Telefónica España: Solid performance, strong trends

Antonio Viana-Baptista
General Manager
London, June 6, 2007
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01 Benchmark set of results in 1Q07

02 Set to continue delivering a premium performance

03 Differential strengths to exploit market opportunities
There are sceptics about the sustainability of our superior performance.

Analysts report 1Q07

“France suffered in 2005, Germany in 2006... Spain should be next...”

“TEF is facing increasing pressure from regulators and competitors, specially in its home market”

“We are concerned that a weakening domestic economy could compound more meaningful competition in fixed. In mobile the risk to revenues from renewed price pressure has substantially escalated”

“Spain is not that different from other EU markets”
01 Our view

- The Spanish economy maintains its strength:
  - +4.1% GDP growth in 1Q07
  - Growing population

- We have been consistently proactive in the market, unlike others:
  - Shaping the market:
    - Aggressive customer acquisition strategy
    - High performance loyalty tools to sustain benchmark churn rates in wireless and to enhance loyalty in wireline
  - Launching innovative solutions to foster usage
  - Leading price reductions in wireless to position our on-net offer as the most competitive in the market
  - Maintaining a quality premium

We continued to deliver a benchmark set of results in 1Q07
Shaping the market, both in wireline ...

### Retail Internet BB Accesses
- **(in millions)**
  - Mar06: 3.0
  - Mar07: 4.0
  - **+31%** y-o-y growth

- 56% market share, stable vs. Dec06
- Promoting 2P/3P

### Pay TV subscribers
- **(in millions)**
  - Mar06: 0.25
  - Mar07: 0.42
  - **+67%** y-o-y growth

- 44% share of net adds
- 11% market share

### Fixed Telephony Accesses
- **(in thousands)**
  - Dec06: 15,950
  - Mar07: 15,920
  - **-1.2%** y-o-y growth

- Market y-o-y growth: 2.2%
- Positive results from free subscription fee campaign

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... and in wireless ...

**Customer growth (1Q07 y-o-y)**

- **Total**
  - >21.8M
  - +7.6%
  - +0.6%
- **Pre-pay**
- **Contract**
  - +13.4%

- 57% of customer base in contract (+3 p.p.)
- Total net adds: 368,000 in 1Q07
- Blended churn: 1.8% in 1Q07 (-0.1 p.p. vs. 1Q06)
- Positive results in number portability

**Contract segment (1Q07)**

- 668,000
  - Gross adds: +8%
  - Churn: 1.1%
  - Net adds: +13%
  - -0.2 p.p.

- 387,000
  - +13%

**1Q07 contract churn**

- 13.3%
  - -2.8 p.p.
- 16.6%
  - +2.5 p.p.
- 28.3%
  - +3.4 p.p.

**1Q07 contract net adds (000)**

- 387
  - +13%
  - -21%
  - -60%
- 336
  - 44

1 Sources: press releases from companies. Rolling 12M data for Orange.

**Solid customer expansion**

**Focused on value customers**

- Residential handset upgrades: +13%
- Long term contracts
... maintaining market share despite the competitive environment

Share of wireless net adds

- **Telefónica**
  - 34%

- **Orange**
  - 40%
  - -9 p.p.

- **Yoigo + MVNOs**
  - 14%

1Q07E market shares

- **Customers**
  - >45%
  - ~50%

1Q07E market shares

- **Outgoing customer revenues**
  - ~2.5x

Yoigo & MVNOs launch

<table>
<thead>
<tr>
<th>SPAIN (Yoigo + MVNOs)</th>
<th>SLOVAKIA (Telefónica)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Population</td>
<td>45MM</td>
</tr>
<tr>
<td>Penetration at launch</td>
<td>104%</td>
</tr>
<tr>
<td>Launch</td>
<td>Nov. 06</td>
</tr>
<tr>
<td>1Q07 customers</td>
<td>~155K</td>
</tr>
</tbody>
</table>

Sources: Telefónica estimates based on press releases from companies and internal estimates for MVNOs. Data for Orange excluding the impact of Euskaltel.

* Excludes loyalty points

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Launching innovative solutions to foster usage across businesses ...

- 1st European Telco to launch IPTV (Imagenio)
- Pioneers in the deployment of BB VAS
  - 3.2MM BB VAS
- Integrated solutions for SoHo & SMEs
- Tailor-made ICT solutions for corporates
- Pioneer in the introduction of m-ticketing in Spain
- Mobilization of business applications
- Innovative /simpler pricing schemes to drive usage ...
... that is bearing fruit ...

**Wireline**

**ARPU**

(€/month)

<table>
<thead>
<tr>
<th></th>
<th>1Q06</th>
<th>1Q07</th>
</tr>
</thead>
<tbody>
<tr>
<td>62</td>
<td>66</td>
<td></td>
</tr>
</tbody>
</table>

+6.7%

- 25.1% of lines have BB (18.9% in 1Q06)
- 75% of retail BB accesses with 2P/3P
- Retail BB VAS ARPU: €7.7

**Wireless**

**ARPU**

(1Q07/1Q06 change)

- 6.9% MTR cut in Oct.06.
- +5.8%
- -0.4%
- -0.5%

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th>Total (1)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Incoming</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>-4.7%</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Outgoing</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>+5.3% growth in outgoing MOU</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

(1) Excludes roaming-in
... with a strong trend in wireless data ARPU

Fostering Data ARPU growth ...

Outgoing data ARPU y-o-y growth

- 1.5%
- 5.8%
- Highest y-o-y growth since 4Q05

1Q06 2Q06 3Q06 4Q06 1Q07

1Q07/1Q06 Data Revenue growth

- +27% Non P2P SMS revenues
- +71% Connectivity
- +14% Total

Data revenues split

- P2P Comm. 33%
- Content 59%
- Connectivity 8%

- +25% in advanced data users (vs. Dec06)
- +25% in Data Flat Rates (vs. Dec06)
- Data traffic x4 (1Q07 vs. 1Q06)
- ~1.5M 3G devices (~220,000 PC Cards)

... based on connectivity & content development
We have led price reductions in wireless to position our on-net offer as the most competitive in the market...

- Aggressive reductions in ARPM in the market: -34% in 2001-2006
- Movistar pricing schemes have been always very competitive

Capitalising our scale:
- Biggest on-net community: >45% market share
- 4.8MM customers with on-net plans:
  - 70% in contract (vs. 57% of total base)
  - 45%-50% lower churn
  - Above average ARPU

- Cheapest on-net price in the market: €0.01/min
- “Mis Cinco”: €0.03/min. (on-net and fixed)
- On-net prices to other movistar numbers abroad
- Uno Familiar (wireline and wireless): €0.03/min

Source: CMT / INE
... and in 2007 “we are not resting on our laurels following the strong first quarter”

New voice and data pricing to stimulate usage & increase loyalty

- Best rates for wireless internet
- Targeted at non intensive Internet Users
  - 1€/10 Mb contract
  - 3€/10 Mb prepay

Simplified offer (4 options)
- Leveraging “community effect”:
  - €0.03/minute contract on-net calls (€0.30/min off-net)
  - €0.05/minute pre-pay (€0.59/min off-net)
- Opt-in

Factored in guidance

New daily rate for wireless internet

April

New tariffs for residential customers

May

New tariffs for SOHO and SMEs

May

1 Fidentiis. May 18, 2007
Maintaining a quality premium

ADSL: Broadband Speed test
1 Mbps connections (Kbps)

Source: Asociación de Internautas (AI). 2007

Global satisfaction index (2006)

Source: Telefónica, based on external surveys

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London, June 6, 2007
01 Our proactive operating approach allowed us to post a benchmark set of results in 1Q07

Telefónica España

**Total accesses**
- Mar07: 44.8
- +5.5%

**Revenues**
- 1Q06: 4,772
- 1Q07: 5,033
- +5.5%

- Internet and BB revenues: +22.3%
- Data & IT revenues: +8.9%
- Wireless customer revenues\(^1\): +8.4% vs. +7.6% in customer base
- Incoming wireless revenue\(^1\): -0.5%

**OIBDA**
- 1Q06: 2,205
- 1Q07: 2,439
- +10.7%

**OIBDA Margin**
- 1Q06: 46.2%
- 1Q07: 48.5%

- Lower ERE provision vs. 1Q06
- Wireline underlying growth: +4.7%
- Stable margin in wireless: 44%

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(1) Comparable growth rates. Pre-pay sales and top-up commissions are accounted for as costs in 1Q07 (netted from revenues in 1Q06). Revenues/costs of portability transit routing are now registered for their net amounts.

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London, June 6, 2007
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TELEFÓNICA ESPAÑA
London, June 6, 2007

01 We have delivered a superior operating performance …

Fixed lines y-o-y losses
Jan-March 2007/2006

Wireline (domestic markets)

<table>
<thead>
<tr>
<th></th>
<th>BT</th>
<th>FT</th>
<th>DT</th>
<th>TI</th>
<th>TEF</th>
</tr>
</thead>
<tbody>
<tr>
<td>Jan-March 2007/2006</td>
<td>-9%</td>
<td>-7%</td>
<td>-6%</td>
<td>-6%</td>
<td>-1%</td>
</tr>
</tbody>
</table>

Retail BB market share y-o-y change
Jan-March 2007/2006

Gap in wireless market share vs. #2
March 2007

Wireless ARPU y-o-y change
Jan-March 2007/2006

<table>
<thead>
<tr>
<th></th>
<th>TIM</th>
<th>T-Mobile</th>
<th>OGE</th>
<th>TEF</th>
<th>VOD UK</th>
</tr>
</thead>
</table>

Source: Company press releases; ML European BB and Wireless matrix (May 2007)
BT and Vodafone: April 06-March 07 y-o-y comparison
01 ... maintaining our differential profile

**Wireline (Jan-March 2007 y-o-y growth)**

<table>
<thead>
<tr>
<th>Domestic markets</th>
<th>Revenue</th>
<th>EBITDA</th>
</tr>
</thead>
<tbody>
<tr>
<td>Telecom</td>
<td>-6.8%</td>
<td>n.d.</td>
</tr>
<tr>
<td>T-Telekom</td>
<td>-5.8%</td>
<td>-19.2%</td>
</tr>
<tr>
<td>Orange</td>
<td>0.9%</td>
<td>n.d.</td>
</tr>
<tr>
<td>BT</td>
<td>3.0%</td>
<td>3.0%</td>
</tr>
<tr>
<td>Telefonica</td>
<td>3.6%</td>
<td>4.7%</td>
</tr>
</tbody>
</table>

**Wireless (Jan-March 2007 y-o-y growth)**

<table>
<thead>
<tr>
<th>Domestic markets</th>
<th>Revenue</th>
<th>EBITDA</th>
</tr>
</thead>
<tbody>
<tr>
<td>TIM</td>
<td>-0.2%</td>
<td>n.d.</td>
</tr>
<tr>
<td>T-Mobile</td>
<td>-2.6%</td>
<td>-11.4%</td>
</tr>
<tr>
<td>Orange</td>
<td>-0.1%</td>
<td>n.d.</td>
</tr>
<tr>
<td>Vodafone</td>
<td>1.5%</td>
<td>-10.1%</td>
</tr>
</tbody>
</table>

**Superior growth, profitability and disclosure**

TI: TI Domestic Wireline (excluding European Broadband project). Organic EBITDA.
DT: Domestic Wireline business = BBFN Germany + T-Systems (T-Systems includes non-domestic operations). Adjusted OIBDA.
FT: Domestic Wireline business=Home France+Business (Business includes non-domestic operations).
BT: Jan-March 2007 vs. 2006 periods for BT Consolidate Group. EBITDA before specific and leaver costs.
Vodafone: April 2006-March 2007 y-o-y growth for Vodafone UK
TEF: Underlying EBITDA growth for wireline division
1Q07 results crystallize confidence in our execution capabilities to successfully face our challenges

Analysts reports post 1Q07 results

"Spanish business particularly strong, which should reduce market concerns on BB competition and Yoigo impact"

"The strength in Spain allays fears held by some that the Spanish market is now ex growth as competition hits"

"Spanish business confounds the skeptics ... This should re-assure those worried that the increase in competition with the launch of Orange, the entry of a 4th player in mobile and of MVNOs would hurt TEF"

"Spain good. Telefónica bears will find little here."
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01 Benchmark set of results in 1Q07

02 Set to continue delivering a premium performance

03 Differential strengths to exploit market opportunities
High growth potential in our market

- Strong momentum in telecoms

- Favourable macro context
  - GDP growth above Euro-zone average: +3.2%
  - Population growth: +1.1%
  - Sustained growth in businesses and freelancers: +3.6%
  - Household increase above population growth: +700,000

Total market customer revenues (€Bn)

- 2005: 25.6
- 2006E: 27.4
- 2007E: 27.95 (27.4 + 6%)

Source: INE, Telefónica

London, June 6, 2007
## Strong opportunities to capture

<table>
<thead>
<tr>
<th>We have enjoyed great successes ...</th>
<th>... but we still have long way to go</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Almost 4MM ADSLs accesses</strong></td>
<td><strong>Only 34% of households</strong> have ADSL</td>
</tr>
<tr>
<td><strong>Imagenio’s customer base</strong></td>
<td><strong>Our market share is only 11%</strong></td>
</tr>
<tr>
<td>almost doubling</td>
<td></td>
</tr>
<tr>
<td><strong>Innovative solutions launched</strong></td>
<td><strong>Nearly 90% of our clients</strong> DO NOT have “desktops”, and “Wireless Desktop” is yet to explode</td>
</tr>
<tr>
<td><strong>&gt;380,000 e-mail devices</strong></td>
<td><strong>Only 7% of our clients</strong> have a 3G device</td>
</tr>
<tr>
<td><strong>Analyzing new business models</strong></td>
<td><strong>Models based on content, advertising ... are yet to take off</strong></td>
</tr>
</tbody>
</table>
Priorities to exploit our distinctive growth profile

- Sustain premium growth
  - Expansion of wireless customer base & data usage
  - Further development of BB

- Enhance revenue quality
  - Enhance loyalty of high value customers
  - Transform variable revenues into fixed

- Network transformation
  - UMTS network densification & HSDPA expansion
  - TdE’s access network transformation

- Enhance efficiency
  - TdE’s 2003-2007 ERE program
  - Accelerate cash generation

Capture integration & convergence value
Index

01  Benchmark set of results in 1Q07

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03  Differential strengths to exploit market opportunities
03 Strong position based on our strengths as an integrated player

- **We are market leaders across businesses**
  - 82% in fixed line access
  - 56% in broadband
  - >45% in wireless

- **We know well our high quality customer base**
  - 57% of our wireless customers in contract
  - Stronger market share in Corporate

- **We have higher customer satisfaction**
  - Best quality, service provisioning and customer care

- **We have a large exclusive distribution channel ready to sell all services and state of the art networks to back our commercial efforts**

- **We have strong financial resources to lead the commercial push**

**Superior capacity to anticipate changes**
03 Differential commercial strength

Driving cross selling

+2,500 sales people

- Integrated sales force in Corporate & joint objectives for small businesses

10,000 Call centre positions

- Signalling and transferring

Strong online channels

- Joint front-end, redirectioning and bundle sales

~7,300 Points of sale

- Strong indirect channel

Exclusive POS¹

- Largest channel: >45% of total PoS in the market
- >75% of wireless commercial activity carried out through exclusive PoS
- Exclusive specialists PoS, a competitive advantage:
  - PoS over any other operator total exclusive PoS
  - Key channel for high value segments

¹ Source: Telefónica estimates. Based on research in cities over 20,000 inhabitants
03 Unmatched profile to exploit convergence

**EXAMPLES**

- **Channel convergence**
  - Stimulating demand through cross selling

- **Integrated sales force & convergent offering for large corporations**
  - Capturing, retaining and winning back corporate clients
  - Lengthening commitment periods

- **Tactical offering for residential**
  - Bundles
  - Pricing plans

**BB & Imagenio sales through TME’s specialist channel**
Units per month

- Jan-April 06
- Jan-April 07

- 1.2x increase

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**Flat rates for on-net wireless calls and fixed**

**UNO Pyme**

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**Images of BB & Imagenio**

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**UNO Familiar**

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**UNO Pyme**

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**Telefónica**

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03 Financial strength

2006 Capex (MM€)

Telefónica España

2,293

x 1.1

Competitors¹

4,128

2006 EBITDA (MM€)

2006 SAC+SRC+ Advertising (MM€)

2006 EBITDA margin

Commercial effort

Unpararel resources allow to lead innovation and keep strong commercial push

¹ Includes VOD, OGE, Ono & Jazztel.
Sources: press releases from companies and ML Wireless Matrix. Fiscal year for Vodafone (April 06 -March 07).
Strong cash-flow generation despite significant capex to transform the network

2006 OpCF¹ (MM€)

7,334 x 4.5 = 34,035

Telefónica España²

Competitors³

1,623

2006-2009E capex: ≈ €9,000MM

- UMTS network densification & HSDPA expansion, to back a commercial strategy fully aligned with market trends
- Wireline access network transformation (FTTx): €800MM

¹ OIBDA– Capex
² OIBDA excluding E.R.E. provisions
³ Includes VOD, OGE, Ono & Jazztel.

Sources: press releases from companies and ML Wireless Matrix. Fiscal year for Vodafone (April 06 -March 07).
03 Superior ability to anticipate changes in the industry

“Management implemented a large restructuring plan in its domestic fixed line operations at the end of the 90s ... TEF deserves credit for the “homework” done .... especially relative to some of the peers group (i.e. FT or DT)” Merrill Lynch, March 2007

Domestic wireline businesses

<table>
<thead>
<tr>
<th>Employees 2006</th>
<th>Lines per employee 2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>97,328</td>
<td>592</td>
</tr>
<tr>
<td>86,315</td>
<td>526</td>
</tr>
<tr>
<td>82,000</td>
<td>467</td>
</tr>
<tr>
<td>55,705</td>
<td>334</td>
</tr>
<tr>
<td>≈34,000</td>
<td>333</td>
</tr>
</tbody>
</table>

ERE TdE 2003/07:
- 15,000 employees
- 37% workforce reduction

Source: Merrill Lynch European Broadband Matrix 1Q07, May 2007 and Telefónica
Fixed lines + retail BB accesses/ wireline business total workforce

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Madrid, April 2007
Conclusions

- Once again we have delivered solid results in 1Q07

- Proven capacity to grow further our revenues through new accesses and increased usage of our services

- Strong opportunities to keep a benchmark profile

- Exploiting convergence opportunities and extracting value from integration

- Our track record reflects our strengths and execution capabilities to capture this growth potential