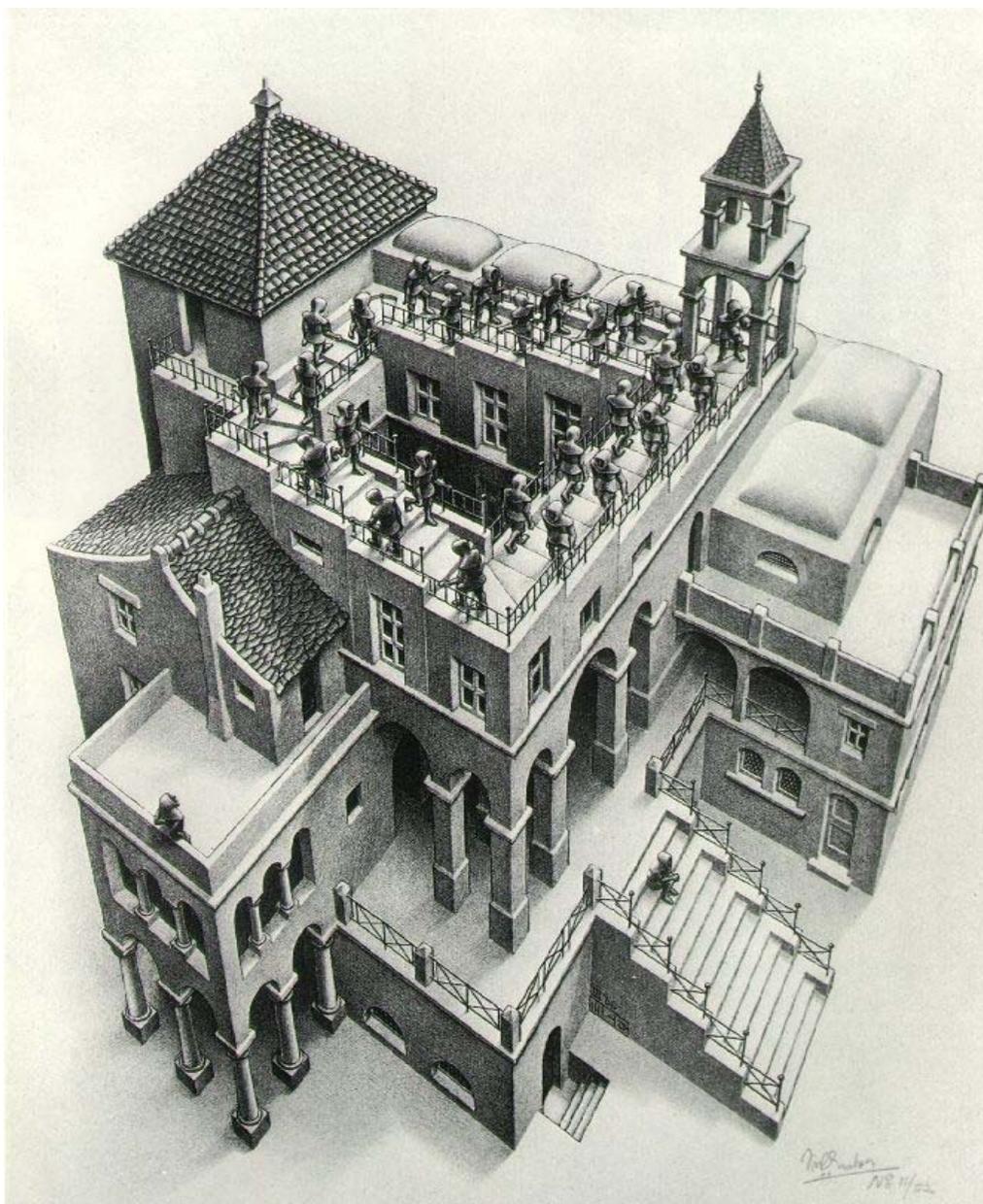


# Sixth Investor Conference

ASCENDING & DESCENDING

Santiago Fernández Valbuena  
London, October 11<sup>th</sup> 2007





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# Index

## 1 **Timing the execution**

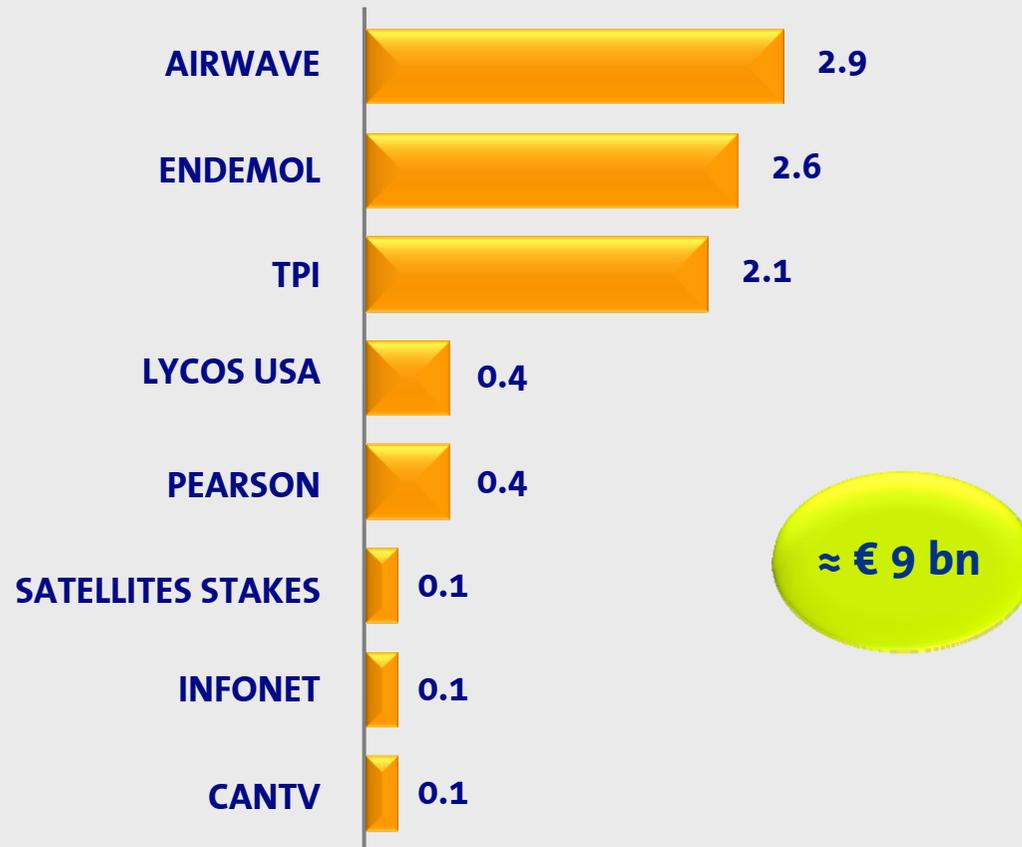
2 Meeting commitments

3 Cash flow and Uses

4 Conclusions

# 1 Active portfolio rotation to drive value creation

## TELEFÓNICA'S DIVESTMENTS 2004-2007 € in billions



# 1 Timing is key in any transaction

**AIRWAVE**

Deal Proceeds € 2.9bn  
 Net Capital Gain € 1.3bn  
 EBITDA Multiple **21.8x**

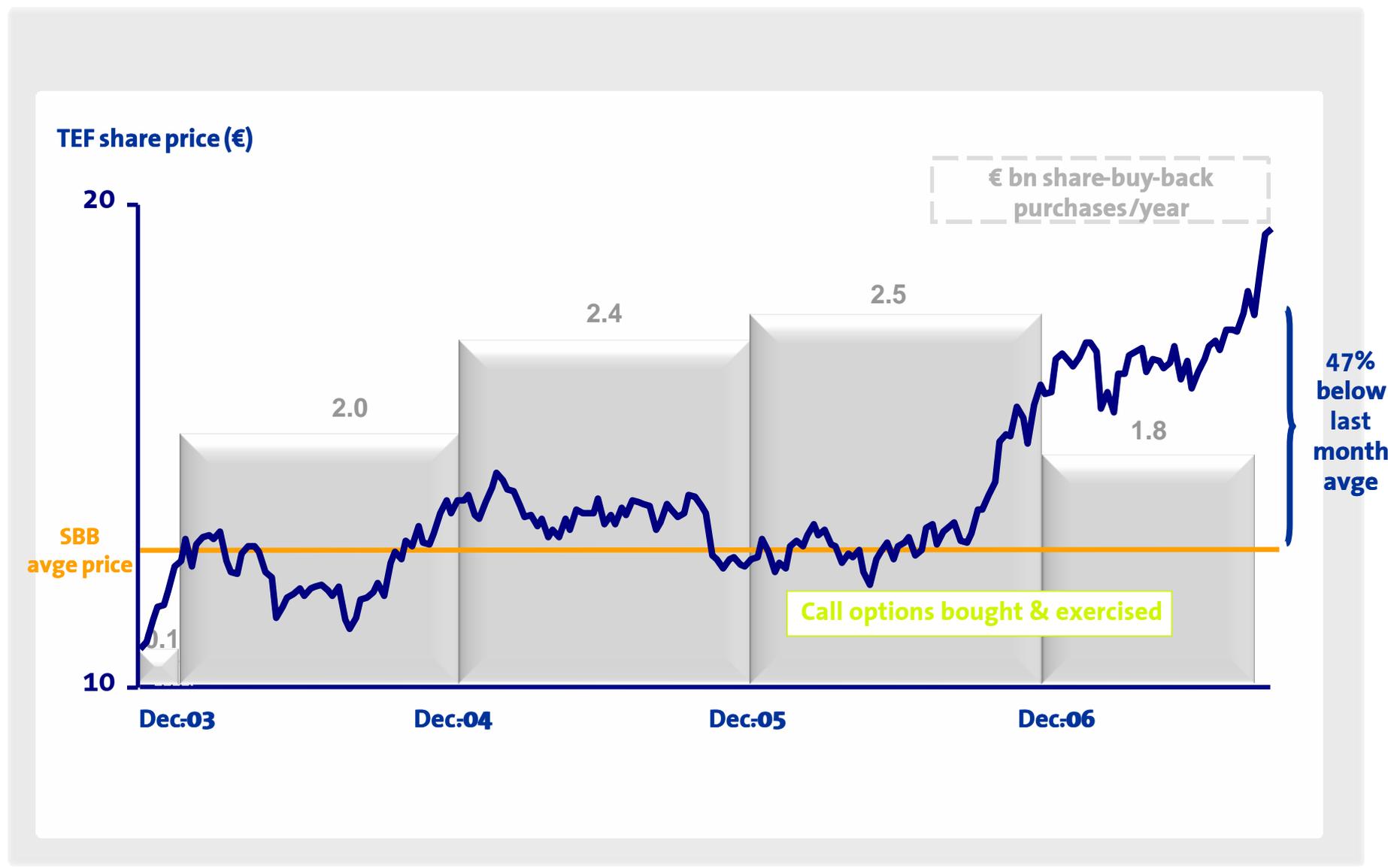
**ENDEMOL**

Deal Proceeds € 2.6bn  
 Net Capital Gain € 1.4bn  
 EBITDA Multiple **17.2x**



(1) Includes MCG, Fraport, Abertis, Autostrade, Brisa, SIAS and Cintra  
 (2) Includes Antena 3, Tele5, M6, Mediaset, ProSiebenSAT.1, RTL and ITV

# 1 €9bn shares bought back at nearly 50% below last month average price



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## 2 Meeting commitments

**2.1** Delivering on financial guidance

**2.2** Debt issues and debt issuance

**2.3** Hedging policy

## 2 Delivering on Valencia's commitments



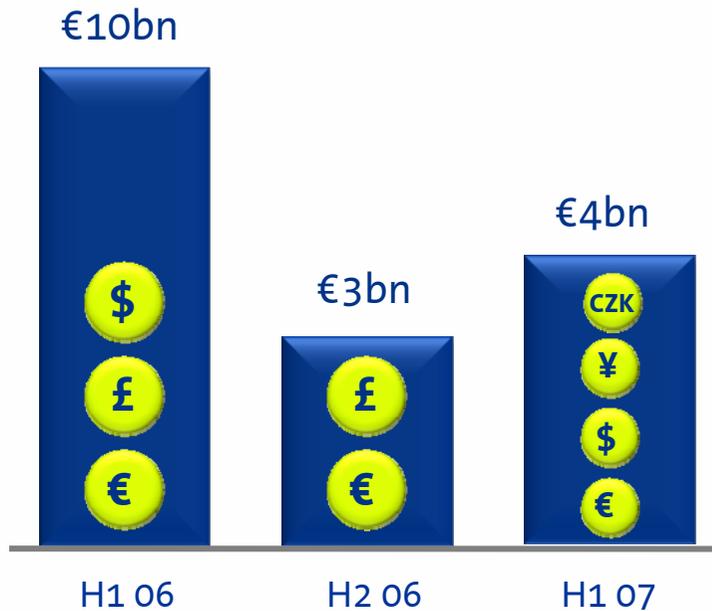
## 2 The absolute size of our debt is significant...



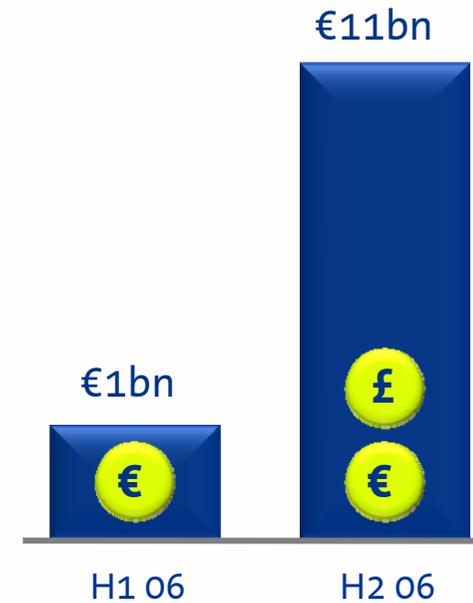
- ...but we have already amortized €7bn in 2006 & H1 07
  - €6bn dedicated to financial debt reduction
  - €1.2bn pre-retirement commitments amortized

## 2 Telefónica's most ambitious refinancing ever is over ahead of market expectations

**€17bn bonds** > 800 investors

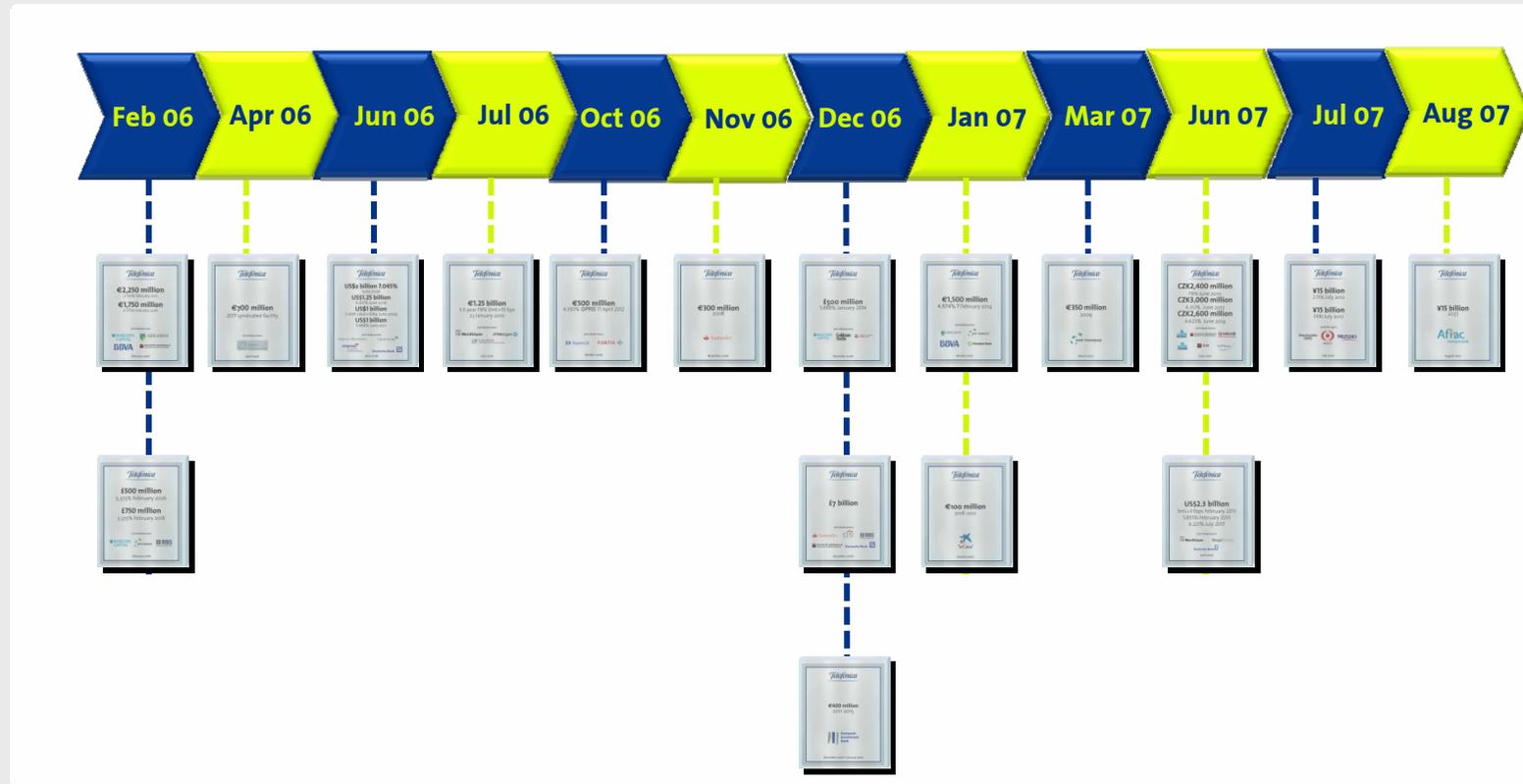


**€12bn bank debt** 80 financial institutions



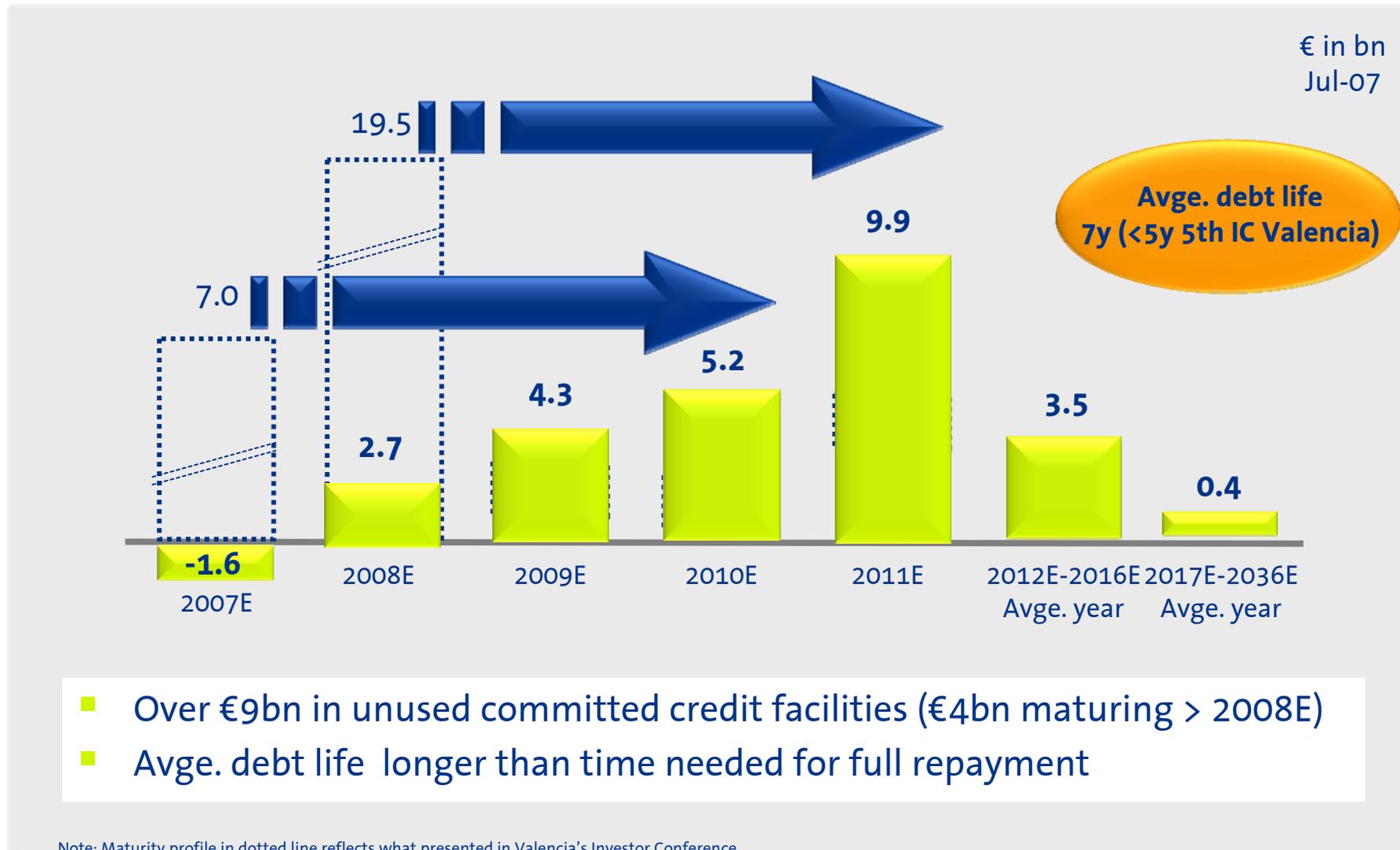
- **Only 1 year to refinance 2nd largest loan to date in the corporate world history**
  - 2nd largest bond corporate issuer in 2006 with €13bn issuances
- **Proactive financing activity in H1 07 allowed us to avoid turmoil markets**
  - 07E financing goal to smooth 09E-10E maturities around €5bn already achieved in H1 07

## 2 Diversifying on financing sources



- Tapping major bond markets €, \$ and £ on jumbo or benchmark deals, as appropriate
  - Inaugurating some peripheral markets like ¥ or CZK.
- Borrowing from non-commercial or non-core relationship financial institutions

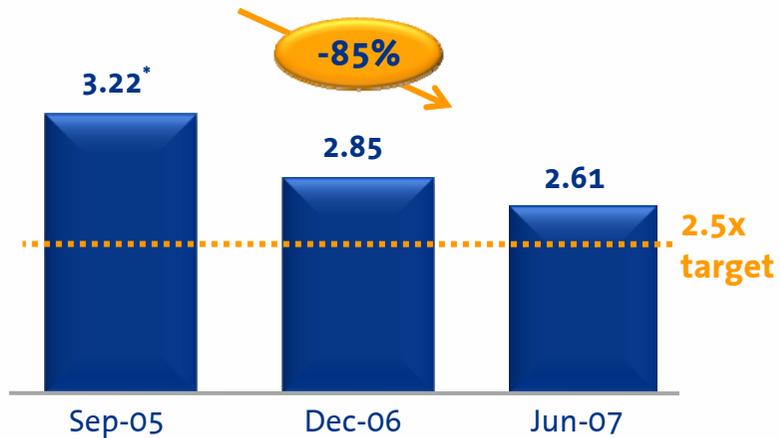
## 2 To gain comfortable maturity profile and no need to access capital markets



## 2 Rapid deleverage

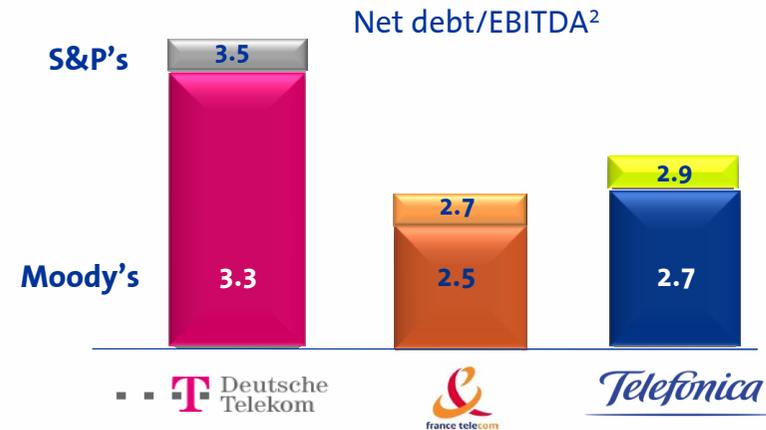
### Net debt + cash commitments below 2.5x OIBDA in the medium term

#### 85% TARGET ALREADY ACHIEVED



Net Financial Debt & Commitments/OIBDA  
\*TEF-02 pro-forma figures

#### EUROPEAN PEERS CAPITAL STRUCTURE COMPARISON



1 Source Standard & Poor's: Europe's Four Largest Telecoms Operators Differ On Financial Policy And Domestic Pressures (12 Apr 07)  
Moody's: Europe's Investment-Grade Telecoms Operators (June 2007)  
2 Net Debt and EBITDA figures adjusted according to Standard & Poor's and Moody's methodology.

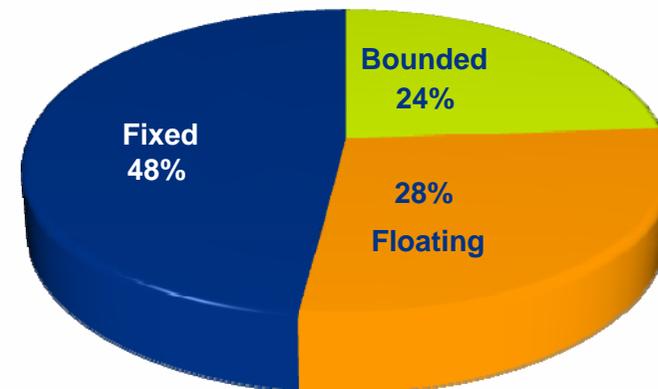
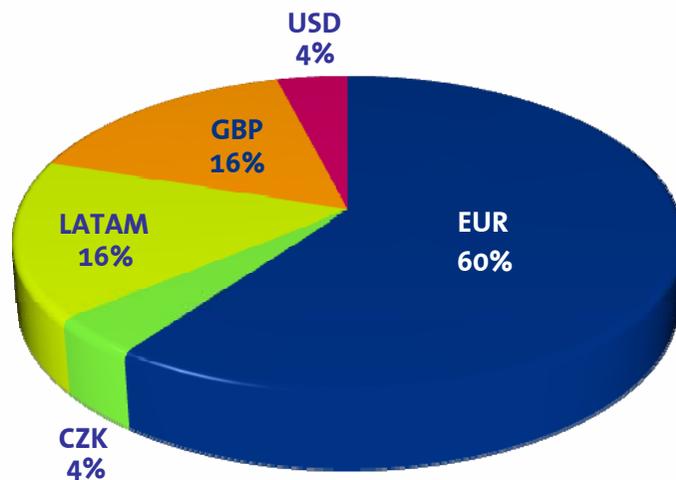
## 2 Divestments before investments



(\*) transactions pending completion

## 2 Hedging policy: FX and interest rates

- Debt denominated in Latam currencies close to 2 times FCF
- Cesky acquisition price 70% funded in local currency and O2 UK acquisition GBP funding reduced from 70% to 50% following Airwave disposal
- Unhedged exposure to rising interest rates only 28% of total



## 2 We have rescheduled maturities in €36bn out of €55bn total

1

### €7bn debt amortized with CF

Debt & Commitments reduced to 2.6x OIBDA from 3.2x (pro-forma)

2

### €29 bn debt extended

From €27bn debt maturing in 2007E-08E following O2 acquisition to just €2.7bn maturing in 2008E

3

### €9bn undrawn liquidity lines

€4bn lines maturing beyond 2008E and net cash position in 2007E removes any need to access credit market

4

### Keeping cost under control

Prudent liquidity and FX hedging, while financial expenses at or below 6%

**Financial cushion built allowing Telefonica to remain focused on business growth and accelerate cash returned to shareholders**

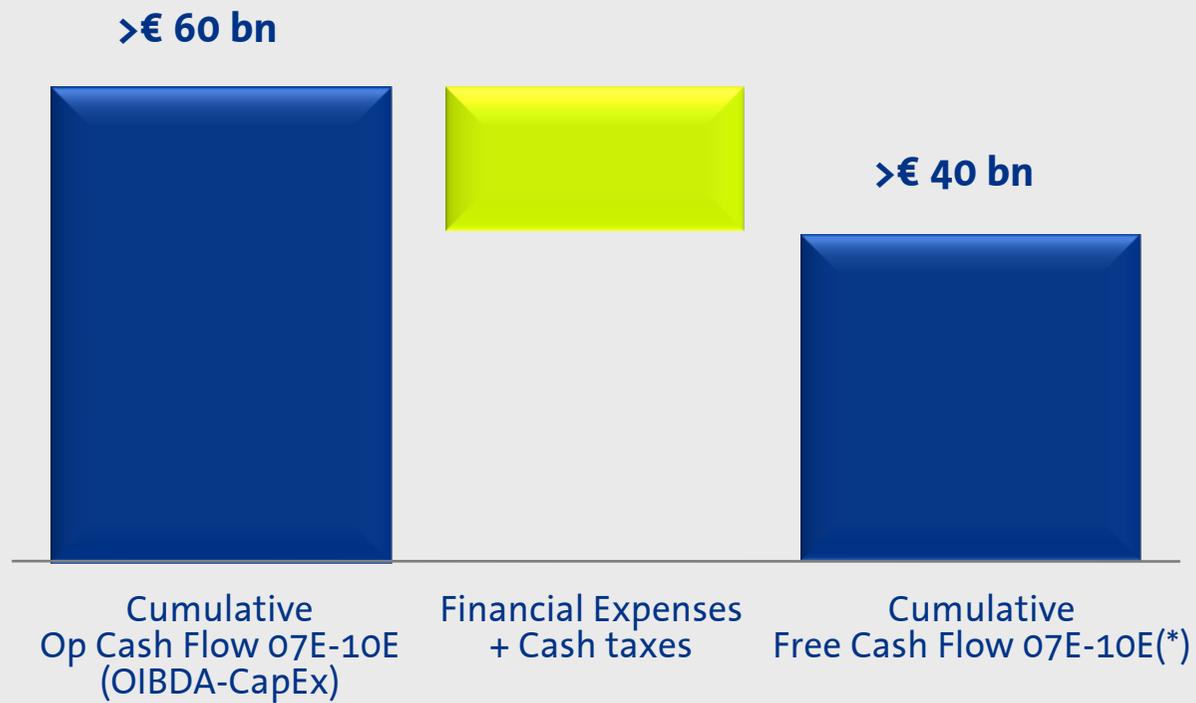
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## 3 Cash Flow and Uses

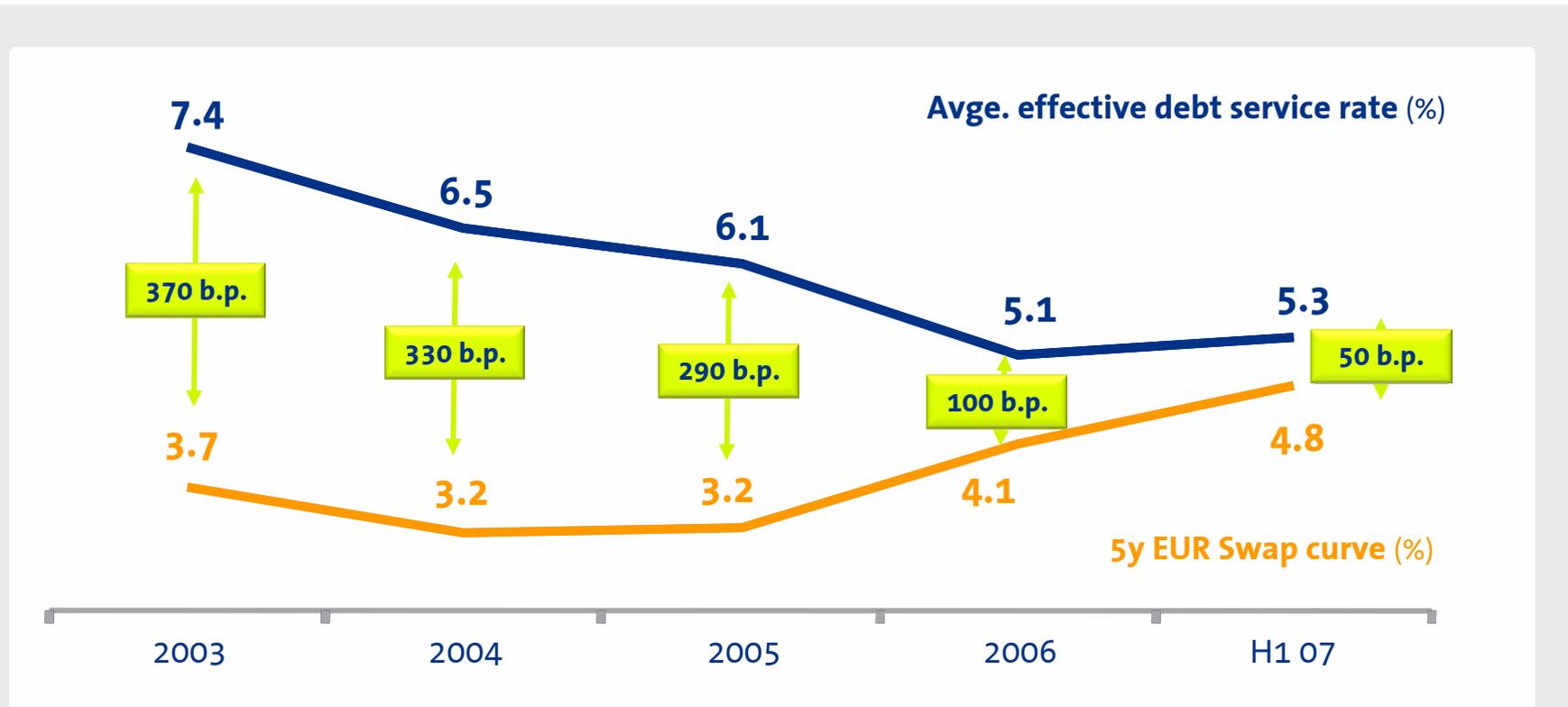
- 3.1 Free Cash Flow generation through 2010E
- 3.2 Interests outlook does not look interesting
- 3.3 Tax on its tracks
- 3.4 Uses of Free Cash Flow

### 3 Free Cash Flow generation



(\*) Free Cash Flow is the cash flow available to remunerate Telefónica's shareholders, to protect solvency levels (financial debt and commitments), and to accommodate strategic flexibility

### 3 Improving financing costs

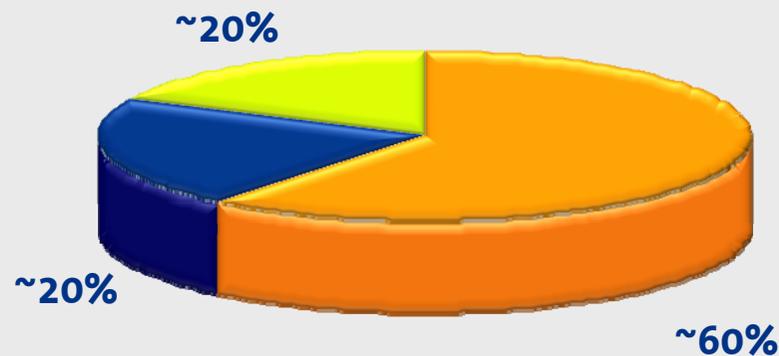


- Ongoing effective interest rate reduction up to around 5.5% in 2007E, trending towards 6% later on.
  - Spread differential vs. Euro rates at a minimum

### 3 Cash taxes reappear on our landscape

- Tax rates are not expected to move significantly from current levels. Thus P&L taxes will rise in line with EBT.
- Cash taxes rise as a fraction of P&L taxes as tax shields get exhausted (mid-2008E) and Latam profits rise faster than Europe's.

#### CUMULATIVE CASH TAXES 2007E -2010E



### 3 A disciplined use of FCF with clear priorities

**Upgraded!**

#### FIRST PRIORITY

#### Shareholder Remuneration

- 2008E DPS of 1 Euro (\*)
- Share buybacks to be considered as stated below

#### SECOND PRIORITY

#### Deleverage

- Net Debt + Cash Commitments over OIBDA in the 2.0 – 2.5x range

#### THIRD PRIORITY

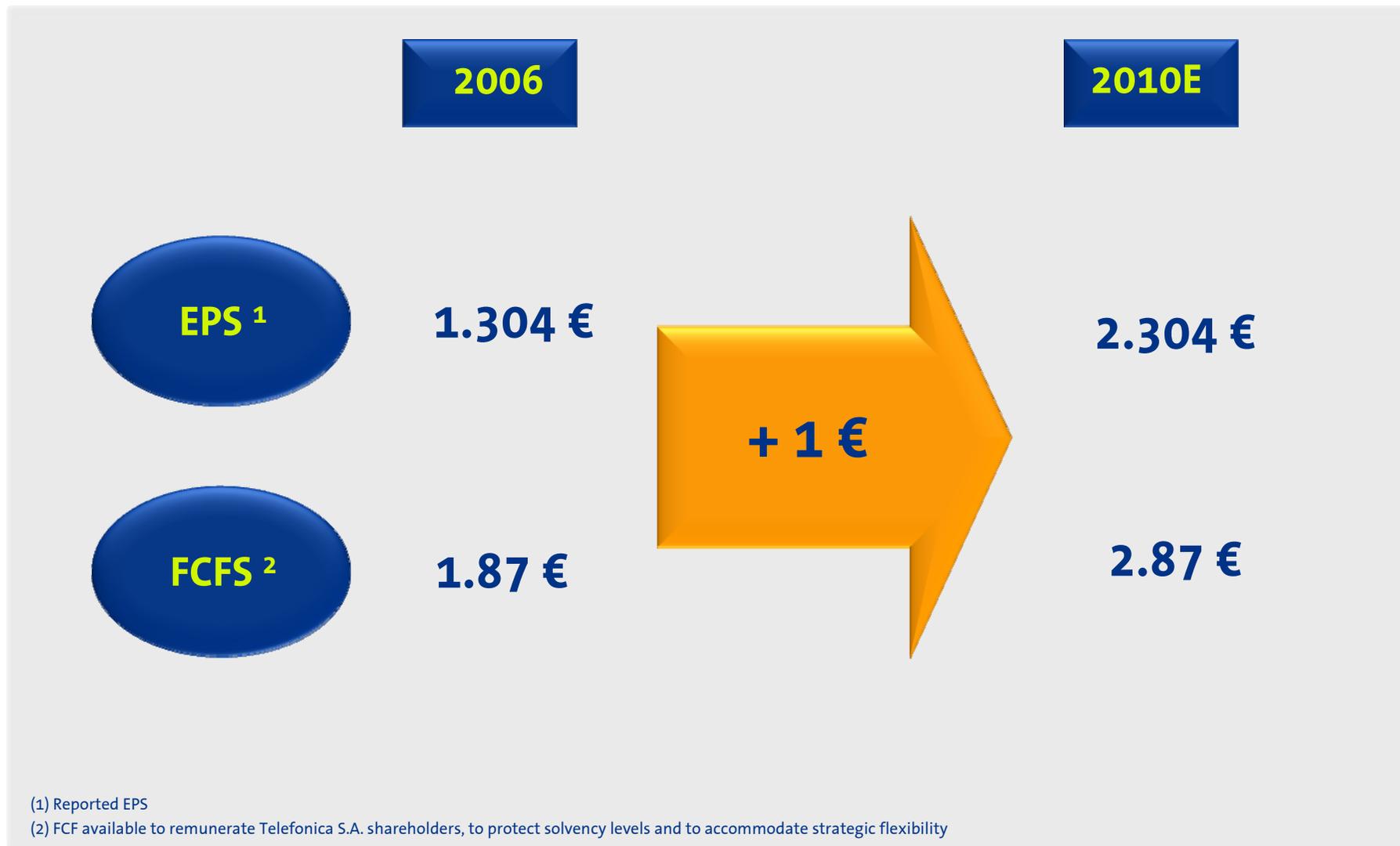
#### Selective M&A

- To foster growth in current markets

**Excess FCF will be allocated once it is generated and following these priorities**

(\*) Fiscal year 2008E, to be paid in H2 08 and H1 09

### 3 We reiterate and even extend our commitments for 2010



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## 4 Conclusions

**Telefónica's debt is not an issue...**

**...Telefónica most ambitious refinancing exercise is over**

**Our target leverage ratio to be in the 2.0x – 2.5x range**

**Interest expense should not exceed 6%**

**Cash taxes will rise faster than P&L taxes**

**FCF allocation priorities are**

**Shareholder remuneration**

**Deleverage**

**M&A**

**excess cash flow will be allocated according to these priorities**

**We expect to add €1.0 to both EPS and FCF by 2010E**

*Telefonica*

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