Focus on profitable leadership

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01

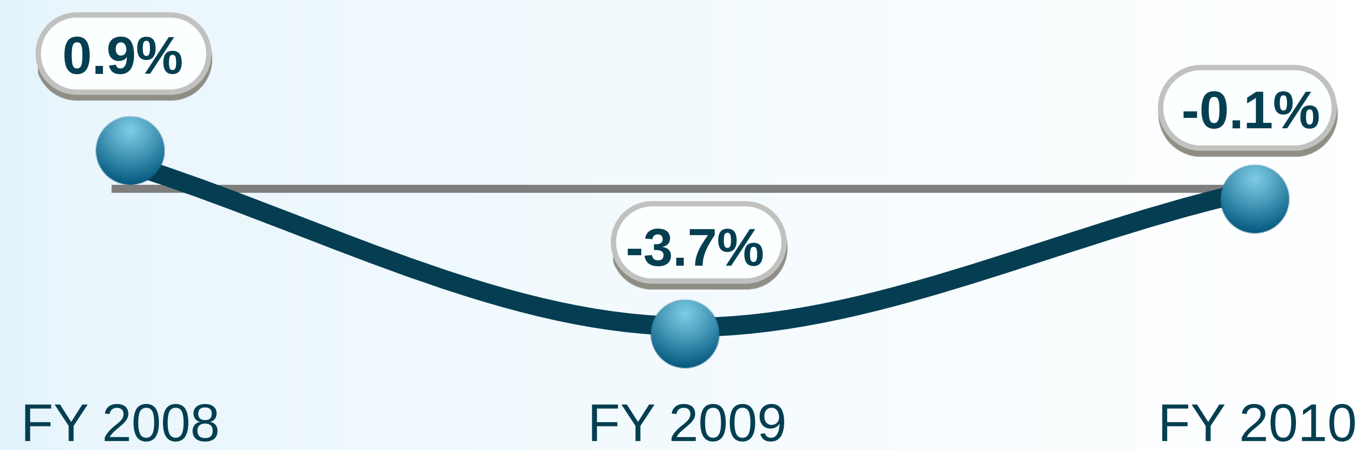
Resilience and flexibility in a difficult environment

Since our last Investor Day, we have faced a tough market environment

y-o-y variation

Difficult macro conditions

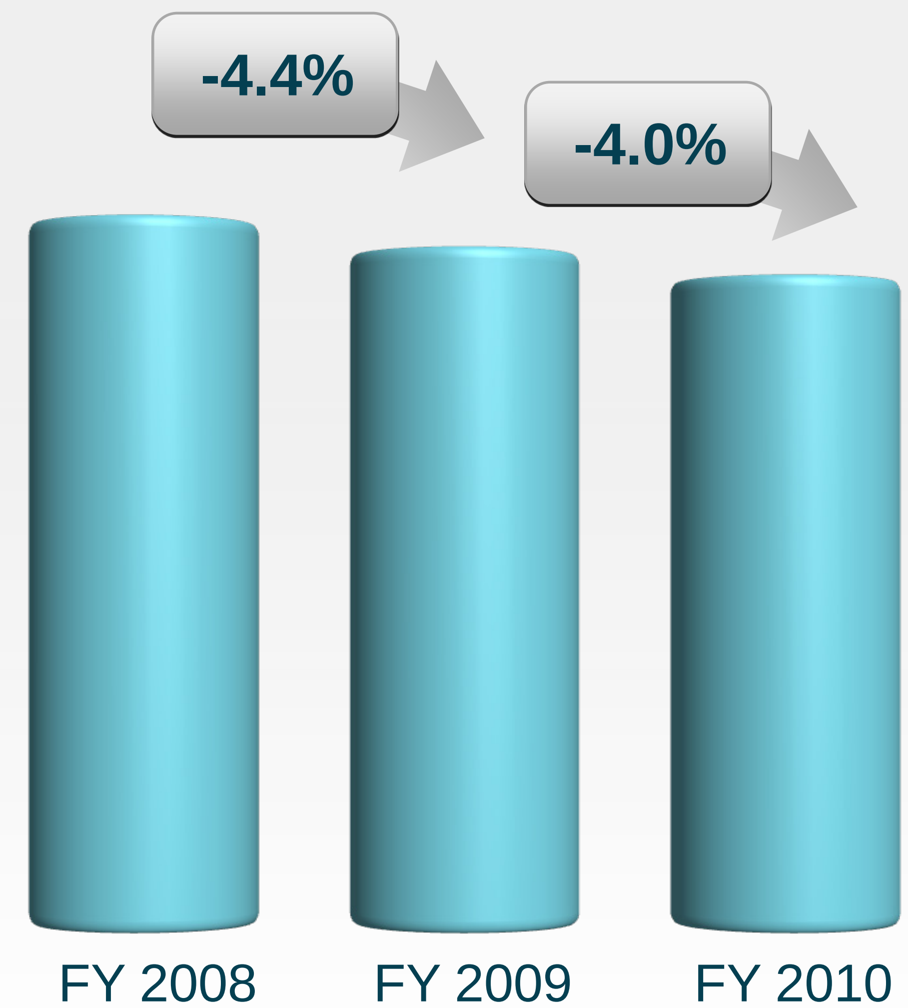
Real GDP[1] var. y-o-y



Increased competitive pressure

- Mobile **ARPM decline** accelerating
- Aggressive **promotions and cross-subsidies** in fixed broadband

Retail service communication market revenue variation[2]



[1] **Source**: INE
[2] **Source:** CMT and internal estimates

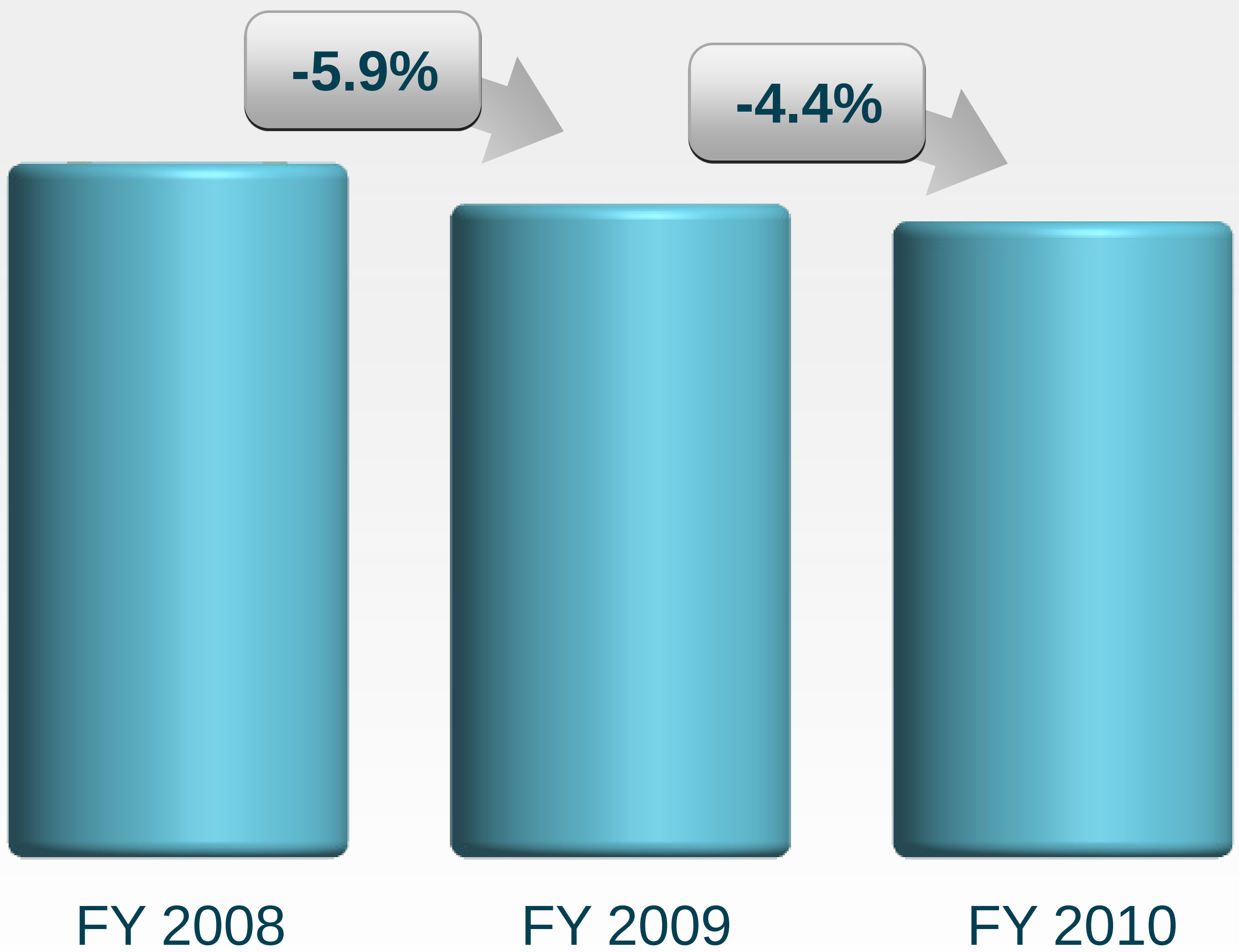
Investor Conference Telefónica

Our performance has been affected…

y-o-y variation

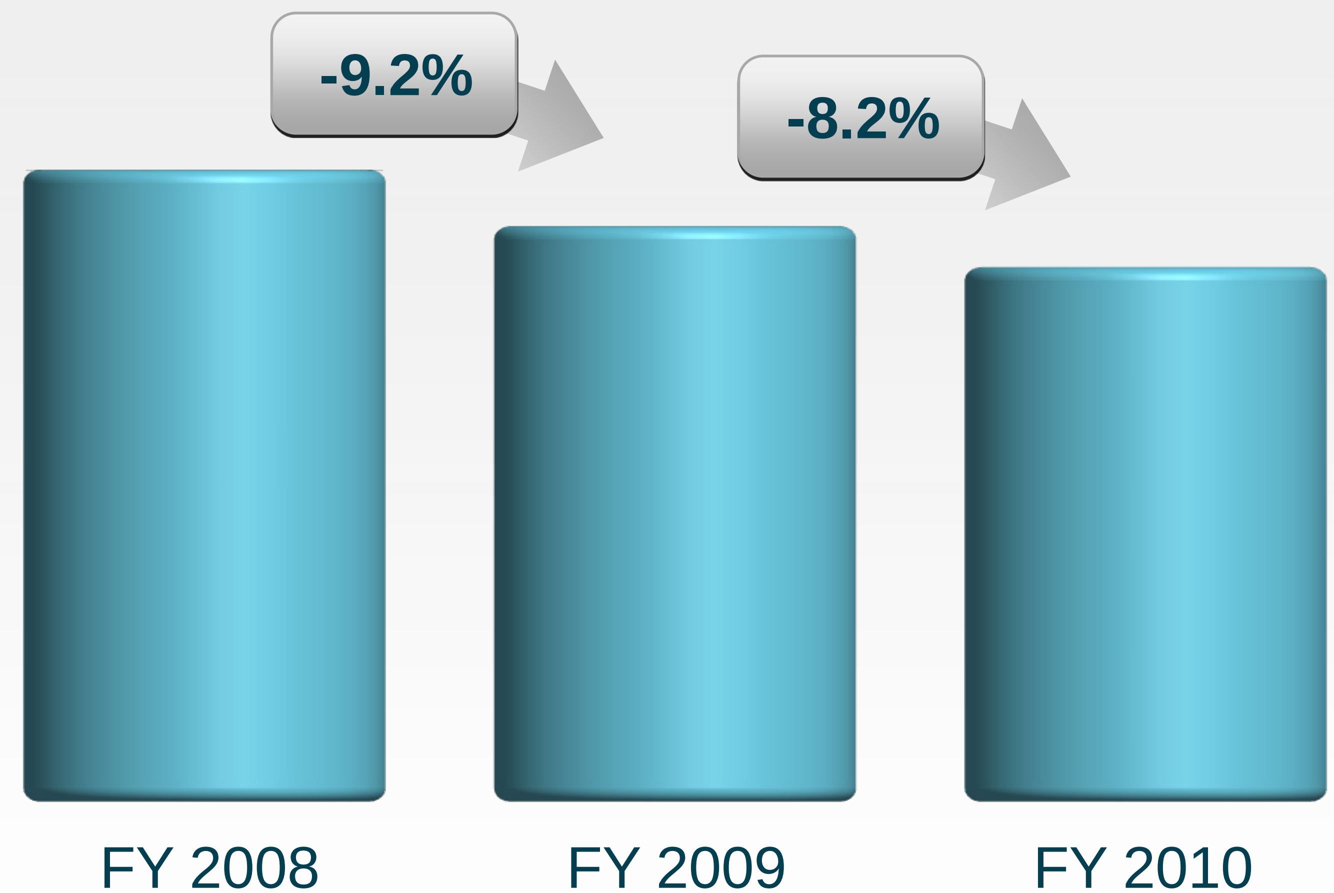
Revenues have fallen…

Comparable revenues evolution[1]
T. España



… mainly in our high margin traditional business

Comparable access & voice revenues evolution[2]
T. España, Fixed & Mobile



Highly affected by price based competition

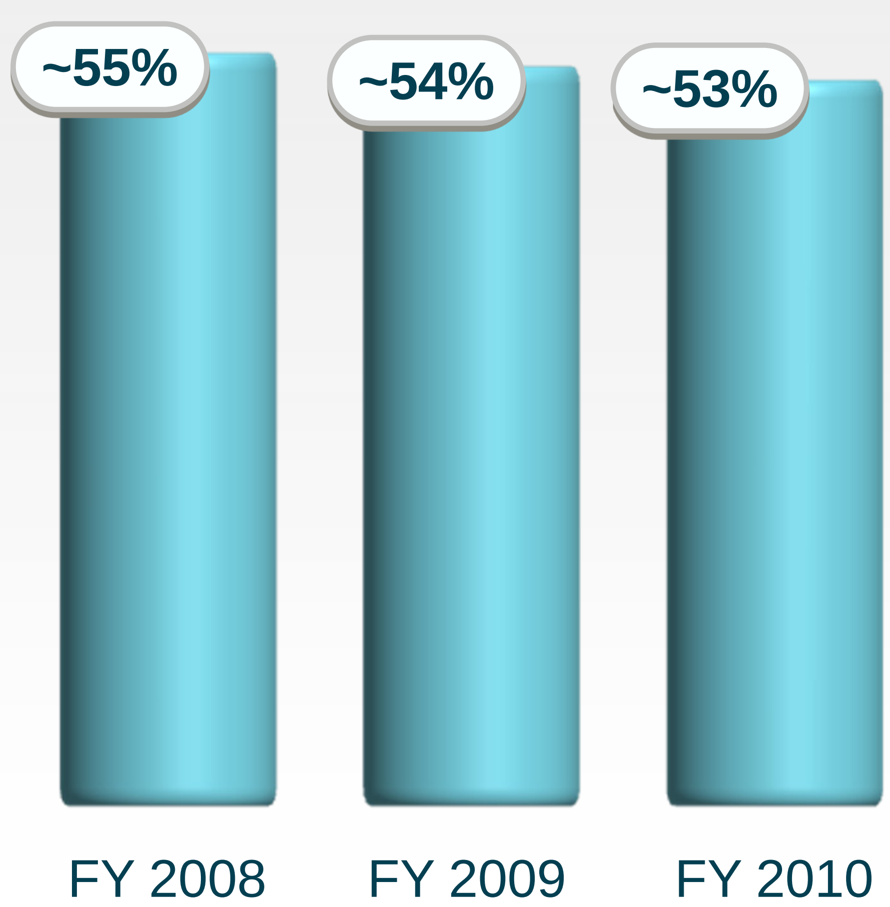
[1] Comparable terms for y-o-y change include Tuenti in the period Aug/Dec-09 and exclude the following effects: USO, Telyco Morocco (since Jan-10) and sale of application rights
[2] Voice and Access Revenue: Include fixed/mobile access & voice (SMS included), narrowband and mobile& fixed equipment revenues and exclude USO and sale of application rights

… though we have been resilient in core value parameters

y-o-y variation

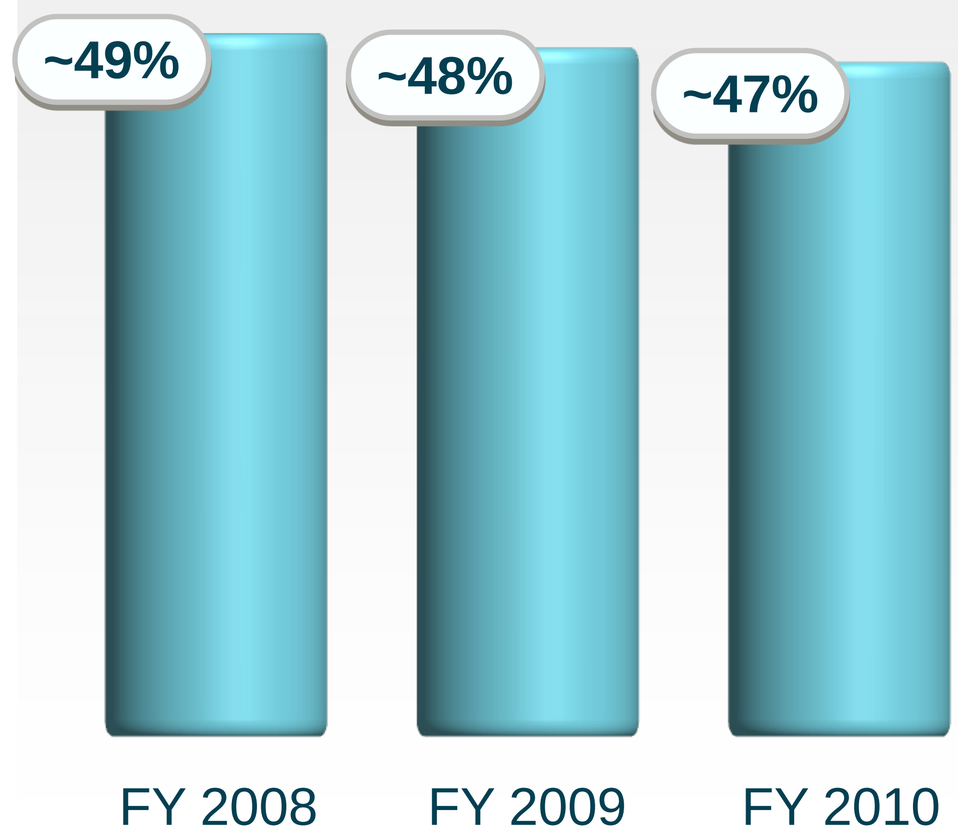
Sustaining market leadership…

Revenue market share[1]
T. España



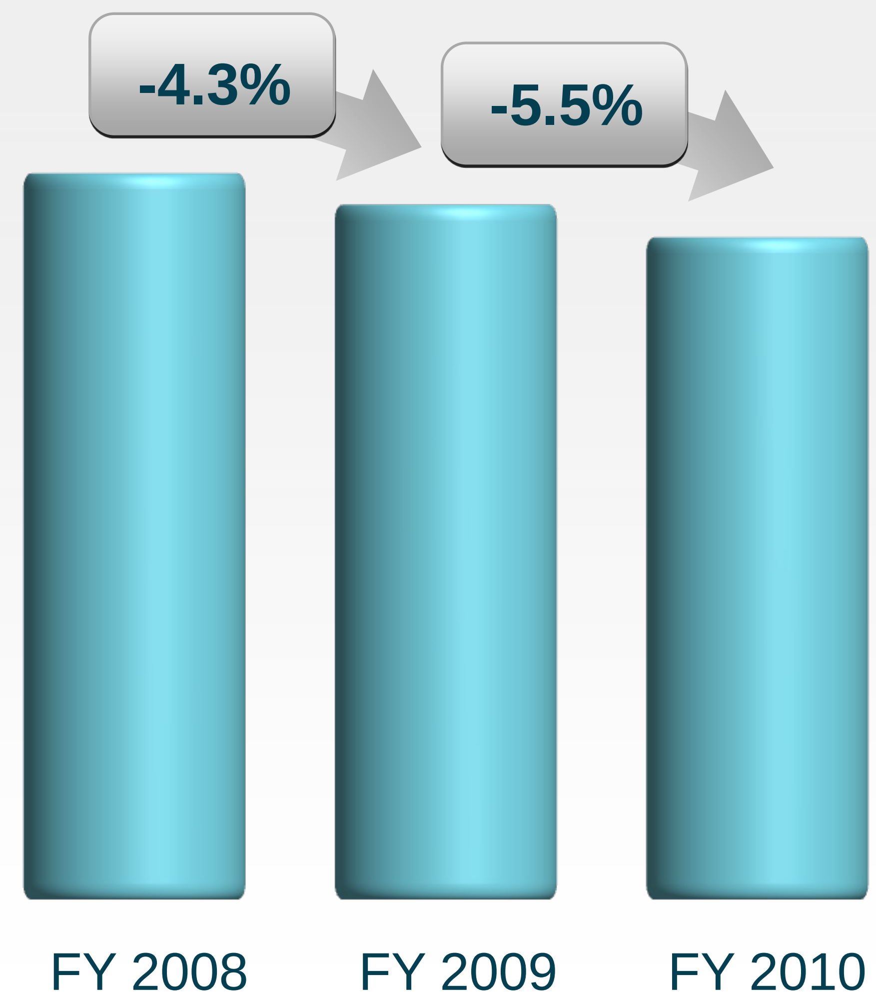
…while maintaining a healthy margin…

Comparable OIBDA margin[2]
T. España



…and protecting cash flow

OpCF after WC change[3]
T. España

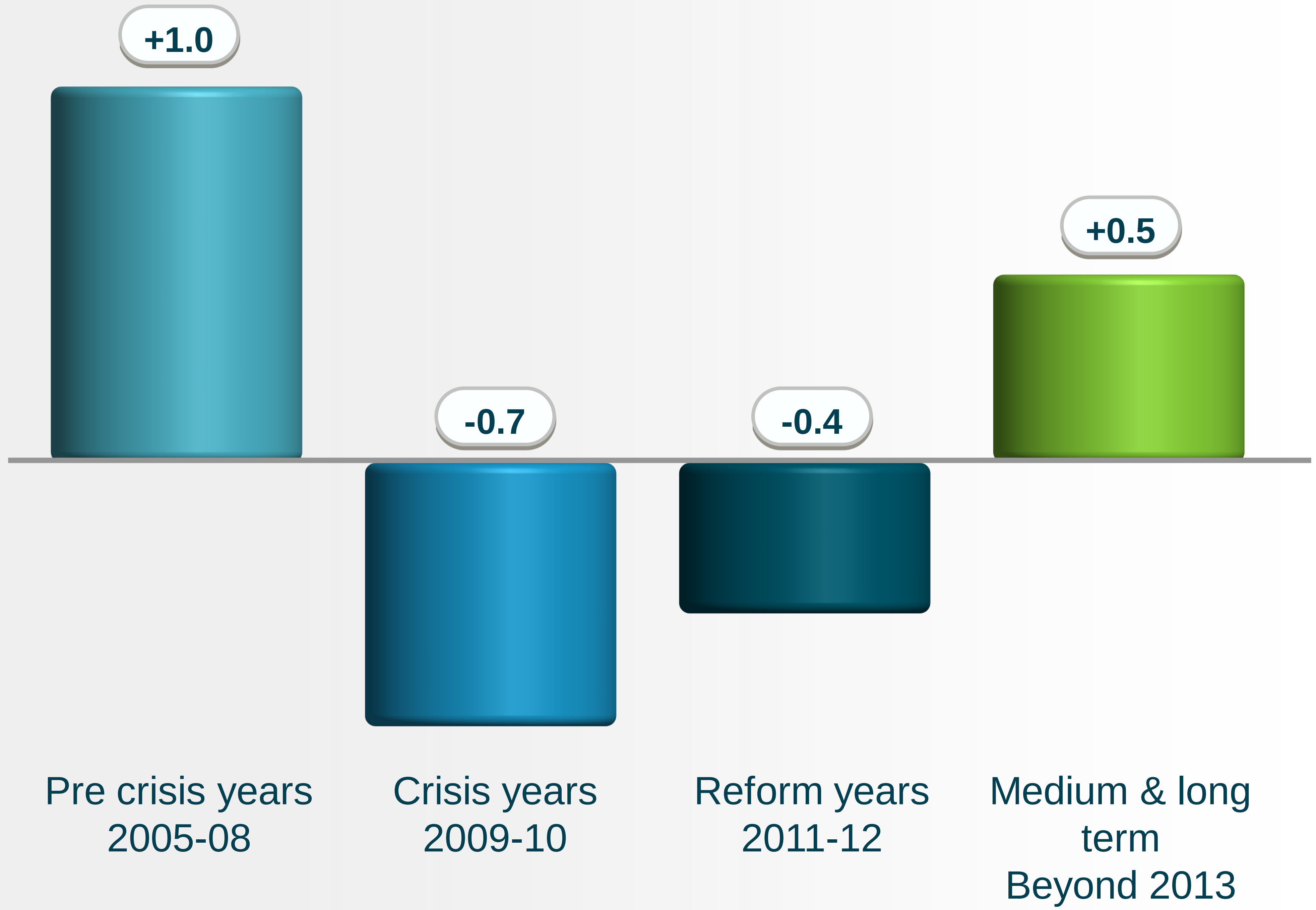


[1] Retail communication (fixed & mobile) revenue market share. **Source:** CMT and internal estimates
[2] Comparable terms include Tuenti in the period Aug/Dec-09 and exclude the following effects: USO, real estate capital gains, Medi Telecom disposal capital gain, Telyco Morocco (since Jan-10), TV Tax, revision of the estimates for the personnel commitments provided for prior periods to 2009, 2010 non-recurrent restructurings costs, bad debt recovery and sale of application rights
[3] Operating Cash Flow after Working Capital change: Operating collections less OpEx and CapEx payments. Adjusted for intragroup fees

Going forward, we maintain our confidence in macro recovery

- **The worst is over and the Spanish economy is expected to grow**
- **Reforms are firmly on track**
- **There are some uncertainties on the timing of the recovery**

Spain vs. Euro Zone: GDP growth rate differential[1]
p.p.

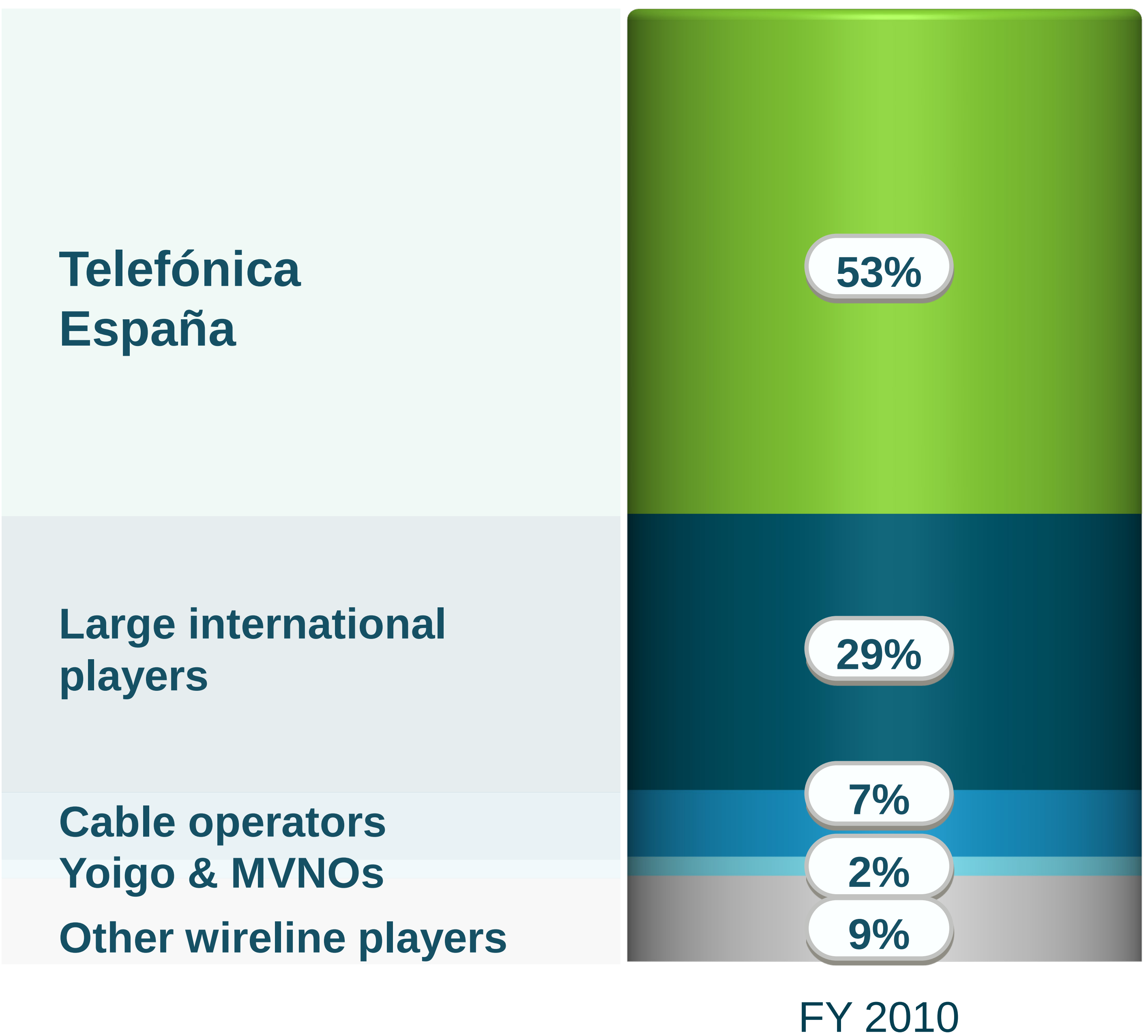


[1] **Source:** IMF and OECD

Competitive pressure is not expected to increase much further

Competitive situation

Revenue market share[1]
Fixed & Mobile



Competitors likely to focus on service as macro improves

Large international players • Financial discipline • Need to ensure revenue and margins	**Focus on long term value**
Cable operators • High leverage ratios • Savings banks major shareholders	**Financial focus**
Yoigo & MVNOs • Small market shares	**Need to ensure positive margin**
Other wireline players • Diverse	**Maintain rational behaviour**

[1] Retail communication (fixed & mobile) revenue market share. **Source:** CMT and internal estimates

The regulatory framework is more predictable

Strict traditional business regulation

- **ULL prices:**
  - **CMT has recently raised prices to € 8.32 (~+7%)**, below European Union average (~€ 9)
  - **CMT decision represents a new regulatory path** for ULL prices going forward
- **Geographic segmentation** expected
- **TV tax** under EU review
- **MTR price cuts** following the glide path (€ 4 c/min by Apr-12)

Critical future issues mostly defined

NGN Regulation

- **Framework already defined**
- **Infrastructure competition is encouraged** (bitstream services up to 30 Mbps)

Spectrum auctions

- **New bands for LTE:** 800 MHz & 2.6 GHz
- **Contests and auctions for existing bands:** 900 MHz & 1,800 MHz
- **Refarming:** Technological neutrality across current 2G bands

New opportunities are arising in the market

y-o-y variation

Total variation FY 2010-2013E

Strong FBB penetration increase

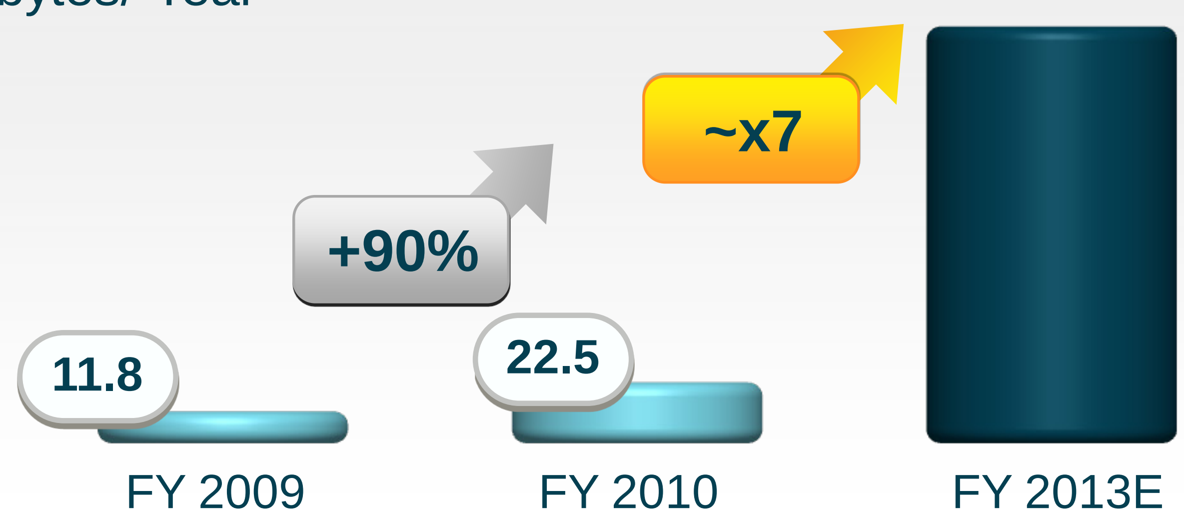
Fixed broadband market accesses[1]
Million

Growing IT importance

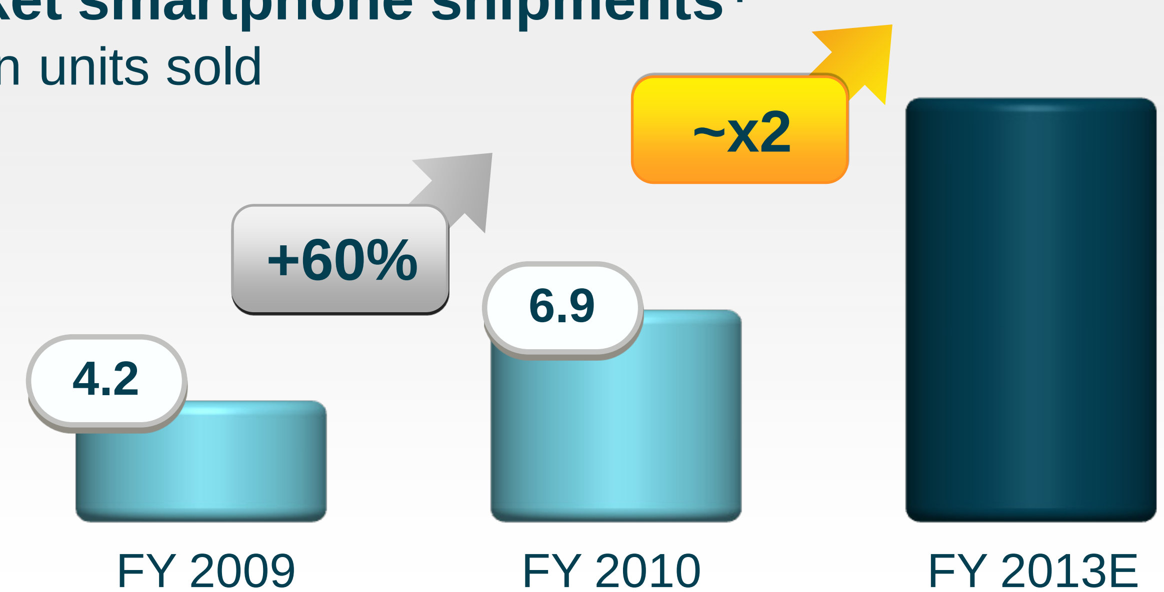
IT market revenues[2]
€ bn

Heavy MBB adoption

IP Data Mobile market traffic[3]
Petabytes/ Year



Market smartphone shipments[4]
Million units sold



[1] **Source:** Internal estimates. Retail FBB: Include FO (Fiber Optic), DSL, cable modem and satellite.
[2] **Source:** Internal estimates. Includes Corporate market for desktops, hosting, security and other applications.
[3] **Source:** Internal estimates
[4] **Source:** IDC

We are focused on profitable leadership to successfully manage this scenario

Focus on profitable leadership balancing short term results, long term sustainability and growth

Core principles

- Defense of our OIBDA and our value **leadership**
- **Flexibility** to adapt to market conditions
- Capture **market growth opportunities** in a profitable way

Strategic priorities

- Smart focus on value vs. pure volume
- Reshaping of our cost base
- Optimized use of capital

02

Our strategy ‘Focus on profitable leadership’

02

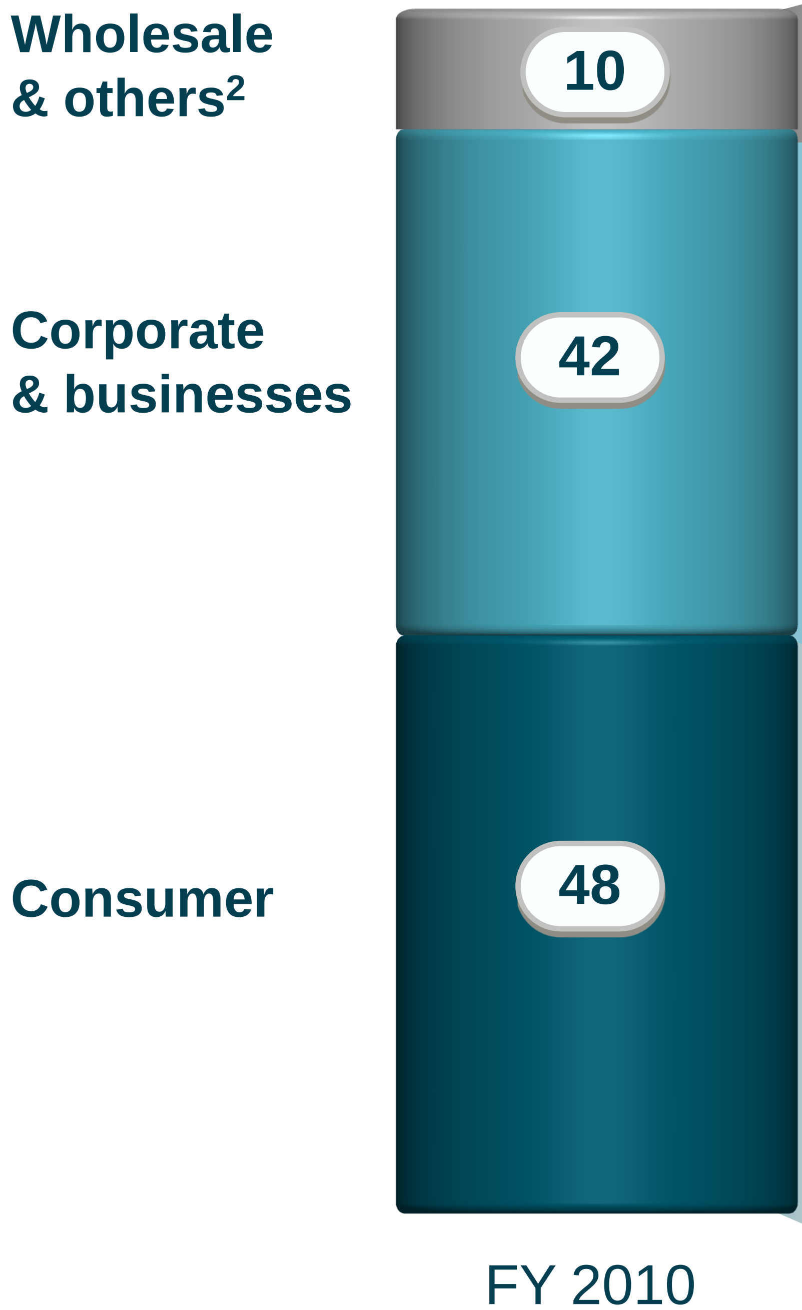
Our strategy ‘Focus on profitable leadership’

- **Smart focus on value**
- Reshaping of our cost base
- Optimized use of capital

We are handling our diverse customer base through a customized strategy

Service revenue split[1]
T. España %

2010



Solid wholesale platform

- **Offsetting** flows (Yoigo agreement, wholesale data revenues…)

Strong position within experienced decision makers

- **High level of service:**
  - § In the field specialized sales force and technical support — **>3,000**
- **Leading quality provider:**
  - § Corporate: fibre premises (up to 10 Gbps) — **>40,000**
- **Integrated value offer:**
  - § Corporate: BB & Services beyond Connectivity[3]/ Total revenues — **60%**

Value leadership in an adverse and very competitive segment

- Stronger position in **higher value segments**: FBB, Mobile Contract, Smartphones, 3P
- The highest customer **satisfaction**:
  - § CSI GAP[4] — **+0.40 p.p.**
- Best Fixed & Mobile platform:
  - § Best in class **fixed broadband coverage**[5] — **98%**
  - § **Best 3G** coverage and quality[6]

[1] Excludes fixed & mobile handset sales, subsidiaries and others
[2] Others include USO
[3] BB (retail and wholesale FBB connectivity, MBB, fixed and mobile devices (PCMCIAs and Dongle) and fixed data services) and Services beyond Connectivity (Content, digital services, ICT solutions and vertical units revenues)
[4] GAP vs. best competitor
[5] Local loop ≥ 1 Mbps over total loops
[6] **Source:** Spanish "Asociación de Internautas" Dec. 2010

A smart focus on value is key to capture recovery and ensure competitiveness

A differentiated customer experience

A product portfolio adapted to the needs and value of the client

A leading approach to growth opportunities

Churn reduction

Differentiated value proposition

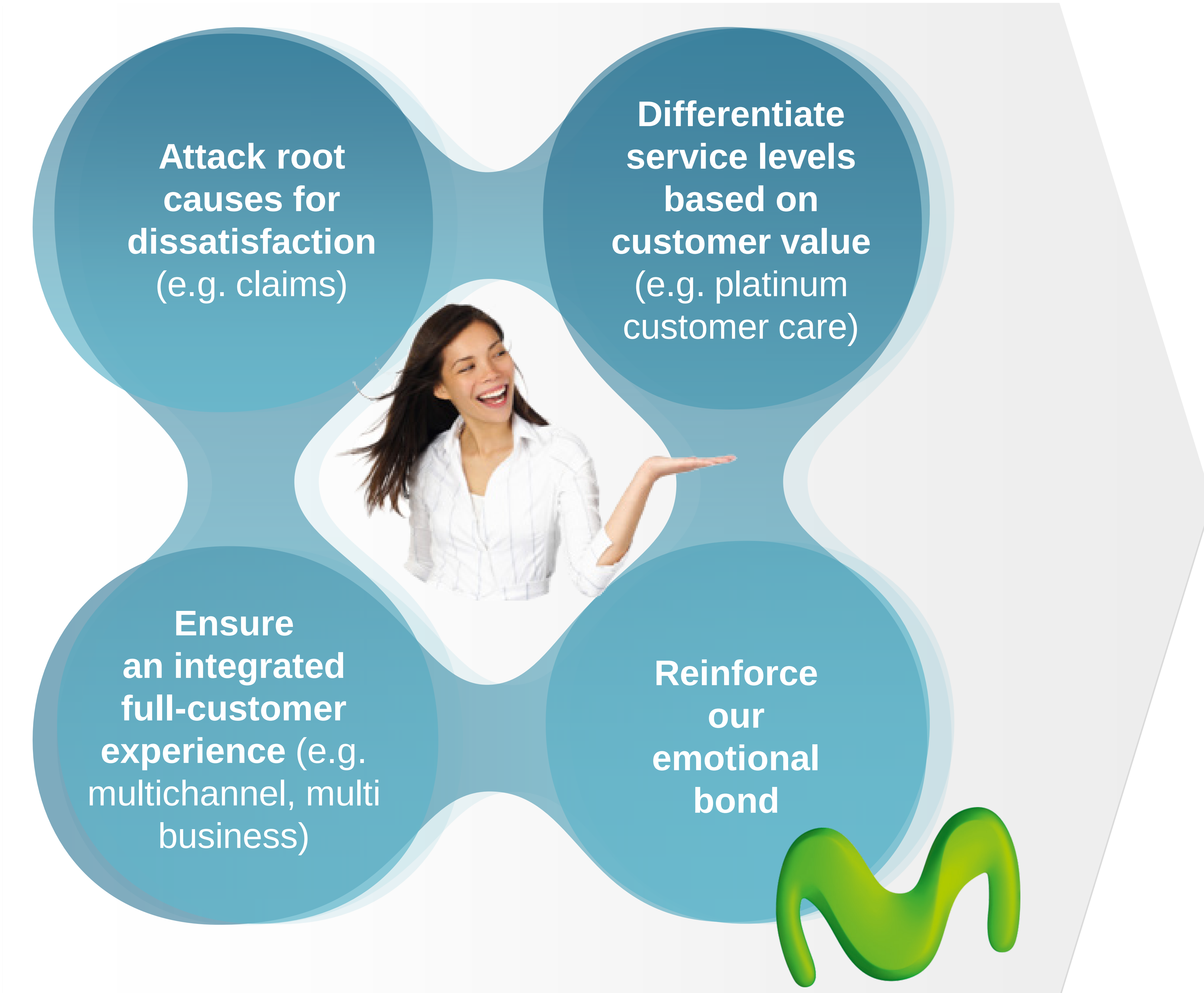
Revenue growth in key opportunities > € 1.2 bn[2]

Moving from "volume" to "value"…

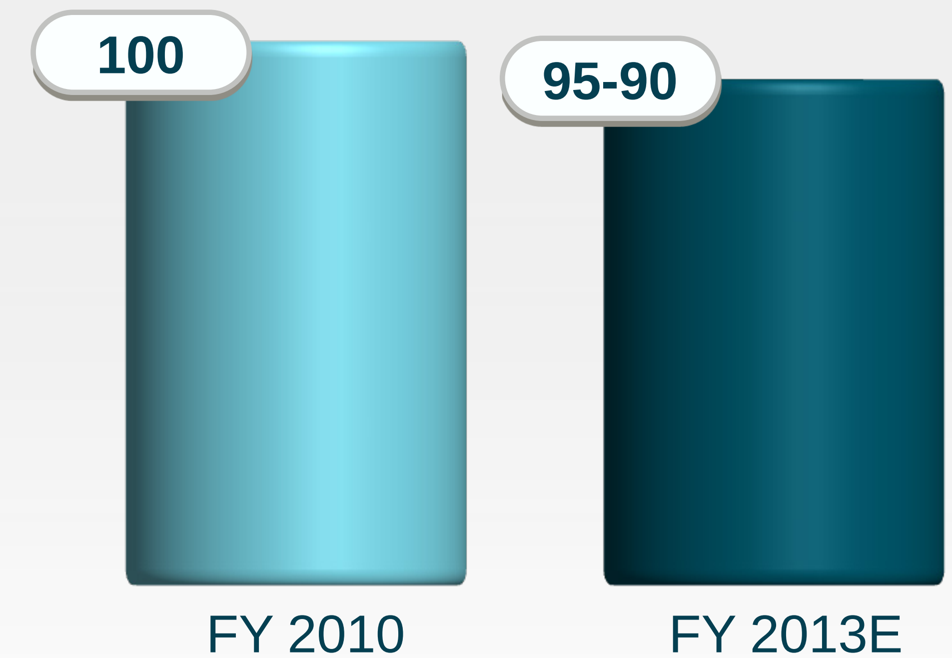
… and sustaining revenue market share ~48%-50%[1] in FY 2013E

[1] Retail communication (fixed & mobile) revenue market share. **Source:** CMT and internal estimates
[2] Revenue increase from FY 2010-2013 E. Includes Services beyond Connectivity revenues: Content, digital services, ICT solutions and vertical units revenues and MBB revenues from smartphones, smart devices and connectivity MBB, mobile mail, MBB equipment (PCMCIAs, Dongles), roaming, and WAP browsing. SMS and M2M excluded

Customer experience remains a crucial differentiating factor



Blended churn evolution
T. España Base 100



Maintaining a gap vs. main competitor

We are adapting our product portfolio to the needs and value of each segment

Developing best practices in the corporate space…

- **Leading the corporate space…**
  - Seamless Fixed & Mobile proposition
  - Global MNC's platform
- … by leveraging our **differentiated IT proposal**

Total variation FY 2010-2013E

FY 2013E[1]

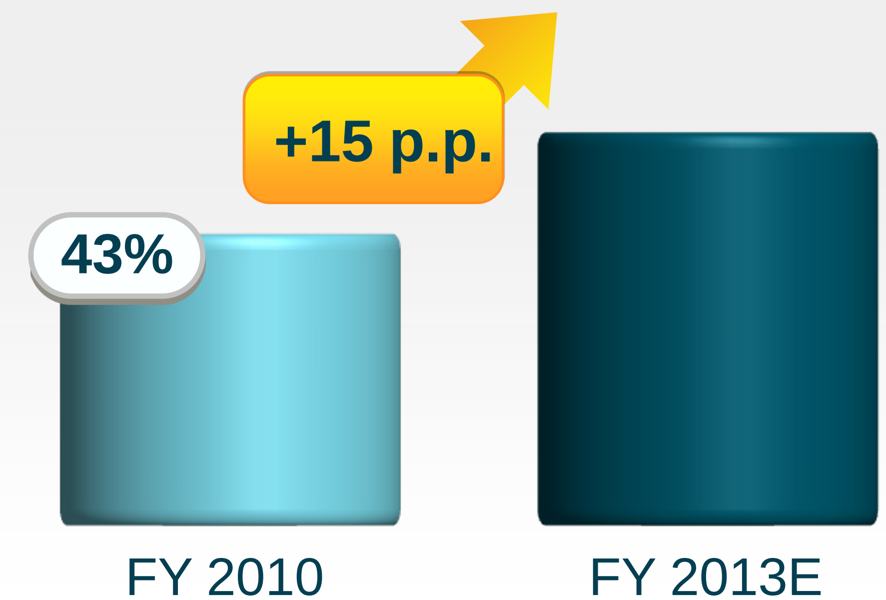
Corporate: BB & Services beyond Connectivity / total revenues

~68%
(+8 p.p. vs. FY 2010)

…and a flexible value proposition for mass markets

- **Acceleration of RGUs growth** through F&M BB and Services beyond Connectivity
- **On-line self-managed bundles** and services configuration
- **Differentiated** product strategies for value clusters

2P & 3P / Fixed lines[2]
T. España



[1] BB (retail and wholesale FBB connectivity, MBB, fixed and mobile devices (PCMCIAs and Dongle) and fixed data services) and Services beyond Connectivity (Content, digital services, ICT solutions and vertical units revenues)
[2] % of fixed lines with broadband and/or Pay TV

In MBB our priority is to actively develop the market in a profitable way

Pushing Smartphone adoption

~65% Smartphone sales/ Total contract handset sales[1]

Offering pricing schemes adapted to different levels of use

100% Customers with tiered pricing

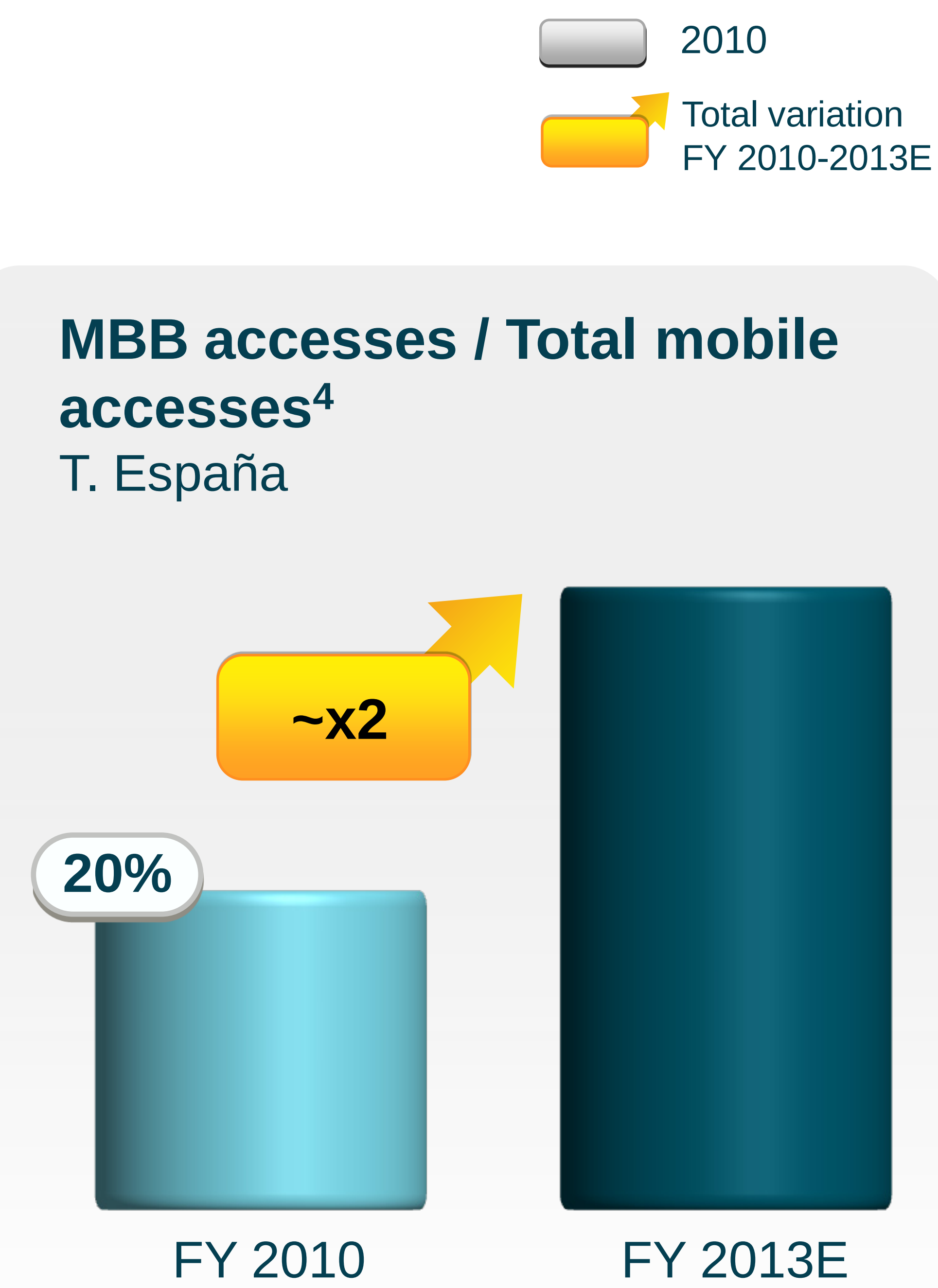
- Evolution towards more **speed, flexibility and value**

Fostering complementary BB proposal

>70% T. España complementarity[2] of MBB and FBB

2% T. España substitution[3] of MBB and FBB

MBB accesses / Total mobile accesses[4]
T. España



[1] Figure as of Q410
[2] Complementarity rate defined as the share of Mobile Connectivity users that have an additional Fixed Broadband connection
[3] Substitution defined as current customers moving from FBB to MBB over total new MBB
[4] MBB accesses with data attached rate/Total mobile customer base

Services beyond Connectivity will continue to be developed enriching our portfolio

TV

- **Pay TV** evolution:
  - **OTT** model[1] (Video Club Movistar) >90% coverage over FBB lines
  - Improved **quality** and **content**

IT

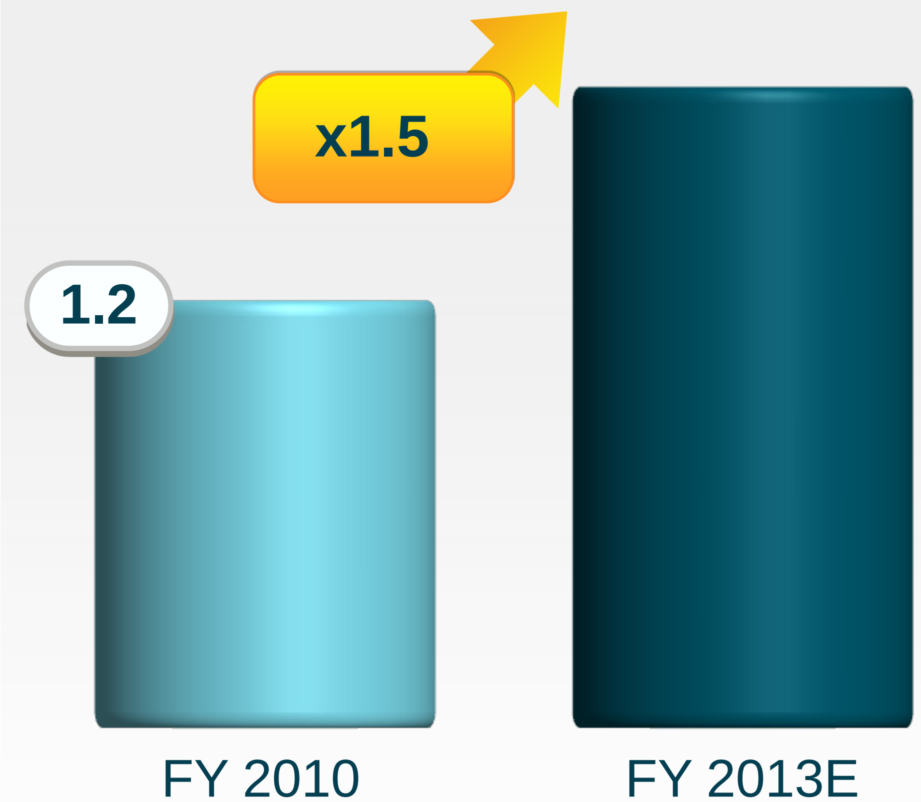
- **Further expansion of our solutions:** private cloud, virtual data center, clean pipes…

New services

- **Leverage of global product development:** e-Health, Security, M2M, Financial Services…

Total variation FY 2010-2013E

Services beyond Connectivity revenues[2]
T. España € bn



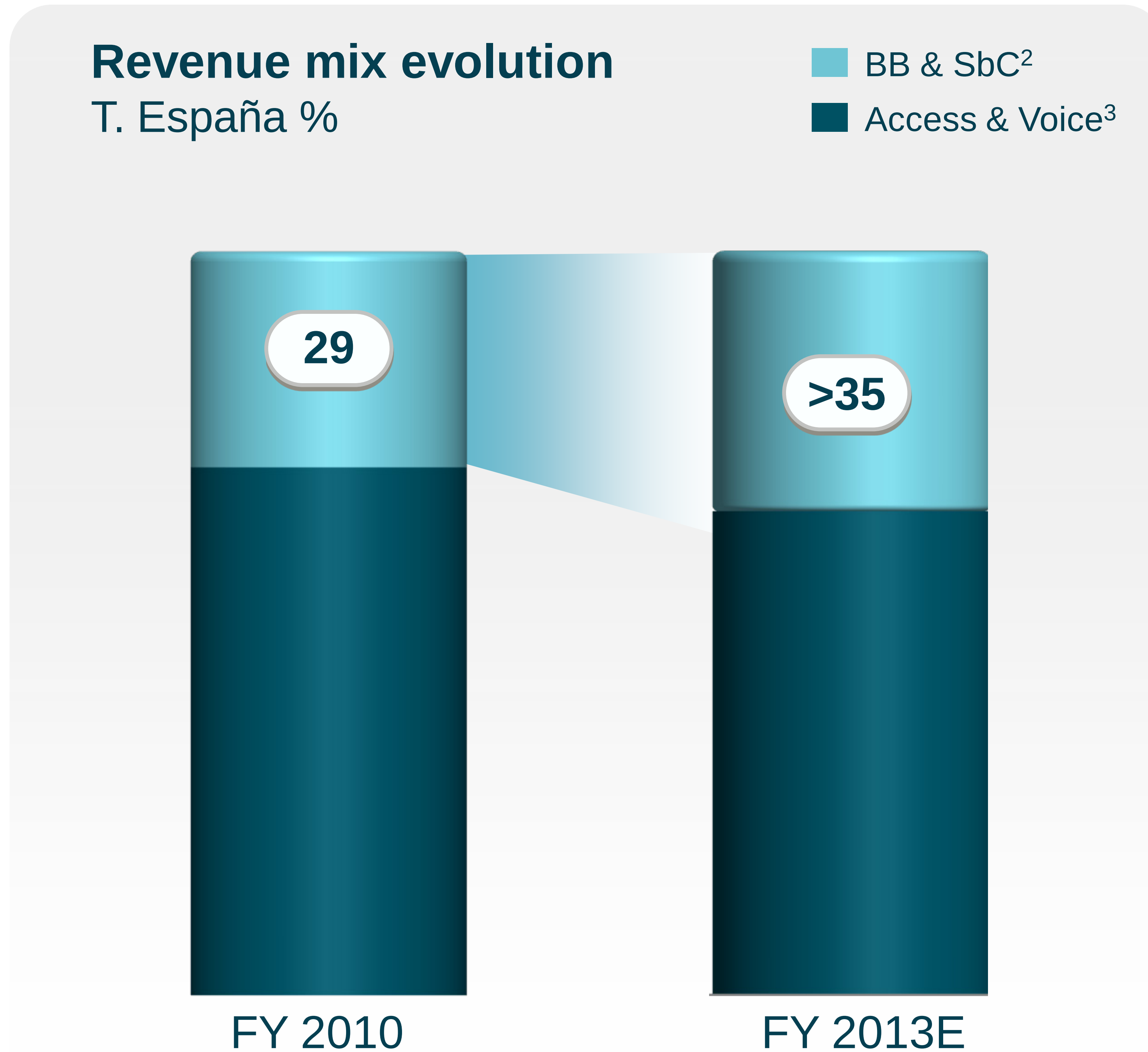
[1] OTT: Over the top.
[2] Services beyond Connectivity revenues: Content, digital services, ICT solutions and vertical units revenues

Our smart focus on value will enhance and diversify our revenue profile

Churn reduction

Differentiated value proposition

Revenue growth in key opportunities > € 1.2 bn[1]



1 Revenue increase from FY 2010-2013E. Includes Services beyond Connectivity and MBB revenues
2 Includes BB (retail and wholesale FBB connectivity, MBB, fixed and mobile devices (PCMCIAs and Dongle) and fixed data services) and Services beyond Connectivity (Content, digital services, ICT solutions and vertical units revenues)
3 Access and Voice revenue Include fixed/mobile access & voice (SMS included), narrowband and mobile& fixed equipment revenues

02

Our strategy ‘Focus on profitable leadership’

- Smart focus on value
- **Reshaping of our cost base**
- Optimized use of capital

There is further room to improve our efficiency and continue delivering a benchmark OIBDA margin

Benefit from our commercial focus on value (vs. volume) and manage direct costs …

- **Gradually balancing SAC to SRC,** acquisition vs. retention
- **Increasing share and effectiveness** of commercial costs
- **Maintaining direct margin[1] over revenues**

More resources dedicated to customers and maintenance of direct margin

+

… while reshaping our non-commercial expenses

- **Leveraging global scale** (purchases and product development)
- Increasing the level **of automation and remote management**
- **Fostering simplicity** in IT applications, offer and legacy networks
- **Fully online** traceable commercial processes in 2013

Focus on reduction of non-commercial expenses

Continuing to deliver a benchmark OIBDA margin

[1] Revenues less supply costs (interconnection, content and other direct supplies)

Additional measures to gain more flexibility and compensate for potential recovery delays

Current initiatives …

- **6% reduction in manager positions**
- **More flexible collective bargaining agreements**
  - § TME pay revisions not linked to CPI in 2011
  - § More flexible structure policies

… and moving towards more flexibility and higher productivity

Higher productivity …

- **Pay and benefit revisions** more **linked to productivity** rather than CPI
- **~ 85%** employees under **collective bargaining agreements**
- Each p.p. of **CPI increase** represents ~ € 15 m cost increase per annum

… and additional alternatives

- **Potential outsourcing** of operations to service providers and/ or…
- …further **workforce restructuring** processes

Ñ ~20% employees in 3 years[1]

[1] T. España perimeter

02

Our strategy ‘Focus on profitable leadership’

- Smart focus on value
- Reshaping of our cost base
- **Optimized use of capital**

We will optimize the use of capital by adjusting our asset base...

Sale of non-core assets

- **Ongoing processes…**
  - Sale of IT applications
  - Real estate
- **… and other programs**

Cash proceeds of € 600 m in the period FY 11-13E

Co-investment

- **Mobile Network sharing**
- **Co- investment** approach for fibre infrastructure inside buildings

... and follow a "smart" investment policy to capture growth

Premium speed and quality

- Selective fibre deployment

Household coverage
%

	Dec-10	Dec-13E
≥10Mbps	~75%	~80%
≥25Mbps	~30%	~45%

Best mobility

- HSPA+ & LTE deployment

Mobile coverage by peak speed[1]
% / Population

	Dec-10	Dec-13E
≥14Mbps	~50%	~100%
≥42Mbps	~0%	~25%

+

New access networks represent up to 1/3 of cumulative CapEx FY 2011 - 2013E

We will remain flexible and adapt to market conditions

[1] Peak theoretical speed supported

03

Closing remarks

Focus on profitable leadership will balance short term results and long term sustainability and growth

Core principles	Strategic priorities	Targets summary
Defense of our OIBDA and our value leadership	Smart focus on value vs. pure volume	• Revenue market share ~48%-50%[1] in FY 2013E • > € 1.2 bn[2] growth in key opportunities
Flexibility to adapt to market conditions	Reshaping of our cost base	• A benchmark OIBDA margin
Capture market growth opportunities in a profitable way	Optimized use of capital	• CapEx adapted to market conditions • Cash proceeds of € 600 m in FY 11-13E

[1] Retail communication (fixed & mobile) revenue market share. **Source:** CMT and internal estimates
[2] Revenue increase from FY 2010-2013E. Includes Services beyond Connectivity and MBB revenues

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