Sixth Investor Conference

Integrated strategy to capture organic growth

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Overview

Our organization is ready…

From…

TdE | T-Latam | T-Móviles | O_2

Integrated management *with special focus on coordinating fixed and mobile businesses*

To…

Telefónica España | Telefónica Latino-américa | Telefónica O2 Europe

Integrated management *with special focus on leveraging global scale*

…to exploit the opportunities ahead

Industry transformation is creating the New Global Digital World

- **Sources of growth**
- +
- **Integrated delivery**
- +
- **Benefits of scale**

Content

Extracting value of industry transformation

- Sources of growth
- Integrated delivery
- Benefits of scale

GLOBAL GOALS

- *Mobility and Broadband are driving a New Digital World around the customer providing plenty of opportunities*
- *We have aligned our organisation to capture these opportunities*

A New Global Digital World has emerged

Customers	Devices	Network	Digital services and content	Service providers

Customers

New consumer trends

Devices

Mobile
- **513 m** mobile phones

PC
- **193 m** PC's

Multimedia equipment
- **24 m** households with **game consoles**
- **44%** households with **digital cameras**

Hyper connectivity

Network

Broadband users
2001 —x13→ 2006

Bandwidth
2001 —x40→ 2006

Broadband Access F+M

IP Digital Network

Traffic
2001 —x25→ 2006

IP traffic: >90%

Bandwidth and volume

Digital services and content

- **6,400 m** MMS sent per year
- **65 m** online community members

- **1.5 m** IPTV users
- **36 m** mobile games downloads
- **72 m** blog users

Proliferation

Service providers

Telecom operators

Internet players

Other service providers

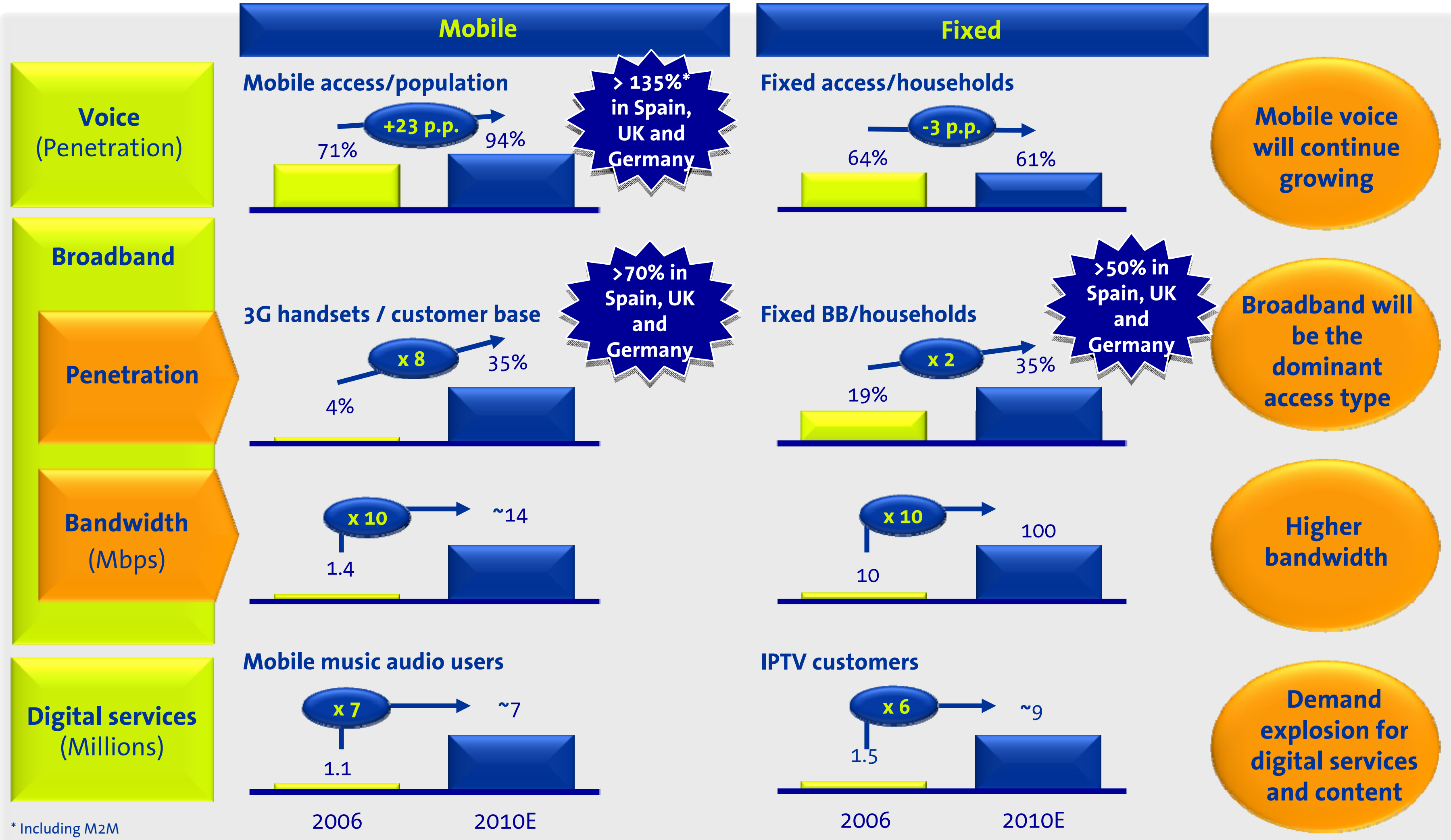
New business models

Note: Data for 2006 in Telefónica markets
Sources: Pyramid, Euromonitor, Yankee, Ovum, WCIS, Comscore and internal estimates

The industry transformation gives us clear opportunities

From the "old" world…	…to the New Global Digital World	Opportunities for Telefónica
▪ **Corporations** drove evolution ▪ Offering around **voice** ▪ Services depended on **location** ▪ **Duration** mattered	▪ **Consumer** needs drive evolution ▪ Multiple services on top of **broadband** ▪ **Mobility** is critical ▪ **Applications** are key	**Sources of growth**
▪ **Ad-hoc, specific** services and **individual** product offering ▪ Services provided over **specific networks**	▪ **Seamless** services and **bundles** ▪ A **common network** can support all kind of services	**Integrated delivery**
▪ **Local portfolio** and local offer ▪ **Local suppliers** ▪ **Local** technological **standards**	▪ **Global portfolio** and local offer ▪ **Global suppliers** ▪ **Global** technological **standards**	**Benefits of scale**

Sources of growth



* Including M2M
Note: Data in Telefónica markets
Sources: Pyramid, Yankee, and internal estimates

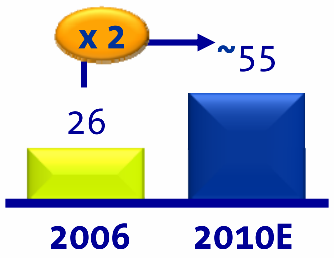
Integrated delivery

Integrated delivery will facilitate a set of opportunities…

To address customer needs

- Access to **any type of service** from **any type of device** in a **seamless** way
- Attractive, easy and user-friendly **customer experience**

Bundles* Telefónica's markets Millions



To achieve operational excellence

- **Efficiency improvement**
  - OpEx and CapEx reduction
  - Better use of resources
- **Better quality**
  - Key differentiation factor
  - Sustainability of price premium

…and technology will enable it

"All IP" networks and platforms

Content Digitalisation

*Includes 2P and 3P bundles

Benefits of scale

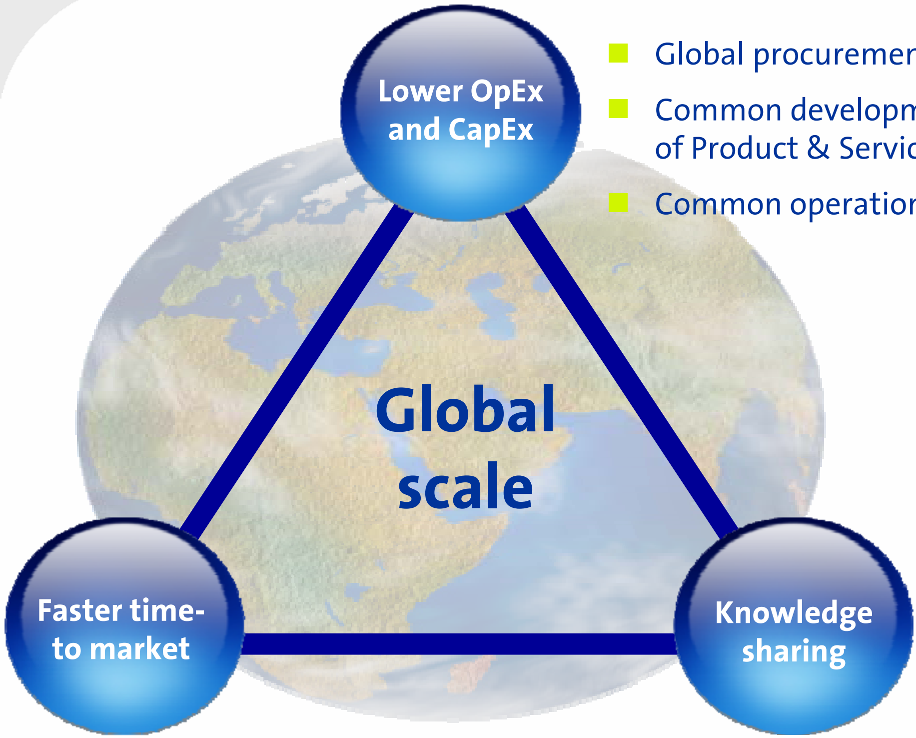
The New Global Digital World ...

Customer needs are increasingly more global

Suppliers are more global

Technology is more global

...provides new opportunities



- Global procurement
- Common development of Product & Services
- Common operations

- Faster deployment of services

- Best practices transferred across countries

Content

Extracting value of industry transformation

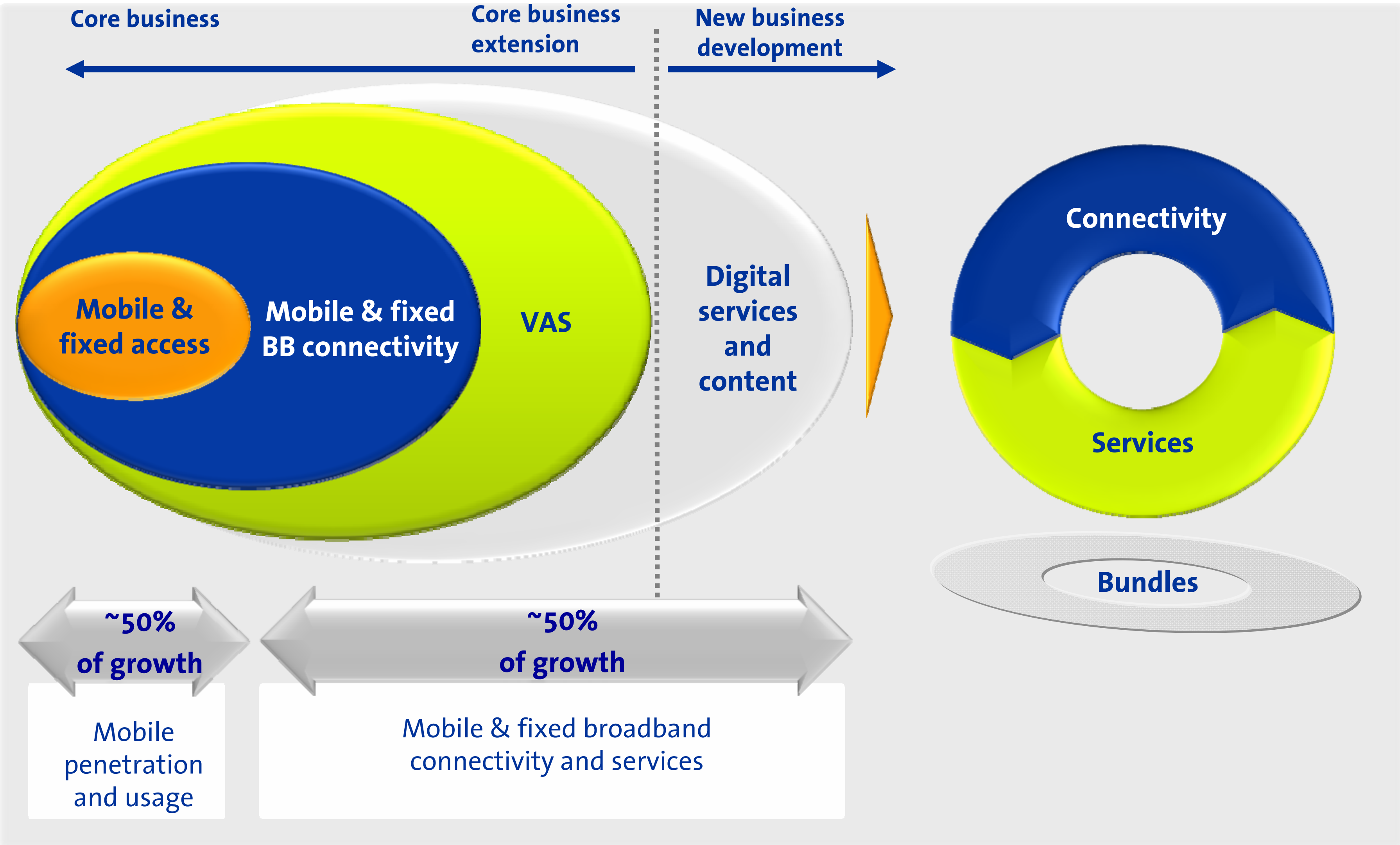
- Sources of growth
- Integrated delivery
- Benefits of scale

GLOBAL GOALS

To capture growth opportunities we will…

- *Continue capturing mobile voice growth and promote our traditional business*
- *Push broadband connectivity and develop digital services for mobile (mobile data) and fixed*

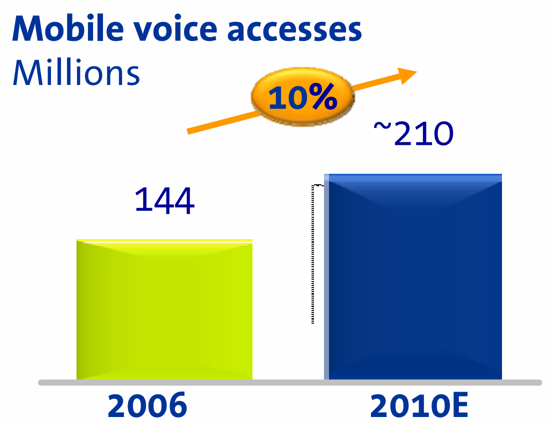
To capture the sources of organic growth we have a strong focus and clear strategy

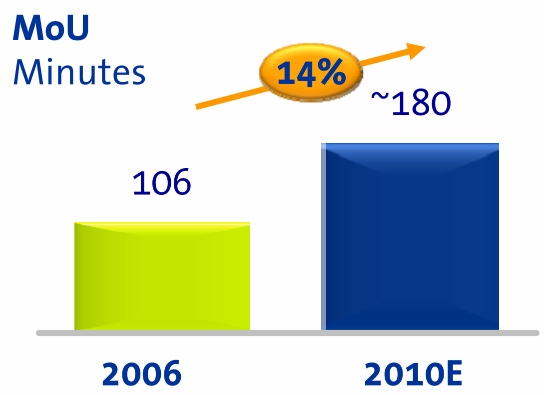


Mobile voice will be our major revenue growth engine

Key levers	Mobile voice
Customer growth	■ Capture **mobile penetration growth** focusing on **coverage and commercial offer**
Churn	■ Increase customer satisfaction through **"Customer Experience"** and **loyalty programs** ■ Move proactively from **pre-paid to post-paid**
Migration	■ Manage **fixed to mobile substitution** optimally, depending on our assets and market conditions
Pricing and ARPU	■ Increase **MoU** through: – Tariff management (price elasticity) – New semiflat rates

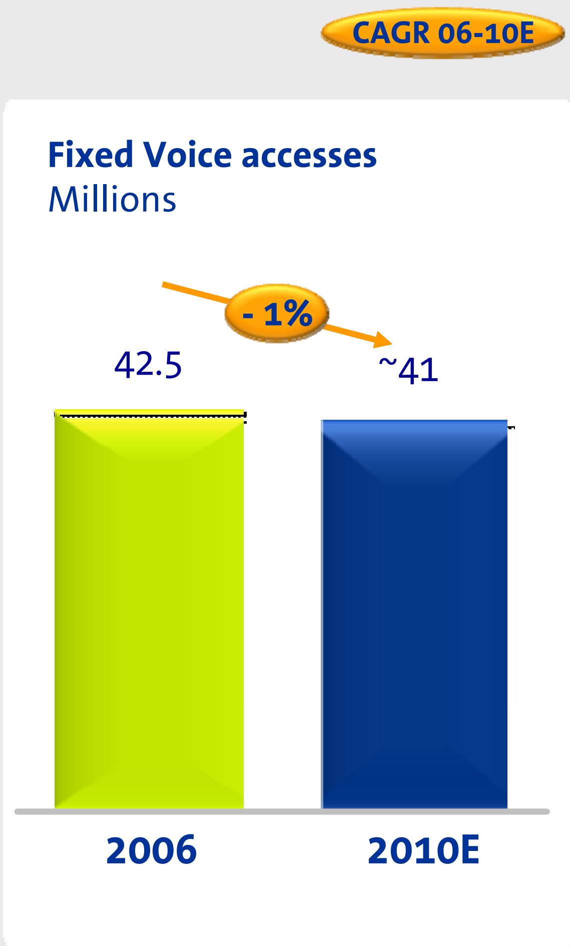
CAGR 06-10E





We will promote fixed access and voice

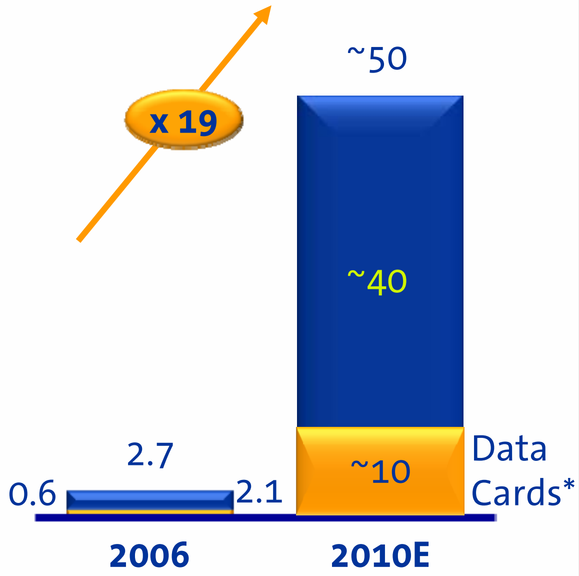
Key levers	Fixed access and voice
Customer growth	▪ Transform fixed access into **multiplay** and **multipurpose** lines ▪ Foster fixed line adoption through **promotions**
Churn	▪ Ensure customer retention through **loyalty programs**
Migration	▪ Continue managing successfully **voice to VoIP migration**
Pricing and ARPU	▪ Extend use of **flat rates** and voice **packages**



Mobile Broadband is showing real signs of taking off

Key levers	Mobile Broadband
Customer growth	■ **Accelerate enablers:** — Roll-out of 3G (UMTS/HSxPA) coverage — Push data cards
Churn	■ Leverage **best practices** for churn prevention and customer retention
Migration	■ **Bundle Fixed BB and Mobile BB** to maximize overall growth while avoiding unwanted substitution effects
Pricing and ARPU	■ Develop **flat /semiflat rates** ■ Offer **new pricing schemes** for **mass market** segment

3G users
Millions



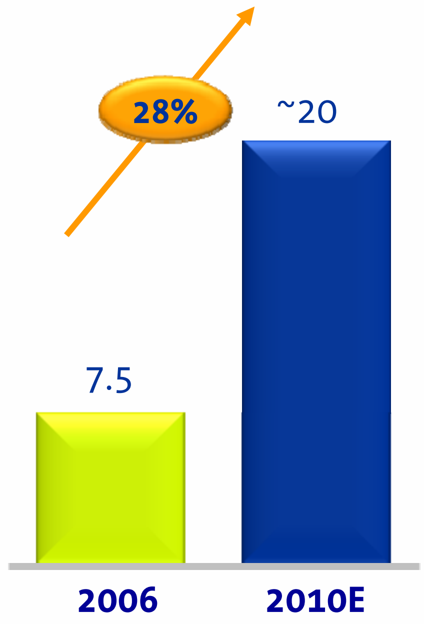
* USB modems and PCMCIAs

Fixed Broadband will be the major driver for wireline business growth

Key levers	Fixed Broadband
Customer growth	■ **Capture penetration-driven growth** (price segmentation, high speed offers, bundling)
Churn	■ Extend **commitment contract policy** ■ Strengthen specialized **retention call centres**
Migration	■ **Continue managing migration effects**: - NB to Fixed BB is over - LL/FR* to BB is being completed
Pricing and ARPU	■ Manage **price premium** leveraging brand and superior quality ■ **Generate additional ARPU** through new services

CAGR 06-10E

Fixed BB Internet connections
Millions



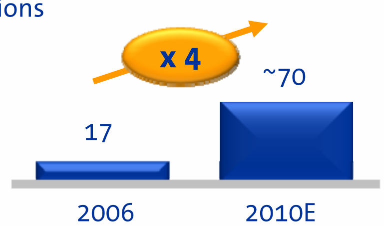
* Leased Lines / Frame Relay

Digital services and content will further contribute to growth

Mobile

- Develop new services with **open garden approach:**
  - Information (e.g. search)
  - Communication (e.g Instant Messaging)
  - Entertainment (e.g. Music, TV)
- **Stimulate Internet usage**, monetising it through data traffic, advertising and pay-per-use
- Foster **friendly** data-enabled **handsets**

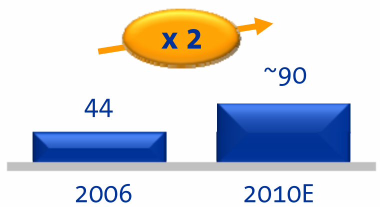
Mobile data active users*
Millions



PC

- **Attract online audience and monetize it**, mainly through advertising
  - Internet TV + Music (Terra TV, Pixbox)
  - Communities (e.g. “Espacio Terra”)
  - User Generated Content (e.g. “Tú Reportero”)

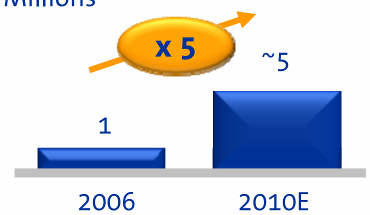
Terra unique users
Millions



TV

- “Personal TV” based on **IPTV**
- **Satellite** to reduce time-to-market
- **Cable** only to leverage existing assets (e.g. Perú)

Pay TV customers
Millions



* Non SMS data active users for the last 3 months

We are working closer with key partners

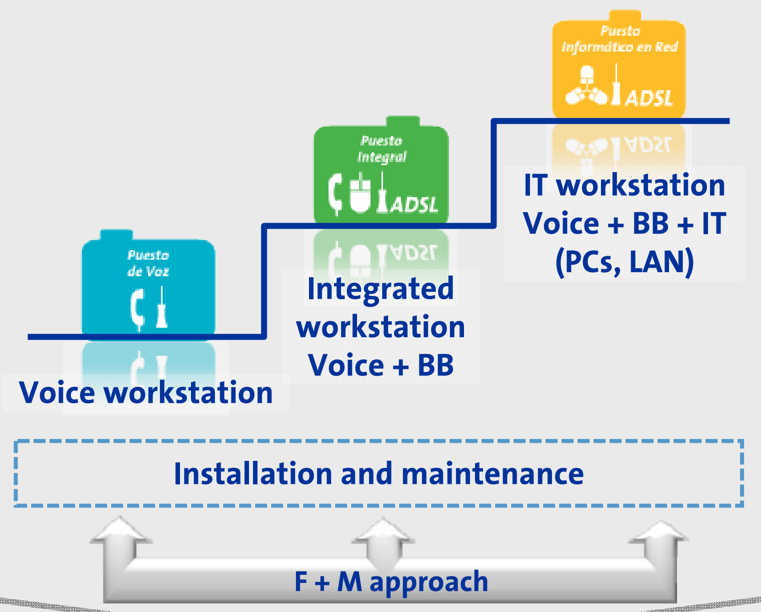
Mobile	PC	TV
Google, RIM, Apple, YouTube, Yahoo!, myspace.com a place for friends, facebook, msn, flickr, NOKIA, Discovery Channel, MTV Music Television	Google, SONY, Concurso Vc Diretor, tú reportero, Discovery Channel, MTV Music Television	Sogecable, TV Globo Internacional, The Walt Disney Company, Paramount, Warner Bros, Sony Pictures, Discovery Channel, MTV Music Television

Services and Content (Cross-platform approach)

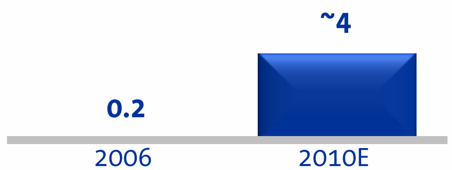
- **Partnerships** with third parties to develop and offer **innovative services and applications**
- **Partnerships** to acquire and distribute **content**
- **Aggregation and distribution of content**
  - Modularity, flexibility and advanced functionalities as main differentiation factors
- **User Generated Content** offerings (e.g. web 2.0.) leveraging Telefónica's own platforms and 3rd party products

ICT solutions will be a source of growth in enterprise segments

SMEs



Number of workstations
Millions



Corporate

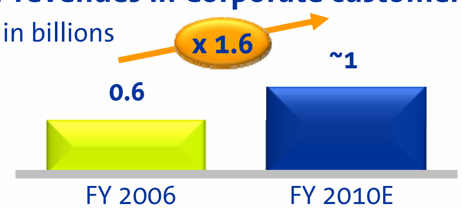
Focused and "industrialized" approach

- Integrated Communications (Voice + Data) (F + M)

+

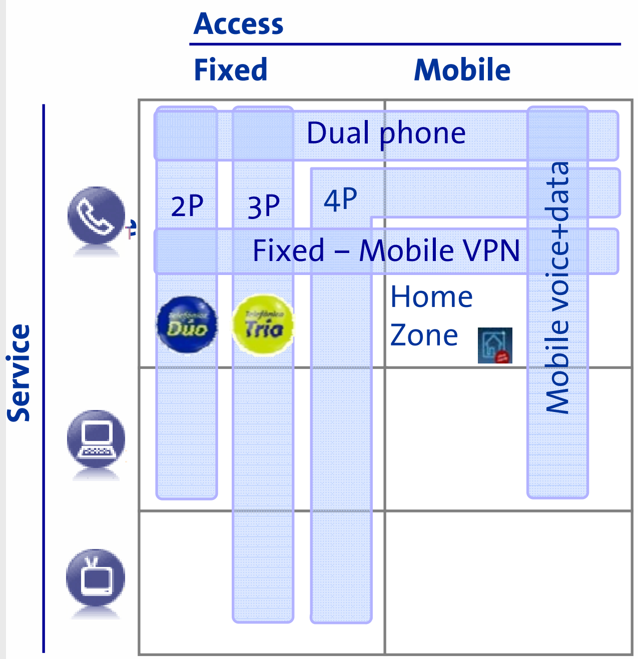
- Workstation management
- Infrastructure outsourcing
- Contact centres
- Security
- Digital asset management
- Mobility
- CRM Solutions

IT revenues in Corporate customers
€ in billions



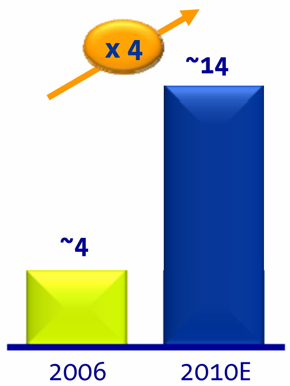
Bundled and convergent offers will help us to capture growth in all our markets

Multiservice and multidevice convergence…



… with different approaches

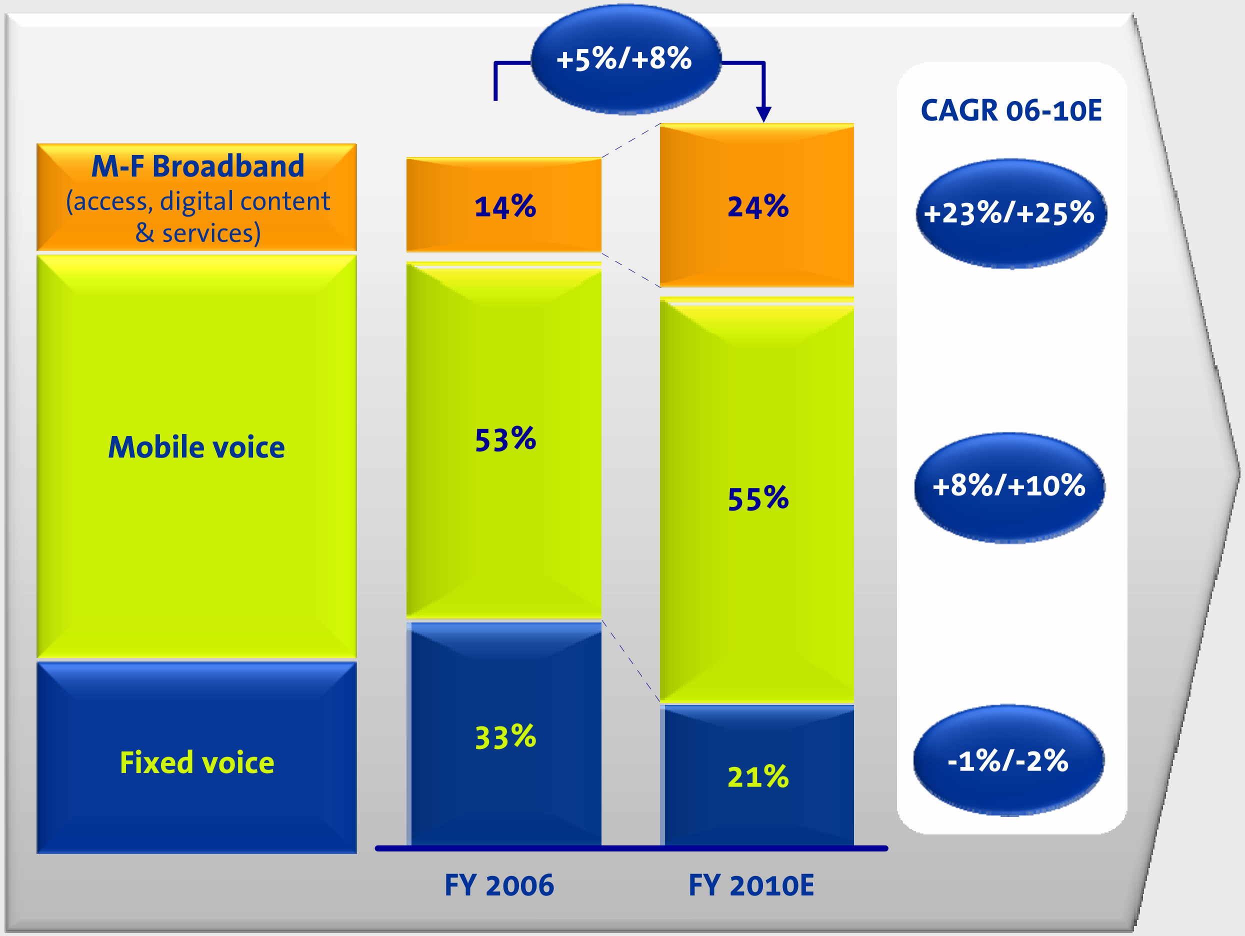
Bundles 2P/3P
Millions



Bundling has already proved to be effective
(78% of Telefónica's retail BB connections installed base as of June 07 in Spain is bundled)

As a result, we are positively rebalancing our revenue mix

Revenue mix



- **Broadband** (access + digital services & content) **will increase its contribution significantly**
- **Mobile voice will keep increasing its weight in our mix**
- **We will become less dependent on fixed voice**

Content

Extracting value of industry transformation

Sources of growth

Integrated delivery

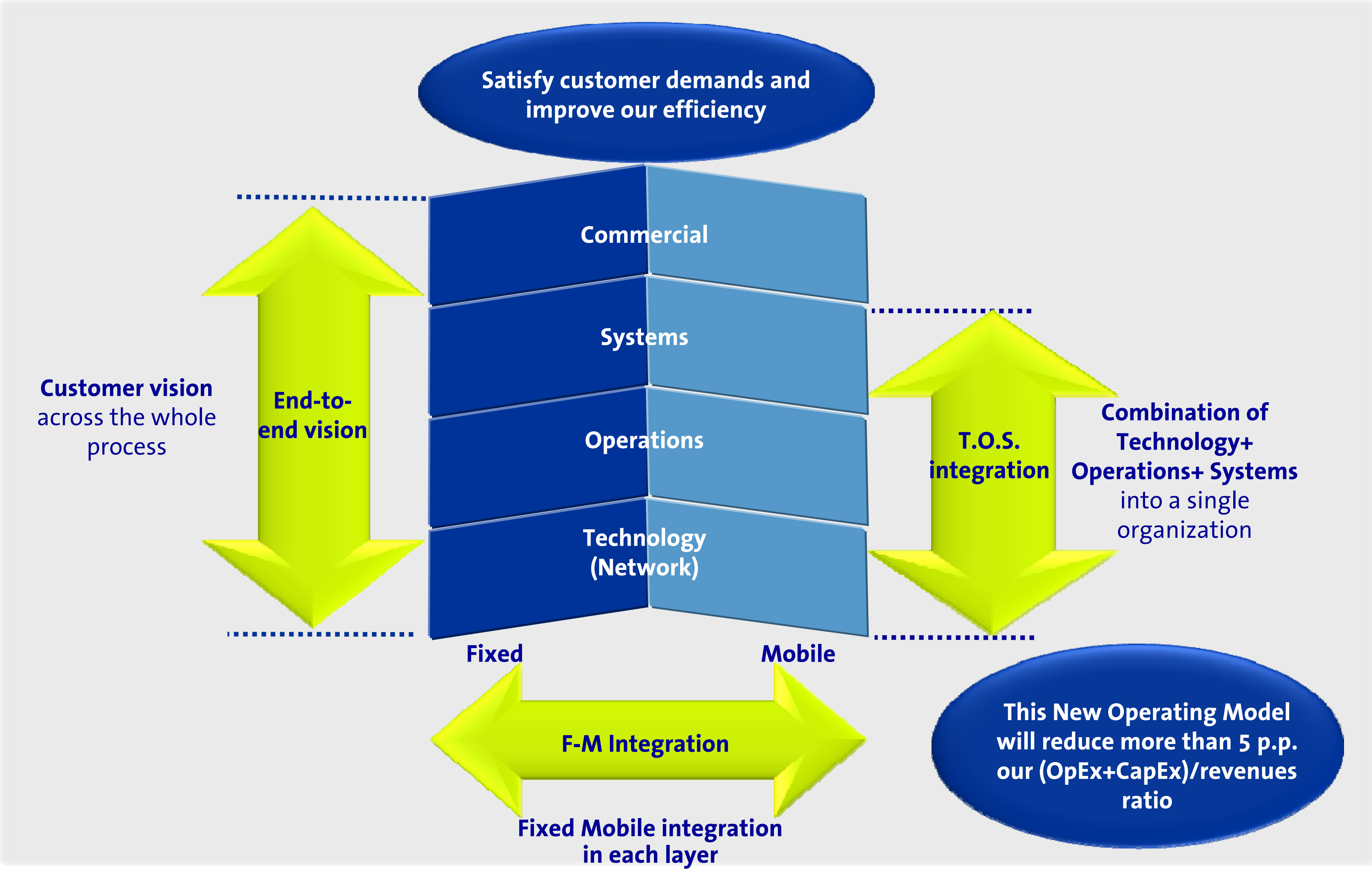
Benefits of scale

GLOBAL GOALS

*To ensure the **best integrated delivery** and capture growth opportunities in a cost-effective way we have developed a **New Operating Model***

- ***Fixed-Mobile integration***
- ***Technology, Operations and IT Systems integration***

We will support organic growth through an integrated delivery



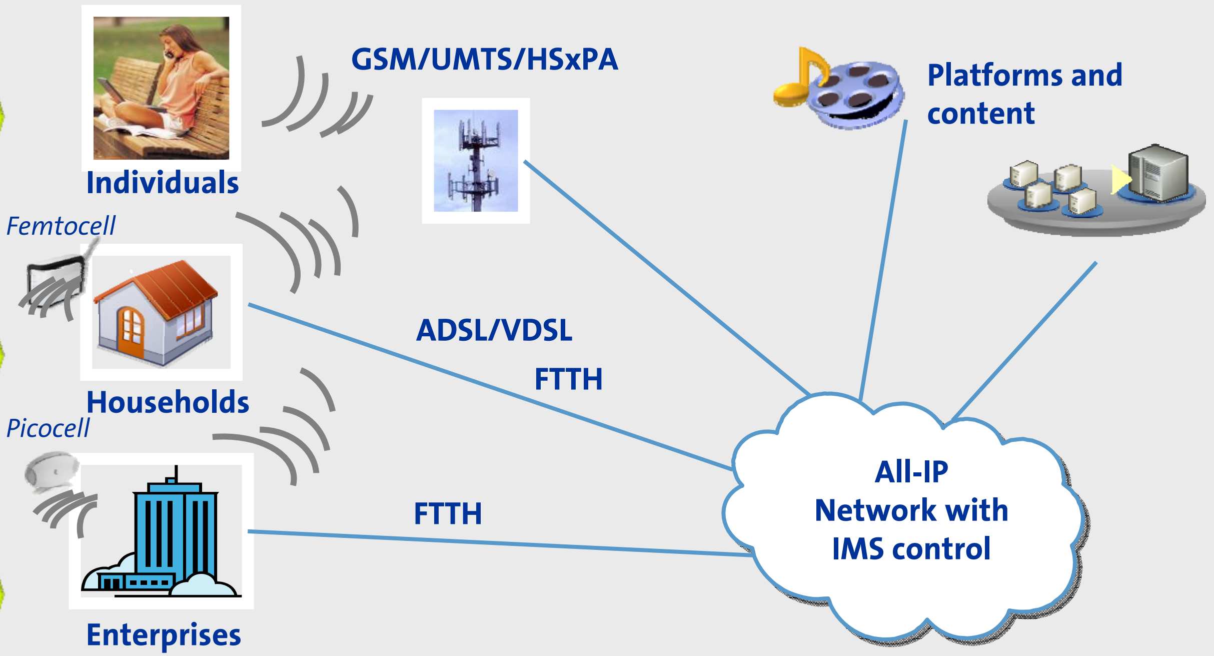
A new integrated broadband network will support growth needs in an efficient manner

Goals of network development

- **Enable growth** through new services
- **Respond to competitive environment** in each market
- **Optimize OpEx and CapEx**

Network strategy (% of OpEx and CapEx)

Access network (70%)	**Backbone network** (30%)



Access network adapted to customer needs and competitive environment	Convergent IP backbone network to support integration and efficiency

Note: Data for 2006. OpEx and CapEx figures for Telefónica España

Our access network strategy will balance market needs and technological opportunities

Strategic approach	Mobile access	Combined access	Fixed access
Countries with fixed and mobile operations	■ **GSM-UMTS-HSxPA** is already the technology of choice in all our operations ■ We foresee **LTE** (4G) as the next technological evolution	■ **"Domestic nodes"** to improve indoor coverage and optimize CapEx ■ **Wireless technology** (2G, 3G, Wimax if necessary): — To expand coverage of fixed services — To offer an integrated portfolio (e.g. Venezuela) where LLU is not available	■ **BB rollout** following a micro-segmented approach — **FTTH** for high capacity access — **VDSL** avoiding street cabinets
Mobile-based countries			■ **ADSL 2+** rollout where **ULL** is available (UK, Germany and Ireland) ■ Other alternatives depending on local conditions

Access network strategy will be aligned with evolving regulatory framework

An "all-IP" network will provide innovative and convergent services

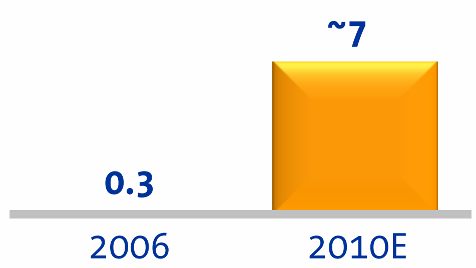
Single F-M integrated "all-IP" backbone network

- **Development of new and convergent services** (VoIP, IP Centrex, IP VPN,...)
- **Faster time to market for convergent services**
- **OpEx and CapEx** reduction through the integration of IP networks and platforms

Selective roll-out of VoIP

Non-PSTN voice customers (VoIP + IP Centrex + IP VPN)

Users



- VoIP deployment linked to FTTH roll-out in Spain and Latinamerica
- VoIP already offered as first voice line in some markets (e.g. Germany)

Controlled PSTN Network Evolution

No major shutdown of the PSTN network is planned :

- The replacement of more obsolete parts is selective and optimally managed
- Real estate efficiencies are being captured

An integrated approach to Operations and IT Systems will allow us to satisfy customer needs in a cost-effective way

Integrated operations

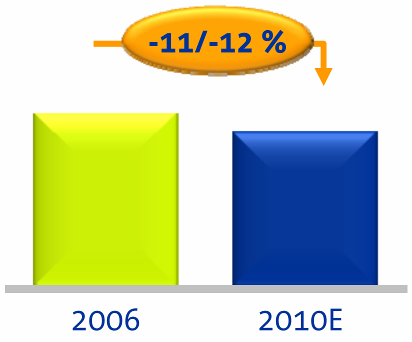
F+M integration

- **Single local F-M field forces, network** deployment, supervision and operation

Relationships with third parties

- Further **outsourcing** (e.g. logistics, I+M)
- Align I+M subcontractors with **cost and quality targets**

OpEx / access



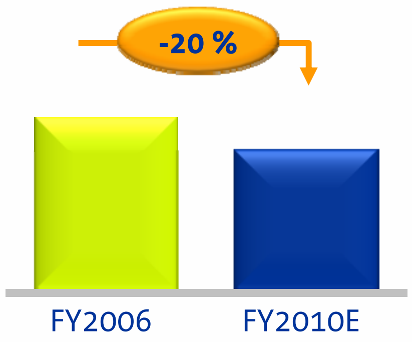
Integrated approach to IT

F+M IT integration

Unified convergent application systems
Support of customer demands and faster time-to-market

Consolidation of IT infraestructure
CapEx+OpEx reduction

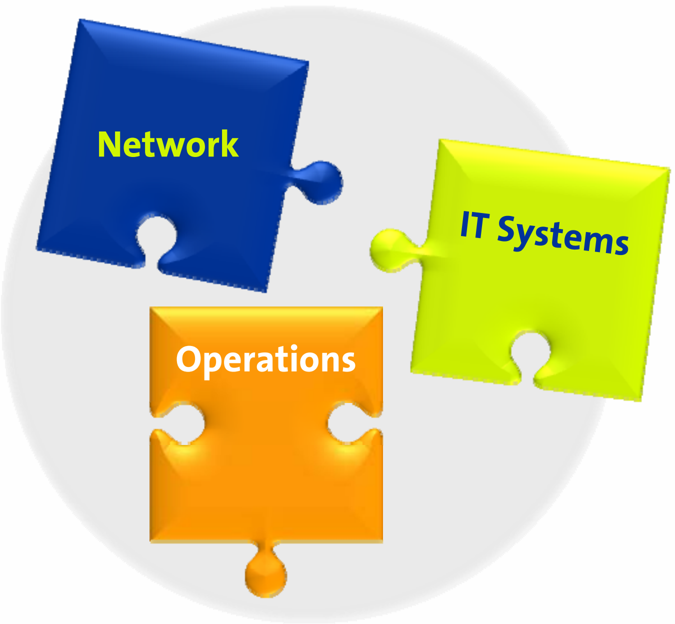
IT spending / revenues



By integrating Technology, Operations and IT Systems we are optimizing end-to-end delivery

From...	To...

From...



Three areas focused on optimizing the individual parts of each process

To...

T.O.S.

- **Unified point of contact** for business units (unified SLAs)
- **Common and aligned understanding of priorities**, resulting in **faster time-to-market**
- **Flexible resource re-allocation**, optimizing OpEx and CapEx

One area focused on optimizing the end-to-end process

An integrated commercial approach will allow us to meet evolving customer needs

	Marketing	Sales	Post-sales / Back-Office
			
Countries with fixed and mobile operations	▪ **Unified customer vision** enabled by common marketing and pre-sales teams ▪ Development of **integrated products and services**	▪ Integrated **F-M account management** for **Corporate clients** ▪ Unified management of **indirect channels** and **own stores** ▪ Coordination of **call centres** and **sales forces** ▪ Progressive unification of **online channels**	▪ **Single point of contact** for **Corporate Customers** ▪ **Back-office coordination for SMEs and Residential** to improve customer care
Mobile-based countries	**Integration of new Product & Services** (e.g. ADSL) **into existing processes and channels**		
	Higher customer focus	**Higher Sales efficiency**	**Higher service quality**

Content

A distinctive "way of working" enables us to capture significant benefits of our scale

- *Leveraging local integrated delivery*
- *Fostering regional integration*
- *Maximizing global benefits through horizontal cross-regional actions*

We are leveraging the benefits of our scale through a three-level approach while maintaining our agility and local market responsiveness

We are implementing our integrated delivery model in each country

Integrated delivery adapted to local market conditions and existing assets

	Cooperation	Integrated delivery	Full integration
Countries with fixed and mobile operations	Brazil Chile	Spain Peru Argentina Colombia	Czech Republic
Mobile based countries		Mexico Uruguay Ecuador Panama Slovakia Venezuela Morocco El Salvador Guatemala Nicaragua (Venezuela to Nicaragua: **Main operations with fixed-wireless**)	Germany UK Ireland

~€1.9bn*

*Cumulative operating cash flow (OIBDA-CapEx) 2007E-2010E

We are fostering integration at a regional level

Regional integration of Technology, Operations and Systems

- Network deployment, supervision and operation
- Services platforms
- SW factories
- Consolidation of data centres
- Back-office integration for key processes

~€2.2bn*

Regional commercial approach

- Brand homogenization
- Development of products and services (e.g. DTH TV in Latam)
- Common commercial actions across countries (e.g. Advertising campaigns in Latam)

*Cumulative operating cash flow (OIBDA-CapEx) 2007E-2010E

We are also fostering global horizontal cross-regional actions to maximize scale benefits

Doing things "only once"

A well defined set of actions through different "vehicles"

Cross Regional Units
- MNC
- International traffic
- Roaming

Centres of Competence
- IPTV
- Internet PC
- Mobile data

Shared services
- Procurement
- Administrative support
- R&D

Coordinate activities, leverage global scale and share resources

+

Sharing knowledge and experience

Tools and processes to share knowledge
- Virtual communities of experts
- Library with all Telefónica shared information
- Groups to implement best practices

"Commercial wings"
- Segment-specific commercial practices

"Technical wings"
- Network
- IT

New culture that encourages innovation

Leverage our diversity and knowledge across regions

~€3.4bn*

*Cumulative operating cash flow (OIBDA-CapEx) 2007E-2010E

We are already extracting the benefits of our way of working

Global purchasing power

- **€24bn** of purchasing volume in 2006, generating **a 10% savings*** and enabling us to be one of the most preferred customer of our suppliers

Contribution of new acquisitions to Telefónica´s "new way of working"

- The integration of **O2** in Telefónica is a **successful example of integration:**
  - **44 managers** have moved between O2 and the rest of units
  - 81% of the **roaming traffic** already internalized
  - **Centre of Competence for Mobile Data** based in UK
  - "**Customer Experience" methodology** transferred across Telefónica
  - Support the transformation into an **integrated operator**
  - Target of €**155m in synergies O2/TEF for 2006** achieved

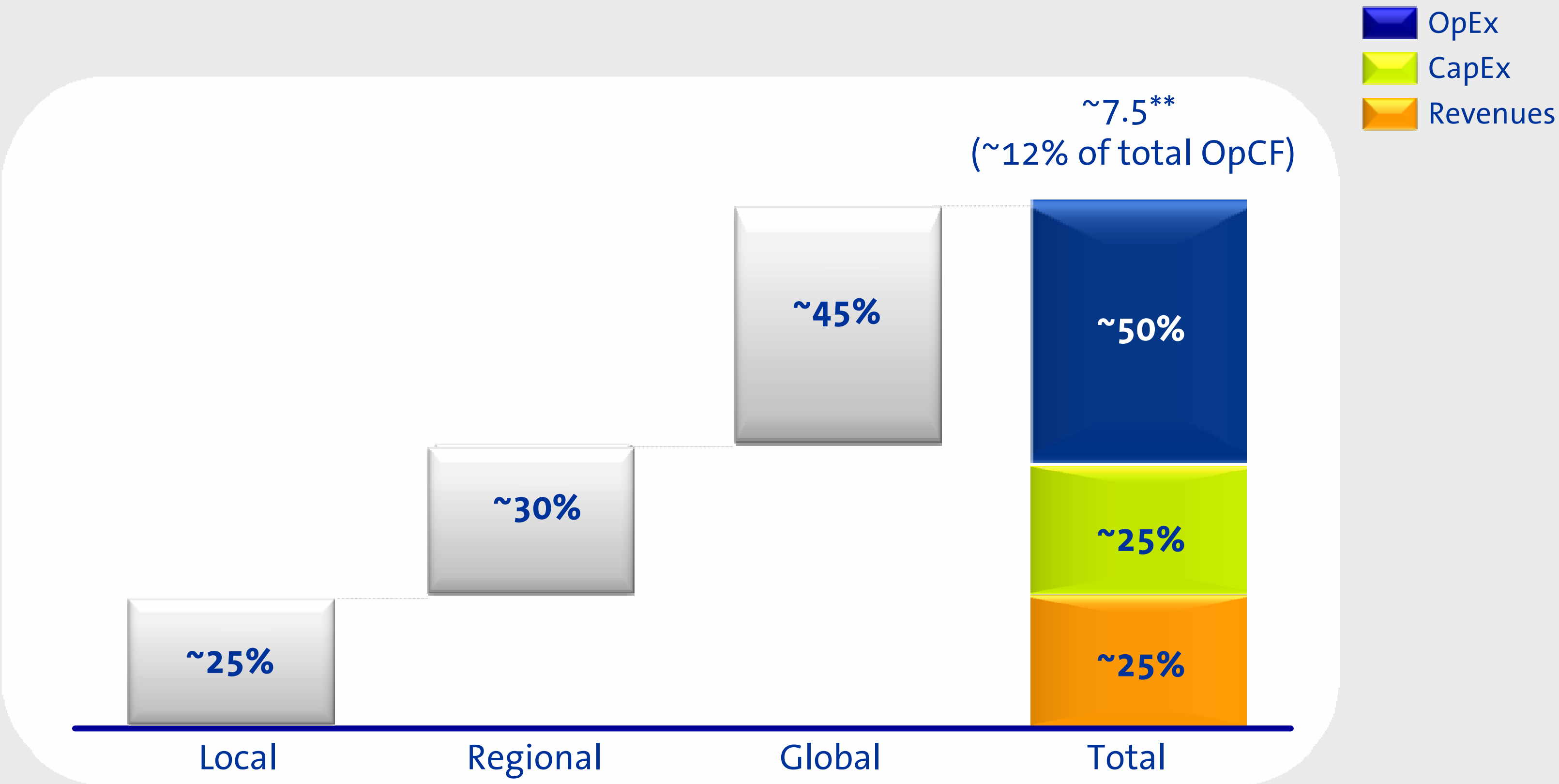
Alignment of managers incentives to shareholders interest

- **New incentives policy** across Telefónica already in place ***(Performance share plan)*** to foster alignment to company's business results and retain talent

*Only purchasing savings due to the integration of new companies (O_2) are included in the synergies guidance (historical purchasing savings not included)

The way we work allows us to create value through synergies

Synergies: Operating Cash flow* 2007E-2010E
€ in billions



The new **2007E-2010E guidance is 42% higher** than the 2006E-2009E guidance given in Valencia

*Operating cash flow= OIBDA – CapEx
**Already included in the overall guidance

Content

Through this triple effort we will enhance our leadership and competitive position, providing superior growth and returns

In summary...

Industry transformation is creating the New Global Digital World

Sources of growth
- > 290 m — Accesses in 2010E
- ~50 m — 3G users
- ~20 m — Fixed BB accesses

+

Integrated delivery
- > 5 p.p. — (OpEx+CapEx)/ revenues reduction 2006-2010E

+

Benefits of scale
- ~€7.5 bn — Synergies for the 2007-2010E period

Telefonica