Telefónica January-December 2012 Results Conference Call Transcript

28th February, 2012

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Introduction

Pablo Eguirón - *Telefónica S.A. - Head of IR*

Good afternoon, ladies and gentlemen, and welcome to Telefónica's conference call to discuss January-December 2012 results. I am Pablo Eguirón, Head of Investor Relations.

Before proceeding, let me mention that this document contains financial information that has been prepared under international financial reporting standards. This financial information is unaudited.

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Now let me turn the call to our Chairman and CEO, Mr. Cesar Alierta, who will be leading this conference call.

Presentation

César Alierta Izuel - *Telefónica S.A. - Executive Chairman and CEO*

Thank you Pablo.

Good afternoon ladies and gentlemen and welcome to Telefónica's 2012 results conference call.

Today with me are the members of the Executive Committee, so during the Q&A session they will have the opportunity to answer the questions you may have.

Let me start with the highlights of 2012.

We are in the middle of a strong operational transformation that is clearly starting to bear fruits. Latam is delivering quality growth amid enhanced profitability, with Brazil as a cornerstone expanding its market leadership.

In Europe, 2012 has been a year of strategic change with Spain at the forefront. Fusion is a clear commercial success. It already reached margin break even in December net adds, in addition there has been a strong OIBDA margin expansion and year-on-year growth in OpCF in the fourth quarter.

All this is reflected in the further sequential cost containment and margin expansion across the whole Group. Allowing EPS and FCFS to continue expanding in underlying terms, which in 2012 are twice the announced DPS for 2013.

In addition to this operating progress we have regained our financial flexibility, with strong deleverage which will continue clearly in 2013.

2012 operational transformation for a sustainable model

If you turn to the next slide you can see that 2012 has been a year in which we have adopted bold decisions to transform our business across the board.

One of the goals of this transformation effort is to lead the Company towards a very sustainable top-line growth. The creation of Telefónica Digital, the growing contribution of Latam, with more than 50% of our revenues, the innovation of our offers and the increase of data contribution are clear initiatives to recover our traditional extra growth gap with the industry.

We are also leading the sector in a new commercial model, moving away from a model based on just subsidies, incentivising customer rotation, to a new one oriented to increase customer satisfaction, breaking the rules through the new proposals.

Simplification has been one of our top priorities, simplification across the board; from simple tariffs to simplify the entire organization. This has allowed us, among other things, to significantly reduce legacy, to increase the focus on core activities with immediate returns in terms of efficiency.

In terms of CapEx, optimisation has been key. We want to have the best networks, but we have a new approach with network sharing and co-investment and at the same time, efficiencies from lower churn are at the centre of our strategy.

Lastly, I also want to highlight that in just six months we have regained our financial flexibility.

One visible consequence of all this, is that we have recovered OpCF organic growth in the fourth quarter.

Transformation is already delivering results (I)

In slide number 4, I would like to show the results that this transformation is already delivering.

In the first place, the better organic revenue performance is driven by T. Latam and mobile data, accelerating organic growth trends. Some examples of this business transformation are the outstanding commercial traction on MBB & FBB and the increase of digital sales.

Regarding OIBDA margin, I would like to highlight our progress towards OIBDA stabilization on the back of strong execution skills, cost transformation, by eliminating subsidies in Spain, and other operating cost reductions in different areas.

In addition, disciplined CapEx management along the year, has very positively impacted operating cash flow, that reached almost 13 billion euros in 2012 and grew 6.2% year-on-year organic in Q4, reversing previous trends.

Transformation is already delivering results (II)

As slide 5 outlines, earnings per share continue their progression quarter-on-quarter, reaching 0.46 euros in the fourth quarter, in underlying terms.

Underlying EPS up to December was 1.44 euros and the free cash flow per share 1.55 euros, providing strong comfort about the full sustainability of our 0.75 euros cash dividend commitment for 2013.

In terms of financial flexibility, the reduction of our net debt figure to 51 billion euros as of December is very significant. Reducing leverage by 0.3x times in just six months demonstrates Telefonica's capacity to deleverage and also the liquidity cushion at the end of the year is materially much higher than the last year figure.

Continued sequential OIBDA growth and margin expansion

Moving to slide 6, our operational transformation is already evident in 2012, as shown by OIBDA progression.

In absolute terms, underlying OIBDA grew sequentially for the third quarter in a row at the Group and regional level. OIBDA margin stood at 37.0% in the fourth quarter and expanded close to 200 basis points quarter-on-quarter.

Let me highlight that year-on-year margin improved 10 basis points in the fourth quarter, changing negative trends registered in the previous quarters and posted the first year-on-year improvement since Q1 09, even despite the lower contribution from tower sales. As such, progressive margin recovery drove OIBDA stabilisation year-on-year.

And now, let me hand over to our Chief Operating Officer, José María Alvarez-Pallete, who will describe in a more detailed fashion our operational transformation strategy.

José María Álvarez-Pallete - *Telefónica SA - Chief Operating Officer*

Transformation for a brighter future

Thank you César. Please move to slide 7, where I will provide two examples of our operational transformation.

In Spain, the new commercial model is a clear example of our transformational approach. The process started in mid-2011 with the launch of new tariffs, which drove both to lower ARPU and lower churn. The second step was to remove mobile subsidies in acquisition, leading to lower commercial expenses. Simplification and focus on quality followed, to end with a quad-play offer, Movistar Fusion.

Fusion implies lower ARPU at the beginning, but it brings also lower commercial costs, benefits from lower churn and high value share gains. It does not only work commercially, it also works very well in financial terms leading to visible results. This demonstrates how acquisition of high value customers is compatible with a rational commercial model, making in addition the model more sustainable.

Another example of our focus on higher sustainability is in Latam, reflected in our data centric services. In this process we are leading sector transformation, we have the best starting point because we have the largest contract base in the region. Our focus now is in leading smartphone adoption and thus to evolve the business towards data. This growth is more expensive short-term but it is more sustainable as well as is based in differential quality and higher customer loyalty.

Telefónica Digital to accelerate growth

Turning to the next slide, let me review the progress made by Telefónica Digital, our platform to capture the value opportunities in the digital world.

First, we continue innovating in the development of new Communication Services in order to strengthen the telecommunications environment. Let me highlight that the first handsets with Firefox OS will be launch in Spain, Brazil, Colombia and Venezuela during summer 2013 .

Second, we have launched a number of digital services, leveraging our global approach and focused in Financial Services, Cloud computing, M2M, Security and Video communications.

And third, now we have a larger billing relationship with our customers, which places us in a privileged position to maximise our customer base value.

These assets and skills are fostering the transformation of our core business and they are already driving growth.

Going forward, we aim to continue accelerating innovation, working on building on our own platforms but also reaching agreements with third parties and partnerships to fulfill our target of transforming Telefónica into the leading “Digital telco”.

MBB & FBB driving growth across the footprint

Moving to slide number 9, we continued to invest to bring enhanced propositions to our customers. These efforts have allowed us to grow our customer base by 3% year-on-year to 316 million accesses.

We recorded a strong acceleration in net adds in the fourth quarter of the year, specially in mobile, driven by record smartphone sales and the superior increase in the contract segment.

At the same time, FBB and fixed line improved momentum, specially in Spain after the launch of our successful convergent offer “Movistar Fusion”.

Lastly, we are doing a selective deployment of ultra broadband services in the markets that meet potential demand, regulation and competition. At the end of the year, aprox. 26% of our fixed accesses are currently ready for commercial UBB services and out of them, 9% are already connected.

Solid revenue growth of Latam and mobile data

Slide number 10 details the evolution of Telefónica’s revenue mix:

We are increasingly capturing growth opportunities allowing to offset headwinds in Europe.

Latin America continued to be our margin growth engine and kept posting growth acceleration in the fourth quarter to 7.5% year-on-year, purely organic. This performance led Group revenues to show a sequential improvement of 0.8 percentage points. It is worth highlighting the remarkable performance of digital revenues in the first year of operation.

On the mobile data business, a key strategic area for Telefónica, we are recording strong results. Fourth quarter non-SMS data revenues continued to deliver a sustained ramp-up in their year-on-year organic increase and already account for 60% of data revenues, on the back of a profitable data monetization strategy. It is worth highlighting the very rapid expansion of smartphone penetration, that reached 19% at the year-end, 6 percentage points more than a year ago. This represents a huge potential ahead, mainly in Latin America.

Further efficiencies on continued execution

Let's turn to slide number 11 to talk about efficiency.

I'd like to stress the substantial sequential reduction in OpEx in the fourth quarter, consistent with performance posted in the last two quarters. This is the result of efficiency improvements, cost control measures and significant decline in commercial costs due to a much more rational approach to subsidies across geographies and spite of record smartphones sales.

As such, good progress of profitability along 2012 reflected firm actions on cost efficiency, highlighting among others overhead, simplification of processes, quality of services, outsourcing, call center, new data centers and synergies from integration of operations.

January-December 2012 profitability stood at 34.9%, with a very limited year-on-year decline reflecting higher network and systems costs to expand network coverage and capacity and commercial costs on the back of a very rapid smartphone adoption.

Prioritised investments to cope with future growth

Please turn to slide 12 for an update in our investment profile.

In 2012 CapEx in growth areas has significantly increased, specially in fiber, up 50% year-on-year, followed by mobile 3G and 4G networks and with higher efforts executed in our Latin American region. Overall, total investments remain stable despite the increased CapEx in growth, thanks to the prioritisation of deployments and benefiting from improved purchase efficiency and the positive impact from churn reduction.

It is also important to highlight that we have a complete spectrum map in the most relevant markets, with the last acquisition in UK demonstrating our commitment to drive future growth in our countries of operation at a reasonable price.

As a result, in 2012 we have been able to continue transforming our networks, investing in high speed broadband, both fixed and mobile, while keeping CapEx to Sales ratio at 14.2%, flat versus 2011.

With all this, I would like to highlight that OpCF grew 6.2% organically year-on-year in the fourth quarter.

T. Global Resources achieving significant results

Main accomplishments reached by Global Resources are based around IT, Devices, Global sourcing and networks & operations.

In IT we have achieved significant savings in both OpEx and CapEx, mainly thanks to the efforts done around simplification and new data centres. In devices, scale is playing a significant role increasing the value of global negotiations and portfolio optimisation. We aim to have in 2013 an even more balanced vendor map.

Global sourcing was also central for increased savings while the most visible results come from network savings and assets optimisation.

TGR is also contributing in our global position/approach to multinationals thanks to our scale benefits.

Let me now hand over to our Group CFO, Angel Vilá, who will take us through the detailed Group and Regional results.

Ángel Vilá - *Telefónica S.A. - Chief Financial and Corporate Development Officer*

Financial Summary: OpCF growth in Q4

Thank you, Jose María. Please turn now to slide number 14 to start with a detailed review of full year results.

Both in 2012 and in 2011 we booked several significant exceptional items, with Q4 12 numbers being particularly impacted by: first the reduction in the value of Telecom Italia investment, second the impairment recognized in the value of T. Ireland and third the devaluation in Venezuela. So, to better understand the underlying performance of the Company we are providing a P&L excluding those non-recurrent effects and non-cash impacts.

In those terms, revenue reached 62.4 billion euros in 2012, down 0.7% year-on-year, while OIBDA topped 21.7 billion euros, with a margin decline of 1.3 percentage points, a lesser margin decline compared to last year and posting a better performance for a third quarter in a row. Underlying net income totalled 6.5 billion euros, with an EPS of 1.44 euros per share.

I would also like to highlight that, although material items such as the assets write-downs are flowing into the P&L, there are other transactions that are enhancing our equity but not flowing through the P&L. For example, the restructuring of the Colombian operations increased shareholders' equity by 1.6 billion euros.

Latam: Quality growth amid enhanced profitability

Let me now summarise our operations by region, starting with Latin America.

In 2012, our selective commercial strategy delivered the results we aimed to: revenue growth outpaced accesses growth as we continued to leverage on booming mobile data and remaining opportunities on increased mobile voice usage while continuing to transform our fixed operations.

Hence, revenue continued accelerating in Q4, at 7.5% year-on-year organic terms, whilst profitability remained strong, with OIBDA growing year-on-year at 1.6% and OIBDA margin above 40% in the quarter, with a lower contribution of tower sales compared to one year ago.

Brazil: Focus on quality delivering results

Please turn now to slide 16 to review our Brazilian operation.

2012 was a key milestone in our transformation journey towards fixed and mobile integration, while consistently improving the quality of our services and the satisfaction of our customers.

In the fourth quarter, commercial activity in the high value segments of the mobile market remained strong, driven by our top service quality. In the fixed business, we are in the process of changing the dynamics as proven by the innovative services launched this quarter.

As a result, revenues accelerated in Q4 fueled by the outstanding performance in the mobile business, which already represents almost 2/3 of total sales. Our successful strategy resulted in a solid revenue trend, outperforming the market and gradually expanding this gap. On the fixed side, convergent offers are limiting erosion in the traditional business.

Brazil: Increased profitability

Turning to slide number 17 let me stress that profitability of our Brazilian operation is consistently improving.

We kept gaining OIBDA market share quarter after quarter as annual growth progressively improved along the year, reaching an outstanding performance in Q4. OIBDA margin stood at almost 45% and expanded on a yearly and on a sequential basis on the back of efficiencies implemented throughout the year, plus contribution from tower sales.

On top of that, despite maintaining strong CapEx efforts at 15% of sales, integration benefits continued flowing to bottom line with a strong cash flow generation.

Latam: Key Metrics (I)

In the next slides we review the operational performance of the rest of the countries in Latin America.

In Mexico, we keep focused on the turnaround process that, as Q4 showed, is starting to deliver results, with commercial activity progressively improving and financial metrics also posting a gradual recovery. Mobile service revenues increased by 2.7% year-on-year in Q4 and OIBDA margin continued improving sequentially and reached 31.4%.

Our operation in Venezuela, showed an impressive operational performance amid increased profitability.

And in Colombia, I would like to highlight that the benefits stemming from the integration of the fixed and mobile businesses are starting to be reflected on the results with OpCF growing by more than 30% year-on-year in 2012.

Latam: Key Metrics (II)

Turning to the Southern region, let me highlight the positive results delivered in Peru across all metrics, with sustained commercial momentum along with healthy sales growth and profitability.

In Argentina, improved commercial activity from Q3 continued this quarter, while revenues and OIBDA margin accelerated.

And in Chile we continued posting solid growth and profitability amid a highly competitive environment.

T. Europe: A year of strategic change

Let me now review the performance of our operations in Europe.

2012 has been a year of strategic change for Telefónica Europe delivering the right balance between customer growth and profitability.

Successful commercial moves in key markets led to sustained momentum in contract mobile throughout the year and a solid uptake of smartphones, leading penetration to 35%, up 8 p.p. year-on-year. Growth strongly accelerated in Q4 thanks to Movistar Fusion in Spain.

The good news is that we achieved this commercial traction with lower operating costs, down 7% year-on-year, thanks to the transformation initiatives put in place across the footprint, focused on optimizing the allocation of strategic costs and investments.

So, efficiency gains and the continued monetisation of tiered data resulted in a sequential improvement of profitability and with Q4 margin posting a year-on-year expansion despite continued revenue pressure.

No doubt, we have laid the foundations for future growth.

Spain: Financial turnaround is taking place

Please turn to slide number 21 to start reviewing the Spanish business.

The successful execution of our transformation, which started back in September 2011, has already delivered visible results, with clear improvement at both OIBDA and OpCF level throughout the year.

T. España has been able to manage the continued top line pressure due to tariff repositioning and lower usage, with multiple initiatives of cost cutting across the board. The strong focus on quality increased customer satisfaction and lowered claims and churn. Subsidies removal and portfolio simplification, processes and personnel have driven a sharp OpEx decline.

As a result, OIBDA has been stabilised while OIBDA margin y-o-y trend has sequentially improved to 47.2% in the last quarter, 5.5 percentage points above previous year.

On top of that, we increased the resources devoted to fiber and at the same time we reduced overall CapEx, positively impacting cash flow. As a result, efficiency gains offset revenue declines in Q4 and OpCF increased by almost 8% y-o-y, returning to growth.

All in all, I would like to stress that this strategy that dramatically changed the business model, has set the basis to keep commercial traction in 2013 while delivering sustainable cost savings.

Spain: Movistar Fusion leading the Spanish market

Let me now update you on the progress made by Movistar Fusion, a key step in our transformation journey.

Movistar Fusion is a revolution in the Spanish marketplace, where convergence is the new name of the game.

Our priority was to recover leadership in the market and in just five months we have achieved this goal. Our quadruple play offer, leveraged on our integrated profile, has made an stagnated market to grow again in a more profitable way.

More than 1.5 million customers have already signed to Movistar Fusion. As of December more than 30% Fusion customers had contracted new mobile or fixed broadband services. But Fusion is not only helping to get new customers: it is also accelerating the take-up of high value services such as fibre and MBB. So, Fusion has improved our commercial performance as shown by Q4 net adds: the lowest loss in fixed telephony in 5 years and the highest additions in FBB since the second quarter of 2008.

Looking at the financials, top line dilution of Movistar Fusion is easing with an increasing proportion of upselling and new customers joining in, so we are on track for Fusion revenue breakeven in 2013.On the cost side, savings in commercial costs are material on the back of no subsidies, lower acquisition and billing costs and lower churn.

All in all, Movistar Fusion is on the right path to be margin accretive. Considering just December, net adds of Fusion have already reached margin breakeven.

UK: Commercial traction flowing through to financials

Turning now to slide number 23, Telefónica UK consolidated the success of the commercial strategy started in Q3 11 and regained momentum specifically in the contract segment, with the contract mix up 3 p.p. year-on-year, reaching 52%. As a result, we continue closing the gap in terms of revenue performance vs competitors, with market leading profitability.

It should also be noted that we continued to gain high value customers, with an expansion of more than 3% of the customer base and noticeable reductions in both prepaid and postpaid churn.

The strong commercial traction flows into financials with underlying revenue trends moving towards growth by the last quarter of the year. In parallel, we balanced the right equation of growth and profitability with the first half of the year heavily impacted by the higher commercial activity while in the second half we saw more comparable trading.

Lastly, let me stress that Telefónica UK has successfully secured two blocks of 10Mhz in the 800 MHz spectrum band for a total investment of 550 million pounds sterling.

Germany: Market benchmark performance

To review our operation in Germany, please turn to slide 24.

Let me highlight our sustained trading momentum in the contract segment that is supported by the continuous improvement of contract churn as we focused on the right balance between growth and value.

This, together with a successful data monetisation strategy, led to grow revenues, despite MTR cuts in December and to gain MSR share outperforming competitors throughout 2012. The higher ARPU of new customers versus churners is the main growth lever, though revenues show a deceleration in Q4 year-on-year due to the increased renewals of the early launched integrated tariffs portfolio within the base.

On the profitability side, continued sales growth and scale benefits flow into OIBDA, up 5% year-on-year in Q4 12, leading to OIBDA margin expansion. CapEx grew as we invested in LTE, reaching a 15% 4G coverage at the end of 2012.

And OpCF is up 12% year-on-year in 2012.

Substantial deleverage on FCF generation and disposal plan execution

Let's now move to the financial side, on slide 25.

Net financial debt has been reduced by €5bn in the year mainly thanks to our strong cash flow generation jointly with our successful portfolio management execution. As a result, our leverage ratio has improved dramatically to reach 2.358 times OIBDA, minimally above our target leverage commitment.

Importantly, we will continue our deleverage in 2013 backed by our cash flow generation as well as continuous asset rationalization measures to place ourselves comfortably below the 2.35 times net debt to OIBDA.

We have delivered almost €7bn of FCF as a result of better operating performance and working capital contribution as quarters were progressing. FCF per share reached 1.55 euros, comfortably covering our €0.75 cash dividend commitment.

Strong financing exercise & improved liquidity while contained interest expense

Slide number 26, shows our outstanding and diversified financing activity in 2012, where we raised close to €15bn, complemented by an additional €4bn in the first two months this year.

Our financial policy has placed our average debt life at 6.4 years and steadily reinforced our liquidity position up to €21bn, covering well in excess of two years maturities. And we have also improved the quality of our liquidity with substantial cash balances and higher percentage of long term unused committed credit lines. Our access to market is normalized.

To wrap up, we have kept our effective interest cost at 5.37%, at the lower part of our medium term guidance, despite the burden of a high cash position.

Now, let me return the presentation to our Executive Chairman and CEO, César Alierta, who will outline the guidance and priorities for 2013.

César Alierta Izuel - *Telefónica S.A. - Executive Chairman and CEO*

2013: recovering our growth DNA while reducing leverage

Thank you, Ángel. Let me now highlight our guidance for this year.

2013 is going to be the year when we will recover our growth DNA while we keep reducing leverage.

We will go back to revenue growth with revenue trends in Europe stabilising in the first part of the year and starting to recover again in the second part. In Latin America revenue growth will continue strong throughout the year based on our customer base expansion, increased MBB penetration and data revenue growth.

We will also keep limiting the OIBDA margin erosion, delivering benchmark OIBDA margins leveraged on our strong diversification and scale.

Let me stress that we will do all of that while maintaining our CapEx/Sales level, allowing us to keep transforming the Company.

On the financial guidance, deleverage will continue in 2013, with a final goal of net financial debt lower than 47 billion euros at the year-end.

2013 Operating Businesses Priorities

In slide 28 we summarise our 2013 priorities.

In Europe, Spain leads the transformation and simplification of the commercial approach and will continue accelerating this journey in 2013, which is already driving lower OpEx and CapEx.

The commercial momentum seen in the UK with innovative propositions will continue as we will do a rational deployment of the 4G network. In Germany we aim to continue outperforming in mobile market share, while improving the margins.

Moving to Latin America and starting with Brazil, we are already working hard on the fixed business turnaround while keeping a full focus on maintaining the mobile business outperformance, leveraged on our top quality proposal.

On the other hand, at a regional level, we are also focused on exploiting the benefits of further efficiency gains while we will grab the advantages and opportunities that our regional footprint provides us.

At the same time, Telefónica Digital will continue fostering digital growth, leveraging our core assets and building powerful positions through partnerships.

On top of that, scale benefits from TGR will further contribute to Telefónica's operational excellence.

Conclusions

To conclude, let me highlight:

First, we have reinforced our growth model in 2012 as solid execution of transformational initiatives is delivering visible results.

Second, we have regained financial flexibility.

Third, we have delivered our 2012 guidance.

And fourth, we are able to provide you with a very realistic outlook for 2013.

Thank you very much and now all of us, the members of the Ex-Com are ready to take your questions.

Q&A session

Georgios Ierodiaconou - *Citi*

Good afternoon. I have two questions. My first question is on asset portfolio management. You have got an extensive portfolio of real estate assets and you started monetizing them the last couple of years. There are some reports in the Spanish press suggesting that you are planning EUR2.5 billion of disposals of towers in Spain and Brazil this year. Is it something that you are considering and should we think of this process come on top of what you guided and therefore, the EUR47 billion of net debt position could actually end up being much lower?

And if possible, could you give us an indication of the multiples you have received on the tower sales last year in terms of the sale price compared to the lease rent that you pay?

And my second question is related to page 11 and the OpEx evolution in the fourth quarter. When I look at the guidance, it suggests that you will have some margin erosion in 2013. So I was wondering whether this is down to specific reasons having made the fourth-quarter numbers look better perhaps on the underlying trend or whether you are leaving yourselves with some room for commercial expenses to go up.

Thank you.

César Alierta Izuel - *Telefónica S.A. - Executive Chairman and CEO*

Thank you. This is Cesar Alierta. First, I want to make clear, a very clear statement, when I said that we are very realistic that our net debt by the end of 2013 will be below EUR47 billion, I have to say two things: this will be, as Angel said, we will be basically down because we are going to have a strong cash flow generation and the second thing which is very important and is unique to Telefónica, all the portfolio management we are going to do in the coming months, which will result in a deleverage, will at the same time increase the profitability of our business. Telefónica is in a position that we can have the portfolio management in which we will deleverage and at the same time we increase profitability, we increase the recurrent, I want to stress, recurrent profitability of our business. And in the coming months, you are going to see.

So we feel so comfortable about it, you know, that you are going to be surprised when we announce how we do that. This is unique in the industry and it is because the position Telefónica has. And now I hand it to Jose Maria to talk about towers.

José María Álvarez-Pallete - *Telefónica SA - Chief Operating Officer*

Thanks for your question. On towers, I mean we are not aware of any offer of this size on towers neither in Spain nor in Brazil, so we are not contemplating that today. But we are open because we are very open in terms of capital allocation as we have been during 2012. That means that we are reviewing the way we allocate capital. That means that we are considering non-strategic towers divestment, but always with the financial criteria that financially makes sense in terms of the lease commitments make sense compared to the financial expenses that we have right now, the financial threshold that we have right now. So, no plans. Nothing is included from the guidance on that purpose. That doesn't mean that we are not contemplating, but we will be very opportunistic and on a case-by-case basis. Just if it makes sense.

And considering the page 11, the OpEx evolution, most of the efforts that we have done in 2012 are sustainable. That doesn't mean that they are recurring in terms of we cannot keep the level of improvement of those permanently because we will keep growing our commercial efforts in Latin America, but we do think that the commercial efforts containment that has been done in Europe and mainly in Spain are there to stay.

So in terms of the OpEx evolution, we feel that, the effort that we have done by changing the model, effectively changing the model, focusing on quality on churn reduction, on simplification, on making our billing efforts much more profitable are sustainable. And finally, we have guided that our margin, OIBDA margin erosion is going to be more limited in 2013 than it has been in 2012. So you can make your own calculation and where we are pointing at.

Georgios Ierodiaconou - *Citi*

And is it possible to give us a multiple on the tower sales that you had in 2012?

José María Álvarez-Pallete - *Telefónica SA - Chief Operating Officer*

No, we are not disclosing that information. Sorry.

Ivón Leal - *BBVA*

Yes, hello good afternoon everybody. Just two questions. My two questions are on OpEx in Spain. I don't know if you could give us a rough idea of what were the subsidy costs in 2011 and 2012? And the second one is on personnel costs. I think the redundancy program was approved back in third quarter 2011, so I don't know up to which quarter in 2013 we can keep on seeing that 12% decrease in personnel costs that we have seen throughout 2012?

Eva Castillo - *Chairwoman & CEO Telefónica Europe*

Thank you. With regards to the redundancy program, I think that we stated that our large-scale organizational restructuring which is particularly EUR257 million savings in 2012.

Ivón Leal - *BBVA*

And is that supposed to continue throughout 2013?

Eva Castillo - *Chairwoman & CEO Telefónica Europe*

Well, as you know, it was a three-year program. So it is up to 2013, end of 2013. So it started in 2011. We completed the whole program in 2012, which was expected and we will finalize it in 2013. So we are on track.

Ivón Leal - *BBVA*

Okay. What about the subsidy costs?

Eva Castillo - *Chairwoman & CEO Telefónica Europe*

Yes, in terms of savings in the commercial costs, we believe that they were more than EUR500 million during the financial year 2012, so mainly coming from a new subsidy policy.

Ivón Leal - *BBVA*

And could you give us the number on the subsidy cost in 2012 just to see how much is left there?

Eva Castillo - *Chairwoman & CEO Telefónica Europe*

Well, I am afraid that I cannot disclose that information now.

Tim Boddy - *Goldman Sachs*

Yes, thanks for taking my question. Just some more questions around Fusion really, just trying to understand a few of the statements you have made and obviously the remarkable progress made on costs. First of all, what do you mean by revenue breakeven? Is that the total revenues on the Fusion products, including new customers, are to be the same as beforehand or is this just on the customers within your base adopting Fusion?

And then I guess kind of around that, it would seem that, as we go into Q1 and Q2 particularly, you get a larger revenue pressure because the customers are taking more of a discount, which is lasting for the whole quarter. So, should we look to see a softer first half both in revenue and EBITDA, growth trends in Spain before we get to that point of stability?

The last question I have really is just more of a wider strategic question about Spain, where just really how you see the regulatory roadmap panning out. And is it really in your interest to have Vodafone and Orange build yet another fiber infrastructure as opposed to allowing them attractive access to your own fiber? Many thanks.

Eva Castillo - *Chairwoman & CEO Telefónica Europe*

Thank you very much. Just to clarify, when we speak, that we are working towards revenue breakeven in 2013. Yes, we talk about the totalized clients, so the former and the new, so basically the ones who are added together with the ones that were already with us. That is the expression. The same way we use it in the what we call breakeven, margin breakeven that were particularly happening in December.

With regards to your second question, again, just to reemphasize what we have stated to December, we had new services accounting for around 30% of the total and that improved during the quarter. So, I can say that we were quite happy. Just to let you know, you know that by the end of December, we accounted for 1.1 million total clients and the Head of Spain already expressed that we were up to 1.5 million in February.

José María Álvarez-Pallete - *Telefónica SA - Chief Operating Officer*

I will take your question on regulation and deployment of fiber or basically network sharing as a philosophical approach. We are very open to that. We think it makes not major sense to have so many networks in Europe so very open to share infrastructure at reasonable prices and at reasonable conditions. We have been doing that in Spain namely with Jazztel you know that and it is public information; so we are open to conversations because we think that time has come for a more rationalized approach to CapEx and namely to effort on CapEx and networks deployment in Europe.

Tim Boddy - *Goldman Sachs*

And just on the first half of 2013, should we see increased pressure on revenue and margin from Fusion before it gets better or you think this is now a very linear type of improvement we should anticipate?

Eva Castillo - *Chairwoman & CEO Telefónica Europe*

Well, I think that Fusion is one of the components of the total offering in Spain and there are many moving parts in that sense. If we ask ourselves what we want with Fusion, it is clearly we want to achieve the goal of revenue growth. And the first thing we need to see that coming from the growth of our customer base. We are, in fact, seeing it, as we have mentioned throughout our presentation. And the beauty of this offer is not just an offer, it is a concept, which we can focus on specific situations in order to make them be even more important to the offer.

I have to emphasize this is still early days and we are still facing a strong competition, but the capabilities of working on particular efficiencies in each of the services and products that we offer, it is quite important.

Mathieu Robilliard - *Exane BNP Paribas.*

Good afternoon and thank you very much. I just wanted to look for a clarification on the guidance. I think that, during the presentation, the Chairman said that revenues in Europe were expected to stabilize and maybe grow in H2. I just wanted to make sure I get that right because, if that is the case, then you are basically expecting Spanish revenues to stabilize because of the size between Spain and the other European assets.

A second question had to do with Spain, very impressive decrease in line loss. Is that due to Fusion in one way or another and is that something you expect to continue into 2013. This low rate of decline? And finally, if I may, are you expecting further spectrum auctions in Brazil this year? Thank you.

José María Álvarez-Pallete - *Telefónica SA - Chief Operating Officer*

Taking your question on the guidance, I mean we start to predict the evolution of the Spanish economy today, but we do foresee a better second half of the year than the first one and Spain has a significant impact in the overall region. So we will keep you posted, but it is true that the guidance implies a better second half of the year compared to the first part.
Trends that we are seeing in the markets, namely in Spain, are still challenging. We are improving in the UK. We are doing better, a little bit better in Spain, but still challenging. So we will see. But it is true that our guidance assumes that the second half of the year is going to be better than the first one.

César Alierta - *Telefónica SA - Chairman & CEO*

The Spanish economy the reality of the Spanish economy at this time is much better than it was earlier, that is a fact and all the trends are pointing in that direction. So this is a fact and it is a reality. Anyway, it's in our guidance, we have been very conservative.

Eva Castillo - *Chairwoman & CEO Telefónica Europe*

In terms of your question regarding if the reduction of line loss was due to Fusion, we believe so. It is due to Fusion. Fusion has marked several impacts into the fixed line business and I think it is important to highlight that we have obtained definitely better fixed line growth than in the last five years, with a very positive fixed broadband net adds, which is probably the highest in four years. So Fusion is fostering growth in the fixed broadband market and that is something that we wanted to highlight.

Santiago Fernández Valbuena - *Chairman & CEO Telefónica Latinoamérica*

Hi, this is Santiago. In terms of the possibility of a new Brazilian spectrum license, you know that it is under study at the government. We think it is unlikely that all the necessary stages will be completed within this year. The 700 frequency is filled with things that need cleaning up and we will not welcome that spectrum process to take place this year, while we are in the middle of the process of deploying LTE for all the sporting events coming up in Brazil. So, we have no way of knowing, but certainly we think it is unlikely and we don't support it being anticipated.

Giovanni Montalti - *UBS*

Good afternoon. Just following up on the improvement in terms of fixed line thanks to Fusion, I was noticing that we do not see this, let's say, inverse of the trend in terms of new full unbundling lines. So I was just wondering if this means that a big share of the clients that are taking Fusion are coming from, let's say, mobile only household. Thank you.

Eva Castillo - *Chairwoman & CEO Telefónica Europe*

Well, we believe that there is some market growth in that particular piece of the business and we are proving so with the new lines. So there is market growth there and we are capturing it.

Giovanni Montalti - *UBS*

Sorry. But is it correct to say that a big chunk of the clients are taking Fusion do not have any, let's say, fixed broadband connection or fixed or not even a traditional fixed line, because this seems, looking at the trend of wholesale unbundling, that it's still strong. Actually in this quarter, it is up versus last quarter, so there is no sequential inversion in the trend of deals and connections? Thank you.

Eva Castillo - *Chairman & CEO Telefónica Europe*

It's actually coming from both, but it is showing growth in the market. I hope this answer.

Robin Bienenstock - *Sanford Bernstein*

Thanks very much. Two questions, if I may. First, I am just wondering whether a deeper relationship with KDG would make sense for O2 Deutschland and whether that would be coherent with the longer-term strategy towards more unified services. And separately, I'm wondering whether you need to accelerate your wireline investment as well in Brazil given GVT access to Sao Paulo or whether it makes sense to do LTE first and then think more about fiber in Brazil afterwards. Thanks.

Eva Castillo - *Chairwoman & CEO Telefónica Europe*

Thank you Robin and I think that basically I don't think we can make any comment on the KDG Vodafone situation or that possibility. Although I think there has been some statement there.

In our case, what we believe is that every market is particularly different and that, in any case, as we have shown before, we have kept quite an open-minded strategy for particular agreements. So if you look at what we are doing in Germany in particular, we have a special agreement with Deutsche Telekom on VDSL, which is working well and we are doing fiber with DTAG, which, somehow as well, shows that we are open for those possibilities.

If you ask us about the particular German market, as you know, it is behaving a lot more rational than other European markets, but it is still knowing the formula of convergence, we would be at least being actively responding to some of potentially these situations by agreements that we have so far.

Santiago Fernández Valbuena - *Chairman and CEO, Telefónica Latin America*

This is Santiago, Robin. In terms of fixed line investment in Brazil, especially in Sao Paulo, which is where we have an exposure, you know that we don't look so much at competitors than to ourselves. We have a clear problem at substituting old revenue sources with new revenue sources that means VDSL and fiber and that is what we are doing. Whether they will be fast enough to compensate the secular decline in voice revenues remains to be seen, but it has nothing whatsoever to do with GVT because we have very limited overlapping markets with GVT in Sao Paulo.

Robin Bienenstock - *Sanford Bernstein*

Yes, my question, sorry, if I may follow up, my question was really given that GVT now has more access to Sao Paulo and potentially under a new owner, whether you thought that they would be more aggressive in places where they could overlap with you. In other words whether the overlap would increase and therefore, whether you would need to build defensively against that.

Santiago Fernández Valbuena - *Chairman & CEO Telefónica Latinoamérica*

Well, when they get there, we will be there.

Frederic Boulan - *Nomura Securities*

Hi, yes. If I can come back on Spain for a second, so we have had a pretty strong decline in contract mobile subs. Is this acceptable and what can you do to limit the market share erosion? What make you confident customers will remain with Movistar when they need a new handset and could get another pricing? Movistar is now about 50% more expensive than Vodafone and Orange, including handset costs? So do you think this premium is sustainable?
And secondly, to come back on the revenue question, so revenue dropped 13% in Spain in 2012. Can you discuss a bit the impact of ongoing macro pressure on your business

and where you can realistically improve this top line in 2013 considering the Fusion upward dilution? Thanks a lot.

Eva Castillo - *Chairwoman & CEO Telefónica Europe*

Thank you very much, Fred. Basically, on the mobile performance in Fusion and in Spain, in particular, I think that the market dynamics have changed significantly from the launch of Fusion. So basically we have seen the market increasing advertising from our competitors. We have seen competitors launching or trying to replicate our offers and very importantly, we have seen new handsets and mobile offering.

After three or four months of Fusion, what we believe is that this is a successful offering, but there is room for improvement in execution and particularly, we need to work harder in all the channels to get the offer closer to our customers. We still are in the early days for the financing model, which I think is what you were referring particularly.

I have to say that, month after month, we have seen the market and the customers understanding a lot better our offering in financing. This was better understood in other parts of Europe, but now we are seeing this as a reality as an opportunity for adding a financing model and the handset of a financing model here.

We believe that still there are market dynamics that are tough. It is not just the macro; it is the fact that we are seeing the market shrinking overall as a cleaning of lines and so that also need to be taken into account. In any case, we think the market can be profitable. We are seeing offers in the market, which we believe are not sustainable. So we need to stick to our principal within Fusion with not handset subsidy, and moving more and more into financing model.

Luigi Minerva - *HSBC*

Yes, good afternoon. The first question is on fiber in Spain. A couple of weeks ago, there was a statement that you would reach 8 million households by 2015. Does this imply that the co-investment agreement with Jazztel will be extended beyond the current 3 million? I mean Jazztel or other players if they join. And the second question is on the cash flow and over the last couple of years, you benefited from a timing difference between reported CapEx and cash CapEx. Do you expect a similar trend in 2013 and in the same amount of 2012 or 2011?

Eva Castillo - *Chairwoman & CEO Telefónica Europe*

Thank you very much. With regard to your question, just to clarify that we have committed to 3 million households in 2013 with Jazztel. So just to clarify that. And as you know, the agreement is flexible, it is a flexible investment approach in the coming years with the goal of reaching 8 million households by the end of 2015.

Ángel Vilá - *Telefónica S.A. - Chief Financial and Corporate Development Officer*

Hello, Luigi. This is Angel. With respect to your question on cash flow, as you have seen, working capital has followed the traditional seasonal profile that has been happening in the last few years and as we had indicated in previous conference calls, it has clearly improved in the second half. Part of this is due to the different phasing of accrual versus payment of CapEx and that probably will be replicated.

Jerry Dellis - *Jefferies & Co.*

In Brazil, you reported a very stable operating cost performance in the fourth quarter. I think growth was just 1% on an underlying basis. And that was particularly characterized by quite tight control of the commercial costs, the selling expenses. So my question is how sustainable you think that performance is going into 2013. Clearly, there is a pretty competitive fixed broadband market, lots of things that are not entirely within your control and there is also one specific issue in 2013, which I guess is the turnaround plan for the pay-TV business. And I am wondering what implications that relaunch might have for cost trends going forward?

Second question is on Spain. On the wireless business, you highlighted in the press release how wireless service revenues benefited from fewer retention upgrades in the fourth quarter. I am just wondering as we sort of model wireless service revenues quarter by quarter going forward, was there a particularly higher volume of those redeemed loyalty points falling in the fourth quarter relative to what we can expect would normally fall in sort of Q1 and Q2.

Santiago Fernández Valbuena - *Chairman & CEO Telefónica Latinoamérica*

Yes, this is Santiago. Let me start on the part of Brazil. Well, first of all, cost-containment has received a greater focus at the end of 2012 and will continue to be one of the top priority items into 2013. We are talking subsidies, we are talking cost control, headcount and we are talking deepening all the synergies that were created by the combination of both companies last year.

The part on pay-TV that you mentioned is important and it is one of our focal points of developing the revenue line this year. But we think it is going to be very likely associated with a variable cost model, meaning it is not going to be the case that we invest large amounts in acquiring customers without them being in the position to allow the amount of revenue that we would expect from them. So all in all, we think those trends should continue well into 2013. And TV is a focal point, but should not be detrimental to this cost-containment effort.

Eva Castillo - *Chairwoman & CEO Telefónica Europe*

With regards to your question on the mobile service revenue in Spain, yes, the year-over-year trend improved mainly due to fewer handset upgrades. And specifically to highlight there is no seasonality in these numbers, which, by the way, were around minus 43% year-over-year in Q4. So the other question is we might act tactically if we think it's necessary, but overall the quarter has shown already what it is our intention at what we do.

If I may, Pablo, I want to answer more completely to Luigi, Luigi, our commitment internally as Telefonica with regards to fiber passed through households is 8 million, but our commitment with Jazztel, in the agreement with Jazztel is 3 million co-investment in 2013. I hope this is clearer now.

Jonathan Dann *- Barclays Capital - Analyst*

Hi, there. The first question is on plans for network sharing and says what is actually happening in places like Germany, but also plans to perhaps extend the model into Latin America. And then, secondly, it is back on I guess the quarter-by-quarter domestic margins. I guess my question, normally the fourth-quarter EBITDA dipped, the margin dipped in mobile and I guess could you give some sort of sense of, you know, in 2012, the ratio of commercial costs in the fourth quarter by comparison to the first, second and third quarter? And I guess what I am really asking is what will we expect Q1, Q2, Q3 margins to be above, in 2013, above the level they were in 2012?

José María Álvarez-Pallete *Telefónica SA - Chief Operating Officer*

Okay, taking your question on network sharing overall globally, we are very happy with the situation that we have in places, like the UK with Vodafone. We think it makes sense, we think it creates a huge amount of value. We think that by investing mostly the same, we have a much better network in a much faster deployment effort and in a much more efficient way.

The same thing applies for Germany, for example, where we have this transport agreement with Deutsche Telecom and the same thing applies for the agreement that we have here with Jazztel. So we are more than willing to do network sharing and to co-invest with people that are really focused on investing on creating network and investing on the networks. We think it makes sense.

And the answer is yes, we are more than willing to extend that model into Latin America and in fact, it is already in place in some of our operations, namely, for example, in Argentina historically and yes, we are exploring ways of collaborating through network sharing agreements all along the region.

So for us, it is strategic. We think it makes sense. We think that having the best network is a must, having the best network as a competitive advantage only if it is sustainable, but if not, negotiating is the answer.

Eva Castillo – *Chairwoman & CEO Telefónica Europe*

And regarding your question on the margins, in particular, as you know and the question is this margin, high margin sustainable? We believe these high margins are sustainable because we have our cost reductions that are quite sustainable. We are, first of all, focusing on quality. As you know, 56% of claims reduction just in fourth quarter and we have effective reduction expected in 2013.

With regard to portfolio and processes simplification in IT and services savings are clearly part of our strategy and the most important is that the new commercial model with the financing of handsets and no subsidies already has that included in the model. We also believe that Fusion is not a margin dilutive concept or a margin dilutive offer and as we mentioned earlier is already margin breakeven in December net adds. So basically no subsidies, lower billing costs and lower marketing costs we've seen.

Just to remember as well that the fourth quarter last year, sorry, last quarter 2012, we had one-offs of around 1 pp of the OIBDA margin. We strongly believe that the market can be profitable and Fusion is helping us. But just to reemphasize that if necessary we can take some tactic moves if it is needed.

With respect to the fourth quarter in particular, if you remember, fourth quarter 2011, we had a strong marketing campaign, so we had lot commercial costs also assigned to that fourth quarter while, in the fourth quarter 2012, we have already the new model, which is different, a completely different approach. So the impact as you pointed out is completely different.

Luis Prota - *Morgan Stanley - Analyst*

Yes, thank you, two questions please. First is on Venezuela and more specifically on margins, whether you see any kind of margin pressure coming from the weaker currency. I don't know whether you could give us a percentage of costs. You haven't had currency and also in this regards whether you see any change following the devaluation of the currency in terms of potential for repatriating any cash from that country?

And the second question is on the potential IPO of Latam, where we have seen some quotes suggesting that you had cancelled this IPO. But to be very honest, I am not sure whether that was an unofficial view coming from the Company or it was just a press article. So if you can confirm that, it would be helpful. Thank you.

César Alierta - *Telefónica SA - Chairman & CEO*

Thank you, Luis. This is César Alierta. With the IPO in Latin America, there is not going to be an IPO in Latin America. As I said at the beginning, we are regaining our total financial flexibility. We are going to be well below EUR47 billion within and this is not a priority anymore to IPO Latin America operations and that is clear.

Santiago Fernandez Valbuena - *Chairman & CEO Telefónica Latinoamérica*

In terms of what is going on in Venezuela, Luis, two observations. One is that margins continue to be very healthy. We continue to have the leading market operation in the country. The Venezuelan devaluation just happened and so it is early days still to know what the final impact is going to be on foreign currency-denominated inputs, which are not a lot and the situation is not likely to be very different from what it was until now. So certainly the translation is going to mean a different number, but I don't think the day-to-day businesses are going to be all that affected by the devaluation. So, certainly we see no sign of improvement anytime of the currency repatriation issues and we have nothing to report on that.

Torsten Achtmann - *JPMorgan Chase - Analyst*

Good afternoon. The first one is on Brazil where you continue to outgrow competition, but overall the market in mobile seems to be slowing down and I wonder is that due to competition or is it due to the economy? And going forward, if do we have now reached a stable base and we expect to grow from that over the next year?

And the second question is on your net debt target of below EUR47 billion. Could you clarify in terms of potential asset sales, if that is included and excluded, and how many of them or if only a few of them would be included what would that be? Thank you.

Santiago Fernández Valbuena - *Chairman & CEO Telefónica Latinoamérica*

Yes Torsten, in terms of mobile growth in Brazil, two observations. One is that growth still is there. We continue to expand both the number of clients and at the same time, we continue to upgrade the existing customer base into more expensive and more interesting products. So I think the growth rate is slowing down a bit, but it is far from having stabilized or having reached maturity the way we see it.

We are also happy to report that we have been moderately successful in upgrading our customers into the better segments of the market and we think that process is at its early days. It is not at its final days. So you have both the expansion and the migration that still have a lot of time to run.

Ángel Vilá - *Telefónica S.A. - Chief Financial and Corporate Development Officer*

Torsten, this is Angel. With respect to deleverage and our target of net debt, we have established a target of below EUR47 billion net debt and we are also stating clearly that we aim to be comfortably below 2.35 times net debt to EBITDA. This is going to be done, as Cesar said initially, organically in a significant way. We expect significant free cash flow generation to be in excess of our dividend commitment that we are confirming to the market, our cash dividend commitment to be paid this year.

Also, we are going to be analyzing inorganic transactions that would improve our strategic position in markets where we operate, that would create recurrent benefits while at the same time providing debt relief. So we expect to be giving you news in the future on this as soon as these transactions and projects that we are working on eventually materialize.

Fabian Lares *- JB Capital Markets - Analyst*

Hi, good afternoon. Two questions. The first one with regards to the current tendency to move towards convergence as you are implanting the Fusion offer in Spain, I was wondering whether you foresee that this type of offering is going to become prevalent throughout Europe and in this case, what would be your strategy in a country like the UK where you are primarily mobile? And second, with regards to the Atento divestment that you carried out, when you are focusing so much on customer service and quality of service, I was wondering if the fact that you no longer own your call centers is not going to be a problem for that strategy. Thanks.

José María Álvarez-Pallete *Telefónica SA - Chief Operating Officer*

Thanks for your question. Regarding convergence, data plus voice plus TV offers can be structured in different markets through different ways. For example, you have access to unbundling in some places or you can play with complementary platforms like satellite that we think will also take a role in the global landscape.

At the same time, remember that an accelerating LTE deployment, being LTE the first wireless technology that equalizes speed of access of data transmission speeds compare with ADSL or VDSL or even fiber replicating voice plus data or plus broadband or even plus ultra broadband offers can be done in different places in different ways.

So we think that yes, convergence in terms of our quadruple plays or integrated offers are going to be the way to go. The way this is going to be structured in different markets is going to be different. The turnaround in Spain, if that is the question, is not just Fusion. Fusion has a convergent offer. Fusion is much more, Fusion is the last step of a significant process that was started by realigning our pricing strategy in Spain, by focusing on quality, significantly improving the quality and therefore reducing churn and reducing the number of monthly claims by more than half. At the same time, the subsidy removal strategy by getting into the financing and putting the bulk of the commercial retention effort on the existing customer base and not on the acquisition and finally, Fusion, which is a product more than a tariff.

So the answer is yes, we believe in quadruple play, in integrated offers. The way they're going to be structured is different. It depends on market dynamics and by the way, remember that roughly more than 80% of our cash flow is generated or is being generated in countries where we have integrated platforms. So we are very well-positioned anyhow.

In terms of the quality, how we have been improving quality and the call center role of that, we do not feel that it's a disadvantage because we have been divesting in Atento.

Simplification is the key. We have too many products. We have become a too complex company and therefore, when you have a thousand, but literally a thousand references of product in each company, you put a burden of interaction at the call centers, at the IT part of your business, which makes a huge complexity transforming to a high operational cost. Keeping complexity going into simplification is the key.

Now we can build our customers with Fusion with one single line. The product doesn't deserve any more promotions, so billing is much easier. The number of calls that we are having through the call center has been significantly reduced. So we do not feel it's a disadvantage at all because we don't have Atento anymore because the key is in the transformation of the Company through simplicity.

Justin Funnell - *Credit Suisse - Analyst*

Thank you, two questions please. Just on this mix of people who are upshifting, bringing back a line or a mobile phone on Fusion versus downshifters, it was 30% for Q4. You said it got better through the quarter. I guess it may have got better again into January. Can you give us a rough feel for what it might have been in January, into the 40% now and what level does it have to be for you to be at this revenue breakeven level?

And secondly, just looking big picture at your margin guidance, still a little bit of a mystery where this margin erosion is going to come from. If Fusion continues, good margins there. Results seem to be doing better. Is your guidance simply cautious or should we be expecting some margin erosion in one or two operations and what might those be please?

Eva Castillo - *Chairwoman & CEO Telefónica Europe*

Okay, with regard to your first part of the question, just to reemphasize that what we are giving up till December is a mix of 30% new services and we are talking about working towards revenue breakeven in 2013, which is already a positive statement. In terms of margin breakeven, we have already got the net adds in December in positive territory. I hope that is clear.

José María Álvarez-Pallete -*Telefónica SA - Chief Operating Officer*

Taking your question on the margin guidance, we get back to the issue if the trends that we have been experiencing in 2012 are sustainable or not and we think they are sustainable because they are structured under our transformation of the operational model. To be more precise, for example, TGR has raised more than EUR1 billion of OpEx and CapEx savings that has been transferred to the businesses. And therefore, this is playing the scale of the group that it is even increasing because now we are increasing the scope and decreasing the responsibility of TGR.

So on top of that, are we being cautious or not? We think that we need to preserve the optionality of growing faster in Latin America if the market is there and therefore, we are keeping some room to manoeuvre to accelerate the market in Latin America if the market is there in a profitable way. So we are keeping, we are trying to keep both options. I mean the sustainability of the transformation of the business that we are doing and the possibility of accelerating our growth.

Keval Khiroya *- Deutsche Bank - Analyst*

If you don't mind, I have got two questions, one on the UK and one on Spain. The UK was less bad this quarter, but the OIBDA was still falling 9%. So how far do you think we are from revenue and OIBDA stabilization? What do you need to do to get there?

And, second, on Spain, just touching back on the OpEx in a slightly different way. How much further do you think commercial costs can fall in 2013 if Fusion continues with its current rate of success? Could it be similar to 500 million euros savings in 2012 or would it be higher or lower? Thank you.

Eva Castillo *- Chairwoman & CEO Telefónica Europe*

Thank you very much. With regards to the UK, as you know, we are very happy with what happened in 2012, which is a combination of a very balanced commercial momentum and profitability. The reality is that we are seeing a more rational market in the UK and it has been illustrated so far by contract price increases from inflation which impacted our operation in the UK, in particular Telefónica UK increased prices by 3.2% actually from today.

The other thing which was important to highlight is that we got close to 1 million contract base growth in 2012 and very importantly, we continue to work towards growth in revenue and profitability on the back of this strong commercial momentum that we have experienced. We need to continue and we will continue stabilizing OIBDA while we continue working in driving efficiencies and, obviously, growing our client base. That is the focus in the UK.

With regards to OpEx in Spain, as you know we cannot release levels -cost levels- but just to give you an idea: we believe the model is sustainable and we have other initiatives in Spain (i.e. insourcing, i.e. increase of productivity) that our team led by Luis Miguel are working very hard on. So just to give you an idea, that is the only thing I can say.

Paul Marsch *- Berenberg Bank - Analyst*

Thank you very much. Back to Fusion again. You talked about 30% of new Fusion connections, or new services rather. What about the proportion of new customers? Have there been any new customers? Or, what proportion of new customers are coming to Fusion?

And then, if I think about the services, if you signed say 500,000 new services, about 30% of the total 1.5 million, it looks from your churn statistics on broadband and from the mobile adds that about 300,000 of those were broadband connections or broadband services and 200,000 were mobile services. Is my calculation about right on that? Thank you.

Eva Castillo - *Chairwoman & CEO Telefónica Europe*

Just to clarify, when we speak about 30%, we talk about 30% new clients. So that is the figure I can give you specifically on the proportion of clients within the totality of Fusion. And I think that I am not sure if I can give the other figures. But in terms of fixed broadband, we have already obtained 130,000 net adds in the quarter and we need to emphasize that that is the major important figure we provide in fixed broadband.

Paul Marsch - *Berenberg Bank - Analyst*

But I think from your churn statistics, I can work out that your gross broadband adds were about 600,000 I think. And that doubled by the looks of it. So can I assume that the increase there is all driven by Fusion?

Eva Castillo - *Chairwoman & CEO Telefónica Europe*

Well, I think that the main message I can give here is that there was an important increase in net adds because of Fusion. You have to count as well the churn, but the reality is that it is very strong, and it is very strong in particular in fixed broadband.

César Alierta - *Telefónica SA - Chairman & CEO*

Thank you, everybody. This is Cesar Alierta. Two years ago, we started the transformation of Telefonica. We created Telefónica Digital unit to grow revenues, we created the Telefónica Global Resources to reduce our costs and increase efficiency and we created two regions. As my colleagues in the Ex-Com have said during this conference call, the key of Telefónica is transformation and simplicity. Transformation and simplicity, and you have seen the numbers, are flowing into increasing the profitability of our business clearly.
2012 was a clear example. 2013 is going to be much clearer.

And I would like only to add two comments. There are two things that are happening in this sector, which are extremely important and are going to be reflected in the profitability of digital telcos like Telefonica.

One, which we think is extremely important, is the Firefox operating system and everything that is going to be implied in the change in the value chain. And this is going to be reflected this year and next year.

And another thing, which I think is extremely important for Europe, is the new approach by the European Union to have a single digital agenda, which is going to be real digital telco players. We are going to be in the most appropriate position for everything this year and the coming years. It is a fact that the two last comments are not reflected in guidance, but let me tell you the results of these new policies are going to be very, very, very positive in the profitability not only of Telefónica, but of the real players in the digital world.

Thank you very much and on behalf of my colleagues for your questions in this call and I wish you a very good evening. Thank you very much.