate in 1997.

Quality, innovation and customer care are the keys to our success in mobile telephony



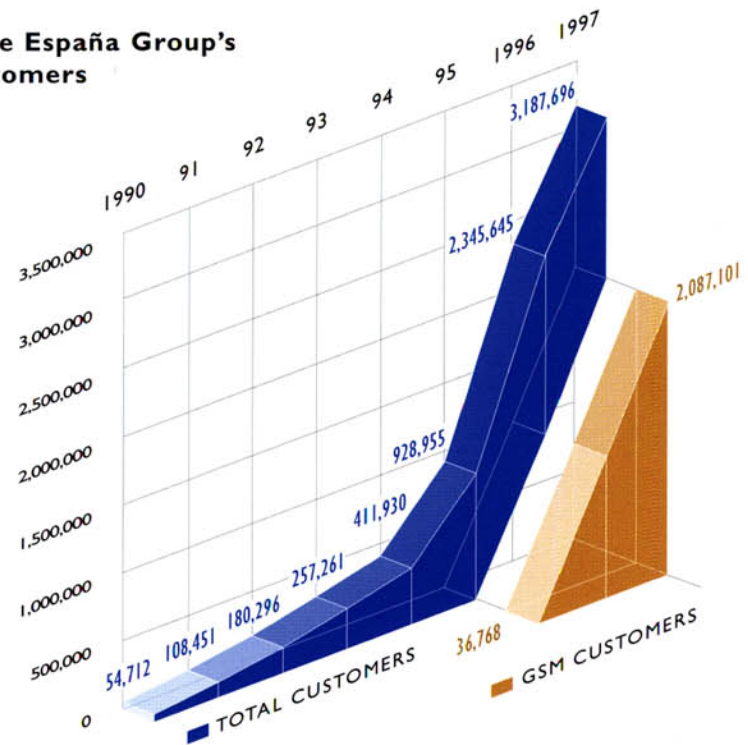
Telefónica Móviles has the most extensive international roaming for GSM networks

In line with our **Quality Commitment**, and in accordance with the firm belief that our customers measure quality in terms of coverage and the degree of efficiency offered by the network, **Telefónica Móviles** has installed over 1,500 new base stations, raising the total number to 5,000.

Although it is easy to measure the tangible commitments achieved, those that are not so physically obvious should not be forgotten, such as our pioneering of the total coverage of the city of Bilbao's subway system, or the total coverage provided along the whole high-speed (AVE) railway line between Madrid and Seville and also along local train routes around Madrid, as well as improving the coverage inside buildings and underground car parks in major cities.

In terms of international coverage, **Telefónica Móviles** provides the most extensive offer due to its GSM roaming agreements with 106 foreign operators. Its customers can also take advantage of the **Americas Service** which covers 10 countries in the American continent that do not use GSM technology or the **Global Service** that gives

Telefónica de España Group's cellular customers



worldwide coverage via satellite or, finally, the **Roaming Service** for **MoviLine** customers that travel abroad.

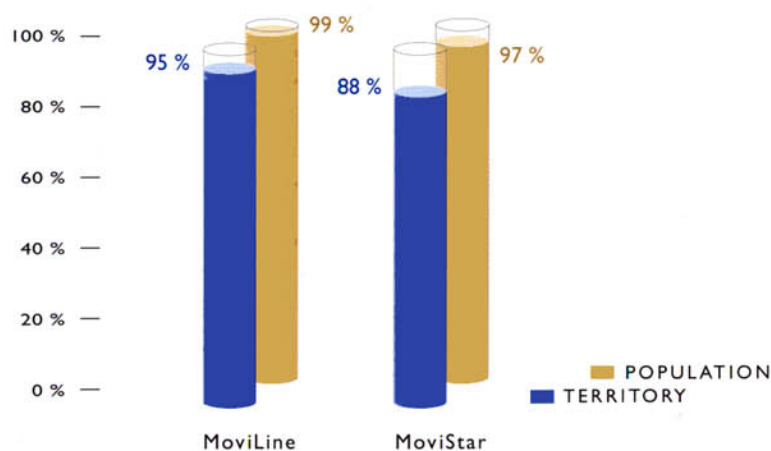
Our **Innovation Capacity** is one of continuous market-focus, which has so far resulted in the launching of almost 100 services and products, of which 39 were presented simultaneously at the state-of-the-art technology fair SIMO 97 held in November, without doubt representing Spain's greatest qualitative leap forward in terms of mobile telephony.

In February the first rechargeable pre-paid telephone card **MoviStar Activa** was launched, to address the clear need for a service that does not require any form of contract or monthly charges. The response to this service has been overwhelming, as by the end of 1997 almost half a million cards were in service. **MensaTel**, the company that operates the radio-paging service, has been the first entity in Spain to offer the **MensaTel Beeper** service which appeals to a high usage segment of the market. MensaTel, who already held the leading position in Spain's radio-paging market, has doubled its market share through the focusing on a new market area, young people. Finally, **RadioRed**, the only provider of **Trunking Services Operating** throughout the whole country, doubled its connections in 1997 thereby raising its market share to over 70%.

More than 100 new mobile telephony services and products have been developed throughout the year



MoviLine and MoviStar coverage at December 1997





With regard to **Customer Care**, steps have been taken to offer our customers a service that is both personalized and segmented. Our free-phone **Customer-Care service** which is open to our customers 24-hours a day, 365 days of the year, has enhanced its capacity through the opening of a new centre in Barcelona, designed to attend to 50% of all the calls made throughout the country.

Public Telephony

The Telefónica Group manages
more than half a million
public telephones, of which 300,000
are in Spain



The **Telefónica Group** is responsible for half a million public telephones. In Spain alone there are more than 300,000. **CabiTel** is now, without a shadow of a doubt, the leader in Spain's public telephony market. In 1997 over 5,000 new telephones were installed in public thoroughfares, bringing the total figure for this market segment to more than 63,000, all offering modular technology. In Latin America, the plant in service exceeds 175,000 terminals. These figures are complemented by the number of indoor public telephones on private premises which has continued its growth trend. Reference should also be made to the new **Tarjetel** telephone which offers the most advanced solution to telephone communications in hospitals.

Regarding forms of payment, telephones have continued to be adapted to accept the electronic cash-card, over and above the existing facilities for **Telefónica** pre-paid cards and credit cards. The sale of pre-paid cards rose 11.42%, demonstrating the favourable outlook for this form of payment.

Advertising and Information

In the sector dedicated to the production of yellow pages directories and classified advertising, the **Telefónica Group** has published over 30 million copies of **Yellow Pages** and **Directories** in 1997 and is also immersed in the electronic aspect of this market, CD ROM and, above all, Internet.

Telefónica Publicidad e Información (TPI) is the company responsible for the development and marketing of directories along with the distribution of information and advertising services in Spain. **TPI** has redesigned its principal product, **Yellow Pages**, gaining, as a result, value added, at the same time as compiling, printing and distributing **Telefónica's** telephone directories. This position confirms the company's leadership

in this sector, with more than 14,400,000 copies of **Yellow Pages** and 6,350,000 of **Directories** published in 1997.

Likewise, over the past year, **TPI** has consolidated its role in the multimedia market, through the launching of **Multimedia Yellow Pages**, the establishing of the subsidiary, **Doubleclick Iberoamérica** responsible for advertising space in Internet, and the agreement signed with Altavista (Internet's principal browser vehicle) in order to offer the same service in Spain.

Not only does **TPI** base its success on the development of its business but also on other business aspects, taking advantage of new technological possibilities, like the development of new products and the international expansion of its operations.

Telefónica Publicidad e Información
is fully immersed in the multimedia
environment





MULTIMEDIA ACTIVITIES

The interactive multimedia services are going to become one of the most important items in the profit and loss accounts if the exponential growth shown by on-line applications is anything to go by.

The Spanish market has 535,000 lines that use **InfoVía**, 149% up on the figure for the previous year. This growth means that the number of calls and connection hours registered has risen five-fold. In 1997 **Telefónica** began work on the new Red IP network (Internet Protocol) which will begin to operate, in its initial phase, in 1998. This new platform will enhance **InfoVía's** competitive edge, offering new access services and the exchange of information that will take greater advantage of the potential offered by Internet technology within a new regulatory framework for access services.

In order to adapt this new offer to the different user segments, two specific service packages have been created, one for corporate needs and the another for retail customers.

UNO-IP Corporativo includes carrier and value added services (professional electronic mail services, Web Hosting...) which cover the needs of companies wanting to create virtual Intranets, this being a natural evolution of the **UNO** service, as this is under high demand in this market segment, as well as the needs of information service and access to Internet providers.

InfoVía Plus is the service aimed at the retail customer, which, besides including the traditional on-line services (WWW, E-mail services, news groups), also offers the most recent developments such as à la carte information and audio and video IP.

The calls and connections hours registered by InfoVía have increased five-fold

In 1998, the new Red IP network will become operative improving the capacity of the Internet access services





The advances made in the on-line services resulted in **Telefónica Servicios Avanzados de Información (TSAI)** launching a 100% operative commercial electronic platform through such services as **Infomall** (a virtual shopping mall) for the promoting of transactions between consumers and virtual retail outlets, and **EdiRed** (the EDI service through Internet) for business transactions among companies. In this way, **TSAI** offers a complete electronic commercial service, as its **EDI Compensation Centre** has been recognised by the Spanish Tributary Agency as qualified to provide electronic billing.

1997 also witnessed the strengthening of **TeleLine**, the Spanish-speaking on-line service belonging to **Telefónica Multimedia** which offers more than 6,000 pages of information and programming exclusively for its customers. Throughout 1998 our objectives will follow a similar course, increasing the number of channels on offer, as well as the information provided, the number of databases and the new services exclusive to our customers, in which quality, the Spanish language and their interactive nature will be of prime importance.

ST Hilo, the **Group** company renowned for its **Hilo Musical** service, has launched a new business line with the production of digital channel broadcasting with CD quality. These channels can be transmitted via both satellite and cable networks, offering 70,000 different types of subject matter and 6,000 hours of digital music.

Audiovisual Businesses

Over the past few years technological advances have permitted a technological convergence and the appearance of interactive multimedia services. As a consequence, the members of diverse industries have come together to compete within the same information hyper-industry, in which the provision of content is becoming an ever-more important business line.

In 1997, **Telefónica** took up an active role in this arena, with two main objectives: on the one hand, the Spanish-speaking market and, on the other, the preparing and distribution of audiovisual content, with particular attention being paid to the 35 million existing customers and the market potential of raising this figure to 200 million.

This market-focused strategy allows **Telefónica** to apply its considerable knowledge of commercial relations and its extensive partner network to the development of

Investments in audiovisual developments represent a foothold in the future coming together of telecommunications and entertainment services

the new business opportunities opening up, benefiting both our shareholders and the Company's partners, at the same time as taking advantage of our know-how in Spanish-speaking markets.

It must also be remembered that these investments represent a foothold in the future coming together of telecommunications and entertainment services.

Within the industry's value-chain, **Telefónica** will focus its efforts on the packaging and distribution of programmes, along with taking an active role in mass audience TV stations both in Spain and Latin America.

Distribution, be it by way of physical carriers such as satellite systems, or cordless networks, represents a natural form of development for **Telefónica's** basic capacities, providing clear synergies and allowing us to take advantage, not only of our tangible assets but also of what could possibly be considered our most valuable asset, our customer relations. The installation of earth digital television is going to mean the opening up of a clearly obvious business opportunity for us.

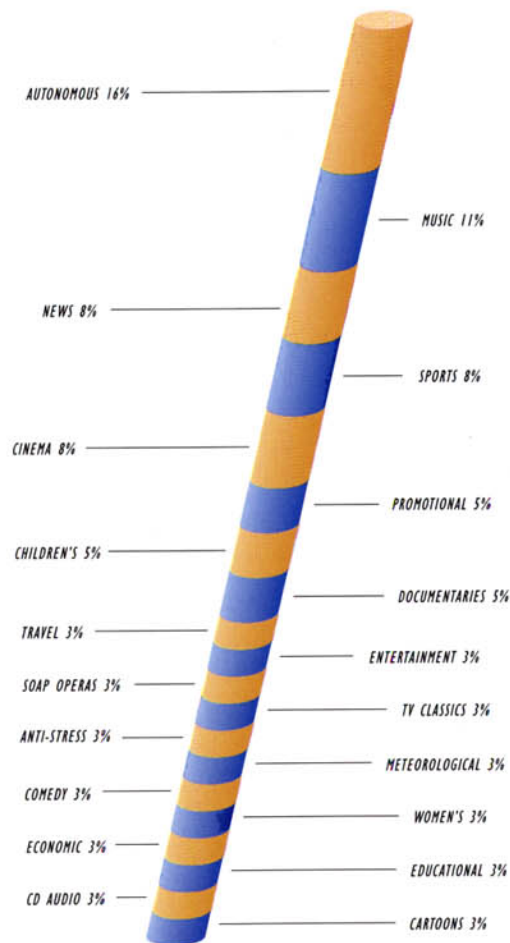
Personal Television: Vía Digital

In January 1997, the company, **Distribuidora de Televisión Digital (D.T.S.)** was incorporated, with **Telefónica** holding a 35% stake, which, in September of that same year, launched a pay TV service under the trade name **Vía Digital**, based on the concept of personal television.

This product has broken away from conventional models, creating a totally new line of business. Instead of offering a limited number of channels focused on a small sector of the population, the offer starts with a basic package of 35 channels, with a reasonable connection charge and monthly subscription fees that fit the pocket of any segment of the market. This commercial policy has proven to be correct, as after only three and a half months on the market, **Vía Digital** already has 200,000 subscribers.

Vía Digital now offers, over and above the basic package of 35 TV and 30 music channels, 52 additional channels grouped into different programme packages which include pay-per-view football and cinema and will shortly provide interactive services on meteorological information, teledownloading software, telebanking and also Internet access via satellite.

Vía Digital
Basic package programmes
(January 1998)



Via Digital will offer interactive services, one of which being Internet access via satellite



Previous to the launching of **Via Digital**, Europe's most advanced **Digital Distribution Centre** was constructed and placed in service. This represented yet another new line of activity for **Telefónica**, and has also allowed the Company to create a centre, with characteristics similar to those of **Televisión Española**, as its support for the distribution of 10 digital channels in Latin America.

Antena 3 TV

As a continuation of the **Group's** audiovisual policy, on July 25th, 1997, **Telefónica** acquired a 25% participation in **Antena 3 TV**, therefore completing the range of television supports currently found in the marketplace: hertzian, cable, satellite and interactive.

As has been previously mentioned, the international markets are following a clear trend towards globalization, from both geographical and technological viewpoints. As a consequence of this acquisition, **Telefónica** is now in a position to guarantee access to audiovisual content for its global telecommunications services, particularly in terms of the rights to broadcast football games, which is the key to success in the Spanish media today.

Antena 3 TV is Spain's leading private television station, in terms of both audience ratings and revenue. In 1997 its market share stood at 22.7% for viewers and 30% for advertising.

Antena 3 TV's objectives are focused, on the one hand, on consolidating its leadership within the private TV stations, and developing programmes that are popular with both viewers and advertisers and, on the other, taking maximum advantage of the synergies and opportunities that will arise from the Company's position as a multimedia corporation. This dedication to leadership is also focused on the international audiovisual marketplace, particularly in the area of Latin America.



Cable Communications

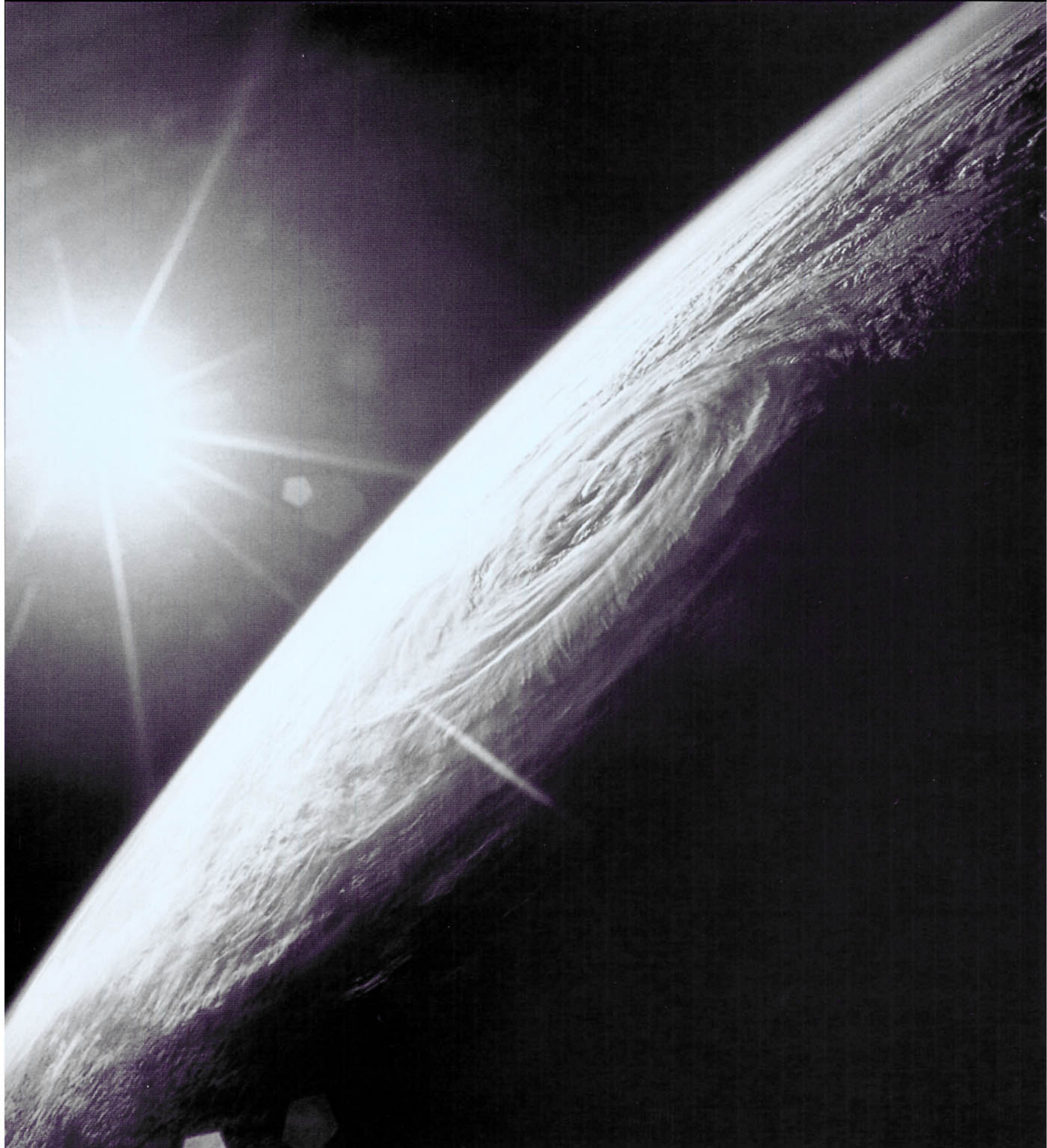
As a result of current legislation, the launching of cable TV operations in Spain has had to be postponed until 1998. To date, **Telefónica** has established **Local Operators** in different areas, incorporating the necessary media, financial and industrial partners from these same areas.

In line with its commitment as a global operator, **Telefónica** is interested in grasping the opportunities that arise in the cable communications arena, profiting from the possible synergies within the **Group**.

All the activities that take place in this line of business will always make the creation of value for our shareholders a priority.



Telefónica is interested in grasping the opportunities that arise in the cable communications arena profiting from the possible synergies within the Group



INTERNATIONAL OUTLOOK

Within the sector's new make-up, the concept of the domestic market as a national one no longer applies. The international scope and character of a global operator are two features that have become the unquestionable qualities that make a leader. Today, **Telefónica**'s domestic market is made up by both Spain and Latin America where a complete range of communications services is being operated and managed.

Throughout 1997, Latin America continued to be the core focus of **Telefónica Internacional**'s investment and management activity, achieving, once again, increased yield on investment and customer satisfaction, at the same time as widening its range of activities to include other such areas as audiovisual content and the media. All this has therefore created value for our shareholders as well as further strengthening the leading position of the **Telefónica**-managed companies in their respective countries and that of the **Telefónica Group** in the Spanish-speaking world.

The **Telefónica**-managed companies have also contributed to the economic development of their countries, strengthening the growth of other sectors, as a result of the services provided by their up-to-date infrastructures, the high investment level and the significant contributions made to the respective State Treasuries, to name but a few factors.

Over the year, **Telefónica** continued its intense search for and evaluation of investment opportunities, with the Brazilian market being our number one priority in the region. 1997 witnessed our entrance into this market through our participation in the management of the **Compañía Riograndense de Telecomunicaciones (CRT)**, as the consortium led by **Telefónica Internacional** won the international public bidding held in December 1996. This consortium is also made up of the **CTC Group** and **Telefónica Argentina**, along with the local operator **RBS**, Brazil's third ranking multimedia group, in terms of billing, and the country's leader in the southern region.

Telefónica continues to hold its position of leadership in the Spanish-speaking markets



The Brazilian market takes priority in Latin America

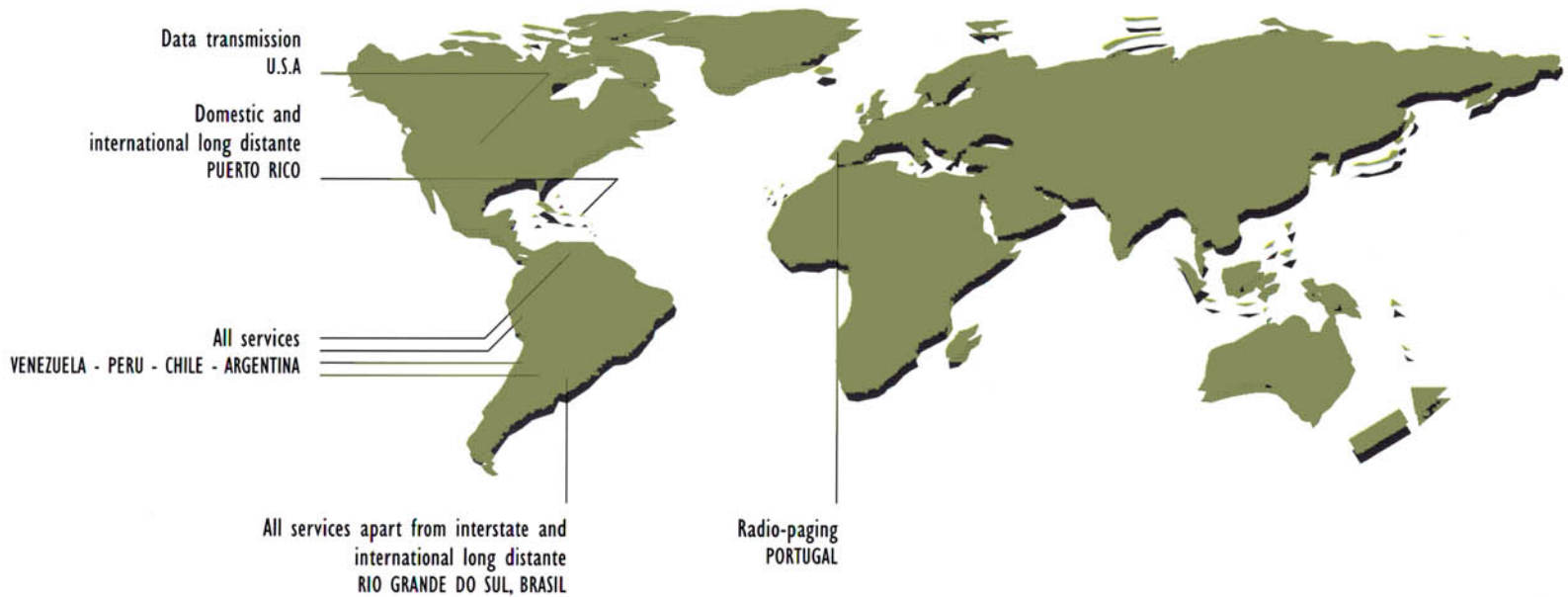
The management carried out in **CRT** during 1997, has reflected a significant improvement in all its financial and operating indicators, at the same time as contributing its considerable experience at a moment when the liberalization of the Brazilian telecommunications market is imminent.

In 1997, **Telefónica** increased its participation in **Cointel**, **Telefónica de Argentina's** majority shareholder, from 33.16% to 50%, thereby further strengthening its

TELEFÓNICA INTERNACIONAL GROUP'S COMPANIES				
Company	Country	Population (Mill.)	Services	Competition
CTC	Chile	14,6	Basic Telephony, Long Distance, Public Telephony, Mobile Telephony, rental and sale of equipment and terminals, cable TV, Radio-paging and Data Transmission.	All telephone services in Chile are liberalized.
TASA	Argentina	17,8 (1)	Basic Telephony, Long Distance, Mobile Telephony, Radio-paging, Yellow Pages and other value added services.	Basic Telephony and domestic and international long distance are under monopoly, through one of the two existing licenses. The remaining services are liberalized.
Telefónica del Perú	Peru	24.6	Basic Telephony, Long Distance, Mobile Telephony, Radio-paging and cable TV.	Telefónica del Perú offers local and domestic and international long distance services, al with exclusive rights. The remaining services in Perú are liberalized.
CRT	Brazil	9.52 (1)	Basic Telephony, Mobile Telephony, leasing of Data Transmission lines, Yellow Pages, 900 Service, value added service and the insertion of advertising in the press.	The services provided in the area of Rio Grande do Sul are not liberalized.
CANTV	Venezuela	22.8	Basic Telephony, Long Distance, Public Telephony, Mobile Telephony, Public Telecommunications Centres, Private Networks, Rural Telephony Services, Data Transmission and directory information services.	Basic Telephony, domestic and international Long Distance, and switched services are provided under monopoly until 2000. The remaining services are liberalized, except Mobile telephony which is under a duopoly.
TLD	Puerto Rico	3.8	Long distance services.	Liberalized.
Cablevisión	Argentina	35.6	Cable TV.	Liberalized.
T y C	Argentina	35.6	Audiovisual content and Media.	Liberalized.
Cocelco	Colombia	35.8	Mobile telephony.	Undergoing liberalization.
Infonet	USA	N/A	Data transmission.	Liberalized.
Contactel	Portugal	10	Radio-paging.	Liberalized.
TUPR	Puerto Rico	22.8	Inter-island and international long distance via satellite and radio.	Liberalized.
TYSSA	Argentina	35.6	Telecommunications systems consulting.	Liberalized.

(1) Population in area of coverage.

Telefonica Internacional: Geographical Location



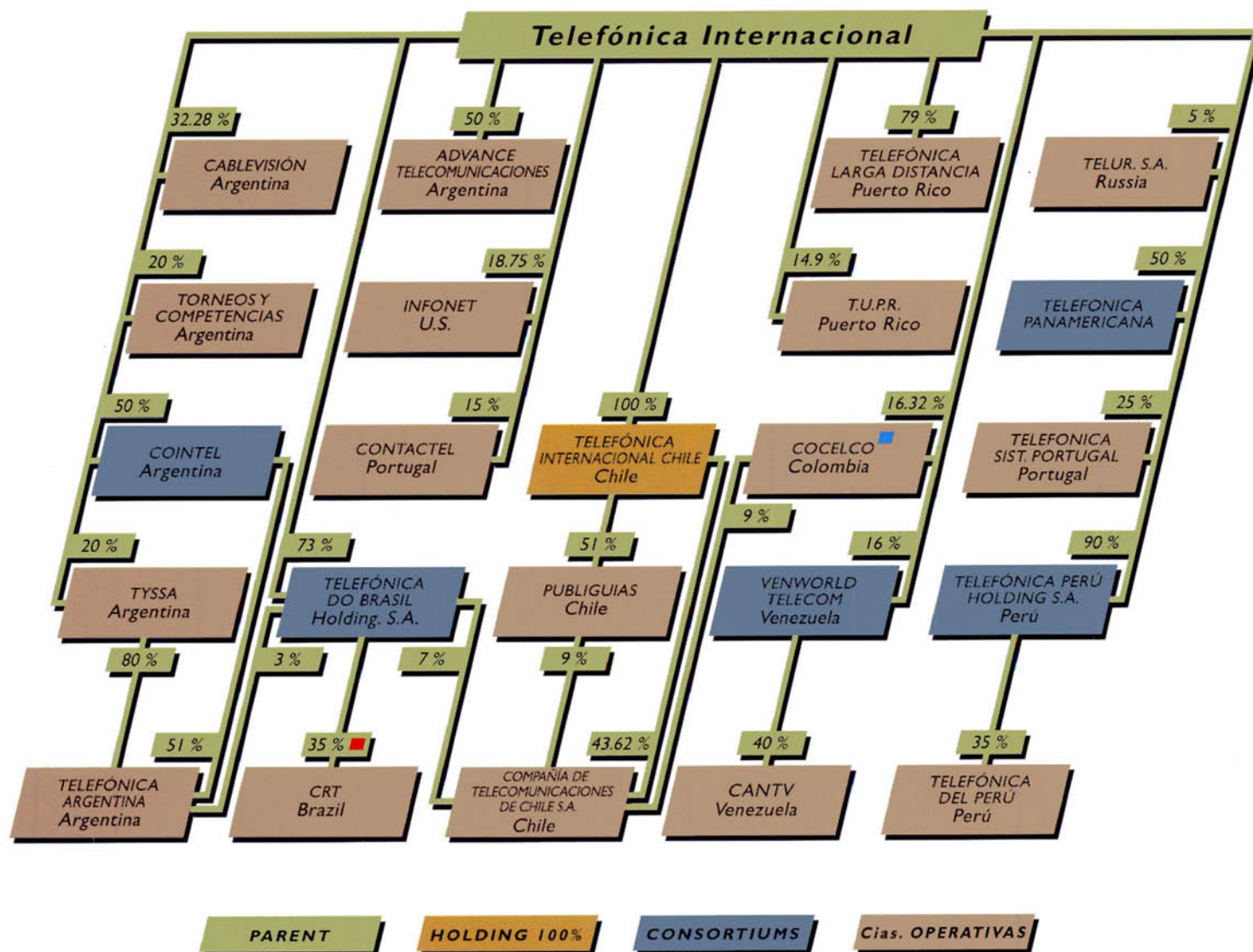
OPERATING INDICATORS

Country	Company	Lines service (1)			Cellular customers			Cable TV customers		
		31-dec-97	31-dec-96	% growth	31-dec-97	31-dec-96	% growth	31-dec-97	31-dec-96	% growth
Argentina	Tasa (2) Cablevisión (3)	3,821,703	3,450,040	10.8 %	620,237	190,477	225.6 %	1,043,111	n.a.	
Chile	CTC	2,393,707	2,056,353	16.4 %	220,070	175,085	25.7 %	256,524	216,630	18.4 %
Perú	T. del Perú	1,645,920	1,436,022	14.6 %	319,749	130,895	144.3 %	252,225	101,387	148.8 %
Brazil	CRT	1,031,806	781,799	32.0 %	359,652	170,427	111.0 %			
Venezuela	CANTV	2,738,450	2,494,859	9.8 %	346,000	213,655	61.9 %			
		11,631,586	10,219,073	13.8 %	1,865,708	880,539	111.9 %	1,551,860	318,017	388.0 %

(1) Include pay-phones.

(2) The information on Tasa corresponds to the fiscal year that closes on September 30.

(3) Includes 50% of the companies VCC, UIH Bahía Blanca and UIH Santa Fe. Does not include Mandeville's customers (430,113)



TISA's structure at 31-XII-1997

■ Telefónica de España a direct 14.51% stake in COCELCO

■ Telefónica do Brazil Holding, S.A. holds a 35% stake in CRT with voting rights; the consortium holds 13.45% in the total share capital

commitment in the management of the **Company**. The remaining 50% is held by Citicorp Equity Investment (CEI), the Argentinian subsidiary of the Citicorp Group.

Within the **Telefónica Group's** commitment to the management of companies which hold positions of leadership in their sector, as well as embodying a wide spectrum of business lines, a policy of divestiture has been introduced for those investments which do not fulfill these requirements. In consequence, the participation held in **Telefónica Rumania** was sold, sale and purchase agreements were signed regarding the divestiture of the investment in **Multicanal** (Argentina) and our withdrawal from **Cocelco** (Colombia) was negotiated, as the Group did not hold a controlling stake in this company.

International Businesses

In 1997, the companies managed by **Telefónica Internacional** in Latin America continued to reflect strong growth in the lines in service in their respective countries, achieving the overall growth figure of almost 14% compared with the previous year. At year-end, **Telefónica Internacional** managed more than 11.6 million basic telephony lines, registering a net increase of 1.4 million lines.

Telefónica de Argentina surpassed the figure of 3.8 million lines with a penetration ratio of 23 lines per 100 inhabitants, therefore maintaining its position as Latin America's leading telecommunications company. Its network digitalization reached 89.5%, and this is expected to be totally digitalized during the first half of 1998.

CTC, reflecting an average annual growth in plant in service of 19% since it was purchased, recorded a net increase in lines of 350,000, raising the total figure to 2.4 million, making it the only operator offering services throughout the whole country.

Telefónica del Perú exceeded the figure of 1.6 million lines, with 88% digitalization.

At the same time, **CRT's** plant in service grew by more than 30%, registering, 60% digitalization.

Regarding mobile telephony, **Telefónica de Argentina** has increased its customer base threefold, now numbering more than 600,000 between its two subsidiaries:



Telefónica manages 11.6 million lines in Latin America

The Telefónica-managed companies in Latin America reflected strong growth in all services



Miniphone in Buenos Aires and **TCP** inland. In Chile, **CTC** acquired 45% of the company Startel, in which it already held a 55% stake. This company was created in June 1996 through the merger of **CTC** and **VTR**'s mobile businesses. This acquisition will undoubtedly permit an even greater degree of convergence between fixed and mobile services, to which **Startel** already has 220,000 subscribers. **Telefónica del Perú**'s customers increased by 144% when compared with the year before, therefore continuing its position of leadership, holding a 73% market share with 320,000 customers.

In terms of public telephony, **Telefónica de Argentina** consolidated its market leadership, reaching the figure of 55,686 lines, reflecting a 16.5 % increase. Likewise, **Telefónica del Perú** registered 38,290 lines (19% annual growth), **CTC** 12,387 (10% annual growth) and **CRT** 29,112 (80% growth).

Regarding directories and yellow pages, in Chile, **Publiguías**, in which 51% is held by **Telefónica** and 9% by **CTC**, its market penetration is 53.6%, publishing almost 3 million copies. In Argentina, the **Telefónica** subsidiary, **Telinver**, publishes the **Paginas Doradas** (Golden Pages) covering 26% of the total market. Both of these companies have greatly improved the quality of their publications, both in terms of its paper edition and in terms of adapting to the multimedia environment.

In Argentina, **Advance Telecomunicaciones** has become the company with the most extensive Internet access network in the country. **Advance** is a joint venture between **Telefónica Internacional** and **CEI**, able to offer on-line and data transmission services, having acquired 100% of **Compuserve Argentina**'s share capital.

In Peru, **Cable Mágico**, **Telefónica del Perú**'s cable TV subsidiary, has reflected significant growth throughout the year and in Chile, **Metropolis-Intercom**, in which **CTC** participates, has consolidated its position as the country's second cable TV operator.

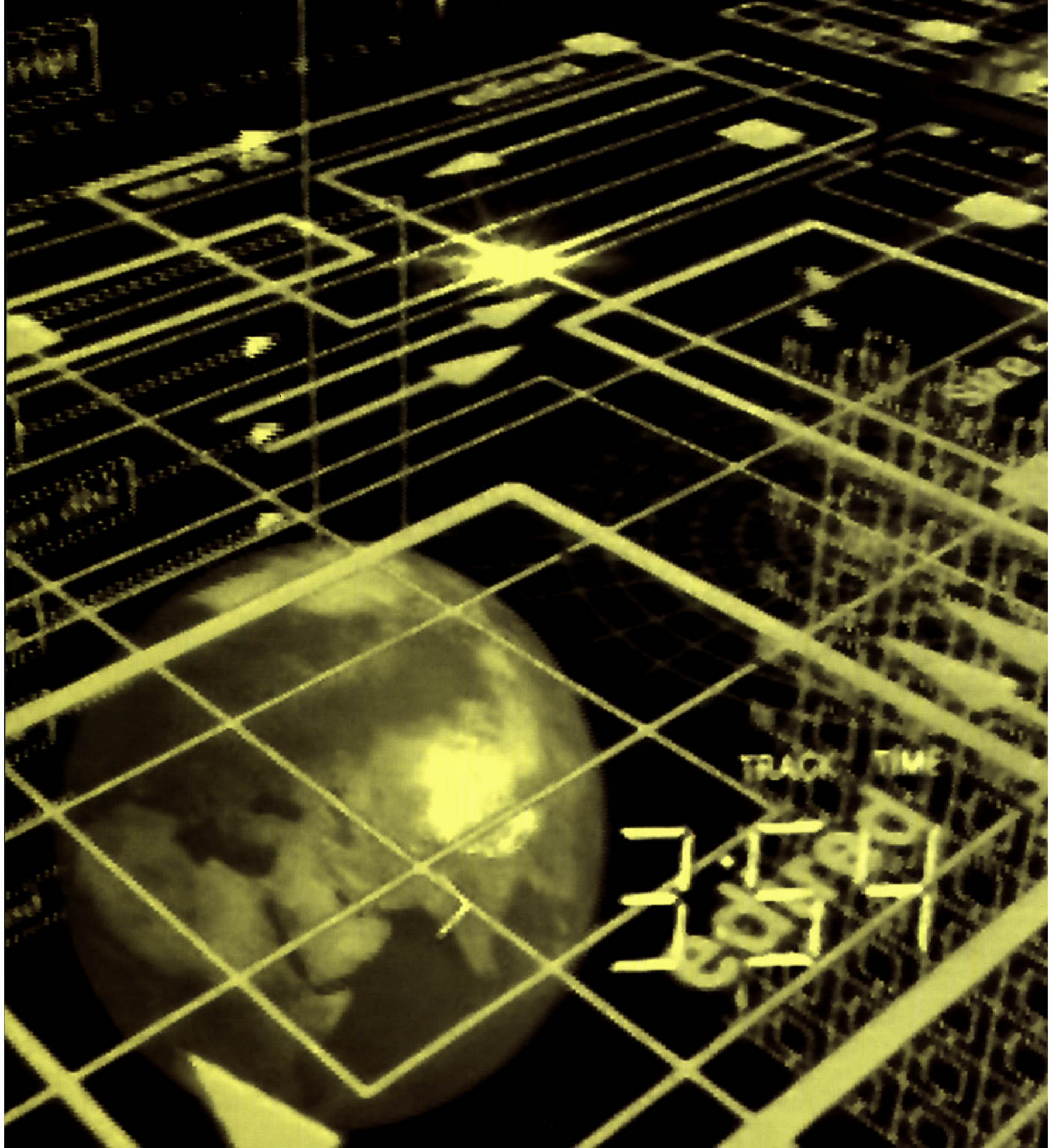
Telefónica, along with Citicorp Equity, has recently acquired participations in three Argentinean cable TV companies, **Cablevisión**, **VCC** and **Mandeville**, as well as taking up a minority stake in **Torneos and Competencias**, a company which controls the football rights in Argentina as well as several businesses which deal with sports events and, also, a 30% participation in Editorial Atlántida, which, in turn, controls the television stations Canal 9 and Telefe.

Moving into new markets

Morocco, whose operator is soon to be privatized, has become one of the **Group's** international objectives, not only due to its proximity, but also due to its development potential. With this imminent privatization in mind, **Telefónica Maroc** has been incorporated, which will compete in the bidding for the second GSM licence, as well as in the privatization of the telecommunications operator ITISSALAT AL-MAGHRIB. In order to successfully carry out this operation, and as is now **Telefónica's** normal practice, it will also have the support of local operators and its international alliances.

Telefónica has also turned its attention to the development of the telecommunications market in other regions, without disregarding the opening up of new business activities, always in line with its priority target of enhancing shareholder value.

**Telefónica is moving into new markets
with the firm intention of becoming
one of the world's five
leading operators**



TRACK TIME

3:54

INTERNATIONAL ALLIANCES

The internationalization and globalization of the economy has made the forming of agreements with other operators a "must", although this alone does not suffice in the serving of our transnational customers. These agreements allow us all to take on new investments aimed at consolidating our leadership, to open up new markets and to share opportunities.

In April 1997, **Telefónica** withdrew from its international alliance with MCI and BT, which included, among others, agreements on international traffic and the distribution of multinational services.

The more than likely success of Worldcom's acquisition offer for MCI enhances the appeal of a possible collaboration agreement between **Telefónica** and this American company.

The increased potential of this new company will allow the undertaking of more ambitious projects, including that of entering the US Spanish-speaking market.

The agreement reached with Portugal Telecom on April 16th 1997, forms part of the double objective of strengthening our international strategy, at the same time as jointly developing businesses, both in Spain and Latin America, with particular emphasis on the Brazilian market and future operations in the Magreb countries.

The agreement with Portugal Telecom aims at jointly strengthening international strategies and developing our businesses



THE REGULATORY ENVIRONMENT

The progress achieved within the framework of the liberalization of the telecommunications sector can be considered to be satisfactory. The most outstanding points are outlined below:

The recognition of the need to rebalance tariffs and the establishing of a Ministerial Order (March 18, 1997) regarding the calendar to be applied for 1998 and 1999.

The signing of an interconnection agreement between **Telefónica** and the second fixed telephony operator.

The necessary rules and regulations were laid down, along with the introduction of a series of measures, in order to increase the pace of opening the market up to competition. The necessary steps were taken to make sure that this process, in terms of the development and structure of the network, takes place in stages and in the most rational way possible.

The new Numbering Plan was approved, which will come into force on April 4th, 1998.

The dispute regarding the entrance of a second mobile operator was solved, with **Telefónica Móviles** being guaranteed access to the 1,800 Megahertz bandwave.

The Digital Television law was passed.

The Government approved the General Telecommunications Bill, which is currently under debate.

Lastly, it should be underlined that **Telefónica** is more than willing to support the whole liberalization process, as it believes it to be the most appropriate way to gain the necessary boosting of the sector, at the same time as being more than aware of the increasingly important role of telecommunications in the worldwide economy.

The existing regulatory framework in Chile favours competition in all the telecommunications market sectors, through the granting of free concessions,

therefore permitting the unrestricted horizontal integration of companies and the regulated vertical integration of local and long distance businesses, as well as promoting the entrance of new competitors.

Telefónica del Perú has signed a concession with the Peruvian State to provide local and long distance telephone services for a twenty-year period, which can be extended another 20 years in five-year periods. The first five years of the concession period grant exclusive rights, laying down a series of obligations for the services included under the concession, such as improved service quality and an expansion programme both of which have been fulfilled. The remaining services are liberalized.

Telefónica de Argentina holds a licence for an unlimited time period by which it is permitted to provide public telecommunications services in the southern region of the country, with exclusive rights until November 8th, 1997, after which time the licence period can be extended for another three years provided that all the terms and conditions stated in the invitation to bidding have been fulfilled. The Company has acted accordingly and has therefore applied for the extension with exclusive rights which is still pending a final decision.

CORPORATE PROJECTS FOR THE MILLENNIUM AND THE EURO

In 1997 two of our corporate projects gained considerable impetus, both of which are going to be of extreme importance in the near future: the **Millennium Project** and the **Euro Project**. The aim of the **Millennium Project** is to identify and carry out the necessary actions regarding business processes, information systems and infrastructure, so that the quality and facilities offered by our products are not affected by the arrival of the year 2000. On the other hand, the **Euro Project** targets are those of adapting the systems and procedures that support the business processes to the new requirements to be introduced as a result of the Euro becoming the European Union's single currency.



*Consolidated
Annual Accounts
and Management Report
for fiscal years 1997 and 1996
along with the Auditor's Report
of the Telefónica Group*

Raimundo Fdez. Villaverde, 65
28003 Madrid

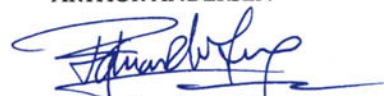
Translation of a report and consolidated financial statements originally issued in Spanish and prepared in accordance with generally accepted accounting principles in Spain (see Note 25).
In the event of a discrepancy, the Spanish-language version prevails.

AUDITORS' REPORT ON CONSOLIDATED FINANCIAL STATEMENTS

To the Shareholders of
Telefónica de España, S.A.:

1. We have audited the consolidated financial statements of TELEFÓNICA DE ESPAÑA, S.A. and COMPANIES composing the TELEFÓNICA GROUP, which consist of the balance sheets as of December 31, 1997 and 1996, and the related statements of income and notes to financial statements for the years then ended. The preparation of these consolidated financial statements is the responsibility of the controlling company's directors. Our responsibility is to express an opinion on the consolidated financial statements taken as a whole based on our audit work performed in accordance with generally accepted auditing standards, which require examination, by means of selective tests, of the documentation supporting the financial statements and evaluation of their presentation, of the accounting principles applied and of the estimates made.
2. As indicated in, 7 and 11, Telefónica de España, S.A. revalued its assets pursuant to Royal Decree-Law 7/1996, which gave rise to a surplus, net of the single tax, of Ptas. 219,076 million, and this amount is included under the "Revaluation Reserves" caption in the consolidated financial statements referred to above.
3. In our opinion, the consolidated financial statements referred to above present, in all material respects, a true and fair view of the net worth and financial position of Telefónica de España, S.A. and Companies composing the Telefónica Group as of December 31, 1997 and 1996, and of the results of their operations and of the funds obtained and applied by them in the years then ended, and contain the required information, sufficient for their proper interpretation and comprehension, in conformity with generally accepted accounting principles and standards applied on a consistent basis.
4. The accompanying consolidated management report for 1997 contains the explanations which the directors of Telefónica de España, S.A. consider appropriate about the Telefónica Group's situation, the evolution of its business and other matters, but is not an integral part of the consolidated financial statements. We have checked that the accounting information in the management report is consistent with that contained in the consolidated financial statements for 1997. Our work as auditors was confined to checking the management report with the aforementioned scope, and did not include a review of any information other than that drawn from the accounting records of the consolidated companies.

ARTHUR ANDERSEN



Eduardo Sanz Hernández

February 25, 1998

Arthur Andersen y Cía., S. Com.
Reg. Merc. Madrid, Tomo 3190, Libro 0, Folio 1,
Sec. 8, Hoja M-54414, Inscrp. 1.*

Inscrita en el Registro Oficial de Auditores de
Cuentas (ROAC)
Inscrita en el Registro de Economistas Auditores (REA)

Domicilio Social:
Raimundo Fdez. Villaverde, 65. 28003 Madrid
Código de Identificación Fiscal D-79104469

TELEFÓNICA DE ESPAÑA, S.A. AND COMPANIES COMPOSING THE TELEFÓNICA GROUP
CONSOLIDATED BALANCE SHEETS AS OF DECEMBER 31, 1997 AND 1996
(Currency-Millions of Spanish Pesetas)

ASSETS	1997	1996
A) Due from stockholders for uncalled capital	446	—
B) Fixed and other noncurrent assets	4,987,098	4,655,150
I. Start-up expenses	2,337	577
II. Intangible assets (Note 6)-	356,109	337,825
Research and development expenses	120,582	104,047
Rights on leased assets	16,336	15,425
Other intangible assets	348,573	313,336
Amortization	(129,382)	(94,983)
III. Property and equipment (Note 7)	4,148,113	3,973,870
Land and structures	717,016	656,279
Technical installations and machinery	159,392	130,487
Telephone installations	6,035,655	5,598,023
Furniture	256,411	237,582
Construction in progress	396,465	327,861
Advances on property and equipment	2,288	23,640
Installation materials	38,977	50,804
Depreciation	(3,458,091)	(3,050,806)
IV. Long-term financial investments (Note 8)	480,539	342,878
Holdings in associated companies	201,390	116,317
Other holdings	92,642	128,540
Other loans	96,834	31,374
Long-term deposits and guarantees	1,754	1,369
Falta traducción	92,763	70,007
Provisions	(4,844)	(4,729)
C) Goodwill in consolidation (Note 5)	284,364	49,798
D) Deferred charges (Note 9)	135,103	130,294
E) Current assets	817,750	602,495
I. Due from stockholders for capital calls	—	—
II. Inventories	37,691	33,834
Inventories	40,149	34,966
Advances	144	38
Provisions	(2,602)	(1,170)
III. Accounts receivable-	629,230	507,775
Customer receivables (Note 10)	479,916	405,722
Receivable from associated companies	4,391	4,453
Sundry accounts receivable	113,138	77,811
Employee receivables	12,612	14,417
Receivable from public authorities (Note 18)	87,188	55,961
Allowance for bad debts (Note 10)	(61,355)	(43,196)
Allowances for sundry accounts receivable	(6,660)	(7,393)
IV. Short-term financial investments-	126,093	35,843
Loans to associated companies	—	61
Short-term investment securities	85,331	8,779
Other loans	40,770	27,496
Provisions	(8)	(493)
V. Short-term treasury stock	369	—
VI. Cash	10,432	12,647
VII. Accrual accounts	13,935	12,396
TOTAL ASSETS (A+B+C+D+E)	6,224,761	5,437,737

The accompanying Notes I to 25 and Exhibits I and II are an integral part of these consolidated balance sheets.

TELEFÓNICA DE ESPAÑA, S.A. AND COMPANIES COMPOSING THE TELEFÓNICA GROUP
CONSOLIDATED BALANCE SHEETS AS OF DECEMBER 31, 1997 AND 1996
(Currency-Millions of Spanish Pesetas)

STOCKHOLDERS' EQUITY AND LIABILITIES	1997	1996
A) Stockholders' Equity (Note 11)	1,991,374	1,863,760
I. Subscribed capital stock	469,735	469,735
II. Paid-in surplus	43,067	43,067
III. Revaluation reserves	868,392	868,392
IV. Reserves	457,559	355,053
Legal reserve	93,947	86,071
Other reserves	175,779	157,061
Consolidation reserve	126,577	75,935
Transition differences in consolidation	61,256	35,986
V. Prior years' income	137	112
VI. Income for the year	190,063	160,282
Income of the parent company and subsidiaries	254,147	211,149
Income of associated companies	9,958	7,811
Income attributed to minority interests (Note 2)	(74,042)	(58,678)
VII. Interim dividend paid during the year	(37,579)	(32,881)
B) Minority interests (Note 12)	394,097	374,693
C) Deferred revenues (Note 13)	112,471	102,218
D) Provisions for contingencies and expenses (Note 14)	388,896	336,615
E) Long-term debt	1,916,627	1,672,907
I. Debentures, bonds and other negotiable instruments (Note 15)-	714,923	654,378
Nonconvertible debentures and bonds	611,472	637,919
Convertible debentures and bonds	103,149	4,645
Other marketable debt securities	302	1,814
II. Payable to credit entities (Note 16)	942,728	843,349
III. Payable to Group and associated companies		271
IV. Other accounts payable-	174,505	103,147
Other accounts payable Notes 2-d and 4-	74,505	103,147
V. Accrued taxes payable (Note 18)	83,444	69,011
VI. Uncalled capital payments payable-	1,027	2,751
Associated companies	452	243
Other companies	575	2,508
F) Current liabilities	1,421,296	1,087,544
I. Debentures, bonds and other negotiable instruments (Note 15)	284,018	147,427
Debentures	192,201	63,580
Other negotiable instruments	77,274	68,854
Interest on debentures and other securities	14,543	14,993
II. Payable to credit entities (Note 16)-	336,525	244,617
Loans and other accounts payable	322,515	234,136
Interest payable	14,010	10,481
III. Payable to associated companies	15,080	28,458
IV. Trade accounts payable-	351,357	374,580
Advances received on orders	2,961	933
Payables for purchases and services	344,832	370,564
Notes payable	3,564	3,083
V. Other nontrade payables	382,872	266,326
Accrued taxes payable (Note 18)	91,407	106,289
Other nontrade payables (Note 19)	291,465	160,037
VI. Accrual accounts	5,444	26,136
TOTAL STOCKHOLDERS' INVESTMENT AND LIABILITIES (A+B+C+D+E+F)	6,224,761	5,437,737

The accompanying Notes 1 to 25 and Exhibits I and II are an integral part of these consolidated balance sheets

TELEFÓNICA DE ESPAÑA, S.A. AND COMPANIES COMPOSING THE TELEFÓNICA GROUP
CONSOLIDATED STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 1997 AND 1996
(Currency-Millions of Spanish Pesetas)

DEBIT	1997	1996
A) EXPENSES		
Reduction in inventories	758	3,253
Supplies-		
Purchases from associated companies and other	195,132	136,314
Work performed by other companies	138,936	92,290
	334,068	228,604
Personnel expenses (Note 20)	570,895	554,682
Period depreciation and amortization-		
Property and equipment	565,472	499,924
Intangible assets	35,575	26,087
Deferred charges	1,610	218
	602,657	526,229
Variation in operating provisions-		
Variation in provision for inventories	1,150	266
Variation in allowance for bad debts	22,711	17,161
Variation in other operating provisions	11,896	9,142
	35,757	26,569
Other operating expenses-		
Outside services	260,760	207,638
Taxes other than income tax	38,763	35,106
Other operating expenses	21,998	19,307
	321,521	262,051
I. Operating income	660,454	575,965
Interest on payables to associated companies	—	60
Other interest on accounts payable and similar expenses (Note 20)	189,967	181,645
Amortization of deferred interest expenses	3,754	3,603
Variation in financial investment provisions	6,464	665
Exchange losses (Note 20)	21,066	20,452
II. Financial income	—	—
Share in losses of companies carried by the equity method	10,968	8,114
Amortization of goodwill in consolidation (Note 5)	33,312	16,786
III. Income from ordinary activities	449,367	390,399
Variation in control portfolio provisions	213	246
Losses on fixed assets	27,513	45,034
Losses on disposals of consolidated companies (Note 8)	68	2,609
Extraordinary expenses and losses (Note 20)	135,593	98,570
IV. Extraordinary income	—	—
V. Income before taxes	337,641	275,881
Corporate income tax (Note 18)	36,554	25,804
Foreign taxes (Note 18)	36,982	31,117
VI. Consolidated income for the year	264,105	218,960
Income attributed to minority interests (Note 12)	74,282	59,287
VII. Income for the year	190,063	160,282

The accompanying Notes I to 25 and Exhibits I and II are an integral part of these consolidated statements of income.

TELEFÓNICA DE ESPAÑA, S.A. AND COMPANIES COMPOSING THE TELEFÓNICA GROUP
CONSOLIDATED STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 1997 AND 1996
(Currency-Millions of Spanish Pesetas)

CREDIT	1997	1996
B) REVENUES		
Net sales and services (Note 20)	2,363,02	2,006,058
Increase in work-in-process	3,779	6,218
Capitalized expenses of in-house work on fixed assets	117,932	127,319
Other operating revenues-		
Sundry and other current operating revenues	36,795	32,653
Subsidies	1,639	1,643
Overprovision for contingencies and expenses	2,863	3,462
	41,297	37,758
I. Operating loss	—	—
Income from shareholdings		
Associated companies	23	25
Other companies	1,746	2,350
	1,769	2,375
Revenues from other securities and loans-		
Associated companies	687	889
Other companies	22,977	15,892
	23,604	16,781
Exchange gains	8,45	10,678
II. Financial loss	187,733	176,591
Equity income of companies carried by the equity method	20,926	15,925
III. Loss on ordinary activities	—	—
Gains on fixed asset disposals	709	2,150
Gains on disposals of holdings in consolidated companies (Note 8)	27,371	0,335
Capital subsidies	1,285	0,35
Extraordinary revenues (Note 20)	12,296	9,141
IV. Extraordinary loss	111,726	114,518
V. Loss before taxes	—	—
VI. Consolidated loss for the year	—	—
Loss attributed to minority interests (Note 2)	240	609
VII. Loss for the year	—	—

The accompanying Notes 1 to 25 and Exhibits and I are an integral part of these consolidated statements of income

Translation of reports and financial statements originally issued in Spanish and prepared in accordance with generally accepted accounting principles in Spain (see Note 25). In the event of a discrepancy, the Spanish-language version prevails.

TELEFÓNICA DE ESPAÑA, S.A. AND COMPANIES COMPOSING THE TELEFÓNICA GROUP

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS FOR 1997 AND 1996

I. GROUP DESCRIPTION AND STATE CONTRACT

Group companies

Telefónica de España, S.A. ("Telefónica") and its dependent companies make up an integrated group of companies ("the Telefónica Group") operating in the telecommunications industry.

Exhibit I to these notes to consolidated financial statements lists the subsidiaries, associated companies and investees in which Telefónica has direct or indirect holdings and their lines of business, net worth and results. Exhibit II describes the main variations in the consolidated group.

Parent Company

Telefónica de España, S.A. is a company which was incorporated pursuant to the Spanish Commercial Code for an indefinite period of time on April 19, 1924. Its registered office is at calle Gran Vía, 28 - 28013 Madrid (Spain).

a) Corporate purpose

The Company's corporate purpose, per Article 4 of its bylaws, is as follows:

1. The provision and operation of all manner of public and private telecommunications services, and for this purpose, the design, installation, upkeep, repair, improvement, acquisition, disposal, interconnection, management, administration and any other activity not included in the foregoing list, in connection with all manner of existing or future telecommunications networks, lines, satellites, equipment, and technical systems and infrastructures, including the land and buildings where they are located.
2. The supply and operation of all manner of ancillary or supplementary telecommunications services or the services derived therefrom.
3. The research and development, promotion and application of all manner of components, equipment and systems, directly or indirectly used for telecommunications.
4. Manufacturing, production and, in general, all other industrial activities relating to telecommunications.
5. Acquisition, disposal and, in general, all other commercial activities relating to telecommunications.

All the activities that constitute the corporate purpose described in the preceding paragraphs may be performed either in Spain or abroad and may be carried on either wholly or partially by the Company, or through shareholdings or participations in other companies or legal entities with an identical or similar corporate purpose.

b) Framework for the provision of services

Telefónica is the State licensee for rendering certain public telecommunications services pursuant to the License Contract entered into with the Spanish Administration on December 26, 1991. In accordance with the provisions of such Contract, Telefónica may also carry on any financial, industrial or service-related activities deemed necessary for its interests, provided they do not cause any deterioration in the normal operation of the ultimate carrier services forming the subject matter of the aforementioned Contract or involve the assumption of obligations contrary to the provisions of the Spanish National Telecommunications Plan.

As the licensee of said services, Telefónica undertakes, in general, to provide them observing such general interest criteria of a noneconomic nature as may be determined in the regulations on telecommunications services, particularly taking into account the maintenance of security in the operation of networks and services, the integrity and the interoperativeness thereof, data protection and the confidentiality of communications.

As telecommunications services have been progressively deregulated and Telefónica has modified the enabling instruments to provide these services, they have ceased to be governed by the License Contract of December 26, 1991. Only the basic telephony service and the related carrier service are currently governed by the aforementioned Contract.

The deregulation process has paved the way for the shift to restricted or full competition systems for part of the services forming the subject matter of the State License Contract entered into with the State on December 26, 1991. In particular, Royal Decree-Law 6/1996, now repealed, and Telecommunications Deregulation Law 12/1997, which superseded it, granted Retevisión an enabling instrument to provide urban, national and international basic telephony services as well as supporting carrier services in connection with basic telephony services, for which purpose it has incorporated a company which will be charged with rendering the service under an indirect management arrangement.

Under the aforementioned Law 12/1997, Telefónica must allow access to its network by all service operators who wish to do so in order to enable circuits to be interconnected with service interoperativeness. On December 30, 1997, Telefónica entered into a general interconnection agreement with Retevisión. The interconnection rates and conditions are determined by a Ministerial Order of March 18, 1997, and will remain in force until the full deregulation of telecommunications in Spain, i. e., December 1, 1998.

The emergence of a second global operator in Spain has made it necessary to regulate various fundamental matters to enable the free-market provision of services under a fully competitive system. Specifically, a Ministerial Order of July 18, 1997, established the conditions for the selection and pre-assignment of operators for long-distance calls, and a Ministerial Order of August 4, 1997, regulated the user's right to keep his number when he switches to a new access operator, provided that his physical location remains the same.

Telefónica also provides other noteworthy services in the telecommunications industry, such as the circuit rental carrier service, regulated by the Technical and Service Provision Regulation enacted by Royal Decree 1558/1995. Telefónica has obtained the enabling instrument to provide the value added service of packet- and circuit-switched data, which is thereby added to that transferred by the Company to its subsidiary Telefónica Transmisión de Datos, S.A. The same can be said of the value added service of voice telephony in closed user groups.

Special mention should also be made of the key role of the Infovia Internet Service Provider in the development of the Internet in Spain. In September 1997 a Ministerial Order was published stipulating the conditions of the service under a system of free competition.

Telefónica is also present in the satellite telecommunications market. Under Law 37/1995, which deregulated such services, the only requirement for providing them is a simple administrative authorization.

The Cable Telecommunications Law empowers Telefónica to supply this service on an integrated basis with the basic telephony service in all areas where it is requested, after 16 months have elapsed from the award of the cable operator tender in each area, unless the tender is declared void, in which case commencement of the provision of services will be immediate. In response to a proposal by the Spanish National Telecommunications Market Commission, the Government may reduce this period depending on market conditions in cases in which such reduction is necessary to ensure effective competition in the provision of cable telecommunications services, provided that it is not against users' interests.

At the end of 1997 the Technical, Final Basic Telephony Service and Carrier Services Regulation was published and enacted by Royal Decree 1912/1997, which envisaged, inter alia, the granting of an enabling instrument to Telefónica for the carrier service supporting the DCS-1800 personal mobile communications service.

1997 was the last year in which there was a Government Representation at Telefónica. Pursuant to Law 12/1997, this arrangement came to an end on January 1, 1998.

c) Rate system

The License Contract established a system of regulated rates and prices aimed at guaranteeing, except with respect to the modifications expressly provided by the Contract deriving from the change from a monopoly to a competitive system, the overall financial balance of the concession, while safeguarding the principle of universal service. To that end, within the framework of cost discipline and efficient management of the Company's production resources, the rate system must ensure that Telefónica is able to cover its operating expenses, appropriations to reserves and return on capital, while striving to align the rate structure and the cost structure.

Recently, Law 12/1997, deregulating the telecommunications industry, determined that the Government, at the proposal of the Ministry of Development and subject to a report by the Telecommunications Market Commission, may establish the cases in which fixed maximum and minimum rates and simple price adjustment rates will apply, and the methods to be used to set them, based on the degree of market demand for the various services.

Rate rebalance mechanism

The preamble to of the Ministerial Order of March 18, 1997, stated that, in accordance with the legally established procedure, Telefónica would be authorized to make certain rate adjustments in the amounts and within the time periods stipulated by the Fourth Additional Provision, thereby commencing the rate rebalance process.

Telefónica has requested the Ministry of Development to commence the rate adjustment procedure, under which the adjustments provided in the aforementioned Ministerial Order will have to be carried out.

d) Tax regime

Telefónica is been subject to general tax legislation for central State and Autonomous Community taxes. As regards local taxes, Telefónica is subject to property tax, the other local taxes being replaced by an annual cash compensation payment equal to 2% of gross billings.

Pursuant to a Ministerial Order of December 27, 1989, Telefónica was authorized to file consolidated corporate income tax returns for 1990, 1991 and 1992. This authorization was extended to 1993, 1994 and 1995 by a Ministerial Order of July 21, 1993. Under Corporate Income Tax Law 43/1995 and pursuant to a resolution passed by the Stockholders' Meeting on March 29, 1996, the tax authorities have been notified that the Company intends to file tax returns for 1996, 1997 and 1998 under the special regime for groups of companies.

2. BASIS OF PRESENTATION OF THE CONSOLIDATED FINANCIAL STATEMENTS

a) True and fair view

The accompanying consolidated financial statements of the Telefónica Group were prepared from the accounting records of Telefónica de España, S.A., and from those of each of the companies which compose the Telefónica Group. The respective individual financial statements were prepared by each company's directors in accordance with the accounting principles and standards provided in Spain by the Spanish Corporations Law as enacted by Legislative Royal Decree 1564/1989, implemented by the Spanish National Chart of Accounts, as enacted by Royal Decree 1643/1990, and by the regulations for the preparation of consolidated financial statements, as approved by Royal Decree 1815/1991 and the applicable regulations in the different countries in which the companies composing the Consolidated Group are located. Accordingly, these consolidated financial statements give a true and fair view of the net worth, financial position, results and funds obtained and applied in 1997 and 1996.

The 1997 consolidated financial statements and the 1997 individual financial statements of Telefónica de España, S.A. and of each Group company will be submitted for approval by the respective Stockholders' Meetings, and it is considered that they will be approved without any changes. The 1996 individual financial statements of each of the consolidated Group companies were approved by their respective Stockholders' Meetings. The 1996 consolidated financial statements of the Telefónica Group were approved by the Stockholders' Meeting on March 21, 1997.

b) Consolidation principles

The companies over which effective control is exercised by virtue of ownership of a majority of the voting rights in their representation and decision-making bodies were consolidated by the global integration method; the multigroup companies which are managed jointly with third parties were consolidated by the proportional integration method; and those in which there is significant influence but not ownership of a majority of the voting rights or joint management with third parties are carried by the equity method. Significant influence is deemed to exist if the ownership interest exceeds 20% in the case of unlisted companies or 3% in the case of listed companies.

All material accounts and transactions between the consolidated companies were eliminated in consolidation. In the case of investees whose accounting and valuation methods differed from those of Telefónica, adjustments were made in consolidation so as to present the consolidated financial statements on a uniform basis. The margins included in the invoices issued by subsidiaries to Telefónica for installations are eliminated at the time of the transaction, and this income is recognized as the related installations are depreciated.

The revenues and expenses through the aforementioned date of companies which have left the Group, and those of the companies which joined the Group from that date through year-end, are recorded in the consolidated statement of income.

The equity of the minority interests in the net worth and results of the consolidated dependent companies consolidated by the global integration method is recorded under the "Minority Interests" and "Income Attributed to Minority Interests" captions (see Note 12).

In accordance with standard practice in Spain, the accompanying consolidated financial statements do not include the tax effect, if any, of transferring the reserves of the consolidated subsidiaries to the controlling company's accounts, since it is considered that such reserves will be used to finance their operations and that those that may be distributed will not give rise to a material additional tax cost.

c) Comparative information

In 1997 the "Long-Term Prepaid Taxes" caption was included under "Long-Term Financial Investments", and the "Long-Term Deferred Taxes" caption under "Long-Term Taxes Payable", except for the credits for deferred investments, which were included under the "Deferred Revenues" caption. The 1996 information was reclassified for comparison purposes (see Notes 14 and 18).

The figures contained in the financial statements, balance sheet, statement of income, notes to financial statements and management report are stated in millions of pesetas unless otherwise stated.

In 1997 the Group changed its method of recording exchange differences arising on foreign currency loans obtained by Telefónica Internacional de España, S.A. to finance foreign investments, in accordance with the resolution of the Spanish Accounting and Audit Institute (ICAC) dated December 19, 1997.

Had this method been applied in the 1996 financial statements, income for the year would not have been altered and net worth would have been increased by Ptas. 2,277 million.

d) Changes in the consolidated Group

The main changes in the consolidated Group in 1997 and 1996 were as follows:

1997

In November Telefónica acquired from SEPPA 23.78% of its shares in Telefónica Internacional de España, S.A. (T.I.) for Ptas. 127,000 million. As a result of this acquisition, the Telefónica Group's percentage of ownership in T.I.'s dependent companies increased by the same proportion. The outstanding amount payable (Ptas. 88,000 million) was recorded under the "Other Nontrade Payables" caption (see Note 19).

Telefónica sold 25% of its shares of Unisource, N. V. to Telia AB, PTT and Telecom BV and Swisscom. This purchase and sale transaction was carried out for a total price of Fl 465 million (Ptas. 34,921 million).

Telefónica acquired all the shares of Telefónica Transmisión de Datos, S.A. (TTD) and Telefónica VSAT, S.A. (VSAT), for Fl 455 million and Fl 10 million, respectively. TTD and VSAT are consolidated by the global integration method.

In addition, the Group increased its holding in Cointel from 33.16% to 50%, involving a disbursement of Ptas. 80,423 million. In December 1997 CTC acquired the remaining 45% of Startel, S.A., bringing its holding to 100%. The purchase price was US\$ 425 million (Ptas. 64,473 million), and this amount was included under the "Other Long-Term Debt" caption in the accompanying balance sheet.

In August Telefónica Multimedia, S.A. acquired 25% of the capital stock of Antena 3 de Televisión, S.A. for Ptas. 26,004 million. The company is carried by the equity method.

In July Telefónica Multimedia, S.A. acquired 49% of the capital stock of Gestora de Medios Audiovisuales de Fútbol, S.L. for Ptas. 18,545 million. This holding was subsequently sold to Telefónica Medios de Comunicación, S.A. The company is carried by the equity method.

In January Telefónica participated in the incorporation of DTS Distribuidora de Televisión Digital, S.A., subscribing 35% of its capital stock for Ptas. 3,500 million. In May, the aforementioned company was sold to Telefónica Multimedia, S.A. In November DTS increased its capital and T. Multimedia subscribed its corresponding share of capital stock for Ptas. 5,250 million. The company is carried by the equity method.

From January 1, 1997, CRT, a company which was acquired in December 1996, became a member of the consolidated Group, having been carried at cost at 1996 year-end. The Group's ownership interest in the aforementioned company amounts to 10.3% of its total common and preferred shares of capital stock, through the various holdings owned by Group companies in the consortium which was awarded 35% of the company's common voting stock.

In October, Telefónica acquired 3.5% of the capital stock of Portugal Telecom, S.A., for Ptas. 41,212 million. The company is carried by the equity method.

1996

Telefónica acquired 25% of Unisource N.V. by exchanging all the shares of Telefónica Transmisión de Datos, S.A. and Telefónica V.S.A.T., S.A. Unisource N.V. is carried by the equity method (see Notes 8D.1 and 8D.2).

On December 17, 1996, the consortium led by Telefónica Internacional de España, S.A. ("Telefónica Internacional") submitted the successful bid in an international call for tender for the acquisition of 35% of the voting stock of Companhia Riograndense de Telecomunicações (CRT), equivalent to 13.45% of the latter's stock with dividend rights, for 681 million reales. The portion of the holding acquired and attributable to the Telefónica Group represents 7.87% of the company's total capital stock. The companies participating in the consortium with Telefónica Internacional are R.B.S. Participações, S.A., Companhia de Telecomunicações de Chile, S.A. Telefónica de Argentina, S.A. and Citicorp.

The acquisition of the aforementioned shares was formally executed on December 30, 1996. The holding in this company was recorded at cost as of December 31, 1996, and was carried by the equity method in 1997.

Telefónica sold its entire holding in Sistemas e Instalaciones de Telecomunicación, S.A. (SINTEL - see Note 8). Accordingly, Sintel Perú, S.A. and Sintelar, S.A. (each 25% owned by Telefónica Internacional and 38% and 50% owned, respectively, by Sintel, S.A.), are now carried by the equity method.

Telefónica Internacional acquired 25% of the Argentine companies Multicanal, S.A. and PEM, S.A., both of which are carried by the equity method.

STARTEL, S.A., a CTC Group company, was incorporated in 1996 as a result of agreements entered into on March 11, 1996, between CTC-Celular and VTR-Comunicaciones Móviles, S.A. to jointly operate in the cellular telephony business. CTC's and VTR's holdings of 55% and 45%, respectively, in the new company, were obtained through the contribution of 75% and 25% of STARTEL, S.A.'s assets, respectively, and through the subsequent sale of 20% of the company's capital stock for US\$ 67 million. As a result of this sale, the Telefónica Internacional Group recorded extraordinary income of Ptas. 2,444 million, net of taxes and the equity of minority interests, the gross amount of which (Ptas. 6,597 million) is recorded under the "Gains on Disposals of Holdings in Consolidated Companies" caption in the accompanying statement of income.

3. DISTRIBUTION OF THE INCOME OF THE CONTROLLING COMPANY

The proposed distribution of 1997 income that the Board of Directors will submit for approval by the Stockholders' Meeting is as follows:

	Millions of Pesetas
BASIS OF DISTRIBUTION	
1997 net income	133,774
Prior year's retained earnings	137
Total amount to be distributed	133,911
DISTRIBUTION TO:	
Interim dividend of 8%, declared on January 19, 1998	37,579
Supplementary dividend of 12.4%, pending approval	58,246
Dividends	95,825
Voluntary reserve	38,000
Retained earnings	86
Total amount distributed	133,911

Interim dividend

In accordance with Article 216 of the revised Corporations Law, on December 17, 1997, the Board of Directors, based on the economic and financial information submitted to it, approved the distribution of an interim dividend of Ptas. 40 gross per share out of 1997 income.

The accounting statement prepared in accordance with legal requirements (Article 216 of the revised Corporations Law), evidencing the existence of sufficient liquidity for the distribution of the interim dividend for 1997, was as follows:

	Millions of Pesetas
Accounting Statement Supporting Liquidity for Distribution of Interim Dividend:	
Income from January 1, 1997, to November 30, 1997	121,780
1996 retained earnings	137
Mandatory appropriation to reserves	—
Distributable income	121,917
Proposed interim dividend	37,579
Financial position (forecast at 11/30/97):	
Distributable funds:	
Cash	2,552
Available credit	108,162
Proposed interim dividend	(37,579)
Difference	73,135

The proposed distribution of the income of Telefónica de España, S.A. that will be submitted for approval by the next Stockholders' Meeting will be accompanied by a request for the distribution of a supplementary dividend for 1997 of Ptas. 62 gross per share.

4. VALUATION STANDARDS

The main valuation methods applied in preparing the consolidated financial statements for 1997 and 1996 were as follows:

a) Goodwill in consolidation

The accompanying 1997 and 1996 consolidated balance sheets include goodwill, net of amortization, arising from the positive difference in consolidation between the amounts paid to acquire the shares of the dependent companies consolidated or carried by the equity method and their underlying book values at the acquisition date.

Goodwill is amortized on a straight-line basis over ten years, since this is the period over which it is estimated that the goodwill will contribute to obtaining income at the Group.

b) Translation methods (year-end exchange rate method)

The financial statements of the Group companies abroad were translated to pesetas at the exchange rates ruling at year-end, except for:

1. Capital stock and reserves, which were translated at historical exchange rates.
2. Income statements, which were translated at the average exchange rate for the year.
3. The companies using accounting methods that include inflation adjustments apply the accounting standards in force in their respective countries, which consist of valuing monetary assets and liabilities at face value and adjusting the historical cost of nonmonetary assets by the inflation from the date of inclusion of the asset in the company's balance sheet to year-end. The effect of the year's inflation on the monetary assets and liabilities is included in the statement of income for the year.

The exchange difference arising from application of these procedures is included under the "Stockholders' Equity - Translation Differences in Consolidation" caption in the accompanying consolidated balance sheets, net of the portion of said difference relating to minority interests, which is recorded under the "Minority Interests" caption on the liability side of the accompanying consolidated balance sheets.

c) Start-up expenses

Start-up expenses, which comprise incorporation and capital increase expenses, are recorded at cost and are amortized on a straight-line basis over five years.

d) Intangible assets

This caption in the accompanying consolidated balance sheets includes the following items:

Research and development expenses

These relate to the costs incurred in developing new products to be marketed or used for the Group's own network, which are amortized by the straight-line method over five years. Costs incurred in projects which are not viable for the future are expensed currently.

Rights on leased assets

The rights under financial lease contracts are recorded at the cost of the related assets, and the total debt for lease payments plus the amount of the purchase option are recorded as a liability. The difference between the two amounts, which represents the interest expenses on the transaction, is recorded as a deferred expense and is allocated to income each year by the interest method. The existing contracts, which relate to computer hardware, are amortized by the straight-line method over five years, which coincides with the years of useful life of the hardware.

Software licenses

Software licenses are recorded at cost and are amortized by the straight-line method over three years.

Other intangible assets

This caption includes other intangible assets; the main items relate to the costs incurred in acquiring capacity and rights of way in other operators' cables. These rights are amortized on a straight-line basis over 25 years.

The administrative concessions related to a concession granted by the Peruvian Government to CPT and Entel Perú at the time of acquisition of these two companies by Telefónica Internacional. It is recorded at the difference between the acquisition cost and the proportional part of the equity of the companies acquired at that date, adjusted by estimates of certain costs to be incurred in the merger and restructuring of these two companies' operations. This intangible asset will be amortized over 20 years (the concession period) and on the basis of the number of lines installed, since this is the variable which determines the obtaining of revenues allocable to the concession.

e) Property and equipment

Property and equipment is carried at cost revalued pursuant to the applicable enabling legislation from 1946 to 1996, including Royal Decree-Law 7/1996 (see Note 7). If the regulations applicable in each country so require, the property and equipment is valued at cost or appraisal value adjusted by inflation.

Cost includes external costs plus internal costs comprising materials used, direct labor used in installation work and the allocable portion of the indirect costs required for the related investment. The latter two items are recorded as revenue under the "Capitalized Expenses of In-House Work on Fixed Assets" caption.

The costs of expansion, modernization or improvements leading to increased productivity, capacity or efficiency or to a lengthening of the useful lives of the assets are capitalized.

Upkeep and maintenance expenses are expensed currently.

The companies depreciate their property and equipment by the straight-line method at annual rates based on the years of estimated useful life, calculated in accordance with technical studies conducted by Telefónica and the Group companies, reviewed periodically based on technological advances and the rate of dismantling, as follows:

	Years of Estimated Useful Life
Buildings	30 - 50
Power equipment	10 - 20
Switching equipment	7 - 17
Transmission equipment	5 - 14
Local and domestic long-distance networks	7 - 25
Subscriber equipment and other installations	4 - 8
Furniture, office equipment and other	4 - 15

The increases in value resulting from the revaluations are depreciated over the years of residual useful life of the revalued assets.

f) Long- and short-term financial investments

Equity securities representing holdings in dependent companies not consolidable by the global integration method or in other companies in which the Group has a holding of 20% or more (3% for listed companies) which do not meet the conditions for consolidation by the proportional integration method, are carried by the equity method. The recording of these holdings was based on the provisional financial statements provided by these companies, which, according to the reviews made, will not differ significantly from their definitive financial statements.

Shareholdings which were not consolidated were recorded in the consolidated balance sheet at the lower of cost or market.

The market value was determined as follows:

1. Listed securities:

The market value was taken to be the lower of average market price in the last quarter or market price at year-end.

2. Unlisted securities:

At cost, net, if appropriate, of the required provisions for depreciation if cost was higher than underlying book value at year-end.

Unrealized losses (cost higher than market or book value at year-end) are recorded in the "Provision for Financial Investments" account.

g) Deferred charges

This caption in the accompanying consolidated balance sheets includes the following items:

Debt arrangement expenses

These relate to long-term debt arrangement expenses and paid-in surpluses on debentures and bonds and are amortized by the interest method on the basis of the principal amounts outstanding.

Interest on promissory notes

This relates to the difference between the par value and the effective issue value of the promissory notes issued at over one year. This interest is charged to income by the interest method.

Interest on financial lease contracts

This relates to the interest expenses on financial lease contracts, which are charged to income by the interest method (see Note 4-d).

Supplementary pension payments to retired employees (shortfall)–

These relate to the shortfall in the provisions recorded for the commitments made by Telefónica to retired employees as of June 30, 1992. Since then, the shortfall has been allocated to income over 15 years by the straight-line method, in accordance with the communication obtained from the Accounting and Audit Institute dated March 1, 1993. On November 1, 1997, an external fund had been set up for these commitments (see Notes 4-l and 14).

h) Inventories

Warehouse materials for installation in capital expenditure projects and consumables and replacement parts are valued at the lower of weighted average cost, monetarily adjusted in the countries whose legislation so requires, or market.

Obsolete, defective or slow-moving inventories have been reduced to realizable value. The provisions for depreciation of inventories are recorded on the basis of age and turnover.

i) Treasury stock

Treasury stock is valued at the lower of cost, comprising the total amount paid or to be paid for acquisition, or market. Market value is the lower of average market price in the last quarter of the year or year-end market price.

j) Capital subsidies

Capital subsidies are valued at the amount granted and are allocated to income on a straight-line basis over a maximum period of ten years, which does not differ materially from the estimated useful life of the subsidized assets.

The main subsidies obtained were granted as follows:

Grantor	Reason for Granting
Official agencies, autonomous community governments and regional and local authorities	Extension of supply to rural areas
European Union	Promotion and development of telecommunications activities
European Union (FEDER Program)	Infrastructures for depressed areas

Most of the aforementioned subsidies were granted to the parent company and all the subsidy grant requirements are being met in all cases.

k) Foreign currency transactions

Fixed-income securities and receivables and payables denominated in foreign currencies are translated to pesetas at the exchange rates ruling at the transaction date, and are adjusted at year-end to the exchange rates then prevailing.

Exchange differences arising on adjustment of foreign currency accounts payable and receivable to year-end exchange rates are classified by currency and due date, and for this purpose currencies which, although different, are officially convertible are grouped together.

The positive net differences in each group of currencies are recorded under the "Deferred Revenues" caption on the liability side of the consolidated balance sheet, unless exchange losses in a given group have been charged to income in prior years, in which case the net positive differences are credited to period income up to the limit of the negative net differences charged to income in prior years.

The positive differences deferred in prior years are credited to income in the year in which the related accounts receivable and payable fall due or are repaid early, or as negative exchange differences for the same or a higher amount are recognized in each homogeneous group.

In accordance with a Ministry of Economy and Finance Order dated March 12, 1993, which adapts the foreign currency transaction valuation method in the Spanish National Chart of Accounts for certain companies, including Telefónica, exchange losses arising in the year must be allocated by the interest method over the term of the transaction. Pursuant to this Order, Telefónica applied the foregoing method to its foreign currency debts.

In view of the foreseeable full deregulation of telecommunications from January 1, 1998, in 1995 Telefónica only deferred exchange losses relating to debts maturing in 1996 and 1997 and wrote off, with a charge to income, those relating to debts maturing subsequent to 1997.

In 1996 the Company recorded, with a charge to income, the exchange losses relating to debts maturing in 1996 and new exchange losses relating to debts maturing subsequent to 1997. The exchange losses relating to debts maturing in 1997 were recorded under the "Deferred Expenses" caption.

In 1997 the Company recorded with a charge to income all the exchange losses arising in the year and those deferred from prior years (see Note 9).

Since 1997 exchange gains or losses arising from specific financing of foreign currency investments in investee companies to hedge the exchange rate risk in these investments have been recorded under the "Translation Differences in Consolidation" caption in the consolidated balance sheet.

In order for these transactions to be deemed to be hedging transactions, they must meet certain requirements. Most notably, the foreign currency in which the financing is denominated must be the same as or match the functional currency of the investment and of the flows generated by it, and that anticipated flows of dividends and management fees must match the loan repayments. As mentioned in Note 2-c, had this method been applied in the 1996 financial statements, the effect on income for the year would have been zero and net worth would have increased by Ptas. 2,277 million.

1) Pension and similar commitments

Through December 31, 1991, Telefónica de España, S.A. personnel benefited from a social welfare system provided by Institución Telefónica de Previsión (ITP). A Ministry of Labor and Social Security Order dated December 30, 1991, provided for the inclusion of the serving and retired employees of ITP be included in the general social security system. Since January 1, 1992, Telefónica and its employees have been contributing to the general social security system.

The methods used to record and calculate the commitments arising from the aforementioned event are as follows:

1) Cost of including pensioners in the social security system

A resolution issued by the Directorate-General of Planning and Economic Organization of the Social Security System on May 25, 1992, stipulated that the cost of including ITP pensioners in the social security system would amount to Ptas. 130,683 million. ITP had to pay this amount to the social security authorities as follows.

1. An initial payment of Ptas. 75,000 million.
2. The remaining Ptas. 55,683 million will be paid in constant annual installments over a period of ten years, with a two -year grace period, with interest at 8%.

Since ITP does not have sufficient resources to meet the payments, Telefónica, although secondarily liable, has been contributing the necessary funds to the social security authorities to make the payments. As of December 31, 1996, the outstanding debt amounted to Ptas. 38,688 million, for which Telefónica has recorded the related provisions under the "Provisions for Contingencies and Expenses" caption (see Note 14). On November 21, 1997, I.T.P. was finally liquidated. Accordingly, a resolution issued by the Ministry of Labor's Directorate-General of Social Security on November 24, 1997, stipulated that Telefónica is directly liable to the social security authorities for the outstanding debt plus the related interest. Telefónica proceeded to make early repayment of this debt (Ptas. 38,688 million) plus the interest incurred through that date (Ptas. 2,815 million), and these amounts were recorded under the "Extraordinary Expenses" caption (see Note 20). As a result of this transaction, Ptas. 7,301 million were recorded under "Deferred Revenues" (see Note 18) due to the accrual for accounting purposes of the tax credit taken.

2) Cost of including serving employees in the social security system

As a result of the inclusion of serving employees in the social security system, Telefónica must make additional contributions to the social security system during a period of 25 years, based on the serving employees' effective contribution bases at every given moment. These contributions consist of the payment of an additional 1% during the first four years and of an additional 2.2% over the remaining 21 years, and the related amounts are recorded under the "Personnel Expenses" caption. Ptas. 5,715 million and Ptas. 5,675 million were recorded in this connection in 1997 and 1996, respectively.

In 1992, Telefónica entered into a collective labor agreement, pursuant to the Workers' Statute, with the workers' representatives for the creation of a pension plan for serving employees. The agreement also recognized the entitlement of retired employees to receive pension payments supplementing their social security pensions. The commitments undertaken and the methods for recording them are as follows:

1) Pension plan for serving employees

Following an offer made on June 30, 1992, and accepted by the workers on September 17, 1992, Telefónica reached a collective labor agreement, pursuant to the Workers' Statute, with the workers' representatives. The main features of the pension plan are as follows:

Creation of a pension plan pursuant to Pension Plans and Funds Law 8/1987 with the following features:

- Employment system pension plan.
- Defined contribution.
- Mandatory contributions by the participating employees.
- Individual and financial capitalization.

Contribution by the promoter of 6.87% of the participating employees' regulatory base salary. For employees who joined Telefónica after June 30, 1992, the contribution is 4.51% of the regulatory base salary.

The obligatory contribution of the participants will be a minimum of 2.2% of his/her regulatory base salary.

The plan came into effect on July 1, 1992. The past service benefits recognized for employees availing themselves of the plan amounted to Ptas. 228,489 million, which, in accordance with the Rebalancing Plan approved on July 18, 1995, by the Directorate-General of Insurance and by a Ministry of Economy and Finance Resolution dated April 24, 1996, will be financed as follows:

1. Telefónica will contribute the Ptas. 121,350 million that it had recorded under the "Long-Term Debt - Other Accounts Payable" caption. This amount will be transferred to the pension plan through the year 2000 at an annual effective interest rate of 6.7%. Ptas. 48,273 million were recorded under the foregoing caption and pending transfer as of December 31, 1997.
2. In accordance with the communication obtained from the Accounting and Audit Institute dated March 1, 1993, the resulting shortfall (Ptas. 107,139 million) must be contributed to the pension plan within 28 years in monthly installments payable in advance at an annual interest rate of 6%. The Company records provisions for the shortfall over 28 years pursuant to a systematic plan, with installments increasing each year by a rate of 1.042 through the year 2002 and based on the Rebalancing Plan thereafter. The provision for 1997 was Ptas. 4,876 million (Ptas. 4,677 million in 1996). The resulting cumulative difference (Ptas. 12,472 million as of December 31, 1997) between the provisions recorded and the contributions made to the pension plan is recorded in the "Provisions for Contingencies and Expenses - Provisions for the Rebalancing Plan" account (see Note 14).

In accordance with the conditions for adhesion to the Plan, transfers have been made for a total amount of Ptas. 149,682 million, as follows:

	Transfer Plan		Unprovisioned Shortfall		Extraordinary Contribution	Total
	Principal	Interest	Principal	Interest		
Through 12/31/95	44,446	23,652	7,661	20,276	1,883	97,918
Transferred in 1996	13,961	4,486	1,625	5,531	578	26,181
Transferred in 1997	14,670	3,556	1,525	5,438	394	25,583
Total	73,077	31,694	10,811	31,245	2,855	149,682

As of December 31, 1997, the principal not yet transferred to the Fund, which is managed by Fonditel, Entidad Gestora de Pensiones, S.A., amounted to Ptas. 141,746 million, of which Ptas. 81,001 million related to the unprovisioned shortfall.

67,618 employees had joined the Plan as of December 31, 1997 (67,135 at the same date in 1996). The retirement, disability and death benefits earned affected a total of 5,583 participants in 1997 (4,615 in 1996).

2) Supplementary pension payments to retired employees

On July 8, 1992, Telefónica reached an agreement with its employees whereby it recognized supplementary pension payments for employees who were retired as of June 30, 1992, equal to the difference between the pension payable by the social security system and that which would be paid to them by ITP. Once the aforementioned supplementary pension payments have been quantified, they become fixed, lifelong and nonrevaluable. 60% of the payments are transferable to the spouse recognized as such as of June 30, 1992, and to underage children.

In accordance with an actuarial study conducted by Telefónica, applying GRM-F80 tables and an assumed interest rate of 8%, as of June 30, 1992, the discounted present value of the commitments amounted to Ptas. 132,025 million, and this amount was recorded under the "Provisions for Contingencies and Expenses" caption. Through that date, the Company had recorded provisions totaling Ptas. 14,356 million in this connection. The resulting underprovision (Ptas. 117,669 million) was recorded under the "Deferred Charges" caption and has been allocated to income since that date by the straight-line method over 15 years, the estimated remaining life of the retired employees (1992-2007).

At each year-end the Company updates this actuarial study by adapting the assumed interest rate used to the market rate (see Note 9). Accordingly, in 1996 the interest rate fell from 8% to 6.5%, which increased the value of the necessary provision by Ptas. 10,597 million. This provision was recorded with a charge to "Deferred Expenses", and is allocated to income over the expected average life of the retired employees from January 1, 1996, i.e. 11.5 years.

In 1997 the Company, as a result of application of the new GRM/F-80-2 tables, adjusted the value of the necessary provision by Ptas. 10,048 million. In addition, the assumed interest rate fell from 6.5% to 6.3%, leading to an increase of Ptas. 1,841 million in the provision. Both amounts were recorded with a charge to "Deferred Expenses" which, in accordance with the method described above, will be adjusted over 10.5 years.

The increase in the present discounted value due to the financial provisions to the fund are recorded as an expense under the "Other Financial Expenses on Debt and Similar Expenses" caption (see Note 20).

Under Private Insurance Law 30/1995, on November 1, 1997, these commitments were externalized to the Group company, Seguros de Vida y Pensiones Antares, S.A. A first payment of Ptas. 28,846 million, equal to the provisions already recorded, was made and the remainder will be contributed over a period of seven years. Antares has used these amounts to arrange a Deposit contract with various finance entities to eliminate the possible risk of future interest rate fluctuations on the outstanding payments.

3) *Group life insurance*

Retired employees who did not join the pension plan continue to be entitled to receive survivorship benefits at the age of 65. The Company has recorded an internal allowance to cover these commitments, based on the actuarial studies conducted internally, applying the GRM/F-80-2 mortality table and an assumed interest rate of 6%. As of December 31, 1997 and 1996, this allowance amounted to Ptas. 13,376 million and Ptas. 13,219 million, respectively, and was recorded under the "Provisions for Contingencies and Expenses" caption (see Note 14).

An external fund must be created for this commitment pursuant to Private Insurance Law 30/1995, within the time limits established in Transitory Provision 14 thereof.

In 1997 Telefónica entered into a Loyalty-Building Plan with a considerable proportion of the Group's executives, whereby Telefónica undertakes to pay them, on February 25, 2000, certain amounts calculated on the basis of the market price of Telefónica's shares and of a maximum number of shares acquired directly by each executive in the market.

In order to meet the payments which may arise under this plan, the Company has arranged with two finance entities the purchase of options on Telefónica shares which would fully cover such payments. The cost of these options will be deferred over three years until the Plan matures. Ptas. 700 million were recorded in this connection in 1997 with a charge to the "Extraordinary Expenses and Losses" caption.

In addition, in January 1998 the Board of Directors of Telefónica Internacional, S.A. resolved to grant to a significant group of executives option rights to purchase a total of 77,985 shares of Telefónica Internacional, S.A. (0.65% of its capital stock). This option may be exercised in a staggered manner over a period of three years, starting in 1998, at the same price at which they were acquired by Telefónica Internacional, S.A. from Telefónica de España, S.A. This price is the same as that paid by Telefónica de España, S.A. to SEPPA on November 7, 1997 (see Note 2-d).

m) Provisions for voluntary pre-retirements and early retirements

The deregulation of the telecommunications industry in Spain made it necessary to adapt the labor force to Telefónica's actual needs and, accordingly, the voluntary "preretirement" and early retirement plan initiated in 1994 and ratified in the 1997/1998 Collective Labor Agreement was continued.

The 1997/1998 Collective Labor Agreement provides for "preretirement" of employees above 57 years of age and/or subsequent early retirement of employees above 60 years of age, at the employee's request and subject to acceptance by the company and to certain agreed-upon financial conditions.

In addition, only in 1997, employees over the age of 55 may opt for "preretirement" under the same terms. The Collective Labor Agreement also envisages the possibility of new plans for the future.

Telefónica records with a charge to income, in accordance with a systematic plan, the amounts required to ensure that the provision for "preretirement" and early retirement is recorded in full at the date on which the employee is terminated, both for employees whose applications have been approved and those who, according to estimates prepared by Company management, might qualify through the year 2000, in order to achieve the desired labor force optimization (see Note 14).

n) Technical provisions

This caption relates mainly to mathematical provisions for life insurance, pension and reinsurance commitments taken on by Seguros de Vida y Pensiones Antares, S.A. and Casiopea Re. These provisions are credited when the commitments covered are paid. The provisions recorded in 1997 relate mainly to the externalization of pension supplements for retired employees (see Note 14).

o) Accounts payable

Accounts payable are recorded at redemption value, except for zero-coupon debenture and bond issuances made through December 31, 1997, which are recorded in the balance sheet at issue value plus earned interest (see Note 15).

p) Derivatives

Transactions aimed at eliminating or significantly reducing exchange, interest rate or market risks on balance sheet positions or on other transactions are treated as hedging transactions. Gains or losses arising over the life of these derivatives are taken to the income statement using the same recognition method as that used for gains or losses on the asset and main transaction hedged by the derivatives, incorporating them in that outcome (see Note 17).

Transactions carried out to obtain returns rather than to hedge risks are not treated as hedge transactions. In transactions of this kind, the differences in market price are recorded for accounting purposes when the transactions are canceled or finally settled. However, if potential losses are anticipated at year-end, the related provision is recorded with a charge to the statement of income.

q) Corporate income tax

The expense for corporate income tax of each year is calculated on the basis of book income before taxes, increased or decreased, as appropriate, by permanent differences. Tax relief and tax credits, excluding tax withholdings and prepayments, are deducted from the corporate income tax charge in the year in which they are definitively taken, except in the case of investment tax credits earned from 1996, which, at the time when they are taken, are deferred over the average life of the assets which gave rise to the tax credits. The difference between the expense incurred and the tax paid is due to the above-mentioned deferral and to revenue and expense recognition timing differences giving rise to prepaid and deferred taxes (see Note 18).

r) Recognition of revenues and expenses

Revenues and expenses are recognized on an accrual basis, i.e. when the actual flow of the related goods and services occurs, regardless of when the resulting monetary or financial flow arises.

The revenues from telephony and other services are recognized on an accrual basis. These services are generally billed every two months. Uninvoiced revenues from the beginning of the billing cycle to the end of each month are estimated or recorded as soon as they are known. The differences between the estimated revenues and those subsequently invoiced are not material and are recorded in the following period. In accordance with the accounting principle of prudence, only realized income is recorded at year-end, whereas foreseeable contingencies and losses, including possible losses, are recorded as soon as they become known (see Note 20).

5. GOODWILL IN CONSOLIDATION

The detail of the balance of goodwill in consolidation, the related accumulated amortization and the variations therein in 1997 is as follows:

	Millions of Pesetas					
Goodwill in Consolidation	Balance at 12/31/96	Additions	Retirements	Transfers	Translation Differences	Balance at 12/31/97
Companies consolidated by the global integration method:						
C.T.C. (Chile)	5,508	—	—	—	—	5,508
Instacom	1,334	—	—	—	253	1,587
Intercom	(111)	—	—	—	(26)	(137)
Invercom	—	—	—	8,822	—	8,822
Multicable T.V. (Chile)	1,095	—	—	—	207	1,302
Publiguías (Chile)	426	—	—	—	—	426
Rem Infográfica	—	143	—	—	—	143
Servicios y Contenidos por la Red	126	—	—	—	—	126
Startel	—	56,801	—	—	—	56,801
T. Perú Holding	461	—	—	—	—	461
T..T. Datos	—	25,794	—	—	—	25,794
T.L.D. (Puerto Rico)	7,479	—	—	—	—	7,479
Telefónica Cable	—	127	—	—	—	127
Telefónica Internacional	—	46,865	—	—	—	46,865
TMP Worldwide	8	—	—	—	—	8
	16,326	129,730	—	8,822	434	155,312
Companies carried by the equity method:						
Antena 3	—	18,446	—	—	—	18,446
C.R.T.	—	85	—	42,813	—	42,898
Cointel (Argentina)	23,836	44,132	—	—	—	67,968
G.M.A. Futbol	—	8,957	—	—	—	8,957
Invercom	7,423	—	—	(8,822)	1,399	0
Lola Films	—	142	—	—	—	142
Multicanal	9,155	—	(9,155)	—	—	0
Portugal Telecom	—	30,657	—	—	—	30,657
Siris y DBKOM	1,130	—	(1,130)	—	—	0
Sofres, A.M.	157	—	—	—	—	157
Unisource, N.V.	7,742	—	(7,742)	—	—	0
Venworld (Venezuela)	22,330	—	—	—	—	22,330
	71,773	102,419	(18,027)	33,991	1,399	191,555
Total goodwill	88,099	232,149	(18,027)	42,813	1,833	346,867

	Millions of Pesetas					
Amortization of Goodwill in Consolidation	Balance at 12/31/96	Additions	Retirements	Transfers	Translation Differences	Balance at 12/31/97
Companies consolidated by the global integration method:						
C.T.C. (Chile)	3,703	551	—	—	—	4,254
Instacom	399	141	—	—	48	588
Intercom	(28)	(13)	—	—	(9)	(50)
Invercom	—	849	—	2,247	30	3,126
Multicable T.V. (Chile)	148	126	—	—	33	307
Publigufas (Chile)	171	43	—	—	—	214
Rem Infográfica	—	143	—	—	—	143
Servicios y Contenidos por la Red	126	—	—	—	—	126
Startel	—	192	—	—	6	198
T. Perú Holding	97	46	—	—	—	143
T..T. Datos	—	15,860	—	—	—	15,860
T.L.D. (Puerto Rico)	2,992	748	—	—	—	3,740
Telefónica Cable	—	8	—	—	—	8
Telefónica Internacional	—	391	—	—	—	391
TMP Worldwide	8	—	—	—	—	8
	7,616	19,085	—	2,247	108	29,056
Companies carried by the equity method:						
Antena 3	—	768	—	—	—	768
C.R.T.	—	4,285	—	—	—	4,285
Cointel (Argentina)	7,898	5,804	—	—	—	13,702
G.M.A. Fútbol	—	622	—	—	—	622
Invercom	1,889	—	—	(2,247)	358	0
Lola Films	—	4	—	—	—	4
Multicanal	704	—	(704)	—	—	0
Portugal Telecom	—	511	—	—	—	511
Siris y DBKOM	1,130	—	(1,130)	—	—	0
Sofres, A.M.	157	—	—	—	—	157
Unisource, N.V.	7,742	—	(7,742)	—	—	0
Venworld (Venezuela)	11,165	2,233	—	—	—	13,398
	30,685	14,227	(9,576)	(2,247)	358	33,447
Total accumulated amortization	38,301	33,312	(9,576)	—	466	62,503
Unamortized goodwill in consolidation	49,798	198,837	(8,451)	42,813	1,367	284,364

The detail of the balance of goodwill in consolidation, the related accumulated amortization and the variations therein in 1996 is as follows:

	Millions of Pesetas					
	Balance at 12/31/95	Additions	Retirements	Transfers	Translation Differences	Balance at 12/31/96
Companies consolidated by the global integration method:						
C.T.C. (Chile)	5,508	—	—	—	—	5,508
T.L.D. (Puerto Rico)	7,595	—	(116)	—	—	7,479
Publiguías (Chile)	426	—	—	—	—	426
T. Perú Holding	463	—	—	(2)	—	461
Multicable T.V. (Chile)	992	—	—	2	101	1,095
Invercom	6,710	—	—	(6,710)	—	—
Instacom	1,216	—	(126)	—	244	1,334
Intercom	—	(111)	—	—	—	(111)
Servicios y Contenidos por la Red	—	126	—	—	—	126
TMP Worldwide	—	8	—	—	—	8
	22,910	23	(242)	(6,710)	345	16,326
Companies carried by the equity method:						
Sofres, A.M.	157	—	—	—	—	157
Venworld (Venezuela)	19,982	—	—	2,348	—	22,330
Tepesa	7	—	(7)	—	—	—
Cointel (Argentina)	23,835	—	—	1	—	23,836
Multicanal	—	9,155	—	—	—	9,155
Invercom	—	—	—	6,648	775	7,423
Unisource, N.V.	—	7,742	—	—	—	7,742
Siris y DBKOM	—	1,130	—	—	—	1,130
	43,981	18,027	(7)	8,997	775	71,773
Total goodwill	66,891	18,050	(249)	2,287	1,120	88,099
Companies consolidated by the global integration method:						
C.T.C. (Chile)	3,151	551	—	1	—	3,703
T.L.D. (Puerto Rico)	2,360	748	(116)	—	—	2,992
Publiguías (Chile)	128	43	—	—	—	171
T. Perú Holding	52	46	—	(1)	—	97
Multicable T.V. (Chile)	35	105	—	1	7	148
Invercom	1,114	—	—	(1,114)	—	—
Instacom	230	130	(126)	—	165	399
Intercom	—	(8)	—	—	(20)	(28)
Servicios y Contenidos por la Red	—	126	—	—	—	126
TMP Worldwide	—	8	—	—	—	8
	7,070	1,749	(242)	(1,113)	152	7,616
Companies carried by the equity method:						
Sofres, A.M.	140	17	—	—	—	157
Venworld (Venezuela)	6,585	2,233	—	2,347	—	11,165
Tepesa	7	—	(7)	—	—	—
Cointel (Argentina)	5,402	2,495	—	1	—	7,898
Multicanal	—	704	—	—	—	704
Invercom	—	716	—	1,052	121	1,889
Unisource, N.V.	—	7,742	—	—	—	7,742
Siris y DBKOM	—	1,130	—	—	—	1,130
	12,134	15,037	(7)	3,400	121	30,685
Total accumulated amortization	19,204	16,786	(249)	2,287	273	38,301
Unamortized goodwill in consolidation	47,687	1,264	—	—	847	49,798

6. INTANGIBLE ASSETS

The detail of the balances of the intangible asset accounts and the variations therein in 1997 and 1996 are as follows:

Millions of Pesetas					
	Research and Development Expenses	Leased Assets	Software Licenses and Development	Other Intangible Assets	Total
Balance at 12/31/95	79,628	10,711	54,178	241,023	385,540
Additions	21,170	4,080	19,330	802	45,382
Retirements	—	—	(168)	(38)	(206)
Transfers	3,170	732	80	(2,155)	1,827
Inclusion of companies	—	—	—	—	—
Variation in exchange rate	79	1	52	295	427
Exclusion of companies	—	(99)	(6)	(57)	(162)
Balance at 12/31/96	104,047	15,425	73,466	239,870	432,808
Additions	19,683	2,192	27,997	1,171	51,043
Retirements	—	—	(553)	(237)	(790)
Transfers	(3,241)	(1,798)	201	4,663	(175)
Inclusion of companies	—	—	241	846	1,087
Variation in exchange rate	93	517	—	1,198	1,808
Exclusion of companies	—	—	—	(290)	(290)
Balance at 12/31/97	120,582	16,336	101,352	247,221	485,491

The main item included under the "Other Intangible Assets" caption was the administrative concession described in Note 4-d, for a gross amount of Ptas. 227,011 million, which decreased to Ptas. 204,501 million as a result of amortization.

The variations in the related accumulated amortization were as follows:

Millions of Pesetas					
	Research and Development Expenses	Leased Assets	Software Licenses and Development	Other Intangible Assets	Total
Balance at 12/31/95	28,862	1,969	27,292	10,178	68,301
Additions	11,768	1,784	5,846	6,863	26,261
Retirements	—	—	(63)	(46)	(109)
Transfers	536	(29)	55	(112)	450
Inclusion of companies	—	—	—	—	—
Variation in exchange rate	61	44	65	(57)	113
Exclusion of companies	—	(2)	(3)	(28)	(33)
Balance at 12/31/96	41,227	3,766	33,192	16,798	94,983
Additions	12,772	1,670	11,644	9,489	35,575
Retirements	—	—	(136)	(167)	(303)
Transfers	(1,191)	(1,634)	(17)	1,030	(1,812)
Inclusion of companies	—	—	66	423	489
Variation in exchange rate	65	91	—	468	624
Exclusion of companies	—	—	—	(174)	(174)
Balance at 12/31/97	52,873	3,893	44,749	27,867	129,382
1997 intangible assets, net	67,709	12,443	56,603	219,354	356,109
1996 intangible assets, net	62,820	11,659	40,274	223,072	337,825

7. PROPERTY AND EQUIPMENT

The detail of the balances of property and equipment, the related accumulated depreciation and the variations therein in 1997 is as follows:

	Millions of Pesetas							Balance at 12/31/97
	Balance at 12/31/96	Additions	Retirements	Inclusion of Companies	Exclusion of Companies	Exchange Differences	Transfers	
Cost:								
Land and structures	656,279	490	(2,556)	8	(18)	11,583	51,230	717,016
Technical installations and machinery	130,487	6,506	(6,347)	408	(45)	2,769	25,614	159,392
Telephone installations, networks and equipment	5,598,023	73,065	(288,417)	48,371	(3,277)	148,274	459,616	6,035,655
Furniture, tools and other	237,582	14,449	(4,319)	1,148	(182)	9,337	(1,604)	256,411
Total property and equipment in service	6,622,371	94,510	(301,639)	49,935	(3,522)	171,963	534,856	7,168,474
Net variation in construction in progress	327,861	552,946	(89)	6,852	—	22,325	(513,430)	396,465
Advances to fixed asset suppliers	23,640	(6,766)	(19)	—	—	2,222	(16,789)	2,288
Installation materials in warehouses	50,804	(6,734)	(165)	—	(41)	2,351	(7,238)	38,977
Total property and equipment	7,024,676	633,956	(301,912)	56,787	(3,563)	198,861	(2,601)	7,606,204
Accumulated depreciation:								
Structures	148,177	20,043	(993)	1	(2)	3,482	40	170,748
Technical installations and machinery	71,599	11,124	(5,641)	160	(22)	1,137	6,940	85,297
Telephone installations, networks and equipment	2,682,757	518,651	(252,011)	34,951	(695)	58,707	(1,550)	3,040,810
Furniture, tools and other	148,273	15,654	(3,348)	314	(77)	5,064	(4,644)	161,236
Total accumulated depreciation	3,050,806	565,472	(261,993)	35,426	(796)	68,390	786	3,458,091
Property and equipment, net	3,973,870	68,484	(39,919)	21,361	(2,767)	130,471	(3,387)	4,148,113

The detail of the balances of property and equipment, the related accumulated depreciation and the variations therein in 1996 is as follows:

	Millions of Pesetas								Balance at 12/31/96
	Balance at 12/31/95	Additions	Retirements	Inclusion of Companies	Exclusion of Companies	Exchange Differences	Transfers	Account Restatement	
Cost:									
Land and structures	570,203	643	(4,098)	90	(900)	4,638	33,896	51,807	656,279
Technical installations and machinery	135,885	3,855	(6,752)	—	(1,029)	—	(1,472)	—	130,487
Telephone installations, networks and equipment	5,285,469	80,178	(430,982)	2,619	—	59,547	429,028	172,164	5,598,023
Furniture, tools and other	231,059	13,702	(6,521)	1,117	(5,365)	6,170	(4,461)	1,881	237,582
Total property and equipment in service	6,222,616	98,378	(448,353)	3,826	(7,294)	70,355	456,991	225,852	6,622,371
Net variation in construction in progress	291,302	564,848	(69)	—	—	6,936	(535,156)	—	327,861
Advances to fixed asset suppliers	10,574	5,812	(238)	—	—	47	7,445	—	23,640
Installation materials in warehouses	14,014	7,338	—	—	—	(183)	29,635	—	50,804
Total property and equipment	6,538,506	676,376	(448,660)	3,826	(7,294)	77,155	(41,085)	225,852	7,024,676
Accumulated depreciation:									
Structures	133,389	14,196	(729)	8	(142)	1,477	(22)	—	148,177
Technical installations and machinery	68,861	9,066	(5,950)	—	(601)	—	223	—	71,599
Telephone installations, networks and equipment	2,605,859	454,045	(381,334)	234	—	21,977	(18,024)	—	2,682,757
Furniture, tools and other	132,971	23,674	(6,170)	100	(3,727)	2,329	(904)	—	148,273
Total accumulated depreciation	2,941,080	500,981	(394,183)	342	(4,470)	25,783	(18,727)	—	3,050,806
Property and equipment, net	3,597,426	175,395	(54,477)	3,484	(2,824)	51,372	(22,358)	225,852	3,973,870

The installation materials in warehouses are recorded net of provisions, which amounted to Ptas. 4,126 million as of December 31, 1997 (Ptas. 5,936 million in 1996). The provision for inventory depreciation recorded in 1997, based on actual diminution in value, amounted to Ptas. 888 million (Ptas. 2,496 million in 1996).

The "Inclusion of Companies" account in 1996 includes the variations in property and equipment as a result of the merger of the Chilean companies VTR and CTC Celular, since this merger resulted in the contribution of assets to the Group. The main variations in this account in 1997 relate mainly to the inclusion in the Group of Telefónica Transmisión de Datos (TTD), Telefónica VSAT and Hispaservices.

The "Exclusion of Companies" account in 1996 includes the accumulated balances as of December 31, 1995, of the Sintel Group companies, Tepesa, Telefónica Transmisión de Datos (TTD), Sociedad General de Cablevisión and Telefónica VSAT, since they were excluded from the consolidated Group in 1996. In 1997 this account includes the balances relating to Telefónica Romanía.

The "Exchange Differences" column includes both the effect of the variation in exchange rates on the beginning balances and the monetary adjustment applied by certain companies to their balances to adjust for inflation, in accordance with the accounting practices in their respective countries. The effect of exchange rates on the period variations is included under the appropriate column for each variation.

As of December 31, 1997 and 1996, the following items had been fully depreciated:

	Millions of Pesetas	
	1997	1996
Buildings	8,525	7,201
Power equipment	30,176	26,583
Switching equipment	355,287	334,529
Transmission equipment	125,264	157,050
Local and domestic long-distance networks	224,613	160,350
Subscriber equipment and other installations	166,953	155,987
Furniture, office equipment and other	107,256	87,454
Total	1,018,074	929,154

Telefónica's fixed assets used to provide telephone services cannot be mortgaged without government authorization.

Telefónica has taken out insurance policies to cover the possible risks affecting its property and equipment used in operations, except for the franchise existing in policies in force for local and domestic long-distance networks and subscriber equipment.

On December 31, 1996, Telefónica revalued its property and equipment pursuant to Royal Decree-Law 7/1996 and paid the related single 3% tax. The Company had previously revalued its accounts pursuant to the enabling legislation specifically applicable to Telefónica de España, S.A. The 1996 revaluation was performed by applying the maximum coefficients authorized under this Royal Decree-Law, with the 40% reduction provided for the effect of Company financing and observing the revaluation limit imposed by the market value of the revalued assets.

The revaluation surplus, net of the single 3% tax, was credited to the "Revaluation Reserves" caption, with a charge to the appropriate revalued asset accounts, without altering the recorded accumulated depreciation amount.

The net increase in value resulting from this revaluation will be depreciated over the tax periods in the remaining useful lives of the restated assets. It is estimated that the 1996 revaluation will increase the 1997 depreciation charge by approximately Ptas. 38,608 million.

	Millions of Pesetas	
	1997	1996
Cost	1,512,435	1,133,947
Accumulated depreciation	(511,793)	(374,528)
Total	1,000,642	759,419

8. LONG-TERM FINANCIAL INVESTMENTS

A) The detail of the balances of and variations in financial investments in 1997 and 1996, of the related provision for depreciation, and of the capital payments outstanding is as follows:

1. Variations in financial investments:

Millions of Pesetas									
	Balance at 12/31/95	Additions	Retirements	Transfers and Consol.	Balance at 12/31/96	Additions	Retirements	Transfers and Consol.	Balance at 12/31/97
Holdings in associated companies (Exhibit I)	85,339	35,350	(6,395)	2,023	116,317	195,061	(41,600)	(68,388)	201,390
Other holdings (Exhibit I)	45,875	85,276	(2,649)	38	128,540	70,433	(4,299)	(102,032)	92,642
Other loans	20,429	17,913	(19,416)	12,448	31,374	53,243	(10,679)	22,896	96,834
Long-term guarantees and deposits	1,262	409	(304)	2	1,369	548	(162)	(1)	1,754
Tax receivables	50,336	22,147	(2,354)	(122)	70,007	41,471	(18,650)	(65)	92,763
Total	203,241	161,095	(31,118)	14,389	347,607	360,756	(75,390)	(147,590)	485,383

In 1997 the transfers of holdings in associated companies related mainly to the calculation of the goodwill in consolidation of Antena 3, GMAF and Portugal Telecom (see Note 5), and the collection of the dividend from Cointel. The transfers of other holdings arose as a result of the assignment of CRT's goodwill (see Note 5) and the transfer of the financial investments of Seguros de Vida y Pensiones Antares, S.A. to the "Other Loans" caption.

The "Other Loans" caption includes the application of the mathematical provisions of the Group's insurance companies, mainly in government debentures, government debt securities and long-term deposits, which mature through 2027 and provide average returns of 8.14%. In addition, the "Short-Term Financial Investment - Short-Term Investment Securities" caption includes Ptas. 43,432 million recorded with a charge to commitments recorded as "Technical Provisions" (see Note 14).

2. Variations in the provision for depreciation of financial investments:

Millions of Pesetas									
	Balance at 12/31/95	Additions	Retirements	Transfers and Consol.	Balance at 12/31/96	Additions	Retirements	Transfers and Consol.	Balance at 12/31/97
Other holdings	3,928	1,702	(901)	—	4,729	133	(490)	472	4,844
Total	3,928	1,702	(901)	—	4,729	133	(490)	472	4,844
Total financial investments	199,313	159,393	(30,217)	14,389	342,878	360,623	(74,900)	(148,062)	480,539

3. Variations in capital payments outstanding:

Millions of Pesetas									
	Balance at 12/31/95	Additions	Retirements	Transfers and Consol.	Balance at 12/31/96	Additions	Retirements	Transfers and Consol.	Balance at 12/31/97
Group companies	10	—	(10)	—	—	918	—	(918)	—
Associated companies	184	169	(110)	—	243	378	(169)	—	452
Other companies	2,544	—	(36)	—	2,508	523	(2,457)	1	575
Total	2,738	169	(156)	—	2,751	1,819	(2,626)	(917)	1,027
Total financial investments, net	196,575	159,224	(30,061)	14,389	340,127	358,804	(72,274)	(147,145)	479,512

- B) Exhibit I to these notes to financial statements provides detailed information on the Group, associated and investee companies, the percentages of ownership therein and the consolidation method used.
- C) In 1995, in application of Law 29/1991, adapting certain tax concepts to EC Directives and regulations, Telefónica carried out the following transactions as part of the reorganization of its corporate group:

- Contribution of mobile telephony lines of business to the subsidiary Telefónica Servicios Móviles, S.A.
- By means of a share exchange transaction, Telefónica de España, S.A. contributed to Telefónica Publicidad e Información, S.A. all the capital stock of Estrategias Telefónicas, S.A.

The disclosures referred to in Article 14 of Law 29/1991 are included in the first annual report approved following the transactions.

- D) In 1996 Telefónica carried out the following transactions in accordance with Title VIII, Chapter VIII of Corporate Income Tax Law 43/1995:

- 1) Nonmonetary contribution of assets to Telefónica Transmisión de Datos, S.A. pursuant to Article 108 of Corporate Income Tax Law 43/1995.
- 2) By means of a share exchange transaction, Telefónica de España, S.A. contributed to Unisource, N.V. 1,208,149 shares of Telefónica Transmisión de Datos, S.A. and 26,200 shares of Telefónica VSAT, S.A., representing 100% of the capital stock of both companies. In exchange, it received 23,000 new shares of Unisource, N.V. of Fl. 1,000 par value each, representing 25% of its capital stock. The mandatory appraisal was carried out by an independent appraiser.

- E) Sale of shares of Unisource N.V.

Telefónica has left the Unisource consortium and, on December 29, 1997, it sold its 25% holding in Unisource, N.V. to Telia AB, PTT Telecom BV and Swisscom. In 1997, the Telefónica Group recorded Ptas. 4,696 million of losses attributable to Unisource, which were recorded under the "Share in Losses of Companies Carried by the Equity Method" caption.

This sale was made for Fl. 465 million (Ptas. 34,921 million at the acquisition date), giving rise to a capital gain of Ptas. 20,556 million.

Prior to the aforementioned transaction, in compliance with the related Company resolutions, Telefónica contributed Fl. 193 million (Ptas. 14,489 million) to Unisource's capital.

- F) Acquisition of Telefónica Transmisión de Datos, S.A. and Telefónica VSAT, S.A. shares.

Telefónica acquired all the shares of Telefónica Transmisión de Datos, S.A. and Telefónica VSAT, S.A. for a total of Fl. 455 million (Ptas. 34,170 million) and Fl. 10 million (Ptas. 751 million), respectively.

The purchase of Telefónica Transmisión de Datos, S.A. gave rise to goodwill of Ptas. 25,794 million in the consolidated financial statements. Ptas. 15,860 million of the foregoing amount was allocated to amortize goodwill in consolidation in the consolidated financial statements.

The remaining goodwill will be amortized over a maximum of 10 years.

- G) Acquisition of shares of Torneos y Competencias, S.A., Cablevisión, S.A. and Advance Telecomunicaciones, S.A.

In 1997 the Group acquired the following Argentinean companies, all with registered offices in Buenos Aires (Argentina):

Torneos y Competencias, S.A.: an Argentinean company whose main activity is the production of television programs relating to sports events, chiefly football, operating under various contracts granting it exclusive rights to this operation. In October 1997 T.I. acquired a 16.67% holding in this company for Ptas. 10,309 million. In January 1998 it acquired an additional 3.33%.

Cablevisión, S.A.: an Argentinean company which provides cable television services. In October 1997 T.I. acquired a 33.28% holding in this company for Ptas. 57,139 million.

Advance Telecomunicaciones, S.A.: an Argentinean company which provides on-line and data transmission services. In September 1997 T.I. acquired a 50% holding in this company for Ptas. 757 million.

These three companies were included at cost in the consolidated financial statements.

H) In 1997 the Telefónica Group sold its holdings in various companies with the following results:

	Millions of Pesetas		
	Percentage of Capital Stock Sold	Gross Book Value	Gain (Loss)
Dependent and associated companies:			
Sintelar, S.A.	25.00%	114	(43)
Sintelperú, S.A.	25.00%	122	(25)
Telefónica Cable Andalucía, S.A.	27.00%	23	3
Telefónica Cable Castilla y León, S.A.	24.00%	21	2
Telefónica Cable Madrid, S.A.	34.00%	26	9
Telefónica Cable Navarra, S.A.	31.00%	26	5
Telefónica de Argentina, S.A.	1.08%	4,789	6,494
Telefónica Romanía, S.A.	60.00%	1,850	197
Unisource, N.V.	25.00%	34,907	20,556
Other	—	730	105
Total		42,608	27,303
Investees:			
I-CO Global Communications (Holdings) Limited	1.69%	2,987	122
Total		2,987	122

The detail of the holdings disposed of by the Telefónica Group in 1996 and of the gains on the disposals is as follows:

	Millions of Pesetas		
	Percentage of Capital Stock Sold	Gross Book Value	Gain (Loss)
Dependent and associated companies:			
Sistemas e Instalaciones de Telecomunicaciones, S.A.	100.00%	7,935	(2,347)
Sociedad General de Cablevisión, S.A.	50.00%	1,069	(222)
Tepesa, S.A.	55.64%	139	(30)
Telecartera, S.A.	0.12%	1	—
VTR	20.00%	67 M,USD	6,597
Telefónica Argentina, S.A.	0.67%	2,526	3,666
Telecom Vallés, S.A.	24.90%	26	—
S.A.P.E.C.	33.00%	13	(10)
Amper, S.A.	0.35%	10	72
Total			7,726
Investees:			
Participaciones de CTC	—	—	183
European Silicom Structures, S.A.	0.38%	460	(6)
Cable del Guadalquivir, S.A.	20.00%	5	—
Grupo Gallego de Empresas para el Cable, S.A.	10.00%	5	(1)
Financial Network Association, S.A.	8.33%	2	1
Total			177

l) The Group companies listed on the stock exchange and their market value at year-end and the average market price in the last quarter are as follows:

Company		Currency	Stock Exchange	Market Price 1997	
				Year-End	Average Last Quarter
Telefónica	Shares	Peseta	Madrid	4,350.00	4,261.00
Telefónica	ADS's	U.S. dollar	New York	91.06	86.58
Telefónica	Shares	Yen	Tokyo	3,750.00	3,456.00
Telefónica	Shares	Deutsche mark	Frankfurt	53.00	50.64
Telefónica	ADS's	U.S. dollar	SEAQ	88.66	86.42
Telefónica	Shares	French franc	Paris	180.00	170.20
Amper	Shares	Peseta	Madrid	4,115.00	4,364.00
CTC (Chile)	Shares A	Chilean peso	Santiago	3,170.00	2,940.00
CTC (Chile)	Shares B	Chilean peso	Santiago	2,200.00	2,200.00
CTC (Chile)	ADS's	U.S. dollar	New York	29.90	28.20
TASA (Argentina)	Shares	Arg. peso	Buenos Aires	3.75	3.30
TASA (Argentina)	ADS's	U.S. dollar	New York	37.25	33.08
Telefónica del Perú (Perú)	Shares B	Nuevo sol	Lima	6.09	5.91
Telefónica del Perú (Perú)	Shares C	Nuevo sol	Lima	6.05	5.31
Telefónica del Perú (Perú)	ADS's	U.S. dollar	New York	23.31	22.06
C.A.N.T.V. (Venezuela)	Shares	Bolivar	Caracas	2,925.00	2,968.00
C.A.N.T.V. (Venezuela)	ADS's	U.S. dollar	New York	41.63	41.66
Portugal Telecom	Shares	Escudo	Lisbon	8,540.00	7,801.47
Portugal Telecom	Shares	Escudo	SEAQ	8,420.00	7,765.47
Portugal Telecom	ADS's	U.S. dollar	New York	47.00	43.53

The market prices are expressed in the currency in which the shares are traded:

- Telefónica: 1 ADS = 3 shares
- T.A.S.A.: 1 ADS = 10 shares
- Portugal Telecom: 1 ADS = 1 share
- Telefónica del Perú: 1 ADS = 10 shares
- CANTV: 1 ADS = 7 shares
- CTC: 1 ADS = 4 shares

9. DEFERRED CHARGES

The breakdown of the balance of this caption and the amortization schedule are as follows:

	Millions of Pesetas							
	Maturity						Balance at	Balance at
	1998	1999	2000	2001	2002	Subsequent Years	12/31/97	12/31/96
Pension supplements (shortfall) (Note 4-l)	9,349	9,349	9,349	9,349	9,349	51,416	98,161	95,642
Debt arrangement expenses	6,506	5,552	4,798	3,337	2,052	1,409	23,654	15,710
Interest on long-term promissory notes	3,741	2,740	1,550	183	—	—	8,214	11,815
Exchange losses (Note 4-k)	—	—	—	—	—	—	—	6,401
Interest on lease transactions	215	42	20	—	—	—	277	616
Other deferred charges	2,067	1,121	350	33	33	1,193	4,797	110
Total	21,878	18,804	16,067	12,902	11,434	54,018	135,103	130,294

The variations in the balances of the "Pension Supplements (Shortfall)" caption were as follows:

	Millions of Pesetas
Balance at 12/31/95	94,154
Amortization	(9,109)
Change of assumed interest rate (Note 4-l)	10,597
Balance at 12/31/96	95,642
Amortization	(9,370)
Updating of new GRM/80-2 tables (Note 4-l)	10,048
Change of assumed interest rate (Note 4-l)	1,841
Balance at 12/31/97	98,161

10. CUSTOMER RECEIVABLES

The detail of the balances of this caption as of December 31, 1997 and 1996, is as follows:

	Millions of Pesetas	
	Balance at 12/31/97	Balance at 12/31/96
Services billed:		
Customers billed	141,546	133,294
Doubtful customer receivables	61,063	39,394
Other	9,518	2,978
	212,127	175,666
Unbilled services	267,789	230,056
	479,916	405,722
Allowance for bad debts	(61,355)	(43,196)
Total	418,561	362,526

The "Unbilled Services" account includes the connection, subscription and metered service charges not yet billed by Telefónica and the other Group operators. This amount arises because these companies' subscriber billing schedules do not coincide with year-end (see Note 4-r).

The balance of the public-sector customer account receivable amounted to Ptas. 37,821 million (at Telefónica de España, S.A. it amounted to Ptas. 34,093 million in 1997 and Ptas. 52,671 million in 1996).

In 1997 provisions amounting to Ptas. 16,448 million (Ptas. 17,804 million in 1996) were released and Ptas. 34,607 million were added (Ptas. 26,303 million in 1996).

11. STOCKHOLDERS' EQUITY

The detail of the balances and variations in equity accounts in 1997 and 1996 is as follows:

	Millions of Pesetas						
	Balance at 12/31/95	Distribution of 1995 Income	Other Variations	Balance at 12/31/96	Distribution of 1996 Income	Other Variations	Balance at 12/31/97
Capital stock	469,735	—	—	469,735	—	—	469,735
Paid-in surplus	43,067	—	—	43,067	—	—	43,067
Revaluation reserve	649,316	—	219,076	868,392	—	—	868,392
Legal reserve	75,453	10,618	—	86,071	7,876	—	93,947
Voluntary reserve	130,149	26,816	96	157,061	18,718	(369)	175,410
Reserve for treasury stock	—	—	—	—	—	369	369
Consolidation reserve	51,597	24,415	(77)	75,935	50,051	591	126,577
Retained earnings	147	(35)	—	112	25	—	137
Consolidation translation differences	21,978	-	14,008	35,986	-	25,270	61,256
Income for the year	133,214	(133,214)	160,282	160,282	(160,282)	190,063	190,063
Interim dividend	(28,184)	28,184	(32,881)	(32,881)	32,881	(37,579)	(37,579)
Total	1,546,472	(43,216)	360,504	1,863,760	(50,731)	178,345	1,991,374

a) Capital stock

As of December 31, 1997, Telefónica's capital stock consisted of 939,470,820 fully subscribed and paid bearer shares of Ptas. 500 par value each, all recorded by the book-entry system of trading and listed on the four Spanish stock exchanges and on the Frankfurt, London, Paris, Tokyo and New York stock exchanges. According to the information to which Telefónica has had access, as of December 31, 1997, significant holdings in its capital stock were owned by Banco Bilbao Vizcaya, S.A. (6.92%), Grupo Corporación Bancaria de España, S.A. (ARGENTARIA, 5.21%) and Caja de Ahorros y Pensiones de Barcelona (5.01%). The State Property Agency owned 0.65% of its capital stock, through Sociedad Estatal de Participaciones Patrimoniales (SEPPA) (0.55%) and Sociedad Estatal de Patrimonio II, S. A. (0.1%).

Pursuant to Royal Decree 8/1997, the prior administrative authorization regime applies to Telefónica de España, S.A. and Telefónica Servicios Móviles, S.A. Accordingly, certain corporate resolutions and other agreements which may give entitlement to the direct or indirect acquisition, including through fiduciary or interposed third parties, of shares of Telefónica de España, S.A. or Telefónica Servicios Móviles, S.A. representing at least 10% of capital stock are subject to such authorization. The administrative authorization regime will be in force for ten years from February 18, 1997.

On April 21, 1995, the Stockholders' Meeting authorized the Board of Directors to increase capital, at one or several times, up to a maximum of Ptas. 704,603 million within a maximum period of five years and without requiring further notice or resolution.

On March 21, 1997, the Stockholders' Meeting authorized the derivative acquisition of treasury stock, for a consideration, by the Board of Directors up to the limits and within the terms and conditions established by the Stockholders' Meeting itself, within a maximum period of 18 months from that date, up to a maximum of 46,973,541 shares, for a minimum value of Ptas. 500 and a maximum value of Ptas. 4,000 each.

In 1997 the Company carried out the following treasury stock transactions:

Transaction date	Number of shares	Price per share	Amount
Acquisitions			
August 1997	175,000	3,977	696
October 1997	335,000	3,469	1,162
November 1997	100,000	3,920	392
Total	610,000	3,689	2,250
Disposals			
December 1997	510,000	4,314	2,200
Total	510,000	4,314	2,200
Shares in portfolio	100,000	3,689	369

b) Legal reserve

Under the revised Corporations Law, 10% of income for each year must be transferred to the legal reserve until the balance of this reserve reaches at least 20% of capital stock. Telefónica covered this percentage with the distribution of 1996 income. The legal reserve can be used to increase capital provided that the remaining reserve balance does not fall below 10% of the increased capital stock amount. Otherwise, until the legal reserve exceeds 20% of capital stock, it can only be used to offset losses, provided that sufficient other reserves are not available for this purpose.

c) Revaluation reserves

The balance of the "Revaluation Reserves" caption arose as a result of revaluations made from 1946 to 1987, and of the revaluation pursuant to Royal Decree-Law 7/1996.

As of December 31, 1997 and 1996, the balances of the revaluation reserve amounted to Ptas. 868,392 million in both years, as follows:

	Millions of Pesetas	
	1997	1996
Revaluations from 1946 to 1987:		
Revaluations made	745,203	745,203
Revaluation reserve Royal Decree-Law 7/1996	225,852	225,852
Amounts used:		
Capital increases from 1977 to 1986	(74,487)	(74,487)
Transfer to provisions in 1982	(18,829)	(18,829)
Single tax on revaluation, Royal Decree-Law 7/1996	(6,776)	(6,776)
Other variations from 1981 to 1986	(2,571)	(2,571)
Total	868,392	868,392

The balance of the reserve relating to the revaluations made from 1946 to 1987 was unrestricted as to its use.

From the date on which the tax authorities have reviewed and approved the balance of the "Revaluation Reserve Royal Decree-Law 7/1996" account (or the three-year period for review has expired), the aforementioned balance can be used, free of tax, to offset recorded losses which might arise in the future, and to increase capital stock. From January 1, 2007 (ten years from the date of the balance sheet reflecting the revaluations), the balance of this account can be taken to unrestricted reserves, provided that the monetary surplus has been realized. The surplus is deemed to be realized in respect of the portion relating to the depreciation recorded for accounting purposes or when the restated assets have been transferred or retired from the accounting records.

d) Consolidation reserve

The detail of the consolidation reserve and of the variations therein in 1997 and 1996 is as follows::

1997	Millions of Pesetas			Balance at 12/31/97
	Balance at 12/31/96	Increase	Decrease	
Companies consolidated by the global and proportional integration methods	58,342	41,160	(2,155)	97,347
Companies carried by the equity method	17,593	12,180	(543)	29,230
Total	75,935	53,340	(2,698)	126,577

1996	Millions of Pesetas			Balance at 12/31/96
	Balance at 12/31/95	Increase	Decrease	
Companies consolidated by the global and proportional integration methods	27,314	33,864	(2,836)	58,342
Companies carried by the equity method	24,283	917	(7,607)	17,593
Total	51,597	34,781	(10,443)	75,935

e) Translation differences in consolidation

The translation differences relate mainly to the effect of exchange rate fluctuations on the net assets of the companies located abroad (see Note 4-b) and the effect of the adjustment for inflation on the assets contributed by the companies at which this accounting practice is applied. Positive differences of Ptas. 62,839 million and Ptas. 17,946 million in 1997 and 1996, respectively, arose at T.I. in this connection. In 1997 this account also includes exchange differences resulting from specific foreign-currency financing transactions carried out by T.I. relating to investments in investee companies and which hedge the exchange risk on these investments. Differences amounting to Ptas. 27,798 million arose in this connection as a result of the revaluation of Ptas. 425,903 million of loans assigned to these investments.

f) Equity of the controlling company

The detail of the capital and reserves of the controlling company as of December 31, 1997 and 1996, is as follows:

	Millions of Pesetas	
	1997	1996
Capital stock	469,735	469,735
Paid-in surplus	43,067	43,067
Revaluation reserve	872,856	872,856
Legal reserve	93,947	86,071
Voluntary reserve	203,229	174,698
Reserve for treasury stock	369	—
Retained earnings	137	112
Income for the year	133,774	120,414
Interim dividend	(37,579)	(32,881)
Total	1,779,535	1,734,072

The differences (amounting to Ptas. 4,464 million) between the revaluation reserves in the individual financial statements of Telefónica and those in the consolidated financial statements arose in consolidation, as a result of the reclassifications to the voluntary reserves account of the reserves of the companies sold and to the consolidation reserve account of the reserves of existing companies.

Contribution of the Group companies to the consolidated accounts

The contribution of the Group companies to consolidated equity as of December 31, 1997, was as follows:

Company	Millions of Pesetas			
	December 31, 1997			
	Contributions			
	(*) To Consolidated Income	To Reserves	To Translation Differences	Total Contribution to Equity
Capital stock of the parent company				469,735
Cabitel	2,891	5,051	—	7,942
Fonditel	588	687	—	1,275
G. Casiopea	1,202	1,495	2	2,699
G. Comet	(2)	(882)	—	(884)
G. Servicio Teledistribución Hilo	118	248	—	366
G. Telefónica Internacional	27,363	88,516	61,255	177,134
G. Telefónica Servicios Móviles	27,814	17,855	—	45,669
G. Telefónica Sistemas	515	2,956	(1)	3,470
G. Telefónica Publicidad e Información	7,136	6,943	—	14,079
G. Telefónica Medios Comunicación	(926)	—	—	(926)
G. Telefónica Servicio Multimedia	(5,823)	(1,122)	—	(6,945)
G. Telefónica Soluciones Sectoriales	(86)	—	—	(86)
Playa de Madrid	18	96	—	114
Taetel	226	1,466	—	1,692
Telefónica Europe B.V.	14	—	—	14
Telfisa	94	(42)	—	52
Telyco	581	(685)	—	(104)
Temasa	1,883	4,676	—	6,559
Tidsa	686	2,974	—	3,660
Urbana Ibérica	1	94	—	95
Telefónica de España and associated companies	121,212	1,213,735	—	1,334,947
Total Telefónica Group	185,505	1,344,061	61,256	1,590,822
Variation in income and reserves due to fixed asset transactions	4,558	(36,162)	—	(31,604)
Interim dividend	—	—	—	(37,579)
Contributions to equity of the Telefónica Group	190,063	1,307,899	61,256	1,991,374

The contribution of the Group companies to consolidated equity as of December 31, 1996, was as follows:

Millions of Pesetas				
December 31, 1996				
Contributions				
Company	(*) To Consolidated Income	To Reserves	To Translation Differences	Total Contribution to Equity
Capital stock of the parent company	—	—	—	469,735
Cabitel	2,794	2,257	—	5,051
Fonditel	390	297	—	687
G. Casiopea	373	1,288	31	1,692
G. Comet	(34)	(848)	—	(882)
G. Servicio Teledistribución	(61)	309	—	248
G. Sintel (through 04/30/96)	710	(30)	—	680
G. Telcartera y Sociedad de Cablevisión	(804)	(82)	—	(886)
G. Telefónica Servicios Móviles	15,135	1,664	—	16,799
G. Telefónica Sistemas	674	2,261	—	2,935
G. Telefónica Internacional	22,445	66,067	34,800	123,312
Telefónica Publicidad e Información	3,611	3,041	—	6,652
Playa de Madrid	12	84	—	96
Taetel	325	1,129	—	1,454
Telefónica Multimedia (Group)	(210)	(131)	—	(341)
Telfisa	65	(107)	—	(42)
Telyco	848	(1,533)	—	(685)
Temasa	1,885	2,791	—	4,676
Tidsa	953	2,021	—	2,974
Urbana Ibérica	4	89	—	93
Telefónica de España and associated companies	111,364	966,953	1,155	1,079,472
Total Telefónica Group	160,479	1,047,520	35,986	1,243,985
Revaluation Royal-Decree Law 7/1996	—	219,076	—	219,076
Variation in income and reserves due to fixed asset transactions	(197)	(35,958)	—	(36,155)
Interim dividend	—	—	—	(32,881)
Contributions to equity of the Telefónica Group	160,282	1,230,638	35,986	1,863,760

The contribution to the income of the Telefónica Internacional Group of the operator companies consolidated by the global integration method was as follows:

Millions of Pesetas		
	1997	1996
Compañía de Telecomunicaciones de Chile, S.A.	20,548	17,092
Telefónica Larga Distancia, Inc. (Puerto Rico)	867	(462)
Publiguías, S.A.	1,176	827
Telefónica del Perú, S.A.	17,564	13,820
Telefónica Romania, S.A.	390	460
Total	40,545	31,737

(*) There may be immaterial variations in the contribution to the consolidated income used in consolidation at the definitive year-end close of the Group companies.

12. MINORITY INTERESTS

Minority interests

This caption relates to the holdings of minority stockholders in the equity and income/loss for the year of the Group companies consolidated by the global integration method.

As of December 31, 1997, the balance of this caption comprised the holdings of minority stockholders in the following companies:

Company	% of Minority Interests	Millions of Pesetas			
		Net Worth	Translation Differences	Income (Loss)	Balance at 12/31/97
C.T.C. Chile	56.38	90,532	51,006	27,425	168,963
Doubleclick	10.00	15	—	(1)	14
Fondtel	19.00	658	—	138	796
Hispaservices	12.00	18	—	(14)	4
Mensatel	10.00	106	—	(70)	36
Publiguías, S.A.	45.07	360	559	856	1,775
Radioed Cataluña	9.00	16	—	(2)	14
Telefónica Cable Andalucía	27.00	266	—	(2)	264
Telefónica Cable Canarias	49.00	90	—	(11)	79
Telefónica Cable Castilla y León	39.00	389	—	(3)	386
Telefónica Cable Madrid	34.00	26	—	(4)	22
Telefónica Cable Navarra	31.00	26	—	(3)	23
Telefónica del Perú Holding	10.00	27,691	1,726	1,169	30,586
Telefónica del Perú, S.A.	65.00	109,791	42,188	36,244	188,223
Telefónica Larga Distancia, Inc.	21.00	3,551	(837)	62	2,776
TMP Worldwide España	49.00	16	—	7	23
Other Chilean companies	—	108	(972)	1,134	270
Other Peruvian companies	—	105	(329)	—	(224)
Other companies	—	9	1	57	67
Total		233,773	93,342	66,982	394,097

The income (loss) attributed to minority stockholders is modified by Ptas. 6,930 million, Ptas. 260 million and Ptas. (130) million relating to the income (loss) arising at Telefónica Internacional, S.A., Telefónica Romanía, S.A. and Rem Infográfica, S.A., respectively, from the start of the year until the holding of the minority stockholder; or the company itself, disappears.

As of December 31, 1996, the balance of this caption comprised the holdings of minority stockholders in the following companies:

Company	% of Minority Interests	Millions of Pesetas			
		Net Worth	Translation Differences	Income (Loss)	Balance at 12/31/97
C.T.C. Chile	56.38	91,955	12,107	21,052	125,114
Other Chilean companies	—	4,472	14	831	5,317
Telefónica del Perú, S.A.	65.00	105,712	7,949	28,518	142,179
Negocios Cibernéticos	50.00	5	—	—	5
Mensatel	10.00	102	—	4	106
Publiguías	45.07	565	80	609	1,254
Telefónica Internacional	23.78	48,914	10,858	7,003	66,775
Telefónica Larga Distancia, Inc.	21.00	2,424	187	(268)	2,343
Telecartera	25.00	135	—	(166)	(31)
T. Romania	40.00	572	58	307	937
Telefónica del Perú Holding	10.00	27,824	998	868	29,690
Other Peruvian companies	—	90	—	—	90
REM Infográfica	40.00	20	—	(63)	(43)
TMP Worldwide España	49.00	14	—	2	16
Radiored Cataluña	9.00	11	—	(4)	7
Fonditel	19.00	539	—	92	631
S.G. Cablevisión Madrid	12.25	12	—	(3)	9
S.G. Cablevisió Barcelona	12.25	12	—	(11)	1
S.G. Cablevisión Cantabria	12.25	12	—	(3)	9
S.G. Cablevisión Canarias	49.00	105	—	(15)	90
S.G. Cablevisión Alicante	12.25	12	—	(1)	11
S.G. Cablevisión Asturias	12.25	12	—	1	13
S.G. Cablevisión Bizkaia	12.25	12	—	(3)	9
S.G. Cablevisión Burgos	23.50	24	—	(1)	23
S.G. Cablevisión Cádiz	12.25	13	—	(1)	12
S.G. Cablevisión Granada	12.25	13	—	—	13
S.G. Cablevisión León	12.25	13	—	—	13
S.G. Cablevisión Lleida	12.25	13	—	(2)	11
S.G. Cablevisión Málaga	12.25	13	—	—	13
S.G. Cablevisión Murcia	12.25	12	—	(1)	11
S.G. Cablevisión Navarra	12.25	12	—	(2)	10
S.G. Cablevisión Rioja	12.25	12	—	—	12
S.G. Cablevisión Sevilla	12.25	12	—	(2)	10
S.G. Cablevisión Valencia	12.25	12	—	(1)	11
S.G. Cablevisión Valladolid	12.25	12	—	—	12
S.G. Cablevisió Balears	12.25	12	—	(2)	10
Gestired	—	21	—	(21)	—
Servicios y Contenidos por la Red	—	39	—	(39)	—
Total		283,764	32,251	58,678	374,693

Variations in minority interests

The variations in minority interests in 1997 were as follows:

Variations in minority interest	Balance at 31/12/96	Capital Contribution Inclusion of Companies	Income (Loss) for the Year	Variation in Translation Differences	Other Variations	Exclusion of Companies	Dividends Distributed	Balance at 31/12/97
Company								
Telefónica Larga Distancia, Inc.	2,343	—	62	371	--	—	—	2,776
Publiguías, S.A.	1,254	—	856	276	—	—	(611)	1,775
Telefónica Romania	937	—	260	146	—	(1,276)	(67)	0
Telefónica del Perú Holding	29,690	—	1,169	698	—	—	(971)	30,586
Telefónica del Perú, S.A.	142,179	—	36,244	23,659	—	—	(13,859)	188,223
Compañía de Telecomunicaciones de Chile, S.A.	125,114	—	27,425	28,770	—	—	(12,346)	168,963
Other Peruvian Companies	90	--	—	16	(330)	—	—	(224)
Other Chilean Companies	5,317	—	1,134	694	(6,875)	—	—	270
Other Companies	—	9	57	1	—	--	—	67
Negocios Cibernéticos	5	—	—	—	—	(5)	—	0
Mensatel	106	—	(70)	—	—	—	—	36
T.I. Telefónica Internacional	66,775	—	6,930	6,430	(80,135)	—	—	0
Telecartera	(31)	—	—	—	31	—	—	0
Rem Infográfica	(43)	—	(130)	—	173	—	—	0
TMP Worldwide España	16	—	7	—	—	—	—	23
Radioed Cataluña	7	9	(2)	—	—	—	—	14
Fonditel	631	27	138	—	—	—	—	796
Hispaservices	0	—	(14)	—	18	—	—	4
Doubleclick	0	15	(1)	—	—	—	—	14
S.G. Cablevisión Madrid	9	17	(4)	—	—	—	—	22
S.G. Cablevisió Barcelona	1	—	—	—	(1)	—	—	0
S.G. Cablevisión Cantabria	9	—	—	—	(9)	--	—	0
S.G. Cablevisión Canarias	90	—	(11)	—	—	—	—	79
S.G. Cablevisión Alicante	11	—	—	—	(11)	—	—	0
S.G. Cablevisión Asturias	13	—	—	—	(13)	—	—	0
S.G. Cablevisión Bizkaia	9	—	—	—	(9)	—	—	0
S.G. Cablevisión Burgos	23	—	—	—	(23)	—	—	0
S.G. Cablevisión Cádiz	12	—	—	—	(12)	—	—	0
S.G. Cablevisión Granada	13	—	—	—	(13)	—	—	0
S.G. Cablevisión León	13	—	—	—	(13)	—	—	0
S.G. Cablevisión Lleida	11	—	—	—	(11)	—	—	0
S.G. Cablevisión Andalucía	13	253	(2)	—	—	—	—	264
S.G. Cablevisión Murcia	11	—	—	—	(11)	—	—	0
S.G. Cablevisión Navarra	10	16	(3)	—	—	—	—	23
S.G. Cablevisión Rioja	12	—	—	—	(12)	--	—	0
S.G. Cablevisión Sevilla	10	--	—	—	(10)	—	—	0
S.G. Cablevisión Valencia	11	—	—	—	(11)	--	—	0
S.G. Cablevisión Valladolid	12	377	(3)	—	—	—	—	386
S.G. Cablevisió Balears	10	—	—	—	(10)	--	—	0
Total	374,693	723	74,042	61,061	(87,287)	(1,281)	(27,854)	394,097

Variations in minority interests

The variations in minority interests in 1996 were as follows:

Company	Balance at 31/12/95	Inclusion of Companies	Exclusion of Companies	Income (Loss) for the Year	Translation Differences	Other Variations	Dividends Distributed	Balance at 31/12/96
C.T.C Chile	107,229	—	—	21,052	7,237	3,285	(13,689)	125,114
Other Chilean Companies	—	4,325	—	831	14	147	—	5,317
Telefónica del Perú	116,510	—	—	28,518	11,776	(3,827)	(10,798)	142,179
Negocios Cibernéticos	—	5	—	—	—	—	—	5
Mensatel	102	—	—	4	—	—	—	106
Publiguías	895	—	—	609	176	(20)	(406)	1,254
T.I. Telefónica Internacional	55,914	—	—	7,003	4,060	(202)	—	66,775
T.L.D. Puerto Rico	2,421	—	—	(268)	10	180	—	2,343
Telecartera	244	1	—	(166)	—	(110)	—	(31)
Telefónica Romania	571	—	—	307	(38)	97	—	937
Telefónica Perú Holding	28,427	—	—	868	1,054	(56)	(603)	29,690
Other Peruvian Companies	—	90	—	—	—	—	—	90
Rem Infográfica	—	20	—	(63)	—	—	—	(43)
TMP Worldwide España	—	14	—	2	—	—	—	16
Radioed Catalunya	9	—	—	(4)	—	2	—	7
Fonditel	500	39	—	92	—	—	—	631
S.G. Cablevisión Madrid	10	—	37	(3)	—	39	—	9
S.G. Cablevisió Barcelona	10	—	37	(11)	—	39	—	1
S.G. Cablevisión Cantabria	14	—	22	(3)	—	20	—	9
S.G. Cablevisión Canarias	60	19	—	(15)	—	26	—	90
S.G. Cablevisión Alicante	—	12	—	(1)	—	—	—	11
S.G. Cablevisión Asturias	—	12	—	1	—	—	—	13
S.G. Cablevisión Bizkaia	—	12	—	(3)	—	—	—	9
S.G. Cablevisión Burgos	—	24	—	(1)	—	—	—	23
S.G. Cablevisión Cádiz	—	13	—	(1)	—	—	—	12
S.G. Cablevisión Granada	—	13	—	—	—	—	—	13
S.G. Cablevisión León	—	13	—	—	—	—	—	13
S.G. Cablevisión Lleida	—	13	—	(2)	—	—	—	11
S.G. Cablevisión Málaga	—	13	—	—	—	—	—	13
S.G. Cablevisión Murcia	—	12	—	(1)	—	—	—	11
S.G. Cablevisión Navarra	—	12	—	(2)	—	—	—	10
S.G. Cablevisión Rioja	—	12	—	—	—	—	—	12
S.G. Cablevisión Sevilla	—	12	—	(2)	—	—	—	10
S.G. Cablevisión Valencia	—	12	—	(1)	—	—	—	11
S.G. Cablevisión Valladolid	—	12	—	—	—	—	—	12
S.G. Cablevisió Balears	—	12	—	(2)	—	—	—	10
Sintelperú	135	—	135	—	—	—	—	—
Sintelar	372	—	372	—	—	—	—	—
Cotronic	68	—	68	—	—	—	—	—
Incosa	94	—	94	—	—	—	—	—
Tepesa	111	—	111	—	—	—	—	—
Radioed Zaragoza	11	—	11	—	—	—	—	—
Gestired	34	—	13	(21)	—	—	—	—
Servicios y Contenidos por la Red	12	—	(27)	(39)	—	—	—	—
Total	313,753	4,722	873	58,678	24,289	(380)	(25,496)	374,693

13. DEFERRED REVENUES

The detail of the balances of and variations in this caption in the accompanying consolidated balance sheets is as follows:

	Millions of Pesetas				
	Capital Subsidies	Exchange Gains	Nonrefundable Third-Party Deferred Taxes (Note 18)	Contributions and Other	Total
Balance at 12/31/95	70,666	13,780	—	6,812	91,258
Additions	13,485	(8,724)	14,732	4,352	23,845
Transfers	—	—	2,295	(2,295)	0
Allocation to income	(10,317)	(2,067)	—	(501)	(12,885)
Balance at 12/31/96	73,834	2,989	17,027	8,368	102,218
Additions	9,071	271	15,433	15,310	40,085
Allocation to income	(11,285)	(2,989)	(1,938)	(13,620)	(29,832)
Balance at 31-12-97	71,620	271	30,522	10,058	112,471

The "Nonrefundable Third-Party Contributions" caption includes amounts received by Telefónica for use of the underwater cable systems in which Telefónica has an interest as owner or co-owner.

Capital subsidies

The detail of the capital subsidies not yet allocated to income is as follows:

Grantor	Millions of Pesetas	
	12/31/97	12/31/96
Official agencies, autonomous community governments, regional and local governments and other	29,264	31,452
EU		
STAR Programme	11,495	14,223
ERDF Programme	6,032	6,570
IRTA Programme	1,677	2,000
ERDF 94/95 Programme	19,571	16,368
Other	3,581	3,221
	71,620	73,834

14. PROVISIONS FOR CONTINGENCIES AND EXPENSES

The detail of the balances of and variations in provisions for contingencies and expenses is as follows:

Millions of Pesetas									
	Balance at 12/31/95	Provisions	Amount Used	Other	Balance at 12/31/96	Provisions	Amount Used	Other	Balance at 12/31/97
Provision for cost of integrating retired employees in the social security system (Note 4-l)	44,794	—	(6,106)	—	38,688	—	(38,688)	—	—
Provision for Rebalancing Plan (Note 4-l)	6,069	4,677	(1,625)	—	9,121	4,876	(1,525)	—	12,472
Provision for supplementary pension payments (Notes 4-l and 9)	117,913	7,853	(14,328)	10,597	122,035	7,296	(40,287)	11,889	100,933
Group insurance (Note 4-l)	16,549	1,620	(4,950)	—	13,219	1,368	(1,211)	—	13,376
Provision "preretirement" and early retirement (Note 4-m)	52,619	58,519	(24,354)	—	86,784	90,166	(52,337)	—	124,613
Technical provisions (Note 4-n)	35,223	13,263	(18)	(30)	48,438	58,967	—	—	107,405
Claims	1,100	—	(160)	(563)	377	—	(119)	(258)	—
Other provisions	13,729	11,807	(6,790)	(793)	17,953	17,110	(7,962)	2,996	30,097
Total	287,996	97,739	(58,331)	9,211	336,615	179,783	(142,129)	14,627	388,896

Most of the provisions are explained in Note 4- The "Technical Provisions" account includes the provisions recorded by the Group companies engaging in the insurance business. The balancing items for these provisions are recorded under the "Short-Term Financial Investments" and "Long-Term Financial Investments" captions.

15. DEBENTURES, BONDS AND OTHER NEGOTIABLE INSTRUMENTS

The detail of the balances as of December 31, 1997 and 1996, of debentures, bonds and other negotiable instruments is as follows:

CONSOLIDATED						
	Peseta Debentures and Bonds		Foreign Currency Debentures and Bonds			Total
	Non- convertible	Convertible and/or Exchangeable	Non- convertible	Convertible and/or Exchangeable	Corporate Promissory Notes	
Balance at 12/31/95	628,384	—	50,938	13,553	45,226	738,101
New issues	—	—	50,809	1,087	168,774	220,670
Redemptions, conversions and exchanges	(61,206)	—	(18,670)	(1,094)	(150,955)	(231,925)
Revaluations and other variations	(46,700)	—	4,519	1,124	7,623	59,966
Transfers	—	—	(278)	278	—	—
Balance at 12/31/96	613,878	—	87,318	14,948	70,668	786,812
New issues	—	—	107,565	99,402	159,871	366,838
Redemptions, conversions and exchanges	(52,365)	—	(19,401)	(12,195)	(152,963)	(236,924)
Revaluations and other variations	51,083	—	15,595	994	—	67,672
Balance at 12/31/97	612,596	—	191,077	103,149	77,576	984,398
Maturity:						
Long-term	431,474	—	179,998	103,149	302	714,923
Short-term	181,122	—	11,079	—	77,274	269,475
Unmatured accrued interest	11,350	—	3,193	—	—	14,543

Debentures and bonds

The detail of the debentures and bonds outstanding as of December 31, 1997, and of the main features thereof is as follows:

		Interest	Maturity					Subsequent	
Issue	Currency	Rate	1998	1999	2000	2001	2002	Years	Total
Debentures:									
Yankee Bonds 1996	US\$	7.63	—	—	—	—	—	30,340	30,340
Series D 1989	U.Fomento	5.80	3,652	1,825	—	—	—	—	5,477
July 1989	Pesetas	12.00	—	—	—	—	—	10,340	10,340
December 1989 (*)	Pesetas	4.48	800	800	—	—	—	—	1,600
January 1990	Pesetas	12.00	—	—	—	—	257	27,654	27,911
February 1990									
Series A	Pesetas	12.60	—	—	9,350	—	—	—	9,350
February 1990									
Series B	Pesetas	12.60	—	—	—	—	—	1,367	1,367
February 1990									
Series C	Pesetas	12.60	—	—	—	—	—	626	626
February 1990									
Series D	Pesetas	12.89	—	—	16,517	—	—	—	16,517
February 1990									
Series E	Pesetas	12.85	—	—	—	—	—	5,381	5,381
February 1990									
Series F	Pesetas	12.58	—	—	—	—	—	592	592
December 1990	Pesetas	13.58	—	—	—	—	—	48,825	48,825
Series E 1991	U.Fomento	6.00	1,522	1,522	1,522	1,522	1,522	762	8,372
Series F 1991	U.Fomento	6.00	348	348	348	348	348	4,695	6,435
February 1991									
Series A	Pesetas	14.25	29,485	—	—	—	—	—	29,485
February 1991									
Series B	Pesetas	14.47	74,630	—	—	—	—	—	74,630
March 1991	Pesetas	14.48	10,086	2,521	—	—	—	—	12,607
Private issue									
April 1991	Pesetas	14.25	20,000	—	—	—	—	—	20,000
April 1991 Series A	Pesetas	13.50	—	—	—	10,000	—	—	10,000
April 1991 Series B	Pesetas	13.67	—	—	—	47,237	—	—	47,237
Series G 1993	U.Fomento	4.50	—	—	—	—	—	4,729	4,729
Series H 1994	U.Fomento	5.80	—	—	1,217	2,435	2,435	13,390	19,477
Series I 1994	U.Fomento	5.50	—	—	—	304	609	8,825	9,738
July 1997	US\$	2.12	—	—	—	—	98,420	—	98,420
October 1997	US\$	5.33	—	—	—	—	—	12,416	12,416
December 1997	US\$	6.38	—	—	—	—	—	75,829	75,829
C September 1998	Pesetas	10.12	46,121	—	—	—	—	—	46,121
D September 2001	Pesetas	10.25	—	—	—	62,415	—	—	62,415
B November 2000	Pesetas	10.06	—	—	20,439	—	—	—	20,439
C November 2002	Pesetas	10.06	—	—	—	—	19,316	—	19,316
B October 2000	Pesetas	8.00	—	—	12,372	—	—	—	12,372
C October 2004	Pesetas	8.25	—	—	—	—	—	11,520	11,520
Total Debentures			186,644	7,016	61,765	124,261	122,907	257,291	759,884

Issue	Currency	Interest	Maturity					Subsequent	Total
		Rate	1998	1999	2000	2001	2002	Years	
Total Debentures			186,644	7,016	61,765	124,261	122,907	257,291	759,884
Bonds:									
April 1991	Pesetas	14.52	—	115,538	—	—	—	—	115,538
July 1991	Pesetas	14.51	—	8,407	—	—	—	—	8,407
Series G 1996	N. Soles	VAC+5.1%	—	4,313	—	—	—	—	4,313
Series I 1996	N. Soles	VAC+5.6%	—	—	—	5,621	—	—	5,621
Single series 1997	N. Soles	14.50	5,557	—	—	—	—	—	5,557
Single series 1997	N. Soles	12.38	—	—	7,502	—	—	—	7,502
Total issues			192,201	135,274	69,267	129,882	122,907	257,291	906,822

(*) Average interest rate for 1997 on floating-rate issues.

The zero-coupon debentures and bonds are recorded in the consolidated balance sheet at their issue value plus the accrued interest through December 31, 1997.

The detail of the maturities and redemption values as of December 31, 1997, is as follows:

Issue	Maturity Date	%	Millions of Pesetas	
		Redemption Rate	Current Value	Redemption Value
Debentures:				
February 1990 Series D	02-26-2000	336.154	16,517	21,447
February 1990 Series E	02-26-2005	613.338	5,381	12,776
February 1990 Series F	02-26-2010	1069.470	592	2,503
December 1990	12-28-2005	675.000	48,825	135,000
February 1991 Series B	02-28-1998	257.500	74,630	76,249
March 1991	03-01-1998	257.729	2,522	2,577
March 1991	06-01-1998	266.659	2,522	2,667
March 1991	09-01-1998	275.899	2,521	2,759
March 1991	12-01-1998	285.353	2,521	2,854
March 1991	03-01-1999	295.022	2,521	2,950
April 1991 Series B	04-17-2001	360.000	47,237	72,000
C September 1998	09-19-1998	196.531	46,121	49,401
D September 2001	09-19-2001	265.543	62,415	89,687
Bonds:				
April 1991	04-15-1999	295.740	115,538	137,519
July 1991	07-15-1999	295.740	8,407	10,351
			438,270	620,740

As of December 31, 1997, the redemption value amounted to Ptas. 620,740 million and the current value to Ptas. 438,270 million.

In July 1997 convertible debentures were issued amounting to US\$ 600 million.

The features of the issue were as follows:

- Issue of 600,000 debentures of par value US\$ 1,000 each.
- Interest rate: 2.125%.
- Possibility of conversion during the life of the issue at the exchange rate of 31.43467 shares per debenture.
- Possibility of early redemption by Telefónica from 07/15/2000.
- Final redemption on 07/15/2002 at 108.02%.

Corporate promissory notes

There are two corporate promissory note issue programs at Telefónica, as follows:

Millions of Pesetas			
Balance Limit	Addressed to	Pesetas Par Value	Method of Acquisition
75,000	Public	500,000	Monthly competitive auctions
	Companies and institutions	100 million	Monthly competitive auctions
75,000	Companies and institutions	500 million (minimum)	Specific transactions

The average interest rate on the outstanding debentures and bonds was 12.69% for 1997 (12.30% in 1996), and that on the corporate promissory notes was 6.05% in 1997 (8.26% in 1996).

16. PAYABLE TO CREDIT ENTITIES

The detail of accounts payable to credit entities is as follows:

	Millions of Pesetas							
	Balance at 12/31/97					Balance at 12/31/96		
	Average Interest Rate 1997	1996	Short Term	Long Term	Total	Short Term	Long Term	Total
Corporate promissory notes	13.39	13.37	1,314	35,541	36,855	365	36,855	37,220
Loans and credits	6.32	8.71	54,697	291,477	346,174	59,594	249,906	309,500
Foreign currency loans	5.40	6.54	266,504	615,710	882,214	174,177	556,588	730,765
Total			322,515	942,728	1,265,243	234,136	843,349	1,077,485

As of December 31, 1997, the payables were scheduled to mature as follows::

	Millions of Pesetas						
	1998	1999	2000	2001	2002	Subsequent Years	Total
Corporate promissory notes	1,314	21,637	1,618	12,286	—	—	36,855
Loans and credits	54,697	49,479	21,046	66,837	47,086	107,029	346,174
Foreign currency loans	266,504	136,901	104,011	111,512	48,613	214,673	882,214
Total	322,515	208,017	126,675	190,635	95,699	321,702	1,265,243

Loans and credits

The peseta loans and credits include the amount used in pesetas of a multicurrency loan originally granted in ECUs by the European Investment Bank for Ptas. 12,113 million and other multicurrency loans swapped for peseta loans totaling Ptas. 69,385 million.

Foreign currency loans

The detail of the foreign-currency loans as of December 31, 1997 and 1996, and of the main features thereof is as follows:

Entity	Year	Currency	Maturity	Outstanding Principal					
				Interest Rate		Foreign Currency		Pesetas	
				1997	1996	12/31/97	12/31/96	12/31/97	12/31/96
Telefónica—									
1st ICO—EIB	1988	ECU	2003	6.29	6.15	91	106	15,296	17,347
1st ICO—EIB	1988	FRF	2003	5.94	5.90	390	455	9,878	11,379
1st ICO—EIB	1988	CHF	2003	4.56	4.30	64	75	6,688	7,258
3rd ICO—EIB (*)	1989	ECU	2004	8.06	7.85	98	240	16,358	39,075
4th ICO—EIB	1989	DEM	2004	6.73	6.70	144	164	12,191	13,872
5th ICO—EIB	1990	ECU	2005	10.21	10.20	—	127	—	20,729
5th ICO—EIB	1990	CHF	2005	8.11	7.65	—	229	—	22,231
5th ICO—EIB	1990	NLG	2005	9.36	8.80	—	98	—	7,356
5th ICO—EIB	1990	JPY	2005	7.68	7.45	—	7,668	—	8,693
7th ICO— EIB (**)	1992	ECU	2007	4.55	5.32	—	150	—	24,422
7th ICO— EIB (**)	1992	FRF	2007	4.98	—	607	—	15,366	—
8th ICO— EIB	1992	JPY	2002	0.90	0.77	—	19,500	—	22,109
9th ICO—EIB	1992	NLG	2002	3.32	3.37	74	82	5,556	6,172
S.B. GRAL.	1987	JPY	2000	2.76	3.11	—	6,364	—	7,215
Credit facility	1997	PTE	5.66	—	10	—	8	—	—
Telfisa									
EIB	1991	ECU	2006	4.28	6.37	212	237	35,592	49,251
EIB	1991	NLG	2006	3.18	4.20	123	137	9,229	10,312
EIB	1991	FRF	2006	3.61	5.90	370	414	9,376	10,348
EIB	1991	USD	2006	5.78	6.29	120	134	18,251	17,652
EIB	1995	LIRA	2000	10.9	—	120,000	120,000	10,358	10,303
EIB	1995	JPY	1999	2.10	—	17,000	17,000	19,922	19,274
EIB	1995	ECU	2000	4.65	—	65	—	10,887	—
Telefónica Internacional									
ABN Amro Bank	1994	USD	2001	L+0.17	L+0.17	975	690	147,909	90,579
Banco Santander	1996	USD	2005	L+0.12	L+0.07	300	478	45,511	62,859
Banco Central Hispano	1993	USD	1998	L+0.15	L+0.15	130	130	19,721	17,066
ABN Amro Bank	1995	USD	2000	L+0.85	L+0.85	275	275	41,718	36,101
Other CTC loans	Various	USD	Various	L+0.17	L+0.50	Various	Various	150,706	108,254
				L+0.85	L+0.85				
Telefónica del Perú loans	Various	USD	Various	L+0.48	L+0.50	Various	Various	105,839	52,865
				L+0.50	L+1.00				
Other loans (***)	Various	USD	Various	Various	Various	Various	Various	175,705	38,043
Telefónica Sistemas									
Argentaria-BEX	1997	PCH	1998	11.56	—	430	—	149	—
								882,214	730,765

(*) From 08/25/97, ECUs 112.34 million were swapped for Ptas. 18,525 million.

(**) From 12/15/97, ECUS 142.5 million were swapped for FF 606.67 million and Ptas. 8,285 million.

(***) This item relates to several loans in different currencies and, therefore, the year granted, currency, interest rate and year of maturity are not indicated

Described below are the main foreign currency loans:

ICO-EIB

In 1988 Telefónica obtained from the European Investment Bank (EIB) a financing commitment for capital expenditure projects aimed at improving infrastructures and new technologies. This financing is obtained through Instituto de Crédito Oficial (ICO). At the same time, a 15-year multicurrency loan was arranged, originally for ECUs 1,200 million (1st to 5th ICO-EIB tranches), which has been drawn down by Telefónica in six different currencies, has a five-year grace period and is repayable in 20 semiannual installments. The loan bears fixed interest in the first five years and is subsequently renegotiable for five-year periods.

In 1992 a new multicurrency loan was arranged for ECUs 150 million, Fl. 82 million and ¥ 19,500 million (7th to 9th ICO-EIB tranches), for the same purpose and under the same repayment terms as those described above. The loan bears interest at three-month Libor less 0.75% for the drawdowns in ECUs and Dutch guilders, and at six-month Libor plus 0.175% for the drawdowns in yen.

In August 1997 the 5th ICO-EIB loan denominated in ECUs and drawn down in several currencies was repaid early, giving rise to an extraordinary expense of Ptas. 7,124 million (see Note 20).

EIB (Telfisa)

In 1991 Telefonía y Finanzas, S.A. (Telfisa) obtained a 15-year multicurrency loan from the EIB for ECUs 600 million, drawn down in four different currencies, with a grace period of five years, repayable in 20 semiannual installments and with floating interest negotiated on a quarterly basis with the EIB.

Syndicated loan (Telefónica Internacional)

A long-term syndicated loan for US\$ 1,100 million was arranged on December 30, 1994. ABN Amro Bank NV and Banco de Negocios Argentaria acted as lead-managers. The loan is repayable in seven years, with a three-year grace period and final maturity in 2001. The interest periods may be one, three or six months, at the Company's discretion, and the applicable interest rate is Libor for the chosen period plus 0.17%.

Credit available

The loans and credits accounts reflect only the amounts drawn against the credit facilities, and there is no penalty or cost for the portion not drawn down. The undrawn credit facility funds available were as follows:

	Millions of Pesetas	
	Balance at 12/31/97	Balance at 12/31/96
Credit available at long term	147,946	253,848
Other credit facilities (floating policies)	50,531	76,000
Credit available at short term	154,220	140,665
Total	352,697	470,513

17. DERIVATIVES

In 1997 the Company continued to use derivatives both to limit interest rate and exchange risks on unhedged positions and to adapt its debt structure to market conditions.

As of December 31, 1997, the total outstanding volume of hedging transactions was Ptas. 656,215 million (Ptas. 140,240 million in 1996), and the total outstanding volume of forward transactions was Ptas. 137,207 million (zero in 1996).

In terms of volume, the most significant transactions carried out in 1997 by Telefónica de España, S.A., included most notably the hedging of a portion of its convertible bond issue. Of the US\$ 600 million issued, US\$ 400 million were hedged, 50% through a five-year US\$/Ptas. swap transaction in variable pesetas and 50% through a five-year forward transaction which can be canceled on the basis of the price of Telefónica shares in US\$.

In 1997 management of the derivatives portfolio gave rise to income of Ptas. 1,674 million (Ptas. 1,041 million in 1996).

The detail, by type of derivative, of the (notional) contractual values of the derivatives held by the Group as of December 31, 1997, is as follows:

Type of Risk Hedged	Millions					
	Notional Value	Derivative Currency Value		Underlying Currency Value		
Interest rate risk:	509,698					
Pta. interest rate swaps (1)	194,787	194,786	PTAS.			
Currency interest rate swaps	12,437	15,000	PTAS.	15,000	PTAS.	
US\$ interest rate swaps	148,817	980	US\$	980	US\$	
Pta. interest rate collar: (2)	120,250	120,250	PTAS.			
US\$ interest rate collar	33,408	220	US\$	220	US\$	
Exchange risk:	146,517					
Exchange swaps	8,926	8,926	PTAS.	120,000	Lire	
	23,074	23,074	PTAS.	17,000	Yen	
	37,388	37,389	PTAS.	227	ECUs	
	15,340	607	FF	93	ECUs	
	61,789	61,788	PTAS.	432	US\$	
Total	656,215					
Forward (trading)	137,207					
	32,580	32,580	PTAS.	221	US\$	
	59,986	395	US\$	12	UF	
	11,894	78	US\$	34,824	Peso	
	10,728	71	US\$	194	N. Soles	
	22,019	145	US\$	181	Reales	

(1) Includes Ptas. 20,000 million with deferred commencement

(2) Includes Ptas. 30,250 million with deferred commencement

The detail, by maturity, of the hedges is as follows:

Hedged Instrument	Millions of Pesetas				
	Amount	Up to 1 Year	1 to 3 Years	3 to 5 Years	Over 5 Years
Promissory notes	4,564	4,564	—	—	—
Loans	561,263	36,261	350,460	—	174,542
Peseta loans (1)	281,873	2,094	159,826	—	119,953
Foreign currency loans	279,390	34,167	190,634	—	54,589
Debentures and bonds	90,388	—	—	90,388	—
Peseta debentures and bonds	28,600	—	—	28,600	—
Foreign currency loans	61,788	—	—	61,788	—
Total	656,215	40,825	350,460	90,388	174,542
Forward	137,207	93,620	43,587	—	—

(1) Includes Ptas. 50,250 million with deferred commencement.

18. TAX MATTERS

Since 1990 Telefónica has filed consolidated tax returns with certain Group companies. 41 companies formed the tax consolidation group in 1997, including most notably, in terms of sales, Telefónica de España, Telefónica Servicios Móviles, Cabinas Telefónicas, Telefónica Publicidad e Información and Telefónica Sistemas.

Prepaid and deferred taxes

The detail as of December 31, 1997 and 1996, of the Telefónica Group's prepaid and deferred taxes, and of the variations therein in the years then ended, is as follows:

	Millions of Pesetas				
	Prepaid Taxes		Deferred Taxes		Intercompany
	Short Term	Long Term	Short Term	Long Term	Long Term
Balance at December 31, 1995	870	50,336	—	61,095	9,918
Reversal	(209)	(2,354)	—	(11,758)	(1,252)
Arising in the year	4,747	22,147	—	24,129	2,203
Exclusion of companies and other	69	(122)	—	(741)	89
Balance at December 31, 1996	5,477	70,007	—	72,725	11,018
Reversal	(5,902)	(18,650)	—	(5,591)	(1,865)
Arising in the year	4,982	41,471	—	3,233	1,484
Net international variations	—	—	—	13,790	—
Exclusion of companies and other (Note 14)	731	(65)	—	(14,732)	3,382
Balance at December 31, 1997	5,288	92,763	—	69,425	14,019

The prepaid taxes recorded by the Company relate mainly to early retirements, provisions for supplementary pension payments to retired employees and exchange differences. The deferred taxes recorded relate mainly to timing differences for accelerated depreciation.

Accrued taxes payable and tax receivables

The detail of the "Accrued Taxes Payable" and "Tax Receivables" captions as of December 31, 1997 and 1996, is as follows:

	Millions of Pesetas	
	Balance at 12/31/97	Balance at 12/31/96
Accrued taxes payable:		
Personal income tax withholdings	10,781	10,142
VAT and Canary Islands general indirect tax payable	5,054	2,122
Withholdings from income from movable capital and other	1,586	2,085
Corporate income tax	39,467	36,817
Single tax on revaluation Royal Decree-Law 7/1996	—	6,776
Local taxes	1,342	6,633
Accrued social security taxes	25,124	24,797
Foreign taxes	8,053	16,917
Total	91,407	106,289
Tax receivables:		
Corporate income tax prepayments-		
Withholdings at source from income from movable capital	2,046	2,547
Prepayments on consolidated income tax returns	48,503	16,514
Prepayments on individual income tax returns	163	71
Taxes, surcharges and other payments recoverable	393	529
Prepaid taxes	5,288	5,477
VAT and Canary Islands general indirect tax receivable	15,482	11,034
VAT deductible	41	9,224
Foreign taxes	15,272	10,565
Total	87,188	55,961

Reconciliation of consolidated income per books to consolidated taxable income

The reconciliation of income per books to taxable income for corporate income tax purposes for 1997 and 1996 is as follows:

	Millions of Pesetas	
	1997	1996
Consolidated income per books	337,641	275,881
Permanent differences	(175,869)	(102,081)
Timing differences:		
Arising in the year	88,790	68,288
Arising in prior years	(36,831)	22,364
Taxable income	213,731	264,452

The adjustments for permanent differences relate mainly to the release of provisions due to the dissolution of ITP, income earned by subsidiaries taxed abroad, income relating to associated companies and amortization of goodwill in consolidation.

The variations in timing differences in 1997 were as follows:

	Millions of Pesetas	
	Increase	Decrease
Voluntary early retirement	66,774	—
Provisions for supplementary pension payments to retired employees	2,661	—
Pension fund	3,352	—
Allowance for bad debts	10,424	—
Unrealized gains on transactions involving fixed assets	26	—
Loyalty bonuses and other	14,177	9,160
Fixed asset provisions	1,516	4
Intercompany transactions	—	4,242
Other	3,341	75
Timing differences arising in the year	102,271	13,481
Reversal of accelerated depreciation taken in prior years	15,897	48
Provision for diminution in value of securities portfolio in prior years	—	1,472
Exchange differences	—	27,277
Unrealized gains on transactions involving fixed assets	—	14,226
Reversal of allowance for bad debts	—	6,230
Reversal of provision for contingencies and expenses	—	640
Intercompany operators	5,329	—
Other	52	8,216
Timing differences arising in prior years	21,278	58,109

Calculation of corporate income tax expense and net corporate income tax payable

The corporate income tax expense and the net corporate income tax payable in 1997 and 1996 were as follows:

	Millions of Pesetas	
	1997	1996
Consolidated income	337,641	275,881
Permanent differences	(175,869)	(102,081)
Adjusted income per books	161,772	175,796
Gross tax at 35%	56,620	60,830
Tax credits and relief	20,066	34,759
Spanish corporate income tax expense	36,554	26,071
Tax effect of timing differences and other	2,913	10,746
Corporate income tax payable	39,467	36,817
Spanish corporate income tax expense	36,554	26,071
Tax accrual	—	(267)
Accrued foreign taxes	36,982	31,117
Total corporate income tax	73,536	56,921

Ptas. 35,336 million and Ptas. 55,755 million of tax credits and tax relief were taken in 1997 and 1996, respectively. In view of the ceilings on investment tax credits, as of December 31, 1997, after deducting the tax credits taken in 1997, the Telefónica tax Group has Ptas. 44,829 million of tax credits available from prior years, as follows:

Year	Millions of Pesetas				Total
	1993	1994	1995	1996	
Amount	4,465	6,460	21,061	12,843	44,829

The years open for review by the tax inspection authorities for the main applicable taxes vary from one consolidated company to another, although they are generally all years since 1993. No additional material liabilities are expected to arise for the Group in the event of a tax inspection.

Accrual of investment tax credit and permanent differences

The effect on the corporate income tax expense of the accrual of permanent adjustments (permanent differences) and investment tax credits was as follows:

	Accrual of Corporate Income Tax Expense (Note 13)	
	Tax Credits	Permanent Differences
Balance at December 31, 1995	—	—
Reversal	—	—
Arising in the year	17,027	—
Balance at December 31, 1996	17,027	0
Reversal	(1,938)	—
Arising in the year	8,133	7,301
Balance at December 31, 1997	23,222	7,301

19. OTHER NONTRADE PAYABLES

The detail of the balances of this caption in the consolidated balance sheets as of December 31, 1997, and 1996, is as follows:

	Millions of Pesetas	
	Balance at 12/31/97	Balance at 12/31/96
Accrued expenses payable	50,833	31,261
Dividends payable	45,531	39,327
Provision for extra-payroll	29,423	23,440
Exchange of telephone service with other operators	15,146	13,168
Guarantees and deposits	10,308	11,291
Provision for third-party liability	11,590	18,245
Other accounts payable (see Note 2-d)	128,634	23,305
Total	291,465	160,037

20. REVENUES AND EXPENSES

Sales and services

The detail, by business line, of net sales and services is as follows:

	Millions of Pesetas	
	1997	1996
Basic telephony		
Basic telephone service	1,007,844	947,748
Rental of circuits	98,133	73,317
Ibercom	73,516	69,290
Digital exchanges, intelligent network, ISDN and other	75,925	49,898
Terminals	73,456	71,696
Directories	12,050	11,547
	1,340,924	1,223,496
International communications	134,659	136,124
Public telephony	68,193	64,655
Data transmission	54,513	44,645
Other revenues	6,812	4,125
Total revenues of Telefónica	1,605,101	1,473,045
Cabitel	43,788	40,482
Telefónica Internacional Group	443,131	331,598
Telefónica Servicios Móviles Group	363,255	259,118
Telefónica Publicidad e Información Group	47,476	35,432
Other subsidiaries	198,210	173,706
Group revenues before intercompany sales	2,700,961	2,313,381
Intercompany sales	(337,859)	(307,323)
Total revenues from Group operations	2,363,102	2,006,058

Personnel expenses

The detail of personnel expenses is as follows:

	Millions of Pesetas	
	1997	1996
Compensation	424,320	413,668
Provisions to the pension allowance and other commitments to employees	23,155	22,823
Employee welfare expenses and other	123,420	118,191
	570,895	554,682

Average number of employees

Professional Category	1997	1996
General management	1,912	1,694
University graduates and special technicians	5,654	5,255
Junior college graduates and technicians	12,695	12,911
Internal plant supervisors and operators	16,386	17,051
External plant supervisors and operators	17,467	18,552
Applications operators and data processing assistants	998	713
Clerical staff	18,779	22,294
Sales staff	4,129	3,289
Operations personnel	8,338	5,696
Warehouse, office and garage personnel	1,602	1,640
Messengers, etc.	933	1,898
Other	3,258	1,155
Total	92,151	92,148

Other interest on accounts payable and similar expenses

The detail of the "Other Interest on Accounts Payable and Similar Expenses" caption is as follows:

	Millions of Pesetas	
	1997	1996
Debentures, bonds and other negotiable instruments	101,509	81,361
Loans and credits	25,756	33,124
Foreign currency loans	53,249	45,017
Promissory notes with credit entities	3,388	3,946
Other	6,065	18,197
	189,967	181,645

Exchange differences

The detail of exchange losses charged to income is as follows:

	Millions of Pesetas	
	1997	1996
Write-off of potential losses maturing in 1998 and subsequent years (see Note 4-k)	—	7,431
Repayment of loans	10,000	6,827
Deferred losses per Ministerial Order dated 3/12/93 (Note 4-k)	8,590	4,226
Operating transactions	2,476	1,968
	21,066	20,452

Extraordinary revenues

The detail of extraordinary revenues is as follows:

	Millions of Pesetas	
	1997	1996
Prior years' revenues	2,935	2,077
Indemnity payments for breach of contract	829	1,063
Consortium for compensation of insurance	281	934
Gain on sale of shares	319	---
Share in EURESCOM	763	67
Recovery of revenue on intergroup transactions	2,221	—
Collections from third-parties	617	—
Other	4,331	5,000
	12,296	9,141

Extraordinary expenses

	Millions of Pesetas	
	1997	1996
Supplementary pension payments to retired employees (Note 4-I)	9,370	9,109
Court-ordered indemnity payments	1,111	—
Provisions recorded:		
Cost of inclusion of retired employees in social security system (Note 4-I)	2,815	3,676
Voluntary early retirement and "preretirement" indemnities	90,166	58,519
Other	7,343	13,707
Compensation for transfers	802	897
Subsidies and voluntary donations	844	882
Early repayment of loans (Note 16)	7,124	—
Airtel Móvil indemnity (Ministerial Order 1252/1997)	2,967	—
PRI Program	1,255	4,444
Sundry	11,796	7,336
	135,593	98,570

Under Royal Decree-Law 1252/1997, Telefónica de España was obliged to reduce by Ptas. 15,000 million the interconnection charges to Airtel Móvil, S.A., thus concluding the dispute between the Spanish Government and the European Commission regarding the contributions made by Airtel Móvil for the award of the license to provide GSM services. In addition to other measures adopted by the Spanish government, said decision was completed with the signature by Telefónica and Airtel of a commercial agreement which is satisfactory to the interests of both companies. Charges are made to expenses for the year as the interconnection revenues arise. Ptas. 2,967 million were recorded under the "Extraordinary Expenses" caption in 1997 in this connection.

Losses on fixed assets

This caption includes Ptas. 38,100 million in 1997 and Ptas. 47,918 million in 1996 recorded as a result of the dismantling of Telefónica's plant for network digitalization.

Management contract with Telefónica de Argentina, S.A.

In November 1990, Telefónica de España, S.A. and Telefónica Argentina entered into a management contract expiring in 2003 regulating the counseling services rendered by Telefónica de España, S.A. and the price thereof. The revenues received in this connection, net of the payments for third-party counseling, amounted to Ptas. 9,219 million in 1997 and Ptas. 8,296 million in 1996 and were recorded under the "Sundry and Other Current Operating Revenues" and "Other Operating Expenses" captions.

Other technical services and management transfer contracts

On May 16, 1994, CPT and ENTEL PERÚ each, on an individual basis, entered into a technical know-how and management transfer contract with Telefónica Internacional de España, S.A., for a five-year term, automatically renewable for additional five-year terms, up to a maximum of 20 years, coinciding with the initial term of the assignment contract.

Telefónica Internacional de España, S.A., receives as compensation quarterly fees net of taxes, which in the case of the transfer of technical know-how is equal to 1% of the revenues for services billed by the companies. The management fee is equal to 9% of the operating income, excluding depreciation, amortization of intangible assets, provisions for future expenses, financial expenses, payment of fees, taxes and levies, rights, duties and royalties contained in the service contracts.

Also, pursuant to clause eight of the contract, and due to the merger of CPT with ENTEL PERÚ, from the last quarter of 1994 the fee will be determined only for the merged entity on the basis of its statement of income results.

In December 1996 following the privatization of CRT, the consortium which was awarded a holding in Companhia Riograndense de Telecomunicações (CRT) and in which Telefónica Internacional has a 73% holding, signed an agreement whereby it receives 1% of CRT's net revenues on the basis of compliance with certain network service quality requirements defined in the agreement. The agreement has a five-year term, renewable for a further five years, and is consequently renewable for consecutive two-year periods.

In 1997, this contract generated Ptas. 1,023 million of revenues allocable to the Group before taxes and withholdings which were recorded under the "Sundry and Other Current Operating Revenues" caption.

21. DIRECTORS' REMUNERATION AND OTHER BENEFITS

In 1997 and 1996 the compensation paid to the Board members for salaries, per diems and attendance fees, amounted to Ptas. 783 million and Ptas. 276 million, respectively.

The pension and life insurance commitments to directors with executive functions arise solely from their status as employees and amounted to Ptas. 2 million for each financial year. There were no other pension commitments to the rest of the Board members.

It should be noted that in 1997 the Company's privatization process concluded, giving rise to a significant change in the composition of the Board of Directors, with the substitution of the Spanish Government's representatives by prestigious personnel from the academic and professional fields. Also, in 1997 the *modus operandi* of the Board of Directors was substantially changed with the setting-up of specific support committees in the Remuneration and Audit Departments, among others.

22. OTHER INFORMATION

a) Sundry commitments and rights-

	Millions of Pesetas	
	1997	1996
Financial transaction guarantees	173,738	84,434
Guarantees provided for employees	209	219
Other	2,333	—

The "Financial Transaction Guarantees" caption includes mainly the guarantees provided by Telefónica for its subsidiaries and investees through bank guarantees of their transactions with third parties.

No loss is expected in connection with these commitments.

Pursuant to the purchase agreement entered into between Telefónica and T. Multimedia, S.A., to acquire a 49% holding in GMAF, the Company granted a put option for the remaining 49% to the seller, for a price resulting from increasing the amount paid for the portion purchased, by one-year Mibor applied to said amount, through the date on which the option were exercised, and reduced by such adjustments to the net worth as might be declared appropriate as a result of the review process currently being concluded. This option was granted for a three-year term as from July 25, 1997, although it may not be exercised until July 24, 1998.

Also, Telefónica has provided guarantees to Banco Santander, S.A. and Banco Central Hispanoamericano, S.A., by means of an agreement dated August 7, 1997, to ensure the liquidity and value of the investment made by them in Antena 3 de Televisión, S.A., including interest at Mibor for the period between the exercise of the option, less the dividends received in said period. This guarantee is applicable after the second year of investment pursuant to the legislation in force.

b) Call option on Telefónica Larga Distancia de Puerto Rico

Under the shareholder agreements entered into between the Group and the Telecommunications Authority of Puerto Rico (TAPR), Telefónica Internacional has a call option on 19% of the shares of TLD owned by PRTA for a price of US\$ 140 per share plus an amount equal to interest earned up to the date of exercise of the option, calculated at 8% annual compound interest. Also, it is obliged to purchase, at the request of PRTA, and not before December 22, 1997 unless a situation of insolvency arises, said number of shares at the above-mentioned price. As of December 31, 1997, this call option had not been exercised.

c) Put option on Telefónica Perú Holding

On November 8, 1994, in compliance with a call option contract, 10% of the capital stock of Telefónica Perú Holding, S.A. held by the Company at that date was transferred to local Peruvian companies. Simultaneously, Telefónica Internacional arranged a put option with these buyers, whereby it undertook, within three years from the original sale, to repurchase from the current owners 10% of Telefónica Perú Holding, S.A. if the owners exercise the put option.

The exercise price of this option will be equal to the acquisition price of the shares capitalized at a market interest rate less any cash flows collected by the purchaser for maintenance of the investment and for participation in the technical know-how and management transfer contract, capitalized at the same interest rate. This option, whose initial maturity was set for November 1997 was extended through May 1998.

d) Put option on CRT shares-

Telefónica Internacional entered into a put option contract with RBS, a Brazilian partner in the consortium to which the shares of CRT were awarded. Under this contract, Telefónica Internacional undertakes to buy 10% of the shares of the consortium or of such investor company as may replace it, owned by RBS. This option will be exercisable on December 27, 2001, depending on whether or not RBS has fulfilled certain financial obligations. The price will be the initial acquisition price of the shares. If a loss arises as a result of the difference between the option exercise price and the market price of the shares at the time of sale, RBS must compensate Telefónica Internacional de España, S.A. by means of shares of the consortium (or of such company as may replace it) owned by RBS. If, on the contrary, a capital gain should arise, it would correspond to RBS.

RBS also holds a call option on 17% of the shares of the consortium (or of such company as may replace it) owned by Telefónica Internacional. The exercise of this option, if appropriate, will take place on the 1,097th day from the date of acquisition of the shares of CRT. Until the date of the possible exercise of the option, the voting rights on these shares are held by RBS. If the option is not exercised on the date stipulated for exercise, the aforementioned voting rights will automatically be assigned to Telefónica Internacional. The price of the above-mentioned option will be the initial acquisition price, capitalized at three-year LIBOR plus 40 basis points.

e) Call option on Multicanal

On October 9, 1997, Telefónica Internacional signed a contract with the CLARIN Group whereby call and put options were reciprocally granted on the shares of Multicanal, owned by the Telefónica Internacional Group. Consequently, the CLARIN Group holds the call option right on the shares, under this contract from the date on which it was signed until April 9, 1998, for an amount between US\$ 302 million and US\$ 320.5 million, depending on the date of execution of the sale of the aforementioned shares, which is stipulated for between April 9 and May 9, 1998, for US\$ 320.5 million.

f) Litigation in progress-

On February 18, 1998, in relation to the appeal filed against the decision of the Ministry of Development authorizing the sale of Antena 3 Televisión, S.A. to Telefónica de España, S.A., the Spanish Court of Appeals ordered the precautionary stay of the authorization granted. Management of Telefónica de España, S.A. declares its total disagreement with the grounds of the order and expects to obtain a resolution favorable to its interests through the appropriate legal action. Until the appeal filed has been not definitively resolved, the ownership and management of Antena 3 will remain unchanged, given the suspension triggered by the appeals filed.

In any event, a hypothetical annulment of the above-mentioned share purchase of shares would involve the recovery by Telefónica de España, S.A. of the investment made by it.

There is litigation against certain Telefónica Group operators relating to the disconnection of entertainment lines, matters relating to competition and other issues. This litigation is at the processing or appeal stage. The companies' legal advisers consider that the outcome of this litigation will not lead to material liabilities.

23. SUBSEQUENT EVENTS

Sale of ownership interest in Cotelco (see Note 2-d)

On January 27, 1998, the Telefónica Group sold its ownership interest (39.83%) in Compañía Celular de Colombia, S.A. (COCELCO) to the majority shareholder of the company (Grupo Sarmiento) for a total of US\$ 50.6 million and obtained gains of approximately Ptas. 1,037 million.

The Telefónica Group's percentage of ownership at the time of its sale was as follows:

Telefónica de España, S.A.....	14.51%
Telefónica Internacional, S.A.....	16.32%
Compañía de Telecomunicaciones de Chile, S.A.....	9.00%

Interim dividend

From January 19, Telefónica distributed an interim dividend of Ptas. 40 gross (Ptas. 30 net) per share out of 1997 income, by means of the presentation of the related ownership certificate issued by "Servicio de Compensación y Liquidación de Valores, S.A. (the Spanish Securities Clearing and Settlement Service).

Issue of debentures

On January 28, 1998, Telefónica formalized the issue of debentures for Ptas. 70,000 million, divided into 7 million debentures of Ptas. 10,000 par value each. The annual nominal interest rate is 4.8414%, which will accrued from March 3, 1998 (date of issue) to March 3, 2008 (date of redemption), payable semiannually.

Loan to Telefónica Móviles

The European Investment Bank (BEI), granted Telefónica Móviles a credit line for Ptas. 65,000 million for 1997/1998 for the "Telefónica Mobile Telephony" project.

The Company arranged an exchange rate hedging SWAP transaction for the dollar tranche with the Chase Manhattan Bank.

Alliance between Telefónica and Recoletos Pearson Group

On February 9, 1998, the Stockholders' Meetings of Antena 3 T.V. and Recoletos, a Spanish subsidiary of the Pearson Group, resolved to increase their capital to cross-sell shares, thus ratifying the agreement reached by them in September with Telefónica de España, which envisages the acquisition by Telefónica Medios de Comunicación of a 20% holding in Recoletos and the acquisition by the latter of a 10% holding in Antena 3.

24. 1997 AND 1996 STATEMENTS OF CHANGES IN FINANCIAL POSITION

Application of funds	Millions of Pesetas		Source of funds	Millions of Pesetas	
	1997	1996		1997	1996
Funds applied in operations	—	—	Funds from operations	1,147,863	948,690
Start-up and debt arrangement expenses	9,740	4,581	Contributions from shareholders-		
Fixed asset additions-			a) Capital increases	—	—
a) Intangible assets	51,043	45,382	b) Paid-in surplus	—	—
b) Property and equipment	634,845	678,871	c) Minority interests	723	4,722
c) Long-term financial investments	545,438	142,944	Deferred revenues	24,381	17,837
Revaluation reserve	—	6,776	Long-term deferred taxes	3,550	5,032
Dividends	116,164	101,593	Long-term debt	518,725	188,469
Repayment or transfer			Fixed asset disposals-		
of long-term debt	424,531	316,587	a) Intangible assets	—	—
Provisions	142,129	58,331	b) Property and equipment	13,108	13,076
Other funds applied	2,144	7,398	c) Long-term financial investments	87,670	36,053
Decrease in working capital due			Provisions and deferred charges	—	—
to disposal of shareholdings	563	11,000	Increase in working capital due to disposal of		
Decrease in working capital due			shareholdings	—	—
to acquisition of shareholdings	—	—	Increase in working capital due		
Variation in working capital due			to inclusion of subsidiaries	9,702	1,474
to translation differences	(2,379)	(924)			
Total funds applied	1,924,218	1,372,539	Total funds obtained	1,805,722	1,215,353
Funds obtained in excess			Funds applied in excess		
of funds applied	—	—	of funds obtained	118,496	157,186
(Increase in working capital)			(Decrease in working capital)		
Total	1,924,218	1,372,539	Total	1,924,218	1,372,539

VARIATION IN WORKING CAPITAL

	Millions of Pesetas			
	1997		1996	
	Increase	Decrease	Increase	Decrease
Due from stockholders for capital calls	—	—	—	4
Inventories	3,857	—	4,798	—
Accounts receivable	121,456	—	106,816	—
Accounts payable	—	308,441	—	245,611
Short-term financial investments	90,250	—	—	32,404
Cash	—	1,845	714	—
Accrual accounts	—	23,773	8,505	—
Total	215,563	334,059	120,833	278,019
Variation in working capital	118,496	—	157,186	—
Total	334,059	334,059	278,019	278,019

The reconciliation of the balances in the statements of income to the funds obtained from operations is as follows:

	Millions of Pesetas	
	1997	1996
Income	190,063	160,282
Income attributed to minority interests	74,042	58,678
Income (loss) attributable to associated companies	(9,958)	(7,811)
	254,147	211,149
Add:		
Dividends at companies carried by the equity method	29,465	5,550
Depreciation and amortization	602,657	526,229
Amortization of debt arrangement expenses	3,754	3,603
Amortization of goodwill in consolidation	33,312	16,786
Provision for diminution in value of financial investments	213	911
Exchange differences	4,166	1,416
Undepreciated plant dismantled	38,100	47,918
Provision for inventory adjustment	888	2,496
Other provisions	179,783	97,739
Deferred interest	55,656	55,987
Paid-in surplus and repayment	1,366	—
Amortization of COOB 92 and EXPO 92 expenses	—	12
Property and equipment and intangible assets	3,444	5,707
Financial provision and supplementary pension payments to retired employees	9,370	9,109
Loss on disposal of consolidated companies	68	2,609
Less:		
Gain on disposal of financial investments	122	73
Gain on disposal of property and equipment	14,740	10,435
Capital subsidies	11,285	10,317
Nonrefundable third-party contributions	13,504	—
Deferred taxes and long-term advances	1,402	7,935
Gain on disposal of consolidated companies	27,371	10,335
Other	102	(564)
Funds from operations	1,147,863	948,690

The funds used for acquisition or disposal of holdings were as follows:

Effect on Working Capital	Millions of Pesetas			
	12-31-97		12-31-96	
	Acquisitions	Disposals	Acquisitions	Disposals
Financial investments and change in consolidation method	(35,155)	50,215	(5,155)	5,852
Due from stockholders for uncalled capital	—	—	—	(198)
Start-up expenses	22	—	—	(67)
Intangible assets	598	(116)	—	(129)
Property and equipment	21,475	(2,767)	3,484	(2,824)
Long-term financial investments	103	(21,064)	225	(3,096)
Goodwill in consolidation	25,795	—	—	—
Deferred charges	—	—	—	(121)
Capital increase	—	—	—	(3,000)
Prepaid taxes	—	—	—	(121)
Minority interests	(18)	1,276	—	1,243
Deferred revenues	—	116	—	4
Income for the year through date of sale	—	—	—	(903)
Provisions	(1,692)	48	—	1,520
Long-term debt	(8,330)	158	(28)	8,542
Losses/gains on disposal of holdings	—	(27,303)	—	2,843
Deferred taxes	—	—	—	1,455
Working capital	2,798	563	(1,474)	11,000
Price of acquisition or disposal of holdings	35,155	50,215	5,155	5,852

25. EXPLANATION ADDED FOR TRANSLATION TO ENGLISH

These consolidated financial statements are presented on the basis of accounting principles generally accepted in Spain. Certain accounting practices applied by the Group that conform with generally accepted accounting principles in Spain may not conform with generally accepted accounting principles in other countries.

EXHIBIT I

DETAIL OF GROUP AND ASSOCIATED COMPANIES AND INVESTEES AS OF DECEMBER 31, 1997

GROUP COMPANIES AND THEIR HOLDINGS	Ownership			Capital	Reserves	Interim dividend	Income (loss)	Book value	Consolidation Method	Value in (10) Consolidation
	Direct	Indirect	Telefónica Group							
Cabinas Telefónicas, S.A. (CABITEL) (*) (**) (1) Installation of public telephones Plaza de Carlos Trias Bertrán, 7 - 28020 Madrid	100.00%		100.00%	200	5,052	-2,045	2,891	200	G. I.	
Casiopaea Reaseguradora, S.A. (3) Reinsurance 73, Rue du Fort Neipperg - L-2230 Luxembourg	100.00%		100.00%	498	134		273	498	G. I.	
Péyade Peninsular Correduría de Seguros del Grupo Telefónica, S.A. (3) Distribution, promotion or preparation of insurance contracts, operating as a broker Avda. General Perón, 38 Master II - 17ª P. 28020 Madrid	16.67%	83.33%	100.00%	60	196		167	60	G. I.	
Seguros de Vida y Pensiones Antares, S.A. (3) Life insurance and pensions Avda. General Perón, 38 - 28020 Madrid	21.33%	78.67%	00.00%	1,500	1,288		747	1,960	G. I.	
Fonditel Entidad Gestora de Fondos de Pensiones, S.A. (3)		3.78%								
Compañía Española de Tecnología, S.A. (COMET) (*) (**) (3) Promotion of business initiatives and holding of securities Villanueva, 2 duplicado planta 1ª Oficina 23 - 28001 Madrid	100.00%		100.00%	1,049	-249		-3	1,682	G. I.	
Satel, S.A. (8) Comandante Zonta, 4 - 28020 Madrid		85.00%	85.00%	125	N/D		N/D	81	C.	8
Cleon, S.A. (3) Property development Villanueva, 2 duplicado planta 1ª Oficina 23 - 28001 Madrid		50.00%	50.00%	1,370	-52			685	P.	
Barcelona Tecnología, S.A. Venture capital company c/60 - 25ª, 27ª Sector A Polígono Industrial Zona Franca 08040 Barcelona.		4.21%	4.21%	238	12		17	10	C.	10
Catalana D'Iniciatives, C.R., S.A.		1.26%								
Fonditel Entidad Gestora de Fondos de Pensiones, S.A. (3) Pension fund management Pedro Teixeira nº 8 - 3ª P. - 28020 Madrid	77.22%	3.78%	81.00%	2,612	848		726	2,115	G. I.	
Playa de Madrid, S.A. (*) (**) (2) Distribution of all manner of goods, operation of sporting and hospitality facilities Doctor Fleming, 3 - 1ª P. - 28036 Madrid	100.00%		100.00%	40	112		15	54	G. I.	
Taetel, S.L. (*) (**) (3) Acquisition, holding and disposal of shares and holdings in other companies Beatriz de Bobadilla, 3 - 28040 Madrid	100.00%		100.00%	4,700	1,466	-158	226	4,700	G. I.	
Telecomunicaciones Marinas, S.A. (TEMASA) (*) (**) (2) Drilling, laying and repair of underwater cables Silva, 1 - Pl. 3ª - 28013 Madrid	100.00%		100.00%	1,376	4,676	-1,285	1,883	1,326	G. I.	
Telefonía y Finanzas, S.A. (TELFISA) (*) (**) (3) Integrated cash management, counseling and financial support for Group companies General Perón, 38 - Master II Pta. 15 - 28020 Madrid	100.00%		100.00%	500	293		94	2,099	G. I.	
Telefónica Investigación y Desarrollo, S.A. (TIDSA) (*) (**) (2) Telecommunications research activities and projects. Emilio Vargas, 6 - 28043 Madrid	100.00%		100.00%	1,000	2,974	-439	706	1,000	G. I.	
Telefónica North America, INC (3) Financial intermediation 1209 Orange Street, 19.801 Wilmington/New Castle County Delaware (U.S.A.)	100.00%		100.00%	1				1	G. I.	
Telefónica Telecomunicaciones Públicas, S.A. (*) (**) (2) Public telecommunications activities Paseo de Recoletos, 41 - 28004 Madrid	100.00%		100.00%	10				10	G. I.	
Teleinformática y Comunicaciones, S.A. (TELYCO) (*) (**) (2) Promotion, marketing and distribution of telephone and telematic equipment and services Raimundo Fernández Villaverde, 28 - Pl. 2ª - 28003 Madrid	100.00%		100.00%	460	958		619	2,075	G. I.	
Telefónica Europe, B.V. Attracting funds in capital markets Aert van Nesstraat 45, 4ª Rotterdam - 3012 CA - Holanda	100.00%		100.00%	8			14	8	G. I.	
Urbana Ibérica, S.A. (3) (*) (**) (2) Collection of debts outstanding and management of the cash generated by the sale of land General Perón, 38 - Master II Pta. 15 - 28020 Madrid	100.00%		100.00%	264	-41		1	14	G. I.	

(*) Companies filing consolidated corporate income tax returns in 1996.

(**) Companies filing consolidated corporate income tax returns in 1997.

DETAIL OF GROUP AND ASSOCIATED COMPANIES AND INVESTEEES AS OF DECEMBER 31, 1997

GROUP COMPANIES AND THEIR HOLDINGS	Ownership			Capital	Reserves	Interim dividend	Income (loss)	Book value	Consolidation Method	Value in (10) Consolidation
	Direct	Indirect	Telefónica Group							
Telefónica Multimedia, S.A. (*) (**) (2) <i>Organization and operation of multimedia service activities and businesses</i> <i>Rafael Calvo, 18 - 28.010 Madrid</i>	100.00%		100.00%	20,000	-334		-6,093	20,000	G. I.	
Telefónica Servicios Audiovisuales, S.A. (*) (**) (2) <i>Audiovisual telecommunications services of all kinds</i> <i>Virgilio, 2 - Edificio 2 - Ciudad de la Imagen (Pozuelo de Alarcón) - 28223 Madrid</i>		100.00%	100.00%	1,000	393		523	1,393	G. I.	
Telefónica Cable, S.A. (2) <i>Cable telecommunications+D149 systems services</i> <i>Virgilio, 2 - Edificio 2 - Ciudad de la Imagen (Pozuelo de Alarcón) - 28223 Madrid</i>		100.00%	100.00%	3,000			-265	3,000	G. I.	
Telefónica Cable Madrid, S.A. <i>Cable television systems and value-added services</i> <i>Virgilio, 2 - Edificio 2 - Ciudad de la Imagen (Pozuelo de Alarcón) - 28223 Madrid</i>		66.00%	66.00%	100	-23		-12	50	G. I.	
Telefónica Cable Catalunya, S.A. <i>Cable television systems and value-added services</i> <i>Avda. Icaria, 136 - 08005 Barcelona</i>		100.00%	100.00%	100			-20	100	G. I.	
Telefónica Cable Cantabria, S.A. <i>Cable television systems and value-added services</i> <i>La Milagrosa, 2 - 39001 Santander</i>		100.00%	100.00%	100	-25		-12	75	G. I.	
Sociedad General de Cablevisión Alicante, S.A. <i>Cable television systems and value-added services</i> <i>Avda. Pérez Galdos, 5-7 - 03004 Alicante</i>		100.00%	100.00%	100	-7		-9	93	G. I.	
Telefónica Cable Asturias, S.A. <i>Cable television systems and value-added services</i> <i>Gral. Elorza, 17 - 33001 Oviedo</i>		100.00%	100.00%	100	2		2	101	G. I.	
Telefónica Cable Euskadi, S.A. <i>Cable television systems and value-added services</i> <i>Gregorio de la Revilla, 27 - 48010 Bilbao</i>		100.00%	100.00%	100	-22		-12	78	G. I.	
Sociedad General de Cablevisión Cádiz, S.A. <i>Cable television systems and value-added services</i> <i>Santa María Soledad, 6 - 11006 Cádiz</i>		100.00%	100.00%	100	-9		-10	93	G. I.	
Sociedad General de Cablevisión Granada, S.A. <i>Cable television systems and value-added services</i> <i>Avenida del Sur, 1 - 18014 Granada</i>		100.00%	100.00%	100	1		3	101	G. I.	
Sociedad General de Cablevisión León, S.A. <i>Cable television systems and value-added services</i> <i>Padre Isla, 16 - 24002 León</i>		100.00%	100.00%	100	1		2	101	G. I.	
Sociedad General de Cablevisión Lleida, S.A. <i>Cable television systems and value-added services</i> <i>Clot de les Monges, 6-8 - 25007 Lleida</i>		100.00%	100.00%	100	-17		-11	83	G. I.	
Sociedad General de Cablevisión Málaga, S.A. <i>Cable television systems and value-added services</i> <i>Hilera, 2 - 29007 Málaga</i>		100.00%	100.00%	100	2		3	101	G. I.	
Telefónica Cable Murcia, S.A. <i>Cable television systems and value-added services</i> <i>San Antón, 4 - 30009 Murcia</i>		100.00%	100.00%	100	-11		-10	89	G. I.	
Telefónica Cable Navarra, S.A. <i>Cable television systems and value-added services</i> <i>Monasterio de la Oliva, 9 - Pamplona</i>		69.00%	69.00%	100	-16		-10	58	G. I.	
Telefónica Cable La Rioja, S.A. <i>Cable television systems and value-added services</i> <i>San Millán, 3 - 26004 Logroño</i>		100.00%	100.00%	100	-1		-8	101	G. I.	
Telefónica Cable Andalucía, S.A. <i>Cable television systems and value-added services</i> <i>Graham Bell, 5 - 41.010 Sevilla</i>		73.00%	73.00%	1,000	-14		-10	720	G. I.	
Telefónica Cable Valencia, S.A. <i>Cable television systems and value-added services</i> <i>San Vicente, 148 - 46007 Valencia</i>		100.00%	100.00%	100	-8		-9	92	G. I.	
Sociedad General de Cablevisión Valladolid, S.A. <i>Cable television systems and value-added services</i> <i>Duque de la Victoria, 10 - 47001 Valladolid</i>		100.00%	100.00%	100			-8	101	G. I.	
Telefónica Cable Balears, S.A. <i>Cable television systems and value-added services</i> <i>Federico García Lorca, 2 - 07014 Palma de Mallorca</i>		100.00%	100.00%	100	-14		-11	85	G. I.	

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(**) Companies filing consolidated corporate income tax returns in 1997.

DETAIL OF GROUP AND ASSOCIATED COMPANIES AND INVESTEEES AS OF DECEMBER 31, 1997

GROUP COMPANIES AND THEIR HOLDINGS	Ownership			Capital	Reserves	Interim dividend	Income (loss)	Book value	Consolidation Method	Value in (10) Consolidation
	Direct	Indirect	Telefónica Group							
Telefónica Cable Castilla y León, S.A. Cable television systems and value-added services Avda. Reyes Católicos, 38 - 09005 Burgos		61.00%	61.00%	1,000	-4		-7	612	G. I.	
Sociedad General de Cablevisión Canarias, S.A. Cable television systems and value-added services Alcalde Mandillo Tejera, 8 - 38007 Santa Cruz de Tenerife		51.00%	51.00%	215	-32		-23	96	G. I.	
Servicios y Contenidos por la Red, S.A. (SCR) (*) (2) Provision of services in the leisure and entertainment areas Julián Comanillo, 6, 2ª P. - 28037 Madrid.		100.00%	100.00%	220	133		-187	210	G. I.	
Ifigenia Plus, S.L. Culture and education software Almagro, 12 -		10.00%	10.00%	16	-4		1		I.	
Servicios de Teledistribución, S.A. (S.T. HILO) (*) (**) (2) Supply of services in the teledistribution industry Luchana, 23 - 28010 Madrid		100.00%	100.00%	210	407		117	297	G. I.	
Producciones Multitemáticas, S.A. (**) (2) Production, distribution, sale and purchase and operation of television and movie productions Virgilio, 2 - Edificio 2 - Ciudad de la Imagen (Pozuelo de Alarcón) - 28223 Madrid.		100.00%	100.00%	2,000			-267	2,000	G. I.	
Rem Infográfica, S.A. (2) Production of 3D objects, promotion and marketing of computer products and services Plaza de Santa Bárbara, 10 - 1ª Dcha. - 28004 Madrid		100.00%	100.00%	10			-362		G. I.	
Lola Films, S.A. Movie production Doctor Gimeno, 12 - Barcelona		33.33%	33.33%	1,050	190		136	600	E.	459
Antena 3 de televisión, S.A. Management of public and satellite TV service Avda. Isla Graciosa, s.n. - San Sebastián de los Reyes - 28700 Madrid		25.00%	25.00%	25,000	2,563		126	26,004	E.	6,922
DTS Distribuidora de televisión digital, S.A. Digital TV via satellite services Rafael Calvo, 18, Pta. 3ª - 28010 Madrid		35.00%	35.00%	15,000	10,000		-13,743	8,750	E.	3,940
Audiovisual Realtime BIT, S.A. (ARTBIT) Production of synthetic images Polígono Industrial de Inca. Solar en intersección de los viales C y D Mallorca 07300 Inca		25.00%	25.00%	100	-29		-89	25	E.	-4
Telefónica Publicidad e Información, S.A. (*) (**) (2) Publishing of directories and advertising for all types of media Avda. de Manoteros, 12 - 28050 MADRID	100.00%		100.00%	502	6,247	-4,500	6,844	996	G. I.	
Estrategias Telefónicas, S.A. (ESTRATTEL) (*) (**) (2) Services, promotion, marketing and market surveys relating to direct marketing Orsen, 4 - 1ª Izq. - 28002 Madrid		100.00%	100.00%	230	707	-634	1,339	411	G. I.	
Tempotel, Empresa de Trabajo Temporal, S.A. (*) (**) (2) Temporary employment agency Hernani, 64 - 28020 Madrid		100.00%	100.00%	10	-2		-5	10	G. I.	
Doubleclick Iberoamérica, S.L. (**) (2) Advertising in Internet Avda. de Manoteros, 12 - 28050 MADRID		90.00%	90.00%	149			-5	134	G. I.	
TMP Worldwide España, S.A. (2) Marketing and advertising of major customers in yellow pages Príncipe de Vergara, 112 - 4ª P. - 28002 Madrid		51.00%	51.00%	45	-14		13	23	G. I.	
Venturini España, S.A. (2) Printing and graphic arts Industria, 17 Tres Cantos - Madrid		25.00%	25.00%	500	72		15	125	E.	147
Euredit, S.A. Publishing of European yearbooks Avda. Friedland, 9 - 75008 París (Francia)		5.00%	5.00%	3 m.f.f.	N/D		N/D	13	I.	13
T.I. Telefónica Internacional de España, S.A. (1) (9) Investment in the telecommunications industry abroad Jorge Manrique, 12 - 28006 Madrid	100.00%		100.00%	119,009	208,225		35,140	217,713	G. I.	
Advance Telecomunicaciones, S.A. (ARGENTINA) Data service+D214		50.00%	50.00%	N/D	N/D		N/D	757	I.	757
Telefónica Panamericana - MCI (HOLANDA) Holding		50.00%	50.00%	N/D	N/D		N/D	802	I.	802
Cablevisión, S.A. (ARGENTINA) Cable television		33.28%	33.28%	N/D	N/D		N/D	57,139	I.	57,139

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(**) Companies filing consolidated corporate income tax returns in 1997.

DETAIL OF GROUP AND ASSOCIATED COMPANIES AND INVESTEEES AS OF DECEMBER 31, 1997

GROUP COMPANIES AND THEIR HOLDINGS	Ownership		Capital	Reserves	Interim dividend	Income (loss)	Book value	Consolidation Method	Value in (10) Consolidation
	Direct	Indirect							
Torneos y Competencias, S.A. (ARGENTINA) <i>Football content and +D311 rights</i>		26.67%	26.67%	N/D	N/D	N/D	10,309	I	10,309
Telefonica International, S.A. (LUXEMBURGO) (1) <i>Holding company</i>		100.00%	100.00%	71	-34	-8	961	G. I.	
Telefónica Finance Limited (ISLA DE MAN) (1) <i>Finance</i>		100.00%	100.00%	1	8,483	-2,028	1	G. I.	
Telefónica Bolivia Holding (BOLIVIA)		100.00%	100.00%	N/D	N/D	N/D	1		
Telefónica del Perú Holding (PERÚ) (1) <i>Holding company</i>		90.00%	90.00%	303,735	-8,035	7,763	249,701	G. I.	
Telefónica del Perú, S.A. (PERÚ) (1) <i>Operator of local, long-distance and international telephone services in Peru Avda. Arequipa, 1155 Santa Beatriz - Lima</i>		35.00%	31.50%	168,910	62,889	57,607	303,735	G. I.	
Telefonica International Holding, B.V. (HOLANDA) (1) <i>Holding company</i>		100.00%	100.00%	95,906	29,746	21,488	69,410	G. I.	
Telefónica Chile Holding, B.V. (HOLANDA) (1) <i>Holding company</i>		100.00%	100.00%	4,909	7,923	-2	31,192	G. I.	
Telefónica Internacional de Chile, S.A. (CHILE) (4) <i>Holding company</i>		100.00%	100.00%	11,272	141,057	25,814	12,880	G. I.	
Compañía de Telecomunicaciones de Chile, S.A. (C.T.C.), (CHILE) (4) <i>Telecommunications operator in Chile Avenida Providencia, 111 piso 29 Santiago de Chile</i>		43.62%	43.62%	160,575	126,219	55,354	42,963	G. I.	
Other holdings		N/A	N/A	N/A	N/A	N/A	N/A	E	1,899
Impresora y Comercial Publiguías, S.A. (CHILE) (4) <i>Publishing and sale of advertising. White and yellow pages Avda. de Santa María, 792 Santiago de Chile</i>		54.93%	54.93%	822	1,397	2,142	958	G. I.	
Telefónica Venezuela Holding, B.V. (HOLANDA) (1) <i>Holding company</i>		100.00%	100.00%	3	-6,532	3,209	11,924	G. I.	
Venworld Telecom, C.A. (VENEZUELA) (1) <i>Holding company</i>		16.00%	16.00%	N/D	N/D	N/D	45,758	E	
Clá, Andánima N. de Teléfonos de Venezuela, C.A.(CANTV) (VENEZUELA) (1) <i>Operador de Telecomunicaciones Avenida Libertador, Centro Nacional de Telecomunicaciones, Piso 1 - 1226 Caracas</i>		40.00%	6.40%	11,091	554,713	77,118	N/D	E	34,732
Compañía de Inver. en Telecomunicaciones, S.A.(COINTEL) (ARGENTINA) (11) <i>Holding company Tucumán, 1 P-18 Buenos Aires</i>		50.00%	50.00%	80,499	110,607	20,688	141,536	E	88,340
Telefónica de Argentina, S.A. (ARGENTINA) (11) <i>Telecommunications operator in southern Argentina Presidente Perón, 949 - piso 7 - 1038 Buenos Aires</i>		51.00%	25.50%	357,640	134,275	69,436	287,569	E	
TYSSA, Telecomunicaciones y Sistemas, S.A. (ARGENTINA) <i>Telecommunications systems consulting Presidente Perón, 949 P-14 - 1038 Buenos Aires</i>		40.40%	40.40%	N/D	N/D	N/D	116	I	116
Telefónica Larga Distancia de Puerto Rico, INC. (PUERTO RICO) (1) <i>Telecommunications operator Calle 1, Edificio n° 8, Metro Office Park, Sector de Buchanan. Guaynabo - Puerto Rico</i>		79.00%	79.00%	16,910	-1,281	6	17,167	G. I.	
Contactel (PORTUGAL) <i>Telecommunications operator (Radiopaging) Rua Luciano Cordeiro, 116 - 1050 Lisboa</i>		15.00%	15.00%	N/D	N/D	N/D	302	I	302
Telecomunicaciones Ultramarinas de Puerto Rico (PUERTO RICO) <i>Telecommunications operator</i>		14.90%	14.90%	N/D	N/D	N/D	3,280	I	3,280
Infonet Services Corporation (USA) (5) <i>Telecommunications operator 2100 East. Grand Avenue. El Segundo, California 90245 - 1022 USA</i>		18.74%	18.74%	N/D	N/D	N/D	5,320	I	5,320
Geostar Corporation, INC (USA)		N/D	N/D	N/D	N/D	N/D	646	I	646
Telefónica Do Brasil Holding, S.A. (BRASIL) <i>Holding company</i>		76.82%	76.82%	N/D	N/D	N/D	1	I	1
Companhia Riograndense de Telecomunicações (BRASIL) (2) <i>Telecommunications operator Avda. Borges de Medeiros n° 512, 15 andar/Porto Alegre - Rio Grande do Sul 90020-022 Brasil</i>		10.33%	10.33%	96,104	122,099	15,070	71,469	E	32,089
Other holdings		N/A	N/A	N/A	N/A	N/A	N/A	I	7,459
Telefónica Sistemas de Portugal (PORTUGAL)		25.00%							
Telur, S.A. (FEDERACION RUSA) <i>Manufacture of telecommunications equipment</i>		5.00%	11.60%	N/D	N/D	N/D	53	I	53

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DETAIL OF GROUP AND ASSOCIATED COMPANIES AND INVESTEEES AS OF DECEMBER 31, 1997

GROUP COMPANIES AND THEIR HOLDINGS	Ownership		Telefónica Group	Capital	Reserves	Interim dividend	Income (loss)	Book value	Consolidation Method	Value in (10) Consolidation
	Direct	Indirect								
T.S. Telefónica Sistemas, S.A. (*) (**) (2) <i>Telecommunications systems, network and infrastructure engineering</i> <i>Sor Angela de la Cruz, 3 - Pl. 9º - 28020 Madrid</i>	100.00%		100.00%	1,403	2,805		630	2,366	G. I.	
<i>Telefónica Sistemas de Información Geográfica, S.A. (TSIG) (*) (**) (2)</i> <i>Computer advisory services and digital cartography</i> <i>Rosario Pino, 5 - 10º P. - 28046 Madrid</i>		100.00%	100.00%	215	81	-40	95	230	G. I.	
<i>Telefónica Gestión de Sistemas, S.A. (TGS) (*) (**) (2)</i> <i>Systems outsourcing</i> <i>Sor Angela de la Cruz, 3 - 28020 Madrid</i>		100.00%	100.00%	50	93		-38	50	G. I.	
<i>Telefónica Sistemas Ingeniería de Productos, S.A. (TSIP) (*) (**) (2)</i> <i>Public communications network infrastructure</i> <i>Torrelaguna, 79 - 2º P. - 28043 Madrid</i>		100.00%	100.00%	150	139	-225	262	150	G. I.	
<i>Telefónica Sistemas Ingeniería de Productos, Seguridad, S.A. (TSIP-S) (*) (**) (2)</i> <i>Security and control installation and systems</i> <i>Condesa de Venadito, 1 - 9º P. - 28027 Madrid</i>		100.00%	100.00%	40	21		54	53	G. I.	
<i>Gestión y Operación de Redes, S.A. (GESTIRED) (*) (**) (2)</i> <i>Management and marketing of networks</i> <i>Sor Angela de la Cruz, 3 - 28020 Madrid</i>		100.00%	100.00%	70	-43			35	G. I.	
<i>T.S. Telefónica Sistemas de Portugal, S.A. (PORTUGAL) (2)</i> <i>Communications systems equipment engineering</i> <i>Proça de Albalade, 6 - 2º A-1 - 1700 Lisboa</i>		74.99%	99.99%	51	-34		-16	57	G. I.	
<i>Bitel Baleares Innovación Telemática, S.A. (6)</i> <i>Provision of systems engineering services in the information technologies and communications fields</i> <i>Paseo Marítimo, 38 A - 07005 Palma de Mallorca</i>		44.00%	44.00%	316	-79		-3	139	E.	103
<i>Servicio Educación a Distancia (S.E.D.)</i> <i>Advisory services and implementation of Virtual campuses+D391 for education purposes</i> <i>Alda. Tibidabo, 39</i>		40.00%	40.00%	10				4	E.	4
Telefónica Transmisión de Datos, S.A. <i>Data transmission</i> <i>Beatriz de Bobadilla, 18 - 28040 Madrid</i>	100.00%		100.00%	6,533	325		1,518	34,170	G. I.	
<i>Telefónica VSAT, S.A.</i> <i>Satellite telecommunications services</i> <i>Avenida Europa, 4. Edificio Bruselas. Parque empresarial de La Moraleja - 28109 Alcobendas</i>		100.00%	100.00%	262	233		33	751	G. I.	
<i>Telefónica Servicios Avanzados de Información, S.A. (TSAI) (*) (**) (2)</i> <i>Value-added services supporting voice, data, text and images for public and private sector systems</i> <i>Julián Camarillo, 6 - 28037 Madrid</i>		100.00%	100.00%	310	340		232	922	G. I.	
<i>Hispaservices, S.A. (2)</i> <i>Data processing via communication and computer networks</i> <i>Edificio Triada, Avda. de Burgos, 17 Torre A, 10º P. - 28036 Madrid</i>		88.00%	88.00%	350	-198		-115	67	G. I.	
Telefónica Servicios Móviles, S.A. (*) (**) (1) <i>Management and marketing of automatic mobile telephony</i> <i>Plaza de la Independencia, 6 - Pta. 5 - 28001 MADRID</i>	100.00%		100.00%	68,100	27,845		27,849	78,460	G. I.	
<i>Radioed I, S.A. (*) (**) (1)</i> <i>Group company management support. Trunking (Parent Company)</i> <i>Manuel Tovar, 43 - 2º - 28034 Madrid</i>		100.00%	100.00%	1,500	155		-428	2,750	G. I.	
<i>Radioed Madrid, S.A. (*) (**) (1)</i> <i>Trunking</i> <i>Manuel Tovar, 43 - 28034 Madrid</i>		100.00%	100.00%	150	-48		-36	260	G. I.	
<i>Radioed Bilbao, S.A. (*) (**) (1)</i> <i>Trunking</i> <i>Manuel Tovar, 43 - 28034 Madrid</i>		100.00%	100.00%	150	-49		-35	240	G. I.	
<i>Radioed Valencia, S.A. (*) (**) (1)</i> <i>Trunking</i> <i>Manuel Tovar, 43 - 28034 Madrid</i>		100.00%	100.00%	140	-35		-39	225	G. I.	
<i>Radioed Málaga - Costa del Sol, S.A. (*) (**) (1)</i> <i>Trunking</i> <i>Manuel Tovar, 43 - 28034 Madrid</i>		100.00%	100.00%	145	-31		-36	215	G. I.	
<i>Radioed Sevilla - Cádiz, S.A. (*) (**) (1)</i> <i>Trunking</i> <i>Manuel Tovar, 43 - 28034 Madrid</i>		100.00%	100.00%	160	-38		-44	255	G. I.	

(*) Companies filing consolidated corporate income tax returns in 1996.
 (**) Companies filing consolidated corporate income tax returns in 1997.

DETAIL OF GROUP AND ASSOCIATED COMPANIES AND INVESTEEES AS OF DECEMBER 31, 1997

GROUP COMPANIES AND THEIR HOLDINGS	Ownership			Capital	Reserves	Interim dividend	Income (loss)	Book value	Consolidation Method	Value in (10) Consolidation
	Direct	Indirect	Telefónica Group							
Radiored Santiago - La Coruña, S.A. (*) (**) (1) <i>Trunking</i> <i>Manuel Tovar, 43 - 28034 Madrid</i>		100.00%	100.00%	130	-29		-30	230	G. I.	
Radiored Zaragoza, S.A. (*) (**) (1) <i>Trunking</i> <i>Manuel Tovar, 43 - 28034 Madrid</i>		100.00%	100.00%	185	-58		-66	287	G. I.	
Radiored Canarias, S.A. (*) (**) (1) <i>Trunking</i> <i>Manuel Tovar, 43 - 28034 Madrid</i>		100.00%	100.00%	200			-25	200	G. I.	
Radiored Extremadura, S.A. (*) (**) (1) <i>Trunking</i> <i>Manuel Tovar, 43 - 28034 Madrid</i>		100.00%	100.00%	10			-1	10	G. I.	
Radiored Baleares, S.A. (*) (**) (1) <i>Trunking</i> <i>Manuel Tovar, 43 - 28034 Madrid</i>		100.00%	100.00%	200			-1	200	G. I.	
Radiored Catalunya, S.A. (*) (**) (1) <i>Trunking</i> <i>Manuel Tovar, 43 - 28034 Madrid</i>		91.00%	91.00%	200	-20		-18	273	G. I.	
Compañía Gestora del Servicio Mensatel, S.A. (1) <i>Management and marketing of the Mensatel radiopaging service</i> <i>Manuel Tovar, 35 - 3ª - 28034 Madrid</i>		89.99%	89.99%	667	398		-698	622	G. I.	
Telefónica Medios de Comunicación, S.A. (**) Holding of shares of companies in the media industry Gran Vía, 28 - 28013 Madrid	100.00%		100.00%	26,300			-1,303	26,300	G. I.	
Gestora de Medios Audiovisuales de Fútbol, S.L. <i>Football rights</i> <i>Consell de Cent, 425 - Barcelona</i>		49.00%	49.00%	20,000			-1,111	18,798	E.	9.256
Audiovisual Sport, S.L. <i>Holder of football rights</i> <i>O'Donnell, 12 - Madrid</i>		40.00%	19.60%	8,250			N/D	N/D	E.	N/A
Agencia EFE, S.A. <i>Obtainment and distribution of news throughout the world</i> <i>Espronceda, 32 - 28003 Madrid</i>		0.06%	0.06%	4,161	-1,275		-3,178	2	L	2
Telefónica Soluciones Sectoriales, S.A. (**) Advisory services for communications and information technologies companies Rosario Pino, 5 - 28020 Madrid	100.00%		100.00%	1,600			-55	1,600	G. I.	
Portel Servicios Telemáticos, S.A. (1) <i>Systems engineering and telecommunications in port areas</i> <i>Avda. de Portenón, 10 Campo de las Naciones - 28042 Madrid</i>		49.00%	49.00%	500	-41		-16	224	E.	217
Madrid 112, S.A. (6) <i>Emergency services and citizen advice in the Autonomous Community of Madrid</i> <i>Carretera de La Coruña, Km. 22 - Las Rozas - Madrid</i>		49.00%	49.00%	1,000			-157	471	E.	413
Tecnología e Ingeniería de Sist. y Servicios Avanzados de Telecom., S.A. (TISSAT) (7) <i>Systems engineering and marketing of advanced services</i> <i>Correos, 1 - 46002 Valencia</i>		30.77%	30.77%	130			23	29	E.	33
Buildnet (2) <i>On-line and sundry information services for the construction industry via own telecommunications system.</i> <i>Edificio Triada, Avda. de Burgos, 17 Torre A, 10ª - 28036 Madrid</i>		33.50%	33.50%	150			-96	11	E.	18
Caser MVS <i>Virtual insurance market research</i> <i>Plaza de la Lealtad, 4 - 28014 Madrid</i>		49.00%	49.00%	580				284	E.	284
Incotel <i>Provision of multimedia services</i> <i>Cebrión, 3 - 35003 Las Palmas de Gran Canaria</i>		40.00%	40.00%	50				20	E.	20
QSL <i>Teleassistance</i> <i>Pabellón nº 11 Isla de la Cartuja - Sevilla</i>		33.33%	33.33%	60			-26	20	E.	11
Casertel <i>Virtual insurance marketing</i> <i>Plaza de la Lealtad, 4 - 28014 Madrid</i>		15.00%	15.00%	500				75	L	75
Agencia de Certificación Electrónica, S.A. <i>Development of "Electronic notary" business+D458 through SET technology</i> <i>Sor Ángela de la Cruz, 3 - 28020 Madrid</i>		40.00%	40.00%	250			-31	97	E.	88

(*) Companies filing consolidated corporate income tax returns in 1996.

(**) Companies filing consolidated corporate income tax returns in 1997.

DETAIL OF GROUP AND ASSOCIATED COMPANIES AND INVESTEES AS OF DECEMBER 31, 1997

DEPENDENT COMPANIES	Ownership			Capital	Reserves	Interim dividend	Income (loss)	Book value	Consolidation Method	Value in (10) Consolidation
	Direct	Indirect	Telefónica Group							
Telefónica Fiat Factoring Establecimiento Financiero de Crédito, S.A. Factoring Pedro Teixeira, 8 - 28020 Madrid	50.00%		50.00%	1,560	-160		261	795	E.	831
Utilitel Comunicaciones, S.A. Value-added services and teleassistance Serrano, 41 - 28001 Madrid	50.00%		50.00%	400			-39	193	E.	180
Torre de Colçerola, S.A. Operation of a telecommunications tower and technical assistance and advisory services. Ctra. Vallvidrera-Tibidabo, s/nº - 08017 Barcelona	42.00%		42.00%	2,000	5		36	845	E.	857
Indra SSI, S.A. Software Velázquez, 132 - 28006 Madrid	36.56%		36.56%	2,302	2,576		1,158	2,121	E.	2,207
Sistemas Técnicos de Loterías del Estado, S.A. Operation of a gaming terminal system for Organismo Nacional de Loterías y Apuestas del Estado Manuel Tovar, 9 - 28034 Madrid	31.75%		31.75%	2,000	3,544		736	635	E.	1,994
Hispasat, S.A. Operation of a satellite telecommunications system Gobelas, 41-45 - 28023 Madrid	22.74%		22.74%	15,312	-5,933		2,240	5,339	E.	2,642
Sofres Audiencia de Medios, S.A. Market surveys and audience measurement Plaza Carlos Trias Bertrán, 7 - 28020 Madrid	25.00%		25.00%	210	507		303	435	E.	255
Amper, S.A. (9) Development, manufacture and repair of telecommunications systems and equipment Torrelaguna, 75 - 28027 Madrid	15.00%		15.00%	4,186	5,958		5,510	2,620	E.	2,348
Portugal Telecom, S.A. (PORTUGAL) Telecommunications operator Fontes Pereira de Melo, 40 - 1089 Lisboa	3.50%		3.50%	190,000 M.ESC	140,378 M.ESC		52,193 M.ESC	41,212	E.	11,105
<hr/>										
INVESTEES	Ownership			Capital	Reserves	Interim dividend	Income (loss)	Book value	Consolidation Method	Value in (10) Consolidation
	Direct	Indirect	Telefónica Group							
Promoció de Ciutat Vella, S.A. Urban improvements in the Ciutat Vella of Barcelona Ramblas, 77 - 08002 Barcelona	3.57%		3.57%	2,800				100	I.	100
Catalana D'Iniciatives, C.R., S.A. Promotion of nonfinance entities Passeig de Gràcia, 2 - 2ºB - 08007 Barcelona.	2.35%	1.26%	3.61%	5,000	874		426	240	I.	240
I-CO Global Communications (HOLDINGS) Limited	0.49%		0.49%	N/D	N/D		N/D	1,002	I.	1,002
Other holdings	N/A	N/A	N/A	N/A	N/A		N/A	4,935	I.	4,935
<hr/>										
TOTAL VALUE OF CONSOLIDATED DEPENDENT COMPANIES (Note 8)										201,390
TOTAL VALUE OF CONSOLIDATED INVESTEES (Note 8)										92,642

- (1) Companies audited by Arthur Andersen.
 (2) Companies audited by Price Waterhouse
 (3) Companies audited by K.P.M.G. Peat Marwick.
 (4) Companies audited by Langton Clarke.
 (5) Company audited by Deloitte & Touche.
 (6) Company audited by Ernst & Young.

- (7) Company audited by Coopers & Lybrand.
 (8) Companies in liquidation.
 (9) Consolidated figures.
 (10) This figure refers to the contribution to the Telefónica Group and not to the sub-groups to which the contributing companies belong.
 (11) Company audited by Pistrilli, Díaz & Asociados.

- I.G. Companies consolidated by the global integration method..
 P.I.. Companies consolidated by the proportional integration method.
 E. Companies carried by the equity method.
 N/A Not applicable.
 N/D Information not available.
 Figures in foreign currencies: M=Millions, t=Thousands.
 Provisional figures for dependent companies and investees.

EXHIBIT II

- The changes in the consolidated Group in 1997 and 1996 were as follows:

1997

- In April 1997 the Telefónica Group acquired a 25% stake in Telefónica Cable, S.A., bringing its holding to 100%.
- Telefónica incorporated Telefónica Medios de Comunicación, S.A. and Telefónica Soluciones Sectoriales, S.A., and acquired all their capital stock. Both companies are consolidated by the global integration method.
- In November Telefónica acquired from SEPPA 23.78% of its shares in Telefónica Internacional de España, S.A. In December 1.25% of capital stock was sold to T.I. itself for treasury stock. The company continues to be consolidated by the global integration method.
- In January Telefónica participated in the incorporation of DTS Distribuidora de Televisión Digital, S.A., subscribing 35% of its capital stock. In May, the aforementioned company was sold to Telefónica Multimedia, S.A. In November DTS increased its capital and Telefónica Multimedia subscribed its corresponding share of capital stock. The company is carried by the equity method.
- In October, Telefónica acquired 3.5% of the capital stock of Portugal Telecom, S.A. The company is carried by the equity method.
- Telefónica left the Unisource consortium and on December 29, 1997, sold its 25% holding in Unisource N.V. to Telia AB, PTT y Telecom BV and Swisscom. In 1997 the Telefónica Group recorded Ptas. 4,696 million of losses of attributable to Unisource, which were recorded under the «Share in Losses of Companies Carried by the Equity Method» caption.
This purchase and sale transaction was carried out for a total of FI 465 million (Ptas. 34,921 million at the date of acquisition), giving rise to capital gains of Ptas. 20,556 million.
Previously, pursuant to the related company resolutions, Telefónica made a capital contribution of FI 193 million to Unisource.
- Telefónica acquired all the shares of Telefónica Transmisión de Datos, S.A. and Telefónica VSAT, S.A. for FI 455 million and FI 10 million, respectively.
The purchase of Telefónica Transmisión de Datos, S.A. gave rise to goodwill of Ptas. 25,794 million in consolidated accounts, Ptas. 15,860 million having been used in consolidated accounts to amortize goodwill in consolidation.
The remaining goodwill will be amortized over 10 years.
- In 1997 the Group acquired the following Argentinean companies, all with registered offices in Buenos Aires (Argentina):
 - Torneos y Competencias, S.A.: an Argentinean company whose main activity is the production of television programs relating to sports events, chiefly football, operating under various contracts granting it exclusive rights to this operation. In October 1997 T.I. acquired a 16.67% holding in this company for Ptas. 10,309 million. In January 1998 it acquired an additional 3.33%.
 - Cablevisión, S.A.: an Argentinean company which provides cable television services. In October 1997 T.I. acquired a 33.28% holding in this company for Ptas. 57,139 million.
 - Advance Telecomunicaciones, S.A.: an Argentinean company which provides on-line services and data transmission services. In September 1997 T.I. acquired a 50% holding in this company for Ptas. 757 million.
 - These three companies were included at cost in the consolidated financial statements.
- In March Telefónica Sistemas participated in the incorporation of Utilitel Comunicaciones, S.A. and acquired 50% of its capital stock. In November Telefónica purchased all the shares in the company owned by Telefónica Sistemas. Utilitel is carried by the equity method.
- Pabellón de Operadores Europeos de Telecomunicaciones, S.A., which is carried in the Telefónica Group's financial statements by the equity method, was dissolved and liquidated in December.
- In August Telefónica Multimedia, S.A. acquired 25% of the capital stock of Antena 3 de Televisión, S.A. The company is carried by the equity method.
- In July Telefónica Multimedia, S.A. acquired 49% of the capital stock of Gestora de Medios Audiovisuales de Fútbol, S.L. In December this holding was sold to Telefónica Medios de Comunicación, S.A. The company is carried by the equity method.
- Telefónica Multimedia, S.A. incorporated the wholly-owned company Producciones Multitemáticas, S.A., which is consolidated by the global integration method.
- In August Producciones Multitemáticas, S.A. acquired 20% of the capital stock of Lola Films, S.A. In December Lola Films, S.A. increased capital up to the current amount of Ptas. 1,050 million and Producciones Multitemáticas increased its holding in the company to 33.3%. The company is carried by the equity method.
- Telefónica Cable, S.A. sold to nongroup entities 34% of its holding in Telefónica Cable Madrid, S.A., its 31% holding in Telefónica Cable Navarra, S.A., 27% of the capital stock of Telefónica Cable Andalucía, S.A., and 24% of the capital stock of Telefónica

Cable Castilla y León, S.A. The latter company increased capital by Ptas. 900 million in November. All the aforementioned companies continue to be consolidated by the global integration method.

- In November Telefónica Publicidad e Información, S.A. participated in the incorporation of Doubleclick Iberoamérica, S.L., in which it has a 90% holding. The company is consolidated by the global integration method.
- In July Rem Infográfica, S.A., which was 60% owned by T.Pl. in 1996, carried out an «accordion» transaction (reduction and subsequent increase of capital stock) as a result of which capital stock decreased from Ptas. 50 million to Ptas. 10 million, with a paid-in surplus of Ptas. 280 million. T.Pl. acquired the remaining 40% of capital stock from minority shareholders.
- The Telefónica Internacional de España group sold its holding in Sintelar and Sintel-Peru, both of which provide installation services, mainly in the telecommunications industry. The companies, each of which is 25% owned by Telefónica Internacional, operate in Argentina and Peru, respectively. The sale gave rise to capital losses of Ptas. 42 million and Ptas. 25 million, respectively. Net losses on these sales were recorded under the «Losses on Sales of Holdings in Consolidated Companies» caption in the statement of income.
- Telefónica sold to Rom Telecom, S.A. its 60% holding in Telefónica Romanía, S.A., which provides cellular mobile telephony services in Romania, for US\$ 13.5 million. The Telefónica Group relieved from its accounts all the assets and liabilities contributed to this company to consolidation, giving rise to capital gains of Ptas. 197 million on this transaction, which was recorded under the «Gains on Sales of Holdings in Consolidated Companies» caption in the statement of income.
- From January 1, 1997, CRT, a company which was acquired in December 1996, became a member of the consolidated Group, having been carried at cost at 1996 year-end. The Group's ownership interest in the aforementioned company amounts to 10.3% of its total common and preferred shares of capital stock, through the various holdings owned by Group companies in the consortium which was awarded 35% of the company's common voting stock.
- In 1997 Compañía Celular de Colombia, S.A. and Multicanal, S.A. were excluded from consolidation. As a result of negotiations in 1997 for the sale of the holdings in these two companies, Compañía Celular de Colombia, S.A. was sold in January 1998; Multicanal, S.A. will be sold by May 1998 (the exercise date of put & call option contracts entered into in October 1997).
- In addition, the Group increased its holding in Cointel from 33.16% to 50%, involving a disbursement of US\$ 554.25 million. The Group also increased to 100% its holding in STARTEL, a CTC group company, for US\$ 425 million. Telefónica Internacional de España, S.A. sold its direct holding in TASA (1.0816%), obtaining capital gains of Ptas. 6,494 million.
- In January Telefónica Sistemas, S.A. acquired an additional 49% of the capital stock of Hispaservices, S.A., bringing its holding to 88%. The company, which was carried by the equity method in 1996, was consolidated by the global integration method in 1997.
- Telefónica Sistemas was also involved in the following transactions:
 - In January the company Buildnet, S.A. was incorporated with capital stock of Ptas. 150 million. Telefónica Sistemas participated in the incorporation of this company and acquired 33.5% of its capital stock. The company is carried by the equity method.
 - In April the company Agencia de Certificación Electrónica, S.A. was incorporated with capital stock of Ptas. 250 million. Telefónica Sistemas acquired a 40% holding in this company. The company is carried by the equity method.
 - In January the company Servicio Educación a Distancia (S.E.D.) was incorporated with capital stock of Ptas. 10 million. Telefónica Sistemas acquired a 40% holding in this company. The company is carried by the equity method.
 - Negocios Cibernéticos, S.A., a subsidiary 50% owned by Telefónica Sistemas, was dissolved and liquidated in 1997.
- Telefónica Soluciones Sectoriales, S.A. participated in the incorporation of the following companies:
 - Caser MVS, with capital stock of Ptas. 580 million, is 49% owned by T.S. Sectoriales.
 - Incatel, with capital stock of Ptas. 50 million, is 40% owned by T.S. Sectoriales.
 - QSL, with capital stock of Ptas. 60 million, is 33.33% owned by T.S. Sectoriales.

These three companies are carried by the equity method.

1996

- Telefónica acquired 25% of Unisource N.V. by exchanging all the shares of Telefónica Transmisión de Datos, S.A. and Telefónica V.S.A.T., S.A. Unisource N.V. is carried by the equity method (see Notes 8D.1 and 8D.2).
- On December 17, 1996, the consortium led by Telefónica Internacional de España, S.A. («Telefónica Internacional») submitted the successful bid in an international call for tender for the acquisition of 35% of the voting stock of Companhia Riograndense de Telecomunicações (CRT), equivalent to 13.45% of the latter's stock with dividend rights, for 681 million reales. The portion of the holding acquired and attributable to the Telefónica Group represents 7.87% of the company's total capital stock. The companies participating in the consortium with Telefónica Internacional are R.B.S. Participações, S.A., Compañía de Telecomunicaciones de Chile, S.A. Telefónica de Argentina, S.A. and Citicorp.
- The acquisition of the aforementioned shares was formally executed on December 30, 1996. The holding in this company was recorded at cost as of December 31, 1996, but it will be carried by the equity method in 1997.

- Telefónica sold its entire holding in Sistemas e Instalaciones de Telecomunicación, S.A. (SINTEL) and, accordingly, Sintelperú, S.A. and Sintelar, S.A. (each 25% owned by Telefónica Internacional and 38% and 50% owned, respectively, by Sintel, S.A.), are now carried by the equity method (see Note 8D.3).
- Telefónica continued to incorporate companies to operate the cable television system and to provide added value services at local level. The companies incorporated in 1996 were as follows:
 - Sociedad General de Cablevisión Sevilla, S.A.
 - Sociedad General de Cablevisión Balears, S.A.
 - Sociedad General de Cablevisión Cádiz, S.A.
 - Sociedad General de Cablevisión Navarra, S.A.
 - Sociedad General de Cablevisión Murcia, S.A.
 - Sociedad General de Cablevisión Lleida, S.A.
 - Sociedad General de Cablevisión Bizkaia, S.A.
 - Sociedad General de Cablevisión Rioja, S.A.
 - Sociedad General de Cablevisión Asturias, S.A.
 - Sociedad General de Cablevisión Burgos, S.A.
 - Sociedad General de Cablevisión León, S.A.
 - Sociedad General de Cablevisión Valladolid, S.A.
 - Sociedad General de Cablevisión Valencia, S.A.
 - Sociedad General de Cablevisión Alicante, S.A.
 - Sociedad General de Cablevisión Málaga, S.A.
 - Sociedad General de Cablevisión Granada, S.A.

all of which were consolidated by the global integration method.

- Telefónica Internacional acquired 25% of the Argentinean companies Multicanal, S.A. and PEM, S.A., both of which are carried by the equity method.
- T.S. Telefónica Sistemas, S.A. participated in the incorporation of Negocios Cibernéticos, S.A. by acquiring 50% of the capital stock of the new company, which was consolidated by the global integration method.
- It also participated in the incorporation of Madrid 112, in which it has a 49% ownership interest. This company is consolidated by the equity method.
- Telefónica Sistemas, S.A. acquired 50% of Gestión y Operación de Redes, S.A. (GESTIRED) from its subsidiary Telefónica Gestión de Sistemas, S.A. (T.G.S.). It subsequently acquired the remaining 49% of this company, bringing its total shareholding to 100%. GESTIRED continues to be consolidated by the global integration method.
- Telefónica Sistemas, S.A. also acquired 50% of the capital stock of Servicios y Contenidos por la Red, S.A., bringing its current ownership interest to 100%. This latter company continues to be consolidated by the global integration method.
- Maptel, S.A. and T.S.C. Telefónica Seguridad y Comunicaciones, S.A. changed their corporate names to Telefónica Sistemas de Información Geográfica, S.A. (T.S.I.G.) and Telefónica Sistemas de Ingeniería de Productos, Seguridad, S.A. (T.S.I.P.S.), respectively.
- Telefónica Sistemas, S.A. sold all its holding (55.64%) in T.P. Servicios Integrales de Protección Civil, S.A. (TEPESA) (see Note 8D.3).
- It also sold all its holding (24.99%) in Telecom Valles, S.A. (see Note 8D.3).
- Telefónica Publicidad e Información, S.A. (TPI) participated in the incorporation of REM Infográfica, S.A., acquiring 60% of the capital stock of the new company, which is consolidated by the global integration method.
- TPI also acquired 51% of the capital stock of T.M.P. Worldwide España, S.A., which is consolidated by the global integration method.
- On December 20, 1996, TPI dissolved and liquidated Promotora de Mercados Telemáticos, S.A. and Central de Compras de Papel, S.A., both of which were wholly-owned subsidiaries.
- Estrategias Telefónicas, S.A. (ESTRATEL) incorporated Tempotel, Empresa de Trabajo Temporal, S.A. and subscribed all its capital stock. This company is consolidated by the global integration method.
- Telefónica Multimedia, S.A. sold all its holdings in Cable del Guadalquivir, S.A. (20%) and Grupo Gallego de Empresas para el Cable, S.A. (10%) (see Note 8.3).
- Radiored I, S.A. acquired a 9% holding in the capital stock of Radiored Zaragoza, S.A., bringing its shareholding in this company to 100%. This company continues to be consolidated by the global integration method.

During the year Radiored I, S.A. incorporated the following companies: Radiored Extremadura, S.A., Radiored Canarias, S.A. and Radiored Baleares, S.A. These three companies, which were consolidated by the global integration method, all are wholly owned by Radiored, S.A.

- In November 1996 Telecartera, S.A. exchanged with Sogecable its 50% holding in Sociedad General de Cablevisión, S.A. for Sogecable's holdings in local operators (10% holdings, except for the local operators in the Canary Islands, Madrid and Barcelona). Telecartera also acquired from Cablevisión its holdings in local operators (39% holdings except in the case of the companies in Madrid and Barcelona -49%- and Burgos -24%) for Ptas. 635 million.

Servicios de Teledistribución, S.A. (ST-Hilo) sold its 33% holding in Sociedad Anónima de Productos Electrónicos y de Comunicación (S.A.P.E.C.) (see Note 8D.3).

- Hispasat, S.A. increased capital in 1996. Telefónica, however, did not subscribe all the shares corresponding to it, thereby reducing its holding in this company by 2.26% to 22.74%. This company continues to be consolidated by the equity method..

- Telefónica sold 30 shares of Telecartera, S.A., thereby reducing its holding in this company to 75%. This company continues to be consolidated by the global integration method (see Note 8D.3).

- It also sold 48,000 shares of Amper, S.A., reducing its holding to 15%. This company continues to be carried by the equity method (see Note 8D.3).

- Telefónica sold all its holdings in European Silicon Structures, S.A. (ES-2) (0.38%) and Financial Network Association (F.N.A.) (8.33%) (see Note 8D.3).

- STARTEL, S.A., a CTC Group company, was incorporated in 1996 as a result of agreements entered into on March 11, 1996, between CTC-Celular and VTR-Comunicaciones Móviles, S.A. to jointly operate in the cellular telephony business. CTC's and VTR's holdings of 55% and 45%, respectively, in the new company, were obtained through the contribution of 75% and 25% of STARTEL, S.A.'s assets, respectively, and through the subsequent sale of 20% of the company's capital stock for US\$ 67 million. As a result of this sale, the Telefónica Internacional Group recorded extraordinary income of Ptas. 2,444 million, net of taxes and the equity of minority interests, the gross amount of which (Ptas. 6,597 million) is recorded under the «Gains on Disposals of Holdings in Consolidated Companies» caption in the accompanying 1996 statement of income.

Throughout 1997, the Telefónica Group has continued to develop its extensive activity, both through actions aimed at the maintaining of its position of leadership in the Spanish telecommunications marketplace, bearing in mind the progressive liberalization of the sector, and the consolidation and strengthening of its international presence, moving into new business lines with high growth potential, especially the multimedia segment. All these actions reflect one prime objective: that of finding effective solutions to the communications needs of our customers.

The Telefónica Group has continued to strengthen the products and services offered by the Group, through the development of publicity campaigns focused on increasing the degree of penetration and usage, and through a higher degree of personal contact with our customers, thanks to our Telefónica Shops, where our customers can purchase, subscribe to and make inquiries about any of our products and services on the spot or dial our free-phone information service.

1997 has witnessed a series of agreements and alliances, not only nationally but also internationally, therefore allowing Telefónica to consolidate and expand its scope in the telecommunications marketplace.

In April, Telefónica signed a collaboration agreement with Telecom Portugal which included the exchange of share capital between the two companies. In line with this agreement, in October, Telefónica purchased a 3.5% stake in the Portuguese operator and this, in turn, acquired 1% of Telefónica's share capital. The agreement also states that the two companies will collaborate in different privatization processes in the Brazilian telecommunications market and in the region of the Magreb.

In this same month, Telefónica formed a strategic alliance with BT and MCI which included agreements on several transactions, such as the incorporation of Panamericana-MCI, the distribution of Concert services, and, the drawing up of agreements with Puerto Rico and the Spanish-speaking market in the US.

In June, Telefónica signed a commercial deal with Airtel Móvil S.A. (Airtel), in which Telefónica, as the majority operator, agreed to provide the circuits for Airtel's GSM service, as well as the international connection for this same network, and the extension of the interconnection contract between Airtel's GSM network and the Telefónica networks.

In August, Telefónica acquired a 25% stake in Antena 3 Televisión S.A., at the same time as it purchased 49% of Gestora de Medios Audiovisuales Fútbol S.L. (GMAF). The investors agreed that Telefónica would appoint the Board members for Antena 3 Televisión, as well as the Managing-Director and the management team. Telefónica would also appoint 60% of the Board of GMAF.

In September, Telefónica de España and the Recoletos-Pearson Group reached a collaboration agreement by which the Recoletos Group would acquire a stake in Antena 3, through the underwriting of a future 10% capital increase amounting to Ptas. 11,500 million. Telefónica, in turn, would acquire a 20% stake in Recoletos Compañía Editorial S.A., for the approximate amount of Ptas 23,000 million, through its wholly-owned subsidiary Telefónica Medios de Comunicación.

Since September 1997, Telefónica de España has been offering its digital television service via satellite, Vía Digital, through the consortium Distribuidora de Televisión por Satélite, in which Telefónica holds a 35% stake and is accompanied by other shareholders such as Radiotelevisión Española, Televisa, Canal 9, Televisión de Galicia, and the COPE chain. This service is provided through the Hispasat satellite.

Telefónica has also created a subsidiary in Morocco, in order to study the business opportunities that arise in the North African telecommunications market.

In November, Telefónica acquired the participation that was previously held by the Sociedad Estatal de Participaciones Patrimoniales, S.A., (SEPPa) in Telefónica Internacional de España, S.A. (TISA), for the amount of Ptas 127,000 million and representing 23.78% of the company's share capital.

In December, Telefónica withdrew from its participation in Unisource, following the agreement reached by the members of the alliance. As a consequence, Telefónica sold its whole participation in the alliance and purchased 100% of the shares of both Telefónica Transmisión de Datos and Telefónica VSAT.

Also in the month of December, Telefónica Internacional carried out the divestiture of its 60% participation in the mobile telephony operator Telefónica Romania for the amount of \$13.5 million. It had held this stake since 1992, having purchased it for \$4.8 million.

Within Telefónica Internacional's strategy of maintaining its position in the Argentinean cable TV market, the Group acquired

several participations in companies within this sector; one of these being Cablevisión S.A. for which it paid \$380 million for a 33.28% stake. Within this same strategy other participations have been or are in the process of being purchased through Cablevisión, namely the 100% participation in Mandeville (33.28% is an indirect participation) and 50% of VCC (16.64% also being an indirect participation). Regarding content, Telefónica Internacional purchased 16.67% of the company Torneos y Competencias S.A., a group responsible for the distribution of the television rights on Argentinean football.

ECONOMIC RESULTS

Throughout 1997 the Telefónica Group has registered extremely favourable results, reflecting growth in all its margins. As a consequence of this performance, the consolidated net result amounted to Ptas 190,063 million, rising 18.6% compared with the figure for 1996. The principal items that have contributed to this result have been:

Operating revenue: At year-end 1997, the figure for this item stood at Ptas 2,526,110 million, having grown 16.0% over that of 1996. This growth is principally derived from the increase in the minutes of usage registered by the basic telephony lines (due, among other things, to the introduction of new services), the growth in the number of mobile telephony customers and the rise in cable TV subscribers.

Operating expenses: This item totalled Ptas. 1,865,656 million, having risen 16.5% over the figure for the previous year. Within this item it is worth mentioning the favourable performance of personnel expenses which grew 2.9% to total Ptas. 570,895 million, mainly as a result of the streamlining of the workforce taking place in the parent. On the other hand, supplies (including stocks) and subcontracts amounted to Ptas. 595,586 million, having risen 35.5%.

Financial expenses: This item rose 7.6% to total Ptas. 200,185 million (excluding exchange losses). This increase is due to the higher degree of external financing in order to cover new investments.

Extraordinary expenses: The figure for this item grew 11.6% to reach Ptas. 163,387 million. This growth derives from the increase in the provisions made for the early and voluntary retirements underway in the parent, as these have not been offset by the lower need for the dismantling of plant pending depreciation, carried out in order to renovate and modernise our infrastructures.

Within the Telefónica Group, at December 1997, the parent managed a plant in service of 15,854,448 lines, 2.9% up on the figure for 1996; Telefónica Móviles was responsible for 3,187,696 cellular lines, reflecting a 35.9% increase; Telefónica Internacional managed 11,631,586 basic telephone lines, 13.8% more than in 1996,

1,865,708 cellular lines, reflecting 111.9% growth and had 1,551,860 cable TV subscribers, which is 35.0% higher than the number registered in 1996.

OPERATING REVENUE

At year-end 1997, the figure for this item amounted to Ptas 2,526,110 million, having risen by 16.0%. Within the components that make up operating revenue, revenue from sales contributed Ptas 2,363,102 million, growing 17.8% compared with 1996, internal expenditure capitalized in fixed assets totalled Ptas 117,932 million having fallen 7.4% compared with the previous year, as a consequence of the slowdown in the need for investment in the parent's infrastructures, combined with the considerable drop in the investment made by Telefónica Servicios Móviles (28.5% down on that of 1996); finally, other operating revenue amounted to Ptas 41,297 million, reflecting a 9.4% increase.

Regarding Telefónica, operating revenue stood at Ptas. 1,712,276 million, having grown by 8.3% and representing 67.8% of the total figure for the Telefónica Group. Within Telefónica's operating revenue, the main contributors were the basic telephony service which contributed Ptas. 1,007,844 million, the revenue derived from the Integrated Service Digital Network (ISDN), amounting to Ptas. 19,353 million and reflecting 225.9% growth, and other operating revenue such as the services provided to other operators, public telephony, data transmission and management fees.

With regard to the operating revenues registered by other companies within the Group, those of Telefónica Servicios Móviles and the Telefónica Internacional Group are worthy of particular mention, due to the substantial increase in the number of customers in the businesses in which they operate.

At December 1997, Telefónica Servicios Móviles had 3,187,696 customers, of which 1,100,595 belonged to the MovilLine (analog) service and 2,087,101 had opted for MoviStar (digital GSM), therefore reflecting a total market share of 73.5%, and 64.5% of the GSM market share, and registering operating revenue amounting to Ptas 362,992 million, this being 40.2% up on the figure for 1996.

The Telefónica Internacional Group, through its principal activity of providing basic and mobile telephony, along with cable TV, recorded a 33.6% rise in its operating revenue which totalled Ptas 443,131 million.

OPERATING EXPENSES

Throughout 1997, operating expenses rose 16.5% to reach Ptas 1,865,656 million. The principal component within this item was operating expenses which stood at Ptas 1,205,244 million, reflecting 17.1% growth. This component also includes stock, supplies, personnel expenses, subcontracts and taxes. The previously growth was

principally due to the increase in subcontracts and supplies, as the personnel expenses were constrained, having only grown by 2.9%. At year-end, the Group's workforce stood at 92,022 employees, 0.7% up on the previous year's figure.

Suppliers and subcontracts amounted to Ptas. 595,586 million at year-end, having grown 35.5%. This growth is derived from interconnection charges paid to other fixed and mobile operators, as well as the expenses incurred from advertising and promotion campaigns focused on those business lines that are open to competition.

Operating expenses for the parent rose 11.8% to reach Ptas 804,825 million, making up 66.8% of the total figure for the Group. Telefónica's personnel expenses amounted to Ptas 448,074 million, having grown 1.2%. The item supplies and subcontracts registered Ptas 325,578 million, reflecting 31.2% growth. Regarding Telefónica's workforce, the company continued downsizing through its policy of early and voluntary retirement, therefore placing the number of employees at year-end at 64,109, 4.6% down on 1996. This has contributed to lines per employee having risen to 266.8 compared with 243.4 at the end of 1996.

The Telefónica Internacional Group's figure for personnel expenses stood at Ptas 78,654 million, growing 10.3%. At year-end, the company had 15,523 employees, 6.6% fewer than in 1996.

The Telefónica Móviles Group contributed Ptas 11,673 million to the Group's figure for personnel expenses. Telefónica Servicios Móviles' workforce totalled 2,363 at the end of 1997, 30.0% up on the figure for year-end 1996, due to the need to address the high expansion rate of the mobile telephony business. The net variation in employees reflected by the rest of the companies was favourable.

At year-end, depreciation stood at Ptas 602,657 million, having grown 14.5% when compared with 1996, principally due to Telefónica's 1996 asset revaluation, combined with the high investment rate reflected by Telefónica Servicios Móviles and the Latin American subsidiaries.

OPERATING PROFIT

The revenue and expenses derived from operations previously mentioned, permitted a net income amounting to Ptas 660,454 million, reflecting 14.7% growth compared with 1996.

PROFIT FROM ORDINARY ACTIVITIES

The figure for profit from ordinary activities amounted to Ptas 449,367 million in 1997, reflecting a 15.1% increase. Of this amount Ptas 284,648 million correspond to Telefónica, representing 63.3% of the total figure for the Group's ordinary activities.

This result is principally derived from the increase in financial revenue and the profit registered by associated companies which

was offset by the growth in financial expenses and the amortization of goodwill.

Financial revenue amounted to Ptas 25,373 million having risen 32.5%, with exchange gains totalling Ptas 8,145 million.

Financial expenses recorded 7.6% growth to stand at Ptas 200,185 million, including interest payments on debts, the amortization of debenture issue expenditure and financial provisions. Exchange losses amounted to Ptas 21,066 million, 3% higher than in 1996.

Within the total amount registered for financial expenses, interest payments on debts stood at Ptas 189,967 million, 4.5% higher than in 1996, due to the external financing used in the financial investment programme, although the average cost of the financial debt has gone down when compared with 1996. Provisions to the amount of Ptas 6,464 million were also made for the provisions for financial investments. Of the total amount for interest payments on debts, Ptas 136,491 million corresponded to the parent, reflecting a 8.6% decrease.

The higher degree of amortization of goodwill was a result of the acquisitions made at the end of 1996 and throughout 1997. This amortization amounted to Ptas 33,312 million, 98.5% higher than in 1996.

Lastly, the companies than consolidate using the equity method, contributed Ptas 9,958 million to the Group's figure, reflecting a 27.5% increase.

PRE-TAX INCOME

Pre-tax income rose 22.4% to total Ptas. 337,641 million. This result derived from the Ptas 51,661 million registered by extraordinary income, reflecting 61.7% growth, and the extraordinary expenses that rose 11.6% to total Ptas 163,387 million.

The figure for extraordinary income corresponds principally to the proceeds from the sale of participations in consolidated companies (164.8% growth amounting to Ptas 27,371 million) and the crediting of the capital grants in the profit and loss accounts (Ptas 11,285 million, rising 9.4%).

In Telefónica, the capital grants amounted to Ptas 11,270 million, representing 99.9% of the total figure received by the Group, and growing by 9.3% compared with the previous year. Of the other Group companies the one that was particularly outstanding was Telefónica Internacional whose extraordinary income reached Ptas 9,818 million, of which Ptas 6,494 million derived from the sale, through Cointel, of its non-controlling participation in Telefónica de Argentina.

The figure for the Telefónica Group's extraordinary expenses stood at Ptas 163,387 million, having grown 11.6% compared with 1996. Of this figure Telefónica contributed Ptas 38,100 million derived

from non-depreciated dismantled plant, and Ptas 90,166 million in provisions for the voluntary and early retirements. This figure is 54.0% higher than that registered for 1996.

NET INCOME

Consolidated net income for the year amounted to Ptas 264,105 million, a 20.6% increase over the figure for 1996, after having subtracted the national and international taxes which totalled Ptas 73,536 million, compared with Ptas 56,921 million in 1996. These taxes reflected an effective rate of 21.8%, 1.2 pp higher than the previous year.

The contribution of minority interests to the results grew 26.2% to Ptas 74,042 million. In 1998, this figure will reflect a substantial decrease due to Telefónica's purchase of the Telefónica Internacional share capital previously in the hands of the Spanish authorities.

Finally, the net income derived from the parent rose 18.6% to reach Ptas 190,063, as a consequence of the success of the business activities in which the Group participates, especially in regard to basic and mobile telephony, and our international businesses.

INVESTMENT ACTIVITY

Throughout 1997, the Telefónica Group invested Ptas 1,231,326 million, 42.0% more than in 1996.

The investment in tangible assets went down 6.5% to Ptas 634,845 million, while the investment in intangible assets grew 12.5%

to total Ptas 51,043 million. Finally, Ptas 545,438 million were channelled into financial investment which is 281.6% up on the figure for 1996.

Breaking the overall figure down into companies, Telefónica's investment amounted to Ptas 709,092 million, that of Telefónica Internacional stood at Ptas 327,754 and Telefónica Servicios Móviles invested Ptas 100,878 million.

The investment made by the Group in R&D was focused on enabling the Group's companies to offer an ever-increasing range of products and services, at the same time as further enhancing our customer-care service. The bulk of our investment was channelled into priority areas such as multimedia services, public telephony and mobile services. Work has continued on our MORE system which focuses on the modernizing of our analog exchanges, the new tools needed for network planning and the new versions of the Operating and Monitoring Structure (EOC).

TREASURY STOCK

Throughout 1997, 610,000 treasury stocks were acquired with a nominal value of Ptas 500 each with an average purchase price of Ptas 3,689. Subsequently, 510,000 of the previous shares were sold for an average of Ptas 4,314. These operations resulted in capital gains amounting to Ptas 319,000,000.

At the close of 1997, Telefónica held 100,000 shares with a purchase price of Ptas 368,900,000.

Financial Exhibits

SELECTED FINANCIAL DATA. CONSOLIDATED (Million pesetas)

	1993	1994	1995	1996	1997	1997 \$ (3)
Revenue from operations	1,297,437	1,578,850	1,740,557	2,006,058	2,363,102	15,577.3
Operating expenses	656,655	806,400	849,258	1,023,065	1,201,465	7,919.9
Financial expenses	242,342	236,101	223,656	206,425	221,251	1,458.5
Depreciation and amortization (1)	413,261	515,116	567,992	594,536	677,823	4,468.1
Net income	96,367	112,608	133,214	160,282	190,063	1,252.9
Cash flow	502,882	644,750	750,357	811,235	961,435	6,337.7
Share capital	469,735	469,735	469,735	469,735	469,735	3,096.4
Shareholders' equity	1,437,055	1,512,031	1,546,472	1,863,760	1,991,374	13,126.9
Long-term debt	1,626,699	1,847,768	1,736,521	1,672,907	1,916,627	12,634.2
Financial debt	1,804,854	1,941,013	1,861,728	1,947,450	2,317,201	15,274.7
Investment (2)	380,634	489,606	632,893	724,253	685,888	4,521.3

(1) Including depreciation of fixed assets, amortization of deferred interest expenses, amortization of goodwill and dismantled plant pending depreciation.

(2) Fixed and intangible.

(3) Figures in million dollars. 30-12-97 exchange rate: \$1 = ptas 151.702

TELEFONICA GROUP: OPERATING REVENUE (Million pesetas)

	1994	1995	1996	1997	Over 96 (%)	Increase Average accumulated 93-97 (%)	1997 \$ (1)
Parent company							
Basic telephony	988,649	1,042,985	1,223,496	1,340,924	9.6	8.8	8,839.2
Telephone service	802,545	843,748	947,748	1,007,844	6.3	7.0	6,643.6
Leased circuits	34,103	29,809	73,317	98,133	33.8	24.6	646.9
Ibercom	54,769	58,517	69,290	73,516	6.1	11.0	484.6
Digital exchanges, intelligent network, ISDN and other	6,728	19,493	49,898	75,925	52.2	115.5	500.5
Equipment	75,154	75,983	71,696	73,456	2.5	(2.1)	484.2
Advertising	15,350	15,435	11,547	12,050	4.4	(5.1)	79.4
International communication services	139,349	145,222	136,124	134,659	(1.1)	2.0	887.7
Telephone service	128,228	134,145	123,120	120,653	(2.0)	(0.1)	795.3
Leased circuits	5,693	7,367	9,833	11,588	17.8	20.4	76.4
Retransmissions	5,428	3,710	3,171	2,418	(23.7)	(18.5)	16.0
Public telephony	62,941	65,452	64,655	68,193	5.5	6.8	449.5
Data transmission	43,735	38,642	44,645	54,513	22.1	4.6	359.3
Mobile services	46,471	76,494	0	0	n.m.	n.m.	0
Other	2,391	3,879	4,125	6,812	65.1	n.m.	44.9
Total revenue from operations for Telefónica	1,283,536	1,372,674	1,473,045	1,605,101	9.0	7.1	10,580.6
Group							
Telefónica Internacional Group	221,451	281,050	331,598	443,131	33.6	121.7	2,921.1
Telefónica Servicios Móviles Group	9,642	38,657	259,118	363,255	40.2	173.5	2,394.5
Cabitel	21,373	33,187	40,482	43,788	8.2	28.1	288.6
Telefónica Publicidad e Información Group	28,564	30,395	35,437	47,476	34.0	14.7	313.0
Other subsidiaries	126,867	145,716	173,701	198,210	14.1	15.6	1,306.6
Sales among group companies	(112,583)	(161,122)	(307,323)	(337,859)	9.9	34.9	(2,227.1)
Total revenue from operations for Group Companies	295,314	367,883	533,013	758,001	42.2	76.9	4,996.7
Total revenue from operations for Telefónica Group	1,578,850	1,740,557	2,006,058	2,363,102	17.8	16.2	15,577.3

(1) Figures in million dollars. 30-12-97 exchange rate: \$1 = ptas. 151.702

RESULTS - PROFIT MARGINS. CONSOLIDATED (Million pesetas)

DESCRIPTION	1993	1994	1995	1996	1997	Increase (%)		1997 \$ (1)
						Over 96	Average accumulated 93-97	
+ Operating revenue	1,297,437	1,578,850	1,740,557	2,006,058	2,363,102	17.8	11.5	15,577.3
- Operating expenses	656,655	806,400	849,258	1,023,605	1,201,465	17.4	16.3	7,919.9
Personnel expenses	448,402	520,918	543,547	554,682	570,895	2.9	6.2	3,763.3
Taxes	23,981	25,826	27,667	35,106	38,763	10.4	12.8	255.5
Subcontracts	184,272	259,656	278,044	433,277	591,807	36.6	33.9	3,901.1
+ Internal expenditure capitalized in fixed assets	109,103	121,391	121,548	127,319	117,932	(7.4)	2.0	777.4
= Operating margin	749,885	893,841	1,012,847	1,110,312	1,279,569	15.2	14.3	8,434.8
+ Other operating revenue	33,068	30,226	33,402	37,758	41,297	9.4	5.7	272.2
- Depreciation of fixed assets	374,259	454,530	501,480	526,229	602,657	14.5	12.6	3,972.7
- Other operating expenses	13,152	9,854	9,728	19,307	21,998	13.9	13.7	145.0
- Other provisions and charges	25,816	27,286	25,159	26,569	35,757	34.6	8.5	235.7
= Operating profit	369,726	432,397	509,882	575,965	660,454	14.7	15.6	4,353.6
+ Financial income	7,837	17,358	18,802	19,156	25,373	32.5	34.1	167.3
+ Exchange income	2,695	4,780	12,685	10,678	8,145	(23.7)	31.9	53.7
- Interest expenses	208,757	205,978	201,151	182,370	196,431	7.7	(1.5)	1,294.8
- Exchange losses	28,631	24,642	19,188	20,452	21,066	3.0	(7.4)	138.9
- Amortization of deferred charges	4,954	5,481	3,317	3,603	3,754	4.2	(6.7)	24.7
+ Revenue from associated companies	20,176	18,513	8,754	7,811	9,958	27.5	(16.2)	65.6
- Amortization of goodwill	4,798	6,191	6,985	16,786	33,312	98.5	62.3	219.6
= Profit from ordinary activities	153,294	230,756	319,482	390,399	449,367	15.1	30.8	2,962.2
+ Extraordinary income	14,904	40,206	29,874	31,941	51,661	61.7	36.4	340.5
- Extraordinary expenses	41,405	99,311	125,645	146,459	163,387	11.6	40.9	1,077.0
= Income before tax	126,793	171,651	223,711	275,881	337,641	22.4	27.7	2,225.7
- Corporate tax	24,845	30,589	39,358	56,921	73,536	29.2	31.2	484.7
= Net income	101,948	141,062	184,353	218,960	264,105	20.6	26.9	1,741.0
- Minority interest	5,581	28,454	51,139	58,678	74,042	26.2	90.8	488.1
= Net income attributed to Telefónica	96,367	112,608	133,214	160,282	190,063	18.6	18.5	1,252.9
Net income	101,948	141,062	184,353	218,960	264,105	20.6	26.9	1,741.0
+ Amortization of deferred charges	4,954	5,481	3,317	3,603	3,754	4.2	(6.7)	24.7
+ Depreciation of fixed assets	374,259	454,530	501,480	526,229	602,657	14.5	12.6	3,972.7
+ Dismantled plant pending depreciation	29,250	48,914	56,210	47,918	38,100	(20.5)	6.8	251.1
+ Amortization of goodwill	4,798	6,191	6,985	16,786	33,312	98.5	62.3	219.6
- Revenue from associated companies	20,176	18,513	8,754	7,811	9,958	27.5	(16.2)	65.6
+ Dividends of associated companies	7,849	7,085	6,766	5,550	29,465	430.9	39.2	194.2
= Cash flow	502,882	644,750	750,357	811,235	961,435	18.5	17.6	6,337.7

(1) Figures in million dollars. 30-12-97 exchange rate: \$ 1 =ptas. 151.702

BALANCE SHEET. CONSOLIDATED (Million pesetas)

ITEMS	1993	1994	1995	1996	1997	1997 \$ (2)
Subscribed shares not paid-in	0	23	174	0	446	2.9
Fixed assets	3,450,964	4,023,780	4,114,692	4,655,150	4,987,098	32,874.3
Capital increase expenses	226	349	714	577	2,337	15.4
Net intangible assets	63,207	300,207	317,239	337,825	356,109	2,347.4
Property, plant and equipment	5,483,037	6,311,527	6,538,506	7,024,676	7,606,204	50,139.1
Depreciation of fixed assets	(2,310,927)	(2,751,943)	(2,941,080)	(3,050,806)	(3,458,091)	22,795.3
Net fixed assets	3,172,110	3,559,584	3,597,426	3,973,870	4,148,113	27,343.8
Investments	215,421	163,640	199,313	342,878	480,539	3,167.7
Goodwill on consolidation	48,236	53,741	47,687	49,798	284,364	1,874.5
Deferred expenses	225,589	186,473	141,310	130,294	135,103	890.6
Current assets	377,094	495,203	514,395	602,495	817,750	5,390.5
Subscribed shares not paid-in	22	0	4	0	0	0
Inventories	16,505	25,362	29,036	33,834	37,691	248.4
Accounts receivable	332,841	369,798	398,837	507,775	629,230	4,147.8
Short-term financial investments	11,804	73,066	68,247	35,843	126,093	831.2
Treasury stock	0	0	0	0	369	2.4
Cash	7,996	17,941	11,933	12,647	10,432	68.8
Prepayments	7,926	9,036	6,338	12,396	13,935	91.9
Assets=liabilities and shareholders' equity	4,101,883	4,759,220	4,818,258	5,437,737	6,224,761	41,032.8
Shareholders' equity	1,437,055	1,512,031	1,546,472	1,863,760	1,991,374	13,126.9
Paid-in share capital	469,735	469,735	469,735	469,735	469,735	3,096.5
Reserves	894,140	929,688	971,707	1,266,624	1,369,155	9,025.2
Net income for year	96,367	112,608	133,214	160,282	190,063	1,252.9
Interim dividend	(23,187)	0	(28,184)	(32,881)	(37,579)	(247.7)
Minority interests	41,798	292,293	313,753	374,693	394,097	2,597.8
Deferred income	55,326	75,029	91,258	102,218	112,471	741.4
Provisions for liabilities and charges	231,775	270,876	287,996	336,615	388,896	2,563.5
Long-term debt	1,626,699	1,847,768	1,736,521	1,672,907	1,916,627	12,634.2
Debentures, bonds and promissory notes issued	708,440	721,323	643,938	654,378	714,923	4,712.7
Debt with credit institutions	681,881	917,607	901,885	843,349	942,728	6,214.3
Debt with associated companies	0	217	0	271	0	0
Other creditors (1)	236,378	208,621	190,698	174,909	258,976	1,707.2
Short-term debt	709,230	761,223	842,258	1,087,544	1,421,296	9,369.0
Debentures, bonds and promissory notes issued	167,271	126,360	108,154	147,427	284,018	1,872.2
Debt with credit institutions	87,815	132,339	168,246	244,617	336,525	2,218.3
Debt with associated companies	19,358	11,286	19,392	28,458	15,080	99.4
Other trade accounts	211,046	266,927	257,112	374,580	351,357	2,316.1
Other creditors	205,592	191,378	260,771	266,326	382,872	2,523.9
Prepayments	18,148	32,933	28,583	26,136	51,444	339.1

- (1) Including tax debts amounting to 57,131, 74,447, 71,013, 69,011 and 83,444 million pesetas respectively, not considered for the calculation of the financial debt ratio.
(2) Figures in million dollars. 30-12-97 exchange rate: \$ 1 = ptas. 151.702

ECONOMIC / FINANCIAL INDICATORS. CONSOLIDATED (Figures in %, unless otherwise indicated)

	1993	1994	1995	1996	1997
Operating margin/Revenue from operations (1)	57.8	56.6	58.2	55.3	54.1
Financial expenses/Revenue from operations (2)	18.7	15.0	12.8	10.3	9.4
Operating margin/Average net plant (3)	23.5	26.6	28.3	29.3	31.5
Fixed asset coverage (4)	91.1	93.8	92.4	90.0	88.8
Self-financing ratio (5)	115.4	115.9	104.1	96.4	121.4
Financial debt ratio (6)	53.1	49.8	47.9	44.7	47.3
Debt repayment capacity (years) (7)	4.6	3.7	3.0	2.8	2.7
Financial expenses coverage (times) (8)	1.1	1.2	1.5	1.7	2.0

(1) Operating revenue - Operating expenses + Internal expenditure capitalized in fixed assets / Operating revenue.

(2) Financial expenses + Exchange losses + Amortization of deferred charges / Operating revenue.

(3) Operating margin / Average net fixed assets.

(4) Shareholders' equity + Outside shareholders' interests + Deferred income + Provisions + Long-term debt / Fixed assets + Goodwill on consolidation + Deferred expenses.

(5) Net income - Telefónica Dividends + Minority Interests Dividends + Depreciation of plant and equipment + Intangible depreciation + Dismantled plant pending depreciation + Amortization of goodwill - Revenue from associated companies + Dividend from associated companies / Capital expenditure in fixed assets + Capital expenditure in intangible assets.

(6) Interest bearing debt / Shareholders' equity + Outside shareholders' interests + Deferred income + Tax debts + Interest bearing debt.

(7) Interest bearing debt: Long-term debt - Tax debts + Short-term debentures notes and promissory notes issue + Short-term debts with credit institutions - Short-term financial investments - Cash.

(8) Interest bearing debt / Cash flow - Internal expenditure capitalized in fixed assets. Cash-flow: Net income + Amortization of deferred expenses + Depreciation of fixed assets + Dismantled plant pending depreciation + Amortization of goodwill - Revenue from associated companies + Dividends from associated companies.

(9) Income before tax + Financial expenses + Exchange losses + Amortization of deferred charges - Internal expenditure capitalized in fixed assets / Financial expenses + Exchange losses + Amortization of deferred charges.

TELEFÓNICA IN THE SPANISH ECONOMY (Telefónica as a % of national total) (Revised series)

	1993	1994	1995	1996	1997
Gross value added	2.03	2.01	1.97	1.93	1.90
Gross operating profit	2.71	2.48	2.38	2.35	2.34
Gross savings	3.83	4.32	3.59	3.86	3.55
Gross capital formation	3.16	3.19	3.03	2.69	2.47

Prices (1)

• GDP deflator	4.3	4.0	4.9	3.3	2.0
• Consumer prices (annual average)	4.6	4.8	4.6	3.6	2.0
• Telefónica (2)	3.8	0.0	(1.4)	(1.4)	(3.6)

(1) Growth rates.

(2) Price index variation of basic telephony tariffs.
Sources: I.N.E and Telefónica

GROSS VALUE ADDED (Real growth rates in %)

	1993	1994	1995	1996	1997
National economy	(0.9)	2.2	2.9	2.1	3.6
Services sector	0.7	2.8	2.9	2.3	3.1
Telefónica	2.9	4.9	7.5	4.9	7.9

Sources: I.N.E and Telefónica.

SELECTED FINANCIAL DATA. TELEFONICA DE ESPAÑA (Million pesetas)

	1993	1994	1995	1996	1997	1997 \$ (3)
Revenue from operations	1,220,084	1,283,536	1,372,674	1,473,045	1,605,101	10,580.6
Operating expenses	547,156	568,199	609,867	719,862	804,825	5,305.3
Financial expenses	235,319	212,639	191,397	165,263	157,241	1,036.5
Depreciation and amortization (1)	406,603	467,274	505,644	474,403	506,680	3,340.0
Net income	84,837	91,734	106,183	120,414	133,774	881.8
Cash flow	491,440	559,008	611,827	594,817	640,454	4,221.8
Share capital	469,735	469,735	469,735	469,735	469,735	3,096.4
Shareholders' equity	1,397,712	1,454,684	1,470,679	1,734,072	1,779,535	11,730.5
Long-term debt	1,582,154	1,502,999	1,363,117	1,234,455	1,154,129	7,607.9
Financial debt	1,749,383	1,655,877	1,537,994	1,395,689	1,414,462	9,324.0
Investment (2)	381,507	406,882	436,720	395,198	388,599	2,561.6

(1) Including depreciation of fixed assets, amortization of deferred interest expenses and dismantled plant pending depreciation

(2) Fixed and intangible

(3) Figures in million dollars. 30-12-97 exchange rate: \$1 = ptas 151.702

RESULTS - PROFIT MARGINS. TELEFÓNICA DE ESPAÑA (Million pesetas)

DESCRIPTION	1993	1994	1995	1996	1997	Increase (%)		1997 \$ (1)
						Over year 96	Average	
							accumulated 93-97	
+ Operating revenue	1,220,084	1,283,536	1,372,674	1,473,045	1,605,101	9.0	7.1	10,580.6
- Operating expenses	547,156	568,199	609,867	719,862	804,825	11.8	10.1	5,305.3
Personnel expenses	408,103	421,624	433,655	442,562	448,074	1.2	2.4	2,953.6
Taxes	23,871	25,569	27,055	29,183	31,173	6.8	6.9	205.5
Supplies and subcontracts	115,182	121,006	149,157	248,117	325,578	31.2	29.7	2,146.2
+ Internal expenditure capitalized in fixed assets	75,742	73,766	72,154	69,926	65,218	(6.7)	(3.7)	429.9
= Operating margin	748,670	789,103	840,222	823,109	865,494	5.1	3.7	5,705.2
+ Other operating revenue	23,632	24,992	29,610	37,620	41,957	11.5	15.4	276.6
- Depreciation of fixed assets	372,401	413,134	446,480	423,736	466,461	10.1	5.8	3,074.9
- Other operating expenses	10,507	11,450	7,289	20,551	21,318	3.7	19.3	140.5
- Other provisions and charges	24,115	22,573	20,383	10,699	12,542	17.2	(15.1)	82.7
= Operating profit	365,279	366,938	390,419	405,743	407,130	0.3	2.7	2,683.7
+ Financial income	10,191	14,388	15,693	27,190	32,969	21.3	34.1	217.3
+ Exchange income	0	0	5,381	4,434	1,790	(59.6)	n.m.	11.8
- Interest expenses	203,124	182,880	171,540	149,295	136,491	(8.6)	(9.5)	899.7
- Exchange losses	27,243	24,533	16,903	13,219	18,631	(1.2)	(9.1)	122.8
- Amortization of deferred charges	4,952	5,226	2,954	2,749	2,119	(22.9)	(19.1)	13.9
= Profit from ordinary activities	140,151	168,687	220,096	272,104	284,648	4.6	19.4	1,876.4
+ Extraordinary income	8,392	29,673	16,262	16,007	38,286	139.2	46.1	252.4
- Extraordinary expenses	41,075	88,756	115,229	148,232	168,189	13.5	42.3	1,108.7
= Income before tax	107,468	109,604	121,129	139,879	154,745	10.6	9.5	1,020.1
- Corporate tax	22,631	17,870	14,946	19,465	20,971	7.7	(1.9)	138.3
= Net income	84,837	91,734	106,183	120,414	133,774	11.1	12.1	881.8
+ Amortization of deferred charges	4,952	5,226	2,954	2,749	2,119	(22.9)	(19.1)	13.9
+ Depreciation of fixed assets	372,401	413,134	446,480	423,736	466,461	10.1	5.8	3,074.9
+ Dismantled plant pending depreciation	29,250	48,914	56,210	47,918	38,100	(20.5)	6.8	251.2
= Cash flow	491,440	559,008	611,827	594,817	640,454	7.7	6.8	4,221.8

(1) Figures in million dollars. 30-12-97 exchange rate: \$1=ptas. 151.702

BALANCE SHEET. TELEFONICA DE ESPAÑA (Million pesetas)

ITEMS	1993	1994	1995	1996	1997	1997 \$ (1)
Fixed assets	3,357,004	3,412,891	3,362,772	3,545,499	3,630,398	23,931.1
Capital increase expenses	162	157	117	76	35	0.2
Net intangible assets	55,520	70,831	89,426	110,822	130,440	859.9
Property, plant and equipment	5,489,734	5,592,518	5,491,583	5,588,247	5,636,818	37,157.2
Depreciation of fixed assets	(2,308,229)	(2,483,296)	(2,600,010)	(2,595,993)	(2,781,678)	18,336.5
Net fixed assets	3,181,505	3,109,222	2,891,573	2,992,254	2,855,140	18,820.7
Investments	119,817	232,681	381,656	442,347	644,783	4,250.3
Deferred expenses	224,113	181,307	135,572	122,554	120,685	795.5
Current assets	328,977	302,822	336,301	397,612	485,333	3,199.3
Inventories	3,832	4,292	4,303	4,634	4,708	31.0
Accounts receivable	317,323	288,428	313,562	371,257	420,804	2,773.9
Short-term investments	1,201	3,358	11,019	14,615	53,169	350.5
Treasury stock	0	0	0	0	369	2.4
Cash and banks	5,031	4,699	5,375	5,240	4,198	27.7
Prepayments	1,590	2,045	2,042	1,866	2,085	13.8
Assets= liabilities and shareholders' equity	3,910,094	3,897,020	3,834,645	4,065,665	4,236,416	27,925.9
Shareholders' equity	1,397,712	1,454,684	1,470,679	1,734,072	1,779,535	11,730.5
Paid-in share capital	469,735	469,735	469,735	469,735	469,735	3,096.5
Reserves	866,327	893,215	922,945	1,176,804	1,213,605	7,999.9
Net income for year	84,837	91,734	106,183	120,414	133,774	881.8
Interim dividend	(23,187)	0	(28,184)	(32,881)	(37,579)	(247.7)
Deferred income	54,765	67,531	78,933	95,160	104,073	686.0
Provisions for liabilities and charges	216,094	232,412	240,995	272,141	253,214	1,669.1
Long-term debt	1,582,154	1,502,999	1,363,117	1,234,455	1,154,129	7,607.9
Debentures, bonds and promissory notes issued	685,614	636,533	571,271	563,464	530,196	3,495.0
Debt with credit institutions	540,494	558,700	496,269	419,505	339,830	2,240.1
Debt with group and associated companies	122,403	140,447	149,319	126,615	177,271	1,168.6
Other creditors (1)	233,643	177,319	146,258	124,871	106,832	704.2
Short-term debt	659,369	639,394	680,921	729,837	945,465	6,232.4
Debentures, bonds and promissory notes issued	167,267	125,094	104,670	117,000	262,594	1,731.0
Debt with credit institutions	59,197	82,526	118,826	60,845	58,659	386.7
Debt with group and associated companies (2)	41,459	37,968	92,150	133,281	135,637	894.1
Other trading debts	179,470	209,933	119,439	173,520	149,914	988.2
Other creditors	195,149	158,512	220,504	222,278	314,128	2,070.7
Prepayments	16,827	25,361	25,332	22,913	24,533	161.7

(1) Including tax debts amounting to 53,003, 52,273, 44,145, 38,352 and 37,535 million pesetas respectively, not considered for the calculation of the financial debt ratio.

(2) Including loan debts amounting to 5,588, 11,920, 41,596 and 33,982 million pesetas respectively for the period 1994-1997, considered for the calculation of the financial debt ratio.

(3) Figures in million dollars. 30-12-97 exchange rate: \$ 1 = ptas. 151.702

ECONOMIC/FINANCIAL INDICATORS. TELEFÓNICA DE ESPAÑA (Figures in % unless otherwise indicated)

	1993	1994	1995	1996	1997
Operating margin/Revenue from operations (1)	61.4	61.5	60.8	55.9	53.9
Financial expenses/Revenue from operations (2)	19.3	16.6	13.9	11.2	9.8
Operating margin/Average net plant (3)	23.4	25.1	27.8	28.0	29.6
Fixed assets coverage (4)	90.8	90.6	90.1	90.9	87.7
Self-financing ratio (5)	112.2	120.9	123.1	128.6	139.6
Financial debt ratio (6)	53.7	51.3	49.1	42.8	42.4
Debt repayment capacity (years) (7)	4.2	3.4	2.8	2.7	2.5
Financial expenses coverage (times) (8)	1.1	1.2	1.3	1.4	1.6

(1) Operating revenue - Operating expenses + Internal expenditure capitalized in fixed assets / Operating revenue.

(2) Financial expenses + Exchange losses + Amortization of deferred charges / Operating revenue.

(3) Operating margin / Average net fixed assets.

(4) Shareholders' equity + Deferred income + Provisions + Long-term debt / Fixed assets + Deferred expenses.

(5) Net income - Telefónica Dividends + Depreciation of plant and equipment + Intangible depreciation + Dismantled plant pending depreciation / Capital expenditure in fixed assets + Capital expenditure in intangible assets.

(6) Interest bearing debt / Shareholders' equity + Deferred income + Tax debts + Interest bearing debt. Interest bearing debt: Long-term debt - Tax debts + Short-term debentures, bonds and promissory notes issued + Short-term debts with credit institutions + Short-term group and associated companies loans - Short-term financial investments - Cash.

(7) Interest bearing debt / Cash-flow - Internal expenditure capitalized in fixed assets. Cash-flow: Net income + Amortization of deferred expenses + Depreciation of fixed assets + Dismantled plant pending depreciation.

(8) Income before tax + Financial expenses + Exchange losses + Amortization of deferred charges - Internal expenditure capitalized in fixed assets / Financial expenses + Exchange losses + Amortization of deferred charges.

*Shareholder
Information*

SHARE CAPITAL

	1993	1994	1995	1996	1997
Share Capital (Mill. ptas.)	469,735.41	469,735.41	469,735.41	469,735.41	469,735.41
Earnings per share (ptas.)	90.8	97.6	113.0	128.2	142.4
Price / earnings ratio	20.5	15.9	14.9	23.5	30.5
Payout (%)	68.3	67.6	67.2	69.4	71.6
Price / Cash flow per share	3.6	2.6	2.6	4.8	6.4

At December 31, 1997 Telefónica's share capital totalled 469,735,410,000 pesetas, divided into 939,470,820 shares with a nominal value of 500 pesetas each fully paid in.

Since 1990 the following capital increases have been made, all of which through the conversion of bonds.

	Number of shares issued (thousands)	Issue Price (Ptas.)	Amount issued Nominal (Million Ptas.)	Effective (Million Ptas.)
1990	1,994.6	858.435	997.3	1,712.3
1992	1.1	924.750	0.5	1.0
1993	12,511.7	1,267.230(*)	6,255.8	15,855.2

(*) Average issue price

QUOTATION OF SHARES

Telefónica shares are quoted on the continuous markets of all Spanish Stock exchanges (Madrid, Barcelona, Bilbao and Valencia) and on the following foreign exchanges: London, París, Frankfurt, Tokyo, New York (*) and the London Stock Exchange's SEAQ International.

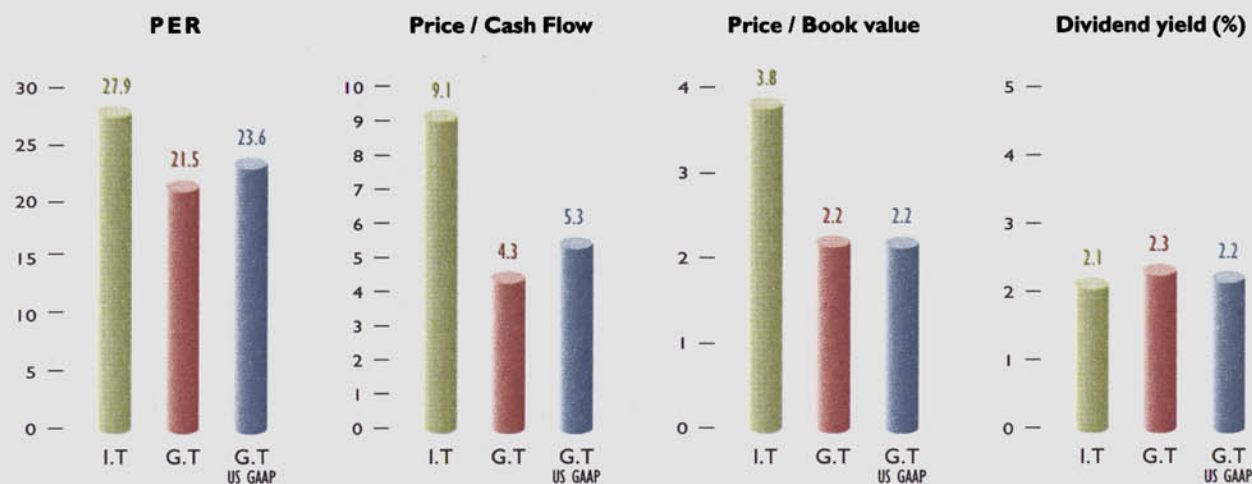
Option contracts on Telefónica shares are carried out on the Spanish Financial Futures Market (MEFF-RV) and on the American Stock Exchange (AMEX) (*)

(*) Quotes American Depositary Receipts (ADR) | ADR = 3 shares

QUOTATION OF TELEFÓNICA SHARES

The table below reflects maximum, minimum and closing prices, in pesetas on the continuous Spanish market.

	MAXIMUM	MINIMUM	CLOSING
1993	1,880	1,135	1,865
1994	2,185	1,450	1,555
1995	1,795	1,470	1,680
1996	3,060	1,690	3,015
1997 1st quarter	3,545	2,970	3,415
1997 2nd quarter	4,590	3,240	4,260
1997 3rd quarter	4,845	3,940	4,690
1997 4th quarter	4,765	3,405	4,350



I.T.: International Telecommunications index (Source: "Capital International Perspective")

G.T.: Telefónica Group (Information in accordance with spanish accounting principles)

G.T. (U.S. GAAP): Telefónica Group (Information in accordance with US accounting principles)

International Comparisons at 31/12/97

DIVIDEND POLICY

Telefónica normally pays an interim dividend at year-end and a final dividend once the total dividend for the year has been approved by the Annual General Shareholders' Meeting, following the proposal made by the Board of Directors.

RECENT DIVIDENDS HAVE BEEN:

	1995	1996	1997
Interim	30 ptas.	35 ptas.	40 ptas
Final	46 ptas.	54 ptas.	62 ptas (*)
Total	76 ptas.	89 ptas.	102 ptas

(*) Pending approval by the Annual General Shareholders' Meeting in accordance with the proposed distribution of net income.

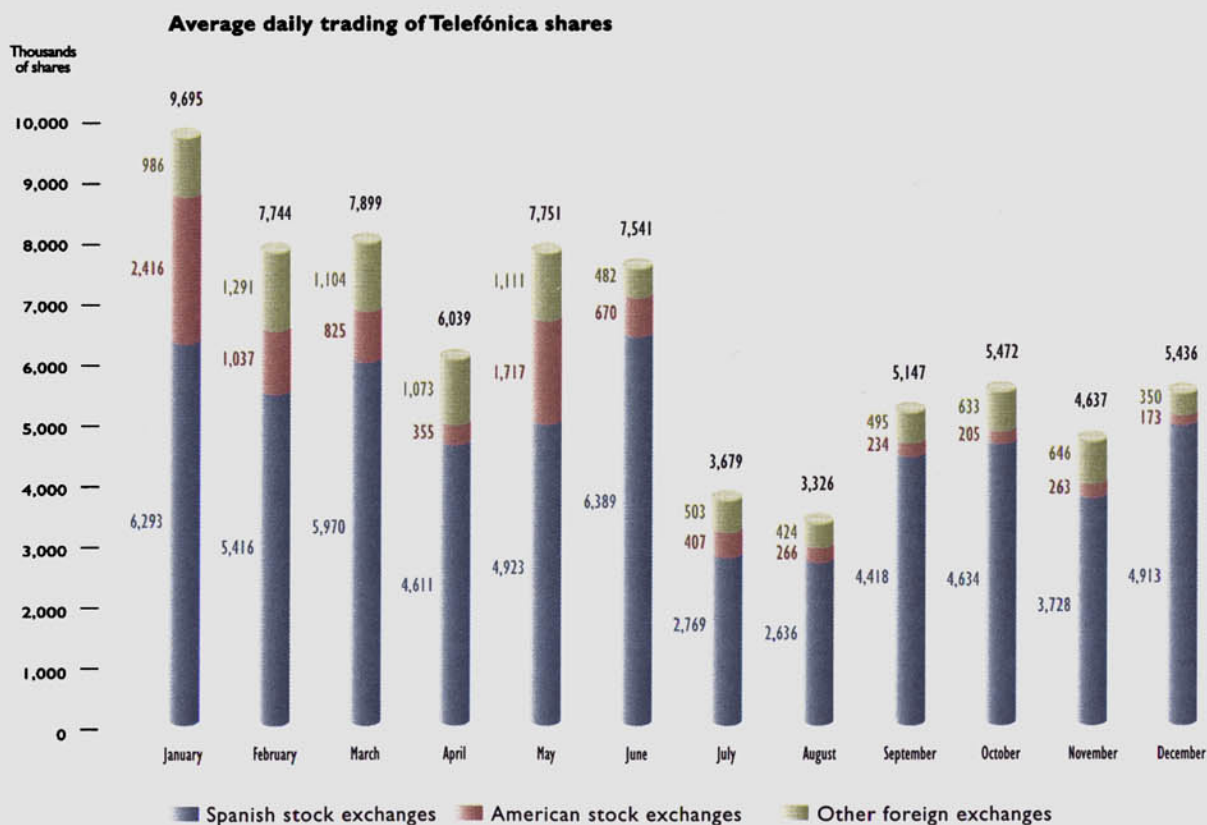
STATE PARTICIPATION IN TELEFÓNICA DE ESPAÑA, S.A.

Under the stipulations of the Royal Decree 116/14/2/92, since December 14, 1995, Telefónica's shares are represented as book entries and therefore the official shareholder list has ceased to exist.

The state participation after Public Offerings on October 5, 1995 and February 18, 1997 was stated as the following:

Sociedad Estatal de Participaciones Patrimoniales, S.A. (SEPPa): 0.55% participation in share capital

Sociedad Estatal de Patrimonio II, S.A.: 0.1% participation in share capital



STOCK MARKET CAPITALIZATION

	1993	1994	1995	1996	1997	Average increase% 97/93
Telefónica (billion pesetas)	1,729.8	1,460.9	1,578.3	2,832.5	4,086.6	23.9
Total Madrid Stock Exchange (billion pesetas)	20,833	20,351	22,899	31,579	44,260	20.7
Telefónica's weighting on the Madrid Stock Exchange Index (%)	9.43	10.44	9.44	11.46	11.63	—

TELEFÓNICA GROUP SHARES

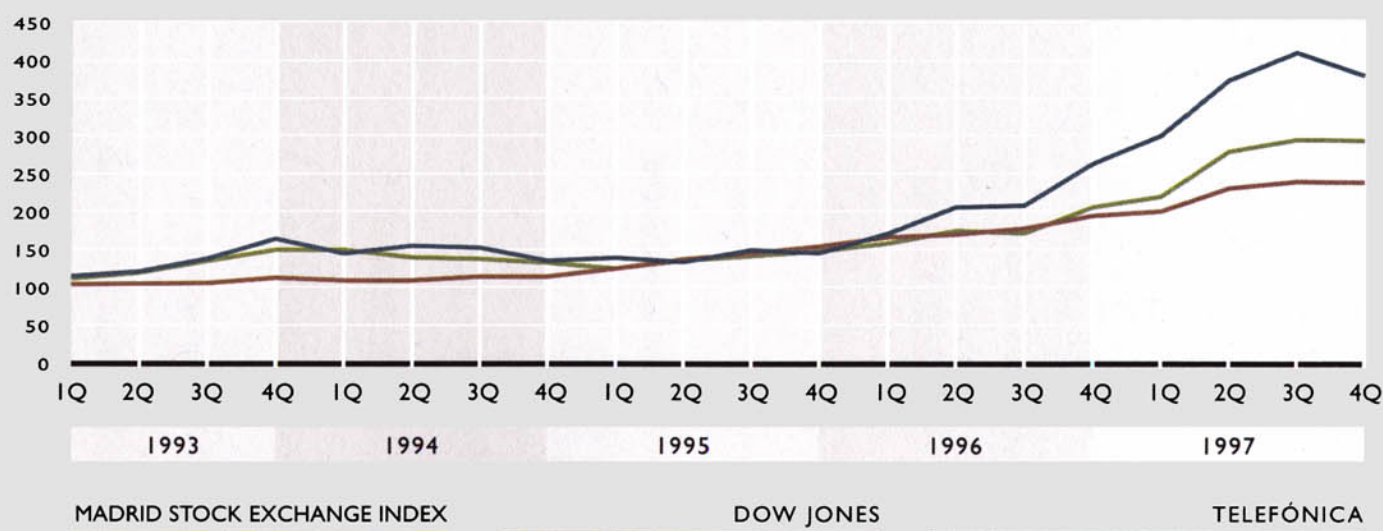
	CTC Chile		CPT Perú		Telefónica Argentina (*)		CANTV(**)	
	1996	1997	1996	1997	1996	1997	1996	1997
Stock market capitalization (mill.\$ US)	4,923	6,322	4,388	5,209	6,177	8,841	4,018	5,832
Closing price(\$US)	5.73	7.2	1.88	2.23	2.62	3.75	4.02	5.83
Price/earnings ratio	13.9	16.7	12.6	13.1	15.3	18.3	9.2	11.2
Price/Cash flow	7.6	8.5	9.0	9.2	6.1	8.0	4.4	5.3
Dividend yield (%)	3.2	2.6	2.9	3.4 (***)	3.9	2.8	—	0.5

(*) The 1996 and 1997 figures are based on the quotation of 31/12/1996 and 31/12/97 and the figures for the financial balance sheets closed at 30/09/96 and 30/09/97.

(**) CANTV shares have been quoted on the Caracas Stock Exchange and New York Stock Exchange since November 21, 1996.

(***) 1997 final dividend pending of approval by the General Shareholders' Meeting of the Company.

Trading index:Telefónica shares



BOARD OF DIRECTORS

At 31 December, 1997

CHAIRMAN

Juan Villalonga Navarro

VICE-CHAIRMEN

José María Concejo Alvarez

Isidro Fainé Casas

Francisco de Asís Gómez Roldán

DIRECTORS

César Alierta Izuel

Gaspar Ariño Ortiz

Pedro Ballvé Lantero

Maximino Carpio García

Alberto Cortina de Alcocer

José Javier Echenique Landiribar

Ignacio Larracoechea Jausoro

Antonio Massanell Lavilla

Juan Perea Sáenz de Buruaga

Juan Antonio Sagardoy Bengoechea

Martín Velasco Gómez

Carles Vilarrubi Carrió

Miguel Zorita Lees

MANAGING DIRECTOR

Javier Revuelta del Peral

SECRETARY OF THE BOARD (non Director)

José María Mas Millet

ASSISTANT SECRETARY (non Director)

Diego L. Lozano Romeral

In accordance with the operating rules of the Board of Directors, the Company's Board members are divided into three groups as shown below:

Board members with executive functions within the Company:

Juan Villalonga Navarro
Javier Revuelta del Peral
Juan Perea Sáenz de Buruaga

Board members representing core shareholders:

José María Concejo Alvarez (Banco Bilbao-Vizcaya)
Isidro Fainé Casas (Caja de Ahorros y Pensiones de Barcelona "La Caixa")
José Javier Echenique Landiribar (Banco Bilbao-Vizcaya)
Francisco Gómez Roldán (Argentaria)
Antonio Massanell Lavilla (Caja de Ahorros y Pensiones de Barcelona "La Caixa")
Miguel Zorita Lees (Argentaria)

Independent board members:

Cesar Alierta Izuel
Gaspar Ariño Ortiz
Pedro Ballvé Lantero
Maximino Carpio García
Alberto Cortina de Alcocer
Ignacio Larracoechea Jausoro
Juan Antonio Sagardoy Bengoechea
Martín Velasco Gómez
Carles Vilarrubí Carrió

EXECUTIVE COMMITTEE

At December 31, 1997

CHAIRMAN

Juan Villalonga Navarro.

MANAGING DIRECTOR

Javier Revuelta del Peral

MEMBERS

Isidro Fainé Casas
Francisco Gómez Roldán
José Javier Echenique Landiribar
Ignacio Larracoechea Jausoro
Juan Perea Sáenz de Buruaga
Martín Velasco Gómez

SECRETARY

José María Mas Millet

TELEFONICA GROUP'S MANAGEMENT COMMITTEE

The Telefonica Group's management committee comprises the following members:

Juan Villalonga Navarro
Chairman of the Board of Directors

Javier Revuelta del Peral
Managing Director

Juan Perea Sáenz de Buruaga
Managing Director, Telefónica Internacional

Fernando Abril Hernández
Chief Financial Officer

Francisco de Bergia González
General Manager, Institutional Relations

Domingo Lampaya Latorre
General Manager, Organization and Information Systems

José María Mas Millet
Secretary of the Board of Directors and General Secretary

Juan José Nieto Bueso
Managing Director, Telefónica Medios de Comunicación

Luis López-Van Dam de Lorenzo
Deputy General Manager, Alliances

TELEFONICA DE ESPAÑA'S MANAGEMENT COMMITTEE

Telefonica de España's management committee comprises the following members:

Juan Villalonga Navarro
Chairman of the Board of Directors

Javier Revuelta del Peral
Managing Director

Juan Perea Sáenz de Buruaga
Managing Director, Telefónica Internacional

Carlos Díaz-Guerra Álvarez
General Manager, Infrastructure

Guillermo Fernández Vidal
General Manager, Corporate Client Business

Rafael Hernández García
General Manager, Retail Client Business

Francisco Mochón Morcillo
General Manager, Reengineering and Cost Management

Andrés Tejero Sala
General Manager, Purchasing and Real Estate

Luis Lada Díaz
Managing Director, Telefónica Servicios Móviles

Julio Linares López
Managing Director, Telefónica Multimedia

Enrique Used Aznar
Managing Director, Telefónica Publicidad e Información

Javier Gimeno de Priede
Managing Director, Cabinas Telefónicas (CABITEL)

Oscar Maraver Sánchez-Valdepeñas
Deputy General Manager, Human Resources

(Telefónica de España's Management Committee meetings are also attended by the members of the Telefónica Group's Management Committee)

January

- ♦ **Telefónica** signs in Brazil the acquisition agreement for 35% of **Compañía Riograndense de Telecomunicaciones (CRT)**, following the international bidding.
- ♦ The company **Distribuidora de Televisión Digital** is incorporated in Madrid. This company is responsible for the marketing of the satellite TV platform **Vía Digital**.

February

- ♦ **Telefónica** is totally privatized following a Public Offering in which the State sells its share capital. One and a half million people are now **Telefónica** shareholders.



- ♦ The telephone numbers for the city of Zaragoza now have nine digits. This is the pilot launching of the **Numbering Plan** to be introduced on April 4th, 1998.
- ♦ **Telefónica Móviles** launches its new prepaid card: **MoviStar Activa**.

March

- ♦ **Telefónica** and Iberdrola jointly create a company to develop value added services.



- ♦ **Telefónica** and Portugal Telecom inaugurate their optic fibre cable between Spain and Portugal (Vigo-Oporto across the international bridge Tui).
- ♦ **Telefónica's InfoVia** service increases its capacity by 40% through the inauguration of a node in Valencia.

April

- ♦ **Telefónica** signs a strategic agreement with BT and MCI. It also signs an agreement with Portugal Telecom for the exchange of share capital and the



development of joint strategies in Spain, Portugal and Latin America, above all, Brazil.

- ♦ An agreement is formed for the development of the underwater cable Columbus III which will connect Spain, Portugal and Italy with the US (Florida) through the Virgin Islands:
- ♦ MensaTel launches its Beeper and forms an agreement with Coca-Cola to carry out an extensive promotion campaign.

May

- ♦ The **Retail Clients** unit begins a pilot project for its "**Single Window**" service, before putting it into commercial use.
- ♦ **Telefónica's Management Committee** approves the launching of **Millennium Project** aimed at solving the computer problems that will arise at the turn of the century, at the same time as giving their seal of approval to the **Euro Project**, aimed at adapting the systems and procedures that support the business processes before the introduction of the Euro as the single currency.
- ♦ The Red IP network service becomes operative, which at the beginning of 1998 will be an alternative to **InfoVia**.
- ♦ **Telefónica Móviles** launches its mobile telephony service via satellite and also **MoviStar Gestion**.
- ♦ The public telephones on thoroughfares can now take electronic cards. Galicia, Cantabria and Asturias are the first regions to launch the new circular telephone booth.

June

- ♦ The **InfoVia** service increases its capacity by 40%, through the opening of connection nodes in Bilbao and Seville.
- ♦ **Telefónica Sistemas** presents its **INFOLINK** service which offers single access to **InfoVia/Internet** for local area networks.



- ♦ **Telefónica Publicidad e Información (TPI)** and **Altavista** launch **Altavista-Magallanes**, the Internet superbrowser for Spanish speakers.
- ♦ **Telefónica Sistemas de Satélites** wins a contract to transmit the motorbike racing Grand-Prix worldwide, with exclusive rights for an additional two years.

July

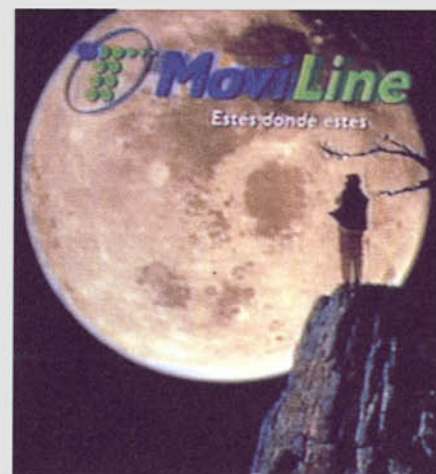
- ♦ **Telefónica** takes over the management of **Antena 3 Televisión**.
- ♦ **Telefónica's Retail Customers'** one-stop-shopping is now available to our customers throughout the whole country.
- ♦ The cable-laying ship, **Teneo**, belonging to **Temasa**, lays the underwater system between Barcelona (Spain) and Savona (Italy).

August

- ♦ The **MoviStar Activa** cards can be charged in the switch-card network 4B.
- ♦ The Bilbao Underground now has total coverage for **Mobile Telephony**.
- ♦ **Infoshowwww** promotes **InfoVia/Internet** in holiday spots.

September

- ♦ **Telefónica** and **Recoletos-Pearson** form an alliance to create a multimedia group in Spain and Latin America.
- ♦ **Vía Digital** begins broadcasting.
- ♦ **Telefónica Servicios Audiovisuales** (previously **Telefónica Sistemas de Satélites**) launches its **Vía Digital Television Distribution Centre** in the Ciudad de Imagen (Madrid).
- ♦ **Telefónica** sends copies of its new billing system to all its customers.
- ♦ **Altavista-Magallanes** incorporates a new system that permits the seeking of information in Internet that is only written in Spanish.



- ♦ **Telefónica** promotes **Netcom**, the new brand name for its medium and low capacity switchboards.
- ♦ **Telefónica de Argentina** applies for the extension of its exclusive rights to offer telephone services after the year 2000, as it has more than amply fulfilled its commitments. **Telefónica's Board of Directors** holds its board meeting in Buenos Aires for the first time.
- ♦ **Telefónica del Peru** initiates the installation of ATM technology.

October

- ♦ **Telefónica** takes up a 3.5% stake in **Portugal Telecom** in accordance with the commitments agreed in April.
- ♦ "**Acción Telefónica**" begins to operate, this being the **Shareholder Attention** service.
- ♦ The **Telefónica** network is now prepared for the launching of the 112 single European emergency service number.

- ◆ The agreement between **Telefónica Móviles** and Iridium (66 satellites in low orbit) will offer 100% worldwide coverage in 1998. **Telefónica Móviles** presents 39 new services for **MoviLine** and **MoviStar**.

- ◆ Those customers who do not pay their telephone bill by bank order may now use their 4B switch-card to pay them. In Alicante, **Telefónica** launches a pilot billing project, through which the customer can check his telephone consumption through **InfoVía**.

November

- ◆ **Telefónica** launches **SAC**, a new system for the **Group's** Procurements and Services, which makes the system smoother and permits significant savings.

- ◆ The Tributary Agency authorizes **Telefónica Servicios Avanzados de Información (TSAI)** to provide electronic billing.

- ◆ **Telefónica** inaugurates its new **Control Centre building (CNSO)**, from which its plant, network and services can be supervised.

- ◆ **Telefónica** creates a subsidiary in Morocco in order to participate actively in North African markets.

- ◆ **Telefónica** and Citicorp Equity create, in Argentina, the company **Advance Telecomunicaciones** in order to offer on-line and data transmission services.

- ◆ **DoubleClick Iberoamérica** is born, aimed at creating the first Spanish-speaking advertising network on Internet.

- ◆ The **Tienda Telefónica** (Telefonica Shop) inaugurates a new space concept for the sale



of the **Telefónica Group's** products and services.

- ◆ The Reina Sofía art museum will exhibit **Telefónica's Art Collection** for four years.

December

- ◆ **Vía Digital** now has 200,000 subscribers.

- ◆ **Telefónica Publicidad e Información (TPI)** and **Telefónica Transmisión de Datos (TTD)** are awarded the AENOR quality certificate.

- ◆ **Telefónica Cable** strengthens its shareholder structure in Navarra, Madrid, Andalucía and Galicia through the incorporation of important partners.



- ◆ **"Integral Services"** is launched (a new system for after-sales corporate customer care) as well as the **Pymes Centres (CAC)**, customer-care for small and medium-sized companies, in Barcelona and Madrid.

- ◆ **Telefónica** finalizes its withdrawal from **Unisource**

- ◆ The department store, El Corte Inglés, initiates the sale of **Telefónica** products and services.

- ◆ The first public Internet access terminals begin to operate.

*Copies of this Annual Report are available
to shareholders on request by mail at
the following address:*

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General Perón, 38. Planta 15
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28020 Madrid

*The information required by law is also available
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Publisher:

Telefónica

Department of Institutional Relations

Graphic Design and Production:

Carlos Serrano G.A.H.
Ricardo Serrano García
Ignacio Martínez-Laya
Editorial A.M.3.

Photography:

Sylvia Polakov (Portrait pag. 8)
Archives of the Department
of Institutional Relations of Telefónica

Process engraving:

Lucam and Cromotex

Photo Composition:

Cromotex

Printing:

T.F. Artes Gráficas

Date of publication: March, 1998
Legal Deposit: M-10820-1998

