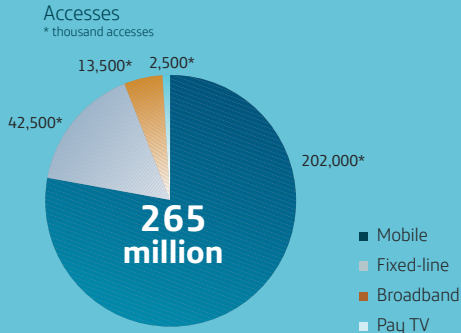


1

Differential scale that generates value

Telefónica, the fifth largest operator in the world by number of accesses

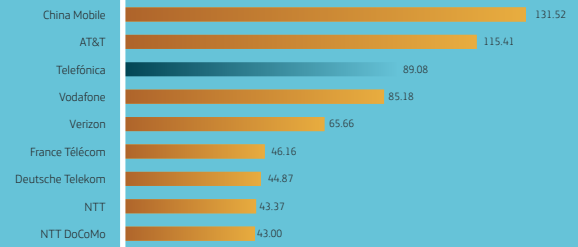


2

Robust financial results

Basic earnings per share of €1.71

Ranking in sector according to stock market capitalisation



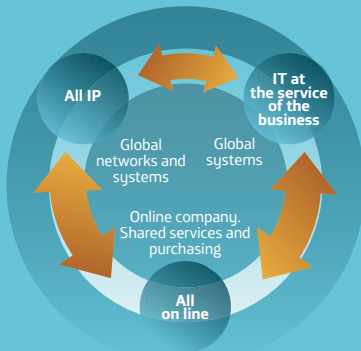
Source: Bloomberg, End of 2009

4

First class efficiency with room for improvement

Telefónica tops the sector for efficiency with a ratio of 74.1%

Towards a new operating model

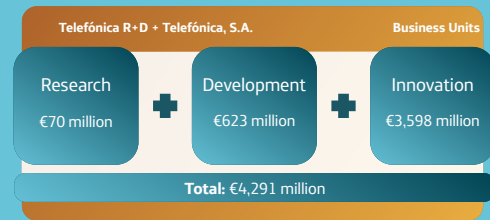


5

Innovation for growth

Investment in R&D&i amounted to 4,291 million euros

Telefónica's open innovation network



7

The commitment of an experienced team

Our employment satisfaction index is 73%

Number of employees, 2009

	Excluding Atento	Including Atento
Spain	40,108	52,060
Latin America	58,031	175,350
Europe	27,031	27,964
Rest of Europe	-	2,052
Total number of employees	125,170	257,426

8

The right alliances and partners

The boost from alliances reinforces the Company's leading position



3

A history of commitments complied with

7 consecutive years of meeting our commitments

Figures related to Compliance with Guidance

	Organic Growth 09/08	Guidance
Revenues	+ 0.3%	✓
OIBDA	+ 1.1%	✓
CAPEX (million euros)	7,459	✓
OpCF	+ 8.4%	✓

6

Solid, reliable brands

Movistar and O2 rank first and second in international rankings of brand recognition

Telefonica

 movistar

O₂

9

Excellent performance in sustainability

Telefónica scored 86 points in the DJSI (+28p.p. above the average of the Telco sector)

Dow Jones Sustainability Index
Global leaders in the sector



DJSI World, GLOBAL SUPERSECTOR LEADERS (2009/2010)

Name	Supersector
Bayerische Motoren Werke AG (BMW)	Automobiles & Parts
Australia & New Zealand Banking Group Ltd	Banks
Xstrata PLC	Basic Resources
DSM NV	Chemicals
Panasonic Electric Works Co Ltd	Construction & Materials
Itausa-Investimentos Itau	Financial Services
Unilever	Food & Beverage
Roche Holding AG	Health Care
TNT N.V.	Industrial Goods & Services
Swiss Re	Insurance
Pearson Plc.	Media
Total SA	Oil & Gas
adidas AG	Personal & Household Goods
GPT Group	Real Estate
Kingfisher Plc	Retail
Nokia Corp.	Technology
Telefónica, S.A.	Telecommunications
Sodexo	Travel & Leisure
Cia Energetica Minas Gerais (CEMIG)	Utilities

Source: http://www.sustainability-indexes.com/07_html/indexes/djsiworld_supersectorleaders_09.html

O2

Leadership based on nine strengths

- 1 Differential scale that generates value **18**
- 2 Solid financial results **22**
- 3 A track record of honouring commitments **26**
- 4 First-class efficiency **30**
- 5 Innovation for growth **32**
- 6 Solid, reliable brands **36**
- 7 The commitment of an experienced team **38**
- 8 The right alliances and partners **40**
- 9 Outstanding performance in Sustainability **42**

Differential scale that generates value

Telefónica, the fifth largest operator in the world by number of accesses

An optimal combination of global, regional and local scale

One of Telefónica's greatest strengths lies in its differential scale at the global, regional and particularly local level, making it a company that is constantly growing. Its scale is global and it is the fifth operator worldwide in terms of the number of accesses. Its scale is also regional, as it holds significant market shares in Europe and in Latin America. However, the Company's most important aspect is its local character, as it is always first or second in the ranking in every market where it operates.

Since the year 2000, the number of customers has increased fourfold. Telefónica closed the financial year 2009 with almost 265 million customer accesses.

The Company's intense commercial activity has led to a 5.1% increase in the number of total accesses compared to 2008, with sharp rises in mobile telephony (+7.4%), fixed broadband (+8.2%) and Pay TV (+9.8%). In terms of geographical areas, the highlights were the growth rates attained by Telefónica Europe (year-on-year increase of +6.9%) and Telefónica Latin America (year-on-year increase of +6.5%).

Fixed telephony

42.5 million accesses (-0.9% year-on-year)

In the mature market of fixed telephony, Telefónica ended 2009 with 42.5 million accesses, compared to 42.9 million in 2008.

In Spain, the Company's retail fixed access base stood at 14.2 million at the end of 2009 (15.3 million in December 2008). Therefore, the Company's estimated market share was around 72% in 2009.

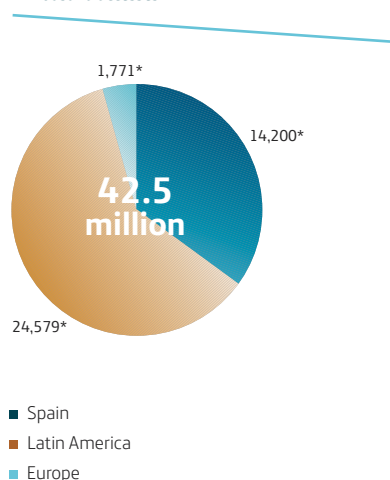
In this regard, it should be highlighted that 66% of the losses in retail fixed telephony accesses was compensated for by the net growth in wholesale accesses; with revenue therefore also being generated for the company.

In Latin America, accesses stood at 24.6 million at the close of the year, down 4.2% compared to 2008 (2.7% if the disconnection of inactive customers affected by fixed-mobile replacement in Colombia is excluded).

In the Czech Republic, accesses stood at 1.8 million at the end of 2009, with a year-on-year drop of 6.5%, compared to one of -8.3% in 2008.

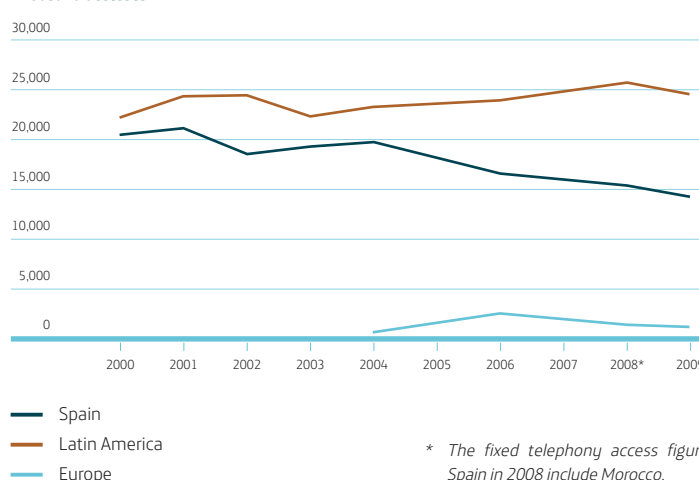
Accesses Fixed telephony in 2009

* Thousand accesses



Changes in fixed telephony accesses 2000/2009

Thousand accesses



* The fixed telephony access figures for Spain in 2008 include Morocco.

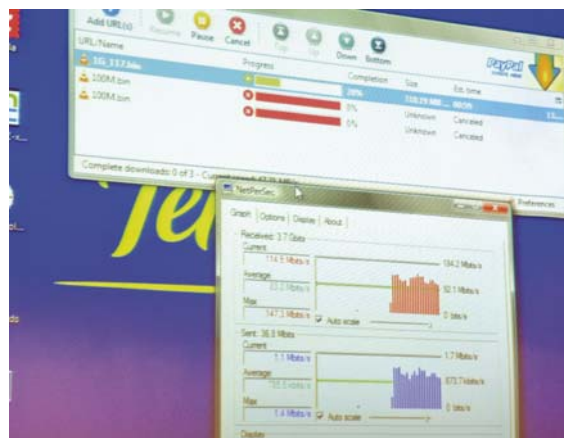
With the trust of almost 265 million customers

Broadband

13.5 million accesses (+8.2% year-on-year)

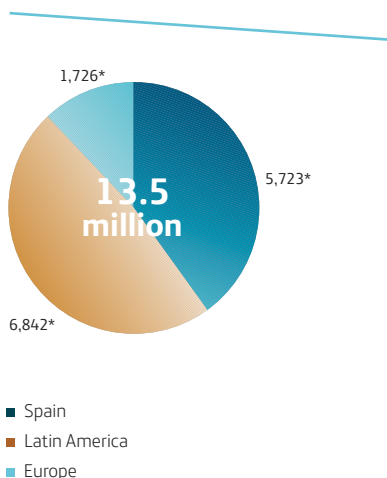
Retail broadband internet accesses stood at 13.5 million, with a year-on-year growth rate of 8.2 %, driven by the increase in the adoption of packaged voice, ADSL and Pay TV service offerings.

In terms of geographical areas, in Spain, Telefónica closed the financial year with 5.5 million accesses, up 4.4% on the previous financial year; in Latin America it topped 6.4 million accesses, which represents a further 5.9% year-on-year increase. Lastly, in Europe data and internet accesses totalled over 1.3 million accesses, i.e. a further 29.5% year-on-year increase.



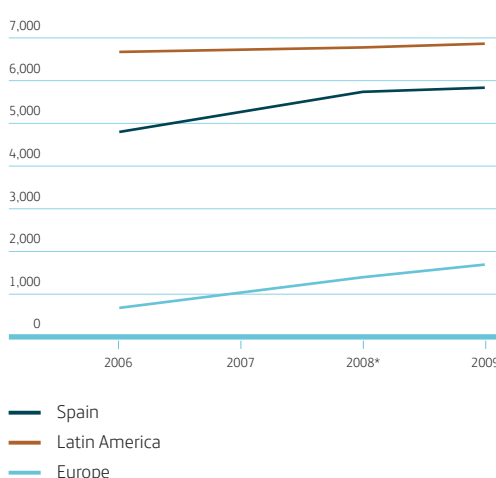
Accesses Data and Internet in 2009

* Thousand accesses



Change in Data and Internet accesses 2006/2009

Thousand accesses



02/1 Differential scale that generates value

Mobile telephony

202 million accesses

(+8% in comparable terms)

The Telefónica Group's mobile accesses exceeded 202 million by the end of 2009, with a net rise of approximately 15 million accesses in comparable terms in the financial year.

In the context of these figures, special mention should be made of the significant increase in the number of mobile Broadband accesses, which exceeded 15 million by the close of 2009 (compared to 9 million accesses in 2008).

Telefónica España's mobile base reached a total of 23.5 million mobile customers. Adoption of flat rates for mobile data is continuously increasing, standing at over 1.9 million at the end of the year, which represents double the figure for the end of 2008.

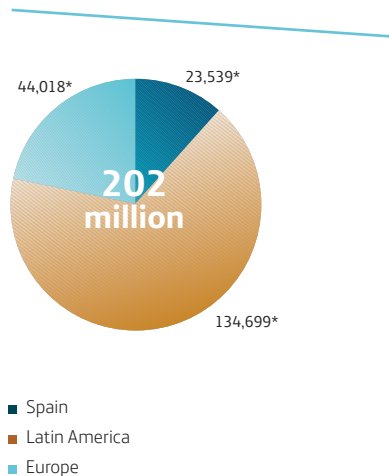
In Latin America, mobile accesses climbed to 134.7 million, maintaining a year-on-year growth rate of 9.2% after registering a net gain for the year of 11.4 million accesses.



In Europe, the Company attained a total base of 44.1 million accesses (year-on-year increase of +6.5 %) after registering a net increase of 2.3 million customers in 2009.

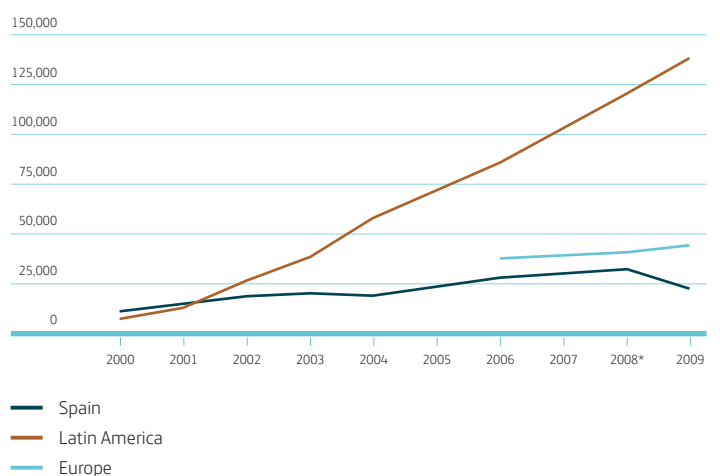
Accesses Mobile telephony in 2009

* Thousand accesses



Changes in mobile telephony accesses 2000/2009

Thousand accesses



* The fixed telephony access figures for Spain in 2008 include Morocco.

All our products
are called Movistar



Fixed Voice

42.5 million accesses

Pay TV

2.5 million accesses (-9.8% year-on-year)

Accesses to Pay TV were approaching 2.5 million at the end of 2009, which represents a 9.8% increase on the figure for the previous year.

Telefónica España gained 90,486 new customers in the last financial year, rising to 702,980 customers (a year-on-year increase of +14.8%), with a significant climb in estimated market share, which stood at around 17% at the end of 2009.

In Latin America, the number of customers stood at 1.6 million (up 7% year-on-year) after having captured 179,556 accesses in the course of the year.

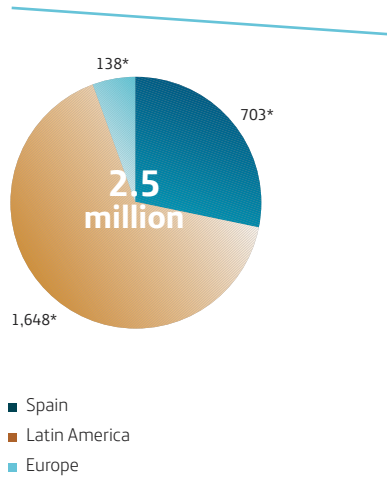
Telefónica O2 Czech Republic totalled 137,630 customers at the end of December 2009, with a year-on-year increase of 20.2%.



Product image of Movistar Imagenio with the new brand identity.

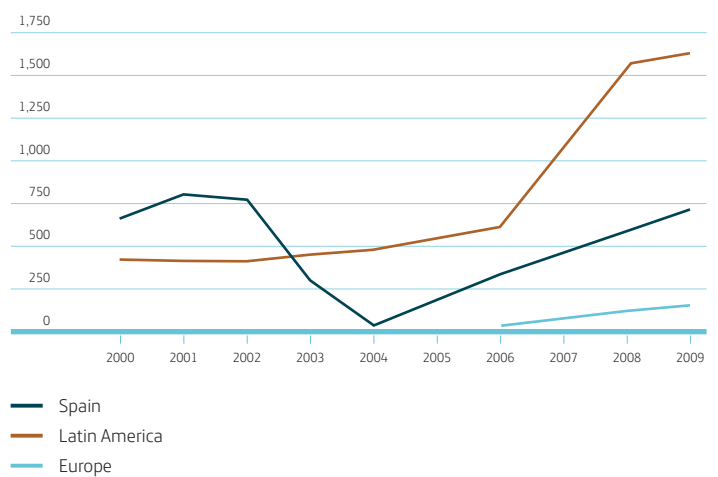
Accesses Pay TV in 2009

* Thousand accesses



Changes in pay TV accesses 2000/2009

Thousand accesses



Mobile Voice

202 million accesses

Tv

2.5 million accesses

Adsl / Internet

13.5 million accesses

Robust financial results

Basic earnings per share of €1.71

Shareholder remuneration

5,516 million euros

In this regard, Telefónica reaffirms its policy of increasing dividends. In 2009 the Company allocated 5,516 million euros to shareholder remuneration; this is equivalent to 61% of the cash flow generated in the year, and 7% of the Company's stock market capitalisation¹.

Shareholder return involved the payment of dividends in cash and buying back shareholders' equity. It should be noted that as at 31 December 2009 the Company owned derivatives on 150 million Telefónica shares, and it owned 27.3 million treasury shares as at 19 February 2010, representing 0.6% of the share capital of Telefónica.

2009 dividend payment 1.15 euros per share

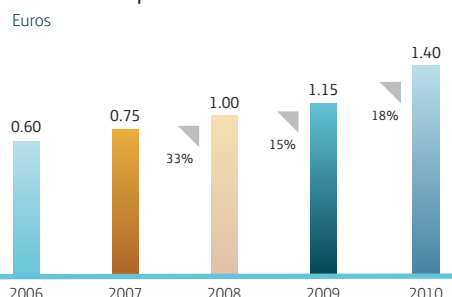
On 12 May 2009, the Company distributed dividends charged to the profit and loss account for the financial year 2009 amounting to 0.50 euros gross to each of the Company's shares in circulation with dividend rights. With this payout and the one in November 2008, the Company honoured its announced commitment to providing a shareholder return of 1 euro per share before the end of the first semester of 2009.

Similarly, on 11 November 2009, Telefónica distributed dividends of 0.50 euros gross per share from Unrestricted Reserves to each of the Company's shares in circulation with dividend rights.

Dividend improvement policy Objective for 2010 of 1.40 euros per share

Following the announcement in February 2009 of a 15% increase in the annual dividend to 1.15 euros per share, and the subsequent reiteration of this commitment by the Company's Board of Directors at its meeting held on 29 April 2009, the Telefónica Group once again committed itself, at the Investors' Conference held on 9 October 2009, to a schedule of gradual increases in dividends in the medium term.

Continued increase in dividend per share



Earnings per share 2009: 29.46%

	No. of shares	Gross amount in €
Value of 100 shares on 1 January 2009	100	1,585
Cash dividend (12 May 2009)	100	50
Cash dividend (11 November 2009)	100	50
Value of 100 shares at 1 January 2010	100	1,952
Value of portfolio consisting of 100 shares	100	2,052
Return		29.46%

¹ As of 26 February 2010

Earnings per share increased by 4.5%

Thus, an increase of 21.7% compared to 2009 was announced for the dividend in 2010, rising to 1.40 euros per share. In addition, a goal of distributing a minimum dividend of 1.75 euros per share by 2012 was set for the medium term.

Since 2003, the year in which Telefónica regained control of its dividend distribution policy, the Company has gradually improved its shareholder returns policy and is currently one of the best companies in this respect and among the few to undertake an express commitment to increasing dividends in the medium term (three years).

Basic earnings per share

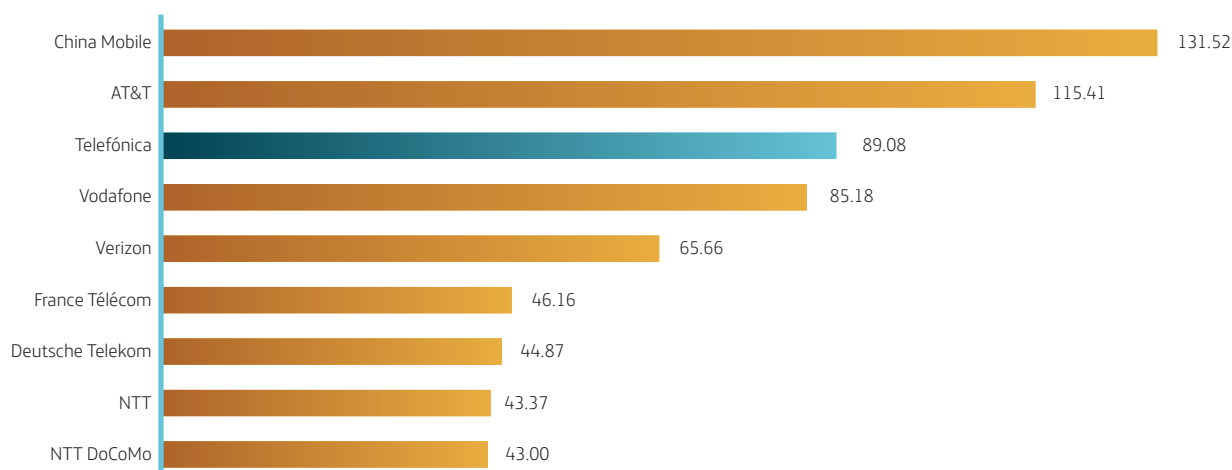
Target of € 2.10 Net EPS in 2010 maintained

In a very adverse economic environment, Telefónica has managed to achieve very solid results for yet another year, after leveraging the opportunities that arose during the financial year and using its differential scale as an important tool for operating in a global market. As a result, the Company has combined the highest rate of organic growth in the sector with the best EBITDA margins.

The basic return per share stands at €1.71, with a 4.5% year-on-year growth rate. The Company remains true to its goal of attaining Net Earnings per Share (Net EPS) of €2.10 per share in financial year 2010 and reaffirms its objectives for growth in the medium term.

Telefónica confirms its goals for dividends through 2012: €1.15 per share in 2009, €1.40 per share in 2010 and a minimum of €1.75 per share in 2012.

Ranking in sector by stock market capitalisation



Source: Bloomberg. Year-end of 2009

Returns to shareholders

7,776 million euros (+2.4%)

The net profit attained by Telefónica in 2009 totalled 7,776 million euros, a 2.4% increase on the amount reported in 2008, while the basic net earnings per share rose to 1.71 euros, a year-on-year increase of 4.5%.

As highlighted in a previous section of this report, the Company remains committed to its goal of Net Earnings Per Share (Net EPS) of 2.10 euros per share in the financial year 2010.

Share performance

29.5% total return

In 2009, Telefónica shares returned to the upward trend seen in 2003-2007, with an annual increase of 23.2%, ending the year at 19.52 euros per share. This solid performance, which was backed by the stock market recoveries in 2009, sets the Company apart as it performed better in relative terms than its reference sector in Europe – the *DJ Stoxx Telecommunications* index recorded an 11.2% increase – and compared to the general *EStoxx-50* index, which was up 21.3%.

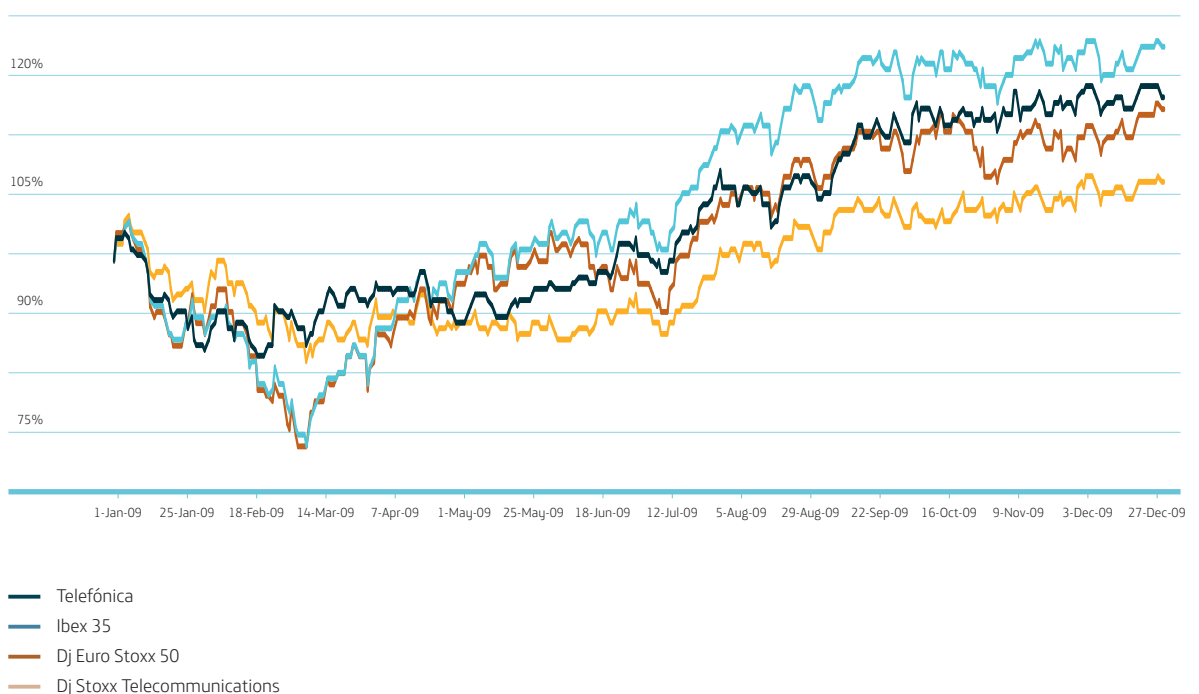
Telefónica's better performance compared to other European operators –Vodafone (+3.2%), BT (+1.5%), *Deutsche Telekom* (-4.3%), *Telecom Italia S.p.A.* (-5.4%) and *France Telecom* (-12.2%)– reflects the advantages of its diversification, both geographically and in business areas; its proven ability to perform in changing environments; the Company's strong cash flow generation; and its commitment to its shareholders. The latter is clearly reflected in its commitment to continue to increase returns for shareholders in the form of dividends, with dividends being announced in February 2009 and October 2009.

This resulted in the total return on Telefónica shares in 2009 reaching 29.5%, following the inclusion of all of the dividends distributed during 2009 (0.50 euros on 12 May 2009 and 0.5 euros on 11 November 2009).

This strong performance by Telefónica has made it into the third largest telecommunications company in the world in terms of market capitalisation, and into one of the top fifty worldwide. Telefónica's stock market capitalisation at the end of 2009 stood at 89,089 million euros.

Telefónica's average daily trading volume on the Spanish continuous market amounted to 48.5 million shares in 2009 (57.2 million securities in 2008).

Stock market performance 2009



Source: Bloomberg

In 2009, Telefónica's shares increased in value in absolute terms (+23.2%), exceeding in relative terms the DJ Telco (+11.3%) and DJ Euro Stoxx 50 (+21.1%) indices. However, the increase in the Telefónica share price was slightly below the increase in the Ibex 35 (+29.8%).

With the exception of Portugal Telecom (for which the increase was 40.4%), Telefónica's share price increased by more than the rest of its major European counterparts.

Telefónica climbed one place to third in terms of stock market capitalisation at the close of 2009 (€89,089 million).

Other information

Stock Markets

Telefónica is listed on the Spanish Continuous Market (as part of the Ibex-35 index) and on the four Spanish stock markets (Madrid, Barcelona, Bilbao and Valencia), as well as on the stock markets of New York, London and Tokyo, São Paulo and Lima.

Share capital

On 28 December 2009, the Company proceeded to reduce its share capital by 141,000,000 euros, by cancelling 141,000,000 of its own shares. As a consequence of this, the share capital of Telefónica, which is fully subscribed and paid up, was calculated at 4,563,996,485 euros, consisting of 4,563,996,485 ordinary shares of the same category and series, each with a par value of one euro and being represented by account entries.

Number of shareholders

Telefónica had 1,500,000 shareholders at 21 May 2009, according to the individualised records detailing private individuals and legal entities, and with the data held by the Spanish Central Securities Depository (Sociedad de Gestión de los Sistemas de Registro, Compensación y Liquidación de Valores - Iberclear).

Significant holdings

According to the information available to the Company, no private individual or legal entity exercises or might exercise control over Telefónica, either on a direct or indirect basis, whether acting alone or jointly.

As of 31 December 2009, Caja de Ahorros y Pensiones de Barcelona (La Caixa) and Banco Bilbao Vizcaya Argentaria, S.A. (BBVA), were the direct or indirect holders of 5.170% and 5.543% of the share capital of Telefónica, respectively.

The Office of the Telefónica Shareholder

The Office of the Shareholder was created to establish transparent and fluid communications with private shareholders and to provide them with information at the same time and in the same form as it is received by institutional investors. There are three channels for this relationship:

Free phone line for shareholders:

900 111 004. In 2009, a total of 73,881 calls were received, up 7.27% on 2008, at an average of 6,157 calls a month.

In addition to telephone queries, the Office of the Shareholder dealt with a further 3,487 queries by email and post (up from 2,360 in 2008). Of the queries received in 2009, 54,955 related to economic and financial issues as follows:

- 25,085 queries about the General Meeting of Shareholders.
- 22,318 queries about stock market performance and the share price.
- 7,507 queries about results and relevant events.
- 45 queries on rights issues and special financial operations.

On line channel:

(www.telefonica.com/accionistaseinversores)

In 2009, there were a total of 1,363,455 page views on the Shareholder and Investors website, a 12.4% increase on the 1,213,070 the previous year. The website is available in Spanish, English and Portuguese, and has specific sections on:

- The Company's stock market performance, including on line share prices. The webpage can generate interactive graphics; compare Telefónica's share price with that of other companies in the sector; calculate returns over a period selected by the user; and provide comparisons with reference indices.
- Dividends, results and communications with the markets, relevant facts and information on Corporate Governance (composition of Governance Bodies, Articles of Association, Regulations, etc).
- Viewing and downloading documents, including annual reports, the Regulations of the General Meeting of Shareholders and the Board of Directors, the Articles of Association, and official records of information on the Company's activities.
- The Shareholder's Corner provides small shareholders with a personalised interactive area for asking questions, receiving specific information and alerts about information relevant to the Company.

The "Acción Telefónica" magazine

The Office of the Shareholder publishes the magazine "Acción Telefónica" for Company shareholders. The magazine is published every three months. In 2009, 603,676 copies were sent to the homes of shareholders. The magazine is filled with information on results, company facts, stock market information, reports and culture.

A track record of honouring commitments

7 consecutive years of meeting our commitments

Responding to commitments

One of the Company's greatest strengths lies in its excellent track record in honouring commitments undertaken, regardless of the economic cycle at the time. This makes Telefónica a Company that is highly predictable and which presents minimal risk levels for investors. Strictly honouring its commitments gives Telefónica credibility and reinforces its leading role in the markets where it operates.

In the financial year 2009, it attained the targets that had been set and made a net profit of 7,776 million euros. The Company achieved robust results in the last year, through its good management in a difficult environment.

Operating cash flow (OIBDA-CapEx) stood at 15,346 million euros, over 8% more than in 2008, and the ratio of net financial debt plus commitments to OIBDA was 2.1 times in 2009, which is proof of the Company's financial solidity.

Despite the fact that the financial year was marked by a difficult environment due to the economic downturn, Telefónica has continued on the path of sustainable profitable growth that it has been following for the last decade.

Compliance with Guidance

7 consecutive years

For the last seven years, the Company has met all of the financial targets it announced in advance for the financial year. The Telefónica Group obtained robust financial results in 2009, despite the complexities of the economic and operating environment, demonstrating the value of the high degree of diversification of its operations.

Income, OIBDA, investment and operating cash flow are just some of indicators where Telefónica managed to attain the targets set, and this clearly demonstrates its leadership and financial credibility.

Effective performance of the financial objectives for 2009¹ is demonstrated by:

1. Revenues increased by 0.3%, in line with the positive growth expected.
2. OIBDA increased by 1.1% and is within the announced range of 1%-3%.

	Guidance			Reported with guidance criteria*			Compliance
	Revenues	OIBDA	OI	Revenues	OIBDA	OI	
2003	5%-8%	6 - 9%	18 - 21%	6%	12.5%	29.7%	✓
2004	7% - 10%	5 - 7%	15 - 18%	8.3%	6%	15.5%	✓
2005	>15%	10 - 13%	12 - 18%	17.2%	12.3%	16.1%	✓
2006	>37%	26 - 29%	26 - 30%	38.8%	28.9%	29.2%	✓
2007	8 - 10%	10 - 13%	19 - 23%	9.8%	12.8%	27.6%	✓
2008	6 - 8%	7.5 - 11%	13 - 19%	7.3%	10.6%	20.4%	✓
2009	>0%	1 - 3%	-	0.3%	1.1%	-	✓

Source: Presentation of TEF results

* The increases in the table are reported using the criteria current when the annual guidance was set, and may as a result not match published figures.

¹ Base guidance figures for 2009: The base figures for 2008 exclude the impact of the sales of assets (143 million euro gain from the sale of Sogecable) and 174 million euros from the appropriation of T. Europe provisions to cover potential commitments resulting from past disposals of shareholdings once these risks had dissipated or failed to materialise) and includes 9 months of consolidation of Telemig. The base figures for guidance in 2009 assume constant exchange rates in 2008 (average for 2008) and exclude the impact of adjustments for hyperinflation in Venezuela. For the purpose of calculating guidance, OIBDA excludes capital gains and losses from the sale of companies and balance sheet cleansing. CapEx for the Telefónica Group excludes Telefónica España's Real Estate Efficiency Programmes and spectrum investments.

For yet another year, Telefónica achieved the goals that it set for itself

3. Investment (CapEx) stood at 7,459 million euros, compared to a target of keeping it below a limit of 7,500 million euros;
4. Operating cash flow (OIBDA-CapEx) increased at a year-on-year rate of 8.4% and was well within the announced target range of 8%-11%.

The Company's strategy has enabled it to reinforce the foundations for future growth and to maintain exceptional operational efficiency, as can be seen in the OIBDA margin and the high cash flow generation.

Revenues of

€56,731 million (+0.2% year-on-year in organic terms)

Despite the complicated operating environment in 2009, which placed strong pressure on revenues in some markets, the Company's strong diversification of operations enabled it to achieve net turnover (revenues) of 56,731 million euros in 2009, up 0.2 % on 2008 in organic terms.

Mention should be made of the excellent performance of revenue from Telefónica Latin America, which contributed 2.7 percentage points to organic growth and, to a lesser extent, that of Telefónica Europe, with a 0.2 percentage point contribution in the period. Furthermore, the improved performance of Telefónica España's revenues in the second semester of the year should be highlighted, as the rate at which revenues were falling decelerated in the fourth quarter for the second quarter in a row.

By area of activity, revenue from Broadband connectivity, both fixed and mobile, and revenue from applications and new services are continuing to make increasing contributions to the Group's overall revenues, adding 2.5 percentage points to organic revenue growth in 2009.

By regions, over the year as a whole, the revenues contributed by Telefónica Latin America represented 40.5% of the Group's total, with Telefónica España and Telefónica Europe accounting for 34.7% and 23.9%, respectively.

Profitability of the business

OIBDA of €22,603 million

(+0.9% year-on-year)

The Company's focus on improving efficiency and leveraging economies of scale was reflected in its operating income before depreciation and amortisation (OIBDA), which amounted to 22,603 million euros in 2009.

In organic terms, the figure for OIBDA presented a growth rate of 0.9%, basically supported by Telefónica Latin America and Telefónica Europe, with the revenue margin increasing to 39.8%.

As regards regional distribution, the OIBDA figure for Telefónica España represented 43.2% of the total OIBDA figure for the Group, compared to 40.5% for Telefónica Latin America and 17.3% for Telefónica Europe.



Figures related to Compliance with Guidance 09/08

	Organic Growth 09/08	Compliance
Revenues	+ 0.3%	✓
OIBDA	+ 1.1%	✓
CAPEX (million euros)	7,459	✓
OpCF	+ 8.4%	✓

Cash flow generation of €15,346 million (+8% year-on-year in organic terms)

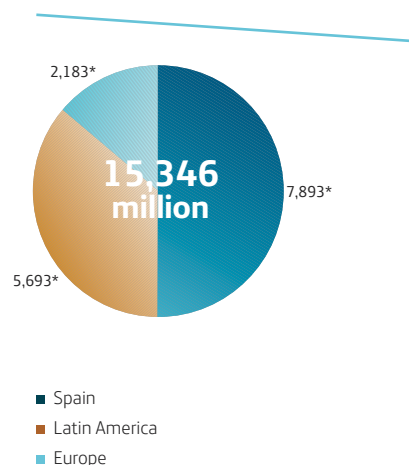
The Company's effort to manage operating expenses and investment translated into an increase in operating cash flow (OIBDA-CapEx) that by the end of last year had reached 15,346 million euros, which represents a year-on-year growth rate of 8.0% in organic terms. In terms of regional distribution, Telefónica España contributed 7,893 million euros; Telefónica Latin America 5,693 million euros and Telefónica Europe, 2,183 million euros.

The free cash flow generated by the Telefónica Group in 2009 totalled 9,097 million euros, of which 959 million euros were allocated to the purchase of treasury stock; 4,557 million euros to Telefónica S.A. dividend payouts; 793 million euros to cancelling commitments undertaken by the Group (mostly derived from workforce reduction programmes); and 1,178 million euros to financial investments and divestments in the period.

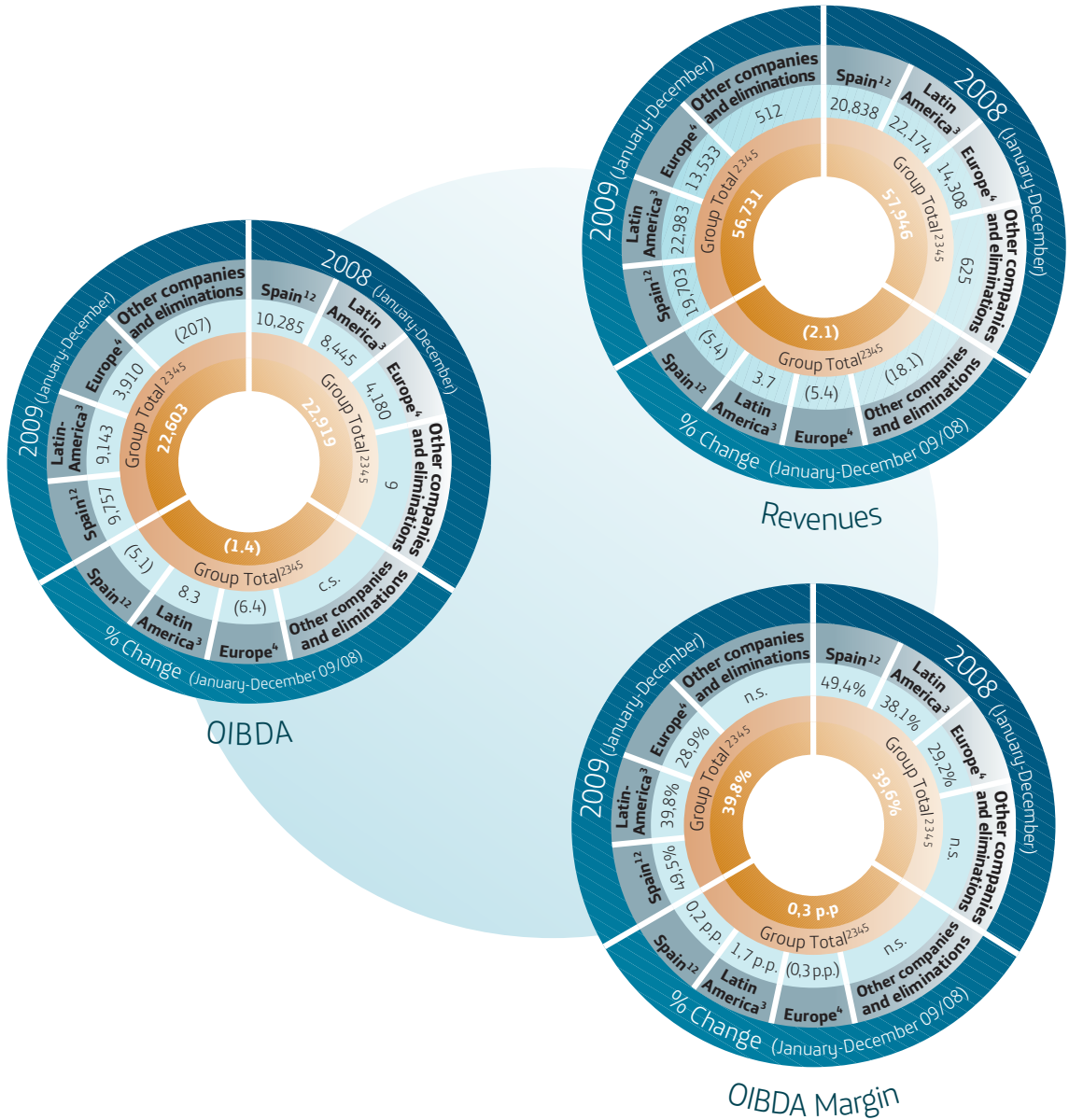
As a result, net financial debt reduced by 1,610 million euros. In addition, there was also a 2,429 million euros increase in financial debt due to variations in exchange rates; changes in the scope of consolidation; and other effects on financial accounts. This resulted in net financial debt of 43,551 million euros at the end of 2009, up 818 million euros on net financial debt at the close of the 2008 financial year (42,733 million euros).

Operating Cash Flow

* Million euros



Telefónica Group
Results by business unit
Million euros



Notes:

- OIBDA and OI for businesses are presented before management and brand expenditure.
- OIBDA margin calculated as OIBDA on net turnover.
- 2009 data impacted by hyperinflation adjustment in Venezuela.

1 In comparable terms, Telefónica España's revenues would be down by 5.9%, OIBDA would be down by 8.0% and OpCF would be down by 5.9%. Comparable terms exclude the impact of the Universal Service: 183 million euros in revenue and 51 million euros in OIBDA in the third quarter of 2008; 75 million euros in revenue and 22 million euros in OIBDA in the first quarter of 2009; and 148 million euros in revenue and 47 million euros in OIBDA in the fourth quarter of 2009; sale of bad debt portfolio: 25 million euros in OIBDA in the first quarter of 2008; capital gains from real estate: 6 million euros in OIBDA January - December 2009 and 74 million euros in OIBDA for the same period of 2008; review of estimates made in previous financial years corresponding to workforce adjustment plans, which led to 90 million euro lower expenditure in the second quarter of 2009; sale of application rights: 48 million euros in revenue and OIBDA in the third quarter of 2009; and capital gains from the sale of Medi Telecom: 220 million euros in OIBDA in the fourth quarter of 2009.

2 The fourth quarter of 2009 includes capital gains from the sale of the holding in Medi Telecom (220 million euros).

3 From April 2008 onwards, the scope of consolidation of Vivo includes Telemig.

4 2008 includes a positive 174 million euro impact from the sale of Airwave. OIBDA and OI include restructuring expenditure of 44 million euros.

5 The second quarter of 2008 includes capital gains from the sale of the holding in Sogecable (143 million euros).

First class efficiency with room for improvement

Telefónica tops the sector for efficiency with a ratio of 74.1%

Efficiency ratios

74% efficiency rating in 2009

In 2008 Telefónica led comparative efficiency ratios ($(Opex+CapEx)/Profits$), with a ratio of 75.5%, the best among its main global competitors. Despite this leadership, there is still room for improvement and the objective is to achieve 70% efficiency by 2012.

The success of the action taken so far in this regard is the decrease in this ratio to 74.1% in 2009.

Improving efficiency is of vital importance, as it improves competitiveness and as a result strengthens the capacity to generate profits. Transformation of its operating model will not only enable Telefónica to be more efficient, but will also enable it to take advantages of opportunities which arise in the new digital world.

This model is based on global networks and technology with full IP; global systems employing IT in the service of business; and processes which are ever more on line.

Greater coverage and increased capacity

3G network coverage: +15p.p.

The focus in this area centres on equipping the Company with the tools that will enable it to leverage future growth in the sector, particularly in Broadband, which will be one of the greatest sources of revenue.

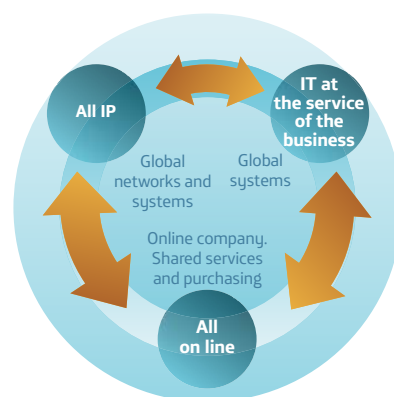
In 2009, Telefónica continued working to develop a powerful, integrated, flexible, intelligent, open and low-cost network. Despite the economic background, throughout the year, Telefónica increased its 3G network coverage by 15 percentage points; it increased fixed lines with capacity for over 25 megabytes by more than 5 percentage points; and it doubled the capacity of its IP network.

Telefónica priority areas of work for networks and technology are:

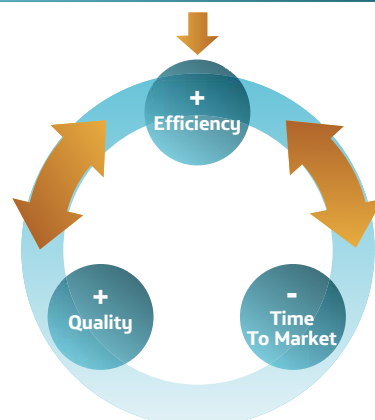
- Integrating the customer's vision of fixed and mobile services from a technological perspective, by offering the best connectivity in all environments.

- Making efficiency of service –in terms of both speed and quality– into one of the main elements that set the Company apart from its competitors.
- Standardising its network model to take advantage of economies of scale in purchasing equipment and contracting services.
- Sharing network infrastructure with other operators and outsourcing processes, where these are not elements which set the Company apart.
- Boosting network automation.

Towards a new operating model



- Taking maximum advantage of scale
- Accelerating the changes required to exploit the advantages of Mobile Broadband, and having a single view of the customer



The target is to reduce it to 70% by 2012

The Company's most recent initiatives in this area include an agreement with Vodafone to share mobile network assets in a number of countries in Europe; the automation of network alarm management; and global purchasing of standardised fixed line broadband equipment for the customer's home.

A new IT company for Group operators

Telefónica's commitment to putting Information Technology at the heart of business, with a clear, customer-focused approach, is helping it to exploit these new sources of growth to the maximum. The goal is to unify customer information using integrated processes with clear internal and external visibility to provide our customers with a differentiated experience, irrespective of the channels and devices used, thus reinforcing their relationship with our brand and products.

The 2009 launch of a standardised systems management model across the whole group was a key step in exploiting the values of scale and aligning priorities with business strategy.

Fundamental elements of this model include:

- Consolidating and optimising Data Centres, providing them with common technical architecture and management processes which will enable them to simultaneously achieve higher levels of efficiency and operational excellence (availability, security, etc).
- Providing employees with better tools (*common hardware and software*) and exploiting scale to combine functionality and efficiency.
- A shared IT model for managing relations with suppliers.
- Common systems architecture, defining a global systems map which maximises scale and reutilisation in the development of applications to implement the business strategy.

A new IT company has been created as a management tool for this model to provide a full range of IT services to Group operators.

Creation of a new global purchasing unit in Munich

Telefónica's new organisation in Munich concentrates purchasing activity for Information Systems, Network Infrastructure and Market Products; it has three objectives: to simplify purchasing processes; to improve relations with suppliers; and to exploit economies of scale by combining demand.

Munich was chosen as the centre for this new unit as many of the main suppliers in the sector are also based in this city. Its team consists of people from Telefónica's purchasing units around the world. This enables it to benefit from the experience and know how of all these professionals.

The new unit receives all purchasing requests for the three product areas mentioned from our operations all over the world and then negotiates global deals with suppliers, resulting in more efficient management, cost savings and simplified processes. The unit will be fully equipped with the tools it needs to function on line. For example, suppliers will submit all of their invoices electronically.

Progressing into an on line Company

In 2009, Telefónica continued working to develop into a company which is fully on line. The Company's objective is to increase the volume of transactions with customers which are performed electronically by 22 percentage points between 2008 and 2012. At the same time, it is continuing to develop more transparent and responsive relationships with suppliers, using on line auctions in a high proportion of its Purchasing processes.

For example, this philosophy of on line working is guiding the work of the new global purchasing unit established by Telefónica in Munich. This unit has enabled the Group to take advantage of economies of scale, which is something it is also achieving through synergies with its partners China Netcom and Telecom Italia.

Innovation for growth

Investment in R&D of 4,291 million euros

Managing innovation

As a result of the changes in the current economic environment, characterised by globalisation and technological convergence, innovation has become key in attaining Telefónica's targets of increasing revenue and optimising operational costs.

This model rests on three basic pillars: a **global innovation platform** with local application in business units, the development of capabilities aimed at securing **long-term business opportunities** and, lastly, offering a **global response** to competitors and partners.

Innovation Management Process

The objective of innovation management is to ensure that there is a portfolio of projects and investments in resources with high rates of return. We currently have in place an annual process to establish the innovation and transformation priorities based on a rigorous review of the Company's strategies, context, consumer and customer trends, emerging technologies, etc.

As a result, during this first year, in the Innovation Committee 12 global priorities were established for the 2010-2012 period, as

specific areas of focus to generate new revenues. In parallel, in the Transformation Area, 18 Global Priorities were established, focusing the company's efforts on technology and network capacities, platforms and specific, vital systems for the support and development of business in these highly important innovation areas.

In this Committee, the three regional business units are represented (Telefónica Spain, Telefónica Europe and Telefónica Latin America) and the corporate areas of Innovation and Transformation.

Research and Development

+4% year-on-year in R&D

R&D (research and development) activity continues to be a catalyst for technological innovation. In the course of 2009, Telefónica's total investment in technological innovation (R&D&i) amounted to 4,291 million euros. Of this amount, 693 million euros were invested in R&D, a 4% increase on 2008.

Telefónica's open innovation network



Investment in R&D&i of 4,291 million euros

As part of this effort in the area of R&D, Telefónica devoted 70 million euros to **"applied research"**, mostly intended for the conceptualisation and development of new services and the networks of the future. Moreover, during 2009, Telefónica R&D registered 57 patents in areas related to information and communication technologies.

The rest of the investment in R&D, i.e. 623 million euros, was mostly in the **development of new products**, services and management systems, as well as in introducing substantial improvements in those already in existence. A major part of this effort was in collaboration with leading companies in each sector. Some examples of these collaborative development platforms are the Morfeo Platform and Movilforum (Mobile Forum).

In the course of 2009, Telefónica also made a major effort in **technological innovation** in order to deploy the services and networks developed through R&D activities, with investment of 3,598 million euros. The two main lines were, on the one hand, measures to ensure the deployment of these innovations, and on the other, the implementation of fixed and mobile broadband networks in the countries where the Company operates.

Some of the projects developed by Telefónica R+D include Rehabilitic, Colabor@ in Chile and Spain, the platform for people with chronic illnesses, and Telecare Móvil, "Mi familia".

Global Products and Services

The goal of the Global Products and Services Development unit is to identify new products, services and applications and develop them on a unified basis for all the markets in which the Company operates.

The creation of a catalogue of global products and services is supported by specialised Competence Centres, based on four operating principles: developments by global units; dedicated resources and clear management rules; clear budgeting of expenses and investments; and alignment of global and local objectives and incentives.

The Company's Competence Centres (CCs) are global teams dedicated to working on specific projects by segment and type of service. Their new structure was approved in July 2009:

Basic Home Station

The Hogar Digital (Digital Home) Competence Centre has designed a new concept in ADSL customer user terminals (routers) called *Basic Home Stations*, which are a technological leap forward for Telefónica's customers. This development enhances user experience through its attractive design and easy-to-use interface.

The functionality of the *Basic Home Station* includes enhanced wireless coverage within the home, and the ability to share printers and USB hard drives on the home network. It also encourages users to take advantage of the full range of Movistar coverage by connecting the equipment to a USB modem with 3G connectivity.

1. People-oriented CC: Mobile Data group (MDG) in T. Europe.
2. Home-oriented CC: IPTV (TdE) and Hogar Digital, in Telefónica, S.A.
3. Company-oriented CC: Corporate ICT, in Telefónica España.
4. Cross-disciplinary CC: provides technological support to other CCs (New Access Services-NAS, in T. Spain).
5. Global project: Open Telefónica, in Telefónica, S.A.

New businesses

The mission of the new business unit is to develop and grow new businesses in new and complementary areas. It currently includes the e-Health, Financial Services, e-Learning, e-Travel and Security business lines.

The first two enable leveraging of the potential technological discontinuities that generate increased purchasing power in new areas. e-Learning and Travel and Security contribute towards the growth of existing businesses.

e-Health

The e-Health corporate unit was created as a result of strategic analysis of new business areas where Telefónica can contribute value to the societies where it operates. The global e-Health initiative divides products and services into three categories (ICT, Telemedicine and Teleassistance) and has been implemented on

Colabor@

Colabor@ is a system developed in the Granada centre of Telefónica I&D, which facilitates collaboration in real time between health care professionals. Its goal is to improve the service to patients and to facilitate the work of professionals by applying ITC to medicine. The Granada centre has more than 50 employees dedicated to innovation and is a pioneer in the development of products and services in the areas of health and tele-assistance.

The system is a simple, agile tool, which allows for the establishment of virtual work sessions which permit medical professionals to share information in real time. Using the capacities offered by multimedia communication, doctors can interact with one another to solve complex cases; hold daily sessions to cooperate and exchange opinions; set up sessions between professionals of a health centre or a geriatric centre with hospitals to treat cases they have in common; or carry out tele-diagnostics via video conference or other methods.

During 2009, Colabor@ was awarded the "Innovation in Telecommunications" prize of the revista Muy Interesante

a global scale throughout Telefónica, with a presence in Spain, Europe and Latin America.

Examples of the activity of this unit include the iPhone application for people with autism developed by Telefónica O2 Ireland, based on communication through images.

Financial Services

In 2009, Telefónica worked to develop financial services using mobile phones. Telefónica's objective is to enable new forms of access to funds and ways to control accounts at low cost; this is generating significant revenues for the Group in Europe and Latin America.

For example, in the United Kingdom Telefónica signed an agreement involving Natwest and O2 in 2009, launching its first pre-paid cash card –the O2 Money Card– based on the concept of spending control and freedom. The card operates through a system of alerts received on the customer's mobile phone and will result in a substantial increase in loyalty among UK customers.

e-Learning

Telefónica Learning Services –until recently known as Educaterra– has 9 years' experience in the market and over 150 clients, including private companies and public bodies. Its main focus is in Spain, although it is currently expanding its presence and services to the other countries in which Telefónica operates.

Mobile Banking (Colombia)



This Mobile Banking pilot project for coffee growers was developed in collaboration with the Federation of Colombian Coffee Growers and Banco de Bogotá. Its purpose is to enable users to carry out financial operations with their coffee cards. The card can also be used to consult coffee prices, balances and the most recent credits to the card. The towns of San Gil, Río Sucio, Socorro and Quinchía were the first to join the scheme, which benefited 5,000 coffee growers up to the year 2009 and registered a total of 1,300 transactions in the first month alone.

e-Travel

A 50-50 joint venture between Telefónica and Orizonia, Rumbo is now active in Spain, Portugal, Argentina, Brazil, Colombia and Venezuela. The two basic pillars of its success are technological innovation and quality customer service. In order to expand its most popular area of business –sales of flight tickets– Rumbo Negocios was launched in 2009; this is a specialist website for business travel which enables SMEs and large customers to achieve savings through low-cost package offers. In 2009, Rumbo recorded revenues of 455 million euros, up 11% on the previous year, with a 28% jump in the number of customers.

Venture Capital

Telefónica has a venture capital fund for investing in companies with strategic capabilities (products, services and technology) for Group businesses. The main objectives of the fund are promoting new businesses and acquiring knowledge of new and emerging technologies. The minority shareholdings of this fund are centred in Silicon Valley and Israel.

This search for new opportunities benefits from carefully nurtured relationships with a number of global venture capital leaders, such as Sequoia, Benchmark and Draper Fisher Jurvetson.

Some of the companies currently in the portfolio include "Amobee" ("Mobile Advertising") and "Kyte" (a video platform).

Assia



"ASSIA is proud of having Telefónica as a strategic investor and an observing member on its Management Board. ASSIA considers Telefónica to be one of the global leaders in telecommunications innovation and it hopes to be able to roll out its solutions through the Group and to combine innovation efforts to increase the global leadership of the Telefónica Group's broadband DSL networks". (John. M. Cioffi, CEO ASSIA)

In 2009, an investment of \$5 million was made in "Assia." This company is a global leader in DSM technology with more than 200 patents. These technologies make it possible to increase the quality and scope of DSL services over traditional copper networks, thus enhancing customer satisfaction and service capacity.

optimises the use of network resources, minimising impact on the existing infrastructure. Secondly, it enables Telefónica to play a role in the "content delivery" market, which is currently led worldwide by companies such as Akamai. In addition, it makes it possible to offer exceptional quality of service to our broadband customers that sets us apart from our competitors, both for content managed by Telefónica and OTT content.

The funds allocated to the project in 2009, which amount to 500,000 euros, have enabled the development of in-house CDN technology (T I+D) and the establishment of a pilot project at 60 points in 10 countries. The estimated commercial launch date for the service is the third quarter of 2010.

Acquisitions

Acquisitions are an important tool for incorporating emerging technologies and innovative services into the Group's capacities in order to develop complementary businesses.

This is demonstrated by the acquisition of Jajah in 2009. This acquisition was a major leap forward for Telefónica's VoIP capabilities.

Best practices as leverage for innovation

The sharing of best practices among business units provides another lever for effective innovation in Telefónica, allowing for the immediate application of local profits and increasing these profits with lower investment of resources in implementation.

Incubators

The incubator initiative focuses on looking within Telefónica to support the entrepreneurial skills of the Company's employees, providing their new ideas with the resources required to bring them to fruition. The incubators make innovation more democratic, taking advantage of Telefónica's diversity and knowledge in its more than 255,000 employees. Anybody in the company with a good idea and an entrepreneurial spirit can develop a new business.

NFC technology

Near Field Communication technology enables fast, easy payments using mobile phones, by equipping them with a built-in credit card. Incubation funds have been used to develop a user-friendly interface for customers and pilot studies have been carried out in various countries to perfect the project and evaluate it in real-life situations.

Hybrid CDN

The CDN initiative has a number of simultaneous objectives. Firstly, it proposes a system for managing video traffic that

Telefónica acquires Jajah, a leading company in IP Communication



In 2009, Telefónica announced that it had acquired Jajah, a leading communication innovator headquartered in Silicon Valley, California and Israel, for 145 million euros (207 million dollars).

Jajah offers integrated VoIP services, instant messaging with social networks in nearly 200 countries. Its solutions for the business segment include integral IP communications services for the entire organization, regardless of the location or device.

Trevor Healy, CEO of Jajah, has said, "This is a very exciting union of a young, innovative company with one of the largest integrated communications companies in the world. Together, we look forward to creating the next generation of communication."

Solid, reliable brands

Movistar and O2 hold first or second place in international rankings of brand recognition

A new brand model

In early 2009, Telefónica approved a new brand model for the entire Group, a model that was first introduced in Spain in May 2010 and which will be implemented in all the countries where the Telefónica Group operates over the course of the next two years. There is no doubt that it will be one of the fundamental pillars on which its future growth will be based.

The new brand model is based on the Company's business vision and, being primarily focused on the customer, it evolves to meet their needs, which are in turn developing in to an increasingly convergent and global environment.

With a view to strengthening the position of the Telefónica Group and leveraging future opportunities, the current brand model, which is heterogeneous and based on growth and acquisitions, is being rearranged into a simplified regional model, which is capable of speaking with a single voice to each target audience.

The Telefónica brand will be used for all corporate and institutional roles in all geographical areas, while Movistar and O2 will embody the Company's commercial offer in their respective geographical areas: Movistar for Spain and Latin America, and O2 in the UK, Ireland, Germany, the Czech Republic and Slovakia.

This new model maximises the value of the brands and gives them the flexibility needed to adapt to the new realities of the markets. The new brand model is a key element in transforming the organisation and building an even more closely integrated Group.

The institutional brand

The Telefónica brand represents the Company at the institutional level, in dealings with institutions, shareholders and investors, multinationals and large accounts, society and employees in all the countries where the Group operates.

The objective of this new role is to support the new strategic stage the Company is entering and to raise the institutional profile of Telefónica, making it more global, more powerful and more resonant for its various audiences, as the link that unites and brings together all the Company's brands and the brand that unites all employees.

Telefónica's new corporate vision, expressed as "The Power to Transform", is based on a tradition of more than 85 years of history. A legacy of growth, innovation, transformation and value creation for the Company's audiences.

The new commercial brands –Movistar and O2– have the support and backing of the financial strength of Telefónica S.A, together with the business vision and the talent of a committed organisation with over 250,000 employees.

The new role of Telefónica as a brand is reflected in a highly evolved visual identity that is in line with the new brand strategy. Thus, we are keeping the current logo, the corporate colours are changing to a darker, premium shade of blue, with a view to reinforcing the relevance and importance of the brand's institutional role.

Commercial brands

Under the new brand model, the Telefónica Group's commercial offering will be embodied in the Movistar and O2 brands, both of which are clearly focused on the customer.

This will drive the integrated carrier model, with an integrated range of products and services in an environment that is increasingly convergent and competitive; this will make it possible to simplify and streamline the customer experience, creating emotional ties that strengthen the commercial brands compared to our competitors and enable greater efficiency in marketing and communication.

Movistar. "Life is better when you share it"

The new Movistar, with its range of capabilities, is the stage for this new reality for Spain and Latin America.

Movistar, with a single voice for both private customers and businesses, brings together for the first time all the capabilities of its world-leading integrated range, placing the customer at the heart of all the Company's activity, thereby building strong emotional ties and lasting relationships.

This has meant that the Movistar brand has had to be repositioned with the help of a brand concept ("Life is better when you share it"), as well as values and a personality that will help to build up



A single voice for each target audience

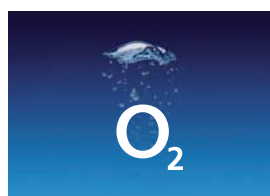


positive differentiation from its competitors; intensify ties with customers; and reorganise the portfolio of products and services to match the new reality of the brand architecture, creating a system that can respond to developments in the sector.

Movistar as a brand has matured, becoming the Company's commercial brand in Spain and Latin America for all its products and services, both fixed and mobile. Therefore, as a pragmatic response to the current situation, its visual brand identity has evolved and become more formal, more adult and more mature. This change responds directly to the new business strategy and the new brand model.

02. Looking towards Europe

The O2 brand is being maintained for our mobile and fixed telephony and broadband services in the United Kingdom, Ireland, Germany, the Czech Republic and Slovakia. Under this new brand model, O2 will have closer links with other Telefónica Group brands. Brand values: Bold, Open, Trusted and Clear are relevant to their markets and consistent with both the Movistar brand and with the institutional brand



Leading the rankings

Both Movistar and O2 occupy top positions in the international rankings for brand presence and recognition. The new approach will reinforce this position and strengthen the institutional brand, extending its presence in all geographical areas.

On a highly selective basis, other brands, such as Terra, Atento and Fonic, may be used in areas not covered by our main brands, Movistar and O2, or where there is no interest in using them.

In order to ensure effective implementation of this model, the Company has implemented Brand Guardianship, which will ensure consistency in all applications and decisions in connection with the brands.

Brand recognition

Spontaneous recognition of the Telefónica brand (data for 2009).

Fixed Telephony

Country	Ranking
Spain	1
Chile	2
Peru	1
Argentina (Broadband)	1
Colombia *	2

Mobile Telephony

Country	Ranking
Spain	1
Chile	1
Peru	2
Argentina	2
Mexico	2
Uruguay	1
El Salvador	1
Guatemala	1
Nicaragua	1
Venezuela	1
Colombia	2
Ecuador	1
Panama	1
Ireland	2
Slovakia	3
Czech Republic	1
UK	2
Germany **	3

Data obtained from the Millward Brown TPSM (ATP), based on accumulated totals for 2009.

* Data for Telefónica Telecom.

** Data obtained from the KANTAR Group's ICON Added Value study (part of the same group as Millward Brown).

The commitment of an experienced team

Our employee climate and commitment index is 73%

Workforce

257,426 employees in 25 countries

At the end of the financial year 2009, the Telefónica Group had a workforce of 257,426 employees in 25 countries. Overall, the size of the workforce remained stable compared to 2008.

By regions, Latin America has the largest percentage of the Telefónica Group's workforce (68%), followed by Spain (20%) and Europe (11%).

If Atento is not included, Telefónica's workforce is mainly divided between Commercial and Production roles, which account for 41.2% and 46.5% of the total respectively. The remaining 12.3% are involved in support functions.

97% of the equivalent workforce have permanent contracts with the Company; if Atento is included, this percentage is 84%.

Women account for 36% of the Telefónica Group's workforce; this figure increases to 50% if Atento is included. The percentage of women in management roles in 2009 was 21%, compared to 17% in 2008, as a result of Telefónica's commitment to equal opportunity and diversity.

Employee commitment

ICC: 73% (+4 p.p. year-on-year)

In 2009, the employee climate and commitment index, which is calculated in the same way in all countries, stood on average at 73%, a 4 point increase on the previous year, exceeding the objective set. Over the last 3 years this index has increased by 7

percentage points. Regionally, the largest increase has been in Latin America, which has increased by 6 p.p. to 83%. This is followed by Spain, which has seen a 5 p.p. increase to 60%. Europe, with an CGI of 76%, has been stable over the last three years, having increased by 1 p.p. in 2009.

The main causes of this increase in labor climate are the results of the Company's transformation and management programmes in Business Units in Spain ("GPS", featuring the "Team Satisfaction" initiative) and Latin America ("Ahora", launched in 2007), that have developed focused, goal-based management, which has reinforced the sensation of teamwork and leadership.

Best Place to Work

22 Group companies included in ranking

As a result of this increase in employee satisfaction, in 2009 the various business units were recognised as being "best places to work".

In Latin America, the number of Group operators in the "Great Place to Work Institute" rankings increased from 17 in 2008 to 22 in 2009, achieving first place in Uruguay, Ecuador and Venezuela.

In Europe, Telefónica achieved first place in the "Best Place to Work" ranking in Germany, second place in Ireland (and best company in the Telecommunications sector), and 16th in the "Best Big Company to Work for" in the UK (awarded by the Sunday Times).

Telefónica España has received a number of awards which recognise the Company as one of the best places to work. These include the "Top Company to Work For" (awarded by the "CRF

Workforce by region

	2009	2008	2007	Change % 09/08
Spain	52,060	52,576	53,300	-1.0
Latin America	175,350	173,014	164,231	1.4
Europe	27,964	29,349	29,310	-4.7
Rest of the world	2,052	2,096	1,646	-2.1
Total	257,426	257,035	248,487	0.2

The Company has over 257,000 employees in 25 countries

Institute"); 8th place in the general "Mercopersonas 2009" rankings; second place in the international "Best Company to Work For" ranking; and first place in the Actualidad Económica ranking (produced by Iberinform), awarded to Telefónica S.A.

Training

63 Million € (+4% year-on-year)

Training is the basis for excellent performance. In 2009, Telefónica invested more than 11 million hours of training, compared to more than 10 million hours in 2008, an 18% increase. In 2009 the Company invested 63 million euros in training.

Universitas Telefónica, which opened in March 2009, plays a key role in training. It is located in an excellent position some 40 km to the north of Barcelona, on an 18,000 m² campus; it has excellent residential facilities, including 180 rooms, and numerous classrooms.

The mission of Universitas Telefónica is to promote the continuous development of the Company's professionals; to promote a distinctive style of leadership; and to disseminate business strategy through teamwork and the exchange of knowledge and best practices in the markets where Telefónica operates.

In 2009 it ran 19 programmes focusing on competencies in the Telefónica Leadership Model 51 times; these courses were attended by 1,395 professionals who returned an overall satisfaction level of 8.7 out of 10. An additional 28 corporate events were organised as supplementary activities for a total of 1,178 attendees.

Talent Management

Talent management in Telefónica aims to reward, develop and retain the skills which will guarantee sustainability of the business. In order to achieve this, Telefónica's Competences model is adapted to business needs, with six key areas having been identified for senior management posts.

The second round of 360° evaluation at the senior management level was held at the end of 2008 and start of 2009, with the same

questionnaire being used in all regions. In Telefónica España and Telefónica Latin America, the rate of completed reports was 99%; in Telefónica S.A. and subsidiaries it was 97% and in Telefónica Europe, it was 96%.

Mobility

Telefónica is aware of the possibilities it has as a global Company to develop an international network. In 2009 it completed implementation of its International Assignment Management Model. 57% of international movements have been long-term (2-3 years); 3% have been short-term (up to 12 months); and 40% have been rotations.

In terms of transparency, in 2009 55 senior management vacancies were advertised globally, of which 25% were filled by candidates from Group businesses, and 95% were expatriates.

Workplace dialogue and collective agreements

186.970 workers covered by collective contracts (73%)

In 2009, the Company's Business Principles, together with its Social Protocols of International Agreements and Code of Conduct (which were renewed and signed in December 2007, between the Union Network International (UNI) and the UGT and CCOO unions and Telefónica), were the main reference points in its workplace dialogue, particularly with regards to rights of association, participation and collective contracts.

In 2009, over 72% of the workforce –some 186,970 employees– were covered by collective agreements.

In Spain in 2009, the companies with the largest numbers of employees continued to apply the agreements which were already in place, applying continuous negotiation mechanisms to ensure on-going workplace dialogue during the life of such agreements.

The right alliances and partners

The boost from alliances reinforces the Company's leading position

Strengthening alliances

The Company's strategic alliances have enabled it to strengthen its leadership position. These alliances enable the Company to reach 650 million customers worldwide, which represents approximately 10% of the world population.

During 2009, the strategic alliances signed by the group were given a significant boost. Firstly, we decided to create a specific area at the level of Telefónica S.A. with the fundamental mission of optimising the management of these alliances with a common perspective and leadership.

Starting in June, the Strategic Alliances and Industrial Holdings Directorate made quantitative and qualitative progress in these aspects of management. These decisions translated into specific initiatives in terms of control of shareholding and industrial management with Telefónica's partners: Telecom Italia and China Unicom.

At the end of the year it was also agreed to extend this operational model of maximising synergies to other markets where the Group does not operate. The ultimate goal is to leverage the scale attained by the Group with third party carriers under a strictly commercial relationship model

Telecom Italia

Indirect shareholding of 10.49%¹

In October 1997, Telefónica joined a group of Italian institutions (Generali, Mediobanca, Intesa Sanpaolo and Benetton) to form the Telco consortium with the aim of acquiring a significant package of ordinary shares in Telecom Italia.

This investment has enabled the Group to become the majority shareholder in the aforementioned consortium and to lay the groundwork for the development of a significant programme of operational synergies with a view to enhancing the mutual scale of both companies by implementing the best commercial and operational practices.

¹ Telefónica owns an indirect shareholding of approximately 10.49% in the ordinary share capital (with voting rights) of Telecom Italia through Telco. If we add Italian preference shares (azioni di risparmio), which do not have voting rights, the indirect shareholding of Telefónica in Telecom Italia is 7.21%.

In October last year, Telefónica and its partners Generali, Mediobanca and Intesa San Paolo agreed to renew the shareholders' agreement to extend the agreements already in place for an additional period of 3 years until April 2013. As a consequence of Sintonía's separation at its own request, Telco acquired control of 22.45% of the ordinary shares of Telecom Italia, thereby giving Telefónica (which owns 46.2% of the company shares) an indirect holding of 10.4% of the ordinary share capital of Telecom Italia.

As a result of the industrial alliance with Telecom Italia, relations have continued to intensify in order to achieve the 1,300 million euros in synergies mentioned previously. By the end of 2009, synergies to the value of 620 million euros had already been captured. 90% of these synergies have been achieved in the Purchasing, Technology and IT departments and from wholesale agreements between the two companies in Germany.

It should be noted that for regulatory reasons, all joint activity specifically excludes Group operations in Brazil and Argentina.

China Unicom

8.37% shareholding

Telefónica has had a permanent presence in China since 2005, when Telefónica entered into a strategic alliance with the fixed carrier China Netcom Corp and acquired a 5% holding in its share capital.



Chang Xianbing, Chairman of China Unicom and Cesar Alierta, Executive Chairman of Telefónica

Through its alliances, the Company reaches 650 million customers

In May 2008, the Chinese Government announced its intention to carry out a broad-ranging restructuring operation of the telecommunications sector. As a result of this, China Netcom Corp. merged in October 2008 with the mobile carrier China Unicom, giving rise to the fourth largest group worldwide in terms of the number of customers. On that date, César Alierta, Executive Chairman of Telefónica S.A., was elected as a member of the Board of Directors of China Unicom.

In January 2009, during the State Visit of the Chinese Premier Wen Jiabao to Spain, and in his presence of the latter and that of the President of the Spanish Government, the Executive Chairmen of Telefónica, César Alierta, and of China Unicom, Chang Xiaobing, signed a first Framework Agreement for Cooperation.

As a result of the close ties between the two companies, on 6 September 2009, Telefónica and China Unicom announced a broad-ranging Strategic Alliance and a Share Exchange Agreement to the value of 1,000 million US dollars.

This alliance by Telefónica was given wide coverage in the international press and media, as it was the first time that a Chinese telecommunications company had acquired a holding in a foreign company.

Shortly after this agreement was signed, on 25 September 2009 China Unicom announced an agreement with the Korean operator SKT to acquire and subsequently cancel the shares it held in China Unicom. At the same time it ended its strategic alliance with this carrier.

As a result of these operations, Telefónica increased its holding in China Unicom to 8.37% of its capital, consolidating its position as the largest foreign shareholder, while China Unicom's holding in Telefónica amounted to approximately 0.9%.

In addition to these corporate transactions, both companies have been developing the Strategic Alliance resulting in major advances in technology, joint purchasing, joint provision of services to multinationals, roaming and joint training for managers in both companies.

A privileged partner in the new digital ecosystem

Telefónica's scale and position in the value chain of the Information and Communication Technologies (ICT) sector mean that it is a perfect ally in the digital world. In order to embrace the opportunities deriving from this situation, in 2009 the Company increased its collaboration with third parties in several fields: innovation, where it strengthened the concept of "Open Telefónica" in order to innovate in collaboration with companies, developers, customers and employees..., marketing, networks, processes... Agreements were signed with companies in the sector and with partners from other sectors.

In 2009, the Company continued to invest in alliances with other internet companies, contents, devices and outsourcing. Some of the most recent agreements are with Microsoft, HP, Nokia, Dell, LG and Yahoo!

For Telefónica, collaboration with other carriers was also of crucial importance. In this regard, mention should be made of the agreement with Vodafone to share mobile network assets in various countries in Europe, and the alliance signed in 2010 with the main carriers to create the WAC (Wholesale Applications Community) platform, which will allow developers to create applications and offer them to a massive customer base of over 3,000 million people.

In addition, Telefónica is considered a privileged partner in the new digital ecosystem for establishing strong intersectoral alliances to make advances in key areas such as education, healthcare, finance, climate change, etc.

Alliances with other sectors



Excellent performance in sustainability

Telefónica scored 86 points in the DJSI (+28p.p. above the average of the Telco sector)

Leading sustainability

In 2009 Telefónica was recognised as the leading global telecommunications company by the Dow Jones Sustainability Index (DJSI). In its annual review, the Ratings Agency evaluates the sustainability of companies –Sustainable Asset Management (SAM)– based on economic, environmental and corporate issues; it awarded Telefónica a score of 86, which is 28 percentage points higher than the average for the sector.

For the DJSI, "Corporate Sustainability is a business approach that creates long-term shareholder value by embracing opportunities and managing risks resulting from economic, environmental and corporate issues".

Among the key aspects, Telefónica was recognised for having the best risk management practices; the best Corporate Social Responsibility coverage of suppliers; its contribution to the reduction in the digital divide; the impact of its telecommunication services on the societies in which the Group operates; brand management; and its business, anti-corruption and social action principles.

Dow Jones Sustainability Index Global leaders in the sector

DJSI World, GLOBAL SUPERSECTOR LEADERS (2009/2010)

Name	Sector
Bayerische Motoren Werke AG (BMW)	Automobiles & Parts
Australia & New Zealand Banking Group Ltd	Banks
Xstrata PLC	Basic Resources
DSM NV	Chemicals
Panasonic Electric Works Co Ltd	Construction & Materials
Itausa-Investmentos Itau	Financial Services
Unilever	Food & Beverage
Roche Holding AG	Health Care
TNT N.V.	Industrial Goods & Services
Swiss Re	Insurance
Pearson Plc.	Media
Total SA	Oil & Gas
adidas AG	Personal & Household Goods
GPT Group	Real Estate
Kingfisher Plc	Retail
Nokia Corp.	Technology
Telefónica, S.A.	Telecommunications
Sodexo	Travel & Leisure
Cia Energetica Minas Gerais (CEMIG)	Utilities

Source: http://www.sustainability-indexes.com/07_html/indexes/djsiworld_supersectorleaders_09.html

Economic Dimension

In terms of economic issues, Telefónica received a score which was 31 percentage points higher than the average for the sector. This made the Group the best company in the telecommunications sector for this area, which includes aspects such as customer relationship management; privacy; risk management; corporate governance; and business, anti-corruption and brand management principles.

Telefónica was judged to have best practices in 3 of these categories: risk management, brand management and management of business and anti-corruption principles. This was achieved by the Telefónica Group's implementation of a single risk management model in all the countries in which it operates, together with inclusion in this of aspects related to sustainability, development of a single brand strategy and its efforts to guarantee integrity through internal regulations and training employees in Business Principles.

Environmental Dimension

In this area the Group scored 19 percentage points more than the average for the sector. This area covers issues such as environmental policies, eco-efficiency, environmental information and climate change.

Telefónica has made progress in these areas through its strategy to combat climate change, which has reversed the downward trend in 2008 with a 34 percentage point increase. The Climate Change Office is enabling Telefónica to implement a more effective global energy efficiency management model; and to reduce its energy consumption and, as a result, its CO₂ emissions. This Office focuses on five areas: Operations, Suppliers, Employees, Customers and Society.