

# Fixed-line telephony

## Fixed-Line Telephony Consolidated Income (Millions of Euros)

	TELEFÓNICA DE ESPAÑA			TELEFÓNICA LATINOAMÉRICA		
	2001	2000	% Var.	2001	2000	% Var.
Operating revenues	10,220.4	10,182.9	0.4	10,137.4	10,371.3	(2.3)
Telefónica de España	9,831.5	9,592.9	2.5			
Other and withdrawals	388.9	590.0	(34.1)			
Work on fixed assets (1)	195.1	236.5	(17.5)	212.5	218.6	(2.8)
Operating expenses	(5,703.4)	(5,884.8)	(3.1)	(4,719.6)	(4,928.6)	(4.2)
Other net revenues (expenses)	(203.9)	(86.1)	136.8	(467.3)	(302.1)	54.7
<b>EBITDA</b>	<b>4,508.1</b>	<b>4,448.4</b>	<b>1.3</b>	<b>5,163.0</b>	<b>5,359.3</b>	<b>(3.7)</b>
Amortization/Depreciation	(2,804.4)	(2,901.2)	(3.3)	(2,625.7)	(2,653.4)	(1.0)
<b>Operating income</b>	<b>1,703.7</b>	<b>1,547.2</b>	<b>10.1</b>	<b>2,537.3</b>	<b>2,705.9</b>	<b>(6.2)</b>
Income associated companies	(1.8)	0.1	c.s.	8.4	(2.9)	c.s.
Financial income	(403.1)	(480.9)	(16.2)	(1,318.5)	(1,046.0)	26.1
Amortization Goodwill	(0.6)	(0.3)	111.8	(86.6)	(53.6)	61.7
Extraordinary income	286.1	(806.8)	c.s.	164.6	(331.4)	c.s.
<b>Income before taxes</b>	<b>1,584.2</b>	<b>259.3</b>	<b>510.9</b>	<b>1,305.1</b>	<b>1,272.1</b>	<b>2.6</b>
Tax provision	(506.6)	(43.6)	n.s.	136.2	(286.1)	c.s.
<b>Income prior to minority shareholders</b>	<b>1,077.6</b>	<b>215.8</b>	<b>399.5</b>	<b>1,441.3</b>	<b>985.9</b>	<b>46.2</b>
Income from minority shareholders	0.0	0.8	n.s.	(166.4)	(538.5)	(69.1)
<b>Net Profit</b>	<b>1,077.6</b>	<b>216.6</b>	<b>397.6</b>	<b>1,274.9</b>	<b>447.4</b>	<b>185.0</b>

(1) Includes work in progress

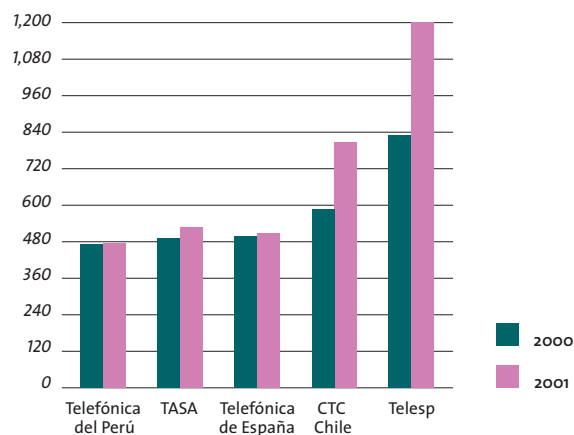
Note: TTP has been included in the accounts of Telefónica de España in both 2000 and 2001

Note: The Telefónica Sistemas Group and TSIP were no longer consolidated in Telefónica de España in both 2000 and 2001

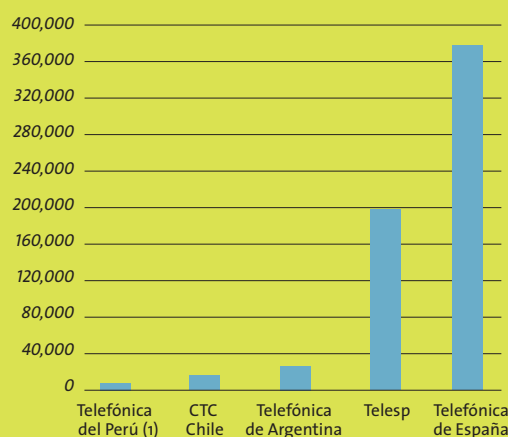
Note: The Telefónica Latinoamérica account reflects the adjustment of the fiscal year of Telefónica de Argentina to that of the Telefónica Group, which means that the statements for the Group's businesses in Argentina for the period January-December 2001 have been included in the corresponding items of the Statement, whereas the October-December 2000 quarterly results have been included in the Extraordinary income item

Note: The financial statements for fiscal year 2000 for Telefónica Latinoamérica include only fixed-line telephony for the Telefónica Latinoamérica Group from January 1, and all shares purchased after the Public Share Offerings made during the year 2000

## Lines per Employee



## ADSL Customers



(t) Includes CABLENET lines in service

# Fixed-line telephony



## Telefónica de España

Telefónica de España developed three key actions during 2001: the evolution towards new businesses, particularly towards Internet and Broadband; the strengthening of its traditional business in a highly competitive environment and subject to substantial regulatory pressure; and its transformation to the new e-business environment, in turn improving quality and efficiency.

### Evolution towards new business

In 2001, Telefónica de España made a significant effort to evolve towards new lines of business, notably Internet and Broadband. The evolution towards the Broadband business is taking place through the implementation of ADSL technology, which, in addition to presenting huge potential for growth, strengthens Telefónica's position in the Internet access business with respect to cable operators.

In this connection, the launch of the retail offer (ADSL Line), and the improvement in installation times, have proved decisive, enabling the company to achieve a daily maximum of 4,614 new subscribers.

Reflecting the strategy of having to be present throughout the entire value chain of the business, in April 2001 it launched Telefonica.net as the provider of Narrow Band Internet access, extending to the provision of Broadband in September. Thus, Telefonica.net ended the year with 187,025 ADSL users, 87,250 domestic switched access flat rate users and 127,700 non-flat rate Narrow Band users.

During the year the company also rolled out and implemented the Rima Network, thus completing the process of migration of ADSL customers to this new high performance IP network, which is designed as the largest and most advanced IP network infrastructure in Spain.

In this connection, Telefónica de España's commitment to Broadband is reflected in a significant increase in the offer of ADSL lines, and in the installation of 101,531 kilometres of fibre optic cable, which have enabled the company to achieve 82% coverage of the lines.



## Strong in traditional business

In the traditional market, subject to substantial regulatory pressure, Telefónica de España's strategy has focused on tackling the competition through an active commercial policy, scrupulously complying with regulatory requirements.

Since the implementation of the "Price-Cap" system in August 2000, the regulatory framework has achieved greater stability, helping to achieve a better readjustment of rates and a 7% drop in prices for 2001.

The Company has made a significant effort to adapt all switching centers in order to enable the global preallocation of Telefónica de España subscribers to other operators, as well as joint actions with other operators to foster the development of the Subscriber Loop Service, which was deregulated at the beginning of the year. The transferability of telephone numbers was also deregulated, and 95,414 numbers were transferred by the end of the year.

The increase in lines (2.0%), coupled with the launch of traffic inducers (USA 15, Bonos Elección, ...), fostered an increase of 1.6% in the total minutes in traditional business, despite the loss of share in access and traffic.

In terms of the supply and improvement of facilities and functionalities associated with the telephone service, it is worth highlighting the full implementation of the Automatic network answering machine (CAR) and Incoming Call Identification services, which required the extension of these facilities to around 2.3 million lines that previously did not benefit from these services.

## Transformation of the company

Within the process of transformation of Telefónica de España towards the new e-business environment, it is worth highlighting the following: E-Domus, the employee portal (accessed by more than 11,000 employees every day); Telefonica on-line, a channel that has become consolidated as a key element in the relationship with its most advanced customers; and E-Ágora, the providers and partners portal for purchases, relations with suppliers, contracts and distribution channels.

The effort to reduce expenses and improve efficiency, which has been maintained throughout the year, meant that operating expenses prior to interconnection remained practically stable despite the significant effort made in connection with Broadband business.

The transformation of the company towards Broadband and new business has coincided with a significant effort in terms of optimizing and containing investment levels in previous years, without neglecting the needs of traditional business (4.02% increase in investment).

Quality improvement was also one of the strategic priorities during the year, representing one of the cornerstones on which Telefónica's transformation and adaptation to the new environment has been based, and an element that distinguishes the company's products from those of its competitors. As part of the strategic measures designed to achieve this improvement, in 2001 Telefónica de España launched the first of the Seis Sigma Projects, forming part of the Excelent.es Project, aimed at boosting the most relevant projects in order to achieve significant improvements in quality. The level of Global Satisfaction at year-end reached 82.8% of Satisfied Customers.



*Telefónica de España's strategy in the traditional market has focused on an active commercial policy*

# Telefónica Latinoamérica

2001 has been a year of huge progress and significant achievements for the company in fixed-line telephony in Latin America. As the leading company in the sector in this region, Telefónica Latinoamérica has consolidated its leadership by increasing its volume of lines in service by 12% to 21.6 million and almost doubling its net revenues to 1,275 million euros.

These advances have been sustained on the achievement of objectives in Brazil, the generation of cash flow in Argentina, the recovery of results in Chile, and the continuation of the restructuring and the consolidation of leadership in Peru.

As part of its efforts to improve management of business as a regional operator, it has worked on a series of projects aimed at acquiring synergies created by Operation Veronica. Among them, the creation of regional centers to align commercial efforts and share best practices in the main business areas (residential, corporate, and Broadband ); the standardization of internal processes and the elimination of duplicated activities in each company; the gradual reduction of operating expenses by taking advantage of the company's economies of scale and the extension of best pan-regional operating practices; the establishment of a common investment process for all operators, and the design of a series of measures to combat bad debt.

As a result of these efforts, Telefónica Latinoamérica has increased its revenues to over 10,100 million euros, contributing 5,163 million to the EBITDA of the Telefónica Group, and which accounts for 40.0% of the total.

# Brazil

## Now that there is no waiting list, the regulatory objectives for 2003 were achieved ahead of schedule

The achievement of objectives in São Paulo by Telesp, which required the elimination of the customer waiting list, and which has led to an increase of more than 2 million lines in service during 2001 (28% average inter-annual growth), was successfully completed in September, 2 years ahead of schedule, and was certified by Anatel in February of this year. This achievement ahead of schedule will enable both Telesp and the rest of the Group companies to operate in Brazil at national level, enabling them to offer their wide range of services to the entire population of the country.

Another significant achievement was the growth in the number of ADSL customers, very close to the 200,000 mark, and four times the figure achieved in the previous year, making São Paulo one of the markets with the greatest development in terms of Broadband services.

This growth in activity was combined with an important effort to continue to improve productivity, which enabled the number of lines per employee to reach 1,198, an increase of 45%. This level of productivity makes Telesp the leader in terms of fixed-line telephony worldwide.

Telesp ended the year with 4,344 million euros in revenues and 2,306 million euros in EBITDA, increases of 25% and 20%, respectively, in local currency.



Values of Telefónica Latinoamérica

*2001 has been a year of great progress and significant achievements for the fixed telephony business in Latin America*

## Argentina

### Control of cash flow in a volatile scenario

In 2001, Telefónica de Argentina achieved solid revenues despite the economic situation in the country, generating EBITDA amounting to 1,523 million euros.

Lines in service increased by 6%, to over 4.5 million. This growth was complemented in turn by the virtual maintenance of the national and international long distance traffic shares. This was particularly important in a market where the long distance business is fully deregulated.

Management at TASA focused on controlling cash flow through the containment of expenses and the restriction of investment in order to adapt to the macroeconomic reality. The measures to contain expenses were implemented from July onwards, and concentrated on renegotiation with providers, development of a package of measures aimed at combating bad debt, and the reduction of personnel expenses. This effort helped reduce expenses 5% below the previous year. The restriction on investment, prompted by the country's crisis, was aimed mainly at the traditional business (with a reduction of 20%), and priority was given to strategic investments such as ADSL. Investment in 2001 was 9% lower than in 2000.

## Chile

### Recovery of the bottom line

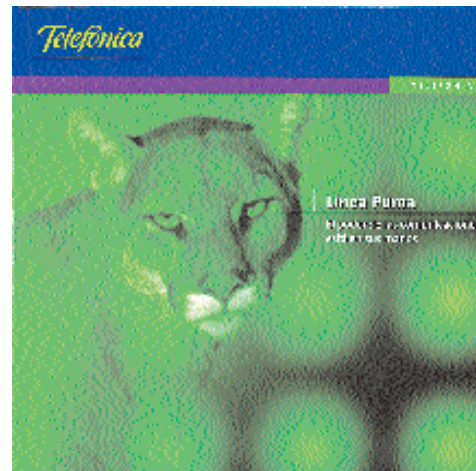
Telefónica CTC Chile managed to end the year with very positive results. After the losses incurred in the previous year as a result of the tariff decree of 1999, drastic measures to control expenses, combined with an aggressive campaign to recover market share in the long distance market, resulted in a gain of 2.3 percentage points, which has enabled the company to make a profit once again.

Initiatives launched in 2000 such as the semi-flat rate through subscription plans, the Plan SLM, and Plan América, as well as the introduction of ADSL, which achieved 15,000 subscribers, enabled the company to increase its volume of revenues by 4% (in local currency).

This growth has been combined with significant adjustments in order to convert overheads into variable expenses. Rigorous cost containment and expense rationalization programmes have had an effect on all accounts, giving rise to an interannual reduction of 10%. In turn, the company's productivity also increased dramatically, with the number of lines in service per employee increasing by 37% to 803.

CTC Chile ended the year with EBITDA amounting to 601 million euros.

*Telefónica de Argentina achieved solid results in 2001, despite the economic situation the country is going through*



## Peru

### Financial restructuring

Telefónica del Perú has continued its efforts to provide a telephone service to the country's population in accordance with the current economic reality in Peru. It has therefore based its growth on products such as prepaid lines, which have grown significantly, and now account for 32% of lines in service, growth of the public telephone service, which increased its lines in service by 14%, as well as the sale of equipment, which increased by 76%.

EBITDA, amounting to 657 million euros, was supported on the growth of prepayment lines, which enabled the bad debt provision to be reduced by 11% compared to the previous year, and the containment of personnel expenses, which fell by 7%.

## Puerto Rico

### The generation of profits

In 2001, TLD generated profits despite the strong competition in the long distance market, thanks to efficient cost management and the renegotiation of interconnectivity contracts. The year ended with 13 million euros in EBITDA, an increase of 269%.

## Targets for 2002

Telefónica Latinoamérica has before it two important opportunities for future growth: firstly, the achievement of the targets in Brazil, which, in addition to enabling the expansion of business to the entire country and winning new customers, will enable Telesp to offer a more complete service to existing customers in São Paulo. Secondly, the opportunity to expand the Broadband business on a regional scale through ADSL, a business that will be boost growth in this new technology quickly and profitably.

Another of the main challenges in 2002 will be the management of the company in a much less certain economic climate, as is the case in Argentina. Management priorities will therefore continue to be a move towards the creation of a regional company, which we plan to continue to build through different initiatives that are already under way, and the adoption of a flexible business model to face changes in the macroeconomic situation or new business opportunities. Therefore work is under way in 2002 to gradually convert variable revenues into fixed revenues, increase efficiency, reduce expenses, and improve operative leverage.



*Christmas advertising campaign  
in Telefónica's public  
telephone booths in Brazil*

